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[This is:

**Gustav Cohn: The Science of Finance.** *Translated by Thorstein.B. Veblen.*

Chicago, Ill.: University of Chicago Press, 1895 (= Economic studies of the University of Chicago. 1.), xi, 800 p. [Note: Book 3, "German tax legislation of the present time," is omitted from the translation].

Original: System der Nationaloekonomie: System der Finanzwirtschaft. Ein Lesebuch für Studierende. Stuttgart: F. Enke, 1889 (= System der Nationalökonomie. 2. - vol. 2 of 3.)]

ECONOMIC STUDIES  
OF  
THE UNIVERSITY OF CHICAGO  
———  
NUMBER I.

IN PRESS

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HISTORY OF THE UNION PACIFIC RAILWAY

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No. III.

THE INDIAN SILVER CURRENCY

By KARL ELLSTAETTER. Translated from the German by  
PROFESSOR J. LAURENCE LAUGHLIN

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IN PREPARATION

No. IV.

HISTORY OF THE LATIN UNION

By HENRY PARKER WILLIS

[iii]

# THE SCIENCE OF FINANCE

*BY GUSTAV COHN*

TRANSLATED BY  
*T. B. VEBLEN*

CHICAGO  
The University of Chicago Press  
1895

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1895

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## AUTHOR'S PREFACE TO THE ENGLISH TRANSLATION.

Under the auspices of the University of Chicago, Dr. Veblen has made a translation of my *System der Finanzwissenschaft*, which he is about to publish with the approval of the German publisher. In response to a wish expressed by the translator, I do not hesitate to say that a reading of the proof-sheets has satisfied me (so far as I am a competent judge) of the excellence of the translation. I can therefore only express the hope that my book may in this new form meet with as cordial a welcome beyond the sea as has already been accorded to many books of mine in the original.

G. COHN.

GÖTTINGEN,  
January 1895.



## TRANSLATOR'S PREFACE.

This translation of Professor Cohn's *System der Finanzwissenschaft* aims to be a faithful rendering of the original, without abridgment or alteration, except such as the exigencies of diction and the differences in terminological usage in the two languages have made unavoidable. In cases where the absence of an English equivalent for a technical or quasi-technical term employed in the German has necessitated an arbitrary rendering, as well as where the insertion of the corresponding German word or phrase would aid in conveying the exact sense of the original, the German words have been added in brackets.

The Third Book, dealing with the German Tax Legislation of the Present Time, has been omitted; the reason being that this Book is entirely historical in character, and as the German edition is now some six years old an English translation would not serve its purpose, as a description of contemporary German fiscal institutions, at all satisfactorily without extensive revision, such as the author finds it impracticable to undertake at the present time. Moreover, Professor Cohn's peculiar theory of finance and of the state, which it is the prime purpose of the translation to present to English readers, is complete without Book III. To facilitate reference, the numbering of the sections has not been changed, the section numbers comprised in Book III. being simply I omitted. Section 173 has also been omitted, for the reason that the discussion at this point in the original turns on a nicety of language which is not reproducible in English. The omission, it is hoped, involves no substantial loss.

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The dedication contained in the original has been omitted and an index has been added. In so far as the translation accomplishes its purpose, its success is in no small degree due to a careful revision of the proof-sheets by Professor Cohn, who has been good enough to read the whole and to make such emendations as might be necessary to bring it up to date. My thanks are due to Miss Sarah McLean Hardy for the correction of many obscurities and crudities in the translation and for assistance in reading the proofs while the book has been going through the press. I wish also to acknowledge the courtesy of Mr. Ferdinand Enke, the publisher of the German edition, in very cordially consenting to the publication of this English edition.

T. B. VEBLEN.

UNIVERSITY OF CHICAGO,  
March 1895.



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## INTRODUCTION.

THE PLACE OF THE SCIENCE OF FINANCE IN  
ECONOMIC SCIENCE

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## CHAPTER I. THE PLACE OF SCIENCE OF FINANCE IN ECONOMIC SCIENCE.

LITERATURE. Lorenz von Stein, *Lehrbuch der Finanzwissenschaft*, 5. Auflage (1885-86), *Erster Theil*, pp. 1-49. Adolph Wagner, *Finanzwissenschaft*, 3. Auflage (1883), *Erster Theil*, secs. 12-20. G. Cohn, *System der Nationalökonomie*, *Erster Band (Grundlegung)*, 1885, pp. 21-22, secs. 192-197, 213-216, 284, 290-292, 298-304, 329-333, 396-403.

### I. THE DEPENDENT CHARACTER OF THE SCIENCE OF FINANCE.

§ 1. A consensus will gradually be reached as to the purport of science generally: what its sphere may be, what is its subject matter, its content, its attainable goal. The doubts and misconceptions that arise in the course of a discussion of this kind, usually - apart from tenets that simply negative all approach to an understanding - have their ground in peculiarities of the field of view with which the scientists occupy themselves. Not without difficulty, but still not without some ultimate result, may we seek to bring about a reconciliation between the ideas of the jurist and the physician, the historian and the naturalist, the investigator and the systematician. These are, when all has been said, nothing but the refracted rays of which the perfect light is made up; and there is, after all, nothing needed beyond such an exercise of good will as shall enable each to view his own contribution to the whole from a more comprehensive standpoint. This has been the purpose of certain remarks that have been inserted in their proper place in the *Grundlegung* that forms part of the present work. The very general character of the point of departure, as well as the elucidation of the subject matter by means of material from outside, is due to the presence of such a purpose; this applies especially to the chapter on The Method-

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ology of the Social Sciences and of Political Economy in particular [*Die Methodologie der Staatswissenschaften und der Nationalökonomie insbesondere*], and to the succeeding chapters on The Place of Political Economy in the Circle of the Sciences [*Die Stellung der Nationalökonomie im Kreise der Wissenschaften*].

More difficult is the question, What constitutes an independent science?

We might with a good conscience evade this difficulty if the question were an idle one.

But that is not the case. The question of the dependence or independence of a given field in the general domain of science has somewhat the same importance as the analogous difference in the relations of states to one another. As, according to Aristotle, it is a characteristic of the state that it should be self-sufficing, so it must also be taken that an independent science is such a portion of the aggregate of scientific knowledge as is complete in itself, and which therefore does not in its essential nature depend on support from without. Just as those commonwealths are in a sad plight, in process of disintegration or of becoming, whose existence depends on the tutelage of a greater state, or on the dissensions of their neighbors; so also is that science on a precarious footing that is obliged to depend largely on resources of knowledge that lie outside its own domain. Such a science simulates independent existence, while it is in reality dependent, and should therefore properly abandon its boundary lines. Or worse still, it feigns life while it is in reality cut off from the source of life.

§ 2. The difficulty of the question as to the independence of a science is due to the causes mentioned below.

I have already reviewed the course of historical development (vol. i. sec. 63) and shown how science only slowly and gradually frees itself from the interested thinking of every-day life and becomes an end pursued for its own sake. Every-day expediency does not concern itself with underlying principles but only with the ready applicability of its maxims, and the most immediate and pressing cares of life are precisely the ones



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which, as regards the principles involved, call for a union of the most divergent points of view. It is therefore this independent, practical purpose or need that urges to the establishment of an independent science. And this sort of independence has, moreover, the weight of a prior title in its favor; inasmuch as it is the practical aim that first gives occasion for reflection. And so long as human inquiry remains under the jurisdiction of expediency, as in spite of all past progress it still does today, it will be exceedingly difficult to bring these venerable traditional sciences to a reckoning. The result is that we find the sciences ranged in groups, departments and branches, in a fashion that is altogether unintelligible except in the light of this fact. The chief institutions devoted to the development and perpetuation of the sciences all bear the mark of this relation. And this bustling expediency stands ever ready to erect out of every fresh acquisition of knowledge new sciences, constructed after its own heart, whose lack of venerableness is made up for by the superabundance of popular applause awarded them.

A second ground of difficulty is the fact that no science is independent in the sense suggested by the analogy of national autonomy. Under the harsh exigencies of national life as we actually find it, the ideal of the solidarity of mankind may have to give way before the boundaries of such national units as are possible for the time being. In science, whose office it is to bring about a progressively wider and profounder knowledge of all being, and so to gain an ever deeper insight into the fundamental unity of all knowledge under a single comprehensive synthesis, - in science no such exclusiveness is practicable, and every considerable innovation in methods of research or of generalization rudely upsets the complacent self-sufficiency of a hard and fast classification.

But this factor of comprehensive generalization is constantly traversed by the other equally inevitable need of all advancement of knowledge, viz., increasing intensity of culture-to borrow a phrase from the vocabulary of industry. As in agricultural industry the magnitude of an estate is not to be measured by

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a geographical, but by an economic standard, it being quite possible to conduct a large industry within a relatively narrow space, if only a high development of human industry has been attained, - so also in science. A narrowing of the field of its labors, such as will correspond with the limitations of its intellectual gifts, is a condition prerequisite to profitable application on part of the average talent employed in the scholar's trade today. The absence of perspective in this bustling activity gives rise to independent sciences that contain but scant suggestion of the profounder unity of all knowledge. But so potent is the tendency that finds widespread and conscious expression in these phenomena, that any effort in behalf of more comprehensive synthesis of the particular under the general finds it exceedingly difficult to effect even a reconciliation of the part with the whole.

§ 3. Under these circumstances it follows that the concept of a science as an independent department of the aggregate of sciences will always be subject to variation. It varies with the point of view to which we may be accustomed, and it varies even within the same group of thinkers and in the same period of time. It is in a state of absolute flux if account is taken of the passage of time and the changing circumstances indicated by the divergent points of view above referred to.

It is therefore bootless to attempt to draw hard and fast boundary lines between the sciences; such lines cannot be maintained.

But one thing is always possible, and is at the same time necessary. It is that every particular fragment of knowledge which puts forth a claim to rank as a distinct science, whether on grounds of the practical purpose it serves, or of usage, or of specialization, should not only be considered as belonging to the general domain of science, but its fundamental elements should be brought into vital connection with the greater whole. Only in this way can the roots of a special science be kept from drying up. Only in this way can we insure to the special science that

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substantial vitality which is the essential object sought in this straining after an "independent" standing.

Hence we see what we see during these latest times; - that the advance of research and the profounder insight gained by employment of the latest methods are upsetting the fancied independence of whole groups of these special sciences and replacing it with a comprehensive relation of dependence. This is what modern Natural Science teaches, when the traditional boundary lines of Medicine, Botany, Zoology, etc., have to be readjusted after every new step in advance, when Chemistry and Physics draw closer together as the potent force of sweeping generalizations based on the great mass of material furnished by research comes to the front.

Something similar, though hampered by the difficulties inherent in a complex subject matter, is to be remarked in the case of our own science. There is no contradiction in the fact - it is rather the fruit of an improved method of research - that the latest developments of our science have been characterized on the one hand by an affectionate attention to the historical material bearing on economic life, and on the other hand - and at the same time - by a broader and more comprehensive view of the nature of all economy. An attempt has been made in the first volume of the present work to form an estimate of the value of this evolution, and, so far as in me lies, to contribute something towards its furtherance. We shall simply be continuing the work on the same line in doing the like for the Science of Finance and placing to its credit what has been accomplished for the science. Just as Political Economy has been traced back to its deeper-lying sources, and has therewith been advanced beyond its narrow traditional limits; so also the science of finance may claim the like within its field after its achievements have likewise been assimilated into the body of the profounder conceptions of all social life.

§ 4. That the Science of Finance is a part of Political Economy is a long-accepted fact.

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There is an objection of a trivial character that may be raised at this point, an objection based on the varying meaning attached to the term "Political Economy." Since the term has been applied now to economic science as a whole, now to the fundamental (general) part of the science only, it has not rarely happened that the Science of Finance and Political Economy have been contrasted with one another as parts of a greater whole. The like was done more intentionally and consciously by K. H. Rau and his contemporaries and followers when they contrasted the Science of Finance with Economic Science [*Volkswirtschaftslehre*]. Indeed, the contrasting of the two was in this case the result of a well-defined purpose, and was consistently adhered to; Economic Science as a whole being designated "Political Economy" [*Politische Oekonomie*] (similarly of late in the *Handbuch der politischen Oekonomie* of Gustav Schönberg, 1882; 3. ed., 1890-91). The aim was to call attention to the difference between an ostensible "pure theory" and its application in the practical working of political affairs.

Neither a purpose of this kind nor the varying usage of the terminology must, in view of the conclusions reached in the first volume of the present work, be allowed to mar the simplicity of the relation in virtue of which we have here to do with a general and a particular, a whole and its parts; - with parts, of which the Science of Finance is one; with a whole, which is Political Economy. For everything contained in the discussions that follow is but a more detailed elaboration of the general outlines that have already been laid down in the first volume.

This view corresponds in the main with the views held at the time when an independent science of economic life first made its appearance. Even the creators of the new science, the Physiocrats,<sup>1</sup> made the theory of taxation the corner-stone of their theory of economy, and so incorporated the Science of Finance indissolubly into the structure of the system. Adam Smith devotes the fifth book of his *Inquiry into the Wealth of Nations* to The Revenue of the Sovereign or Commonwealth, and English manuals

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<sup>1</sup> See vol. i. secs. 71-73.

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have to this day followed the tradition initiated by him. So John Stuart Mill, in his *Principles of Political Economy*, likewise devotes his fifth and last book to the same subject, and he even unmistakably follows Adam Smith in his arrangement of details, only he introduces discussions of a general character on the influence of the government upon industry. A separation of the part from the whole has not hitherto been attempted in England, for the reason that the slightness of the subsidiary structure has offered no temptation to a claim of independence. There has also been no work, worth mentioning, which treats separately of this subject.<sup>1</sup>

§ 5. The place of Financial Science in the general science of Political Economy has also been questioned on other grounds.

A treatment of the subject that makes the distinction between "Social Sciences" and the "Political Sciences" its point of departure relegates Political Economy to the former head, the Science of Finance to the latter. My opinion regarding the contrasting of these two great groups of sciences has been expressed in the proper place (vol. i. sec. 54). Among the consequences of making this distinction would be that the treatment of private law would come under the general head of the social sciences, and that of administrative and public law generally under the head of the political sciences, - a separation of things that belong together such as is manifestly untenable when we consider that precisely the latest advance in jurisprudence goes to show the impossibility of drawing any line between so-called private law and so-called administrative law. In like manner the latest progress of Economic Science places the state in such intimate relation to the factors of the social economy that any classification of the subject matter to be dealt with which places the State in contrast with Society becomes no less false in theory than it is in actual life. Such a distinction would be tenable only in case we had a science of the instinctive movements and activities

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<sup>1</sup> C. F. Bastable's *Public Finance* (1892) has been published since this was written. [TR.]

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of society (such as Sociology actually claims is possible), which could then be contrasted with the ethical "ought" as applied to the state. This question, however, has been so fully discussed in the general portion of the present work as to leave nothing more to be said about it at this point.

A much nearer approach to the real facts of the case is made in the observation that when the matter is viewed from the standpoint of the national administration we find ourselves confronted with a special phase of social life and a special problem, which require that the science should be treated as a political science in the narrower sense, and that hence arises a group of political sciences, in the narrower sense, which treat of the various phases of the political range of activities. But even if this be granted, a useful purpose will be served by this classification only in so far as the special science takes up a special subject matter for scientific treatment; so that the political sciences, in this narrower sense, will accordingly have to take up the particular institutions that go to constitute the state and through which the state acts. It then becomes a question between these "political" sciences and the other special sciences, how far the latter are to be deprived of their substance for the benefit of the former. It results that a theory of the State, of the Constitution, of Administration, may be developed up to a given point out of the principles special to the State as such; while beyond this point we pass to ground where these principles alone will no longer serve our purpose, and where recourse must be had to knowledge drawn from elsewhere. It is at this point that Jurisprudence, Economic Science, and Natural Science come in and demand recognition, the one or the other of them, according to the particular sphere of political activity under consideration.

The like is true of the Science of Finance. We may approach the public economy from the summit of the political structure as well as from the lower-lying fields of the economic life of the people. But the knowledge required in order to a scientific treatment of the public economy remains the same, and it

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depends, in a greatly preponderating degree, on an understanding of what goes to make up the economic life of the people.

If, now, both these avenues of approach are open to us, the logic of our method decides us in favor of the one which affords the more vital connection between the fundamental elements of the problem.

## II. THE RELATION OF THE SCIENCE OF FINANCE TO POLITICAL ECONOMY.

§ 6. A few words will be necessary to justify the classification here insisted on.

In the Introduction to the general doctrine of Political Economy contained in the first volume of the present work, it is attempted to lead up to the general body of the science by means of the following named chapters: An Exposition of the Scientific Method necessary to the Attainment of Truth in our Branch of Knowledge, The Relation of Political Economy to the other Sciences, The Historical Development of the Body of Doctrines, Fundamental Concepts.

The unity of part and whole - of the Science of Finance with Political Economy - has been so fully pointed out in the Doctrine of Method that there is no need of repeating here, in connection with this special point, what has already been said in discussing the general subject. It may therefore be sufficient simply to refer back to the earlier discussion. The meaning and import of the general principles, set forth after the fashion of the old school of thought; the relation of deduction to induction, of hypothesis to empirical knowledge; and more especially the value of financial history and financial statistics for the purposes of the Science of Finance; - all this could be intelligibly discussed only with the aid of appropriate illustrations, and bearing in mind what has already been said in the general portion of the work. But this would necessitate a great deal of repetition, which will best be avoided by simply referring back to the general introduction for the whole matter.

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I flatter myself that in this preliminary exposition, and more especially in those portions which touch the relation of what ought to be to what is in social life, I have said much that may be of substantial assistance toward clearing up existing misconceptions. This exposition has set aside that customary disruption of our science into a duality of problems, which is wont to insist on directing our attention at one time exclusively to the historical-statistical materials furnished by investigation and to their causal connection, and at another time to the solution of the questions of the day. The fallacy of this position has been exposed both as regards the Science of Finance in particular and as regards Political Economy in general. It has been set aside both in so far as its outcome is an historical quietism that ignores the presence in all the subject matter of history of a ceaseless drift in the direction of that is to be; and it has also been set aside in so far as its meaning is a clamorous demand for innovation, which, under the pressure of the impulses of the moment, overlooks the continuity of the past with the future. The bringing of these conflicting elements into harmony in the science and in the affairs of life, is the really conclusive test of the value of this preliminary methodological exposition which might seem to the superficial glance to be but an idle speculation.

As in the second chapter of the general introduction we dealt with the position of Political Economy within the domain of science generally, so here we shall attempt to trace more in detail the connection between the general science of Political Economy and the Science of Finance. In so doing we shall indicate the place held by Finance in the group of sciences that treat of industrial life. In performing this task we shall find that the fundamental principles peculiar to the Science of Finance will come to light of their own accord in the course of establishing this connection of the part with the whole, somewhat as was done for the general sciences of Political Economy in the fourth chapter of our general introduction.

The historical development of the science, together with the necessary indication of the more important literature of the sub-



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ject will also claim a chapter in this special introduction to the Science of Finance, just as was found necessary for the Science as a whole in the general introduction.

§ 7. The lines of connection between Political Economy and the Science of Finance are the following:

In the first general subdivision of this work, which treats of the elements of industrial life, the central fact is The Wants of the People. Even at that point it was found necessary, in order not to leave unnoticed a factor of great consequence in the collective needs of any community, to speak of The Demands of the Public Economy and to indicate their chief objects and aims (vol. i, secs. 213-216). The same chapter discusses the orderly relation and comparative importance of wants considered from the general economic standpoint, and at the same time, in dealing with the general problems of industrial society, it touches also upon the peculiar features of the public budget (vol. i, secs. 192-197).

These several lines are taken up in the first book, treating of the Science of Finance, the first chapter of which, under the head of The Nature of the Public Economy, treats of the state and its functions, while the sixth and seventh chapters of the same book treat of Order and Sequence [*Ordnung*] in the Public Economy, and the Various Kinds of Public Expenditures and Demands [*Bedarf*].

But there are also other points at which work done in the first volume will serve in the way of introduction to the discussions of this first book: as, e.g., the discussion of The Structure and Activities of Industrial Society [*Gestaltung des Wirtschaftslebens*], which takes up the state as a constituent factor in the moral system (sec. 284); and again, under the head of The Organization of Social Life [*Gliederung des Zusammenlebens*], where trade and other associations [*Verbände*] are treated of in connection with so-called free competition (secs. 298-304). Both topics are taken up again in the first chapter of Book I. following.

The question of voluntary action or coercion in public affairs is

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dealt with, partly in the discussion of associations (secs. 301-302) partly in treating of business activity (secs. 290-292). The fifth chapter of Book I. is devoted to this question. In its treatment of self-government, it also connects with the discussions of the chapter on the Division of Labor (secs. 246-247).

What has been said in the general portion of the work, under the head of The Disposition of Society into Groups, with respect to The Development of National Unity and of a Community of Nations (sec. 329-335) is taken up again in the fourth chapter following, in discussing The Structure and Relations of Public Bodies [*Gliederung der öffentlichen Verbände*].

Finally, the great problem that forms the main topic of every system of financial science, the theory of taxation, has already received due attention in the general theory of prices, under the head of The Determination of Value within Public Bodies [*Die Werthbestimmung in den Verbänden*] (secs. 396-403).

The third chapter of Book I. connects with this discussion in treating of the various classes of contributions to the public expenditures. And two entire books of the Science of Finance (Books II. and III.) are occupied with the theory of taxation, general and special. While Book IV., finally, on Public Debts, is based on the general theory of credit previously discussed (vol. i. secs. 415-423).

This then is the relation of the general to the special portion of the work.

## CHAPTER II. THE HISTORICAL DEVELOPMENT OF THE SCIENCE OF FINANCE.

LITERATURE. W. Roscher, *Geschichte der Nationalökonomik in Deutschland*, 1874. A. Wagner, *Finanzwissenschaft*, 3. Auflage, *Erster Theil* (1883); secs. 21-30. G. Cohn, *System*, vol. i. secs. 63-122.

### I. CAMERALISTICS AND FINANCIAL SCIENCE.<sup>1</sup>

§ 8. It lies in the nature of things that the pre-scientific stages, preparatory to the development of a science, follow the inexorable law of growth which governs human thinking as well as the phenomena of life generally, and so present results that look paltry when viewed from the standpoint of later, fuller development.

<sup>1</sup> Grimm (*Wörterbuch*, vol. iii. p. 1639) has been unable to find the word "Finanz" in German literature prior to the sixteenth century, and finds it constantly used in an evil sense, equivalent to cheating, deceit, etc. So used even by v. Seckendorf (*Der Teutsche Fürstenstaat*, 1656). Only in the seventeenth century did this evil meaning of the word gradually disappear, and only in the eighteenth did the term come to be narrowed down to designate the revenues of the state, - as, e.g., in Justi. While in the vernacular even today (in Germany as well as abroad) the broader meaning of early times, though not with the evil connotation, is still retained. The etymological derivation (Diez; *Etymolog. Wörterbuch der romanischen Sprachen*, 3. Aufl. 1869, vol. i, p. 180) is from *finis*, which in Low-Latin denotes end, peace, conclusion of any matter; and so payment; - Old French *fin*; English *fine* = *composition*. Hence in Low-Latin we have the derivative *financia* = *præstatio pecuniaria*, money payment generally. Closely analogous to this etymology is that of *pagare*, payer from the Latin *pacare* = *pacify* = *solvere* (Diez, vol. i. p. 300). In English the signification of the word "finance" remains to this day, even in scientific usage, a very variable one. So, e.g. the widely-accepted *Chambers' English Dictionary* (edited by James Donald, 1872) defines "finance": "revenue from fines or compulsory payments, public money, the science of public revenue." But even very lately (1886) a well-known English economist and statistician, Robert Giffen, uses the title "Essays in Finance" for a collection of papers which contain no financial matter whatever (in the sense understood by the Science of Finance), but which treat exclusively of such topics as Trade Depressions, Gold Imports, Bank Discount, Progress of the Laboring Classes, The Increase of Wages, and the like.

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Human thought in its best estate, as knowledge of the world spontaneously sought for its own sake, comes within the horizon of mankind only at a relatively late date. And even when this point is attained, there are but a very few among any people to whom the consciousness of its presence penetrates. The great majority even of those who call themselves the cultured class ask what is the useful purpose of knowledge, and grow impatient if the practical application is not forthcoming; while any such tangible utility is hailed with unquestioning enthusiasm, as may be seen in the case of the natural sciences today.

During the early stages there is simply no mental effort put forth, save that which serves an immediate useful purpose, and the nearer we approach the beginnings of culture the more undisguised is this practicality of purpose. The thinking is but the employment of an untrained fancy on a scanty experience, but these deliverances of fancy bring out the homely practicality of its purpose in all the more glaring a light. Such has also been the course of development of our science. And, more especially, such has been the case with respect to that portion of the science with which we are here occupied.

The last stage of this pre-scientific period of thinking is the outgrowth of a system of management which the supreme organ of practical life, the state, developed in order to carry out its purposes. It was the best intellects employed in this administrative work that prepared the way for scientific thought.

The name which this system of thought goes by is the well-known term, "Cameraristics" [*Kameralwissenschaft*].

§ 9. Johann Heinrich Gottlob von Justi, the most important representative of Cameralistic Science<sup>1</sup>, in his *Staatswirthschaft* (or Sys-

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<sup>1</sup>For the earlier literature of Cameralistics I may refer again, as I have already done in the first volume, to Roscher's *Geschichte der Nationalökonomik in Deutschland*. I have, at the proper place (vol. i. § 63 *et seq.*), indicated the reason which has decided me not to take up this literature in detail. It is always possible, if one only approaches the task with a sufficient enthusiasm, to discover in the early Cameralists expressions of a pretty adequate insight into the nature of the economy of society and of the state. Still, even apart from the fact that such an accomplishment is a rare

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*tematische Abhandlung aller ökonomischen und Kameralwissenschaften, die zur Regelung eines Landes erfordert werden, 1755)* speaks of Colbert as the greatest of finance ministers, probably, that has ever lived, and for the reason that, like the true-bred Cameralist that he was, he strove to improve the country and enrich it with commerce and manufactures, and so enable it to bear a heavier burden of taxes, he having actually increased the royal revenues threefold, as compared with what they were at the time when he entered on his ministry.<sup>1</sup>

In all this Justi has simply reflected the ideas which dominated the times in which he lived. The wealth of the people and the people itself (which for its part was part and parcel of the state<sup>2</sup>) was treated of solely from the point of view of the state's revenues. The furthering of the people's well-being is but a means to the ends of the state.

Proceeding on this ground Justi divides his work into two parts, the first of which treats of The Theory [*Lehre*] of the Maintenance and Augmentation of the Wealth [*Vermögen*] of the State; the second, of The Theory of a Judicious Use of the Wealth of the State.

The topics discussed in the first part are: State-Craft, The Science of Public and Commercial Regulations, together with "Economics" [*Haushaltungskunst*]; the second part deals with "Cameral, or Financial Science proper."

Here we find Cameral Science in the narrow sense contrasted with the Cameralistic Sciences in the broader sense, and used as a synonym for Financial Science.

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and creditable deed, one ought to carry the investigation undertaken so far toward completion as not to leave oneself liable to too jarring blunders. Such a blunder seems to me to have been made by Lorenz von Stein in speaking of "Klock's potent personality" (*Finanzarchiv*, 1884, p. 30) as the creator of German financial science; when the earlier literature of the subject is at pains to say of him that "his greatest service is that he has looted and plagiarized Faust's *Consilia* in an altogether unconscionable fashion, without giving the man the slightest credit" (Karl Heinrich Lang, *Historische Entwicklung der Deutschen Steuerverfassungen*, 1793, p. 10), a statement which is enforced by a series of citations, some of them covering as much as some forty-eight pages. This same Faust is to Stein's mind "of pretty slight consequence compared with Klock:"

<sup>1</sup> Vol. i. p. 18.

<sup>2</sup> Vol. ii. p. 5.

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The subject matter treated of by this science is as follows: The first book, which occupies two-thirds of the whole work, treats of the procuring of means required for the expenses of the State; the second book, of the expenditures of the State; the third book, of Administration, that is to say, of the organization and management of the cameral mechanism.

In his discussion of his main topic; the procuring of revenue, Justi rejects the traditional distinction, based on a legal distinction, between the exchequer [*Fiscus*] and the treasury [*Aerarium*]. The revenues of the exchequer, which included more particularly the crown lands and the royal prerogatives, were to be applied particularly to the maintenance of the sovereign's person and state; the revenues of the treasury on the other hand were to serve for the public defense and to further the public welfare, the former being under the control of the exchequer, the second, as being the produce of contributions granted by the estates, being under the supervision of representatives of the nation. This distinction, which, in Justi's time, "was in nearly all countries treated with little or no consideration, has no substantial foundation in the nature of things, and is therefore of small consequence for the theory of the revenues of the state." All expenditure on the part of the state has but a single, common purpose, viz., the furtherance of the state's welfare; and the personal maintenance of the sovereign falls under this head just as much as all other expenses.

The ordinary revenues of the state may, according to Justi, be treated of much more in accordance with their true nature if we classify them according to their source and their purpose. The sources of revenue are four. The first consists of estates belonging immediately to the sovereign or the state (crown lands, domains); the second source of revenue is dependent on rights and privileges pertaining to the crown or to the state's sovereignty and attaching to property held by the state. These rights had their chief ground and purpose in the furtherance of the public welfare, but they had at the same time an important secondary purpose in the revenues to which they gave rise.

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These go by the name of Royalties [*Regalia*]. The third source is that of the contributions made by the subjects toward the great expenses of the government out of their private means (which at the same time are part of the aggregate wealth of the state). This contingent goes under the names of Contributions, Taxes and Imposts. The fourth source, finally, arises from certain prerogatives whose purpose is not so much the revenue derived from them, but which nevertheless incidentally yield a revenue. As in his rejection of the formal, legal distinction between the exchequer and the treasury, so also in the great prominence he assigns to taxation as contrasted with domains and royalties, Justi stands forth as a leader of the new era. But also in point of theory he approaches closely to the true scientific standpoint of Financial Science, when he holds that the wealth of the state is mostly in private hands, and that this wealth would shortly be destroyed if its substance were applied to meet the expenses of the state; that accordingly the "usufruct" of this property, the "earnings" alone must be so employed; and that, inasmuch as the subjects must also draw their livelihood from their earnings, only a part of the earnings can be appropriated to the expenses of the state.

But if Justi has herein done his part toward supplying to the subject the systematic treatment which he felt the absence of (he expresses astonishment, in the introduction to his Work, that philosophical minds had not previously concerned themselves with Cameralistics), his French contemporaries, the Physiocrats, took up the philosophical consideration of the matter with still more decided results.

§ 10. The Physiocratic theory of taxation has this much in common with the Cameralists, that in the one case as in the other the needs of the state furnish the point of departure for their economic speculations. In the one case as in the other the idea of the state is struggling to assert itself and seeking the means needed for its administrative work. The

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Cameralists find that the way to accomplish their purpose is to enrich the country in order that it may the more readily bear an increase of imposts. The Physiocrats, as a consequence of the reactionary movement against the increase of national imposts, deny the necessity of any such increase. But in this matter they are not always consistent. Turgot, for example, had quite extravagant notions of the state's duties in the matter of public instruction; so that in this respect he is well abreast of the modern socialists. The Physiocrats recognize the need of the impost in each individual case and seek to so strengthen the national industry as to enable it, if not to bear an addition to its burdens, at least to afford the existing revenues without diminution. They therefore look upon the nation's industry with the eyes of a sovereign who, in the spirit of the shrewd manager of a private business undertaking, strives to get the highest and most permanent net product possible from the business, and seeks to reach this result by dealing as gently as may be with the productive agencies under his control, and more especially with his workmen. Every sacrifice demanded of any one link in this chain of productive forces acts to the detriment of the aggregate productive power. Hence a view of taxation, the aim of which is to avoid such disturbances of the process of production by placing the burden, by means of the "single tax" (*impôt unique*), directly on the surplus product of industry, on the net product. Plainly, according to this view, taxes which bear upon the personal necessities of the producers are obnoxious to the same criticism as holds against taxes that interfere with the process of production by putting the burden on raw materials, machinery or means of communication. But since, according to this view, the process of production includes among its elements the whole of the population engaged in industry in any way, save only the landlords, the tax policy based on this view reduces itself to an indiscriminate rejection of all "indirect" taxes; and in order that some "direct" tax may be left, which, as the only permissible one, may afford the requisite funds for the commonwealth, the theory of a net product becomes indispensable.



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It is of some importance for the purposes of this brief survey of the development of our science, to note how the philosophical acumen which was brought to bear on this theory of a net product became a creative force in the hands of the callow Economic Science, with its rudimentary logic. Now for the first time the fundamental principles that cluster about the concept of "productivity" found expression; the practical problems of a newly reconstituted policy of taxation hastened in this way the birth of a new science of finance and industry.

In its original form, according to the theory as held by the Physiocrats, the available net product of industry makes its appearance exclusively in the rent of private land owners. According to the theory in its improved form, as it stood after half a century of elaboration, it occurs in both rent and profits.

It took still another half century for the theory to work itself clear of the traditional point of view which took account of industry only as an elaborative process for the production of taxability; that is to say, to dismiss the doctrine of the net product definitively, after it had served the purposes of the science.

§ 11. But while it is true that the practical problem which influenced the thinking of this first school imposed on political economy the point of view of taxation and for a long time held it to that point of view, there was after all a more potent factor to which this school owes its importance. This was the body of philosophical speculations from which this economic science was an offshoot, or rather into which it incorporated reflections on economic and financial matters. This other, higher factor that goes to the creation of a new science, besides the progress of practical knowledge, - the mother science out of which the affiliated science grows, played a pre-eminently important part in the genesis of the first scientific system of political economy.

Now, from the fact that it was in this case Moral Philosophy that in this way assisted at the founding of the new science, it resulted that this new science also attained quite another field of

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vision than that of a well ordered tax policy. It is accordingly possible to trace back to this initial point that broader view, which took a century to find its way to a full and conscious acceptance, and which makes the structure and functions of economic society the main object of the inquiry, finance being but one of its subdivisions. As is well known, it was not the French Political and Moral Philosophy alone that exerted such an epoch-making influence on science; the nearly related English-Scotch Moral Philosophy exerted a like influence at the same or a slightly later point of time. Adam Smith's *Inquiry into the Nature and Causes of the Wealth of Nations* (1776) assigned to the Science of Finance the place in the system of Political Economy which it has held for a hundred years. And just as it is true of this work as a whole that the position it takes is distinctly more moderate and conservative than that of the Physiocrats and is more in accord with the facts of the time, so also is it true that its utterances on the theory of finance are so far in consonance with the then existing state of things as to contain the essential features of the theory as held by the different peoples of today.

The theoretic structure of the science in Germany owes its characteristic features to the fact that it combines the legacy of the Cameralists with the new theory. If we compare Justi's Science of Finance with Karl Heinrich Rau's *Grundsätzen der Finanzwissenschaft*, published nearly eighty years later (1832), and if we then follow this latter work down into its last edition (1864-1865), we shall find that the heritage of the Cameralists has lasted on in a practically unchanged form over a period of one-hundred-and-ten years. The leading principles of Adam Smith have found a place beside it, it is true, and they may even have come to be the guiding principles. But a process of approach on the part of the fundamental principles of Financial Science to facts of actual life, and therefore to the empiricism of Cameralistic Science has been going on, in part due to a gradual weakening of the radicalism of these principles themselves, in part to the fact that the cameralistic science itself had absorbed into its sub-

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stance a good deal of the radicalism of the period of the enlightenment. So we find Justi, in the introduction to his Financial Science, declaring it a truism that the sovereign must not be personally interested in any sort of trade or business (vol. ii. p. 63); so also he pleads for a gratuitous administration of justice (vol. i. p. 118) and condemns fiscal royalties in the strict sense, and will allow only an incidental fiscal aim to attach to institutions calculated to serve the public welfare.

§ 12. When contrasted with the abstract dogmatism of the school of Smith, as represented in Germany by the Kantian, Ludwig Heinrich von Jakob (*Staats-Finanzwissenschaft*, 1821), the influence of Cameralistic Science on the development of the theory in the nineteenth century appears of great value. And in this connection it may be noted as a significant fact that the men who have done such good service to the science have been practical financiers and have approached the subject from the standpoint of the practical life of the time. So for example, Friedrich Nebenius, the Baden statesman, in his work on the public credit (1820; 2<sup>nd</sup> ed. 1829); likewise von Malchus, *Finanzpräsident* of Wurtemberg (*Handbuch der Finanzwissenschaft und Finanzverwaltung*, 1830); likewise, and more distinctly, the Prussian State Councillor, J. G. Hoffman (*Die Lehre von den Steuern, als Anleitung zu gründlichen Urtheilen über das Steuerwesen, mit besonderer Beziehung auf den preussischen Staat*, 1840); and finally, the Austrian financier, Karl von Hock (*Die öffentlichen Abgaben und Schulden*, 1863).

Thanks to this influence exerted by practical experience, a broad realism has come to displace the doctrines of the eighteenth century, as is notably shown in the case of J. G. Hoffmann.

Still it must be apparent that the development of the science is at best a paltry one so long as it oscillates between doctrinairism and empiricism in this fashion. The real element of progress is to be sought, on the one hand, in the broadening and deepening effect due to the philosophic basis afforded the youthful science of the last century; on the other, in the fact that the material

offered by financial and political life has been vitalized by the employment of an improved method of handling.

Here again I must content myself with referring to the general part of this work, and to the bibliographical discussions contained in its introduction. I can at this point only discuss quite briefly the special features of the later literature of the science of finance.

## II. MODERN FINANCIAL SCIENCE.

§ 13. We shall first have to speak of Lorenz von Stein.

If we compare his *Lehrbuch der Finanzwissenschaft* (1860; 5<sup>th</sup> revised edition 1884-86) with that of K. H. Rau, which it was intended in a way to replace, and which it actually did to some extent replace, the contrast is as great as could well be imagined. No work, whether compendium or other book, can offer definitive conclusions, but it can present with approximate faithfulness the accepted body of scientific doctrines in a relatively definitive form. Herein lies the strength of Rau's work. A complete disregard, or rather an evident ignorance of the profounder problems of the science, and therefore of all that gives charm and significance to the later developed science, brings it about that the novice accepts with a pleasing sense of security the superficial exposition which the book affords: - an easily comprehensible classification, sensible and preferably commonplace truths, backed by a painstaking presentation of legislative and statistical material, together with its bearing on practical life. This is what the common sense of the learner will most kindly take to and what he can most easily grasp. He has no occasion to complain of being called on for severe mental effort.

Lorenz von Stein, on the other hand, is to be counted as the one who, more distinctly than anyone else, has written a compendium of the opposite kind. The importance of his book lies by no means in its presenting a resumé of the aggregate of previous investigations. Rather, he makes use of the form of the compendium as a vehicle for some bold constructive work that goes far beyond the bounds of an exposition of scientific doc-

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trine and erects new and independent doctrines. These constructions may in some part be compared to the rockets of a pyrotechnic display, which momentarily shed a dazzling light, only to leave us in a still profounder darkness the next instant. Stein's doctrinal edifice is all the less calculated to inspire a feeling of security and habitability, since the architect himself presently replaces it with further developments, designed on still bolder lines and of a still more problematical character. Much less can his treatment of positive materials, of the literature, of legislation, of statistics, contribute to a feeling of security. These matters of detail, too, are disposed of at one bold stroke. And still, we should be devoid of all intelligence, and be possessed of a very finical conception of the development of all science, our own included, if we entertained a doubt as to the desirability of having a Lorenz von Stein replace a K. H. Rau. Not that anything new has been erected which the new era may accept in place of the earlier structure, but a ferment has been introduced into the science which has been at work for a generation past, and which serves to stimulate, if not to excite, every reflecting reader of Stein's works unto this day. It is a characteristic fact that the man's lengthening years and the successive editions of his book bring results the opposite of what we should expect of any other author under like circumstances. Instead of further establishing and reinforcing the truths attained, there is a continual extension of the structure. From the original single volume there presently develop two, and finally four, in close connection with this is the fact of a continual widening of the scope of the work, - something of doubtful value by itself considered, and more than doubtful for the purposes of a compendium. In consequence we have in the treatment of the subject, a significant accentuation of insignificant matters, as also frequent reassertion of what is itself quite open to question.

According to the conception of the science which I have advocated above, the profounder and more far-reaching relations subsisting between the financial system and the state by no means require that the later expositions of the Science of Finance

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should submerge themselves in a sea of general economic considerations. It is rather to be accounted a mark of an overwrought propensity to systematization, which works confusion for the development of the science and especially for the purposes of a compendium of the science, if each new branch of Economics is sought to be built up on an independent and wide-reaching foundation, as is done by Stein when, in consonance with his general dialectical method of contrasting state and society; he treats Social Economy, Administrative Science, and the Science of Finance as distinct and separate subjects. The lucidity of this method is further obscured by employing the same concepts with a different value in the different branches of the discussion; as happens in the latest edition of the *Finanzwissenschaft*, where great emphasis is laid on the distinction between "Financial Constitution" [*Finanzverfassung*] and "Financial Administration" [*Finanzverwaltung*], and this distinction is permitted to traverse at discretion the concepts of "Constitution" and "Administration" as commonly accepted both by Stein and others.

I shall have to refer again, at this point, to what has already been said, both of an encyclopedic and a methodological nature with respect to the relation of Law [*Recht*] to Economy [*Wirtschaft*]. It is only by reaching a clear and dispassionate comprehension of the elements entering into the inquiry that we can hold our ground against this imposing mass of fog reared out of a superabundance of stately words.

§ 14. Nothing more than a brief mention can be made of Karl Umpfenbach's *Lehrbuch der Finanzwissenschaft* (1859-60), which appeared simultaneously with Stein's book. It attacks the accepted doctrines at many points, with a good deal of incisiveness<sup>1</sup> (among other things the theory of the Regalia).

In its externals, the work of Adolph Wagner connects directly with that of Rau. While Wagner was the one to whom Rau himself chose to intrust the elaboration of the sixth (posthumous) edition of his *Finanzwissenschaft* (1870) there is none

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<sup>1</sup> A new edition appeared in 1887.

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among the later generation of German economists on whom the conviction has so deeply impressed itself as on Wagner that the Science of Finance must be brought into a closer and profounder relation with general Political Economy and that this result is to be attained by means of a profounder acquaintance with the facts of economic life. The reconstruction of the science which this involves differs essentially from that attempted by Lorenz von Stein. It is not attempted to erect a spacious structure of a general political-scientific character. Rather, what is sought to be effected is a thoroughgoing reorganization of the general theory of Economics, a theory which Stein did little or nothing to alter - apart from the great indirect influence which his work has exerted, but which he has not allowed to affect his own economic theory.

It was a remarkable coincidence that this conflict between the traditions of Cameralistics - the complacent self-sufficiency of cameralistic therapeutic dexterity - and the impatient onset of the new spirit, strongly charged with socialism, should come to a head within the same house. Wagner's efforts, directed solely to an elaboration and extensive emendation of Rau's work, presently led to the need - perfectly characteristic of the new epoch - of finding a new basis on which to erect a new and independent science of finance. This work on the general principles<sup>1</sup> (first published in 1875; 3. ed., 1892-95), was not entirely completed before Wagner's great energies were again bent on the Science of Finance in a work planned on such broad and profound lines as to unite views widely different from Rau's on general questions with what was best in Rau's work - painstaking compilation and indefatigable application to the preparation of a compendium - and that in improved and augmented form.

To this is to be added that Schönberg's *Handbuch der politischen Oekonomie* (1882; 3. enlarged edition, 1890-91), with all its numerous array of contributions, had among its collaborators no more powerful supporter than Wagner. In unselfishly lending his aid, in the way of exhaustive monographs on Direct

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<sup>1</sup> Cf. *Nationalökonomische Studien*, by the present writer (1886), pp. 679-720.

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Taxes and on Public Credit (as also on Credit, Banking, and Insurance), the motive was ever present of making his own treatment of finance all the more exhaustive. In this way, when his *Grundlegung* is counted in as a necessary substructure to the system, Wagner's *Finanzwissenschaft* comes to be a work which, for volume and energy, has no rival in the literature of the subject. And it is only to be hoped that the author may be permitted soon to complete this great work, and may then return to the prosecution of the work on his *Grundlegung*.

So far there has been made public the first part (2. ed., 1877; 3. ed., considerably enlarged and revised, 1883), containing: the Introduction; The Organization of Fiscal Administration [*Ordnung der Finanzwirtschaft*]; Fiscal Demands [*Finanzbedarf*]; Industrial-Fiscal Institutions [*Privaterwerb*]. Further, the second part (1880), containing: Fees, and the general theory of Taxation (2. enlarged ed., 1890). Of part third, which gives a history of taxation in different countries, there have (1889) appeared three instalments (1886, 1887, 1888). To judge by the elaborate treatment of the tax legislation of the principal countries which these contain, the conclusion of the work is not yet near at hand.

§ 15. The reason for not having mentioned Wilhelm Roscher's work earlier is perhaps rather a formal than an intrinsic one. It is only quite lately that the fourth and nearly the last volume of his *System der Volkswirtschaft*, containing the *Finanzwissenschaft*, has been made public. The first was published in 1854.

Below the city of Zurich, the waters of the Sihl pour into the Limmat, but long after the two streams have united it is possible to distinguish the colors of the two currents flowing side by side in the same channel. Very similar is the case with the process of assimilation brought about by the advancing development of life and science. In Roscher's work the juxtaposition of the tra-

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<sup>†</sup> The concluding portion of the work is to deal with Poor Relief (part second of vol. iv.)



ditional, half English half cameralistic body of doctrines and the newly acquired philological-historic elements is particularly striking. The Columbus's Egg which we find in the *Grundriss* of 1843 (vol. i. sec. iii.) has remained to this day the egg of Columbus; the development of what it suggests is reserved for later generations. And what yet remains to be worked out on the lines of this suggestion, as also what is unattainable in it, has been briefly indicated in the first volume of the present work.

Roscher's *System der Finanzwissenschaft, ein Hand- und Lesebuch für Geschäftsmänner und Studierende* (1886) has, just as was the case with the preceding, third part of his course in Political Economy, met so widespread a demand that a second edition was necessary immediately after its first appearance. Yet Roscher thinks necessary in his preface to offer an apology for his "venture," inasmuch as the works of Lorenz von Stein, Adolph Wagner, and Leroy-Beaulieu were already "in possession of the literary market." From the standpoint of the literary market this apology would be manifestly uncalled for if it were true that this work - as contrasted with the earlier works named above - had carried the germ contained in the historical method out to an adequate development.

But unfortunately that is not the case. Precisely as in the other volumes of the course, or perhaps even more distinctly, we here again meet with the old subdivision and method of treatment, in much the form in which it was handed down from the Cameralists. In the one case, just as in the other, the peculiar features of the work are to be found mainly in the notes - peculiarities lying not in the multitude of citations which are drawn from first, second and third hand sources quite after the traditional method of the compendium, but in the attractive method of treatment, which brings a great mass of polyhistoric material to bear on the cameralistic maxims. When employed in this direction Roscher's talent is at its best; whereas, when his great industry is applied to the new ideas and problems of the science his efforts, though worthy of respectful attention, are not always valuable for their results.

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It is to be mentioned, among the good features of this book, that it is of such a character as to render it accessible even to the most moderately gifted intellect. And this office, of a textbook for beginners, it will probably continue to perform for some time to come.

§ 16. It is not only as a part of our duty of enumeration of eminent services rendered the science that we have to call attention to particular monographic works, as well as to the compendiums; it is also a characteristic fact in the development of any energetically progressive science, and especially as regards the latest methods of research employed in our science, that a continually greater volume and variety of work will assume this form.

Attention is to be made, in the first place, of certain works which, both as regards date and as regards spirit and point of view, belong to the earlier period. Such are the painstaking writings of K. G. Kries, which penetrate deeper into the fundamental principles of taxation than his predecessors had done; as instance his discussions of the tax on land (*Vorschläge zur Regelung der Grundsteuer in Preussen* (1855), as also his papers, of the same date, treating of the English local taxes, the New York property tax, the Prussian income tax (*Zeitschrift für die gesammte Staatswissenschaft*, 1855). These labors have been continued in a like spirit and with similar industry and insight, but unfortunately in a very inaccessible form, by F. J. Neumann (*Die progressive Einkommensteuer in Staats- und Gemeindehaushalt*, in the *Schriften des Vereins für Sozialpolitik*, 1874; also several unfinished papers in various scientific journals; and finally, *Die Steuer und das öffentliche Interesse*, 1887).

The later years of the development of our science have brought forth chiefly works of an historical character. Particular mention is to be made of Gustav Schmoller's investigations in Prussian financial history (*Die Epochen der Preussischen Finanzpolitik*, 1877; *Studien über die wirthschaftliche Politik Friedrichs des Grossen und Preussens überhaupt von 1680-1786*, in Schmoller's *Jahrbuch für Gesetzgebung, Verwaltung und Volkswirtschaft im*

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*Deutschen Reiche*, 1884 to 1887). Further is to be mentioned Gustav Schoenberg's *Finanzverhältnisse der Stadt Basel im vierzehnten und fünfzehnten Jahrhundert* (1879). Also the yet unfinished work of Karl Buecher, of which one bulky volume has already been published; *Die Bevölkerung von Frankfurt am Main im vierzehnten und fünfzehnten Jahrhundert; Sozialstatistische Studien* (1886), the second and third volumes of which, still to be published, are to discuss more particularly the finance - historical material contained in the Bede books of the archives of Frankfort.

In addition to historical research, very efficient service has also been rendered the science of finance by statistics. In some directions official sources have been of great service. So, for example, the work of Ernst Engel, in his *Zeitschrift des Königl. preussischen statistischen Bureaus*; likewise the related work of Herrfurth in Prussian communal statistics; likewise the work carried on at the instance of the International Statistical Congress. The prospective arrival of a hitherto remote ideal seems to be promised in the announcement by K. Buecher of a presentation of the rich materials in the Frankfort archives, treated by a method which is to unify the statistical with the historical.

§ 17. As it always happens that the most notable currents in the development of any special science find expression in the journals, so it also happens in this case that the exuberant growth of German political economy is most immediately reflected in our periodical publications. And it is accordingly also true that the special branch of the science of which the present volume treats, just at present manifests its vitality in this way in an especial degree:

It is not only that the journals occupied with economic and political science generally give evidence of a developing activity (*Jahrbücher für Nationalökonomie und Statistik*, edited by Johannes Conrad; *Jahrbuch für Gesetzgebung, Verwaltung und Volkswirtschaft im Deutschen Reich*, edited by Gustav Schmoller; *Zeitschrift für die gesammte Staatswissenschaft*, edited by Albert Schaeffle; *Schriften des Vereins für Sozialpolitik: Staats- und Sozialwissenschaftliche For-*

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*schungen*, edited by Gustav Schmoller). As indicative of the considerable division of labor already attained, we have, in the *Finanz-Archiv*, a special journal devoted to Financial Science, edited by Georg Schanz (beginning with 1884), and we have further, in the *Annalen des Deutschen Reiches für Gesetzgebung, Verwaltung und Statistik*, a progressive compilation in the form of a periodical, which is at the same time occupied with a variety of materials bearing on matters of taxation and tariffs, and which also admits scientific discussions. While the work of this last named journal is in the nature of the case confined to the legislative and administrative affairs of the German Empire, at the same time that it gives some attention to matters of a different character lying within the same geographical area, the *Finanz-Archiv* on the other hand aims to give a continuous and comprehensive view of the financial affairs of all countries of importance, from a general point of view or through discussion of special problems. Valuable auxiliaries are also the periodically published manuals that give in condensed form the statistical data of finance from year to year. Such is the *Genealogische Hofkalender* of Gotha, with its well-known *Diplomatisch-statistisches Jahrbuch*. So also, latterly, the *Statistisches Jahrbuch für das Deutsche Reich*, published by the Statistical Bureau of the German Empire, in imitation of the *Statistical Abstract of the United Kingdom* dating back a generation earlier. This gives in a brief form a comprehensive view of the more important political and financial data of Germany.

§ 18. It holds true even in a more eminent degree with respect to the Science of Finance than with respect to the general science of Political Economy that the literature of other countries at the present time ranks below that of Germany. This is owing to the antecedents of the science in Germany. Cameralistic Science has afforded a broader area of cultivation for the subject, and this breadth has been cultivated, under the guidance of the later scientific movement, with great historical and philosophical depth.

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It is well known that during the period of its prime, and the period following its prime - from Adam Smith to the close of John Stuart Mill's activity, that is, for fully one hundred years - English political economy treated the science of finance as nothing better than a scanty appendage. It is a significant fact that no work worth mentioning on the science of finance has yet (1889) been published in the English language (though some considerable contributions have been made to financial history, as, e.g., by Sinclair, and later by Dowell<sup>1</sup>). In this respect, too, the latest phase of the development of economic science in England serves to give greater promise.<sup>2</sup> The restless activity of the Americans, their gratifying participation in the development of the science in Germany, which speaks so well both for them and for it, will no doubt in due course of time bring forth - good fruit, as it has indeed already yielded some excellent things. This is evidenced more particularly by the new scientific journals that are now published at so many of the American seats of learning. So we have the *Political Science Quarterly* (published by the faculty of political science in Columbia College, New York, beginning with 1886) devoted to the political sciences generally, but also occupying itself at the same time with topics of an economic and financial character. Also the *Publications of the American Economic Association*, which likewise date back to the year 1886. Also the *Quarterly Journal of Economics* (published for Harvard University, beginning with 1886).

Gratifying as have been the results of the influence exerted by German science on American students, the painstaking industry which it has inspired in Italian students has been no less so. The latter country has the advantage of a longer period of preparatory growth and a great number of universities and schools. Hence the presence, for a long time past, and more particularly recently, of an exuberant literary productivity. But the most characteristic feature of the new science in the new Italy is, after

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<sup>1</sup> *History of Taxation and Taxes* (1884, 2<sup>d</sup> ed. 1887).

<sup>2</sup> "Die heutige Nationalökonomie in England und Amerika, " *Schmoller's Jahrbuch*, 1889.

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all, its leaning on the German school. There is a very general familiarity with the German language (a knowledge of which the younger generation of Italian scholars acquire by residence in Germany) which they are accustomed to read and write, while they also eagerly study German publications. Hence a faithful adoption of the German method and assimilation of the German point of view. The outcome of this frank acceptance of the best result obtained elsewhere will be, in this case as in so many others, the ultimate attainment of an independent standing. Just as we find that in modern German art a thorough-going deterioration, or rather extinction of all true taste, has given place to norms borrowed from other ages and other peoples, and that the taste so regenerated is working itself clear and expressing itself in creations of its own, - so also will the science of Italy, through its unreserved acceptance of foreign norms, one day find itself rewarded with splendid achievements.

It is a notable fact that at the same point of time with the appearance of the above-mentioned North American journals a similar, but more comprehensive organ of our science has made its appearance in Italy, the *Giornale degli Economisti* (edited by Alberto Zorli), in which Carlo Ferraris, a disciple of Wagner, takes a specially active part.

§ 19. We know what a peculiar position France holds in the development of Political Economy. It has already been reviewed under the head of the History of Political Economy, from the earliest school of the Physiocrats down to the time of the Socialists and the later scientific movement.

As regards the science of finance, however, certain peculiar circumstances, outside of the general science of Political Economy, have had their influence.

While their general Economic Science, and with it their financial speculations, are yet confined, in that country as in England, within the limitations imposed by the old school, the situation is, after all, quite different from what it is in the latter country. France is and has been possessed of a large and well-

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educated class of administrative officials, to whom the country owes a financial literature of like character with that dealing with the other branches of her administrative system.

It is true, this literature occupies a middle ground between compilation and science proper (I may refer to what has already been said of the relation of Law and of Administrative Law to our science). Still it is to be recognized as a fairly effective preparatory work for the establishment of a vital relation between the science and the affairs of practical life; and in any case it is a great advance over the wide chasm that exists in England.

So far as a real French economist has applied himself to the treatment of the Science of Finance (as Leroy-Beaulieu has latterly done) the result has been a combination of the facts offered by this financial administration with the theoretical views peculiar to the old school, in which matters of fact have at times so far asserted themselves as to bring into consonance with this orthodoxy financial institutions which economists of the same faith in England or Germany hold to be entirely incompatible with it (such as the tobacco monopoly).

And conversely, the French economists, in harmony with the body of legislative enactments and all the dominant political parties far out towards the left, are for the most part inclined to condemn those kinds of tax legislation which orthodoxy in England and Germany has long ago given in its adherence to, and they have reached unanimity on this matter from the standpoint of this same school. The income tax may be cited as an example.

The common ground in all these contradictions is a habit of thought which shows a narrowness that is incapable of passing the boundaries of their own country - the lack of such a reasoning faculty as would find its way through the data of practical life and arrive at a general truth. Or it is the inexpensive profundity of the "practical man," who carries his point on the ground that what exists here and now is and must be all right. Of the literature which I have thus characterized the following works may well be particularly mentioned:

Esquirou de Parieu, *Traité des impôts, considérés sous le rapport*

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*historique, économique et politique en France et à l'étranger* (2<sup>nd</sup> edition, 1866, 4 vols.).

Paul Leroy-Beaulieu, *Traité de la science des finances* (1877, 4<sup>th</sup> edition, 1888, 2 vols.).

Amé, *Études sur les tarifs de douanes et sur les tarifs de commerce* (1876, 2 vols.).

Vuatrin et A. Batbie, *Lois administratives françaises; première partie: organisation administrative; seconde partie: matières administratives - finances, travaux publics* (1876).

*Dictionnaire des Finances; publié sous la direction de Leon Say par L. Foyot et A. Lanjalley* (began to appear in 1887; now nearly finished).

An idea, of the great volume of this class of literature may be got from Baron von Reitzenstein's paper on "Indirekte Verbrauchsabgaben der Gemeinden" (*Conrad's Jahrbücher für Nationalökonomie und Statistik*, 1884; *Neue Folge*, vols. viii. and ix.), and from Wagner's chapters on French taxation in the third volume of his *Science of Finance* (1889).



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BOOK I.  
THE PUBLIC ECONOMY.



## CHAPTER I. THE STATE AND THE PUBLIC BUSINESS.

LITERATURE. Bluntschli, *Allgemeines Staatsrecht*, 3. Auflage, 1863. Rudolph von Ihering, *Geist des römischen Rechts auf den verschiedenen Stufen seiner Entwicklung*, vol. i., 3. Auflage, 1873. Rudolph Gneist, *Das Englische Verwaltungsrecht*, 3. Auflage, 1883. Lorenz von Stein, *Handbuch der Verwaltungslehre*, 2. Auflage, 1876. Adolph Wagner, *Finanzwissenschaft*, *Erster Theil*, 3. Auflage, 1883. secs. 1-11.

### I. THE EVOLUTION OF THE STATE.

§ 20. There are few points at which the historical conception of social life has so completely carried the day against the notions of natural right as in the debate about the beginnings of the state. It is true the favorite analogy of a plant-like or "organic" growth is not to be taken too literally. Also, it is undoubtedly true that after a certain advanced stage of culture has been reached the foundation of a state by contract is not only possible, but is substantiated by historical fact. But the essential point is not touched by such objections as these. The essential fact is that long before a "contract" in the sense required by the abstract conceptions involved in the notion of natural right, could have been entered into, that is to say, long before the peoples had attained the stage of culture at which such a conscious recognition of the developed idea of a political organization is possible, an instinctive banding together is brought about by the pressure of the natural course of development, - a banding together of kindred for protection against common danger and common enemies.

This is the fundamental fact in the formation of all states. The principle of self-preservation which urges every living being to defend himself against every other being from whom danger threatens, leads, through the action of the natural bond existing

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between individuals connected by ties of blood, to concerted action in defense of a common existence.

All that comes to pass in the long course of the subsequent development of the state is traceable, finally, to this fundamental fact. None of the higher developed civilized states has yet been able to eradicate the traces of its childhood in respect of the fundamental importance which the need of a common defense and a common organization of force continues to claim.

And in this fundamental fact there is given the primarily democratic character of every primitive political body, This is not a national characteristic and does not distinguish any one people above others - a view which for obvious reasons has been acceptable to our historical school, whether they have been pleased to find that this peculiar feature characterized the Roman or the German people - but it is something that arises by universal necessity from universally efficient causes. What is related by African travelers, as for example by Henry M. Stanley,<sup>1</sup> concerning the peoples of the interior of Africa, agrees, as respects this fundamental characteristic, with what we know of the earliest stages of development of the Romans and of the Germans, however great may have been the difference in point of race descent and later culture.

What Tacitus relates of the Germans is therefore something that holds true without regard to national lines of demarkation, and describes in its essential features a typical fact.

Here we find the state a living identity of people and army. Army and People were not discrete concepts in the early days.<sup>2</sup> The army was nothing more than the people under arms. The population, constantly armed as they were,<sup>3</sup> when they were assembled, also constituted the army. Therefore the words which denote the army were used, even in later times, to designate simply the populace.

Accoutred with their weapons they congregate in the

<sup>1</sup> *Through the Dark Continent* (1876).

<sup>2</sup> Georg Waitz, *Verfassung der Deutschen Urzeit*, 3. Auflage, 1880.

<sup>3</sup> *Nihil autem neque publicæ neque privatæ rei nisi armati agunt.* - Germ. cap. 13.

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popular assembly where they transact such business as may be necessary even in the primitive commonwealth, in addition to the use of arms: determination on war or peace, punishment of offences and the like. Only matters of lesser importance are decided by the leaders alone; the more important by the whole body.

This participation of the individual members of the community in public affairs is so profound that their life-activity may be said to be made up of war and the popular assembly. Between whiles they sleep and eat and idle, while house and fields are left to the care of the women, the aged and the infirm. Such is the life of these men.<sup>1</sup>

§ 21. For the purposes of a discussion introductory to the Science of Finance the meaning of this primitive form of the political structure may be indicated as follows: It is the embryonic form of public obligation which contains the germs from which the various elements of the developed public economy are evolved by a process of differentiation.

In the first place, the personal factor is, at this rudimentary stage, still undifferentiated from the material [*sachliche*] factor. The individual member of the community not only contributes his personal service in the army, he also brings with him into the field whatever is required in the way of arms and accoutrements; for these he carries as his own from the day when, having reached manhood, he is publicly invested with them in the assembly of the people as a symbol of his public dignity and obligation - as a mark that he has become part and parcel of the state.<sup>2</sup>

A second fact is closely related to this first.

The man's participation in the affairs of the commonwealth has not yet been differentiated into honor or privilege on the one hand and burden or obligation on the other. It is true, we are told by the writers on law that public law is distinguished

<sup>1</sup> Tacitus, *Germ. cap.*, r5.

<sup>2</sup> Ante hoc domus pars videntur, mox rei publicæ. - Tacitus, *Germ. cap.* 13.

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from private law by the fact that in the former every right on part of the individual is at the same time a duty, and every duty a right. It follows from the nature of an abstract conception of the state which is guided by the requirements of certain accepted ideals rather than by the facts, that it should more or less consciously blur the clearest distinctions that are brought home in a very sensible degree to the men of the modern state. In the primitive state this distinction is not present, or at any rate it is but faintly perceptible. The great functions through which the state becomes a living entity in the activity of its members - military service and the popular assembly - are still, at this point of development, both privilege and obligation alike. The opening of the assembly may be subject to delay for some two or three days because the men do not assemble punctually at the appointed time (this is evidence of a lack of discipline according to Tacitus, a result of liberty, of the absence of authority), - but so little does this go to show the contrary, that the significance attached to participation in the popular assembly by the free men of that time is to be taken as evidence of its being considered both an honor and a burden. Later on we find that the laws of the German people impose severe penalties for absence from the popular assembly, relics of which have survived down to modern times; but this again is but evidence to the same effect, though it does at the same time indicate a decreasing appreciation of the element of honor and privilege involved.

§ 22. Finally there is the third fact, of a division of labor in the work of the State - if we may employ the expression in its broadest sense - which comes in to disturb the primordial type of the primitive commonwealth and develops differences and contrasts which are absent at the outset, or at most are present only as imperceptible beginnings.

There are elected leaders, there are illustrious families, but there are no rulers and no subjects. The element of authority finds its field within the household of each individual citizen. The head of the household rules over wife and child, over the

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aged and infirm, over servants and slaves, but in the state there is no such sovereign authority. What there is of authority and subordination is nothing more than that necessary minimum of order that is indispensable even under conditions of the greatest and crudest freedom, if anything in the way of a commonwealth is to be possible at all.

On all hands there are visible the initial stages of a differentiation that speaks of future culture, and without which even a very low form of social life is impossible. But the fundamental and characteristic fact remains that the work of the community is done directly by the members of the community, and without separation into a class to whom service is rendered and another class by whom the work is performed.

Incipient differentiation is perceptible in the consideration shown the priests, as also in the influence exercised in the popular assembly by those who are distinguished for deeds of valor or for superior sagacity. The decisive word, however, still lies with the assembly as such; the speakers are listened to and the decision is then made.<sup>1</sup>

In war there is of course a leader at the head of the expedition, but the leader and those whom he leads compete on common ground for the palm of bravery. It is a lifelong disgrace to "outlive one's leader - "the leaders fight for victory, the followers for the leader."

§ 23. No doubt this delineation of a primitive commonwealth, even apart from the Roman historian's studied contrasts, has a charm for any thoughtful observer of political and social life. It appeals to us with all the bracing vigor of a breath from the primeval forest. Unfortunately it is impossible - it is contrary to the nature of all normal, historical evolution that this primitive community should ever meet the demands of advancing culture.

Let us first take up the point last mentioned.

If it is true, as our best thinkers claim, that history is to be conceived of as a record of the education of the human race, then

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<sup>1</sup> Auctoritate suadendi magis quam jubendi potestate. - *Germ.* cap. 11.

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there is little hope that any autonomous association of peasants should ever be able to rise from their primitive rudeness to the full fruition of the potentialities immanent in humanity simply by a spontaneous exercise of their sovereign will.

Stanley<sup>1</sup> relates of Mtesa, the despot of Uganda, that he stood high above the plane of culture occupied by his people. To him alone was it due that a stranger could enter the kingdom of Uganda, as his people had not the slightest regard for human life or human right. The revolting atrocities of the despot were necessary in order to hold the plundering, thieving, bloodthirsty people in check. As a companion piece we have the account given by another traveler<sup>2</sup>, of the cannibalism raging in the free republic of Hayti, against which the authorities were afraid to take any measures because of the republican institutions of the country.

More fortunate circumstances in the way of culture or of natural surroundings may have availed to raise one people to a plane of development as much above the plane of others as the Germans of Tacitus stood above the Negro tribes of Africa; but the interval is never so wide that the salient fact expressed in this contrast loses its significance for any people whatever.

That is to say in other words: the relation of ruler and subjects is a condition indispensable to any people that has an historic mission to fulfill.

§ 24. While this contrast may originate in the difference everywhere observable between the higher endowments or nobler descent of certain individuals than of the majority of the people, it is also true that a progressive division of labor takes place, to correspond with the growth of the mass and the increase of the duties of the commonwealth, beyond what may suffice for the first crude beginnings.

Every widening of the extent of a small commonwealth of itself gives rise to the problem of the state, in that it removes the

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<sup>1</sup> *Through the Dark Continent*, vol. i, p. 408.

<sup>2</sup> Spencer St. John, *Hayti*, (1881).



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individual farther from the periphery of the aggregate. The problem lies in the question, whether the individual, from the standpoint of his own daily life, is capable of comprehending the interests of the aggregate. All the past experience of humanity has gone to enforce the fact that whenever a commonwealth of free citizens has made any approach to a realization of its ideal, the indispensable condition of success has been that of small extent, and that every increase beyond the original narrow limits has also carried with it a dissolution of the primitive constitution of the state. Such has been the course of events in Greece and Italy; such also in the countries of Germanic Europe. This distance between the individual member and the environment of the community is further increased by the changes that take place at the other end of the scale, in that the course of evolution of the life of the individual results in an intensive culture. The indolent hunting tribe, which has not yet achieved steady habits of labor and knows no other activity than that of war and the chase, finds in this crudest form of participation in the affairs of the commonwealth the gratification of its impulse to action. An agricultural people with habits of industry, which has mingled its sweat with the soil and which guards house and home with a jealous hand, has therewith made so much of an investment, and this the interested individual balances against the claims of the commonwealth.

An intenser culture and an increase in the extent of the commonwealth accentuates the problem of the identity of the state and its individual members. The result is that with every step in the growth of these two factors the inherent contrast between man and the state finds expression in corresponding institutions calculated to bridge the interval. The sentiments, capacities, services, which the state requires are, as it were, segregated out from the body of citizens as such, and make their appearance as a plastic precipitate in the form of distinct classes and professions which the state sets apart for its own purposes. It is true, they continue to be constituent parts of the people; but they are parts specialized for political functions, and differen-

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tiate themselves continually more and more from the mass of the people, who for their part continually lose more and more of their civil character.

§ 25. The course of the resulting development varies from one period to another and from one people to another, but the essential features are everywhere the same. To the extent to which the conditions are present, to that extent the consequences will also follow.

In every case it is a gradual transformation in which certain features of earlier times long continue recognizable, in spite of constant change, but in which the successive stages are always closely linked together.

Whether we pass in review the thousand years between the founding of Rome and the final full development of the bureaucracy of the Roman Empire, or trace the permutations of the Germanic constitution in the states of Europe from the fall of the Roman Empire down through the Middle Ages to modern times; whether in the one case we examine in detail the contrast between the plebeian and the patrician classes of Rome, between the optimates and the mass of the people, between the emperor, senators and bureaucracy on the one hand and the populace of Italy and the Roman provinces on the other; or whether in the other case we watch the development of the aristocracy and the professional official class out of the germ of *nobilitas* and *principes* among the Germans of Tacitus as organized in the service of the king after the Roman model, or bound to the glebe in the legal bonds of the feudal state, or under the form of the professional official class of the oncoming régime of absolutism, in peace or war, in judicial or executive office; - all is but the outgrowth of a single fundamental idea.

A consideration of all these facts brings out two points of importance to the modern state: first the necessity of a high degree of division of labor in the work of the state, which results in a constantly increasing separation between the body of citizens and the actual, effective political activity; second the inex-

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tinguishable reminiscence of a primordial union of citizen and state: The historical development has brought about a progressive evolution of the former, at the same time that the latter has never ceased to be present to the eyes of humanity. During the very same centuries of the Middle Ages when the way was being prepared for the monarchical state and professional officialism, there arose in the mountains of Switzerland a reconstructed model of the primitive democratic commonwealth, while at the same time a different type of a free community, more nearly approaching the requirements of modern life, grew up in the mediæval towns.

§ 26. Viewed from the financial standpoint, the division of labor in the work of the state results in a relation of the individual to the commonwealth in virtue of which the individual figures as the beneficiary of a number of services rendered by the state; services which in the primitive form of organization are performed directly by the individual members of the community.

It now becomes a problem how these offices of the state which serve the needs of each individual citizen, are to be compassed by extraneous means, after the direct and spontaneous participation of the citizen in public affairs has apparently ceased.

These extraneous means may be of various kinds. The simplest is the adoption and consistent application of the method which the division of labor has brought into vogue in industrial intercourse in all the economic relations of life: paid service for which a compensation is rendered in economic goods.

As a matter of fact this simplest of all methods, consistently with the general course of economic development, does find an ever wider acceptance as time goes on. Every highly developed commonwealth gives evidence of the presence of this relation of bargain and sale in an ever increasing degree.

But this is not all.

For one thing, there are to be found at every epoch certain

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survivals of direct political activity by the body of citizens. In the midst of that process of erosion by which a professional army grows out of the folk-army, some remnant of the universal liability to military service continues to assert itself. In the midst of state absolutism which negatives all participation by the citizen in the affairs of the commonwealth, the idea retains its vitality in the towns that it is the business of the entire body of citizens to decide on the management of municipal affairs.<sup>1</sup> Where the antecedents in the way of race character and historical experience of the people have favorably influenced the development of a commonwealth, the element of primitive popular autonomy retains a larger share of power and asserts itself in the struggle against the progressive division of labor.

Especially, the element of initiative and direct participation on the part of the body of citizens is awakened to a new life by any popular movement, - which is at its best nothing but an awakening on a large scale of the national spirit that has long lain dormant. And precisely this is the characteristic phenomenon of the present century. Not that this national sentiment has already attained a full consciousness of its own significance - we shall find in what follows that one of the chief difficulties of our finances consists in the inadequacy of that sentiment - but it can at any rate be said that a beginning has been made in our modern states which must either be a false step or must lead to further development in the direction indicated.

§ 27. The political activity of the body of citizens in the modern state ramifies itself in the following manner.

The substructure consists, significantly enough, of the group of activities which proceed on the supposition that the relation of the state to the citizen is that of an apparatus created to perform certain services for him. These activities are an exercise of the rights of suffrage and election, which can have no effect beyond a controlling interposition, and whose immediate office is simply

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<sup>1</sup>Ernst Meier, *Die Reform der Verwaltungsorganisation unter Stein und Hardenberg* (1881), p. 79.

to afford the aggregate of citizens a means of supervising the course of political affairs through the agency of their representatives. But a rational exercise of the suffrage and the right of election, and more especially an adequate supervision of the `affairs of state through their representatives, does not necessarily follow from the bare fact of the possession of civil rights by the body of citizens; as a matter of fact the capacity for an adequate exercise of these functions has to be acquired. This fundamental fact of political action therefore leads naturally up to a consideration of the facts relating to participation in the conduct of the every-day business of the state.

This brings us to that broad field of activity which we are accustomed to call "self-government." Within this field the citizen of the modern state is actually directly occupied with a multitude of public duties, quite in contravention of the principle of division of labor that dominates both private and public life, or at least his activity supplements the action of that principle.<sup>1</sup> The simpler the duties, the more moderate the requirements in the way of capacity and energy on the part of the citizen, and the more independent the working of self-government; the more serious the duties, the greater the requirements, the more will the local self-government have to depend on the skilled and organized forces of the national administration. The administration of a small rural commune to this day rests in, or has at the present day reverted into the hands of men chosen from among the inhabitants of the place. In the administration of an urban commune, the larger the commune the more help does the element of self-government require from the highly differentiated professional element, and the greater, consequently, the demands on its administration.

A third field is the great and burdensome one of military service. All the way down from the beginnings of German antiquity, with its folk-army gradually transformed by elevation and depression of classes, differentiated into a contrast of armed freemen and unarmed bondmen, then developed into a military pro-

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<sup>1</sup> See vol. i. secs. 246-247.

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fession for the upper classes, followed in turn by an epoch of mercenary armies and professional soldiers, through all these mutations in the development of the state, military service has remained a duty incumbent on the entire male population. Only, with the new era it has been reclaimed from its lowly and degenerate state, transfused with a new life and invested with a new dignity. After it had for centuries served to characterize the lowest social class, it has become again what it originally was - a universal duty of all able-bodied citizens.

In view of the difficulty of the problem involved in securing the defense of a modern state, the relation of this portion of the citizen's public duties to the unavoidable demands of a division of labor is naturally a very peculiar one. A juryman or a justice of the peace on whom the local self-government devolves the administration of justice, is, according to the premises of local self-government, endowed with an average capacity for the office simply in virtue of his character as citizen. The conscript on the other hand is so far subjected to the demands of a division of labor and of the professional nature of military service, as to be held for a long series of years to the strict discipline of the army very much after the fashion of the professional soldier. Division of labor in the work of the state here trenches so far on the domain of division of labor in private life as to take the citizen away from house and home for years together, simply in order to teach him what belongs to the adequate performance of military duty.

§ 28. While this enumeration covers the chief kinds of personal services rendered the state by the modern citizen, there are certain further considerations to be brought out in the same connection.

In the first place there really is in the modern state, as in the states of the past, a sphere within which what we have held up as contraries are to be found united. It happens even to this day, under a peculiarly favorable conjunction of circumstances, that the demands of modern public life in the way of professional

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devotion to the public service, meet with sentiments and conditions such that this vocation is not only adequately recognized to be the logical consummation of the duties of citizenship, but this recognition is also adequately carried out in practice. Wherever there exists an aristocracy which is possessed of an adequate comprehension of its own mission - the devoting of its energies to the conduct of public affairs - and is at the same time possessed of such economic means as will enable it to put forth its energies, not in the character of a paid official class, but with the independence that goes with an "honorary office," there the point is attained where the primitive ideal of civic duty coincides with the intensity of application required in the work of the modern state.

While among the rude men of the commonwealth of Tacitus the charm attaching to adventuresome deeds of violence was a dominant factor in determining the direction taken by the people's activity, it may surely be hoped that at our present advanced stage of culture habituation to work through a period of a couple thousands of years has extended this charm to other activities as well. In point of fact, amidst the great complexity and intricate gradation of activities in the modern state it is not to be overlooked that there is a decided variation in attractiveness as between the different kinds of activities.

I may here refer back to the conclusions reached in the general portion of this work (vol. i. secs. 135-137). The intrinsic attractiveness as well as the dignity attaching to the work varies according to the nature of the occupation. The "honorary office" [*Ehrenamt*] will therefore begin only at a point where a certain measure of this element is reached. The office of member of parliament, or of the head of the affairs of state will partake of this character; whereas the designation can have but a negative application when the office of juryman or justice of the peace is spoken of as an honorary office, - that is to say, negative in the sense of denoting the absence of compensation rather than implying a positive sense of dignity that leads the citizen to seek the office. Still lower in the scale of occupations,

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in the services performed by the constable or policeman, no efficacy whatever can be ascribed to the pleasure or dignity of office. And even of the grave duty of the defense of the fatherland an effective sentiment of this sort can be counted on, if at all, only in seasons of patriotic exaltation, certainly not through the tedious years of preparation and training.

The consequence is this. The aggregate of personal services required of the citizen by the commonwealth must appeal to different psychological motives according to the different tastes and sentiments of the citizens.

§ 29. As to details we find considerable variation from one country to another. Political usages, inherited differences in the tenure of property and in the social features connected with it, the form of the constitution of the state and the administrative mechanism, and other like causes, have resulted in variations which come to figure in the eyes of the one state as national peculiarities attaching to other states. The practical working of the state mechanism within the lines imposed by these peculiarities, then, suggests the question whether this or that existing institution is the more serviceable. But after allowing for these national variations there remains for any given epoch a certain essentially common ground, in consequence of which services of a similar character come to be performed by means of similar contrivances.

The great contrast in point of psychological motives that is brought out in political institutions is the contrast between voluntarism and coercion.

Not that the system of voluntarism on the one hand and that of coercion on the other comprehend each a homogeneous mass of sentiments; there is no such uniformity either as regards the sentiments of the individual citizen or as regards the different classes of activities. But this much is true, that there are certain comprehensive groups of activities with respect to which we can say that in order to a given result a given pressure is required, whether the motives appealed to be external or subject-



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ive. And just as the subjective motive has at its disposal impulses of greater or less intensity, so also may the appeal from without, the factor of coercion, be of different degrees of energy. In the former case we have the great attractiveness of the foremost offices of the state contrasted with the feeble inducements offered by obscure honorary positions in the everyday service of the community; in the latter case we have the slight penalties attaching to neglect of jury duty as contrasted with the severe penalties of the military code against deserters.

The exacting coercive measures adopted as regards the fundamental - and the greatest - duty of the citizen contrast significantly with the conditions that prevailed during the early stages of political development. In the early days war was the man's chief occupation, invested as it was with all the charm which its contrast to steady work lends it during those ruder stages of culture; while today peaceful industry is the central fact of life, and military service is an unusual employment which the peaceable citizen avoids as far as may be.

The exacting demands of a highly developed military art also require a strictness of discipline which cannot at this day be enforced without forcible coercion, except in cases where an unusual degree of national sentiment is present.

§ 30. It is moreover highly characteristic of the development of the social substructure of a modern state, that the exercise of precisely this most important of all the functions of citizenship cannot be required at the hands of the modern citizen without the intermediation of an economic factor.

True, the new era, with its rehabilitation of citizenship, has infused a new spirit into the duty of military service handed down from past centuries. Liability to cantonment on part of the lower classes of the population has, by virtue of the new democratic ideas, been developed into the general liability of all citizens to bear arms. But the development of this ignoble service into a duty of citizenship, the conversion of what was a one-sided burden into a privilege belonging to all citizens alike, has

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not altered the traditional economic basis on which the structure of modern life in state and society rests. The altered spirit, the altered sense of dignity with which the majority of the people meet the requirements of the common defense today, still leaves the fact unaltered that this same majority are economically incapable of rendering their personal service to the state, unless the livelihood for which they usually depend on a society organized on a basis of division of labor is furnished them by a similarly organized state.

At this point, therefore, the material factor enters as a menstruum into the system of civil activities and duties. Only for a small portion of the aggregate body of citizens is it possible to offer their personal service to the state on the basis of their own possessions, as is seen in the so-called volunteer service. For the great majority, who are accustomed to live by the labor of their own hands and who lose their livelihood as soon as their labor ceases, means of subsistence furnished by the state must be supplied.

We have, consequently, a combination of the personal service of the citizen with a material factor which has to be drawn from contribution made by the entire body of citizens.

This is the point at which the modern concept of democracy diverges from that of antiquity. The early, original view conceived the state to consist in the equal participation of all men; this equal participation being possible on the basis of an equality of social conditions. The modern concept of a democracy on the other hand sets out with the undeniable fact of social inequality, the fact of the pecuniary feebleness of the majority, and those measures are now-a-days called "democratic" by which the state seeks to come to the aid of this economic incapability. Where the ancient concept of democracy, owing to specially favorable circumstances, has maintained itself down into modern times, as in the cantons of Switzerland, the ancient usage has continued in force down to the present, the man who is liable to do military duty being required to provide his own equipment, and only very lately has the old usage yielded before

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the neo-democratic principle. In ancient Rome it was, significantly enough, the Gracchi who were the advocates of this neo-democratic reform. While the senate had enacted, in laws dating from the years 406, 403, 401 B.C., that citizens serving in the infantry were to be paid out of the public funds, it is a law of Caius Gracchus that for the first time directs that the clothing of citizens liable to military service is to be furnished them gratuitously by the state.<sup>1</sup>

§ 31. This undermining of the earlier democratic concept of the state by the modern social organization and its division of labor comes out even more distinctly when we consider that not only has the great body of the lower classes become unable to contribute their service to the state without pay, but that even for the higher classes a system of payments for all kinds of public service gains ground continually more and more, in so far as this service interferes with the everyday business of private life beyond a brief occasional interruption. Hence the payment (allowances, mileages) even for the highest and most honorable activities in political life, - a payment due to the exigencies of modern society which continually leaves a relatively smaller number of its members the leisure required for the business of the state, at the same time that it finds it desirable to afford a continually larger number of its members access to a participation in the state's business.

Modern society has not yet passed through the final stage of this development, though antiquity has done so in the decline of its republican institutions, both in Rome and Greece. The point is reached when even the last shriveled residue of public activity, the bare attendance in the popular assembly, is paid for out of the public funds; when the place of the privileges of citizenship is finally usurped by a public alms.

Modern states will be wise enough to avoid this final consequence of deterioration. But in the situation as we find it, the

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<sup>1</sup> See a paper by the present writer on "Ehre und Last in der Volkswirtschaft," (*Volkswirtschaftliche Aufsätze*, 1882, p. 350).

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unavoidable necessity for any modern state of employing a system of material compensation in order to insure the exercise of the personal duties of citizenship is manifest. This material compensation is nothing but the economic equivalent of those personal activities which, having themselves come to bear an economic character, require an economic return.

§ 32. The considerations brought out in the last few pages bring us face to face with that great system of economic ways and means [*Leistungen*] on which all modern states rest. However imperative the need of participation in political affairs in the present century may be; however indubitably every reasonable gratification of this demand may lead and may have led to a progressive development of the citizens' political activity; the fact remains after all that the growth of the economic character of modern state activity comes constantly more and more into the foreground. In other words, the state is developing a constantly growing public economy, based on the exchange and circulation of economic goods.

It lies in the nature of the division of labor that it acts constantly and progressively to erect each particular form of activity that serves the purpose of society into a distinct trade standing in economic relation to all other occupations. And the state itself partakes of this development, in that the special services it renders are offered in the form of professional performance of the work of the public economy, in exchange for all other kinds of work. But since the underlying principle of industry requires that these services be paid, there arises the need of material wealth (money) that will serve as an equivalent for this work in this as in any other business transaction.

But this covers only one category of the offices incumbent on the state.

A second category is constituted by the material apparatus required in order to the proper exercise of the personal activities that make up the state's work. It is only in the early beginnings of political organization that courts of justice are held under the

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open sky; a civilized state requires extensive structures for the purposes of the administration of justice. It is only in the first rude beginnings (of which, it is true, survivals may be found here and there in our civilized communities to this day) that offenders are punished with the summary severity that dispenses with the expensive structures and maintenance of prisons. It is only the folk-army of primitive days that is acquainted with no breastworks but what are thrown up on the spur of the moment; the progress of the art of war, and more distinctly still the stupendous development of military science in modern times, involves the sinking of a continually greater portion of the nation's wealth in fortifications, strategic roads, naval vessels. The modern phase of public economy is characterized throughout by an increase of the capital invested in material appliances, and these serve to indicate what is the current conception of the state's function. Our schools, universities, museums, libraries, archives, etc., may be called to mind.

§ 33. We shall accordingly have to conceive of the public economy after a fashion analogous to what we already know to be true of the economy of the people in general. In the foreground we find a great mass of industrial goods, industrial exchange, industrial capital, growing greater with every fresh advance of civilization; in these latest times so markedly occupying the foreground that current popular opinion sees nothing but this phase of the matter. Beside this and diffused through it, barely manifest, or at any rate quantitatively inconspicuous, we have that multitude of non-economic potentialities which derive their force from motives of a higher order and figure as the gratuitous effects of civilization. It is also not progress simply as such that fosters this relatively great development of the economic factor in the state; this phenomenon is referable to a one-sided progress within the particular epoch of cultural development in which we live. A development of a higher form, which shall leave this stage behind, is not only possible; it lies within the sweep of the modern concept of the state, and it

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is even distinctly foreshadowed by the contradictions existing in modern national life. However, for all practical purposes, and for any period of time that it is necessary - here to take into consideration, the public economy remains the central fact of national life. Indeed, the most immediate problem in actual practical affairs concerns the inculcation of such an intelligent insight as shall comprehend the reasonableness and the necessity of this traffic on the part of the state, in order that the individual citizens may come to live up to their duty as loyal members of the commonwealth.

For, spite of all declamation about political liberty and the dignity of citizenship with which our century resounds, the modern man still falls so far short of the true political disposition and political insight, that it will yet for a long time continue a difficult and necessary task to impress on his stubborn spirit the utter necessity of the state, and, since he is neither willing nor able to devote his energies to the service of the state, to bring him to an honest recognition of the economic consequences for the state, that result from the modern system of division of labor in private and public affairs.

The following pages are an attempt to contribute what I may toward this end.

## II. THE DEVELOPMENT OF THE FUNCTIONS OF THE STATE.

§ 34. A discussion of the functions and the purpose of the state from the point of view of the underlying principles may quite as well start from the question as to what classes of activity the state should leave to private initiative, as from the correlative question stated from the opposite point of view, viz., what functions the state should assume in order to round out the individual life of its members.

Every investigation that proceeds from the historical standpoint sees in the state a process of growth, in the course of which both the structure of the state itself and the trend of development in the social life of the community undergoes a progressive adaptation to the requirements of the unfolding

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national life. The meaning of the state's activity, the bearing of the so-called encroachment of the state upon the private life of the society which it comprises, is ever conditioned in the course of this historical development by the stage of culture already attained at any given point of time. So that the degree of culture attained at the same time indicates the height and amplitude of the state's proper activity; a scanty culture expresses itself in a scant measure of national development. For this reason any discussion which aims at an elucidation of the general principles which are to govern the limits between state action and private initiative will be futile if it does not take account of this process of historical growth. It is only on the basis of a definite consciousness of social aims, and therefore only on the supposition that a certain definite stage of culture has been attained, that we are able to say anything as to where and why the line should be drawn.

We must also not allow ourselves to be deceived by the possibility of fluctuations to one side and to the other in points of detail as to what matters the requirements of advancing culture may intrust to private initiative on the one hand, and to state action on the other; the main fact remains that what we have to do with is an ever swelling stream which irresistibly carries forward the progressive development of the functions of the state, - provided only that the general culture continues to advance.

It may very well happen that in matters of detail the state will withdraw its hand from a variety of activities, or at least that the hand of the state may not continue to bear upon a given point with the same weight as before; but this is nothing more than such an alteration or contraction in the aggregate functions of the state as is much more than compensated for by the multiplicity of new duties which an advancing culture is continually urging upon the state on every side.

It is therefore true that a comparison of our own times with the state of the last century gives the impression that a preponderance in the degree of state activity and state control rests

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now on one side, now on the other, - here with the earlier, there with the later era. Which term of the comparison is to carry off the palm will depend on the point of view from which we contemplate the old times and the new. The preponderance seems to belong with the earlier state in so far as regard is had to the recklessness with which, in the earlier times, the life of the individual was constrained by the superior discretion of the administrative authorities - the degree to which, in the thousand and one petty affairs of everyday life, of business and pleasure, of morals and religion, the magistracy meddled with pedantic hand. But the picture changes as soon as attention is called to the fact that the space afforded by the widening of the sphere of private life and the corresponding lightening of the duties of the state has been filled by a body of new state functions, which may, in principle, have been contained in the theory of the earlier state, but which still are of so novel a character and of such considerable magnitude that, taken altogether, the ancient state and its economy are dwarfed by comparison with the state of the present.

§ 35. But *magnae molis erat romanam condere gentem*. From the beginnings of national development to the stage at which we stand - even though that point is very far short of the consummation of development - is a long and irksome way. J. G. Hoffmann, in the introduction to his *Lehre von den Steuern*, very aptly says: "The delusion that security of life and property, the productivity of labor, and the consequent possibility of acquisition and enjoyment, and even the elevation of the spiritual and the ennobling of the moral nature - that all these good gifts come to man in the guise of gratuities, is itself a proof of the advanced stage of culture which the greater part of Europe at present occupies. As the grown man has long since forgotten the pains it cost him to learn to speak, so have the peoples, in the days of the mature growth of the state, forgotten what was required in order to free them from their primitive brutal savagery."

In point of fact, how significant was the involuntary testimony



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which the eighteenth century, with its repudiation of the historic state and its yearning after the primordial state of nature, bore to the blessings of the inherited culture which it ungratefully enjoyed. For the yearning after a state of nature was possible only on condition that all those achievements which separate man from the real state of nature were assumed as spontaneously existing. The craving was for an escape from the refinement of a civilization which had turned its back upon nature, but by no means for a return to the actual conditions of primitive culture, to the "primitive state of Nature, where man is man's enemy"; it was a craving for a paradise of amiable innocence and simplicity, such as had for thousands of years filled the childish daydreams of the peoples. It was in fact an instance of that oft-noticed optical illusion of the human spirit, by means of which the images seen by poetic fancy in the remote future are reflected back into the remote past; an illusion which was made possible by, and which will ever recur as an outcome of, a method of historical study that sees in the past not so much what has actually taken place as what it is thought desirable should have taken place. Accordingly it also came to pass that the word "Nature" acquired such a shifting, iridescent sense as to leave it uncertain whether it was not employed rather as an expression of the demands of the new departure than as a serious claim with respect to the character of what lay in the past. And as a matter of fact we have come to see in the course of our *Grundlegung*, (vol. i.), that the concepts of "Nature" and "Natural" as employed in Political Science have long been in an unsettled state, and have only lately acquired a substantial consistency through the means of profounder research.

§ 36. It lies not within our power to reverse the current of history. But each succeeding period in the course of history contains in itself the whole stupendous difference between one epoch and another, in that it comprehends a variety of races and of state organizations.

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The eighteenth century was by no means without a knowledge of and an interest in this sort of comparative study. And all the more remarkable is the dominant influence exerted by the veil through which they were wont to see these obvious facts and in virtue of which their affections went out toward the fancied innocence of the "children of nature." An historical research of such abundant fruitfulness has by this time so prepared the way for our study that the daily increasing wealth of observation of primitive stages of culture which not offers itself affords us a veritable laboratory of ethnology.

And this not only speculatively. An increasing commercial intercourse with such primitive races, in which also the German people is now daily coming to be more and more concerned, affords abundant opportunity in practical life for modern civilized man to rid himself of the illusions which have veiled the actual course of national development from his eyes. It is brought home to him immediately in his own person - as a matter of life and limb - what a debt of gratitude he owes for the security afforded by that ancient fatherland from which he has taken his way out into the outlying regions of humanity as it exists in a state of nature. The horrors of primitive savagery which threaten him, and which make all life precarious from day to day, help him to appreciate the enormous interval between his home and his foreign environment. Here, in the absence of state organization, he learns to understand the hard necessity out of which sprang the earliest efforts of mankind in the direction of order and security.

§ 37. This primary need, which so laboriously lays the foundations of all human development, furnishes an explanation of the fact that the culture of all peoples is for many centuries of its earlier stages occupied with the establishment of authority and order. These are the necessary conditions of growth for any higher or more complex culture. Such is the case even under the exceptionally propitious circumstances of that favored branch of the human race which has occupied the foreground, or rather

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has alone occupied the stage of history. In the meantime the great number of other peoples have never succeeded in establishing this primary condition, but on the contrary, in their attempt to lay a secure foundation for an orderly-social life, have been toiling and struggling in vain from the very beginning down to the present under the never-ending curse of pristine violence.

European humanity, destined to the attainment of a highly developed culture, has, during these last centuries, reached an amplitude of national development which seems very far removed from the rudeness of primitive times. But this European humanity has also passed through a protracted struggle, and the sole effort of their states for a long time past has been directed to the establishment of that reign of order under which each individual citizen rejoices in the security of person and property.

§ 38. The well-worn concept of a "civil-legal-state" [*Rechtsstaat*] is sometimes contrasted with the other concept of a "police-state" or a state organized for the public welfare, or again, with the "culture-state." This shifting of the contrast shows that the content of the idea is a variable one. In the form in which it has been handed down to us by the philosophy of the last century, the idea covers simply that fundamental function of the state which secures to each member of the social organism the enjoyment of his rights. The second meaning of the "civil-state" which has been brought into the foreground in our own time on the contrary has come to terms with the more comprehensive modern range of state activity, and has accordingly no quarrel with the "welfare-state" or the "culture-state," but quarrels only with the "police-state," and even this only in the more objectionable sense of the word; that is when it is used to denote a state that rules by the method of arbitrary discretion as contrasted with a state that governs under the forms of law.

Even our political terminology has been at great pains to emancipate the concept of the earlier "civil-state" from the

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restrictions of its narrow meaning; still the service rendered by history in exhibiting to us the civil-state in this narrower sense is none the less important.

The most primitive institutions of the Germanic commonwealth with which we are acquainted do after all mean nothing further, than a coincidence of law with force. The individual member of the commonwealth enjoyed security for his own person and possessions just in so far as he, being an able-bodied man, could make his claim good. The coincidence of the franchise with the ability to bear arms is a simple consequence of the conditions in which the primitive state is placed. What the modern poet expresses in high-flown words and in metaphorical language - "He alone deserves liberty, as well as life, who daily has to conquer it" - holds true literally of these peoples. Advancing human culture has not stood its final test until it has successfully abolished the necessity for this union in the same person of order and the force which secures it. So long as that has not been accomplished there is but this single alternative offered: either every man must put all his energies into the struggle for the prime necessities of life, or he will have to submit to living without these prime necessities and at a correspondingly degenerate level of existence. The course of history teaches that the solution of this problem calls for a process of many centuries' duration, in which progress seems impossible except by passing through apparent regressions.

§ 39. The progress and regress which we have in mind manifest themselves in the following manner.

In the first place there is always present a tendency to differentiation. In point of fact even the franchise belonging in common to all able-bodied men stands out in harsh contrast with the disfranchisement of menials, slaves and all who are physically infirm. Further development widens the chasm through the opportunities afforded by an increasing differentiation. The growth of population, the stationary character of settlements,

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the limited extent of the available land, the intensification, through growing complexity of social life, of the agencies tending to produce a rise or fall in the social scale, and not least the commendable habituation to steady and peaceful labor, - all these alienate the man more and more from an obligation which is held to consist in standing ready daily to assert one's right to life and property with armed hand.

In consequence there arises a separation of that part of the population which by inclination and aptitude continue to bear arms, from the others who by inclination or of necessity take to a peaceful life. Now since the possibility of such a life of peace is as yet a desideratum the conditions for which are wanting, inasmuch as a defenseless, peaceable element in the midst of this rude environment is at any instant exposed to an armed, unpeaceful element; therefore there is but a single expedient at hand, namely, the submission of the peaceable element to the force of those who bear arms.

Nothing sheds so clear a light on this matter as the connection subsisting between two different kinds of allegiance which, it seems to me, have been conventionally placed in too sharp a contrast to one another: the relation of villenage and that of citizenship in the medieval towns. Not only that the duties of the lord in relation to the villein were expressed in the same form of words that served to describe the relation of the burgess to the town (the lord was to defend and champion the cause of the poor man, to succour and shield him); it is also to be noticed that the burgesses who removed from the town into the country accepted villenage as a substitute for the municipal franchise which they lost, or while still retaining the rights of the burgess they sometimes (perhaps on account of having frequent occasion to pass back and forth overland) acquired allegiance to some neighboring lord, in contravention, it is true, of the inhibition by the municipal council. And by preference allegiance was sworn to whomsoever was the most lawless in all the land, and men were wont to change masters according as they expected more efficient protection from one than

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from another. And all this took place as late as the fifteenth century.<sup>1</sup>

Peace and the security of person and property therefore appear here as a service which was tendered to and acquired by private persons as a matter of bargain and sale. The consequence of the situation was, as follows naturally from the character of the service rendered, that the one offering the service was the powerful party, the purchaser the feeble one.

§ 40. Evidently progress will consist in rendering possible the secure enjoyment of a peaceful life without the dependence of the weak on the strong. This can be fully attained only in that the superiority of the strong over the weak disappears through the growth of a peaceful disposition. But inasmuch as this would require an infinitely long course of progress from the beginnings of human social life to a millennium of peace, the question comes practically to concern itself only with particular stages of this progress, within which the purpose is in each case to widen the sphere of the peaceable activities and as it were to remove the element of violence to the margin of this widening field.

The City of the Middle Age is the prototype of a peaceable community in the respect that here for the first time, within very narrow limits (made possible by the adoption of industrial occupations), the interests that make for peace combine and fence themselves off by means of fortifications from the violence of the surrounding country. Wall and moat which serve to render a peace-needing, industrious community secure, are really the foundation of the state organization the end of which is the establishment of peace. There is of course still a demand for able-bodied burghers who are to man the breastworks and defend the town against the enemy; and also, of course, the peaceableness of the life within the walls is only relative, as contrasted with the turbulent world outside; but in this way alone is it pos-

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<sup>1</sup>Karl Bücher, *Die Bevölkerung von Frankfurt am Main im 14. und 15. Jahrhundert* (1886), vol. i. pp. 480-97.

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sible to make a beginning and redeem an oasis of peace from the waste of all-prevailing turbulence.

Further progress for centuries consists in what is equivalent to progressive extension of these town walls so as to create territories; states, kingdoms, whose essential nature in so far as concerns their relation to the towns expresses itself in the securing of a correspondingly wide field within which the peace is kept. While at one time a community of interest in the securing of a peaceable existence led people to shut themselves up within the narrow space of the town and so secure themselves against disturbance from without, there has, by slow degrees, grown out of these beginnings a domain of peace such as includes a commonwealth of thirty, forty, fifty millions of people; people whose life interests centre in peaceful labor, in peaceful industry and enjoyment, and who no longer are exposed to a disturbance of peace at the limits of the town but only at the boundaries of the nation. And this again is not the result of a process of nature, but a heavy piece of forge-work from the workshop of history, in which it lies to rise through progressive transmutation of the commonwealth to higher forms and wider spheres.

§ 41. Precisely because the serious hardships which were necessary in order to bring about the possibility of a peaceful organization of life are not tangibly present to the senses of the modern man, or because - fortunately for him - disturbances occur but infrequently to remind him of what he ungratefully enjoys in the placid flow of existence; for this reason he is, in good human fashion, inclined to take the good that comes as a matter of course, and only find fault with and feel the absence of whatever may still be lacking.

But the central fact of this evolution is to be sought at a point which lies without the conscious life of the modern man and citizen. To him it seems natural that he should inhale the atmosphere of peace every moment of his life, just as he inhales the oxygen of nature, - in truth it is the grand achievement that

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has come of the protracted efforts of culture in its struggle with primitive human nature. But while this unconscious acceptance of the attained security furnishes a striking testimony to the achievements of civilization, there is needed, in order to a theoretical insight into the intimate relation subsisting between public sacrifice and benefit, a consciousness which shall grasp the significance of past expenditures and more particularly of such expenditures as are still requisite to further this purpose. Great as is the advance already accomplished along this line, it can be maintained only at the cost of further continued great sacrifices. Indeed, the habitual bearing of heavy burdens in order to secure the peace, grave as they may seem, constitutes, but a relatively easy burden in comparison with the more painful and dangerous disturbances which would result in case these burdens were not submitted to.

§ 42. We have now seen how protracted a piece of work it is to elaborate the mechanism of a commonwealth which shall maintain tranquillity among men in place of the rude savagery of the state of nature - which creates such organizations as will suppress every disturbance of the peace within the bounds of the community, and erect an iron circle of defense against the threats of hostile forces from without. It is evident that this preliminary work will have to be accomplished before the state can turn its energies to other, higher, nobler purposes, which will thrive only under the shelter afforded by a state of peace. However, when this fundamental prerequisite has been compassed there are innumerable agencies in the developing civilization which will climb and spread over the walls of these great institutions established for the keeping of the peace. There is at hand the organized force which first came into being as an authority established to suppress the disturbing forces, but which, being present, is ever a powerful means for other purposes which may likewise need the aid of such a force.

This intimate connection of the fundamental function of the



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state with all ulterior purposes of the "culture-state" is sufficiently obvious. It is something in the way of a miracle, this segregation of a superior authority which, though itself originating from the multitude, still compels this multitude into the way s of an amelioration that runs counter to their natural instincts. But from the accomplishment of this segregation there follows as a matter of course a necessity that this superior power should take all tendencies for good under its protection.

A state of peace, however, is the soil in which such tendencies rapidly and plentifully increase. Indeed, it is worthy of remark how these tendencies venture out into the light of day even in the midst of an age when this preliminary work is not yet accomplished; as, e.g., already in the depth of the Middle Ages, in the midst of bloody feuds and daily deeds of violence, universities arose and arts and sciences were cultivated which presaged the coming of a happier era. And even more remarkable! We find that through all the centuries which separated the downfall of the classic world from the close of the Middle Ages, in the midst of the preliminary work required when the state was only beginning to take shape and emerge out of the rudimentary stage, the attempt was constantly renewed to recall to life the relics of ancient splendor. A series of attempts at reawakening into broad daylight the spirit of Rome and Athens, which have attained their results only after the state of later times has long ago trodden out its mediæval baby-shoes.

§ 43. A second point is worth noticing in this connection. We speak of the centuries of the Middle Ages as an evolution out of the beginnings of Germanic nation-making simply. But the influence of the civilization of antiquity affects the process from the first. These influences were not lost to European culture. Indeed, there evolved out of the bosom of antiquity an institution whose office it was to take into its care, and to instill into the new civilization in process of becoming, the sum of all past achievements in religion, morals, art and science.

This was the Church.

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The church is one of the most intelligible means for solving the riddle of the elevation of refractory man from a state of nature to a state of peaceful civilization. Indeed, taken in a general sense, this is the means by which the nobler impulses of crude human nature are awakened to life, by which the heritage of earlier culture, fortified by authority, is transmitted to the peoples of a later day. Through the church, then, comes about an habituation to the ways of peace; through the church comes also the fostering care of all those things which are first made valuable by a state of peace. Nearly every branch of activity of the modern state in so far as concerns that fostering, furthering, helping activity which bears upon the processes of productive industry, on science and art, on the higher and lower education; on charities and the care of the sick, was either exercised or outlined in the activity of the mediæval church.

For centuries together it has been the church alone that possessed adequate power, and at the same time occupied the requisite standpoint for enterprises of this rank. And it is only after the church has brought it to pass that such duties are understood and such forces engendered in the world outside, then only does the state undertake to supplant the church.

The co-ordinate position which the church of the Middle Ages occupied beside the state is due to this fact. The mediæval church performed duties for civilization which served not only to supplement the yet incomplete state, but also, by its appeal to a higher court, to reach out beyond the state's sphere of action. But so soon as the state has itself become possessed of these elements of civilization it comes to refuse acknowledgment of the need of any such supplemental agency or of any authority which transcends its sphere. The state does not deny the significance of the ecclesiastical functions nor the authority to which the church appeals, since it transfers both to its own domain.

§ 44. It is a characteristic of the state, in the form in which it has developed since the sixteenth century; that it reaches out

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with a long arm and takes all the activities of life under its care. The state of classic antiquity, typified by the Greeks and developed by the Romans into the powerful bureaucratic state of the later empire, has also become the model for the modern state. The state is again becoming or is about to become what it then was, - the highest organ of human social life.

Herewith we have already seized the position that whatever is a vital factor in the existence of the individual citizen is also a proper object of state action. It is not the difference in aims or interests that serves to distinguish the sphere within which the state administration should further the life purposes of the citizen, but the distinction between the two spheres, of state and of private activity, depends on causes which, under the particular circumstances of an age or a people, serve to give the one sphere a preponderance over the other. I may here refer to the statement of these reasons in the first volume (secs. 213-216), as also to the examination of the circumstances which lead "free competition" and corporate activity mutually to supplement one another (secs. 293-304).

If the state is constituted by the combined forces of the units which it includes, then its action will properly reach wherever the purpose sought to be accomplished is of such a character as to call for this consolidated force. We have satisfied ourselves that such a contingency is present in an extreme form as regards the great fundamental work of laying the foundations upon which that authority is erected which establishes peace and security, the prerequisites of all the other ends of life.

In close relation to this, and in dependence on it, is that further function which goes to secure or reinstate the peace of the land by decisions with respect to a violated or a disputed right. The institution of a superior tribunal which is to determine the objective right of a case as between the wrangling contradictions of private life, is essentially a matter requiring organized spiritual and moral forces.

With this convergence of spiritual forces it also becomes possible to establish such institutions for the development of the

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spiritual life as will realize as high a level of culture as is possible under the circumstances, and such as for this very reason overpasses the horizon of the individual. Hence arises the important function of public instruction.

The grounds for the consolidation of powers which the state brings about may also sometimes be found in the technical character of the contrivances which are to meet certain wants of society. In this connection we may call to mind the communal management of roads, inclusive of the means of transportation, whose peculiar nature makes it expedient to have a single concern minister to a considerable group of wants. In so far as great mechanical progress has latterly created a great extension of the work to be done in the direction last spoken of, the aggregate progress due to these improvements carries with it a tendency to concentration of forces which will affect the sphere of state activity, at least indirectly through its consequences. The greater, e.g., the consolidation of powers under the management of individuals, the more urgent becomes the necessity for bringing the mass of these interests into harmony with the interests of the community.

But after the state has created whatever institutions are thought desirable, there still remain a great variety of directions of individual activity, which may each in its own way serve toward advancing the consummation of human effort. Therefore does the superior spiritual and physical power of the state have to do with these also, so far as there may be need of help, support, prohibition, relief. Herewith we have indicated the whole domain of the controlling action of the state, which is in an especial degree a varying one and which in principle comprehends every sphere of individual life.

§ 45. I have already (vol. i. secs. 187-212) discussed the development of wants as a fact incident to advancing civilization. In this discussion it is not the range of wants - which is infinite - but rather the rational disposition and regulation of them in

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detail and the rational character of the aggregate selected that constitutes the central point.

With respect to the state, as concerns its various lines of activity, we are led to the application of the same principles which we have already become acquainted with in the general part of the work.

The characteristic feature of the state in respect of the development of its wants consists in the superior rationality of the state as compared with the private economy of the individual. In the life of the individual the motive to a development of his wants springs directly from the natural impulses; it is only on the broad foundation furnished by supplies sufficient to cover the essentially primary wants that a higher culture can bear fruit in the form of nobler wants.

On the other hand, it is inherent in the nature of the state that its demands, taken as a whole, go through a clarifying process, or are the outcome of intelligent deliberation. Food, drink, clothing, shelter, amusement, social intercourse - these are the primary wants with the covering of which private economy is mainly occupied; peace, order, security, culture, relief, - these are the higher needs which are mainly served by the public economy.

While the state has for a long time past felt called upon to prune the superfluous growths of the system which serves the primary wants, it has on the other hand also become an awakener of the higher wants, in that it has created institutions for education, science, art, charity, sanitation, etc. And not only has it awakened such higher wants, but in peculiarly urgent cases, as e.g., school attendance and legislation for protection of laborers, it has even made use of its power of coercion in order to create a general demand for the institutions which it has established.

§ 46. The increased range of public demand in modern times is especially due to two causes: progress in technical efficiency, and the spread of democratic ideas.

In the first place as regards technical efficiency. This is of peculiar significance for that branch of state activity which is pri-

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mary and fundamental, namely, provision for self-defense. This provision and solicitude comprehends in itself two distinct pairs of contrasted factors: the contrast between the means available for offense and for defense, on the one hand; and that between different commonwealths that stand opposed to one another, on the other hand. As a consequence of this relation, advancing technical efficiency means a progressive incitement to the achievement of further improvements on the basis of the improvements already achieved. Every improved means of defense calls for an improved means of attack; every advance in weapons of offense calls forth an advance in the means of defense. Technical knowledge, however, after it has once entered upon the course of development into which progressing natural science has carried it, serves the purposes of either side alike. It serves equally each of two opposing peoples, for it is a common possession of the age, and any advantage which one nation may today possess above another will tomorrow be surpassed by a fresh advance achieved by that other nation.

This race, kept up as it were by an automatic regulating apparatus so long as progress in technical knowledge goes on, of course presumes continually increasing sacrifices. And these sacrifices, as also the continued progress of the technology of war; is made possible by the ever increasing productivity of peaceful industrial knowledge. As fast as an advance is made in the technical knowledge of peaceful industry the technology of war stands ready to claim any new resource made available. This fateful inseparability of the two movements might be broken only by means of a radical change in the bearing of peoples, originating from within. And this inseparability of war and progress, it is to be remarked, is therefore a fact necessary to be taken into account for the present and for the future; for alterations so radical and profound as that referred to can take place only very slowly.

It is possible to contemplate with less mixed feelings those advances of technical knowledge which serve the manifold improvements and comforts of a peaceful existence. Compare the modern accommodations of an American house or of the Amer-

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ican metropolis with the ineptitude of a German provincial town; compare the contrivances for cleanliness, lighting, water-supply, street-management, etc. Notice the great progress which our cities have made or are on the point of making in this direction. Especially noteworthy is what our larger German cities have accomplished in this respect during the last generation, and the changes they are engaged in today. The progress of technical knowledge so intimately touches the primary demands of civilized life that also within this domain of peaceful industry the improvements of technology give rise to an increasing influx of new wants.

§ 47. Inasmuch as the class of improvements in technology last spoken of has to do mainly with amelioration of the conditions of life for the community, it will naturally come about that the democratic ideas of the new era will exert their influence in the same direction to hasten and heighten the effect.

The more widespread the concepts of human rights and human dignity are among any modern people, the more readily will the public bodies undertake to supplement the customary rights of suffrage with such social machinery as shall serve to elevate the culture-plane occupied by the lower classes.

It is not only a fact of great financial significance for our age that the common schools, the care of the poor, sanitary regulations, insurance of laborers, and other like enterprises have come to be recognized as properly public business. How great this significance may be depends, in the case of each commonwealth and at every epoch, on whether they comply more or less willingly with the ever growing demands made for these purposes. The subventions to the common schools, the care of paupers, etc., are evidently of a very extensile nature; and we may see how this extensile quality is put to the test under circumstances where the force of democratic tendencies is highly developed. But since the age is everywhere permeated with this class of ideas, in one country as in another, the continual increase of this class of expenditures is unavoidable and unmistakable.

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If it is true that the idea of equality achieves in the course of history a slow but ever progressing realization (cf. vol. i. secs. 312-16), and that our century constitutes a segment of distinct advance in this direction; then are these contrivances whose purpose is the elevation, physically and spiritually, of the lower classes by means of the fulfillment of certain fundamental conditions requisite for all culture, an essential feature of the process.



## CHAPTER II.

### THE HISTORICAL DEVELOPMENT OF THE PUBLIC ECONOMY.

LITERATURE. A. Wagner, *Finanzwissenschaft* (3. Auflage, 1883), vol. i. secs. 212-217, and especially vol. iii. (1886-88). Lorenz von Stein, *Lehrbuch der Finanzwissenschaft*, 5. Auflage, 1885, vol. i. pp. 103-174. Karl Heinrich Lang, *Historische Entwicklung der Teutschen Steuerverfassung seit der Karolinger bis auf unsere Zeiten*, 1793. Georg Waitz, *Deutsche Verfassungsgeschichte*, vol. viii. (1878). Rudolph Gneist, *Das englische Verwaltungsrecht mit Entschluss des Heeres, der Gerichte und der Kirche*, vol. i. 2. Auflage, 1868. The Same, *Englische Verfassungsgeschichte*, 1882. Gustav Schmoller, "Die Epochen der preussischen Finanzpolitik" (*Jahrbuch für Gesetzgebung, Verwaltung und Volkswirtschaft im Deutschen Reich*, 1877). The Same, "Studien über die wirtschaftliche Politik Friedrichs des Grossen und Preussens überhaupt von 1680-1786" (*Jahrbuch*, 1884-87). Sigmund Adler, *Die Organisation der Zentralverwaltung unter Kaiser Maximilian*, vol. i., 1886. K. G. Kries, *Historische Entwicklung der Steuerverfassung in Schlesien*, 1842. A. F. Riedel, *Der brandenburgisch-preussische Staatshaushalt in den beiden letzten Jahrhunderten*, 1866.

#### I. PRIVATE ECONOMY AND PUBLIC ECONOMY.

§ 48. The purpose and scheme of this book require that the discussion must no more here than elsewhere be allowed to lose itself in a multiplicity of details. All we can expect to do will be to describe the main lines of the historical development by which the public economy and administration has come into existence, and demonstrate the necessity of what has resulted; this will enable us to enter into the spirit of the resulting institutions and to understand how they have come to be what they are.

Early writers on the Science of Finance<sup>1</sup> distinguish the revenues of the state into those earned by the government and

<sup>1</sup> Rau, *Lehrbuch*, vol. iii. (5. Auflage), secs. 84-87.

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those levied by the government. The former are subdivided into the revenues from "purely private business" carried on by the government, domains, and receipts from government monopolies (*regalia*); the latter are divided into imports which are levied in case of particular transactions taking place between government and citizens (Fees), and imposts which are levied on the body of citizens simply on the ground of their obligation as citizens and without any special return service on the part of the government (Taxes).

Later writers on the Science of Finance have reduced this scheme to a gradation in conformity with historical development, in such manner that the course of development of the last few centuries - whereby the modern concept of the state as a public institution has grown out of the earlier legal concept of the state as a matter of private right and privilege - shall be reflected in the course of the progress of fiscal administration from its earlier status of personal income to its modern status of national revenue. As a matter of fact, such a gradational advance from manorial revenues to taxes is traceable. We may notice how in the first place the business enterprise of the state came to assert a privilege above private enterprises of a related character in virtue of the prerogative attaching to the affairs of the commonwealth. Then, before attaining to taxation as the means of revenue proper to the fully developed fiscal administration, there intervened a transitional stage of fees, which, indeed, are of a nature akin to the tax, but which still retain some features of the system of industrial income in their dependence on the relation between special service and special payments.

The unsatisfactory feature about this conception of the matter lies in its attempting to compass at one and the same time a presentation of the history of finance and an exposition of the modern methods of finance. This advance from the status of private economy to that of public economy may correctly describe the actual line of development in the course of the centuries; but the attempt to make the modern system of finance intelligible as a structure whose foundations are of the character

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of private industrial enterprise, while its upper stories are of the nature of public business, contradicts the requirements of that logic which conceives of the modern public economy in a manner analogous to that in which we are accustomed to conceive of the modern state as seen from the standpoint of public law.

Precisely as in the case of public law certain fundamental concepts - sovereignty, citizenship, etc. - constitute the premises out of which, in logical sequence, there follows the essential character of the modern state, so likewise must the fundamental principles of the modern public economy be sought, not in the gradation and stratification of the historical development of public wants, but in the logical relation of parts to a whole.

§ 49. The designation itself, which is in vogue even in the most recent works on finance, betrays the absurdity to which we have called attention. How is it admissible, we may well ask, to speak of a *Privaterwerb* on the part of the government of the modern state?

The following objections present themselves. In the first place there is the obvious reflection that in the modern state the concept "private" has a meaning only as opposed to "the state," and that it must accordingly be only in a special meaning of the word that anything which the state acquires can be called a "private income." What the government today acquires it acquires not only not as a private person, but not even from the motives or with the purposes which determine a private person in his pursuit of gain. For the difference of purpose and of point of view here indicated constitutes the characteristic fact of governmental action, and an appreciation of this disparity results in an analysis which immediately excludes the portions of government activity in question from the domain of finance. Domains and royalties are facts belonging in the financial history of the formative period of the public economy. In the fully developed economy of the modern state these institutions can continue to exist only on condition that some other basis be assigned for their retention than the fact that they yield a revenue. They must be

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viewed and justified from the point of view of public expediency: a point of view which differs radically from that which characterizes private economy.

In the second place, it is precisely the latest developments of socio-political and socialistic views that invert the whole standpoint of this so-called "private enterprise." So that the mode of looking at things which gives rise to this concept of a "private enterprise" on part of the state is completely turned around in the discussion between the advocates of private ownership and the friends of collective ownership. For if it is really to be the mission of the present and the future - to a greater or less extent - to widen the sphere of state ownership, then we are directly confronted with the fact that what has lately, simply in virtue of the incompatibility of its name with the requirements of the modern state, been figuring as a relic of the past, comes forward as the essential characteristic of the new social and economic order.

From this we have the following consequences. A systematic discussion of the public economy must either take for its point of departure public ownership and public enterprise as the basis of the satisfaction of the public demands: in this case the concept of "private enterprise" disappears altogether, not only as applied to the government, but also within its proper sphere as a means of livelihood for the body of citizens, since it rests on private ownership and private industry. Or conversely, the discussion of the public economy must start from the private property and private industry of the citizens - as happens at present; in which case the public economy comes to rest on the receipts which the private productive industry of the individual citizens will afford it.

§ 50. It is necessary to call to mind at this point that in the economy of the modern state private property is the fundamental fact on which - more or less consciously - the whole structure of the relations of the body of citizens is based.

This by no means excludes the possibility of a mass of public

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property being held in public ownership, whether it be as a survival of the past or due to the new era and its tendencies.

But even in the face of the undeniable fact that such public property exists in our modern states and communities; even though it is in fact, from a variety of causes, on the increase; just on this account it is necessary to avoid an ambiguity, which could only serve to obscure the relation subsisting between public ownership and the decisive, fundamental fact of private ownership.

There are only two starting points possible. Either we must start from the basis of common ownership, or from that of private ownership. If the state is the common owner, and if the social economy is accordingly the public economy of the state in the sense of Rodbertus's ideal, then it follows as regards the fiscal system that the whole economy of the state proceeds on a radically different basis. The immediate consequence is that there no longer exists any contrast of the sort we have been accustomed to accept as a matter of course as subsisting between the revenues of the public economy and those of private life. For the collective revenue will in this case come to occupy the central position, and private individuals will draw their incomes from it as officers and operatives in the employ of the state establishment. They, the officers and employees, who are in this case the aggregate body of citizens, then draw their incomes from the state, instead of, as is the case under the existing system, the state drawing its income from the incomes of the citizens.

That is the alternative. Contrary to what is once in a while insisted on in these later times, this contrast is not sublated by the presence of state establishments for the management of public industries, such as are distinctly on the increase in the modern state. These facts rather confirm our claim, in that this management is obliged to appeal for a justification of its methods to social facts which owe their existence to the institution of private property. The stratification of society, which rests on private property and private industry, furnishes the basis on which the fiscal management of public instruction, public means of com-

munication, etc., proceeds. Indeed, many of the comprehensive state establishments are really nothing but a contrivance for collecting from private industries the contributions wanted for state purposes, as e.g., the fiscal monopolies.

## II. THE PUBLIC ECONOMY IN PROCESS OF GROWTH.

§ 51. The whole historical development of the public economy has hitherto consisted of nothing but an increasing differentiation between the private economy of the individual citizens and the public economy of the commonwealth to which they all belong. The strength of our modern concept of the state lies in the consciousness of a developed individuality on the part of the body of citizens, which, however, is in turn supposed to lend a powerful support to the whole.

But as is necessarily the case in all human development, a long and arduous course of historical growth is needed to bring this to pass.

In the first place it is to be remarked as we have already seen, that at the beginning of national development this contrast is entirely absent. The primitive populace is the visible manifestation of the primitive state. This crude primitive type, which, significantly enough, closely resembles a certain high-strung ideal of the free state, sinks the individual man in the state, and also at the same time sinks the state in the simple aggregate of men.

But all this changes. The crude equality of the earliest times (even imperfect as that equality is) gives place to a differentiation in the course of which arises an hereditary monarchy, an hereditary nobility, then a nobility of service which in turn develops into an hereditary nobility, repeated changes in the distribution of property by the fortunes of conquest, rise and fall of different industrial classes accompanied by a greater contrast in property relations; all these causes, together with a great many others, conspire to bring about a manifold gradation of society in place of an equality.<sup>1</sup>

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<sup>1</sup> G. Waitz, *Deutsche Verfassungsgeschichte* (2. Auflage, 1870), vol. ii. pp. 300 *et seq.*

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In like manner as this highly differentiated society owes its peculiar structure in part to the presence of a hierarchy, so does it itself contain elements which further the establishment of a permanent monarchical power.<sup>1</sup>

The earlier constitution, based on a principle of co-partnership, no longer expresses the actual facts of the existing inequality. The autonomy of free members of the community results in the subjugation of the weak by the strong. Hence the need of a regal power, such as develops out of the struggles of the warring chieftains.

The mingling of the duties of personal service and material contribution, handed down from the régime of communal freedom, with the services and burdens imposed by the subjection of weak to strong, as well as the complex gradation of this subjection from the power exercised over his serfs by the local Lord up to the juridico-national relation of the sovereign to his people; all this results in a party-colored mixture of civil and public duties such as frequently to defy all attempt at analysis.

§ 52. In order to reach any sort of a clear notion of the character of this early fiscal system, it is necessary to restrict the field of view to a single country, and also, further, to select for consideration that country which has had the earliest as well as the most unbroken course of development within the European group of nations. That country is England.

The fiscal system of the Anglo-Saxon kings<sup>2</sup> rested on the same basis as that of any large landed proprietor; namely, the private estate of the king. Besides this there is the usufruct of such portion of the conquered land as yet remains common property after the more valuable part of the public domain in most sections of the country has been bestowed on servants of the crown as a living, and as long as the public domain has not all been squandered in donations to churches and convents and in remuneration or favor bestowed for service rendered.

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<sup>1</sup> Gneist, *Das Englische Verwaltungsrecht* (2. Auflage), vol. i. pp. 18 et seq.

<sup>2</sup> See Gneist, vol. i. pp. 28 et seq.

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However, even after the whole of the public domain has been disposed of there remain certain royal prerogatives attaching to it, as e.g., in the case of harbors, docks, military highways, which become the source of the royal dues, particularly of those on wool and pelts.

As the public domain diminishes there supervenes a more complete development of such lucrative prerogatives as attach to the exercise of public power and authority- the war power, the administration of justice and police supervision. Out of the war power arises the claim on the service of the people in building and maintaining the royal castles and residences; out of the function of dispensing justice springs the royal claim to property (real as well as personal) forfeited through treason or other offense, as also the claim to a variety of fines, which, however, within the manorial jurisdiction fall to the lord of the manor. From the police function is developed, apart from a comprehensive system of fines, a market privilege which is turned to account chiefly by a granting of licenses; from the same source arises also an extension of the system of dues levied in harbors and on navigable streams, as well as a variety of fees paid for the royal protection by traders, Jews and other foreigners who may be in need of protection. On the other hand the right of direct taxation is unknown to these times. The Germanic chieftain might levy tribute from conquered peoples; from his own people he received gifts, especially of cattle and produce. Honorary contributions of this kind were tendered at the time of the popular assembly; but also whenever the king made his progress for purposes of war or of justice he was, himself and his retinue, entertained free of expense, - a practice which presently came to apply to the entertainment of the royal stewards and royal emissaries in their peregrinations. The tax as a normal constituent of the fiscal system is excluded for the time being by the fact that the military and judicial functions on which the Teutonic commonwealth was based were entirely of a personal character. It was only in the last extremity that the national assembly could bring itself to decide upon a



national contribution with which to buy off the Danish pirates, from which originated the Dane-geld as a permanent tax on land.

§ 53. In the Anglo-Norman state established by the Norman conqueror the fiscal system of the Anglo-Saxon period attained a more vigorous development.

The groups of financial elements chiefly to be considered are the following:

First, the royal domains, established after the conquest by a large reservation of estates and forests; and augmented by frequent escheat of fiefs. Second, the lucrative prerogatives attaching (a) to the war-power - the customary services of vassals in the construction of bridges and strongholds, as also, and especially, the newly introduced revenues derived from the military contributions attaching to feudal tenure, which attached in the form of a money payment to wardship, marriage and succession; (b) those attaching to the administration of justice - fines and fees which in the Anglo-Saxon period had become of very inconsiderable importance, but which now flowed in freely in consequence of all the more important suits at law being now brought under the jurisdiction of the *curia regis*; the comprehensive power of forfeiture in cases of felony also became quite lucrative; (c) from the police power arose a number of fines that are also not to be overlooked.

In the third place there were also the vigorous beginnings of a system of direct taxation based on the military duties attaching to feudal tenure, and comprising: the aids due from vassals of the crown and limited to three occasions of honor or necessity (the knighting of a son, the marriage of a daughter, and the ransom of the king's person from prison); scutage, a money composition paid in lieu of service in the field; and finally the *taille* (the constant attendant of the feudal system),<sup>2</sup> a con-

<sup>1</sup> Gneist, vol. i. pp. i 82 *et seq.*

<sup>2</sup> The German word *Steuer* as it first occurs is used to designate these feudal dues. According to K. H. Lang (*Ursprung*, p. 92) it is first used in an edict [*Urkunde*] of

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tribution levied from the inhabitants of towns and of the open country not liable to military service in the field.

The Norman administrative system succeeded in turning every sphere of the national administration to fiscal account. Its pliable administrative spirit carries its indispensable system of fines and amercements into every field, in a way that defies all methodical classification. And through being centralized in a royal treasury (*exchequer*) the finances acquire quite a new prestige.

§ 54. The fiscal system of the Middle Ages, the earlier and later types of which as exemplified in the development of the Anglo-Norman state which we have here briefly described, has been regarded as a system based on private law [*Privatrecht*], in the same manner as it has been the tradition to consider the mediæval state as a system of private-law relations.

This view, however, is tenable only with limitations. We do, it is true, recognize as ever present in these institutions which went to prepare the way for the modern state, the necessity of connecting the functions of the state with something concrete, tangible, familiar to the thoughts of common men; hence came this blending of public duty and private gain; and this holds true throughout, from the apex of the feudal system to the undermost layer. This dependence on the concrete has in fact continued down into the present as regards certain fundamental elements of our existing system. Such is the weakness of human nature that the only stable point in our public law is that afforded by an hereditary dynasty.

The main outlines of a public fisc are after all present already in the Feudal state of the Middle Ages.

In virtue of the military character of that state, the duty which, as a matter of fact, constitutes the foundation of every

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Louis III., of the year 879, as "*steura*," equivalent to *Heersteuer*, *Königssteuer*. In the same connection and with, at least approximately, a like meaning, occurs also the word "bede," which etymologically (*Bitte*, *petitio*, *rogatio*, *precaria*) seems to indicate its having had its beginning in solicitation. In an edict of Count Albert von Holstein, of 1428, *Tallie* and *gemeine Bede* are used as synonyms.

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state, becomes the central fact in its system of public duties. And this is true whether the contribution takes the form of personal service or of such a contribution of goods as comes continually more and more to take the place of personal service. Scutage and tillage are contributions of a genuine political character towards defraying the expenses of war, and they replace the liability to personal military service and form the transition to the modern system of taxation.

It is, however, to be noticed that the development of this system of taxation to satisfy the growing demands meets with obstacles. In order to appreciate this fact we have no need of that gift of abstraction which enables men to transport themselves from the present to the remote epochs of the past. On the contrary it is unfortunately very easy to appreciate from present facts alone what a difficult matter it is to keep the sense of duty to the commonwealth ever alert and ready.

Hence, under the exigencies of this development, there arises a series of intermediate links which serve to bind together in a tangible manner the natural self-seeking of the private citizen and the public needs. The services which go to afford the subjects dispensation of justice and preservation of the peace are coupled with a heavy payment, which - to our notions of what a rational public economy should be - seem a crude expedient, but which are, after all, the means adapted to those times for obtaining an increasing income. These props of human or civic feebleness have also, for good cause, persisted down into the present, in less crude form it is true, but so far as concerns the service they render in linking the tangible self-seekings of private life with the great abstraction of a commonweal, they remain essentially the same.

The linking together of lucrative civil rights and public duties is in many cases counted on to secure the due fulfillment of the latter. As a case in point we find in the towns of lower Saxony the liability to bear arms and to pay taxes attached to the right of brewing.<sup>1</sup>

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<sup>1</sup> Julius Jaeger, *Duderstadt gegen Ende des Mittelalters* (1886), pp. 14 et seq.

§ 55. As it is in the German towns of the Middle Ages that the microcosm of the modern state first makes its appearance,<sup>1</sup> so it is also more particularly in these cities that a fiscal system is first developed, and then in succeeding centuries analogous devices were developed in the larger commonwealth of the state.

If we are to select a typical instance of this, the city of Basle in the fifteenth century will serve our purpose.

Indirect taxation constitutes the basis of the municipal fiscal economy. The so-called *Ungeld* (indebitum) - a tax on consumption<sup>2</sup> - was to a certain extent an invention of the municipalities. Inasmuch as the *Ungeld* did not invade the traditional forms of taxation reserved to the king and his feoffees, the princes of the empire, it was a new kind of tax to which no one had a prior title and which its inventor, the municipal council; could therefore levy without coming formally in conflict with existing privileges.<sup>3</sup> An independent municipal fiscal system begins with the *Ungeld*. The earliest form of it is the *Ungeld* on wine; i.e., a tax on wine sold from the tap. Another especially prevalent form was the *Ungeld* on milling, a tax levied on millers in proportion to the amount of grain ground in their mills.

These taxes on consumption had the advantage, in the municipal economy of the Middle Ages, as well as in different situations subsequently, of reaching all classes of the population without distinction, and especially the clergy, who, in virtue of the *privilegium immunitatis* secured them by canon law, claimed and achieved exemption from direct taxes.

Beside the wine and mill dues, there are three other regular forms of indirect taxes on consumption which the towns,

<sup>1</sup> Andreas Heusler, *Der Ursprung der deutschen Stadtverfassung* (1872).

<sup>2</sup> The designation *Ungeld* comes later to have a broader signification. At the end of the eighteenth century, in the free-city of Rothenburg on the Tauber, the revenue from houses, real estate, trades, is also called *Ungeld*. - Lang, *Ursprung*, p. 268.

<sup>3</sup> Rudolph Sohm, *Conrad's Jahrbücher für Nationalökonomie*, 1880, vol. 34, pp. 260 *et seq.* Gustav Schönberg, *Basler Finanzverhältnisse im 14. und 15. Jahrhundert* (1879).

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through acquisition of existing princely rights to tax, have been enabled to introduce: town-dues, poundage (levied on imported commodities) and the salt-tax.

The receipts from indirect taxes, as a regular thing, afforded only one-half of the aggregate annual revenue. The remaining one-half was raised by loans, a fiscal expedient constantly employed in Basle since the year 1365-66, and of historic significance as a symptom of advancing development on part of the municipal fiscal system as contrasted with the neighboring rural districts. This system of borrowing served on the one hand to meet an unforeseen deficit for any given year, and on the other hand it also indicates the gradual growth of a body of municipal debt which served as an investment for private capital.

At a time when national credit, as regards extended territories, was yet unknown, we find the German towns already involved in innumerable, regularly recurring public loans which were managed on well-defined principles. In like manner as they were hastening onward into the future in the matter of credit, so also with respect to the banker - like business which they pursued in interest - bearing deposits and in annuities, undertaken in order to meet the demand for investments for private capital. On no other hypothesis can we explain the regular recurrence of loans in every annual budget. But there certainly also was present, in this development of municipal credit a powerful financial factor, inasmuch as the town was enabled by this means to raise considerable amounts to meet sudden emergencies.

§ 56. In addition to these ordinary sources of revenue to the municipal economy there were the property tax and the personal tax, for the most part employed as extraordinary imposts. But however full an account of the population and distribution of property the tax lists which deal with those matters may afford, and however frequently these imposts may recur at the period of highest municipal development, still they seem never to have ripened into a permanent institution; at any rate in many of the foremost municipalities they were not present at all.

This becomes quite intelligible when we call to mind that the levying of a direct tax on a freeman seemed, to the Teutonic man as to the man of antiquity<sup>1</sup> (and with a remarkable similarity in the line of thought), to be a degradation. In Athens, too, the oft-mentioned property taxation which is credited to Solon, was only an expedient employed in cases of extraordinary necessity and not a regular source of national revenue. The regularity of the personal tax seems to have had, in their eyes, the odium of a sort of bondage.

It is also worth noticing that (in exact contradiction to the maxims of a modern rational fiscal system; these sentiments of theirs should be repelled by the arbitrary character of the tax on personalty with its uncertain appraisalment of property and income, and should seek refuge in a fixed tax on realty, or should consider it a step in advance to replace the arbitrariness of the personal tax with the invariability of the tax on real property. This is what Lang says:<sup>2</sup> "It would have been unbearable to the

<sup>1</sup> Böckh (*Die Staatshaushaltung der Athener* (2. Ausgabe, 1851), vol. i. p. 407), indeed says: "Of all imposts none is so objectionable to the sentiment of liberty, not only in general but also to the accepted principles of the ancients, as a poll-tax. In Athens it was an accepted principle that a tax must be levied not on the body but on property; but even the property of the citizen was taxed only in emergencies, and then only in an honorable manner. In Athens, and certainly in all the other Greek republics, no tax was levied directly on property, except perhaps on slaves, apart from the extraordinary war tax and the contributions to the Liturgies, which latter was considered a matter of personal honor. A regular tax on realty, or a tithe, was not to be found in the Greek republics, .... The sources of revenue most in vogue and most favored were public estates or domains. Beside these there were indirect taxes levied on aliens; also court fees and fines. Athens also had resort to another special source of revenue: the tribute paid by the allies." Of the Solonian distribution into classes Böckh says (vol. i. p. 653) that it was available as a basis for the levy of a contribution only in very rare emergencies; its chief purpose being war contributions, the Liturgies, and the apportionment of claims to participation in the government. Marquardt (*Römische Staatsverwaltung*, 1876, vol. ii. p. 145): "It is an accepted principle in the republics of antiquity that the poll tax is the basest form of taxation, and the form most unworthy a freeman. In Rome, as in Athens, a citizen paid no tax on his personal income; his property also was burdened with taxation only as an extraordinary resource in case of need. The *Aerarium* accordingly has but three regular sources of income in the days of the Roman republic: first the income from the public lands; second, after supremacy over foreign territories had been established, the tribute from the subject countries; and third, indirect taxes."

<sup>2</sup> *Ursprung*, pp. 59 et seq.

German of antiquity to remain in uncertainty as to what he would have to pay in taxes the coming year; and it accordingly actually came to pass that the "*Bede*" due the feudal lord was commuted into a rent-charge on houses and lands. So, later, also Alexis de Toqueville<sup>1</sup> concludes that a chief fault of the earlier system of taxation at large lay in the uncertainty of the *Taille*, as contrasted with the more advantageous position of certain provinces where there was an unchangeable tax on realty. And as a matter of fact the French Revolution hastened to make this advantage universal by means of its system of an income tax.

But even if this more perfect form of taxation had not yet become a permanent element in the municipal finances, still, in spite of its variable character, as a factor in the course of historical development it marks an important step in advance in the direction of the new era of national spirit. And as a matter of fact controversies took their rise, or even came to an issue in that movement, which bring us down into the midst of our own times. For example, in Duderstadt in the year 1438 the nine guild masters carried through in opposition to the council - on its motion to augment the impost on property - a proposition that the appraisement was to be made in their presence; they demanded also that "Patrimony and Estate" [*Erbe und Gut*] be taxed at a relatively higher rate, that is, that a higher rate be levied on property as contrasted with personal income from handicraft.<sup>2</sup> An ordinance of the city of Stendal of the year 1345 enacts: For such sum as a citizen may rent his property may the council appraise it. The town laws of Freiberg declare: Whoever sells the rent of his house out of a consideration of the tax, in order that he may pay the less hearth-money, he hath malice [*welch Mann Zins verkauft von seinem Haus durch Geschosses willen, dass er desto minder schatze von der Feuerstatt, der hat arge List*]. An ordinance [*Richtebrief*] of Zurich for 1304 declares: Whenever the *Gewerf* is imposed, the tables on which the *Gewerf* is engrossed

<sup>1</sup> *L'Ancien régime et la révolution* (1856), p. 208.

<sup>2</sup> Jaeger, *Duderstadt*, pp. 42 et seq.

shall be read in the presence of all the citizens. All this goes to show that the difficulties and struggles of the modern income-tax question were already being fought out in the economy of the mediæval municipalities.

§ 57. A further point worthy of remark in the municipal finances of the mediaeval towns, is that in the matter of indirect taxation they were forced into paths which were adopted centuries later, in their peculiar fashion, by the princes of the land.

So, for example, even at this early date, the comprehensive sumptuary laws so much in vogue (prohibitions affecting ornament, dress, but especially festivities) are commuted into a fiscal composition. The final clause of an ordinance of 1434 regulating weddings, declares<sup>1</sup> that: Whosoever will not observe these directions, he shall pay unto the city two marks, and, shall then be at liberty to invite as many guests as he may wish. As a matter of fact a very liberal use was made of this concession, and the rubric *de nuptiis* in the account books of the town covers a pretty regular source of income. Further, there is a distinct effort directed to the development of municipal monopolies; such for example is the very usual custom of retailing wine on public account, which afforded a yearly net profit. Where the surrounding country is a wine-producing region, and where accordingly the citizen supplies the wants of his household directly from the neighborhood, the council retails imported wines (in Zurich, the "alien" [*elende*] wine); but in the North, where no wine is produced, there the council controls the entire wine supply, sometimes with such marked advantage both to the consumer and the revenue that usage, prescription without any public coercion, has secured to the town-cellar [*Rathskeller*] its patronage and its profit even down to the present (Bremen). This system of monopolies extends also to other things. In Duderstadt there are three municipal baths which are farmed out. The right of brewing has taken on a very peculiar form as

<sup>1</sup>Jaeger, pp. 48 et seq.



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a municipal concession to the public houses, which are in turn permitted to brew for domestic consumption and for the townspeople (hanging out a fir twig as a sign). This concession was made to bring an income to the town council in various ways: by means of a payment for the use of the town - owned brewers' copper-kettle - which was passed in turn from one to another of those entitled to use it; also by means of an impost on hops, a tap-fee for every cask of beer, and the like.

§ 58. After we have in this way come to recognize in the mediæval municipality the precursor of the modern state, as being in possession of a fiscal system having the character of a public business, the true character of these earlier centuries and the slowness of the later course of development becomes still clearer. We see the cities rising into power and then in their turn seeking to fortify their supremacy by using their fiscal superiority for the purpose of extending their own territorial dominion. Being in themselves a complete unity which in some sense anticipated the modern state, they acquired power in the world about them by making use of their sovereignty, in feudal fashion, as a cross between public authority and private investment, which refers to their possession of disposable capital made available to them. The attempt made by feudalism to provide a national organization for a numerous population, was made possible only by the fact that this organization rested on a disposition to administer public law with a strict view to private gain. Exploitation of office for fiscal purposes is a mark of this disposition, and the contrast between the mediaeval city as possessor of these feudal rights, and the surrounding territory, throws a light on the course of development.

The reverse aspect of this conception of public office comes into view in the fact that at every emergency in the shifting and varying necessities of princes and governments, offices and places are sold or pawned, and that it grows to be a lucrative business for people of means to purchase offices and make what they can out of them. When the Hohenzollerns came upon the field a good nine-tenths of all the revenues of the crown had been either

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pledged or sold. The classes who were in possession had bought out the state (if we may speak of a state at that date) at a nominal price and at an enormous profit.<sup>1</sup> In France it is a mark of the prevailing corruption of the state and the finances down to the end of the eighteenth century, that offices are sold and resold again and again, and that a multitude of offices were created with this sole purpose. In this way there is gradually erected an administrative machinery so cumbersome; so complicated and so unproductive, that it becomes necessary to let it go on working only as a dummy administration, and set up a distinct apparatus beside it for carrying on the work of administration. From century to century the estates of the realm protest: "He who sells an office sells justice, and that is a base thing." But all in vain; for this was the form, says Tocqueville, under which the government disguised the tax which it dared not let the people see in its real character.<sup>2</sup>

§ 59. As an approach to modern times, we will now take a look at the German territorial state of the seventeenth and eighteenth centuries, taking Prussia as an example.<sup>3</sup>

The German princes of the sixteenth and seventeenth, and even of the eighteenth century, looked upon themselves as great land owners and landlords. The administration of domains and forests was, or was coming to be, the chief element in their finances.

As late as the reign of William I. the opinion is distinctly held that the utmost conceivable stretch of taxation alone will not avail to maintain the state and the army, and that this fact necessitates a domanial administration that shall be equally parsimonious and shrewd, and directed both to the production of the highest possible net income and to the acquisition of new sources of income. Leasing for a term of years to a class of

<sup>1</sup> Schmoller, *Die Epochen der preussischen Finanzpolitik*, p. 38.

<sup>2</sup> Tocqueville, *Ancien Régime*, pp. 178 et seq.

<sup>3</sup> Schmoller, *Die Epochen der preussischen Finanzpolitik*. The Same, "Die preussische Kolonisation des 17. and 18. Jahrhundert," *Schriften des Vereins für Socialpolitik*, vol, xxxii. p. 31, 1886.

farmers-general who were possessed of a high degree of professional skill, great accumulation of capital and a modern spirit of enterprise, together with certain of the characteristics of an official class, yielded the largest cash income. This financial advantage even outweighed the king's master-passion for a growth of population, and the granting of hereditary leases of domains, which had been introduced under Frederick I. by Luben, was discontinued. Not until the time of Frederick the Great was the latter policy again adopted, especially after the seven years' war. The extension of the domanial possessions ceased. The king forbade the purchase of manors by the state. He wished to see the baronial estates retained in the ownership of the nobility in order to constitute the basis of the social order and of the official class.

Even in the more highly cultivated south-western states of Germany it happened that the state was able even down to the end of the eighteenth century to get along very well without any taxation at all in times of peace. So, for example, in Wurtemberg the revenue from the "crown lands" [*Kammergüter*] was amply sufficient to defray the expenses of the central government and the requirements of the court.<sup>1</sup>

Even in our time there are distinct traces of the survival of a conception which saw in the domains the most important source of national revenue. We may notice that the extremely modern laws of the canton of Zurich, of March 2, 1870, relating to a Property, Income, and *Aktivbürger* tax, begins with the words: "So far as the revenues from the public estate and from the other sources of income established by law may not suffice to defray the expenses of the state; a tax shall be levied on property, etc." In the canton Graubunden, indeed, such part of the expenses of the government as exceeds the amount covered by the revenues from domains is designated a "deficit" to this day.

§ 60. But inasmuch as, everywhere and for a long time past, at least as regards extraordinary times and extraordinary

<sup>1</sup>G. Ruemelin, *Reden und Aufsätze*, vol. ii. (1881), p. 450.

emergencies, the revenues of the *domanium* have not sufficed, the princely power in its struggle against the estates was obliged to seek additional income. The difficulties in the way of the granting of taxes, partly of a practical character and owing to the circumstances of the time, partly of a constitutional nature, led to the adoption of means for raising revenue which would free the royal power from the onerous right of assent asserted by the estates. The doctrine of Roman law which is based on the conception of the state in vogue in the days of the Roman Empire, declares even at the middle of the seventeenth century: "*optime sibi constat respublica in qua imperantur tributa non rogantur.*"<sup>1</sup> But by the year 1782, for having asserted that the will of the sovereign was the sole and sufficient law in matters of taxation,<sup>2</sup> the prince-bishop of Salzburg was censured by a *conclusum* of the Imperial Aulic Council.

An expedient was not far to seek. It was to be found in the traditions of feudalism with its fiscal exploitation of all prerogatives of sovereignty belonging to the state. All that was necessary was to extend these sovereign rights (*regalia*) as far as might be, both as to kind and quantity. Kaspar Klock enumerates not less than four hundred *regalia*, and, indeed, the ingenuity of the time-serving jurists of the Roman law had already got as far as the discovery of a royal prerogative of counterfeiting.

And yet who can fail to recognize as a factor in this system of royalties, spite of all abuse, the pressing necessities of the developing national idea, which was making good, against the obstacles opposed by the tax-granting powers of the estates, the claim of the state's necessities. In place of the taxes, which could only be solicited, not commanded, was adopted a disguised form of taxation, which nominally derived its mandatory character from another, more plausible power than the taxing power.

The various countries of Europe have been running a race in this matter of *royalties*. Even in Russia at the middle of the seventeenth century, we find the czars carrying on several branches

<sup>1</sup> Joh. Friedrich Horn, *Politica* (1664), p. 316.

<sup>2</sup> K. H. Lang, *Ursprung*, p. 232.

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of trade, even the retail trade in meats and fruit. Incredible sums were received even at that time from the licensing of the retail trade in spirits.<sup>1</sup> And at the same time the fact should not be overlooked that this system of royalties, also as concerns the relation of the state to industry, in many ways affords an adequate expression of the growing power of the state. So, e.g., it was very usual in the various countries of Europe for the state to take the colonial trade into its own hands. So also in France in the sixteenth century the industrial system, and consequently the responsibility of its development, was declared *droit domanial*.

But just this fact that the different points of view were mingled and confused together, that there was a complete absence of any distinct discrimination between the question of prosperity and that of fiscal expediency, this fact itself - apart from all abuses in matters of detail - is a characteristic mark of the spirit of this royalty system.

In Brandenburg-Prussia we find, for example, the following contrivances which have persisted down into later times.

The Great Elector introduced the government sale of Lunenburg salt. But after the great salt works of Magdeburg in the days of Frederick I., had passed into the possession of Brandenburg, Frederick William I. was able to extend the salt monopoly pretty much to the entire community and to carry on a considerable export of salt. This was continued through the whole of the eighteenth century.

The Great Elector likewise instituted a model letter post which presently extended itself far beyond the confines of Prussia. It was not administered on a narrow revenue basis, and had also not assumed the character of a strict monopoly down to 1712, but still it yielded a very appreciable net income.

Frederick the Great introduced the lottery, the coffee monopoly and the tobacco monopoly. The first of these is still in existence; the second was a failure; the third was modeled after the pattern set by France and other European nations, but under the pressure of public disapproval and the influence of liberal

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<sup>1</sup> A. Brückner, *Finanzgeschichtliche Studien* (1867), pp. 6 et seq.

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principles with regard to industry it was discontinued by Frederick's successor.<sup>1</sup>

§ 61. But the state of Brandenburg-Prussia was vigorous and pushing and consequently in great need of funds, and it found a way, even in that age, to erect other institutions in the field of taxation besides royalties and domains.

These are the Contribution and the Excise.

In Brandenburg usage "Contribution" denoted everything that had to be paid by the country, whether in money or in kind, for the support of the troops. The feudal system and the *arriere-ban* had been replaced by hired mercenaries, recruited by captains and colonels, leased to the princes, and put in charge of commissaries. Out of this mercenary army gradually developed the Prussian army. From being a private enterprise undertaken by the colonels it came to be a public institution, and so regained the status it had temporarily lost, of a fundamental element in the state. In the first place the mercenary troops hired by the month were replaced by a standing army, for the support of which the Great Elector carried on a severe struggle with the estates, until little by little the contribution in kind came to be patiently borne and at the same time the grant of taxes was also carried year by year and even, almost imperceptibly, grew redundant, and the conviction of the legal perpetuity of the contribution came to prevail.

In assessing the contribution, use was made of the ancient *scot-cadaster* [*Schosskaster*]. Town and country, county and village, were taxed according to the proportion indicated by the figures of the cadaster. The details of the levying of the tax were left to the estates, that is, to the nobility, who did their best to shift the burden from their own shoulders.

The Elector tried from the outset, and with persistent effort, to bring the estates to the point of imposing the burden of taxation on an impartial basis, and to the adoption of a uniform princi-

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<sup>1</sup>W. Schultze, *Geschichte der preussischen Regieverwaltung* (1887). See also Schmoller, *Deutsche Rundschau*, 1888, No. 7.

ple in the levy of taxes. In response to a plan of reform submitted in the year 1647 to the estates, who were still stuck fast in the traditions of feudalism, he got an expression of their opinion that an unconditional liability to taxation was something that pertained to bondmen alone: "How is it possible," says the document, "to compel any one, who is ready and willing as a good patriot to bear his share of the burdens of the Fatherland, to disclose the entire amount of his possessions, as if our Electoral Highness's loyal subjects were bondmen and serfs?"

After a number of minor amendments of the ancient cadaster, the first thorough tax reform was finally effected under Frederick William I.,<sup>1</sup> at a time when the estates were prostrate and powerless: The reform applied to the province of East Prussia. And even then it was not carried without serious collision with the nobility, of whom the king in his irritability flung the since famous declaration that he would crush the power of the squirearchy and establish the crown as a *rocher de bronze* against their; arbitrary caprices. The general land-tax which took the place of the taxes heretofore levied on the open country was based on the computed production of each particular estate, whether of noble or peasant ownership. A large part of the nobility now paid six times what they had previously paid. Under Frederick the Great a new cadaster after the pattern set by this reform was executed for Silesia in 1742 and for West Prussia in 1772. The like was done for the other provinces not until the land tax reform of the year 1861.

§ 62. The obstacles referred to which the great Elector encountered in his efforts for reform, were influential in introducing, at least so far as concerns the towns, a new tax: the Excise.

This had originally been but a part of the system of "contributions." Certain of the provinces belonging to the electorate had adopted it experimentally in 1641 with the assent of the Elector, in place of the earlier *matricular*, as being a more expedient

<sup>1</sup> Zakrzewski, *Die preussischen Reformen der direkten ländlichen Steuern im 18. Jahrhundert* (1887). *Schmoller's Forschungen*, vol. vii. p. 2.

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form of taxation. A few of the towns had retained it from that time. The nobility opposed it more and more strenuously, for this tax fell on them as well as on the rest of the people. But in the towns, where the amount and apportionment of the "contributions" were growing ever more unbearably, the preference for it grew apace, and even occasionally expressed itself in riots. The Great Elector was well inclined to the excise from the outset; but it was not until 1667 that the decisive struggle took place, when the Elector asked for the introduction of a tax on consumption in place of the existing contribution. The nobility declared that in that case they should retain nothing but the name of their prerogatives, that they would then stand on an equality with the burghers and peasants. On renewed petition from the towns they were allowed freely to adopt the excise; while taxation of the open country was left as it had been. The excise was introduced in the towns of Magdeburg in 1680, in those of Pomerania about 1700, in the towns of the remaining provinces after 1713.

This excise is a system of consumption taxes, which in addition to a land, license [*Gewerbe*] and poll tax, were levied on beverages, grain, meat and merchandise, and was collected partly on their entry into the town, partly at the point of their production, partly at their sale. The individual rates of these taxes were low, but they were levied on a correspondingly greater number of objects.

The excise was looked on all over Europe at the time as a "newly discovered gold mine"; for it was capable of meeting the growing demands of a progressive age with comparative ease and flexibility, as contrasted with the feudal method of direct taxation which raised the necessary public funds only in the crudest and most burdensome manner. In the seventeenth and eighteenth centuries men were enthusiasts for the indirect taxes, much as we have since the time of the Physiocrats and Adam Smith been enthusiasts for direct taxes, and even for a single direct tax, and finally have come, in Prussia, since the liberal reforms in the beginning of the nineteenth century, to condemn the once admired



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excise as the embodiment of absurdity. But the reverberations of that era, of the "gentle excise" (1685) as contrasted with the "violent contribution" have reached down into the present. For the saying of Montesquieu, that the excise is an attribute of liberty, is repeated by Thiers, who says: *L'impôt indirect est celui des peuples les plus avancés dans la civilisation, tandis que l'impôt direct est celui des peuples barbares.*

§ 63. Public credit was but meagerly developed in the territorial state of the seventeenth, or even of the eighteenth century.

We have already seen that as regards this point also the cities of the Middle Ages showed an early ripeness for modern national and fiscal institutions. Indeed, it is especially noticeable that the stage at which we find this pioneer development existing is not that of a remedy for an acute need of funds which cannot be covered otherwise than by a debt, but it is the stage at which the credit is made the basis both of a permanent loan and of a banking business in the service of private investment.

The situation is quite different as regards the sovereign. We find him nearly down to the present in the position of an embarrassed private person. His need of credit as well as the satisfaction of it bears all the marks in substance and form of distress. Nothing indicates so clearly the painful course of development of the state institutions of the past few centuries as the contrast visible between private credit, as shown by a highly-developed system of trade and banking, and the pitiable plight of the public credit. The general course of national development in different countries of course differs in this respect also. In a state such as England, with its rapid development, credit also naturally develops early, but the contrast pointed out above is visible even here.

The adoption of abnormal expedients - the sale and mortgaging of the future revenues of the state, an extortionate financiering in all departments of the public administration, debasement of the coin as a customary practice - points to the gap that was filled

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for the first time by the modern system of loans. When Czar Alexei got a refusal from the Venetians in answer to a request for a loan, he debased the coin. Even France and Germany found themselves driven to this expedient during the seven years' war. It is by no means a failure to appreciate the pernicious effects of such expedients - that was appreciated even during the Middle Ages - but simply downright distress that compels their employment.

When the Great Elector came to the crown his pecuniary necessities were so great (as a consequence of the Thirty Years' War) that it became necessary to pawn offices and places in order to meet current expenses. It happened repeatedly that a loan of fifteen thalers was obtained from the city officials of Berlin in order to keep the royal kitchen supplied from one day to another. And this state of things lasted for a considerable time.

The domanial debts of Brandenburg amounted in 1620 to two million thalers, and it rose considerably after that time. The chancellor, Schwarzenberg, held claims on places in the public service to the amount of 400,000 thalers. The toll of Lenzen was pawned to Denmark for 200,000 thalers. A debt of 100,000 thalers to the Dutch Collector-General [*Generaleinnehmer*], incurred to enable the state to enter into possession of Cleve-Mark, had grown, by usury, interest and compound interest, to five or six millions.

After the extraordinary warlike activity of this prince it became the part of the peaceful Frederick William I.; devoted to the reform of the home administration, to put the finances of the country also in order. The hypothecated domains were all redeemed; a great number of new domains were acquired; expensive fortifications and structures for civil purposes were erected; and in addition to all the rest, a national treasure of eight or nine million thalers was accumulated.

This treasure was sufficient to cover the first Silesian war of Frederick the Great; at the breaking out of the second war it had again been brought up to six million; at the outbreak of the third, to sixteen or seventeen million. The seven years' dura-

tion of this war was a trial of strength, but at the same time it was also an evidence of the undeveloped resources of the national economy of that time. The entire aggregate of the ordinary revenues of the state was applied to the purposes of the war; all payments were suspended; officeholders received instead of pay certificates that were not payable until the close of the war. The fact that the king had no debts worth mentioning at the close of the war, if it was on the one hand a proof of his having triumphantly surmounted all financial embarrassments, was at the same time equally an evidence of the absence of public credit, in the sense in which the term is understood in the days of the maturer state.

### III. THE PUBLIC ECONOMY IN ITS DEVELOPED FORM.

§ 64. While we have, in what has gone before, discussed the distress incident to the national economy in process of development, the question now is what is to be the outcome of this process of development.

So long as the national economy has not attained the point at which it comes to be recognized by those concerned as the common provision out of private economies for common purposes, and comes in fact to profit by this recognition in such a manner that contributions from private resources are placed at its disposal; so long will it be obliged to get along with expedients for filling the gap between the idea of the state as it exists for the time being among the average of those concerned and the actual needs of the existing administration.

If we take into consideration the imperfect development of this sentiment - when sacrifices are continually demanded from the state for the furtherance of class interests, without any clear conception of where the responsibility for the public burdens incurred will fall; when every requisition for state purposes meets with ill-will and murmuring, at the same time that benefactions of all sorts are expected from this same state; when, in short, even in the midst of our own advanced and politically wide-awake age, it often looks as if everybody wanted to get

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something from the state, and nobody were willing to give anything to it; - when we take these facts into consideration we get a lively impression of what the situation was at an earlier stage, where the degree of political development attained is indicated by the fact that the state administration cared for the interests of the citizens in the same manner and with the same motive as a landlord cares for his tenants.

Hence the propriety of the choice of such means of income as should depend to the least possible extent on a sentiment of citizenship, seeing that such a sentiment had not yet reached a conscious recognition. Hence the preference for such sources of revenue as should either not require any conscious sacrifice on part of the individual for the purposes of the commonwealth, or should at least put such requisitions as were unavoidable in the familiar form of a tangible *quid pro quo*.

But are we, after all, today, quite past this stage of immature national consciousness, and the forms of national income corresponding to it?

By no means. The prevailing conception of the state has caused our whole system of taxation to proceed on the principle that the least possible offense must be given to the modern citizen's irritable spirit of resistance to all public demands. It is at present held to be a mark of statesmanlike financial policy to make this realistic maxim the basis of reforms for the future as well; while all that is habitually considered utopian in schemes for tax reform is comprised in a single idea that amounts to nothing else than a frank recognition of the duties of citizenship. This concept of the duties of citizenship, however, departs very widely from the actually prevailing public sentiment of the day.

§ 65. If the public economy is ever to reach a satisfactory basis it will have to come to this, that every public purpose must be pursued only on the condition that the sacrifices necessarily involved are accepted as a matter of course by the body of citizens. Every public activity that may require sacrifice should be enabled to pursue its end in all serenity, without being disturbed by any questions as to the raising of the necessary funds. Or if

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it must be made the vehicle of a fiscal return, then that should be permitted only to such an extent as it can take place without clashing with the citizens' duty in this matter. And if it should actually come to pass at some time in the future that (at least as regards externals) the latest stage of social development shall be shunted in on the track belonging to the earliest stage, so that private property and profit, and production by private industry shall be replaced by communal property and production by a national organization of industry according to the programme of the socialists; then it would follow that the fiscal aims and consequences involved - while making an end of all taxation - would be of the nature simply of an unintended by-product; while the essential purpose of the change would be an alteration of the conditions of social life, of which the change in financial methods would be but an unavoidable concomitant. The recognition of these facts will afford us the criterion necessary in order to a systematic criticism from the standpoint of developed national fiscal institutions as we find them. That blending of purposes and aims in our fiscal methods which has been handed down from the earlier stages of the growth of the fiscal system, and which has been infused into the current fiscal doctrine by the science of cameralistics, is to be obviated by such a knowledge of the facts as will assign to the purely fiscal ends their own independent weight, and in so doing will also relegate aims and purposes of a foreign kind to their proper place.

The task immediately before us is to trace this in detail.

§ 66. We will begin with what by tradition constitutes the first great factor in the public revenues - the Domains; and we will give the traditional method of dealing with the problem a hearing in person.

K. H. Rau<sup>1</sup> enumerates the following reasons for and against alienating the domains.

For alienation:

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<sup>1</sup> *Lehrbuch*, vol. iii. secs. 94-98 (5<sup>th</sup> ed., 1864).

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1. The government is ill fitted to carry on industry. Private owners as a rule make better use of a source of income because they devote themselves to the business with greater zeal, etc., while the government is obliged to employ an expensive personnel, who are less industrious and less thrifty than men working in their own employ. Experience teaches that the domains will yield a greater net revenue in private hands.
2. The sale of the domains is a ready means of paying the public debt.
3. The possession of domains brings the government into conflict with a special class of private undertakings, which tends to make it disinclined to certain reforms of a general character, as, e.g., the abolition of special burdens on realty.
4. Experience goes to prove that domains are by no means necessary in order to adequately meet the national expenses.

For the retention of the domains:

1. Viewed from the general standpoint of state-craft, it has been customary to consider domains an essential support of an hereditary monarchy; because, as this institution has originally sprung from the possession of large landed estates, so it must continue to rest on this basis; and because the revenue from domains is not dependent on parliamentary consent, etc.
2. The income from domains excites no dissatisfaction and no feeling of deprivation, since it is the product of an independent business carried on by the government by means of possessions that have already long been withdrawn from private ownership.
3. It cannot be asserted that domains are invariably less well and profitably managed.
4. The income from domains must in the long run rise because rent rises.
5. Public loans can be more readily floated by the help of the domains, as the latter afford an acceptable collateral security to the public creditors.
6. Crown estates are of considerable service in facilitating the introduction of agricultural improvements.

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§ 67. In this enumeration of the reasons offered for and against, we have tried to present, as adequately as may be, the various views usually brought forward in the chapters devoted to domains in discussions of finance. A decision of the question after the manner of the solution sought by Rau is not to our purpose, as will immediately appear from an examination of the arguments already cited. To this we will now proceed.

Either the reasons given are something already contained in our review of the historical development of finance, and so will serve only to confirm what we already know, - that the domains are part of a fiscal system which does not belong to the present; or they are not financial reasons, - in which case they have no place in a science of finance, and equally so whether the reasons are to be accepted as valid or not - whether we regard them as establishing the desirability or the undesirability of domains.

To the former category belong such arguments as these: Experience teaches that domains are nowise necessary in order to adequately meet the public expenses, or, The revenue from domains excites no discontent and no feeling of deprivation, or, The sale of the domains is a ready means of paying the public debt, or, Public loans may be more readily floated by the help of the domains as the latter afford a collateral security to public creditors. Reasoning of this sort is based on nothing but an acceptance or denial of the old or of the new fiscal economy. Disconnected from this their historical relation, they cut a brilliant figure among the amazing commonplaces that make up the dispensatory of the Cameralist. So e.g., the statement that no feeling of deprivation is excited by raising the public revenues from domains instead of from taxes is equally indisputable with the precept that the state had not best give its domains away.

Under the second category belong such reasons as the favorite objection of Smith's school to all state industry; or the apology for domains as being a prop to an hereditary monarchy; or the usefulness of domains for the introduction of agricultural improvements; or the increase of rent.

None of these considerations has any place in the science of

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Finance. The discussion of the importance which domains have for an hereditary monarchy belongs to the Science of Politics, and even there it can be intelligently discussed only in its historical connection and will probably be conceded to have little significance.

The other considerations enumerated belong in Social Science - in the theory of industrial administration or among the fundamental questions respecting the limits of state and private industry. On this ground alone can they be definitely settled.

In point of fact the recognition of this truth has latterly gained some footing in consequence of the spread of more thoroughgoing study in Economic Science.

§ 68. In this connection it is interesting to note the very significant bibliographical incident that Adolph Wagner, in the course of his researches into this, by tradition, introductory part of the Science of Finance, found himself constrained, in order to place his exposition on a satisfactory basis, to scrutinize more closely these general fundamental principles that underlie all industrial intercourse.

And as a result of these thoroughgoing researches of his, this eminent authority in financial theory arrived at the following criticism of Rau's method of dealing with the question.

Rau's argument, says Wagner<sup>1</sup>, constantly moves on the plane of the productive capacity of private and state industry, and leaves altogether untouched all other phases of the question, such as the economic question of distribution and its social consequences, or in other words the effect of the distribution of land on the life of the community. So also, his argument uniformly proceeds on the assumption, without adequate proofs, that state ownership is by nature inferior to private ownership of land, and consequently involves the assumption of an exaggeratedly general and serious economic disadvantage attaching to the retention of the domains.

Wagner then goes on to discuss the question of domains on the lines indicated by this criticism. But his discussion is

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<sup>1</sup> *Finanzwissenschaft* (3. ed., 1889), secs. 219 *et seq.*



not strictly in accord with the results of his criticism, in so far that he suffers the subject to retain its place within the Science of Finance instead of removing it, as I am persuaded he should, to its proper place in the theory of social and industrial policy. Neither the question as to the relative advantage of private ownership and state ownership of the soil, nor the question as to the proper distribution of the land within an industrial community, nor the question as to the most expedient manner of alienating public lands, whether in feefarm or according to some other scheme of agrarian reform; - none of these are questions that properly belong within the Science of Finance. As a matter of fact, wherever they may occur in financial science they are rather relics of that (historically intelligible, but scientifically unsound) appendicular method of dealing with economic problems that is quite at home in the old-fashioned Cameralistic Science. The umbilical cord is still unsevered that connects our science with those early beginnings in which, after the manner of all beginnings in science, the starting point was some question of tangible, pressing necessity, from which the inquiry proceeded only reluctantly and unconsciously to more general and profounder questions.

It is to be hoped that we have by this time reached the point at which these results of systematic thought should be accorded their true place.

And should not also the hint be taken to heart which is contained in the fact that it is already many years since the domains belonging to the state of Prussia were removed from the jurisdiction of the Ministry of Finance and turned over to the Department of Agriculture? Has not the course of events at this point outrun the science?

§ 69. To Lorenz von Stein undeniably belongs the credit of having, by the powerful current of his speculations, initiated the necessary distinction between things essentially disparate and the separation of things connected only in time and place.

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If we let Stein speak for himself, this among other things is what he has to say:<sup>1</sup>  
The more highly developed the idea of administration, the more does the thought of making the state's industrial activity a source of income at all, recede into the background. Hence the financial element proper, with the advancing development of national life, tends more and more to be swallowed up in the principle of Administration, and the character of the whole matter undergoes a change. At the outset, the revenue which the state derives from its industrial enterprises is the chief consideration, but gradually their effect on the life of the people assumes the greater importance; so that in the nineteenth century the feeling has gained predominance that the state must not hesitate to surrender all net income from these forms of activity, or even to contribute something additional in the way of supplementary funds, in case it appears that these state activities will in this way best serve the purposes of the people's life. The application of these propositions in practical life is indicated by the maxim that the fiscal income is not to be determined simply with a view to the greatest possible net revenue, but with a view to the effect which the industrial activities in question exert on the nation's industry considered as a source of revenue. This is the economic point of view which fiscal administration must take in the management of each particular branch of state enterprise: Finally it also follows that the entire discussion of this part of the public revenues properly belongs under the head of Home Administration, instead of, as formerly classed, under the head of Finance. And so we arrive at the result, which for the main purpose of our science is of the gravest consequence, that all state activity of this sort has grown to be simply an administrative function. It is true, all the three kinds of business incomes (domains, royalties, fees) are just at present at a transition stage; a fact which further adds to the difficulty of the treatment of them. But there is no doubt that this higher function of these means of revenue is resistlessly asserting itself, and that the earlier view

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<sup>1</sup> *Lehrbuch der Finanzwissenschaft, 5. Auflage (1885), vol. ii. part i, pp. 140 et seq.*

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respecting these activities has already in many cases practically given place to the new.

So far Stein. His position, it seems to me, is in general sound. Only, I believe he should have drawn the full inference warranted by his general position; that the Science of Finance should not permit itself to be kept waiting till "the earlier conception shall have been replaced by the later conception in practical life," but that it is the office of financial science as a science to prepare the way and light the onward steps of practical administration by an adequate exposition of the "higher nature" of this class of sources of income.

It is precisely from one occupying a position that makes so much of systematic arrangement and treatment that we might properly demand a systematic scheme of fiscal administration, constructed on the lines of the modern idea of the state, as well as a clear exposition of the manner in which this system is in practice traversed by historical survivals from earlier stages of the state's evolution.

In direct contradiction to all this we find Stein (even in the latest edition of his work), in his first chapter, discussing the public income from agricultural crown lands, from crown forests, crown mines, game preserves and fisheries, rents and reversions; also industrial investments of state-owned capital, state banking enterprises, model establishments, public means of communication; also in the same chapter, state monopolies - the post office (including the telegraph and the telephone), the coinage, the issue of paper money, the monopoly of the means of communication and the monopoly of lotteries.

§ 70. Umpfenbach has, so far as I am aware, been the first to make a definite move in this direction.

He makes the statement in his *Lehrbuch der Finanzwissenschaft*.<sup>1</sup> There can be but one principle governing the procurement of revenue, and according to this principle the public revenue figures as the correlate of the public expenditures. Since

<sup>1</sup> *Erster Theil* (1859), pp. 54 *et seq.*

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the parties concerned for whose behoof the state undertakes any industrial function, are its own citizens, it logically follows that the state's expenses should be defrayed out of their productive capacity. "The possessions of the individual members of the state constitute the basis on which a sound, all-sufficing revenue system for meeting the necessary expenses of the community may be built up." The function of the state as exchequer, when reduced to its lowest terms and stated in the form of a principle, is nothing else than the proper performance of the part of mediator between a certain group of the wants (government activities) and a part of the industrial capacities of the members of the state. The economic capacities of the citizens constitute the "organic" source of the revenues of the state. In addition to these, Umpfenbach designates as "mechanical" sources of state revenue such sources as serve to render the exchequer independent of the property held by other business undertakings, and so put it in a position to relieve the organic sources of revenue from a burden which would otherwise fall on them. All this will be intelligible only in case the adoption of a merely mediatory function is, in consequence of the imperfections of the fiscal system, still attended by considerable friction. By "mechanical" sources is here meant domains and fiscal prerogatives (monopolies).

The consequence of taking this standpoint is, for Umpfenbach, that he reverses the traditional order handed down from Cameralistic Science, and deals first with the "organic" sources of income (the levying of fees and taxation), and afterward with the "mechanical" sources (domains and monopolies).

In this manner has Umpfenbach endeavored to assert the claims of the method based on principle and system as against the traditional method of treatment. Only, he has failed to draw the remoter consequence which follows from the considerations adduced above.

Domains and monopolies with him take their place after taxes in like manner as they have by tradition been placed before them. But they still stand, and they are treated quite

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after the fashion of Rau and the school of Smith. Monopolies are, in Umpfenbach's vocabulary, known as Fiscal Prerogatives, and it is a step in advance on his part to have put aside the idea of the monopoly. But the new idea of fiscal prerogatives brings back our old acquaintances of the cameralistic tradition, and in the same order of logical sequence: succession prerogative, occupation prerogatives, game and fishery, prerogative, mining prerogatives, salt-mine prerogatives, tobacco prerogative, bank-note prerogative, lottery prerogative, etc.<sup>1</sup>

§ 71. We now pass to a critical discussion of monopolies; and in pursuance of this purpose we shall take a glance at the earlier scientific discussion of this matter. In the first place then, it was Justi who first constructed a theory of fiscal monopolies that has retained its authority in the science for a century and is still in force in practice to this day. Even he divides the aggregate of the ordinary state revenues into domains, monopolies and taxes. The character of the monopolies [*Regalia*] he defines in the following manner:

He is of opinion<sup>2</sup> that there are contained in the aggregate possessions of the state various things which are by nature wholly unadapted to become the private property of the citizens, or that may at best become such only under the constant supervision and coöperation of the supreme authority; for this reason the management and use of this class of things has been committed to the supreme authority. How, inasmuch as these possessions belong to the state collectively, they have been looked upon as belonging to the supreme authority in the state-to the crown, and the rights arising out of them have been called royal prerogatives or *regalia*. In no other way can we arrive at a satisfactory theory of this designation; for if we were to call them "royalties" simply because they are in the hands of the sovereign authority, or because they are rights vested in the national sovereignty, we should have to admit as many "royalties" as

<sup>1</sup> *Lehrbuch*, vol. ii. pp. 1-80.

<sup>2</sup> *Staatswirtschaft*, vol. ii. p. 113.

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there are different objects comprised in the government's business; as many special contrivances as are possible under the police power, so many *regalia* would there be: "We should have to assume a bank royalty, a fire assurance royalty, a lottery royalty, a penitentiary royalty, and no one can tell what a fine lot of other royalties." If, however, police establishments are to be excepted from the class of royalties, we shall have to assign some intelligible reason why these things are not to be called by that name just as much as any other prerogative belonging to the supreme authority which is classed as a royalty.

Justi's conception of royalties is accordingly as follows: Royalties are such rights over property not adapted for private ownership as are vested in the supreme authority in order that they may be managed for the best interest of the community, and may at the same time, as a subordinate end, also, yield a revenue. He admits no *regalia fisci* whatever, if this term be taken to designate such royalties as exist for the sole purpose of yielding a revenue. This latter can never be the chief object of any royalties, since in the case of each and every one of them; the prosperity of the state must be an object of immediate consideration. The result might, in practice, be very detrimental to the general well-being of the state, if revenue were made the chief end in the case of tolls and duties, of the post-office, of mines, of salt and coinage monopolies. Justi insists that the right of the sovereign authority to levy taxes on its subject is not to be classed as *regalia*, in the sense in which he uses that word; since in the case of every *regalium* by means of which a contribution is levied on the subject, it is necessary that a transaction should take place affording occasion for the collection of a contribution. This transaction is absent in the case of taxes, their basis being rather an immediate obligation resting on the subject to meet the necessary expenses of the state. An effort is here made to reach an expurgated conception of royalties, and the expurgation consists in bringing the common welfare into the foreground in place of the fiscality which pushed itself forward so persistently in the actual course of things in the

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past. In its struggle for the development of the exchequer, the practice of earlier times made use of a particular mixture of the most diverse public institutions for purposes of income alone, being pushed by the necessity of disguising the tax whose real character none dared to let the subjects see. Then, presently, the later age of improvement came to appreciate the abuses of this fiscal management, though not the causes of it, and believed itself to have done its duty in having brought the "public good" into the foreground. As a matter of fact, nothing but a closer scrutiny of the historically operative causes tending in the one direction and the other could avail to bring out the relation in which the state establishments classed as royalties stood, either to the finances or to the public good. The extreme radical character of Justi's criticism is visible not only in his condemnation of court fees in favor of a gratuitous administration of justice, but quite as much in his indiscriminate confounding together of t<sup>1</sup> tolls and imposts, salt-tax and seigniorage."

Later times have, as to this particular point, gradually overcome the confusion. But, after all, Justi's example was followed for a long time; not without transitional stages it is true, for which the *Klärung* prepared the way even while temporarily leading farther away from the truth at the outset.

§ 72. Ludwig Heinrich von Jacob, the theoretical writer on Finance, may be taken as exemplifying this latter fact. His *Staatsfinanzwissenschaft* (1821) takes a position with respect to the *regalia* which may be characterized in the following propositions.

If the state surrenders all industries to free competition, says Jacob, it will (1) result in increased production, since free competition yields the same product at a less cost; (2) the state is freed from all special interest in industry, and so loses the false motive it otherwise has to restrict competition or to favor monopolies, etc. For these reasons we are constrained to discountenance all income from monopolistic industries owned by the state.

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<sup>1</sup>Vol. i. secs. 315 *et seq.*

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If there are certain monopolies which the public good requires should be managed by the state, then these should at all events be administered, not as sources of revenue, but rather as institutions of public utility. In that case, however, it would very soon appear that private enterprise could much more advantageously undertake their management and that the state could in this latter case exercise a much better and more thorough supervision of them than if it undertook to manage them directly. Such state industries as are administered as monopolies by the state simply for the sake of gain are under all circumstances detrimental to the national prosperity, and are accordingly to be put aside. In conformity with this opinion, Jacob is of opinion that the postal service would gain very greatly both in point of cheapness and of public convenience if it were left in private hands (under government control). But even while the postal monopoly is retained, the state should cover no surplus into its exchequer from the post-office revenues, since it would serve the public utility to better purpose to lower postal rates to the necessary extent and so still further facilitate communication, or else apply the surplus to improve the postal service.

Malchus (1830), indeed, opposes Jacob's position, and in his *Handbuch der Finanzwissenschaft und Finanzverwaltung*<sup>1</sup> he brings the results of his experience as administrator and financier in the government of Wurtemberg to bear against the abstract dogmatism of the dominant school of his time. The view that in case the royalties were surrendered to private enterprise the state would be able to raise as large, or even a larger sum by taxing them, rests on an arbitrary assumption which is contradicted by experience. Malchus cites, among other instances, the example of the French tobacco monopoly of 1810 and its fiscal results, as contrasted with the scanty revenue and the oppressive character of the French tobacco tax of 1804-1809. But when he goes on to defend the postal revenue against Jacob by classing it under a separate category (it is not to be regarded as a tax but only as compensation for special services and benefits) he succeeds only so far as

<sup>1</sup>Vol. i. pp. 109 *et seq.*



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to make this dubious means of defense do service in bridging the chasm and carrying him over to the general principle that the Post is in its nature and essential character not adapted to become a source of revenue, but is to be looked on simply as an institution established for purposes of the national economy (i.e., for economic purposes) and is devoted to a class of services which the government is in duty bound to undertake, even though the income from the service should not cover the expenses."

§ 73. How nearly the position of K. H. Rau coincides with that of the old-fashioned Cameralists comes out with striking distinctness in his manner of dealing with the royalties, in his *Lehrbuch der Finanzwissenschaft* (5<sup>th</sup> ed. 1864). Not only is the formal classification of state revenues the same as that of Justi, but the topsy-turvy lumping together of undigested facts concerning the royalties also recurs quite in the manner of Justi's discussion. Mining royalty, salt royalty, game royalty, tobacco royalty, postal royalty, etc. The only difference is that the toll royalty is thrown out of this promiscuous assemblage and is replaced by the telegraph and railway royalties, which have been discovered and added to the list. If anyone today entertains any doubts as to whether our science has made progress these late years, let him come face to face with the spiritual equanimity that goes with this manner of thinking, and if he has learned any part of what would qualify him to pass an opinion on the present position of the science, he will be affected by this juxtaposition of coinage royalty, tobacco royalty, postal royalty, precisely as a musical ear is affected by a succession of false notes. If kindred spirits exist who feel themselves at home in Rau's range of ideas, they are welcome to it; they probably have their own reasons. At the same time these purely subjective sentiments can in no way prevent the latest popularizer of Rau's *Science of Finance* from deserving the credit of having done a scientific piece of work, in that he paused before that wooden structure and sought to lay a deeper foundation before going on.

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Rau was quite right in thinking that the Science of Finance is authorized, regardless of what the public law may recognize under the head of *regalia*, to proceed according to its own principles. But he does not carry out his position to its legitimate conclusion. He restricts this privilege of the science so far as to retain the *regalia* as a branch of the public revenues. In achieving an historic sense of the policy in which the royalties properly belong there was also achieved the scientific dissolution of this idea for the purposes of our time.

In his estimate of the royalties for the financial purposes-of the modern state, Rau does not greatly diverge from the position of his predecessors, Jacob and Malchus; although he agrees with Jacob as to the line of thought (that is to say, with him he lies under the spell of the individualistic school of Smith), still, in consequence of his innate attitude of moderation, he is favorably inclined to existing institutions and so approaches the practical position of the experienced financier, Malchus nevertheless, in proportion as existing usage and institutions are made the standard and guide of scientific thought, the science degenerates into a mere reflex of existing facts and falls short of its true office.

Rau's definition of Royalties is cautious, but it is also correspondingly superficial: "A prerogative of the national authority with respect to an occupation which would, in the absence of special legal enactment, belong among the ordinary means of livelihood of the citizen" (sec. 166).

He goes on to say: Only a few occupations may properly be subject to a royalty; otherwise the enterprise of the people would be unduly encroached upon. Individual undertakers are, as a rule, able to obtain greater results and to reduce expenses to a lower figure (sec. 168). The continued retention of a royalty is proper (1) as regards a given industry, if by exception it is capable of being managed as economically by the government as by individual enterprise; (2) with respect to the profits of a monopoly, if it conforms to the requirements of a good tax, that is to say, if it neither interferes with the production of

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goods nor narrows the chances of acquiring a livelihood, and if, further, the net income so obtained is not obtainable by means of taxation; (3) from other considerations of statecraft (sec. 169).

In the succeeding discussion of particular royalties, Rau adopts not the indifferently tolerable classification here indicated, but the genuine cameralistic one (sec. 171): The objects of a royalty are (1) industries that deal with the land (mining, salt-works, game, etc.); (2) manufactures (coinage, tobacco manufacture, gunpowder and, once more, salt); (3) trade (again salt); (4) services which afford immediate profit or pleasure (freight and express [*Fortschaffungsgewerbe*], post, telegraph, railways; also lotteries). In view of the party-colored character of his presentation I may, or rather I must spare myself the hopeless task of searching for a consistent point of view in Rau's discussion of royalties.

§ 74. J. G. Hoffmann has a clearer insight into the historical character of the royalties than does Rau. Since the constitution of modern states has undergone a substantial change, says he,<sup>1</sup> there is no longer any reason for regarding any contributions toward the public expenditure as of a nature different from other taxes merely because the government secures their payment by reserving to itself exclusively the trade in the commodities on which the tax is levied. The royalties now surviving are, however, anything but a form of taxation; they are not kept up for the sake of the revenue flowing from them; the revenue being, on the contrary, simply incidental to certain kinds of business which the government has reserved to itself for the reason that the unhindered pursuit of the occupations in question by the subjects would jeopardize their own interests, - as, for example, in the case of the letter-post, coinage, ownership of rivers.

Twenty years later we are told by Umpfenbach: It is high time the hobgoblin of royalties that has haunted the Science of Finance for so long were laid.

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<sup>1</sup> *Die Lehre von den Steuern* (1840), p. 25.

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However, Umpfenbach's changing the style and title of the royalties into "fiscal prerogatives" is not of itself sufficient to achieve this result.

Lorenz von Stein<sup>1</sup> sets out with the curious assumption that it is the task of modern financial science to subject the concept of royalties to such a revision as will give it a new lease of life. Neither the ground of this assumption nor the results of his efforts in this direction are readily discernible.

The Royalty and the fact of Regality are in Stein's opinion two categories which are not contained in the abstract notion of the state, but are the historical outcome of the gradual development of an independent administration on part of the state. Hence it comes that these words have had different meanings at different times, as also that their meaning is not fixed even today. But what has given them their standing in the theory of administration is, after all, the concept of the state's industrial sovereignty. What serves to bring them within the jurisdiction of financial science is the fact that in them the industrial sovereignty takes form in independent establishments belonging to the State, with state-owned capital and state management, and that these state establishments are also in part capable of yielding to the state a revenue, based on their industrial service and collected in the form of fees paid for their use.

There is no proof whatever offered to show why "the notion of the industrial sovereignty of the state" is connected in any peculiar manner with "the idea of royalty"; or why, if the idea of royalty is to be conserved at all by a process of dialectical permutation, it is the State's industrial sovereignty alone that is to be permanently connected with that idea.

Stein goes on to conclude: "Royalties are, therefore, only to be considered as a particular, definite portion of the fiscal revenues of the state. They are an outgrowth of that industrial sovereignty in virtue of which the state, as the organ of the common interest, not only undertakes the performance of certain special services by means of its own capital and under its own

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<sup>1</sup> *Finanzwissenschaft*, 5. ed. vol. ii. part i. pp. 307 *et seq.*

immediate direction, but also obtains an income in the form of a business profit. The form under which this income is received is the fee; its rate, however, is not fixed by the fiscal standard of the highest possible net income, but is in part regulated by the requirements of the general industrial development and the principles of political economy; or the net income may even disappear entirely."

Adolph Wagner<sup>1</sup> is at one with Stein to the extent that he divides the royalties of Rau into two great classes: those in which the form of a royalty is adopted simply as a convenient method of taxation; and those which primarily are made to serve an "administrative" purpose. In matters of detail Wagner's criticism is the more searching and thorough, in that he differs from Stein in recognizing that the Royalty as it occurs in the lottery is also nothing but a form of taxation.

On the other hand, Wagner discards the definition of Royalty set up by Stein, and sums up the revenues classed under that head partly under "fees" (post, telegraph, coinage), partly under "quasi-private" [*privat-wirtschaftliche*] revenues (railways). In this way he argues from the position introduced by Rau and Hoffmann that the fiscal royalty is an historico-legal conception which serves no purpose in the modern public economy or in modern financial science.<sup>2</sup>

What this conclusion of Wagner's leaves as matter for discussion is his view of the so-called "quasi-private receipts" and "fees."

The foregoing attempt at indicating what efforts have already been made toward placing the developed exchequer in its true theoretical position, as opposed to the narrow views of the past, could not well be avoided if we are to reach a clear conception of what the problem before us is. The aim is to establish a clear distinction between the administrative office and the fiscal office of the modern state (see sec. 65 above).

<sup>1</sup> *Finanzwissenschaft*, vol. i. 3. ed. sec. 207.

<sup>2</sup> Likewise H. von Scheel, "Die Erwerbseinkünfte des Staats," in Schönberg's *Handbuch der politischen Oekonomie* (3. ed. 1885), vol. iii. pp. 63 *et seq.*

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Let us now, with this in mind, examine the position of royalties in the scheme of the traditional Science of Finance; and in order to deal with the matter in its integrity as it stood while yet untouched by criticism, we shall select for examination the view of Rau (it recurs, by the way, in a very similar form in Roscher).

Rau classifies royalties on two different principles: (1) according to their degree of adaptation to the purposes of the modern state; (2) according to the group of industries in which they belong. The latter classification has the merit of a complete *naïveté*, in that it presents the historical data of the earlier state in a simple mechanical order for the purpose of discussing them according to the principle of adaptation laid down in the former canon of classification.

It is worthy of remark how the material at this point bursts the thin shell of the "royalty" as of its own motion.

The discussion of the salt royalty (sec. 186) develops into a comparison of the system of salt taxation employed by different states. The tobacco royalty is treated in the same way; although, as being the most important example of the "industrial and commercial royalties," it is treated of in another place in company with the gunpowder royalty, and then again in company with the brandy royalty, which, by the way, is not treated in the same fashion, apparently for the reason that it is not so obtrusive a fact as the tobacco royalty. As a consequence of this method the chapter on taxation of spirits goes over into the theory of taxation (sec. 438 *et seq.*), as is also the case with a fraction of the discussion of the tobacco tax.

The need which finds expression in this unwieldy manner in Rau's discussion has now more and more come to receive the recognition which was expressed in J. G. Hoffmann's words: "Since the constitution of modern states has undergone a substantial modification, there is no longer any reason for regarding contributions toward the public expenses as of a nature different from other taxes simply because the government secures their payment by reserving to itself exclusively the trade in the com-

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modities on which the tax is levied." Lorenz von Stein, Adolph Wagner, H. von Scheel (simply to mention the names of recognized manuals) are agreed on this point. Umpfenbach and Roscher, it is true, still occupy Rau's standpoint.

§ 76. The multiplicity of the earlier royalties cited by Rau: mining royalty, game and fisheries royalty, coinage royalty, postal royalty, railway royalty, water royalty, gambling royalty, are, in Rau's treatment, still slumbering under the crepuscular light of Cameralistics where fiscal and administrative aims are inextricably entangled. Stein's new formulation sets forth the form under which the greater part of these royalties have retained a semblance of continued theoretical existence down to the present. A defensible theoretical existence they do not possess.

While advanced criticism has come to recognize the Royalty in some cases as simply a form of taxation and has accordingly relegated these cases of royalties to their proper class, the remaining cases fall into line under the head of Administration. The coinage royalty has no more to do with finance than has the crown supervision of weights and measures. It is to be noted as a matter of fact in the history of finance that the debasement of the coinage has been seized upon as a royalty, and that a Russian czar once established a lucrative monopoly of measures to be employed in trade. Modern science treats these matters as questions of administration.<sup>1</sup> The traditional royalty is in the eyes of modern science solely an administrative fact, and when fiscal considerations in the modern state begin, the concept of royalty as such ends. The question of paper currency finds its place in the theory of the public credit, the question of royalty involved possessing but a secondary importance, or none at all. Then there are the great establishments for purposes of intercourse, of recent origin or but recently developed into their present gigantic dimensions - post, telegraph, railways. The erection of establishments of this class into a royalty is, aside from other considerations, also questionable on this ground, that the

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<sup>1</sup> In the sense employed by Stein. See vol. i. sec. 61 of the present work.

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invariable mark of this concept - the exclusiveness of the state establishment - is not, according to modern conceptions, an essential feature of the matter at all. The essential point to which the railway policy of modern Prussia is directed is quite distinct from the question of an exclusive state monopoly of the railways. This latter point is in fact not the object of anybody's efforts in connection with our railway policy. The reservation of a state power of grant and concession to private railway enterprise is a practice common to all civilized countries, and rests on sufficient, though certainly not financial grounds. But if this reservation is to be counted as an example of royalty, then we might fairly count every case of grant or concession to any industrial undertaking as a case of royalty. In so doing we should in point of fact openly revert to the habits of thought of past centuries.

In the case of the letter-post the fact of a royalty is a matter of history. How far it is essential to a public postal service today is doubtful, to say the least.

The element of peculiar strength in these great establishments is to be sought in quite another direction. It is their organization and magnitude that gives unity and strength to these undertakings, and thereby secures the best service at the lowest cost; and it is this fact of the importance of the result to be secured that makes the undertaking worthy the attention of, or rather an unavoidable duty incumbent upon the commonwealth itself. If there are today, or for a number of years to come, a few roads in Prussian territory remaining in private hands, that is a matter of very slight consequence as compared with the great central question of a state railway policy. If the laws of the Empire have left room beside the Imperial Post for that local letter carriage which has of late been trying its fortune, that is by comparison a trifling incident when contrasted with the unquestioned importance which the Imperial Post-Office possesses today, independently of any exclusive monopoly that may belong to it.<sup>1</sup>

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<sup>1</sup> Compare the speech of the Secretary of State for the Imperial Post-Office, Dr. von Stephan, before the Reichstag, 30 November, 1886, in which, among other things,



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§ 77. Meanwhile there remains an undissolved residuum in the case of these non-fiscal establishments. It is an undeniable fact that they do after all - not necessarily, but in an incidental way, and occasionally to a great extent - yield a financial surplus; which gives them theoretically such a claim to be incorporated in the theory of the public revenue as cannot be rejected.

In this respect the case of the letter-post is especially in point. In earlier times, in consonance with the generally undeveloped economy of the state, this fiscal element occupies the foreground. Even the good intention of administering the Post-office for the common advantage is hindered by the external circumstances of the situation. The lower the stage of development in point of density of population, roads, intercourse, enterprise, culture, etc., the greater are the expenses and the less are the receipts of the postal service. Compare Russia and England even at the present day. But as soon as these conditioning circumstances reach a vigorous development the whole situation changes. Even a very considerable degree of regard for "public utility" may be compatible with a fiscal surplus that is quite commensurate with the results obtained by the exclusively fiscal methods of administration, and it may even surpass them in this respect. When we come to look more closely into the essential

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occurs the following: "As concerns the competition of private carriers, it is to be said that they invariably have presently failed and vanished from the scene. This has been due particularly to two reasons: because the promoters of these schemes have set out from false assumptions, especially as regards the financial side of the undertaking; and because the service of which these establishments were capable has not been satisfactory. As to this latter point, it was a fatal mistake on part of the originators to suppose that it would be a very easy matter to establish a system of letter-carriage. It requires an extensive organization and a large capital; it requires centuries of experience, a thoroughly trained and select personnel; it requires a considerable exercise of control, buildings, a comprehensive mechanism for transmission, the support of all other state departments. ... At any rate the Post-Office has nothing to fear from competition from this source. Although the proposition has frequently been made, especially in the newspapers, that the postal law should be so broadened as to extend the monopoly of the Post-Office also to local letter-carriage, I have believed it to be my duty to express myself against this proposition and to assume a deprecatory attitude toward it. The Post-Office is nowise in need of an extension of its monopoly in this direction. It finds sufficient protection in the character of the service and in the confidence which it commands."

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character of this "public utility" in respect of its economic and financial value,<sup>1</sup> it will appear that in this case an important administrative function has attached to it, as it were involuntarily, an effective contrivance for the levying of a tax, such as to require that the post-office be taken up in connection with the theory of taxation.

Leroy-Beaulieu, the French writer on finance, in his *Traité de la Science des Finances* (1877), has duly conformed to this requirement. We here find a separate chapter<sup>2</sup> set apart for the consideration of *Droits sur les Correspondances et sur les Transports*, and the letter-post is the chief topic treated of.<sup>3</sup>

Having taken this point of view it will not be much of a strain for us to treat the surplus yielded by the state railways after the analogy of that from the post-office, and if our French authority ranks the taxation of freight on French and English railways with the taxation on correspondence in the form of a postal net surplus revenue - as I believe he properly should; then we may with even better reason class the net revenue of the state railway system with the net revenue yielded by the postal service.

The like holds true of all similar state establishments.

§ 78. The terms "Administration" and "Finance" used for purposes of contrast and distinction, as well as the entire course of thought contained in the present chapter, will find their full

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<sup>1</sup> See a discussion of the financial management of the means of communication by the present writer in *Schmoller's Jahrbuch. N. F.* vol. x., "Nationalökonomische Studien," 1886.

<sup>2</sup> *Livre ii. Des Impôts*, ch. xii, vol i. pp. 115 *et seq.*

<sup>3</sup> From this point of view, and in order to properly criticise and to second the further development of the existing system, it is desirable to determine what are the peculiar circumstances to which the surplus afforded by the modern postal service is due. It is, e.g., a fact too little known, that the surplus yielded by the German Imperial Post-office is not so much a net profit of the post-office establishment proper as it is a result of unpaid transportation by the railways. A more careful analysis - as yet a desideratum - would probably show that in case full payment were to be made for the transmission of the Imperial Post there would be no surplus but rather a deficit, especially with the present popular system of parcels-conveyance. Quite otherwise in England we shall get to that in its proper place.

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Justification only as an outcome of the discussion in the succeeding chapter on the various kinds of payments which are employed in the public economy.

In this way only will the real significance of the different methods of arrangement and treatment become apparent, whether the discussion deals with the question of the so-called quasi-private or "business" sources of income on the one hand, or, with taxes and fees on the other. In this way only will it become clear that, and with what propriety, post, telegraph, railways are managed according to maxims which are termed business principles, and that it is inherently necessary that they should always be managed according to these principles, without our taking any other standpoint with regard to the matter than that of public utility. This of itself will make it clear that all branches of the public administration, whether they yield a surplus or leave a deficit, are comprehended in the great complex of giving and receiving services, in which the just balance in any particular case depends on the form of compensation which the beneficiaries of the service may see fit to establish.

## CHAPTER III. DIFFERENT KINDS OF PUBLIC CONTRIBUTIONS.

LITERATURE. Lorenz von Stein, *Lehrbuch der Finanzwissenschaft*, 5. ed. 1885, vol. ii, part i. pp. 248 *et seq.*, 307 *et seq.*, 346 *et seq.* Adolph Wagner, *Finanzwissenschaft*, 3. ed. 1883, vol. i, secs. 202-212. F. J. Neumann, *Die progressive Einkommensteuer im Staats- und Gemeindehaushalte*, 1874. The Same, "Die Gestaltung des Preises," in *Schönberg's Handbuch der Politischen Oekonomie*, 3. ed. 1890. The Same, *Die Steuer und das öffentliche Interesse*, 1887.

### I. ANALYSIS OF THE SERVICES RENDERED BY THE PUBLIC ADMINISTRATION.

§ 79. If we picture to ourselves a community situated in some remote Utopia, all the members of which are precisely equal in respect of means and wants, it would be an easy matter to devise an equitable mode of collecting from them the means required to meet the public expenses. Since, by the terms of the abstract supposition we have made, the benefit which they derive from the public establishments as well as the ability to contribute toward the maintenance of those establishments, is precisely the same for each of them; therefore there could be no question of adopting any mode of contribution other than the simplest that is possible in any group of beneficiaries, that of apportioning the aggregate expense by a simple capitation.

If we make a search for such a Utopia in the real world surrounding us we shall find that this form of social organization is possible only on a relatively very small scale - only in case of segments of the strongly differentiated society of today, which are enabled to afford some sort of exemplification of our hypothesis only because they are far from being a reproduction of the community as a whole.

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I will take as an example one of our ordinary reading clubs, such as go by the name of "museums" in German towns. The membership in the case of these clubs is a strictly limited one. It consists of members of the middle or upper social strata, of approximately equal means, or at least practically so for the purpose in hand. The object sought is of such slight consequence, as compared with the aggregate of ends for which men band themselves together in, or have coalesced into communities; the difference between the advantages derived from the establishment by which this object is sought is so insignificant on account of its slight absolute value, that it is held to be permissible, indeed it seems imperative to disregard it altogether and proceed on the summary hypothesis of equal participation by all. It is to be added that there is a complete absence of all such external coercion as would make membership, with its burdens and benefits, an unavoidable duty incumbent on each individual; though, it is true, public opinion within the particular social circle concerned may exert a certain pressure, such as will somewhat modify this unconditional freedom with respect to participation in the payments.

At the same time it is not to be denied that, in spite of the fact of their belonging to a common social group, there do occur; among the hundreds of members that make up the club, a considerable number of instances in which the contrast in respect of means is great. It is also plain that different members partake in very different degrees in the advantages offered. It may vary from the maximum exemplified by individual cases of people who make the club-house their home outright, to the minimum at which membership has shriveled up into a mere social duty owed to one's rank or reputable standing, and from which not the slightest direct personal advantage accrues. These institutions resemble banks of issue in proceeding on the expectation that but a portion of the claims upon them will ever be presented at any one time; but with this difference as compared with banks of issue, that a part of the claims upon them are expected to never be presented at all.

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§ 80. As a matter of fact we find that even within the narrow limits of the clubs this convenient method of managing the accounts between the individual member and the aggregate is sometimes violated out of considerations of justice.

The first fact that brings about a graduation of the dues is the possibility of subdividing the privileges afforded by the club into separate items. The reading of books and periodicals at the club-rooms, the drawing of books by members, social entertainment in addition to the mere privilege of reading, balls in addition to everyday visits to the club-parlors, - these constitute particular items in the aggregate of what the club has to offer its members, and they may be so subdivided and distinguished as to allow members to accept a part or the whole as they may choose, and to pay accordingly. It is looked on as undignified, as well as impracticable, to go the length of graduating dues according to the length of time members spend in the club-rooms, the number of papers made use of, and the like, but these other differences above cited seem readily distinguishable and sufficiently appreciable to be made the basis of such a graduation. A second fact is to be noted. Difference in economic ability is also taken account of whenever it is indicated by some easily discernible external mark. It is true, the matter in question between the members being nothing more than a yearly fee of some 30 or 40 marks, it is not thought to be of sufficient importance to warrant an inquiry into the amount of income enjoyed by individual members, especially in face of the recognized difficulty of such an undertaking. But a difference in age and social position such as is indicated by a person's being a student resident at a university, as distinguished from the common run of members, affords an acceptable ground for some moderation of the amount of the contribution in favor of this special class.

Accordingly we find that even in a body of this character, proceeding as it does on the simplest possible principle of distribution, the need of differentiation makes itself felt in both of

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the two directions above indicated, and presently breaks down the original simplicity of method.

In proportion as the necessity of differentiation becomes urgent in either or both of these directions, and also in proportion as the amount of the contribution in question becomes more considerable and so makes it impossible to disregard the question of greater or less benefit derived, or greater or smaller burden to be borne, in the same proportion with there present itself the ungracious urgency of a departure from this conveniently simple rule of equal contributions, and with it the need of seeking a more complex rule of equity.

Finally, when we come to consider the case of public administrations, we find that not only are all the above-mentioned elements present in their greatest intensity; but there is also generally added, with all its grave consequences, the element of public coercion, - a fact which calls for redoubled mindfulness of all considerations in favor of equity.

§ 81. In order to apply these considerations to the problem in hand it will be necessary to make an economic analysis of the various classes of services rendered by the public administration.

The instant we abandon the utopian conception of a community made up of typical individuals we are forced to take account of the two causes of differentiation above spoken of. A detailed scrutiny of these two causes of difference is necessary in order to arrive at any adequate norm of equity, for guidance in striking the balance between the individual and the aggregate.

One cause of differentiation lies in the variety of the benefits enjoyed by the individual at the hands of the community; a second ground of differentiation lies in the variety of that which the individual members are in position to render in return. That is to say in other words: Difference of benefits received and difference in ability to contribute are the causes which decide us to enter on a closer scrutiny of the relations existing between the individual citizens and the commonwealths within which they are placed.

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First as to the difference in respect of the benefits enjoyed by different members of the community. There is a large field within which a method of settling accounts in due accord with this class of differences seems practicable. Whenever the state or the commune sets up an establishment which tenders its services to the citizen in such a form as to admit of their being subdivided and measured by tale or by quantity, an opportunity is afforded for making the individual pay *pro rata* for whatever benefit he receives, both as to quantity and kind. Post, telegraph, railroads, gas and water works, afford an opportunity for realizing this method of balancing accounts. The post tenders its services to all men, computing the remuneration on the basis of the number of parcels carried, their kind and weight, the distance and security against any extra risk. The dispatch of telegraphic messages is performed on analogous terms. In railway transportation the like method is employed with the principle of gradation developed to its highest. In the passenger traffic regard is had to the number of persons, the distance, the class of coaches occupied, the speed of trains, and the like; in freight traffic, number, weight, car-space, class and value of goods, length of haul, etc. Or in the case of gas or water works: in every house for which the municipal gas or water service is desired there is placed an apparatus which, by a simple mechanical contrivance, indicates the consumption of the household, and this measurement gives a ready indication of the amount of benefit for which the community may require payment from each of its members.

§ 82. Unfortunately this simple method of keeping accounts between the individual and the community, based on the measure and quantity of benefit rendered to the individual, deserts us very early.

This is true even as regards the particular establishments cited. Letter-carriage, passenger and freight traffic, lighting, etc., may take on the character of services rendered directly to the community as an aggregate, instead of being distributed to



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individuals in measured quantities, and the instant this happens the simple and direct method of accounts breaks down. The individual citizen is no longer the direct beneficiary of any one particular service rendered, but the aggregate of citizens profit by the undivided aggregate of services.

This happens whenever the municipal gas works are employed to light the streets and squares of the city. The light that fills the public streets affords the aggregate of individual citizens the needed artificial light without discrimination or admeasurement. Something analogous happens in the case of waterworks when employed for sprinkling the streets, in case of the postal service when employed to carry the mail for purposes of the public administration, in case of the telegraph when used, in peace and war, for the transmission of public dispatches, in case of the railroads when employed in the public service, and more especially if they are in the first place constructed for administrative or strategic purposes.

Moreover, this more difficult part of the keeping of accounts between individual and aggregate with respect to the benefits conferred on the individual by the aggregate by no means concerns something incidental or accessory. As a matter of history, it is in this direction that the original motive for the undertaking of this class of enterprises is to be sought. We need only to call to mind what was the origin of the post and the telegraph, the reasons which led to the introduction of municipal gas works, the fact that it was for military and administrative purposes, at least in the case of certain countries, that the earlier railways were constructed.

§ 83. But this second class of functions performed by these establishments only serves to direct attention to other much greater and more fundamental institutions to whose functions these are accessory.

I may here refer back to observations contained in chapter I., (secs. 37 *et seq.*)

The elemental function of every civilized state organization,

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that which constitutes the basis of every other of its functions; consists in the establishment of an authority which will secure the peace; and the authority performs this function all the more effectively the less it obtrudes itself on the consciousness of the members of the community. At the lowest stages of undeveloped national life the abiding relation between the enjoyment of peace and the disposition necessary to the maintenance of peace is constantly enforced by the direct evidence of the senses. The more we succeed in surrounding the life of every member of the state with an atmosphere of peace, and the more we are able to remove from his sight the instruments necessary for securing the peace, the less evident to the mind of the individual does the connection between the result and the necessary means become. The squatter who builds himself a cabin on an isolated farm in the Far West, or the able-bodied man in the primitive commonwealth, the pledge of whose security is his arms, or the burgher behind the walls of a mediæval city; to all these the correlation of the maintenance of peace and the enjoyment of peace is immediately and tangibly present. The modern man, the citizen of the civilized state of today, enjoys the results not only of a long historical development of institutions, but also of the indispensable permanent material instruments and structures. But they are both - the past and the present alike - so far removed from his perception that he has no appreciation of the manner in which alone this result can be attained.

Moreover, the farther the enjoyment of peace is dissociated in the mind of the beneficiary from the means by which the peace is maintained, the more difficult and complicated becomes the admeasurement of the benefit enjoyed. The isolated homesteader knows to a nicety the proportion existing between the instruments by which peace is maintained and the advantage he enjoys. The citizen of the modern German Empire would be able to appreciate it with the same exactness only in case it were possible to retail to the individual citizens the atmosphere in which they live, as gas and water are measured out to the consumer by a mechanical contrivance and paid for by the cubic foot.

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§ 84. The development of that organized power which forms the basis of every civilized commonwealth is the foundation on which every branch of public administration rests. The highest function of an imposing military power is the securing of the peace by convincing every intending disturber of the peace beforehand of the futility of such an attempt. With the European world in its present attitude this is the highest and best result we can soberly entertain hopes of reaching; for the feeling of a need of peace is present in but an imperfect way, and the impulse to violence is constantly lurking under the surface. So also is it in the internal domain of the administration of justice, which is concerned with deciding and enforcing disputed or violent points of law between members of the same commonwealth. The highest efficiency at this point consists in impressing upon the entire people a conviction of the absolute authority of the law, while it is at the same time indispensable that a comprehensive apparatus for the administration of justice should be maintained by the state, as in this way innumerable temptations to exceed the law, innumerable desires to question the legal rights of a fellow citizen or to infringe upon them with a high hand will be suppressed by the fear of the power with which the administration of justice is clothed.

That there still remains a considerable residuum of doubts and malice is due in part to the stage of culture, or lack of culture, as yet attained, in part to the practical difficulty of so clearly enunciating the law as to resolve all doubt. This much, however, is certain: So far as concerns the maintenance of that atmosphere of legality in which the members of a modern civilized community pass their lives, by far the greatest significance of the efforts actually put forth by the public administration of law, civil or criminal, lies in their serving as exemplary decisions that practically decide thousands of cases besides those immediately dealt with.

But from these considerations it follows that, in like manner as we have found it to be the case with the military establishment, the chief service rendered the citizen by the public administra-

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tion in enforcing the law is made up of that medium of morals and custom that can not be subdivided and measured in order to find how much of it goes to each individual. That is no doubt an exaggerated rationalism and radicalism that would draw from this, or at least from closely related considerations, the inference that the administration of justice should be gratuitous, as is advocated by Justi and repeated from his time down to the social-democratic programs of the present. But in all this exaggeration, it is to be said, expression has been found for a perfectly justifiable reaction against the opposite extreme - the tradition which had been handed down by the historical development of the public executive, - the one-sided exploitation of litigation and litigants for fiscal purposes.

The golden mean in this case is to be found in the acceptance of the principle of so-called gratuitousness accompanied by the requirement that the private individual who has wrought on the litigation shall pay for the special expenses involved. For while it is true, in accordance with what has already been said, that the particular case which comes before the tribunal is of the nature of a precedent serving to decide a thousand other cases, yet the case is at the same time a concrete application of the law, and as such it has to do with the interests of certain specific private persons who, for their part, are accordingly bound to show some acknowledgment of the fact. On the other hand, if the case had been simply a typical decision, rendered directly in the interest of the community, it would also have been a matter of concern to the community only, and not of special concern to any one individual in particular.

§ 85. The military establishment and the administration of justice are here selected for the purposes of an economic analysis, as typifying two great classes of the primary functions of the state. An exhaustive inquiry which should deal in detail with every branch of the state's activity is hardly necessary.

What is wanted is simply to bring out whatever may offer any peculiar feature in the way of principle or of consequences, in

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virtue of which the defrayment of its expenses requires special treatment in a discussion of the public finances. But it is not desirable to canvass in detail everything which may partake of these principles and consequences.

We may therefore go on to the discussion of a different class of institutions.

There are certain great establishments belonging to the public economy which, so far as regards technical availability, are very well adapted to the employment of the simple and convenient means of accounting which we have become familiar with in treating of means of communication and gas and water works.

There is the educational system. There are numerous private enterprises of an industrial character, of different grades, which are devoted to the purposes of education in all its varieties and gradations. These undertakings demonstrate the possibility of conducting establishments of this class on the basis of the payment of an equivalent from each beneficiary. Whether it be the smaller primary schools, or the girl's boarding-schools, or the commercial schools established by private enterprise, or the establishments devoted to preparing persons for the various civil-service examinations (and so entering into a peculiar sort of competition – *concurrence déloyale* - with the state schools established for the same purpose); in every case we find examples at hand which go to prove that it is practicable for educational establishments to dispense their services and to be paid for them by tale and quantity. It is nowise physically impossible in the case of these establishments, as it is in the case of the military establishment and the administration of justice, to subdivide and measure the services rendered, for the purpose of keeping accounts with the persons benefited by the services.

It must therefore be in whole or in part on other grounds that the state desists from the employment of this method of balancing accounts. These other considerations belong in the second class of considerations above (sec. 81) pointed out as going to decide the choice of a method of payment for public services, - namely,

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the difference existing between the different individuals and classes in point of ability to pay.

§ 86. With the Reformation the church handed over to the state the control of the schools as well as of charities. In consequence it has become the duty of the state to place the great business of popular education on a plane far higher than that indicated by the payment of an equivalent for the advantages enjoyed. The proper solicitude of the commonwealth for its weaker members, whether in spiritual or in worldly good, is a question of the first importance in this connection.

This thought has found legislative expression in the principle of obligatory attendance at school. It may have been embodied in an uninterrupted series of enactments reaching from the time of the Reformation down to the latest constitutional provisions adopted; or it may, as in the case of England, France, etc., have found its way into legislation indirectly, as the occasion for its application has arisen, now through the growing needs of a civilized age, now through the evils of modern child-labor.

But the principle of obligatory school attendance has everywhere had a severe struggle to assert itself, not only from the failure of the people to appreciate the benefit conferred in the instruction, but also, and especially on account of their straitened pecuniary circumstances. The surprising interval that frequently exists even today between the letter of the requirement and the actual facts of compliance is mainly traceable to the fact that the requirement of school attendance has conflicted with the pecuniary interests of the family. Any additional stringency in enforcement, any raising of the legal requirements, such as now-a-days belong everywhere to the order of the day, is feasible only so far as it takes due account of the economic situation of the parents: A child that is withdrawn by the school from household employment, from the farm, the workshop or the factory, and is put to non-productive employment instead of being productively employed, becomes by this fact alone a pecuniary drain on the parents.

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This state of the case - the existence of a conflict between the compulsory attendance at its schools required by the state and the pecuniary strain which the compliance with this requirement involves for the parents - makes it impossible, on grounds of expediency and of equity both, to apportion instruction and its attendant cost by number, length of time, etc., although such a method of admeasurement is not hindered by the intrinsic nature of our schools, considered from the point of view of industrial practicability.

§ 87. Such is the state of the case as regards that part of public instruction which is known as "popular instruction" in the narrow and everyday sense of the word. As regards those grades of public instruction which rank above the lowest grade, the relation between the public administration and the individual is essentially different. In the first place, there can be no question of compulsory attendance beyond a certain minimum of instruction enjoined on the entire population. Beyond this minimum the state cannot use coercion. The most that can be done in this direction is gradually to raise the minimum required. The difficulties in the way of enforcing the law as it now stands are so great as to constitute a sufficient warning against any headlong extension of the system of coercion.

It is further to be remarked that above a certain moderate grade of popular instruction the occasion for such coercion ceases. Those middle and upper strata of the population for whom the middle and higher grades of the public schools are intended, need no such coercion. They are in possession of the necessarily economic means, and the inclination to afford their children a proper development is also present in a sufficient degree.

Indeed, the consideration of an insufficient economic ability has no meaning in connection with these higher grades of instruction. The fact is, rather, that if we confine our attention to these higher grades the whole state of the case tends to reverse

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itself. For while it may be reasonable enough, and may even be both expedient and equitable to bear lightly on the scanty means of the lower classes of the people in connection with any such work of public utility, there can be no sense in sparing the adequate, or rather abundant, means of the middle and upper classes in the compensation required of them for benefits which they derive from public institutions. There must accordingly be some other reason present if any such element of gratuity appears in existing institutions of this class.

§ 88. This other reason is to be found in the conviction that the blessings a people derive from popular education are not confined to the benefits which the particular individual may derive directly from the school, but that the indirect benefit conferred on the entire body of the people, and therefore also on those who do not directly enjoy the middle and higher grades of instruction, is equally important. The conception is that the rays which science sheds penetrate with their heat and light every part of the social organism, and that those who are the immediate beneficiaries of the instruction imparted are but the bearers and dispensers of these benefits in behalf of the community.

How far this view is a true one is of course a question that admits of dispute. It will appear presently that this view involves peculiar dangers for the public administration, and that the extension of this view so as to include such other forms of state activity as in a similar manner serve the purposes mainly of the well-to-do portions of society, is to be admitted, if at all, only with the utmost caution.

It is therefore all the more imperative to take into consideration the possible concurrence of reasons of another kind.

Such a reason is perhaps the following.

It has probably always been recognized that the instruction offered in the upper and highest schools is really offered to those strata of society which are best able to pay their way, and that



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such exceptional cases of neediness as constantly occur might be provided for as exceptions by suitable remissions. But at the same time there has been a feeling that, unlike the eagerly coveted material advantages of the business world, the benefits of education, even of the higher grades, would not be sought for with due earnestness, and that it is therefore expedient to render advantages which are of such importance to society as accessible as possible. Payment in full for university instruction might, in itself considered, not over-tax the means of the beneficiaries. Still it has been thought best, in view of the actually prevailing disposition of moderate zeal on part of these beneficiaries, to minimize the disagreeableness of the demand upon them, it having been conceived to be for the public interest to reach as large a number of beneficiaries as possible.

It is clear that the discussion at this point turns on a difference of opinion, and that for this reason alterations in the relations in which public institutions of this class stand to the individual citizen are possible, such as would be impossible in a case where the decisive factor is the technical character of the institution itself.

§ 89. This fact, of a varying economic competency on the part of different portions of organized society, when developed in certain special directions, gives occasion for intervention on the part of the collective power in behalf of relative deficiency that may exist at any given point.

In the case contemplated, the deficiency exists not as a chronic debility on part of a particular stratum of society, but as an acute shortcoming on part of a portion of society which is temporarily in distress, or at any rate in need of assistance.

This fact seems to explain the numerous contrivances of the public administration by means of which it freely lends a hand to certain particular forms of industry. Agriculture, manufactures, commerce, transportation continually demand such measures for their assistance; whether it be that the private undertakings of individual citizens are granted subsidies from the pub-

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lic funds, or that public establishments for the like purpose are erected independently. State railways, or subventions granted to private undertakings; model establishments for manufactures, or protective duties and bounties; state-owned studs, or corn and cattle duties; these are all relief measures by which the surplus energy of the community is directed to the weaker spots.

Such weakness is most frequently due to imperfect development. And so we find that the great industrial commonwealths have all and several laid their collective strength under contribution for the purpose of developing the various particular branches of their production and building up their manufactures, commerce, shipping, to the standard of efficiency existing at the time.

But even when this degree of efficiency has been achieved it is of itself no sufficient guaranty against seasons of exceptional disturbance, which may in their turn be productive of further progress, but which for the time being require the application of such remedial measures against imminent dangers as only the community as a whole is in a position to afford.

The central thought in this connection is ever that of a solidarity of all the parts of the whole. The ruling principle is the conviction that if one member suffers all the other members suffer in consequence; so that for the maintenance of the common welfare the several members enter into a relation of the nature of a mutual insurance, in virtue of which now one now the other of the various members receives assistance.

§ 90. At the extreme limit, in contrast with the element of selfish interest and resting entirely on the fact of a difference in economic competency, is the provision made by the community for its paupers.

Here the decisive fact is the sensible difference in this competency between the members of the various classes of the population; a difference which at the lower limit merges into absolute economic inability, not only to meet the demands which the

public administration makes in order to satisfy its own needs, but even the ability to provide one's own livelihood.

It is this phase of public administration that puts to the severest test that moral sensibility which seeks to make the differing degrees of economic strength a criterion for the apportionment of the public burdens.

This sensibility has stood the test so far without failure, being less beset by doubts as to practice than as to theory.<sup>1</sup>

A variety of circumstances have contributed to this result. The first point to be gained was the broadening of that principle of nature according to which the able-bodied man is bound to support his needy relatives, so as to apply beyond the bounds of the very narrowest circle. In the original cantons of Switzerland the so-called kinship tax [*Verwandtschaftssteuer*] has subsisted even down into our times.

In the second place the influence of the Christian church - and in this respect there are precedents to be found not only in Judaism, as asserted by current theological opinion, but also among the Greeks and Romans - has ever been directed toward a broadening of the sentiment of fellowship beyond the circle of consanguinity, and its extension to the entire congregation and even to the whole of Christendom. The state of the time of the Reformation has fallen heir to the responsibility of the mediæval church in this matter, as also with regard to the administration of the schools. Indeed, the duties of the modern state have grown greater with the growth of intercourse in modern society; the progressive mobility of modern life has lessened the significance of the remoter degrees of kinship and so has shifted the entire responsibility to the political organization.

The legislation of the different states (at least of the Protestant states) has made so great an advance in this direction during the past century, and especially during the last few generations, and has made such serious demands on the public administration - in spite of the theoretical doubts of individualistic

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<sup>1</sup> Cf. a paper by the present writer on "Arbeit und Armut."- *Volkswirtschaftliche Aufsätze*, 1882, pp. 367 *et seq.*

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economists, as formulated more particularly by Malthus - that doubts on this head are gradually disappearing; and it is to be said they were also based on untenable theoretical ground. The feeblest of these objections, and at the same time the one most in vogue, was the position that while the moral obligation was not denied, the voluntary character of alms was made much of, and any legal claim to assistance was disputed. But if the moral obligation were once granted, the legal claim and therefore the public coercion followed as a matter of course in every case where voluntary charity proved insufficient.

§ 91. I believe the foregoing discussion has brought out the essential elements which it is necessary to consider in any analysis for economic purposes of the services and requisitions incident to public administration.

To summarize briefly what has already been said:

We have, first, a class of services of such a character as to permit the account between the community and the individual members to be settled by the simple method of a *quid pro quo*.

A second class, comprising the fundamental institutions of the state, does not admit of such a simple method of accounting, for the reason that the benefit conferred cannot be subdivided and measured. Such a method of accounting is applicable only in cases where institutions of this kind render some specific service to individual members.

A third class would admit of the method of accounting employed in the first class, but foregoes its employment in whole or in part, and substitutes payment according to ability in place of payment according to benefit received - with a view to the more general participation in the benefits conferred.

In addition to these there is also a fourth class, comprising cases of such disability, relative or absolute, on part of certain strata of society, as to constitute a claim on the greater ability of the other strata.

An analysis like the present can of course lay no claim to being a definitive exposition of the many complex elements

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which are to be taken account of in this connection. But it may at least be accepted as an attempt at presenting a simple and comprehensive view of the great complex of services rendered by the public administration, taken in their relation to the compensation required in return for them.

## II. THE VARIOUS KINDS OF COMPENSATION.

§ 92. Those services rendered by the public administration which belong in the first of the above enumerated classes are those that admit of being admeasured and requited by kind and quantity, so that each individual member of the community shall pay for what he gets. We have adopted as a briefer characterization of this class the standard of measure employed, i.e., the "benefit" enjoyed.

On looking about us to see what is usual as regards the forms which compensation assumes in industrial intercourse, we find directly that this class runs in the well-worn ruts along which the intercourse between private establishments is accustomed to move. The same form which has become the customary one in private intercourse for the discharge of thousands of diverse mutual services is also the form adapted to this class of public services. In looking into the history of the past we have seen how this most readily intelligible form of compensation, coming as it does closer than any other to the ideas and habits of thought of everyday life, has been found extremely desirable and acceptable for the purposes of the public administration, and also that its ready adaptation to the cruder views of early stages of national development has repeatedly led the government to extend its use to branches of the public business that are not by nature well adapted to it. Down to the present hour this method has been, and unquestionably also for a long time to come it will be found to be the most convenient, and it will therefore maintain itself wherever it can be legitimately employed.

If we want a concise designation for this form of public contribution we shall find it ready to our hand in the usage both of everyday life and of the science. It is of the nature of a price. Had

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this been the only form of compensation employed by the public administration, no other designation would have been required. The main facts of finance would then have been discussed from the standpoint of the general economic doctrine of Price, just as is conventionally the case with respect to the affairs of private life.

In any case we shall have to fall back on this general doctrine of Price wherever and to the extent to which it applies to this first class of public contributions. And for this first class the principle of Price is in fact to be taken as the essential principle by which to determine the proper amount of the contribution.

§ 93. In case we had to do with this class of contributions alone, the chief problems of finance would simply not exist. Every government undertaking would in that case automatically defray its own expenses - very much after the fashion of a public railway whose receipts are sufficient to defray operating expenses and interest on its fixed capital; it would then cease to figure in discussions of finance at all, or rather would not ask for consideration by the finance department, being fully able to take care of itself, - for the reason, in other words, that such a public undertaking would be competent to find any economic means it might require. The like is true of water works, gas works, post, telegraph, etc.

But such is the case only up to a certain point, and in fact, only up to a certain imaginary point which in the actual course of affairs is very rarely attained, - which, indeed, neither need nor ought to be attained, and which in many cases even cannot be attained.

The premise on which the view in question proceeds is this, that there shall subsist a precise equilibrium between the expenditures of the business and the receipts which it itself brings in. At the instant at which an excess or deficiency on one side or the other disturbs this equilibrium this whole self-sufficiency is at an end. An excess on the side of the expenses indicates a shortage in receipts, which will have to be covered by some

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other means; while an excess of receipts confronts the administration with the question, To whom does this surplus properly belong?

§ 94. But it follows directly from the essential nature of the purposes for which public administration exists that this equilibrium will unavoidably fail (cf. vol. i. secs. 400-402). The following are some of the reasons:

Among the more cogent reasons for the building of railways by the state (rather than by private enterprise) is the consideration that under the actually existing circumstances there is a necessary period of transition during which the receipts of the business cannot be expected to cover the expenses. The gradual development of the transportation system to such a position as to afford adequate receipts is a main part of the end to be sought by the public control of the means of communication.

Or it may be that the possibility of covering expenses is intentionally made subsidiary to the remoter object of favoring certain branches of industry, of goods, or of passenger traffic.

Deficiencies which may arise in this way will have to be made good from other sources. The nature of the causes to which such deficits are due indicates a difference in economic ability on part of the different sections and classes of the population; and, indeed; it indicates a difference in ability of such a character as not to admit of its being compensated for within the limits of this branch of the administration, but which calls for remedy from without.

On the other hand, it may happen (quite acceptably) that a surplus comes in from an undertaking which is primarily carried on for administrative purposes alone. A striking instance of this is afforded by the letter-post. If the administrative purpose in question admitted of no aim beyond the covering of its own expenses. Such a surplus would have no meaning, or at any rate no other meaning than that of a surplus in the hands of a consumers' club, which is returned to the members on the closing of the accounts for the year, in the proportion in which they have contributed to it.

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The fact that the postal service not only retains any such surplus, but even (with due regard to its primarily administrative function) consciously seeks it, is to be explained on the ground that, without hindrance to the administrative function, the different abilities of the citizens to contribute to public purposes may be drawn on by this means, with desirable results which are not attainable in any other way.

In this way the "price" of everyday industrial life becomes, in the service of the public administration, a means of levying a contribution of a different kind.

§ 95. This is more particularly the case when the "price" is not intended to serve the purposes of a department which partly or entirely covers its own expenses, but is with conscious purpose made the form under which, as a matter of expediency, a contribution is levied for other administrative purposes.

This happens in the case of those fiscal monopolies which make the enjoyment of such things as tobacco, salt, spirits, games of chance, a subject of traffic by selling the means to these enjoyments to the citizens after the manner of a private business. The purpose here is not (at least not primarily) the supplying of the public with tobacco, salt, etc., consciously adopted as a distinct administrative function on account of the advantage possessed by public as compared with private enterprise, but is adopted primarily, or even exclusively, because of the relative ease or convenience of this means of obtaining a revenue which is to be applied to ends that have nothing to do with the method of obtaining it.

§ 96. There is yet another form of compensation by means of which an administrative establishment may find the means it requires. This method also, significantly enough, has become familiar to us from its use in the intercourse of private life quite as much as from its employment for the purposes of the public administration.

This is the method of "contributions." In its everyday use the word suggests the method by which the members of a club



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or association balance their accounts. Such a club or association may be of a permanent character, or it may have been organized for a temporary purpose only; it may exist simply for purposes of gain or of generosity, from motives of public expediency or of benevolence. It will be seen that in this everyday use of the word the various motives which go to constitute the specific characters of these clubs and associations are lumped together under the one term.

But for the purposes of the science it is necessary to systematically analyze this diversity of character, as we are endeavoring to do in the present chapter. In practical; everyday life we apply the term "contribution" [*Beitrag*] indiscriminately to, payments made by members towards the expenses of a charitable organization, a clubhouse, or a dike; but science has of late properly appropriated this term to designate a particular class of payments. To my mind very appropriately it has been restricted to such payments as approach to the character of a "price" in the respect that in the case of the contribution just as in that of the price, it is possible as well as desirable that the individual benefit should be distributed by measure. The only respect in which these payments differ from the "price" is this, that there is a technical difference in the form in which settlement is made for the benefit received. While in the case of a "price" the measuring of individual benefit is carried to the extent of measurement by the piece, the unit of quantity of service - of which a great number and variety are turned out by a single establishment; the "contribution," on the other hand, serves for the creation of a common, comprehensive establishment which turns out an undivided product and answers the purposes of the members only if employed as a whole. A contrivance of this kind may benefit the contributors in varying degrees, and it may accordingly be paid for by them in contributions of various amounts to correspond with the varying measure of the benefit enjoyed.

Accordingly, in the case of the post, where the service performed naturally subdivides itself into hundreds of thousands of

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distinct items, which are, moreover, of many diverse kinds, the participation enjoyed by each individual can be equitably paid for only on the plan of paying a fixed "price" by the piece. A dike, on the other hand, which is built to protect adjacent lands against an encroaching stream, or a common drainage system serving to drain a connected group of estates, can and ought to be paid for only by apportioning the expenses among the proprietors in proportion to the benefit conferred upon the several estates. But this is precisely what is meant by "contribution."

§ 97. Neither "price" nor "contribution" are available forms of public income when the question is as to state institutions the advantage of which to the individual members of the commonwealth can not be measured and apportioned (secs. 83 *et seq.*).

This of course does not set aside the fact of a difference in the benefits enjoyed by different individuals as a result of this class of institutions; neither does it remove the necessity of seeking a method of defraying the expenses which shall take account of this difference in the advantage enjoyed.

The enjoyment of peace and civil liberty is unquestionably a privilege of very unequal value to different members of the commonwealth. The fact that these advantages cannot be measured or apportioned by no means prevents the rich and the poor deriving very widely different benefits from them. One who is able to call his own not only a bare existence but also an extensive estate, who may be exposed to the violence of foreign armies or domestic malefactors not only in his person but also in his property, is entitled or rather he is in duty bound to look upon the institutions which secure him against these dangers as being contrivances of the same kind with those coparcenary dikes which are constructed to protect his own and his neighbors' estates against destructive floods. He is bound to pay in due proportion for this peculiar advantage which accrues to his property above what other less well-to-do, or propertyless members of the commonwealth enjoy. The thought readily suggests itself, too, that it would be an equitable plan to gradu-

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ate the payment in proportion to the greatness of the property possessed, in a manner analogous to what we find in the case of "contributions."

It is also to be remarked that the greatness itself of these public institutions with which we are here dealing, and their far-reaching consequences, are the source of difficulties. But while it is not to be overlooked that these institutions do, in addition to their other purposes, also serve this particular Purpose, yet this is never true in such a sense that this special purpose - the securing of property against dangers from within and without - can be treated as their exclusive function, nor even as a function distinct and independent of their other purposes. Rather it is characteristic of a highly developed commonwealth that such an intimate connection prevails between the interests of the individual and those of the aggregate, with respect to every class of interest, that it would appear impossible to bring any one special interest - as here the interest of property - into a distinct and exceptional relation, in virtue of which it would be practicable to compute how much this particular interest owes to the national institutions.

§ 98. The absurdity of a computation of advantages, based on the assumption that the national organization is nothing but an insurance-office for property, and unmindful of the security afforded at the same time for human interests of a higher order, - the absurdity of this view comes out glaringly when we reflect that the means necessary to this security comprise not property alone, but also goods of a higher order. For it will not be questioned that demand is made upon such goods of a higher order, in view of the ever wider acceptance by civilized nations of, the maxim that every citizen is bound, to the best of his ability, to guarantee the national security even at the risk of his person and his life, at the same time that the culture of our time ascribes to human life an infinitely high value - a value such as is simply incapable of being measured by any industrial standard.

Clearly, when sacrifices such as these are demanded, the end

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to be attained by their means must be conceived to lie beyond the range of calculable economic advantage. Interests must be at stake which are of such importance as to justify the demand, if need be, upon the citizens' life as security for them. It would be absurd to stake one's life for the maintenance of one's ownership of economic goods. If we are in search of a single word by which to denote the aggregate of these higher goods, the word Fatherland probably is the one word that symbolizes to the modern citizen all those higher interests which, apart from economic goods, are what the national organization conserves. The citizen of the German Empire of today, who backs up the hard-won national union with an expensive armament and a universal liability to military service, is very well aware that these sacrifices by no means stand for the security of property alone, but that above all else their purpose is to secure the conservation and independent development of national characteristics in usage and law, in state and church, in science and art.

§ 99. In this way we come to what is the essential characteristic of the Tax proper. The tax is a payment made by members of a political community toward its expenses, simply in virtue of their being members and without its being possible to balance accounts as regards particular expenditures and the particular benefits accruing to individual members (vol. i. sec: 397).

We have already found in the discussion of first principles (vol. i. secs. 380, 398) that when the terms of the relation are in this way made to consist of the aggregate advantage of the commonwealth as such on the one side and the collective personality of the several citizens on the other, no method of reckoning is admissible in assessing the public expenses which does not provide that each citizen must contribute toward the common expense according to his ability. This forms the correlate, in the domain of economic means, of the now-a-days well-accepted principle of personal responsibility exemplified in the

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requirement of universal liability to military service. As in the one case solidarity of responsibility for the independence of the common country leads to the principle that every member of the community is held answerable for the welfare of the whole, in his person and his life, to the extent of his ability, as conditioned by sex, age and health, - so also in the matter of economic ability.

It is a problem devolving on the general theory of taxation to investigate the nature of these various kinds of economic ability which constitute the basis of the ability to pay taxes.

§ 100. In the case of the term "tax," as in the case of any of the terms used technically in the political sciences, it will be difficult to bring any precise definition of it into complete accord with the usage of every day life and the changes which this usage has undergone in the course of history.

If a definition of the tax is fixed upon in the manner above indicated, a considerable portion of existing tax legislation will be left unprovided for. There are taxes which are indefensible from the standpoint of this definition, but which it may be desirable to maintain on other grounds, and these not only occupy a large space in tax legislation, but have been growing in importance, or have even been introduced within the period of development of Political Economy and of the Science of Finance. Taxes which are levied without regard to the economic ability of the owner, and simply on the basis of the market value of a piece of land, a house, and the like, must either be regarded as very inadequately corresponding to the economic ability of the tax-payer, or they must be justified on other grounds, basing the plea for their retention on facts characteristic of these taxes alone.

But this kind of a justification brings us out upon that middle ground which lies between the "contribution" and the "tax," in the narrower sense above defined.

§ 101. There are, for example, certain special cases of gain resulting from expenditures incurred by the commonwealth,

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which are on the one hand so intimately dependent on the public functions of the establishments in question as not to admit of their being paid for by means of Contributions, while they are on the other hand so obvious and so considerable as in all justice to demand some special compensation.

We need only call to mind the close dependence of real property and its value on the expenditures required by the great, fundamental institutions of the State. And this relation holds in two different respects. First, there is no form of property that is so closely identified with the country as is real property, which constitutes, in fact, the physical substratum of any community.

Every contrivance which furthers the security and welfare of the state, therefore, is first of all of advantage to real property. Other kinds of property, so far as they are movable, can sever their fortune from that of the country; which real property never can do. So that even in virtue of this fact alone its special interest will in a peculiar degree bind it to the support of the national establishment. But in the second place, the same conclusion is even more strongly enforced by the phenomenon of which the law of rent is an explanation (vol. i. secs. 455 *et seq.*). As the origin and growth of rent is due to the activities of the aggregate and not to the efforts of the individual owner, real property is in justice bound to bear a specially heavy burden in the apportionment of the aggregate expenditure. The justice of this demand is also borne out by the history of our science. The earliest constructed system (that of the Physiocrats) put the recognition of this claim in the most unqualified form, in the demand that real property alone should be made to bear the public burdens; and the science has ever since, in spite of all its progress and purification of the physiocratic teaching, held steadfastly by the essential substance of this claim.

§ 102. But even apart from this, there is a great number of cases where there exists a special relation of dependence between private interest and public institutions. On comparing the expenditures which any great modern city,

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such, e.g., as Berlin, has incurred in the course of the past generation for the comfort of its inhabitants, with the simultaneous advance which shows itself in as striking a manner in enhanced values of building-lots as in any other one fact, we shall not find ground for assuming that a direct relation of cause and effect exists between the two facts in the sense that the enhanced value of building-lots is due solely to these communal expenditures.

At the same time it is not to be denied that the effects of these expenditures have very distinctly helped the value of building-ground. Improved streets, lighting, water supply, canalization, sanitation, police, schools, charities, etc., have in a very appreciable degree increased the attractiveness of the city as a whole, and of certain quarters of the city in particular, and have thereby increased the value of building-ground. The fact that apart from and independent of these expenditures such an increase of values would follow from the well-known nature of land, need not stand in the way of the effect of which we are speaking; the advance in values has been considerable enough to admit of a concurrence of several causes. Some of the improvements which have been undertaken at public expense are of such a kind as might have been undertaken directly by the owners of the property, or at any rate could have been carried out in a way by levying proportional "contributions" on the property owners interested. Such are thoroughfares, lighting, water supply, canals, and the like. Defective appliances for these and like purposes are felt by the occupants, - by the occupants of the particular pieces of property in the first place, and therefore also, and immediately, by the owners. In the absence of an adequate police provision for the streets and precincts in question a more effective and therefore more costly provision for security (in the way of area walls, manner of building, watchmen, etc.) will have to be made for each particular house. As soon as an adequate police force is present these provisions at private cost become superfluous, and the indebtedness of the private owner to the community on account of the provisions made then becomes obvious.

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A case of a still more special and immediate connection between public expenditure and private gain occurs where particular industrial pursuits on part of private individuals are the cause of some peculiar expense to the community; as, for example, the damage done to streets by heavy wagons, the damage to rivers from discharge of wastage, the burdening of public charitable establishments and the public schools (which are either entirely or prevailingly gratis) by the proletariat of the factory. It will be made plain later on that these peculiar special relations seriously affect the system of taxation.

§ 103. A special benefit enjoyed by property in general as an effect of the public establishments will hardly give rise to a special compensation by means of a peculiar tax. For a taxation proportioned to the economic ability of the tax payers will of itself effect this purpose. Indeed it effects it so thoroughly that as a result of the distaste of property owners for a proportional taxation and the desire for greater leniency in the burdening of property for public purposes, the contrary principle, of pecuniary benefit as contrasted with pecuniary ability, has been made to serve as an argument for a less than proportionate obligation.

The result of applying the principle of pecuniary ability is such a gradation of the sacrifices undergone for the good of the community as will discard the apportionment of the public burdens according to pecuniary interest and allot the expenses according to differences of economic strength. Further, this difference in economic strength has the consequence (as will appear farther on, in the theory of taxation) that the majority, consisting of the weaker members, will pay at a relatively lower rate than the minority of stronger members.

§ 104. A matter to be considered in connection with the question of what the community may equitably require of a member, is the varying size of the individual households that are the units with which the commonwealth has to do, and with



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which it usually deals through the father of the family. It is also a matter on which the most divergent and even contradictory views are held.

Now, as a matter of equity, it is evident that, counting the person as unity, the obligation due on account of advantages accruing from the institutions of society increases in the same proportion as the number of individuals deriving such advantages. The father of a family, whose domestic life comprises a numerous flock of children, owes correspondingly more to the community for the peace and security enjoyed by so many of his dear ones, than is due from the single man, the childless couple, or the man with a less numerous household.

This fact would seem less doubtful if it were not thrown into the background by considerations of quite another kind.

There is in the first place the undecided population question, which of itself gives rise to diverse and contradictory views. The one view - and this is perhaps, the most widely prevalent one, as it is also the traditional one - sees in the procreation and rearing of a numerous Hock of children a virtuous action, whereby the head of the household merits the gratitude of the community. This view will of course lead to a very extreme position, unless it is tacitly assumed to proceed on the premise that the household in question is possessed of the means necessary for such rearing of children. The mere procreation of offspring regardless of the pecuniary means required for rearing them is scarce looked upon today as a work meriting the gratitude of society.

Herewith we come to the point of transition from this first view to the second, which likewise makes this important function of domestic life a matter of serious interest to the community, though by no means in the sense that the end in view is the supplying of the greatest possible population and that the extent of participation in the accomplishment of this office is the measure of desert. The meaning of this second view is rather the position dictated by a scientific insight into the true significance of the movement of population (cf. vol. i. secs. 163 *et seq.*). This scientific insight into the question of population will not permit

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us to regard an increase of population as desirable on any such general grounds. It is, in truth, the standing fundamental problem which chronically and persistently obtrudes itself on society for a solution simply in consequence of certain fundamental instincts, and is a persistent cause; in all classes of society, of a discomfort to which society as a whole is at least as sensitive as the individual household.

It may also be remarked that even in case of an increase of population which is desirable from the point of view of the commonwealth, the state has no call to express gratitude. There can be ground for gratitude only in case the useful deed was done with a view to its usefulness. But of this there can be no question in the case in hand. The entering upon married life and the procreation and rearing of children are occurrences which, as moral facts, begin and end within the scope of self-interest and its peculiar instincts and inclinations; and if it happens that, by exception, these instincts and inclinations are sometimes accompanied by a conscious purpose of accomplishing what is for the public advantage, there are to be offset against this the much greater number of instances in which an increase of the family signifies nothing but a yielding to a self-interest which is harshly at variance with the interest of the community.

§ 105. If the discussion so far may seem to favor the view which insists on the recognition and compensation of those special public advantages which result from the size of the individual household, the whole matter assumes a somewhat different aspect as soon as the element of economic ability is also taken into account.

Taking the matter from this point of view, the heads of families may confidently count on a ready assent to their demand for a reduction of the burden of taxes on the plea that the man who is blessed with a flock of children is thereby rendered less able to pay the tax. It is not to be doubted that the economic ability of the taxpayer is lessened by the expense of supporting a numerous family, and that he is in consequence less able to contribute to the support of the public establishment than is

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another taxpayer, who, under otherwise equivalent economic circumstances, has no such family and consequently possesses a larger residue from which to contribute to the public purse.

This reasoning has repeatedly influenced legislation, and especially it seems of late, along with the ever-growing insistence on economic ability as the basis of tax apportionment, to be gaining an ever wider acceptance.

The limits of its application are indicated by the considerations mentioned in the foregoing paragraphs. These are, first, that for the benefits conferred by the state the greater number of human beings included in the household unit and so deriving benefit are properly chargeable in a proportionally increased amount; and second, there are the scruples due to a recognition of the principle underlying the growth of population, the apprehension being that legislation framed on these lines may unduly foster the already sufficiently prevalent misconception that the procreation of children is always and everywhere a meritorious service and that the community is much beholden for what is in point of fact the improvidence of individuals.

§ 106. But if it is true that the consideration of this personal: factor, of the number of persons comprised in the family represented by the taxpayer, affords no decided result, or at least none that has been clearly recognized in legislation hitherto, and if, further, the preferential benefit derived by the property owner in general from the public institutions (sec. 103) affords no sufficient occasion for varying the form of taxation from what would be adopted on other grounds, we shall find, on the other hand, that another factor above spoken of (secs. 101, 102) has a decided effect on the form which legislation takes. This factor is that enjoyment of peculiar advantages which attaches to the possession of particular kinds of property.

These peculiar forms of taxation accordingly occupy a middle ground lying between the territory of the Contribution proper and the Tax (in the narrower sense as defined above - sec. 100), for the reason that the advantages for which it is sought to collect

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payment are so intimately dependent upon and bound up with the general purposes of public institutions as not to admit of an equitable employment of the Contribution.

The result is a compromise with which we are familiar under the name of a Tax on Produce or on Proceeds [*Ertragssteuer*], or an Objective Tax.

The development of those sentiments, in the, course of history, to which this kind of tax owes its origin, discloses a gradual progress, both as regards apprehension of the nature of the tax and as regards apprehension of the relation subsisting between the individual citizen and the national organization. As to the point first mentioned, the course of development has been this: At the outset the taxation of "proceeds" or of "objects" was regarded as conforming to the principle that each citizen should contribute proportionally toward the whole of the necessary national establishment, while at a later stage it came to be the accepted view that the imposition of this class of taxes is expedient only within the narrower field which we have assigned them. As regards the second point, a growth of national sentiment is to be noted, in consequence of which the Income Tax came to be regarded as (in point of principle) a relatively less adequate means of balancing accounts between citizen and commonwealth, and has been relegated to a more modest sphere. The narrow self which was the determining factor in the earlier public sentiment has retreated within a more restricted field, within which it has better been able to hold its own.

§ 107. This is perhaps the proper place for some consideration of a form of public exaction which, since the time of K. H. Rau, has been distinguished from the rest of the national income under the head of Fees (*Gebühren*).

Fees have this in common with the Tax on Proceeds (*Ertragssteuer*) as discussed above, that they consist of a special payment for some special benefit which individual members of the community derive from the public institutions, beyond what falls to the share of the other members; or (what comes to the same

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thing as regards the matter of equitable compensation) the private interest of individual members occasions the commonwealth some special detriment (costs) which is to be made good by the members in question.

The difference between Fees and the Tax on Profits is this, that while it is intended that the latter, by means of annual payments, shall pay for effects wrought by the public establishment continuously through considerable periods of time, Fees on the other hand are payments rendered for isolated acts by which special advantages are offered or special expenses incurred for the benefit of individual citizens.

§ 108. It is well to call to mind at this point what was explained above (secs. 84-88), in the discussion in the course of which the Administration of Justice and Public Instruction were treated of as typical institutions.

In the course of that discussion we came to the conclusion that with respect to the administration of justice it is necessary to adhere to a middle course between the traditional financing methods of primitive public economy and the completely gratuitous administration demanded by the radicalism of the past one-hundred years. This middle course finds expression in the employment of the tax on the one hand and the fee on the other, as the proper method of defraying the expenses of the public administration of justice. The tax, in recognition of the incomputable benefit derived by every citizen - the advantage enjoyed in living in the atmosphere of peace and legality of a civilized state; the fee, in compensation for the palpable special advantage, or the special expense incurred for the benefit of individual citizens who may require the machinery of the courts to be set in motion.

An institution of a type somewhat different from that exemplified by the courts of justice is the public school. In this case the peculiar structure of the public establishment in question does not make it necessary, in order to comply with the demands of equity, that it should be based primarily on a tax; on the con-

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trary the advantages offered and the expense incurred in behalf of individual citizens are in this case quite readily computed and apportioned. That this method of apportionment is after all made subsidiary to the principle of the tax is due the conviction, based on social-political considerations, that a helping hand should be extended to the needy majority of those who make use of the schools. But in proportion as these straitened circumstances are not present, in proportion, that is, as the question concerns those grades of instruction which in a preponderating degree serve the purposes of the well-to-do classes alone, the necessity of apportioning payments to advantages enjoyed by individuals makes itself felt, and therefore arises also the expediency of fees.

It is true, the recognition of the indirect effects of public instruction modifies this view of the question to some extent. At the same time the requirement of that equity which is to be preserved as between members of the same social stratum, with respect to their varying pecuniary capacity, demands that this recognition should be allowed but a guarded influence. The outcome of all this is that in the middle and higher grades of public instruction a broad field is left open for the fee.

§ 109. We have now passed in review all the different kinds of public exactions, so far as they have hitherto been recognized and adopted in the administrative system of any political organization.

The foregoing analysis of the services rendered by the public administration, which constitute the basis of the corresponding forms of payments exacted, has brought to light one other important consideration in the way of peculiar motives existing in the relation of the individual to the community, but which does not result in any peculiar adaptation in the form of payments.

This is the difference in ability between the different individuals and strata of society already explained above (secs. 85-90). There is no further peculiar form of payment avail-

able to meet this difference. The form which we have come to know as a tax in the narrower sense will also have to serve for the equitable satisfaction of the claims represented by this consideration.

If the tax, in the sense above (sec. 99) developed, of itself goes in the direction of apportioning payment to ability, this further consideration, which demands that the stronger should assist the weaker, can only help on in the same direction and bring the tax system into a form that shall still more distinctly graduate payments in proportion to pecuniary ability.

What is exacted in accordance with this view will continue in any case to figure as a sort of "compensation," in the best sense, if the profounder view is taken of the relation in which the life of the individual stands to that of the whole - the view expressed in the old phrase of Montesquieu: "*en naissant on contracte envers la patrie une dette immense dont on ne peut jamais s'acquitter*";<sup>1</sup> which has again quite lately been expressed so felicitously by the English philosopher, Huxley.<sup>2</sup>

As Huxley, in his beautiful essay on the Struggle for Existence, says: "If I was not at my birth immediately annihilated I owe it either to the natural affection of those about me, which I had done nothing to deserve, or to fear of the law which had been established centuries before my birth by the society into which I made my entrance. If I was nourished, cared for, educated, I know of nothing I had done to deserve those advantages. And if today I possess anything, even if I owe to the sweat of my brow what I do possess, I must not forget that without the organization of society, which is the outcome of the struggles of a long series of generations, I should probably possess nothing more than a stone hatchet and a miserable hut, and even these would be mine only so long as no more powerful savage happened to come my way. But from this it follows that if society has done

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<sup>1</sup> *De L'esprit des lois*, vol. v. p. 3. It is true, Montesquieu's own theory of taxation is not in accord with this maxim: *Les revenus de l'état sont une portion que chaque citoyen donne de son bien pour avoir la sûreté de l'autre.* - vol. xiii, p. 1.

<sup>2</sup> In the *Nineteenth Century*, February 1888.

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all these things for me gratuitously, and then requires me to pay something toward its support - suppose this something is a contribution toward the education of children belonging to others - should be ashamed, in spite of all my individualistic inclinations, to say no. And in case I were not moved by shame, I believe society would be in the right if it were to convert its moral claim into a legally binding one. It would be thoroughly unjust to let the willing horse draw the whole load."



## CHAPTER IV. THE STRUCTURE AND FINANCIAL RELATIONS OF PUBLIC ORGANIZATIONS.

LITERATURE. Alexis de Tocqueville, *De la démocratie en Amérique*, 1834; 14<sup>th</sup> ed. 1864. L. Stein, *Lehrbuch der Finanzwissenschaft*, 5<sup>th</sup> ed. 1885, vol. i. pp. 50-89. A. Wagner, *Finanzwissenschaft*, 3<sup>d</sup> ed. 1883, vol. i. secs. 38-59. A. Wagner, "Reichsfinanzwesen" (v. Holtzendorff's *Jahrbuch für Gesetzgebung, Verwaltung und Rechtspflege des Deutschen Reichs*, vol. i. pp. 581 *et seq.*, 1871; vol. iii. pp. 60 *et seq.*, 1874). *Schriften des Vereins für Sozialpolitik*, vol. xii. -" Die Kommunalsteuerfrage," 1877. G. Cohn, "Die Steuerreform im Kanton Zürich und der Bundeshaushalt: der Schweiz," 1884 (*Nationalökonomische Studien*, 1886, pp. 315 *et seq.*); F. Freiherr von Reitzenstein, "Ueber finanzielle Konkurrenz von Gemeinden, Kommunalverbänden und Staat" (*Schmoller's Jahrbuch*, 1887, 1888). "Das kommunale Finanzwesen," by The Same (*Schönberg's Handbuch der Politischen Oekonomie*, 2<sup>d</sup> ed. 1885).

### I. THE STRUCTURE OF THE COMMONWEALTH.

§ 110. If I use the expression "public organizations" (*öffentliche Verbände*), rather than "the public organization" it is because the unity of that public organization which answers to our concept of the state presents itself to us in the guise of a multiplicity of organizations, rising one above another and resulting in a totality only through their organic union with one another.

From this point of view the state presents itself to us as a structure making up an undivided whole, rising to a single, central apex, but the constituent parts of which rise one above another in sharply defined gradations.

In the current views of the matter this unity is but imperfectly apprehended, as is shown by this, among other things, that the inclination commonly is not so much to conceive of the state in this broader sense, but rather to narrow the concept far enough

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to admit of contrasting the state with its own constituent parts. This view has a substantial ground in the sense that it is a survival handed down from an era when the national idea was yet engaged in a struggle to reduce these disjointed members to order and unity; but it is a conception which falls far short of apprehending the essential character of the modern state.

§ 111. If we examine the state, considered as a structure of the nature indicated above, the lowest form of political association is the Commune (*Gemeinde*).

The commune is the elementary structure, both in the sense that it is accepted by the consciousness of the individual members as the immediate fundamental form of public organization, and also in the sense that in point of historical development it is the first link of the chain.

The characteristic feature of the commune is the fact that it is a neighborhood organization; which owes its origin to an extension of the relation of kinship beyond the limits of the family and the individual household, and signifies that the members of the commune have come to share in those good offices of human intercourse of which, within its narrower sphere, the family affords a ready illustration.

The nearer we approach its beginnings, the more self-contained and exclusive is this elementary social organism; the more does it unite in itself all the essential functions which in the course of development fall to the state. The commune is the ultimate cell, as it were, of the state, from which, by progressive segmentation and differentiation, arises the organism with which we have here to deal.

§ 112. The character of this neighborhood organization is somewhat modified by the divergent conditions under which rural and urban social life is carried on.

In the historical development, the rural commune, occupying a greater space, is the earlier of the two. The large area occupied by agriculture as contrasted with handicraft and trade, requires

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a relatively great extent of inhabited country, which distinguishes the rural from the urban commune. On the other hand the intensive character of the distinctively urban occupations brings about a great and constantly growing concentration of the population of the commune within a relatively narrow space.

In the very beginnings of towns and town-life this contrast is not perceptible. During the earlier centuries of the Middle Ages the legal maxim that nothing divides the burgher from the peasant but the town wall, is literally true. The towns are nothing but fortified hamlets - places of refuge and asylum in a country of peasants.<sup>1</sup> Every town was united in a defensive league with the unfortified villages; the villages were bound to keep the walls of the town in repair, in return for which they found refuge behind the walls in times of war, with their goods and chattels.

But it is evident that the advantages of continuous residence within the walls would especially accrue to those whose occupation least led them out into the open country, such as handicraftsmen and tradesmen. Hence the mercantile character of the towns was a consequence of that slighter requirement in the way of space, which could find room enough within the town walls. Hence, also, the towns became the seat of all those occupations, offices, functionaries, which in this respect resembled handicraft and trade.

As the development goes on the relative importance of the characteristic features of the town is reversed. The walls of the town fall under the sway of the new departure which is changing the face of matters political and military. Concentration of population and social intercourse now come to be the decisive characteristic.

The shifting character of the concept of the mediæval town, which is such as to embarrass modern statisticians, comes partly of a failure to distinguish between the historical and the

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<sup>1</sup>K. Bücher, *Die Bevölkerung von Frankfurt am Main im 14. und 15. Jahrhundert*, vol. i. p. 469. Cf. Maurer, *Geschichte der Städteverfassung*, vol. i. pp. 125, 491 *et seq.*

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economic connotation of the term, partly from the impossibility of drawing a hard and fast line of demarkation, in the economic sense, between the town and the rural commune.

The facts lying on the border between the two classes do not, however, constitute any obstacle in this any more than in other, analogous cases to the recognition and acceptance of an essential contrast which in a typical way marks off the modern city from the commune of the open country, a contrast founded on the density of population and the higher tension of social life. Hence that dissimilarity of communal life and activity, in aims, functions and powers, which presents itself to our view in an imposing form in the modern city corporation, as contrasted with the rural commune.

§ 113. Although the commune attempts to perform the elementary functions of the state, we still find, even in the ruder stages of culture, an organization wherein the fundamental fact is the submission of a number of communes to a superior power.

This superior power arises partly out of a superimposition of the stronger political organization upon the weaker, partly out of an organization of the smaller units into a larger whole. The ambiguity of the term State, above referred to, is largely due to this fact. In its historical development this subordination and incorporation takes the form of a contrast between the greater political unit and the less. From the point of view of the developed state the commune is regarded as a part, the state as the whole.

This contrast between the part and the whole, between the elementary organization of the neighborhood community and the national dominion that includes all these individual primary units and binds them together in a sovereign whole, expresses the most striking fact of the organization of social life.

The State stands forth as "the self-sufficing," the complement of organized social and political intercourse, varying - with respect to the extent of population which it comprises - with the

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stage of development which it occupies. The commune, on the other hand, is the group next removed from simple individual existence, and its repetition in a series of structurally identical units constitutes the substratum on which national life rests.

§ 114. Within the field of these two fundamental phenomena of political life - the commune as the elementary fact, and the state as the centralized organization of the whole - is further developed a diversified multiplicity, both of intermediate members whose special functions intervene between the commune and the state, and of peculiarities of structure modifying the central organization of the state itself. Naturally, as the interval between center and circumference widens, expediency leads to the introduction of certain intermediary institutions, whose purpose is the performance of functions which lie beyond the sphere of the local commune and still do not fall within that of the central authority.

These intermediary structures are the outcome partly of that historical development whereby the smaller political units are subordinated and organized into constituent elements of the greater whole (counties, provinces), partly of systematic constructive effort which, starting from the national center, lays down the boundaries of the lesser administrative units (precinct, ward, arrondissement, department).

Under the head of qualified centralization of the sovereign state we shall have to take up the class of political phenomena of which our recent history affords so many examples.

The relation of the individual states of the North American Union to the Union as a whole, the analogous relation of the Swiss Cantons to the Confederation; the relation of the individual German states to the Empire, the different relations of the same states to the German Confederation before 1866, as well as the relation of the Swiss Cantons to the old Helvetian League previous to 1884, - all these are questions which belong under the above head.

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The aim has thus far been to call attention to the facts of the organization of public bodies; we shall now have to discuss further what are the causes to which these facts are due.

## II. THE CAUSES AFFECTING THE STRUCTURE AND ORGANIZATION OF PUBLIC BODIES.

§ 115. A comparison of the several states of Europe (or states representing European civilization) from the point of view of structure brings out such a multiplicity of forms, existing and extinct, that we find ourselves obliged to begin with a consideration of the historical grounds of this diversity of structure.

What, for example, is the reason that in France and England the functions of the central national authority have for centuries past been vested in a stable centralized state, in which no subdivision or diffusion of the supreme authority, in the sense of a subdivision of sovereignty, is traceable; while in Germany on the other hand, the wearisome advance toward national unity has been content to leave the sub-states their sovereignty, at first with the fuller measure of sovereignty they enjoyed under the Confederation, and afterwards with the diminished measure of autonomy which they possessed under the Union, of which a good share has had to be conceded to the newly constituted Imperial authority? Again, what is the reason, I ask, that Italy, immediately on emerging from the earlier disunion of its petty states into a reconstituted national unity, was able, as contrasted with Germany, to achieve at a stroke the finished unity of the entire nation, with complete suppression of the previously existing sovereignties; while on the other hand the Swiss Confederation, with a country and population no greater than a German principality, such as Baden or Wurtemberg, is still far from having achieved the unity of such a German principality, and even fosters the relatively great independence of its constituent cantons as a characteristic and essential source of strength; and the modest measure of centralization hitherto attained by the Confederation in the constitutions of 1848 and 1874 has only with

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great difficulty been wrested from the traditional sentiment of particularism?

And what is to be said of the Austrian Empire - the latest exponent of the time-honored velleity for a Roman world-empire - which still holds in union (or rather has but now united) wide dominions and diverse nationalities, the union of which has, during the past generation, wavered between the necessity of an absolute or a relative disintegration and the possibility of a greater measure of consolidation?

Foremost among all that goes to explain these differences stand the great number and variety of historical conjunctures, and the peculiar historical situations of the different peoples.

§ 116. Sober rationalistic reflection alone, without regard to the conditioning historical circumstances, will never be able to satisfy itself that there is any sufficient reason why:, these differences do or should exist. The great result of a development of peoples and of states is worked out by the combined action of many forces, both helping and hindering, and the outcome is necessarily a different one in each particular case; indeed, the very substance and purpose of the movement-the development of the nation-is itself of a mutable and fluctuating nature. Only if we take this fact as our point of departure shall we come to appreciate that in this field the force of special circumstances must, in each case, prevail over the forces that make for the norm of greatest expediency.

But from these considerations it is clear that, as concerns this particular point, the destiny of the English, the French, the Germans, the Swiss, is a "destiny" in much the same sense as is the life-lot of any individual. That is to say, the helping and hindering circumstances encountered in the outward conditions of life are, at least in some degree, qualified by the intrinsic character of the peoples themselves. Or even if this be disputed, it will at least have to be conceded that the course of outward events has reacted upon the intrinsic characteristics of the people (as e.g., habitual political centralization has acted

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upon the character of the French, or excessive political subdivision on the character of the Germans), and we shall therefore; in any case, come back to the fact that the specific character of a people determines the peculiarities in structure of its political organization.

On considering from this standpoint the relation in which the individual states of the German Empire stand to the federal state as constituted today, we find that, owing partly to habituation to the traditional form of political organization, partly to the desire for an immediate control of the local administration, the newly constituted imperial government has been vested with only such powers as are indispensable in order to secure for the German people the necessary degree of cohesion over against the other great nations.

And in the relation of the Swiss cantons to the federal authority of the League, there crops out at every turn - and all the more saliently that the traditional political unit is here so diminutive - a great and effective particularistic aversion to federal-national institutions. And this state of affairs seems to be a faithful expression of the national character, for in no other country is such thoroughgoing provision made for the control of the course of public affairs by the popular wish, at least as concerns a restrictive control.

§ 117. We are therefore able to formulate the proposition: In like measure as any people has achieved its own unity in its struggle with external and internal obstacles, will the aggregate of its political functions take the centralized or the decentralized form.

Only we shall have to add that the concept of a "people" as here used, is itself an historical category and is accordingly of a shifting nature (cf. vol. i. secs. 329 *et seq.*). The Swiss nation has arisen out of a number of smaller "peoples," who even to this day - obstinately tenacious of old-fashioned ideas and opinions - feel themselves to be distinct peoples; but taken as a whole, the Swiss are, as a nation, rather to be com-



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pared to the Suabian nation than to the German. The German nation of today is after all but an historical datum of the present period, and is neither in prospect nor in retrospect to be looked upon as an immutable and indissoluble unit.

If we take a still broader field, so as to comprise within our view that comprehensive republic which is an aspiration of the past and of the remote future alike, - which includes within itself several great heterogeneous nationalities, - we are met by still further special modifications, whose purpose is to reconcile the diverse tendencies of unionism and separatism. In Austria this diversity of nationalities is the occasion of various, partly experimental, arrangements and understandings between the whole and its parts. In Switzerland the discrepancy between the German and the Romance nationalities contributes its share toward the difficulties which the traditional separatism of the country entails on the federal commonwealth.

It is still an open question how far it is practicable to construct a homogeneous commonwealth out of diverse nationalities, even where external circumstances favor, and where the foreign elements are inconsiderable both in quantity and in degree of diversity.

§ 118. But after having in this way allowed the widest scope to historical circumstances and to peculiarities of national character as factors in determining the structure of the commonwealth, it will after all appear that, on the basis afforded by these historical circumstances, the great factor of simple expediency must have its effect. This factor will always, in every land and people, make its claims heard, and will prevail. It is this factor, with all its tactful sagacity, that must ever prevail, both in the present and in the remoter future, in its struggles with the essentially mutable historical situation. It is this element that gives occasion for improvement and innovation in the management of political affairs both local and general, - for the change or abandonment of methods as the progress of knowledge may direct. And finally, this factor is most facile in accepting sug-

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gestions from observation of the institutions of foreign states. Indeed, the varied historical development of different states and countries is itself, even, an outcome of this expediency of institutions conforming itself to the pressure of the peculiar situation in each particular country. And it is precisely the discrepancy which exists between the organization handed down by history and that struggle for practicality which is latterly making so great a stir, that has led to an intelligent appreciation of the basis on which this factor of expediency rests. It is precisely this international character of the modern progress of knowledge and of the movement for practicality that has brought about a certain uniformity of type in the methods of administration in all countries, as contrasted with the diversities of national character.

How is it possible for the system of petty administrations under the cantonal autonomy of Switzerland to hold its own against the modern demands for centralization? How is the German principality's traditional jealousy of its sovereign powers to be reconciled with the ever-increasing requirements of national life in the direction of national institutions under imperial control?

No answer to such questions as these is possible without a discussion of the factor of expediency and practicality, which supplies the motive for the one tendency or gives support to the other.

§ 119. The prime factor bearing on the question of structure and organization is the simple fact of size.

It is possible for a single commune, especially under the stimulus of the latest improvements in means and methods of intercourse, to attain such proportions, in population and in popular wants and capacities, as will call for the performance of functions that are ordinarily required only by a group of populous communes and circles [*Kreise*]. The municipal commune of Berlin has functions to perform such as nowhere else in the Kingdom of Prussia fall to the share of a civil division of lower rank than a province, and, indeed, through the latest legislation it is in fact constituted a province.

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On the other hand, there are many village communes so small as to be unable, both on the score of size and of strength, to support the usual institutions of a municipality, and which are therefore compelled to unite for these purposes with neighboring municipalities.

Conversely, the requirements in the way of magnitude, due to practical exigencies of various public establishments, vary with the technological character of the different establishments in question.

The diversity of practical requirements and demands on this ground is analogous to the difference that exists between wholesale and retail business in productive industry.

This point merits more detailed examination.

§ 120. There are certain special branches of the public business for which this analogy holds, strictly and in detail, - for which the relation is not simply that of analogy, but is in fact identity of principle.

The post and the railroad are typical of this class.

These not only belong to the general class of undertakings which require a large investment of capital, and which in order to be employed to full advantage must be organized in a single consolidated system and be the exclusive purveyors of the public wants they are intended to serve; they constitute a genus of their own within this general class, inasmuch as it is their purpose, provided, for in their material requirements, to cover a very large territory and so lessen the distance between men and goods as far as possible. This purpose they accomplish all the more effectively the greater their extension and the more thoroughly consolidated their management. It may even be maintained that the trend of development in this direction in the case of these means of communication is not limited by national boundaries, - that the ideal in their case is a unified international system.

The consequence of this peculiar industrial character is that the post and railway system always expands as far as the bounds of the most extensive political organization that lies within the State's

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jurisdiction will permit. These means of communication immediately fall, or tend to fall, under the management of the central authority, wherever the modern process of consolidation of petty states takes effect. And these branches of the public service are the part that first drops out of public control and falls into private hands whenever the structure of centralized national public service falls into decay through the overgrowth of constituent structures vested with sovereign power. But even when under private management, the technological character of these branches of industry requires their organization on an equally extended scale.

These branches of the public service, moreover, have for some time past shown a tendency to an international organization, pushing boldly forward over the boundaries of great empires and nations, on the road to an international union, - e.g., the International Postal Union, the beginning already made toward a uniform system of railway service and railway legislation.

§ 121. The reasons for vesting the control of the really fundamental institutions of a people in the most comprehensive political organization into which that people enters at the time are of an analogous nature, though mixed with considerations of other kinds.

The system of defense is clearly made more effective by a consolidation of the national forces and an orderly disposition under a centralized management. In the latest forward step taken by Germany (and by Switzerland) this reconstruction of the military system occupies the most prominent place in the programme of national regeneration: a union of the scattered forces of the people into a single consolidated force.

Viewed from the standpoint of practical efficiency, there can be no question of a subdivision of the military power, in the sense of surrendering the control of particular fragments of it to minor political divisions. Wherever anything of this kind occurs it can only be of the nature of a concession to insurmountable historical circumstances.

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Apart from the technological advantage gained by this consolidation, its great importance as an element of national strength lies in the moral force of a sense of national unity, of which no other form of expression is so adequate and so effective as a united national army.

The requirement of centralization in the administration of justice is not equally uncompromising. As contrasted with the material mechanism of the army, the essentially intellectual structure of the administration of justice proceeds, in its transition to the centralized form, more slowly and by a greater number of intermediate stages. Hence a greater length of time is apt to elapse before the most expedient degree of consolidation is attained, in the case of this than in that of the other institutions spoken of. Special (local) laws and systems of law may survive for generations after the unification of the military system has, under the heavy pressure of necessity, been perfected. But it is only that the tendency toward centralization on the part of the administration of justice is more pliant; the tendency is no less distinctly present here than elsewhere.

For this there are two reasons.

In the first place - in spite of all the tenacity of the particularist spirit - the influence of national unity must continually make for an ever more thoroughgoing uniformity in the administration of justice, because it will in the long run prove insufferable for a politically united people to accept more than one award as the truth in any given case, and because the consciousness of a common national life, a social solidarity of all the members of the nation, grows ever stronger and more pervading with the growth of improved means of communication.

In the second place, when a judgment reads, "in the name of the king," it imparts to the decision a superior sanction that removes it from the petty sphere of village affairs, and so gives it a character of impersonal generality that virtually works a change of venue from the immediate neighborhood of the interested parties.

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§ 122. The case is different as regards the system of public instruction.

Here the plan of organization and gradation is very similar to that of the state itself. The grades in the school system rise one above another in close correspondence with the gradation of the classes of society to whose wants they minister. The lowest and broadest stratum, the elementary schools, corresponds to the lowest and broadest stratum of society, to that portion of the population which is specially designated the "people" ("popular schools") [*Volksschulen*]. Towards the apex the breadth of the strata dwindles, to correspond with the diminishing breadth of the upper social strata to whose wants the higher grades of instruction minister. So that the very apex of the pyramid, the high-school system, meets the least considerable demand.

The greater the breadth of a given grade in the school system, the more does it approach the broader substrata of the political system in its plan of organization; thus the elementary schools resemble the communal system, in so much that the extended need of elementary schools - being sufficiently great to afford both adequate demand and adequate means of support for such a school within the limits of a single commune - relegates the management of this grade of instruction to the communes as a matter of course. For a school of a higher grade the demand as well as the means of a commune are insufficient, unless it be an exceptionally strong one. For a high school, except in the case of the largest cities, the needs and the means of a single commune are still less adequate. Accordingly, the high school and the university regularly become a part of the business of the central organization of the state. Besides this, there are some of the larger towns that support academies, provinces that support technological schools, etc.

There is still another special reason why the highest institutions of learning should continually more and more gravitate toward the control of the central authority, even in cases where the local organization might be large enough and strong enough to employ and to support them. Precisely the highest organ of

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control which a nation possesses is the only one that is capable of occupying a standpoint sufficiently high for the adequate administration of its highest schools. The lower we descend in the scale of political stratification the greater becomes the danger from influences which tend to impair that intellectual freedom which is essential to the best scientific work.

But it happens here, just as in the case of the administration of justice with its system of higher and lower courts, that the ideal nature of the institution makes possible a longer continued compromise with inherited particularist methods than is practicable in the case of those great institutions of peace and war that rest on a system of material appliances, whose physical character makes a correspondingly tangible demand for a centralized management.

§ 123. The above discussion of the functions devolving on public bodies has led us step by step from the sphere of what may be called national industry on a large scale to that of national industry of a retail character.

What is it that is counted to the credit of the small industry in production?

There are certain industrial and socio-political advantages. First, the close relation between individual interest and the factors of production, such as is possible in a small establishment; whence results a corresponding care and economy with regard to the expenses of the business and the quality of the work done. Second, as viewed from the social standpoint, the subdivision of industry into a great number of small establishments gives rise to a greater number of independent entities, which, as contrasted with the centralizing tendencies of the large industry and the harsh disparity between the large capitalists and the proletariat, creates a large and powerful middle class.

In both of these respects it is possible to find something analogous in the field of public administration.

In the former respect there is the notable instance of the administration of poor-relief.

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The freedom of movement of modern life, and more especially of the modern proletariat, constantly urges the transference of the poor-management of any country from the hands of local authorities to the national administration. The petty casuistry as to the precise obligations of the different local units, as also the manifest over-taxing of particular ones, has often suggested the desirability of such a reform of the poor-management as would place it directly in the hands of the state. But projects of this character have uniformly been rejected. There is always the danger that the local organization having charge of the poor-relief will use no economy in the management of resources, with the gravest consequences both morally and financially - the waste of public means and the attraction of paupers.<sup>1</sup> The commune therefore remains the body with whom the responsibility and the discretion in matters of poor-relief immediately rest, since here alone we can expect to find the requisite solicitude and personal knowledge coupled with an economical use of the necessary means. Management of the poor-relief by means of a centralized system of officials is entirely out of the question. It is only in those matters connected with the poor-management from which this financial and ethical difficulty is absent that the larger political organizations properly can take a hand.<sup>2</sup>

§ 124. As to the second point, it has been insisted on with great frequency, especially of late, in the course of the struggle for political liberty and popular participation in the management of public affairs, that the solid substructure of a vigorous and effective communal organization is indispensable to any sound national political life. The oft-cited example of England is well known. It is also well known that local self-government in England, through the ascendancy given it by the people's historical development, has retained such a degree of vigor as to have held its ground for a long time in the struggle against the

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<sup>1</sup>E. Münsterberg, *Die deutsche Armengesetzgebung und das Material zu ihrer Reform* (vol. vi. of *Schmoller's Forschungen*), 1887, p. 306.

<sup>2</sup>Adickes, *Zeitschrift für die ges. Staatswissenschaft*, 1881.



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centralizing tendency of the time; and this result is by no means due solely to superior efficiency on its part in serving the public needs.

It is therefore to be remarked that there are certain branches of the public service, which, in point of technological adaptation, readily admit of being administered by the central authority, but which still are everywhere administered by the commune simply because they afford a field of activity for the latter, at the same time that they admit equally well of being managed by the local body.

The care of streets and thoroughfares, as well as their construction, repair and lighting, is always the business of the communal administration of the locality whose needs they serve.

It is otherwise with the local police. The management of this branch of the service may fall to the local administration or to the central authority, according as the dominant view is or is not the one above indicated. The greater the difficulty of the task, the more its adequate performance becomes a matter of more than local interest, and of importance to the nation at large, the more does the inclination toward a national administration of the police come to prevail. Hence we find the latter method adopted for large cities, the former for smaller towns and villages.

### III. THE FINANCIAL RELATIONS OF THE MEMBERS OF THE COMMONWEALTH.

§ 125. The foregoing discussion has, for the sake of clearness, passed over an important factor which we shall now have to examine.

No mention has been made in the foregoing of the differences in benefit derived and in ability to pay, due to differences in the relations subsisting between the state and its constituent parts, and between the parts among themselves. These differences are especially noticeable in a great empire comprising a considerable area and a large population, with the consequent variations in

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wealth and needs from one locality or one civil division to another.

In point of fact, there is, strictly speaking, nothing among all the variety of public apparatus and service which serves the ends of the various parts of the nation in an equal degree; and there is no one part of the country, no province, no town, which is exactly on an equal footing with any other part or town in point of ability to contribute to the state.

But this being so, it will be found that special problems arise out of the question: What effect should these differences in the advantages derived and in ability to pay, have on the financial relations subsisting between the nation as a whole and its various constituent parts?

The variations may conceivably be as great and as many in this case as in the case of the individual's relation to the state, with respect to variations in point of individual benefit and ability.

§ 126. In the first place, as regards the different degrees of advantage derivable by different parts of the country, the difference is present even in the case of such establishments as appear on the face of the matter to serve only a common and undifferentiable public purpose, which are equally of advantage to every part of the nation. So, e.g., the maintenance of a defensive armament is most certainly of greater, more pressing importance to the border provinces that are exposed to the incursions of an aggressive foreign nation, than to the provinces lying in the interior of the empire or bordering on the territory of a peaceable people. It is likewise of greater importance to the great city, the modern industrial city of the large class, whose peace is threatened from within by the turbulence of a revolutionary proletariat, than to the unruffled, peaceful rural commune, or the humdrum existence of a provincial town.

Passing to the opposite extreme, to that class of public establishments whose strictly localized character emphasizes the fact that special benefit is derivable from them by persons living in

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the place, we may cite the construction and care of the streets in a city, with all its attendant expenditures.

It would of course be an exaggeration to say that the streets of a town are of use to none but its inhabitants. The tendency of progressive improvement in the means of transportation and of the centralization of trade, is in fact rather toward giving the inhabitants of the whole country a share in the local advantages enjoyed by its largest cities. But the local gain is after all in this case so far predominant as to remove all doubt with respect to the equity of letting the locality defray the expense; just as, on the other hand, the justice of a national provision for the military expenses of the country is beyond question, whatever special importance the military establishment may have for particular districts and localities.

§ 127. Between these two typical categories which are here contrasted with one another there is a middle ground. As an example of this middle class we may well take the collective system of highways in any country, with all its gradations and ramifications, highways and byways.

Between the great strategic railway which connects the center of the country with the fortifications on the border, and the city street which serves the business and pleasure of the townspeople, there is a multitude of railways and roadway s of first, second, or third rank, of great waterways and their affluents, channels natural and artificial - all serving the ends of the whole community or of the neighborhood in a greater or less degree.

One of the most difficult problems in economic discussion is to determine how far the several thoroughfares of the country are to be treated from the point of view of the general advantage derived from them or from that of the special local advantage derived. This may seem less difficult in the case of the minor roads of an eminently local character, but it is simply an insoluble problem as regards the great highways that are of indisputable importance for the industry of the entire country, at

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the same time that they in a special degree serve the needs of those portions which they traverse.

This question is thrown into the shade by the practical end to be gained, so long as we occupy the happy stage of industrial development at which the receipts of such an undertaking will fully cover expenses of construction and operation. It will also not require discussion so long as there is at least a prospect of such an equilibrium between receipts and expenditures, and so long as this prospect is a sufficient incentive to speculative enterprises on private account, capable of taking the place of public establishments that would otherwise be necessary.

But at the very beginnings of our modern transportation system, during the early stages of the development of railways; the absence of such a probability frequently gave a very practical significance to the question whether the general advantage to be derived from a contemplated state railway would be sufficient to warrant investing the nation's funds in a road to be built through a particular province; or whether the individual province did not derive by far the greater advantage from the new means of communication and so ought to bear the expense.

The method of meeting the expense suggested by this latter view has not been adopted. The trend toward centralization inherent in our great railway systems has led to the assumption of the financial burden, also, by the central organization. Indeed, it has even come to pass that in the course of the magnificent development of the Prussian railway system we find of late that the expense incurred for "secondary" lines (which surely are of no advantage to the national finances) is to an ever increasing extent defrayed by the national treasury. That all these things are so is evidence of the fact that there is another consideration, beside the difference in the advantages to be derived from the roads, affecting the mode of settling accounts between the commonwealth and its parts.

§ 128. Especially complicated are the relations between the various parts of the country in matters concerning poor-relief.

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At least they are complicated, as a matter of fact, under that condition of things which we know as the existing situation, and with which the great efforts of modern poor-law reform are concerned.

The same is not true of the primary type of public poor relief. This is based solely and entirely on the parish organization - at first ecclesiastical, afterwards civil. In such a neighborhood association the distress and the obligation of relieving it develop together, as it were within the widened circle of the family. So long as this type of poor-relief answers the exigencies of the national organization, that is, so long as the means of the local organization suffice to meet the local demand for assistance, so long does the self-support of each local organization remain the basis of a satisfactory arrangement between the whole and its parts.

But this condition of things changes with time. The mobility that comes with modern industrial life disturbs the simple relation on which this arrangement is based. The genesis of poverty, as well as the obligation of relief, ceases to be comprised within the bounds of any individual commune. From being a local matter it becomes a matter of national concern. The habit of permanent inhabitancy of a given neighborhood gives place to the habit of frequent removal from place to place; hence an incalculable shifting and migration of the laboring population and a great change in and increased variety of the causes which may reduce them to mendicancy, with the consequence that the burden of supporting the poor must in equity be apportioned over a broader field than the boundaries of the single commune. Equity demands, in an ever-increasing degree, that the nation as a whole must assume the responsibility of the public charities.

This uncertainty and the vacillation between local and national administration of poor-relief visible in the legislation of today, as well as the obstacles to a practical reform, are due simply to an inherent contradiction between this principle of equity and the well-known practical difficulties in the way of administering poor relief by centralized authority.

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In addition to this, it is to be said, there is also the difficulty that wherever the past still asserts its mastery and holds the social life to the old lines of neighborhood organization, its weight is cast in favor of the retention of the system of local management of poor-relief.

§ 129. The above classification of the public business has for its object the explanation of the differences between the various parts of the commonwealth with respect to benefits derived. It is undoubtedly an easier task to set forth the differences that exist between different parts of the country with respect to pecuniary ability.

Difference in pecuniary ability between different localities is a patent fact, and it would be a laborious and bootless undertaking for any one to maintain the contrary with respect to any country.

All the factors that have to do with the prosperity of a people are here at work to produce a complicated diversity. Their are such facts as the physical environment, the degree of culture of the people - as it expresses itself in their capacity for labor, their possession of property, their moral standards, their industrial discipline and application, etc. Inasmuch as these material and cultural factors vary greatly from place to place and from one individual to another, it is impossible to claim anything more than an approximate and relative homogeneity for any people. Immediately on passing the limits of a pretty small area account will have to be taken of marked differences and contrasts - town and country, manufacture and agriculture, factory and handicraft.

When the discussion concerns the state of things in a large modern commonwealth - when we have to do with an aggregate made up of so heterogeneous elements as is the German Empire of today - we are confronted with very great contrasts and differences, many of them due to the presence of different stages of civilization.

It is, in itself considered, a matter for congratulation, but it is all the more significant in connection with the contrast here

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spoken of, that the advance of civilization carries with it an increase of wealth and a consequent enhanced ability to meet the demands of the state. The stage of culture achieved by the various states and provinces of the German Empire is at the same time an index of their economic strength; contrast the West and Southwest with the East and Northeast. And as, in this contrast, the divergence in economic ability is in large part a matter of difference in the length of time covered by the process of development, so likewise it is true - in spite of all its harsher incidental features - that the focus of the latest and highest industrial development is at the same time the focus of wealth.

§ 130. The development of the relation in which these diverse economic capacities stand to the commonwealth exhibits features of a character very analogous to what we find in the relation of individuals to the commonwealth.

There is, in the first place, a narrow self-seeking, so extreme as to refuse even such sacrifices as are to its own immediate, palpable advantage. We need but call to mind the examples afforded by the later history of Germany. This history shows us that perverse spirit at the stage where it stands out in successful opposition to any sacrifices for the purposes of the greater whole; the stage where the consciousness of community between parts and whole is as yet entirely absent. A short-sighted selfishness on part of the minor political bodies, which figures in national life as "particularism," and opposes every move in the interest of the common weal.

There are, of course, also other factors that work in the direction of particularism; as, e.g., the instinctive clinging to what is customary, predilection for independent local management of Public affairs, a bigoted prejudice in favor of the kind of people to whom we are most accustomed, and the like. But the dominant influence of the economic factor, which makes itself felt in all the affairs of public and of private life, renders it easily comprehensible that the provinces which surpass the other portions of the

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Empire in point of civilization, and consequently in wealth, should, for economic reasons, be reluctant to cast in their lot unreservedly with those other portions.

§ 131. History accordingly shows us different stages in this course of development. The first and oldest is that of the unqualified assertion of particularism, in the form of the autonomy of the petty state. The independence of the petty commonwealth conceded nothing to the needs of the larger political organization, whereof, as viewed from the higher standpoint of the general national development, it figures as a member. The second stage is reached when absolute particularism has yielded ground so far that the sub-state is compelled to cede some portion of its sovereignty to the national organization. It may have been compelled by a change of relative strength, or by the force of growing public opinion, or by changes in industrial life, or by a combination of these factors.

At this point the features with which we are here concerned came out in a more glaring light even than before. The struggle between the unwonted demands of the larger whole and the reluctant yielding of the traditional particularism serves to show the difficulty of the transition. Concessions of course take the place of the earlier downright refusals of national demands; but there is an anxious balancing of accounts between the individual members of the federal whole, as regards their respective gains and sacrifices, which is significant of the great interval by which this stage of national unity is still removed from perfect union.

Hence we have not only the defective unity of the "federal state" [*Bundesstaat*], instead of the consolidated "unit state" [*Einheitsstaat*]. Within the federal state we find, moreover, "reserved rights" [*Reservatrechte*] possessed by particular states; and in addition to this there is a scrupulous calculation necessary in the adoption of every particular measure, lest it result in some advantage to another sub-state and some disadvantage to our own.



§ 132. It is a characteristic of the mature commonwealth that it has overpassed the narrowness of such a calculation of benefits.

The individual members of the federal commonwealth have come to stand in the same relation of indissoluble solidarity and uncalculating devotion to the nation as does the patriotic citizen to the state. It is not the calculation of special benefits to be derived, but the consciousness of a common benefit accruing to all parts of the nation, one with another, that is the guiding principle in the apportionment of sacrifices among the various parts of the country in proportion to their ability to pay. This difference in point of ability does not afford ground for a corresponding arrangement of exclusive spheres, within which the activity based on this ability is to serve the inhabitants of this particular territory alone; on the contrary, precisely this diversity in ability to pay is a chief means by which the solidarity of the parts is to be preserved.

The more fully this solidarity is developed the more active and intimate is the giving and taking, the exchange of benefits and sacrifices, within the different parts of the nation, and the more does shrewd calculation of advantages tend to fall into disuse.

Naturally this becomes most plainly evident in the case of the great national establishments; as, e.g., when the flourishing business of the more highly developed provinces contributes the profits by its railroad traffic toward the construction of lines in the poorer provinces. And where such national or central establishments do not exist or are not available the larger whole will even offer its support in the form of subsidies to the lesser unit to help out its insufficient resources.<sup>1</sup>

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<sup>1</sup> Cf. von Reitzenstein, "Ueber finanzielle Konkurrenz von Gemeinden, Kommunalverbänden und Staat" (Schmoller's *Jahrbuch für Gesetzgebung im Deutschen Reich*, 1887, pp. 123 *et seq.*), makes out that a dominant feature in the modern apportionment of public functions as between the state and the local administrations is the fact that the state and the larger political units assume an increasing share of the burdens of the communes, with a view to reducing the pressure upon the latter.

The paper contains a somewhat detailed exposition of the line of thought briefly

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The contrary happens when a section of the country possessing resources above the common is favored by the national establishments beyond what falls to the share of other sections. The same equity which in the former case requires a subvention from above downwards, from the stronger to the weaker body, will in this case demand a subvention from the weaker to the stronger. In this point, also, the trend of development of the national unity seems rather to favor a broad construction of the duties of the central administration. Whereas it is rather a mark of undeveloped unity and of particularist pettiness if the normal predominance of the central organ of a great commonwealth is curtailed and frittered away in all manner of petty affairs.

§ 133. This attitude of superiority assumed by the larger, and the largest, civil unit of the nation toward the smaller unit is also visible in the development of their formal relations to one another in fiscal matters, if it does not rather presuppose the latter. It is a mark of low development, if not rather of an utterly abnormal condition of things, if the higher political unit is obliged to resort to the lower for its sustentation, because it does not itself as yet possess independent revenues obtained through a direct relation between itself and the private individuals.

Such is the case with a federation which is supported by the "matricular fees" [*Matrikularbeiträge*] of its members. Such is also the case with a union of states in which these rudimentary survivals of an earlier, less perfect unity are still present, as, e.g., the German Empire of today.

In case of a vigorously developing commonwealth, survivals of this sort are to be looked upon merely as a transient feature handed down from an earlier constitution, which will disappear as soon as the fiscal system of the new commonwealth has

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indicated above, together with citations of the legislation bearing on the point. Von Reitzenstein makes a distinction between the principle of Bounties [*Dotation*] and that of subsidies [*Subvention*] (pp. 153 *et seq.*), and classifies the legislative enactments separately under these two heads. - Cf. A. Wagner, *Finanzwissenschaft*, vol. i. sec. 49.

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reached an adequate development. It is a piece of "federalism" surviving in the midst of political union, which is only waiting for the establishment of an adequate fiscal relation between the consolidated national organism and its citizens. The latter is the only method worthy of the state.

§ 134. Finally, we shall have to add a word in this place touching a factor the full development of which belongs in the discussion of taxes, namely peculiarities of fiscal technique.

Quite independently of the question of the necessities of the one civil division, and of the obligation of the other to contribute, or of the degree of development of financial balancing of accounts and adjustment of claims between the different bodies, there is a further factor which affects the problem, but which is often erroneously confounded with the other group of factors already spoken of. This is the special advantage which one political body may possess as compared with another in the levying of taxes.

In the United States of America it has happened of late (as, indeed, has also happened before) that the receipts of the Union from customs and internal revenue have produced an unavoidable surplus, contrasting curiously with the embarrassments and large deficits of the state and municipal finances of that country.<sup>1</sup>

The difficulty of raising taxes in the case of the small bodies and the ease with which they are raised by the larger, suggests the existence of circumstances of a technical character connected with peculiarities attaching to the different kinds of taxes, and which therefore work an advantage to the larger as compared with the smaller political body, whether it be special legislative enactments or natural causes that place the more effective method at the disposal of the larger organization.

Something similar is to be seen in other countries. Switzerland, agreeably to the traditions of her customs administration, has hitherto been unable to develop her customs revenues to a point where the full productivity of this fiscal mechanism appears

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<sup>1</sup> Richard T. Ely, *Taxation in American States and Cities* (New York, 1888).

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in anything like the degree attained in the United States. Still less has there, in the case of Switzerland, so far, been any question of a lucrative internal tax on consumption. But in spite of all this, Switzerland offers a contrast within its own limits similar to that seen in the United States of America. Here, too, we notice during the past decade a marked ease in increasing federal revenues from import duties, and an increasing difficulty in obtaining increased receipts from other customary forms of taxation, either federal or communal; so much so that a remedy for this technological difficulty has finally been found in diverting the advantageous means at the disposal of the federation into the dried-up channels of the minor civil divisions.

Or take the German Empire. In view of its great and unavoidably increasing expenditures, there has of course been no noticeable surplus to speak of. At the same time the development of the means available for an effective and lucrative Imperial system of taxation has been scanty indeed. Nevertheless it is true, and certain special reforms in the tax system of the Empire have already given proof of the fact, that the greatest political organization of the German people is also the one that has at its command the most effective fiscal means and methods, and that the technical difficulties of financiering increase as we descend in the scale of the minor civil divisions.

Indeed, the widespread conviction so frequently met with in the current discussions of tax reform in the German Empire, that the municipalities are in need of some assistance at the hands of the larger civil divisions, amounts practically to the same thing. Plainly, it can not hold true that the communal divisions and municipalities are intrinsically feebler financially than the Imperial or state organizations, inasmuch as these latter are composed of the same ultimate elements as the former. When the existence of a difference of this general character is asserted (independently of any difference in wealth between particular districts, communes, etc.) it can only be on the ground that greater fiscal advantages of a technical nature are at the command of the larger political unit.

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We therefore find that there is a relation of a fiscal character between the various civil organizations, which consists simply in the one acting as tax gatherer for the other. It is not necessarily the larger political unit which in this way acts as tax gatherer. There are also taxes with respect to which the smaller civil division performs the same service for the larger. This is a rare occurrence, however.

## CHAPTER V. SELF-GOVERNMENT AND VOLUNTARISM.

LITERATURE. Alexis de Tocqueville, *L'ancien régime et la révolution* (1856). Rudolph Gneist, *Geschichte und heutige Gestalt der englischen Kommunalverfassung oder des Selfgovernment* (3<sup>d</sup> ed. 1871). Rudolph Gneist, *Verwaltung, Justiz, Rechtsweg, Staatsverwaltung und Selbstverwaltung nach englischen und deutschen Verhältnissen* (1869). Adolph Wagner, *Finanzwissenschaft* (3<sup>d</sup> ed. 1883), *Erster Theil*, secs. 44-59. J. W. Probyn, *Local Government and Taxation in the United Kingdom* (1882).

### I. THE NATURE OF SELF-GOVERNMENT.

§ 135. The immediate point of departure for the present discussion is afforded by certain discussions of a general character inserted in the earlier portions of the present work, incidentally to the course of the exposition; as, e.g., what has been said in the present volume touching the evolution of the state (especially secs. 27-30), and the discussion, in the first volume [*Grundlegung*], of Coercion and Spontaneity (vol i. secs. 290-292).

We shall here have to devote a separate chapter to the consideration of voluntary contributions to the public establishment and the question of their relation to compulsory contributions, that is, to the great mass of taxes, and also how far and why they are adequate or inadequate to supplement the taxes.

In view of the still very considerable vogue, and in part well-grounded, and very gratifying vogue of a predilection for the spontaneous action of public spirit, as contrasted with state compulsion and the sacrifices imposed by compulsion, it is particularly desirable to come to a clear appreciation of the position which holds self-government to be of the nature of a political organ, and so removes it from the sphere of "Voluntaryism"

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(as it is latterly styled by the English) and draws a distinct line of demarkation between these two disparate spheres of activity, by pointing out the intimate and indissoluble relation in fiscal matters between self-government and the national administration.

§ 136. The widespread admiration of English political and industrial life rightly makes much of that characteristic feature of, personal initiative, which relies much on itself and little on the helping hand of the state.

We are all well aware that not only is the factor for which this concept stands an indispensable prerequisite to any sound and virile commonwealth, but also that in this respect the English type offers a particularly sharp contrast with what we are accustomed to on the continent, - a pattern from which we have already learned much, and from which we have much yet to learn.

It is however necessary, here as in every case of strongly developed individualistic tendencies, to go into a somewhat detailed analysis. It is necessary to take explicit account of a certain ambiguity in the relation of this individualism to the commonwealth and to the proper performance of the state's functions.

What is necessary to an adequate recognition of this relation is a profounder appreciation of the fact that wherever individual activity comes into play in relation to the commonwealth, the quality of the activity put forth is of at least as great importance to the discussion as its quantity; or in other words, the measure of its consonance with the purposes of the community is quite as much to be considered as the measure of its scope and intensity.

The more this consideration is pushed into the background, - the more stress is laid on the strength and volume of individual activity, without asking how far the energy put forth goes to serve the ends of the community or how far it is intended to serve those ends, the greater is the danger that we shall come to make the brute intensity of purpose of the speculating man of business the center of our concept of a free commonwealth.

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The quality of these individual activities is of the greatest consequence; the standard of valuation, to be derived from such qualitative appraisal and to be applied in rating the complex array of these activities, is of importance.

Here we have, in its crudest form, the entire system of individualistic endeavor, whose sole aim is the individual gain of the undertaker. The most convenient, most plausible view, the view which deals most indulgently with the weaknesses of human nature, goes on the presumption that all the business of human society may safely be entrusted to the keeping of such a system as this. For such a position flatters the callow egotism of the business mind with the acceptable conceit that in its striving after the highest possible profit for itself it is at the same time a benefactor of mankind. In point of fact, human society is not so advantageously placed. The harmonious interplay of individual activities is a dream which has never come near being true. What there really is for us to do is to reach an understanding of the narrow limits within which it is possible at all that this crudest development of individual endeavor can suffice for the purposes of the commonweal. It does, in fact, suffice for all matters that lie sufficiently near to the habits of thought of everyday people, so that the barriers of egotism - on part of those with whom it lies to make provision and of those for whom provision is to be made - will not hinder an adequate provision for the wants of society. As concerns the great mass of everyday wants, the palpable physical needs of mankind as commonly understood - food, clothing, shelter, etc.; here the service may be rendered and may be rated with tolerable accuracy by the ordinary methods of the market, between producers and consumers, sellers and buyers. Whenever these limits prove too narrow, other forces, of a higher, ethical order must come into play.

§ 137. A higher stage has been reached when the individual comes to a consciousness of the fact that his work-day self-



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seeking alone is not sufficient to insure the existence of society, and that nobler impulses are necessary for the purposes of social life.

It is a very acceptable, and therefore well accepted view, that these indispensable nobler emotions are to be had in sufficient quantity spontaneously, if not as a general rule, at least in the case of modern bourgeois society. They are conceived to be present at least in a measure so far adequate, that if only the state, with its coercive power, were willing to desist from what it need not undertake, there would be required but a slight remnant of its present activity. This view, too, is based much less on the actual facts of the case than on a seductive self-delusion, which sets up as the criterion of a desirable organization of social life the natural antipathy of men to any political restraint, however necessary.

As a matter of fact, the nature and scope of the functions whose performance is necessary in order to the social intercourse of civilized men are such as to require the extensive exercise of ethical springs of action, lying far beyond the bounds of self-interest. In Chapter III. above (secs. 79-91), in the course of the economic analysis of the services rendered by the public administration, we have seen what are the reasons for this being so. Partly they are functions which lie so entirely beyond the scope of self-interest that the private individual is even unable to comprehend what may be for his own interest; partly they are functions which stand in sheer contradiction to all selfish considerations and call for a distinct sacrifice of self-interest. In either case it is necessary to lift the every-day man above the sphere of his habitual interests and activities. In either case spontaneous private initiative will contribute in but a very modest degree to this end, and coercion by the state must be resorted to.

But inasmuch as we found, in the course of the general discussion in Volume I., that in the last analysis any absolute contradiction between this state compulsion and the voluntary motion of the individuals is a psychological impossibility, inasmuch as the question, in point of fact, is always one of expedi-

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ency, concerning a series of intermediate links between these two elements, - this relation being moreover involved in the constitution of our modern commonwealth; therefore it becomes a question of the proper intermediary mechanism which shall serve the purpose of this voluntary motion, in the guise and with the prestige of public institutions, and so help it to the adequate achievement of its national mission in the state.

Such is the foundation on which is reared the system of self-government.

§ 138. It is eminently the business of the Science of Finance to study diligently the interplay of coercion and voluntarism as it appears in the system of self-government. The development of the public revenue, the tedious rate of progress in the tax system and its various branches and forms, is closely related to this fundamental idea. Even the compulsory measures of the most heartless despotism are remarkably impotent to hasten the course of this evolution; and under conditions of the highest degree of political development hitherto attained, the achievements actually possible have been possible only by virtue of a nice adjustment of coercive measures to the actually available degree of more or less whole-hearted readiness to stand by the commonwealth.

Those requirements of modern national constitutions which are all intended to secure a large participation on part of the body of citizens in the formation and achievement of national aims, immediately set the factor of popular initiative in motion against any *ex parte* development of coercive measures by the central organ of the state. In consequence of these favorite constitutional maxims, the acceptance of the principle of popular sovereignty involves the incorporation of this concept of organized public coercion with its opposite, the concept of a myriad headed individual will. The nearer we approach the attainment of this result in the constitutional development of any particular state, the greater is the degree of political maturity, or in other words, of ethical maturity, presumed on part of this collective

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mind of the multitude; and the less nearly this presumption is justified, the greater a source of danger to the commonwealth does this public mind become.

In this dilemma there is no expedient left but a prudent combination of these two factors of coercion and spontaneous action. Hence a long-continued, gradual education of an ever larger number of citizens in the discharge of public duties.

§ 139. Among current conceptions of the nature of self-government the following are to be noticed.

The most widely accepted view is that which simply makes individualism, as such, the essence of self-government. This view is to be rejected, as being disproved by the argument of the foregoing paragraphs.

In sharp contrast with this view is that advocated by Rudolph Gneist; a view which he bases on the system of English Constitutional Law and English self-government, and which he has repeatedly published during a period of several years past.

This view of Gneist's<sup>1</sup> is to the following effect: Self-government is a method of national administration, a second, supplementary agency for the execution of the national will. It comprises the performance of such functions as are adapted for administration by the vicinage. All offices under self-government are offices in the full sense of the word, inasmuch as self-government rests on authority delegated to the communes by the state. The extent of the sphere of self-government is accordingly determined by national exigencies, not by the interests of particular social classes that may seek an accession of power. English legislation has been guided by the principle that the local unit should be called on for the rendering of personal service and the contribution of rates to the extent of its capacity; what may be needed in excess of this is borne by the county; what passes the county's ability is to be performed by

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<sup>1</sup>*Verwaltung, Justiz, Rechtsweg, Staatsverwaltung und Selbstverwaltung nach englischen und deutschen Verhältnissen, mit besonderer Rücksicht auf Verwaltungsreformen und Kreisordnungen in Preussen* (1869), pp. 95 et seq.

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government officials and national funds. The resulting "decentralization" is a decentralization of the administration only, not a decentralization of legislation and taxation. But inasmuch as all public burdens, whether of a personal or of a material sort, are opposed to the most obvious interests of the citizens, there can be no self-government without a seriously accepted and legally enforced constraint. Self-government, in that it makes certain official duties obligatory on the propertied classes, brings prominently into view the ultimate connection of state and society in all their parts and in the affairs of everyday life.

Such is the nature of self-government according to Gneist, as he finds it in operation in the English commonwealth, and as he presents it as a model for Germany.

Lorenz von Stein thinks otherwise.<sup>1</sup> He finds that within the aggregate structure of self-government there are two great divisions, essentially distinct in character: the organs of self-government proper, and associations. Both of these, according to Stein, are of the nature of public personalities. Under the first head he classes not only so much as what, according to Gneist, exhausts the concept of self-government, but also corporate bodies [*Körperschaften*], whose purpose is the performance of a definite administrative function by means of a definite capital, and whose several varieties fall into three distinct groups - corporations proper, charitable foundations, and public stock. The "association system," above spoken of, constitutes a part of the machinery of self-government in so far as the associations or companies in question exist for "administrative" purposes, and (as distinguished from business partnerships) employ their capital for the performance of an administrative function at the same time that, in performing this function, they afford a revenue to their members. The two typical examples of this class of "administrative" companies are joint-stock railroad companies and jointstock banks of issue.

It will be seen that this broader concept of the nature of self-government comprises under the idea of self-government matters

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<sup>1</sup> *Lehrbuch der Finanzwissenschaft* (5<sup>th</sup> ed. 1885). *Erster Theil*, pp. 57 *et seq.*

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which the view held by Gneist will distinctly exclude. On the one hand, while charitable foundations and the like do their work under state supervision, they are nevertheless voluntary organizations (in which respect they are unlike the governmental:communal mechanism of administration); on the other hand, the so-called "administrative" companies are, in point of fact, part of that well-known system of private enterprises whose egoistic speculative working may be checked by government regulations, but which can not thereby be raised to the dignity of an organ of local self-government. If it were competent for us to say that governmental control of any private business enterprise may constitute the latter an administrative organ, it would follow that this entire system of private business enterprise would be drawn bodily into the system of self-government, - and we should reach the conclusion which we have deprecated in the earlier discussion.

§ 140. But it is also possible to overrate the importance of self-government even when understood in its proper sense. The cause of so doing may be a predilection for local decentralization, as opposed to the present growing necessity for a centralized national organization. This may in part be due to a nebulous romanticism that insists on making the simple ways of life of a primitive democratic community the immutable standard for a large and highly developed commonwealth; in part it may be a prejudice in favor of certain of the maxims of radicalism as opposed to a sober recognition of the facts of the every-day life of the modern state. These two factors conspire to tempt us to the retention of an ideal of social life which would be impracticable for actual men in the modern state and under the conditions of modern society.

The English writer, Toulmin Smith,<sup>1</sup> is an example of a fanatical worshiper of the democratic principles of Anglo-Saxon self-government, who has become a champion of yet another type of

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<sup>1</sup> Cf., e.g., his work *Government by Commissions Illegal and Pernicious, The Constitutional Principles of Taxation, The Rights; Duties and Importance of Local Self-Government* (London, 1849).

Cf. also L. Bucher, *Der Parlamentarismus wie er ist* (Berlin, 1855)

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misconceptions of the nature of self-government, He offers a mixture of profound truths and profound perversions.

Local self-government, according to Toulmin Smith, is the real foundation of any liberal constitutional government and the sole effective guaranty for the responsibility of those to whom authority is entrusted. The mechanism of local self-government alone can adequately protect the interests of the minor civil divisions, or afford a fair opportunity for thorough discussion and comprehension of those interests. By its means alone is it possible to exercise a jealous control of the encroachments to which the officials entrusted with the general affairs of the state are constantly tempted. By its means, too, will the people best be able to comprehend and to deal with national affairs. Self-government also, and especially, constitutes a safeguard against anarchy and violence, in that it accustoms the citizens to give expression to the public will by peaceful and legal means.

But these very important, indeed eternal truths bearing on the nature of every free commonwealth, are placed in a false light when, as in Toulmin Smith's discussion, they are made to serve the turn of an appeal in behalf of the primitive institutions of a country, and so are held up as the sole and sufficient norm for the life of today, and are at the same time made the basis of an unqualified disallowance of all the peculiar needs incident to a great modern commonwealth.<sup>1</sup> The severe judgment passed on all centralizing measures in legislation and administration falls with unmerited harshness on the dominant parties, parliaments, statesmen, etc. This tendency to centralization in the first place goes to establish the fact that the ever-growing volume of business of a great civilized commonwealth can not possibly be managed without increasing centralization, and secondly, that in the conflict with the exigencies of this growing centralization the ancient traditions of local self-government are of constantly decreasing avail. Nor is it political reasons alone that go to lessen the relative significance of the institutions of self-government in the

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<sup>1</sup> It is a significant fact that Smith finds himself in sympathy with the individualism of Dr. Ure. Cf., *inter alia*, *Government by Commissions*, pp. 266 *et seq.*

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course of this shifting of governmental functions; the fact is due also to cultural, economic, social-political mutations of a general character, changes which alter the inclination as well as the capacity of the modern citizen for self-government. Men change, and the business of the commonwealth changes as well.

The outcome of the discussion is that on these grounds, too, the sphere of local self-government is necessarily a restricted one. Within its proper bounds local self-government remains none the less essential, but it is distinctly to be relegated to this its proper sphere. Exactly where its limits lie is a point to be established by specific considerations, in part of an historic nature, in part technical - considerations with which we have become familiar in the course of the preceding (fourth) chapter.

§ 141. Self-government in all modern states, as in fact in all times, in its actual workings, is divisible into two factors - the element of personal service and the element of material aid.

In virtue of its economic nature the material aid rendered is definitely measurable sacrifice rendered to the commonwealth on the general ground of the duties of citizenship or for special cause. With this we shall have to deal in the next following section. The personal services, on the other hand, owing to their not being translatable into economic terms, belong in an indefinite region of psychology; indefinite because of the difficulty of accurately grasping, and the still greater difficulty of defining the scope of the motives from which the rendering of these personal services proceeds. Gneist designates this class of duties "honorary offices" (*Ehrenämter*), as contrasted with the salaried offices of the professional civil official or the jurist; the term "honorary" serving in this case mainly to express the absence of any salary. As a descriptive designation it could only serve to express the ideal to be sought after, as an appeal to the motives from which the duties of office ought to be discharged under a system of self-government, without implying that these are actually the motives from which the office is ever or anywhere accepted. If such were not the case, if the so-called "honorary" office were as a matter

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of fact felt to be a honorific charge, in the positive sense of the term, and as fully and constantly so as the material aid rendered the commonwealth is recognized to be of an exclusively economic character, then the rating of these "honorary" offices and assigning them their proper place in the economy of the state (or of the commune) would be a very simple matter indeed. They would then be of a distinctly non-economic character, in much the sense in which the material aids rendered are, for their part, of a distinctly economic character, and they would accordingly not come into consideration in the Science of Finance at all.

But in point of fact the matter is not so simple; for, as has already been pointed out, while the thought of honorable distinction may be present in the case of the personal services demanded under self-government (sheriff, juryman, assessor, and the various local administrative offices), there is also distinctly present a feeling that these duties are burdensome and therefore involve a sacrifice of an economic sort. Practically, this is made evident by the fact that, in spite of the perfect readiness of the citizens to appreciate at its full the honor attaching to an "honorary" office, such offices are economically in so sad a plight that the fact of their involving a sacrifice has to be recognized by law in the form of a salary paid out of funds derived from other sources.

§ 142. These considerations are evidently of a wider scope than the domain of local self-government alone. It is rather in the system of national defense that they find their chief application. A satisfactory financial rating of this phase of the personal services required by the commonwealth, which is so great both in extent and in its importance for state and people, is one of the most difficult problems of economics.

A scientifically adequate comparison of the military burdens of states which have different systems of defense is therefore a sheer impossibility.

To construe the universal liability to military service of today as a case of an "honorary" office in the strict sense, and thereby exclude all consideration of its economic bearing on the citizen



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subject to conscription, - that would be impossible, unless we are to ignore the plain facts of the case for the sake of an overwrought conceit. On the other hand, to compute the burden involved (and a burden it unquestionably is) according to the standard of wages customary in industrial employment, and so encumber the finances with enormous expenses, would be very nearly as bad. For while the economic significance of military service considered as work done for the commonwealth is to be recognized, still this simple method of computing its value will never commend itself to our sober second thought. There is the difficulty, first, that it is a pretty dubious view to rate the personal burden of a universal military service simply as labor in the economic sense; and second, even if we put aside this doubt we encounter other doubts as to how this economic burden is to be fairly rated in terms of money.

As to the first point the reflections that offer themselves are the following. As, on the one hand, it is surely an exaggeration to construe military duty simply as an honorary distinction, in order to remove all conception of an economic appraisal of human life and happiness; so, on the other hand, it is certainly a mistake to conceive of military duty simply as a sort of statute labor, which differs from the other burdens imposed for the purposes of the commonwealth only in being paid in kind, and is simply awaiting the time when in the course of modern industrial development it shall, like other similar relics of the past, be commuted into its money equivalent. Such a view is contradicted by the essential nature of a universal military duty, by the course of past development of which it is a product, by the great importance which it is conceded to have for the defense of modern civilized states. The peculiar ethical character which attaches to this way of serving one's country, and which gives it its special value as compared with any other method of national defense; the peculiar mingling of diverse ethical factors; the magnificently devised scheme of education which it comprises, serving to awaken the slumbering nobler impulses, together with much undeniable hardship and exacting service; the beneficent influ-

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ences of the service in the way of outward culture, hygiene, cleanliness, etc.; all these considerations forbid our treating it simply as a performance of labor in the economic sense. To say nothing whatever of that minority of the conscripts whose previous intellectual and moral training places them at the outset above the level of the great mass of recruits, to whom the element of honor in the service appeals in a peculiar degree, even, when it is not all in all, and for whom the attractiveness of the service is further increased by a variety of adscititious concessions.

So much for the first point. The second difficulty lies in the impossibility of properly rating military service as an economic fact, even after we have conceded the propriety of so construing it. The horse-breeder can readily ascertain the market value of horses, and when wanted for the army they can be taken at their customary money-value. Men are reared for their own sake; they have therefore no economic value, except, possibly, where this proposition will not hold on account of their being slaves - objects of value owned by other persons. The attempt to compute the economic value (that is to say the loss) of the time spent in military service on the basis of the customary daily wages is nugatory, inasmuch as the able-bodied man contains only the possibility of a valuable use of his labor power, not the certainty of it. On the contrary, under the latest existing circumstances of the labor market it is exceedingly probable that the hundreds of thousands of soldiers, who in many states are held to service for several years together, would, in case Utopia were realized and standing armies abolished, simply encumber the labor market with their supply of labor, and would in great part be left without employment. As it is now, the population has, as it were, discounted the fact that there are at any given time so or so many hundred thousand men under arms. Our conclusion therefore is that universal military service is a quantity not reducible to strict economic terms, and that in this respect it is but an exaggerated example of what is true of the entire personal element in the system of self-government.

## II. THE FINANCES OF SELF-GOVERNMENT.

§ 143. The assertion has repeatedly been made that the material means required by self-government are necessarily, or at least properly, to be correlated with the personal services required; the tax system of self-government should correspond to the system of personal requirements.

This, however, holds true only to a limited extent; and this for reasons which have been indicated in the preceding chapter. It is right that that same manly vigor which is under self-government called on to partake directly in the discharge of the business of the vicinage, should likewise be immediately responsible for raising the funds necessary for the purposes of the vicinage, The patriotic sense of a free man demands that the immediate circle of his life-interests should rest on his own shoulders, much as does the wider circle of the general commonwealth.

There are also other less sentimental reasons that go in the same direction.

So, for example, other things being equal, the necessity of raising the funds required for the purposes of self-government will undoubtedly always exert a wholesome pressure on the local administration in the way of economy; whereas, for obvious reasons, the disposal of revenues that are turned over to the local organization from without involves the danger of wasteful extravagance.

Also, the local character of the levy will favorably affect its collection, much as if it were within the circle of a large household. Of course, all past experience goes to say that it will not by any means entirely overcome the immaturity of the civic sense, which shows itself in a particularly crude form in the taxpayer; but it will go some way toward helping out the weakness of human nature, in that the more direct and obvious connection between the common burden and the personal advantage of the individual citizen belonging within the local jurisdiction seconds his sense of duty, at the same time that it sharpens the vigilance of the taxing authorities. As an example, in the cantons of

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Switzerland, where a simple local, communal board of assessors has charge of the property tax (levied by the commune) and the income tax (levied by the canton), the board is found to have an appreciably keener perception for "property" than for "income," in the taxation of which latter the canton alone is interested (though the canton is small enough, and extends but little beyond the limits of the commune). It is sufficiently notorious how, in the administration of the Prussian income tax, the individual communes have developed a local patriotism - deplorable on moral and political grounds alike - which, through the means of the (local) assessment boards, takes care that the commune shall not fulfill its duty toward the state, in the payment of the legally established tax, in any more liberal measure than other communes. The result being that, in the absence of any adequate representation of the national interests on the board of assessment, a tacit understanding has been established that the assessments are to depart as widely from the truth as practicable. And the oft-mentioned supplementary local rates added to the national income tax are, at least in part, nothing else than the form under which what is withheld from the state is turned over to the commune.

§ 144. But while the reasons mentioned speak for a close correspondence between local taxation and local administration, there are other weighty reasons against it, which considerably hamper the possibility of this ideal scheme.

The first and most obvious of these reasons is the scanty financial means of the local organization, in consequence of which it finds itself obliged to fall back on the support of a larger organization to which it belongs. We have already seen reason to believe that with increasing culture and increasing political development the solidarity of parts and whole also increases, in such fashion that any indigence of this sort on part of individual minor divisions comes to be met by aid from the other parts. So that in this direction, too, it becomes apparent that a self-sufficing local self-government - in the sense made

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familiar to us by current democratic vagaries - is a thing of the past, while in the actual political development of today this element is to an increasing and gratifying extent giving way to a growing centralization.

A second reason is an intimate connection between the business of the local administration, or at any rate some parts of this business, and the affairs of the commonwealth. Here, too, we are met by the fact of an increasing centralization that goes hand in hand with the progress of society and of industrial life. A striking instance is the administration of poor-relief. The greater the mobility of the populace - the more freely the mass of the laboring classes, and therefore of the classes that lie nearest to pauperism, move about from place to place in the search for employment, the greater the industrial area within whose limits this shifting back and forth goes on, the smaller is the ground for hope that a merely local provision for the relief of the poor, supported by local financial means alone, will meet the requirements of fiscal equity as between the locality and the state. The question concerns an obligation resting on the nation as a whole, and every attempt to shift the responsibility to the shoulders of the individual local divisions runs counter not only to the dictates of equity but to the requirements of expediency. The outcome is an overburdening of many of the local organizations, and a consequent resort to the superior organization for relief and remedy.

Third, there is to be considered the technico-fiscal side of the matter. In view of the difficulties visible on every hand today - difficulties attending a system of taxation which is at once efficient and adjusted with a view to the least possible friction and the easiest possible meeting of the tax requirements of the commune, the state and the empire-it will not do for a system of taxation to neglect any method that may go to make it as efficient a tax system as possible. This factor of fiscal method will largely decide for success or failure in meeting the growing demands for revenue in modern communities without too serious dissatisfaction on part of the taxpayer. A skillful selection

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of the proper means and method will enable us to construct an elastic mechanism that will adapt itself to new requirements as they arise.

We therefore conclude that it is imperative for the finances of local self-government to submit to this demand of expediency. If the most efficient means of raising the revenue required by one of the minor civil divisions are to be found only under the control of a political unit of larger compass than that for whose needs the revenue is required, then the larger body should properly become the taxgatherer for the smaller, and it would be a piece of vicious doctrinarianism to sacrifice this consideration of expediency to an abstract ideal of self-government as applied to taxation. It is true, the assumption on which this argument proceeds holds by no means invariably. On the contrary, the conviction is spreading of late that in a sober, commonsense system of taxation the communes, too, have a useful part to play, and that in this respect we have much to learn from the French<sup>1</sup> - who are practical as well as conservative in matters of taxation.

§ 145. The reverse of the situation here contemplated may occur if there is some motive of public policy for administering local affairs by the central organization of the state. In such circumstances the same public interest which calls for the management of local affairs by the central authority, will also justify some contribution out of the national funds toward defraying the local expenses. But, on the other hand, since the fact remains none the less that the purposes of the local organization are served by the administrative department so constituted, although it may be under the control of the national administration, it follows that the central finances should combine with the local in meeting the resulting expenses.

The administration of a city's police by the national authorities is a case in point, in the form in which it occurs, or has

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<sup>1</sup> Cf. von Reitzenstein, "Ueber indirekte Verbrauchsabgaben der Gemeinden, ein Beitrag zur Reform der Gemeindesteuern," *Jahrbücher für Nationalökonomie und Statistik*, 1884, N. F. vol. ix.

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occurred, abroad and in Germany (in Prussia, in the former kingdom of Hannover, etc.). When a city reaches a certain size and degree of importance, the national government believes the administration of its police can no longer be left to the local authorities, without danger to the commonwealth. It therefore reserves to itself the right to direct this branch of municipal administration through its own agents. Not only is there no warrant for unconditionally condemning this centralizing of the municipal police as being opposed to the principle of local self-government - local self-government is not an end in itself rather it is an open question in each particular case how far the powers and the services of local self-government are adequate to the needs of the state, and what are its proper limits, and where it needs to be supplemented by an organ of the national administration.<sup>1</sup>

Nor are we justified in making the national management of a branch of the municipal administration a decisive reason for national payment of the resulting expenses, for the fact of its being primarily a municipal purpose that is served is not set aside by the further fact that the municipal interest in the matter coincides with and is further enforced by a similar interest on the part of the commonwealth; still less so if - as may readily be the case - the motive for the national government's action is the knowledge that the measures taken by the local self-government are not sufficient to insure the peace and security of the city itself.

§ 146. After all the reservations made in the preceding paragraphs there remains an undoubted sphere of independent financial action for local self-government. But even within this sphere it must so choose its ways and means as to conform to the spirit of the modern state and fit into the structure of the larger whole. Just as we must not confound local self-government with local autonomy, so also there is no place in the modern

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<sup>1</sup> For the relation of the police to the municipal self-government of Prussian cities cf. Arguments for Municipal Reform, cited by Ernst Meier, *Die Reform der Verwaltungsorganisation* (1881), pp. 308 *et seq.*

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state for a sovereign taxing power vested in a local organization. The tax system of a local self-governing body, as well as that body itself, is part and parcel of the sovereign state.

It follows, in the first place, that the question as to whether we are to adopt the more highly centralized method of supplementary communal rates [*Zuschläge*] or the more decentralizing method of special communal taxes reduces itself to a mere secondary question of fiscal-technical expediency. It is a consequence to be expected that countries with a highly centralized organization, as, e.g., France, have made use of the supplementary rates; and that, on the other hand, countries like England, with a predominantly decentralized organization, have granted to their local self-governing bodies a great measure of independent taxing power, or rather, what is historically the more accurate view, they have not carried the development of local autonomy into local self-government proper beyond the early stage at which this method is tolerated.

For all practical purposes the question is essentially a question of expediency. The end to be sought is a serviceable method of distributing the aggregate financial burden of the state, commune, etc., so as to make it bear equally on the different supporting points by means of a shrewd selection and combination of the various forms of taxes. It is not out of any consideration in favor of centralization or decentralization, but simply because of its inefficiency as a fiscal apparatus, that the modern Prussian method of superposing a direct communal tax upon the national tax, is so much in need of reform. The reform needed is a relief of the unequal pressure of the burden, and of the disproportionate strain that falls on one branch of the tax system - and on a defective mechanism at that.

§ 147. Apart from and independent of this question, and back of it, the principle must be accepted as decisive that all taxation by the local administrative body should be subject to the right of supervision by the state; that with respect to kind and scope the particular tax measures must be made to depend



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on the legislation and the sanction of the central authority. Not from any disinclination toward the free development of a spirit of local independence, but simply as a necessary consequence of the indispensable system and unity of the aggregate fiscal burden of the members of the state.

While there is, in this connection, an inalienable duty resting upon the national legislature and the national administration to guard the interests of the commonwealth, there are also many other considerations, enforced by much and varied experience, going to show the shortcomings of self-government.

In the first place, in this matter as in all other matters of national concern, the duty rests upon the central authority of using its power to correct the trend of the social forces at work whenever that may become necessary. If, generally, and in every community, erring human nature is everywhere open to the danger that opportunity to influence public affairs will become the occasion for exploiting this influence in the interest of one's own particular class, the remedy is nowhere so easily applied as within an organization which is not itself in possession of sovereign powers, but is part of a greater whole. While the sovereign state, if it suffers from disorders of this sort - and it does so suffer, to some extent, everywhere - can look for a remedy only from within itself and its own gradual development and approach to the ideal of national organization, every local organization on the other hand, as being a part of the whole, is subject to the authority of the whole, and may so get rid of these abuses, as it were by appeal to a higher court, at least in case the relation of the local administration to the national government is what it should be.

Protection of the lower classes of the population against class legislation and class administration in the interest of the upper classes, protection of the upper strata against the democratic tyranny of the penniless or the less well-to-do classes, who, in human fashion, are eager to turn the oppression and injustice which they have so long suffered into its converse, and to play the hammer instead of the anvil; the one abuse or the other, if it shows itself in a local administration, may be set right by means

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of a proper control exerted by the central authority, unless the state suffers from the same ailment. The mission of the national administration in such a case is that of the unprejudiced third party, who, unbiased by considerations of interest, is to see that justice is done between the contending classes.

The antagonism is not always that between rich and poor, between the higher and the lower classes. There are also antagonisms within the limits of these groups - secondary class differences. So, e.g., the hereditary middle-class citizens of a place; in their assessment of property, will be tempted by their class interest to a criminal connivance as regards the members of their own class, coupled with an excessive vigilance as regards the taxable effects of the higher classes, the official class, or persons of alien birth. In such a case there is no remedy save through the employment of national agents, who, it is true, will not be able to dispense with the knowledge of local affairs possessed by the local administration, but may nevertheless lend their moral support to the employment of this local practical knowledge on the side of truth and good citizenship. This holds with added force if the question concerns a function of the local administration which involves, partly or mainly, the interests of the national taxation.

§ 148. While there may be room for a variety of opinions as to the exact requirements of justice in the apportionment of the fiscal burdens of the commonwealth among the various classes of which it is made up, there are, at any rate, certain kinds of mismanagement that are too palpable to leave room for doubt. Unfortunately, there is no lack of experience of this kind.

We may call to mind the reckless expenditure that has been so dangerously stimulated by the modern development of public credit, and then has come to the end which waits on all recklessness of this sort - bankruptcy. The greater the degree of autonomy exercised by the local self-government, that is to say, the less developed the national organization not, as the erroneous teachings of radicalism would have it, the more highly devel-

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oped, the greater is the scope allowed for fiscal transactions of this sort.

The more completely the management of local affairs is surrendered to the dictation of the so-called public will; that is, in point of fact, the more exclusively it lies in the hands of an irresponsible organization of demagogues; the more unquestioningly will considerations of permanent public policy be made to yield to the exigencies of present party interests. As regards other pathological phenomena, so also with respect to this matter modern democracy has afforded a fertile field of experimentation. Indeed, the experiences of democratic municipal finances have furnished new topics for scientific treatises on modern jurisprudence.

It is the office of an adequate guardianship of the finances of communes and other local organizations, such as a well regulated national organization implies, to prevent such developments of demagogical financing.

### III. VOLUNTARY AIDS.

§ 149. Having now reviewed the nature and the financial system of local self-government, the field is clear for the discussion of a class of public aids, which, as we have already had occasion to remark in the general exposition, must not be made too much of, but which nevertheless demand a place in any fiscal system, and especially in modern finance, and therefore can not be omitted altogether from the discussion. These are the Voluntary Aids rendered the community by private individuals for public purposes, and in competition with the more rigid system of national and local administration.

<sup>1</sup> Cf. in this connection the American political economist, Henry C. Adams, *Public Debts* (1888), who sets forth the experiences of his country. He says, among other things (p. 25): "The great danger to self-government in the United States lies in municipal corruption, and municipal corruption is in large measure traceable to the manner in which cities have used their credit."

<sup>2</sup> Cf. F. Meili, *Die Schuldexekution und der Konkurs gegen Gemeinden* (Zurich, 1880). *Die ökonomische Lage der Gemeinde Turbenthal (Kanton Zürich); Finanzielles Gutachten von H. Cramer-Wysz, und juristische Glossen von Professor Dr. Meili, Advokat in Zürich* (1888).

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As to ideals we are all pretty well agreed. The best and most desirable arrangement would surely be that the aggregate of what today is required for the purposes of the empire, state, and commune should be tendered spontaneously, - from an unconstrained inclination, with a full knowledge and consciousness, from the force of an enlightened and cordial recognition of what is due to the commonwealth. But seeing that this ideal is very far from being realized, it is after all, or rather it is all the more gratifying to find, at least by way of exception, that something is done from this motive, and it is not for us to make little of this gratifying feature in so far as there is substantial ground for rejoicing.

It is also not an easy matter for us to dispense with this ideal. For all the difficulties in the practical working of a system of taxation are in large measure due to the fact that the coercive measures of our tax legislation and tax administration find the lack of sentiment for the commonwealth so great an obstacle as to make the struggle against it always difficult and sometimes futile. The success of these coercive measures rests not exclusively, though to a considerable extent, on the growth of a relative willingness on the part of the citizens. We need only call to mind that the contrast between direct and indirect taxation is intimately connected with this question. The problem is to make the most of the deficient willingness to pay taxes, by a skillful employment of ingenious methods of taxation, just as a medicine must be administered to a child in some form that is palatable to him. We may also call to mind that modern constitutional provisions of every civilized state concede to this element of voluntary readiness a dominant influence in legislation and administration. The basis of political "liberty" is the fact that "society" makes its will felt in the affairs of the state, not only in the sense of forming a realistic limit to the application of the high strung projects of political idealism, but also in the sense that it constitutes a permanent counterpoise which holds every measure looking toward an ideal national organization down to its own lower plane.

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Any one who desires instances of this has only to turn to the everyday experiences of any modern state, not last to those of the Prussian state, with its ineffectual tax reforms and the shortcomings of its tax administration.

There is therefore no occasion to take one's stand on the high ground of national institutions and contemptuously dismiss this ideal factor of spontaneous assumption of financial burdens. On the other hand, there is a great deal to be hoped for financial progress from a growth in this direction.

At the same time it is well to be on one's guard against convenient illusions that go to overrate the services rendered by simple volunteer efforts, as judged by the standard of actual financial necessities.

For this reason it will be best to examine a little more closely what are the services actually rendered by volunteer effort.

§ 150. First as regards the range of voluntary aids, as judged by the standard of the aggregate of public needs.

No motive of practical charity is to be denied its due appreciation. But this appreciation cannot set aside the fact that even the noblest and best efforts of voluntary charity, such as we find it in practice in German countries, amounts in the aggregate to but a very modest portion of what is required for the purpose. The peculiarly pathetic circumstances which afford the special occasions for this work of compassion themselves go to strengthen the ease. They indicate that the utmost that can be accomplished by voluntary effort has already been accomplished; they constitute an empirical proof as to what point can be attained by this means, by the utmost exertion and with the best conceivable moral disposition.

If we make a comparison, e.g., between the expenditures required of the German finances on account of the armaments of the German states plus the French-Prussian war on the one hand, and the aggregate of all charitable gifts collected under the immediate pressure of the misery incident to the war on the

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other, we shall find that the latter are related to the former, in character and volume, somewhat as the delicacies offered a convalescent are related to the aggregate expenditures incurred in the care of the sick.

This ought of course to be otherwise, and there is some ground to hope that the very wealthy upper classes especially will gradually learn to discharge their duties to society in a far more adequate measure than hitherto, - that the dangers incident to the great social inequalities of the time will oblige them, out of regard for their own best interest, to seek this means of conciliation. In the meantime, it is to be remarked, what has actually been done is, in spite of all deceptive show, extremely inadequate.

The ground of hope lies elsewhere, in the examples offered by other times and countries, which go to indicate the possibility of a transformation of custom and of moral standards. Such, e.g., are the customs we find prevailing in the early towns with their numerous foundations, in the Swiss cantons, and especially in the United States of America. It is a difficult matter to find out just what part has been played in this connection by the truly ethical motive, either in early times or in the present. On the one hand it may be safe to assume that divergence of interests in our modern industrial society must have strengthened the egoistic factors, and that consequently the modern increase of wealth has diminished the inclination to incur sacrifices for the public good. The Earl of Shaftesbury, with his wide experience in the English philanthropic world of a generation ago, expressly declares that the difficulty of raising money for philanthropic purposes increases with every year that passes, and will ever increase with the increase of wealth; inasmuch as the love of money and the passion for amassing it ever increases with the greatness of the wealth possessed. Still, the testimony which the United States furnishes in eloquent deeds seems to speak to a different purpose. It exhibits

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<sup>1</sup>*The Life and Works of the Seventh Earl of Shaftesbury*, by Edwin Hodder (1888), p. 597.

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a series of voluntary gifts to the community, which, in comparison with what we are used to, are of a magnitude to be viewed with amazement. A merchant of Baltimore, Johns Hopkins, in 1876, donated a sum of seven million dollars, one-half to the founding of a university, the rest for a hospital. Girard, of Philadelphia, gave two million dollars for the foundation of Girard College. Smithson gave half-a-million to the Smithsonian Institution in Washington. Vassar gave a like sum toward the foundation of Vassar College in New York state. Lick gave to the University of California the sum of \$700,000 to build and equip the most complete astronomical observatory in existence. And all this falls within the last few decades; for down to 1846 the highest figure of any gift of this kind given, during the donor's lifetime did not exceed \$50,000. These facts are the more significant as coming from the classic home of modern industrialism; but they are after all, as we shall presently see, not to be rated too high.

§ 151. But even if the volume of voluntary contributions and in particular such as we meet with in Germany, is of itself a contracted one, there are yet certain qualitative drawbacks, to be considered, which will go far to dissipate altogether the impression they make.

It very frequently happens that spontaneity, in the sense in which we are fond of conceiving it, is not present at all. In all cases where the familiar subscription list is passed around for the relief of some sudden or chronic distress, or for the erection of monuments, churches, and the like, it is in great part nothing voluntary whatever, and can properly bear this name only to distinguish it from compulsory taxation by the government. In such a case it is not the coercion of the tax law but the compulsion, less rigorous it is true, but still the compulsion, of public sentiment, of usage, of decency, of reputability, of social standing, that acts as a power from without to enforce the very moderate inclination to afford voluntary aid.

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<sup>1</sup> Cf. R. A. Procter, "Capital and Culture in America," *Fortnightly Review*, August, 1888, pp. 260 *et seq.*

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In view of this state of the case, with respect to the ethical aspect of a large portion of the so-called voluntary contributions, the question may well be asked, whether the whole business is really sufficient to justify the very appreciable expenditure of energy involved in getting the means together in this scattering fashion, as well as the great amount and variety of annoyance undergone by the members of society who bear a hand in the matter. Might it not be more to the purpose to raise this much additional contribution by the directer method of taxation?

This directer method is also pretty obviously suggested by a familiar fact. These same benefactors of mankind on whom their hundreds of thousands and millions devolve the duty, and more especially the honor, of distinguishing themselves by liberal subscriptions, as honorable as they are easily afforded, are in the habit of leaving a margin of such proportions in their legally obligatory tax payments that this ostentatious liberality of theirs is but a very inadequate "conscience fund" when set off against what, in performing their less public obligations, they have neglected and continue to neglect. They would do better to conform to the requirements of the law, and then let all this ostentatious pretense alone - the pretense of giving something to the community beyond what is legally due from them, while in point of fact, they have fallen far short of doing their duty. The praiseworthy instances in which the gratuity is not pretense alone, but very truth, are surely not to be underrated, but they make up most decidedly only a small minority of the cases.

§ 152. There is a further circumstance to be taken into account in connection with this voluntary contribution to public purposes, namely, the manner of looking at certain public objects that appeal to our philanthropy.

The view taken is largely determined by certain narrow conceptions of the nature of the functions of the state, based on the emotion produced by particular occurrences, instead of an intelligent appreciation of the great necessities of national life. The so-called charitable gifts prompted by a sentimental compassion



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for a particular misfortune, and analogous instances, are in themselves worthy of all respect. But their moral dimensions turn out to be sadly shrunken when we come to find that this very habit of mind, that is so sensitive to an emotion, seems to have no suspicion of the fact that the aggregate of public objects, - all that the state requires of the individual - should properly claim the same cordial response, regardless of how much or how little it is calculated, superficially, to appeal to sentiment.

And a second consideration goes along with this one. This same view of the functions of the state which proposes to meet the serious requirements of the commonwealth by means of an impotent voluntarism, is moreover; in attaining its slight actual results, given to the employment of all sorts of questionable financiering, which is to be justified only by its laudable aims. Entertainments are got up, which afford the usual circle of sociable acquaintances of the season another occasion to come together and kill time. High official sanction is obtained for the institution of lotteries, which the government ought to prohibit for any and all purposes, if it only had something more of a conscience than it has.

However we may look at the matter, therefore, whether from the point of view of their scope or of their nature, the category of voluntary contributions serves no other purpose than that of bringing into a stronger light the great importance of a fiscal system backed by coercive power and resting on national legislation.

## CHAPTER VI. ORDER AND SEQUENCE IN THE PUBLIC ECONOMY.

LITERATURE. Adolph Wagner, *Finanzwissenschaft* (3. Auflage, 1883), Buch i. Cap. iii., iv. Adolph Wagner, "Die Ordnung der Finanzwirtschaft und der öffentliche Kredit," in Schönberg's *Handbuch der politischen Oekonomie* (2. Auflage, 1885), Band iii. pp. 477 et seq. A. Schaeffle, *Zeitschrift für die gesammte Staatswissenschaft*, 1883, 1884. Erwin Nasse, *Zeitschrift für die gesammte Staatswissenschaft*, 1868. Paul Leroy-Beaulieu, *Traité de la Science des Finances* (1877), 2<sup>me</sup> partie, livre I: du budget.

### I. CLASSIFICATION OF PUBLIC FUNDS.

§ 153. Some reference has already been made in the introductory portion of this work (vol. i. secs. 187-216) to the logical sequence necessary in all organization of demands or expenditure (*Bedarfsgestaltung*). Whether the question concerns public or private economy, there is a single ethico-economic norm on which any systematic ordering of demands must be based. This norm consists not simply in the requirement that the aggregate volume of demands must be brought into conformity with the aggregate of available means; it requires further that the order of precedence as between the different classes of requisitions, must be made to correspond with the order of their relative importance for the life of the individual or of society.

The first half of this general rule imposes on the demands of civilized life - in themselves considered, boundless - certain rational limits, determined by the magnitude of the economic means available for their satisfaction. The second half of the rule defines the proper limits of each particular class of these demands, in that it requires them to justify their claims as against other like demands, in an appeal to the standard estab-

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lished by a rational gradation from the necessary to the dispensable.

It may be taken as evident that there lies within the horizon of modern social life in state and commune a countless number of possible undertakings calculated to serve the purposes of a physical or spiritual amelioration; works of some human use, which, in themselves considered - apart from the necessary expenditure involved - are of undeniable legitimacy. Indeed, we are well aware that precisely the public economy of modern civilized states, by the nature of the case, rises above the danger of a growth of expenditure for trivial ends, such as we so frequently have occasion to deprecate in private life, or at least that it is relatively free from such danger. The danger lies much less in the direction of ignoring any growth of a commendable popular demand, than in the over-zealous acceptance of the functions which the new demand may impose.

No one would dispute the fact that in any modern state, within the sphere of the obscurest village and of the highest departments of the general government alike, there is present an endless array of activities waiting to be undertaken, for the furtherance of health and comfort, of schools and charities, of science and art, - tasks which remain unfulfilled for no other reason than because of the excessive sacrifices which they would require.

But if we accept this truth in its general form, it appears that its application to practical affairs is conditioned by the fact that the alternative presented is not a simple negative, but consists of counter claims of a positive character. Hence the necessity of a more detailed analysis.

§ 154. What is it, precisely, that we mean when we say that sacrifices demanded by any public undertaking are excessive?

There is, of course, an extreme limit, where this phrase would hold true literally, But this uttermost limit is never seriously under discussion. As a matter of fact, the discussion concerns only those burdens whose exorbitancy (in case experiments could be made in political affairs) would very speedily be disproven in

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case the required sacrifices were increased by the exigencies of a disastrous war. The question therefore practically concerns only the greater or less degree of pressure, of sacrifice, which would be involved in meeting the necessary expenditure. And how would this pressure, this sacrifice, show itself? Plainly in this way, that certain demands would intrude on ground already fully occupied by other demands, whose disallowance would be felt as a privation because their claim to satisfaction seems so much more pressing.

This is the important point. The question is as to the order and sequence of all classes of demands; not only as to the particular demand which is to be satisfied by means of the public contrivances in question, but also as to that class of demands which is met by private business. Within the sphere of this aggregate of organized demand, some decision will have to be reached as to what place in the scale should be assigned to each particular demand.

Just as every prudent housekeeper<sup>1</sup> is wont to calculate whether his income will allow him to afford a pleasure journey, a purchase of paintings, or to indulge the gratification of any other like want of the second or third rank, and to consider whether the gratification of this new want will not unduly stint

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<sup>1</sup> The oft-repeated statement that, unlike the private individual, the state adapts its receipts to its expenditures, recurs again in the writings of one of the latest French economists, Charles Gide (*Principes d'Économie politique, 2<sup>me</sup> édition, 1889, p. 593*). This statement holds true only so far as concerns the superficial, juridical aspect of the case. After the national requirements have been fixed at a certain amount, the state proceeds to demand such an amount from its subjects in the form of taxes. The private individual, who is not clothed with such sovereign power, is of course obliged to inquire into the extent of his income before determining what his expenditure is to be. But viewed from the economic standpoint this contrast disappears; inasmuch as the determination of the public requirement rests upon an elastic basis in just the same way as is the case in private life. In order to a rational solution of the problem, regard must be had to the available means, and, just as in a case of private expenditure, a balance must constantly be maintained between the urgency of each particular item of expenditure and the pressure which its defrayment throws upon other needs of the economic unit in question. And so far as it holds true in the economic sense that income is affected by expenditure, it is true alike of private and of public economy. If the burden of taxation spurs the private individual to greater effort and parsimony, an expenditure of another kind may also serve the same purpose.

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certain other wants which are undeniably more important, such as the need of shelter, clothing, food, care of children, provision for the future by the saving of a part of the yearly income, -so likewise does the same question come up when reference is had to that class of the needs of each particular household and of the community which are provided for by state and communal institutions.

The question will now read, is the new demand on behalf of the national defense, for better lodging and victualing of the troops, for the construction of new warships and harbors, for the provision of new ordnance and arms, or more serviceable uniforms, - will this new military requirement be warranted as against demands for other purposes? What goes to make up these other demands, however, is not simply the aggregate of services which the commonwealth renders to the aggregate of the citizens, not simply the various public institutions and their requirements, but it consists likewise of all those things which each particular private establishment would regard as its special want, together with that which they contribute in the way of taxes to the support of the state and of the commune. This other demand, accordingly, with which the new military demand is to be compared for measurement, and as against which it will have to justify itself, comprises the need of nourishment, shelter, clothing, education, sociality, benevolence, provision for the future, as well as the requirements of the public administration of justice and police, public encouragement of art and science, poor-relief, etc. And the like is true with respect to every other new demand on part of the commonwealth.

§ 155. An increase of the means available for meeting this demand, through a favorable turn of circumstances, affords nothing more than an apparent simplification of the problem which the supposed case offers. As a matter of fact, it is practically desirable to be able to contrive new means to meet the new demand, means which need not be withdrawn from their previous disposition. But this is no answer to the question whether this

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new need has the first claim to the new resources, and there is nothing to hinder the same thing from repeating itself in the economy of the state and commune which has so often been noticed in private establishments, - namely, that the new abundance is turned to purposes which should have been the very last to have received attention. The real difficulty still remains in such a case. It lies in the adjustment of the relation of each particular object of expenditure to all the rest. Even within the smaller circle of the household, the solution of the problem is difficult enough, and as a matter of fact, it is only partially effected in most cases. In the public economy, and more particularly in a large commonwealth, the difficulty is very great indeed. Indeed it would be a problem of stupendous difficulty were it not that every new adjustment arrived at in this balancing of proportions has but slight effect, as compared with the crystallized precipitate of a long-existent, gradually developed body of persistent demand. Still the problem is always difficult enough, and shows us, in the ever-renewed controversies, the impossibility of a thoroughly satisfactory solution.

The inherent difficulty of a decision as to what particular needs of first, second, third rank may deserve attention, and what may be the degree of urgency of each particular kind of demand, is augmented by obstacles of a subjective character due to the inadequacy of human insight.

So long as the crude intelligence of the average citizen remains inaccessible to any rational conception of the essential character and of the necessity of a public revenue, so long will there remain, subjectively, the constant consciousness of a burden, even in a case where the tax demanded by state or commune is required to cover a need equally urgent with the need of daily bread. The subjective feeling of annoyance will always remain; for the most frivolous indulgence is paid for with a lighter heart than any tax whatever.

Moreover, so long as the more well-to-do classes of society regard the payment of taxes simply as the price paid for a

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selfishly calculated benefit, and are inaccessible to any deeper feeling of duty in the matter, so long, surely, will they continue to feel the burden as oppressive, which, with a better comprehension of the relation of the individual to society, should be accepted as a matter of course and easy to be borne.

Conversely, the proletarian masses at the other end of the scale, who simply do not contribute out of their abundance what they pay to the state and commune, are easily disposed to judge of every object of expenditure on the part of the state according to the standard set by their own necessities, and will - at least as soon as class consciousness develops among them - regard every item of expenditure as heavy and oppressive if it falls outside the circle of their own every-day necessities, and is devoted to the higher aims of art and science.

The one class errs, in that they, without any sense of obligation, seek the advantage of their own more cultured class at the expense of the crude conditions of existence of the lower classes. The other errs in that the narrow horizon of their hapless life hinders them from seeing the true goal of advancing civilization. But every administration in a modern state will have to deal with both these classes alike.

## II. THE DEFRAYMENT OF THE PUBLIC EXPENDITURE.

§ 156. But a good deal nearer the surface, and therefore nearer to the point of view of the common run of practical discussion, are the questions, which concern the defrayment of the public expenditures, that is to say, the maintenance of a balance between the expenditures and receipts of the public treasury.

The fact of the necessity of maintaining such a balance is obvious and requires no detailed discussion. Every good citizen is well acquainted with this necessity from its daily and ever recurring presence in the affairs of private life. As we have already frequently called to mind the identity of prudence as applied in public and in private economy, so also at this point. The deceptive appearance due to the peculiar resources at the command of the public administration, as compared with private

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sources of income, makes it necessary to begin by correcting the misconception according to which the maintenance of an equilibrium here is less imperative than it would be in the case of a private establishment. Only when this has been done can we proceed to give our attention to those peculiar resources which state and communal administrations have at their disposal, together with the special difficulties with which they have to deal, as contrasted with any private establishment.

It is evident from this universal experience in economic matters that a chronic excess of expenditures over receipts - what is called a "deficit" in the public finances - is an abnormal condition and must be avoided.

The affairs of everyday life offer fewer illustrations of the failure of the adjustment in the other direction of an excess of receipts over expenditures. For obvious reasons this case is much rarer than the contrary. It is evident, however, from its repeated occurrence in the national finances of the United States of America, in early years and also of late,<sup>1</sup> that, under given circumstances - in this particular case on account of the smallness of the national expenditure and the peculiarities of the tariff policy - a disturbance of the equilibrium may also take place in

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<sup>1</sup> President Cleveland's message of Dec. 6, 1887, contains the following remarkable utterances: "You are confronted at the threshold of your legislative duties, with a condition of the national finances which imperatively demands immediate and careful consideration.

The amount of money annually exacted, through the operation of the present laws, from the industries and necessities of the people, largely exceeds the sum necessary to meet the expenses of the government.

When we consider that the theory of our institutions guarantees to every citizen the full enjoyment of all the fruits of his industry and enterprise, with only such deduction as may be his share toward the careful, and economical maintenance of the Government which protects him, it is plain that the exaction of more than this is indefensible extortion, and a culpable betrayal of American fairness. ... The public treasury, which should only exist as a conduit conveying the people's tribute to its legitimate objects of expenditure, becomes a hoarding place for money needlessly withdrawn from trade and the people's use, thus crippling our national energies, suspending our country's development, preventing investment in productive enterprise, threatening financial disturbance, and inviting schemes of public plunder. ... It will not do to neglect this situation because its dangers are not now palpably imminent



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this direction. And this brings us to an appreciation of the fact that the fiscal administration, must be prepared to meet this emergency also. The precautions taken must follow the same general rule that has been laid down for the avoidance of a deficit, namely, such a change in the amount of the expenditures or of the receipts as shall suffice to establish an equilibrium.

§ 157. With a view to the maintaining of an equilibrium in the public finances it is necessary to examine the aggregate of expenditures in detail, with respect to the regularity or irregularity of recurrence of the particular objects for which the expenditure is incurred.

Adopting the usage of private business, it is customary to distinguish public expenditures as ordinary and extraordinary expenses. In the economy of the household we are wont to consciously contrast the annually recurring and relatively invariable, or at any rate only gradually changing expenditures, for dwelling, food, clothing, social intercourse, recreation, education, etc., with the exceptional expenditure incurred for a household establishment or for some other like provision. Likewise in the case of the public economy we make a distinction between "current," "permanent," "annual," "regularly recurring" expenses and the objects for which they are incurred on the one hand,

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and apparent. They exist none the less certainly, and await the unforeseen and unexpected occasion when suddenly they will be precipitated upon us.

On the 30<sup>th</sup> day of June, 1885, the excess of revenues over public expenditures after complying with the annual requirement of the sinking-fund act, was \$17,859,735.84; during the year ended June 30, 1886, such excess amounted to \$49,405,545.20; and during the year ended June 30, 1887, it reached the sum of \$55,567,849.54, ...the excess for the present year amounting on the 1st day of December to \$55,258,701.19, and estimated to reach the sum of \$113,000,000 on the 30<sup>th</sup> of June next, at which date it is expected that this sum, added to prior accumulations, will swell the surplus in the Treasury to \$140,000,000.

There seems to be no assurance that, with such a withdrawal from use of the people's circulating medium, our business community may not in the near future be subjected to the same distress which was quite lately produced from the same cause. And while the functions of our National Treasury should be few and simple, and while its best condition would be reached, I believe, by its entire disconnection with private business interests, yet when, by a perversion of its purposes, it idly holds money uselessly subtracted from the channels of trade, there seems to be reason for the claim that

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and the "non-recurring" expenses on the other, and call the former class the ordinary, and the latter the extraordinary expenses.

This terminology is questionable. It indicates an elementary stage of economic thought in that it classes as "extraordinary" an item of expenditure which in many cases is to be distinguished from the so-called ordinary expenses by a technicality alone, and not by the extraordinary character of the object for which it is incurred. If we accept this view we are led to the curious conclusion that the "ordinary" expenses are smaller, relatively to the "extraordinary," the more confused our economic speculation is, and conversely, the extraordinary expenses grow relatively smaller the more highly developed our economic conceptions become.

It is a well accepted fact in private life that wherever systematic management in household economy is but very slightly developed, where "hand to mouth" is the rule of life, there is a great number of items of expenditure which present themselves to a thriftless improvidence under the unwelcome head of "extraordinary" expenses; - items which a rational foresight would very easily have been able to bring in under the head of "ordinary" expenses. On the other hand, there is such a devel-

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some legitimate means should, be devised by the Government to restore in an emergency, without waste or extravagance, such money to its place among the people.

If such an emergency arises there now exists no clear and undoubted executive power of relief. Heretofore the redemption of three per cent, bonds, which were payable at the option of the Government, has afforded a means for the disbursement of the excess of our revenues; but these bonds have all been retired, and there are no bonds outstanding the payment of which we have a right to insist upon. The contribution to the sinking fund which furnishes the occasion for expenditure in the purchase of bonds has been already made for the current year, so that there is no outlet in that direction.

In the present state of legislation the only pretense of any existing executive power to restore, at this time, any part of our surplus revenues to the people by its expenditure, consists in the supposition that the Secretary of the Treasury may enter the market and purchase the bonds of the Government not yet due, at a rate of premium to be agreed upon. The only provision of law from which such a power could be derived is found in an appropriation bill passed a number of years ago; and it is subject to the suspicion that it was intended as temporary any limited in its application, instead of conferring a continuing discretion and authority. No condition ought to exist which would justify the grant of power to a single official, upon his judgment of its necessity, to withhold from or release to the business of the people, in an unusual manner, money

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opment of systematic foresight possible as will bring a continually larger number of extraordinary expenditures into the category of ordinary, annually defrayed expenses. The whole question turns on a technical distinction.

§ 158. Elementary discussions in political economy have long been accustomed to make a distinction between goods which are wholly consumed in a single use (as food, drink, fuel) and goods which are consumed only gradually, and so are capable of a continued use (as clothing, shelter, furniture, tools).

The need for any given commodity will evidently recur more frequently the more distinctly it belongs in the first class, and less frequently the more distinctly it belongs in the second class, that is to say, the more durable a basis for a continued use its physical characteristics will afford. The need of food recurs daily in every household; the need for tables and chairs recurs in most households scarcely once in a lifetime. Now, since any scheme, such as is desirable in private life and is altogether imperative in every public administration, naturally covers a certain definite period, whether of one year or more than one, it follows that any items of expenditure which in consequence of the physical character of the objects for which

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held in the Treasury, and thus affect, at his will, the financial situation of the country; and if it is deemed wise to lodge in the Secretary of the Treasury the authority in the present juncture to purchase bonds, it should be plainly vested, and provided, as far as possible, with such checks and limitations as will define this official's right and discretion, and at the same time relieve him from undue responsibility.

In considering the question of purchasing bonds as a means of restoring to circulation the surplus money accumulating in the Treasury, it should be borne in mind that premiums must of course be paid upon such purchase, that there may be a large part of these bonds held as investments which can not be purchased at any price, and that combinations among holders who are willing to sell may unreasonably enhance the cost of such bonds to the Government. It has been suggested that the present bonded debt might be refunded at a less rate of interest, and the difference between the old and new security paid in cash, thus finding use for the surplus in the Treasury. The success of this plan, it is apparent, must depend upon the volition of the holders of the present bonds."

[The extracts from the President's message are here given without abridgment, instead of in the somewhat condensed form given in the German. - TR].

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they are incurred, regularly recur within the stated period, will readily fall into the periodicity of such a scheme.

On the other hand, such things as are too lasting to need renewal every year or two will appear under the head of "irregular" or "extraordinary" expenses.

Plainly this is nothing but an arbitrary classification resulting from the distinction of expenditures according to certain time-limits; whereas with an indefinitely extended time-limit those items would be recognized as "regular" and "ordinary" whose regularity is now disguised by the arbitrary limits of the period selected.

§ 159. The difficulty arising from these arbitrarily chosen, narrow time-limits may be set aside by taking thought; and the expenditures for such relatively imperishable objects may accordingly be conceived of as likewise regularly recurring and as subject to the same regulations as the annually recurring body of expenditure. This is on the supposition that the extent of the longer period in question is known; so, for example, it is possible to calculate beforehand the length of time which army uniforms or railway rails will last.

There are, surely, difficulties in the way of applying this principle. In the first place, the degree of permanency in the case of a great man - things cannot be known beforehand. Further, we have to do not only with what may be calculated beforehand, but also with other contingencies which simply defy all prevision. In an age of such striking progress in the mechanic arts as ours, many a contrivance which is calculated to last for a long time ceases to be of any use long before its natural death, simply in consequence of its being left behind by the march of improvement.<sup>1</sup> They may call to mind the vessels of the navy, ordnance,

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<sup>1</sup>In the memorandum appended to the navy estimates of the German Empire for the year 1889-90, in justification of the demand made for 116.8 million marks for the construction of new vessels, there occur among other things the following statements: "Our fleet consists in the main of vessels which are still of some use, but out of date, whose decrease in value proceeds *pari passu* with the progress of improvements in the construction of warships by other nations. .... as regards the

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fire-arms, fortifications, etc. We may mention the very extensive demands made by our modern higher schools for purposes of scientific and medical research and instruction. Our departments of education and finance find themselves called upon year by year to make costly innovations at one point or another, in order to retain or to secure the services of the indispensable pioneer of research.

But still further; wars, inundations, industrial depressions recur, but not with any regularity that is discernible by the human eye. Preventive measures, and therefore the expenditures they involve, may serve to lessen the intensity of such fortuitous calamities, and may even in many cases prevent them; but, after all, there still remains a body of indefinite demands which cannot be calculated beforehand. Dikes and works for the control of dangerous rivers, as a safeguard against floods, a prudent industrial policy for the obviation of trade depression, a jealous care of the national defense - all measures of this class may be of use as preventives and so may serve to bring the "extraordinary" expenses, to some extent, under the head of the regular annual expenditure. Still, these measures can avail only to reduce, never to abolish these calamities and the financial demands arising out of them.

So we are led to the conclusion that the line of demarkation between ordinary and extraordinary expenditure may be shifted but cannot be obliterated.

§ 160. Corresponding to the customary distinction between ordinary (regular) expenditures, and extraordinary (irregular)

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ironclad vessels now available for coast defense, in the stricter sense, the case is much the same as with the vessels of the regular fleet. The greater part of them, though still fit for service, are yet to some extent obsolete, and to some extent no longer adequate to the ordinary demands made upon them. .... In consequence of the increased speed of all other classes of vessels, including warships proper, dispatch boats in the navies of all nations have been compelled to increase their efficiency of service to so considerable an extent that dispatch boats which a few years ago were rated as fully up to the standard must now be regarded as out of date. Accordingly in the construction of this class of vessels, too, we can not afford to remain inactive, but must continue to make improvements."

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expenditures, there is the other customary distinction between ordinary and extraordinary resources.

While it appears that, as regards the former distinction, there will always be some occasion for an extraordinary expenditure, owing to the fact that the periodicity of certain of the needs of the community does not admit of calculation; so also it appears; as regards the latter distinction, that the line between ordinary and extraordinary resources is a shifting one, inasmuch as there is no extraordinary resource which may not, under given circumstances, have to be applied to meet ordinary expenditures; and conversely there is no ordinary resource which may not, under given circumstances, come to be applied to the extraordinary expenditure.

Yet something of a distinction remains. The resources preferably to be drawn on for meeting regular expenditures are those which are adapted to yield a regularly recurring income; whereas, for meeting an irregular or occasional demand, such fiscal means may advantageously be employed (although it is not imperative that they alone should be) as can be drawn on only for occasional purposes and not for expenditures that recur annually.

As a concrete example, the annually recurring expenditures for the support of a standing army, for the salaries of the civil service, and for the like purposes, will in any well-ordered fiscal system be met by annually recurring taxes; it is only when the accustomed order is disturbed by unusual exigencies (war, famine, industrial depression) - exigencies which threaten the orderly course of business and the tax-paying capacity of the community to a much less extent in modern society than in earlier times - that such financial expedients should be resorted to as are primarily adapted to meet occasional demands only. Of such expedients during the earlier history of finance, may be mentioned the alienation of productive public property (domains, etc.); in the later development of financial policy by far the most important of such expedients is the public credit. Both of these fiscal expedients, both the alienation of domains and the use of the public credit, are by nature ill adapted for meeting

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annually recurring expenditures. Just as property once sold cannot be sold again the second time, so also resort to public credit cannot be made a source of annually recurring income without resulting in an annually increasing debt, and a consequent annually increasing burden of interest. And these difficulties will, with each succeeding year, increase all the more, the greater the difficulties were which were sought to be evaded by such expedients.

It is therefore imperative that this class of expedients should be reserved for such extraordinary exigencies, as by their infrequency and the suddenness and intensity of their demand upon the treasury, make resort to some such means indispensable. But even for exigencies of this kind, of which war is now and long will be the chief example, it should ever be kept in mind that some provision of another kind is also desirable whenever the special circumstances of the case will admit of it.

§ 161. In order to a clear comprehension of these questions some discussion of the nature of public credit (national and communal) is desirable.

In this field, too, theory has been influenced by the course of events in the historical development. In the early stages of public economy, credit appears in such an extremely precarious position - pawning of crown lands and revenues, onerous conditions attached to loans, usurious interest and the like, on the one side; breach of faith, insolvency, exhaustion of resources, on the other side - that theoretical discussions of the matter are largely determined by the palpable destitution of the borrowing state. As fast as the ethical and economic character of the modern state has developed, all this has changed. From having been a perpetually embarrassed debtor, the state, with its demand for loans, has come to be sought after as affording the very safest form of investment. This happens because public sentiment, in all matters relating to the state, has changed; because this altered public sentiment is backed by the infinitely increased resources at the command of modern industry and

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modern finance. There results a general confidence in the permanency of the state - in its ever-increasing strength and its unquestioned integrity and soundness. The impression made by the enormous amounts which for some decades past have been raised by this means in nearly all the great states of today, without destroying the country's wealth or its financial system, and often without in the least impairing either, - this impression has been so pervasive as to inevitably leave its traces even in the theories held concerning public credit.

There resulted an extravagantly optimistic theory, which, significantly enough, had a great vogue in its time, and found many adherents. Contemporary admiration for these clever theories leads to rating them higher than they deserve. They are nothing but a reflection of passing events, whereas the object of scientific inquiry is not only to reflect the events but to understand them.

Such a reflection of passing events was the view held a generation ago by those who, in accordance with the materialism and optimism of the older Political Economy, explained the state and the national activity as a whole as being an "incorporeal capital," represented by the productivity of all outlay made for national purposes, including war expenditures. There seems to have been no appreciation of the extent to which the best and highest elements of life were debased by attempting to erect them into an industrial investment.<sup>1</sup>

§ 162. It is true, there are certain objects of public expenditure in which the funds raised by means of public credit take the form of a productive investment. In such cases the objections which might be made against "consumption loans" from the business point of view, are out of place, since the question really concerns a case of a "productive loan."

Although Prussia, during the decade 1878-88, invested in

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<sup>1</sup> Cf., for correction of the exaggerations of Dietzel and Stein, the restrictions offered in A. Wagner's *Finanzwissenschaft*, *l. c.*, and more especially A. Schaeffle, *Zeitschrift für die gesammte Staatswissenschaft*, 1884, pp. 134 *et seq.*, as well as a critical paper by the present writer in the same journal, 1868, pp. 594 *et seq.*



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the purchase and construction of some 18,000 kilometers of railroads a capital of over three milliards of marks, and although it has met this expenditure by recourse to its credit, on the other hand the railroad capital which it has acquired represents a productive investment which sufficiently offsets this large debt. In point of fact, this capital is so far productive as not only to cover the interest on the national debt incurred, but also to afford a surplus toward its gradual extinction, and even something more.

This is an example of a "productive loan" in the traditional sense. The example is a particularly favorable one, and is typical of a great number of other cases that occur in national and communal economy, especially in view of the present tendency towards a greater extension of state and communal activity in the direction of many and various business undertakings (gas-works, water-works, horse-cars, etc.).

But this is only one side of the question, and moreover the side which offers the fewest difficulties in the way of a discussion of public credit.

The other and more difficult side begins where the scope of the so-called consumptive credit begins. And on this point opinions vary all the way from that prudent moderation which insists on applying the maxims of private business in such a sense as to condemn all "consumptive credit," even in the economy of the state proper, to the opposite extreme of the exaggerated views that stand for nothing but a spontaneous expression of the latest phases of the development of public credit, but which must be admitted, on this very account, to contain a legitimate protest against the former excessively narrow view.

§ 163. Even within the narrower field of private economy it will not hold that productive credit alone is to be commended, and that consequently consumptive credit is to be in all cases discountenanced.

This position amounts to nothing more than a well-grounded protest of common sense against the well-known and wide-spread abuses of the practice of living on credit. It is the intention to

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rebuke this practice without discountenancing all forms of consumptive credit indiscriminately. For there are cases where necessity and expediency require that the accustomed routine of the household, which may be in itself commendable, should yield to the urgency of some exceptional demand.

But in the economy of the state the occasions of this kind are so urgent and at the same time recur so inevitably that, for one thing, they cannot be disregarded, and for another they cannot be met except by contracting a large debt. The question in such a case concerns the very gravest interests of the nation, and in such a case no sacrifice of an economic nature, even including that of the accepted and commendable adjustment of income and expenditure; is too great. And still, sacrifices of this sort are not "productive," especially not in the cases where they are the greatest. What productive end, for example, did the French gain by the expenditure of the enormous sums which the last war with Germany cost them? They have not even acquired the "incorporeal capital" of having learned to guard themselves against the like mischief in the future.

There is one thing, however, about this particular resort to public credit, that is really wonderful. And that is, that a modern state should be able, at the close of so unhappy a war as that of 1870-71 was for France, to borrow, on any tolerable conditions, milliards after milliards, when the new loans went to increase enormously the burden of a national debt that was already very great. This is a triumph for those moral and economic forces which go to make the modern state independent of the limits of the resources immediately at hand, and to place at its disposal further resources that are made available only through the confidence that exists in its permanence and continued development. It is the relative immortality of the state

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<sup>†</sup>The expenditures of the French nation immediately before the great war, in the year 1869, amounted to 2209 million francs; whereas in the year 1872 it was 2655 millions. From that time on it increased rapidly and in the year 1877 it had already reached 3052 millions; in 1887 3234 millions. According to the budget of 1887, the annual interest charge on the consolidated debt amounted to 740 millions; that on the redeemable debt, to 337 millions.

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as compared with the short life of any individual, that serves to set these limits aside, and offers to the credit of the fully developed state resources which are accessible to it alone.

§ 164. We have now reached the point at which it will be well to give some attention to the doubts that occur as regards this seductive fiscal expedient, and come to some decision between the claims of this and other means of revenue. The discussion will, of course, be confined to that limited field of financiering within which the extent and suddenness of the demands does not make recourse to the public credit imperative. One thing is constantly to be kept in mind. In the last analysis every public debt, however unusual and however large, must always rest on the taxes, as the regular and ordinary means of satisfying all fiscal demands. It is the nature of a debt to require payment, and at least the greater part of the debt bears an annual interest charge, and these charges can be met in a rational way only by means of current taxes. An extinction of the old debt by means of a new loan is no extinction; the payment of the interest charge on the old debt by revenues obtained from a new loan subverts the foundation on which public credit rests. Credit will grow constantly weaker, and the terms on which each successive loan is obtained will grow constantly less advantageous. Whereas a determined effort on the part of a community to meet its expenditures by means of the greatest possible exertion of its tax-capacity and an avoidance of all debt, cannot fail to produce such a moral effect as will increase the readiness of capitalists and of the money-market to advance any amount that may be required in such extraordinary cases as will unavoidably occur. And in case of the opposite financial policy a corresponding penalty will ensue. So it appears again that all business policy [*Wirtschaft*] in private and in public life partakes of an ethical character.

It follows therefore that the readiest and most expedient method, in so far as adequate resources may be obtained in that way, is the method of taxation. The burden falls, in the last

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resort, on the taxpayers, and can in any case be shifted from their shoulders only temporarily by recourse to public credit; while if resort is had to taxation this burden will fall immediately upon the taxpayers, and what has once been raised by this method need not be raised a second time.

But between the two alternatives of an unavoidable resort to loan and a plainly expedient recourse to taxation; there is a middle ground, within which there is room for discussion as to the relative advantages and disadvantages of these two financial methods.

§ 165. Among the objections against contracting a national debt, which the earlier school of theoretical writers were wont to place in the foreground, a prominent one is the apprehension felt about withdrawing capital from industry.

This objection is an expression not only of the standpoint of industrial capital, which dominates the older school of thought, but also of a stage of industrial development which had come to an adequate consciousness of its own lack of the capital made necessary by the state of development of the industrial arts and the business methods of the time. This same objection, further, involves a protest against that exaggerated conception of the magical potency of credit, which is really open to the criticism that the means for meeting today's fiscal needs can under all circumstances whatever be drawn only from the stock of commodities, on hand today; no soldier can be fed now with the corn that is to be grown next year, nor can he be armed with the musket that is to be manufactured next year.

However, this objection has lost much of its force in consequence of the great increase of accumulated capital in all modern civilized states, and indeed the latest phase of the development shows a surplus of capital which has given rise to a condition directly the contrary of the apprehended difficulty on which this objection proceeds. And it is not simply this surplus of capital, by itself considered, that fosters a sentiment favorable to the contraction of public debts. There is among the owners of capital a well-founded conviction of the superior character of

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national bonds as an investment, as compared with the opportunities for investment offered by industry. No one who is not infatuated with the point of view of the old school will find anything to deprecate in this new departure in the investment of capital, or be inclined to rate speculative enterprise above it. As a matter of fact the modern system of national debts has brought into existence a class of investments eminently suited to the wants of a great number of people, and destined to restrain precisely this class of people from rash speculative ventures.

Even in the earlier days of public credit and of the accumulation of capital, it will hold true that the international character of the money market went far to equalize the discrepancies in the distribution of capital due to differences in industrial development between different countries, and that the superior character of national securities attracted capital from a distance, which would not have migrated so far for other purposes.<sup>1</sup>

§ 166. More serious, it seems to me, is the objection that national debts act, as far as in them lies, to determine the distribution of the nation's wealth in a manner which is already favored by the other factors at work in our industrial age, and which is by no means to be regarded as desirable. The objection is that they serve to strengthen the tendency which, in modern society, makes for contrast between those that have and those that have not, in that they add to the burdens of the portionless and increase the income of the property-holding class.

A well-regulated system of taxation, even when it requires

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<sup>1</sup> Furthermore, in a country which is rich in capital, the international market for securities serves the purpose of a large reserve fund which can be drawn on in case of a great and sudden demand for capital. A striking example of this fact also is afforded by the placing of the French milliard loans during the years 1871-72, Leon Say, in his report, gives figures to show the export from France of foreign securities which were to serve as payment of the war indemnity, that is to say, for the payments made by the new subscribers to the French rentes. Among other things it may be noted that there were paid in Paris during the year 1868, for matured coupons on Italian bonds, eighty-five million francs, while in 1872 only sixty million francs were so paid. Cf. *Rapport fait au nom de la commission du budget de 1875 sur le payement de l'indemnité de guerre*. (*Theory of the Foreign Exchange*, by George G. Goschen; French translation by Leon Say, 2<sup>nd</sup> ed. 1875, p. 282.)

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great sacrifices for the nation's welfare, should be so contrived as to burden all classes of society, and especially the classes that are best able to contribute, in due proportion. The avoidance of raising funds by current taxation and a preference for the use of public credit, on the contrary, will not only exempt the property-owning classes from their share in the sacrifice incurred, but the national loans will at the same time afford them an opportunity for advantageous investments, the annually recurring interest charge on which is drawn from the income of society as a whole, and consequently in an especial degree from the great number of people of moderate means, and passes over into the income of the nation's creditors.

An example of this occurs in the conduct of the financial affairs of the French government at the time of the French-German war of 1870 and 1871. These extensive loan operations resulted in a considerable addition to the interest charge and a consequent disproportionate burdening of the lower classes, and even to this day no tax reform has been undertaken that would neutralize this inequality.<sup>1</sup>

It is to be noticed that in this case, as in all cases, the question is far more as to the conformity of the tax system to the requirements of equity, than as to the desirability of loans in preference to taxes. The tax system wants reform, and so long as this want is not met, it is of no avail to emphasize the shortcomings of national loans.

Here we come face to face with a fact which needs closer attention.

§ 167. Apart from extreme cases, in which the contracting of national debts is and will always be unavoidable on account of

<sup>1</sup> The aggregate of the taxes which the French budget for the year 1887 calls for, amounts to about 2600 million francs. Of this aggregate

The tax on beverages yields	425 million francs.
The sugar tax yields	168 " "
The salt tax (including duty) yields	33 " "
The tobacco monopoly (net receipts) yields	<u>320</u> " "
Total	946 million francs.

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the urgency of a great immediate demand, there is a middle ground within which there is space for the extension of a productive tax system, instead of a resort to public debt. There is no room for doubt that in the case of the state debts hitherto contracted (and municipal debts as well) no small part of the debt represents what may be called a makeshift made necessary by the inadequacy of the tax system of the time. For in all cases where there can be any question - and therefore exclusive of the cases where absolute impossibility precludes question - as to the possibility of meeting the new demand by augmenting taxes, - in all such cases the question really is as to whether the resulting pressure upon the constituent units of the community is bearable, regard being had to their customary requirements in other directions (cf. § 155 above), and this again resolves itself into the question as to how patiently or impatiently the subjective effect on their feelings will be submitted to by the citizens on whom the burden rests.

Hence the historical character of the problem: Hence the view which finds in this middle ground the basis of all that development of national spirit which has ripened into a willingness to afford such sacrifices as the exigencies of the commonwealth require. The farther advanced a commonwealth is, the more highly developed its tax system, the less will it be compelled to resort to the expedient of a loan.

§ 168. There is one peculiar function, and a legitimate one, in our political economy which will always devolve on credit. It is, in fact, the same function that credit performs in private business.

This function is the maintenance of that elasticity which is necessary to a balance of income and expenditure in cases of a temporary discrepancy between them. For example, if the state habitually pays its officials their salaries at the beginning of each quarter or month, while its receipts from taxes come in only at the end of the quarter, or may perhaps be delayed by difficulties

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affecting the taxpayers' ability to pay; in such a case a discrepancy occurs which will have to be provided for.

For this purpose there are special forms of credit which are calculated for no greater length of time than the duration of the exigencies which they are intended to meet. A form of loan which has latterly come into great favor for this purpose is that which has spread from England into other countries under the name of Exchequer Bills; these fall due in a period of from three to six months to one or two years and bear a moderate rate of interest, very much as ordinary securities of corresponding character. A second form is non-interest-bearing paper money which serves the same purpose of a variable volume in the public economy that bank notes do in private business.

§ 169. Adolph Wagner has called attention to a certain peculiar lacuna which the use of the national credit does not adequately cover. In so doing he has evidently been influenced by the experiences of the Prussian war management during the last few decades. It is the lacuna which is sought to be covered by a war fund.

There is no essential incongruity between the use of the public credit and the war fund. It is by no means inconceivable that in the absence of other sources from which a war fund may be accumulated (surplus revenue from the annual tax-receipts, alienation of property belonging to the state, receipts from war indemnities) a loan might be issued for this special purpose. The point of contrast is simply as to the particular measures which it is thought expedient to employ when the crisis arrives.

And as to this point, experience proves that during the initial stage of a war-during that sultry calm preceding the storm, when the expectation, declaration and preparation for war follow on each other's heels - the sudden war demand on the treasury coincides with a violent disturbance of credit, and a consequent stringency in the money market. The North-German army (exclusive of the Saxon contingent) required, during the weeks



from July 15 to August 3, 1870, no less than two million thalers daily for mobilization and for carrying on the war, that is to say, an aggregate of fully 40 million thalers. As had already appeared in the war of 1866, so now again, the possession of an adequate cash fund, which had been accumulated for this purpose in times of peace, proved itself the most available means of meeting such a contingency, at the same time that it served to strengthen the tone of the general money market, and especially to maintain confidence in the state's own securities.

As a result of repeated experiences of this kind, the imperial war fund has come to take its place as an essential constituent element in the German financial system (fixed by imperial statute of November 11, 1871, at 40 million thalers).

So it has come to pass that an institution which at one time, before the development of public credit, the best financiers found indispensable, and which afterward, when public credit had reached a fuller development, came to be regarded as obsolete, has again found acceptance in the theory<sup>1</sup> and the practice of public finance.

A war fund of course finds its limit in the fact that the great Waste involved in letting the money lie idle (preferably for as long a time as possibly puts a limit to the amount, so that, for all purposes beyond the immediate expenditure of the first few weeks, recourse must always be had to public loans.

The adoption of a system of "extra taxes" for which legislative provision has been made beforehand, is essentially a matter which depends on that development of national spirit and of readiness to submit to taxes, which has already been emphasized in what has gone before. Under present circumstances nothing considerable is to be expected from this source. On the other hand it is quite conceivable that at some time in the future special war contributions<sup>1</sup> regulated by law may find a sufficient motive in an enhanced sentiment of patriotism, and may, at the same time, serve to obviate any general panic.

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<sup>1</sup> See also Leroy-Beaulieu, *Traité*, vol. ii. livre ii. chap. 2, where this matter is discussed at length.

### III. THE FORMAL ORGANIZATION AND MANAGEMENT OF THE PUBLIC ECONOMY.

§ 170. It is very desirable in the case of all private establishments, though relatively few have attained the point, that estimates should be made out from time to time with a view to the orderly management of the affairs of the concern. As regards the public economy, on the other hand, we have now very generally reached the point, so far as concerns civilized communities; that an estimate (*État*, Budget) is submitted at stated intervals and to cover a stated period of time. For the state at large the requirement of such an estimate is made by the fundamental provisions of the constitution; for communal bodies, as part of the duties of properly constituted state officials.

So far as concerns the national finances, the participation of the body of citizens in legislative and administrative matters takes the form of an exercise of control over the regular expenditures of the state. The voting of expenditures and revenue, the balancing of accounts by adequately covering fiscal demands, the decision as to the various kinds of fiscal means to be employed, discussions as to the urgency of different classes of demands upon the treasury, consideration of the claims of this or that demand relatively to the means available, - all these things are matters on which the tax-payers are constitutionally entitled to be heard through their representatives (Parliament, Landtag, Reichstag, Town Council, etc.).

Differences in the manner and extent of this constitutional control are therefore due to differences in the fundamental law of the particular nations. To such an extent is this true that many essentially technical features of financial administration have their character determined by political considerations rather than by considerations of expediency.

So, for example, with respect to the length of the fiscal period adopted. In view of the disproportionately great trouble involved in an annual repetition of all the labor which the estimate costs the various departments of government and the representative

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bodies that bear a hand in it, it is evidently desirable on grounds of expediency to extend the fiscal period beyond the limits of a single year. But there are other reasons - such as the desirability of an annually recurring opportunity for the people's representatives to criticise the estimates of the government, item by item - why annual estimates have as a rule continued to be preferred to estimates covering a longer period.

Even the time-tried example of England, the model parliamentary government, in favor of exempting the unavoidable expenditures from the requirement of a yearly appropriation, has so far been unable to find acceptance on the continent, evidently for constitutional and political reasons rather than for reasons of fiscal administration.

§ 171. It is obviously expedient, as a matter of financial policy, that the periodical estimates should be thoroughly overhauled and passed upon in due conformity to constitutional requirements, by a parliamentary body representing the country (the state, the city, etc.). The particular manner in which this function is performed in any commonwealth is determined by legislative provisions regarding the budget.

In England a considerable part of the expenditures and receipts is permanently fixed by law, answering to the permanent necessity that exists for the carrying on of the fundamental functions of the state. Only a part of the annual expenditures and receipts is variable, and is therefore made dependent upon an annual appropriation.

Deliberation on the budget takes place only in a full session of the lower house; which is different from the method usually adopted by parliamentary bodies on the continent, of submitting the estimates to a detailed overhauling by a budget committee and so forestalling and shortening the deliberation of the whole assembly. Latterly the English custom has in part been adopted in Prussia, in that certain portions of the

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<sup>†</sup>Rudolph Gneist, *Budget und Gesetz nach dem konstitutionellen Staatsrecht Englands mit Rücksicht auf die deutsche Reichsverfassung*, 1867. Cf. Gneist, *Englisches Verwaltungsrecht*, 3<sup>d</sup> ed. (1883), vol. i. p. 431.

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estimates are taken up forthwith and discussed by the whole house, while other and more important parts are first overhauled by the budget committee. The deliberation in the whole house secures to each member of parliament the opportunity to take part in the revision of the estimates as required by the constitution; the deliberation by the committee removes the weight of responsibility to that body, probably results in a more thorough overhauling, offers better opportunity for intimate and confidential conference with the representatives of the government, but is at the same time clumsier and less expeditious on account of the necessity of repeating much of the discussion before the white house.

§ 172. The submission of the estimates and the deliberation upon them in due accordance with the requirements of the law, as the normal and ordinary provision for each fiscal period, implies an exercise of control over the execution of the scheme adopted for the period in question.

This control partly concerns administrative or executive matters, partly it concerns the legality of items of receipt and expenditure.

For the former purpose, which, apart from a simple supervision of accounts, aims to secure the due execution of the administrative measures adopted, as well as a judicious and economical management of receipts and expenditures, the suitable organ is a central auditing board [*Ober-Rechnungsbehörde*], independent of all the other departments, as well as of the department of finance. The progressive development of this sort of control is shown by the increasing independence of this board (*Ober-Rechnungskammer*) of all the other central organs of the State. Even the absolute-monarchical state found itself obliged to give its superior courts of revision [*Revisionsbehörden*], an independent position beside its ministries. (So, for example, in Prussia, Frederick William I. instituted the *Ober-Rechnungskammer*.) It is obvi-

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<sup>1</sup> Cf. the paper "Ueber den Rechnungshof mit besonderer, Rücksicht auf das Deutsche Reich" in the *Zeitschrift für die gesammte Staatwissenschaft*, 1876, 1877.

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ously for the interest of any monarch to place his ministries under the control of an independent authority which shall be responsible to the sovereign alone.<sup>1</sup>

It may perhaps seem self-evident that the proper body to see that the measures adopted are duly carried out is the representative assembly itself, or a committee of the assembly. But this method, after all, is in the spirit of the feudal state [*ständische Staat*] (in which the several estates really possessed such special organs of control, apparently for the purpose of defending the interests of one party against the other parties), rather than in the spirit of the modern constitutional state. It is the whole state as a unit that finds expression in the legislative act, so far as this act is established by concurrent action of the government and of the representatives of the people. And it is conformity to statute law that is here in question. It is therefore also appropriate that in this case jurisdiction should be left in the hands of an independent tribunal (Verwaltungsgerichtshof). And in view of the very close connection between these two lines of control, the most appropriate body in which to vest this controlling power will be a suitably constituted superior court of accounts (Ober-Rechnungshof). This would be a board holding the position of a supreme court of judicature and possessing the qualifications pertaining to that office, together with the resulting attitude of independence, both towards the central government and towards the representative assembly and its parties.

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<sup>1</sup> Cf. Löbe, "Die oberste Finanzkontrolle des Königreichs Sachsen in ihrer organischen Entwicklung von den ältesten Zeiten bis auf die Gegenwart" (*Finanzarchiv*, 1885, pp. 589-715).

## CHAPTER VII. THE VARIOUS KINDS OF PUBLIC REQUISITIONS AND EXPENDITURES [BEDARF].

LITERATURE. K. H. Rau, *Grundsätze der Finanzwissenschaft*. 5. Ausgabe (1864). *Erste Abtheilung*, 1. Buch. A. Wagner, *Finanzwissenschaft*: 3. Auflage (1883), 1. Theil, 2. Buch.

### I. THE DEVELOPMENT OF CONTRIBUTIONS AND EXPENDITURES IN KIND INTO CONTRIBUTIONS AND EXPENDITURES IN MONEY, AND THE LIMITS OF EACH CLASS.

§ 174. It is well known that, for reasons familiar to everyone, the course of historical development due to the division of labor and to technical improvements in industry, has constantly tended away from the employment of barter and payment in kind; and towards the use of money. The public administration has not only taken part in this general economic development, but has distinctly furthered it.

It is a mistake, however, as has already been pointed out in the general discussion of economic theory (see vol. i. secs. 246-249) to regard this course of development in the division of labor and the use of money as a supreme law of nature. It should rather be our aim to reach a valuation of the subject considered as an ethical matter and not as a matter of natural law: In the absence of such a valuation from an ethical point of view, we shall simply be amazed at the fact that in the midst of the highest development of modern national life, our financial system has, for some of the most important purposes, retained, or rather returned to, the method of receipt and expenditure in kind. This qualification will of course not prevent our recognizing the fact that the great mass of financial transactions has continually more and more been assuming the form of money transactions, just as has been the case with regard to the products and

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articles of consumption in private economy.<sup>1</sup> For most purposes the public administration, in like manner as is the case in private life, makes use of money as its means of purchase, and it must therefore require the contributions of its members in the form of money. Indeed, the fact serves to mark the character of this development, that it is in times of war, that is to say, at times when the accustomed course of industry is violently disturbed, that to a greater extent than usual recourse is had, and must be had, to transactions in kind in place of money transactions.

§ 175. But there is also another respect in which the employment of a division of labor and of money transactions is subject to limitations within the sphere of the military activity. Within this sphere whose function it is to build and maintain the foundation walls of political autonomy by the development and manifestation of power, both at home and towards external enemies - which will presumably have to fulfill this function for a very long time to come; in military matters, and precisely in their latest developments, the character of the human material required for military service on the one hand, and the special character of the arms, munitions, fortifications, war-vessels required on the other hand, leave considerable room for the employment both of expenditures and of contributions in kind.

The most highly developed modern system of defense does not require of its citizens the money with which to hire mercenaries; it requires the citizens themselves personally to bear arms; and this for the reason that such general military duty results in a more effective defense than any and all payments of money for hiring defenders of the Fatherland. But this also is no never discovery on the part of the modern state. On the contrary, the idea of a universal military duty has never been entirely extinguished, from the very beginnings of national life and through all subsequent changes; it has only been neglected and lost sight of, and with the awakening of the national spirit it has broken forth with renewed vigor and has set an example that all

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<sup>1</sup> I may here refer to the *Grundlegung*, vol. i. secs. 337 *et seq.*

other nations, even those which have resisted most stubbornly, have been constrained to follow. And the fact that this phenomenon has become such a prominent feature in the life of the modern commonwealth serves to bring out the significance, for the present and the future, of this element which does not partake of the nature of a money-transaction.

A second fact of the same character is the extensive factories, navy-yards, fortifications, barracks with their attached cooking establishments, bakeries, etc., by which the state (the Empire) provides, without the interposition of bargain and sale,<sup>1</sup> the weapons, munitions, vessels, provisions, which it may require. This is partly due to the fact - frequently underrated - that for purposes of production on a large scale the government may possess advantages equal or superior to those possessed by private industry.<sup>2</sup> To some extent it is due to the presence of certain facts of a technical character, such as the possession of exclusive knowledge of new discoveries and inventions in the art of war, which incite to the effort to keep the state independent of private industry.

Of course these transactions in kind, in modern financial management, go on side by side with money transactions; they occur only, as it were, scattered through the texture of a system of bargain and sale which predominates in the economy of the state in like manner as it does in the general economy of the people today; but they do, after all, have a definite significance, and are indications of the future course of development.

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<sup>1</sup> At least there is an evident tendency towards supplying the wants of the state with the least possible intervention between it and the prime producer. This is the effect reached by the system which prevails in the German administration of military affairs of making use of military stores instead of a system of purveyors. According to a statement made by the Prussian Minister of war in the German Reichstag, December 5, 1888, the wants of 91.78 per cent. of the forces were supplied from the stores, and only 8.22 per cent, through purveyors (this last consisting of small garrisons in places where no stores were at hand). Of the rations for the horses, 94 per cent. were supplied from the stores and only 6 per cent. through purveyors.

<sup>2</sup> Note, as a small but instructive example of the fact, the experiences of the communal bakeries of Leipsic as given in the report of Ludwig Wolff, member of the City Council (*Schriften des Vereins für Socialpolitik*) 1888, vol. xxxvii. pp. 19 *et seq.*



## I. THE PERSONAL SERVICE REQUIRED BY THE STATE (THE CIVIL SERVICE).

§ 176. The relation of the state to those persons who constitute the living forces of which the state's activity is a product, is necessarily conditioned by the stage of constitutional development attained; for this latter expresses the relation in which the citizen stands to the formation and execution of the national will.

In primitive political organizations where the sphere of the state is small and the public functions are of a correspondingly low degree of development, this relation has a simplicity such as will not serve the purpose of a great complex of functions. At the same time it is to be noted that always after a higher stage of culture has been reached, the influence of democratic ideas, resting as they do on the fundamental concept of a free people [*freier Volksstaat*], leads at least to the effort to maintain a semblance of this primitive simplicity in the relation between citizen and state. Indeed, this democratic idea is never altogether lost, so that under every conceivable constitution of the state, in every development of the bureaucracy, some trace of it is discoverable. In any civilized community there will always be two distinct elements in the activity of those operative forces that constitute the state a living whole.

The one is the element of division of labor between state and society; the other is the element of personal participation of the citizen in the affairs of the state.

The latter follows from the claim of every civilized people - especially at the stage of national development which we occupy today - to have some part in the shaping of its own destiny. The former results from the requirements of the principle of division of labor - valid for all stages of culture - both as conducive to a fuller development of the individual capacities of the citizens and to the efficient performance of the work of society.

The overlapping of these two elements gives us that peculiar mixture of the two which characterizes the civil service at the present stage of political development.

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§ 177. This mixture of the two elements assumes a different form under the different national constitutions of the present day.

Democracy, as it exists in the Swiss Federation, or in the United States of America, true to its name, seeks to realize the participation of the people in the legislation and administration of the state as effectually as may be. After all the concessions which democracy may make to the principle of division of labor, it still leaves the lines of demarkation of a democratic self-government so vaguely and loosely drawn that the distinction between State and Society is at best a shifting and uncertain one.

It is very significant, how, even under a constitution of this sort, the contrast between professional employment in the service of the state and the general participation of the people in state action, asserts itself.

In the first place, by the very letter of the constitution and the laws of the land, the actual participation by the people is reduced to the dimensions of a ballot and an election, which; however frequent and burdensome they may appear to the body of the people absorbed in their private business, are, after all, when measured by the standard of a vital popular participation in legislation and government, but a scanty substitute. But far more than appears from the letter of the law does it appear, in the actual political life which has grown up under these forms of law, that there exists an irresistible gravitative force, in consequence of which the decisions of this million-headed popular will are really made by comparatively very few men, who have adopted politics as a calling. Whether the ballot be made to apply to general or to special legislation, whether to the selection of subordinate or of superior officials, there always lies back of the semblance of a decision by the majority the reality of a decision by a small number of politicians. In this contradiction between appearances and reality lies the danger to this particular form of national life; inasmuch as what, under other forms of national organization, is honestly recognized as a necessity, and therefore need not be hidden from the light of day, will here become the occasion for a systematic falsification of the facts.

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But there is one point at which, as a genuine development of the modern age, this form of government takes its place side by side with that form of which it is the exact opposite, viz., the purely bureaucratic state. This is the absolute necessity of payment for all actual work done in the service of the state in a democratic community. Since the attractiveness and honor of this work are not a sufficient inducement, in a democratic society, to attract men of independent means; since it is rather of the nature of such a society that every household should depend on its own labor for its subsistence; therefore, work performed in the employ of the state must be paid in like manner as all other professional work.

The consequence is a comprehensive system of salaries and allowances; all the more comprehensive the more highly developed the democracy, and the more fully conscious it consequently is of its divergence from the principle of division of labor that underlies modern society. Only, the lax organization of this civil service does not admit of any length or security of tenure, which, under the political circumstances, is to a great extent not even desired. As short intervals between elections as possible - in the interest of liberty, - no life tenure, and consequently no pension system. Only in cases where the traditions of earlier times and a corresponding sentiment on the part of the populace, admit of it, is this folly of short terms of service to some extent neutralized by repeated re-election of the same officials. But this does not happen where party lines are closely drawn, and where the chance of rich spoils of office makes each recurring election a chase after fresh booty.

§ 178. Since it is impossible for all to bear a part in the everyday business of the state, it is quite conceivable that even under a democratic constitution - and numerous historical instances go to prove it - an inevitable tendency towards the domination of a few will concentrate authority in the hands of a few wealthy families. These will then come to hold the offices of the state by a sort of hereditary right, without sacrificing the accessories of a democratic form of government; rather, these latter will be

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retained as a convenient cloak for a popular administration of the government at their hands.

This would be a case where democracy, either openly or covertly, passes over into aristocracy.

In other countries, again, we find, as the outcome of the past development of society and of the national organization in the direction of aristocratic rule, that the aristocracy manages the affairs of the state with but a slight survival of democratic forms.

Under the rule of an aristocracy there is no place for the contradiction that exists in any democratic society between a nominal popular sovereignty and the actual sovereignty of a few on the one hand, and between the universal duty of participation in the service of the state and payment for such service on the other hand. In the place of All, we have, even as a legal fact, only a minority; in the place of a demand for payment of work done for the state, we have the hereditary wealth of the ruling families.

Only when this result has been reached, can the State's work be done simply out of inclination for the work, from motives of honor and patriotism, without regard to any economic return. This is the ideal of a free commonwealth; it is the ancient ideal of a life spent in the service of the state and for the state's sake; it is the grand and undying conception handed down from antiquity, of a freeman's work, whose spirit instinctively recoils from the thought of a pecuniary motive. These features, which elevate the concept of an aristocracy to an ideal height, serve to direct our attention to the wide divergence between this ideal and the reality.

The hackneyed example of such a national constitution is England. For centuries past there has been in England a ruling class backed by great wealth, more particularly by landed property. The better element of this class has habitually spent its life in the service of the nation, in the minor civil divisions performing the duties of local self-government, in the central government constituting the legislative and executive organs.

But even this favorite example manifests the shortcomings

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of an aristocracy under the conditions existing in a great modern state. For, in the first place, the ethico-political question has hitherto remained an unsettled one, as to how far the aristocracy of England has actually given its life to the service of the state, and not rather made the state a means of furthering its own class interest, so that its ostensibly gratuitous service may; in point of fact, have been dearly paid by the English nation. In the second place, this aristocratic official system has eventuated in a system of salaried offices, with the pay calculated on the scale of an aristocratic standard of living, whose character of permanency, together with the exacting work and the considerable expense involved, has made a high salary appear indispensable (embassies, diplomatic positions, high judicial positions, etc.). In the third place, it lies in the nature of an aristocracy that, while it will take up its abode in the higher altitudes of the official system, it will leave all the lower lying regions to the care of an unpropertied and consequently paid class of professional officials, except so far as the moderate duties of office in these lower stations and the immoderate salaries attached to them may make them available as a provision for younger sons and younger brothers.

But when it happens - as has happened in England during the last generation-that the stress of the modern democratic movement acts constantly more and more to displace such an aristocratic constitution, and to develop a feeling of distrust on part of the majority of the people towards the traditional aristocratic administration of the affairs of state - in such a case the system of salaried professional officials will irresistibly gain ground in parish and in county affairs, as well as in the numerous administrative bodies required by the increased demand of the new life of society. So that the end of the development is the payment of members of parliament - discontinued centuries ago, when the transition was made from a democratic to an aristocratic constitution of parliament.

Herewith the transition is made to the "functionary" state, which is the form that must be adopted if the modern state is to

meet the requirements of our democratic society in a satisfactory manner.

§ 179. The functionary state [*Beamtenstaat*] often slightly spoken of as a "bureaucracy") is the logical outcome of circumstances. The principle of the division of labor demands a specialized, professional civil service in order to an adequate performance of the increased duties due to increased social wants, just as advancing civilization gives rise to new employments and professions.

Germany, in its development since the close of the Middle Ages, presents the classic example of a functionary state. The peculiar character of such a state lies in a frank acceptance of the fact that the profession of the civil service, just as any other profession, must afford a livelihood to the people who follow it. The civil service takes its stand on the pay-roll of the country, and this latter, whether it goes by this name or by any other, must, economically considered, in the last analysis, fall under the concept of Wages.<sup>1</sup>

There are views held on this point somewhat at variance with that expressed above. In part these rest on a confusion of genus and species, in that they place the concept of allowances, pay, salary, in contrast with wages, while all these are properly to be classed under the general head of wages; in part they rest on the notion that the peculiar organization of the working force of functionaries is an element sufficiently characteristic to differentiate the maintenance afforded by the pay-roll, graded as it is by rank, from wages; while this matter of organization is, in point of fact, nothing but a question of detail, with respect to which the practice in the civil service differs from that of the competitive labor market.

The substratum of fact on which these views rest amounts to this, that there are certain special constituent elements in this class of work and wages that are still struggling for recogni-

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<sup>1</sup> Cf. *Zeitschrift für die gesammte Staatswissenschaft*, 1881, pp. 52 *et seq.* Also Ihering, *Zweck im Recht*, vol. i. pp. 186 *et seq.* (2<sup>nd</sup> ed., 1884). Adolph Wagner, *Finanzwissenschaft*, vol. i. p. 340.

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tion as such, due to the fact that an undertrained economic speculation has denied them their proper place.

There is one point with respect to which economic science, in spite of much vacillation and many misconceptions, has in the main been fairly consistent from the early days of scientific writing down to the present. This is the principle that the rate of wages rests on the necessary, traditional standard of living proper to the persons concerned. From Turgot, Smith, Ricardo, John Stuart Mill, Cairnes, down to the latest authorities in the science the principle has been uniformly accepted that the "natural" price of labor depends on the cost of living of the laborer. The advance in this matter - and this is true in general of the position of the science today as compared with a century ago - consists simply in a recognition of the fact that this natural price is measured by a moral standard.

The pay which the state allows its functionaries is nothing else than this. It vouchsafes a livelihood commensurate with the requirements of rank, in accord with the postulates of the scientific doctrine of wages. So also the provision for old age, for infirmity, for widows and orphans, is nothing but a legitimate extension of the principle of a graded standard of living so as to apply to the household, such as has long been recognized by the commonly accepted theory of wages.

The facts of everyday life likewise go to show that preparation for, and application for admission into, the civil service is chosen or avoided in very much the same fashion as other ways of earning a livelihood. The question is whether the civil service offers greater economic advantages than these other similar occupations. As is sufficiently established by repeated instances in German countries, every increase in the pay offered by the state attracts a greater number of candidates, while conversely, whenever the offer of the state falls short of the inducements offered by business, this number decreases.

§ 180. The nature of wages is by no means such as to exclude the possibility of the presence, in the work for which

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they are paid, of psychological factors that are not strictly of an economic character. The fact that the extra-economic factors do not predominate - and for the reason that an economic (pecuniary) basis is indispensable to the work so long as it has no economic support from an independent, extraneous source - is for the present purpose altogether decisive as to the character of the state pay. The graduated livelihood which the state guarantees expresses an unreserved acceptance on the part of the state, of the economic necessity formulated by the theory of wages. If it were true, as has been asserted, that the emoluments of office are of a "mixed" nature - being made up partly of honor and partly of money - then it would have to hold true that a deduction should be made from the money payment because of the honor. But that position is manifestly untenable. It may happen that the state declines to meet its full obligation in this respect; and this, again, is possible only in case the aggregate income of the functionary is made up of two distinct economic elements - in case the salary is helped out by independent means. But this latter is an aristocratic element which the bureaucratic state is by its nature estopped from counting on.

Are we to say that the honor of the office of an English Lord Chief Justice is so much less than that of a judge in a Prussian provincial court, as would be indicated by the fact that the former receives an annual salary ten or twenty times as great as that received by the latter? Or is the honor of the position of Archbishop of Canterbury so slight that it is necessary to make good to the incumbent, in his notoriously large revenue, what is lacking in the way of honor in his position, as compared with the Prussian Superintendent General?<sup>1</sup>

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<sup>1</sup> The Lord Chancellor of England receives annually £10,000; the Lord Chief Justice receives £8,000; each of the superior judges of the Court of Appeals £6,000; all other superior judges £5,000. The Archbishop of Canterbury receives £15,000; the Archbishop of York £10,000; the Bishop of London £10,000. (*Whittaker's Almanack*, 1889.) On the other hand, the Superior Judge of a Prussian provincial court [*Oberlandesgerichtsrath (Kammergerichtsrath)*] receives 4800-6600 marks (£235-£324), with an allowance of 400-900 marks (£20-£44) for house rent. The President



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This can of course not be taken seriously. The truth is rather that the entire notion of such a "mixed compensation" is due to the impression produced by the scantiness of our German salaries, and this latter is in its turn a result of the very general poverty of the German social economy and of the German finances: In placing the salaries of its functionaries as low as we find them, the German state has been guided partly by the traditional standards of living in vogue in our society, and partly by a parsimony imposed by the scantiness of its resources. The view that a payment in terms of "honor" may possibly replace the maintenance due its functionaries is entirely unworthy of the state.

There is but one alternative possible: either the state, in violation of its obligation toward its professional official class, requires them to get along on half pay, or it counts on a supplementary income from their private means - a presumption which will hold only in exceptional cases.

§ 181. But even if what has been said above sufficiently indicates what is the character of the salaries of officials under normal circumstances, at the same time that it clears up the confusion involved in contrasting salaries with wages, it is to be noted that the same factors are decisive in fixing the salaries of civil servants as in fixing the wages of other occupations; especially is this true when they are compared with wages in the liberal professions.

There is one vocation which, in Germany, is always crowded, and which, apart from a few notable exceptions, offers a miserably scanty pay for very exacting work. This is the vocation of the trained musician. The necessary prerequisite for this work is a special endowment; and, conversely, this special endowment constitutes a powerful incentive to adopt this vocation. This

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of such a Supreme Court of Judicature receives 14,000 marks (£686); a judge of the supreme court of the Empire 12,000 marks (£588); the highest judiciary in the German Empire, the President of the Supreme Court, 25,000 marks (£1225), besides lodgings. A Superintendent General receives 9,000 marks; the President of the Superior Evangelical Ecclesiastical Council 21,000 marks (£1,030).

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subjective incentive of talent urges to the choice of this vocation in spite of the inadequate pecuniary results to be obtained: This incentive is also greatly reinforced by habit and by the example of parents from whom the talent and the profession have been inherited.

Something similar is to be observed with respect to the official class, and especially in the German service. The part played in the musician's profession by artistic endowment is in the case of the civil service filled by a lively sense of loyalty to the state, which has become a heritage in official circles. Tradition handed down from generation to generation constitutes a nexus between the man and the state that persists under circumstances where, for the majority of men, such attachment has been lost. In like manner as the artistic leaning urges to the acceptance of a meagre livelihood, so in this case the ingrained sentiment of attachment to the state renders the individual to a certain extent unable to decline the offer of a scanty living. Indeed the traditional union of these two things, of poverty and attachment to the state, has in a great number of instances brought forth fruits which were quite marvelous in their way. Still, all this is not as it should be. It is unworthy of the state to take advantage of this offer of services which, under given circumstances, may be coupled with an exceedingly low standard of living.

It is, however, by no means to be asserted that the excessive number of candidates for the civil service today are uniformly to be fairly compared, in point of disinterestedness, with the musicians spoken of above. The fact is, rather, that in very many cases the predominant motive in the choice of their calling is a pecuniary one, often without any admixture whatever of nobler motives.

§ 182. If these considerations bring us to the conclusion that the personal service required in a bureaucratic state, even that required for the higher and the highest functions of the state,

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should be paid for according to the general principle of wages, there still remains a further point for consideration.

We may properly speak of difference in the psychological character of different kinds of labor. The higher grades of labor, the "liberal" professions, are more reserved about the matter of accepting pay than other forms of labor. Since this is a phenomenon of a psychological nature, it is influenced by the course of historical development. It may be maintained that in the sentiments with which we today regard the service rendered to the state (and services of a similar character) there is a sense of something not adequately covered by a pecuniary reward, which in a certain sense discountenances such payment and crowds it into the background, as being an unwelcome necessity which is not willingly recognized in words. This thought of pecuniary reward is repugnant to a delicate moral sense, which hereby pronounces in favor of a civil service freed from the constraint of existing social conditions.

There is at least one thing forcibly suggested by the presence of this social constraint, namely, that the payment for services rendered to the state should be made in such a form as would to the least possible extent offend this delicate sense of propriety. In like manner as at an earlier stage the state will usually bind up its duties with the private interests of its agents, before it has reached the point where it acquires an official class possessed of a due sense of devotion to the public service - so also when a salaried civil service is employed. Here this earlier stage of development is represented by the fee system, which makes the concession to human infirmity of attaching to each particular act of the state official a particular recompense, and by this means keeps him to the performance of his work when it would otherwise be neglected.

This piece-wages system, which is very confidently recommended for adoption in the lower grades of work, is opposed to the very nature of the higher grades. If these latter cannot be made gratuitous ("liberal" in the ancient sense of the word) they must at least not be made to submit to the stigma that they

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are performed piece by piece for money. The man must devote his entire energies to the service of the state as such, and the state's provision for his maintenance is to be carefully disconnected from the performance of the state's work. The developed constitutional form of the state, as contrasted with the method of personal government, meets this requirement. The annual salary paid from the public treasury enables the state official to live his life for his official duties alone, and free from all pecuniary concern:

Wherever we find remnants of the fee-system still existing today, they are survivals of the old order, of the old state, which has yet to make way before the progress of modern ideas. They are antiquated abuses which the self-seeking functionaries clothe in a garment of reverence, while they ought to perceive that in so doing they are degrading their own dignity far below the general level of the modern state and its functions.

§ 183. With the adoption of the system of fixed salaries for the professional civil service, graduated according to the standard of living appropriate to the rank of each (and similar provisions for the salaries of communal, provincial and other like officials), a distinction which is characteristic of the aristocratic method of filling offices disappears, viz., the distinction between the superior, the honorary offices proper (*honores, magistratus*); and those commonplace services performed for the state and the commune that are paid in the same manner as the meaner occupations of everyday life.

The distinctions with which we are here concerned are those which depend on differences of grade in the services rendered by the functionaries, together with the consequent differences in the qualifications required of the candidates, and the different ways and means by which the state makes provision for a graduated livelihood in keeping with the standard of living proper to the rank of each.<sup>1</sup>

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<sup>1</sup> Here, as in so many other places, the narrow limits within which our discussion is confined makes it necessary to refer, for particulars of legislation and statistics, to the exhaustive and painstaking work of Adolph Wagner. See especially *loc. cit.* secs. 152-167.

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The various distinctive classes of work required by public service depend, just as do the different kinds of work offered in the labor market and the higher grades of work in industrial life, on a difference in intellectual endowment and training. Just as in the ordinary demand for labor there is a gradation of services from the simplest mechanical occupations up to the highest classes of intellectual labor, so also in the service of the state and of the commune. Just as in the general industrial organization this gradation of services runs parallel with a gradation of society according to wealth, breeding, education, - so also here. In both spheres alike do we therefore also find the same connection between the rank of the social class in question, and the length of the period of education and the beginning of profitable labor. The lower the culture, the lower the social class, the earlier do the necessities of life put in their claim and so shorten the period available for the education requisite to independence, and extend the years of gainful labor backwards into childhood. The higher the culture, the more elastic is the pressure exerted by the necessities of life as against the requirements of the education and preparation necessary for the person's life-work, and the more time is consequently allowed for meeting these requirements.

But inasmuch as the ideal of development in this direction would lead us to the aristocratic ideal which discountenances any pecuniary object in the professional service rendered the state, it follows that the ideal of the bureaucratic state lies within narrow limits-limits marked off by the exigencies of the economic situation, frequently opposed to the quasi-aristocratic ideals which influence the body of state officials and even the national administration itself.<sup>1</sup>

§ 184. Under the influence of such ideas as these it has come about that provision for a properly graduated scale of maintenance for the official class, in spite of the many improvements

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<sup>1</sup> A discussion of this question from the economic point of view is to be found in Ernst Engel's paper on *Der Preis der Arbeit* (1866).

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that have been made, remains so very inadequate, even in such a classic example of a bureaucratic state as has been developed in Germany.

The difficulties of the matter are, of course, considerable; very much in proportion to the grade of work and the preparation required.

In the first place, there is the difficulty of maintaining an equilibrium between the personal services actually required, both as to quantity and quality, and the supply, in view of the already excessive inclination to enter the civil service, which would be increased by every improvement made in the scale of maintenance of the official class. In point of fact, the number of candidates for the civil service has been excessive, with the result that the service has been underpaid and the period of preparation and waiting has been unduly lengthened, while the requirements in the way of qualification for the work have declined in a corresponding degree.

In the second place, skilled and specialized work in the civil service is of such a nature as to prevent its being begun very early in life or continued down to a very late period. A letter-carrier in the service of the German Imperial Post-office might very well enter the service as soon as he had passed the primary school and had devoted a few additional years to the development of his physical and intellectual energies. He might, without detriment to the service, continue in the same occupation, supposing his health to be normal, until old age. It is otherwise with respect to the higher functions of the government - in the administration of justice and other like offices. The difficult character of the work to be performed requires a preparation in school, university and practical experience, together with the passing of the necessary state examinations, such as to extend the period of education (taken in the broadest sense) down to the twenty-eighth or thirtieth year. And then it is also true that the period during which these hard-won intellectual and moral powers can be employed to the best advantage is a limited one and does not reach anywhere near the termination of life, although

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it is true that in actual practice they frequently continue to be employed until a very advanced period.

There is but one of the higher professions in Germany in which this last requirement is, on the whole, lived up to with considerable strictness. This is the officers of the army. The excellence of the body of officers as a whole is due to the fact that a sifting process is constantly going on, that a great portion of the officers are weeded out at a comparatively early age, in the prime of manhood, and that only in cases of very high position, with men of unusually good connections, is that indulgence exercised which is the rule in the higher grades of the civil service proper.

The severity of the strict requirements in the case of the army officers, only to a slight extent affected by an early partial provision for the young lieutenant, calls attention to the shortcomings of the state in the matter of adequate provision for its officials; just as connivance at the continuance in office of superannuated and infirm functionaries does in the civil service. The fact that an officer is past usefulness for his profession before he has reached his fiftieth year, and that this is not the exception but the rule for the majority of the members of the profession, imposes on the state the duty of a generous provision for such cases, in place of the inadequate pension system hitherto employed; just as the retention of office by an infirm judge after his continuance in the service has become detrimental to the interests of the state should be prevented by such a pension system as will afford an economic justification for a seasonable removal from office.

If it is further borne in mind, as Engel, particularly, has impressively shown, that a great part of this functionary class and of the army officers is recruited from the same social class generation after generation, the difficulties in the way will become sufficiently evident, and the problems which the state has yet to solve in the matter of an adequate maintenance of its servants will be seen to be stupendous.

### III. THE FINANCIAL CHARACTER OF THE SEVERAL BRANCHES OF THE ADMINISTRATION.

§ 185. A discussion of the fiscal demands of the several branches of national and communal administration leads unavoidably into the technicalities and details of each of these different administrative functions, and so out of the sphere of financial science proper and into that of what has latterly (following the example of Lorenz von Stein) been called Administrative Science [*Verwaltungslehre*]. If, consequently, such a discussion does not properly belong in the science of finance we may surely omit it here, since the present purpose is to present in brief space and as concisely as may be, the leading features of the Science of Finance proper.

Still less do I feel myself tempted in this connection to go into the customary statistical comparisons of one time and country with another. Such comparisons seem to me to be much better adapted to serve as material for a yet unwritten manual on the subtleties of statistics; so persistent is the practice of comparing things essentially incommensurable, so constantly does this method lend support to those deplorable misconceptions that claim statistics as an infallible witness one day and treat it with ridicule the next.

What is in place at this point is a consideration of the different financial character of the various branches of state and communal administration.

On taking a survey of the aggregate of the divisions and ramifications of the administration of a modern state, we find that the various "ministries" which have the oversight of different public functions for the most part look to the ministry of finance for the requisite fiscal means; this latter standing to the other ministries in a relation similar to that of a head of a household towards his family. This relation of dependence on the ministry of finance, however, does not hold to the same extent for the various departments. Indeed, certain ones of them are in the fortunate position of carrying on an important administra-



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tive work for the community without having to require any of the means for their purpose from the ministry of finance. The operation of their own branch of the administrative machinery produces the fiscal means which they need, and even much more than they need. Other branches of the administration are at least able to cover part of their expenditure by means of the receipts for the services they render. Still others, however, do nothing, or as good as nothing, towards meeting their own expenses.

It goes without saying that in this matter of a greater or less degree of financial self-sufficiency, the decisive consideration in a modern civilized state is the question of expediency and equity, as within the sphere of the particular administrative department in question. The norm is not now, as in the nature of the case it was with the undeveloped state, a crude fiscality, which, on account of the difficulty of finding a productive system of taxation, exploited every state function indiscriminately as a source of fees.

§ 186. If we take for the basis of our discussion the modern Prussian-German administration, we find that the management of Prussian state-railways is far and away the foremost of those branches of the administration which satisfactorily perform the public service required of them and at the same time fully meet their own expenses out of the receipts from their own business.

The roads have by no means been built by the state, or taken out of the hands of the stock companies and placed in the possession and management of the state for fiscal purposes. They have come to constitute a department of the national administration as a logical consequence of the universal customary right of roadway; in virtue of which, in order to best subserve the purposes of the public business, the control of the public highways has been withdrawn from private hands and placed in the hands of the public, for the reason that it has been found by experience that the frequent and varied points of conflict between the common interest in the means of communication, and the interests of

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private speculative enterprises, can be properly controlled only by public management. But the state is more especially urged to this position by the following considerations. In the course of time, the state will again and again find itself obliged to take the part of such portions of the country and such lines of communication as do not promise a sufficient profit to attract private enterprise. The result is a contrast between a dividend-paying private railway system, and a deficit-bringing state railway system within the same country. This contrast can be done away only by means of a unified state system which shall include both.

In the second place, in an age which makes every improvement in the mechanic arts serve its military purpose, the railway is indispensable to the state on strategic grounds. The state is induced to assume direct administration of the railway system not only in order to have unhampered control of the lines in case of mobilization and war, but also in order to the construction of the shortest lines and the lines most desirable for military purposes. The situation demands an expenditure in the interest of the commonwealth as a whole - a purpose for which private enterprises are not undertaken.

In the third place, the traffic of every section of the road requires careful attention on the part of the railroad officials, whether the business of each particular section is great or small, whether it is more or less lucrative in the aggregate. The details of transportation are so varied, and the interests involved are so great and many, that the business cannot safely be made dependent on the degree of lucrativeness. Such a careful supervision requires sacrifices; and this fact is the reason why the interested parties demand a state railway system. This fact, that part of the business of the railroads has to be done at a sacrifice, involves the danger of class discrimination at the expense of the community, but this danger will have to be guarded against by proper precautions.

But if the administration of a state railway cheerfully assumes all these losses, and still is able to make the excess of its income

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not only cover its outlay, but even run up a surplus in addition, which may be applied to the expenses of other branches of the national administration; if it can do all this without laying itself open to merited censure for discrimination; then it may truly be said to have reached the limit of the attainable in the way of financial independence on the part of an administrative department.<sup>1</sup>

§ 187. The case of the post-office is much the same as that of the railways.

<sup>1</sup>The Report of the Prussian Minister of Public works to the King (1888) contains the following statement: "Although the industrial situation of the country and the development of the traffic during the last ten years cannot be said to have been extraordinary, still, the surplus receipts of the state railways during this period have not only sufficed for the payment of interest and the discharge of the entire debt representing railway capital, as fixed by the provisions of the law of March 27, 1882; but have also afforded a further surplus aggregating in round numbers 330 million marks, which has been applied partly to meet the other expenditures of the national budget, partly to the further discharge of the national debt, or to balance unsettled accounts. To this is to be added another 56 million marks which, in accordance with the provisions of the above-mentioned law, is to be considered as the surplus of the years 1880-81 and 1881-82. If to this sum is added the funds which the acquisition of the private lines has released from their former destination and placed at the disposal of the state, aggregating 182 million marks, as also the 98 million marks which the national railway administration has applied, out of the receipts of the current fiscal year, to the systematic payment of the preferred bonds of the railways acquired by the state, we have an aggregate of 666 million marks. Against this is to be set down expenses of some 687 million marks provided for by special loan bills since the year 1879, for the building of new lines and the extension and completion of the plant. It need not be pointed out that what still remains of this amount is much more than covered by the expenditures for payment of interest and discharge of debt. It may therefore be maintained that the extensive building operations of the state during the last ten years might approximately have been met out of the reverted funds and the railway surplus left over after payment of the permanent expenses and the interest on the debt representing the capital of the railways, without resort to a national loan, if only this surplus had been left at the disposal of the railway administration, and not diverted to the general expense, of the state. If the surplus receipts of the (Prussian) Railway Administration during the last ten years are compared with the sums applied by the National Debt Bureau [*Staatsschuldenverwaltung*], during the same period towards the payment of the interest on, and the discharge of, the entire (Prussian) national debt, it appears that the former have, since the year 1880-81, not only regularly sufficed to cover the latter, but even to leave an excess so great that during the last few years it would have sufficed for the payment of interest on the aggregate of the debts of the Empire-if that had been Prussia's concern."

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It originated, mainly, in the government's own need of letter carriage, just as at a later date the state telegraph has often been established, at first exclusively for the government service. In the one case as in the other it is only gradually that the private business transacted has come to be of greater importance than that transacted for the state. If a means of communication is to serve the needs of the state alone, the resulting expenses will also have to be defrayed by the finances of the state. The possibility of covering the expenses of the government's use of the means of communication, by increasing the volume of business done by the state-owned establishment, arises only with the development of a private business that will yield an income. This result has latterly been so fully attained that the payment of these expenses out of the net receipts of the post-office is taken as a matter of course. But the financial results attained are much greater than this fact alone would indicate. As density of population and the facilities for communication increase, as the occasions for exchange of letters for business, social and domestic purposes, multiply, the volume of the business of letter carriage becomes so great as to reduce the cost of carriage to a minimum. It results from the very nature of the means of communication - and this is especially true of the letter post - that a maximum volume of business results in a minimum cost; this result being attained by the full utilization of a consolidated plant.

A very great effort to meet the wishes of the letter-writing public, in the way of cheap and expeditious service, such as has been made on all hands during the last few decades, and such as has been the practice in England for half a century past, has always resulted very satisfactorily for the finances, and has even yielded a very large net revenue (as is especially the case in England).

The financial surplus of the Post-office<sup>1</sup> includes not only the

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<sup>1</sup> According to the official estimates of the German Empire for the fiscal year 1888-89, the surplus revenue of the Imperial Post-office and the Imperial Telegraph (exclusive of Bavaria and Wurtemberg) amounted to 28 1/6 million marks. In order to

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gratuitous transmission of official correspondence. It would be much greater if it were not that provision has to be made for the transmission of private matter other than letters - business which is less profitable than the carriage of letters, and even, by its nature, or rather in consequence of the demands of the public, has to be transacted at a loss. Not to mention things of less importance, we may safely count the transmission of parcels through the German Imperial Post-office as matters stood at that time, as being a branch of the postal business carried on at a loss, certainly this will hold true if, as is proper, the unpaid services of the railroads be counted in in the costs. The question as to this branch of the postal service relates mainly to the parcels rates, which are by no means unchangeable, and which are, in fact, quite different abroad from what they are in Germany. Indeed, until lately, the government has been quite willing to surrender this part of the business to private enterprise, as involving a loss to the state. But the carriage of passengers by the German (Swiss) post is, in consequence of the modern development of the road system and traffic, almost inevitably a losing business. It is, in certain countries, a function traditionally devolving on the state and undertaken in the interest of the public; whereas most of the great civilized nations (England, France, United States of America) are strangers to the system, and leave the business to private enterprise, to the disadvantage of travelers and the benefit of the postal revenues.

We shall come later on to the discussion of the nature and

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a closer analysis of the net revenue it would be necessary to take account of the expenses of transmission incurred by the railway's without payment on part of the Imperial Post-office - a computation which, for the present, is wanting. The English Post-office, on the other hand, yielded (for the fiscal year 1887-88) a net revenue of 3.76 million pounds sterling, after paying liberally for transmission by the railways, without any legal rights beyond those possessed by private parties. It is to be added that the population of Great Britain and Ireland amounts to 37 millions, while the territory served by the German Imperial Post-office contains 40 millions (middle of 1887).

Quite different from the case of England is that of the United States of America, the receipts of whose Post-office Department, for the fiscal year ending June 30, 1888, amounted to 52.20 million dollars, while its expenditure amounted to 55.9 millions, leaving 3.70 million dollars to be defrayed out of the receipts from taxes.

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extent of the surplus revenues (and deficits) of the postal service, as well as of the like facts with respect to the revenues of the railway business. For the present it is sufficient to note that here, again, we have to do with a branch of the administration which, while performing a function of great importance to the state and to private parties alike, is still able to take a position of independence of the ministry of finance.

The telegraph business is, on a small scale, in much the same position as the postal service. It is another instance of a public function which is undertaken by the state in order to satisfy its own need of telegraphic communication, as well as to meet the demands of the public, and is carried on without requiring any financial support from the national treasury.

§ 188. Quite different is the case, as regards its financial position, of a branch of the means of communication, which is old in point of development, but new in point of financial management, viz., the public highways.

The abolition of the turnpike tolls<sup>1</sup> that were formerly (and still are in many cases of survival) collected, has left the public roads and their maintenance entirely dependent on financial means which they cannot themselves directly procure. This is the necessary reverse of a view which advocates making all the means of communication gratuitous. This is not the place for discussion of this point; we can here only call attention to the fact.

This is also not the place for a discussion, though it is the place for an articulate enumeration, of those other branches of administration which, at the stage of culture we occupy, seldom produce an income, and therefore regularly draw on the general finances.

Most important of these are the expenditures for military purposes. For reasons already indicated, military expenditures can, in the nature of the case, never be placed on a financially independent, self-supporting basis. The great and costly public

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<sup>1</sup>With respect to Saxe-Weimar, see *Finanzarchiv*, 1888, pp. 1059 *et seq.*

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services for which these expenditures are incurred cannot be paid for by the piece. They constitute an indivisible and intangible whole whose cost can be defrayed only by contributions from the whole body of citizens as such, - that is to say, by taxation.<sup>1</sup> Such is the case, at any rate, in every civilized community. It is otherwise in the crude beginnings of national growth, when war is a plundering foray, when it is held disgraceful to acquire by the sweat of one's brow what may be got by violence. With civilized peoples it is only in exceptional cases that war can be made to cover its own cost, by means of a war indemnity extorted from a conquered enemy - as, e.g., the payment of the five milliards by France to Germany after the year of 1870-71. Moreover, in the first place, this favorable outcome depends on a conjunction of circumstances: the indemnity is of course a one-sided affair, and throws a double burden on the defeated nation;

<sup>1</sup> According to the Finance Report for the year 1876 the expenditure on account of the German Imperial army and navy amounted to:

The Imperial Army	316.2	million	marks
The Navy	21.0	"	"
General Pension Fund	23.4	"	"
Imperial Invalid Fund	28.8	"	"
Extraordinary Expenses for the Army (Fortifications, Barracks, etc.)	35.9	"	"
Extraordinary Expenses for the Navy	4.8	"	"
	<u>430.1</u>	"	"

According to the Finance Report for the year 1888-89:

For the Imperial Army:			
Ordinary Expenses	362.8	million	marks
Extraordinary Expenses	372.5	"	"
For the Navy:			
Ordinary Expenses	35.9	"	"
Extraordinary Expenses	12.8	"	"
Imperial Invalid Fund	26.4	"	"
General Pension Fund (exclusive of Civil Pensions)	<u>28.0</u>	"	"
Total	838.4	"	"

The interest charge on the Imperial debt (incurred for war purposes) amounted in 1876 to 0.3 million marks, in 1888-89 to 30 million marks. In addition to this there is the interest charge (unchanged) on the Imperial war fund of 120 million marks, amounting to four million marks annually.

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it can also be exacted only in case of a very decisive conclusion of the struggle, as in a different case each of the parties to the fight would let the matter rest with the expenses already incurred; also the conquered enemy must be wealthy enough to be able to pay such an indemnity. In the second place, the war indemnity cannot be looked on as a means of covering the expenses annually incurred for military purposes, for the reason that these expenditures are, at the best, incurred as a means of postponing or preventing war; so that the ideal to be hoped for, according to this view, is to make it as nearly impossible as may be to exact any war indemnity.

We are aware how great are the efforts made in our own commonwealth in this direction, and we must be prepared to expect that the heaviest demands on the national finances will continue to be for this purpose.

§ 189. As is the case with the preparations for defense, so also with the administration of justice; it serves its purpose most effectively when it succeeds in obviating litigation. It is for the resulting unapportionable atmosphere of peace and security that the citizens have mainly cause to show themselves grateful.

At the same time the mechanism of the administration of justice is of such a nature as to make it not only possible but also just and expedient to collect individual payment from individuals who are served by it. In the administration of the law there are continually arising special expenses to the government, at the same time that special benefits often accrue to the individual concerned in the particular case in question, and these are properly to be paid for in fees. This happens in actions under the civil law, both in cases of litigation and in case of decisions rendered at the instance of interested parties [*Freiwillige Gerichtsbarkeit*], as also in criminal actions. The abolition of such special payments has been demanded for more than a hundred years past by the reaction against the "fiscality" of the earlier administration of justice; but such a change would be fraught with great danger, especially as regards civil actions. The



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courts would be crowded with a multitude of petty disputes; as indeed they already are, to some extent, in spite of the quite considerable costs involved.

The expenses of the Prussian administration of justice for the fiscal year 1888-89 amounted to 86 million marks, besides 2.25 millions non-recurring [*einmaligen*] expenses; while the receipts were 48.50 million marks, 47 millions of which was derived from court fees.

In the related branch, the police administration, it is more difficult to procure any appreciable part of the necessary funds from the receipts coming in to the department. The administration of the Prussian Ministry of the Interior (Ministerium des Innern) for the year 1888-89 involved an expenditure of 43.50 million marks - 23.50 millions for police and *gensdarmrie*, 9.50 millions for penal institutions (besides 1.75 millions for jails, defrayed by the department of justice), nine millions for the general expenses of the department. The receipts amounted to not quite four millions, for the most part derived from the labor of penal institutions, together with 1.25 millions derived from the labor of persons under the management of the department of justice.

§ 190. Coming now to the subject of public education, it appears that here, for several reasons, the figures of the finance report fall far short of being a satisfactory indication of the state of the case. For one thing, the greatest single item of expenditure for public instruction, that for the elementary schools [*Volksschulen*], is borne by the communes, the state bearing a hand in it only to the extent of (quite considerable) supplementary contributions to the communal expenses. Further, the remaining branches of the school system, the upper grades and especially the higher institutions [*Hochschulen*] are to some extent provided for by endowments, so that here, too, the demand on the national administration frequently goes only to the extent of a supplementary contribution of funds.

It is further to be noted in this connection that, under the

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influence of a progressive social-political bent of public opinion, the whole question of pecuniary provision for education is in a state of flux. The method of defraying the cost of schools by means of individual payment from those attending the schools (a method by no means impracticable, by itself. considered, simply on technical grounds) is more and more giving way before the latest views (as expressed in state constitutions and school laws), so that the public schools are becoming a constantly increasing fiscal burden on state and commune. This result is to a considerable extent due to enhanced demands in the way of the number of schools, the character of the school-houses, the wages of teachers, etc. During the fifteen years 1871-86 the cost of maintenance of the public schools of Prussia has risen from 55.6 million marks to 116.6 millions.<sup>1</sup> The supplementary funds contributed by the state for the same years increased from hardly three million marks to fourteen millions;

<sup>1</sup>The following exhibit is taken from the report of an official investigation by the Prussian ministry of Education made in 1886:

The expenditure for maintenance of schools amounted,		1871	1878	1886
On an average for the whole country, to	Mk.	55,648,398	Mk. 101,016,623	Mk. 116,615,648
For the country districts alone		32,002,388	57,117,873	66,134,918
Or per 1000 inhabitants:				
On an average for the whole country		2,262	3,924	4,118
For the country districts alone		1,925	3,370	3,724
For each scholar per capita:				
Average for the whole country		14.27	23.65	24.10
For the country districts		11.40	19.09	19.83
These funds were obtained:				
(a) In town and country taken together:				
From tuitions		10,498,794	12,975,527	10,926,085
From contributions by taxpayers		42,254,418	75,629,731	91,667,677
From state funds		2,895,186	12,411,365	14,021,886
(b) In the country alone:				
From tuitions		5,090,040	5,718,761	6,135,591
From contributions by tax payers		24,754,142	41,263,584	48,400,229
From state funds		2,158,206	10,135,528	11,599,099

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whereas the receipts from tuition are but slightly greater in 1886 than in 1871 (10.9 millions in 1886 as against 10.5 millions in 1871). Even this payment is, according to the proposals of the central government, to be gradually done away.

As concerns the higher branches of public instruction, if the various items of expenditure under that head, given in the Prussian fiscal estimates for the year 1888-89, are summed up, the total will amount to some 18 or 20 million marks. In this case as in

Or per 100 marks:	1871	1878	1886
(a) In town and country taken together:			
From tuitions	18.87	12.84	9.37
From contributions by taxpayers	75.93	74.87	78.61
From state funds	5.20	12.29	12.02
(b) In the country alone:			
From tuitions	15.91	10.01	9.28
From contributions by tax payers	77.35	72.24	73.18
From state funds	6.74	17.75	17.54

Of the total expenditure (116,615,648 marks) for the year 1886, 75,245,144 marks was for personal services, and 41,370,504 marks for material equipment; in the country districts alone 44,015,968 marks were expended for personal services, and 22,118,950 marks for materials for the public schools. To this is to be added an outlay by the central government, for inspectors and the like, amounting to ten or eleven million marks.

The city of Berlin alone, in the estimates for the fiscal year 1889-90, makes provision for an expenditure of (in round numbers) eight million marks for its parish schools (receipts being 83,146 marks). The number of children of school age is assumed to be 172,000 (in 183 parish schools, comprising 3,082 classes, with a like number of teachers, male and female). The net expense for each pupil is accordingly 46.50 marks, which is defrayed by means of communal taxes.

<sup>1</sup> According to the estimates for 1888-89 the expenditures for public instruction are as follows:

	Million marks.
Universities,	7.25
Higher institutions,	5.17
Science and Art,	3.25
Technical Education,	2.

The expenses for elementary education are this time entered at 36.25 million marks, instead of 25.33 millions for the previous year. Then there is for Ecclesiastical Affairs and Public Education 7.67 millions; for general departmental expenses one million; for provincial school boards one-half million. Besides the funds contributed by the state, the universities also derive from endowments 1.50 million marks annually. The different universities are very differently placed in this respect. Gottingen derives about two-thirds of its aggregate expenses (1,038,275 marks) from its own property;

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that of the army and navy no adequate idea of the expenses is got by taking into account only the ordinary expenditures and leaving the non-recurring [*einmalige*] expenditures out of consideration. Just as in the case of the military expenditures this latter class of expenses are far from being really "non-recurring." They constantly recur; only their periodicity is not as easily made to conform to the limitations of the fiscal year as that of the so-called ordinary expenses.

More particularly, the universities and the technological schools, with their ceaseless demands in the way of new scientific and medical equipment, very closely resemble the progressive demands for military equipment, in that in the one case as in the other the advance of science and of the arts based on natural science constantly demand new appliances to replace the old before they have been worn out. There are of course also other causes at work to bring about a like result, due to a general development in the requirements of life, in the way of taste, sanitation, etc.

As regards the question of the financial standing of the various branches of public instruction, it is to be said that the high-schools resemble the elementary schools [*Volksschulen*] to the extent that only a moderate part of their expense is covered by receipts from fees. The aggregate expenditure of the Prussian universities for 1888-89 amount to 9.50 million marks, of which sum only 1.20 million is obtained from the receipts of the business.

It is otherwise with the secondary schools<sup>1</sup> [*höhere Lehren-*

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the contribution of the state amounts to only 370,892 marks. Greifswald (aggregate expense 636,850 marks) receives but 216,385 marks from the state. Quite otherwise is the case with the University of Berlin, which, with a yearly expense of 2.25 millions, receives two millions from the state.

<sup>1</sup> Taken altogether, the "higher institutions of learning" (national, municipal, and endowed) drew their revenues in 1888-89, from the following sources:

1. From state funds	4.8 million marks
2. " their own property	1.9 " "
3. " endowments	1.3 " "
4. " municipal funds	6.8 " "
5. " receipts of the business	<u>13.2</u> " "
Total	28.0 " "

*stalten*], that is to say, gymnasia, *Realschulen*, etc., which, with an aggregate expenditure of 28 million marks, defray nearly one-half their expenses out of their own receipts.

§ 191. The above account does not exhaust the subject of the public finances; still less can it be said that we have adequately disposed of the great multitude of communal<sup>1</sup> expenses.<sup>2</sup>

That, however, has not been our object. It has rather been to point out what is the varying significance, as to kind and volume, of the chief varieties of public expenditure. In order to this, the main types of public administration have been brought under review, and in the case of a majority of them it has been found that some provision has to be made for meeting their expenses from resources that are not to be had within their own domain.

The discussion next following will be occupied with the nature of these fiscal resources.

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See Anlagen, vol. iii. No. 21. Supplement [*Beilage*] 8 of the *Minist. der geistl. u.s.w. Angelegenheiten* to the Estimates for 1888-89.

<sup>1</sup> As one of the chief items of communal expenditure may be mentioned the Poor Relief. As shown by an official inquiry for 1885 (*Statistik des deutschen Reiches, Neue Folge*, vol. 29), 1,592,386 persons received assistance from the public funds in the German Empire, - that is to say, 3.40 per cent of the total population; at an aggregate expense of 92.5 million marks, - that is, approximately two marks per capita of the population. With an average of 55 marks for each person relieved, the expense per individual varies from 18 marks (in Waldeck) to 91.5 marks (in Berlin). For a discussion of the difficulties and the many doubtful points about this statistical survey, see M. Schumann in *Conrad's Jahrbücher für Nationalökonomie und Statistik*, 1888, *Neue Folge*, vol. xvii. pp. 594 *et seq.*

<sup>2</sup> The growth of communal expenditure may be seen from the following figures. In the cities of Prussia the communal taxes for 1849 amounted to 3.77 marks per capita of the population; whereas in the year 1883-84 it had reached 11.46 marks. (*Finanzarchiv*, 1884. p. 764.) Joseph Körösi publishes a comparative study of the financial statistics of the cities of Europe in *Finanzarchiv*, 1884, pp. 254 *et seq.* The same paper may serve also as an illustration on a small scale of the difficulty involved in making comparisons in financial statistics.



BOOK II.  
THE THEORY OF TAXATION.





## CHAPTER I. THE JUSTICE OF TAXATION.

LITERATURE (also for succeeding chapters). J. G. Hoffmann, *Die Lehre von den Steuern mit besonderer Beziehung auf den preussischen Staat* (1840). K. G. Kries, *Zeitschrift für die gesammte Staatswissenschaft*, 1855 and 1856. C. von Hock, *Die öffentlichen Abgaben und Schulden* (1863). Lorenz von Stein, *Lehrbuch der Finanzwissenschaft*, 5. Auflage, *Zweiter Theil*, pp. 346-561 (1885). *Schriften des Vereins für Sozialpolitik*, vol. iii. 1873. Fr. J. Neumann, *Die progressive Einkommensteuer im Staats- und Gemeindehaushalt (Schriften des Vereins für Sozialpolitik*, vol. viii., 1874). Fr. J. Neumann, *Die Steuer und das öffentliche Interesse* (1887). Adolph Wagner, *Finanzwissenschaft, Zweiter Theil* (1880) (2. ed. 1890). Albert Schaeffle, *Die Grundsätze der Steuerpolitik und die schwebenden Finanzfragen Deutschlands und Oesterreichs* (1880). Robert Meyer, *Die Prinzipien der gerechten Besteuerung in der neueren Finanzwissenschaft* (1882).

### I. THE RIGHT TO TAX AND THE OBLIGATION TO PAY TAXES.

§ 192. The evolution of the right to tax on part of the commonwealth, and of the liability to taxation on part of the individual members of the community, goes on *pari passu* with - the evolution of the state itself, as the conditions of its development are the same.

The relation of the individual citizen to the state generally, as well as the special relation of his participation in the covering of the public expenditure, depends, after a certain stage in the development of any nation is passed, on the degree of the intimacy of connection between the whole and the individual. This connection will soonest find a lodgment in the consciousness of the members of the community in cases where the group is a small one - where the interval between its center and its environment is consequently slight. But inasmuch as the inevitable

trend of history is toward a progressive widening of the social groups and a continued increase of the population comprised in each group; since this course of development goes hand in hand with the growth of the demands of advancing culture and the increasing ability to obtain the means of subsistence; there arises a discrepancy between the circumstances that condition the development of this connection and those which condition the advance of culture. A discrepancy of the kind which we observe at various stages of the historical development, and which also presents itself for solution in more than one direction at the hands of the nations of the present day. The tax system of the German cities of the Middle Ages and succeeding centuries is the correlate of that political maturity which here first developed itself, in these oases of political liberty as it were.<sup>1</sup> Machiavelli<sup>2</sup> accords high praise to the republican virtue with which the ancient property tax of these cities was duly paid; and we find survivals of it (in Bremen) in force even in our day. Outside the city republics, the idea of an obligation to pay taxes finds acceptance only very slowly, in the course of the struggle of a developed concept of the state against the individualist claims of a constitution based on class privileges. It is true that even as early as 1664, speaking from the standpoint of the absolute state, J. F. Horn says:<sup>3</sup> *optime sibi constat respublica in qua imperantur tributa, non rogantur*. But about the same time (1654) the delegation of Braunschweig-Wolfenbützel in the German Reichstag declares it "an immutable principle that taxes and imposts are fundamentally at variance with the nature of a commonwealth; inasmuch as it is only with a view to the conservation of one's effects that one enters into civil relations; men become citizens precisely in order to be able to retain their belongings in peace and security."<sup>4</sup> And even as late as 1782

<sup>1</sup> Gierke, *Deutsches Genossenschaftsrecht*, vol. ii. (1873), p. 698. Cf. Andreas Heusler, *Ursprung der deutschen Stadtverfassung* (1872), pp. 218, 251.

<sup>2</sup> *De republ. Lib. i, cap. 55*.

<sup>3</sup> *Politica*, p. 316.

<sup>4</sup> K. H. Lang, *Historische Entwicklung der Teutschen Steuerverfassungen* (1793), p. 206.

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the Lord Bishop of Salzburg was rebuked by a conclusion of the High Court of Judicature for having presumed to assert that in matters of taxation the will of the sovereign was the only law, and that taxation was one of the royal prerogatives.<sup>1</sup> The systematic thought which prepared the way for the state and the public economy of the nineteenth century made its first decided step in advance at this point.

§ 193. The Political Philosophy and the Political Economy of the era of the enlightenment erected an ambitious structure, in which the motives of the individual are claimed to be in full harmony with the interests of the community. The result of their labors is an imposing scheme, a sort of ideal to be worked out practically in the development of a new concept of citizenship. The speculations of these theorists disregarded the differences which divide the concrete man, whom the earlier era transmits to the new, from the great abstract concept of the commonwealth. For more than a hundred years past, science has been at work to enforce the consciousness of the duty of tax paying, and therewith to further the development of a fuller sense of citizenship. And it is never to be forgotten that in the earliest beginnings of an independent science of economics the point of departure was the subordination of the economic individual to the concept of the state, and therefore to the idea of taxation. At this point the German Cameralists are at one with the French Physiocrats. Justi<sup>2</sup> says, to cite but a single utterance out of many that we have from this eminent man: "There is no doubt whatever but that the subjects are in duty bound to render this contribution towards the great expenses of the state; the private property of individuals, in so far as the common welfare of all subjects unites them into a single body or moral person, is, at the same time, the common, though not immediate property of the state, and the state is therefore fully competent to make use of this its mediate property for the purposes of its own welfare whenever its immediate

<sup>1</sup>K. H. Lang, p. 232.

<sup>2</sup> *Staatswirtschaft* (1755), vol. ii. p. 288.

property is insufficient. Since the subjects have once voluntarily organized a commonwealth for the furtherance of their common welfare, they cannot refuse the means required for the purpose .... so that they are bound to contribute towards all proper expenditures and necessities of the state, not only a part, but the whole of their incomes, and even, in cases of extreme necessity, to place the body of their possessions at the disposal of the state ....”

The Physiocratic theory of the net product, which is the cornerstone of their structure,<sup>1</sup> is but an expression of that idea of the state which dominated all their economic thinking. (The same is true of the German Cameralists, cited above, who wrote in the time of the Physiocrats.) As is the case with so much else, this doctrine too has been laid at the door of the later political economists of the English school because neither the origin of the doctrine nor its historical connection was known. Its connection was this, that private economy figured as the foundation of the state's finances and the prosperity of private industry was regarded as the basis of a productive tax system. The idea of the rising absolute state, according to which men are but the ways and means for the purposes of the state, was taken over by the philosophy of the new economists. It is true they lay down new principles for a rational system of taxation which is to clear away the old empiricism; but the course of argument, which conceives of private industry as the means and the economy of the state as the end, is the same as ever. Hence the peculiar views, so foreign to us today, which are frequently misconstrued when expressed by the later theoretical writers on the doctrine of the net product. Quesnay, for example, says:<sup>2</sup> "It is not so much men as riches that are wanted for the development of a country; for the greater the riches employed in agriculture the fewer men will it employ, the more will it prosper, and the larger a net product will it yield." Whereas a numerous peasant population

<sup>1</sup> Cf. vol. i. sec. 424.

<sup>2</sup> *Maximes générales du gouvernement économique* (1758). Éd. Daire, p. 91. Cf. also p. 101 *et passim*.

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produces but little more than the necessary costs of cultivation, and can scarcely afford the lightest tax.

And in order to make the close connection between production and taxes perfectly clear, Quesnay says in a neighboring passage in the same work:<sup>1</sup> "Next to the means for cultivating the soil, it is the net product and the tax that are the things most urgently needed by a state, in order to protect the subjects against scarcity and against the public enemy, and in order to maintain the prestige and the power of the monarch." In beautiful accord with these ideas of his time, the German poet shows us the ideal of the modern citizen [*Staatsmensch*] as contrasted with the Philistinism of the olden time.<sup>2</sup> Just as he alone, says Lothario, is a good father who first serves his children at the table, so is he alone a good citizen who lays aside what he is to contribute to the state, before affording any other expense. But Werner assures him that he has never in all his life thought of the state.

§ 194. In the state of today, the state's right to tax and the individual's obligation to pay taxes are a matter of necessity, and correlated with this necessity is the external constraint to pay taxes. This necessity rests on the universally accepted idea of the state and of the national economy, and the varying requirements of a modern national constitution and the rights of popular representation which it specifies do not limit, but only confirm it. The right of granting taxes by a representative body does not imply a lessening of this requirement, but only provides for a discussion of the kind and volume of the growing national wants, and of the taxes necessary to meet them.

This element of coercion - the expression of the consciousness of the necessity of the payment of taxes in the modern state - distinguishes the tax liability of today from the shifting phases of the state's finances in earlier times. It is no longer possible as was the case down to the end of the eighteenth century, and even later,<sup>3</sup>

<sup>1</sup> *Maximes*, p. 93.

<sup>2</sup> *Wilhelm Meister, Werke* (1828), vol. xx. p. 147.

<sup>3</sup> Cf., among others, for the state of Wurtemberg, G. Rümelin, *Reden und Aufsätze, N. F.* (1881); p. 450.

for the state to place its dependence in its own domanial possessions. This is the most convenient manner of obtaining public revenue, for it does not arouse the citizen's slumbering sense of duty towards the commonwealth. In the constitutions and the tax legislation of many modern states this form of income is still retained as the normal basis of the public finances, very much as a tale that has been handed down from the olden time. It is no longer possible to make use of the circuitous method of government prerogatives, which seeks to obtain the needed revenue by humoring the individualistic notions of the citizen in offering its services in a palpable form and requiring payment for them. It is no longer possible to depend on taxation by voluntary extraordinary grants, with their narrow, anxiously specified time-limit and their specific appropriation to certain definite, temporary purposes.<sup>1</sup> For the modern state the tax and the national finances are indissolubly bound up together. The possibility of a change lies entirely in an alteration of the relation subsisting between private economy and the public economy. So long as private property continues to be the fundamental institution in modern society and the basis of industry and of the public economy, the tax must also necessarily continue to be the foundation and the corner-stone of the public finances. The socialism embodied in the radical party programs of today is quite right in regarding the system of taxation which they demand as nothing more than a part of the "transitional measures" which are intended to further the interests of the laboring proletariat; abolition of indirect taxes, exemption of a subsistence minimum, a single progressive income tax for state and commune - all these are measures calculated to serve the social-democratic class interests only so long as the existing legal relations of our economic system endure. These measures presume a national and communal fiscal system which depends on private industry and on private production carried on with private capital, and

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<sup>1</sup> Cf., With respect to taxation under the direction of the estates, the exhaustive investigation of H. G. Kries, *Historische Entwicklung der Steuerverfassung in Schlesien unter Theilnahme der allgemeinen Landtagsversammlungen, ein Beitrag zur Geschichte der schlesischen Städte* (1842), especially pp. 5 *et seq.*

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which therefore draws its revenues from the same source as private establishments, in so much that it requires its share of the means of subsistence from the latter. And this share is the taxes.

So soon as socialism has traversed the region of transitional measures, it abandons the institution of private ownership of productive capital, and therewith it abandons the method of production by private enterprise. Under the socialistic method of production all the incomes of private individuals are transmuted into official salaries drawn from an all-comprehending state activity. The ideal of the coming commonwealth and of the coming national economy becomes identical with the type of the primitive national economy, with its comprehensive national possessions and its revenue drawn from them.

For the present, and, in point of actuality, for the future as well, private ownership, and therefore the necessity of the tax, remains. This logical consequence should not be lost sight of by the political parties that wish to preserve the state.

## II. THE PRINCIPLES OF EQUITABLE TAXATION.

§ 195. The general principle being admitted that each individual private economy is in duty bound to contribute to the taxes, there remains for discussion the more difficult question as to the method by which this great multitude of dissimilar private establishments are to be laid under contribution to meet the expenses of the general public economy in such a way as to distribute the burden equitably among them all. We have here to do with a postulate which the presence of moral considerations in every fundamental question of economics obliges us to take account of. I shall allow myself here to refer back to the more detailed treatment given to these questions in the introductory portion of this work (vol. i. secs. 366 *et seq.*).

It is unnecessary to recur to the fact that in any investigation of the ground for a determination of prices, whether in the market or in the affairs of the public economy, we have to do with historical problems yet awaiting solution, inasmuch as they are

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problems involving a moral factor. It may be sufficient to call to mind the point already established, that it is a meretricious subterfuge to erect what is, into a norm of what should be. Whoever puts the question as to the ground for a determination of prices, or taxes, or any other form of payment employed in human society, thereby puts the deeper lying question: What has the judgment of men in the past declared to be just and right in their adjustment of business matters? and how far is their judgment to be accepted as good? To the observation and appraisal of the ethical desiderandum which expresses itself empirically in the judgments already passed, there is to be added an exposition of the further desiderandum wherein the decisions of the past are to be cleared up and further developed.

Far from its being possible to accept any fixed datum from which to proceed as from a basis of "natural" right, and beyond which nothing would be necessary but a dry, deductive logic (mathematically exact and subtle), we have on the contrary to do with the evolution of moral impulses, judgments, activities; matters which appear definitive and statical only to the most superficial view, but which, in point of fact, constitute an unceasing movement, while they present as statical data nothing more than a certain body of average, customary decisions, which on closer inspection resolves itself (like any other average) into an aggregation of diverse individual cases.

§ 196. The development of judgments concerning what is equitable is a progressive development, just as all historical development is progressive.

Starting from very crude beginnings, the sense of equity gradually gains strength in the struggle against the selfish motives and the force of the strongest. But even after a lively sense of equity has been attained and has been incorporated into the social structure and habits of thought, there still remains a wide scope for development in the way of extending and deepening it; while there also remains open a path of indefinite progress in respect of quality.



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The principles of prices and taxes afford a wealth of special materials illustrative of this general law.

A great advance in the progress of society has been achieved when the distribution and the recompense of work in an industrial society have been freed from every element of coercion, and are determined solely on grounds of a recognition of equitable reward. But even though the element of force has been eliminated, there still remains a broad field for the exercise of judgment with respect to the nature and the reach of the principles on which is based an equitable determination of prices, wages, contributions, taxes, - a field which the present age is far from having exhausted.

The facts of past progress in this respect, and the problems offered by the present and future in the way of further development, are the matters with which our discussion will next have to deal.

§ 197. Free Contract and Authoritative Enactment are but different forms of the same process of judgment in the determination of values - in price, wages, contributions, taxes.

Whether prices are determined by the "higgling of the market" or by legislative enactment and regulation; whether the question concerns the exchange of the products of private industry between individuals, or services rendered its members by the commonwealth; whether governmental authority simply regulates prices in private intercourse, or fixes the price of what itself contributes toward the general well being - the basis of this multiplicity of determinations of price, etc., is always a multiplicity of judgments as to values, which may be carried out in practice with or without the intervention of the public authority.

It only makes the case clearer, it simply serves as a more palpable confutation of the illusory belief in determination of price by natural forces, to have the state enact what is to be done in squaring accounts for services rendered. And this authoritative manner of determining price moreover affords a more potent means of progress in the growth of equity in price determination.

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But in point of substantial fact, the process is just the same whether controlled by the organized action of the state or not; it is always the existing sense of equity that has to decide with respect to the equitable adjustment of prices (taxes, etc.). The state has nothing at its disposal beyond the human material of which it is made up, being nothing but an organized society.

The state's enactments, therefore - price schedules, taxes, salaries, dike regulations, etc. - are but the expression of views that lie within the compass of the insight and intelligence already achieved and current. In virtue of its office it becomes the state's duty as a matter of course to give expression to the best and ripest sense of equity attained, and in so doing it will be able to rise above the level of free contract. The state is hereby enabled to bridge the interval between the backward sense of equity of today and the higher plane of a riper equity yet to be attained. But even in so doing it affords a proof of its dependence on present attainments in moral and spiritual development

§ 198. All determinations of value rest, as we know, on the two elements of Utility and Scarcity. Scarcity resolves itself, so far as concerns all reproducible goods, into the cost of production. Utility, with respect to goods of all kinds, resolves itself into a complex of elements, some of which are only now struggling into recognition. (Cf. vol. i. secs. 370, 378-380, 396-403.)

Current views as to what is an equitable compensation are very largely agreed in looking for the ground of decision to the principle of cost of production. It is a simple and easily comprehensible postulate of the practical reason that every man, so far as he has the ability, should make good the cost at which another has wrought in his interest. When the pains, the labor, the consumption of materials undergone by another have served to afford me an advantage which I should otherwise have been obliged to compass by my own effort, etc., there is a manifestly equitable relation present between the sacrifice and the benefit conferred.

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The appreciation of this principle of equitable reward is, indeed, so general and thorough that the need is rather of an effort to limit and circumscribe it than to advocate its wider acceptance.

And this for two reasons. In the first place, even in cases where the principle of cost of production has found adequate recognition in practice, we find expressions of views at variance with this principle and favoring a comparison of the benefits conferred, where benefits of different magnitudes are conferred at equal cost.

In the second place, there are large groups of facts, especially within the domain of the public service, where, from the nature of the case, it is either impossible or impracticable to set off individual expenditure against individual gain. Here the sense of equity accordingly turns perforce to other grounds for an equitable adjustment of the compensation required.

§ 199. Under the first head it may be noted that the current views of equity demand that in cases where the municipal authorities construct a new street, not only should the owners of the adjacent real property be required to bear a considerable share of the cost of construction, but the owners whose property is benefited in an especial degree, on account of a specially advantageous situation of their property relatively to the new street, should be made to bear a larger proportion of the cost than the owners of property less advantageously situated. They reap a greater advantage from the same proportional cost, and should therefore bear a proportionally larger share of the expenditure by which they have been benefited.

As to the second point, we are aware that in the current views of what constitutes an equitable equivalent for benefits enjoyed there occurs a second, less definite principle of award, which may be designated simply as the ability to pay. The indefinite character of this element lies rather in uncertainty as to its scope, and as to the various remoter questions into which it ultimately resolves itself, than in any doubts entertained with respect to its own legitimacy.

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As regards the scope of this principle, it is to be said that its legitimacy is questioned as far as concerns the great mass of private business intercourse. We are shocked to hear that the same merchant or landlord demands a higher price for the same goods from a wealthy customer than from a poorer one. Indeed, it is the traditional attitude of the government in case of services which are of great importance to the public and are of a monopolistic character (railways and other common carriers), to forbid "discrimination" between customers, under penalty of law.

But one may easily see that ethical concepts are less fixed and definite with respect to this point than with respect to the other principles governing the equity of compensation. The point which arouses antagonism is the arbitrariness, the discrimination between persons, etc., rather than the connection between the prices charged and the buyer's ability to pay. It is at any rate certain that we find other portions of the industrial field, even in private business relation, where such a dependence of price on ability to pay is not only accepted as equitable, but is even required. In railway passenger traffic the classification of coaches as first, second, and so on, proceeds on the assumption (frequently not in accordance with fact) that fares are graded according to the ability of the various classes of passengers to pay; so that the fares charged for third or fourth class may not only afford less profit, but may even fail to cover expenses, as compared with prices for first and second class.

On comparing this case with the examples previously cited it appears that in private business, for large classes of society, the gradation of prices according to ability to pay is approached of, while personal discrimination is disapproved.

But even this rule does not hold in the case, e.g., of the physician, who actually regulates his charges by an elaborate scale of prices, and rates his services according to the ability of his patients to pay for them. In this case the principle (habitually accepted as equitable) seems to be connected with the peculiar nature of the physician's services, which, as is the case in all the higher professional occupations, rises above the plane of a pecu-

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niary equivalent, being in a numerous class of cases constrained by the pecuniary position of the patients to forego it and therefore, on the other hand, constrained to recoup from the patients who can pay, in order to cover pecuniary necessities.

§ 200. But the principle of Ability to Pay finds its widest scope and most unquestioned recognition in the field of state and communal affairs.

Not that this field does not afford ample play for the practice of an adjustment of price to cost; but nowhere else does it hold true to the same extent as here that wide-reaching and fundamental relations of social life demand the application of the principle of pecuniary ability as the equitable and unavoidable norm of adjustment, scarcely questioned by current conceptions of equity.

I may here refer back to the discussion contained in an earlier chapter (book i. chapter iii., On the Various Kinds of Public Contributions).

The demand of equity that individuals are to pay in proportion to their varying pecuniary ability, is accepted so unresistingly within the field of the public economy for the reason, in the first place; that a computation of proportional cost and benefit is, in regard to many very essential services, impossible, and in the second place, and more especially, because the more fundamental phases of the public activity in some degree condition the very existence of the individual in society, so that it appears right and just that these fundamental conditions of human social life should be intimately bound up with the total personal and economic strength of each individual. The appeal to the principle of the pecuniary ability of the individual in matters of national concern touches our sense of equity so directly and irresistibly because it is a principle of wider scope than that of the economic field alone, and is but a special application of the broad principle of a moral solidarity.

But the degree to which this principle has won acceptance in the convictions of any generation of men is not the same with

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respect to all matters. And then, again, there are large classes of relations, even in public matters, for which the method of payment according to cost and benefit received is both possible and expedient, not only for the present, but for an indefinite distance into the future. So that the principles of equitable adjustment prevailing at any given point of time are a complex - a varying combination of the factors that bear on the question of equity, varying according to the relative importance ascribed to one or the other factor in different fields of public activity.

§ 201. It follows from what has already been said that the struggle between the two principles of taxation which the ethical conceptions of earlier historical writers have presented as antagonistic, viz., the so-called utility principle (or the principle of taxation according to interest, or benefit received) and the so-called sacrifice principle (or the principle of taxation according to ability to pay) is not to be set at rest simply by a decision in favor of one or the other alternative, to the exclusion of the other.

Rather, the question of equity in all taxation, inclusive of payments not usually classed as taxes (fees, contributions), reduces itself to the question of an equitable determination of values, such as has already been discussed in what has gone before. The question concerns the same elements, in varying combinations according to the degree in which one or another of these elements is in any particular case recognized as equitably decisive.

In the course of the exposition in which there has been attempted an analysis of the services rendered by the public economy and the formulation of the methods of payment properly to be adopted in requiting these services, the conclusion has been reached, not only that the "utility" principle alone does not afford a tenable basis for taxation, but also that the principle of sacrifice, or ability to pay, cannot be accepted as the sole principle.

To state the matter briefly and in a general form, the two principles simply serve to indicate the prevalence of certain concep-

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tions of equity. And - historically considered - their significance, in the sequence in which they have won acceptance, is that they indicate the course of development from the egoistic, individualistic conception of equity to the conception of solidarity. There has been an evolution of the moral attitude of men and a progressive recognition of the equitableness of taxation.

§ 202. There is a class of speculative writers on history who seek to insure the unhampered claim of coming generations to a free choice of any peculiar norm of equity, by recognizing as valid, without reservation, whatever conceptions of equity have prevailed in times past. In freely accepting as sufficient the grounds on which each successive generation holds its peculiar tenets with respect to equity in taxation, they fancy that they are leaving so much the freer scope for conceptions of equity that may arise in the future.

To me it seems that this conception blurs the unquestionably legitimate idea of an historical development of equity by overstating it. On the basis of an unproven premise there is conceded to each succeeding epoch the capacity to give adequate expression in its institutions to the idea of equity answering to the circumstances of the time; so that we should have to look for progress in the conception of equity not from any advance in knowledge and moral sentiment, but simply as depending on the historical epoch from which it emanates. Still, in the facts of daily life, and in our scientific researches as well, we are constantly confronted with the obvious fact that the concept of equity in the period of history to which we belong is in dispute at every point.

Adolph Wagner has not been entirely uninfluenced by historical-philosophical views of this nature in drawing his distinction, in his *Allgemeine Steuerlehre*, between a "purely financial" (or fiscal) principle of taxation and a social-political principle. The former of these principles being assigned to the "civic (*staatsbürgerliche*) period," as good and fair for that period, while the latter is insisted on as the true principle for the present and

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the coming period, as the basis of the "social phase" of taxation.

But if we are to construct our "civil period" out of the material furnished by the actual course of political and social development, and not replace reality by a utopia, it becomes absolutely impossible to accept the purely fiscal principle as a tenable sole principle at all; that principle not only claims to afford a justification for thoroughgoing individualism and egoism, but also seeks to justify a complete disregard of the unavoidable fact of solidarity in all political and social life.<sup>1</sup>

In the second place, the justification offered for the "social-political" principle of taxation, to which this other principle is made to serve as a foil in the same manner as the "civic" period serves as a foil to the "social" period - this principle, with its contained purpose of abolishing existing inequalities in incomes and property - with its struggle against the inequities of the "competitive system;" is but an exaggerated expression of the legitimate sentiments of equity which have grown out of the principle of pecuniary ability in the course of its development, and which we shall have to discuss later on.

I apprehend that the placing of these two principles in antithesis is but the rending asunder of a single fundamental principle, the investigation of whose historical development is our real task.

### III. THE HISTORICAL GROWTH OF EQUITABLE TAXATION.

§ 203. The discussion has, so far, dealt with the course of development out of which the principles of equitable taxation have emerged as an historical product. It will now be necessary to give some attention to the way in which these principles have been applied in the course of history to the relations subsisting between the different social classes.

The significant point here, apart from the central fact of a growth of clearness in the conceptions of equity, is that of the prevailing views as to what are the equitable claims of a more or

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<sup>1</sup> See a paper by the present writer in *Conrad's Jahrbücher für Nationalökonomie und Statistik*, 1880, N. F. vol. i. pp. 206-232.



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less considerable portion of society to a certain fullness of life, In the degree in which the apex of the social pyramid looks upon the underlying layers as a means to the attainment of its own ends, in such degree will we have an unscrupulous exploitation of these lower strata in the distribution of the public burdens. The slow, uncertain growth of the recognition of the inherent rights of each and all members of the community necessarily carries with it a gradual progress in the views of what is an equitable taxation of the different social strata.

Down to the present period, which begins with the French Revolution, the system of taxation, through preceding centuries, was determined by the relation of domination on the one side and subjection on the other. The "dishonor" attaching to a personal tax is a consequence of a system of taxation whose aim was to exempt the ruling classes, cities, peoples from personal taxation, for the reason that they had the power to unload the burden from their own shoulders and shift it to the shoulders of the lower classes, provinces, peoples. The position of the subject countries (provinces) in the Roman Empire, with their enforced submission to a lower legal status, has in view a fiscal exploitation just as distinctly as has the policy of the individual cities that used all means, of force and fraud, of blood or money; to bring the circumjacent country into a state of dependence in order to exploit it pecuniarily.

The same thing repeats itself within the different classes of any given commonwealth. Here, again, there is the same irresistible desire for the sweet fruition of a domination over other men, whose subjection is turned to advantage in making them bear the public burdens. Here the ruling class wrings "surplus-value" from the subject classes, just as in the other case it was wrung from the subject countries and peoples.

Exemption from taxation was just as much a matter of course under such a system of domination as it now seems a monstrosity to us.

In point of fact, even the *Aufklärung* of the eighteenth century made an energetic protest against the tax exemption of the

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<sup>1</sup> See Mommsen, *Römisches Staatsrecht*, vol. iii. pp. 728 et seq. (1881).

upper classes. It is a fundamental principle, says Justi,<sup>1</sup> that taxes and imposts are to be borne by all subjects equally; for in this matter the same obligation rests upon all subjects, and all share alike in the state's protection and the other benefits arising from the constitution of the commonwealth. Indeed, Justi, in like manner as his contemporary, the founder of the French school, replaces the traditional injustice of the earlier social organization with its opposite, in that he demands that in the distribution of taxes special regard is to be shown the poor and the people of moderate means, in the exemption of an "existence" minimum.

On the other hand, in the constitutional enactments of the French revolution, and in the declaration of the rights of man,<sup>2</sup> the universality of the obligation to pay taxes is constantly insisted on. No citizen, says the decree of June 24, 1793, is exempt from the honorable duty of contributing to the public burdens.

§ 204. In the case of Prussia, the edict of October 27, 1810, dealing with the finances and the new measures to be instituted with respect to the imposts, declares "that a complete reform must be had in the impost system, the point of departure for which is that all taxes are to be borne by everyone alike, according to uniform regulations throughout the realm; that all exemption is to be abolished, as being no longer consonant either with natural right or with the spirit of administration of neighboring states." The hope is expressed "that those whom this provision touches will comfort themselves with the fact that they are no longer open to the reproach of avoiding the public burdens at the cost of their fellow subjects."

Still, the constitutional enactment of January 31, 1850 (Article 101), is constrained to speak of a revision yet to be carried out with respect to existing tax exemptions, which will put in

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<sup>1</sup> *Staatswirtschaft* (1755), vol. ii. p. 293.

<sup>2</sup> *Declaration 3-14 Sept. 1791*, section 13 (repeated in the constitution of 1791), cf. *Constitution, 24 juin 1793*, section 101. Cf. Louis Tripier, *Les constitutions française* (1849), *passim*.

force what Rönne calls the principle of "natural public law" [*Natürliches Staatsrecht*]. This became necessary for the reason, in the first place, that the regulation of June 21, 1815, under Article 10 of the German Act of Confederation, provided "that mediatized persons were to enjoy freedom from the ordinary personal and land taxes, as concerns their persons and their families, as well as their domains." In the second place, the lower nobility, had also been able to preserve their ancient exemption from taxes on landed property down to the middle of the nineteenth century, although the Prussian crown had for centuries past been engaged in a struggle with them, and had even achieved a notable success<sup>1</sup> against them as early as the beginning of the eighteenth century,<sup>2</sup> in the revision of the general land-tax payable by the East Prussian nobility. An ordinance for the latter purpose was for the first time promulgated in the legislation of May 21, 1861, providing for changes in the tax on landed property, and for a general building-tax of universal application. The point first spoken of above was sought to be dealt with by the legislation of May 1, 1851, concerning the classified income and class tax, amending the law of December 7, 1849, and which expressly abolished the exemption hitherto enjoyed by "immediate" princes (*die Reichsunmittelbaren*) from the class tax.<sup>3</sup> Nevertheless, a further (unpublished) order in council, of March 16, 1857, ordained that the exemption of the mediatized German princes and counts of the empire, not only from the ordinary taxes on landed property, but also the ordinary personal taxes, as concerned their persons, families and domains, was reestablished. This was, it is to be said, at an epoch in Prussian national life when mediæval romanticism was struggling, for the last time and in the last ditch, to uphold or to reestablish institutions which have no place in the constitution of the modern state. Under modern views of taxation an exemption of this kind is

<sup>1</sup> Zakrzewski, *Die wichtigeren preussischen Reformen der direkten ländlichen Steuern im 18. Jahrhundert* (1887), *Schmoller's Forschungen*, vol. vii.

<sup>2</sup> Ludwig von Rönne, *Das Staatsrecht der preussischen Monarchie*, 3. Auflage, vol. i. secs. 70, 105.

<sup>3</sup> *Instruction* of May 30, 1820.

open to the further objection that it abolishes the obligation to pay taxes, at the precise point where, as we shall presently have to point out, the special duty of the upper classes of society in the payment of taxes rests. In this regulation the traditional position of indirect taxes, in relation to the different classes of society, is reversed in a remarkable way. This class of taxes, which is generally decried by the spokesmen of the majority as oppressive; becomes the sole recourse of a necessitous exchequer.<sup>1</sup> The crude conceptions of the Middle Ages which intimately connected the honor of the upper classes with tax exemption, equally with the more fully developed conceptions of the modern state which find an element of honor in a wide distribution of the payment of taxes, are willing to admit none but this inadequate form of the performance of a public obligation - without having any clear appreciation of the reason for formally excluding tax exemption beyond certain purely technical reasons or certain grounds of prejudice.

§ 205. Quite different is the case of an exemption of the public servants in the civil and military service, as well as of all appointees of any public organization, so far as they are declared exempt from taxes levied by the body in whose employ they are. While the questions which arise out of the legal relations existing between the employees of one civil organization and the taxation levied by another (e.g., the empire, individual states, communes) are difficult and involve a great number and variety of considerations, the relation of an employee of the state to the state's taxation, of the communal employee to the communal taxation, etc., is quite a simple matter. In this case the payment of taxes by the employee, so far as it touches the salary paid him in his official relation, is nothing but a concession to the sentiment in favor of the universal obligation to pay taxes, being

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<sup>1</sup>The Prussian decree of June 21, 1815, above cited, provides that the exemption "is, however, not to be construed as applying to extraordinary and war taxes, nor to indirect taxes."

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in fact only a payment out of one hand into the other. What income the civil servant possesses beyond his official salary is of course properly subject to the same obligations in the way of payment of taxes as the income of any other citizen. As far as this is concerned, there is no reason for an exemption.

This formal tax liability of the civil servant has an indirect consequence, in that in taxing him the assessing mechanism is enabled, on account of the publicity of his income, to ascertain its exact amount, while in dealing with the general mass of private incomes, it is to some extent incapacitated by the lack of publicity, and has to content itself with less than the truth. So that the assessment levied on the income of the civil servant suffers the same practical increment, compared with the burdens borne by the majority of other incomes, as does the burden of the honest minority of private tax payers, compared with that of the dishonest majority. The only difference being that in the case of the civil servant honesty is compelled by publicity, while with private persons it is a voluntary matter. In the case of the civil servant, moreover, in consequence of his intimate relation to the public service, there is a more urgent call of duty to a conscious loyalty toward the public law, and so an inducement is offered him to stand as a model for the rest of the citizens.

A more realistic view of the matter finds in this state of the case an argument for partially exempting the civil service from taxation, in order to do away with the practical inequality that has arisen under the law as it is.

§ 206. Although exemption from payment of taxes, such as had a place in the public law of the past, no longer has a place in the political life of today, still there is a tendency perceptible, common to the old state and the new - to the old social organization and the new, in the direction of some relative exemption from participation in the bearing of the public burdens which every stratum of society is in duty bound to bear. Hence the contrast of social classes in respect of their ability to pay taxes and in respect of the degree to which they are taxed.

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In this connection it is a very significant fact that that class of taxes which by their nature are the least available for purposes of legal exemption, and which also, in point of fact, through this peculiarity, first served to realize the idea of a nominally universal and uniform liability to taxation, - it is very significant that this class of indirect taxes has for centuries past borne the reputation of being a means of oppressing the lower classes. On this account indirect taxes were condemned by the earliest scientific system of taxation, that of the Physiocrats, and they have ever since been condemned by radical defenders of the rights of the people:

The fact is significant, as showing how great importance attaches to the substantial relative weight of taxation, even apart from any formal, absolute exemption from taxes. It serves to show how, accompanying or following the question between obligation to pay taxes and exemption from them, this other question comes to the front: as to how great a burden of taxation each class of society is properly bound to bear, under the rule of a universal obligation to pay taxes.

Ever since scientific thinking first sought to fathom the profounder questions of taxation, the attempt has continually been made (and without a satisfactory result) to find out a thoroughly reliable standard or measure by which to distribute taxation among individuals and classes possessed of different pecuniary ability. Practical egoism has sought in vain to turn the absence of any accepted standard for the computation of equitable distribution to account as a pretext for avoiding its fair share of the burden. There is no universally applicable norm of equity in this matter. This is but another of those cases where the chase after economic truths that shall admit of being expressed with mathematical accuracy, and shall hold with the rigidity of natural law, turns out to be a chase after a will-o'-the-wisp, for the reason that the realization of equity in the course of historical development comes to pass after the manner of all things moral.

§ 207. This course of historical development presents a startling contradiction. The contradiction, or contrast, has been

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thrown into the historical-philosophical form of three successive phases of development: the feudal [*ständische*], the civic [*staatsbürgerliche*], and the social. In this triad the civic phase or epoch is made to bridge over the contradiction between the first and the last of the series by establishing a legal equality [*Rechtsgleichheit*] in the universal obligation to pay taxes, while it leaves the existing inequality in income and property undisturbed. It is reserved for the third, the social epoch, to establish a new norm of equitable taxation, whose function it will be to achieve a systematic alteration of the distribution of income and property.

Originating with socialistic writers, who claim to speak for the lower classes, this contrast of phases of development has come to express a change in the conception of equity, according to which the "equality" of taxation, as soon as it is attained, passes into its contrary. It is an application of the speculations of J. G. Fichte<sup>1</sup> to the question of taxation. He makes the objection to the principle of the so-called "legal" state [*Rechtsstaat*], according to which the state's function is simply to protect each one in the enjoyment of his personal rights and possessions, that "the purpose of the state is first to give to each his own, to invest him with what belongs to him, and, then only, to protect him in his possession of it." The scope of this view becomes apparent when Fichte demands that "all must first have their fill and a settled habitation, before anyone adorns his dwelling; all must first be warmly and comfortably clad before anyone adorns his dress."<sup>2</sup>

This makes plain what is the aim of the new conception of justice, even if we must designate its historical-speculative formulation as an untenable abstraction, and recognize that the contrast between "legal equality" [*Rechtsgleichheit*] and "social equality" (see vol. i. secs. 312 *et seq.*) is a distorted one. The new postulate confronts us not in the form of a scientific truth, but as an historical fact in the social-political movement. The whole thing

<sup>1</sup> *Der geschlossene Handelsstaat* (1800), pp. 10 *et seq.*

<sup>2</sup> *Loc. cit.* p. 32.

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is an inversion, As soon as something has been gained for the populace a much larger portion is demanded, for gaining which what has been achieved is made to serve simply as a vantage ground.

§ 208. Let us come to a clear conception of the matter in Controversy.

The entire social movement, of which the agitation for exemption of the lower classes from taxation and subjection of the upper classes to taxation is but a part, rests on the democratic movement of the century. Democracy vests the national will in the aggregate people; the whole people makes the laws, decides as to the functions and the needs of the state; it is the people as a whole that decides on the financial means to be employed, and prescribes the requisite legislation, in kind and scope.

In so far as this ideal of popular sovereignty emerges from the letter of radical political philosophy and becomes clothed in the flesh and blood of actuality, the old relation of subject and ruling classes is reversed. The quondam ruling classes, the minority consisting of the nobility, the cultured and the wealthy, yield their place to the mastery of the majority, consisting of all those who are not noble, not cultured, not well-to-do, who were for so long the subject classes.

The national will has shifted its seat to lower ground, to the broad strata of the lower classes. The concept of equitable taxation now takes form and color from their wishes, their interests. The shifting of taxation from the shoulders of the upper to those of the lower classes now changes into a shifting in the contrary direction, from the lower classes to the shoulders of the upper classes.

Must we accept this drift of interest which asserts itself in altering the conception of a just taxation as the source of what is to be accounted a desirable norm of equity, as something affording a basis for a just apportionment of taxation?

Certainly not. It is always contrary to the essential nature of political sovereignty to make it a means for the gratification



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of social instincts, equally so whether the state is ruled from above or from below. The sovereignty of the state should in every case serve the interest of the whole, a function which imposes on the sovereign power duties and restrictions at variance with its special social interests. In case the converse were accepted as true, the consequence would be that every ruling class (whether a majority or a minority) would exempt itself from taxation and so reinstate the iniquity of the "period of status."

This immoral tendency of popular sovereignty is accordingly all the more to be combated, as contrasted with the iniquity of the olden time, because there is so much in it that is of a specious character.

§ 209. The danger that lies in the democratic tendency just spoken of for the development of the concept of justice in matters of taxation, is, however, circumscribed by the tempo to which all historical development is subject. The ideals of democracy will no more than any other system be free to realize themselves unconditionally by a development in empty space. They are confronted by potent historical facts which will yield ground only slowly. They come forward boldly, as tendencies embodying new conceptions and backed by new strata of the people, but can attain their end only by gradually displacing and altering traditional features of the social structure.

Even under circumstances where apparently the whole of the historical-political and social institutions have been swept from the board, when for a limited time and space the boldest logical results of popular sovereignty seemed to have been realized, the results of past development have presently proved themselves the stronger in the struggle, and the branches of the ancient tree, bent back temporarily, have sprung into place again with all the more violence, and set at naught the efforts at innovation. So that even in our day, a full century after the great Revolution, we have in France only a gradually accelerating ascending movement from below, and by no means a democracy with all its social and financial consequences. How else are we to understand

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all the measures taken, and all the abuses of legislation that indicate the continued influence of the upper strata rather than the sovereignty of the majority?

The influence of democracy should logically have first reached consummation where an earlier historical development had prepared the ground for it; where social conditions are sufficiently simple to permit its force to assert itself more readily; where, especially, the size of the community is so moderate as to afford popular sovereignty a favorable field. In the cantons of Switzerland, accordingly, the danger above pointed out has actually approached near the horizon and has become a matter of serious apprehension, which is concerned not so much with what has taken place, however, as with the trend of what is taking place.<sup>1</sup>

For the present, danger is not to be apprehended from this source in the German Empire and its constituent states. It is true, the German constitution, in its fundamental provisions, has accepted the primary demand of democracy - universal, equal, direct suffrage. But the historical forces embodied in the ancient state and the ancient order of society are more powerful here than in France (or in England). The results of democratic suffrage have so far been but as the waves that have broken about the base of the "*rocher de bronze*" without undermining it. The influence of the old order of society, backed by a traditional monarchy with its bureaucracy and its army, has so far maintained its supremacy and may look upon the rush of the breakers of democracy as but a reminder to use its privileges with reason and circumspection.

§ 210. It is only by keeping in mind the above considerations that we can hope to solve the problems embodied in the expressions, a "proportional" and a "progressive" basis of taxation.

Even Justi<sup>2</sup> expressed the opinion as early as 1755 that "If

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<sup>1</sup>The Income-tax in the Canton of Zürich (*Volkswirtschaftliche Aufsätze*, 1882). The Tax Reform in the Canton of Zürich and the Federal Administration [*Bundeshaushalt*] of Switzerland (*Nationalökonomische Studien*, 1886).

<sup>2</sup> *Staatwirthschaft*, vol. ii. sec. 228.

a just equality is to be observed in taxation, it is preeminently the proportion of means that must be taken as a basis, inasmuch as the protection afforded by the state is mainly concerned with property."

We have here a close connection between the old "benefit theory" and the taxes, leading to a decision in favor of a proportional basis of taxation, very much as if it were a payment of the nature of an insurance premium, which the owner of a house pays to the insurance company in proportion to the value of the house insured. A full century after Justi this theory has been unreservedly accepted by Thiers.<sup>1</sup> Each one, he says, is to contribute proportionally to the public expenditure - in proportion to what he earns or possesses, for the natural reason that the contributions to purposes of social protection should be proportioned to the sum of the goods protected. Assuming, he goes on to say, that the gross annual income of France amounts to 12 milliards of francs, and that 1,200 millions are required to meet the public expenditures, then it would follow that every one is bound to pay in to the state one-tenth of his receipts of all kinds whatsoever. Thiers explicitly insists that the comparison of the state with an insurance company is the most proper and most exact that can be employed.

K. H. Rau<sup>2</sup> opposes the "benefit theory," and calls especial attention to the higher conception of the state's function, appealing to the authority of Plato, Aristotle, Cicero, Fichte and Hegel. He demands that the taxes are to be apportioned according to the pecuniary ability of the individual tax payers. He also remarks that any given sum of money has a higher value for its owner, the larger a proportion of his aggregate disposable possessions it constitutes. But the only conclusion he draws from this is that "Each individual can about equally well or equally ill afford to contribute a certain maximum portion of the goods at his disposal." And that is precisely the ground of the proportional basis of taxation.

<sup>1</sup> *De la propriété. Nouvelle édition* (1849), p. 202.

<sup>2</sup> *Grundsätze der Finanzwissenschaft. 5. Ausgabe* (1864), vol. i. secs. 252 et seq.

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Adolph Wagner,<sup>1</sup> in the logical sequence of his scheme of historical stages, of a "civic" and a "social-political" period, has sought to justify the proportional basis of taxation on the ground of its being a consequence of the "competitive system" and of a "purely fiscal" system of taxation. This sequence serves him as an argument to prove that the civil period belongs in the past and that the social-political phase of taxation is at hand. Since, by as much as the necessary consequences of the former system are found wanting judged in the light of existing sentiments with respect to equity in taxation, by so much the more are we driven to the acceptance of the second phase.

The asserted sequence, however, rests largely on a confounding together of theories about free competition, individualism, taxation according to benefit received, the conception of the state as an insurance concern, etc., on the one hand, with the actual course of historical development on the other.

In spite of all theorizing, the state as it exists in fact, at least the state of the last three centuries, is and has always been incompatible both with the "benefit" theory and the proportional basis of taxation.

§ 211. The sequence holds only as regards the benefit theory and the proportional basis of taxation. If the benefit theory, the conception of the state as an insurance concern, etc., is found untenable (as is true for us today, and that in full accord with long established scientific convictions), then it follows with the same necessity that the proportional basis of taxation must be abandoned. For those who, with Rau, hold to the proportional basis, after having disallowed the benefit theory its presumptuous claim to be the basis of all tax obligation, the proportional basis of taxation is nothing more than an inconsequential conclusion based on their own inclinations, to which they cling in order to avoid the oft-portrayed dangers of progressive taxation.<sup>2</sup>

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<sup>1</sup> *Allgemeine Steuerlehre* (1880), secs. 397 *et seq.*

<sup>2</sup> French financial theory still occupies Rau's standpoint. Parieu (*Traité des impôts*. 2<sup>e</sup> edit. 1866, vol. i. p. 4), like Rau, contends for the broader conception of the

Rau's own words really surrender the whole position. And we may be permitted to cite this once eminent authority as the representative of a certain stage in the progress of the science. When Rau says: "A given sum of money possesses a higher value for its owner the greater a proportion of his aggregate disposable goods it constitutes and the greater a portion it consequently represents of the aggregate enjoyments at his command, especially in case the one who is to be deprived of a given sum will have to stint himself in expenditures for the most necessary articles in order to afford it," in all this he furnishes no proof of the legitimacy of the "therefore" by which he connects this proposition with the succeeding one, that: "Each individual can therefore about equally well or equally ill afford to contribute a certain maximum portion (quota) of the goods at his disposal."

Doubt is cast upon this doctrine by the facts of tax legislation,<sup>1</sup> as also by a closer consideration of the undoubtedly sound premise. Not to mention any of the ancient instances, as for example the Solonian tax legislation, the following laws may be

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state, but he likewise reaches a conclusion in favor of the proportional basis as the most equitable norm of taxation. He even approaches the position of Thiers, when he holds that the protection of property is the chief benefit conferred on every citizen by the institutions of the state (p. 33), and explicitly gives in his adherence to Adam Smith's principle, who argues for the proportional taxation of incomes that come under the protection of the state. Parieu believes he has herein found a weapon with which to combat tax exemption on the one hand and the progressive tax on the other. To him (p. 60) the opposition of the French nation to progressive taxation is evidence of the close logic and precision of their intellect, as contrasted with the "vague" sentiments of the Germans.

Leroy-Beaulieu (*Traité de la science des finances*, vol. i. book 2, pp. 103 *et seq.*) exhaustively combats the conception of a tax as an insurance premium, taking his stand on a broad view of the nature of the state. The tax, for him, follows logically from the principle of national solidarity. But this does not hinder his opposing the progressive tax (p. 137) with the demand that every citizen is to be taxed in proportion to the service rendered him by the state, and he enforces his argument with the question: "What would we say to a shopkeeper who should ask a different price for the same goods from different customers, according to their ability to pay?" See also Ch. Gide "*Principes d'économie politique. 2<sup>e</sup> edit.* (1889), pp. 600 *et seq.*;" "La forme la plus naturelle de l'impôt direct c'est l'impôt proportionnel sur le revenu."

<sup>1</sup> F. J. Neumann, *Die progressive Einkommensteuer* (1874), pp. 113 *et seq.* Parieu, *Traité des impôts* (1866), vol. i. pp. 35 *et seq.*

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cited: Under the Elector Frederick Augustus a general income tax was levied in Saxony, in 1742, which was assessed on all incomes between 100 and 1,000 thalers at the rate of one per cent., between 1,000 and 10,000 thalers at the rate of two per cent., between 10,000 and 12,000 thalers at the rate of three per cent., and so on up to eight per cent. on incomes of 25,000 thalers and over. The Austrian class-tax of 1799-1800 subjected all incomes to a tax graduated in twenty-three classes, the rate rising progressively from two and one-half to twenty per cent. The income [*Erwerb*] and property tax of 1808-13 in Baden exacted from all incomes exceeding 600 gulden a tax at a rate increasing from one-half to six per cent., according to the amount of the income. Similarly in Prussia, the Netherlands, etc.

But if these, as well as the many instances of income and property taxes in earlier times and in antiquity, are to be regarded simply as extraordinary and temporary taxes, it is to be noted that tax legislation since the establishment of peace has incorporated the principle of progression in its permanent measures. So, e.g., the Prussian tax legislation of 1820, which at every subsequent stage of its development (1851, 1873, and repeatedly since then) has applied the principle of progression with ever increasing emphasis. So the later tax legislation of other German states, and more especially the English income and property tax, has from the outset rested on the principle of exempting small and medium incomes entirely, or has at most taxed them at a lower rate.

§ 212. But in this disregard of the proportional basis of taxation, advocates like Parieu see not its refutation, but only an erratic departure from the correct principle. To them it is an indication of the influence of modern socialism and communism (though it would tax their ingenuity to trace such an influence in the extraordinary departure from the principle in the case of the German progressive taxes levied about the close of the eighteenth and the beginning of the nineteenth century).

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In any case, the fact and its repetition, however frequent in tax legislation, affords ground but for an inference and a more or less probable generalization; it does not prove the truth of the position.

The proof of our position lies in the fact that if we take Rau's principle seriously it will lead us not to the proportional but to the progressive basis of taxation. Rau is quite in the right when he says, in making his distinction between "concrete" and "abstract" value, that a given sum of money has a higher value for its possessor the greater a portion of his aggregate disposable; goods it constitutes. Undoubtedly, the smaller the income of a household is, the more will a given sum levied as tax abstract from the means required for pressing necessities, and the tax will fall so much the heavier on the particular household. On the other hand, the larger the income, the more will the tax tend to fall only on less pressing or even trivial needs, and will consequently exert but a slight pressure or none at all.

But how we can legitimately draw the conclusion from these premises that an equal percentage levied on the means of all taxpayers, great and small, is the proper basis, that is not comprehensible. The pressure of the same five per cent. tax will be very different in the case of small and of large incomes. And when it is borne in mind that (due account being taken of other than direct taxes, levied in the form of a percentage) the actual amount demanded by taxation considerably exceeds five or ten per cent. of the incomes out of which the taxes are paid, it is clear without further argument that a tax of 200 marks must be a far greater burden to an income of 1,000 marks than 2,000 marks on an income of 10,000.

It is the consideration of this fact of equity that has continually more and more (from antiquity to the present day, with the growth of the sentiments of fairness and justness) commended not the proportional but the progressive basis of taxation.<sup>1</sup>

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<sup>1</sup> Frederick the Great expressed himself with especial force in favor of the progressive basis of taxation, in the Instruction to the President of the Chamber of Accounts, Roden, with respect to the west Prussian contribution for 1772. The following passage occurs in Roden's protocol. "A wealthy man possessing an income

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That this latter principle does not possess the "precise logic" which the French genius ascribes to the proportional basis of taxation cannot alter the fact of its equitableness. This precise logic is nothing but a delusion based on false premises. In the theoretical field its basis is a wrong-headedness which expends itself in a search for mathematical truths in the ethical and historical domains, where they can never be found; in practical affairs it is an egoism seeking to fortify the "sacredness" of its property against the dangers of so-called communism by reducing this sacredness to figures.

§ 213. If an attempt is made to determine the extent to which a progression has been realized in the existing tax legislation of different states, in order to a verification by facts of the equity of the principle in general and the extent of its application in practice, we shall scarcely be satisfied with discovering it at the point where it has reached the developed form of the income tax, or even (after the fashion of the earlier Science of Taxation) to discuss the principle only in connection with this special form of its application. The principle is one which either does and should underlie every tax system, or does not and should not do so. It will be more to the point to find out what is the actual amount of taxation, calculated as a percentage of the tax-paying capacity of each individual, when account is taken of all forms of taxation. Noted men of the science, who rejected the principle of a progressive tax and were anxious to avoid the argument from existing progressive-tax laws, have tried to explain the fact of a progressive class and income tax legislation by pointing out that the resultant lightening of the burden for the people of smaller tax-paying capacity is but a fair compensation for the existing inverse progression, i.e., for the too heavy burden which this class of incomes is compelled to bear in the shape of other (consumption) taxes; that it is there-

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of 5,000 thalers might well be able to spare one-half of it, as he could still live; while a poor man, having an income of 80 thalers, could not spare one-half, as it would leave him nothing to live on; in the case of this latter, he would have done his part if he contributed one thaler." - Zakrzewski, *Die ländlichen Steuern*, pp. 83 *et seq.*



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fore the function of the progressive tax to readjust the proportional taxes to a true level for all pecuniary capacities.

But a computation of the kind suggested is a difficult matter. It presumes a very exact ascertainment of the distribution of the tax burden by means of the various kinds of indirect taxes; an ascertainment which must be based on an examination of a great number of types of individual establishments, such as will adequately cover the multiform gradations of society.

While such a calculation would be particularly tedious as regards the actually existing situation within the German states, on account of the heaping up of imperial, state and communal taxes one on top of another; on account of the particular character of our tax systems; on account of the varied gradations and classes of German society; still an approximately correct estimate will fairly support the assertion that in the German states including Prussia (as well as in Great Britain and Ireland), the visible relative lightening of the burden of the poorer and middle classes by the progression of the income tax, is at least fully offset by the less manifest relative overburdening of those classes through other forms of taxation. For it will not take much in the way of a comprehensive imposition of taxes on the general consumption of bread, salt, spirits, beer, tobacco, etc., in order to bear so heavily on the lower classes as to affect the abatement afforded them by the progression of the class and income taxes, which impose not more than a nominal three per cent, even on the largest incomes.

If, according to the provisions of the Prussian Class and Income Tax legislation, an income of 1,000 marks has now to pay some one per cent, in taxes, and an income of 5,000 marks three per cent., then we note that by requiring of the former income not more than 40 marks under the head of the various taxes on consumption, we require it to pay five per cent. per annum, while in order to raise the aggregate paid by the latter income to five per cent. on 5,000 marks the corresponding taxes on consumption must amount to 100 marks. To this latter sum the consumption of bread, salt (and probably beer) would contribute a no

greater absolute amount, the consumption of spirits absolutely less; that of tobacco rarely more, often less, than the like consumption of the establishment with an income of 1,000 marks. The lacunæ which occur in this estimate (which is intended to serve as an illustration only, and does not insist on the accuracy of the figures cited) are easily covered by the practical remission which occurs in the assessment of the 5,000 marks income (falling far short of the legal amount of three per cent.). So that the estimate made above would have to be amended, if at all, in a direction to correct this inadequate assessment, and so would still further emphasize the original proposition.

§ 214. Plainer to be seen, and also more sharply defined, is the tax progression in the cantons of Switzerland, especially in the canton of Zurich.<sup>1</sup>

On every inhabitant of the canton of Zurich rests an average tax burden of 40.15 francs. Of this, 30.45 francs goes to the canton and the commune, in the form of income and property taxes, etc.; only 9.70 francs goes to the canton and the confederation, in the form of indirect consumption taxes, 7.70 francs of this amount going to the confederation (mainly from import duties, with something also from postal revenues) and the slight residue to the canton.<sup>2</sup> The new federal taxation of spirits affects this canton, together with many other cantons similarly situated, but little, because the consumption of spirits is slight.

But if in this way indirect taxes on consumption, falling on the feebler tax-paying capacities, dwindle to an inconsiderable amount, there is an energetic development in the direction of relieving the smaller and the moderate tax-paying abilities from taxation and laying the stronger abilities under contribution.

This differentiation proceeds as follows: there is, in the first place, a great difference in the weight of taxation falling on

<sup>1</sup> *Finanzarchiv*, 1884, pp. 61 et seq.

<sup>2</sup> In Prussia as early as 1882 the taxes amounted to 24.25 marks *per capita* of the population, reckoning all imposts, inclusive of imperial taxes. Of these 11.97 marks was indirect taxes, 12.28 marks direct. - Gerstfeldt, *Conrad's Jahrbücher*, 1883, N. F. vol. iii. p. 40.

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income from property and personal income (communal taxes being levied almost exclusively on income from property, cantonal taxes to a very great extent); in the second place, there is a strongly developed system of lightening the burden of small and moderate incomes, as far as concerns the tax on personal income, while as regards income from property also a very appreciable gradation is to be observed (in the national tax).

A property income of 4,000 francs (from property worth 100,000 francs) pays at present to canton and commune 17-20 per cent. An income of the same amount, if it is personal income, pays to canton and commune together scarcely 3 per cent.

A personal income of 20,000 francs pays 6.16 per cent. to the canton; whereas, a personal income of 1,000 francs pays only 0.8 per cent. And this progressive character comes out even more strongly in the case of larger incomes. A personal income of 50,000 francs is taxed 7.26 per cent., the very largest income close to 8 per cent.

It is to be added that none of these rates is fixed by law. All that is necessary in order to raise the rates of taxation is a resolution of the Federal and Cantonal Councils in deciding on the annual budget (the same holds true of the corresponding communal authorities as regards the communal budget). The scale of the progression alone remains unchanged; the height of the scale can easily be increased.

This is therefore a case of a strongly accentuated progressive taxation. The form of taxation in which progression is a prominent feature makes up by far the larger proportion of a very considerable aggregate of taxes; while the alternative form of taxation, with its regressive tendency, is made little or no use of (salt tax, etc.).

§ 215. This noteworthy example of progressive taxation, as it has hitherto been realized in tax legislation, differs strikingly from the progression to be found in Prussian or in English tax

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<sup>1</sup> Cf. *Finanzarchiv*, 1884, pp. 131 *et seq.*

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legislation (where its range is regularly confined to a variation of a few per cent. and where it is met by full compensations in other taxes). We come therefore to the question as to the causal connection - as to the circumstances which go to determine that one thing will be found equitable in one place, and another in another place. The explanation suggests itself as obvious that the ground of difference lies in the difference of political constitutions. From this reasoning it would follow that the unhindered dominance of the democratic idea in Switzerland has resulted in a distribution of the burdens of taxation and a demand on tax payers in proportion to their tax-paying capacity, such as has not been attained in any other country in spite of the influence of a widespread democratic tendency - neither in England, nor in Germany, nor in France. It is a fact of great significance that the tax system of France should present so sharp a contrast to that of the Swiss cantons. It teaches us the lesson that there is a compact structure of institutions interposed between democracy with all its equipment of suffrages, electorates and constitutions on the one side, and the ultimate consequences of democracy in the way of practically decisive political institutions on the other, - a structure whose form and substance is determined by the influence of the past in state and society, and which yields only very slowly to the disintegrating forces of radicalism.

The simpler and more diminutive relations and proportions of the Swiss cantons have set these interposing structures aside more easily, or rather, they will more easily set the remnants of them aside. So we see what results democracy has led to in this case, and we believe that we have herewith discovered the cause of this highly developed progressive taxation. But what about its justice? What of its significance for other countries?

We have at this point occasion to envy the "historian." He assures us that the whole problem is to show what has come to pass and in what manner things have developed; what should be, is something about which the "historian" has nothing to say. This has been considered equitable here, and something

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else there; we are to declare ourselves content with knowing that very widely varying views are held as to what is equitable. But while this renunciation may be convenient for the "historian," the science would have to renounce a good share of the ground of its significance if it were to leave it entirely to the course of events to decide the direction in which the sense of equity should develop.

What each is to contribute toward the commonweal will either be determined by brute force working out its results through class sovereignty, majority rule, and the like, or by a reasoning intelligence which keeps ever in view the end of historical development, and projects the lines of evolution into the future, to serve reality as norms of growth.

§ 216. The substructure requisite for the discussion in hands to be found in the expositions contained in the general part of this work, which are occupied with the Social Gradation of Demand (vol. i. secs. 204-212) and the Differentiation of Society (vol. i. secs. 312-322).

In seeking for the proper form and method of progressive taxation, we shall find that the matter is to be discussed from two distinct points of view, each of which is of so great importance as to be indispensable to the development of civilization, at the same time that the two are so far mutually contradictory that we shall have to take thought to bring them into consonance with one another. The boundary line between these two points of view shifts from one side to the other during the course of history according as the one or the other of the two forces is the stronger. It will be found that at a given epoch, and to a certain degree even repeatedly during a period of some centuries, in the case of any given people, the one of these two forces is dominant, while the other falls into the background; but it is always a matter of more or less - the progress of history cannot dispense with either.

In the introductory portion of this work the one of these forces has been designated the aristocratic, and the other the democratic tendency of historical development.

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The distribution of pecuniary strength and of income in society, the consequent gradation of ranks, occupations and classes, the accompanying cultural differentiation in matters physical and spiritual, the diverse development of all human faculties in the direction of progressive maturity and completeness of life throughout the aggregate of the people, - in short, the social gradation in respect of the progressive amelioration of human life; all this is due primarily to the factor of individual initiative and activity. Without this no progress is conceivable. The individual powers of the superior organism, individual superiority in point of ability of any kind whatever, this is the pioneer which, setting out from the crude primitive capacities, pushes forward into the broad field of culture. The advantage which nature has given to the individual takes on the derivative form of advantages which he has himself achieved. Physical strength and virtues, courage and shrewdness, these raise him above his peers, and this vantage ground is transmitted as a heritage of blood, so that for his descendants it acts as a cumulative cause of further advantages. These favored individuals and the groups which they presently found, the upper strata, the higher occupations, the superior classes of every civilized society, these are the source of qualitative, intensive progress. Without this kind of leadership there not only can be no such progress, but there is not even that extensive development which J. G. Fichte and the extreme socialism demand, viz., that all must first be supplied with necessaries and a fixed habitation before anyone adorns his dwelling, and that all must be warmly and comfortably clad before anyone dresses elegantly. If this demand of rigid equality be granted, there is not only danger that our civilization may exhaust itself in the feeding of a great number of human beings, and achieve nothing beyond that; but it is at the same time to this civilization itself, with its technical, scientific, moral, economic progress, that we owe the possibility of feeding an increasing number of human beings. The spiritual elevation of an individual man is not only, in itself considered, the consummation of human culture; it is also the seed of the suste-

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nance of thousands of human beings whose life is spent in poverty.

§ 217. It is to be remarked that this course of development of individual advantages points to a dependence of the individual development on a greater whole, it being essentially of a relative nature.

How many are these favored individuals? What differences exist between them? How far are they removed from the aggregate? What are the intermediate gradations? What is the absolute cultural altitude of the aggregate? What is that of the highest elevations? and, What of the lowest depressions? These and other like questions will teach us that there is in history no conceivable genuine progress of any stability unless there exists a harmonious co-operation of individual forces with the social substructure, - a full compatibility of intensive culture with its general diffusion. And this indicates what is the duty of the favored individuals and classes towards the whole. Their advantages are a talent entrusted to them to be devoted to the service of the rest. This is the historical justification of their existence; and this is likewise their defense in their own generation whenever the democratic masses have come to a consciousness of the inconsistency of such privileges.

If it is true that history shows us an alternate rise and fall of the two factors spoken of above, it will certainly hold true for the present that the democratic tendency is the stronger, and that the trend of development is in the direction of an extensive culture. Whether we look to the constitution of different states and the changes they have undergone during the last hundred years, or to the legislation of the different civilized nations; whether we consider the routine of public life or the growth of works of public utility; the dominant principle is ever the same: a recognition of the demands of the lower classes of the populace for a participation in the amenities of civilization.

§ 218. The above considerations afford the norm of development for an equitable distribution of the burdens of taxation

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according to the tax-paying capacity, such as expresses itself in the form of a progressive taxation.

The great industrial productivity of this century undoubtedly serves the purpose (and especially in Germany) of affording a basis of affluence for the upper and middle classes, which are sorely in need of such recuperation. At the same time, this productivity has an undeniable tendency to leave its golden fruits by preference clinging to certain elevated summits of wealth, and this fact enforces with increased cogency the necessity of satisfying an excited public sentiment which demands a larger degree of participation in these fruits by the community at large.

This demand is not to be met by a distribution of the burden of taxation alone, but an essential part of the problem may be solved in this way. It may be solved by a shrewd and energetic further development of the progressive taxation, which has lately been, or is about to be, introduced to a moderate extent in our great civilized states.

And there is but a single alternative. The force of the democratic current is already so great as to rather be overrated than underrated in judging of the political situation. This force, as we are well aware, has so far by no means worked out its ultimate consequences, but like a torrent it sweeps before it the debris of the old political life and is continually overflowing new regions of society with its swollen waters. George Canning's old maxim, that those who discountenance every improvement because it is an innovation, may presently find themselves obliged to accept innovations which are not improvements, embodies a warning and a threat for all those who are responsible for the continued existence of our civilization and for the preservation of the conditions which make it possible.

If that organization of society and of political life which we call aristocratic in the best sense of the term, is to survive (and it is indispensable for the progress of civilization that it should survive), the corresponding aristocratic attitude of the upper classes must come up to the demand made upon it. They



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will, among many other things, have to fulfil this requirement also in the way of accepting an adequately developed system of taxation. Their degree of readiness will make up in quality for what the democratic masses would otherwise demand, some day, in quantity. The voluntary acceptance of an increasing burden will serve to strengthen their traditional influence at a slight expense, and the strengthening of this influence is indispensable to the best civilization as well as to the existence of the higher classes themselves. On the other hand, the more an increasing progression comes as the result of the importunate demands of a discontented populace, the more reckless will it be, both in the new demands which it embodies and in its changes of the old order of things.

§ 219. The half-consciously accepted principle of progressive taxation has so far found but a very timid expression in our legislation. And there has been an avoidance of too great offense even in cases where (as in the canton of Zurich) this timidity has been outgrown. The result we have is the so-called degression in the rates of taxation.

As a classical example of this there is the Athenian tax legislation which is ascribed to Solon. This legislation, says August Böckh,<sup>1</sup> embodied the principle, worthy of any philanthropic legislator, that the smaller the income, the less a proportion should the state abstract from the income of the citizen; and in this manner, that the *Pentakosiomedimnos* was assessed for his entire estate, while the knight was assessed for five-sixths, and the *zeugites* for five-ninths of his land.

The progression was hereby fixed in such a way as to produce a descent from the full rate assessed on the highest class to five-ninths assessed on the lowest class. The rate was accordingly fixed for the highest class, and the progression appeared in the form of an exemption of the lower classes.

The degression which occurs in the tax legislation of Zurich and other Swiss cantons is of an analogous form. Here, too,

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<sup>1</sup> *Die Staatshaushaltung der Athener*, 2. Ausg. 1851, vol. i. pp. 655 *et seq.*

the law<sup>1</sup> established a fixed gradation from the full rate downward, increasing the degree of exemption the lower it descends. Just as in the case of the Solonian legislation, this law determines only the scale of exemption, not the absolute rate of taxation, which is fixed from year to year by the budget [*Etatsberathung*].

It is otherwise in Great Britain, where the budget of each fiscal year fixes not only the rate of taxation, but also the degression. So that, for example, during the years 1871-1886,<sup>2</sup> in the first place the rate of taxation fluctuated between eight and two pence to the pound sterling (240 pence), in the second place the degression varied, the full rate during the years 1871-1876 being charged upon incomes down to £300; while all incomes under £300 enjoyed an exemption for an amount equal to £80, and every income under £100 was entirely exempt; whereas during the years 1877-1886 the full rate was charged only on incomes of £400 and upward, all smaller incomes enjoying an exemption equal to £120, and all incomes under £150 being entirely exempt.

In Prussia also both the scale of degression and the rate of taxation is fixed by act of the legislature. The law of May 1, 1851, imposes the full rate of three per cent. on incomes of 1000 thalers and upward; for incomes of less than 1000 thalers the scale of the class tax applies, the tax being graded from .24 to .50 thalers, that is to say from about 2.50 to about .25 per cent. The law of May 25, 1873, adheres to this scale in its essential provisions, defining the rate of taxation for the different classes in percentages, and further increasing the nominal rate of three per cent. in the case of the larger incomes. But the legislation of March 26, 1883, adopts the more flexible principle of a varying degree of exemption, such as we find in the English legislation. Hence we have not only an abolition of the class tax so far as concerns the two lower grades (420-900 marks), together with an accentuation of the degression at its lower limit, but also a

<sup>1</sup> Cf. the text of the law in *Conrad's, Jahrbücher*, 1880, vol. 34, pp. 310 *et seq.*

<sup>2</sup> *Statistical Abstract for the United Kingdom*, 1886, p. 8.

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partial lightening of the burden for the other grades by a remission of monthly installments (three monthly installments in the case of classes 3 to 12 of the class tax, two installments for the first grade of the income tax, one instalment for the second grade of the income tax). - The project which the government submitted to the Chamber of Deputies in November, 1883, went considerably further in the same direction. It retained the rate of three per cent. as a normal rate, but this rate applied only to incomes of 10,000 marks and over; from 1200 to 10,000 marks there is a progression in the rates from one to three per cent.; while all incomes under 1200 marks are exempt. In addition to this there is also a tax on income from capital, of a degressive character, with a normal rate of two per cent., which likewise applies only to incomes of 10,000 marks and over, while from 10,000 to 600 marks there is a degression from two to one-half per cent.; there being no tax on income from capital under 600 marks.

These are a few typical examples of tax legislation, or of projected legislation. In every case the idea of progressive taxation is realized by fixing on a certain point in the size of incomes (property), at which the full rate applies, and upwards from which the rate is maintained unchanged, while downwards from this point exemptions are conceded, which are greater the smaller the income.

Such is the character of degressive taxation.

§ 220. A discussion of progressive taxation would not be complete without taking up the question of what is known latterly in the science and in political practice, by the name of the exempted subsistence minimum.

This term has attracted a degree of attention, not only in social-political (particularly social-democratic) discussion, but even in the science, which lends it an authority analogous to that of the "iron law of wages." And this resemblance is not an external one only. In both cases alike, the older economic theory has not only been undeservedly erected into a canon of

truth, but it has been made use of to serve the very practical purposes of the modern social struggle. In point of fact, the two theories are very intimately connected.<sup>1</sup>

The doctrine of the exemption of the existence minimum has its scientific origin in the doctrine of a net product, which is the basis of the first strictly scientific theory of taxation, viz., that of the Physiocrats. The doctrine of the net product, whether it be taken in its earliest form or as further developed by later schools of economists, particularly by Ricardo and his followers, includes as its logical consequence the exemption of the existence minimum from taxation.

In its advocacy of a rational basis of taxation, and especially in its attempt to guard against the overburdening of the lower classes of the people, this doctrine of the net product finds that the tax-paying capacity consists of the excess of product above cost of production, and it includes under cost of production everything that belongs to the necessary means of subsistence of the laboring population. In this way a line of demarkation is drawn between the necessities of subsistence, which must be satisfied by every individual in the community, and the demands of the state, which are secondary to these, and which presume a tax-paying capacity that can dispose of further means after the necessities of subsistence are satisfied; that is to say, which can afford an outlay for superfluities.

The sympathetic attitude of this theory of taxation towards the people involves an unsympathetic attitude towards the state, such as well suited the political science of the eighteenth century and which would at least be congenial to the state-abhorrent views of the next succeeding generation. But this attitude is not easily to be reconciled with an insistence on the democratic forces which rule the modern state, and which have no sooner succeeded in identifying themselves with the state than they declare, with an injured air, that they are unable to support the burdens of the state.

The inconsistency of this theory of the state and of taxation

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<sup>1</sup> Cf. vol. i. secs. 424-426.

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is not explained away by citing other kinds of burdens borne by the mass of the people, in particular the universal liability to bear arms. For these same modern advocates of democracy and of the existence minimum are very far from accepting the doctrine of a universal military service in any serious sense, as a means of filling up the void in their theory of taxation. It is true they cite the fact of this burden existing in the modern state, but in theory (and in their party programmes) they oppose universal military service, and set up in place of it the idea of a militia, that is to say, the doing away of all military service of a serious character.

§ 221. The men of the epoch of the *Aufklärung* certainly did not look for this development. They had before their eyes the subject masses of the people, and saw them grievously oppressed by the burdens which the ruling classes had shifted to their shoulders. The sombre iniquities of the capitation taxes, the salt taxes, and the like, form the historical background of their theories of taxation. Even Justi<sup>1</sup> is of the opinion that: "In the adjustment of taxes great regard must be had to the poor and the less well-to-do subjects, for it cannot be said that these classes earn anything, since even if they obtain their most pressing necessities and their subsistence, it cannot be asserted that they earn anything as long as they have nothing left over."

The man who comes in as a mediator between the eighteenth century theory of the state and of taxation and nineteenth century radicalism, and for the first time formulates the doctrine of the exemption from taxation of the existence minimum, is Jeremy Bentham. This doctrine was then taken up and carried forward by Bentham's disciple, John Stuart Mill. But Mill, at the same time, condemned the progressive basis of taxation and defended the proportional basis.<sup>2</sup> English legislation has incorporated Bentham's theory in the scheme of its income tax; that is to say, it has incorporated it but to a slight extent, as is evident from

<sup>1</sup> *Staatswirtschaft* (1755), vol. ii. p. 293.

<sup>2</sup> Mill, *Principles of Political Economy*, 1865, book v. chap. 2. sec. 3.

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what has been said above. Under other forms of taxation than that of the income tax British legislation has imposed very heavy taxes on the necessities of life, down to a very late date, and it retains many survivals of the kind to this day. As concerns the income tax, however, incomes under £60 were exempted as early as Pitt's time (1798).<sup>1</sup> And the like was the case at the re-introduction of the income tax in Great Britain, only to a greater degree, as we have seen above.

As happens in Mill and in the English legislation, the existence minimum has frequently been taken up quite after the manner of the old school, at the same time that the principle of a progressive taxation has been rejected. This has by preference taken the practical form of an apparent exemption of the lower classes, together with a less apparent imposition of burdens on the same classes by means of other forms of taxation.

The radicalism of today is not generally satisfied either with the one or with the other. The programmes of social-democracy are in the habit of speaking in a general way of a "heavy progressive tax" (e.g., the *Communist Manifesto* of Karl Marx and Frederick Engels), or of the adoption "of a single progressive income tax for the purposes of State and Commune, to replace all other taxes, particularly the indirect taxes that now burden the people" (the *Gotha Programme*, 1875). For they have all the time been fully aware how this progressive tax would look in case the "elevation of the Proletariat into the ruling class" were to become a fact.

Of national constitutions of a radical character, during the last generation, it is to be noted that the constitution of the French Republic of February 24, 1848, contented itself with abolishing the newspaper stamp, the salt tax, and the octroi, and promising a reform of the other indirect taxes.

The constitution of the canton Zurich, of April 18, 1869, speaks more plainly when it says, among other things, in its "Economic and Fiscal Principles" (Article 19): Small properties belonging to persons incapable of work, as well as "such a

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<sup>1</sup>Rau, *Finanzwissenschaft* (1865), vol. ii, sec. 400.

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portion of every income as is necessary to subsistence, are exempt from taxation." This principle was embodied in the law of March 2, 1870, to the effect (sec. 5) that 500 francs of every income was declared exempt from taxation. At the same time, it is to be added, this law also imposes a so-called "active citizen-tax" (of a very low rate) on all citizens entitled to vote. In the meantime the radical element is making efforts on the one hand to abolish this latter tax, and on the other hand to increase the exempted existence minimum from 500 francs to twice that sum.

§ 222. It follows, from the profound revolution which has taken place in our views of the nature of the state and of the relation of national taxation to the economic powers of the individual citizens, that the view prevalent today favors a policy precisely the opposite of what was once in favor. This, the latest view, condemns the exemption of the existence minimum at the same time that it rejects as untenable the arguments for proportional taxation. It advocates progressive taxation and holds that to be the only tenable position. Plainly, as viewed from the standpoint of the latest theory of the state, there is no room for a doctrine which admits the state and its demands only as second to the necessities of life. The state, above all things, is part of these necessities, and its demands are therefore part and parcel of the demands of subsistence.

The reasons will presently be discussed under the heading of the Objects of Taxation, with reference also to the general discussions contained in Volume I., going to show that from the standpoint of modern political economy, the old doctrine of a net product cannot be maintained. And therewith the doctrine of the subsistence minimum is deprived of its theoretical foundation.

This defect in theory shows itself in every practical application of the erroneous principle. How large, for example, should this subsistence minimum properly be? As we are well aware, it is not a physically necessary minimum. Its limit is a moral

one, and is subject to change during the course of historical development. And on the other hand, the position of the necessities of the state in the scale of the aggregate necessities of a nation is also determined only by moral factors, which vary with time, race, and political constitution.

We are especially bound to enter a protest against that immoral claim which (in strict contradiction of all principles of political ethics) demands for the populace an increasing share of political power together with a progressive exemption from taxation. At this point lies the danger there is in the latest development of the doctrine of an exempted existence minimum. At the same time sufficient provision is made for an adequate exemption of the feebler tax-paying capacities by the policy of progressive taxation.

#### IV. CONFLICTING TAXATION.<sup>1</sup>

§ 223. In the observations we have just been making, we have touched upon things for the understanding of which a previous acquaintance with the chapter discussing the Objects of Taxation would be desirable. At the same time, we have now reached a certain phase of the question of equity in taxation which is touched upon in another of the succeeding chapters, viz., the one on the Practical Administration of the various ramifications of the tax system. It follows from the nature of any subject of an historical kind that the logical sequence of the discussion must always leave this sort of lacunæ, and we will therefore have to content ourselves with a relatively satisfactory arrangement of the material only. Accordingly I believe it will be found desirable to take a survey of the various questions of

<sup>1</sup> Th. Clauss, *Das Reichsgesetz vom 13. Mai, 1870, wegen Beseitigung der Doppelbesteuerung* (*Finanzarchiv*, 1888, 138 et seq.). G. Antoni, *Die Steuersubjekte im Zusammenhalte mit der Durchführung der Allgemeinheit der Besteuerung nach den in Deutschland geltenden Staatsgesetzen* (*Finanzarchiv*, 1888, 916 et seq.). E. Zürcher, *Kritische Darstellung der bundesrechtlichen Praxis betreffend das Verbot der Doppelbesteuerung* (*Gekrönte Preisschrift*) Basel, 1882. F. Schreiber, *Kritische Darstellung ... betr. das Verbot der Doppelbesteuerung* (*Zweite vom schweizerischen Juristenverein gekrönte Preisschrift*), 1882.



equity in taxation in this place, and then deal with the objects and the system of taxation in separate chapters.

The discrimination between the various grounds on which rests the obligation to pay taxes has only lately come forward into the foreground of discussion. The practical occasion of this has been, especially, that it has happened that several public organizations have simultaneously made demands on a single person for the payment of taxes to meet their fiscal necessities, and in so doing, principles of equity have been cited which raised a presumption of relative justice in favor of each requisition.

For example, two different communes may have required payment of a taxpayer, because the taxpayer had his domicile in one of them and carried on his business in the other; or two different states may have made their demands on the taxpayer because he held a landed estate in one of them, while he lived and exercised the rights of citizenship in the other. Hence the necessity of clearing up the question as to what are the ultimate constituent elements of the aggregate liability of the individual to pay taxes. Only in this way is it possible to satisfy the just claims of each of the two states or of the two communes to a portion of the taxes to be paid, and so bring the apparently conflicting rights of the two into harmony.

The number of cases in which doubts of this kind occur has grown with the increasing mobility of modern life, and the voluminous casuistry resulting is a stimulant to the theory of taxation in the same degree as the question is still unsettled in practical legislation - it is in some directions only beginning to be dealt with. It is very difficult to make these salient and re-entrant angles fit together properly, even within the same tax system and under a uniform system of laws, for the unifying idea of an orderly system does not readily penetrate the heterogeneous mass that has resulted from the historical development. But the difficulties become insuperable when we pass beyond the limits of a single state, or of the empire; and attempt to bring entirely different systems of taxation into conformity, systems

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which are not under the control of the same legislative authority, but have to be brought into adjustment by the slow and difficult means of international convention.

§ 224. It is a favorite idea with the social-political radicalism, as well as with that other radicalism whose distant attitude towards the whole subject greatly inclines it to a very simple formula, that an ideal system of taxation should consist of a single tax for both the state and the other public organizations. This idea derives its origin from the earliest school of financial science - that of the Physiocrats, who wished to put the "single direct tax" in the place of all existing taxation. This idea has lived on through a diversity of phases, down to the programmes of the social-democratic party, which insist on a single progressive income tax for national and communal revenue, to replace all other taxes.

It is the office of the exposition of the "system of taxation" to show that and why practical requirements, as well as the principles of equity, require a complex system of different kinds of taxes. The question immediately in hand suggests that an equitable adjustment as between the competing public economies holding claims upon the individual is impossible, except by the help of an analysis of the various relations in which this individual stands to the public bodies in question.

Two kinds of relations, especially, are indicated by the terms "subjective taxes" and "objective taxes," which have lately been made much of, and which direct attention to the contrast that exists in this respect in the case of every industrial individual. If we consider, for example, a landed estate, it appears that the substratum of the estate, the soil, enjoys certain benefits from the state (national, provincial, or communal organization), which benefits come to the land entirely independently of the personal relations and circumstances of the individual who cultivates the land, whether he is owner or tenant, whether he is a good or bad farmer, whether he is in debt or in comfortable pecuniary circumstances, whether his industry is profitable or

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not. Quite independently of all these personal relations of the manager [*Subjekt*] of the estate, benefit accrues to it from the general prosperity of the nation as a whole, and from the expenditures undergone by the state (the empire) for the furtherance of this prosperity; the estate grows in value, or it is preserved from a decline in its value. Through the expenditures of the communal organizations an estate is protected against the ravages of floods without any regard whatever to the personal circumstances of its occupant; by the construction of new roads it is brought nearer to the markets; in case it is sufficiently near an urban center it may even be taken up in the development of the city, thanks to the growing prosperity of the nation and of the neighboring city, and may advance to a high price as building ground. And all this by virtue of changes of an entirely, "objective" character, changes which have a relation to the impersonal factor [*Objekt*] of the rural economy, not to the personal factor [*Subjekt*].

On the other hand it is conceivable that on this same soil, and apart from all changes in the value of the soil of the kind ye have been speaking of, we may find widely varying economic developments due to differences in the personal factor [*Subjekt*], differences in personal efficiency, in pecuniary circumstances, etc. And these differences have to be taken into account if we are to reach an equitable settlement of accounts as between these various persons and the services rendered them by the state. Great exertions on part of the public administration to which these persons belong, and to which their obligation is due, are necessary in order that they may work and enjoy, that they may be able to live as civilized human beings and to rear another generation of such human beings, that they may live in happiness within the circle of their family, as well as in the wider circle of the community as a whole.

§ 225. The contrast spoken of in the preceding paragraph marks only the first and most tangible distinction. Within each of these two groups of relations there are a number of special

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relations of the individual to the public organization, each of which corresponds to some peculiar phase of equity.

The landed estate spoken of above in justice owes some requital to the state and the empire to which its security is due; it owes further compensation to the national or provincial organization which constructs and keeps in repair artificial roads, and thereby increases the marketability and so the value of agricultural produce; it is still further indebted in case it comes to be taken up into the suburban region through the growth of the neighboring city, and so is benefited by the municipal expenditures of the city.

Which of these relations comes in question in any given case, and whether one or more, will have to be decided on a review of the facts of the case.

On the other side, under the head of subjective relations there are likewise a number of different relations to be distinguished from one another. The relations in which the individual stands to the community to which he owes a return may differ in kind, duration and intimacy: The ideal conception of a citizen living and working in a fixed place within a country resolves itself in actuality into the ultimate constituent facts of the totality of existence (and with the increasing mobility of modern life this holds true in an ever increasing degree). Indeed, this ideal is not to be conceived in any other sense than as a pure abstraction. For various reasons it is not the ideal to be desired.

In point of fact, the life of a great many people (for reasons of business, official position, education or health) shifts from place to place and from land to land. The duration of residence in a given place is short or long according to the nature of the object sought: Changes of place are to some extent not confined within the boundaries of a given state or realm, They may include long continued residence in foreign countries, while the relation of citizenship to the individual's original country remains unbroken.

§ 226. This dissolution of the individual personality, on whom the duty of tax-paying rests, as well as of the industrial founda-

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tion of this personality's existence, into a number of constituent elements and relations, will help us to understand the possibility of equitable claims by different co-ordinate bodies upon the same taxpayer. For since the unit itself is resolved into constituent elements, carrying on its business here, having its domicile there, here a citizen, there a consumer of goods, here owning land, there holding office, the aggregate of the returns due from such an individual taxpayer to the various public economies, will also resolve itself into a similar series of constituent parts.

The manner in which these claims have hitherto been adjusted has corresponded to the development of equity in matters of taxation generally. Might was at the outset the decisive fact. This stage of development is represented by certain forms of taxation which do not reach the plane where the question of right or wrong with respect to a particular tax occurs at all. This is the case especially with taxes on consumption, which are imposed on articles of general use. Consider, for example, a large city, which raises the whole or the greater part of its revenue by means of this form of taxation. In such a case the question as to the tax-paying relation of the individual persons to the city does not come up at all, or only in a very subordinate degree. These persons may be living in the city for a shorter or longer time, for business or for amusement, as residents or as transient visitors. Every day, every hour becomes liable to taxation, independent of all such questions, and for all taxpayers alike. Whether it is a city or a state which by preference employs this form of taxation, the consequence is the same, so far as concerns the differentiation of tax liability. The differentiation is absent in both cases.

But while the sentiment of equity as expressed in law is usually very readily aroused against might in times like our own,

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<sup>†</sup>The indirect taxation on consumption resting on the population of Paris amounts (1879) to 68.56 francs per annum (von Reitzenstein, *Conrad's Jahrbücher*, 1884, *N. F.* vol. ix. p. 224), to which is to be added the income from the gas supply and the water rates. The annual expenditure amounts, according to the budget of 1883 (without counting interest on the city debt) to 154,000,000 francs, the receipts from the octroi to 143,000,000.

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this particular manifestation of might is allowed to pass without protest; this happens partly because no form of taxation is so flexible and unobtrusive as this, partly because it would be impracticable to avoid the inequitable taxation in the manner suggested, without drawing an impossible distinction; partly also because the range of taxation of the kind in question does not vary so greatly from country to country and from city to city as to urge the necessity of its abolition. Consumption, however; and with it the tax on consumption, is not incurred in a place where one is not living at the time.

It is otherwise with those forms of taxation which obtrude themselves on the consciousness of the taxpayer by hard and fast demands. The public body which makes such a demand within its own domain, finds itself in controversy as to its rights in the matter with conflicting demands put forth by other similar bodies. The demands of the different communal bodies are reconciled, according to some formulation of the equities of the case, by the sovereign power of the state, the conflict between the individual states by the superior power of the empire; but as between independent states and nations a decision has to be reached by means of international agreements and under the international fiscal law resulting from them.

Such competing demands and such collisions give rise to a good deal of irritation when the rough edges of the tax requisitions of two public bodies come in contact. (It is different with the taxes on consumption, where the form in which the tax is levied itself provides for this difficulty.) As for example, when a citizen of Prussia who is living in England and there becomes liable to pay the English income tax, is at the same time required to pay the Prussian income tax; or where a landed estate is liable to the land tax in the state in which it is situated, and is at the same time subjected to a property tax in another state in which its owner lives; or when something similar takes place in the case of interest on foreign national bonds at the hands of the debtor state and of the home government of the holder of the bonds, etc.

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In such a case the remedy is to be found only in the bold application of principles which belong in the domain of law, and not in that of theory, i. e., if an effort is to be made to satisfy the requirements of equity.

§ 227. Reference may be made to the great number of cases in point and the attempts at their solution by positive law, which have been made by the German and the Swiss federal legislation in endeavoring to avoid double taxation (see the abovementioned works). Neither this subject nor the subject of inter-communal fiscal law, which each state has to settle for itself, nor the conflicting claims of independent sovereign states can be entered on here.

We shall have to content ourselves with a brief survey of a series of cases of practical importance, as enumerated by Adolph Wagner in his *Allgemeine Steuerlehre*,<sup>1</sup> and then add the solution which recommends itself as the most satisfactory one.

1. Subjects of the country living at home may draw an income from abroad. They should pay taxes on this income to their own government in so far as a similar tax of a like degree has not already been paid on it abroad. While the determination of the rate of taxation in such a case is easy, the decision as to the class of the tax in question is very difficult, especially as between two very different systems of taxation: We may look for an approach to a solution of the problem in proportion as advancing science promotes a uniformity of tax legislation.

2. Subjects may live abroad and draw their income from foreign sources. It is a high-wrought conception of the relation of tax liability to citizenship which asserts (as happens, e.g., in the Prussian law of May 1, 1851) that in such a case the full liability to taxation holds. Even in case no tax of a similar character is levied in the foreign country in which the subject lives, while other taxes are required of him in like manner as of all other inhabitants of that country, it is still laying great stress on the bond of citizenship to require the subject to pay the full tax

<sup>1</sup> Secs. 402 et seq., especially 406 et seq. (1. ed.).

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simply on account of this fact of his citizenship. At the same time it is assuredly an open question whether the payment of a certain part of the tax or some peculiar kind of tax is not just and fair. But even this matter would have to be regulated by international agreement. In point of fact, it may be remarked, the practical working of the tax administration mitigates the harshness of a law like that of Prussia.

3. Subjects may live abroad while they draw their income from home. In point of principle the decision in this case would be essentially the same as in the preceding case, so far as it is a question of subjective taxes. It is quite otherwise as regards objective taxation, which belongs where the income affording object is. In the degree to which considerations of this kind may enter into subjective taxation (claims on a pensioner in behalf of the state paying his pension, and the like), the inclination would be to allow full weight to the claims of the home government also as concerns this class of taxation. But it is to be added that where a widespread usage on part of rich subjects to consume abroad their incomes drawn from home is to be combated, the motive of equity will reinforce or traverse the social-political motive, which in such a case is apt to find expression in a very harsh disregard of the hardships of double taxation.

4. Aliens may live within the country, whether for purposes of business or for any other reason. This is the reverse of the last case. Whether employed in business or not, whether a foreigner or a native, anyone that lives within the country should have his taxes like any other denizen, and with just the same reservations as may be conceded to the latter. If it is found best to levy a special tax for the fact of citizenship, then the amount of this special tax might fix the difference in the burden of taxation as between citizens of the country and aliens. The distinction between foreigners engaged in business in the country and foreigners living on an income (such as is made by certain Swiss communes, certain cantons) is very hard to explain from the standpoint of an equitable taxation. It may most



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easily be explained on the principle of the Widening of the Market (vol. i. sec. 399). The object may be to attract customers for the state and communal establishments intended to serve these foreign guests. This distinction may perhaps also be explained as due to the interested motives of the business people of the country who wish to increase the number of consumers, and these consumers are to be allured by a partial exemption from taxation, in order to be all the more thoroughly exploited by the citizens. It is precisely within this field that the system of consumption taxes holds its own, for that system does not stir up controversies of this kind and is therefore, as we might say, practically created to supply the absence of conscious civic duty within this field.

5. Foreigners living abroad may draw an income from sources within the country. In this case the well-known arguments for the objective tax come into play. For sources of income within the country the foreigner should pay taxes the same as a citizen. This position becomes somewhat dubious when the question concerns income from foreign capital loaned to the state levying the tax, i.e., in so-called coupon taxation. In the first place it is doubtful if this kind of a tax is to be considered an objective tax; in the second place, so far as there is not a palpable defect that is to be remedied in the tax system, the tax on interest that is imposed or increased after the loan has been contracted is little else than a reduction of the rate of interest (without the consent of the creditors). While the equity of such a measure is questionable, the expediency of it, especially in the case of a state with a large foreign debt, is very doubtful, and may avenge itself in an impaired national credit.

§ 228. The object of this enumeration of practical cases, such as frequently occur and demand a solution in one country and another at the present stage of social life and international relations, has been to point out a few of the concrete problems of equity that arise between competing public bodies and are to be solved on the basis of a consideration of the nature of taxes.

And herewith we shall have to leave the matter without considering the analogous cases that occur in intercommunal taxation.<sup>1</sup> Cases of this latter class are also more easily remedied - and the remedy has been applied - by uniform general provisions made possible by the subordinate position of the communes relatively to the central authority.

So, also, cases of conflict within the same realm are but examples of the same general principle, except so far as they are modified by the different relations subsisting between the individual states of a federal state, as contrasted with independent sovereign states. As is well known, the legislation of the German Empire and of Switzerland has been quite active in this field and has resulted in a correspondingly large number of legal decisions.

## V. THE JUSTICE OF COMPENSATORY TAXES.<sup>2</sup>

§ 229. Just as the conflict of tax claims between competing public bodies served as an occasioning cause to the investigation of all taxation, so it has latterly happened that a peculiar kind of tax has arrested attention and directed it to a general class of taxes. This particular tax has led an unobtrusive existence, and it is only during these late years that it has attracted a great deal of attention and has found an extended acceptance, through a widespread impression that it is peculiarly equitable. The tax of which I am speaking is the military-service tax [*Wehrsteuer*]. The general class whose chief exemplification this tax is, and to the consideration of which it has afforded the occasion, is the class of Compensatory Taxes (or "special" taxes - as contrasted with "general" taxes).

Taxes of this class have been adopted through a feeling that they are equitable. This feeling has been aroused by the per-

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<sup>1</sup> Cf. *Schriften des Vereins für Sozialpolitik*, vol. xii. *Die Kommunalsteuerfrage. Ten Decisions and Reports*, 1877.

<sup>2</sup> Adolph Wagner, in *Schönberg's Handbuch der politischen Oekonomie*. 2. ed. 1885, vol. iii, pp. 318 *et seq.* F. J. Neumann, *Finanzarchiv*, 1887, pp. 109 *et seq.* G. Cohn, *Volkswirtschaftliche Aufsätze* (1882), pp. 175 *et seq.*; 267 *et seq.*; *Zeitschrift für die gesammte Staatswissenschaft*, 1879, 1881.

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ception that certain persons are not capable of rendering the personal services required by the commonwealth. These personal services may be said to form a parallel series with the taxes, and are levied on the citizens in proportion to their capacity to render such services. Where this capacity is absent, it being impossible to levy such services, a defect in the equity of distribution of public burdens arises, favoring the part of the population not capable of performing such services; this defect must accordingly be covered by the requirement of a material contribution (taxes) which shall draw on the economic capacities instead of the (missing) personal capacity.

Although the principle which comes into view at this point has been much disputed, it seems to be making its way and to be gaining ground both in practical life and in the science. It is the office of the science to develop the vague sentiment of a new tendency in the growth of equity to an ever increasing certainty and consistency; to clear up the foundations of this sentiment; to ascertain the value of doubts and objections; and so bring the unmistakable trend of legislation in the large modern states into closer and firmer relation to the foundation of all taxation and of all equity.

§ 230. The sentiment of the new epoch at this point again demands a new sort of equity (perhaps, rather, it is but an old idea that is brought up from the forgotten past and applied to institutions already established). But if this is so, it is necessary at the outset to meet a certain objection, superficial but widely accepted.

It is asserted that there is at this point no real occasion for demanding an equalization of the public burden, and that the whole agitation is but a new example of the mistaken efforts of the French leveling system. It is not rational equality of taxation that is aimed at, but the unreasonable *égalité* whose dangers the world learned by the French Revolution.

This objection is very effective with an audience of the right kind. Science, that is to say, thinking that is not hampered by

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national antipathies, is unable to discover the alleged contrast between "German" and "French" equality. But it does appreciate the imperishable services which the French nation has rendered, towards the development of the great concepts of equity and equality in taxation, and in political affairs generally, and also that Germany would in all probability not yet have reached the stage of development in the concept and practical application of equity at which it now stands, except for these services.

So far as regards taxation in particular, France is not to be censured for having pushed equity and equality too far, but rather for not having gone far enough in this direction, so that there is still much left undone before the demands of the science are satisfied. But if any blunders have been made, in the direction of an exaggerated equality either in practical affairs or in theoretical speculation, it is unbecoming to lay the blame of the mistake on a single country or a single nation. Rather, every country and every nation should do what it can towards remedying its own errors. And the question as to where such errors occur is not a question of geographical or national boundaries, but is to be solved by dispassionate argument and discussion.

As regards the particular matter under discussion, it is the German-Swiss who have gone farthest in the direction of the new equality, both in thought and action. And their example has been the occasion of the Austrian legislation, has called forth a project for similar legislation in the German Federal Council, and has provoked like efforts in Italy, without having come to anything more in France (apart from the abortive efforts of the Napoleonic era) than that a project has tardily been put forward, modeled on the projects and laws of these other countries.

§ 231. We already know that the aggregate of what the individual citizen contributes to the state (in its various gradations) falls into two great groups, personal services and material contributions.

These personal services are of just as indefinite and problematical a nature as the material contributions are simple and definite. These latter differ only in form, to the extent that they may be contributions in kind or in money. The personal services, on the other hand, are based on a medley of psychical factors, ranging from the very highest motives of civic virtue to the meanest calculations of pecuniary greed. In the case of a material contribution (taxes), we have the unquestioned definiteness of economic value; in the case of the personal services we have an uncertain fluctuation between the high motives of loyalty, honor, duty, on the one side and the grievous burden of labor on the other.

Wherever we look, this contrast faces us. It is most strongly marked where the political system comprises a highly differentiated, highly civilized social life, which is struggling to realize the exalted ideals of free political life and self-government, in the midst of the difficulties inherent in such a situation. From a very early day the contrast between *honores* and *munera* was marked in the Roman state. The former term was used as quite synonymous with *magistratus* and was employed in speaking of the higher offices, the honor attaching to which affords a contrast to the burdensome character of the *munera*. The fundamental signification of the word *munus* is apparently: to work at compulsory labor [*schanzen, frohnen*].<sup>1</sup> This word properly denotes those required services which were considered the burden of citizenship. They are to be classed with the simple economic burdens, the taxes; that the taxes were classed with the *matyzera* is evident from the fact that exemption from taxation is termed *immunitas*.

We find something quite analogous, though without the contrast in the official titles, in the multitude of personal services required by the modern state. Here too there is a relatively small number of *honores* contrasted with a great mass of services that are appreciably burdensome. And the contradiction which the latter class involves is heightened by the fact that, at the present

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<sup>1</sup>Mommsen, *Römisches Staatsrecht* (1887), vol. iii. pp. 224 *et seq.*

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stage of industrial development, they are no longer to be called statute labor [*frohndienst*], but are to be considered as honorary burdens, however grievous they may be in reality, and however little the honor involved may appeal to the consciousness of the majority of the persons liable to them. And what makes the matter still worse, even in those infrequent cases where the consciousness of the honor is present, the pecuniary circumstances of the persons liable to render these services are not such that they can unreservedly yield to the sentiment. The pressure of their necessities keeps them in mind of their pecuniary inability, which makes it necessary to obtain some compensation in pecuniary means as an indispensable condition to devoting their life to the service of the state.

§ 232. A not altogether definitive mark, but still for the most part a characteristic feature of the "burden" in public contributions, is public compulsion. The presence of compulsion implies that the burden involved in the required contribution, the abstinence, the sacrifice, the trouble, are so great as to deter from the voluntary performance of the duty, at the same time that the sense of honor, and the like, is not so great as to incite to its performance.

Compulsion, according to the letter of modern legislation, now applies high up in the grades of honorary offices. The state is not satisfied with using compulsion to enforce payment of taxes, military service, and the like; it also, for example in the latest legislation concerning self-government, prescribes penalties for anyone declining an election to an honorary office. The Prussian Act regulating, Towns<sup>1</sup> says (sec. 74): Every citizen entitled to vote is bound to accept an unsalaried position in the communal administration or in the communal representation, and to perform the duties of the office accepted for at least three years; in order to decline or to resign such an office, none but the following reasons are sufficient for an excuse: (a) con-

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<sup>1</sup> In its latest development and extension, the Prussian legislation on self-government coincides with the above, with only inconsiderable exceptions; as, for example, the district regulations for the province of Hanover of May 6, 1884 (sec. 8).

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tinued illness, (b) business which requires frequent or long continued absence, (c) an age of over sixty years, (d) the administration of an unpaid office during the previous three years, (e) the administration of another public office, (f) medical or dental practice, (g) other peculiar circumstances which in the opinion of the municipal council constitute a sufficient excuse; whoever, except for some one of these reasons, refuses to accept an unpaid office, either in the communal administration or the commune representation, or to continue in the duties of an office until the expiration of three years, as also anyone who, in point of fact, evades the performance of the duties of such office, may, by resolution of the municipal council, be declared to have forfeited his rights as a citizen, for a period of from three to six years, and be assessed at a higher rate for the direct communal taxes, by an addition of from one-eighth to one-fourth.<sup>1</sup>

That this is not simply a question of good will, but that pecuniary embarrassment may stand in the way of the performance of the duties of an honorary office, may be inferred from the fact that there have, in recent years, been organized associations for mutual support of jurymen, which pay a daily allowance to citizens that are drawn on the jury, in consideration of an annual membership fee. It appears then that the honorary office, on account of the pecuniary detriment to the citizen's ordinary occupation, is regarded as a mishap, against which an insurance association is organized among those threatened by this class of disasters.

But if this holds true with respect to offices which are relatively so slightly burdensome, and so distinctly honorary, how much more will it be true of the heaviest of the citizen's duties - the universal military service - where the question concerns first the years of military drill, and then, further and especially, the onerous burden of a campaign (or even of a mobilization) for the man of maturer years who is enrolled in the reserve, the *Landwehr*, etc.

<sup>1</sup> Von Rönne, *Das Staatsrecht der preussischen Monarchie* (3<sup>d</sup> ed.) sec. 345.

<sup>2</sup> There is, e.g., such an association in Einbeck, which guarantees a daily allowance of 6 marks in return for an annual contribution of 3 marks.

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There is nothing whatever derogatory to the honorable character of these civic duties in pointing out the palpable facts of the case and computing the weight of these burdens in adequate, that is to say pecuniary, terms.

§ 233. The claim is made under the general rule of universal military service that equity demands that the large number of male inhabitants of a country who are exempt from military service on account of some physical defect should be required to assume some compensating burden of a pecuniary kind in return for this exemption. And in point of fact, this demand falls in with a sense of fairness which is traceable in history for a long time past.

The most obvious method of compensation would be by a personal service of another but equally onerous kind. But as this would be practicable only for a small portion of all the people exempted from military service (sick-nursing or the like), there apparently remains no other method than that of a compensatory tax.

This is a repetition under our political system of what was always present in an analogous form in the differently constituted systems of earlier times. At that time the question concerned the division of labor between classes - between those who rendered personal service to the state and those who paid taxes, or it concerned the shifting of the whole political system from the direct participation of the body of citizens to management by a professional civil service. In France, for example, the *taille* was originally a tax paid by those liable to military service, by which the king obtained the means for hiring mercenaries.<sup>1</sup> Similarly Gneist finds that the English communal taxes originated in a "commutation of court, police and military services required by the larger or the smaller civil division as the case might be."<sup>2</sup> Or it might be the ransom of a wealthy man who furnished and paid for a substitute in his own stead.

<sup>1</sup> Tocqueville, *L'ancien régime*, p. 212.

<sup>2</sup> *Geschichte der englischen Communalverfassung* (1863), vol. i. p. 188.



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The modern State with its universal military service is past the stage of class contrast, past the system of mercenaries, that is to say of pure division of labor in military matters, and is also past the stage of a social contrast between the wealthy who are exempt from military service, and the poor who are required to bear arms. The modern State has outlived the one-sidedness of these distinctions but has retained and further developed the demand of equity which they contain.

Every citizen is today liable to bear arms without distinction of rank or of wealth, and with only a relatively slight recognition of the need of division of labor in the work of the State. Under this rule of generality and equality of military service, the only distinctions made are such as depend on capacity for the duties required. In the upper grades it is a question of differentiation in training with a view to the demand for officers; in the lower grades it is a question of physical powers, considered in the light of the necessary qualifications in point of health.

There is no reason why the purified sense of justice in political life which characterizes an advanced century, as contrasted with earlier times, should not be as watchful of the inequalities that occur in the performance of duty today, as those earlier epochs were for their part.

§ 234. The compensatory tax for military duty is the chief example of this class of taxes. But it is by no means the only one.

The same relation of equity recurs wherever there is a commutation of personal service due to the commonwealth, if it is not of a general character, based on a division of labor, but takes place only by way of exception for such persons as are for special reasons unable to render the personal service. The fire-brigade service required of the citizens of a municipality has, for the most part (for reasons of technical efficiency), given place to the professional trained fire-brigade and so has given rise to the payment of a general tax in place of personal participation by the citizen in extinguishing fires. But where this change has

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not taken place, justice obviously requires the imposition of a compensatory tax on those citizens of the municipality who are prevented, by reasons of health and the like, from rendering the personal service. So, e.g., the Wurtemberg law of June 6, 1885, enacts that all male inhabitants of a commune, between eighteen and fifty years of age, may be required, by resolution of the communal board, to pay an annual tax of from 1 to 10 marks towards the expenses of the fire department, in case they do not serve in the fire-brigade. In the canton of Baselstadt<sup>1</sup> the fire-brigade tax and the so-called safety fee [*Sicherheitsgebühr*] show plainly a development from a compensatory tax to a simple income tax, similar to the Swiss legislation on the military-service-compensation tax.

Any difference which may exist between these lesser civic duties and the military duty does not touch the essence of the question in hand. So, while the requirement of military duty does not permit its rule of universality to be affected by considerations of the wealth of any citizen, but is, for good reason, unwilling to exempt the better, more cultured and wealthier classes of the people, or to leave it to their choice whether they will serve or pay, the legal compulsion attaching to a duty like the fire service is of a more complaisant kind, and may easily permit a social differentiation in the manner of performing the duty whereby it comes about that the wealthy pay and the poorer classes serve. The latter tax therefore occupies a stage in the development which the modern military system has outlived. For the purposes of the argument, however, this difference is not of much consequence; the equity of the arrangement is only more palpable in the latter case than in the former.

§ 235. This difference becomes important when we come to discuss the principle which is to regulate the rate of the compensatory tax. In case of the mere payment of a substitute, such as characterized the French and South German systems down to

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<sup>1</sup> *Rathschlag des Regierungsraths von Baselstadt betreffend die direkten Steuern* (1879), pp. 66, 89-90.

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1866, the rate is measured by the price of the substitute. On the other hand, a universally incumbent duty of citizenship which every individual is required to perform according to his personal capacity, and whose dignity and political significance do not admit of its being compounded for by anyone that prefers to make a money payment, - the equivalent for a duty of this character must be adjusted on the same basis on which all public duty rests, viz., the solidarity of every individual with the community and the consequent equal obligation of every individual to serve the community according to his ability.

But wherever personal capacity fails pecuniary capacity takes its place; pecuniary ability is the proper substitute for personal capacity.

In the services required under self-government, as in distinguishing between the qualifications for justice of the peace and jury service, or between those of the foreman of the jury and jurymen, etc.; or in military service, as in choosing between the better educated, the half-educated, and those having an elementary education only, for service as officers, subalterns, corporals, etc., or in choosing mechanics, surgeons' assistants and the like, - the decisive fact within the field of personal services required for the state is invariably the capacity for the service. It is the same principle that demands recognition in taxation generally, in the compensatory tax as well as elsewhere.

It is therefore not by accident that the legislation of Switzerland on the military-service-compensation tax has continually been assimilated more and more to the Swiss property and income taxes. It is only that the logical consequence of the idea of the compensation tax is finding expression.<sup>1</sup>

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<sup>1</sup> Cf. the federal law on the military-compensation tax of June 28, 1878. - *Zeitschrift für die gesammte Staatswissenschaft*, 1879, p. 535.

## CHAPTER II. THE OBJECTS OF WHICH TAXES ARE LAID.

LITERATURE. F. B. W. Hermann, *Staatswirtschaftliche Untersuchungen* (1832), pp. 297-326. G. Schmoller, *Zeitschrift für die gesammte Staatswissenschaft* (1863), pp. 1 *et seq.* C. von Hock, *Die öffentlichen Abgaben und Schulden* (1863), secs. 15-17. A. Wagner, *Finanzwissenschaft*, vol. ii. (1880), secs. 369-395. A. Schäffle, *Die Grundsätze der Steuerpolitik* (1880), pp. 54-198. G. Schanz, *Jahrbuch für Gesetzgebung, Verwaltung und Volkswirtschaft im deutschen Reich* (1882), pp. 563 *et seq.* J. Kaizl, *Die Lehre von der Ueberwälzung der Steuern* (1882). G. von Falck, *Kritische Entwicklung der Lehre von der Steuerüberwälzung seit Adam Smith* (1882).

### I. THE SOURCES OF TAXES AND THE OBJECTS OF TAXATION.

§ 236. The material substratum of the whole discussion of Chapter I., dealing with equity in taxation, is the economic substance which constitutes the objects of taxation. The purpose of the present chapter is to examine the nature of this substance. What is the source from which taxes flow? What is the economic force which is continually restored after having yielded the taxes, like the fountain which fills the broad river bed constantly without being exhausted?

It follows as a matter of course that every rational discussion of taxation has had to deal with this question from finding itself face to face with a crude empiricism that took the taxes "Where it could find them," and that by so doing had conjured up consequences that had to be met by seriously taking thought. In fact, it is this question which forms the foundation and the corner-stone of the first scientific system of political economy and financial theory. The Physiocratic theory of the net product (*produit net, revenu net*) of industry is an attempt to answer this question.

Cameral Science, even at the stage which Justi had reached, contains no discussion of precisely this question. This writer is of opinion<sup>1</sup> that the contributions of the subjects to the great expenditures of the state should be taken from what property they have immediately at hand ["*aus ihrem bereitesten Vermögen*"]; except in cases of great need or misfortune, the state should demand no more than a portion of the income or produce of the property; a fourth or a third of the income or of the earnings is about as much as the subjects can afford in times of peace; for if higher taxes were to be levied, a part of the people would suffer for the want of the necessary means of subsistence, and another part would have to cut into the substance of their property; and such management could not possibly go on forever, but would shortly result in the downfall of the state. For meeting extraordinary emergencies, however, Justi pronounces for the unlimited tax-liability of subjects; he even lays stress on it. To meet a growing fiscal need in ordinary times he advises the development of the industry and income of the subjects; he, as is well known, regards Colbert as the greatest of finance ministers, in that, like the true Cameralist that he was, he sought to develop the country and to enrich it with commerce and manufactures in order to enable it to bear an increased burden of taxation.<sup>2</sup>

The most prominent precursor of the Physiocrats in France, Boisguillebert, who had nothing to do with strenuous abstract thinking, speaks to much the same effect. He regards *revenu* and *consommation* as equivalent concepts.<sup>3</sup> This is much truer to life than later systematic writers and logicians from Quesnay to Ricardo and John Stuart Mill. But however unsatisfactory the abstract notion of the net product and net income may seem to us today, it was indispensable at an intermediate stage of scientific thought, whose earliest stage becomes intelligible to us on reading these pioneers.

§ 237. In Rau's *Finanzwissenschaft*<sup>4</sup> there is a terminological

<sup>1</sup> *Staatswirtschaft*, vol. i. secs. 401 *et seq.*

<sup>2</sup> *Ibid.*, sec. xii.

<sup>3</sup> *Zeitschrift für die ges. Staatswissenschaft* (1869), p. 406.

<sup>4</sup> Secs. 254 *et seq.* (5<sup>th</sup> ed. 1864).

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discussion on the distinction between tax-object and tax-source. The former is the object with reference to which the tax-liability of each taxpayer is rated. On the other hand, the property from which taxes are drawn (in the sense that it suffers a diminution through payment of the taxes is called the Source of Taxes.

The problem of scientific discussion has evidently been to penetrate from the Objects to the Sources of taxes; much as the problem of economic speculation has been to penetrate from the material objects constituting wealth to the sources of wealth. Taxes were laid on land and houses, on articles of food and drink, on superfluous and on indispensable articles of daily consumption; there were also taxes on persons, income, property, inheritances, etc. These were all objects of taxation. Naturally it became necessary to find out what it was that lay concealed behind these objects as the source of supply of taxes, in order to meet the requirements of equity in taxation, in order that every person liable for taxes might be assessed with proper regard to his ability to pay, both in itself considered and relatively to the ability of other taxpayers.

Our scheme, which places the various demands of the public economy in immediate relation to the aggregate demands of the nation's industry and of individual establishments, which regards the public demands as but a portion of the aggregate demand of the people in another form, and to be met by different organs - to be fitted into its proper place in the scale of needs, like every other human need; - our scheme places the problem on the common ground of all economic science. The source of taxes is to be found nowhere else than where the means of satisfying all wants are drawn from.

But all wants which recur from year to year and from day to day presuppose as a condition to their satisfaction sources which likewise constantly renew themselves. This supply can only be the result of production, which is placed at the disposal of these demands in the form of income. It is income, therefore, which constitutes the normal source of taxes.

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In the life of the individual there are conceivable extraordinary cases where the demands of the occasion exceed the means at hand, and which must be met by drawing on means which are not of the nature of income. In such cases expenditure must exceed income, because there are human interests whose importance outweighs any pecuniary consideration. In like manner there are extraordinary occasions in the life of the state when these limits are exceeded and the tax demand falls on what does not by nature bear the stamp of renewal; that is to say, on property.

Property is by nature the trunk which annually bears the fruits that may be disposed of to meet expenses. Income represents these fruits. If the tree were destroyed by repeated depredations the fruits would also cease. Accordingly, realized property cannot be drawn on for regular expenses, but only for extraordinary occasions. But this latter may be done with less risk to the national well-being as well as to the permanent taxpaying capacity of the nation, the more productive the industry of the time is, and the sooner, consequently, the new products of industry will avail to make good the inroads on the national wealth.

§ 238. To a superficial glance it would appear that the taxation of wealth (instead of income alone) in practice extends beyond the extraordinary emergencies spoken of. But there are a number of things to be taken into consideration in this connection. It is, first of all, the long and well-known "property tax" which gives this impression. But in point of fact, the property taxed is only the object on which the tax is imposed, not the source from which it is drawn. The tax is proportioned to the property, but it is intended to reach as its source of supply the income derived from the property. It is at the most in exceptional cases only that the property tax aims to reach the property itself as a source of supply.

This suggests the distinction introduced by Adolph Wagner between the "nominal" property tax (in which the property is

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only the taxable object), and the "real" property-tax (in which the property is also the source from which the tax is drawn).

But in the second place, in cases where the property is the source of the tax, where we consequently have to do with a real property tax, it is necessary to bear in mind the distinction between what is property to the individual and what is property from the standpoint of the nation. Evidently; as viewed from the national standpoint the aggregate wealth is not diminished by the state's confiscating all that is coming to its creditors living within the country, whereas the property of the individuals whom this confiscation touches will suffer very appreciably. It is simply a case of the shifting of ownership, a change in the distribution of the national wealth. The case is quite similar when the state appropriates certain items of wealth by means of a real property tax in order to invest them for national industrial purposes. Supposing the investment to be worth what it cost, we have here again to do with a redistribution of property, a change of ownership.

Now, there are a great many purposes for which the state may make such investments of capital. All productive investments (productive in the true sense and not only in the sense of yielding a revenue) which the state or the commune may make, belong in this category: railways, harbor improvements, mines forests, agricultural land, gas and water works, etc. A heavy tax imposed on property as the source of the tax may, moreover, have the indirect and less obvious result that greater saving will be effected in the less well-to-do households because of the reduced tax burden required of them; so that as much property would be laid up, by these as the state appropriates from the upper strata by means of the tax.

§ 239. Real property taxes, even in the sense last referred to, are not frequently met with in existing taxation. One of the chief examples of this kind of taxes, and also a very widely prevalent one, is the inheritance tax. These taxes, especially in



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the case of the remoter degrees of kinship<sup>1</sup>, as a rule take so large a sum from the total of the inherited property as to leave no doubt but that they are real property taxes. The strongly progressive rate of the inheritance taxes, increasing with the degree of remoteness of kinship (beginning with a minimum, or with zero, and rising to 8 or 10 per cent. and even more), goes to prove that the occasion of the tax lies in the peculiar circumstances connected with this transfer of property. The increase of the rate in proportion as a greater element of chance has conspired to transmit the property to the particular heir in question suggests the logical consequence of the eminent right of the state to ownerless goods. It is also evident that the present stage of development of this class of taxes is not the final one, probably it is rather the beginning of a very large development of public inroads on egoism. And this is true as well in respect of the rate of the tax as in respect of the possible multiplication of taxes of an analogous kind. Such a tax, even as we find it today, is of course hard to reconcile with any theory which condemns the taxation of property as a source of the tax payment, either altogether or at any rate under ordinary circumstances. The justification offered for the inheritance tax, as being a supplementary tax added to the annual income tax at a favorable moment, is not consistent with the fact that this supplementary tax is made to depend on the degree of kinship of the heir. It is, in fact, a real property tax. Nominal property taxes have been in use for a very long time. The term has frequently been used to designate taxes which are not even assessed in proportion to property, The well-known English "Property and Income Tax" which the younger Pitt introduced in December, 1798, was from the outset, and still remains, as he expresses it, an indiscriminate "general tax on all the chief branches of income."<sup>2</sup>

<sup>1</sup> In Prussia 8 per cent., in Baden 10 per cent., in Wurtemberg, Bavaria, Saxony, Oldenburg, Hesse, 8 per cent. - *Finanzarchiv*, 1885, pp. 296 *et seq.*

<sup>2</sup> *The Speeches of the Right Honorable William Pitt in the House of Commons* (2<sup>d</sup> ed. 1808), vol. ii. p. 432.

Pitt expressly declined to make any distinction between income from property and personal income<sup>1</sup> - for reasons, it is true, that do not appear to be sound. He claimed that the property whose continued existence was urged as a reason for taxing it at a higher rate, is already taxed more heavily in that it continues to pay the tax as long as it may be required, whereas the income from labor ceases when life ceases and is therefore taxed but once; the safest way is, moreover, to accept the inequalities which are the lot of man and which financial legislation neither ought to nor can improve upon.<sup>2</sup>

It is otherwise with the property taxes so widely employed today in the Swiss cantons, especially for the communal finances. We have here to do with a class of cases in which not only is the property the object of the tax, but in which the purpose of making this the basis of apportionment and object of taxation (as contrasted with the income tax in the narrower sense) makes itself very sensibly felt. In the canton Zurich, for example, the entire communal revenue, apart from a slight capitation and house tax, is raised by a property tax; while for the purposes of the cantonal revenue a discrimination is made between the "income-cadaster" and the "property-cadaster," in such a way as to afford a much greater degree of exemption to the smaller and medium personal incomes than to the corresponding class of incomes from property. This contrast is visible even in the early taxation of the mediæval cities. We find the guild masters of Duderstadt in the year 1438 demanding that, in the assessment of the scot, *Erbe und Gut* were to be taxed at a higher rate than receipts from the handicrafts.<sup>3</sup> And the justice of this discrimination seems

<sup>1</sup> Speech of December 14, 1798. (Speeches, vol. iii, p. 13.)

<sup>2</sup> Sinclair objected to Pitt's argument of Dec. 14, 1798, against treating personal income and the income from property alike. In his speech (which opposes the whole of Pitt's project) he says: "Indeed, how is it possible to require the same rate of taxes from two persons one of whom has an income without capital, and the other of whom has an income and capital in addition? How can we require a barrister with, £600 yearly income, and an annuitant with a capital of £20,000 bearing interest at 3 per cent., to pay the same amount of income tax?" - Sinclair, *History of the Public Revenue*, vol. ii. p. 237.

<sup>3</sup> Jaeger, *Duderstadt* (1886), pp. 42 et seq.

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at the present day to be constantly gaining a wider recognition. For objections of the kind urged by Pitt are scarcely to be taken seriously, and weightier objections would be hard to find.

After it has been agreed that ability to pay the taxes is to constitute a chief principle, or the chief principle governing the rate of taxation, it will also have to be admitted that an income which is drawn from property should be taxed at a higher rate than a personal income, if it can only be shown that the income from property is more certain and enduring, and therefore possesses a greater ability to pay taxes, than does the personal income.

§ 241. It is to be remarked that the effect of a heavier taxation of an income from property (funded income) could be produced without the form of a property tax. The Prussian government, for example, has in fact made repeated attempts to impose a heavier tax on funded income under the form of an income tax.<sup>1</sup> It was attempted in the first project, which was laid before the United Diet in the year 1847; and again in the year 1883, in the attempted reform which was to have included among other things a tax on income from capital, in addition to the already existing tax on income.

It is to be added that the older methods of tax management from which the old property taxes have been handed down, are in great part adapted to so low a stage of development that the precedent is by no means to be accepted as authoritative under modern circumstances. In point of fact, property taxes have to a good extent been the *pons asinorum* to the undeveloped understanding of the nature of income. Undoubtedly it is "income" (as the term is understood by German Political Economy since F. B. W. Hermann's time) that the owner of a house gets from his dwelling, that the owner of a park gets in the enjoyment of his park, that another man gets from his game preserve or from his picture gallery. It is income consumed in kind. It is only

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<sup>1</sup>Kries said (*Zeitschrift für die ges. Staatswissenschaft*, 1855, p. 371) that this is "an idea which we must declare to be as unjustifiable as it is impracticable."

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a little less palpable than the fruit which a landowner harvests from his garden; it surely answers less precisely to our ideas of the income usually obtained in modern industrial society, with its division of labor and its system of money payments; but it is income none the less.

The fact that our tax system is constructed with a regard to the use of money, and that therefore all items of income which are not primarily expressed in terms of money have to be translated into such terms, that is to say, have to be assessed, - this fact does not change the essential nature of the case. Whether the picture gallery as such is rated, or whether the rating takes place at a step farther on under the form of an estimated yearly dividend, amounts to the same thing. If it is not to be decided by an appraisal it will have to be decided beforehand by the law, that is, under the form of a "nominal" property tax by which some rate of interest is adopted as expressing the relation between the property cadaster and the personal income cadaster.

§ 242. Our taxation has today, for the most part, not attained to such a logical consistency, the reason being that we are in practice, not in theory, still bound by the prejudices which scientific discussion has long since put away, as well as that a widely prevalent reluctance honorably to perform our duty in the matter of tax payment hinders our seeing things in their true relations. From this cause there are several questions that require our attention.

It is objected that no tax, and certainly no special tax, should be levied on such property as either cannot, or at any rate actually does not, yield a money income; that such a tax may easily tend to become, and may even set out with being, a "real" property tax.

This is an error. Whether the tax brings the fact into consciousness or not, the fact at any rate remains that a park, a game preserve, a picture gallery, a library and the like represent, so far as concerns annual income and annual expenditure, a sum corresponding to the annual interest on their capitalized

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value. If the taxation of objects of this kind causes a disturbance in the pecuniary circumstances of the taxpayer in question, that is simply an indication of an abnormal development of consumption on his part. If the possessor of a collection, etc., which costs millions does not know, until the tax amounting to some thousand marks makes him aware of it, that he is indulging himself in a gratification that exceeds his pecuniary strength, that he does not possess the means necessary to retain so expensive an object in his possession and use, then this method of affording him practical instruction is but one of the possible ways in which a remedy may be applied to the abnormal growth of his consumption, It may just as easily happen, without the tax, that the dilapidation of his house or the wretched state of some other portion of his necessities, will bring him to appreciate the fact and to reduce the extent of his collection. Lord Shaftesbury, when he succeeded to his father's estate in the year 1851, sold a portion of the paintings inherited in order to provide better dwellings for the people on the estate.

But why this solicitude with regard to the demands of the state and the commune? We are here again brought face to face with the well-known attitude which people assume towards these demands. If we only had thoroughly assimilated the fact that the state belongs among the prime elements of the necessities of daily life for every civilized human being, then we should be less given to sentimental talk about the possible chance of this fundamental necessity trenching in some slight degree on some people's superfluities or luxuries. If it happens that the tax requirement compels a taxpayer to give up a dozen pictures or a portion of his game preserve, it is only that the less serious need gives way to the more serious.

It is a gravely significant fact that in countries where this line of argument has been embodied in legislation the execution of the law at this point is extremely lenient.

§ 243. There is a further point closely connected with the last mentioned. There are circumstances, seasons, crises in which

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the income from productive property ceases. This is a different case from that dealt with in the last section. There the question concerned useful possessions [*Gebrauchsvermögen*] whose income yielding character was not understood, owing to the undeveloped state of the concept of income. Here we have to do with productive property, which for the time, and by exception, owing to disturbing circumstances, affords no product and consequently yields no income. The North German agriculture during the twenties of this century, modern industry with its varying gains and losses, with its alternation of inflation and crisis, every speculative enterprise, afford examples of seasons during which the income-bearing capacity of capital fails.

In this class of cases also there seems to be a reasonable ground of argument against the taxation of the income, or at any rate, there seems to be a defect in the system whose aim is to make the income the regular and permanent basis of taxation.

But still, we have to do with a confusion of the same kind here as in the class of cases previously discussed. If we have once thoroughly convinced ourselves that the demands of the commonwealth are made for purposes of fundamental importance to the well-being of all civilized men, we shall also understand that in years when the productivity of the property in question fails, it is no less admissible to draw on capital for the necessities of the state than for the other necessities of the taxpayer. It is not a case of an external power intruding with alien demands on what, by good right, belongs to the private wants of the individual.

It may be conceded that the case is an abnormal one; it may be accepted as a matter of course that the assessment of the tax should be different from what it would be in a productive year.

But the principle is not to be given up. If the principle were surrendered we should logically reach the conclusion that the least of the workmen in such a factory, or the like, must be considered capable of paying taxes seeing that he possesses an income, while the wealthy, possibly very rich, employer should be exempted. It would be preferable, if it were possible, to find

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a reliable average of the annual produce and then base the income tax on this average. But that is not practicable. Even the longest periods which intervene between one valuation of income and the next are much shorter than the periods in which the great fluctuations and cycles in industry, agriculture, etc., run their course.

The difficulty arising out of the non-use of useful possessions is not a serious one. In case a rich man (a man of small means is not exposed to the temptation) lets his parks, collections and the like - objects that may have a value of several thousands or millions-lie idle, the tax legislator who imposes a tax proportioned to the average normal income has simply to tell him: "*habeas tibi.*" We have here to do with an abnormality resulting in an unreasonable luxury, or one required by social rank, of which, for this very reason, legislation can take no cognizance whatever. One must either make some use of one's use-property [*Gebrauchsvermögen*] or resign the possession of it.

But least of all can there be any question as to the taxation of wealth which is for speculative purposes temporarily withheld from productive employment or prevented from affording its normal product. The best example of this class is building-lots in towns, and especially in large cities - property, frequently of considerable value, which simulates an arcadian existence under the innocent guise of a potato patch, the pretense being taken seriously by an undeveloped tax legislation (Prussia), or treated with considerate indulgence by the owner's honest friend and neighbor who assesses the property (Switzerland).

Equity and the logic of the case here demand an adequate appraisal of the market value of the property and a taxation on the basis of the average income from a capital of like value.

The tax in such cases of suppressed income both in regard to use-property and in regard to productive property has the secondary but important function of reminding the owner of the duties towards the community attaching to ownership. The pressure of the tax urges to a management more in accord with public utility. It may be that it disturbs the indolence which

has permitted valuable property to lie unused, or it may serve to discourage the obstinate disregard of the public interest which withholds large areas from present use.

§ 244. In the foregoing I have been at pains to explain what is meant by the term "property tax" and to point out how far it is apparently or actually associated with the real taxation of property. Likewise there is something further to be said with regard to the term "income tax" and its connection with the taxation of income as source of the tax. In the case of the latest project of the French government for the adoption of an income tax (which is now to be adopted again, after so many futile efforts<sup>1</sup>) the bourgeoisie, still influential in spite of all the democratic institutions, offers its customary resistance and makes use of the argument, among others, that the taxes already in force are every one of them taxes on income.

This is an instance of a confusion with which we are already familiar, the confusion of the tax-source with the tax-object.

The "income tax" is one of many forms of taxation of income. While all these various forms of taxes presuppose income as the source of the tax, the "income tax" is that particular form which not only presupposes the income as the tax-source, but also makes it the tax-object, that is, makes it the basis of the distribution of the tax.

It is therefore no objection to the introduction or retention of an "income tax" that all other taxes also draw on income as their source. The "income tax," in proportioning the tax according to the income, is laid with special purposes in view, which cannot be accomplished by the other taxes. These purposes may be distasteful to certain classes of society, but precisely this fact is a proof of their desirability. To go into the details of this matter, however, belongs to the discussion of the System of Taxation.

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<sup>1</sup> Bill introduced by the Minister of Finance, Peytral, Oct. 30, 1888, printed, with comments, in the *Journal des Économistes*, Nov. 1888, pp. 312 *et seq.* Cf. the objections offered by A. Neymark in his journal, *Le Rentier*.



## II. THE SHIFTING OF TAXATION.

§ 245. The connection between the tax-object, on which the tax is levied, and the tax-source which the law is intended to reach is, under the circumstances of modern industrial life, a problematical one.

In a consistent socialistic organization of society in which there were no free exchange of the products of private industry, each individual producer being rather an organ of the national productive organization, the tax-object and the tax-source might both be reached with some certainty. For the absence of exchange would deprive each individual of the ability to shift the taxes demanded by the state to the buyer of his products as part of their cost of production.

But given the freedom of exchange between individual producers, and given the prevalence of an economic organization in which the great body of private industrial establishments produce for all other establishments, we have also given the possibility of treating any tax levied by state or commune as part of the cost of production and of the producer's recouping himself for this cost of production in the price demanded of the buyer.

Tax legislation and administration have here to do with processes which, as being constituent elements of the process of price-determination in the private competitive system, are essentially independent of any interference from the side of the government. It is impossible, under this economic system, to be sure that the tax which the law imposes and which the tax administration collects is borne by the man from whom it is collected. The only alternative would be to adopt a system of coercive measures, which has no place in this field at all.

What measures can government take to hinder a person engaged in industry and paying a heavy income tax, from following his natural bent and adding the amount of this tax to the cost of production of his goods? This may traverse the intention of the legislator whose aim is to reach precisely this profit of industry that accrues to the taxpayer, but which is

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beyond the reach of the government. The taxpayer may meet with opposition in his efforts, but opposition of quite a different nature from that which the legislator can exert.

§ 246. There are certain classes of taxes, of considerable extent, with respect to which the legislator himself proceeds on the expectation that the person who pays the tax to the state will consider it simply in the light of an outlay, and will succeed in recouping himself and so realizing this view of the tax. It even happens that the tax is refunded in cases where it is manifestly impossible to shift it.

This happens in the case of those taxes which, by reason of convenience in collecting the tax, regularly avoid demanding the amount required directly from the tax-source, but require it of some third party who is expected to take care that the tax is ultimately paid from the source intended. By a prevalent usage, to some extent also adopted in the science (Rau, and later Adolph Wagner), these taxes are called "indirect" in contrast to the "direct" taxes which it is intended shall be borne by the person by whom the law requires the tax to be paid.

For example: if the legislator sets out from the assumption that the consumption of coffee, taken in conjunction with other articles of consumption, affords a fair indication of ability to pay taxes he will not attempt to put this (in point of fact widely accepted) view in practice by levying a tax directly on the individual households which; as consumers of coffee, the tax is intended to strike. This arrangement would be so burdensome for all parties that the tax might better be abandoned if there were no more feasible method of collecting it. The law consequently adopts the more convenient method of levying the tax on the goods when they enter the country, and since the importation is only to a slight extent effected directly by the consumers, but almost entirely by the trade, the result is that the importer pays the amount of the tax in a lump sum which is ultimately added to the retail price paid by the consumers, who thereby become the actual payers of the tax

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This feature of this class of tax legislation is so fully recognized that in cases where it is impossible for the original payer of the tax to recoup himself, the sum paid as taxes is refunded. So, for example, in the case of the tax on the consumption of sugar. At the very beginning of the beet-sugar industry this tax was levied on the quantity of beets. It is quite uncertain whether the consumption of the sugar so taxed takes place within the geographical limits which define the field within which the tax legislation applies. Now since the law intends to tax consumption only within the limits of its own country, and since the tax paid in neither should nor can be shifted to the foreign consumers, the law refunds the tax wherever and to the extent to which the fact of exportation is proven.

§ 247. There are still other cases where the tax required by the law is in fact regarded as a part of the cost of production, and is therefore classed as outlay which the producer paying the tax is expected to demand of his customers in the price of his goods.

An undertaker may pay a tax to the state or commune because certain public expenditures have been incurred which have benefited his industry. Justice demands that expenditures of this kind should be paid for, just as the same undertaker would pay for any other expenditures made in his interest by anybody else. We have accordingly a further class of cases in which, for simple reasons of equity, the legislator regards the tax simply as a business outlay on part of the taxpayer. The tax itself in this case is of a different character from the taxes on consumption. This tax does not aim to reach the income from which the tax payment is ultimately drawn, through the medium of exchange and consumption; it does not seek a general payment on the part of individual households for benefits of a general character rendered to these households by the state or the commune; all it seeks is payment by the individual producer for the increase of his productive capacity. If the service rendered and the payment required for it, in such cases, do not accurately balance each

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other, the fact is due to external circumstances, not to the requirements of equity. In itself considered it would be perfectly just and fair to require payment for the use of a road by wagons or for the pollution of streams by refuse from factories, payment to be made to the public organization that has to repair the damage done. It is only the difficulty in the way of computing the proportionate cost that leads to the abandonment of this method of exact payment and the adoption of certain approximately exact forms of taxation instead. These taxes are designed to require payment in a general way for the presumable damages and the presumable benefits accruing to individual producers.

It appears therefore that however widely this class of cases may differ from those dealt with in the last preceding section, the tax legislator's view of them is undoubtedly the same. The market price of the product is expected to repay the tax, which is accordingly ultimately borne by the consumer.

The question here concerns certain constituent elements in the cost of production, for which the producer pays the state (the commune, or the like) with the expectation of being repaid by the consumers of his product. In the previous section the question concerned fiscal administrative measures which for the sake of convenience apply to the producer instead of going to the consumer in person.

§ 248. In the cases already considered, the legislator regularly regards the tax as simply a matter of outlay. Still it is by no means certain that this shifting will take place as intended by the law, for the reason that the process of price-determination is left to the working of free competition. The legislator, however, is justified in his course of action by the fact that there is a very reasonable expectation of such a result. Similarly in the converse case, where the legislator does not intend a shifting of the tax there is room for a thoughtful consideration of the possibility or probability of such a shifting taking place after all.

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The case is but the converse of the one last considered, when the question arises of remitting taxes already in force. It is questionable whether, in point of fact, the remission will accrue to the benefit of the persons who have actually borne the tax and whom it is desired to exempt.

The strength and the weakness of the earlier schools of Political Economy and of Financial Science appeared in their discussion of the question of shifting. Their strength lay in the fact that ever since the days of the Physiocrats they distinguished clearly between the source and the object of taxation; that they insisted on the necessary fact that every object of taxation must ultimately shift its burden to the source of the tax; that they (supposedly) had to do with definite quantities into which the aggregate income of the community distributed itself; finally, that they were content, with a felicitous ingenuousness, to soar high above the world of facts and simply draw certain conclusions from certain abstract premises. Their weakness lay in this, that all the quantities with which they had to do were only symbols and not living facts; neither the "net product" which they considered the source of the tax, nor the "natural wages," nor any of the rest were actualities. A further source of weakness is the fact that they made no attempt to solve the question as to what force or value was in fact possessed by the tendencies whose presence was asserted or assumed. Ricardo, as well as the Physiocrats, (with the most creditable intention) draws an abstract line of demarkation between the income necessary to subsistence (to efficient labor), and the surplus disposable for purposes of taxation. Opinions differ considerably as to where this surplus is to be found. Ricardo departs so far from the views of his earliest predecessors as to find a net product and therefore a surplus above natural wages in the customary wages paid in actual life.<sup>1</sup>

But here difficulty arises in determining what the abstract quantity of natural wage means in actual life, and so fixing the

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<sup>1</sup>Ricardo, *Principles of Political Economy and Taxation* (3<sup>d</sup> ed. 1821), Chap. xxvi. Note.

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point beyond which any additional tax will rebound and be shifted to the real source of taxation, wherever that may lie. The position taken today, which stands much nearer to actual life than these early abstractions (whose services to the science are by no means to be underrated), aims to solve the problem by an appeal to actual phenomena, but is able to offer only very modest results after a great deal of painstaking. For the observation of the workings of distribution and price-determination in the phenomena of real life is infinitely more difficult than the drawing of certain conclusions from hypothetical facts and forces of nature. It is not easy even to determine with satisfactory accuracy what the facts are; but it is much more difficult to discover the causal relation of the factors which have produced any given actual results in the matter of price-determination. The results so far attained have been for the most part of a negative character.

It is quite in accordance with this fact if we have little to offer at this point that is acceptable to the science at its present stage of development.

§ 249. While the Physiocrats insisted that all indirect taxes, since they do not fall directly on the net product, must unavoidably be shifted, they by no means regarded this process favorably. They condemned all indirect taxes because of their being imposed on the shoulders of those who could not bear them. The English school, with its widespread following, has more and more inclined to regard the matter in a favorable light. This was quite in consonance with the general attitude which gradually came to prevail in the school, quite in contrast to the popular inclinations of its precursors. The same optimism which led them to regard society from above, with the complacency of the propertied classes, and afforded no room for doubt of the natural harmony of all economic forces, and of their all working together for right and equity in industrial society, and which shut out all disturbing influence of an observation of the facts, - this same optimism it was which enabled them consistently to comfort

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themselves with the reflection that the burden of taxation, just like all the other elements in the distribution of income, would adjust itself by the "free play of the natural forces of exchange, and that "in the long run" the burden would attain its just level. This view no longer prevails in the science. Examination of the philosophical foundation of the earlier schools and observation of the phenomena of real life have led to this result. The older theory occupied itself with forces which were not present in the form and manner assumed, and with assumed effects which were simply a broadly exaggerated generalization of certain possible results. As to whether and when these results actually occur, these are questions to be decided by observation of the facts. The reason for its being a priori quite uncertain whether the facts in question occur, when they occur, what effect they have, lies in the heterogeneous character of the forces concerned. It is psychic forces, moral factors, that are here concerned. It is not a question of a natural equilibrium which natural forces left to themselves will seek and establish, but of an equilibrium of equity which is to be sought after, which is not established by a "free play of forces," rather by a progressive development of convictions, which, on the basis of exact observation, bring the facts into conformity with the idea.

To cite a conspicuous example, it is quite possible that a tax laid on the laboring majority will be shifted, from them to shoulders better able to bear it, for the reason that it falls on the necessary means of subsistence. Whether this possibility is realized depends in the first place on the view taken of the equity of the tax, and in the second place on the spirit, the actions, organization, the pecuniary means of all the various parties who are expected to bear a part or the whole of the burden. Energy in pushing their own interests, the sense of fairness in considering the interests of others, the means disposable for competition in market, the nature of the ideals aimed at by the parties to the struggle - these are the real forces which, under furthering or hindering conditions of the market, decide what is to be the actual course of events.

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§ 250. Accordingly we find that on no point touching the question of shifting and incidence, is the modern science so thoroughly agreed as on the disillusion with respect to the traditional a priori assumption which originated in the doctrine of prices held by the old school. It is no longer confidence in the effectiveness of the assumed tendency, but rather the appreciation of the actually operative causes that is decisive. The tax legislator, therefore, in every case where he adopts, increases, lowers or abolishes a tax, will accordingly have to make himself familiar with the forces at work, in order to prevent the intent of the law and therefore the equitable provision which the state has in view, from being thwarted. In a question of the taxation of the necessary means of subsistence he will beware of assuming, with the old school of thinkers, that the equity of the case will take care of itself in that the new burden will presently be shifted to the employers or the consumers of the products of labor, etc.; he will rather try to find out what are the chances of the laborers being able to shift the burden from their own shoulders by effecting a rise in wages. Even this new attitude of doubt is a step in advance as compared with the old error. When the question concerns the abolition of an existing tax on consumption, we shall have, in place of the assumption that the abolition of the tax will be sure to accomplish its purpose (that is, to take the burden from the consumers) an investigation as to what are the intermediate personal factors whose co-operation is necessary in order to accomplish the object of the legislator.

The great variety of the facts of life and the peculiarities of each individual piece of legislation are of course to receive due consideration; but there are, after all, certain general observations whose application is not bounded by the peculiarities of any individual case.

Shifting of taxation will take place regularly in proportion as the following cases are present: (1) the consciousness of unequal distribution of the burden of taxation, (2) the wish to rid oneself of the unequal burden, (3) the pecuniary ability to accomplish this purpose.



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From these considerations it follows that a shifting of taxes can more readily be accomplished by capitalists than by laborers, by well paid and organized laborers better than by other classes of laborers, by organizations of employers better than by individual employers, by owners of movable capital better than by owners of immovable capital, by professional business people better than by amateur business men, by merchants better than by the consumers who are their customers, - or what amounts to the same thing, they are in a better condition to withhold the benefit of a reduction from the classes of the population which it was intended to benefit.

## CHAPTER III.

### THE HISTORICAL FORMS OF TAXATION.

LITERATURE. K. H. Lang, *Historische Entwicklung der Deutschen Steuerverfassungen* (1793), G. Waitz, *Deutsche Verfassungsgeschichte*, vol. viii. (1878). G. Schönberg, *Finanzverhältnisse der Stadt Basel im 14. und 15. Jahrhundert* (1879). K. Bücher, *Die Bevölkerung von Frankfurt a. M. im 14. und 15. Jahrhundert* (1886). Karl Zeumer, *Die deutschen Städtesteuern, insbesondere die städtischen Reichssteuern im 12. und 13. Jahrhundert* (1878). Johannes Falke, *Die Geschichte des deutschen Zollwesens* (1869). Hubert Hall, *A History of the Customs Revenue in England* (1885). Stephen Dowell, *A History of Taxation and Taxes in England from the earliest times to the year 1885* (2<sup>d</sup> ed. 1888). Alexis de Tocqueville, *L'ancien Régime et la révolution* (1856). G. Schmoller, "Die Epochen der preussischen Finanzpolitik" (*Jahrbuch des deutschen Reichs*, 1877). G. Schmoller, "Studien über die wirtschaftliche Politik Friedrichs des Grossen und Preussens überhaupt von 1680 bis 1886" (*Jahrbuch des deutschen Reichs*, 1884-1887). H. Bielfeld, *Geschichte des Magdeburgischen Steuerwesens von der Reformationszeit bis zum 18. Jahrhundert* (1888). Walther Schultze, *Geschichte der preussischen Regieverwaltung von 1766 bis 1786* (1888). C. A. Zakrzewski, *Die wichtigeren preussischen Reformen der direkten ländlichen Steuern im 18. Jahrhundert* (1887). B. Gliemann, "Die Einführung der Accise in Preussen" (*Zeitschrift für die gesammte Staatswissenschaft*, 1873). Von Inama-Sternegg, "Der Accisestreit deutscher Finanztheoretiker im 17. und 18. Jahrhundert" (*Zeitschrift für die gesammte Staatswissenschaft*, 1865). J. G. Hoffmann, *Die Lehre von den Steuern* (1840). Carl Dieterici, *Zur Geschichte der Steuerreform in Preussen 1810-1820* (1875). K. G. Kries, *Zeitschrift für die gesammte Staatswissenschaft*, 1854, 1855, 1856.

#### I. THE SINGLE TAX AND A PLURALITY OF TAXES.

§ 251. As old as financial science itself is the idea of embodying the whole system of taxation in a single tax.

The Physiocratic theory of taxation points to the tax on rent (assumed to be the only surplus of industrial production available for purposes of taxation) as being the direct and the

only tax. Voltaire (in his *L'Homme aux quarante écus*) ridiculed this as well as the other doctrines of the Physiocrats - the *impôt unique* was the *impôt inique*.<sup>1</sup> Still the interests both of the theory and the practice were on the side of the Physiocratic idea.

The Single Tax came as a great relief to the theory after the chaos of taxes which the historical development had been piling up for some centuries past. Aversion to the results of the historical development seemed to offer special inducement at this point to a radical transformation of existing institutions. Simplicity, which, as the adage has it, is an earmark of the truth, was in this case, as happens so often on the introduction of a new doctrine, urged as a strong argument for the truth of the doctrine put forth. The entire view of the state and of society which dominated the era of the Revolution, with all its rationalistic, atomistic theory of the state and the man, favored and was attracted by this simplification. The administrative practice of the new era seized upon this simplification of an intricate problem with alacrity, and applied it in good earnest at the instant when the French Revolution was realizing its programme. And even after the legislation had discovered and attempted to remedy the defects of the "single tax" the magic word retained its spell, and continued to figure as an article of faith in the radical party programmes. It was not only that the complete simplicity and intelligibility of the single tax fell in with the spirit of these programmes, but more especially that it recommended itself as of practical value for certain social-political purposes. It was only a secondary question whether the doctrine of the single tax was to be construed to mean an exclusive tax on rent (as was not usually done), or a "single progressive income tax for state and commune," in accord with the requirements of the most advanced thought.

The application of the single tax has, under favorable circumstances, even passed beyond the stage of party platforms and

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<sup>1</sup>The single tax was criticised in detail by Necker, *De l'administration des finances de la France* (1785), vol. i. pp. 153-192; and earlier by Justi in criticising Vauban (*Staatwirthschaft*, vol. ii. p. 297).

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been adopted, at least with approximate completeness, into the fiscal administration of some smaller communities. The canton Zurich has afforded a notable instance for twenty years past.

§ 252. The question is, whether the ideal of radicalism which claims so very respectable scientific antecedents, is to be accepted by modern science. Is the single tax also our ideal, or are there scientific reasons which restrain us from availing ourselves of its apparent advantages.

It is in the first place to be granted that the necessity of at least a relative simplification has made itself felt and produced an effect in all the tax systems of Europe; whether we look to the French, the German, the British, or even the Swiss tax legislation, this proposition holds true. A great deal of the relics of the older tax system has been cleared away with the help of the light of financial science, even though this work of reform; has not in all cases gone so far as in Great Britain, where the free-trade movement gradually reduced the number of dutiable articles from several thousand to half-a-dozen, or as in the cantons of Switzerland, the more advanced of which have cleared away practically the whole of the earlier tax system in order to make room for the income and property taxes.

Still, this relative simplification of the tax system always leaves room for some plurality of taxes, so much so that even in the experimental field of radicalism - in Switzerland - there is enough of it left to challenge reflection. It is to be noted that the increasing fiscal demands of canton and commune have for a number of years past found the "single tax" an intractable instrument which refuses to meet any considerable demands upon it; as a consequence of this fact the necessity of meeting the growing outlays has compelled the refurbishing and exaltation of nominally obsolete and long-discarded forms of taxation; at the same time the finances of the Swiss federation have never ceased to place their chief dependence on consumption taxes in the shape of a comprehensive taxation of nearly all articles of import, and under the pressure of new fiscal necessities these taxes have even

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been energetically pushed to a further development. It must therefore be said that even under the exceptional circumstances of national and constitutional activity which are to be found in Switzerland, the test of experience does not favor a "single tax."

Observation of the practice of modern states would therefore go to show a general tendency toward simplification of the tax system, but not to support the doctrine of a single tax.

§ 253. The observation of the actual course of development of the tax legislation of modern states accords with the conclusions to which we have been brought by our previous discussion.

A single and exclusive tax to replace a system of diverse taxes fails to answer a series of requirements which are made from the standpoint of equity as well as from that of expediency.<sup>1</sup>

(1) The payment of taxes rests, as we are well aware, on various principles of equity which cannot all be satisfied by a single tax. For example, if an owner of real estate is in fairness bound to pay for the advantage accruing to his property through the expenditures of the commune or the state, this object cannot be attained by means of the same tax which the same real estate owner is called on to pay toward the support of the public schools and of the poor, in proportion to his personal ability to pay taxes.

(2) When we come to consider the psychological character of every tax burden, we find ourselves per force entering on a lengthy discussion of practical questions of tax administration; it being one of the practical problems in every tax administration to lighten the pressure of a given burden of taxation as far as may be.

As is the case with every sensation of pleasure or discomfort in economic life, so also the payment of a tax does not figure as a fixed mechanical quantity that may be mathematically meas-

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<sup>1</sup>Justi, even, makes some very sensible remarks on this point. - *Staatswirtschaft*, vol. ii. pp. 293-300.

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ured in degrees of pressure on the taxpayers, but as an historical phenomenon influenced by the varying sentiments of the taxpayers. The question here concerns the entire development of the sense of citizenship, intelligence, self-sacrifice, patriotism, as opposed to the individualist motives of private life, with its primitive crudity or its more refined love of gain and of pleasure.

This relation subsisting between the commonwealth which imposes the tax and the individual taxpayer, requires forms of taxation adapted to its purpose; just as the development of the fiscal policy as a whole necessitates a series of grades, within each of which grades the tax is levied at a proportionate rate; this being especially true after the tax has come to be the normal dependence for the public revenue (Book I, Chapter II.); so the tax system too requires a gradation in its development, which shall correspond to the gradual evolution, the advance and decline, of the sense of nationality.

The rapid growth of the need of tax revenue, which ordinarily increases much faster than the consciousness of civil duty, constantly urges the tax administration to invent suitable forms of taxation, whose flexibility is put to the test by the elasticity of the demand for revenue.

The result of all this is that we have a number of different forms of taxation, which, judged by the ideal of the single direct tax intended to make the tax-source the tax-object, may appear very imperfect in the eyes of abstract doctrinarianism, but which are, after all, nothing but the adequate expression of the nation's immature sense of citizenship.

§ 254. (3) It is to be added that even where the intelligence and sense of citizenship on part of the taxpayers is relatively mature, the practical difficulties attaching to a single tax on income are so great as to necessitate supplementary taxes of other kinds in order to carry out the purpose of the single tax.

The mobility of modern life makes it difficult, or rather impossible, to levy accurately and in proper season on a large body of tax-paying ability, by means of this single form of tax-

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ation alone. For this purpose, too, we need other more flexible forms of taxation, which will adapt themselves to these changes of residence.

But even when the great and hitherto rarely accomplished task of any income tax is achieved - the ascertainment of the income - that is not all that is necessary. The problem consists not alone in ascertaining the amount of the income, but also in finding the relation between the income and the aggregate necessary expenditure of each taxpayer. The inflexible standard afforded by the amount of the income alone gives no information as to the individual's tax-paying capacity, this latter depending on the peculiar conditions of his life. And to ascertain what these are, the tax legislation requires a deal of supplementing which must be got through other means than the income tax.

(4) The organization of a commonwealth under a system of larger and smaller civil divisions, especially in a federal state [*Bundesstaat*], gives rise to peculiar fiscal conditions, such as do not admit of our placing at the disposal of each of these civil divisions a single form of taxation which is to be used by all in common. Rather, the federal state has special reasons of its own for discarding the single tax on income, reasons involving the innermost nature of such a state, and which would not be present if the people in question were prepared for a national union.

(5) There flow into the treasury tax revenues which arise out of measures adopted on the ground of economic policy, and are, according to the views accepted today, desirable and judicious taxes. But the occasion for measures of this kind, we may assume, will recur in the future, and this class of taxes will therefore continue to be levied. The chief example of this class of cases is the tariff on imports.

§ 255. In order to clothe these introductory remarks with flesh and blood, it will be desirable to consider the historical forms of taxation.

It is only by examining the actual course of development that we come to appreciate the difficulty of progress in the direc-

tion of abstract ideals on the one hand, and the significance of the peculiar content and purpose of each particular group of taxes on the other. The gradual development of the historical institutions is shown by the import duties, the stamp taxes, and the monopolies. These forms of taxation were made intelligible and acceptable to the childish understanding of earlier times by appearing in the guise of payment for an equivalent, and have disclosed their true character only at a later stage, after the dawn of an era of a more mature sense of citizenship, when it has appeared that what was so long taken for their substance is only their form. The successive stages in the historical development, and its wonderful changes and alterations, are manifested in a specially impressive way in the rise and decline, the fixity or instability, the disappearance or prominence, of the scot, the property tax, the income tax, etc. These most perfect forms of taxation attained relatively early to an energetic application, and flourished in a remarkable degree, and then, after half a thousand years, they have been taken up again as an ideal of taxation to be striven for. The introduction of the so-called "proceeds-tax" [*Ertragssteuer*], which was adopted at the beginning of the nineteenth century, especially in France, as a redeeming improvement over the old direct tax, brings out the same difficulty of historical progress. It presently manifested all its native ineptitude when compared with the old direct tax in its revised form, and has in many cases been altogether discarded.

The difference in content and purpose between the different historic forms of taxation will be brought out by a discussion of the historical material from the point of view of modern science.

In pursuance of this purpose, and referring back to the observations previously made on the National Economy in Process of Becoming (secs. 52 *et seq.*), the present chapter will attempt an historical survey. The succeeding chapter will then go on to combine the historical data with the deliverances of theory, in order, in this way, to arrive at a tax system based on history and theory alike and adapted to the fiscal exigences of a modern European State.



## II. THE EARLY PERSONAL TAXES.

§ 256. The purpose of this historical survey is not a collection of all sorts of curious and obscure facts from the records of all ages and all peoples, such as often characterizes the infantile stage of historical research. It is of no consequence to us that certain kinds of taxes have made their appearance in this or that country at such or such a time during its development. What it concerns us to know is the relation of these forms of taxation to the political and fiscal development of a given people.

It is already a hundred years since K. H. Lang (in his *Historische Entwicklung der Deutschen Steuerverfassung seit der Karolinger bis auf unsere Zeiten*) discussed in this manner the phases of German taxation in connection with the development of the military system. The motley array of varieties and forms of taxation is there exhibited, freed from the appearance of accident, and subject to the law of historical development.

It is also not to the purpose to sever the individual kinds of taxes which go to make up the fiscal system of each historical epoch from one another, and take up each one by itself. At the same time, the object of the present discussion could scarcely be accomplished without our singling out for examination certain leading groups of taxes which are to afford the material for the construction of our system.

No class of taxes is more deserving of such special attention than the one which, very significantly, makes its appearance right at the beginning, and recurs constantly in the later stages of the development of the tax system. For in spite of all reservations, it remains true that the one tax which the groping hand of the primitive national economy, as well as the radicalism of advanced political systems, laws hold of, is above all others the tax of taxes. It is also a notable fact that on the most diverse occasions, based on the need of revenue or on the demand for equity in the distribution of the public burden, this one form of taxation has been resorted to for ages past, over and over again, for this reason if for no other, that it is the simplest in form.

§ 257. A characteristic of the old personal taxes is the fact that they were levied on some extraordinary occasion.<sup>1</sup> From the earliest beginnings down into the nineteenth century they are for the most part a temporary impost justified by a special plea of unusual necessity. This state of things changed only very slowly. The German writers on financial theory, even as late as the close of the eighteenth century, regarded the tax as an extraordinary impost, as a malady with respect to which there was an uncomfortable doubt whether it would ever be cured. Thiers reflects the sentiment of modern individualism in close touch with mediæval individualism, when he airs his aversion to the direct tax in the assertion that it is characteristic of barbarous, as contrasted with civilized peoples.

The earliest form of this tax occurs in connection with the feudal state. In the place of personal service, and supplementary to the personal obligations of the vassal in cases of the *trinoda necessitas* (ransom of the sovereign, knighting of the vassal's son, betrothal of his daughter), the tax comes to be substituted<sup>2</sup> in times of war - *adjutorium*, *scutagium*, *tallagium*. The usual German term for it is "Bede" - etymologically,<sup>3</sup> as well as by its conventional Latin equivalent (*petitio*, *rogatio*, *precaria*), indicating a petitionary character, at least in its origin. Where, contrary to its nature, it takes on the character of a fixed burden, it is transformed into a burden on real property; a fixed personal tax being, to the mediæval sense of personal liberty and dignity, a mark of the bondman. And as we have already found in the general survey of the historical development of the public economy (Book I. Chap. II.), this class of imposts blends with the peculiar burdens pertaining to villenage; a fact which becomes intelligible when it is remembered that villenage originates in personal inability to bear arms.

It is quite in accord with the traditions of the feudal system that we find that the Great Elector of Brandenburg, as late as the year

<sup>1</sup> Cf. secs. 55 and 56 above.

<sup>2</sup> Cf. also Bluntschli, *Staats- und Rechtsgeschichte der Stadt und Landschaft Zürich* (1838), vol. i. p. 207.

<sup>3</sup> Grimm, *Deutsches Wörterbuch*, vol. i. p. 1221.

1662, had gradually, and only after long and tedious negotiations with the estates of the realm, succeeded in substituting, in place of special grants for the purpose, fixed contributions from his territories toward the support of the standing army which he had created. At the same time the obligation of the knighthood to follow the sovereign in war was commuted into a money payment of forty thalers for each horseman.<sup>1</sup>

In the towns, wherever the requirements of the tax administration permitted, the excise was generally introduced after 1667, to take the place of Contributions; a step which lightened the taxes of the burghers and increased the revenue. The inadequacy of the Contribution became evident as early as the years 1677 and 1679, when an extraordinary subsidy, a "poll-money" [*Kopfschoss*], was levied on all inhabitants. In point of fact this contribution appears to have been an income tax; we are told that (towards the total of 200,000 thalers) the Elector himself headed the list of contributors with a sum of 1000 thalers for his own person, 500 thalers for his consort, and so on for all the members of his household, with the purpose of taxing all inhabitants down to a minimum rate of 4 groschen. This poll tax was repeated under his successor with increasing frequency<sup>2</sup> but was made the subject of a formal waiver by Frederick William I. (1715), and was restricted to the case of a defensive war. Frederick the Great finally found other means of obtaining a revenue in order to provide for the heavy expenditures of the wars, and was able to leave the Prussian state at the end of his reign with a clear annual revenue of 20,000,000 thalers.<sup>3</sup> So far as this was accomplished by means of taxes it was by the use of those real taxes which are to us the opposite of direct personal taxes.

The Contribution, however, was made use of by both the two: great Prussian kings of the eighteenth century as the point of departure for reforms which prepared the way for the modern land tax by means of a registry of incomes; they aimed partly to

<sup>1</sup> Riedel, *Der brandenburgisch-preussische Staatshaushalt*, pp. 31 et seq.

<sup>2</sup> *Ibid.*, pp. 48 et seq.

<sup>3</sup> *Ibid.*, p. 132.

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consolidate the burdens resting on the land into a single impost, partly to lessen the inequality of the burdens resting on land owned by peasants compared with that owned by the knighthood.<sup>1</sup>

§ 258. But even during these earlier centuries the personal taxes developed into quite a different form when employed under circumstances which approached modern political life in being freed from the trammels of the feudal system and the territorial state.

What I have in mind is the democratic organizations of the old cantons of Switzerland and the city republics of the Middle Ages. The rule is the same here as elsewhere during those centuries.

The tax is for the most part an extraordinary burden, levied to meet cases of special necessity or the exigencies of war. Still, in certain ones of them there is a relatively early development of a fixed tax constituting a permanent element of the public finances.

Looking first to the early democracies of Switzerland<sup>2</sup> we find that the facts are as follows. In most of these democracies a general tax on the country was resorted to only as an extraordinary resource when the ordinary revenues of the treasury were insufficient, especially in case of war. So, for example, in Uri it was usual to impose a general tax in times of need. This tax, by ancient usage, was primarily levied on landed property, which was assessed by public officials, the creditors of the landowner being required to contribute toward the owner's payment of the tax in the proportion of their claims. At the same time, everybody was required, under oath, to return to the proper authorities all his other property, whether situated at home or abroad; whether in the form of securities, rents or business establishments; the penalty being confiscation of everything not so returned. The same is true of Schwyz, Nidwalden, etc. In

<sup>1</sup> Zakrzewski, *Die wichtigeren preussischen Reformen der direkten ländlichen Steuern im 18. Jahrhundert* (1887),

<sup>2</sup> J. J. Blumer, *Staats- und Rechtsgeschichte der schweizerischen Demokraten oder der Kantone Uri, Schwyz, Unterwalden, Glarus, Zug und Appenzell*. Part ii. (1858), pp. 295 et seq.

Glarus, where the property tax occurs as early as the time of the wars of Burgundy, the religious convention of 1683 mentions as a customary source of revenue for the general treasury, "imposts per capita and on estates," what afterwards was usually spoken of as the *Hab-, Gut- und Kopfsteuer*. This was a combination of the capitation tax with the property tax, such as occurs in the case of the general tax of the German Empire as early as the fifteenth century, and such as we find it in the extraordinary taxes levied by the Great Elector and by Frederick I. In this latter case the capitation tax becomes incorporated with the privileges of the "independent gentleman" in a thoroughly democratic fashion; so much so that it became a condition of participation in the public privileges and immunities. During the eighteenth century a "uniform general tax" [*Einfache Landessteuer*] was regularly levied (one in a thousand gulden of property and one-fourth gulden per capita). To prevent unequal taxation, the estates of the realm enacted in 1725 that all persons must return, on honor, all their property, excepting only household articles and clothing; if it appeared in case of succession that the property was greater than returned, then the amount concealed was to escheat to the state, the officials being for this purpose empowered to make the necessary official inventory.

§ 259. In the mediæval towns we find something similar, only at a distinctly earlier date. In Zurich, Hans Waldmann, who was chosen Burgomaster in 1483 in opposition to the old families, introduced, in the town and in the territory belonging to the town, both the salt tax and the so-called *Reisbüchsen* into which all taxable inhabitants were to pay a yearly contribution; the purpose being to provide beforehand for the case of war in order to meet the expenses of war so much the more easily.<sup>1</sup> It is true this institution, created under the democratic administration of Wald-

<sup>1</sup>Bluntschli, *Staats- und Rechtsgeschichte der Stadt und Landschaft Zürich*, vol. i. p. 354.

mann, disappeared with his overthrow. At the same time it is instructive to note that the *Richtebrief* of the citizens of Zurich<sup>1</sup> of the year 1304 speaks of the *Gewerf*, that is to say, the property tax, as a tax of frequent occurrence. Whenever [Swenne], says the document, the *Gewerf* is levied, the tables in which the *Gewerf* is engrossed are to be read in the presence of all the citizens. This is followed by provisions respecting exemption from taxes and liability to pay taxes; among other things a provision for the equal taxation of citizens of Zurich living outside the city, whether knights or citizens. In the year 1417 a property tax [*Gutsteuer*] was levied, for three years,<sup>2</sup> towards which the Great Council ordained that everyone must pay one penny in the pound on all his estate, real and personal, house, chattels, clothing and raiment, except only the harness in which he served in the city guard. From persons who live expensively or are engaged in a profitable business and still own but little property, the assessors of the tax are empowered to require payment in proportion to the profitableness of the business.

Side by side with this *Gutsteuer* was a *Leibsteuer* (poll tax) levied on all persons. It appears that during the fifteenth century, and also during the sixteenth and seventeenth centuries, the tax<sup>3</sup> was continually approaching the character of a fixed impost, being thrown off in displeasure every once in a while by the citizens after having been in force for decades together (not unlike the fortune which the English income tax has experienced in the nineteenth century).

In Duderstadt<sup>4</sup> the scot [*Schoss*] makes its appearance as a regular and considerable factor in the annual revenues, about the middle of the fifteenth century. The accounts rendered for each year invariably begin with a list of those liable to pay the scot, that is, of persons required to pay a tax on land, on house

<sup>1</sup> *Archiv für schweizerische Geschichte*, vol. v. (1847), p. 219.

<sup>2</sup> Bluntschli, *Rechtsgeschichte*, vol. i. p. 401.

<sup>3</sup> G. Meyer von Knonau, *Der Kanton Zürich von den ältesten Zeiten bis auf die Gegenwart* (1846), vol. ii. p. 257.

<sup>4</sup> Julius Jäger, *Duderstadt gegen Ende des Mittelalters* (1886), pp. 21 et seq., 22. et seq.

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and home, tithes, incomes, rents, and personal property (except clothing), church livings and foundations, the guilds, the citizens and the disfranchised inhabitants, the citizens living outside, the Jews, and the outlying farms. At Michaelmas, at the beginning of each fiscal year, the clerk of the treasury drew up the tax lists, and the tax was paid according to these lists, in two installments. Anyone who failed to pay the scot forfeited his brewery privileges for the year, or else he was obliged to pay an additional one-fourth of the scot as a penalty. The scot amounted to more than half the aggregate annual revenue. As early as 1435 and 1438 there occur discussions between the town council and the guilds with regard to increasing the scot. The guilds demanded that property [*Erbe und Gut*] should be taxed at a higher rate than the earnings of the handicraftsmen; they succeeded in effecting that the assessment was to be made before the nine guild masters. On account of the town's being involved in a variety of feuds, an extra scot [*hulpe, hulpegelt*] amounting to about one-fifth of the regular tax was levied, and that repeatedly, between 1443 and 1456. The guilds made this a lever by which to further their demands for a fuller participation in the city's affairs, and in fact it enabled them to effect the appointment of the so-called *Viermänner*, and so to control and even to displace the treasurer.

§ 260. There is one thing, especially, about the old personal taxes which impresses on the modern observer the closeness of the connection between the past and the present, viz., the varying character of the measures taken to insure a proper assessment of the taxpayer.<sup>1</sup> We find a high-strung reliance on the uprightness of the taxpayers on the one side, and severe penalties on the other. There is a great variation from place to place and often from one decade to another.

Adam Smith<sup>2</sup> cites, as examples of the exceptional conditions

<sup>1</sup> Cf. K. Zeumer, *Die deutschen Städtesteuern im 12. und 13. Jahrhundert* (1878), pp. 61 et seq.

<sup>2</sup> *Wealth of Nations*, book v. chap. ii.

under which he regards the income tax as admissible, the taxation of Hamburg, Zurich, Unterwalden and Holland. Regarding Hamburg he relates that (as was true of Bremen until very lately every taxpayer assessed himself, and paid the amount due (one-fourth per cent. of his property) into the public treasury, making oath as to its correctness without naming the sum. - Smith explains the general confidence entertained as to the honest payment of this tax<sup>1</sup> by pointing out that the community in question was a small one, that the people had great confidence in their government, and that they were thoroughly persuaded of the necessity of the tax. Of Zurich he relates - and similarly of the other Swiss cantons - that each citizen publicly states the amount of his property under oath; such a measure would seem a very great hardship to a body of citizens engaged in trade, as the people of Hamburg were, while it would seem quite unobjectionable to a sober and thrifty people like the Swiss.

In point of fact, this contrast of race and occupation which Smith points out does not explain the matter. Within the Swiss cantons, and often in places but little removed from each other, the arrangements differ widely.

In the Zurich *Richtebrief* of 1304 it is provided, as has been pointed out, that the amounts assessed are to be read in

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<sup>1</sup> Machiavelli praised this system of tax-paying employed by the German towns, in extravagant terms (*Discorsi*, vol. i. p. 55; cf. K. H. Lang, *Ursprung*, p. 166; Kries, *Zeitschrift für die ges. Staatswissenschaft*, 1852, p. 276). He compares the virtue which it indicates with the patriotism of the ancient Romans. He says: "when the German cities require a sum of money for public purposes, the magistrates draw up an ordinance that every inhabitant is to pay in one or two per cent. of his property. Thereupon each one appears before the collectors of these imposts and after having made oath that he is about to pay the sum due from him, he drops into a sealed box as much as he conscientiously believes he ought to pay, no other test being required of him. From this we may understand how great an uprightness and religion still prevails among these people." Machiavelli adds: "The uncorrupted morals of these people deserve our admiration all the more that the like today survives nowhere but in Germany; this is probably due to the fact that this country keeps aloof from the merchants, has no intercourse with its highly corrupt neighbors, the French, Italians and Spaniards, and contents itself with its homely sustenance and clothing and its domestic products, without aping foreign manners." It may be noticed that this explanation is quite a different one from that of Adam Smith, in fact, to some extent contradictory of it.



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public. But Bluntschli<sup>1</sup> tells us that in the fifteenth century the amount of the tax was thrown into a vessel by the taxpayers without being counted, and he adds (much the same as what Smith says of Hamburg) that the reasons for this method were personal confidence on the one hand, and the wish to avoid publication of the amount of property - belonging to the individuals, on the other. Close by, in the Province of Zurich, in the village of Elgg, the tax law was quite a different one. If the magistrate and the council were of opinion that anyone had, under oath, returned his property at too low a figure, any citizen whosoever might "seize and purchase"<sup>2</sup> the property at the price returned.

In the canton of Glarus,<sup>3</sup> again, self-assessment prevailed from 1725 to 1735; but in 1735 a committee was appointed to manage the assessment, and in 1764 a law was passed making the assessment a duty of the magistrates. Then, on complaints being made of inequality of taxation, self-assessment was reintroduced in 1781 and was confirmed in 1794, but only to be abolished again in 1796 as "altogether too rigorous," and again replaced by official assessment.

### III. TOLLS.

§ 261. The discussion under the last preceding head has dealt with that class of taxes which have, on account of their simplicity, lasted through from the beginning to the end, and combine the earliest tentative efforts and the ideal of developed taxation. Under the head of tolls (duties) we shall have to do with a kind of taxes which are of a diametrically opposite character, and reflect all the changes of the political system and of the public economy.

In the first place the tolls are, in their origin, to quite as great an extent as any other kind of payment towards the primitive public economy, an individual payment for individual

<sup>1</sup> *Rechtsgeschichte*, vol. ii. p. 29.

<sup>2</sup> *Herrschaftsrecht von Elgg von 1535*, art. 56, 5. Something similar occurs as early as 1345 in Stendal. Cf. sec. 56.

<sup>3</sup> Blumer, *Demokratie*, vol. ii. p. 297.

benefits.<sup>1</sup> They are payments due from the individual to the lord of the land for the establishment and security of roads, rivers, bridges, harbors, markets. Whether, with Gneist,<sup>2</sup> we derive them from the police power (preservation of the peace), or lay special stress on the service rendered as an equivalent, - in any case it is a fact of great significance for the nature of these imposts that they constantly tend to develop into private rights, in that everybody asserts the right to collect tolls who feels himself strong enough to enforce the claim. This usurious exploitation for private gain of what is properly a public right, and the further development of a well-founded right into an abuse, was a subject for magisterial prohibition from very early times.

The capitularies of the Frankish kingdom mention a variety of tolls: bridge-toll, river-toll, harbor-toll, road-toll, wheel-toll, pack-horse-toll, foot-passenger-toll, market-toll, and the like.<sup>3</sup> That these and other tolls had, even at that time, been carried to excess, and were frequently abusively collected by great lords and small, is evident from the ordinance enacting that in general, no toll is to be collected on the open road where there is neither bridge, nor ford, nor ferry;<sup>4</sup> similarly this other provision that no toll was to be levied except what had been levied since ancient times.<sup>5</sup> While it here appears that the rulers of the Frankish kingdom sought to protect their subjects against the oppressive collection of tolls by the powerful, and their constantly renewed prohibitions bear witness to the futility of their ordinances, in England, under the Norman kings, this same subject is a matter of complaint against the kings. An integral part of the rights of the English people, confirmed by John in the Magna Charta,<sup>6</sup> is the right of all tradesmen to a

<sup>1</sup> Johann Falke, *Die Geschichte des deutschen Zollwesens*, p. xiii.

<sup>2</sup> Gneist, *Englisches Verwaltungsrecht* (1867), p. 41.

<sup>3</sup> *Pontaticum, rivaticum, portaticum, plateaticum, rotaticum, saumaticum, pedagium, foraticum.*

<sup>4</sup> *Capitul.* I. III. c. 54.

<sup>5</sup> *Capitul.* I. V. c. 202.

<sup>6</sup> Gneist, *Englisches Verwaltungsrecht*, p. 287.

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safe-conduct to go out of England and to come into England, to sojourn in and to pass through England, both by land and water, to buy and to sell "without all *malis tollis per antiquas et rectas consuetudines*," that is to say, in violation of the ancient and lawful tolls. The restriction of tolls to what has been established by ancient customs (*consuetudines*) is so firmly bound up with the idea, that the prevalent name for tolls in English is derived from the term for a customary right (*coutume, custuma, custom*). The revenue from customs tolls was still quite inconsiderable at the time of King John; the customs being farmed out in the fourth year of his reign for £50 silver.<sup>1</sup>

§ 262. We are now in a position to discuss the English development as contrasted with the German, and to follow up the development of tolls under the influence of an orderly and consolidated government, until it becomes what it is today for the purposes of the modern state, namely, a payment of a general character into the public treasury. It is therefore a form of taxation, usually levied on articles of consumption on their crossing the national boundaries, especially on their import. It is a form of taxation which does not exclude other than financial considerations, and which may even, under given circumstances, give such considerations the chief place.

A significant contrast appears in the fact of a much earlier development in England than in Germany. It is shown even in the fact that the differentiation of the name took place earlier in England. The Low-German-Saxon term "toll" began to be used quite early, and has continued until the present to denote the payments by individuals, and in part to private individuals, such

<sup>1</sup> Madox, *History of the Exchequer*, p. 529. Sinclair, *History of the Public Revenue*, vol. i. p. 100.

<sup>2</sup> *A History of the Custom Revenue in England from the Earliest Times to the Year 1827*, by Hubert Hall, contains a great deal of historical information regarding the details of the origin and development of the English customs, based on the original documents. Hall shows the complexity of the subject and the tardy process of elimination by which a system of individual payments for an equivalent developed into a system of public revenues - taxes in the special form of duties, and a system of political measures for the regulation of imports and exports - protective duties, etc.

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as bridge-tolls, road-tolls, canal-tolls, and the like; while the term "customs" is used to designate import and export duties as known to modern political administration. In Germany, on the contrary, these different classes of payments are designated indiscriminately by the single term *Zoll*, a usage which connotes centuries of confusion in the public administration and public law. It is not that England simplified the practice of import and export duties. They were, in England as elsewhere, developed into an extremely complex and variegated structure, so much so that even Pitt's Customs-Consolidation Act (1787) contained twelve hundred dutiable articles of import, besides fifty dutiable articles of export. But the idea of the duty had long been clearly and distinctly conceived, while in Germany a similar clear conception had been sought in vain for centuries. This clear conception had been reached early because a consolidated political organization had developed a uniform organization of the revenue system; the public [*öffentlich-rechtliche*] nature of the national government brought out the public nature of the tax which had originated in these individual payments. In Germany the course of development was much slower.

As is the case in the Capitularies of the Frankish kingdom, so we find it also happens that the German Emperor, in his struggle for the establishment of the imperial sovereignty, attacks the abuses that occur in the collection of tolls. Very significant is the edict promulgated by Frederick II. at the Reichstag in Regensburg (1235). This edict provides that all tolls on land and water, whose collection was begun after Henry's death, wherever and by whomsoever levied, are to be abolished, except the taker of the toll could prove to the Emperor that he had a right to levy it. Persons violating this provision were to be punished as robbers and highwaymen. Moreover, those entitled to levy tolls were required to improve bridges and roads and to provide for the peace and security of travelers.

The imperial edicts of the following century show how the abusive collection of tolls increased as the imperial authority

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<sup>1</sup>Falke, *Das Zollgesetz*, pp. 33 *et seq.*

declined. The imperial edict of the Emperor Sigismund (1430) reasserts the principle that the right to levy a toll is based on the rendering of an equivalent. Finally, in the midst of the decline of the Empire, a notable attempt was made to establish an imperial toll system, which was intended to further the realization of the imperial idea, but for this very reason was impossible of realization under the circumstances then existing. This was the scheme of Charles V.<sup>1</sup> to establish a system of toll collection at the frontiers of the Empire; duties at the rate of four per cent. to be collected on all goods imported or exported, with the exception of all food products indispensable for daily use, but including all members of the Empire,<sup>2</sup> even the Emperor and the Electors (1522). The scheme failed, both on account of the difficulties besetting the Empire at the time, and especially on account of the opposition of the imperial cities, which pointed out that the German Empire, beyond all other nations, was burdened with a multitude of heavy internal tolls and that trade would be unable to bear such an additional burden.

In point of fact, this reform could be achieved in Germany only by passing through an intermediate stage. The power of the territorial princes had grown so great through the feebleness of the imperial authority, that the reform would first have to work its way through this intermediate structure, and from that point gradually penetrate the imperial commonwealth.

§ 263. The German Empire had not succeeded in transforming the mediæval toll system into a national system of frontier duties, after the manner of the other European states. This service had to be performed for Germany by the territorial princes. We shall briefly review the policy of the principality

<sup>1</sup> Falke, pp. 60 *et seq.* Cf. Ranke, *Deutsche Geschichte*, vol. vi. p. 36.

<sup>2</sup> Similarly the *gemeine Pfennig* of the German Empire is levied on every prince, archbishop, nobleman and official, as well as on citizens and peasants; this was of course one more reason for the opposition to the measure on part of the estates of the realm. The legislative recognition of the tax exemption of immediate members of the Empire [*Reichsunmittelbare*] in the laws of the nineteenth century, therefore, answers not so much to the legal ideas of the Middle Ages as to the deteriorative form of these ideas current in later centuries. - Lang, *Ursprung*, p. 190.

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which has, more than any other, been instrumental in resuscitating the imperial idea, and substituting it for the inherited scheme of independent states; this principality was Brandenburg-Prussia.<sup>1</sup>

All historical development proceeds by degrees. The great end of the movement is reached by first compassing the lesser intermediate ends which mark the stages along the way. The consolidation of the imperial territory into an economic whole is the concluding act of a movement towards which the political unification of the territory, centuries earlier, served as an introductory measure. The unified territory itself had for its model the unified economic domain of the mediæval city. The system of tolls was, for this evolution, both a hindrance and a help. The advance which it promoted consisted in this, that the economic domain which was at any given time united in a single political organization - the city, later the territory, finally the Empire - drew the line of prohibition and hindrance along its frontier, and thereby furthered its own internal economic unity. An attitude of forbidding egoism towards outsiders leads to the strengthening of the city, then of the principality, or in England, France and the like, of the realm. The toll system, and its employment in the interest of the country and against all outsiders, is an effective means to this end. The economic policy of the mediæval city, therefore, furnishes the model for the toll policy of the large states, or, more immediately, of the principalities. The so-called mercantile system is not simply a phenomenon of the seventeenth and eighteenth centuries; the deeper meaning of the system is this tendency which has been working itself out gradually from the Middle Ages down to the latest times. It is not an ephemeral doctrine belonging to a single generation, but it is the expression of an immutable bent towards a conscious shaping of the national economy into a unified organic whole.<sup>2</sup>

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<sup>1</sup> Schmoller, *Studien über die wirtschaftliche Politik Friedrichs des Grossen*. - Jahrbuch 1884-1887. The Same, *Die Handelssperre zwischen Brandenburg und Pommern im J. 1562*. - *Zeitschrift für preuss. Geschichte*, 1882.

<sup>2</sup> Cf. K. G. Kries, *Historische Entwicklung der Steuerverfassung in Schlesien* (1842), pp. 72-84.

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The lever which served the Hohenzollern princes in the development of the toll system within their principality was the privilege granted by Emperor Frederick III., in 1456, to apply to their Brandenburg and Franconian territory, of increasing or changing existing tolls according to their pleasure, of levying neGV tolls, of taxing wine, beer and other articles consumed in their territory or transported through it. The first attempt to use this privilege on a large scale was made by Albert Achilles in 1472. His scheme was thought out with equal care both in its political and its financial bearings. The new tunnage was to be collected by royal officials in the cities, entirely independent of all previously existing tolls; only a small number of articles in extensive use, viz., fish, herrings, wine, honey, lard, tallow, meat, tar, and other goods in barrels were to pay three groschen per tun. Beer was left untaxed because it was the most important article of manufacture and export in the cities of Brandenburg. The toll was to be of the nature of a frontier duty, in that it was paid only at a custom house and that the dutiable goods were thenceforth free. The cities opposed this plan in much the same way as they afterwards opposed the project of the Emperor Charles V. for an imperial toll system. But the sixteenth century is taken up with a long series of efforts of the same kind, this time successful, by the Electors of Brandenburg. In particular, the Lenten corn duty was developed (1569) into a general export duty on corn and remained the chief source of the revenues of the Electorate throughout the sixteenth and seventeenth centuries. It was farmed out to Denmark for a time at 200,000 reichsthalers. In the Marches the course of events was the same as in Pomerania and in all the other larger territories. The dominant motive was furnished by the interests and fiscal needs of the state, which necessarily traversed the interests of neighboring states, as, in detail, they also traversed the interests of the cities and of domestic commerce. It was a toll system which combined fiscal considerations with considerations of industrial policy, and in both of these respects served as an instrument in

the hard work which it has cost to build up the modern national organization.

§ 264. The era of the territorial toll policy of the princes in Germany closed with the development of the Zollverein, which prepared the way for the unified toll system of the newly created Empire. The tariff wars of the seventeenth and eighteenth centuries<sup>1</sup> were replaced by a common toll policy and common toll frontiers among the individual territorial states of Germany.<sup>2</sup>

In Prussia, which afterwards became the centre of the Zollverein, the preparatory steps (1816) towards a reform of the toll and tax administration began immediately after the Wars of the Liberation. On July 11, 1816, the water-tolls, the internal-tolls, the provincial-tolls were abolished (first in the older provinces), and the government on the same occasion for the first time declared its intention to introduce "a general and uniform system of frontier duties instead of the complicated system of tolls, transit duties and commercial duties which had grown up in earlier times." The intentions of the government coincided with the wishes of the business population, as is shown in an address by manufacturers of the Lower Rhine provinces, of April 27, 1818, where the complaint occurs: "Our products are excluded from all the markets of Europe by tariff boundaries, while all the products of Europe find an open market in Germany." The new tariff law went into effect May 28, 1818.

This law<sup>3</sup> had, in the first place, to solve the problem of a uniform tariff frontier<sup>4</sup> for the scattered territory of the Prussian

<sup>1</sup> Johann Falke, pp. 269 *et seq.*

<sup>2</sup> Gustav Fischer, "Ueber das Wesen und die Bedingungen eines Zollvereins" (*Jahrbücher für Nationalökonomie*, 1861), Falke, pp. 348 *et seq.* Fr. List, *Ges. Schriften* (1850), vol. ii. pp. 15-62. Fr. Nebenius, *Denkschrift für den Beitritt Badens zum Zollverein* (1833).

<sup>3</sup> T. G. Hoffmann, *Die Lehre von den Steuern* (1840), pp. 340 *et seq.* Dieterici, *Zur Geschichte der Steuerreform in Preussen 1810-1820* (1875), pp. 197 *et seq.*, 112 *et seq.*

<sup>4</sup> On May 8, 1768, for the first time appeared a declaration requiring custom houses to be established all along the frontier; cf. Dieterici, p. 13. The earliest edict dealing with the question of a uniform toll administration and the abolition of internal tolls appeared on Oct. 26, 1805.



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state, and the difficulty of this problem drove the government to a Zollverein with the neighboring German states. The tariff frontier which Prussia had to guard in 1819 stretched over 1073 miles; by the end of the year 1837 the Zollverein, with a population of 25,500,000, of which little more than half belonged to Prussia, had a tariff frontier of only 1064 miles in all.

The tariff of 1818 originally made a distinction between a duty (on the gross weight of the goods), and a consumption tax on the net weight. The duty amounted to a uniform tax of one-half thaler per cwt.; the consumption tax was for the most part levied at a rate of about 10 per cent. *ad valorem*. (Exports were free of duty, with a few exceptions.) By 1821 the duty and the consumption tax were consolidated into an "import tax" [*Eingangsabgabe*].

This tariff, as well as its successors in the united tariff territory of the German states, has the qualities both of a fiscal tariff and a moderate protective tariff. The import duty is well adapted to serve the purposes, on the one hand, of levying a consumption tax on articles the use of which is taken to indicate the degree of ability to pay taxes, and on the other hand, of erecting these same taxes into a barrier against the free competition by foreign products in the domestic market. By blending of these two purposes, both of which are readily served by the tariff frontier, arises even unintentionally in the case of all articles which are produced at home as well as abroad; a protective tariff will afford some revenue from the foreign imports, while a tariff for revenue acts to some extent as a measure of protection for domestic production. The purely fiscal duty reaches its logical consequence only in cases where every measure of protection for domestic production is avoided, and the import duty is confined to such goods as are not produced at home. Most of our modern states, Great Britain excepted, have never yet reached this stage in their tariff policy, however near to it they may often have believed themselves to stand; they have rather, in point of fact, departed farther from it during the last ten or fifteen years, and are in possession of a tariff

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system which, on account of its blending of the two purposes of a tariff, has lately been well named the "mixed" tariff.

But whether taken together or separately, these two objects represent the public function of the tariff system which, in our most mature state organizations, has replaced the primitive market, river and road toll, at the same time that the frontier of the consolidated industrial territory has taken the place of the mediæval subdivision and diversity.<sup>1</sup>

#### IV. THE EXCISE.

§ 265. Even as late as the Prussian tariff of 1818 we find a distinction drawn between Duty and Excise. The latter term has been used since the Middle Ages as the customary designation for what we today call taxes on consumption. It answers to the earlier term<sup>2</sup> *Ungelt (indebitum)*, which was chiefly used during the earlier centuries. But in a document dating from 1340 the word *Zyse* is used as synonymous with "Ungelt."<sup>3</sup> From the fifteenth century *Accise* (or more frequently the more convenient form *Zise*) gradually comes into general use. Just as was the case with the term *Ungelt*, so also this term is applied in the case of those articles of consumption which are taxed on being imported into the tax territory, as well as in the case of articles produced at home and therefore taxed at home.

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<sup>1</sup> As is the case generally, so also on this particular point, Switzerland exhibits the conditions of the Middle Ages the longest and carried to the highest degree. A report of May 13, 1823, by the Swiss Federal Revisor of Toll Accounts, I. C. Zellweger, to the Assembly, on the Swiss toll administration, says: "There are in existence within the boundaries of the League over four hundred duties and road and bridge tolls, which make up a very parti-colored picture. In some places road and bridge tolls are levied on the team or on the wagon, in other places on weight or on the goods; it is even possible to find instances where the toll levied on each horse may vary as widely as one to four, according as the animal is used in transporting one kind of goods or another. Again, we find an accumulation of fees under the designations *Zölle, Geleit Fuhrleitengeld, Bruchgeld, Trattengeld, Weggeld, Brückengeld, Sustgeld.*" The public clerk of Zurich, J. H. Hottinger, who cites this report, remarks (*Der Staatshaushalt der schweizerischen Eidgenossenschaft und ihrer einzelnen Republiken*, p. 118) that the same statement will hold true generally in 1847.

<sup>2</sup> Cf. sec. 55 above.

<sup>3</sup> Lang, *Ursprung*, p. 169.

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But as this form of taxation came to be transferred from the mediaeval towns to the territorial states, it became the usage, specially in Brandenburg-Prussia, by preference to apply the term Excise [*Accise*] in the case of such articles as were most usually subjected to a consumption tax in the territorial domains of the seventeenth and eighteenth centuries—that is to say, domestic products for every day consumption. In explanation of this it is to be noted that, for one thing, the consumption of foreign products in those times was not sufficiently extensive, and for another, and more especially, that the political boundaries were so ill-adapted to the purpose that an effective supervision of the boundary for the levying of taxes on imports seemed to be impossible.<sup>1</sup> The levying of imports on articles of consumption was confined to the towns, which were, for this reason, shut off from the country by barriers. The open country, however, was obliged to pay this class of taxes by the fact that the rural population purchased its supplies of town-made and foreign products in the towns. Then came the further development of the tariff boundary of the country, the increase of international trade and consequently of the consumption of foreign products, together with a growing sentiment that the taxable consumption of foreign products should equitably be made to bear a heavier taxation as compared with the consumption of domestic products. This development first drew the line (1821) between the concept of an excise and that of an import duty as an independent and important form of consumption-tax, and led to the creation of import duties in addition to the consumption-tax (excise) levied within the country,

§ 266. In like manner as the personal tax, the excise also proceeds by gradations from the loose and indefinite forms of the extraordinary grant, through those of the voluntary contribution and the occasional extra tax, to that of a fixed and permanent constituent of the finances. In the one case as in the other, there is a gradual development of the bony framework out of the primordial gelatinous mass.

<sup>1</sup> J. G. Hoffmann, *Die Lehre von den Steuern*, p. 341.

The term *Ungelt* (*indebitum*) implies a contribution which is not paid on the basis of a legal claim. And while this impost very early developed in the mediæval towns into a permanent element of the public revenue, it continued, in the territorial finances, to be for centuries, just as was the Contribution, a tax granted by the estates from time to time for a few years.<sup>1</sup>

On account of the general consumption of beer, the beer excise was a favorite subject of grants made by the estates. The estates of Brandenburg granted the Elector in the year 1467 an excise on beer for a period of six years. During the sixteenth century this excise gradually comes to recur constantly in the deliberations of the estates.<sup>2</sup> The estates were not at the outset inclined to regard it as a burden assumed permanently; on the other hand they explicitly declared in Silesia (1546) that the grant was, at the expiration of the four years, "to be entirely null and void." But the actual result proved to be different. The tax was not only not discontinued, but it increased fast and considerably (1546-1585 from one to six groschen per barrel). In Brandenburg-Prussia the excise acquired a definite and per-

<sup>1</sup> Gliemann ("Die Einführung der Accise in Preussen," *Zeitschrift für die ges. Staatsw.*, 1873, p. 178) says: "As a territorial tax, the Ungelt comes later than the Bede, while as a municipal tax it comes earlier than the Bede, so that, whereas the development of the taxes of the territorial finances has been from direct to indirect, in the communal taxes the course of development has been in the opposite direction." He is able to cite the authority of W. Arnold, who says (*Verfassungsgeschichte der deutschen Freistädte*, vol. ii. p. 139): "The earliest, and for a long time the only municipal tax was one requiring the payment of a small impost on the commonest articles of necessary consumption, on corn, wine, and beer, and which was originally paid in kind. Direct taxes are of a much later origin in the cities." In agreement with this, and very explicit, is the statement of R. Sohm (*Conrad's Jahrbücher*, 1880, vol. xxxiv. p. 260): "As in Basle, so in all the other German towns, the municipal fiscal administration had its origin in the Ungelt." It is to be remarked that the Prussian excise continued to be collected for the benefit of the state at the gates of the towns, down into the nineteenth century. This suggests, as an obvious explanation of the levying of an excise in the walled towns of the Middle Ages earlier than in the open country, the much greater difficulty of collecting the excise in the country. The aversion to personal taxes outside the cities was at least as great as inside. I shall not venture to decide whether the views held by Arnold, Sohm and others are well founded. K. Zeumer seems not to be of the same opinion (*Deutsche Städtesteuern*, 1878, pp. 91-94).

<sup>2</sup> Kries, *Historische Entwicklung der Steuerverfassung in Schlesien*, pp. 63 et seq. On Saxony cf. Gliemann, *Zeitschrift für die ges. Staatsw.*, 1873, p. 189.

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manent form only in the latter part of the reign of the Great Elector (sec. 62), after having, through the fifteenth and sixteenth and the greater part of the seventeenth centuries been the object of constantly recurring negotiations between the Elector and the estates. For the town population it was the correlate of the Contribution, for the population as a whole it became a supplement to the latter.

§ 267. Lotze, in a passage in his *Microcosmus* where he speaks of the rise and decline and reappearance of philosophical systems, says that systems of thought which have long ago been in vogue and have then disappeared before a prevailing sentiment of disapprobation, will come forward again after the lapse of a few years and appear as new to the short memory of men, just as a garment that has been hung away in a closet is brought out again after a few months with a semblance of renewed youth. It is not only philosophical systems that run this course. The like happens in all other fields of human thought and activity. It recurs in the constitutional development of States as well as in special branches of the administration. The republican form of political organization had fallen into disrepute in the eighteenth century, on account of the abuses prevalent in the existing republics of Europe. It was the independence of the United States and the new ideas of liberty which came in with the revolutionary era that rescued this form of national organization from general contempt and set it up as an object of general enthusiasm.

In the matter of taxation, much the same has happened. The chief forms of taxation have alternately been approved and disapproved with the shifting of sentiment; for centuries past the one class has been taken up with a one-sided enthusiasm, while the other has been treated with undeserved contempt. In this, as in other matters, maturity of thought will show itself in avoiding the exaggerated notions of the past and holding to a reasonable balance between praise and blame.

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The dogma of the single tax has been in favor ever since the days of the Physiocrats. During our own century this dogma has gradually assumed the form of the single income tax which is to replace all other forms of taxation; and as a matter of fact, we find that this dogma, under favorable circumstances, exerts a great influence on constitutional and legislative development. In the seventeenth century it was the Excise that was in a similar manner made the object of a prevalent enthusiasm whose relics have come down to us in the shape of a voluminous literature; an enthusiasm that seemed to be in complete ignorance of the fact that the Excise had been in existence for a long time in the cities, under one name or another, dating far back into the Middle Ages.

How this form of taxation was to be more extensively applied, and altered to suit the larger needs of the developing national organization. It was to comprise not only isolated articles, such as beer, corn and the like, but the aggregate of all articles of consumption; a universal excise was to be introduced. In this matter, as is so often the case, the impulse was given by the example of foreign countries which took the lead of our own country in wealth and in public institutions. These examples held out the hope of deliverance from the unspeakable annoyances and hardships of the personal tax. From the point of view of the state as a whole it was considered as an effective means of establishing equality of taxation, of abolishing the tax exemption of the privileged classes. Even in the mediæval towns the *Ungelt* had come into great favor with the municipal administration as being a means for nullifying the tax exemption of the clergy. Later the princes used it in their struggle against the exemption of the nobility. Here we meet with another example of the changes wrought by altered circumstances. A form of taxation which was in its time employed as a means of equalizing the tax burden, insomuch as it served, at least in some slight degree, to defeat absolute tax exemption, - this same form of taxation, in a later age, after legal tax exemption has been abolished and has left only

scanty remnants to recall an odious memory, has become the special object of attack of modern radicalism as producing a relative tax exemption of the rich.

§ 268. The increase of wealth, which showed itself in the consumption of many articles not necessary to subsistence, drew the attention of statesmen more and more strongly to the Excise. Even Colbert<sup>1</sup> united with his efforts for the reduction of the salt tax a heavy taxation of tobacco, wine and similar articles. While he was occupied throughout his fiscal administration with successful attempts to lighten the salt tax because salt is a necessity of life, he laid stress on the propriety of the wine tax as being a taxation of what is not necessary to life. He turned his attention to tobacco, and established a tobacco monopoly in 1674, and sought consistently to increase the revenues from it - the tax was so much the more equitable as anybody was free to smoke tobacco or not, as they chose; he points out that the revenues from the tobacco tax in the states bordering on France were higher, and sets as his goal a sum of one and one-half million livres, while the receipts had so far been only half-a-million.

The tax-reform project of Marshal Vauban (1698) was directed to a great simplification of the existing French tax system through the employment of his *Dîme royale*; but from an inclination to favor the people, the tax is laid primarily on the many new articles consumed by the wealthy. He wishes to retain or to reintroduce the taxes on tobacco, spirits, tea, coffee, chocolate, dress, carriages, wigs, wine and beer, because they are *impôts volontaires*, because they fall on consumption which is a matter of choice; indeed they are only penalties on luxury, vanity or extravagance.<sup>2</sup>

These taxes on consumption and on articles of luxury were at that time already highly developed in Holland,<sup>3</sup> the country

<sup>1</sup> Cf. *Zeitschrift für die ges. Staatsw.*, 1869.

<sup>2</sup> *Dîme royale*, édit. Eug. Daire. *Economistes financiers du xviii<sup>me</sup> siècle* (1843), pp. 99 et seq.

<sup>3</sup> The first comprehensive excise on beer, wine, cider and tobacco (1643) was introduced in England under Charles I. (W. Vocke, *Geschichte der Steuern des britischen*

which surpassed all others in wealth. The number of taxes was so enormous that the English ambassador, William Temple, (1672) was able to state that anyone who ate a dish of fish in Holland paid thirty different taxes on it.<sup>1</sup> Even Justi says there is no article of subsistence or necessary consumption to be had in Holland which has not paid taxes five or six times.

It was the example of Holland and of the Electorate of Saxony, bordering on Brandenburg, which gave the decisive impulse to the fiscal policy of the Great Elector and his successors.

§ 269. From the close of the seventeenth century the General Excise [*General-Accise*] became a national tax institution. Its

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*Reiches*, 1866, pp. 360 *et seq.*), The most important article seems, at that time, still to have been beer, on which an excise was levied of one shilling for each cask of strong beer (of a price of eight shillings). On tobacco was levied, in addition to the already existing import duty, four shillings for each pound sterling in value (two shillings on tobacco from the English colonies). Cf. Cobbett's Parliamentary History of England, vol. iii. (1808) p. 115, which affords certain corrections to Vocke. Sinclair (History of the Public Revenue, vol. i. p. 46) supposes the impulse to the introduction of the excise to have been given by the success of the Dutch excise. It was solemnly declared in 1643 that the excise was to be abolished at the close of the war; but as the struggle continued, the impost was extended to bread, meat, salt and many other articles, bread and meat being afterwards exempted. Towards the close of the seventeenth century there is a further development of the excise. Under William III. and Anne the revenue amounted to from one to one and one half million pounds. By 1733 the estimation in which this form of taxation was held had risen to such a degree that Walpole proposed a scheme for a "General Excise" (Sinclair, vol. ii. p. 28) which was to replace all import duties. The scheme met with serious difficulties - the displeasure of the people at the proposed "servitude" defeated it; but even half a century later Sinclair sounds its praises. And in fact, the idea of free-trade herein expressed itself in quite a modern fashion, being fostered by the then existing abuses of the tariff. Of the gross receipts from duties at that time (£3,500,000) £2,000,000 went to drawbacks (for the most part on smuggled goods) etc. But even without Walpole's scheme the excise made great progress-in the rate of the tax, in its extension to a variety of articles, and in the receipts. The receipts amounted to £10,000,000 in 1792, £25,000,000 in 1810 with George Canning (1822) begins the era of exemption of articles of necessary or extended use, the simplification of the excise and its concentration on a few objects yielding a large revenue.

<sup>1</sup> *Observations upon the United Provinces*, chap. vii. A Dutch writer confirms Temple's statement as being literally true (*Dialogue sur les impôts en Hollande*, 1688). Cf. E. Laspeyres, *Geschichte der volkswirtschaftlichen Anschauungen der Niederländer* (1863), pp. 217 *et seq.*



collection was originally entrusted by the prince to the existing organs of municipal self-government (the directors chosen from the Council and from the body of citizens. The mechanism necessary to its collection was afforded by the inclosing city wall or by the barriers more recently erected to supplement it. Any product whatever that was carried in through these barriers paid a consumption tax. In particular there was the so-called *Umschüttegelder* levied on grain at its entrance, and it was afterwards taxed again at the mill in different ways according to the different uses to which it was put. Cattle intended for slaughter were placed in custody after entering the town, and when slaughtered they were taxed differently according to their kind and weight. But more than that, things of the very slightest importance paid a gate-toll at entrance: eggs, cheese, strawberries, huckleberries and mushrooms. In most parts of the country, butchers and bakers were not tolerated in the open country at all.<sup>1</sup>

The principle underlying the Prussian excise was that the entire country was to be taxed through the towns. The excise was intimately bound up with the guild system, to the extent of presuming that handicrafts were carried on only in the towns, and that the open country was supplied with domestic and foreign goods and manufactures only through the towns, and that both town and country would therefore have to pay the consumption tax levied in this way.

The excise varied from one province to another, as was the case with all the other institutions of the state, but it was well administered in detail, afforded a large net revenue and was "one of the most effective means for the aggrandizement of Prussia, through the supplies of money which it furnished for carrying on war."<sup>2</sup>

At the same time the Minister of State, Struensee, declared that the toll and excise system, of which he had the direction, was like a chaos brought about by blind chance. In the year

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<sup>1</sup>J. G. Hoffmann, *Lehre von den Steuern*, pp. 315 *et seq.*

<sup>2</sup>*Immediatbericht* of Finance Minister von Bülow, January 14, 1817.- Dieterici, pp. 65 *et seq.*

1817 there were in force, in the old provinces alone, 57 toll and excise tariffs, comprising 2775 taxed articles.<sup>1</sup> In Prussia and outside of Prussia, the excise was condemned on account of the bother and annoyance which it involved, according to Finance Minister von Bülow's declaration. The abolition of the earlier organization of industry and of the industrial privileges which it afforded the towns, gave the towns an added grievance in connection with the excise and so increased the dissatisfaction. The reform took the direction of an abolition of the old system and its replacement by a few productive and not oppressive consumption taxes (flour, meat, beer, wine, spirits, tobacco). According to Bülow's scheme, the tax was to be confined to the place of production, and where that was not practicable, as in the case of the consumption of meat in the open country, it was to be replaced by other taxes. In its report of June 20, 1817, which took up Bülow's plan, the tax commission of the *Staatsrath* went still further and proposed to abolish the grist tax entirely,<sup>2</sup> condemned the tax on meat, at least in the form proposed, modified the few remaining consumption taxes included in the plan, as being too burdensome, and reduced the revenue to be derived from them. They disputed Bülow's view that the grist tax was to be regarded simply as an advance on the part of the working classes, the burden of which they could shift to their wages; they also found that the other consumption taxes, although not falling on articles as necessary to subsistence as bread, still imposed a proportionally heavier burden on the poorer classes than on the wealthy. Further, they objected to the method of collecting the grist tax (at the mill) as being ill suited to the purpose, but favored a taxation of the wheat bread consumed by the wealthy by means of a fixed furnage levied on the bakers. The taxes on beer and on spirits were likewise to be fixed, and

<sup>1</sup> Dieterici, p. 69.

<sup>2</sup> The grist tax, says the report, will be very odious to the people; it falls on the prime necessary of life, taxes the physical existence of man, and taxes it in a much higher degree for the poor man than for the wealthy, because the former consumes more bread than the latter. Neither England, with all its ingenuity in inventing taxes, nor France, in the days of its worst tyranny, had ventured to introduce such a tax. - *Ibid.*, p. 135.

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the former also lowered. (The scheme proposed to levy a tax of about eighteen per cent. *ad valorem* in the form of a malt tax.)

The report of the Council therefore takes a position as far opposed as possible to the old system of excise. While it accepted Bülow's proposition of a moderate protective and fiscal tariff system (for the most part on a basis of ten per cent., in exceptional cases rising to thirty per cent. of the value, but levied by weight, it sought to avoid as far as possible any internal tax on consumption, partly to obviate over-taxation of the lower classes, partly to avoid interfering with business. It was inclined, even to a much greater extent than the finance ministry of those years, to a simple system of direct taxation, quite in the spirit of the times, which was much influenced by the youthful science of Political Economy and Finance.<sup>1</sup>

§ 270. The results of many years of discussion were finally embodied in the legislation of the years 1818-1820.

The aggregate annual expenditure of the Prussian government amounted at that time to 51 million thalers. Of this, ten millions was covered by the receipts from domains and the like; the remainder, amounting to 41 millions, had to be provided

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<sup>1</sup> In his reply to the report of the Council Bülow says: "It is an irrefutable truth that the necessities of the nations today, since the establishment of standing armies, can no longer be defrayed by means of direct taxes alone. It is likewise true that the indirect taxes have been the foundation of the greatness and prosperity of those states which make use of them as well as of taxes on realty to cover ordinary expenditures, and resort to personal taxes only by exception from the rule, in extraordinary cases. England and old Holland are examples of this, and Prussia would certainly not be what she is without the indirect taxes. But Prussia can also not remain what she is without considerable indirect taxation. Indirect taxes alone will avail to meet the necessities of an army and to keep the country in such a state of defense as is required by a territory extending from Memel to Saarlouis. Prussia will have to resign its existence if it confines itself to direct taxation. Whatever may be our future - wars have been, wars will be ..... and for these let us reserve the direct taxes, as England and Holland do - the sentiment of patriotism at such times overcomes the difficulty there is in collecting them in ordinary times ..... An impost on bread, meat and clothing has the effect of an immediate impost on wages, is therefore not borne by the laborer himself who consumes the goods, but is advanced by whoever employs the laborer, and the latter recoups himself in the price of the goods. In the case of taxes on beer and spirits, the laborer pays the tax only in case he has laid by so much in order to buy beer and spirits :...." - Dieterici, pp. 166 et seq.

for by taxes, eight millions from import taxes levied under the law of March 26, 1818, five millions from the internal taxes on spirits, crude wine and leaf tobacco, collected under the law of February 8, 1819; nearly four millions from the salt business; three and one-half millions from stamp taxes (Act of March 7, 1822); ten millions from the old land tax; six and one-half millions from the class tax (Act of May 30, 1820); one and three-fourths millions from the trade-license tax (Act of May 30, 1820); and finally (under an act of the same date) two and a quarter million thalers from the grist and slaughter tax.

It appears hereby that the form of legislation finally adopted was a compromise between the views of the Ministry of Finance and those of the *Staatsrath*, between the views which agreed more nearly with practice and sought to retain the excise in an amended form,<sup>1</sup> and the abstract liberal views of the times as expressed in the report of the *Staatsrath* (Wilhelm von Humboldt presiding). Instead of the taxation of flour and meat proposed in the original plan, was substituted a personal tax in the form of a class tax. Only in the case of the larger cities (the Act enumerates 132) the grist and slaughter tax were to be added as supplementary, for the reason that the mobility and the great numbers of such a city population was held to render the assessment of a class tax impracticable.<sup>2</sup> But in these cases the tax on flour and meat was to be collected in the form of a gate toll.

In addition to this, five million thalers was counted on from internal consumption taxes on spirits, beer, wine and tobacco, and four millions from the salt monopoly. There was from the outset much greater unanimity as to the import duties (amounting to eight millions). The taxes on consumption accordingly yielded in the aggregate about one-half the tax revenue.

<sup>1</sup> The promemoria of the projected legislation for equalization and regulation of taxes in 1820 recites that in nearly all countries the great cities have for a long time past levied taxes on beverages, meat and other victuals, to meet their municipal expenditures, necessitating an inspection of the goods entering the gates; this has become usual and is not felt as an appreciable disturbance of business. - Dieterici, p. 274,

<sup>2</sup> J. G. Hoffmann, *Lehre von den Steuern*, p. 159.

§ 271. The grist and slaughter tax, which continued in force in Prussia for half a century, was regulated as follows:

It adopted the traditional form of the gate toll; even at that time there was a very general apprehension that the price of bread and meat would not fall in proportion if the tax on those articles were abolished. On the other hand, personal taxes, such as the class tax, were an unfamiliar burden, which demanded at stated times and in a lump sum what had previously been paid penny by penny in the price of bread, meat, etc. At the same time the method of levying the tax on flour and meat depended on the differentiation of industries and the concentration of the work of grinding and slaughtering in a few places; at that time this process of concentration had not developed to any extent in the open country or in the small towns of Prussia. The greater part of the inhabitants slaughtered what was needed for their own consumption; to a great extent they even had their own corn ground for their own use, and took their own dough to the bakers. The personal tax was preferred to the still greater annoyance which would have attached to a grist and slaughter tax under these circumstances. In the western provinces, even in the larger towns and without this special incentive, the preference for the personal tax was relatively very great. Altogether the class tax was paid by about six-sevenths of the population of Prussia and the grist and slaughter tax by the remaining one-seventh.

The rate of the slaughter tax was about three pfennigs (old style per pound of meat; the average annual consumption of meat was seventy pounds per capita of the inhabitants of Prussia liable to the tax;<sup>1</sup> the rate of consumption varying greatly from one place to another (Berlin, 113,33 lbs., Rhine provinces 75 lbs., Pomerania 52 lbs.). The annual revenue from the tax was one and one-sixth million thalers (counting the average of the years 1833-1838).

The grist tax amounted, on rye, to about 9.50 per cent., on wheat to 18.66 per cent. of the average price. It was estimated

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<sup>1</sup> Hoffmann, pp. 332 *et seq.*

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that in the year 1821 the average annual consumption per capita of the population liable to the grist tax was 77 pounds of wheat and 191.50 pounds of rye. The receipts from the tax (counting the average of the years 1833-1838) was one and one-half million, and was distributed among the various parts of the country in such a way that the province of Brandenburg paid 357 pfennigs (old style)<sup>1</sup> - Berlin 410, Saxony 304, Pomerania 289, Prussia 235, Silesia 225, annually, per capita of the population liable to the tax.

§ 272. Under the earlier Prussian tax system the brewing and distilling industries<sup>2</sup> were untaxed outside the towns, while within the towns they were subjected to considerable taxes. It therefore became desirable, on fiscal grounds, to reserve these two industries to the towns, which was possible only so far as the landed estates had not, as was often the case, secured the privilege of brewing and distilling. By an edict of October 28, 1810, the urban taxes on brewing and distilling were extended to the rural establishments. As in other matters, so also at this point, the provisional tax reform of 1810 was revised in detail after the war, and was permanently regulated by the Act of February 8, 1819; with respect to the method of collecting the tax on spirits this Act was further supplemented by the regulations of December 1, 1820, and January 10, 1824. The tax on spirits was to amount to 15 pfennigs (counting 288 pfennigs to the thaler) per quart of brandy of 50 degrees proof. It was to be levied on the capacity of the mash-tub, that is to say, of the vat in which the materials were mixed in order to develop the spirits, and it was to be levied anew every time the vat was filled. The computation in the year 1820 was that a quart of brandy requires a mash-tub capacity of twenty-five quarts. As early as 1824, and again in 1838, it was found necessary, on account of a more effective utilization of the capacity, to increase the rate of taxation (one-fifteenth thaler per 20

<sup>1</sup> 360 pfennigs = 1 thaler = 3 marks = 71.4 cents.

<sup>2</sup> Hoffmann, pp. 262 *et seq.*, 276 *et seq.*

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quarts mash-tub capacity, according to the order of June 16, 1838). A reduction to eight-ninths and afterward (1838) to five-sixths of the full rate of taxation was made in favor of the small rural distilleries. The receipts from the tax were, on an average for the years 1833-1838, 5.25 million thalers, of which Brandenburg alone paid one million. The tax on beer was levied in a manner similar to that on spirits. It was levied on the malt, at the rate of two-thirds of one thaler for each hundredweight of malt mashed. As a concession to rural breweries producing beer for household consumption, they were permitted to come to an agreement with the tax officials as to a lump sum to be paid annually. The income from the tax on malt amounted (after deducting drawbacks to 1.25 million thalers, counting the average of the years 1833-1838; of this Brandenburg paid 282,000 thalers, Prussia 180,000 thalers, Posen 67,000, Pomerania 49,000, Westphalia 50,000, the Rhine Province 199,000. Hoffmann estimates that the average annual consumption at his time was very near ten quarts of brandy per capita, together with thirty quarts of beer in Prussia (1833-1838). "Somewhat considerable" is the consumption of beer in the large and busy towns; reaching 55 quarts in Brandenburg, and 53 quarts in Saxony, as contrasted with 20 quarts in Pomerania, 19.5 in Posen, 12.75 in Westphalia. This was at the time preceding the development or the resuscitation of skilled brewing in the German towns. Later events have shown how readily the consumption develops with the development of skill in production and the growth of wealth. The tax on spirits was the heavier also in point of rate of taxation; it amounted, in fact, to one-half the average price, while the tax on beer amounted to one-sixth.

§ 273. The Act relating to the tax on beverages, February 8, 1819, also regulated the taxation of domestic wines.

On account of the burdensome and annoying measures of control involved, it was decided not to adopt the more productive form of tax which is employed in the true wine-producing countries (South Germany, Switzerland), viz., the taxation of the

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goods at the point of entrance into the wholesale or the retail trade. At the same time the great variation in annual yield (from 1 to 20) would not admit of taxing on the basis of the area planted in vines. The basis chosen was the quantity of wine produced each year, the rate of the tax varying by six gradations according to the quality of the land cultivated (varying from one-fourth thaler to one and one-sixth thaler per bucket of 60 quarts).

The income from the wine tax was, for example, in 1829, 204,000 thalers; 1830, 9,000 thalers; 1831, 16,500 thalers; 1835 224,000 thalers; being on an average for the years 1829-1838, 116,000 thalers.

The disproportion between this revenue and the great difficulties of its collection, as well as the annoyance to which it subjected a great number of wine-growers, for the most part very poor, was recognized even at that time. But at the same time it was recognized that expediency here was in conflict with equity, if any account were taken of the heavy taxation of spirits as well as of beer.

The taxation of domestic tobacco was treated in a not dissimilar manner. The Act of February 8, 1819, prescribed a tax of one thaler per hundredweight of the dried leaf, to be paid by all persons cultivating more than five square rods (from 1828 the specification was: more than six square rods). The objectionable means of control necessary to hinder concealment of the taxable tobacco occasioned the issuance of a Cabinet Regulation of March 29, 1828, which made the superficies of the land cultivated in tobacco the basis of the tax; arranging the land in four classes according to its average yield, and taxing it at the rate of three, four, five and six silver groschen per six square rods; the assessment of the land was to be made by the officials of the circle. The revenue derived from the tax, on an average of the years 1829-1838, was 150,000 thalers, of which one-half was paid by the province of Brandenburg.

§ 274. To these objects of the internal taxes on consumption, which were established at the time of the revision of the Prussian



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tax system during the early decades of the nineteenth century, later decades have added another article of consumption; a product of the modern application of science which has greatly affected the course of German agriculture and industry, and has triumphantly replaced a colonial product by a domestic one.

This is beet-root sugar.

Even as late as 1841 J. G. Hoffmann<sup>1</sup> was of opinion that the replacing of the consumption tax on Indian sugar by a tax on domestic sugar production is not to be thought of. The production of sugar from beet-roots could be profitable only so long as the price of Indian cane-sugar was abnormally raised by temporary circumstances. Moreover an industry which was carried on in a great number of small establishments scattered over the whole country could never be taxed so as to yield revenue to compare with the productiveness of the import duty on foreign goods. Cane-sugar was at the same time, fiscally, the most productive of all the articles of consumption imported into the German Zollverein, etc.

The development of half a century past speaks a different language.<sup>2</sup> In the fiscal year 1836-1837 there were in Germany 122 beet-root sugar factories which produced an aggregate of 1408 tons of raw sugar, while in the year 1884-1885 there were 408 factories which produced 1,146,740 tons. At the outset we had an average annual product of 11.50 tons for each factory; it is now 2811 tons for each factory (1 ton = 20 cwt.). The beet-sugar has not only crowded the colonial sugar out of the domestic market, but is competing with it on an equal footing in the world's market. This development has been appreciably furthered by the, taxation, in that it on the one hand favored the infant industry as against the foreign product, and on the other hand furnished an incentive to a progressive perfection of the method of utilizing the beets, by levying the tax on the beets.

The first tax on beet-sugar in Prussia was laid by the ordi-

<sup>1</sup> *Die Befugnis zum Gewerbebetriebe*, pp. 431 *et seq.* Cf. *Lehre von den Steuern*, p. 362.

<sup>2</sup> Paasche, *Conrad's Jahrbücher*, 1887. N. F. vol. xv. p. 274.

nance of March 21, 1840.<sup>1</sup> It was quite moderate: three pfennigs per hundredweight of the crude beets, that is to say, according to the sugar equivalent of that time (20 cwt. of beets = 1 cwt. sugar), one-sixth of one thaler per hundredweight of sugar, while at the same time, under the Zollverein tariff of October 24, 1839, Indian cane-sugar paid five thalers. Gradually, as the new industry secured a footing, and with the progress in the utilization of the beets, the rate of the tax was raised. After an agreement had been reached, on April 4, 1853, according to which this tax was to be made general and uniform throughout the Zollverein, the rate was fixed (dating from September 1, 1858) at one-quarter of one thaler per hundredweight of beets. With the sugar equivalent obtainable at that time (1:11) this meant the same as 2.75 thalers per hundredweight of raw sugar, while the import duty on raw sugar amounted to 4,25 thalers.

The duty on raw sugar yielded in 1847, 7,000,000 thalers, and in 1860 only 393,000 thalers. Contrariwise the tax on beet-sugar amounted in 1845 to 194,500 thalers, and in 1860 to 9,477,000 thalers.<sup>2</sup>

The change which supervened during the course of these twenty years is sufficiently indicated by these figures.

§ 275. In connection with the preceding we may properly discuss briefly the chief import duties of the period preceding the present.

As is well known, the purpose of the Prussian tariff of 1818 was, apart from a moderate protection of domestic industry, to impose a consumption tax on foreign goods at such a moderate rate as would comport with the difficulties of superintendence of so disadvantageous a tariff boundary. The duties were based on the weight of the goods, as there had been sufficient opportunity in earlier times to learn to appreciate the annoyances of an *ad valorem* tariff.<sup>3</sup> The duties were for the most part calculated on a

<sup>1</sup> Hoffmann, *Gewerbebetrieb*, p. 435.

<sup>2</sup> C. J. Bergius, *Grundsätze der Finanzwissenschaft mit besonderer Beziehung auf den preussischen Staat* (1865), p. 375.

<sup>3</sup> Dieterici, *Steuerreform*, pp. 81 *et seq.*

oasis of ten per cent, of the value, rising in the case of articles of luxury as high as thirty per cent. and over. In general, as compared with the wealthier foreign countries (England, Holland), the duties determined upon were regarded as low, out of consideration for the limited means of even the better situated classes in Germany at that time. The opinion was better founded at that time than now, that articles of consumption coming from abroad could bear a relatively higher taxation than those produced at home because they were to a greater extent articles of luxury and were therefore consumed by the wealthier classes.

International trade in the great staple products of daily consumption, such as we see it today, was at that time so far removed from the thoughts of those best able to judge, that Hoffmann, even as late as 1840, declared<sup>1</sup> it quite impossible for Great Britain to import from abroad as much as 33,000,000 bushels of corn in case of need, whereas by 1871 Great Britain was already importing as much as 44,333,000 hundredweight of wheat and wheat flour alone, and in 1883 almost twice that quantity - 84,500,000.<sup>2</sup> The import duties, therefore, furnished the chief field for the *impôts volontaires* which experience had commended even in earlier times. It also appeared from experience with the internal taxes on consumption that several of them (wine, tobacco met with difficulties of administration which were much greater even than the difficulties attaching to an unfavorable tariff boundary. A tax payment which must be regarded as moderate and equitable in view of the tax-paying capacity which showed itself in the consumption of the goods, could not be collected without great annoyance on these articles in the form of an internal consumption tax, but quite readily in the form of an import duty.

§ 276. The chief articles were sugar, coffee, wine and other spirits, and tobacco. Of the average annual revenue of 8.50 million thalers which the import duties yielded during the years 1822-1828, these four articles furnished appreciably more than

<sup>1</sup> *Lehre von den Steuern*, p. 360.

<sup>2</sup> *Statistical Abstract for the United Kingdom*, 1886, p. 70.

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one-half (4.80 millions); sugar coming first (2 millions), then coffee and wine (each rather over 1 million), and last of all tobacco ( $\frac{1}{2}$  million). The rates of duty were: raw sugar 5 thalers, coffee 6.50 thalers, wine 8 thalers, tobacco 5.50 thalers (manufactured tobacco 11 thalers).

Apart from the change wrought in the production of sugar, a great increase has also taken place in the consumption of sugar in Germany. In the Zollverein<sup>1</sup> the per capita consumption was

In the year	1840	4.69	pounds
"	"	1864	9.29 "
"	"	1871-73	12. " <sup>2</sup>
"	"	1881-83	14.6 "
"	"	1883-87	15.7 "

The consumption of coffee in the Zollverein rose from two pounds per capita during the years 1836-1840, to near five pounds during the years 1881-1887. The increase in consumption is appreciably less than in the case of sugar, besides which a change in the habits of life greatly affects the increase in the consumption of coffee without its necessarily implying an equally decided increase in wealth. It is otherwise with the consumption of sugar. The latter is a clear indication of the prosperity which the industrial life of Germany has experienced during the century, although the cheapening of sugar has also contributed its share to the development.<sup>3</sup>

The amount of the sugar tax (including the duty) was, during the years 1844-1855, .57-.61 marks per capita, while in 1882-1883 it was 1.47 marks;<sup>4</sup> or, counting the aggregate revenue, it rose during that period from 18 million marks to 67 million marks.

<sup>1</sup> Bienengräber, *Statistik des Verkehrs und Verbrauchs im Zollverein 1842 bis 1864* (1868), p. 33.

<sup>2</sup> *Statistisches Jahrbuch für das deutsche Reich*, published by the Imperial Statistical Bureau (1888), p. 132.

<sup>3</sup> The price of a cwt. of refined sugar was, in 1836, 28-30 thaler, in 1867, 16-18 thaler.- *Bienengräber*, p. 33.

<sup>4</sup> The rate of taxation was, from and after Sept. 1, 1844, .15 marks per cwt. of crude beets, from and after Sept. 1, 1850, .30 marks, after Sept. 1, 1853, .60, after Sept. 1, 1858, .75, after Sept. 1, 1869, .80, after Aug. 1, 1886, .85 marks. - *Statist. Jahrbuch des deutschen Reiches*, 1888, p. 192.

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The amount of the duty on coffee rose from .43 mark per capita during the years 1836-1840, to .98 mark on an average during the years 1883-1887. During the early decades of the Zollverein the duty was 6.50-6.66 thalers per hundredweight, but was afterward, from and after January 1, 1854 (in consequence of the inclusion of Hanover and Oldenburg), reduced to 5 thalers.

In earlier years<sup>1</sup> wine was subjected to an import duty in the Zollverein of 8 thalers per hundredweight, but from 1854 it was reduced to 6 thalers (8 thalers for wine in bottles). The tariff of July 1, 1865, reduced it again to 4 thalers on wine, whether in casks or bottles, but in later years it has again been considerably increased. In May 1885 it was fixed at 48 marks per hundred kilogrammes for wine in casks (equal to the original duty levied by the Zollverein) and a somewhat heavier duty on wine in bottles and on champagne. The amount of the duty on wine in 1836-1840 was .16 mark per capita of the population, as compared with .31 mark in 1882-1887.

Tobacco, raw and manufactured, yielded an income in import duties of .15 mark per capita of the population included in the Zollverein in 1836-1840, as compared with .78 mark in 1885-1887 (aggregating in 1887, 38 million marks). Both the duty and the internal tax on tobacco were considerably increased by the Imperial legislation of July 16, 1878. On raw tobacco the duty is 85 marks per hundred kilogrammes (previously 24 marks, on manufactured tobacco 180 marks, on cigars 270 marks. In order to be able to increase the rate, the internal tax on tobacco was again levied on the weight of the leaves (45 marks per hundred kilogrammes), and yields, 1882-1887, .87 mark per capita (aggregating in the year 1886-87 47.50 million marks).

§ 277. The brief survey just given of the development of taxes on consumption is primarily intended to afford the substructure for a further discussion of the system of taxation. It

<sup>1</sup> *Bienengräber*, p. 83.

is only at a later point<sup>1</sup> that questions regarding the existing German and Prussian legislation will be taken up and discussed in connection with the development of the system and policy of taxation in other countries. We will now give some attention to one phase of the old-time excise, in which it shows its tenacity as well as its expediency under all the changes of times and circumstances.

What I have in mind is the taxes on consumption levied for municipal purposes, which have experienced all the variations of favor that have affected consumption taxes and indirect taxes generally.<sup>2</sup>

The period of liberal reform of the years 1808 and onward in Prussia<sup>3</sup> was primarily a German version of ideas coming from France and partly from England. The leading statesmen concerned in the reform were filled with a high-strung doctrinarianism. Hardenberg declares straight out that he is going to introduce into Prussia the ideas of the French Revolution. Both he and Altenstein wished, among other things, to introduce the democratic principle of election in the army, so that the subaltern officers were to be chosen by the soldiers and the inferior officers by the subalterns. Even the more moderate statesmen, who have been more appreciatingly criticised by later historical research, such as Stein and Vincke, give in their adherence to a far-reaching doctrinarianism, only they borrow their ideas from England, not from France. Stein's notions about self-government are almost as highly overwrought as Hardenberg's French ideals. His opposition to the Prussian professional official, class, his predilection for the administration of the state by burghers and farmers, is just as visionary an application of abstract notions as the enthusiasm for the French ideas.

In taxation we have already met with something similar. After the tentative efforts of the earlier years of the reform

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<sup>1</sup> In Book III., omitted in this translation.

<sup>2</sup> Cf. von Reitzenstein on indirect consumption taxes by the commune (*Conrad's Jahrbücher*, 1884, N. F., vol. viii. pp. 1-100, vol. ix. pp. 219-294).

<sup>3</sup> Ernst Meier, *Die Reform der Verwaltungsorganisation unter Stein und Hardenberg* (1881).

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are past and the reform of the years 1817-1820 finally achieved, the doctrinarianism of the new economic theory takes sides, as we have seen, on one side and on the other. One side enthusiastically demands unconditional abolition of the excise, exemption of the lower classes, freedom of internal trade; the other side is occupied with arguing concerning the theory of the shifting of every tax on articles of necessary consumption to wages and to the consumers of the service rendered by the laborer. That side finally wins which differs least from the actual facts of tax administration and demands the least in the way of innovation during this time of returning sobriety. The concessions that were made to the other side were confined to a little patchwork, which, as was the case with so many other things in the constitution and the administration of that time, was not seen until a later day to be a necessary result of circumstances.

Such was the case with the remarkable arrangement by which the wealthiest and most advanced portions of the Prussian population were exempted from the class tax in order to be subjected to an equivalent in the form of the grist and slaughter tax of the rehabilitated octroi.

The further development of the class tax must tend to an alteration of this condition of things; equally with the revival of French-English economic doctrinarianism that supervened at the middle of this century. But only the positive side of this development was calculated to last. The exemption of the towns from the new personal taxation, to suit Adam Smith's pusillanimous theory of the income tax, was bound to disappear. On the other hand the dissatisfaction with indirect taxes, to which the grist and slaughter tax in Prussia became obnoxious (1873), was for the most part a symptom of that doctrinarianism which enjoys a popular triumph today and is replaced by its opposite tomorrow. The growing necessities of the municipalities which, together with the state, had made use of this form of taxation,<sup>1</sup>

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<sup>1</sup>Of seventy-six Prussian cities which were consulted early in the sixties as to the expediency of abolishing the grist and slaughter tax, only a few had favored the measure. - Faucher's *Vierteljahrschrift für Volkswirtschaft*, 1864, p. 160.

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brought them in the course of time to appreciate the permanent value of the old municipal *Ungelt* to the municipal treasury, and directed their attention to the instructive development of French legislation on this head.

§ 278. In the matter of tax legislation, as in legislation touching industrial matters generally, quite in contrast with the ever-recurring crises in its political constitution, France ordered its affairs in a stable manner immediately after the great upheaval of the first Revolution. This goes to show the sagacious character of the French administration, as well as the conservative side of French character.

In this reaction of reason against the Revolution, approved expediency presently took the place of Physiocratic doctrine. The first act of violence of the Revolution (July 12 and 13, 1789) was the storming of the octroi offices of Paris. In the capital as well as in the provincial towns the system of gate excises was enforced, differing from the old Prussian system in this, that ever since the thirteenth century, and especially since the fourteenth century, this tax had served the purposes of the communes and municipalities, while the state had only to a limited extent drawn a revenue from the octroi. The name, even, was derived from the royal authorization which it was necessary for each city to secure. Under this form there was in force a most comprehensive taxation of articles of urban consumption, the rates and amounts of which may be inferred from the fact that in 1789 Paris alone paid 36 million francs, in spite of all the hardships and exemptions which characterized the ancient régime. Turgot and the other Physiocrats, and the cahiers of the nobility and of the third estate, demanded its abolition. The National Assembly passed a resolution to that effect on May 1, 1791, amid the rejoicing of the Parisian populace. But as no adequate substitute had been created, the failure of the customary revenue resulted in great confusion, especially in Paris and Lyons. The municipal supplementary real estate tax and the personal



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property tax established by the National Assembly were insufficient; the administrations of the communes came to a standstill; nearly all the cities demanded the re-establishment of the octroi; as early as 1797 steps were taken by law in that direction; in 1799 the octroi was re-established in Paris, and directly afterwards in the other cities, at first optionally. In 1805 the number of cities which collected the octroi had risen to 3262. The Laws of 1809, 1814 and 1816 gave this class of taxes their permanent form.

§ 279. The new features of this legislation, as contrasted with the arrangement under the old political system were such as were made necessary by the new political system itself, viz., uniformity of administration, abolition of class exemptions, removal of all obtrusive harshness, and rigor in respect of kind and scope of taxes on consumption. But the characteristic substantial nature of this taxation remains the same as of old, because it was found expedient under the new political régime as under the old. Its fundamental traits are as follows.

The object of the octroi, as contrasted with supplementary local taxes added to the national taxes, is to afford independent means for meeting the expenses of a local administration. It is levied on objects of local consumption. The selection of these objects of taxation, as well as the rate at which they are to be taxed, is left to the discretion of communal councils. All doubt as to this right of local discretion was removed in 1852 by decision of the Superior Court. In fact, the ordinances of 1809 and 1814 had, for the protection of the poorer classes, set a limit to the taxation of the necessary articles of sustenance. But this limit was removed by the law of 1816 and was replaced only by administrative advisory regulations. By tradition the number of taxable articles is very comprehensive; it comprises beverages and liquors, food products, fuel, fodder, building materials. The general schedule of February 12, 1870, adds, as a sixth category, all other things. The same schedule prescribes maximum rates which in the case of each article are graded according to the

number of inhabitants in the commune. The octroi is collected on articles imported from abroad at their entrance into the commune, on articles produced in the place it is collected within the commune. Since 1814, however, it has been expressly provided that the latter class of goods are to be taxed equally high with similar goods coming from abroad, in order to secure freedom of trade within the country and to prevent local protective duties. A superposition of national and communal taxes is sought to be avoided. For this reason those things only are by preference subjected to an octroi in the general schedule which are exempt from national taxes, spirituous beverages being an exception from this rule, and an exception of very considerable importance.

In the year 1880, out of a population of 37.50 millions, in France, more than 11 millions were subject to the octroi; the gross receipts rose from 54 million francs in 1831 to 277 millions in 1880 (net 255 millions) of which nearly one-half was derived from beverages and liquors (122.50 millions). The cost of collection is lowest in Paris (5 per cent.), where the receipts from the octroi are as great as those of all other communes taken together. Heavily taxed articles, as for example wine (12 francs per hectolitre), have been increasing in consumption in spite of the high tax (the consumption in Paris in the years 1841-1845 being 100 litres per capita of the population, in the years 1872-1877, 215 litres).

All considered, this class of taxes is a striking example of the triumph of expediency over doctrinarianism, originating in France, but bound to seek and to find a foothold in other countries.

## V. STAMP TAXES.

§ 280. The stamp fee, says K. H. Rau<sup>1</sup> has been pretty generally adopted on account of the ease of collection and superintendence. It is based on a legislative requirement that stamped paper must be used for certain documents, the price of the paper being fixed according to the nature of the document to be

<sup>1</sup> *Finanzwissenschaft* (1865), sec. 231.

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inscribed on it, and the absence of the stamp affords an obvious evidence of the evasion of the law the instant the document comes under the eyes of a government official. All transactions, as Rau goes on to say, which necessitate a written record, can therefore be subjected to the stamp duty, and fees exacted on a great variety of occasions can be collected in this form ... Latterly the adhesive stamp adopted in the letter-post has also been made use of for collecting this fee in cases where, for any reason, the stamped paper is not obtainable, or at any rate has not been used; and this is something of a relief.

With complete *naïveté* Cameral Science here records a passage of financial history, and then reproduces as part of its "Fundamental Principles" something that went to make up the elements of a bygone political and fiscal system.

It is Rau himself who lays stress on the difference between the Fee [*Gebühr*] and the Tax, characterizing the fee as the "accompaniment of an act of government," an act "which would be no less necessary even if no particular payment were demanded for it, so that it can evidently not be regarded as performed in consideration of the payment:" Now, this conception of the fee cannot be reconciled with the discussion of the stamp fees just cited unless we accept as a reality the pretense of a governmental act with which the old fiscal methods disguised the stamp-tax: But just how there can in reality be and governmental act concerned in the fact that stamped paper is used for certain documents between private individuals is not comprehensible. What we have to do with is certain transactions on the part of private persons, to which the only relation the government bears is that of collecting a tax, using for the purpose the convenient form of the stamp. The pretense was less transparent in the cases where the government, with some additional inconvenience to all concerned, added its stamp to the document after it was completed, in order to keep a public register of such instruments (as was the case in Prussia. with respect to bills of exchange and the like, even during the last few decades). But this pretense

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<sup>1</sup> Sec. 227; cf. sec. 86 of his *Finanzwissenschaft*.

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has latterly had to make way, as being a useless burden both on the government and on the individuals, and its place has been taken by the simple accepted expediency of the stamp, a fact of which even Rau was aware.

The stamp honestly confesses that it is nothing more than a useful form of taxing certain objects, or of collecting fees from objects which have no intrinsic connection whatever with the "fee." Being a piece of paper, it is well adapted for objects which are in the form of a piece of paper, or are wrapped in paper - for documents as well as for playing cards, for instruments of exchange as well as for articles of consumption. It may serve for the collection of fees as well as for the collection of taxes.

§ 281. The stamp-tax was invented, according to Beckmann<sup>1</sup> in the country in which everything used by a man is taxed; that is to say in Holland. The view that something similar was in use under the later Roman Emperors, rests on an erroneous reading of a passage in the text of a law.

It was first introduced by an Act of August 13, 1624. The States General had offered a large reward for the invention of a new tax which would not press heavily on the inhabitants, and at the same time yield a large revenue to the republic; an ingenious man invented the *impost van bezegelde brieven*,<sup>2</sup> to which the prize was awarded. No petition was to be entertained by the government or by any official, national or municipal, which was not inscribed on stamped paper; no legal document, no receipts or other documents were to be written by notaries, attorneys, etc., no papers of any kind whatever were to be recognised as evidence in court, unless a certain sum had been paid under the name of a stamp tax, varying with the kind and value of the article in question. In justification of the tax it was recited that its amount in any individual case was insignificant, that the

<sup>1</sup> *Beiträge zur Geschichte der Erfindungen*, vol. ii, (1785), p. 304.

<sup>2</sup> An account is given by Boxhorn, *Disquisitionum politicarum casus* 59 (2<sup>d</sup> ed. 1651).

poorer classes of the people were almost entirely exempt from it, and that the well-to-do burghers would pay a considerable revenue to the state on account of their frequent need of using stamped paper.

According to Adam Smith<sup>1</sup> there is no art which one government more quickly learns from another than the art of drawing money out of the pockets of the people. Agreeably to this maxim we find that the stamp taxes spread from Holland over the whole of Europe within a hundred years. They were introduced into England by a late of Charles II. (1671),<sup>2</sup> and their amount by the time Smith wrote was so great that he says it exceeded the total national revenue under the government of William and Mary.<sup>3</sup> It is to be remarked that he recognizes that the stamp tax is but a form under which a variety of essentially different taxes are levied. He declares, for example, that the stamp tax on cards, dice, newspapers and the like "are properly taxes upon consumption."

In France a regulation was published in 1657, and repeated in 1674 under Colbert, regulating the stamping of tinware, which was to prevent the use of a fraudulent material in the ware, but which also confessed to a fiscal aim, inasmuch as "the great expenses of the war necessitate the finding of extraordinary means of payment."<sup>4</sup>

Stamp taxes were introduced into Germany in 1682. They were introduced about the same time into the electorates of Saxony and Brandenburg.<sup>5</sup>

For the present purpose we shall have to be satisfied with reviewing the stamp tax legislation of Prussia of March 7, 1822, which was adopted in connection with the reorganization of the rest of the tax system, and we shall then be in position to make a very interesting comparison of this with the French legislation.

<sup>1</sup> *Wealth of Nations*, bk. v. chap. ii.

<sup>2</sup> Sinclair, *History of the Public Revenue*, part iii. chap. iv.

<sup>3</sup> According to Sinclair it amounted, in 1802, to 3,192,052 pounds sterling.

<sup>4</sup> *Zeitschrift für die ges. Staatswissenschaft*, 1870.

<sup>5</sup> *Mylius Corpus Const. March. P. 4, sec. 5, cap. iii.*

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§ 282. The centre of gravity in the stamp duties, considered as a tax, lies in their imposition on commercial transactions and other similar transactions in business. Prominent among the objects of taxation, from very early times, has been real estate, which in the early stages of economic development was the chief, and still continues to be the most obvious form of property. By prescription of custom real estate was bought and sold in a public way; the assistance of governmental officials at these transactions afforded an equitable claim to the collection of fees and a plausible justification for a heavy tax. Taxes of this kind in individual cases have not only risen to a great height earlier than other taxes, but they have also maintained themselves intact down into the present, as, for example, is the case with the *Enregistrement* in France.<sup>1</sup> This class of taxes were less productive of results when applied to movable property, the taxes on such objects reaching a high rate only in early times, while in later times it has been sought to meet the necessities of business and to obtain an appreciable revenue (if at all by imposing a moderate rate).

Under the Prussian law of March 7, 1822,<sup>2</sup> at the purchase and sale of real estate the notarial publication of the transaction is made the occasion for collecting a stamp tax amounting to one per cent. of the purchase price; in case of a sale of chattels, if the sale is concluded by means of a formal contract, one-third of one per cent. is collected; in case of leases the like proportion of the value of the usufruct contracted for is collected.

In case of inheritance no tax is levied on the transmission of property to descendants or ascendants, whereas on inheritance by less immediate relatives a percentage is collected which rises by gradations from one to eight, according to the remoteness of the degree of relationship. The tax on inheritances and legacies is collected by means of a stamp which is required by the court before whom the partition of the estate takes place.

<sup>1</sup>Wagner, *Finanzwissenschaft*, part. iii, pp. 502-596 (1888).

<sup>2</sup>J. G. Hoffmann, *Lehre von den Steuern*, pp. 418 *et seq.*

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Where no judiciary assistance is exercised the heirs are required to make the payment directly to the tax officials.

The element of the fee falls very much into the background in this class of stamp duties, but it comes into prominence in cases where the tax is not only paid in return for an official act which serves the interest of the private individual, but where the amount of the tax is, at the same time, sufficiently inconsiderable to correspond in some measure to the effort put forth by the official.

This character belongs to the stamp duties on transactions in writing which take place between officials and private individuals in the interest of the latter: applications, petitions, complaints, etc., on the part of private individuals; advice, certificates, decisions, decrees and judgments on the part of the officials. The greater part of these dues consists of court fees.

The usual minimum of the stamp duty is one-sixth thaler on all papers presented by private individuals, and one-half thaler on each official communication (in matters of slight consequence not over one-sixth thaler, and in matters involving less than fifty thalers, nothing). The costs of litigation are fixed according to the value of the object in litigation: one per cent. on the first thousand thalers, one-half per cent. on 1000-20,000 thalers, one-sixth per cent. on any sum exceeding 20,000 thalers. For decisions in courts of higher instance, one-sixth of the charges of the court of first instance is collected.

The income from the stamp tax in Prussia amounted, in 1823-1828, to an average of 2.75 million thalers, in 1829-1834, 3 million thalers, in 1835-1838, 3.50 million thalers. Of this, the stamp on sales of real estate paid 900,000 thalers (1835-1838).

A small amount was derived from the stamp on drafts (77, 000 thalers). Not inconsiderable were the consumption taxes levied in the form of a stamp tax, especially that on playing cards (levied under the form of a monopoly until the Act of June 16, 1838) which for the years 1835-1838 yielded, on an average, 165,345 thalers; also the newspaper stamp tax, 47,736 thalers, the almanac stamp, 43,932 thalers.

The later development of the stamp-tax legislation in connection with the general tax legislation of the German Empire is to be traced in a later portion of the present work.<sup>1</sup> It can only be mentioned here that the stamp tax on bank paper paid in Prussia is set down in the estimates of the Imperial Treasury for 1889-90 (based on the average of the years 1885-1888) at 3,50 million marks; that, further, the stamp on playing cards yielded .75 million marks, court fees 43 million marks (including 7 millions from the stamp tax), the inheritance tax 7 millions, the stamp tax 18.50 million marks;<sup>2</sup> besides which the Empire collected, in round numbers, 20 million marks from stamp duties on securities, brokers' certificates, bills and lottery tickets (under laws of July 1, 1881, and May 29, 1885).<sup>3</sup>

§ 283. In France the field of stamp duties has habitually yielded a rich, and, in some portions, an astonishingly large revenue. The blending of the element of fees with that of taxation in this class of taxes is in that country not only an inheritance from the old political system which consistently avoided letting the subjects see the tax in its true character, and sought to give it such a form as to preserve the appearance of an individual equivalent for each particular payment; this method is no less in consonance with the new political system of the French, which preserves an individualistic character wherever it makes a direct demand on the citizens, and so reduces the tax to the position of a schedule of payments for the cost of production of the public services.<sup>4</sup> At the head stand the Registration Dues (*droits d'enregistrement*), which were re-established by the law of December 19, 1790, and definitely reorganized in their general features by the law of

<sup>1</sup> In Book III., omitted in this translation.

<sup>2</sup> *Statistisches Handbuch für das deutsche Reich*, 1888, p. 197.

<sup>3</sup> *Anlagen zum Staatshaushalt für 1889-90*, vol. i. No. 6.

<sup>4</sup> Vuatrin et Batbie, *Lois administratives françaises* (1876), pp. 483-632. Cf. M. Block, *Dictionnaire de l'administration française* (2<sup>d</sup> ed. 1877), art. "Enregistrement," pp. 877-889. R. von Kaufmann, *Die Finanzen Frankreichs* (1882), pp. 277-306. And especially, A. Wagner, *Finanzwissenschaft*, vol. iii. 502-596.



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December 12, 1798. Then there follow the stamp duties in the narrower sense (*droits de timbre*), recast by the laws of 1790-91, and established on a permanent footing by a law of November 13, 1798. Finally there are the Recorder's Fees (*droits de greffe*), the main law dealing with these being dated March 11, 1799. A great number of laws and regulations have effected changes in these during the course of the nineteenth century. In this field, as in the political system generally, the point of departure for the legislation has been the earlier institutions. Except for this continuity of development, the great compass of this taxation and the relative ease with which it is borne would scarcely be comprehensible.<sup>1</sup>

The old *droits de contrôle*, the origin of which is traced back to Henry III., were, as the *droits d'enregistrements* have been since 1790, an impost on all legal transactions performed with or without the cognizance of the courts. These acts are now classed under three heads according to their character, one class being subject only to a fixed tax, the second class subject to a graduated fixed tax, and the third class subject to a tax proportioned to the value involved. The two former approach the character of fees, and are of slight fiscal consequence relatively to the degree of their interference with business and to the income yielded by the proportional tax, the latter being of greater financial consequence. This latter tax is levied do documents and on events which confer rights of property or ownership; the revenue derived from it amounts (1886) to 413.50 million francs, of which 200 millions come from the tax on inheritances and donations, 139 millions from the tax on sales of real estate, 56 millions from the tax on leases, rentals, evidences of debt, etc. The average rate of taxation of inheritances and donations (ranging from one to nine per cent., the lowest rate mentioned falling on the nearest degrees of kinship is 3.13 per

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<sup>1</sup>In the year 1788 the answer returned by owners of rural property to the circular letter of inquiry of the provincial assembly declares, among other complaints of tax oppression: "Les droits d'enregistrement sont écrasants." --Tocqueville, *L'ancien régime*, p. 299.

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cent.; the average rate on the value of real, estate is 6.61 per cent.<sup>1</sup>

We have here a tax falling heavily on property, and so serving to make good the absence of income and property taxes which is characteristic of the French tax system. It serves this purpose in a somewhat dubious fashion, but quite effectively as judged by results. There is this to be said in its favor, that it is levied in a relatively more agreeable and therefore less oppressive form than the income and property taxes, to which the French character seems to harbor an antipathy.

The stamp dues proper, which are by principle levied on all papers used for business or legal documents, are classed as dimension stamps (according to the dimensions of the stamped paper), proportional stamps (increasing in proportion to the value of the objects), and special stamps of filed value. The latter have been developed especially during the last generation and are attached to a great variety of commercial papers (receipts, brokers' certificates; checks, freight bills, insurance policies and the like). Drafts and securities, on the other hand, are subject to the proportional stamp, which amounts to one-half per cent. on drafts and similar papers and yielded (1886) 14 million francs; on securities (stock exchange papers) it is imposed as a tax on their issue (one per cent. of the face value), and yielded 20 million francs. The aggregate revenue from stamp dues was 156 million francs.

As a third class there is to be added to the preceding the *droits de greffe* (recorder's fees). These are payments for the services of the Recorder, and are therefore of the nature of fees (1886, 8 million francs); with these are to be classed mortgage fees (1886, 5.68 millions).

The growth of this class of taxes, which are of so great importance to France (and so instructive for other states, is shown by the following figures:<sup>2</sup>

<sup>1</sup>Wagner, vol, iii. pp. 523 *et seq.* A supplementary taxation of securities was introduced in 1857, which yielded in 1886, 37 million francs. - *Wagner*, pp. 533 *et seq.*

<sup>2</sup>Wagner, vol. iii. p. 567.

1816	143 million francs
1850	248 " "
1869	461 " "
1886	655 " "

## VI. MONOPOLIES (ROYALTIES).

§ 284. Although the system of royalties, as a fiscal resource, properly belongs to an early stage of the development of the public exchequer, and is intelligible only as conditioned by the circumstances of the epoch to which it belongs, while in connection with the modern public economy it is to be treated of only for the purpose of destructive criticism (cf. secs. 71-77 above), still there is one element of that system which has maintained itself as part of the modern system of taxation at the same time that it dates far back into the past. This is the state monopoly.

Aristotle<sup>1</sup> tells us that the buying up and exclusive sale of a given article was known to the commercial world of antiquity as a favorite method of acquiring wealth; that Thales of Miletus had employed this means to silence those who ridiculed his poverty, by showing that the wise man is poor by choice because he despises wealth although his knowledge gives him the power to acquire wealth. He was able to foresee by observation of the stars that the olive crop would be unusually large; accordingly he bought up all the oil-presses in Miletus and Chios and let them for hire during the harvest at a great profit. Many states have profited by this class of traffic, adds Aristotle (μονοπωλίαν γάρ τῶν ὀνίων ποιούσιν). From other sources we have accounts of a variety of monopolies in Greece and Egypt. It was an obvious expedient for the Greek statesmen, since the state looked upon the control of trade as its proper function.<sup>2</sup>

In Rome the salt monopoly was introduced during the early years of the Republic, because the price of salt had been greatly increased by speculation on the part of the traders.<sup>3</sup> A reg-

<sup>1</sup> *Politics*, i. 4 (Ed. Bekker, i. 11).

<sup>2</sup> Böckh, *Staatshaushaltung der Athener* (2. Ausg. 1851), vol. i. p. 75. Cf. Strabo, 17, p. 798.

<sup>3</sup> Marquardt, *Römische Staatsverwaltung* (1876), vol. ii, p. 155; cf. vol. ii, p. 271. Mommsen, *Römisches Staatsrecht*, vol. iii. p. 1115 (1887), supposes the monopoly to have

ulation in the laws of Justinian also points to the existence of a salt monopoly during the later times of the Empire.<sup>1</sup> During the Republic this monopoly appears to have afforded no considerable profit, but to have been maintained chiefly for the public benefit, to keep the price of salt down (as is the case with the salt monopoly in the canton of Zurich today). Under the Empire however it seems to have been used for fiscal purposes, and to have been farmed out.<sup>2</sup>

§ 285. The mediæval city is to be mentioned in connection with these accounts handed down from antiquity, inasmuch as it shows a predilection for the salt monopoly as a factor in its revenue system, employing it along with a variety of other monopolies, such as that of the retailing of wine (sec. 57). The relative importance of salt during earlier stages of culture,<sup>3</sup> the extreme localization of its production,<sup>4</sup> the public obligation to provide a sufficient supply, readily suggest to the public authorities the expedient of taking over the business of its sale. The salt monopoly was introduced into Zurich by the burgomaster Hans Waldmann (1483). It was chiefly by this means that he improved the finances of the city:<sup>5</sup> all who paid taxes or rendered military service to the town were obliged "to provide themselves with salt from the town." Until that time the trade in salt had been in the possession of one of the thirteen guilds in Zurich which had, even during the thirteenth and fourteenth centuries, had the exclusive sale of salt, selling it in their own salt warehouse in the salt-market.<sup>6</sup>

From the middle of the seventeenth century the salt monopoly

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been such only in point of fact, as a consequence of the low price at which the goods were offered.

<sup>1</sup> *Cod. Just.* 4, 61, 11.

<sup>2</sup> Mommsen, *Römisches Staatsrecht*, vol. ii. (2<sup>d</sup> ed. 1877), pp. 430 *et seq.*, note 7.

<sup>3</sup> V. Hehn, *Das Salz, eine Kulturhistorische Studie* (1873).

<sup>4</sup> Justi, *Staatwirthschaft*, vol. ii. sec. 199, goes so far as to derive the salt monopoly from the mine monopoly.

<sup>5</sup> Bluntschli, *Staats- and Rechtsgeschichte der Stadt- und Landschaft Zürich*, vol. i. p. 353.

<sup>6</sup> S. Vögelin, *Das alte Zürich* (1829), p. 215.

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was exercised by the governments of Berne and Lucerne within their cantonal district, and was gradually extended also to the city's manorial estates. It came to be the custom that each of the ruling classes, during the years for which it had the right to appoint the district governor, was also entitled to farm the salt trade [*Die Besalzung*] of the district.<sup>1</sup>

In the year 1399 the city council of Zurich enacted<sup>2</sup> that the city exclusively was to retail all imported wines; the office of wine master was erected into a civil office, but it was afterward (1578) farmed out.

§ 286. The fuller development of the system of monopolies belongs to the centuries following the close of the Middle Ages and during the rise of the monarchical state. The monarchical power of England, France and certain of the German principalities turned to the monopoly as a means of remedying their financial embarrassments, and at the same time as a means of furthering the public welfare by encouraging industrial activity in various directions. It is instructive to note that such a statesman and financier as Colbert in France, and that the Tudors, especially Queen Elizabeth, in England, furthered the development of the monopolies.

In Germany the Electorate of Saxony led the way. Its example was followed by the Great Elector and his successors. They figure as undertakers of industrial enterprises and bring craftsmen into the country by means of monopolies and privileges.<sup>3</sup> The fiscal glass industry was extended and expanded into a manufacture of mirrors; copper and brass forges, iron and steel works were erected at public expense, and the import of competing goods prohibited or discouraged. The Elector came to a settlement with Luneburg in 1651 with respect to the debts of his house, and at the same time also with respect to new supplies of salt;<sup>4</sup>

<sup>1</sup> Blumer, *Staats- and Rechtsgeschichte der Schweizer Demokratien*, vol. ii. p. 286.

<sup>2</sup> Vögelin, *Das alte Zürich*, p. 214.

<sup>3</sup> Schmoller, *Die Epochen der preussischen Finanzpolitik*, pp. 66 et seq.

<sup>4</sup> Schmoller, *Jahrbuch*, 1887, pp. 866 et seq. Riedel, *Der brandenburgisch-preussische Staatshaushalt*, pp. 20 et seq.

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the edict of February 15, 1652, announced an exclusive royal privilege of the salt trade. The nobility alone retained their right to fetch their salt on a free pass. In 1664 the villages were assigned to certain cities, where they were obliged to get their salt. The income from the salt monopoly was seventy to seventy-five thousand thalers yearly. In the reign of Frederick I. it was developed further and was made to yield a larger revenue by raising the prices. The newly acquired territory, including the salt springs of Halle, superseded Luneburg as the chief source of supply of salt.

Just as the salt monopoly (by means of which the Great Elector had at least intended to cheapen the price of salt) occupied a middle ground between public utility and fiscality, so did also the Brandenburg letter-post<sup>1</sup> which he organized. It very shortly came to be looked up to as a model throughout Germany, and at the same time yielded a considerable net revenue (1685, 39,000 thalers, 1712, 137,000 thalers, 1740, 220,000 thalers). For many decades it was carried on simply under the virtual monopoly afforded by its centralized and efficient administration; it was only after 1712 that the postal regulations reserved an exclusive privilege for the public post.

§ 287. As we approach the nineteenth century, interest centres to those monopolies which have retained a prominent place in the present. The objects included under these monopolies are salt, tobacco, the lottery and the post.

During the eighteenth century the salt monopoly in Prussia was developed into the form of the "salt conscription" (after the French model) by Frederick the Great, in order to meet the growing demands on the treasury.<sup>2</sup> The number of the people and of heads of milch cattle (each person being counted at five pecks and each head of milch cattle at two pecks of salt) was taken yearly, in order to prevent the use of foreign salt; an account was kept with each taxpayer as to the amount of salt which he

<sup>1</sup> Stephan, *Geschichte der preussischen Post* (1859).

<sup>2</sup> Riedel, *Der Brandenburgisch-preussische Staatshaushalt*, pp. 78, 218.

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must legally procure from the royal factory, and at the close of the year a fine was collected for the amount of salt shown by this account not to have been purchased. Not until the early years of the nineteenth century (1816) was the salt conscription abolished, after a uniform price of salt had been established for the whole kingdom (1806).

The government procured the salt<sup>1</sup> partly from its own extensive salt works, partly from private salt works within the country, from which it bought the requisite portion of their product at a price contracted for, partly from abroad (for such portions of the country as, by their remoteness from the places of production of the domestic salt, would be obliged to pay a higher price for the domestic than for the foreign article. The salt was sold to the consumers from the royal storehouses scattered all over the kingdom, in barrels of 405 pounds, and at a uniform price of 15 thalers (decree of January 17, 1820). Anyone procuring this salt for retail trade was obliged to obtain a special permit, and was bound to sell at a certain official price: The net revenue from the salt monopoly amounted, in 1821, for 437,120 barrels, to 3,779,500 thalers; 1836, for 549,580 barrels, to 5,590,257 thalers, or 61-69 per cent. of the gross income (1821, 6.50 million thalers; 1836, 8 millions).

The rate was slightly lowered by a decree of June 16, 1838 (on salt used for cattle and the like), and by a decree of November 22, 1842 (on kitchen salt to 12 thalers). The net income was consequently:<sup>2</sup>

1844	4,315,000 thalers
1861	5,732,850 "

The liberal economic movement, and especially the Radicals, had long looked upon the salt monopoly as a relic of ancient abuses. Economic liberalism was more particularly concerned with opposing the monopoly as such,<sup>3</sup> while the radical popular element condemned the salt tax in any form. In point of fact

<sup>1</sup> J. G. Hoffmann, *Steuern*, p. 250.

<sup>2</sup> Bergius, *Grundsätze der Finanzwissenschaft* (1865), p. 214.

<sup>3</sup> Cf. Bergius, *op. cit.* pp. 217 *et seq.*

this tax was one of the chief causes of the hatred with which indirect taxes had been regarded in France for centuries past. Even Colbert had planned to reduce the price of salt as being taxation of a necessity. But during the eighteenth century the government increased the price of salt to such a figure that in 1788 the French people were deprived of from one-tenth to one-eighth of their entire income under this form of taxation alone.<sup>1</sup> The Revolution put an end (1790) to this feature of the old régime, and abolished the form of a monopoly finally. On the other hand, as was the case with so much else which the Revolution had discarded, the salt tax came to life again under the free-trade administration of Napoleon (the rate since 1806 varying from ten centimes to thirty centimes per kilogram, and fixed at ten centimes after 1848). The great demands on the public treasury since the war of 1870-1871 have advanced the rate only to twelve and one-half centimes.

In Great Britain the reform was of a more radical character. Although the salt tax was enormously increased in the early years of the century during the war (in 1805, to 15 shillings per bushel, equal to fifteen times the market price of the goods), it was entirely abolished by George Canning in 1825.

In Prussia the form of monopoly was done away; but the tax remained. Under the influence of the individualistic drift of the times, a law of the North German Federation of October 12, 1867, repealed the legislation on the subject of the salt royalty and imposed (dating from January 1, 1868) a tax of two thalers per hundredweight.<sup>2</sup> Many expert authorities were more favorably inclined to the abolition of the salt tax than to the abolition of the monopoly, the effect of this latter, apart from its financial results, being to furnish the inhabitants of the country with good salt at a uniform price.<sup>3</sup> In point of fact, the latter view has been put in practice in the

<sup>1</sup> Leroy-Beaulieu, *Traité de la Science des Finances*, vol. i. p. 626.

<sup>2</sup> It amounted in 1868-1887, on an average, to .92 mark per capita; for the Empire, during the years 1886-1887, it aggregated 42.76 million marks. - *Statist. Jahrbuch*, 1888.

<sup>3</sup> Hildebrand's *Jahrb. F. Nat.-Oekon.* (1873), vol. xx. p. 154.



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legislation of Switzerland since 1870, at least in the canton of Zurich. The salt monopoly (which exists in all the cantons) is deprived of its fiscal character in Zurich; it continues to serve only the purpose of supplying the people with the necessary salt. In this connection it is not to be ignored that not only does the salt monopoly continue to exist in all the other cantons, but also that the demand for a lowering of the price of salt, inspired by the example of Zurich; has been voted down by an adverse majority of the popular vote (the country district of Glarus, 1880).

§ 288. The tobacco monopoly deserves special attention at this point, as being the tax monopoly which has a peculiar significance, not only for the past, but for the present, and in all probability also for the future.<sup>1</sup>

The tobacco tax, says Necker in his work on the French finance administration,<sup>2</sup> is of all taxes the gentlest and least obtrusive. Introduced in 1629 into France as an import duty, it was made the subject of a monopoly by Colbert (1674), and rose from a net income of one-half million at the outset to thirty million francs<sup>3</sup> in Necker's time, inside of a hundred years. By 1780 the monopoly extended over the greater part of the country, with a population of 22 millions, certain provinces (Flanders, Artois, Hainault, Alsace, Franche-Comté) being exempt. The monopoly was farmed out; over 15,000,000 pounds of tobacco were sold. The ready sale was to some extent due to the perfection of the royal tobacco manufacture. In answer to the aversion of the new era to state manufactories,

<sup>1</sup> "That a barbarous habit of the Indians," says Viktor Hehn, "of inhaling the smoke of the dried leaves of a stupefying plant into the mouth through a tube or through a roll of leaves, and then exhaling it again, or of stuffing these same leaves, in the form of powder, into the nose, should have spread from the redskins to the white, yellow, and black races all over the globe, and should have taken so deep root among them all, is a fact that merits a good deal of thought." - *Culturpflanzen und Haustiere in ihrem Uebergang aus Asien nach Griechenland und Italien, sowie in das übrige Europa* (2. Aufl., 1874), p.449.

<sup>2</sup> *De l'administration des finances de la France* (1785), vol. ii. p. 104.

<sup>3</sup> Necker, *l. c.* p. 100.

Necker warningly urges that this perfection was the fruit of a long course of experience, and that it would be a useless experiment to discontinue the national factories and allow a number of private undertakings to take their place, as the competition between them might easily lead to deterioration of the product.

But the Revolution made this experiment also, along with so many other experiments. In 1791 the monopoly was abolished, and tobacco culture was freed of restraint after having been confined, in 1781, to certain provinces for the purposes of the monopoly; only a duty was adopted, taxing the tobacco imported from abroad, while the home-grown tobacco was exempt from taxation. Not until 1798 and again in 1799-1800 and 1804) was a tax laid on the domestic manufacture and sale of tobacco and the import duty increased. Still the income from the tobacco tax in all forms did not rise above twenty to twenty-one million francs<sup>1</sup> during the years 1805-1810, and it declined in 1809 to fourteen millions.

The decree of December 29, 1810,<sup>2</sup> reinstated the tobacco monopoly. It recites that tobacco is the most suitable subject of taxation, but that under the existing system the manufacturers have appropriated the better part of the profits, inasmuch as the price of manufactured tobacco had remained the same as it was under the old monopoly; the smallest portion of the income had come into the public treasury; the tobacco growers were at the mercy of the manufacturers. It was for the interest of all, including the tobacco growers of the country, that the tobacco manufacture should be carried on under a royalty for the bene-

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<sup>1</sup> A report to the Emperor in 1805 returns 8.20 million francs revenue from the internal tax, 9 millions from the duty, 824,000 francs from licenses of manufactures, 1.77 million from licenses of retailers. - Parieu, *Traité des impôts* (1866), vol. ii. p. 460, Cf. Malchus, *Handbuch der Finanzwissenschaft* (1830), vol. i. p. 111. The rates were: 40 centimes per kilogram of manufactured tobacco and 80 centimes to one franc per kilogram import duty.

<sup>2</sup> This, as well as the other laws (since 1798), is to be found in the appendices to the report of the Commission of Inquiry on Tobacco (of the German Empire), vol. iii. appendix xii. pp. 99-150. Cf. Vuatrin et Batbie, *Lois administratives*, vol. i. pp. 772 *et seq.*

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fit of the national treasury.<sup>1</sup> A net income of about 80 million francs was intended to be raised. After the Restoration the tobacco monopoly was continued in existence by a law of April 28, 1816, and new regulations were established as to the administration, prices, etc. This law was limited to five years; but it was renewed at the end of each five year period, and later on, for the most part, for periods of ten years, being dealt with in this way by the laws of 1872 and 1882.

The net receipts have been:<sup>2</sup>

YEAR	MILLION FRANCS
1815	32
1820	42
1830	47
1840	70
1859	130
1869	197
1872	217
1878	273
1883	303
1887	320

The consumption of tobacco increased from 11 million kilograms in 1830 to 32.50 million kilograms in 1869, and in spite of

<sup>1</sup> The essential provisions of the decree are the following: the purchase of tobacco in the leaf, and its manufacture and sale at wholesale and retail alike, are made the subject of a royalty. This monopoly must procure not less than one-fifteenth of its supply of raw tobacco from the home-grown product. The ministry of finance is to announce year by year how large an area may be cultivated in tobacco in each department. Anyone who wishes to grow tobacco must give notice of his intention to the maire of the commune before the first of March of each year. The area allowed for tobacco culture must not be reduced except in cases of a large over-supply. During January of each year the price to be paid for the tobacco of the next succeeding harvest is published, varying from one arrondissement to another, according to the local variation in the value of the product. Three grades, in quality and in price, are established for each arrondissement, and the product is graded in November of the same year by a board of inspection. For the collection of the leaf tobacco the monopoly erects storehouses which are distributed over the tobacco-growing districts in such a manner that the growers are in no case to be obliged to transport their product more than twenty-five kilometers. The leaf is delivered between November 1 and March 1, against payment in cash. The manufacture is carried on exclusively on the account of the monopoly, in public factories; the prices at which the various qualities of tobacco and cigars are sold are fixed by the law and the decree respectively.

<sup>2</sup> Leroy-Beaulieu, *Traité*, vol. i. p. 666; Malchus, vol. i., p. 111; *Finanzarchiv*, 1885, p. 854.

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the pronounced increase of the tobacco tax and the diminution of the French territory after the war; it rose again to 32.50 million kilograms by 1833. The net per capita payment is the largest yielded by the tobacco tax in any country (1883, 8.58 francs, as compared with .81 mark in the German Empire); while the consumption in the German Empire is 1.90 kilograms per capita, it is only .85 kilogram in France.<sup>1</sup>

The French tobacco monopoly has kept its footing through all constitutional changes, under the Empire as well as under the Restoration and Louis Philippe, under the Second Empire as under the Republics of 1848 and 1871. The form of taxation of the *ancien régime* was not only reinstated after the great Revolution, but it has also come off victorious in all the changes and periodically recurring debates and inquiries, and at each renewal of the law it has shown itself to be an indispensable constituent of the finances.

Even so faithful an adherent of the old school as Leroy Beaulieu recognizes the tobacco monopoly as an incomparable financial means, in point of productiveness and inoffensiveness.<sup>2</sup>

§ 289. It may not be out of place to glance at the tobacco monopoly which once existed in Prussia, although the reorganization of the Prussian finances did not follow the French example.<sup>3</sup>

After the Seven Years' War Frederick the Great tried to increase the public revenues, especially by adopting the fiscal methods of the French. He wished, without oppressing the lower classes of the population, to take over the trade in articles of general but still not indispensable consumption, as an income-

<sup>1</sup> *Finanzarchiv* (1885), p. 859.

<sup>2</sup> "L'impossibilité de retirer par tout autre moyen une somme aussi énorme de l'impôt sur le tabac, l'impossibilité de faire payer au pays d'une manière aussi inoffensive, aussi peu vexatoire, est la justification, au moins temporaire, du monopole." - *Traité*, vol. i. p. 664.

<sup>3</sup> Riedel, *Der brandenburgisch-preussische Staatshaushalt*, pp. 102 et seq. Cf. also pp. 198 et seq., 213, Walther Schultze, *Geschichte der preussischen Regieverwaltung von 1766 bis 1786* (1888), Schmoller, "Die Einführung der französischen Regie durch Friedrich den Grossen, 1766," *Deutsche Rundschau*, 1888, Heft vii.

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yielding monopoly.<sup>1</sup> Among the foremost of the reforms, it was intended to introduce the traditional French system of Farmers General, whose private interests would, in comparison with the abuses of the then existing public administration of the taxes, lessen the cost of collection and increase the revenue. His French friends, who praised this system to the king, were equally able to tell him of the tobacco monopoly which at that time brought 14-15 millions into the French treasury. In May 1765 the tobacco monopoly was offered to a company of French adventurers at an annual rental of one million thalers. But in July 1765 it was awarded to a syndicate of manufacturers, in Berlin, who offered to pay one-hundred-thousand thalers more. The undertaking failed, however, and by the end of twelve months the king established an independent royal commission for the general management of the tobacco business.

This fiscal contrivance not only yielded a considerable net income (1785-86, 1,286,289 thalers), it also became a means of fostering the production of tobacco, for the king spent a remarkable amount of thought and care on the furtherance of the tobacco culture and of the domestic tobacco manufacture.

But immediately after the death of Frederick the Great the new ideas of industrial freedom asserted themselves in the fiscal

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<sup>1</sup> The most noted contemporary of Frederick the Great among the German Cameralists, Justi, was a determined opponent of monopolies; he gives evidence at this point also to how slight an extent the common conception of "Mercantilist" is applicable to him. He says (*Staatswirthschaft*, 1755, vol. ii. sec. 258): "Still less is the tobacco tax based on a sound principle. In practice it is usual to make a monopoly of the tobacco trade, and to farm it out to some one for a considerable sum. But since a very close watch has to be kept in order to prevent the importation of foreign tobacco, which involves close inspection and a great limitation of men's freedom of action, and as it also frequently leads to bloody encounters between the tobacco inspectors and the subjects, the estates in some countries have adopted the expedient of taking over this tobacco lease and then imposing a tobacco tax on every inhabitant of the country to cover it. .... If the purpose is simply that of a tax, then no sensible man can comprehend why the subjects should be put under such a strict restraint, or why the tobacco tax should be taken up as a special business in this way, seeing that the purpose could be more easily attained by introducing an ordinary capitation tax, or by increasing the tax already in force. To the subjects, who will be obliged to dip into their purse in one case as in the other, the latter is surely the more acceptable method."

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and industrial policy of his successor, and in 1787 brought about in Prussia the results which the Revolution achieved in France a few years later. The tobacco monopoly together with the coffee monopoly and the French *régie* were abolished. But by the end of another decade Frederick William II. found it expedient (1797) to establish a new General Tobacco Administration. Of all the monopolistic contrivances of Frederick the Great, the tobacco monopoly had best approved itself. It was now hoped that the revenue would amount to three times what this monopoly had yielded in 1786. The territory had increased and the consumption of tobacco had increased. In order to lighten the burden the king professed the intention "of satisfying the poorer classes of humanity in their necessary consumption at a moderate price, but to make the wealthy pay an adequate price for their tobacco as an article of luxury."<sup>1</sup> A few months after the reintroduction of the tobacco monopoly the king died; and his successor, by a patent of December 25, 1797, made his subjects a Christmas present of the freedom to cultivate, manufacture and trade in tobacco.

The liberal ideas of the time had triumphed in Prussia;<sup>2</sup> the strong hand of Napoleon I.; which established the French tobacco monopoly in 1810, the sober sense of expediency which urged to its retention under the later governments in France, were wanting in the tax reform of Prussia, then and afterward.

§ 290. Prussian statesmen and the Prussian people have for a long time past been on a friendly footing with the lottery monopoly.

The lottery made its appearance as a fiscal expedient in

<sup>1</sup> Order in Council of May 21, 1794.

<sup>2</sup> The words of J. G. Hoffmann (*Lehre von den Steuern*, p. 28) may be taken as an expression of these ideas: "The more the governments come to recognize that it is their office to protect and secure to each one his own, and to assure to all men law, order, and the fullest and freest exercise of their capacities, and to do this in a spirit of lofty awe-inspiring sovereignty, uncolored by any private interest, and rising free above the multitude of conflicting endeavors to secure gain and enjoyments; the more they come to appreciate this, the more unseemly will it appear to them to take part, as the owners of domains, in the struggle of landlords and business men for gain."

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Florence, in the year 1530, when the Republic, being in great financial straits, set up a lottery with chances selling at one ducat.<sup>1</sup> It is also mentioned in France about the same time. Francis I. gave permission to establish a lottery in 1539, under official supervision, or payment of a bonus to the king.

About the middle of the seventeenth century lotteries came to be widely adopted. The Neapolitan, Tonti, succeeded in gaining the favor of Louis XIV. for the lottery; in 1661 the lottery was made a royal prerogative. In Holland<sup>2</sup> and England it was made use of just as in France and Italy. At the beginning of the eighteenth century Savary speaks with commendation of its widespread employment and of the blessed work it was doing in furthering many good and pious objects. The great commercial companies made use of it as well as states and towns.<sup>3</sup>

The earlier form is the less hurtful one, the one which we know as the class lottery; the later form, which is more distinctly calculated to appeal to the gambling propensity, is the lottery of numbers, formerly known as the Genoese lottery (still practiced in Italy,<sup>4</sup> with the employment of the numbers 2, 3, etc.).

The older form was, according to Justi (1755), "very much in use throughout Germany" during the first half of the eighteenth century.<sup>5</sup> It rarely happened that the prince carried on the lottery himself, but the privilege was granted to a corporation in the town or to some private person, in consideration of the payment of a stipulated annual sum. Since these lotteries are, in Justi's opinion, extremely profitable for the undertaker and very tempting for the people, they are, in point of fact, a form of taxation which properly belongs to no one else than the sovereign.

<sup>1</sup> Varchi, *Storia Fiorentina* (1721), vol. xi. p. 366. Beckmann, *Beiträge zur Geschichte der Erfindungen*, vol. v. (1805), pp. 317 *et seq.* Savary, *Dictionnaire de Commerce*, art. "Loterie" (Geneva, 1742), vol. ii p. 1125.

<sup>2</sup> R. van der Borght, *Finanzarchiv*, 1888, pp. 384 *et seq.*

<sup>3</sup> Savary, *Dictionnaire de Commerce*, vol. ii. p. 1128.

<sup>4</sup> Pope Benedict XIII. (1724-1730) forbade gambling in the Genoese lottery; his successor, Clement XII. (1730-1740), finding that the prohibition had no effect, established a lottery himself. - Beckmann, vol. v. p. 336.

<sup>5</sup> *Staatwirthschaft*, vol. ii. p. 436.

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In Prussian it was the number lottery [*Zahlenlotterie*] which was first reserved as a royal prerogative. The class lottery [*Klassenlotterie*] has been in existence since the beginning of the eighteenth century, but was not monopolized by the state until 1767. On the other hand the number lottery was taken over by the government at its first establishment, by letters patent on February 8, 1763. It was in this case also an Italian (Calzabigi) who organized it for the king. It belongs in the system of new financial expedients which the kings resorted to after the great war. The preference shown for this most dubious form of the lottery at the outset may be taken as evidence of the unflinching realism of the king in his choice of means to carry out his purpose, but in this particular case the end attained is by no means proportioned to the means employed. As happens elsewhere so frequently, so also here, it was sought to justify the lottery to the public conscience by appropriating a portion of the revenue to benevolent objects. The total receipts, to begin with, were quite insignificant; experiments in administration had to be made before a satisfactory method was found; the method of farming out the monopoly proved itself relatively the best, and remained in force until 1794. Beginning with scarcely 20,000 thalers, the annual rental advanced to 30,000 (1770), and at the king's death it had reached 55,000, and finally reached 60,000 thalers. Since 1794, when the administration took the lottery into its own hands, the income from it has been greater; from the number lottery and the class lottery together, the latter being now organized in a more effective way, there was obtained in 1797-98 a net income of 515,475 thalers. And similarly for the succeeding decade. The Lottery Edict of May 28, 1810, abolished the number lottery and pronounced in the preamble a condemnatory judgment on its tendencies and effects. It had diffused and fostered the propensity for gambling among the lower classes of the population to a disastrous extent. In particular cases

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<sup>†</sup>Riedel, *Staatshaushalt*, p. 102. Otto Warschauer, *Geschichte den preussischen Staatslotterien: i. Die Zahlenlotterie in Preussen* (1885). The same, *Finanzarchiv*, 1885, pp. 716-746.



(e.g., in Luckenwald) it had resulted in a scandalous state of affairs.<sup>1</sup>

After short-lived experiments with the quinine lottery, the real estate lottery<sup>2</sup> (raffling for landed estates, and later with the small money lottery, the class lottery became the permanent form in which the Prussian lottery monopoly has continued through the nineteenth century.

§ 291. The method by which the Prussian class lottery is managed is as follows: There are every year two lotteries, in which four drawings (classes take place. The number of prizes and the amount increases from the first to the fourth class; the latter class contains the majority of prizes and the largest prizes. The price of a chance is 13 thalers for each class, and therefore 52 thalers for the four classes together. Only whole, half and quarter tickets are sold, in order to confine participation in the lottery to the wealthier classes of the population. In point of fact, however, many poor people will club together to buy a quarter ticket, and so set at naught the purpose of this provision.<sup>3</sup>

The number of tickets, and consequently the profits obtained by the state, have increased as the years have gone by. In 1852 it amounted to 971,200 thalers, in 1861 to 1,315,900 thalers, at which figure it remained until 1886. Since 1886-87, after the views on the subject had been unsettled for several years the number of tickets, and consequently the amount of the profits, has been doubled, in accordance with a resolution of the Chamber of Deputies (191-131). In the estimates for 1889 -90 a sum of 8,287,500 marks is set down as income from the lottery. The revenue accruing to the state is due to the fact that a deduction of 13.75 per cent. is made from all

<sup>1</sup> Cf. Beckmann's judgment, *loc. cit.*, as expressing that of many contemporaries.

<sup>2</sup> As early as 1712 the privilege of putting up real estate to be raffled for was conceded to private parties in Berlin by ministerial rescript in consideration of a contribution to certain benevolent foundations. - Warschauer, *Finanzarchiv*, 1885, p. 728.

<sup>3</sup> Marcinowski, "Die preussische Staatslotterie vor dem Forum der Landesvertretung," *Finanzarchiv*, 1884, pp. 530-557 Bergius, *Grundsätze der Finanzwissenschaft*, p. 222.

prizes, together with a deduction of two per cent. for the lottery collectors, while the purchasers of the tickets pay five per cent. as a stamp duty (by an imperial law of July 1, 1881) in addition to this, and one mark as a clerk's fee for each class.

By doubling the number of tickets and the revenue this institution has by so much been placed on a firmer footing in Prussia, while in England it was abolished in 1826, in France in 1836, in the Grand Duchy of Hesse in 1832, in Bavaria in 1861. There has also been no want of discussion looking to the abolition of the lottery in Prussia. Since the United Diet of 1847, and until a few years ago, the question has continually come up for consideration.<sup>1</sup> The opponents of a state lottery are wont to assert that it is reprehensible on moral and religious grounds, to draw the revenues necessary to the preservation of the state from lotteries; more particularly for the reason that it is the needier classes of the population who are most easily tempted to patronize it, and that to such an extent as to trench upon the means necessary to their sustenance, and at the same time the effect of the resulting gambling propensity is to paralyze their industry and economy. In favor of the retention of the lottery it was claimed (especially on the part of the government) that the fiscal income derived from the lottery could not be spared, - that in point of fact the detrimental effect on the economic and moral characteristics of the people does not supervene, - that the gambling propensity innate in the population had best be guided into the channels which the state in this may assigns it, - that the abolition of the Prussian lottery would simply foster gambling in private or in foreign state lotteries, - that the joint measures necessary to be taken in order to its abolition in the states included in the German Empire have been broached, but that for the present there is no prospect of their realization.

These idealistic and realistic arguments have constantly recurred. The growing fiscal needs of the government have inclined it to keep its hold on the income; but in the course of years this

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<sup>1</sup> Marciniowski gives an account of the various debates in the Prussian parliament and in the Reichstag during a period of forty years. *Loc. cit.*

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realism has itself received a shock, so that the national government shifted its standpoint more and more in the direction of placing the responsibility on the representatives of the people. Realism carried the day in the Committee on the Budget and in the full Chamber of Deputies, when the estimates for 1886-87 were under consideration. The motive force was a survival of the old misery of special interest on the part of the small states. It appeared that certain of the smallest of the German states maintain lotteries which for the most part find a sale for their tickets in Prussia, not being effectively restrained by the prohibition against gambling in foreign lotteries (Ordinances of July 5, 1847 and June 25, 1867). Hamburg<sup>1</sup> derives a revenue of 3.36 marks per capita of its population from the state lottery; Brunswick 3 marks, Saxony 1.50 marks, Prussia only about 1/7 mark (since 1886-87 less than 1/3 mark). An attempt was made in 1881 in the Reichstag to abolish the state lotteries, which, in view of the provisions of the imperial constitution; had but very slight chances of success. The committee appointed to report a bill for levying imperial stamp taxes included in their report of May 20, 1881, a resolution to ask the imperial chancellor to use his influence towards the abolition of all existing state lotteries in the states of the empire; and in the meantime to hinder any extension of the lotteries. The commissioner of the Federal Council [*Bundesrath*] replied that the maintenance or abolition of state lotteries was a question entirely within the competency of the governments of the several states, and that the resolution consequently exceeded the limits of imperial jurisdiction.

The situation is not made any the less surprising by the fact that the states which turn the lotteries to account under cover of their competency are precisely those particular ones of the smaller states which are distinguished above all others by

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<sup>1</sup>In its budget for 1888, Hamburg has an income of 1,743,300 marks from lotteries, with a population of 518,620 inhabitants (that is to say, 3.36 marks per capita). Brunswick, with 372,452 inhabitants, obtains 1,113,500 marks (= 3 marks per capita). The Kingdom of Saxony, with 3,182,003 inhabitants, gets 4,592,234 marks (= 1.44 marks per capita).

their accumulated wealth or the flourishing state of their finances.

§ 292. Among financially important monopolies we have finally to mention the Post. Its character and its place in the discussions of the science of finance have already been explained in the course of some earlier observations (cf. above, sees. 76-77, 81, 93-94, 108), because its peculiar intermediate position affords occasion for discussion of it from different standpoints. The material on which these theoretical discussions are based is the precipitate of the experiences of the Post in history. Its purpose has for centuries past varied from fiscality to public utility and back again; now one and now the other being the dominant purpose; both being frequently inextricably blended. But there have also been times when the Post was devoted exclusively to the service of the government and had nothing to do with the carriage of letters for private parties, either with a view to revenue or from any other financial motive.

Such was the case in the Roman Empire.<sup>1</sup> Just as the Roman system of highways was of an entirely administrative-strategic nature, so also the administration of the Post was calculated exclusively for the conveyance of officials and of state dispatches. It was only by exception, requiring the consent of the Emperor, that a private person was able to make use of the Post. Augustus was the first one who established a definite system; the expenses of the postal stations were defrayed by the adjacent country; it was only gradually that a certain centralization was developed in this matter, and that the expenses of the local stations came to be defrayed by the treasury.

The mediaeval antecedents of our modern postal system are partly survivals of the Roman establishment (under Charlemagne and his successors, partly establishments created to serve certain particular interests which were brought into prominence by

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<sup>1</sup>Marquardt, *Römische Staatsverwaltung* (1873), vol. i. p. 417. Mommsen, *Römisches Staatsrecht* (1877), vol. ii. p. 987. Hirschfeld, *Untersuchungen auf dem Gebiete der Römischen Verwaltungsgeschichte*, vol. i. pp. 98 et seq.

the advance of civilization and increase of intercourse,<sup>1</sup> - corporate messenger service of the Universities, of cities, of the Teutonic Order, which extended over hundreds of miles of territory as early as the thirteenth century. In the second half of the fifteenth century, when the monarchical state was beginning to increase in power, state postal establishments began to develop in France, England and Germany. These, too, served only official purposes at the outset. But very shortly they were made accessible to private intercourse as well, and that to the extent that the Post undertook the conveyance of persons as well as of letters.

In the second half of the seventeenth century the Post was already yielding a considerable income in France. In that connection it is to be mentioned that in 1681 it was declared a monopoly of the state, and then like the other fiscal establishments of the government utilized by the method of farming. In England the postal monopoly was introduced as early as 1635-1637. Here, too, it was farmed out, and in 1685 it yielded an income of £65,000. State management of the Post began in England in 1710; in France not until 1792. The conveyance of persons, which was especially profitable during the early centuries of the governmental postal business, gradually fell into the background as compared with letter-carriage. The monopoly of the conveyance of persons was relinquished in England in 1779; in France this branch of the postal service was entirely discontinued by the administration after the Revolution (1805).

§ 293. In Germany<sup>2</sup> the evolution of the Post is a reflex of the general development of the state. The Taxis, contractors of Italian descent, gradually secured, at the hands of the German Emperors (1545, 1563, 1595, 1597, 1615, 1621), an hereditary concession of the Imperial Post, which came into conflict with the old messenger service of the towns and with the incipient

<sup>1</sup>E. Sax, *Die Verkehrsmittel in Volks- und Staatswirthschaft* (1878), vol. i. p. 318.

<sup>2</sup>Hartmann, *Entwicklungsgeschichte der Posten von den ältesten Zeiten bis zur Gegenwart* (1868), pp. 218-400.

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state postal establishments of the more powerful territorial princes, but for the many small and scattered fragments of the Empire it afforded a very desirable centralization of the postal service. Austria, Brandenburg, Saxony, Brunswick, Hesse, created postal establishments of their own. In the conflict with the smaller states the power, and consequently the somewhat questionable right, of the Taxis was successful. Still, even as late as February 13, 1680, an ordinance of Emperor Leopold was issued directed against the old messenger establishments and casual conveyance. By the middle of the seventeenth century the postal business is said to have afforded the Taxis a yearly income of 100,000 ducats. Even after the fall of the old Empire the relative expediency of the institution was recognized in the German Articles of Confederation, and led to the re-establishment of the postal privilege of the Taxis in spite of the distracted state of a portion of Germany. This lasted until the reorganization of Germany in 1866, which resulted in the abolition of the old establishment.

In Prussia<sup>1</sup> it was the Great Elector who established a main post route through his extended territory, from Memel to Cleve, in 1646, and he placed it under direct state management in 1649. Contrary to what happened in Austria, the immediate state management of the postal service was not abandoned. It presently came to be looked upon all over Germany as a model, and although it was not managed with a view exclusively to a fiscal return until 1740, still it yielded a considerable surplus - 1685, 39,213 thalers; 1712, 137,450 thalers; 1740, 220,000 thalers. It was Frederick the Great who first was constrained by his great need of revenue to turn this branch of the administration also to fiscal account. At about the same time with the royalty of the excise and tariff revenues, and under similar conditions, the administration of the postal system was, in 1766, placed in the hands of a French Intendant-General,<sup>2</sup> but after some discouraging experience, it was again taken in hand by the government

<sup>1</sup>Stephan, *Geschichte der preussischen Post vom ihren Ursprüngen bis zur Gegenwart*, (1859).

<sup>2</sup>Riedel, *Staatshaushalt*, p. 106.

management in 1769. It had been Justi's teaching, even as early as 1755,<sup>1</sup> that the postal monopoly as well as all other monopolies should neither be farmed out nor be granted as a feudal right, for the reason that its administration is intimately related to the welfare of the state; that its purpose is the convenience of travelers and the furtherance of commerce and industry; the revenue derived from the postal service, as from all other royalties, is of only secondary importance. He holds that it is quite contrary to the essential nature of this monopoly to charge an extremely high postage,<sup>2</sup> whereas if the rate of postage is moderate a correspondence will often be kept up on very slight occasion and merely for friendship's sake; the post office should afford all convenience to the subjects, and without imposing burdensome conditions and restrictions, such as prohibiting travelers from conveying letters and the like. If only the rate of postage were lowered, people would be, willing to spend a couple of groschen rather than inconvenience a friend with the carriage of letters.

§ 294. For a hundred years after that time the postal administration changed back and forth from one guiding principle to another. Now the aim was that of a one-sided fiscality (to some extent under the pressure of necessity, now it was public utility, and again an attempt would be made to harmonize and combine these two interests, as being the simplest solution of the problem. After the unsuccessful experiment with the French method of managing the Prussian postal service the confession was made in an edict that the postal revenues had suffered seriously by this immoderate and ill-proportioned increase of the rates? But there was also a similar epoch of fiscality in the management of postal rates in other countries at the same time.

<sup>1</sup> *Staatswirtschaft*, vol. ii. p. 159.

<sup>2</sup> He relates that while in Vienna, when other learned men did him the honor to send him a copy of some moderate-sized volume of theirs, he had been obliged to pay as high as a thaler or even two golden in postage, although half the postage had already been prepaid.

<sup>3</sup> Holzamer, *Zeitschrift für die ges. Staatsw.* 1878, p. 7.

In England the minimum rate,<sup>1</sup> which had been fixed at one penny in 1765, was raised in 1783 to two pence, 1797 to three pence, 1804 to five pence (for greater distances within the country to 12-14 pence. In France the fanaticism of the Revolution sought to make use of the postage rates also as a means of taxing the luxury of the rich. The French postage rates had, in 1763, been fixed at five sous for the greatest distance; in 1795 it was increased to twenty-five sous (for the shortest distance ten instead of two sous as before). But as the receipts decreased, the postage was increased in 1796 to a rate of 2.50-10 francs (according to the distance)! Thereupon correspondence ceased, and a new change was made during the same year to a rate of 6-18 sous. The practice remained the same in principle throughout the period of the Empire. The Finance Minister of the Kingdom of Westphalia states, in his report for 1809, that the receipts from the Post are decreasing in spite of the fact that the rates of postage have been doubled and trebled. At the same time the newspapers relate that the Westphalian subjects begged their correspondents to abstain from letter-writing, as the postage teas more than they could afford to pay,

In Prussia, on the reorganization of the national finances, the remark was made by the postal administration that improvement and extension of the means of communication were the only true means of increasing the postal revenues; but the decisive word uttered was that it would be necessary to draw more heavily on the Post as a source of national revenue than had hitherto been the case. On the director general of the post office was imposed the task of bringing the surplus revenues (which had risen during the year 1797-1806 from 462,000 thalers to 667,000 thalers,<sup>2</sup> and had afterward increased to 700,000-800,000 thalers) up to 1,200,000 thalers.<sup>3</sup> The postage regulation of December

<sup>1</sup>When Charles I. established the letter post in 1635 the postage was two pence for distances under eighty miles, four pence for distances from eighty to one hundred forty miles, six pence for any place in England, eight pence for places in Scotland. - *Twenty-ninth Report of the Postmaster General*, p. 12.

<sup>2</sup>Riedel, *Staatshaushalt*, p. 212.

<sup>3</sup>Holzamer, *loc. cit.* pp. 8 *et seq.*



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18, 1824, increased the rates, on an average, by one-fifth. A letter within the limits of Prussia, for the greatest distance, then cost very nearly one thaler.

§ 295. The great reform in the direction of simplicity and a lower postage<sup>1</sup> which for England, and for the rest of the world as well, is intimately connected with the name of Rowland Hill,<sup>2</sup> does not go the length of the radical propositions for postal reform which had long before that time declared in favor of relinquishing all surplus revenue from the Post. Hill is an enthusiastic advocate of the theory of the harmony of interests, in virtue of which it is as well to retain a surplus revenue from the Post because a very low rate will lead to such an increase of correspondence as will very considerably decrease the relative cost of the postal service. Since the whole matter hereby comes to depend on the question as to how low the rate shall be fixed, and as there is some danger that the enthusiasm for what afterward came to be known in England as the free-trade principle may depress the rate below the limits of prudent management, the belief in a harmony of interests may readily act to the detriment of the finances: But the radical programme, making a virtue of necessity, is apt to defend this breach by resuscitating the fertile declaration of the era of the *éclaircissement* that the postal monopoly cannot legitimately be used as a means of obtaining a surplus revenue. Rowland Hill's language too, seemed to incline to this view of the matter.

In England a great revival of trade and industry had taken place after the war, but the net revenue from the Post had not increased during the twenty-four years (1815, £1,619,000; 1838, £1,576,000; 1838, £1,649,000). The reason for this was supposed to be the high rate of postage.<sup>3</sup>

Hill<sup>4</sup> says in his plan of reform: "What I have endeavored to

<sup>1</sup> Down to 1810 the postage on a letter from London to Edinburgh amounted to 42 pence; after January 10, 1840, it was only one penny.

<sup>2</sup> *Postoffice Reform, Its Importance and Practicability* (1837).

<sup>3</sup> Cf., *inter alia*, Porter, *Progress of the Nation* (1843), sec. 7, chap. 5. pp. 294 *et seq.*

<sup>4</sup> A penny post had already been established for London and the suburbs by

show is that it is highly probable that the Post will show no considerable deficit, and it is quite possible that there will be no deficit at all. But if a serious deficit should in fact result, the productive power of the country would receive such an impulse from the cheapening of correspondence as to produce so much the greater a revenue from the other branches of the administration." In point of fact, the net receipts declined from £1,649,088 in 1839 to £495,914 in 1840, and £564,407 in 1841. And it was only very gradually that the net income rose again to the level of 1839 (1872, £1,622,000); a result which was of course in large measure due to the growth of population, industry and wealth. The result was therefore a very considerable loss to the finances, both absolutely and relatively, which could have been avoided by greater moderation in the reform of 1839, at the same time that the substantial advantages of the reform might have been secured.

But what would considerations of this sort count for when running counter to the free-trade enthusiasm of that time, when the English newspapers were in the habit of dating the era of universal peace from the introduction of the penny post?<sup>1</sup>

In the meantime, it is to be noticed, the net receipts of the English postoffice have gone on increasing (1886-87, £8,462,567 gross receipts, with an expenditure of £5,403,408; there being on the other hand a deficit of some £100,000<sup>2</sup> in the telegraph service.

§ 296. In Prussia and Germany there was more hesitation about following the example of the English reform. There was at that time (the middle of the century) but a gradual approach

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Robert Murray in 1683. This came into the hands of the state under the name of the London District Post and remained a distinct postal department until 1854. Then, a Mr. Povey made an attempt in 1708 to introduce a half-penny post in competition with the government penny post, but this enterprise was suppressed by legal proceedings, as being an infringement of the post-office monopoly.- *Twenty-ninth Report of the Postmaster General on the Post Office* (London), 1883, p. 14.

<sup>1</sup> Holzamer, p. 17.

<sup>2</sup> Receipts £1,841,161, expenditures, £1,940,012, - *Whitaker's Almanac*, 1889, p. 180.

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attempted toward the consummation which seemed in the end to be inevitable for every country and for the whole world.

The gradual unification of the German postal systems within the German Confederation went hand in hand with the lowering of the rates of postage. The main impulse to this came from the movement of 1848. The German-Austrian Postal Union was established on the 6<sup>th</sup> of April, 1850; on December 21, 1849, the law went into effect which established for Prussia a three-grade postage with a maximum rate of three silver-groschen, which was also to be the maximum rate for Germany and Austria. The net receipts of the Prussian postoffice were, in 1856, 1,756,948 thalers, in 1862, 2,210,609 thalers.<sup>1</sup> The results which followed the radical reform of the English postal service had been successfully avoided.

The latest phase of the development appeared with the establishment of the unity of the Empire. It coincided with the high-strung free-trade movement whose demands upon the postal administration were expressed by the standing committee of the German Chamber of Commerce: abolition of the postal monopoly, abandonment of the "purely fiscal" administration of the post office, reorganization of the postal service as a means of communication on "business principles," adoption of a uniform rate of one silver-groschen, lowering of the registration fee to one silver-groschen, etc., the establishment of postal communication with foreign countries by the concerted adoption of schedules as cheap and uniform as practicable, especially for the letter post.

At the German postal conference at Karlsruhe, in 1865, Prussia, in contrast with Austria, Bavaria and Baden, showed herself disinclined to enter on this path of postal reform. After the establishment of the North German Union the tendency seemed irresistible. Commissioner of the Postoffice, Stephan, had declared himself in favor of the uniform rate of one groschen as early as 1859. But until the abolition of the postal monopoly nothing was done to gratify the free-trade aspirations on this

<sup>1</sup> Bergius, *Finanzwissenschaft*, p. 145.

<sup>2</sup> Holzamer, *Zeitschrift für die gesammte Staatswissenschaft*, 1878, p. 555.

head. The law of November 2, 1867, dealing with the postal system of the North German Union, was in substance based on the Prussian postal legislation of June 5, 1852, but the scope of the postal monopoly was somewhat limited.<sup>1</sup> The transfer of the management of the postoffice from the different states to the Union went into effect January 1, 1868. The postage law of November 4, 1867, established a uniform rate of one groschen, as well as a uniform schedule for the conveyance of parcels and money and for newspapers; it also abolished a great number of incidental fees. The two imperial laws on the postoffice dated October 28, 1871, closely followed the legislation of the North German Union. Bavaria and Wurtemberg alone - retained an independent administration so far as concerned their own internal postal service.

By the late of October 28, 1871, the conveyance of passengers was left entirely free to private enterprise; whereas the conveyance of all sealed letters, as well as of all political periodicals issued oftener than once a week, from places having a postoffice to other places having a postoffice, was reserved exclusively to the Imperial Post.

Of importance to the financial management of the German Imperial Post is the provision contained in the Railway Postoffice Law of December 20, 1875 (based on the Prussian Railway) Law of November 3, 1838. This law (Art. 2) provides that with every train included in its regular service the road is required, on request of the postoffice management, to convey, free of charge, one mail-car supplied by the latter. This gratuitous conveyance comprises letter-post matter, newspapers, money, bullion and other postal matter in parcels not exceeding ten kilograms, together with the persons required for the postal service.

With the increase in the postoffice business which has been witnessed of late years, especially in the carriage of parcels and printed matter, this gratuitous conveyance has become an item of ever-increasing importance. And without a thorough-going

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<sup>1</sup>P. D. Fischer, *Die deutsche Post- und Telegraphengesetzgebung* (1876). Cf. Hermann Rösler, *Lehrbuch des deutschen Verwaltungsrechts*, vol. ii. (1873), pp. 461-477

investigation of the economic scope of this gratuitous conveyance with which the railways (of late for the most part state railways are burdened, nothing can be determined as to how far the net receipts of the Imperial Post above expenditures are really net earnings of the postoffice and not simply a donation from the railway department.<sup>1</sup> It may be remarked that in England, under the law of August 18, 1882, there was paid in 1885, for the conveyance of the parcels-post alone,<sup>2</sup> a sum of £291,967 out of a gross revenue from the parcels-post of £577,958, that is to say, more than one-half the gross receipts.<sup>3</sup> According to this we should have to deduct from the net revenue of the German Imperial Post, for railway service, 17,000,000 marks on account of the parcels-post alone.<sup>4</sup>

		RECEIPTS	EXPENDITURES	NET RECEIPTS
1874	109	millions	104 millions	5 millions
1879	131.50	"	114 "	17.50 "
1888	193	"	165 "	28 "

<sup>1</sup> *Statistisches Jahrbuch für das deutsche Reich*, 1888, p. 179.

<sup>2</sup> Cf. *Untersuchungen über die englische Eisenbahnpolitik*, by the present writer, vol. iii. (1883), p. 184.

<sup>3</sup> *Statistical Abstract for the United Kingdom*, 1886, p. 184: 25,870,454 parcels = 461,972 cwt.

<sup>4</sup> According to the statistics of the Imperial Postoffice, the receipts for the conveyance of parcels, in 1886, with and without assigned value (71,434,700 parcels), amounted to 33.79 million marks. The number of parcels carried by the Imperial Postoffice stands in nearly the same proportion to the number of parcels in Great Britain and Ireland as the proportion between the receipts from the parcels-post in the two countries. The aggregate net receipts of the Imperial Postoffice in 1886 were 27.70 million marks. Deducting the 17 million marks derived from the parcels-post leaves only 10.70 millions for all else, printed matter, letters, postal cards, etc. The aggregate receipts from postage during 1886 were 139.54 million marks; deducting the receipts from the parcels-post, 105.75 million marks. It needs but to count one-tenth of this as payment for railway transportation in order to account for the 10.70 million marks above mentioned, which means that the entire surplus represents unpaid railway transportation. Cf. Ch. H. Hull, *Die Deutsche Reichspacketpost* (1892).

The following figures are from the *Thirty fourth Report of the Postmaster General* (1888, p. 3). The number of parcels (of which a portion were not carried by rail) rose from 22.90 millions in 1884-85 to 36.70 millions in 1887-88. The receipts in 1887-88 were £811,764, of which the railways received £401,295 (55 per cent. of the receipts from the parcels-post). The difference is due to the fact that other means of transportation besides the railways were employed for the carriage of the mails. In addition to this, the postoffice paid £891,782 (1888-89). - According to a statement received by letter from the English General Postoffice.

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This brings us face to face with questions which are not as often supposed already disposed of, but require further discussion. This matter will be taken up in its proper place later on.

## VII. OBJECTIVE TAXES (TAXES ON PROCEEDS).

§ 297. In taking up the consideration of objective taxes, the concept of which contains implicitly a contrast with subjective taxes, we are treading the historic ground of the scientific period of tax development.

The consciousness of this contrast is absent in earlier times. It was not until the nineteenth century theory brought it forward that it came into the foreground; its logical consequences have become evident only very recently. Objective taxes, however, considered as a distinct group of taxes, are of so great importance, their presence in the modern system of taxation is of so great consequence that at least the leading types of the development deserve to be noticed.

The scientific epoch in the history of taxation, although it partakes largely of the character of the eighteenth century and of the new science of political economy, and although it very boldly opposes and criticises the abuses of the earlier political and financial system, is still, in one respect, affected by the sobering influence of experience, and that to such a degree that it is only very lately that the idealistic view of life and of the science has been able to set aside the realism of that early day.

There took place a sobering of the views on personal taxes. Very much in the same manner as the small city republics brought the idea of popular sovereignty into disrepute in the eighteenth century,<sup>1</sup> so that a considerable further development in theory and experience was necessary in order to reinstate it in the position of importance which it holds at present, so also in the case of the personal taxes. The days of the republican virtue, and of its tax system, such as Macchiavelli found it existing in the German cities alone, were by this time past in those cities

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<sup>1</sup> H. S. Maine, *Popular Government*.

also. It is the abuses of the tax which obtrude themselves on the notice of any observer of the state of affairs in the eighteenth century. The best that we can expect to find will be exceptions from the demands and presumptions which arise out of the greater size which is normal to the modern commonwealth. Theoretical writers, like Justi and Smith, combat the predilection for personal taxes by citing the unfavorable experiences of the past.<sup>1</sup> The teachers of Financial Science followed in their footsteps for a hundred years.

<sup>1</sup> One reason which was present in the substitution of taxes on realty for personal taxes was the wish to avoid double taxation. K. H. Lang (*Ursprung der Deutschen Steuerverfassungen*, p. 240) notices difficulties of this sort which had, as early as the middle of the sixteenth century, been the occasion for treaty agreements between the princes of the small German states. In practice, says he, a subject paid taxes on his entire estate to the lord within whose jurisdiction he was domiciled, even if a few acres, or even entire farms, were situated in territory belonging under another jurisdiction. So that if, for example, a citizen of an imperial city bought a piece of land in a neighboring village which was in the jurisdiction of a territorial prince, the land having previously belonged to a subject of the prince, then the tax on this land would no longer be paid to the prince but to the city treasury. Such property was called "rolling estates" [*walzende Güter*], because they shifted from one tax to another according to the domicile of their owner. This shifting could not but be highly exasperating to the lord to whom taxes were to have been paid. He was unable to count on any income with certainty, and an estate which today owed taxes to him might shift over-night, by an unforeseen sale or inheritance, so as to owe its taxes to his neighbor. The neighborhood of the imperial cities was especially detrimental to the territorial princes, inasmuch as the wealthier inhabitants of these cities frequently bought up whole villages with their outlying fields, and so left frightful gaps in the tax list. It is, therefore, not to be wondered at that the territorial princes opposed this continued shifting with all their might, and finally brought it about that thenceforward the estates should no longer shift but should "fly" [*fliegen*] instead; that is to say, they might pass out of the hands of one owner to any other, whether citizen or alien, but they must pay taxes the same as before (an example occurs in a decision of the city council of the imperial city of Nuremberg, August 11, 1719). Still, the "flying," too, encountered great obstacles, and the princes finally succeeded in making the estates "lie immovable." For this purpose they were then duly surveyed and were entered in a regular cadaster on register and invoice books, their area, boundaries, and the names of their owners being specified. They were then subjected to a schedule of taxes (as to the details of this taxation, see I. D. Eulner's *Praktische Vorschrift, welchergestalt Steuer und Kontribution nach Anleitung der Reichsabschiede einzurichten sei. 2. Aufl.*, Marburg: 1741). In the territory of Wurtemberg, e.g., the process of redistributing the tax and assessing the estates began in 1713 and continued until 1741. The instructions are that the Commissioners must not assess according to the current price of the estates, as in former times, but are to base the assessment on the income they

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The tax theory of the entire abstract school of the Physiocrats, in whose theory empirical knowledge plays but a negative part, afforded a staunch support to this direction of the development of Financial theory; for their doctrine of the single tax became the foundation of the whole of the modern European system of objective taxation.

It is not exactly praiseworthy, although it is excusable in a youthful science, to have gone on in this direction long after the new epoch in taxation, though unrecognized in theory, had been introduced into practice by the course of events. The greatest of Adam Smith's disciples among practical statesmen, William Pitt, is far in advance of his teacher on this point.

§ 298. Justi<sup>1</sup> sets up the fundamental principle of taxation that the taxes must rest on a secure, stable and unequivocal basis and must consequently be laid on objects from which it cannot only be collected expeditiously and with certainty, but with regard to which fraud and concealment on part of the subjects, and speculation on part of the tax collectors, cannot easily take place. These requirements are best fulfilled by the tax on landed property, and this tax has consequently come to occupy a prominent place in the fiscal system of every civilized people. In comparison with this land tax a general income tax<sup>2</sup> is condemned by Justi, for the reason that it involves a publication of the amount of the taxpayer's property, which is detrimental to the

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yield, no distinction being made between those owned by citizens and those owned by aliens; the arable land is to be ranged in six classes for the purpose of assessment, meadow and pasture in seven classes, vineyards in five classes, on the basis of the average yield of six, three, and ten years respectively. The general disposition being made, the aggregate of the revenue required by the country was then distributed among the different districts, either in the form of fixed amounts or by months, and, inasmuch as every subject had a definitely computed capital on which to pay taxes, there was no difficulty in the way of determining the amount of taxes to be paid by each hundred within each district [*Amf.*], and by each individual subject in detail. This contrivance, says Lang, had been pretty commonly in use in the countries of Germany since the middle of the eighteenth century; a readjustment being effected from time to time by a revision of the tax registers.

<sup>1</sup> *Staatswirthschaft*, vol. ii. pp. 294-320.

<sup>2</sup> Vol. ii. pp. 321 *et seq.* Cf. also vol. ii. pp. 418-420.



credit of merchants and is annoying to all men. Such an income tax could scarcely be adopted by a wise government. There is a warning in the example of the city of Nuremberg, at one time wealthy and beautiful, but whose population is now dwindling daily, which must be attributed mainly to their employment of this class of taxes.<sup>1</sup>

We are familiar with the similar views held by Adam Smith. The historic structure of the French tax system prepared the way for the Physiocrats and for the development of French taxation along the lines of their theory; a development which came to serve as a model for Germany and for other states.

Even under the old régime there is distinctly perceptible a tendency toward the transformation of the burdensome system of personal taxes into the less burdensome and less arbitrary form of objective taxes. The *taille*, by tradition the cardinal form of the personal tax, was, according to an official expression dating from the year 1772,<sup>2</sup> "arbitrary in point of apportionment, *solidaire* in the method of collection pursued, a personal, and not a land tax in most parts of France, and subject to continual changes in conse-

<sup>1</sup> Personal taxes frequently develop into taxes on realty. So, for example, the tax on realty in the province of Silesia grew out of what was originally a property tax [*Schatzungssteuer*] (K. G. Kries, *Historische Entwicklung der Steuerverfassung Schlesiens*, pp. 37 *et seq.*). Similarly the English land tax was originally an income and property tax. Sinclair (*History of the Public Revenue of the British Empire*, 1803, vol. i. pp. 277, 304, vol. ii, p. 8) repeatedly cites evidence of this fact from the history of the seventeenth century. He says that at the accession of William III., none other than a tax on landed property would be sufficiently productive, land being at that time the chief source of wealth. In order to make this tax as effective as possible, a new assessment of the property and income of each individual was undertaken. The result varied greatly from one person to another. The taxpayers were more or less ready to make an adequate return of their property in proportion as they were more or less well inclined to the new government. The adherents of the Stuarts returned their property as low as possible. For this reason, adds Sinclair, the assessments which have since then been known under the name of the land tax were by no means so productive of revenue as they should have been. Even earlier than this, under Charles II., Parliament decided (vol. ii. p. 277), in order to the better support of the troops, "to levy assessments on the personal and landed property of the people . . . . Under the denomination of a land tax, they have since formed a very considerable branch of the public revenue." Cf. also Gneist, *Englische Verwaltungsrecht*, 3<sup>d</sup> ed., pp. 625 *et seq.*

<sup>2</sup> *Tocqueville, L'ancien régime*, p. 207. It is a confidential communication from the Comptroller General to the Intendants.

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quence of alterations occurring every year in the pecuniary means of the taxpayers." The office of tax-assessor and tax-collector was held by a member of the commune, and since it was looked upon by everybody as a misfortune, it was held by each one in turn, for a year at a time; the miserable incumbent was surety with his person and his property for the payment of the prescribed amount. Turgot says of this office that its consequence was desperation and, almost invariably, the ruin of the incumbent; whence it came that the well-to-do families were, one after the other, reduced to beggary, while in their relation to the lower classes it was a fearful incentive to the exercise of arbitrary power. Under this system it teas everybody's interest to conceal his own wealth and to keep a watch upon his neighbors and inform the assessor. Such was the state of the case in the greater portion of France. But there were, even at that time, particular provinces in which - in connection with certain survivals of self-government<sup>1</sup> that had been preserved by good fortune - the Taille had not assumed this oppressive character because it had remained an

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<sup>1</sup> With this may be compared what Gneist (*Englisches Verwaltungsrecht*, 3<sup>d</sup> ed., p. 624) says about the parallel development of English institutions: England had, in the course of this century, developed so varied a system of direct taxes as to have made a very thorough acquaintance with the legal difficulties in the way of assessed taxes. The Norman tallages and proportional taxes, as administered by the Exchequer, the itinerant commissioners and the sheriffs, impressed upon the island nation earlier than upon the continental peoples the fact that there can scarcely be any free ownership so long as the individual is liable to be taxed arbitrarily by officers of the crown. The corrective to this evil is to be found in the following principles tested by the experience of centuries, (1) that all assessed taxes must be assessed exclusively by officers of the local self-government, (2) that the development of this national tax went hand in hand with the development of local taxes, with a like method of assessment, reclamation, levying and collection, (3) that with the gradual destruction of free choice on the part of the people a tendency to make assessed taxes objective and specific, asserted itself. The income taxes of the local self-governing bodies have, both in practice and in law, uniformly been changed into taxes on visible, useful, real property, which permits of an assessment on the basis of leases and rents. In the collection of national taxes the custom came to prevail more and more as time went on, of basing it mainly on landed property, which was readily ascertainable by the officials who made the assessment. At the same time there was manifested a constant tendency on the part of landed property to commute its taxes payable to the state into fixed annual payments, and to rid itself of the demands by payment of a lump sum without regard to the increasing needs of the public treasury.

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objective tax, in fact a tax on realty. In the Languedoc,<sup>1</sup> for example, one of the most fortunate of the provinces under the old régime, the case was such as we have described. The Taille rested only on landed property; it did not change with the changing fortunes of the landowner; its basis was a hard and fast cadaster, which was constructed with great care, and was revised once in thirty years. By this means every taxpayer knew beforehand exactly what part of his net receipts he had to pay yearly. There was no personal or other security for the tax, except the plot of ground on which it rested.

All these provisions, remarks Tocqueville, correspond with precision to those which we apply today; no improvement has been made since that time in the provisions, but they have been extended to apply to the whole country uniformly. And this historical fact is not all; it is an integral part of what Tocqueville aims to prove - namely, the intimate connection between the political machinery of old France and the new - but he also goes on to argue from this development of the new French tax system to the permanent adequacy of the tax reform; so excellent a historian is he, and so excellent a Frenchman.

§ 299. In view of this historical relation the objective tax system of the French Revolution appears in quite a different light from what it does when viewed from the standpoint of the modern German tax system and its theory. For that epoch and that people, it was a great deliverance and a great step in advance.

The prominent place occupied by the tax on realty in this system is due to causes which had, for hundreds of years past, acted to make landed property the chief object of taxation; it was the chief element of wealth at the stage of industrial development which was then prevalent, it is the most palpable object at every stage of industry, and there subsists, in an eminent degree, a connection between landed property and the wel-

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<sup>1</sup> Tocqueville, *L'ancien régime*, p. 211; cf. p. 347; cf. Parieu, *Traité des impôts*, vol. i. pp. 223-224.

fare of the commonwealth. This view was expressed in scientific form by Justi, and Adam Smith and his school afterwards spread it abroad. The Physiocrats are advocates of the same doctrine, only in a cruder, more abstract, more exaggerated form. In view of all that we observed with regard to the legislation generally and particularly the tax legislation, of the French Revolution, it seems improbable that the authority of the Physiocratic doctrine alone would have been sufficient to establish the tax on realty as so essential a factor in the French tax system, if that tax had not at the same time fitted in so precisely with the facts of the case.

The law of November 23 and December 1, 1790,<sup>1</sup> introduced a tax on realty, to be assessed in proportion to the average net rental. The net income from property was to be found by an appraisal, taking account of the character of the soil and the kind of cultivation, and with deduction of the cost of cultivation. For city property (buildings) the basis of the tax was to be the rental, after deduction of one-fourth for wear and tear, etc. The sum to be raised by the tax was to be determined beforehand by a legislative act, so that the officials having charge of the assessment would simply have to distribute the aggregate amount of the tax among the individual parcels of property. The tax was to be collected beginning with January 1, 1791. The uniform appraisal of net income from the land met with great difficulties. The provision that the tax must in no case exceed one-sixth (1791), afterwards one-fifth (1793) of the net rental was not found sufficient. It appeared that resort must be had to a cadaster, in which each particular property was registered, specifying the character of its cultivation, its net rental and its boundaries. The cadaster was begun in 1807 and was not finished until 1850. But inasmuch as this painstaking and tedious task was carried out without taking into consideration changes in cultivation and in the net rental, it presented only a

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<sup>1</sup> Vuatrin et Batbie, *Lois administratives françaises* (1876), pp. 342-481. A. Wagner, *Finanzwissenschaft*, vol. iii. (1888), pp. 432-502. Von Reitzenstein, *Das Kommunalsteuersystem Frankreichs und die Reform in Preussen* (*Schriften des Vereins für Sozialpolitik*, vol. xii. 1877).

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picture of the situation at the moment of the first assessment, no account being taken of any change except changes of ownership, changes in tax exemption, and the destruction or construction of buildings. But in consequence of the lapse of time since the beginning of the cadastration, it came to pass that the cadaster was not an accurate expression of a real situation with respect to net rental, even at the time of its inception. Immediately after the cadastration was concluded it was officially ascertained that the tax on realty in France varied from 3.74 per cent. to 9.07 per cent. of the net rental. It amounted on an average to 6.06 per cent. of an appraised revenue of 2645 million francs.

In addition to all this, changes in the net rental have also taken place, and (according to official enquiries, 1851-1880) the net rental varies greatly with variation in the kind of cultivation.<sup>1</sup>

The intention of the legislators to establish a distribution of the tax on realty in proportion to the net rental was therefore not accomplished by means of the cadaster either.

At the same time the harshness of these inequalities have been, to a slight extent, made more tolerable by avoiding any increase of the aggregate amount of the tax. In 1790 the aggregate was fixed at 210,000,000 francs, in 1804, at 184,000,000, in 1821 it was lowered to 154,000,000, in 1859 it was 162,000,000, in 1884, 175,700,000 francs. Of course the supplementary taxes for departments and communes are a factor of some importance, and of growing importance (1838, 70.78 millions, 1851, 96.3 millions, 1885, 192 million francs). If the question were simply that of increasing the tax to correspond with the increase in net rental that has taken place during the century, this increase of the communal supplementary taxes might probably be regarded as a sufficient increase of the tax as a whole. Even an increase of

<sup>1</sup> The net income per hectare was:

	1851	1880	Increase
	Francs	Francs	per cent.
Garden	119.61	166.06	38.0
Arable	42.49	56.47	33.5
Meadow	72.60	96.67	33.1
Vineyard	69.38	129.95	87.3
Forest	20.18	22.50	11.5

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the tax beyond this proportion would be quite feasible and proper. The inequality that is properly to be complained of is that which results from the imperfect character of the cadastration.

§ 300. Even at the outset the tax legislation of the Revolution did not proceed on the Physiocratic doctrine that the land tax was to be the sole tax. On the other hand there was introduced at the same time (December 5-19, 1790, January 13, and February 18, 1791) the "Personal and Personal-Property Tax" [*impôt personnel et mobilier*].

The purpose of this latter was to supplement the land tax by reaching incomes which are not drawn from landed property. In this case, too, the problem was to divest the *taille* of the arbitrary character it had hitherto borne; by the addition of objective, impersonal specifications. As such an external aid, the amount of rent paid by the taxpayer had been favorably considered even before this time. After some tentative experiments, among which was also a personal class tax, the law of April 24, 1806, incorporated as permanent elements in the tax: (1) a personal tax amounting to the value of three days' labor (minimum 50 centimes, maximum 1.50 francs); (2) the personal property tax [*impôt mobilier*] based on the rent of dwellings.

The aggregate amount of this tax for the whole country, as well as its repartition among the departments, is determined yearly by the budget; the departmental quotas are then distributed among the arrondissements and communes, and the communal quotas are distributed among the individual taxpayers. The personal tax, limited by law to the value of three days' work, is the fixed element in the tax; the product of this is deducted before distributing the amount of the tax among the individual communes, arrondissements and departments, in proportion to the rent paid for dwellings. From the tax so distributed are exempted industrial and business establishments together with the usufruct of furniture in dwellings which are rented furnished.

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This Personal and Personal-Property Tax is therefore, in part, a very moderate poll tax, which, in spite of repeated attempts at its development in the direction of a Class and Income Tax, still remains in an embryonic state. In part - and this comprises the greater part of the entire tax - it is an ordinary tax on dwellings, based on the rental of the dwelling.

Here, as well as in the case of the tax on realty, it follows from the inflexible form of the tax that the revenue has developed but slowly and not in proportion to the development of the national expenditures and the people's taxpaying capacity. The national tax was, in 1832, 39.41 million francs; in 1870, 55.51 millions; in 1885, 70.26 millions. The repartition of the aggregate amount of the tax among the departments has remained unchanged since 1832. Within, the arrondissements and communes there is a greater flexibility; the supplementary taxes for communal purposes showing the more vigorous development: the supplementary taxes have risen from an aggregate of 9.13 millions in 1838, to 32.86 millions in 1885; the communal supplements - have increased during the same period from 4.04 million to 28.97 million francs.

A modification of the tax is possible, in that the communal quota may be in whole or in part paid out of the receipts from the octroi (on resolution by the common council and authorization by the national government), and in point of fact this is the practice in the larger cities. Paris, for the payment of the portion not covered by the receipts from the octroi, lays a rental tax of a strongly progressive character (while the rate of the ordinary *impôt mobilier* is a proportional rate), rising from zero (for rentals of less than 250 francs) to 9 per cent. (for rentals of 1500 francs and upward).

§ 301. Originating in 1798 as a supplement to the *impôt mobilier*, the Door and Window Tax presently became a tax on realty, by making the landlord surety for the payment of the tax. The owner's name alone is carried on the tax list. It is left entirely to him to recoup himself from the tenant for the pay-

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ment of the tax. But this is not commonly done; so that the tax is, in practice, a house tax, which may, under given circumstances, be shifted to the tenant, but is not primarily expected to be paid by him.

The schedule of rates under this tax was fixed by a law of April 21, 1832. The rate is graduated in proportion to the size of the dwelling and the number of openings and windows of the house, with a slight reduction on the windows of the upper (third, fourth, etc.) stories in the larger cities. This tax, also, therefore, is levied by a hard and fast schedule, and based on outward symptoms as far as possible without any attempt to penetrate into the personal circumstances of the taxpayer; it is an objective tax of characteristic French precision. But the precision is a negative one, so to speak, in that it defines very clearly what are the rights and liabilities of the taxpayer (though it leaves room for a good deal of casuistry - in individual cases), rather than positive in the sense that the particular external specifications on which the tax is based are well chosen, or even favorable to the development of proper housing of the people.

In 1802 the aggregate sum to be raised by the tax was arbitrarily fixed, because the receipts had been too low during the years immediately preceding. But inasmuch as the data were wanting for a proper repartition of the tax among the departments, etc., it was quite in order (March 26, 1831) to replace this repartition tax by a proportional tax, which increased the receipts and drew more heavily on the portions of the country that were better able to pay. But by April 21, 1832, the favorite system of a repartition tax was reinstated, the aggregate receipts being now fixed at 22,000,000 francs (instead of 16,000,000 francs in 1802). At the same time greater flexibility was given the tax (1835, 1844) by graduating the schedule of rates according to the size of the establishment, and by taking account of new buildings.

The aggregate receipts have therefore increased - 1870, 40,000,000 francs; 1885, 47,000,000 francs. The number of



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houses (and factories) in 1876 was 8,630,182; so that the average amount of the tax is quite moderate.

§ 302. Finally, there is the Trade-License Tax [*Gewerbsteuer*] (*contribution des patentes*). This was originally based on the rental of the place employed for the trade (decree of February 19-25, 1791). It was abolished in 1793, re-established by a law of July 22, 1795, altered during the years following, especially by the, law of October 22, 1798; it was further developed and adapted by the law of April 25, 1844, and later by the law of July 15, 1880.

It is contrasted with the other three taxes spoken of in not being a repartition tax, but is like them in being based on external indications which, during the development of the past century, have been the subject of a progressive casuistical treatment. The name (*contribution des patentes*) is due to the fact that the governmental concession under the rule of free choice of employment established by the Revolution, involves the obtaining of letters patent, the granting of which was based on purely fiscal conditions, namely, the payment of a yearly tax. But as a uniform annual payment, incumbent on all persons following a trade, could at best be but very low, there came to be gradually introduced an ever more exact gradation in the rates of the tax. This was accomplished in part by graduating the fixed yearly license fee, in part by means of the Proportional Rates combined with it and based on the rental of the place employed for the trade or of the dwelling.

To the trade-license tax are subject trades and occupations, in the conventional sense which excludes agricultural pursuits. It includes, however, the chief liberal professions, in so far as these are carried on independently. Exempt are the business establishments on the smallest scale (without assistants, apprentices, or the like.

In the case of occupations serving the needs of the local population only, the rate of taxation is graduated according to the number of inhabitants of the place. All occupations are classified (in four classes) according to the character of the

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industry, and within each class the establishments are classified according to the rental paid. The maximum tax paid as a trade license, as, for example, by a Parisian banker, may amount to three or four thousand francs. For the great majority of persons liable to this tax, the rate (assessed anew every year fluctuates between two and four hundred francs. To this is to be added the supplements levied for the purposes of the department and of the communes.

The aggregate receipts have increased considerably. The revenue going to the state increased from 31 million francs in 1838 to 107 millions in 1885. But the supplementary additions, which at the outset were quite low (6 millions), have now risen to 65 millions; the total has accordingly increased from 37 millions to 172 millions.

The efforts of the French legislation to base the amount of direct taxes on external indications alone, have met with greater success in the case of the license tax than in that of other taxes, even including the tax on realty, because, in the first place, in this case the changes undergone by these external indications from year to year are taken into account; second, because the great number of indications taken into account is being continually more and more developed and better classified; third, because this more accurate ascertainment of the actual incomes of taxpayers enables the taxing power to augment the demands made on the taxpayer in proportion as the needs of state and commune increase. That perfection has been reached in this direction no one will assert. Rather, this legislation is to be looked upon as an experiment to ascertain the limits which tax legislation of this class must not exceed. Within "the limits of a simple income and objective tax, however, the French trade-license tax is probably to be taken as a relatively successful solution of the problem; the problem in this case, analogous with that of the tax on realty, being to determine the average (that is to say, without regard to variations in individual cases) net income, regard being had to objective, external indications alone, and to fix the rate of taxation on this basis.

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§ 303. The unity of presentation of the matter which must be preserved in such a brief survey of the history of taxation, and for the sake of which we have constantly kept the Prussian-German tax legislation in view - this unity is not impaired if, as in the present case, developments of tax legislation in foreign countries are introduced into the discussion, so long as they are developments of such importance for the history of financial science, and at the same time closely related to the practical measures through which the tax system of the Fatherland was built up. The science of taxation and the practice of tax legislation have for nearly a hundred years past been incorporating into the French model which we have briefly described such ideas as our century has found to afford the most satisfactory solution of the tax problem. We shall now take up Prussia, and first of all, the legislation dealing with taxation of realty.<sup>1</sup>

Here, as in France, the eighteenth century prepared the way for the nineteenth century in the matter of a carefully constructed cadaster of rentals and usufructs, and land taxes apportioned on the basis of such a cadaster. The prevalent abuses of the *taille* in France, as a personal tax varying from year to year, are not a feature here, but the oppression of the lower classes of the rural population and the exemption of the nobility are present here as they were there. Differences in the taxes on realty from one place to another are a more prominent feature here, in consequence of the relative newness and imperfect centralization of the political organization. It is also not entirely due to differences in our favor, that the burden of taxation resting on the lower classes was lighter here than in France. The persistence of serfdom even down into the nineteenth century, shielded a large part of the lower classes of the rural population from the

<sup>1</sup> K. G. Kries, *Historische Entwicklung der Steuerverfassung in Schlesien* (1842). Zakrzewski, *Die preussischen Reformen der ländlichen direkten Steuern im 18. Jahrhundert* (1887). H. Bielfeld, *Geschichte des magdeburgischen Steuerwesens von der Reformationszeit bis ins 18. Jahrhundert* (1888). C. Dieterici, *Zur Geschichte der Steuerreform in Preussen 1810-1820* (1875), pp. 217-224. J. G. Hoffmann, *Die Lehre von den Steuern* (1840), pp. 94-140. K. G. Kries, *Vorschläge zur Regelung der Grundsteuer in Preussen* (1855).

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incidence of the land tax, by depriving them of the possibility of ownership; whereas in France villenage disappeared centuries ago, and the widespread peasant proprietary was the prerequisite of a general incidence of the land tax.<sup>1</sup>

In strong contrast with what happened in France, the idea of the new century (expressed in the Fiscal Edict of October 27, 1810), that equality of taxation was to replace the inequity of the olden time, failed to make good its promise. This is a point at which the Revolution shows itself superior to the peaceful methods of reform which prevailed in the Prussian state. The peaceful reform requires another half century to overtake the Revolution.

The land taxation which immediately preceded the reform period in the Prussian territory varied greatly from place to place. An attempt had been made as early as the times of Frederick William I. to terminate the cruder inequalities in the distribution of taxes; he sought to adjust the Hide Tax [*Hufenschoss*], and the Horn and Hoof Tax in East Prussia to the real productive capacity of the property, whereas the quality of the fields had hitherto been left out of account, and this mechanical uniformity of taxation had resulted in the grossest inequality in the burdens imposed. In this attempt was included an endeavor to tax the nobility and the peasantry on the same basis,<sup>2</sup> as also to impose an income cadaster, of the nature of an objective tax, which should take no account of incumbrances on the land, etc. Reforms of the same nature were in progress in Pomerania and in Citerior Pomerania at the same time. In Silesia the Austrian government had begun the construction of a cadaster in 1723, and Frederick the Great had, since 1743, tried to introduce a uniform tax on land instead of the numerous burdens that had accumulated in the course of time; dating from 1748 he had established a cadaster which was in part based on an extremely artificial

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<sup>1</sup> Tocqueville, *L'ancien régime*, p. 55. Taine, *Les origines de la France contemporaine*, vol. i. (1876), livre v. ch. ii.

The nobility should enjoy no preference, declared Count Waldburg in one of his memorials to the king in 1715, inasmuch as the monarch is obliged to afford protection to the fields of the nobility as well as to those of the peasants. - Zakrzewski, p. 28.

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method of computing the income. For West Prussia a cadaster was established in 1773. In the duchy of Magdeburg, Frederick William I. introduced order into the rural tax system, with such effect that at the end of the eighteenth century Klewiz, the historian of the Magdeburg tax system, very significantly expresses the opinion that the people could from that time on rely upon the immutability, the fixed and stable character of its taxes; every farmer knew the amount of the tax and could plan his work and his expenses accordingly.<sup>1</sup>

§ 304. The edict of October 27, 1810, on the national finances and the new revenue regulations, made the following promise "A new cadaster will be put in force as expeditiously as possible, by which to regulate the land tax; our intention in so doing is by no means to increase the amount hitherto levied, but simply to effect an equal and proportional distribution of the tax among all taxpayers; still, all exemptions are to be abolished, as they are no longer consistent either with natural equity or with the spirit of tax administration in neighboring states; the lands hitherto exempted from the land tax will accordingly be subjected to it without exception, and it is our pleasure that this decision shall apply also to our own domanial estates."

The inequality of the taxes on land in the different parts of the country was such that the five provinces, East and West Prussia, Posen, Brandenburg and Pomerania, which comprised an area of more than three thousand square miles and a population of nearly 4.50 millions, yielded a revenue of only three million thalers, while the provinces of Silesia, Saxony, Westphalia, Cleve-Berg and the Lower Rhine, which had not quite two thousand square miles and something less than 6.33 million inhabitants, yielded a land-tax revenue of over seven million thalers.<sup>2</sup> The Lords-Lieutenants of the western provinces declared in the discussion of the tax-reform projects laid before the Privy Council in 1817, that they considered the imposition of uniform tax

<sup>1</sup> Bielfeld, *Geschichte des magdeburgischen Steuerwesens*, p. 166.

<sup>2</sup> *Report of the Department of State (of January 31, 1820) to the King*. - Dieterici, p. 241.

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burdens in the form of personal and consumption taxes throughout the country to be impracticable, so long as a uniform taxation of land was not also introduced. The disparity in the land tax in the old provinces had, down to the introduction of the reform, been measurably neutralized by differences in the other taxes. Of the three million thalers, it is true, two million was borne by Silesia alone; but Silesia yielded scarcely 2.50 millions of excise out of an aggregate excise revenue of 7.5 millions (1810), many occupations properly belonging to the towns being, in Silesia, suffered to be carried on in villages free of excise. Of an aggregate of 18.25 million thalers, in 1810, Silesia's contribution was 6.25 millions, although it comprised two-fifths of the population of the entire state. All this was changed by the reform of the excise. Still the state department declared, January 1, 1820, in its report on the tax-reform law, that it would be impossible immediately to abolish all inequality in the land tax, if for no other reason, because a new distribution of the land tax would have to be preceded by long and expensive surveys and appraisements. It was therefore proposed to equalize the burden by making a change in the other kinds of taxes, whereby the amount required of each taxpayer would be reduced by as much as it had previously been too great. The difficulties of such an equalization (which the majority of the Council, under the leadership of von Bülow, formerly Minister of Finance, pointed out) lay in the absence of a universally applicable standard of apportionment such as was not afforded by the number of the inhabitants alone. The recognition of this difficulty resulted in the reference of further consideration of the matter to the provincial assemblies, which were presently to be called together, and so postponed it to an indefinite future date, as the law dealing with imposts was adopted on May 30, 1820.

It was only in the two western provinces, where there was a demand for an equalization of taxes on land as between individual taxpayers, as well as a need of equalization as between provinces, that an improvement was made in the distribution of the land tax, based on a survey and assessment and without

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increasing the aggregate revenue from the tax. It was an improvement over the uncertain assessment on which the land tax in those parts of the country had been based at the time of the French governments, an assessment which even at the time it was made, was regarded as provisional only, and was coupled with the promise of a future, more accurate survey and assessment of the individual parcels of land.<sup>1</sup>

The aggregate income from the land tax in the whole of the Prussian territory was, in 1821, 9,878,752 thalers; in 1838, 10,163,942 thalers. The amount per capita of the population has varied from 11.5 silver-groschen (in the province of Prussia to 35.5 silver-groschen (in the province of Saxony). Westphalia and the Rhine province made a good second (34 and 33 silvergroschen). Brandenburg paid scarcely 16 silver-groschen; Pomerania, 15.33, Silesia, 26.75.<sup>2</sup>

§ 305. The movement of 1848 and immediately succeeding years, which pushed on so many of the arrears of the reform period of 1810-1820 towards a solution, brought up again also the demand for a settlement of this old legislative debt. The exemptions from the land tax and the inequalities in taxation remained in force afterwards as they had been before; the absolute amount of the land tax had remained unchanged (10,085,387 thalers in 1855) although the population had increased from 11 to 17 millions during the period 1821-1855, while the expenditures of the state had risen from 86 million to 105 million thalers during the years 1849-1855 alone.<sup>3</sup> The state and local bodies were alike deprived of the chance of making an adequate use of this tax. While the purpose of the reform in 1810 had been simply a better distribution of the tax, it was now, after a lapse of half a century, and in view of a great increase in popu-

<sup>1</sup> A lucid presentation of the land-tax systems of Prussia is given by Struensee, *Die Grundsteuer mit besonderer Beziehung auf das Königreich Preussen* (1810). More detailed is the account by Schimmelpfennig, *Die preussischen direkten Steuern* (2<sup>d</sup> ed., 1843).

<sup>2</sup> J. G. Hoffmann, *Die Lehre von den Steuern*, pp. 126-130.

<sup>3</sup> K. G. Kries, *Vorschläge zur Regelung der Grundsteuer in Preussen*, p. 4.

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lation and wealth, quite fair and equitable that some increase in the amount to be raised by the tax on land should be made. To this is to be added that the taxation of cities, relatively to the rural districts, still bore plain marks of the tax methods of the eighteenth century. As an equivalent of the land tax there had been introduced into the towns, after the abolition of the earlier excise, an increased billet tax [*Servisløst*] (as a contribution towards the expense of quartering the troops).

In the western provinces, where the sense of national solidarity was still slight, and where French-Liberal views prevailed, it was a constant source of complaint that the land tax bore more heavily on these than on the eastern provinces, and that the government showed no inclination to mend the difficulty; a decree of the Diet with regard to Westphalia, dated December 30, 1834, embodied a distinct refusal to do anything about the matter. The new movement made the preference shown the estates of the nobility above the lands owned by peasants a prominent point of the agitation; it became an eminently political question; the Liberals demanded an abolition of this mediæval survival. As early as 1847 the committee appointed to consider petitions regarding the land tax expressed themselves (11 to 5) to the effect "that the government should be requested to reorganize the land tax on a basis of equality and with the abolition of all privileges." In March, 1849, the proposal was brought forward simultaneously in both chambers of the new parliament by members of the Right (to which the owners of noble estates chiefly belonged), to request the ministry as soon as possible to submit bills for the abolition of existing inequalities in the direct taxation. On February 24, 1850, a law was passed which (through lack of time for consideration of details) simply declared the general principle that all exemptions and privileges in matters of taxation were forthwith to cease. The question of indemnification was reserved for future decision. A bill brought in by the government in the year 1851-52, dealing with the execution of this law, fell through on March 7, 1853, because the Right was unwilling to content itself with an indemnity amount



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ing to only two-thirds of the value, while the Left refused to grant any indemnity whatever, at the same time that the government had made unanimous consent on this point a condition on which the whole law depended.

The success of the project at this time, as in earlier years, was hindered by a variety of obstacles of a general character, but there was also the special objection, on grounds of administrative expediency, which J. G. Hoffmann<sup>1</sup> had brought out as early as 1840, and which K. G. Kries urged with decisive arguments in 1855, - the objection of the inexpediency of such a cadaster as had then recently been completed in France, after protracted labors, and which, instead of meeting the high-strung expectations with which it was begun, turned out to be a stupendous disillusionment. It had been Hoffmann's wish that the existing taxes on land should be declared a redeemable rent, and that it should be replaced by a license tax on agricultural occupations. Kries pointed out that the experience of both the western Prussian provinces and of France showed that the newly constructed cadaster was of considerable service in equalizing the land tax within a relatively small area, but not as a basis for alterations in the contingents to be paid by large and widely separated regions. The officials in charge of the cadaster on the Rhine, as well as those in France, themselves admitted that any computation of net income was uncertain; that the coincidence of the figures obtained by the cadastral computation with the actual net income could never be assured; that the figures afforded by the cadaster were rather of the nature of a proportion, while uniformity of assessment was to be attained rather by observation of the business transacted than by depending on the figures obtained by computation. In every one of the various cadastrations that had to do with the ascertainment of the net income from business of any kind (classifications of soils, determination of the gross product, computation of the money value of the product, determination of the cost of cultivation) a considerable margin is allowed for estimates by experts, very appreciable

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<sup>1</sup> *Lehre von den Steuern*, pp. 105 et seq.

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divergencies appearing in the figures obtained from different persons and under different circumstances (especially in a large territory), even apart from any influence that may be exerted by practical interests; to this is to be added the changes in the industry which take place from year to year.<sup>1</sup>

Instead of the produce-cadaster [*Ertragskataster*], therefore, Kries sought to find a method of assessment that should be simpler, cheaper, more adequate, and should conform with the facts of industrial life and keep pace with industrial progress. He called attention to the importance and the necessity of a productive tax on land, and showed that the income cadaster was not an expedient means of assessment, whereas there were other means available which he thought were to be found in the example afforded by England and its local taxation, as also in the property tax system and the method of assessment in use in the United States. In both these countries a heavy burden of taxation rested on real estate, but it was not levied by means of an income cadaster. In neither of these countries, according to Kries, does the valuation of real estate involve either great expense or great difficulties; complaints of unfair assessment are rare. The reason is that the assessment is based on data afforded by business transactions. In England the guiding principle is afforded by the rental, in America by the market price. The fact that the tax on land is by preference employed for local purposes only in both these countries simplifies the problem of assessment, in that it requires consistency of assessment only within the limits of the minor civil divisions. Now, in Prussia it is an urgent question how the communal bodies and their functions may be strengthened and extended: At this point, therefore, a great principle of political reform falls in with

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<sup>1</sup> Kries thought (p. 67) that we must admit that the men are in the right who think that the time and energy, the means and labor spent in the construction of a cadaster of parcels of land, are for the most part spent to no purpose. Hoffmann had asserted that the circumstances affecting the value and use of agricultural land change so greatly even within a moderate space of time as to destroy the value of the entire painstaking and expensive labor of cadastration, with the exception of the simplest item alone, that is to say, the survey (p. 105).

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the aims of administrative reform involved in the reform of the land tax. The depression prevalent in the western provinces, due to the oppressive character of the existing land tax, would be relieved just as soon as it should come to pass that the revenue from the income tax should be kept in the country for provincial and local expenditures. The flexibility of the land tax, which would so take the place of its traditional rigidity, would render it more available and more productive under the rule of the new method of assessment and expenditure.

These recommendations of Kries's have been spoken of here in detail, because they were not successful in finding acceptance. The example of the French income cadaster was still able to exert a decisive influence when, at the beginning of the regency (1858), the reform of the land tax was again placed on the order of the day with somewhat more of a prospect of success than before.

§ 306. The law of May 21, 1861, establishing the new order of things in the land tax, divides the aggregate taxation of real estate into the land tax proper, levied on property employed in agriculture or in forest industry; and the tax on buildings [*Gebäudesteuer*], levied on buildings and the attached courtyards and gardens (not exceeding one morgen).

The land tax proper was, from January 1, 1865, fixed at a yearly aggregate of ten million thalers, that is to say, two millions more than the old land tax produced, if deduction were made of the amount now to be paid by the tax on buildings (7,920,231 thalers). The ten millions were to be repartitioned among the provinces, local divisions, precincts, on the basis of a new valuation of the net product differing from the earlier one. Exempt from the land tax are lands belonging to the state, the domanial lands of the German barons, lands belonging to the provinces or to local civil bodies and appropriated to some public service (roads, canals, cemeteries), certain lands belonging to churches and schools. All other lands previously exempt or privileged under the land tax are, from January 1, 1865, to be

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taxed on their net income, equally with other lands, but with the payment of an indemnity fixed by a special law of the same date. Authenticated exemption from taxation was to be indemnified at the rate of twenty times the new land tax; otherwise an indemnity of two-thirds of this amount was to be paid.

A special ordinance was issued simultaneously with the new law, regulating the method of appraising the net income. Quite in contrast with the long-protracted work of the French cadaster, the limit was, at the outset, fixed at three and one-half years, and this limit was in fact observed.<sup>1</sup> An assessment commissioner was to be appointed for each circle, who was to have charge of the business and to act as chairman of the circle committee, this latter consisting of from four to ten persons, according to the extent of the circle, one-half of the membership to be appointed by the representatives of the circle and one-half by the central government. A department commissioner was to have the charge of the business for each department, assisted by a department committee of a composition similar to that of the circle committees. At the head of the entire organization was the central committee, under the presidency of the Minister of Finance. There were 302 commissioners appointed for the 342 existing circles, but by a further consolidation of circles the number was afterwards reduced to 284.

The valuation gave a net income; for the entire kingdom,<sup>2</sup> of 140,446,993 thalers (an average of 34 silver-groschen per morgen over all; for the province of Prussia, 19 silver-groschen; for the Rhine provinces, 54 silver-groschen; for Saxony, 62 silver-groschen). The average rate of the new land tax, therefore, amounted to 9.50 per cent. of the net income. Of this amount, Silesia, Saxony and the Rhine province have to pay about one-

<sup>1</sup> The legislation on the land tax in the kingdom of Prussia was somewhat different. For a statement of the method of assessing the land tax, the more important results of the survey and assessment, the resulting distribution of the tax burden, and the expenses of the assessment, cf. the special supplements to Nos. 19, 24, 27, 32 of the *Königlich preussische Staatsanzeiger* for 1866.

<sup>2</sup> Exclusive of the exempted estates, whose net income was estimated at 7,866,735 thalers, with an average net income of 21 silver-groschen per morgen; this low figure being due to the great proportion of woodland classed under this head.

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half, in very nearly equal proportion; the province of Prussia, 1.33 million thalers; Brandenburg, 1.11 millions; Westphalia, 0.96 million; Posen, 0.73 million; Pomerania, 0.82 million. The absolute increase as compared with the old land tax, was greatest in the province of Prussia (previously 0.55 million), and somewhat the same in Brandenburg (0.54 million: It was relatively greatest in Posen, where the new tax amounts to nearly twice the old (0.73 million as compared with 0.37 million, and in Pomerania (0.83 million as. against 0.41 million). A relatively moderate increase also resulted in Saxony and the Rhine province (0.21 million and 0.15 million respectively). An absolute decrease took place in Silesia and Westphalia (0.16 million and 0.04 million respectively).

The cost of the cadastration amounted to 7.32 million thalers, that is to say, two silver-groschen per morgen on an average (whereas the cadastration in the western provinces, in 1818-1834, had cost nearly seven silver-groschen per morgen).

Simultaneously with the law introducing these changes in the land tax, a law was also passed, on May 21, 1861, establishing a general building tax.

This tax supersedes all the earlier taxes on buildings, where such had existed.

Exempted are buildings belonging to the state, to the provinces, to the circles and communes, devoted to public purposes; also unoccupied buildings which are intended to be used in agricultural industry only. The assessment of the tax is based on the annual usufruct of the property. The rate is 4 per cent. for such buildings as are used mainly as dwellings, 2 per cent. for such as are used mainly for industrial purposes. So far as possible the rents customary in the place during the previous ten years are taken as the basis for determining the value of the usufruct. The assessment of the tax on buildings is to be subject to a revision every fifteen years.

Both these laws were afterwards introduced in the provinces annexed in 1866. By a law of February 11, 1870, the land tax was introduced into the provinces of Schleswig-Holstein, Hanover and Hessen-Nassau, dating from January 1, 1875. It was

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fixed at an annual amount of 3,200,000 thalers, and was distributed between the provinces in proportion to the net income on which the tax was paid. The building tax was introduced into the new provinces by ordinances issued April 28 and May 11, 1867.<sup>1</sup>

The land tax has therefore maintained itself as a permanent and, apart from slight variations, unaltered burden, yielding, for a considerable number of years past, about 90 million marks. The tax on buildings on the other hand, better adapted to the exigencies of the situation in respect of assessment, as Kries has pointed out, has increased with the increase of wealth (1878-79,<sup>2</sup> 18.84 million marks; 1887-88 30.15 million marks; 1889-90, 31.50<sup>3</sup> million marks).

While it may be true that the land-tax reform in Prussia was delayed for half a century beyond the date at which it was first seen to be a political and fiscal necessity, so that the adoption of the French example in its fiscal administration has often been spoken of as the result of an obsolete point of view, the recent measures taken by the Kingdom of Italy may be cited as a striking parallel. In Italy, after the consolidation of the country, the differences existing in the taxation of land presented a situation not unlike what existed in Prussia at the beginning of this century.<sup>4</sup> After the lapse of a quarter of a century, a law was finally adopted, March 1, 1886, dealing with the reform of the land tax. This law ordains a cadaster of the net product of land, with the double purpose of an authentication of ownership and an equalization of the tax on land. So we find that here again; and very recently, the French example has been honored.

§ 307. Another form of a tax on profits was established by the tax reform in Prussia during the years 1810-1820, earlier

<sup>1</sup> Rönne, *Das Staatsrecht der preussischen Monarchie*, vol, ii. sec. 528.

<sup>2</sup> *Finanzarchiv*, 1887, p. 316.

<sup>3</sup> Of this Berlin alone yields 6.24 million marks.

<sup>4</sup> Ricca-Salerno, "Die neue Regelung der Grundsteuern and die Steuerreform in Italien," *Finanzarchiv*, 1885, pp. 747-807. Cf. also, *Finanzarchiv*, 1888, pp. 362-383.

than the land tax. This was the license tax on occupations [*Gewerbsteuer*].

In the Prussian state, down to the year 1810,<sup>1</sup> the pursuit of certain occupations was subject, here and there and with no uniformity, to licenses and taxes on occupations. But a general tax on occupations was for the first time introduced by the edict of November 2, 1810, which followed the French example in incorporating fiscal designs in its carrying out of the new principles of a free pursuit of occupations. The receipts were somewhat over 600,000 thalers. Permission to follow any occupation was to be had by the yearly purchase of a certificate of license from the government. Exempted were those who followed agricultural pursuits on their own account, day laborers, common servants, national and communal officials. The highest license fee was 200,000 thalers, the lowest one thaler; it was impossible to effect anything but a very general classification of occupations in the schedule, the final decision being in the great proportion of cases left to the discretion of the local authorities.

After the close of the war the increased size of the Prussian state made it necessary to bring order and unity into the particolored local provisions for the taxation of occupations, and to extend the license tax over the whole country. The license tax of November 2, 1810; however, called for a careful revision, the results of which were embodied in the law of May 30, 1820, dealing with the payment of the license tax. The provisions of the earlier law were so altered as to leave the liberal professions exempt from the license tax; likewise the smaller handicraftsmen employing not more than one journeyman and one apprentice.

In character, this tax is half way between a tax on profits and a personal tax; indeed it partakes somewhat of the character of the class tax (presently to be spoken of) which was introduced at the same tune, and in so far it diverges from the

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<sup>1</sup>"Promemoria for the bills to be proposed for the equalization of taxes and the regulation of imposts," Dieterici, pp. 291 *et seq.* J. G. Hoffmann, *Die Lehre von den Steuern*, pp. 190-225.

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French pattern. Its purpose is to neutralize the inequality arising from the fact that an appreciable proportion of the persons following a trade are not taxed, either by the class tax or by taxes on consumption, in a fair proportion to their ability to pay. The law has accordingly, in the case of the greater number of taxable occupations, only imposed an average rate [*Mittelsatz*] to be paid by the aggregate body of persons carrying on the same trade within a given department; it leaves the persons subject to the tax to repartition the required aggregate among the taxpayers, by assessment through the agency of delegates chosen out of their midst. These average rates are divided into four classes, according to the wealth and prosperity of the place where the trade in question is carried on. The first class comprises the ten largest cities of the country; the second class, cities of more than 6000 inhabitants; the third class, places of more than 1500 inhabitants; the fourth class, all smaller places. The highest average rate (for merchants in places of the first class) is 30 thalers a year.

The rates of this tax have, in the course of years, been repeatedly altered, being generally increased (Order in Council of November 24, 1813, Acts of July 19, 1861, and March 20, 1872). There are at present three main classes: (1) commerce and manufactures; (2) hotels; (3) handicraftsmen employing several journeymen. Within each of these three categories are a greater or smaller number of subclasses, according to the extent of the business. So, for example, the group A (commerce) has three subclasses, the two higher ones of which (A I. and A II.) each constitutes a distinct tax-paying association, assessing its own members, while the third (B) is assessed by the officials of the circle and commune in consultation with the merchants subject to the tax. The entire country is divided into two parts according to the greater or less preponderance of an industrial-mercantile character. One of these portions is subjected to an average rate of 96 thalers for class A I., while for the other part the corresponding average rate is 72 thalers, but throughout the country a minimum rate of 48 thalers for each taxpayer



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under class A I. is required.<sup>1</sup> The aggregate amount of the tax to be paid is found by multiplying the number of payers into the rate. It is then the duty of the seven delegates, chosen every third year from among the persons constituting the tax-paying association, to repartition this aggregate sum among the individual taxpayers. The other subclasses and groups fared somewhat similarly, but with lower average rates. The receipts from the license tax increased during the period 1821-1826 from 1.70 million thalers to 1.85 millions; from 1827-1838 it rose very gradually from 1.95 million thalers to 2.30 millions. The assessment of 1864 aggregated<sup>2</sup> 3.68 million thalers; that of 1878-79 amounted to 18.67 million marks; for 1887-88 it was 20 millions; for 1888-89, 20.62 million marks (of this amount Berlin paid 2.76 million marks). The population was, at the

Close of 1822	11.66 millions
" 1837	14.10 "
Dec. 1, 1885	28.32 "

The receipts from the license tax, as appears from these figures, have been nearly quadrupled during the period 1821-1889, while the population has increased to not quite threefold. This moderate increase of the rate per capita of the population (0.45 mark to 0.68) is certainly far from expressing the people's industrial progress and increased productivity, whether viewed from the standpoint of the volume of business or from that of the wealth of the people concerned in it.

## VIII. THE INCOME TAXES OF THE NINETEENTH CENTURY.

§ 308. The great truths of national life are simple; their realization is difficult. The new era which is now at the close of its first century can make no new discoveries in matters of taxation, in which the innovation extends beyond the technical details of administration. In the great fundamental principles and in

<sup>1</sup> The license tax of 1810, which was divided into six classes, imposed a rate of from 96 to 200 thalers in the highest class. - Hoffmann, *Steuern*, p. 207.

<sup>2</sup> Bergius, *Finanzwissenschaft*, p. 330.

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their contrasts there is a continual recurrence of what is already long familiar. The difficulties with which the method of taxation which recommends itself to the unsophisticated mind as a matter of course is beset, have been as clearly seen in the earliest beginnings of a scientific knowledge of the subject of finance as they are at present. The progress has been altogether preponderatingly on the side of practical administration; this is shown by the gradual, circumscribed alteration of the difficulties referred to; it appears also in this connection qualified by those limitations of all historical progress which result from interminable deviations from a direct and uninterrupted succession of stages of development.

The problem of the income taxes of the nineteenth century is in intimate relation with the general transformation of social and political life, with the helping and the hindering factors which enter into it, with its influence upon the relations subsisting between the state and the individual. The principalities and the great powers of past centuries afford the traditional contrast to the free cities, in which the significance of a close union between the burghers of the town individually, as well as between the burgher and public affairs, was brought out in a clear light. The towns were the oases of civil liberty in the Middle Ages they were the prelude to the greater national development which was presently to pass over the stage of the principalities and the great centralized states. With the era of the Revolution a new element entered, which hastened and furthered the development. This was the awakening of the sentiment of a participation in the state, which had been slumbering or had been stifled for centuries past. The purpose of this movement, so far as regards the ideas underlying it, was the strengthening of the sentiment of civic duty; nor was the declaration of human rights chary of its magniloquent speech on the subject of the "honor" of taxpaying.

But precisely these swelling words showed that in the practical experience of their immediate surroundings there was a great difference between words and deeds. It was only very

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gradually that the sense of civic duty was able to penetrate the new social organization; at the outset the new national life was intelligible to these people, who had put aside the state, only so far as regarded their rights. It is to be added that the other great factor of the new era, the new industrial productivity, constituted a force which, while it was not in itself antagonistic to the first factor; proved, in its consequences, to be inimical to it. The new means of communication and the redistribution and regrouping of the population which resulted from their introduction; the new means of gain and the resulting new stratification of property-holding; the new examples of gain and its enjoyment, and the chase after success and enjoyment to which they gave rise; the unexampled increase of the population and the resulting struggle for existence; - all this served to accentuate the contrast between society and the state; between the individual and the whole, and, to say the least; all this had an unfavorable influence upon the advantageous results achieved by the new political life.

There is one state which takes the lead of all our great powers, in this new era of civic development. This is England, The peculiar development of its constitution enables it to preserve intact the traditional bond between state and citizen, and therefore to carry over from the past into the new era the habits of political Liberty which in other countries existed at the outset only in words It is a significant fact that England has taken the lead in the income taxation of the new era: Its example is not by any means a faultless model to be followed; there is in it much of the spirit of the olden time with its plea of exceptional exigencies arising through the demands of a war, and it disappears immediately with the close of the great war against France. The influence exerted by the new industrial life is as strong in England as anywhere; the mature growth of a hearty sense of duty in this matter has perhaps come no nearer achievement in the course of the nineteenth century than it was at its beginning. And still, the results attained during the first period of income taxation, with its great patriotic sacrifices on the one

hand, and the early resumption of the income tax and its practical incorporation as a permanent constituent of the English tax system of the nineteenth century on the other hand, are so much of a new departure that we are fully warranted in dating the introduction of the income tax into the new tax systems of civilized countries from these reforms. It is true here as it is with respect to the development of national credit, that it is not the economic phase of the matter alone that is decisive and significant; the essentially decisive element is the ethical-political principles involved.

§ 309. On December 3, 1798, the House of Commons, after a patriotic speech from Pitt, passed a resolution that from April 5, 1799 a tax was to be levied on all income of any British subject, whether residing in Great Britain or elsewhere, and of every inhabitant of Great Britain, to raise the means for carrying on the war against France.<sup>1</sup> The tax was to be levied at the rate of 10 per cent. on all incomes over £200, while incomes under £60 were exempt; for incomes between £60 and £200, distributed in twenty-eight classes, the rate was a progressive one, rising from 1/120 to 1/11. Pitt estimated the aggregate income of Great Britain at £102,000,000, and hoped to raise an aggregate revenue of £10,000,000. The actual results fell considerably short of the expectation (5.6-6.25 million pounds).

This law superseded another and more complicated tax law imposed the previous year, which served as immediately introductory to the income tax, in that, in like manner as the latter, it embodied the principle of a progressive tax, the exemption of incomes under £60, the reduction of the rate of taxation in proportion to the number of the taxpayer's children; especially, it required proofs of the amount of the income in all proceedings

<sup>1</sup>W. Vocke, *Geschichte der Steuern des britischen Reichs* (1866), pp. 505-590. Adolph Wagner, *Finanzwissenschaft*, vol. iii. (1886), pp. 195-198, 238-256, Dowell, *History of Taxation* (1884), vol. ii. pp. 305-353, vol. iii. pp. 103-137. Kries, *Zeitschrift für die ges. Staatsw.* 1854. Gneist, *Das englische Verwaltungsrecht der Gegenwart*, 3. Aufl., (1884), sec. 85. Sinclair, *History of the Public Revenue* (3<sup>d</sup> ed. 1803), vol. ii. pp. 230-252; William Pitt, *Speeches in the House of Commons* (2<sup>d</sup> ed. 1808), vol. ii. pp. 425-458.

for recovery or indemnification. The Property and Income Tax continued to be levied until the peace of Amiens (1802), and was reintroduced immediately on the fresh outbreak of the war (1803). At this time it was given the form which it has permanently retained, and which it also resumed upon being reintroduced by Robert Peel after the interval 1816-1842. Being levied to meet the exigencies of war, it varied down to 1816 with the shifting fortunes of peace and war; it was modified in detail, the rates were raised and lowered, and it was finally abolished, by a large majority (238 to 201), on March 18, 1816, against the proposal of the Vansittart-Castlereagh ministry, which desired to retain the income tax at half the war rates for times of peace. From 1806 the rate of 10 per cent. had been reintroduced, and it brought in a revenue which not only increased from year to year, but was in absolute amount so enormous (£16,000,000 in 1815 as to furnish a striking evidence of the political and economic development of England;<sup>1</sup> when contrasted with the similar attempts by Continental states during the war against Napoleon. The Lord Lieutenant, von Vincke, wrote to Baron von Stein during his first residence in England (1800) expressing his great admiration of the patriotic emulation with which nobility and commonalty devoted themselves to meeting the requirements of the income tax. He found an explanation of this self-sacrificing spirit in his study of the political institutions which for a long time past had served as a bond between the citizen and the state in England.

§ 310. After an interval of a quarter of a century, Robert

<sup>1</sup> In 1806 not less than 1021 persons declared their income to exceed £10,000 (*Darstellung der inneren Verwaltung Grossbritaniens*. By L. Freiherr von Vincke, edited by B. G. Niebuhr (1815, 2<sup>d</sup> ed. 1848), p. 13). The expenses of collection amounted, in 1799, to only .50 per cent. (Vincke, p. 83). In Prussia, according to the tax lists, there were, even as late as 1886, only 737 persons whose income exceeded one-half of this figure (100,000 marks), out of an aggregate population amounting in round numbers to 28,000,000, as contrasted with the population of Great Britain and Ireland, which reached the figure of 21,000,000 only in the Year 1821. (Porter, *Progress of the Nation*, 1836, vol. i. p. 13. Adolph Soetbeer, "Zur Einkommenstatistik von Preussen, Sachsen and Grossbritannien," *Vierteljahrsschrift für Volkswirtschaft, Politik and Kulturgeschichte*, 1887-88.)

Peel again took up the income tax, in 1842, to cover the deficit created by the reduction of import duties. It was at first granted, according to earlier custom, only for a limited term (three years); but it was renewed at the expiration of this term, was increased on the outbreak of the war with Russia, afterwards lowered, being in part reduced to a very low rate, and being altered from year to year according to the varying demands of the national treasury and the varying amounts of revenue derived from other taxes. It is true, the leading statesmen of England have continually flattered the propertied classes with the prospect that the income tax is to be abolished as soon as may be. But the practical fact of its uninterrupted persistence for nearly half a century past seems rather to have erected it into a permanent institution, the equity of which is constantly being more and more clearly impressed on the mind of the propertied class through the growing power and importance of the laboring classes. The propertied class seems by this time, in point of fact, to have accepted the income tax as a permanent institution.<sup>1</sup> The rate was,<sup>2</sup> from 1842 to 1853, a uniform one of seven pence in the pound on every income in Great Britain over £150; it is only since April 1853 that this law has applied to Ireland. During the years 1854-1857 occurred a considerable increase of the rate (14-16 pence in the pound = 6 - 6 2/3 per cent.), but the revenue obtained amounted to no more than what was paid forty years earlier, during the Napoleonic war, by the same country, with a much smaller population, with a much smaller aggregate of wealth, and while subjected to much heavier taxes of other kinds. Since 1857 the rate has been lowered; during the succeeding years it was successively 7, 5, 9, 10, 9 and 6 pence; during the years 1864-1873 it ordinarily amounted to 4-5 pence (1 2/3 - 2 per cent.); in 1874 it declined to 3 pence, and in 1875-76 to 2 pence. During the decade 1876-1886 it rose somewhat (5-6 pence); it has since risen to 8 pence (3 1/3 per cent.) in

<sup>1</sup> "Notwithstanding its inequalities the Income and Property Tax must now be regarded as permanent." - *Whitaker's Almanack*, 1889, p. 178.

<sup>2</sup> *Statistical Abstract for the United Kingdom*, 1843-1888.

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1885-86 and 1887-88 (being 9 pence in 1886-87), but in 1888-89 it declined again to 6 pence. The net income in 1887-88 was £14,275,502.

The depression changes, and is determined annually in the budget; as has already been pointed out (sec. 219). The tendency so far has been to exempt the smaller and medium incomes more and more from the tax. While Pitt exempted only incomes under £60, Peel exempted incomes under £150; in 1853, however, incomes of £100-£150 were again subjected to a moderate tax. But in its latest form (1882) the law favors incomes under £400 by deducting £120 from the taxable amount, at the same time that it entirely exempts all incomes under £150. In addition to this there are special modifications favoring particular classes of incomes; the incomes of leaseholders; for example, in 1888-89, are subject to half-rates only.

The social-political significance of the income tax as a permanent institution in times of peace has long been properly appreciated by sensible men in England. Shortly after its reintroduction by Robert Peel, Lord Ashley, afterwards Earl of Shaftsbury; occupied himself with a tax-reform scheme on a large scale, in which it was proposed to abolish the beer tax and the duties on corn entirely, and to lower the duties on tea and sugar to one-sixth of the then existing rate, at the same time that the income tax was to be raised to five per cent.<sup>1</sup>

§ 311. The English income tax has (since 1803) in a peculiar degree been based on the distinction of all kinds of incomes into classes corresponding to the sources from which the income is drawn. Of these classes the law enumerates the following five: A, landed property, B, income from rural leaseholds, C, interest-bearing capital the interest on which is paid within Great Britain and Ireland, E, official salaries, D, industrial enterprises and the liberal professions, together with all

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<sup>1</sup>An entry in Ashley's diary for November 28, 1844. - *The Life and Work of the Seventh Earl of Shaftesbury*, by Edwin Hodder (1888), p. 316.

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Incomes which are not included under the four other classes (as, for example, receipts from capital invested abroad). It is thought that the facts will be ascertained with greater accuracy by means of this classification of incomes,<sup>1</sup> than if, as is the practice in income-tax legislation elsewhere, the aggregate income of the individual is made the basis of assessment. Habituation to this method of assessment seems to have recommended its retention in England, while in other countries there is little evidence of an inclination to follow this example.

Subject to the tax are all British subjects resident in the country or only temporarily absent, as well as all amounts payable within the country (whether they are remitted abroad, and whether they are paid to a citizen or to an alien within the country) and all amounts due from foreign countries.

The revenue from landed property (A) is found by ascertaining the rental value which, owing to the peculiar features of the English land system, it is possible to determine on the basis of a great number of actual cases. In case of an incumbrance on the property the owner is entitled to deduct a proportionate amount from the tax. It also frequently happens that the tenant (lessee) pays the tax for the owner and then deducts the amount from the rent. Incomes from leaseholds (B) are assessed in a fixed proportion to the rent (in England one-half, in Scotland and Ireland one-third) with reservation of the privilege on part of taxpayer of proving that his actual gain is less than this proportion. In both of these classes the declaration of the taxpayer is taken, and the assessment is subject to revision every three years.<sup>2</sup>

<sup>1</sup> This method of assessment has been retained in England ever since its first introduction, though quite at variance with the usual method of assessing an income tax. In the year 1801, when every taxpayer was required to report the aggregate amount of his income, the income tax, at a rate of 10 per cent., yielded, £5,628,000. In 1806 the now prevalent method was introduced, and at the same rate of 10 per cent, the tax yielded rather more than twice that amount (£11,633,000). - Cf. *Report from the Select Committee on the income Tax (Minutes of Evidence, Questions 61, 5061 et seq.)*, and Kries, *Zeitschrift für die ges. Staatsw.*, 1854, pp. 203-207, 548-549, and 1855, p. 384.

<sup>2</sup> In 1888-89 tenants' incomes pay a lower rate (3 pence) than other incomes (6 pence). In Scotland and Ireland the rate is only 2 ¼ pence.



On interest-bearing investments (C) the interest on which is paid within Great Britain and Ireland, deduction of the amount of the tax is to be made by the payer at the time of the payment of the interest. Private establishments doing this kind of business are required to make the necessary reports to the tax commissioners. Similarly in the case of salaries of officials (E) the tax is deducted by the establishment paying the salary and is turned over directly to the tax administration. The profits of business and the like (D) are assessed by means of an obligatory declaration on part of the taxpayer (penalty for omission £50) which is required to be made every year, but under the supervision and control of the tax officials. This class presents the weakest point of the method of assessment. Its peculiar character is indicated by the fact that the usual practice in English assessment, as in that of other countries, of intrusting this duty to local organs of assessment chosen by the taxpayers, is in this case (out of regard for the privacy of business disregarded, and the assessment is intrusted to special commissioners appointed by the government.

The assessment of the tax, generally, is based on the traditional institutions of local self-government.<sup>1</sup> Still, by means of the relatively permanent tenure of the assessors and their independence of any election by the taxpayer, by suitable limitation of the assessment districts, and especially by the right kind of influence exerted by the national tax commissioners, much more adequate provision is made for an honest assessment<sup>2</sup> than is

<sup>1</sup> Gneist, *Englisches Verwaltungsrecht*, 3<sup>d</sup> ed., pp. 632 *et seq.* Cf. also Kries, *Zeitschrift für die ges. Staatsw.*, 1855, pp. 402 *et seq.*

<sup>2</sup> The results of the assessments for the five classes in Great Britain and Ireland have been as follows:

YEAR	ANNUAL INCOMES IN MILLIONS OF POUNDS				
	A	B	C	D	E
1871	152.34	59.12	38.11	189.02	26.86
1880	185.37	69.38	39.86	249.49	32.79
1885	194.37	65.23	41.02	295.52	38.52
1887	196.66	62.71	43.85	285.87	40.31

In each of the five classes a continual increase is noticeable, excepting class B alone where a decrease set in in 1880, which, it is to be remarked, is confined to

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possible where an unmitigated local self-government results in impaneling the citizen's and farmer's aversion to taxes in the jury box (cf. sec. 317 below).

§ 312. The relativity of all institutions for political and tax purposes is made clear by a comparison of the attempts at an income tax made on the Continent at the time of its employment in England in the early years of this century. In the one case as in the other the occasion for the attempt was the extraordinary demands created by the war against France, which necessitated resort to extraordinary means. As such extraordinary means of revenue, it was sought to make use of heavy taxes on property and income. But the practical results differed widely in the one case and the other. In Prussia a property tax and an income tax had been introduced by an edict of May 24, 1812, the former of which was to be not only a nominal but also a real property tax; as a result of this aim it was a mixture of forced loan and tax on all property (landed property, investments; stores of merchandise) 3 per cent. (of the amount of the property itself) was to be paid as a tax. Everyone was required to return his property under oath; in case of grave suspicion of too low a return the commissions in charge were to institute a detailed investigation of the property; a special method of valuation was adopted in the case of merchants to avoid publishing the amount of their assets. All taxpayers were, if possible, to be repaid two-thirds of the tax by means of a sale of the public domains. It was expected that the property tax would produce 25 million thalers, the aggregate wealth of the country being estimated at 850 million thalers (Pitt had, in 1798, estimated

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England only (1880, 51.62; 1887, 45.65), In class D there was a decrease from 1876 to 1880 (1876, 271.97 millions) which however was recovered by 1883.

Taking the five classes together we have the following amounts (in millions of pounds):

1871	465.48
1880	576.90
1885	631.48
1887	629.40

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the yearly revenue of Great Britain at a sum not much less than this, viz., 102 million pounds), but the receipts actually obtained amounted to only 4.50 million thalers:

The income tax enacted at the same time required (in addition to the property tax) a payment of five per cent, on every income of 300 thalers or over; incomes of 100-300 thalers were to pay 1 per cent.; incomes below 100 thalers, subdivided into two classes, to pay one-half and three-quarters thaler, respectively.

A burden of such extraordinary weight could be imposed only as a resort in extreme need, and only temporarily. On September 7, 1814, was issued the edict which abolished the tax. The experiment had been made under the most unfavorable circumstances. The country was already exhausted by war expenditures running over a series of years; the people were not habituated to bearing such a tax, although the patriotic enthusiasm of that time might be counted on for something; the demand was an extravagant one, for although the actual receipts from the property tax amounted to only one-fifth or one-sixth of the estimated receipts, still, even that was more than 10 per cent.<sup>1</sup> of the annual income; and therefore more than the nominal rate of Pitt's income tax at its highest. And this takes no account of the 5 per cent. income tax. In England the people had, for nearly two decades, been gradually habituating themselves to the income tax and learning to manage it in connection with the existing institutions of the fiscal administration. There was already a good foundation present on which to erect the income tax into a permanent constituent of the tax system, and the government, too, was determined to retain it after the close of the war, while only a moderate majority were opposed to it. It was quite otherwise in Prussia. Here the demand was for a single, extraordinarily heavy contribution, coupled for the most part with

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<sup>1</sup> It is true that Hoffmann places the aggregate wealth of the Prussian people appreciably higher than this. He holds that the value of landed property alone amounted to 840 million thalers. The annual production of the industry of the Prussian population at that date (4.75 millions) ought, according to him, to aggregate at least 190 million thalers (not less than 40 thalers per capital. This he holds to have been out of all proportion (over 22 per cent.) to an aggregate wealth amounting to only 855 million thalers.

the promise of restitution, a promise which, it is to be added, was not lived up to in the midst of the financial straits of that time. What favorable conditions were present, either in the people or in the government; for the introduction of and habituation to a moderate income tax as a permanent feature, were largely destroyed by this unsuccessful attempt. J. G. Hoffmann, in his memorial of May 22, 1812, to Prince Hardenberg, had argued in vain against the property tax, whereas he was relatively well inclined to an income tax. On the occasion of the reforms of the years 1817-1820 he was a most determined opponent of the income tax also; he wished to narrow it down to a class tax of the kind that Justi<sup>1</sup> had recommended as early as 1755, when Justi also condemned the income tax.

Minor attempts at introducing the income tax had been made as early as 1808 and 1810. In connection with the earliest financial reforms of 1810, Stein had come forward as an enthusiastic advocate of the income tax;<sup>2</sup> he claimed that it was under all circumstances the most equitable impost, inasmuch as it falls upon all citizens and all sources of income;<sup>3</sup> that it was the most uniform and the most productive tax. It was Stein's view that little attention was to be paid to public opinion in Prussia; that this people is dominated by a deep-rooted egoism, a half civilization and license, combined with the rudeness and absence of feeling that belong to the North; that this unregulated public opinion was to be corrected by severe penalties, and by no means be led farther afield by leniency and indulgence. A royal Order in Council (written by Hardenberg) of January 11, 1811, expresses displeasure at the proposal made by the Estates of the Circle of Heilsberg in favor of a capitation tax.

But even at that date von Raumer (in his work on the British Tax System, especially on the income tax, 1810) had found that

<sup>1</sup> *Staatswirtschaft*, vol. ii. pp. 418-422.

<sup>2</sup> Dieterici, p. 22.

<sup>3</sup> Cf. Bismarck's speech in the Lower House on February 5, 1850, where he says: "... The income tax, which, in point of principle, is the most just and reasonable of all taxes, whatever may be the shortcomings which attach to its administration in consequence of human imperfection." - *Die Reden des Abg. von Bismarck-Schönhausen in den Parlamenten, 1847-1852* (1885), p. 83.

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the experience of England with the income tax was an "*auf immer schreckendes Beispiel*." At the same time Privy Counsellor of Finance, von Prittwitz, in his report to Hardenberg (May 18, 1810), recommended a Class Tax, objecting to the income tax that it could not be levied except by applying most odious measures, inasmuch as it lies in the nature of this tax to pry violently into the secrets of ownership, thereby demoralizing the nation, restraining foreigners from coming into the country, and driving the well-to-do inhabitants out of the land.

§ 313. So the class tax came to be the median line; on which the majority agreed in the tax legislation of 1820; but even this tax could be adopted only in the mutilated form (sec. 270) in which it was expected to serve simply as a complement to the grist and slaughter tax within the limits of the smaller local units, for only within such narrow limits was it thought feasible to undertake even such a class assessment. In towns of five to six thousand inhabitants, and still more distinctly in all larger places, the more convenient grist and slaughter tax was preferred. "The secret of finance is to take without irritating," said Hoffmann in his memorandum on the tax bills of 1820.<sup>1</sup> Labaye, a high official in the fiscal administration, had in 1810 remarked in criticism of the class tax, especially of its higher grades: So long as we do not adopt as our guiding principle some rate per cent. of the income we are simply playing blindman's-buff.<sup>2</sup> The demand for a heavier taxation of the upper classes also found expression in the Privy Council; in a *Separatvotum* of May 5, 1820, Prince William (afterwards Emperor) urged that the new taxes should be discontinued or lowered; and that to this end the wealthier classes of the nation and the more highly salaried officials should be taxed more heavily, and so lighten the burden of the poorer classes of the population. Prince William was by no means alone in holding this view. It was a fact well calculated to urge reflection on the subject of the class tax that in the year 1820, when a number of attachments were

<sup>1</sup> Dieterici, p. 284.

<sup>2</sup> *Ibid.*, p. 32.

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made in Luckenwalde on account of failure to pay the quartering impost, it appeared that, in more than one hundred of the houses subjected to the attachment, not more than 30 thalers' worth of attachable property was found.

So the class tax came to serve as an initial stage towards the development of the income tax in Prussia - a preparatory stage which, for a generation, answered, or was required to answer, to the demands of the existing situation, in much the same way as the provincial estates did service in the political constitution of the nation. A growth of the sentiment of equity, an increase of wealth, together with the development of modern industrial life in Prussia, a growth of the sphere of public activity and of the interest taken in public affairs and the resulting growth of the mechanism of taxation, - these various factors gradually carried legislation beyond this initial stage. In proportion as this rudimentary structure developed into a maturer form, an ever-increasing pressure made itself felt for a fuller development of the higher gradations of the class tax, as well as for a relative exemption of the lower classes of the people, the direct taxation of whom presented itself in an increasing degree, as time went on, to one party as oppression, to the other as idle doctrinarianism.

§ 314. It was intended that the repartition of the new tax should be based not on the incomes of the taxpayers but simply on their position in social life.<sup>1</sup> By tradition, society was subdivided into four classes, and these classes were to serve as the norm for the distribution of the Prussian class tax of May 30, 1820.<sup>2</sup>

The way had been prepared for the class tax by the legislation of the years 1810-1811. Among the new taxes on consumption, which were at that time introduced to replace the earlier municipal excise, was a grist tax [*Mahlsteuer*] amounting to one-half thaler per scheffel of wheat and one-tenth thaler per scheffel of rye. The difficulty of adequately superintending the grinding of grain in the country and in the smaller towns led

<sup>1</sup> J. G. Hoffmann, *Lehre von den Steuern*, p. 163.

<sup>2</sup> Supplemented by the Act of September 5, 1821.

to the substitution, by Act of September y, 1811, of a personal tax [*Personalsteuer*] for the grist tax, which was in point of fact a capitation tax, being levied on every subject of twelve years or over; its amount, one-half thaler, being the computed equivalent of the grist tax payable on an average annual consumption of five scheffels of rye. This amounted to the introduction of a capitation tax for three-fourths of the population of Prussia.

From this it appears that the capitation tax of 1811 was the germ out of which was developed the Prussian class tax of 1820, which afterwards gave rise to the income tax. Instead of three-fourths of the population of Prussia, to whom the capitation tax of 1811 had applied, the class tax comprised six-sevenths of the population. It distinguished four chief classes, each of which was subdivided into two or three subclasses. In the highest class the monthly rate was (according to the subclass affected) four, eight or twelve thalers, in the next highest class it was one to two thalers per month, in the third one-third to two-thirds thaler, in the lowest class one-sixth to one-fourth thaler. These rates applied to the household, single persons without a household establishment paying one-half the rates. The assessment was in the hands of the communal officials, under the supervision of the president of the district. The idea was to substitute in place of differences in incomes the more readily ascertainable differences in social stratification, as a standard for the graduation of the tax, and at the same time to call into service the element of social ambition as a motive to prompt payment of the tax.<sup>1</sup> But this social ambition was confined to certain of the upper strata of society; furthermore there was, even at that time, so great a diversity of tax-paying capacity within each class that an accurate knowledge of this tax-paying capacity was necessary in order to a proper division of the class into subclasses. This of course held true to the greatest extent of the

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<sup>1</sup>As to the mean results of the communal income tax in Breslau, 1820-1843, cf. Kries, *Ueber die Einkommensteuer in Breslau, eine historisch-kritische Abhandlung* (1844). After a review of these experiences he falls back on J. G. Hoffmann's position, and holds that "a gradation of classes in which the inhabitants are classified according to readily perceptible characteristics is the only permissible classification" (p. 79)

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higher classes. In this respect, too, the class tax therefore came to serve as a preparatory stage to the income tax that was to follow. The evolution of social life itself tended to break down the limits of the class tax. This first became evident in the most modern and the wealthiest part of the monarchy, - in the Rhine province. An attempt was made in 1830, for the behoof of this province, to mend matters by a greater specialization and subdivision of the upper classes (the first into six, the second into five subclasses. But the results hoped for were not attained.

During the years 1833-1836, out of every 100,000 thalers paid as class tax in the Rhine province; only 3375 thalers were paid by the first class; in the remaining seven provinces the figure was 3574 thalers; nearly one-half was paid by the lowest class (48,174, and 46,247 thalers respectively).<sup>1</sup> The average annual receipts for the whole kingdom, during the eighteen years 1821-1838, were 6.83 millions; of this the Rhine province afforded 1.10 millions with a population subject to the class tax amounting (1833-1838) to 2.12 millions, while that of the other seven provinces amounted to 9.65 millions. But this tax proved inept also in other respects; in 1822 it brought in an aggregate of 6.72 million thalers, in 1838 not more than 7.16 million thalers, in 1849, 7.57 millions. During this time the population of the places subject to the class tax had risen from 9.85 millions to over 12 millions. The tax had not even kept pace with the increase of population, not to speak of the increase of wealth.<sup>2</sup>

The provocation which acted to hasten this rudimentary structure forward in the line of development lay on the one hand in the hardship which direct taxation imposed on a great number of poor people whose industrial development was not yet ripe for such taxation; and on the other in the cramped condition of the higher classes subject to the tax, where it achieved a minimum of satisfactory results together with a maximum of claims for remission.

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<sup>1</sup>J. G. Hoffmann, p. 181.

<sup>2</sup> Hoffmann, p. 178, explains it as being due to "the government's yielding to the representations of the taxpayers."



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§ 315. The government attempted a reform when it called the Diet together in 1847. The proposed scheme would have abolished the grist and slaughter tax as well as the existing class tax, introducing in place of these an income tax on all incomes of 400 thalers and over, while incomes under 400 thalers would be subjected to an improved form of class tax. The proposal was rejected, although it did not contemplate an increase of taxation but only a better distribution of the burden, seeking thereby to meet the demands of equity which again came into prominence only at a considerably later period; it sought to tax funded incomes at a higher rate than unfunded.

On September 22, 1849, the government submitted to the lower house a new scheme, out of which was evolved the Act of May 1, 1851. The old class tax was nominally abolished, but it was in point of fact virtually retained for its higher classes, which were recast under the form of a classified income tax - another halfway measure, partaking both of the class tax and the income tax ("income tax" proper).

The essential provisions are as follows:

On persons who neither possess an income of 1000 thalers, nor live in a town subject to the grist and slaughter tax, a new class tax is levied. On persons having an income of more than 1000 thalers a classified income tax is levied, and in case they live in a town subject to the grist and slaughter tax they are entitled to an annual rebate of twenty thalers on the income tax.

The new class tax distinguishes three classes, with an aggregate of thirteen subclasses. The rate varies from one-half thaler to three thalers annually in the lowest class, four to ten thalers in the second, and twelve to twenty-four thalers in the highest class. Every person over sixteen years of age is subject to the class tax, excepting such as belong to a household already liable to the class tax.

The classified income tax distinguishes thirty classes, each of which represents a certain space within which the amount of the tax is the same, this space being narrower the lower the

class<sup>1</sup> (20 per cent. of the lowest figure included), The rate is within each class 3 per cent. of the minimum income included in the class, so that those incomes which exceed this lowest figure enjoy a partial exemption under the law. This exemption is greatest in the highest class, where the rate of 3 per cent. on the minimum income (240,000 thalers) applies in the case of incomes exceeding this figure by any amount whatever.

The valuation is in the hands of a commission appointed annually for each circle (or town), presided over by the district president, its members being elected by the representatives of the circle (or commune). The president of this commission of valuation, who also represents the interest of the state, directs the work of assessment. The commission revises the estimates of incomes submitted by its presiding officer, employing in this work all means of information which it can command, but with the proviso that "every offensive intrusion into the pecuniary affairs of the individual taxpayer is to be avoided." From this, assessment appeal may be taken to the departmental commission appointed for each governmental department; this commission is chosen by the provincial representatives and is presided over by a commissioner appointed by the government. It is the duty of this official to see that the assessments are made on a uniform basis and to superintend the work of the commissions of valuation. The whole is under the control of the Minister of Finance, who has to hear and decide complaints against the action of the department commissions. A fine is imposed only in case the taxpayer, in his claim for remission, is proved to have knowingly made too low a return; the fine amounts to four times the amount by which the return falls short.<sup>2</sup>

<sup>1</sup>	CLASS	INCOME		RATE PER YEAR
	1	1000-1200	thalers	30 thalers
	2	1200-1400	"	36 "
	5	2000-2400	"	60 "
	29	200,000-240,000	"	6000 "
	30	240,000 thalers and over		7200 "

<sup>2</sup> Von Rönne, *Das Staatsrecht der preussischen Monarchie*, vol. ii, sec. 529. K. G. Kries, "Ergebnisse der preussischen Einkommensteuer und Vorschläge zu ihrer Verbesserung," *Zeitschrift für die ges. Staatsw.*, 1855, pp. 359-420.

§ 316. The expectations of the government in the way of a revenue from the income tax were quite moderate at the time of the discussion of the bill. It was assumed that there were in the Prussian state not more than 27,400 persons liable to the tax, with an average rate of 70 thalers (aggregating 1.9 millions). The results obtained in 1854 showed that there were then as many as 47,750 persons liable to the tax, yielding a revenue of 2.8 million thalers;<sup>1</sup> but from this amount there was a deduction on account of the grist and slaughter tax, considerably in excess of what the government had assumed.<sup>2</sup>

At the same time the receipts from the new class tax also exceeded expectations. The revenue from this tax - after making allowance for the transfer of the higher classes to the income tax - had been estimated at the same amount which the old class tax, including these higher classes, had yielded in 1849 (7.50 million thalers). The receipts actually obtained in 1853 were 7.94 Million thalers, of which one-half was paid by the lowest class (3.89 million thalers).

The results obtained by the income tax, therefore, indicated an increase in the taxation of the middle and upper classes of the population.

The impression produced by these results was so favorable that the government was able, in 1854, to cover a deficit of 3,000,000 thalers by adding a supplementary tax of 25 per cent. to the income and class tax (including also the grist and slaughter tax).

The moral effect of the income tax on the lower classes served also to strengthen the position of the class

<sup>1</sup> There were 23,545 persons liable to the income tax living in the towns subject to the grist and slaughter tax, that is to say one-half; while the government had assumed that these persons would amount to only one-fourth of the total. The remissions actually made amounted to 465 thalers, instead of 145 thalers as had been expected. - Kries, *loc. cit.* p. 380.

<sup>2</sup> The persons liable to the tax in 1854 were distributed by classes as follows:

INCOMES VALUED AT	PERSONS
1000-2000 thalers	34,459
2000-4000 "	9,655
4000-9600 "	2,835
9600 thalers and over	773

tax; the equal taxation of the upper classes, which had so long been avoided, had now become an accomplished fact. This form of taxation now appeared to be sufficiently well established and feasible to admit of building up a system of communal supplements [*Kommunalzuschläge*] upon it, which increased in importance more and more as time went on.

Still it is necessary to use all moderation in speaking of the insignificant results of this income tax, as compared with its English prototype, if we are not to judge it too harshly. It was certainly extravagant, at the time the new law was in preparation, to recommend the "only equitable" law as capable of replacing all existing taxes whatsoever, and of affording a revenue of some 30,000,000 thalers; even that gifted and realistic deputy, Bismarck-Schönhausen, had been wrought up into enthusiasm over this tax, but what was to be said of these 2.50 million thalers when it was remembered that at the same time, in Great Britain, with the same rate of 3 per cent. and with the same minimum limit of 1000 thalers, a population but slightly greater paid in a revenue of 38,000,000 thalers; indeed, under the exigencies of the Crimean war both the rate and the aggregate revenue were doubled, and much more than doubled.<sup>1</sup>

§ 317. It was in fact the English example which incited to emulation. Thoughtful people, such as K. G. Kries, who had formerly occupied Hoffmann's standpoint, took their stand on the new income-tax legislation and looked to the future rather than the past. Another man thoroughly familiar with English political institutions, Erwin Nasse, at a slightly later date pointed to this same example as the goal to be striven for in Prussian tax legislation.<sup>2</sup>

It goes without saying that in all this we have not to do with an indiscriminating admiration of English "wealth." This

<sup>1</sup> For the fiscal year 1854-55      10.60 million pounds  
    1855-56                              15                                      "  
    1856-57                              16                                      "  
    1857-58                              11.58                                 "

*Statistical Abstract for the United Kingdom, 1853-1867, p. 5.*

<sup>2</sup> *Bemerkungen über das preussische Steuersystem* (1861), especially pp. 49-61.

point, of superior wealth, was rather regarded as a factor to be eliminated from the problem and so not counted as affecting the result. The point in question, the point which these men insisted on, was quite a different one. It was impossible, said they, that the difference in wealth between the two countries, could be as great as the figures afforded by the income tax would indicate; they insisted that there entered into this result a difference in political morals as well as a difference in pecuniary ability, - that it was a difference in the degree of moral maturity which was revealed in the payment of this tax. It was to be noted that the per capita receipts from the income tax, even in the metropolis of Berlin taken by itself, was much less than the receipts of the English income tax, levied at the same rate and computed per capita of the entire population of Great Britain (1.25 thalers against 1.92 thalers).

In view of our experience with the Prussian income tax for something over a generation past, it seems rather naive for Kries to assure us that not only the members of the commission of valuation, but the taxpayers as well, admitted quite openly in private conversation that it had never yet been possible to assess the tax on the full income of the majority of the taxpayers. But it is also a characteristic fact that many people at that time did not consider the attainment of such a result to be in any way the purpose of the income tax; they were of opinion that the government had good reason to rest content with the undoubted improvements that had been effected, as compared with the earlier state of affairs. It was, in fact, still necessary to combat views of this kind with insistence on the grave injustice of an arrangement under which one person is taxed on his last penny, while the next man pays a tax on less than one-third or one-fourth part of his income.

The reform of the Prussian method of assessment presented itself, even in the earliest beginnings of the income tax, as an urgent question, and on this head, too, the experience of England<sup>1</sup> offered many valuable suggestions.

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<sup>1</sup>While Kries calls special attention to the fiscal results obtained by the English

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The organization of the Prussian mechanism of assessment (the owners of baronial estates with their county chairman [*Landrath*], the inhabitants of the town with their burgomaster, the too far removed and therefore uniformly ineffective higher instance of the department commission with its president appointed by the government had already at the start given evidence that it needed reform, and had continued to do so for more than a generation. The first principle of all self-government is that no one is to be judge of his own case; the organization of self-government must provide that no citizen in the exercise of an office is exposed to the temptation of serving his own private interest while fulfilling a public duty. If anywhere, this is difficult in the case of a tax assessment by the method of self-government, and still the aid of the neighborhood factor cannot be dispensed with; the intimate knowledge of the affairs of the neighborhood which can be made use of in this way is necessary to success, and the fact of local co-operation in the assessment acts to increase the good-will with which the inhabitants of the place pay their tax.

Better provision has been made against these dangers, in many ways, in England than in Prussia. The extent of the assessment district is much greater than that of a Prussian circle, and still not too great; this obviates the dominance of neighborly connivance. The composition of the board of assessment is not dependent on the choice of the taxpayers (the taxpayers might frequently be inclined to choose men from whom they could expect a low assessment). The board of tax commissioners (seven) fills vacancies by co-optation, and traces its historical origin back in unbroken continuity to the land-tax commissioners, who appointed the first income-tax assessment board. The interest of the government is represented by professionally

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method of assessing the tax according to the source of the income, he declares that this method is impracticable under Prussian conditions. He even expresses the opinion that this method of assessment is the chief reason why the income tax has not been successfully established as a permanent constituent of the financial system. The lapse of time has decided this question in a different sense. - Cf. *Zeitschrift für die ges. Staatsw.* (1855). p. 390.

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trained state officials (surveyors) whose district comprises some ten assessment districts (with some 2000 taxpayers); the care of the public interest is not an incidental, *ex-officio* duty to be performed in a medium of agreeable social relations that are by no means to be disturbed. Over these surveyors are placed ten central inspectors. This regulative apparatus of the general tax administration subjects the assessment of the local boards to inspection by experts; it stands in no social relations to the membership of the boards; and with the support of a staff of subordinate officials it independently possesses itself of the facts with regard to incomes in any given locality, in order to report to the board of commissioners any apparent case of too low assessment. It makes such a report simply as state's attorney, while the decision of the case rests with the board, which has by numerous decisions of this class given evidence of the indispensability of the surveyors.

We therefore have here an institution of self-government, and a combination of this institution with the organs of the national administration. The example should be all the more instructive since it occurs in the native land of self-government, and may well serve as a model for the bungling efforts at self-government in our bureaucratic states. To return from this digression, we have found that prevalent opinion in Prussia for a long time countenanced the deficiencies of the income tax administration; for more than a generation it was thought necessary to introduce an intermediate stage between the old class tax and any seriously administered income tax, just as the class tax itself was in its time adopted as a preliminary to any income tax whatever. If the wording of the Act of May 1, 1851, is at pains to say that all "annoying intrusion into matters of property and income" is to be avoided, what was to be expected in the execution of the law? And what prospect of success during the next following decades could there be for any legislative reform based on the conviction that such intrusion was indispensable to an equitable administration of an income tax, even if it were at the same time annoying to the individual taxpayers?

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§ 318. The number of payers and the revenue from the income tax have gradually increased. In 1864 there were 68,111 persons subject to the tax,<sup>1</sup> as compared with 47,750 in 1854; a rapid increase, not equaled by the increase in the aggregate revenue from the tax (3.56 million thalers), It was otherwise with the class tax, the revenue from which increased during the same period about twice as fast as the number of persons taxed (in 1864, 9.63 million thalers was paid by 16.20 million persons).

With the increase of population and the extension of the field of government activity<sup>2</sup> since 1866, the number of persons<sup>3</sup> liable to the income tax has increased:

1876	157,096
1886	207,608

With respect to this increase, of course, it remains an open question whether it is not due to improvement in the assessment, and therefore in the willingness to submit to the payment of the tax, quite as much as it is due to the increase of wealth.

The receipts from the income tax were, in 1876, 29.34 million marks; in 1884, 35.80 million marks (of which one million marks is to be deducted for remissions under the Act of March 26, 1883); and finally, in the estimates for 1889-90, 41.90 million marks. The number of persons liable to the income tax amounts now (1889) to 777,319,<sup>4</sup> in an aggregate population of 28,313,833, that is to say, 2.74 per cent. of the total; it is therefore about twice what it was in 1864 (1.40 per cent.). The revenue derived from the tax has increased during the period 1864-1889 in a still greater ratio (from 10.68 million marks to 41.90 millions = 1 : 3.92).

<sup>1</sup> Bergius, *Finanzwissenschaft*, p. 345.

<sup>2</sup> The number of inhabitants in Prussia was

YEAR	MILLIONS
1864	19.30
1876	25.77 (December 1, 1875)
1886	28.31 ( " 1, 1885)

<sup>3</sup> Adolph Soetbeer, *Vierteljahrschrift für Volkswirtschaft*, 1887-88.

<sup>4</sup> "Estimates of the administration of the direct taxes for the year beginning April 1, 1889," p. 20. - *Anlagen zum Staatshaushaltsetat*, vol. i.



Changes in the law have somewhat affected this result and the bearing of these changes will be discussed presently. The effect of such changes has been especially great in the case of the class tax, which has been gradually lowered by successive enactments, until the receipts, as given in the latest estimates, amount to only 24 million marks; that is to say, 5 million marks less than was derived in 1864 from the same tax on a population amounting to not more than two-thirds of the present total, at the same time that the law did not then apply to the new provinces, whose lower classes are relatively well-to-do.

319. The gradual precession [*Verschiebung*] of the progression in the Prussian class and income tax legislation has already been spoken of in its proper place (sec. 219). In the further development of what was established by Act of May 1, 1851, the reform of May 25, 1873, has been of especial importance.<sup>1</sup>

The views of the men who gave its character to the legislation of 1820 were just as consistently in favor of making the direct tax apply to the lowest classes as they were opposed to the development of the class tax into an income tax. Hoffmann sees in the nominal uniformity of the class tax for higher and lower classes alike an expression of the idea of the dignity of citizenship, as contrasted with conditions under the old régime.<sup>2</sup> This view exerted its influence for half a century after that time, and it shows some vitality even today. Still it appears that this view has had to yield to the force of circumstances, in much the same way as the class tax has been affected by altered times and Opinions.

The Act of May 1, 1851, lops off a fragment from the apex of the class tax; the Act of May 25, 1873, cuts a piece out of the foundation; later enactments have repeatedly done the like; the original structure of the class tax of 1820 and 1851 is set

<sup>1</sup> Adolph Held, *Hildebrand's Jahrbücher*, vol. xx. 1873, pp. 373-389. Cf. F. J. Neumann, *Die progressive Einkommensteuer im Staats- und Gemeindehaushalte* (1874), pp. 156 *et seq.*

<sup>2</sup> *Lehre von den Steuern*, p. 151.

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aside by the Act of 1873; a classified income tax is substituted for it also as applies to the lower classes; but precisely these lower classes are more and more influenced by experience and are continually better inclined to a tax policy which is realistic in form while it is idealistic in theory.

The lowest class of the class tax of 1851 comprised, in the year 1851, approximately 5,000,000 taxpayers, paying an annual tax of one-half thaler. Incident to the collection of every 100 thalers of the tax for this class, 797 special notifications, involving costs, were necessary in the department of Koenigsberg, 689 in the department of Marienwerder; of legal executions there were ordered, in the department of Koenigsberg, 354 for each 100 thalers of receipts; 167 of these executions were fruitless. Backed with such empirical data as these the government, in 1872, submitted to the House of Deputies a memorandum announcing its intention of abolishing this lowest class of the class tax. But the House of Deputies acceded to this proposal only to a very limited extent, in fixing the limit of the class tax for the future at an income of 140 thalers.

Upwards from this minimum there were twelve grades specified by the Act of 1873, the upper limit being 1000 thalers.<sup>1</sup> The rate per cent. varied from about .75 to 2.50 per cent. The income tax was also further developed; the higher classes under this tax were further subdivided, and the upper limit of 7200 thalers (for incomes of 240,000 thalers) was discontinued, the

<sup>1</sup> CLASS	INCOME ( THALERS )	RATE PER TAXPAYER ( THALERS )
1.	140- 220	1
2.	220- 300	2
3.	300- 350	4
4.	350- 400	5
5.	400- 450	6
6.	450- 500	8
7.	500- 550	10
8.	550- 600	12
9.	600- 700	14
10.	700- 800	16
11.	800- 900	20
12.	900-1000	24

rate increasing also beyond that point so that every additional 20,000 thalers of income would pay an additional tax of 600 thalers<sup>1</sup>. In the assessment of persons liable under the first and second classes (1000-1400 thalers) the taxpayer was henceforth to be entitled to some consideration on account of any circumstances that might diminish his ability to pay (a large number of children, poor relations, etc).

At the same time the grist and slaughter tax was abolished (from January 1, 1875, on) and the class tax introduced in its place; only the slaughter tax, and that only for communal purposes, remained optional (requiring a triennial resolution to that effect by the communal officials and a ministerial authorization). By means of the communal supplements [*Gemeindezuschläge*] (under official supervision both the class tax and the grist and slaughter tax had long been made use of for communal purposes. An ordinance dating back as far as April 4, 1848, had assigned to the towns liable to the grist and slaughter tax one-third of the gross receipts from the grist tax, and this had been confirmed by the Act of May 1, 1851. But even as early as 1847<sup>2</sup> the government had submitted to the Federal Diet a memorandum looking to the abolition of this tax and the substitution of an income tax for it; the provisional regulation of April 4, 1848, had sought to accomplish the abolition indirectly. Suggestions to this effect

<sup>1</sup> The fiscal significance of this reform is indicated by the following figures, which are taken from official publications For the year 1886-87. There were altogether twelve taxpayers in Prussia who were obliged to pay a larger tax in consequence of the Act of 1873 than they had paid under the Act of 1851. These twelve now paid 608,400 marks in all, while under the old law they would have paid 259,200 marks The figures are as follows:

TAX PAYERS	INCOMES (MILLION MARKS)	Tax (MARKS)
1	5.04	151,200
1	2.70	81,000
1	2.58	77,400
1	2.28	68,400
2	1.08	32,400
3	1.02	30,600
2	.84	25,200
1	.78	23,400

<sup>2</sup> Von Rönne, *Staatsrecht der preussischen Monarchie*, sec. 535.

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came in repeatedly from the House of Delegates (1850, 1868, 1869). The grist and slaughter tax had (apart from the communal supplements) yielded 4.75 million thalers in 1872. The number of towns liable to this tax had declined in the course of years (in 1820, 132, whereas according to the Act of 1851 there were only 83, and of these 8 additional ones had fallen out by 1872).

§ 320. For several reasons there was some improvement in the class and income tax legislation contained in the Act of 1873, but it was an improvement that was everything but definitive. It was a step in advance which divested the class tax of its obsolete form, abolished the lowest grade of that tax, and further developed the income tax in the higher grades. On the other hand it is to be doubted if the substitution of the class tax for the grist tax was a commendable measure, and it is a matter for serious question if the abolition of the slaughter tax was not simply an outcome of a preference for direct taxation on abstract grounds. In this case, as so frequently happens, the question of the relative taxation of the lower classes was mixed up with the question of the form in which the tax was to be laid; it might have been the proper thing to exempt the Lower classes altogether from the burden laid on them in the form of the grist tax (and slaughter tax; but that would have amounted to an admission that an over-taxation existed in the form of the class tax as the alternative and equivalent of the grist and slaughter tax. But to retain the burden, and simply transmute it into the form of the class tax as that already existed in the greater part of the kingdom, was merely a change of form which could not be justified in face of the experience already had, and which had been reviewed in the memorandum submitted by the government in 1872. This state of affairs led to further reforms which have not even yet reached a definitive conclusion.

An Act<sup>1</sup> was passed July 16, 1880, which, in conjunction with the increase of duties in 1879, had the avowed purpose of chang-

<sup>1</sup> *Conrad's Jahrbücher*, 1884, N. F. vol. viii. pp. 134 *et seq.*

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ing the relative shares borne by direct and by indirect taxes so as to effect a lowering of the direct taxes. The increased receipts from the imperial taxes on consumption were to be made available for lightening the burden of the class and income taxes on the lower and middle classes. This action was fairly contrary to the views which in 1873 had prevailed even among a majority of the Chamber of Deputies. It was decided that the funds made available to Prussia out of the imperial taxes were to be applied towards remission of the monthly rates payable by the several classes under the class tax and by the five lowest classes under the income tax.

On March 10, 1881, a second act was passed which made permanent provision for a remission of three monthly dues payable under the class tax and by the five lower classes under the income tax. And again, during the session of 1882-83, a proposal was submitted by the government which contemplated a still more radical measure. It was proposed that, dating from April 1, 1883, the four lowest grades (420-1200 marks) were to be abolished altogether. In presenting its reasons for the measure the government again cited the experience on which the memorial of 1872 had been based.

By the exemption of these four grades, which comprised 86 per cent. of all persons liable to the class tax, there would have resulted a shortage of 11.70 million marks in the tax receipts. To cover this shortage a tax on the sale of spirituous beverages and on the manufacture of tobacco was to be introduced. As a result partly of disinclination to such a tax, partly of a preference for the class tax on part of the majority of the Chamber of Deputies, the measure proposed by the government was somewhat modified and curtailed. The Act of March 26, 1883, abolished only the two lowest grades of the class tax (420-900 marks) which, it is true, exempted the greater number of those previously liable to the class tax (3742 million = 75 per cent.), as the third and fourth grades comprised only some 619,000 taxpayers. But some further results were also accomplished. All the remaining grades (3-12) of the class tax were henceforth to

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enjoy a remission of three monthly dues; the lowest grade of the income tax (3000-3600 marks), two monthly dues; the second grade of the income tax (3600-4200 marks), one monthly due.

The government had only yielded temporarily to a large adverse majority (four-fifths) of the Chamber of Deputies. At the opening of the next session (1883-84) it introduced a new measure which went much further. It provided in the first place for the exemption of all incomes under 1200 marks, and in the second place for a lowering of the rate on all incomes under 10,000 marks (the rate to increase gradually from 1 to 3 per cent. with the increase of incomes from 1200-10,000 marks. At the same time the relief already afforded to the lower grades, on account of a large number of children and the like, was to be extended also to incomes of 9000 marks and upward. The shortage resulting was to be covered by improvement of the method of assessment, by extending the income tax to joint-stock companies, and, finally, by a progressive tax on dividends in the case of income from dividends amounting to 600 marks and over. The exhaustive discussion which arose over this proposal led to no positive result, and after that time the whole matter remained in abeyance for a number of years. On January 21, 1885, the Minister of Finance declared in the Chamber of Deputies that it was the wish of the government to abolish, not only the third and fourth, but also the fifth and sixth grades of the class tax (1200-1500 marks), but without finding any support among the deputies.

§ 321. Finally, there is a word to be said about the income tax in the cantons of Switzerland.

We have seen (sec. 214) how great has been the growth in those communities of the income and property taxes as compared with other forms of taxation; this has at least been shown so far as concerns the typical canton of Zurich, but there has also been perceptible a general movement in this direction in the other

cantons, showing a decided partiality for this kind of taxes and so contrasting sharply with what was the case at a not very remote period.

Towards the end of the eighteenth century the finances of individual cantons for the most part still bore the impress of the Middle Ages. As in so many other respects, so also in its financial system, the epoch of the Helvetic Republic exerted a radical influence; under the constitution of April 12, 1798, the Republic, by an act of the seventeenth of October, 1798, dealing with imposts<sup>1</sup> introduced, among other things, a property tax amounting to 2 per mille, together with a tax of 2 per cent. on the profits of trade.

The system of taxation adopted by the League contributed not a little to the dissatisfaction with a constitution and legislation that disregarded the results of past historical development. A considerable portion of the Swiss population was stirred to an intense opposition to direct taxes, not having been accustomed to that form of taxation. When the era of the restoration reinstated the old régime in Switzerland and elsewhere, these oppressive taxes were thrown off, together with so much else that the French period had introduced. The fiscal accounts of the canton of Zurich in 1830 showed no trace of a property or an income tax.<sup>2</sup> Not until 1832 was a moderate tax of this kind introduced, as one of the consequences of the Liberal movement. Even in 1847 the receipts from this source amounted to only one-eighth of the aggregate revenue; in Schaffhausen one-twelfth, in Thurgau one-eighth, in the largest canton, Berne; there was no tax of the kind at that time. In the communal finances, on the other hand, a moderate property tax seems to have been in pretty general use by this time. But every glance into the accounts that have come down from that time shows how very sensitive people were with respect to any considerable employment of this tax. What complaints and what discontent would manifest

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<sup>1</sup> I. H. Hottinger, *Der Staatshaushalt der schweizerischen Eidgenossenschaft und ihrer einzelnen Republiken* (1847), p. 5.

<sup>2</sup> Eduard Sulzer, *Die Finanzen des Kantons Zürich, 1832-1850* (Zürich, 1851), p. 22.

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itself everywhere if it were proposed to substitute for the federal import duties a permanent advance of the property tax from one per mine to one and one-half per mille! says the Zurich Director of Finance in 1850. As regards the communal expenditures and the communal property taxes intended to cover them, another writer<sup>1</sup> expressed the opinion that they had already reached their highest development, and that the future ought to bring a reduction.

But it all turned out quite differently during the next generation.

In 1881 a man with 3000 francs of personal income and 60,000 francs property, paid property and income tax to the state and commune in the ten cantonal capitals as follows.<sup>2</sup>

It appears from this that there are still a number of cantons in which this tax is levied for communal purposes only; in others the commune gets at any rate the larger share of the tax: This is also the case in Zurich, where the aggregate amount is an extraordinarily large one. (In particular communes outside of the capital it is even appreciably larger. About one-fourth to one-third of the yearly income from property is demanded for the state (4 per mille) and the commune (7-10 per mille) in the form of a property tax. The commune has as good as no other taxes, and the canton very few. The centre of gravity of the indirect taxation lies continually more decidedly in the federal import duties, in their further development, and in the incipient adoption of other federal taxes on consumption.

<sup>1</sup> Hottinger, p. 147.

<sup>2</sup> *Finanzarchiv*, 1884, p. 60.

CITY	COMMUNAL TAX (FRANCS)	NATIONAL TAX (FRANCS)	TOTAL (FRANCS)
Basle (city)	16.00	80.00	96.00
Liestal (canton Basle)	166.00	.....	166.00
Soleure	172.00	.....	172.00
Aarau	252.00	.....	252.00
Schaffhausen	177.50	94.80	272.30
St. Gall	198.50	82.80	281.30
Glarus	200.10	126.25	326.35
Berne	165.75	165.75	331.50
Lucerne	336.00	.....	336.00
Zurich	359.60	197.30	556.90



§ 322. The development of the Swiss taxes is noteworthy as a counterpart to the development of the income tax in all other states.<sup>1</sup>

As the demands on the state and commune (poor relief, schools, roads, railway subsidies continued irresistibly to increase, there supervened in the Swiss cantons a condition of things in which, on the one hand, the basis for an adequate development of a system of taxes on consumption was lacking (in part a purely administrative shortcoming, while on the other hand, the force of the democratic current, with its favorite views of taxation, was such as to sweep all considerations out of the way. The questions of equity, as well as the questions of expediency, that centred about the increase of the property and income tax during the last generation, were easily answered in a case where circumstances put the shaping of constitutions and laws into the hands of a majority possessed of little or no property.

Characteristic features in this peculiarly Swiss development are, apart from the high rate of the tax absolutely considered, the strong ratio of progression, the marked exemption of small personal incomes, the preponderant taxation of incomes from property (especially for communal purposes as contrasted with personal incomes. But there is also another characteristic feature, which is likewise an outcome of democratic institutions, - which does not stand out in contrast with the arrangements in other states, but is very similar to them. This is the method of assessment. On this head it is to be remarked that democracy has not yet nearly reached the logical result of its method of taxation, that is to say, democracy is still to an extent a civil democracy, and not as yet a social democracy. If it had reached the ultimate stage of its development then its assessment machinery which lies entirely in the hands of the

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<sup>1</sup> The somewhat legendary conceptions that have prevailed on the subject of the property tax in American states and cities have been subjected to a sobering process through Richard T. Ely's *Taxation in American States and Cities* (New York, 1888). Cf. also a paper by the present writer in the *Political Science Quarterly*, vol. iv. March, 1889. On Swiss Taxation cf. Georg Schanz, *Die Steuern der Schweiz* (5 vols., 1890).

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communal officials, in conformity with the principles of democratic self-government, would reflect the same social contrast which is shown in the legislation on the rate and progression of the tax. For the time being, this is not the case; for the time, property relations have not yet been sufficiently differentiated for such a result; the extreme dangers of democracy have so far been staved off by the preponderance of the middle class.

Hence we find an application of the taxation of property and income calculated to show up the dark side of any system of assessment of equals by equals; it has disclosed the existence of such a dark side to an extent that is possible only in a case where the individual and the state are so directly and immediately in contact with one another as here. Among the consequences of this management has been a moderation in demands made by the law, of such a character as to make up for much of the apparent hardship involved in the law; but this has been done in a perverse and inequitable fashion. While this Swiss method of self-government as applied to taxation is very suggestive as compared with the experiences of Prussia, it affords a particularly instructive contrast to the carefully planned method of assessment in use under English self-government.

§ 323. The Swiss taxes on income at and in the sharpest contrast to the great democratic state of France, and its system of taxation.

It has already been remarked in another place that the influence of democratic ideas, even when a favorable ground is afforded by a radical constitution, will work out very different results in a large political and social organism from those seen in small democratic republics, such as those of Switzerland. It is, relatively, such a long and intricate way from the individual to the whole; further, the preponderance of the historical forces which continue to govern the state under any and all changes of constitutional forms, the ascendancy of the proper-

tyed classes, the frequently decisive influence of the capital, - these are breakwaters opposed to the currents of democracy.

There has, of course, been no lack of incitement to the domestication of the income tax in France also i But none of the attempts made have so far led to any result, not even the legitimate result which ought to be attained by this class of tax in a modern system of taxation, still less the extravagant outcome proper to a triumphant radicalism.

In 1848, Goudcheaux, the Minister of Finance, submitted a project to raise 60 million francs by means of a repartitioned income tax, to be distributed upon the departments and communes and levied by communal assessment upon the individual taxpayers. A committee of the national assembly, whose chairman was Parieu, altered this project essentially, especially by introducing certain bureaucratic features in order to perfect the mechanism of assessment,<sup>2</sup> but when Parieu presently succeeded to the Ministry of Finance, he withdrew this project, and substituted another in 1849, which was to tax all incomes at the rate of 1 per cent., the assessment being based on returns made by the taxpayers under the supervision of a communal commission, to consist of the mayor, a citizen selected by the prefect and the comptroller of the direct taxes. This project was also presently withdrawn, Fould having succeeded Parieu in the Ministry of Finance.

Since that time proposals of the same nature have frequently (1855, 1862, 1863, 1871, 1872, and later) been made by various deputies, but the government has invariably opposed the measures from apprehension of the unpopularity of any income tax. With the shifting of the majority of the Chambers over towards the left, the idea has again suggested itself to the ministries that have lately succeeded one another. Gambetta included the income tax in his programme, very much as he did so many other reforms which were intrinsically desirable, but practically

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<sup>1</sup> Paul Leroy-Beaulieu, *Traité de la science des finances*, vol. i. pp. 466-470.

<sup>2</sup> The indispensability of these bureaucratic elements is insisted on by Leroy-Beaulieu, vol. i. 470.

impossible. Very lately (October 30, 1888) the Minister of Finance, Peytral, submitted the draught of a bill i for a general income tax, which has shared the fate of others - being forgotten in the rabid succession of ministries.

The antipathy of the propertied and cultured classes, even of experts, in France; to this tax is yell illustrated by the position of Leroy-Beaulieu. In his *Science des Finances* (1877) he advocates the adoption of the income tax, as an indispensable corrective to other, especially indirect taxes, as being in a peculiar degree calculated to reach the well-to-do and the wealthy classes, but he offers the criticism on Peytral's proposed law, that an income tax would be inequitable in France for the reason that the upper and middle classes already "contribute more than their proportionate share of the public burdens" under the taxes now existing. A further illustration to the same effect is afforded by the fact that while G. de Molinari, the editor of the *Journal des Économistes*, opposes<sup>2</sup> this view of Leroy-Beaulieu's, he offers the very characteristic objection that the upper and middle classes, who, after all, continue to exercise a predominant. influence in the state, are fairly unanimous in rejecting the income tax, and that, moreover, with the country broken up into factions as it is, it would be impossible to find honest assessors.

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<sup>1</sup> Cf. the report and the text of the bill in the *Journal des Économistes*, November 1888, pp. 239 *et seq.* Peytral's report contains a review of similar attempts that have been made since 1848, especially those made under the Third Republic.

<sup>2</sup> *Journal des Économistes*, November, 1888, pp. 309 *et seq.*

## CHAPTER IV. THE TAX SYSTEM.

LITERATURE. Adolph Wagner, *Finanzwissenschaft, Zweiter Theil* (1880); *Allgemeine Steuerlehre, Dritter Hauptabschnitt: Das Steuersystem und die Hauptarten der Steuern*, pp. 362-565. Lorenz von Stein, *Lehrbuch der Finanzwissenschaft* (5<sup>th</sup> ed., 1885), *Zweiter Theil, Erste Abtheilung*, pp. 495-533. Karl von Hock, *Die öffentlichen Abgaben und Schulden* (1863), secs. 4, 13, 14. Fr. J. Neumann, "Schwebende Finanzfragen, Erster Abschnitt: Die Unterscheidung direkter and indirekter Steuern" (*Schmoller's Jahrbuch für Gesetzgebung, Verwaltung und Volkswirtschaft im Deutschen Reich*, vol. i. 1882, pp. 945-976). Fr. J. Neumann, *Die Steuer; Erster Band: Die Steuer und das öffentliche Interesse, eine Untersuchung über das Wesen der Steuer und die Gliederung der Staats- und Gemeinde-Einnahmen* (1887). Albert Schaeffle, *Die Grundsätze der Steuerpolitik and die schwebenden Finanzfragen Deutschlands und Oesterreichs* (1880), pp. 51-198.

### I. CONSPECTUS OF THE VARIOUS KINDS OF TAXES.

§ 324. A conspectus of the various kinds of taxes might be most simply and easily effected by means of an historical survey in which it is attempted to arrange the main facts of taxation in an orderly manner by groups, provided only that the historical material were of a nature to lend itself to this treatment by showing an orderly gradation of development from one kind of taxation to another. It would then be possible to trace some sort of necessary connection between certain stages of political development and certain forms of taxation, and to show that in accordance with well-known conceptions of the evolution of political, juridical and economic institutions, a gradual progress in forms of taxation has gone hand in hand with the gradual development of the state.

It is not only true that in the earlier treatment of tax systems a lively sense of the desirability of such a generalization

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has been present; the promptings of this sense have been heeded, with the result that the existence of such a parallelism of progress has been asserted, and a simple and perspicuous scheme of historical development has been constructed. The favorite attempt in this direction was the predication of a progress from the stage of indirect taxation to that of direct taxation, which was claimed to go hand in hand with a development from an absolute to a liberal constitution.

This position is right, not only with regard to the general claim that there is a progress of development in the form of taxation and that this development is connected with the general development of political and social life; it is also right in assuming that a transition from indirect taxes to direct taxes follows as a result of certain general features of the political and social development. But it falls short through the superficiality which hermits itself to overlook the complex of relations and circumstances that condition any such progressive development; it also falls short in that it sets up this generalization as a convenient and adequate programme to be immediately applied in tax legislation. For the purposes of such a conspectus of the leading facts of taxation it is of little use to point out such a general tendency, so long as the realization of this tendency lies in the distant future, and so long as there is a great number of taxes that are for the present indispensable, but for whose orderly classification the fact of this general tendency is of slight or no significance.

On this head, as on so many others, the science in its maturer and more thoughtful days has arrived at conditional and qualified conclusions in cases where the youthful science thought itself to have discovered simple and sweeping laws.

§ 325. As the result of the historical exposition contained in the last chapter we have reached a generalization of the history of taxation for a thousand years past which may be summed up in two propositions: (1) there has taken place a process of clarification whereby the taxes, being recognized as a necessary compensation of the public administration, have come to be

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segregated out from other state activities directed to other ends than that of raising taxes; (2) we have an aggregation of experiences with the various kinds of taxation, which is calculated to bring us to a modest appreciation of the fact that our modern practical sagacity in matters of taxation is very old.

The process of clarification is visible in this, that the taxes have developed out of the position of a temporary and extraordinary effort on part of the members of the state to the position of an unquestionable public necessity; it appears also in this, that tolls, stamp dues and monopolies, in consequence of a full consciousness of this necessity; have ceased to be privileges of a quasi-private character and have taken on the character of contributions rendered by the body of citizens under the forms of public law. But what this process of clarification affords us in the way of positive data accumulated, by this long historical experience is a great number of means and appliances for the realization of the purpose of taxation, and these numerous ways and means are yet waiting to be intelligently classified according to their relative importance. This orderly classification is not to be drawn immediately and directly from the history of the past, but must be reached by means of a critical review of the historical material. For just as in our everyday life it is the part of an intelligent being to make use of the experiences of past days only as a guide to the realization of a rational plan of life, aiming at the accomplishment of what ought to be, and so continually improving upon the past, in like manner it is the office of the science within the field of human social life to make use of, the experiences of the past as a guide for the efforts of the future. To avoid this duty, the science would have to show that historical events succeed each other without the intervention of reflection, and would have to persuade us that they ought to succeed each other in this way.

§ 326. The Physiocratic doctrine has given evidence of its incisive scientific character also in this, that it subjected the complex variety of taxes handed down from the vast to a systematic

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criticism, a criticism which brought order into the matter at a single stroke in such a way that the classification of the taxes at the same time embodied a decision as to their expediency and justice.

In point of form this was a solution of the problem. The deficiencies of the solution lay in the substance of the theory of taxation, in the bold conception of productivity and of the tax source resulting from it; its deficiencies lay in a rationalistic disregard of the results of historical growth, and in the habit of mind which, according to the fashion of that time, saw nothing but confusion in the tax systems of the past, instead of finding in them material for a thoughtful analysis and discussion.

If we should ever succeed in constructing an orderly scheme of taxation based on an enlightened appreciation of the nature of the tax and of the tax source, and at the same time in organic connection with the past development of taxation, the goal would have been reached.

For the present there is but slight prospect of such a consummation. All attempts that have been made since the time of these earliest systematic writers have departed from their simple scheme of tax classification in the same measure as they have acquired a more adequate knowledge of facts. Very instructive in this connection is the fortune experienced by the Physiocratic terminology of "direct" and "indirect" taxes.

In contrast with every other of the manifold significations which these terms have assumed since their time, to the Physiocrats the antithesis of the direct tax to the indirect taxes was at the same time, and above all, a decision as to the proper structure of the tax system. The direct tax was the only admissible kind of tax, because it falls immediately upon the tax source; all other kinds of taxes are called indirect because they are levied on a tax object which is not identical with the tax source, and are, therefore, objectionable forms of taxation.<sup>1</sup>

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<sup>1</sup>"La forme essentielle de l'impôt consiste à prendre directement l'impôt ou il est, et à ne pas vouloir le prendre où il n'est pas ... les fonds qui appartiennent à l'impôt ne peuvent se trouver que dans les mains, des propriétaires fonciers. ... Changer cette forme directe de l'établissement de l'impôt pour lui donner une forme indirecte, c'est renverser un ordre naturel dont on ne se peut s'écarter sans les plus



§ 327. The radical precision and simplicity of the Physiocratic theory of taxation is like the other efforts of this earliest scientific school in its boldness of conception; it was a conception that has been fruitful in the later development of the science, but fruitful after the manner of the seed corn, whose substance dissolves to reappear in structures of a different character. It is true of Adam Smith's theory of taxation, which influenced science and practice for several generations, that, as is the case with so much else in Adam Smith's work, it bears the traces of this writer's great indebtedness to the French school. If we compare Smith with James Steuart<sup>1</sup> it immediately becomes apparent that the former's theory of taxation has passed through the Physiocratic school, that of the latter not. But as so frequently happens in Smith, as a consequence of the relative independence with which he constructs his own theory, the rigorous logic and adherence to the requirements of the system, characteristic of the French school, have disappeared. The net product upon which the Physiocrats focused their tax system by means of the single direct tax, resolves itself in Smith's hands<sup>2</sup> into three kinds of income, Rent, Profits, and Wages. He prefaces his discussion with four briefly stated rules of taxation, somewhat illogically arranged, but of practical value, and repeated with great frequency; and by these rules he tests the tax contrivances of the past, and by so doing shows his superiority over the abstract radicalism of his French contemporaries.

There is no longer any talk of a "system" of taxation. The distinction between direct and indirect taxes disappears in Smith's discussion. It is of course true that the locution introduced by the Physiocrats recurs both in the science and in practical life, and that it had a great vogue, but the emotional content of the

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grands inconvénients." Mercier de la Rivière, *L'ordre naturel et essentiel des sociétés politiques*, chap. iv. (*Physiocrates*, éd. Daire, 1846, p. 474). He goes on to say: "La forme de l'impôt est indirecte lorsqu'il est établi ou sur les personnes mêmes ou sur les choses commerçables; dans l'un et l'autre cas, les préjudices qu'il cause au souverain et à la nation, sont énormes."

<sup>1</sup> *Inquiry into the Principles of Political Economy* (1767).

<sup>2</sup> *Wealth of Nations*, bk. v. chap. ii. part ii.

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concept disappeared. A distant follower of the Physiocrats, Theodor Schmalz, utters a note of warning in the beginning of the nineteenth century against the "customary division of taxes into direct and indirect"; these expressions could have a definite meaning only if by direct are meant those taxes which are levied immediately upon the productions of nature, and by indirect all others, because they also finally fall upon natural products, but only indirectly and by a very circuitous path.<sup>1</sup> But this theory has long ceased to be anything more than the mistake of an obsolete school of thought. The classification of taxes as direct and indirect is no longer a question as to the remoteness of the tax object from the tax source, but simply a question regarding different kinds of tax objects; it is a question of the technique of taxation.<sup>2</sup>

§ 328. Of the many attempts at defining the terms in this latter sense it will be possible here to cite only a few of the more noted ones, which have gained a wider acceptance than others.

The view already spoken of above (sec. 246), which is probably the most widely accepted in the usage of practical life, is the one which is represented in the science by K. H. Rau and later by Adolph Wagner. If the demand, says Rau, is made immediately on the persons whom it is desired to tax, then the tax in question is levied without mediation and is a direct tax; the person who pays the tax is, in this case, also the person who bears the burden of the tax. If, on the other hand, the taxes are demanded of persons whom the government does not intend should bear the tax themselves, but who are expected to recoup themselves from the persons whom it is desired to tax, then the tax is mediate, advanced or indirect. But as this "distinction between direct and indirect collection is an external distinction," Rau prefers the distinction between Assessments and Expenditure Taxes. "Assessments" have to do with the person on whom

<sup>1</sup> *Handbuch der Staatswirtschaft* (1808), sec. 410.

<sup>2</sup> Taxes, says Rau, may also be classified according to the method pursued in obtaining the payment from the citizens liable to the tax; this method may be simple and direct, or it may be roundabout. *Finanzwissenschaft*, sec. 293.

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is imposed year by year an obligation to pay a certain tax; whereas the "expenditure tax" is based on the outlay of the taxpayer, as indicating the amount of his property. Assessments are for the most part, though not always, levied directly, expenditure taxes for the most part indirectly.

While Rau, very significantly, is not satisfied with the classification of taxes as direct and indirect, and so sets it aside as "extrinsic" in favor of the other classification, into assessments and expenditure taxes, J. G. Hoffmann<sup>1</sup> is concerned to bring the usage of practical life into consonance with the requirements of scientific thought. The separation of the totality of taxes into direct and indirect, says Hoffmann, is familiar to everyone, and most people understand the terms in approximately the same sense, although there is usually a great lack of clearness and precision; the etymological derivation of the word would indicate that those taxes are to be called direct which are borne by the person who pays them; whereas those are indirect which in the intention of the tax officials are advanced by some one else on behalf of the persons by whom they are ultimately to be borne; but in most cases it is quite impossible to say who really bears a given tax, and it is to be added that, if the word be taken in the sense specified, the same tax will be indirect or direct according as a merchant or the actual consumer imports the goods on which the tax is levied. It is therefore necessary to find a profounder definition of the concept, and such a definition Hoffmann finds in the distinction that direct taxes are taxes levied on possession, while indirect taxes are taxes levied on transactions - a distinction which is at the same time of practical value, inasmuch as this distinguishing characteristic points to the necessity of a very different treatment of the two kinds of taxes; it requires a different apparatus to collect taxes on possessions from what is adapted to collect taxes on transactions; possession being more or less permanent, while a transaction is by nature transient.<sup>2</sup>

<sup>1</sup> *Preussische Staatszeitung*, 1829, No. 304. *Die Lehre von den Steuern* (1840), pp. 66-73.

<sup>2</sup> Somewhat similar is the distinction made by J. B. Say (*Cours complet d'économie politique pratique*, 1829, vol. vi. p. 68) between direct and indirect taxes; at least such

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§ 329. It is a matter of repeated experience in the political sciences that the efforts to establish harmony between colloquial usage and the notions of the science attain their end but very slowly. To begin with, agreement between the individual men of the science is reached with difficulty. And then, colloquial usage is very apt to be guided by the momentum of established habits. The case in hand, however, is a somewhat unusual one; the usage in question originated with a theory which has had no practical application and was thereupon presently supplanted in colloquial usage by a quite different signification (according to Hoffmann's view of the etymology, and now this latter colloquial usage is also incapable of reaching a stable and satisfactory definition because it will not stand the test of a closer analysis. Improved definitions, as this of Hoffmann's, also labor under the difficulty that they are, in the first place, in conflict with the usage of practical life (of legislation, of the administration, etc.), and in the second place, they are themselves open to criticism. So we find that, on the one hand, logicians, such as J. S. Mill<sup>1</sup> and Adolph Wagner,<sup>2</sup> have gone back to that meaning which the word has in colloquial usage, while on the other hand, Leroy Beaulieu<sup>3</sup> (as contrasted with Parieu<sup>4</sup> and other French writers on finance, dissatisfied with the current explanations, returns, consciously. or unconsciously, to the sense which the Physiocrats attached to the term, but without returning to their ideals. The definition (closely. related to that of Hoffmann) which has gained

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is its sense, although it is very clumsily formulated: "Ou bien on demande directement au contribuable une somme que certaines indications font supposer qu'il est en état de payer, comme dans le cas où il est taxé en raison de la propriété foncière ... soit en raison de la grandeur du logement ...; ou bien on le taxe en raison de la marchandise qui est l'objet de son travail ou qu'il veut consommer ou qu'il fait transporter d'un lieu dans un autre."

<sup>1</sup> *Principles of Political Economy*, book v, chap. iii.: "A direct tax is one which is demanded from the very person who, it is intended or desired, should pay it; indirect taxes are those which are demanded from one person in the expectation and intention that he shall indemnify himself at the expense of another."

<sup>2</sup> *Finanzwissenschaft*, vol. ii. secs. 338, 388.

<sup>3</sup> *Traité de la science des finances*, vol. i. p. 214.

<sup>4</sup> *Traité des Impôts* (1866), vol. i. p. 9.

acceptance in the official language<sup>1</sup> of France he dubs "empirical"; it lumps things together which should be kept distinct. For example, it includes taxes on inheritances and donations under indirect taxes, for the reason that these taxes are levied on occasion of a particular isolated act. If a more scientific definition were desired, he would suggest the following: By the direct tax it is the legislator's aim to reach the actual payer of the tax, and to tax him in proportion to his property and his ability to pay; he therefore suppresses every intermediate link between the taxpayer and the treasury and seeks to make the tax strictly proportional to the property and the tax-paying capacity. By the indirect tax, on the other hand, the legislator seeks to reach the actual taxpayer only by a sort of repercussion (*par ricochet*) instead of going directly to the end to be attained; he relinquishes the idea of a strict proportionality, and contents himself with an approximation.

§ 330. There has been, latterly, a considerable writing of monographs with a view to bring order into the inconsistency of these conceptions, the results of which, it is true, have scarcely been proportional to the efforts put forth. It can therefore not be in place to take up the question here anew. But it may be in place to call attention to whatever fundamental element is common to all these diverse definitions, and to what is of vital importance to the economy of the tax system.

Common to all the definitions, and at the same time of practical value, is the contrast between the flexibility, imperceptibility and relative voluntariness of the indirect taxes, and the inflexibility, publicity and harsh imperativeness of the direct taxes. This contrast, quite independently of all varying definitions, is forever present in the historical development of taxation; it results in or is the result of the more general contrast of a realistic

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<sup>1</sup> This definition reads: Les impôts directs portent immédiatement sur les personnes, sur la possession ou la jouissance de la richesse; - les impôts indirects sont perçus à l'occasion d'un fait, d'un acte, d'un échange. "Telle est la définition administrative," adds Leroy-Beaulieu; it is therefore the authoritative definition, binding in administrative law.

or idealistic character in the different historical phases of taxation, abstract idealism, in its earliest scientific form and at the height of its ascendancy, rejects indirect taxes unconditionally. Theoretical writers who hold closer to the facts of everyday life are as a rule apt to appreciate the realistic value of indirect taxes.

Justi<sup>1</sup> puts it forward as a fundamental principle, applicable to all contributions, taxes and imposts, that, as far as possible, ways and means should be found and adopted, such as will lead the subjects to make the payment willingly and readily and, as it were, on their own motion; for just as undeniable as is the duty of the subject to pay taxes, just so undeniable is the annoyance and hardship which most men find in the payment of taxes. James Steuart<sup>2</sup> finds (as so many others have done since his time), in direct contradiction to his contemporaries, the Physiocrats, that taxes on necessary articles of consumption should commend themselves to producers precisely for this reason, that such taxes are repaid to them in the price of the product. Adam Smith incorporates in his rules of taxation<sup>3</sup> (extolled as "classic" by J. S. Mill) the requirement that taxes should be levied in the manner most likely to be convenient to the contributor, and he counts as especially conforming to this requirement consumption taxes levied on superfluities in such a manner that the contributor pays them in small installments and, moreover, pays them voluntarily, seeing that the articles taxed are not necessities of life, it being therefore his own fault if such taxes become oppressive.

"The secret of finance is to take without causing discomfort,"

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<sup>1</sup> *Staatswirtschaft*, vol. ii, p. 290.

<sup>2</sup> *Principles of Political Economy*, book v, chap. iii.

<sup>3</sup> 1. The subjects of every state ought to contribute to the support of the government as nearly as possible in proportion to their respective abilities. 2. The tax which each individual is bound to pay ought to be certain and not arbitrary. The time of payment, the manner of payment, the quantity to be paid, ought all to be clear and plain to the contributor and to every other person. 3. Every tax ought to be levied at the time, or in the manner, in which it is most likely to be convenient for the contributor to pay it. 4. Every tax ought to be so contrived as both to take out and to keep out of the pockets of the people as little as possible over and above what it brings into the public treasury of the state. - *Wealth of Nations*, book v. chap. ii.

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says J. G. Hoffmann in the *Promemoria* drawn up by him for the purposes of the Prussian tax legislation of February 20, 1820;<sup>1</sup> and in his *Lehre von den Steuern*,<sup>2</sup> Hoffmann says that taxes on transactions bear less heavily on the taxpayer than taxes on possessions, for the reason that the extent to which the taxpayer is subject to them always depends somewhat on his own choice.

From this valuation of *indirect* taxes in the old Cameralistic science and in the school of Adam Smith, the contrary estimate of the value of direct taxes follows as a matter of course.

§ 331. It is quite obvious that the distinction between direct and indirect taxes could no longer satisfy the student after it had yielded its most valuable and suggestive results and had been reduced to a simple technical distinction in financial terminology, as it has been for a hundred years past. In order to accomplish, for the purposes of a more highly developed stage of economic thought and a maturer view of the history of finance, something analogous to what the Physiocrats once achieved at a single bold stroke, it would be necessary to follow their example in placing all existing kinds of taxes in intimate connection with the sources and the purposes of taxation. The purpose to be accomplished was at that time a systematic classification of historical data, in order to prepare the way for a reform of the existing taxation.

The task before the later generation was a harder one. While taking their stand on the historical development of taxation in the past, they were required to work out a system which should exhibit the reasonable nature of this past development and at the same time exert a salutary influence on the course of taxation in the future. Their task was a harder one than that of the Physiocrats, insomuch as the latter threw overboard everything handed down from the past, and looked for no rationality in existing institutions.

Our past discussions of the ideal of a single tax (secs. 251-254) have already so far converted us into advocates of the

<sup>1</sup> Dieterici, p. 284.

<sup>2</sup> p. 67.

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historic tax systems as to have shown us the decisive arguments in favor of a plurality of taxes, both on grounds of equity and of expediency.

The particulars as to what kinds of taxes are to be adopted, and why, remain yet to be discussed. History affords us the data for answering these questions, but not the complete answer. We are thoroughly aware that these data show a progress, but we are also aware that the progress has never been so rapid as since the beginnings of a conscious reflection on these questions, - a science of taxes and scientific systems of taxation.

What were the motive forces in the reforms effected in the Prussian tax system which we have reviewed, in the reforms at the beginning and during the course of the nineteenth century? Among the very foremost (in this as in other fields of economic life was the influence exerted by the French-English theory upon the brains of our leading statesmen. It is only as a secondary factor that we can here cite the influence of historical facts; their share in the movement was more frequently that of a drag on the new concepts reached by the science, and resulted in a sort of compromise which presently yielded again to the influence of the theory.

Keeping in mind these experiences it must be said that the science would be ingloriously renouncing its historic office if it were to do honor to the poorer of the scientific schools of the past as exemplified in the established institutions handed down from the past, and at the same time decline to do its duty for the present and the future by saying what line of action is to be followed.

§ 332. Our systematic classification of taxes starts from the premise that incomes, and in exceptional cases, property, constitute the tax source from which any and every kind of taxes are drawn (sees. 236-244).

The distinction to be made in respect of all taxes, therefore, will depend on the relation in which the tax object stands to these tax sources.



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The numerous economic phenomena to which all taxes hitherto levied attach, will, with respect to the above-mentioned relation, group themselves under three heads: (1) those which show us the income (or property in its genesis; (2) those which show it in its finished (or achieved form; (3) such as show it in its expenditure for private consumption. Hence we have the three chief classes of taxes: taxes on Earnings [*Erwerb*], taxes on Possession, and taxes on Consumption.<sup>1</sup>

A more detailed examination of these three general classes is necessary in order to an appreciation of the peculiar office of each class, and of each particular kind of tax belonging under one or the other class. By this means we shall come to understand the necessity of their mutually supplementing one another in the completed structure of the tax system.

The historic evolution will thus come to its rights, in that the materials afforded by past forms of taxation will be assimilated into the system; while at the same time room will be afforded for scientific criticism, in the opportunity offered for sifting the historical material, and so preparing the way for further progress in taxation.

§ 333. Before proceeding to this detailed examination it may be proper to consider briefly the "classic" rules of taxation of Adam Smith.

These rules are a typical example of the "principles" which for a hundred years were so much in vogue in the school of Adam Smith, and before his time in the German Cameralistic science, and not least in the crossing of Justi and Smith, together with its hybrid progeny, down to Rau and Roscher.

A few maxims of prudence, so drawn, if possible, as to admit of being immediately adopted in practice, while they are themselves but a generalization from everyday practice, and arranged and numbered with the greatest care; interspersed among these

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<sup>1</sup>Wagner, *Finanzwissenschaft*, sec. 451 (vol. ii. *Allgemeine Steuerlehre*, p. 410). I adopt Wagner's classification as above given, with the thought that it may serve the purpose of bringing uniformity and agreement into the systematic treatment of taxation.

and in the same series with them, embryonic indications of the presence of important questions of principle, the passing, superficial reference to which contrasts most significantly and curiously with the gravity with which the maxims of everyday expediency are expounded.

The first of Adam Smith's rules of taxation is a rudimentary statement of principle, which does not belong with the three rules following it. It is concerned with the questions dealt with in the first chapter of the present book, "Equity in Taxation," which were in part also treated of in Book I. Chapter III., on "The Various Binds of Public Contributions." It is quite characteristic that in this first rule Smith follows up the proposition "The subjects of every state ought to contribute to the support of the government in proportion to their respective abilities," with this second proposition: "The expense of government to the individuals of a great nation, is like the expense of management to the joint tenants of great estate, who are all obliged to contribute in proportion to their respective interests in the estate."

The ground is shifted to quite a different category when to this first principle is added a second one which prescribes that "The tax which each individual is bound to pay ought to be certain, and not arbitrary," and that "The time of payment, the manner of payment, the quantity to be paid, ought all to be clear and plain," since "where it is otherwise, every person subject to the tax is more or less in the power of the tax-gatherer," etc. We have here to do with a point in the struggle between the constitutional state [*Rechtsstaat*] and the earlier police state, a question which is no longer a question in the modern state, and like so much else in the writings of Adam Smith and his contemporaries, is to be taken retrospectively.

The third rule, as also the fourth, recites certain considerations of expediency which are no more exhaustive than they are well arranged. In the third rule stress is laid on the proper choice of the tax period and on the convenience to the taxpayer of the quasi-voluntary taxes on consumption; in enforcement of the maxim that "Every tax ought to be levied at the time, or in

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the manner, in which it is most likely to be convenient for the contributor to pay it." In the fourth rule the principle is inculcated that "Every tax ought to be so contrived as to both take out and to keep out of the pockets of the people as little as possible, over and above what it brings into the public treasury of the state." This principle is expounded somewhat in detail, divers causes being cited from which undesirable expenses would result, and among these are the cost of collection, the disturbance to industry, penalties for fraud and annoying interference by the tax officials.

The truth contained in these two rules is vitiated by being mixed up with opinions which are altogether peculiar to the times of Adam Smith, so that not even within the narrow field of prudential maxims do these rules merit the epithet "classic" which is applied by Mill, unless we use the term classic to designate whatever has been repeated an infinite number of times, often without an appreciation of its meaning. Such is the following reflection on smuggling: "The law, contrary to all the ordinary principles of justice, first creates the temptation, and then punishes those who yield to it; and it commonly enhances the punishment too in proportion to the very circumstance which ought certainly to alleviate it, the temptation to commit the crime." Here, as in other propositions contained in these rules of taxation, we have an expression of the individualism of the eighteenth century, which rises against the state instead of appreciating the great necessity of its presence.

What there is left of positive content in these rules is accordingly reduced to a collection of simple considerations of common sense, such as would find their place as a matter of course in a discussion of the different classes of taxes; whereas, such matters as the historical estimate of direct and of indirect taxes demand other treatment than they receive in the modest position awarded them by Smith under his third rule.

## II. THE TAXATION OF EARNINGS.

§ 334. Reasons of equity as well as of expediency have led to the construction of a system of taxation out of many and diverse

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constituent elements; these constituent elements are classed under three general heads. The same reasons have brought it about that each of these groups also is a similar systematic structure. In the first place, each particular kind of tax taken by itself is so far inadequate as to leave gaps that have to be filled by other taxes, and in the second place, particular forms of gain, possession or consumption stand in such a peculiar relation of indebtedness to certain public institutions as to require special payments.

For reasons of this kind the general group of taxes on earnings is subdivided into Subjective Taxes, Objective Taxes, and Taxes on Business.

The two former classes have this in common, that they are levied on a regularly recurring gain, on yearly proceeds, yearly receipts, whereas the third class, the taxes on business, are levied in individual transactions of exchange. Subjective and objective taxes are distinguished from one another by the fact that the former strike the gain only after it makes its appearance as an item of income at the disposition of the taxable person; whereas the latter, the objective taxes, fall upon the gain-yielding material goods from which the income of the person is derived.

The subjective taxes are undeniably the most perfect form of taxation, so far as concerns the purpose of enforcing the public obligations of the person.<sup>1</sup> It is to be added that this relative per-

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<sup>1</sup> The realistic sense of modern statesmen is for the most part not inclined to acknowledge this fact, not even in England. Gladstone once (*Speech on the Budget*, April 15, 1861) compared direct and indirect taxes to two charming sisters, the one blonde the other brunette, the one more frank and outspoken, the other inclined to be shy and retiring, but more winning; as Member of the House, and more particularly as Chancellor of the Exchequer, he had always considered it his duty to pay his respects to both. He held it to be a great mistake to think that it had been the occupation of Parliament for the last twenty years to destroy the indirect taxes; the tree had only been pruned in order to let the trunk grow all the more vigorously, with the consequence that the indirect taxes were now of more consequence and more productive than at any previous period of English history. At the same time it was a disagreeable fact that the income tax now amounted to ten pence in the pound (a trifle over four per cent.); he found this high, and would gladly be the man to abolish it. (*Financial Statements* by W. W. Gladstone, 2<sup>d</sup> ed. 1864, p. 241). It is however to be added that the same Gladstone, in his speech on the Budget, April, 1861, says that he knows of no tax by which the large incomes of the country may be reached as effectively as by the income tax (*ibid.* p. 516).

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fection is accompanied by practical difficulties in the way of bringing them to a full development. From these practical difficulties it results that these taxes are developed in a graduated series (capitation taxes, household taxes, class taxes, classified income taxes, income taxes proper, low income taxes, high income taxes) in which the idea of the subjective tax develops gradually from a minute germ into full bloom. There are difficulties connected with this gradual development such as to lead to the employment, by preference, of less perfect, but for that reason more available forms of taxation. Such, for example, are the other taxes on gains, which afford a more convenient means of taxation in being levied on easily accessible tax objects (dividends, transactions); such are also taxes on consumption, which are levied on obvious manifestations of tax-paying capacity in the form of the taxpayer's consumption of goods. But in addition to the difficulties in the way of an adequate development of the subjective taxes there is also the intrinsic difficulty that they leave uncovered gaps which require other kinds of taxes to cover them. One important failure of this kind on part of subjective taxes lies in the fact that they are too inflexible, too one-sided to serve as an exclusive measure of tax-paying capacity; only the active employment of the earnings in serving the demands of the household can lend this measure of tax-paying capacity the requisite flexibility. Another inherent shortcoming lies in the necessary inability of the subjective tax to meet the requirements of the objective liability; to meet which the objective taxes have been adopted.

The strength of objective taxes lies in this, that they are well adapted to fill up the gaps left by any subjective taxation, and that they can attach to tangible and easily accessible objects without prying into the more intimate relation existing between these tax objects and the aggregate income of the person taxed. But apart from these reasons in its favor objective taxes have also their undesirable features. If they are to be taken as a sufficient measure of tax-paying capacity, then instead of the praise bestowed by the Physiocratic school (that this class of taxes attach to

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obvious facts and are not arbitrary, as every personal tax is),<sup>1</sup> they are met by the impatient declaration of the science that "*die todte Sache kann nicht steuern, sondern nur der lebende Mensch.*"<sup>2</sup> As soon as the attempt is made to reach profit-yielding objects which are not pre-eminently conspicuous, such as a trade, securities and the like, the practical advantage attaching to objective taxes immediately disappears; the difficulties of administration become as great as the corresponding difficulties in the case of the subjective taxes.

As regards taxes on business, they have with good reason been wont to disguise themselves during their early development under the semblance of payment for a service rendered. They possess this advantage, that they reach a great variety of visible events; the disadvantage attaching to them lies in the fact that these events or transactions afford a much less reliable indication of tax-paying capacity than do the income-yielding objects - apart from a single class of events (not included under taxes on business by Wagner, for example) viz., inheritances, donations and the like. Unless they are used with moderation, therefore, they will result in great inequalities, such as only long habituation can render bearable.

§ 335. The early stages in the development of subjective taxation are characterized by a lack of clearness in its relation to objective taxes; there is even a pronounced tendency towards a transformation of subjective taxes into objective taxes (taxes on realty), which is to be taken partly as an expression of the absence of a developed idea of the different character of the two classes of taxes, partly as expressing the urgent need of definiteness and tangibility of the tax requirements under an undeveloped system of taxation; as a protection against arbitrary and defective assessment.

The difficulties in the way of subjective taxation are also somewhat lessened by the gradual character of the historical

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<sup>1</sup> L'impôt sur les personnes est nécessairement un impôt arbitraire, destructif par conséquent du droit de propriété .... Car tout ce qui n'a rien d'évident est arbitraire. - Mercier de la Rivière, *L'ordre naturel*, chap. iv.

<sup>2</sup> J. G. Hoffmann, *Lehre von den Steuern*, p. 106.

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development; at the outset the structures are quite embryonic, and are then succeeded by slightly higher developed stages, presently to be followed by a still higher development, - the evolution going hand in hand with the progress of development in state and society. It is a very significant fact that after the subjective taxes of earlier centuries had long since assumed the character of objective taxes, the Prussian tax system of the nineteenth century began this course of evolution over again, starting with the capitation tax [*Kopfsteuer*], which was at that time literally what financial science in modern times understands by the term, whereas in the tax system of the times of the Great Elector, even, the tax levied under this name had assumed the character of a progressive income tax, by no means levied on a capitation basis alone. But every capitation tax (in the strict sense) tends, in any progressive society, to a broader development. It is only under primitive conditions, under a régime of relatively stable economic conditions and a primitive uniformity and equality in respect of acquisition and possession of wealth that a capitation tax answers to the requirements of justice. As the social differentiation progresses this kind of taxation must decline in importance, relative or absolute. It declines in relative importance in case other taxes, better adapted to that end, are introduced for the purpose of graduating the tax in proportion to the diverse degrees of tax-paying capacity possessed by individual households. It declines in importance absolutely in case other forms of taxation are found to be better adapted than the capitation tax for the collection of its due contingent from each household liable to the tax obligation. It declines, nominally and apparently, in all cases, because even where it is retained in point of fact it is brought in under the more comprehensive head of a class or income tax.

In Prussia it was only during the short experimental epoch of the tax-reform period that any attempt was made to adopt a capitation tax in the strict sense (1811-1820). The next higher stage, of the class tax, was reached very shortly. The latter

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embodies the compromise effected by the earlier liberalism, and contains the contradiction between an abstract enthusiasm for direct taxes and the empirical difficulties of an exact assessment of incomes. During this period of liberalistic enthusiasm there was, in the first place, an aspiration to do honor to the personal tax as the most perfect form of taxation, as being in a special degree an expression of the awakened consciousness of the identity of the people and the state; but in the second place, experience and the doctrines of Adam Smith effectively combine to discountenance the carrying out of this view to its logical consequences. A tax which does not resort to that class of demands that make the income tax seem insufferable to an immature sense of citizenship, which contents itself with conspicuous external indications of wealth instead of resorting to an annoying intrusion into the private concerns of the individual, is an obvious measure of compromise. As the evidence afforded by palpable facts was accepted as a substitute for an appraisalment of a person's pecuniary condition in the administration of the French system of objective taxes of that era, similarly with us the readily ascertainable fact of social position was made use of for the same purpose.

But this expedient, too, is nothing more than a beginning which tends constantly to further development as the evolution of life goes on, and tends therefore to break up and disappear.

Even the social stratification which the class-tax system takes as its point of departure, everywhere contains intermediate layers between the strata and layers pitched on for the purpose of the tax, and these intermediate layers have also to be taken account of; hence arises the necessity for what is sought to be avoided bar the class tax, viz., the valuation of individual tax-paying capacities within the same stratum. And what is of still greater consequence, the economic development of the nineteenth century has, in a very brief space of time, utterly confounded the typical social strata which have come down by tradition from previous centuries. In all this later process of fermentation there is a single indication of pecuniary ability coming ever more



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strongly into the foreground and displacing all traditional distinctions and indications; this is the amount of money which each household acquires. But this indication is not a very conspicuous one; it has to be ascertained, and that by the adoption of measures before which the era that breeds the class tax recoils. A survey of a very short period suffices to establish the necessity of the consequences indicated.

The income tax makes its *début* in a very instructive relation to the renewed aggression of liberalism in the constitutional development of Prussia about the middle of the nineteenth century.

§ 336. But even at that time all that was achieved was a transitional measure (1851-1873).

The class tax was retained in substance for the great majority of the population, being modified only in certain details. It is based on the old stratification of society, quite after the fashion of a generation earlier. A decided alteration is made only as concerns those classes of society which possess an income of one thousand thalers and upwards. As affects these classes, the requirements of equity and the awakened public sentiment with regard to the obligations of the well-to-do towards the commonwealth, carried the day to the extent of introducing a real income tax. This new step in advance was sought to be mitigated by a variety of provisos. The statute explains that all annoying intrusion into private matters is to be avoided in the assessment of the tax. The organizations in charge of the assessment are genial social bodies, organized on a basis of self-government, and with more regard for social amenities than for a strict performance of their duty to the state; the assessment is also somewhat lightened by the manner in which the new classes of incomes are constructed.

Still a gradual progress takes place, though by loosely defined methods impregnated with grave abuses, and after the lapse of a couple of decades a new reform is brought under way, - this time, too, being associated with far-reaching changes in the constitution of the commonwealth.

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The class tax was still retained for incomes under one thousand thalers; but it was now (1873) for the first time given a form answering to the requirements of the new era, being modeled after the classified income tax and based on a classification according to the money value of incomes. The income tax became a classified income tax, but it narrowed the intervals between classes and extended its action uninterruptedly into the highest grades of income; whereas the older form of the tax, as adopted in 1851, stopped short on reaching its highest class. At one essential point no change has yet made: the method of assessment remained as it had been.

But the aggressive vitality of this young tree would suffer no standstill. From this time the reforms follow one another with accelerated frequency. The obsolete method of the class tax was displaced in 1873, but in point of substantial fact the doctrinarianism of the years 1810-1820 still remained master of the situation. But the great events of the new era clear the way for realism at this point also. The class tax itself must gradually yield; as a first step in this direction the very lowest grades crumble away under the action of irresistible social facts. But even that is not sufficient; the view gains ground ever more decidedly, especially with the national government, that the class tax should be abolished or reduced, and even that the reduction should apply to the lower grades of the income tax as well as to the class tax.

In this we are following the example set by the practical English people, whose income tax has, for a hundred years past, given up taxing the poorer classes. This is in part a practical acknowledgment of the difficulties of levying a personal tax on the lower classes, in part it is an expression of a sense of equity which finds that the lower classes are sufficiently drawn on by means of other taxes for their proportional share in the burden of taxation.

The further development of the progression, the distinction between funded and unfunded incomes, in brief, a progressive realization of an equitable apportionment of the burden to the

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various grades of tax-paying capacity, but also as an indispensable means to this end, a thoroughgoing reform of the method of assessment, - these are reforms that follow necessarily as the next succeeding steps of the reform movement.

The difficulties of levying an adequately productive tax on large incomes by means of the other forms of taxation already spoken of will always necessitate a recourse to the subjective tax and the development of that tax in the direction above indicated. This is the office of the subjective tax as it is to stand in the new era, after it has cleared itself of the old-time accretions of capitation and class taxes, and so shall have reached an all the more vigorous development in its own proper direction.

§ 337. Apart from this social-political purpose, the further development of the income tax has set another office to perform. This is the attainment of that flexibility which will enable the tax system to adjust itself year by year to the varying fiscal demands. Also on this head the English income tax affords us an instructive example. It is to be said that this positive advantage possessed by this tax is due to what may be called the negative characteristics of the tax, - to the circumstance that it came into the world as an extraordinary tax, to be adjusted to the fiscal demands year by year, and to be dispensed with as soon as possible. But this negative feature has practically been set aside by the development of the last half century, and the positive advantages of the tax for meeting an annually increasing expenditure have been established for a long time past.

The reasons for this use of the income tax lie in certain peculiar characteristics belonging to it, as contrasted with other taxes. Objective taxes are too rigid to admit of any mobility of this sort; they are characterized by a definiteness and relative fixity of the rate of taxation - in some respects an excellent quality on general principles, but at all events an excellent quality in the eyes of the taxpayers. A rate varying greatly from year to year in accordance with the variations in the

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demand would under the objective tax (only remotely related to the individual's tax-paying capacity) frequently result in grievances which it is in the nature of the subjective tax to lessen. Still less adapted to this purpose are the taxes on business and on consumption. Both these classes of taxes are, for the most part, levied on acts which are, in a way, "voluntary." an increase of the rate in case of these taxes may easily result in the opposite of what was intended by their introduction; the business or consumption in question may decline under the pressure of the higher rate. Moreover, an annual adjustment of the rate is even more annoying in these cases than in that of the objective taxes, and this is to be avoided. The course of business and of the markets, the proper shifting of taxes from the first payers to the consumers, will be greatly disturbed by anything of the kind.

It is the office of the income tax - in an adequately developed form - to infuse flexibility and extensibility into the tax system, and so to put an end to open or covert deficit financing, as well as to the ever-recurring necessity of a new loan to meet even the most moderate "extraordinary" demand on the treasury.<sup>1</sup>

§ 338. Objective taxes [*Etragssteuern*] are, in point of historical origin, an outcome of the difficulties which beset the development of the tax system as well as of the growth of a sense of civic obligation to pay taxes; they therefore represent a low development of the methods of appraising tax-paying capacity, being employed under circumstances where the mature public sentiment on which to base a more perfect appraisal is lacking, where the "arbitrary" character of the income tax is dreaded and the obviousness of the assessment on proceeds is made much of. Further, in point of present expediency, the objective taxes are an equitable form of taxation so far as concerns the relation

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<sup>1</sup> On this point Gladstone says in his speech on the Budget, April 18, 1853: "The general position of her Majesty's government with respect to the income tax is this, that it is an engine of gigantic power for great national purposes." - *Gladstone's Speeches* (London, 1870), p. 308.)

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between the household and the state (empire, commune), where no regard is had to the subject's relative ability to pay.

While by its nature the subjective tax, in more or less developed form, taxes the aggregate income of the individual, it lies in the nature of the objective tax to follow up the particular taxable items [*Erträgen*] with or without a view to their equal taxation. The classic example of this kind of tax is the English income tax, which is based on the five specified classes of incomes, but which, as is well known, really is, as it purports to be, a subjective tax (sec. 311).

Whenever the objective tax is in reality an objective tax, the question arises whether the peculiar relations of certain income yielding objects to the community, in contradistinction to other income-yielding objects and their relations to the community, are to be followed up with a special objective tax. On grounds of historical development, as well as for enduring reasons of equity, this question is answered in the affirmative (in Prussia, France, etc.) so far as regards receipts from real property in town and country; - on historical grounds, because of its dominant importance among the different kinds of property, and because of its conspicuousness; for permanent ethical reasons, because of the intimate connection of landed property with the various organs of the commonwealth.

The question as to whether an objective tax is to be levied at all or to the same extent on proceeds arising from other forms of property, is suggested by the above question with respect to landed property. It goes without saying that other forms of property will also be taxed in a community where there has been considerable development of other kinds of property than real estate. If they are taxed at a lower rate than real estate, it is to be taken that the eminent importance of real estate for the commonwealth affords a substantial practical justification for so doing. On the other hand, the little else than technological advantage of a greater tangibility of real estate as contrasted with the professions, commerce, investments of capital, can afford no definitive solution of the matter; it is rather to be looked

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upon as an incentive to improvements in the methods of taxation, with a view to adequately reaching the income from these sources.

Whether the tax on realty, in the form of a tax on proceeds, is regarded as a means of laying the tax-paying capacity under contribution, or is taken to fulfill its office of payment for special advantages enjoyed; in either case something similar will hold with respect to a tax on professions, trade or profits of capital. In the Prussian tax system there is a gap at this point, which can in any case be only partially filled by the tax on realty. The requirements of equity remain unsatisfied so far as concerns the demand that our great industrial establishments, and the like, should bear their proportionate share of the burdens of the commune, etc.

§ 339. The relative importance of objective taxes was greatly increased by the later development of business life, at about the same time that the science came to an appreciation of the inadequacy of this class of taxes for the purpose of equitably taxing the subject (taxpayer).<sup>1</sup>

The increased mobility of modern life has given rise to an ever-increasing number of such relations between the individual establishment and the public treasury as separate the subject (taxpayer), spatially, from the tax object, so that the tax subject and the tax object frequently fall within the jurisdiction of different tax-levying authorities. Every such case of separation gives rise to a question of equity, requiring for its solution a distinction between the tax liability of the subject and that of the tax object (secs. 223-228).

The development of the means of communication must of necessity develop tendencies to a dispersion in space, a feature for which even the old régime (sec. 297) had been led by experience to make provision by means of its objective taxes.<sup>2</sup> It must of necessity happen more and more frequently that a tax-

<sup>1</sup> *Schriften des Vereins für Sozialpolitik*, vols. xii., xiv., 1877, 1878.

<sup>2</sup> Cf. the citation from K. H. Lang in the note to sec. 385.

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payer's estate, or his place of business, or his business activity, lies in a different commune from his domicile. As an example of the development here spoken of I may refer to the typical and very characteristic phenomenon of a gradual depopulation (as regards residents domiciled in the place) of the City of London at the same time that the business life of the City is taking rapid strides in advance.

This class of cases increases constantly, intensively and extensively, in volume and diversity. Both as regards the commune and as regards the larger communal organizations (circles, provinces), as regards states and empires, there makes itself constantly felt the need of a balancing of accounts between the individual and the public economy, such as objective taxes are well adapted to effect.

§ 340. But it is not the development of the means of communication alone which affords occasion for a growth of this need; there are developments in other lines in modern industrial life whose tendency is in the same direction. There are forms of industrial enterprise whose nature involves the result that the place where the undertaking in question develops its activity is nowise related to the place of domicile or of the business activity of the persons whose means are invested in the enterprise. Joint-stock companies are the chief example of this class of enterprises. They gather the large capitals which are required for carrying on certain industries from the most varied sources and from ever-increasing distances, and by means of an ever more extended sale of shares.

Hence it happens, with growing frequency, that the place where the invested capital puts forth its industrial activity is remote from the place of domicile of the shareholders in the company. The result is that we have a great number of cases in which subjective taxation and objective taxation do not keep company, a diversity of demands on part of various tax-levying bodies crossing one another. The business of a joint-stock railway company with its extensive plant, necessarily comes into

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intimate relations with local political bodies within whose jurisdiction its stations, workshops, etc., lie. These local tax-levying bodies have an equitable claim to some payment from the company, independently of all question as to whether or how far the railway plant and its business affords any profits (subjectively considered) to the stockholders of the company. A factory, whether it declares a dividend of 1 per cent. or of 30 per cent., in any case makes use of the streets and highways, and in so doing it occasions an expense to the local civil body, at the same time that it frequently increases the burden of the communal poor relief and public schools by attracting a laboring population to the place; for such expenses the industrial enterprises within the commune (of the province, etc.) are properly chargeable, just as much as for any other expenditure made in the interest of the enterprises in question.

This is a place where the objective tax should be employed. The employment of the subjective tax is entirely out of the question, either because there are no profits obtained or because such subjective tax as may be levied falls to those communes, etc., in which the persons live to whom the dividends go.

This taxation of joint-stock companies, it therefore appears, is of a twofold nature, involving two distinct principles of taxation, and therefore two kinds of taxes. From this is to be distinguished the other taxation of joint-stock concerns, which is intended to act as a double taxation with only the appearance of single taxation, the purpose of the legislator in its employment being to reach, by the taxation of the joint-stock company, what he is unable to reach directly by taxing the members of the company subjectively. So it was the purpose of the tax-reform proposition of the Prussian government in 1883 (following the example of the Saxon law) to tax the profits of joint-stock companies in order to cover the unavoidable gaps in the assessments on dividends (and other similar incomes), which were already nominally taxed by the law of May 1, 1851, but with very unsatisfactory results. It was therefore an attempt to accomplish, by what was in theory a double taxation, a result



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which in point of fact would amount to nothing more than a single subjective tax.<sup>1</sup>

The case of associations [*Genossenschaften*] (in the strict sense) is to some extent analogous. But only to some extent. The complicated question as to whether a society is a business concern in the same sense as a joint-stock company, and should therefore be required to pay the taxes levied on business associations, introduces a special point of some difficulty.<sup>2</sup>

§ 341. Closely related to the objective taxes, and in some part employed for a similar purpose, are the taxes on business or on transfers [*Verkehrssteuern*]. These are levied on particular transactions, a great variety of which are occasioned by the exigencies of business intercourse, and which constantly increase in number and variety with the increase of business.

They differ from objective taxes in this respect, that they are levied not on regularly recurring profits, but on certain business transactions recognized by the law (purchase, lease, loan, insurance, inheritance, gift), from whose occurrence the tax legislation infers the presence of corresponding receipts and incomes.

The designation adopted for this class of taxes, as well as their theoretical basis and their classification, has hitherto been a shifting one. The step taken by Lorenz von Stein,<sup>3</sup> in advance of the position occupied by K. H. Rau,<sup>4</sup> on this head, is significant of the entire attitude of Stein toward Rau's Financial Science; it is a needed disintegration of the earlier doctrine, which is, however, far from having reached a definitive conclusion and a satisfactory systematic structure.

But the disintegration of the untenable concept of a stamp

<sup>1</sup> For the legislation of the German states cf. *Finanzarchiv*, 1885, pp. 317 *et seq.*, 1886, pp. 803 *et seq.* and 1888, pp. 1009 *et seq.*

<sup>2</sup> For the controversy on this point in connection with the German and Austrian legislation, cf. Schanz, *Finanzarchiv*, 1886, pp. 674-762; Lewald, *ibid.*, 1886, p. 805; von Myrbach, *ibid.* 1888, pp. 674-720.

<sup>3</sup> *Lehrbuch der Finanzwissenschaft* (5<sup>th</sup> ed. 1886), *Zweiter Theil*, 2. *Abtheilung*, pp. 210-226.

<sup>4</sup> Cf. sec. 280 above.

tax, or rather of a stamp fee, is definitively accomplished.<sup>1</sup> It has been made plain that the stamp is nothing but a particular means of collecting a tax or a fee, and that it may be employed in the collection of various kinds of taxes, taxes on business as well as on consumption. The difficulty of constructing an adequate scientific definition, but not the tenability of the earlier notion of a stamp tax, is increased by the fact that many stamp taxes partake of the character of tax and fee both, and that other stamp taxes occupy an uncertain middle ground between the tax on business and the tax on consumption (taxes on bills of lading, on railway tickets - transportation taxes).

While this field affords an opportunity for the exercise of scientific acumen,<sup>2</sup> it also appears, on the other hand, that the further development of taxation will, for a long time to come, afford a place for the employment of taxes on business transactions. These taxes seem to me (and in this I substantially agree with Adolph Wagner) to be of service as supplementing the taxes on earnings [*Erwerbssteuern*], subjective as well as objective. This position is in consonance with a view of taxation - idealistic in its aspirations and realistic with respect to the means to be employed - which recognizes the shortcomings of each particular class of tax as well as the great difficulty of removing these shortcomings, and is therefore thoroughly - convinced of the necessity of supplementing any single class of taxes by taxes of another kind. We have not even the conviction, but only a hope that a painstaking elaboration of the tax system in detail will make the various kinds of taxes mutually supplement one another and fit the salient and re-entrant angles of taxation together.

Of course this point of view does not exclude, but rather demands a persistent criticism and improvement of existing taxes on business transactions, under the guidance of scientific theory. But at this point, as well as elsewhere, we must carefully avoid underrating the importance of existing results of historical growth; the French taxes on transactions have been cited

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<sup>1</sup> Cf. R. Friedberg, "Zur Theorie der Stempelsteuern," *Conrad's Jahrbücher*, 1878, pp. 69-94. The same, *Die Börsensteuer* (1875).

<sup>2</sup> Wagner, *Finanzwissenschaft*, vol. ii. pp. 439-480.

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(sec. 283) as an historical example of taxes on the transfer of realty, serving to illustrate the force of habit, at the same time that it is a result not to be reconciled with any scientific system of taxation.

§ 342. Whether (with Adolph Wagner) we construct a special class of "succession-taxes" [*Anfallsteuern*] beside the taxes on transfers, or, as seems not incongruous to me, we comprehend this class of taxes under the general class of taxes on transfers, in any case this is a branch of taxation resting on a solid basis and of great significance for the future.

For while in the great variety of other occurrences that are reached by the taxes on transactions we have to do with transactions of the nature of bargain and sale, which logically afford nothing more than a basis of inference, and even a qualified inference, as to the taxable gains resulting from the transaction, the nature of inheritances and donations, on the other hand, is that of gratuitous transfer, so that these occurrences of themselves indicate an accession of property; and although the significance of such accession may vary with the varying relations subsisting between the parties concerned, still the fact remains that there is in every case a real gain.

It may be that other taxes on business [*Verkehrssteuern*] as well as taxes on proceeds [*Ertragssteuern*] will have to acquiesce in the imputation that they fall upon business transactions which afford no safe inference as to any gain derivable from them (even the taxes on proceeds, as regards some portion of them, are of the nature of advances made in productive industry, in that they are simply a payment for services rendered by certain public establishments without there being any question as to whether a gain will result to the taxpayer). But the case for the tax on inheritances and gifts is a much stronger one; these events are not expressions of a simple one-sided relation alone, but what is much more important, there is a manifest connection between the transaction taxed and the paying capacity of the taxpayer.

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§ 343. The category constructed and introduced into the theory of taxation by Adolph Wagner, and commended by him as peculiarly important and desirable - Taxes on Speculative Gains [*Konjunkturgewinne*] - occupies a middle ground.

From one point of view these gains appear to be gratuitous gifts of chance, accruing to the individual under circumstances calculated to shed light upon a dubious spot in every industrial community organized on the basis of private love of gain. The taxation of these gains, when viewed from this standpoint, commends itself not only as a direct logical consequence of the accepted principles of taxation, in the same sense as does the tax on inheritances, but it is at the same time a social-political measure directed to an equitable neutralization of the harsh discords of modern business life. It is unnecessary here to recall Lassalle's highly colored account of the nature of the "conjuncture"<sup>1</sup> - *als rohe Naturmacht auftretende gesellschaftliche Zusammenhänge.*" This is one point of view; but there is also another.

Speculation is not, as Lassalle asserts, simply "a guess at the results which unascertainable circumstances will bring forth." It is more than that. It is the struggle of intelligence, armed with a knowledge of the ascertainable conditions, against the blind workings of chance.

This struggle takes the form of commercial transactions between two parties holding opposite opinions as to the results to be expected from known conditions, and so testifying to the uncertainty of any anticipation of the future. It is these transactions, based on the uncertainty of the future, on which the tax must be levied if it is to reach the speculative gains under the general form of a tax on business transactions.

Precisely this recognition of the blind working of chance in human affairs casts doubt upon the legitimacy of such legislative interference, at the same time that it neutralizes the effort to reach the speculative gain. It is only on such portion of the transactions in question as have actually resulted in a gain, and only on the ground that they have so resulted, that a special tax can be

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<sup>1</sup> *Kapital und Arbeit* (1864), chap. i.

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imposed, after the fashion of the inheritance tax; provided always that practicable means of levying such a tax are at hand, and that such means are available only in the form of a subjective tax - a taxation of income and property - and not in the form of a tax on business.

§ 344. The problem seems an easier one in cases where the nature of the speculative article excludes the possibility of two alternative speculative aims - a rising and a falling of the price both. In such a case an exceptional preponderance of the ascertainable and the known conditions affecting the particular article in question confines the force of chance within a narrower range. In these cases the development of value in the process out of which speculative gains accrue to private individuals takes the form of an undeviating, continuous chain of increments of value, and in such cases there is a more available opportunity for the imposition of a practicable and equitable tax on the transactions in question.

The course of values in real estate has frequently, under favorable circumstances, given the impression that it affords a case of development of the kind above spoken of. During a period of strongly progressive development of industrial productivity and of population, and especially at every focus of economic growth, in the great cities and their immediate surroundings in the city-like industrial countries, the record of increase in real values shows a movement which appears to be quite the opposite of the rise and fall above contemplated, both in point of absolute increase and in point of steady growth. Especially striking are the instances, to be found in any modern metropolis, of the value of building ground advancing in the course of years, decades, centuries, moving constantly in the same direction:

But even at this point the tax on business transactions will not find as ready application as might be expected or as might be desired.

In the first place, it appears on analyzing the movement in detail that the steady advance of values which is observ-

able in the movement taken as a whole is not to be found in each particular case. It may be fully established as a point of theory, and it may also be sufficiently borne out by experience, that under certain favorable conditions the course of values of realty is, in the long run, towards; but the ownership of a given piece of property by a given person is, under modern economic conditions, not a matter of centuries, and frequently not a matter of decades; it is the course of values during the lapse of a shorter time that is the decisive point for the owner, and it is this fluctuation of shorter periodicity that is had in view in very many of the transactions in real estate. And within this briefer period it is to be remarked that (especially under existing agricultural conditions in Great Britain, Germany, etc.) what we find is at best a stagnation, or even some decline of values. The rental value of landed property, therefore, falls into the same category as other goods whose rise and fall is to be taken into account.

In the second place, so far as it is well founded, the expectation of an advance in the value of real estate - such as is unmistakably to be seen in a modern city like Berlin - will give rise to an effort, as widespread as the tendency itself, to take advantage of this "calculable appreciation." The prices which are paid for a building lot under such circumstances may of course be expected to comprise the equivalent of the currently expected future advance. The degree in which these expectations affect prices may be greater or smaller, according as times are good or bad, but it is always an active factor for the simple reason that the future rise of land values is a generally accepted article of belief. From this it follows that such an advance in the prices is not necessarily due to a present favorable turn in the movement of population or of industry, but rather that the effect of any such favorable turn in the future has already been discounted in the present price. The greater the number of speculators concerned, the more highly developed the speculation, the more sensitive is the fluctuation of values and the more difficult, consequently, is it to infer any speculative gain from the fact of a transfer of property.

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Still, it is conceivable that demonstrable gain from the sale of real estate might be made an object of taxation just as a gain by inheritance or from a lottery ticket is taxed. It is also not to be denied that the publicity of the transfer of real estate affords a readier indication of such a gain than is to be had in the case of other business profits. But on this point the following considerations are to be taken into account.

In the first place it would lead to the adoption of annoying regulations to be observed in every transfer of real estate with a view to determining, from the special circumstances of the individual case, whether any gain has resulted or not. How far these regulations would be burdensome to the officials and to private parties, how far they would accomplish their purpose, what kind and amount of evasions they would encounter; this would be a problem to be settled by experience alone.

But in the second place, even a relatively successful taxation of the speculative gains on real estate might easily be regarded as an anomaly, or as a case of one-sided taxation (as is so often the case with respect to existing imposts on landed property, in view of the absence of any similar taxation of other business gains. But the attempt to supply this deficiency with respect to the taxation of other gains would probably encounter very great difficulties, inasmuch as it would require the application of similar methods of publicity to other business, and these arrangements would have to be created, and created for the purposes of the tax, whereas, in the case of the transfer of realty these requirements of publicity already exist, even apart from any purpose of taxation, and are in the nature of the case readily enforced in spite of the mobility of business life as it actually exists. At the same time, the unreserved disclosure of the condition of other business enterprises to the officials for purposes of taxation would involve an amount of intrusion into private affairs such as is entirely foreign to existing methods of tax administration and would therefore appear to be a harsh and unequal requirement. And in addition to this, the artifices for the evasion of any such requirement in themselves offer a problem of some difficulty.

§ 345. In itself considered, the idea of seeking out and adequately taxing the speculative element in the gains of modern business is quite legitimate, but it is scarcely if at all feasible by the proposed method of a tax on business. Still, the difficulties of this method serve to point out another and more practicable way. The fact has already (sec. 243) been spoken of that there is a point here at which tax legislation may fail, either in the enactment of the law (Prussia) or in the administration of it (Switzerland). Land adjoining the city and increasing rapidly, in value by reason of the city's growth is permitted to escape with a tax answering simply to its agricultural value, so long as it has not actually undergone the transformation into an urban building site. A piece of suburban property - according to the provisions of the Prussian tax legislation (sec. 306) - is not transferred from the land-tax cadaster to the building-tax cadaster until it is covered with a building; there is no tax for a building lot, as such, so long as it is not occupied by a house, however great may be its actual value, and however manifestly it is withheld from occupancy for the sake of a speculative gain. The justice of this claim is not impugned by the fact that the good intention has, in a particular instance, taken a vicious form.<sup>1</sup> What is wanted is a more adequate application of the canons of equity than is to be expected in the caricature of legislation comprised within the jurisdiction of a state covering a fete square miles, where the merchants make laws to suit their own interests; as Aristotle says, a wagon one span long is no wagon.

But the question does not concern values of real estate alone; the omission which claims our attention at this point is one which calls for reform in our income-tax legislation as well. There are, in fact, very grave problems calling for solution at this point.<sup>2</sup> These problems stand in close relation to what has already been said (secs. 317-322) on this head in speaking of

<sup>1</sup> Cf. the opinion of G. Hanssen on the law of Bremen and the *Superarbitrien* (Bremen, 1877), Also *Finanzarchiv*, 1884, pp. 100 *et seq.*

<sup>2</sup> *Conrad's Jahrbücher*, 1885, pp. 24-45 ("Ein Wort zur Börsensteuer"). Reprinted in *Nationalökonomische Studien*, 1886.



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the Prussian legislation, as well as with what remains to be said farther on. Their consideration would lead to a discussion of certain peculiar supplementary tax contrivances calculated to impose special taxes on the great aggregations of profit from speculative business.

It is therefore to subjective taxation that we must turn for the effective means of compassing the required equity.

§ 346. Taxes on transactions, in the strict sense (exclusive of "succession-taxes" in the sense used by Adolph Wagner), show, in respect of the objects on which they are levied, the same course of development which we find in the case of other taxes. Just as in the case of taxes on proceeds the tax on land stands first in importance and in point of time, because of the preeminent importance of landed property in the economy of the community, because of the relative unimportance of other sources of income during the early stages of industrial development, because of the obtrusiveness of this as contrasted with other forms of property; - so, likewise, in the case of taxes on transactions it is the transfer of realty that is constantly required to bear a burden beyond what is imposed on other property transferred.

In a commonwealth in which the propensity - for innovation turns by preference to alterations of the constitution, while the methods of administration all the more persistently retain their ancient form, - in France we find even to this day a tax on the transfer of real estate, which is a faithful image of this earlier method of taxation. And in this taxation it will even hold true that imposts of a private and of a public character are blended together quite after the fashion of what occurs under the feudal state.

The contrast between the established institutions and what reason would require is in this case a very striking one. The evidence of the fact of transfer is desirable for purposes of taxation, but the imposition of the burden has nothing to do

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with equity. The special tax imposed on the basis of the evidence so obtained is justifiable only in case the (in itself considered, justifiable) purpose is not adequately attained by other forms of taxation. The hardship involved in a considerable tax on transfers (with a view to taxation of the speculative gain might be dispensed with in case a great and constant advance in the value of real estate could be assumed to take place; but the difficulty at this point lies with the assumption here made, which may either be wholly unfounded or may not hold with sufficient permanence and generality.

We accordingly find that the tendency of the latest legislation is toward an abatement of the tax on realty which has been handed down from the past.

§ 347. The need of some equalization on grounds of justice, the development of personal property and the resulting increased transfer of personalty [*Mobiliarverkehr*] and the complaints of excessive taxation on part of landowners, have in later times given our tax legislation an occasion to extend itself along the lines of the earlier stamp taxation. But it has always been with a well-founded horror of interfering with business transactions, such as must result from any but moderate rates of taxation.

Still, it is instructive to note that those countries of Europe whose industry stands at the head of modern development have applied the tax on transactions to a greater extent than those whose industrial development has been later and slower. Great Britain, and also France, have, as contrasted with the German legislation, made earlier and more extended use of the tax on transactions. The British law taxes bills of exchange, bank notes, life and marine insurance policies (previous to 1869 also fire insurance policies), receipts. None of this occurs in the legislation of the German Empire. Receipts, taxed since 1855 at an invariable rate of only one penny (for sums of £2 and over), yield at the present time an annual revenue of £1,000,000,<sup>1</sup>

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<sup>1</sup>The amount for the fiscal year ending March 31, 1888, was £992,325, as against £733,158 in 1874, and £257,631 in 1856. - *Statistical Abstracts for the United Kingdom, 1853-1867 and 1873-1887.*

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that is to say, four times what it amounted to thirty years earlier.

The legislation of the German Empire (Acts of July 1, 1881, and May 29, 1885) omits all these items. It applies, apart from drafts, only to securities, broker's notes and bills of transactions in securities, and the aggregate amount of the tax was for the fiscal year 1886-87<sup>1</sup> 12.88 million marks; that is to say, not much more than one-half of what the tax on receipts alone yielded in Great Britain. The stamp tax on drafts, habitually in extended use in Germany as in other countries, was reduced to uniformity for the first time by a law of the North German Federation of July 10, 1869, and afterwards (1870-71) extended throughout the German Empire. This tax, in spite of the appreciable increase in its aggregate amount as compared with the results obtained during the first half of the century, still yields only 6.50 million marks in Germany, while it yields 14 million marks in Great Britain. At the same time it is to be noticed that the stamp tax on drafts in the latter country has fallen off<sup>2</sup> very considerably on account of the great spread of business transactions on a large scale since 1874, much more so than in the German Empire, where the amount of the tax in 1873 was 7.85 million marks (in 1874, 7.04 million marks).

§ 348. It appears, therefore, from the foregoing considerations that there are grave difficulties connected with the taxation of transactions; it is only in cases where the business in question is very brisk that it is possible to collect a considerable revenue, because the rates are perforce extremely low; while the classes of transactions which would seem at first sight to be especially fitted for this kind of taxation prove unproductive of revenue. In coming now to the taxation of inheritances and gifts, however, we have to do with a more amenable subject, which

<sup>1</sup> *Statistisches Jahrbuch für das deutsche Reich*, 1888, p. 197.

<sup>2</sup> The revenue obtained was, in 1874, inclusive of the tax on bank notes, £1,127,945, and has constantly declined from that time until late years, being in 1887, inclusive of the tax on bank notes, £765,059; precisely the opposite of what happened in the case of the tax on receipts.

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may more properly be made a subject of heavy taxation both on grounds of justice and of expediency.

All the elements which are absent in the case of the common run of business are here combined - a coincidence of an independent act of the court with the act of proving and entering upon an accession of wealth, and therefore of an increased taxpaying capacity. It is of course necessary to take cognizance of the kind and degree of relationship between the heir and the person leaving the inheritance, in order to satisfy the requirements of equity in taxation; it may be that an adequate appreciation of this relation will, under given circumstances, result in an exemption from the inheritance tax (as happens in point of fact under the inheritance laws of most countries with respect to the inheritance of property within the first degree of relationship); but after all due allowance has been made, there is still left a broad field for an inheritance tax of undoubted equity and expediency, as is proven by the testimony of all existing systems of tax legislation (in other words, all convictions as to equity handed down from the past), as also by cogent arguments of policy both as regards taxation simply and as regards social expediency.<sup>1</sup>

§ 349. In order to an understanding of the inheritance tax in its relation to existing tax legislation it is necessary to reach some definite appreciation of the meaning of the right of inheritance.

The right of inheritance is, on the one hand, a civil recognition of the bond of kinship, which is an expression of an ever active sentiment of humanity as well as of a necessary condition of civilized life (vol. i. sec. 308); but at the same time it is also, on the other hand, the expression of the owner's arbitrary choice seeking to perpetuate itself beyond the grave.

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<sup>1</sup> Cf. H. von Scheel, *Erbschaftssteuern und Erbrechtsreform* (2. ed. 1878). The Same, *Hirth's Annalen des deutschen Reichs*, 1877. E. Leser, "Die britische Erbschaftsbesteuerung," *Zeitschrift für die gesammte Staatswissenschaft*, 1881. A. Wagner, *Finanzwissenschaft*, 3. Theil (1889), pp. 266-276. *Finanzarchiv*, 1885, pp. 877-892. Otto Bacher, *Die deutschen Erbschafts- und Schenkungssteuern* (1886). *Hildebrand's Jahrbücher*, 1873, vol. xx. pp. 373-384. Karl Krüger, *Die Erbschaftsteuer nach ihrer Ausübung in den ausserdeutschen Staaten, die Berechtigung ihrer Reform in Deutschland und ihrer Einführung als Reichsteuer* (1889).

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According as the right of inheritance is one or the other of these two things it does or does not appear to society and to the state as unimpeachable, or at least a restriction of it will or will not seem to be a hardship, as the case may be. The sentiment which has found expression in the gradation of the inheritance tax is quite in consonance with this view. Inheritance by a son or a daughter is simply an accession to what the sentiment with regard to kinship as well as the consciousness of the great significance of this relation for the commonwealth recognizes as theirs by right. Accordingly the sense of equity does not see in an inheritance of this kind an increase of possessions in which the state can claim a share on the ground of its being a fortuitous gain. Even where the prevalent views as to the equity of an inheritance tax call for a taxation of such cases they are wont to content themselves with the imposition of the lowest rate employed.

In proportion as the transmission by inheritance passes these narrow limits of kinship, sentiments of a different character with regard to the equity of an inheritance tax come to prevail. The less close the bond of relationship is, whether because of greater remoteness or because of the prevailing conceptions as to the degree of importance of such a relationship, the more will the view prevail that inheritance is of the nature of an extraordinary accession and partakes of the character of fortuitous gain. The heir is conceived to enter upon the possession not of something that is properly his own and that by the nature of the case has long pertained to him, but of something alien, accidental and unexpected.

This contrast and this tendency in the evolution of the inheritance tax will always be present, so long as the now prevalent views of the family, property and inheritance on the one side, and of the state and the obligation to pay taxes on the other side persist. At the same time the practical realization of these tax gradations in the future will be subject to the like course of development as the varied tax provisions of different countries show to have prevailed in the past.

§ 350. The contrast afforded by the amount obtained from the tax in different countries may serve to show to how great an extent the inheritance tax is a product of historical conditions.

In the German states the amount of the inheritance tax was on an average for the years 1880-1884 not more than 29 pfennigs per capita of the population, in Prussia only 19 pfennigs<sup>1</sup> (with a very gradual increase resulting from the increase of wealth, and for 1889 in Prussia about 24 pfennigs.<sup>2</sup>

On the other hand the inheritance tax in France, in 1884, yielded a revenue of 2.85 marks per capita, in Belgium (1880) 3 marks, in Italy .83 mark, in Great Britain (1884) 4.37 marks, in Holland 3.02 marks.

There is no doubt but that diversity in point of wealth, at least as regards certain ones of these countries, has something to do with this difference in results. Also some part of the difference is due to the different degrees of strictness with which the tax law is administered (somewhat as we have found is the case with the income tax in England as compared with Prussia). But the chief cause of difference is no doubt a difference in the provisions of the law, in great part the taxing of the nearer degrees of kinship in some countries instead of exempting them as is done in other countries.

In France, with an aggregate revenue (1883) of 138 million francs derived from the inheritance tax, the taxation of inheritances in the direct line alone yields 35 million francs and the tax on inheritance between man and wife 15.50 millions; while both these degrees of relationship are exempt in Prussia and in pretty nearly all the other German states (Baden, Schwartzburg-Sondershausen and the Duchy of Lauenburg impose a tax on inheritance between man and wife of 1.66, 3, and 1 per cent. respectively). France taxes inheritance in the direct line at a rate of 1.25 per cent. and inheritance between man and wife at 3.75 per cent.

To this is to be added that the other, remoter degrees of relationship, as well as the cases where there is no relationship,

<sup>1</sup> *Finanzarchiv*, 1885, p. 877.

<sup>2</sup> The estimates for 1889-90 assume a probable revenue of 6,900,000 marks.

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are taxed more heavily. Inheritance between brother and sister is taxed in France at 8.125 per cent., in Prussia at only 2 per cent. The highest rate imposed on the remotest degrees of relationship and on non-related heirs is 8 per cent. in Prussia and 11.25 per cent. in France.

In Great Britain the inheritance tax in its various forms has yielded a progressively increasing revenue whose amount has been as follows:<sup>1</sup>

1859-60	£3.46 million
1873-74	5.48 "
1879-80	6.23 "
1887-88	8.24 "

In this latter year it made up about one-ninth of Great Britain's aggregate revenue from taxation (75.66 million pounds).

In this case, too, there is a taxation of inheritance in the direct line (1 per cent.), a higher rate for the nearer degrees of kinship (3 per cent. for brothers or sisters) and a further increase of the rate for the remoter degrees of relationship and non-related heirs (10 per cent.). There is also a second, subsidiary form of inheritance tax (probate duty) which is levied without regard to the degree of relationship and is graduated by classes according to the amount of the property, the rate being about 2 per cent.

§ 351. Tax legislation has so far reached a much lower degree of development in another direction - viz., in the development of a progressive rate, to increase with the increasing amount of the property inherited.

In this case, as elsewhere in taxation, a beginning in this direction has been made at the lower end of the scale, by the exemption of the very small and the smallest amounts. A measure of this nature, moreover, has the support of a principle involved in the taxation of inheritances. If, as happens in France, Great Britain and many other countries, inheritance in the direct line is also taxed, there is at least this much to be said for the views which prevail today in the German states,

<sup>1</sup> *Statistical Abstract for the United Kingdom*, 1888, p. 17.

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that in case of very modest pecuniary circumstances (such as are so common in Germany) the decease of the head of the household and the succession of his immediate heirs to the property carries with it a pecuniary change for the worse rather than for the better.<sup>1</sup> It is in accord with this fact that the idea of the inheritance tax requires the exemption of this class of cases, or at the most that they should be taxed at a lower rate than others, and the case is analogous if legacies of small amount in favor of needy relatives who may have habitually received support from the testator during his lifetime are exempted, relatively or entirely, from the inheritance tax.

Following out the same thought higher up in the scale, into the development of the idea of a progressive taxation we come upon demands which lie rather in the region of what ought to be in the future than of what actually exists today. It is only in isolated instances that existing legislation has been affected by this line of thought, and, very significantly, it is (in connection with existing taxes on income and property) in three Swiss cantons, Zurich, Soleure and Thurgau, that anything of the kind occurs.

In Zurich it is provided by the law of December 22, 1869, that "these amounts of the tax are to be increased: by one-tenth in case not less than 10,000 francs, by two-tenths in case not less than 20,000 francs, by three-tenths in case not less than 30,000 francs, by four-tenths in case not less than 40,000 francs, by five-tenths in case not less than 50,000 francs fall to a single recipient." In Soleure the law of December 13, 1848, provides: "If the amount inherited by a single heir (or legatee) amounts to less than 100 francs, only one-half the fee will be collected; whereas the like fee will be increased by one-quarter for all such legacies amounting to not less than 5000 francs, by one-half for amounts of not less than 10,000 francs, by three-fourths for amounts of not less than 15,000 francs, and doubled for amounts of not less than 20,000 francs." In Thurgau the law of May 23, 1850, provides: "If the amount received by an heir falls

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<sup>1</sup>J. G. Hoffmann, *Lehre von den Steuern*, p. 424.



short of 212 francs (= 100 gulden) only one-half the fee will be exacted; whereas the like fee will be increased by one-fourth for legacies amounting to not less than 6350 francs, by one-half for amounts of not less than 12,700 francs, by three-fourths for amounts of not less than 19,000 francs, and doubled for amounts of not less than 25,000 francs."

In other countries the development of tax legislation in this direction has so far taken place to so slight an extent that it even happens in many countries (in a manner quite analogous to what occurs in the case of the undeveloped income tax) that the rate of the tax decreases in the higher grades of the scale, so that the larger inheritances bear a relatively lighter burden than the smaller ones. Such is the case in Great Britain. Here the probate duty for amounts of £30,000 and over is about one and one-half per cent., whereas for amounts of £3000 to £30,000 it is about two per cent., and for still smaller amounts usually over two per cent. A reform has been attempted only very lately (1889). The Chancellor of the Exchequer, Mr. Goschen, proposed to introduce a new form of inheritance tax to be added to those already in force, by which it is proposed to levy a tax of one per cent. on every estate amounting to more than £10,000, whether land or personalty. The purpose avowed by Mr. Goschen (a correct Manchesterist, by the way) is to reach the growing body of accumulation, because "people of considerable means habitually pay very low taxes in proportion to their aggregate income."<sup>1</sup>

"On the whole, I think it will be found that the men whose fortunes are considerable are those who pay the least in proportion to their aggregate income." (*Economist*, April 20, 1889.) A reform was introduced in England as early as 1888, the purpose of which was to raise the disproportionately low rate of taxation on realty to correspond to that on personalty by adding one-half per cent. to the succession duty. An inheritance of £20,000 (lineal succession to unsettled property) bore a burden aggregating as follows:

	REALTY	PERSONALTY
1887	£ 84 18s. (Succession duty)	£ 600 (Probate Duty)
Law of 1888	£ 124 3s. (Succession Duty)	£ 600 (Probate Duty)

It is to be remarked that, as happens in the case of the income and property tax, so also in the case of the inheritance tax, we have to do with the solution of problems of financial equity and of social policy, towards which existing legislation serves as the rudimentary substructure on the basis of which a further development is to proceed. It is only by bearing this purpose in mind that we shall be able to maintain the existing system of property in substantial integrity, as against the far-reaching demands put forward not only by the radical opponents of the rights of property, but also by scholarly critics, such as John Stuart Mill,<sup>1</sup> who claims that "no one person should be permitted to acquire by inheritance more than the amount of a moderate independence."

### III. THE TAXATION OF PROPERTY OR POSSESSIONS.

§ 352. The taxation of earnings [*Erwerbsbesteuerung*] as it exists today leaves but scant room for taxes on possession [*Besitzbesteuerung*].

In point of the extent to which it is employed the property tax is the chief item under this head. As viewed from the standpoint of the modern science the property tax is to be regarded as comprising several heterogeneous elements.

First, the property tax is the ancient form of the tax on earnings, making its demand upon the taxable earnings on the basis of the most obvious and accessible evidence. To this day it commends itself to the Swiss peasant as a much more convenient and expedient method of assessment to return the aggregate value of his property than to compute the annual income which it yields. The further provision by law for a return of the "income" is evidence of the difficulties in the way

	REALTY	PERSONALTY
	£ 124 3s.	£ 600
	(Succession duty)	(Probate Duty)
Bill of 1889	£ 200	£ 200
	(New tax)	(New tax)

<sup>1</sup> *Principles of Political Economy*, book v. chap. 9.

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of properly collecting the tax under the incredible circumstances that prevail in the assessment of rural property.

Second (not without some regard to the above-mentioned difficulties, modern financial science, so far as concerns certain of its representatives, is also inclined to recognize the practical technical advantages of the, "property tax" as contrasted with the "income tax."<sup>1</sup> By its means we not only avoid the vagueness and indistinctness of the idea of "income," we not only avoid the difficulties involved in a return of the produce of property, but we also accomplish certain positive results which cannot be as readily attained by any other method.

These positive results to be attained are (1) the compensatory taxation of property which does not, for the time, yield an income, (2) the taxation of consumable goods [*Gebrauchsvermögen*] as well as of property productively employed, (3) the heavier taxation of income from property as compared with income from personal effort, and, finally, (4) the ability to demand a portion of the principal [*Vermögensstamm*] for certain (extraordinary) purposes of the commonwealth (real property tax in case of need. We shall now have to discuss these several purposes of the property tax proper.

§ 353 In the first place, as regards the compensatory taxation of property, a consideration of this point confronts us with the technical difficulties in the way of a taxation of income. These are difficulties which have to some extent been augmented by the later development of industry.

There are certain classes of income which - apart from any difficulty in getting at the truth - stand out in perfect distinctness and regularity and so are well adapted for the application of the income tax. This class of incomes is made up of the permanent interest payments derived from loan capital invested in good securities for a long period. Of a similar nature are the salaries drawn by higher and lower officials holding permanent

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<sup>1</sup> For the meaning of these terms, cf. secs. 237-244 above.

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positions in public and in private life. In cases of this kind, of course, we can no more speak of an unlimited permanency of the income than we can speak of an unchangeable uniformity in it. But with regard to both of these points the actual limits are so narrow as to effectively serve the purpose of the tax assessment, which is that of reaching the regularly recurring incomes.

There are large regions in the field of industrial life within which the circumstances are not so favorable to the appraisal of income as here. Strong and frequent fluctuations in the earnings of capital and of labor give rise to the necessity of a frequently recurring, annually (biennially, triennially) repeated appraisal, which encounters special difficulties even on account of this frequency of recurrence. The more frequently it recurs the more difficult will it be to so allow for the annual fluctuation as to reach any kind of a stable average of the income in question. If we have regard to the relatively great space of time within which the periodicity of rise and decline in modern industry and modern business completes itself, it will appear that an appraisal covering a period of one, or even of three years is quite inadequate. Any extension whatever of the period covered by the assessment, of which there could be serious talk would - even apart from its doubtful applicability to other classes of incomes - be ineffective for the desired end. The uniformity of income sought to be attained by means of an average of a great number of varying annual amounts could in any case not be reached.

By replacing the income tax by the property tax this difficulty is avoided. But the difficulty is not removed. How much is to be demanded annually of the property in question in the form of a property tax remains an open question, just as it was when the same demand was made in the form of an income tax. In both cases the problem is to pitch upon the proper average figure for a tax on a certain regularly recurring, average taxpaying capacity.

It is only when we come to apply it to property which yields

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no profits that the property tax is anything more than an income tax under a different form.

In such a case the income tax ceases to be operative because the income on which the tax is based has ceased for the time. It therefore becomes the office of the property tax to assert the right of taxation which (even in the absence of income) pertains to the state and to the public organization generally simply in virtue of the fundamental importance of these public institutions for the life of every civilized man. This fundamental importance of the state for the life of all its members gives it a claim to a tax on property of the same validity as the claims of the other fundamental necessities of life - of food and drink, of shelter and clothing.

Here we have accordingly come upon an actual gap left by the income tax, which it is the office of the property tax to fill out; a gap which the income tax as such can scarcely remove, and which plays so unobtrusive a part in the assessment of incomes only because the assessment of income in practice departs even more widely from the strict principle than the tax legislation does.

§ 354. The taxation of property employed in consumption [*Gebrauchsvermögen*] (as distinguished from productive property) is also a matter that comes up for consideration in connection with any thoroughgoing income-tax system; but so long as the prevailing indefiniteness of ideas as to the nature of income continues, and especially so long as the prevailing instinct of the majority continues to assert itself against the payment of taxes, this problem, too, has a better chance of solution by the method of the property tax.

Crude notions as to the nature of income, as well as apprehension of the insuperable difficulties of assessment, have inclined the income-tax legislation to recognize an income only in cases where a money value emerges - where there is a receipt in money or where there are proceeds in kind which bear an obvious money value. The tax administration follows this inclination still

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further, so as to close its eyes to the presence of any proceeds in kind even if they possess an obvious money value.

The income tax should fall on the house occupied by its owner, or rather on his use of it, as well as on the rent which he receives for the house occupied by a tenant. The more prevalent the business of renting dwelling houses is, the more surely will the use of a house occupied by its owner be brought under the income tax, but where, as in the country, it is the rule (at least for the well-to-do, who mainly contribute to the income tax) to own one's own house, while the renting of houses is not a usual source of money income, tax legislation, and especially the tax administration, will be inclined to disregard this element of income.

Something analogous occurs quite generally, so far as concerns items of property which afford their owner a use that does not take the form of a money income, whether in town or country, that is, things which in the nature of the case are neither hired nor leased. A typical example of this is the possession of a picture gallery. If the occupancy of one's own house is to be counted at the rental value of a house of the same value, and therefore as representing so much of an increment to the owner's income, then it is plain that the same will hold of any house, however expensive, by whatever accessories the expensiveness of the house is increased, whether by a greater number of rooms, by gardens, parks, works of art, picture galleries, or anything whatever. The enjoyment of a house that has been rendered beautiful by art is a consumption of greater money value, just as much as it is more expensive to occupy ten rooms than to occupy five.

This simple course of argument will lead to a practical result much more readily by the method of the property tax than by that of the income tax. If we start out from the fact of the ownership of property as our point of departure, the misconceptions of everyday life will not blind us to the obvious principle that every item of property carries with it the same obligation to pay taxes, independently of what may be the particular steps

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by which it serves its purpose of utility to its owner. Indeed, how true it is that certain kinds of property devoted to consumption give rise to the impression of a greater tax-paying capacity on the part of their owner than the possession of productive property, is evident from the need which is felt of reaching this wealth by some other means - in the absence of a property tax, more especially by means of the so-called "direct taxes on luxuries." But this method has the disadvantage of attaching to special items of the wealth devoted to consumption, and so only circuitously approaches to the true goal, very generally without reaching it.

§ 355. In the other hand it is quite usual even where a general property tax is enforced to afford some relief in favor of such consumable wealth as serves the necessities of life. There is, therefore, observed in practice a sort of subsistence minimum in the application of the property tax, which differs from the principle of progression and exemption of a certain class of small properties in this, that the precise amount of the necessities of life is not here sought to be expressed in figures and therefore varies with a certain elasticity according to the standard of living and the pecuniary strength of the taxpayer.

The property-tax legislation of the Swiss cantons has applied this measure of relief more than once. The practice seems to have been less extended in earlier times than at present. The mediæval property tax [*Gutsteuer*] in Zurich,<sup>1</sup> which was frequently levied after 1343, was to be borne by all property, fixed and movable, to be levied on *Hus, Plunder, Kleider und Gewand*. The harness alone, *da mit er gemeiner Stadt wartet oder der zu seinem Leib gehöret*, is exempted. The property-tax law of 1417<sup>2</sup> contains a provision to the same effect.

In the next succeeding centuries this seems to have changed; not only weapons and armor,<sup>1</sup> but also plate, ornaments, household utensils, clothing and tools are exempt from the property

<sup>1</sup> G. Meyer von Knonau, *Der Kanton Zürich* (1846), vol. ii. p. 256.

<sup>2</sup> Bluntschli, *Staats- und Rechtsgeschichte der Stadt und Landschaft Zürich* (1838), vol. i. p. 401.

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tax in Zurich.<sup>1</sup> In Glarus<sup>2</sup> the Common Council [*gemeine Landgemeinde*] ordained in 1725 that everyone was to return, *bei Ehr und Gewissen*, all his property, with the sole exception of household furniture and clothing, etc. The later property-tax legislation in force at present pretty generally provides for a similar exemption. The Zurich law of March 2, 1870, provides that from the property tax is to be exempted the clothing, books, field and handicraft implements used by the taxpayers, and the necessary household furniture." (Similarly the Zurich law of February 14, 1861.) The law in Glarus (May, 1850) exempts household furniture and implements used in handicraft or field work. A similar provision is in force in Zug by a law of December 5, 1861 (March 10, 1862); also in St. Gall by a law of May 30, 1863; in Vaud by a law of August 21, 1862, ("the bed and the clothing required for the family, kitchen utensils, agricultural tools and implements, the tools and implements of handicraftsmen and laborers").

There are a number of cantonal tax provisions which go further, in that they apply under the term "capital-tax" only to realty and wealth productively employed. So,<sup>3</sup> for example, Schwyz (law of September 10, 1854), Soleure (March 9, 1832), Unterwalden nid dem Wald (June 5, 1848), Basle province (August 11, 1856), Schaffhausen (December 15, 1862), Thurgau (March 6, 1849), Valais (May 31, 1856, and November 26, 1862). Here, then, the use of the property tax for the purpose of reaching wealth devoted to consumption is definitely abandoned, quite in contrast with the earliest property-tax legislation of Switzerland, which was manifestly intended to reach wealth employed for consumption.

The Swiss federal law of June 28, 1878, dealing with the military-compensation tax [*Militärpflichtersatz*], provides, as does the Zurich law of 1870, that in the assessment of property "the

<sup>1</sup> Bluntschli, vol. ii. p. 28.

<sup>2</sup> Blumer, *Staats- und Rechtsgeschichte der schweizerischen Demokratien* (1858), vol. ii. p. 297.

<sup>3</sup> Renward Meyer, *Materialien zur Revision des Steuergesetzes, vol. ii.; Zusammenstellung der in den Kantonen geltenden Steuergrundsätze* (Lucerne, 1865).



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value of chattels required for the needs of the household, as well as of tools for handicraft and agricultural work, is not to be included."

These provisions of the Swiss legislation embody a certain tendency to limit the taxation of wealth employed in consumption; the precise determination of its scope is yet to be decided by the future evolution of the property tax, together with the further improvement that may take place in the method of assessment. It is not only true that the inadequacy of such a defining concept as "necessary" when introduced into a tax provision, points to the necessity of a closer definition of what is to be exempt from the tax, but it is very doubtful if an exemption of this kind can be justified at all in case it covers much more than the strict physical necessities, so as to include also the luxuries required by a socially necessary standard of living.

§ 356. The third office of the property tax, as enumerated above, is the imposition of a heavier tax on income from property than on personal income.

In point of fact, this object is compassed by the property tax as employed in the Swiss cantons and the Confederation (under the above-mentioned law dealing with the military-compensation tax). This has already been shown in detail in the earlier portions of the present volume (secs. 214, 321). In the canton of Zurich an income of 4000 francs (from property worth 100,000 francs) pays at present 17 to 20 per cent. to canton and commune together; a personal income of the same amount pays scarcely 3 per cent. to canton and commune together. In other cantons this contrast is rarely as striking as in Zurich. But as it is a very prevalent custom to employ the property tax exclusively (or as good as exclusively) for the purpose of communal revenue, the result is that throughout Switzerland, even outside the canton of Zurich, there is a very general heavy taxation of property coupled with a relatively slight taxation of personal income. The federal law above referred to, on the military-compensation tax of June 28, 1878, taxes every 1000 francs of

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property at the same rate (1.50 francs) as 100 francs of personal income; the result being that by so much as the average proceeds from property fall short of ten per cent., by so much does the burden on income from property exceed that on personal income. The repeatedly projected legislation of the Prussian government (1847, 1883) goes to show that the same purpose may be sought without employing the form of a property tax; the method adopted may be that of a higher rate of taxation on funded than on personal income under the provisions of the same general income tax. But these projects have not been carried through. The Swiss system of property taxation on the contrary has now been in force uninterruptedly for a long period of years and has become so much of a fixture that its characteristic features are no longer subject to change.

This result may possibly be due to the intrinsic justice-of the demand that income from property should pay a higher tax. This rests on the claim, which is scarcely to be seriously questioned, that the tax-paying capacity of income from property is much greater than that of personal income because of its greater security and permanence. It is also not to be overlooked that objective taxes (taxes on proceeds) ordinarily are not to be found in Switzerland, and that the property tax consequently is also called on to supply their place.

Progressive evolution of taxes on income in the great states of the present and the future will also be required to solve certain problems of this kind which have hitherto remained unsolved chiefly because of the dominance of the propertied classes and their disinclination to pay their share of the taxes.

In the usual objections to a higher taxation of funded income than of personal income I am, in fact, unable to detect any argument which has as much force as this practical fact above cited, which enables us to comprehend the delay there has been in recognizing the simple justice of the demand. That the income from property, too, is "uncertain" is an assertion of that undeniable sort that proves nothing. With human arrangements of wealth

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or of well-being are "uncertain," but that fact does not affect the relativity with which the question is concerned; the fact remains that the certainty of the one class of income, as well as its duration, or even perpetuity, is much greater than that of the other. And what we are concerned with is entirely a matter of a difference of degree; we require a larger percentage of the one class of income because it is held to possess a greater tax-paying capacity than the other. The objection that the taxation of income from property at a higher rate would discourage saving and accumulation of capital is the same well-known objection which on other occasions is raised against every kind of income tax. Any proof founded on experience in support of this objection has not yet been brought forward. And when put forward on general grounds only this objection has no more cogency than the contrary position which is urged on an equally general ground, viz., that the payment of taxes acts as an incentive to the industry and thrift of the citizens. It is a substantial gain to have hunted the aversion to this form of taxation into a corner and established the fact that it has its origin in an unripe public sentiment and not in a conviction which will bear scientific investigation.

§ 357. Finally, in the fourth place, the purpose of a tax on property as a "real property tax" cannot logically be compassed under the form of an income tax, and can be accomplished under the form of an inheritance tax (cf. sec. 239 above) only under special circumstances.

In this connection it is to be remarked that a real taxation of wealth (sees. 237-240), apart from the inheritance tax and other taxes of that class, is, for the existing stage of development of taxation, nothing but a remote possibility.

In the first place, the high development of public credit in our modern states has made available a very convenient method of raising the means necessary to cover any extraordinary expenditures. The imposition of a property tax, such as was repeatedly attempted in Prussia at the beginning of the century,

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for year purposes, and which failed so signally that its failure was used as an effective argument against the introduction even of a moderate income tax, - a measure of this kind in Prussia, as in any other state with a similarly developed system of finance and public credit, would be crowded to the wall by the greatly superior expediency of a public loan.

In the second place, the moral factors, the maturity of civic sentiment requisite for the successful adoption of such a property tax, are a feature of the future rather than of the present. In discussing the relative advantages of war taxes and of public loans we came to the conviction (sec. 167) that the sensitiveness to the pressure of a tax is greatly conditioned by the stage of development of the political sense, which is closely related to the growth of insight into the indispensability of the state and the consequent necessity of taxes. We have in the foregoing chapters repeatedly had occasion to remark how great are the difficulties which beset the states of today in this respect, how far in the future lies the last step in the progress if the consummation is to be a system of taxation which shall be based on a full recognition of the greatness of the burden together with a ready acceptance of it.

#### IV. TAXES ON CONSUMPTION.

§ 358. The taxation of wealth in the form of a tax on consumable wealth affords the transition to the important field of taxes on consumption (consumption taxes, taxes on expenditures). So long as we have to do with objects of the nature of durable wealth, the basis of an enduring utility (capital, consumable wealth), which are turned to use in their original form and not through the medium of an exchange in the market, so long, we have seen, is the "property tax" or the "direct tax on luxuries" the proper form of taxation. As soon as these utilities are thrown upon the market, as happens with the important class of rented houses, they lend themselves more readily to taxation on the basis of their market value. It is quite in accord with the general deliverance of experience on the subject

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of the relation of the value of the goods consumed in kind to the money value of the same goods, that it is only after the development of marketability in these utilities that the tax ("rental tax") assumes a form which has long been in use and has proved itself very practicable in other lines.

Something similar may be observed in the broader field of those consumption taxes the tax-object of which is not the usance of invested capital but objects of immediate use. It is true in this case even to a greater extent than in the case of productive capital that there are practical difficulties in the way of subjecting products consumed in kind to a consumption tax, whereas the same products if they are put on the market are extremely well adapted to a tax on consumption (tobacco, beer, wine, etc.). So true is this that it may even be said that the development of production for a market by the method of great centralized industrial establishments is to some extent necessary as a foundation for a highly developed and effective system of taxes on consumption (distilleries, breweries, beet-sugar factories).

§ 359. The fundamental principle of the tax on consumption is this, that it accepts the demand of the taxpayer for consumable goods as the standard by which to measure his ability to contribute to the public expenditures. The fact that a household consumes a given quantity of beer, wine, spirits, tobacco, tea, coffee, sugar, etc., is accepted as evidence that the same household is capable of rendering for public purposes a contribution proportioned in quantity (and if practicable in kind) to this consumption. This principle of consumption taxes is no more fundamentally opposed to the principle of equity in taxation than is a tax on earnings in any of its various forms. Nor are the difficulties which stand in the way of the application of this principle anything more than what every other form of taxation has to contend with, and in this case as in every other the chief problem is to bring the practical working of the tax continually more and

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more into conformity with the requirements of equity. It is to be remarked that it is the unavoidable shortcomings of every form of taxation that necessitate a mutual supplementing of these shortcomings, as it were a fitting together of salient and re-entrant angles. And it is true not only of the less manageable kinds of the taxes on earnings, those which by nature are necessarily more imperfect, but even of the relatively most perfect of them, the income tax, which has its defects, partly inherent in the nature of the tax, partly defects in its practical working; and these defects and shortcomings plainly point to the taxes on consumption as well adapted to supplement and correct them. Defects inherent in the nature of the tax are due to the fact that the method of ascertaining the income necessarily applies too inflexible a standard in measuring the tax-paying capacity, and so makes a more flexible, subsidiary standard desirable. The defects in its practical working are due to the obstacles which a "direct tax" encounters in the immature civic and economic sense of the majority, which gives an advantage to "indirect" forms of taxation that collect the amount of the tax in dribbles and in an inconspicuous way.

§ 360. The literary and social-political struggle against taxes on consumption ("indirect taxes") which has now been going on for two hundred years, turns out on closer examination to be directed not so much against the substance of this kind of taxation as against a special form of it which is at variance with the demands of equity. One of the greatest of the precursors of the Physiocrats in France, Vauban, who submitted to the king the radical scheme of tax reform of a universal *dîme* (1698) as a means of achieving an equitable distribution of the public burden, was willing to retain a number of taxes on consumption so far as they were not levied on necessities, and he even would have retained the salt tax in an improved form.<sup>1</sup>

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<sup>1</sup> *Projet d'une dîme royale. Économistes financiers du 18<sup>e</sup> siècle* (éd. Daire, 1843), p. 97.

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Every one of the later opponents of "indirect taxes"<sup>1</sup> (apart from those occupying very extreme positions on the theory of taxation, as for example the Physiocrats) opposes primarily the inequitable forms of taxes on consumption and the substantial injustice which results from these forms. No one has established that there is any necessary connection between this substantial injustice and the form of the consumption tax. Even in the discussion of the facts the emphasis is frequently thrown very decidedly upon the existing inequality in the most diverse forms of taxation; so that we find the famous modern opponent of indirect taxes - consciously or unconsciously - construing the *taille* as an indirect tax and so bringing it under Boisguillebert's condemnation.<sup>2</sup> But the struggle against indirect taxes is, further, closely connected with that unhistorical radicalism which was initiated and is typified by the Physiocrats. And in a qualified form, dissociated from the bold projects of the Physiocrats, this doctrinarian view of the matter has lasted on for a hundred years. It takes offense at this class of taxes, now because they hinder the freedom of trade, now because their cost of collection is high, now because they are inequitable as between taxpayers of different tax-paying ability, and always with an air that seems to assume there are other forms of taxes available which are ideally perfect in these respects; but when we come to examine these other kinds of taxes we find to our disappointment that their shortcomings, too, are very great. So that this carping criticism,

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<sup>1</sup> Cf. especially the numerous instances cited by Ferdinand Lassalle, *Die indirekte Steuer und die Lage der arbeitenden Klassen* (1863), pp. 14-54.

<sup>2</sup> Lassalle, p. 31: "Boisguillebert points out that the indirect taxes then in force in France, the *taille*, or the taxes resting on agriculture, the *aides*, or wine tax, and the duties .... render consumption impossible." In fact the *taille* was as thoroughly a "direct tax" as any tax is, and was most assuredly not an "indirect tax" in the sense in which that word is employed by Lassalle and in modern usage. But this tax was the most grievous burden of the French people; it made "consumption impossible," to use Boisguillebert's expression, not because it was a consumption tax, but because it left too little of the means for consumption. Henri Taine computes from documentary sources that the aggregate of the four direct taxes of which the *taille* was the chief amounted to 53 per cent. of the aggregate national income. - *Les origines de la France contemporaine* (1876), p. 543.

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in so far as it means anything, turns out to be nothing but an expression of that state- and-tax-abhorrent attitude whose ideal in the matter of taxation consists in the absence of all taxation.

§ 361. The office of the science in relation to taxes on consumption is the same as what we have found to be the office of financial science and of the theory of taxation in general; it is a dispassionate investigation and appreciation of the developments of the past and their causes on the one hand, and a shrewd guidance of their further development in the future in conformity with the principles of justice and expediency on the other.

There exists at present a relatively very general consensus, both in the theory and in the practice of finance, as to how this problem is to be solved. It is not thought possible, in the first place, to attain the desired equitable taxation by taxes on consumption alone; in the second place it is further recognized that taxes on consumption are a necessary constituent of every modern system of taxation; third, matters of detail in consumption taxes are considered open questions, both with respect to their expediency and with respect to their justice.

The problem is greatly simplified by the attainment of such a unanimity in the dominant views of the matter. We have hereby reached a position with respect to the problem from which it is possible to initiate a reconciliation of the historic tax systems with the ideal tax system of the future.

That we have already found to be true with respect to taxes and financial matters generally and with respect to the state as a whole, repeats itself within the field of the consumption taxes; all historical development is gradual and precarious; the less perfect is gradually replaced by the more perfect; but the rate of this approach towards perfection must always continue to be slow and very modest, for the decisive factors in the progress, the psychological elements involved, are incapable of a development by leaps and bounds.



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§ 362. If we look into the nature of the taxes on consumption with a view to ascertaining their office in the fiscal system we shall find that it is as follows:<sup>1</sup>

The point from which we must approach the question is the amount of the public expenditure, or of that portion of it which it is thought proper to cover by means of taxes on consumption.

The second step is duly to consider, in connection with, this first point, what is the kind and quantity of the different items that go to make up the actual expenditure and consumption of the economic units comprised in the system with which we have to do. As has been pointed out in the preliminary discussion, in treating of the evolution of demand (vol. i. secs. 187-212), we have here to do with a question of historical growth, varying with the time and the people in question and with the plane of culture attained by the society as a whole, as well as from one stratum of society to another. The problem is to get a correct appreciation of this diversity and of the proper significance of each particular branch of consumption and of each particular object of consumption in the community which is to be laid under contribution; and also to appreciate the true significance of these relatively to the aggregate demand of the community as a whole and to that of the various classes of the community.

Even within the circle of the modern civilized countries of Europe and within the brief space of time comprised in the present century we meet with appreciable alterations in the character of the aggregate consumption and considerable variations from one people to another. This fact is especially obvious as regards the articles commonly subjected to a consumption tax, more particularly the great variety of stimulating beverages in use at present. It is not only that coffee and tea are products introduced into our consumption from abroad; which have only gradually and to a great extent not until the present century replaced certain domestic products; it is also true that they have penetrated the daily life of the different countries of Europe in

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<sup>1</sup> Cf. G. Hanssen, "Die Normirung der Eingangszölle aus dem rein finanziellen Gesichtspunkte." *Zeitschrift für die ges. Staatsw.*, 1855.

very different degrees and play a very different part in their aggregate consumption. Tea has become the popular beverage most generally consumed in England, while in Germany (apart from certain sections of the northwest it is chiefly a luxury of the upper classes. On the other hand, coffee is the popular drink of Germany and has gradually more and more driven the national meal or milk porridge from the field, while in England coffee is properly to be considered a luxury.<sup>1</sup> The consumption of tea during the last generation has increased in England just as steadily as that of coffee in Germany. The consumption of coffee has constantly declined in England, while the consumption of tea in Germany has increased but very slightly, and the moderate increase which has taken place, as shown by the figures cited in the note, is in part due to the accession of new tea-drinking countries lying outside the limits of the old Zollverein.

Spirituous beverages (beer, wine, brandy) have a very different importance for different countries and localities, according to the varying circumstances of climate and culture. In the wine countries wine is the staple popular beverage; so, for example, in the Rhine country in the wine-producing cantons of Switzerland, in the corresponding sections of France, Italy, Spain, etc. It is only under circumstances of exceptional indigence that its place is taken by cider and the like. Whereas in countries where wine is not produced, where no wine is consumed except what is imported from abroad, wine is the drink of well-

<sup>1</sup> The consumption per capita of the population in the United Kingdom was (*Statistical Abstracts for the United Kingdom, 1868-1888*):

Year	Tea, lbs.	Coffee, lbs.
1853	2.14	1.34
1867	3.68	1.04
1880	4.57	.92
1887	4.95	.79

The consumption in the Zollverein per capita was (*Statistisches Jahrbuch für das deutsche Reich, 1886, p. 158, and Hanssen, loc. cit. p. 64*):

Year	Tea	Coffee
1853	.02	3.
1867	.04	4.
1880	.06	4.66
1885	.06	5.

to-do people and is not generally used as an everyday beverage even by them. accordingly, in such countries beer is the article generally consumed, and latterly, in consequence of improvements in processes and the product, the consumption of beer is becoming extremely common.<sup>1</sup> The extended use of distilled liquors is often due to the same causes which hinder the general consumption of other spirituous beverages. The distilled liquor being the cheapest is consumed by the poorer classes of the people in proportion as the more expensive beverages are beyond their reach, at the same time that lack of proper nutriment and the rigors of the climate make brandy a desirable means of keeping warm. Hence we find a much greater consumption of spirits in the more northerly and poorer localities than in the more southerly and wealthier; frequently in adjacent territories there may be no consumption of spirits at all in a wine-producing locality on the one hand and a very great consumption in a neighboring mountainous district.

The facts about the consumption of tobacco in modern countries are of much the same kind. But the facts of tobacco consumption as they are today are the result of a recent historical growth, and the figures afforded by the accounts of the French tobacco monopoly which have been reviewed above (sec. 288) are an evidence and an approximately reliable index. of the change, the receipts having increased during the years 1815-1887 from 32 million to 320 million francs.

§ 363. These examples (which, as will presently appear, are of great practical significance for any application of a system of consumption taxes have served to show that a demand for a particular class of consumable goods may vary greatly according to time, place and people, and they serve also to show what far-reaching consequences this relativity of demand has for the question of taxes on consumption.

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<sup>1</sup> In Great Britain and Ireland the per capita consumption in 1887 was 27 gallons = 122 litres (the consumption in the German Empire in 1884-85 being 90 litres of beer), whereas the consumption of wine was only .37 gallon, having been .25 gallon in 1853.

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The question as to the relation between the public demand and the various directions taken by private demand, such as comes up for consideration in all taxes on consumption, means in the last analysis a question as to the limitations which the public consumption imposes on the various directions of private consumption. The pressure exerted by the tax will, of course, vary according to the degree of importance which the article taxed assumes in the aggregate consumption of the tax-paying household. Articles of necessity will be more sensitive to the pressure of the public burden than the less necessary or superfluous articles. And, conversely, this latter class will develop an elasticity in the adaptation of private consumption to the enhanced cost of the articles subject to the tax, such as the articles of necessary consumption will not admit of.

Consequently the urgency of the public need will, on the one hand, have to decide how far the imposition of taxes on the necessities of life is to be carried, while by a painstaking adjustment of the taxes on consumption on the other hand the pressure of the tax is sought to be kept within bounds.

It is, however, an exaggeration, which is readily explicable as an outgrowth of historical events, to condemn all and every taxation of articles of necessary consumption. It is true that this particular class of taxes on consumption falls short in point of that flexibility and spontaneous adaptation of private consumption to the pressure of the public burden which constitutes the great advantage of consumption taxes generally as contrasted with taxes of other kinds; the decrease of the consumption of salt or of bread can never be taken into consideration as a factor of any consequence in the employment of consumption taxes. And still it is quite conceivable, and it is borne out by the very latest events, that a tax on necessities may be justly and expediently imposed in place of many another less feasible form of taxation; so it may be noticed that quite recently (see sec. 287) the assembled populace of the country district of Glarus decided to retain the salt tax.

The point not to be lost sight of is not the avoidance of all

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taxation on necessary consumption, but the proper relation of this taxation to the rest of the taxes on consumption and to the general tax system; it is this relative weight of consumption taxes that has so frequently suffered an abnormal and offensive development in the past.

§ 364. This brings us to the point of view of that social equity which is to be maintained between the various classes of society.

Since consumption taxes are always levied on the articles of consumption and not on the persons of the consumers, they can make no distinction between the salt which serves the necessity of the poor man and the salt on the table of the rich. It is, therefore, the article of consumption simply as such, taken with a view to its importance to the various classes of society, with which the tax policy has to do and which affords the norm in the imposition of consumption taxes. Let us imagine a social pyramid in which the most necessary and therefore the most extended wants constitute the lowest strata, while the nearer we approach the apex the more dispensable are the articles and therefore the less extended the want of them. Every taxation of the lowest and broadest strata of this pyramid of wants is pre-eminently a taxation of the lowest strata of society; the higher we ascend the more does the taxation fall upon the more well-to-do classes. The advantage of a taxation of necessary consumption lies, therefore, in the great number of persons liable to it and the consequent great relative productivity of such a tax; but there is also bound up with this fact the danger of throwing too much of a burden upon the slight tax-paying capacity which manifests itself in the consumption of the necessities of life. On the other hand those consumption taxes which fall only upon the apex of our pyramid are quite sure to touch only the most dispensable objects of consumption and the wealthiest consumers; but they are for this reason also open to the objection that they fall upon a very limited number of taxpayers and have at the same time to make allowance for the

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possible shrinkage of the taxable consumption which may result from the enhancement of the price of the articles taxed.

This contrast between the two classes of consumption taxes not only indicates the point of view for practical tax legislation in the present and future; it also serves to explain the historical evolution of taxes on consumption in the past. The slighter the degree of wealth, and therefore the narrower the range of consumption, of the masses of the people, the more is the consumption tax constrained to fall back upon the broad lower strata of the necessary wants. Hence it may happen that a friend of the people, like Vauban, may favor the retention of the salt tax and may wish to derive a revenue of 24 million livres from it in a country such as France was two hundred years ago. The development of the consumption tax in this direction finds support in the relative absence of any lively sentiment of social equity, the state being primarily concerned about the amount of the tax and only secondarily about the manner in which it is to be borne.

As the people advance in wealth and in a sense of social equity all this is changed. The acquisition of wealth leads to an extension of the consumption of dispensable articles, so as to include a larger portion of the taxpayers, There results the much to-be-desired but hitherto missing coincidence of a dispensable and a widely extended consumption; the tax in such a case falls upon a great number of households, but without pressing heavily upon them. But at the same time there comes into the foreground an enhanced sense of the justice of distributing the burden of taxation among the different classes of society. Even where the economic development seconds the fiscal productivity of the tax and affords an abundant revenue, this fact alone is not sufficient to meet all requirements; the further question then comes up whether the distribution of the burden is what it should be - whether the lower classes are not disproportionate if taxed. It is only after having reached a lively appreciation of the cogency of these considerations that we are fairly prepared to face the objections which are brought forward against "indirect taxes" as such.

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§ 365. Taxes on consumption will accordingly have to be arranged with a view to bringing the state's requirement of a productive tax more and more into accord with the requirements of justice. An effort is to be made to achieve this end within the field of consumption taxes alone; but so far as this end may prove unattainable - in consequence of the difficulties alluded to above in the way of a taxation of the upper strata of the social pyramid - recourse must be had to proper supplementary taxes of other kinds.

A well-constructed system of taxes on consumption is a financial work of art. Its purpose is to bring the great variety of wants which are met with in any modern civilized country within the lines of the tax legislation in such a manner that the portion of the taxes payable by each individual household shall represent a variegated mosaic, in which the harmonious blending of the colors is represented by the rate of taxation and the surface of the individual blocks by the volume of the consumption on which the tax is levied. This work of art is imperfect in the degree in which glaring contrasts occur between the burdens imposed on different articles of consumption and in the degree in which the system of taxation is of a one-sided character.

To illustrate what is meant we may select an example of great importance from existing tax legislation, viz., the system of consumption taxes in force in Great Britain and Ireland.

The aggregate taxes of the state (for the fiscal year ending March 31, 1888) amount to nearly £80,000,000.<sup>1</sup> Of this sum consumption taxes of various kinds yield some £45,000,000. This latter amount is made up of £20,000,000 from customs and £25,000,000 from excise. Of this, £17,250,000 is derived from spirits (£13,000,000 from the excise and £4,250,000 from import duties); further, £8,750,000 from beer and the same from tobacco. That is to say, £35,000,000, or nearly one-half of the entire revenue of the state, is derived from spirits, beer and tobacco, the burden, therefore, falling in a strikingly one-sided manner on the great mass of relatively dispensable articles of

<sup>1</sup> *Statistical Abstract for the United Kingdom, 1873-1887*, pp. 9, 16.

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consumption. This one-sidedness which taxes the majority of the population for the benefit of that portion which does not smoke or drink, has no adequate counterpoise within the British system of consumption taxes. The 3.50 million pounds paid for licenses also falls chiefly upon the same class (liquor licenses and the like). The 4.66 million pounds derived from the tea duty (6d. per pound) falls in great measure upon the general body of the people and constitutes a very inadequate and unsatisfactory counterpoise to this one-sidedness. We have, therefore, left only the receipts from the duty on wine, amounting to one million, and the approximately equal amount derived from the duty on coffee, fruits, spices, etc., making together about £2,000,000; this may to some extent be assumed to constitute a compensatory burden imposed on the wealthier classes, but it is to be remarked that only one-half of it falls on persons who do not drink.

The British system of consumption taxes accordingly proves to be a bit of consumption taxation in which the very realistic requirement of fiscal productivity is satisfied while the requirement of equity is lost sight of. It marks a stage in the development which presents a finished and typical system only to the superficial glance, while in reality it calls for further development and improvement of a qualitative kind. As compared with earlier systems of taxation, the British system, it is true, gives evidence of the pleasing fact of great and widely distributed wealth and a corresponding distribution of consumption, but this relatively high development must not blind us to the shortcomings of the system as it stands, or to the further advance still necessary to be made.

These further improvements yet to be made lie in the direction of an increase of the scope and number of taxable articles, and a more adequate equalization of the burden by further special taxation of the upper classes. Either these objects will be accomplished more and more completely as time goes on, or the system of consumption taxes must yield the ground to other forms of taxation which are capable of meeting these requirements.



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It is the tendency of the present realistic age to thrust these duties that are concerned with the attainment of equity into the background. The science would fail of its highest duty if it did not oppose this realistic tendency by calling attention all the more persistently to the unalterable goal of advance and improvement in this field.

§ 366. In order to a proper appreciation of the realistic and the idealistic aspects of taxes on consumption it is necessary to occupy a point of view which has so far not been adverted to and which we shall now have to discuss, viz., that of the practical limitations of taxes on consumption.

It would, however, be unjust to the British system of consumption taxes to disregard the many and urgent reasons of expediency which have led to its adoption and the repeated experiences which have led to the substitution of this particular system for a different one which was, in itself considered, more in accord with the requirements of equity.

It is regarded as a chief advantage of taxes on consumption that they are levied in an imperceptible manner, drop by drop; but this presupposes that by the provisions of the law the tax is collected upon the taxable articles in a mass at a point of time when these articles are aggregated together in great quantities. The assumed advantage would entirely disappear if this supposition did not hold, if it were necessary to collect the tax separately on each minute item of the articles taxed.

The practical question involved in taxes on consumption therefore reduces itself to the question whether articles of consumption which commend themselves for taxation on general grounds of equity present any such convenient stages of concentration as the collection of the tax requires, and which articles of consumption are in this respect the best adapted to the tax.

Experience answers the former question in not a few cases in the negative. It may happen that the tax legislation of the German Empire imposes a tax of ten marks per kilogram on silks imported

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from abroad, and of twelve marks per kilogram on ready-made garments under the same circumstances, while it lays no tax on the same quality of silks or garments of home production. Now, looking at the matter from the standpoint of equity it may readily be admitted that the consumption of foreign silks and of foreign garments ordinarily indicates a greater degree of luxury than the consumption of similar home products; still the sense of equity finds it hard to reconcile itself to so radical a distinction as that the one case should be taxed at a high rate and the other not at all. And in point of fact the decisive ground for avoiding the taxation of this class of objects by any other than the one convenient method of an import duty is not the equity of the case, but simply the practical expediency of this method of obtaining the tax.

To cite another example. The consumption of the better grades of wine is habitually accepted as an indication of wealth and luxury; justice would therefore require that this consumption should be subjected to an adequate, and by no means inconsiderable tax. Still, the wine tax as it stands, and as it was in Prussia (sec. 273) from 1819 to 1868, makes not the slightest distinction between the poorest product and the "Schloss Johannisberger" or the "Steinberger Kabinet;" on the contrary, it taxes all wine alike and at an extremely low rate; and it is to be added that the great annoyances and expenses connected with the collection of the tax, taken together with the very slight revenue derived from it, has led to the entire abolition of this tax. The consumption of the best and most expensive wine produced at home is therefore entirely untaxed in the German Empire, whereas the poorest wine imported from abroad bears an import duty of 24 marks per hundred kilograms (48 marks if in bottles).

In both the cases which we have cited as illustrations, it is the fact of a practical advantage offered by the tariff boundary, where the taxable articles of consumption can be dealt with in quantity, which has decided that the tax is to be imposed upon an article on its importation; while it is exempt from any consumption tax in case it is produced within the country, where

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such a practical advantage for the collection of the tax is absent; and this in spite of the fact that justice would require, if not an equal, at least a similar tax in both cases.

§ 367. What has here been brought before our minds in the sheer contrast between taxation or no taxation, according as the practical circumstances do or do not admit of the imposition of a consumption tax, comes up again in a great number of cases as a difference of degree in the extent to which the exigencies of practical life favor the imposition of such a tax.

We have already conceived of the tariff boundary as being, for the purpose in hand, simply a convenient place for levying taxes on consumption, - convenient as contrasted with the method of taxing consumption within the country. This idea is, however, to be qualified by the consideration that the practical value of the tariff boundary of different countries for this purpose differs widely.

The political boundary of a state such as the Prussian state once was, whose king was styled the King of Frontiers, is, of course, for the levying of taxes as for every other purpose, much less advantageous than the frontier of a well-rounded domain which comprises the greatest possible area and population within the shortest possible tariff boundary. A wooded or mountainous frontier, offering convenient hiding places for smugglers, is less well adapted for a tariff boundary than the seacoasts of England.

The evolution of the tariff system will accordingly in all cases be influenced by circumstances of this kind; while a developing tariff system at the same time will seek to alter these conditions and adapt them to its purposes (e.g. the Zollverein). Historical events as well as natural conditions may influence the development of the tariff boundary, and in the more fortunate cases the course of historical development may even modify the natural disadvantages of the tariff boundary, as, e.g., by means of a political or tariff union which removes the former disadvantageous tariff boundary to a point within the resultant new tariff territory.

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Conversely, the course of historical development may affect the tariff system unfavorably, as, e.g., the ascendancy of free-trade ideas or a solicitude for the international trade may prevent or limit the imposition of import duties which might be commendable on fiscal grounds. The one-sidedness of the English tariff which has been referred to above has its origin for the most part in the principle of freedom of international trade which has been in the ascendant in that country for a generation past. This principle has been violated by the imposition of import duties only to the least possible extent; the exceptions have been scarcely anything but taxes on narcotics, which would for the most part leave trade relations with the more important foreign countries unaltered. The earlier tariffs of England and the existing tariffs of the German Empire, Austria, Switzerland, France, the United States of America, etc., are not liable to this one-sidedness in their consumption taxes, so far as concerns any necessary consequence of the practical exigencies of a system of import duties; these countries have not only not applied the principle of free trade after the radical fashion of England, but have even systematically made use of their import tariff to hinder free trade. Still, even these countries, as the development of modern industry makes them more and more dependent on the world market, will find themselves obliged by their mutual interest to forego the levying of many fiscal duties which might commend themselves on all other grounds. For example, the Swiss import duty on French wines remains extremely low although the Swiss Confederation has increased the rate on many other items in its tariff, the reason being simply the pressure which France has exerted in the negotiation of treaties and the danger there would be to the graver interests of international relations, and the danger of a disturbance of trade relations with France.

§ 368. In the domain of internal taxes on consumption, as in that of import duties, the problem is to discover certain points or stations where the consumable goods in question may

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be dealt with collectively or in a wholesale way; and the absence of any feasible stations of this kind makes a great number of consumption taxes practically impossible though they might be desirable on other grounds.

Viewed from the standpoint of equity, simply, it is an incomprehensible inconsistency that the consumption of domestic wine in Prussia is exempt from taxation while the consumption of domestic beer and spirits bears a considerable tax. This incongruity is only to be explained (but it is also sufficiently justified by the fact that it has been found by experience that the practical obstacles to a taxation of domestic wine make such taxation inexpedient, while the taxation of beer and spirits has progressively developed in consequence of the progressive centralization and consolidation of the production of these goods.<sup>1</sup>

So far as this concentration is absent the practical advantages favoring an internal consumption tax are also absent. The system of taxation habitually employed in wine-producing countries, which makes use of the place of sale as a medium by which to collect the tax, is so burdensome to the business that there is properly a great hesitation about introducing this form of taxation in any place where it has not already long been established. The decentralized character of tobacco culture is of the nature of a downright calamity so far as regards the taxation of homegrown tobacco, and it is only on the ground of other considerations which speak so strongly for the eminent propriety of a tax on tobacco, that such a tax is collected in spite of the serious practical difficulties connected with it. Viewed from the standpoint of the tobacco tax England occupies a very enviable posi-

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<sup>1</sup> Within the territory covered by the Imperial tax system there were in 1872 2216 potato distilleries paying each less than 6000 marks in yearly taxes; in 1886, there were only 1664. On the other hand the very large distilleries which pay more than 12,000 marks each in taxes have increased in number during the same period from 986 to 1836 (*Conrad's Jahrbücher*, N. F., 1887, vol. xv. p. 6). Of breweries there were in the territory comprised in the tax system in 1872 an aggregate of 14,157, with an aggregate product of 16.1 million hektolitres; whereas in 1884-85 there were only 10,520 breweries, with an aggregate product of 24.6 million hektolitres (*Statistisches Jahrbuch für das deutsche Reich*, 1886, p. 58). For beet-sugar factories, see sec. 274 above.

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tion, because it has no home-grown tobacco to tax, but is able to tax the entire tobacco supply of its population at the tariff boundary.

§ 369. An artificial concentration of the production of domestic products may be specially created as an expedient for the levying of an internal tax on consumption. This is the principle embodied in so-called tax monopolies.

The extreme subdivision of the tobacco culture into an enormous number of very small establishments makes the taxation of this industry just as difficult as the taxation of the greatly subdivided industry of tobacco manufacture (household industry and the like). The tax on the consumption of tobacco, instead of collecting the amount required from the still more extremely subdivided business of the retail trade, or from the consumers in person, goes directly to the establishment where the tobacco is grown or where it is manufactured; but even in so doing it imposes the burden upon many shoulders, and the majority of them feeble ones which are not well able to bear it although it is but a single item of expenditure. This subdivision of the tax collection is as burdensome to the government as it is to the taxpayers. The measures of supervision required for the purposes of the tax are as annoying to the taxpayers as they are troublesome and odious to the officials. If the culture and manufacture of tobacco were consolidated to the same degree as the beet-sugar industry the chief difficulties of an internal consumption tax would be removed. But where this consolidation does not result from the free development of the industry the state may interfere and bring about a compulsory concentration.

This is the fundamental principle of the tax monopoly. As an illustrious example of a tax monopoly we have already (sec. 288) given a brief review of the history of the French tobacco monopoly.

Where a tax monopoly has been introduced early and has become incorporated in the habits of thought of the people, there are but slight traces perceptible of those difficulties which

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are so apparent in cases where the requisite concentration of the industry is sought to be introduced at a later stage - to replace a widely extended and subdivided production by private enterprise. The obstacles are partly the economic and financial difficulties of a change from the old method of production to the new, partly the opposition to and prejudices against a monopoly bred by long-continued freedom of the business. These obstacles can be overcome only under the pressure of very great financial straits or through a great advance in popular insight and intelligence.

§ 370. There are a few taxes on consumption which find the state monopoly ready to their hand, established for other purposes than that of taxation.

One of the chief instances of this is the Post. In this case a consolidated single establishment and centralized management follows from the practical requirements of this means of communication. Any surplus receipts that may result (and there is certainly occasion and inducement to derive a real surplus revenue from this source, such as is obtained in Great Britain, and not an apparent surplus only, such as we have at present in the German Empire) have not hitherto been clearly recognized as being of the nature of taxes, for the reason that the postal monopoly rests on other than fiscal grounds. But it is none the less true that apart from its other purposes this monopoly also serves the purpose of taxation so far as it affords a real net revenue.

Also the lottery monopoly (which in any modern tax system has to be counted with not as something that ought to be comprised in the system but simply as an empirical fact) is of course a tax monopoly to the extent that it would not exist at all except for the purpose of taxing (human folly). At the same time it is distinguished from other tax monopolies by the fact that it has been established not for the purpose of taxation alone but also for the sake of obviating the more deplorable effects that would follow from a "free play of natural forces."

§ 371. In the last few paragraphs we have discussed the practical limitations and obstacles to taxes on consumption and the means of overcoming them. It is now to be added that there are also inducements on other than fiscal grounds which may urge to the taxation of articles of consumption.

Such other grounds are the suppression of the use of an article which is regarded as hurtful, and the exclusion of foreign articles of import as a protection to the domestic products.

As is the case with so much of what the institutions of the seventeenth and eighteenth centuries have handed down to modern times, so also the policy of prohibiting a luxury - which was then sold by the state for fiscal purposes as a means of taxation<sup>1</sup> (sec. 57) - was already well known in the mediæval towns. Such is the origin of many consumption taxes which are extensively used at present; such, e.g., is the case with the taxation of tobacco, which, however, does not retain this character in any of the modern states. On the other hand there is even today a motive of this kind present in the taxation of spirits, and this motive has also been influential in bringing about the latest increase of the brandy tax in the German Empire (June 24, 1887), being acknowledged by the government to be one of the reasons which influenced its action. If the fiscal purpose and the pedagogical purpose of the consumption tax could be made to go hand in hand we should have a charming harmony of interests. But it is plain that these two purposes logically traverse one another, and that it is only under very special circumstances that they mutually further one another. The pedagogical purpose, whose aim is the restriction of the consumption of a given article through the interference of the state, will of course tend to diminish the quantity of the article

<sup>1</sup> Quod si quis est qui scire de me velit, quodnam genus vectigalium immortalī Deo gratissimum, civitatibus pulcherrimum, principibus honestissimum, plebi utilissimum videatur, illud est quod iis rebus imponitur quae ad corrumpendos civium mores, quae ad delicias, quae ad luxum, quae ad libidinem spectant .... quae prohibenda non sunt, nec, si velis, possis .... Quamobrem principes qui Aquiloniis regionibus imperant, nullum vectigal majus habent quam ex vino, quo subditi, ut carere possint, nolint tamen, sed assidue locis omnibus sese ingurgitabunt semper.- Bodini, *de Republica, lib. VI*, p. 661 (ed. Paris, 1586).



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liable to the tax; the fiscal purpose, apart from fiscal considerations with which we are not at present concerned, does at least not aim at this result. If we succeed, by means of increased rates, in obtaining an increased revenue from the tax in spite of a diminished consumption of the article, that of course does not prove that it would be impossible to obtain a still greater aggregate revenue by lowering the rates.

The presence of this foreign purpose in the imposition of the tax accordingly acts as an inherent limit to the taxation of consumption at the same time that it may furnish an extraneous motive to the imposition of the tax.

Something similar occurs when an import duty is levied as a measure of protection for the home product.<sup>1</sup> The duty may be intended, by its creator to serve this purpose, or it may accomplish the purpose independently of, or contrary to the intention of the legislator. It is only in the case of such articles of consumption as cannot be produced at home that the duty is only a tax. The simplicity of the English tariff is largely made possible by the fact that neither tobacco, wine (and formerly sugar) nor tea, coffee or other like articles are produced in the country. The protective character of the English duties can come into play only indirectly by affecting the home-produced substitutes for the taxed articles.

The more effectively a protective duty serves its purpose, or the more a duty is intended for protection, the less is its financial importance. On the other hand, the more completely the duty is made to serve the purpose of a tax, or the less it acts as a protective duty, the less effective will it be as a protective measure for the home industry.

The term "mixed duties" has lately been used officials to designate import duties which are intended, or at any rate serve, to effect both these purposes.

§ 372. This examination of the practical limitations both

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<sup>1</sup> Depuis Colbert, dit l'abbé Galiani, on distingue entre l'impôt de profit et l'impôt d'encouragement. - Le Trosne, *De l'intérêt social (Physiocrates*, éd. Daire, vol. ii. p. 985).

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external and internal on the taxation of consumption serves to show not only that such a system of taxation is in need of continued development and improvement in order to overcome its peculiar difficulties and to meet the requirements made upon it; it also points to the necessity of supplementing any system of consumption taxes by taxes of other kinds.

The one-sidedness which so persistently attaches to a system of consumption taxes, and which can scarcely be entirely removed by the development and perfecting of such a system, suggests a recourse to supplementary taxes of another kind in the interest of equity.

The difficulty, or rather impossibility, of levying on the greater tax-paying capacities in due proportion by means of a taxation of the peculiar goods consumed by them, especially where there is a steadily increasing need of revenue coupled with a progressively deepening conviction of the greater obligation properly incumbent on the greater tax-paying capacity, - these considerations lead to the adoption of taxes which are essentially of the nature of taxes on earnings (income, property, inheritance and objective taxes).

Even the relative advantages attaching to taxes on consumption have their reverse aspect. The flexibility of all those consumption taxes which are levied on articles of voluntary consumption has the consequence that it is impossible to secure a definite and stable revenue by this means alone, because the volume of consumption will vary under the pressure of the tax. Recourse must therefore be had to taxes which are less flexible and which can therefore better be depended on.

The relative, unobtrusiveness of the tax on consumption is also of great practical importance for any system of taxation, and, in spite of all the protests of the radicals and the doctrinaires, it will continue to be so for a long time to come; for the question of the burden of taxation is largely a question of subjective appreciation of the pressure of the tax, or at any rate it does not depend on the amount of the tax alone. At the same time it is also to be recognized that the aim of any modern pro-

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gressive tax policy comprises also such a moral development on the part of the people as shall alter the popular sentiment on this head and bring it into conformity with that ideal of civic virtue which must not be condemned as a piece of folly merely because it would be premature to apply it unreservedly in the systems of taxation in vogue today.

## CHAPTER V. TAX ADMINISTRATION.

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### I. ADMINISTRATION OF THE TAX SYSTEM BY NATIONAL AND BY LOCAL AUTHORITIES.

§ 373. The dependence of the different kinds of taxes on the conditions of their administration, on the circumstances which condition the ascertainment of the object on which the tax is levied and the collection of the taxes, has come into view in the course of the foregoing reviews of the historical development, as well as in the theoretical discussion of the taxes. The purpose of the present chapter is to make a survey of the points bearing on this subject.

As a preliminary point of a general character there is something to be said on the relation of national administration of the taxes to administration by the organs of local self-government.

Something has already been said (secs. 135-148) of self-government and of its general relation to the state. The discus-

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sion was there concerned with the position of local self-government as an intermediary between the centralized national administration and that class of services which are voluntarily rendered to the commonwealth, the question being as to the scope and significance of local self-government in this its most general character, for the finances of state and commune. We have now to do with that special phase of local self-government which is concerned with the administration of taxes, - with the special problems which arise out of the mutual interference between the national administration of taxes and administration by local self-government. The problems which are to be worked out by the central authority and its organs or by the organs of local self-government have received some consideration in the course of the more general discussion. The means at the disposal of both of these two kinds of organs for carrying the tax legislation into effect, as well as the limitations of each and their relation to one another, are properly to be taken up at this point.

The general principle of self-government of course reappears in this phase of self-government. In one case as in the other its chief purpose is an intermediation between the coercion embodied in the decrees of the central government and the spontaneous inclination of the citizens to perform their public duty. In the one case as in the other some attention is to be given to the difficulties in the way of such an intermediation and the consequent necessity of supporting the local administration by the more effective machinery of the central authority.

The great advocates of local self-government, such as Freiherr von Stein, do not appear to have stated the difficulties and discrepancies inherent in the problem with sufficient clearness in all cases, at the same time that they have very forcibly described these same difficulties and discrepancies as occasion has arisen. The same Stein who is eager to tear down the *Formenkram und Dienstmechanismus* of the professional officials by "bringing in men from the turmoil of practical life" and to replace this method by "*einen aus der Fülle der Natur genommenen Reichthum von Ansichten*"

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*und Gefühlen,"* who "is quite unable to comprehend why the burgomaster may not be engaged in business,"<sup>1</sup> - this same great statesman, on occasion of the Prussian finance reform of 1810, when he very strongly advocated the income tax as the fairest, most equal and most productive of all taxes, condemns in the harshest terms the public opinion then prevalent in Prussia, and characterizes it as an ingrained egoism and as "northern license and barbarity, which ought to be corrected by the application of the severest penalties, and not led still further astray by indulgence."<sup>2</sup>

It is quite evident that he is speaking of the same people from two very different points of view, or in two very different frames of mind. It is the office of the science, of disinterested thought, to seek out the unity which underlies the contradictions due to the shifting tendencies of life and the shifting moods of our statesmen.

§ 374. So long as the have not reached a clear comprehension of the questions of principle involved, a discussion of the questions of practical administration, which by preference centers about the system of direct taxes (income, property and produce taxes), will lead to an infinity of delusion and self-deception regarding the importance of the form of these institutions as contrasted with their substantial content; whereas the latter alone is of any decisive importance.

If there is any law which suffers from the eternal contradiction that affects so many of our laws, - of attempting, under sanction of public compulsion, to command something which will not be performed voluntarily, while still obliged to recognize that compulsion alone is no adequate substitute for voluntary inclination, - if this is the case with any law it is eminently the case with the tax laws. The tax law owes its origin to the necessity of formally demanding from the members of the community the pecuniary sacrifices required to carry on the public business when

<sup>1</sup> Ernst Meier, *Die Reform der Verwaltungsorganisation*, pp. 142, 330.

<sup>2</sup> Cf. sec. 312 above.

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the indispensability of these sacrifices is for the most part not appreciated by the taxpayers, who are therefore habitually unwilling to render such sacrifices except on formal requisition and under public coercion. Since, in point of fact, the taxpayers have no other spontaneous feeling in the matter than a disinclination to comply, the tax law is very speedily brought face to face with the impossibility of making the letter of its provisions a living fact. This sheer contradiction between the injunctions of the law and the disinclination to comply with them of course does not occur in the public life of any modern civilized people. The old question, "*quid leges sine moribus?*" is to be taken everywhere, at least in some degree, in the conciliatory sense which it fundamentally implies-that no law can become an actuality which, not being based on the morals, habits and free inclination of the people, attempts, by means of public coercion, to advance but a single step further than the majority is inclined to go, - which seeks to exert a pressure that shall carry the movement beyond the point of everyday habit and in the direction of some ulterior moral aim.

But in view of the force with which the modern state, with its ever-increasing demands and its social-political and fiscal ideals, pushes its legislation forward on this line of tax policy, there is always danger that the aim of the law may be in advance of the inclination of the citizens on a point of extreme sensitiveness - the point of their pecuniary interests.

The idea that at this point, as at so many others, what is, may, by the aid of the organs of self-government alone be brought into accord with what should be, carries an attractive and, abstractly considered, a valuable suggestion. The reasons, which in other connections are urged in favor of a recourse to this means are in this particular case reinforced by the practical advantage of an intimate acquaintance with the affairs of the neighborhood, which is available to this method as contrasted with the employment of professional officials of the central government. In the case of other functions undertaken by local self-government (jury service, justices of the peace) the contrary is nearer being true with

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respect to the practical advantages of taking the functionaries from the immediate neighborhood.

Still, as has already appeared in the course of the historical comparison between the Prussian administration of the income tax by local self-government and the English methods of local self-government, a very great deal depends on the form which this idea takes.

Just as it is a mistake to believe that the unhampered activity of industrial society, or of self-interest, means the same thing as a true self-government, so it is also true that that must be a very undeveloped self-government in which the everyday views and ideas of the neighborhood are called into activity in the service of the public without the requirement of any training or habituation whatever to the duties of offices.<sup>1</sup> If sufficient time is allowed them, the better fitted members of the community will, by habituation to office, presently acquire the moral and intellectual qualifications necessary for its administration. If the jury panel were a perpetual or relatively permanent office to be administered by the citizen, it would gradually raise the jurymen above the narrow range of ideas belonging to his business, and bring his concepts up to the level of the national administration of justice, - the peasant would be less lenient towards perjury and the burgher would be less lenient towards dishonesty. But where the self-interest which dominates the everyday life of the business man stands in sheer contradiction to the duties of office, as happens in the case of the administration of taxes by local self-government, even permanency of office and habituation to its duties will not avail to raise the individual to a full sense of his public duty. What is needed in such a case is a complex artificial mechanism whose efficiency depends on the fact that it

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<sup>1</sup> It is therefore quite intelligible that in any country where the habit of participation in public affairs is extinguished or has not been developed, we also find that the difficulties in the way of those forms of taxation that require such participation are extremely great; as, for example, in the France of today, as testified by French authorities, Montesquieu characterizes this state of things when he says (*De l'esprit des lois*, bk. vi. chap. viii.): "Dans les lois de Platon, ceux qui négligent d'avertir les magistrats ou de leur donner du secours, doivent être punis; cela ne conviendrait point aujourd'hui; la partie publique veille pour les citoyens; elle agit, et ils sont tranquilles."



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comprises a great number of psychological elements which are bound up together and mutually supplement one another; whereas a one-sided load imposed upon any one of these various elements would bring but an inconsiderable result.

§ 375. We have now to examine the sequence and gradation of these elements in the light of the institutions which the history of taxation offers, proceeding in order from the individual to the central authority.

At the lower end of the scale, but one remove from the spontaneous contributions by the individuals to public expenditures, we have the method of secret [*stillschweigende*] self-assessment handed down to us from the Middle Ages, - a bit of voluntarism incorporated into the public law, and hence invariably a rudimentary contrivance which is set aside in favor of more effective contrivances that face the necessity of public coercion more frankly. According to this method everything is left to the inclination and the conscience of the individual; he is in no fear of coercion; the letter of the law and his own sense of duty are the sole deciding factors. Accordingly, the largest demands on this sense of duty as well as its most satisfactory practical application are to be found under the circumstances offered by a diminutive commonwealth, where the relations between the individual and the whole are close, the sense of community highly developed, the habituation to a close attachment of the part to the whole thoroughly ingrained and fortified by tradition, and where, in addition to all this, the amount demanded by the tax is inconsiderable, or where any demand of considerable magnitude is made only on occasion of events that profoundly stir the sentiment of patriotism.

Under the circumstances existing in the large states of today, where these conditions are absent, wholly or in part, this rudimentary method of assessment is condemned at the start.

One step further brings us to that method of self-assessment (declaration) which consists in a public statement, written or

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oral, before the tax officials. The interval between this stage and the first is not so great as is often assumed; especially it is not so great as is claimed where this method is not in use, and where it is accordingly overrated in the manner in which untried institutions commonly are. The advantage of this stage over the previous one is bound up with the question, what effect the superadded publicity will have. It is quite possible, and experience goes to prove the fact, that - where the outcome of this publicity is a mutual neighborly connivance - self-assessment before the officials remains about as much an affair of private conscience, or consciencelessness, as the method of secret self-assessment.

The efficacy of publicity is a matter depending on a great number of conditions which must be fulfilled by the adoption of the proper contrivances and institutions. This is the point of contact between individualism and self-government in taxation. If the assessing authority is endowed with the full measure of civic unripeness that many countries know so well through their experience with local self-government, then this authority will be practically useless as a means of publicity in self-assessment. It is not until this authority is clothed with the power attaching to a national office, and only in the degree in which it is so endowed, that it can have any effect in fortifying the conscience of the self-assessing taxpayer. It is only in the presence of such an authority that the sanctions coupled with self-assessment become effective. All this holds true of the penalties attaching to false returns (which in the absence of such authority remain a dead letter) and of the submission of the tax lists to inspection by the taxpayers (which in an atmosphere of prevalent evasion of the tax will in any case not receive any attention from the public). Public sentiment is inclined to seek improvement in the adoption of certain mechanical contrivances which unaided can never lead to improvement, and which can achieve an improvement only when helped out by an organic growth of institutions.

It therefore appears that the hopes entertained regarding the

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individualist factor in tax administration presently point to the need of something lying beyond that factor-tax official clothed with the powers of the national authority. How can local self-government create an authority clothed with these powers?

§ 376. The great point is the same in this instance as in the case of all the machinery of self-government, viz., the citizen's administration of office must, as far as possible, be removed from the influence of his selfish instincts. But there is a second point of considerable difficulty, by which the administration of the taxes is distinguished from other phases of self-government, viz., that it is indispensable that the administrative official should combine an intimate knowledge of the affairs of the neighborhood with all these general qualifications.

K. G. Kries,<sup>1</sup> after a few years experience with the Prussian income-tax legislation, was able to point out the way by which this purpose may be accomplished. In this work he took his suggestions partly from the English model, partly from the practice of the local administration of taxes in Berlin, as contrasted with that of the Prussian provinces. The members of the Berlin board of assessment are taken from all classes and all parts of the city, so that they are not bound together by any personal or class interest; the great number of taxpayers prevents more than a relatively small number of them from standing in any close relation to the members of the board; at the same time, the members of the commission are so numerous and are brought together out of so widely different spheres of life as to bring to naught the influence of all personal interests which might otherwise affect the result.

The result is that as contrasted with the degenerate self-government of shopkeepers assembling in the market Place, or with the rural idyl, we have such a complexity and inclusiveness in the organs of self-government as to raise them above the business interests of the individual citizen to the level of public

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<sup>1</sup> *Zeitschrift für die gesammte Staatswissenschaft*, 1855, p. 397.

duty and neutralize the influence of private interest through the great number and diversity of such interests which it comprises.

There is a variety of this scheme, and indeed a somewhat dubious variety, in which the class contrasts subsisting between the taxpayers are marshalled not so much in the spirit of self-government as in that of class administration [*Klassenverwaltung*], a parallel to class legislation. Under the circumstances which would supervene with the realization of the social-democratic ideal the tax legislation and tax administration in the hands of the proletariat would be an effective handle for the taxation of the bourgeoisie. In such a case they should have not the spirit of self-administration - the sense of public duty as opposed to the promptings of individual interest - but the struggle of interest against interest. There are other class contrasts than the social-democratic one which may be made to serve this purpose; the legislation of Bremen, of 1873, is a case in point, where the merchants taxed the farmers; and especially worthy of mention is the American method of tax administration, such as exists, for instance, in the state of New York, where there is a combined assessment of the property tax for the town, county and state, but subject to reapportionment or equalization within the county by county officials and for the state at large by state officials, in such a manner that it is possible, for instance, for the officials representing the rest of the state to increase the taxes for New York City out of all proportion to those paid by the state at large. A further modification consists in supplementing the still surviving human infirmity by the rigid framework afforded by a professional official class, and a succession of stages of appeal leading up to the central power of the state.

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<sup>†</sup> According to facts collected from the several states of the Union by Richard T. Ely, in his work on *Taxation in American States and Cities* (1888), the workings of American self-government in tax administration seem to be exceedingly unsatisfactory. There are (according to the letter of the law) very stringent provisions in many of the states with respect to the assessment of the customary property tax, but these provisions are brought to naught by an extremely lax administration, a fact which in its turn is a consequence of democratic self-government. In Ohio, for example, there is a provision requiring taxpayers to appear, on request, before the tax officials and

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The Prussian legislation of 1851 recognized this necessity fully, but the practical application of the principle was and is defective in a high degree; and under the influence of the latest reforms in the direction of local self-government the principle has even been weakened. Where, as is the case at present in Prussia, the court of first instance, and, for the great body of assessments, practically the court of last instance, is made up of an elective committee of members of the commune, under the presidency of the mayor in the towns and of the county chairmen in the country districts, it is to be said that this leaves the administration of the public business entirely to the organs of local self-government. The office of mayor or of county chairman must be filled by persons of very unusual qualifications if they are to rise above the level of the views held by their constituency and (in accordance with the intention of the law) raise it to the dignity of an office of the state. Ordinarily, according to the bent of their everyday habits of mind, these men feel themselves to be in some sort attorneys for their commune; they prefer to exercise their courage against what lies outside rather than inside, counting it a patriotic duty to shield their fellow townsmen from a more honest payment of taxes than other towns and provinces.

If any serious reform is to be effected, then this indispensable element of the national authority must be provided for under one form or another. In place of the mayor with his social connections and incumbrances, or of the county chairman, must be substituted an officer of the state, with a permanent tenure, appointed for this special duty, answerable to the central government alone, independent of the organs of self-government, not bound to the narrow interests of a town or a

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make a sworn self-assessment or return; the result being that there is no well-to-do man in that state who is not a perjurer (p. 159). An exceptionally conscientious assessor was practically removed by not being re-elected (p. 150). The New York assessors say in their report for 1881 that personal property is on an average assessed at less than one-tenth its value (p. 176); in 1888 the assessed value of real estate in the state of New York was 2669 million dollars, while the assessed value of personal property was 345 million dollars (1885, 2762 million and 332 million respectively). Personal property paid only 11.50 per cent. of the property tax of New York.

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district, and therefore also not hampered by the social considerations of the neighborhood; but at the same time his duties must be confined within a district small enough to admit of his acquiring and making use of an intimate knowledge of the affairs of the individual inhabitants. In virtue of his direct connection with the central tax-administration and by means of the proper official relations with like commissioners of other tax districts, the duties of such a tax commissioner will also include a care of the uniformity and equality of assessments; in addition to his watchfulness over the equity of taxation as between individual taxpayers within his own district, he must also keep watch of the equity of taxation as between different districts. Without some such organ there is no assurance of uniformity of taxes, especially in a country of great extent. It may be remarked that one of the chief obstacles to an imperial income tax in Germany, as in any other federal state, lies in this, that the very nature of a federal state is opposed to the establishment of the requisite centralized control, partly because of the particularist attitude of the individual states, partly out of consideration for the hardships involved in any thoroughgoing centralization. The many causes of friction already existing and difficult enough to be overcome are reinforced by an additional one, and one of a very sensitive nature.

Arrangement must also be made for an appeal from this lowest organ of the state tax administration to higher authorities of the same character. The bodies which hear complaints must likewise contain representatives of the national tax administration as well as of the higher organs of local self-government. All historical development, and especially that of the difficult questions whose solution goes to make up progress in tax policy, is of slow growth; we may therefore look upon the imperfection of the Prussian tax administration as a result of the difficulties with which all innovations have to contend.

§ 377. There is one means offered by the technique of taxation for an approach to that goal which the foregoing discussion

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has shown to be very difficult of attainment in the administration of taxes; this means will contribute materially to bring the performance of the taxpayer up to the standard of the law.

If, instead of leaving the amount to be derived from the tax dependent upon the greater or less discrepancy between the letter of the law and its fulfillment, we start out with fixing the aggregate revenue to be required, levying this aggregate upon the aggregate of taxpayers and then leaving them to distribute the burden among themselves, we have not only defined the letter of the law, but have at the same time secured the certainty of its realizing a given aggregate result. This leaves no discretion, in substance, to the intermediaries between the state and the individual.

The greater rigidity of this method as contrasted with the one already spoken of is brought out by the most striking case of its application, that is to say, the war indemnities which have traditionally been levied in this form by the victors upon the conquered country or upon its provinces, communes and other constituent bodies, leaving these bodies to make any distribution of the burden among individuals. But there are noteworthy examples of this method being adopted by preference even in taxation that is intended for times of peace; the French direct taxes are an especially well-known example (sec. 299). It has also become customary to use the French name for this method of apportioning taxes, taxes levied in this manner being called "taxes of repartition," while the converse method, by which the law fixes a quota or percentage to be levied as a tax-rate on the individual taxpayer or tax-object, is called a "proportional tax" [*Quotitätssteuer*].

These two methods are, in point of form, diametrically opposed to each other, but considered as fiscal expedients the contrast between them is only relative. For, even in adopting the method of the repartition tax, the legislator contemplates an approximately ascertained and fixed rate of taxation, and similarly in case of the proportional tax the law contemplates a more or less definitely fixed aggregate revenue. But it is the

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relative contrast between the two methods alone with which the are here concerned. For the point immediately in hand relates to those props and coercive measures by which assistance is afforded the taxpayer's vacillating sense of duty. If certain fixed annual sums are required of the provincial and communal self-governing organization, with the expectation that these local authorities will distribute the burden among individuals, this affords the administration of taxes by the local authorities a fixed support and standard from which they cannot depart.

In Prussia, according to the law of May 21, 1861, the land tax is a repartition tax, but with certain peculiar conditions attached which have been mentioned above (sec. 306). Significantly enough, the house tax is not of this character, and this fact serves to bring out the extreme rigidity of the repartition tax on land. Of the variable taxes in the Prussian system the trade-license tax (sec. 307) has something of the character of a repartition tax, in that certain average rates are prescribed, which rates multiplied by the number of taxpayers liable to the tax give the sum which is to be jointly paid by them. In the case of the class tax and the income tax the limit set by the early income has also something of the character of repartition, hut in a negative rather than a positive sense; for example, the law of May 25, 1873, introduced an element of proportionality [*Kontingentierung*] into the class tax by means of the provision that any amount by which the aggregate revenue from the tax exceeded a certain fixed sum was to be applied in abatement of the tax.

The flexibility of consumption taxes (and taxes on transfers) is coupled with the drawback that, while they are amenable to treatment by this negative method, the positive method by which the aggregate amount of the tax is fixed at a given figure cannot be applied in their case.

## II. THE ASCERTAINMENT OF THE TABLE OBJECTS.

§ 378. In the administration of the tax law, in applying the provisions of the statute to the phenomena of actual life, the



great problem is to ascertain what these phenomena are. Viewed in the light of the foregoing considerations on state administration and administration by the local self-government, the feature which first obtrudes itself is the great difference between the two chief classes into which taxes are divided. It has of late been thought a pertinent characterization of this difference, as regards the Prussian territory, to say that the officers of the indirect taxes wear uniforms, and those of the direct taxes civilian's dress.<sup>1</sup> This external distinction in some degree coincides with an intrinsic difference between the organs of administration which are required for these two great classes of taxes. The uniform of the officials of the indirect tax points to the fact of a professional class of permanent officials which it would be impossible to replace by the organs of local self-government, a point in which the administration of the direct differs from that of the indirect taxes. And this difference results from a substantial difference in the work to be performed. If the facts with which the tax administration has to deal are of a stationary nature, then a relatively impermanent class of officials may suffice for the work, - such an official class as is afforded by local self-government, especially if it is to some extent supplemented by the professional administrative officials of the national authority. If, on the other hand, the facts which the tax law is to cover are in a state of constant flux, if they are of the nature: of instantaneous phenomena which must be seized at the instant of their appearance, if at all, then it is necessary to have a permanent administrative organization at hand, which can be on the watch at every hour of the night or day.

It is further to be remarked that in the practical work of ascertainment of the taxable objects the neighborhood element afforded by the method of self-government is of great use in the former of these two classes (assessment for the purpose of the income tax, the land tax, house tax, trade-license tax), as by this method use can be made of information which is not available to any professional official class - personal acquaintance

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<sup>1</sup>Neumann, *Schmoller's Jahrbuch*, 1882, p. 971.

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with the circumstances of the neighbors in respect of property and business, knowledge of customary prices, values, rents, income, etc. With respect to the second group of taxes above mentioned this kind of information is of small consequence; the facts to be dealt with here are, as it were, of a mechanical nature, palpable and definite, not involving the uncertainty of an appraisal; they admit of being set down according to kind and quantity. This is especially true of the great number of consumption taxes, whether they are collected as an internal tax or as a tariff duty, - whether it is the tax official's business to keep watch of the receipts of beets at a beet-sugar factory in order to record their weight before they are reduced, or the customs official inspects dutiable goods in vessels, railway cars, cases, etc., coming from foreign countries.

The fact is not to be overlooked, however, that the legislation dealing with this second group of taxes achieves a formal simplicity of the tax at the cost of a substantial sacrifice. This requires some further consideration.

§ 379. Among the great shortcomings of the taxes on consumption (to confine ourselves to this category) is to be counted the circumstance - which viewed from another side is a merit - that the collection of the tax takes place without reference to, or contact with, the person on whom it is intended that the burden should rest. We proceed on nothing more definite than the estimated average of the proportion between the consumption of the taxable article and the tax-paying capacity of the individuals. This average on which we proceed is necessarily of the most superficial character, since it comprises the greatest possible variety of individual cases. The consumption of objects of luxury pure and simple, such as champagne for example, bears such a very uncertain proportion to the taxpaying capacity of the household by which these articles are consumed, that the wish, however impracticable, obtrudes itself upon us, on grounds of equity, that every bottle which passes the custom-house might show on its face who is going to consume

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it. And how much more true is all this of the great staples of consumption - beer, wine, tobacco, tea, coffee and the like and how constantly we have occasion to regret the fact that under this tax it happens in a large proportion of cases that a tax-paying capacity ten times as great as another pays not a single penny more than the latter. How while this wish of ours has no chance of being realized, we must and do, at least, make such effort to correct this short-coming as the technique of consumption taxes will permit. The attainable in this direction seems to be to take due account of the different grades and qualities of all articles of consumption, or - what amounts to the same thing - to take account of the value of the article in fixing the rate of the tax. In fixing a much higher rate of taxation for the better grades of wine, cigars, etc., than for the poorer articles we are justified in believing that we have done something appreciable towards correcting the superficiality of the average of which we have spoken above. But even in this effort we meet with great difficulties. The ascertainment of this difference in value by the tax official involves so much labor, and is, in part, so far impracticable, that even this modest requirement of equity in consumption taxes fails of accomplishment; the tax official is only required to perform the easier task of taking note of such gradations in quality, and consequently in rates of taxation, as do not require an excessively minute inspection of the contents but are evident from obvious superficial characteristics. We confine ourselves, for example, to taxing imported manufactured tobacco higher than the unmanufactured, cigars higher than tobacco cut for the pipe, foreign wines in bottles higher than foreign wines in the wood, ready-made clothing higher than materials for clothing. To use the commonly accepted terms, "*ad valorem*" duties have, after a good deal of discouraging experience with them, been given up, and "specific" duties substituted in their place.

The outcome would surely have been different if the declaration made by the payers, which is ordinarily taken as the basis of

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the tax, had been found by experience to be reliable. Experience has shown that such declaration is pretty generally very much in need of supervision by the tax officials. The chief advantage of the tax monopoly consists in this, that it enables the tax to follow up differences in the quality and value of the goods which necessarily escape the other customary forms of taxation. The monopoly places this distinction between grades and qualities entirely within the discretion of the authorities, in permitting them to fix the price at which the goods are sold to consumers.

§ 380. With respect to the measures taken by the tax administration for the ascertainment and assessment of the taxable objects, it will be found that these measures admit of a graded classification according to the degree of publicity of these objects or facts. It will be found that there is a graded succession, beginning with subjective taxes and running through objective taxes to taxes on exchanges or transfers and, finally, taxes on consumption.

The more intimately the facts to be ascertained are woven into the texture of household affairs, the greater are the difficulties which the tax administration will encounter in trying to ascertain them; the more the facts lie on the surface the less the difficulty. The knowledge of the income and property of a person, particularly under the complex circumstances of modern industrial life and property relations, is ordinarily, both as to aggregate amount and as to constituents, shielded from the public eye by the same boundary wall behind which the household jealously shelters its private affairs from the eyes of outsiders. Just as is true of every other private matter of domestic life, so also, and in an especial degree, is it true that prevalent sentiment loops upon the knowledge of private pecuniary circumstances as a *noli me tangere* which may properly claim a sort of sanctity even as against the obligations towards state and commune. It is true that in this case as in so many others, really venerable sentiments are appealed to simply to cover

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sentiments that are in no wise venerable; and there are large classes of persons (state and communal officials and the like) who will serve as an instructive example of the fact that an appreciable number and a select class of households do not suckle for this domesticity and sanctity. Still, the fact of a prevalent immaturity in moral and political sentiments exists and manifests itself in this way. This sentiment is unmistakably the outcome of long-continued habits of life adopted under the constrained and narrow conditions of the earlier political system and the old-time seclusion of individual life from the public, or it is an outgrowth of an innate self-seeking which will have to be overcome by a long and arduous process of moral and civic growth and education. Only in proportion as these sentiments give place to a more liberal habit of mind is there any fair prospect of penetrating the obscure ground of individual pecuniary circumstances, and the hope of the various legal measures employed by the administration for this purpose lies in the fact that there exists a certain, perhaps very modest, degree of readiness to comply, and that this incipient readiness will be strengthened by the pressure exerted by the law.

If after the manner of the Prussian law of 1851, in its modification of the earlier legislation of 1820, assessment by men taken from the neighborhood is made use of in an attempt to pursue a middle course between the method of co-operation on part of the taxpayers themselves and that of an energetic interference by the central government, nothing is accomplished beyond showing a lack of confidence in the readiness of individuals to publish their pecuniary affairs, without doing anything to correct this shortcoming.

If the declaration of the taxpayer is made the basis of the assessment, this indicates, at any rate, a greater degree of confidence in the taxpayer; but the precise extent of this confidence, as well as the extent to which it is justified, will appear only on taking account of the other measures bearing on the same point, and of the results achieved.

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§ 381. Self-assessment in its most primitive and least rigid form may be entirely optional; so that failure to make a declaration carries no penalty nor any disadvantage to the individual; it may therefore be left entirely to his own discretion what his conscience or his sense of his own advantage may prompt him to return. Obligatory self-assessment must be backed by the sanction of some penalty or other, at least some disadvantage (such as loss of the right to make complaint of too high an assessment), if it is to deserve the name at all. But the simple requirement of some return of income or property is entirely nugatory if no penalty attaches to an excessively low return. Herewith we have reached the domain at whose boundary the representatives of the taxpayers in our legislative assemblies (and to some extent even the national government itself, in the degree in which they are possessed of sympathy for human infirmity, timorously draw back.

The obvious method of requiring an oath as to the accuracy of the return, coupled with the severe penalties attached to all perjury, have been found by experience to be of very doubtful expediency. The history of taxation in the United States has long since established the fact, on documentary evidence, that in that country this requirement has made perjury habitual in tax assessments and the experience of our own courts, which gives evidence of a veritable epidemic of perjury,<sup>1</sup> does not encourage a further extension of the employment of this means. The danger of using the oath in connection with self-assessment of taxes lies in this fact, that, besides its evil effects on morals, it still further increases the inequality of assessments; one part of the taxpayers will have their conscience aroused by the oath, while others do not, so that the inequality to be expected under any system of self-assessment will simply be augmented.

Other means of compulsion - fines for failure to make returns,

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<sup>1</sup>As an example may be cited the list of cases at present (1888) being decided before the Court of Jury in Gottingen. On June 24, C. K., miner, from Andreasberg, sentenced for perjury; June 25, H. S., lath-cutter and woodman from Sievershausen, sentenced for perjury and libelous accusation, etc., etc.

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penalties for too low returns, whether in the more usual form of a money penalty or the less usual form of personal detention - are effective only in proportion as the threat is expected to be put into execution. In case of a lax administration of the tax system by local authorities these penalties are just as ineffectual as the assessment oaths in the United States. If they are to be made effective they will therefore require an adequate organization of the officials in charge of the tax administration, such as has already been spoken of above.

Indirect measures of compulsion which are intended to accomplish their object through publication of the tax lists, whether by exhibition of the returns posted in the office of the board of assessment, or by publishing them in the newspapers, may, though not necessarily, be of some use in getting at the truth. It will appear, in this matter as in all others, that the point of substantial importance is the question of morals, of sentiments, and of the prevalent habits of mind. This remedy, of a publication of the tax lists (often spoken of as extremely strict and rigorous, may remain without effect wherever there is a prevalent remissness and toleration, especially if it is coupled with a lack of conscientious insistence on the rights of the community. (Where there is jealous and ill-will between neighbors, where there are strong class contrasts, or where there is a jealous watchfulness of the public interest, such a measure may be of some service, although it will always achieve a more satisfactory result if it acts preventively (by quickening the conscience) than where it acts only repressively (through informers and the like).

It appears, therefore, that the prospect for a progressive improvement in the ascertainment of the facts in this most recondite field of taxation, lies not so much in particular practical measures that have been tried and found effective, but rather in the gradual evolution of a sense of civic duty, to be fostered by sagaciously chosen measures for promoting the observance of the law, and even more particularly, by a proper development of the organs of tax administration.

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§ 382. Very appreciably easier is the ascertainment of the facts in the case of those taxes which are levied not upon personal relations and circumstances, not on the "subject," but which attach simply to the "object," that is to say, objective taxes.

The facts to be ascertained in this case are much more obvious and external. We no longer have to do with personal relations, possessions, gain, credit, debt, business activity, profit and loss, but with things, external objects which serve simply as a basis, as a readily ascertainable constituent factor in these personal relations. In order to their ascertainment the person of the taxpayer and his knowledge of the facts are not only dispensable, but are of no use whatever; we have nothing to do with the individual or personal element, but only with general facts and averages.

The task seems especially to be lightened by the fact that - quite different from what is the case with subjective taxes - when the facts are once ascertained the results commonly hold good for a number of years; so that the laborious investigation has to be repeated only at rare intervals, perhaps once in a generation, while it is of the nature of subjective taxation that it requires this operation to be repeated frequently, commonly every year, in order to keep abreast of the continual change that goes on in each person's pecuniary circumstances.

However, experience teaches that ordinarily, even in this field, the ascertainment of the facts is practically not so simple and easy. It is true there are objects with regard to which the facts can be ascertained with little effort, and for which a single valuation will serve tolerably for a long period. A good instance of this is the Prussian house tax (sec. 306). In this case the objective taxation in question is confined to a particular and generally simple form of land tax; where the practice of renting prevails, as in the large and medium-sized towns and cities, the ascertainment of the facts required for this tax is especial) easy; if the repetition of the assessment takes place only after an interval of fifteen years this method of assessment



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becomes one of the most convenient and satisfactory that is to be found.

But in most cases the advantages are not so pronounced. The account given of the French land tax, and the accompanying discussion of the manner of constructing a land-tax cadaster, and the observations made on the Prussian land-tax reform (secs. 299, 305) will serve to indicate the practical difficulties with which this phase of objective taxation and assessment have in experience had to contend. While the work of cadastration promised great things and was intended to dispose of the question for a long time to come, employing a great and expensive apparatus and organization for a number of years, or even (in France) for a number of decades, it is after all a work which bears on its face the stamp of error, transiency and inequality, from the very start. The reason for this is simply that the computation of the net produce of agricultural land, even when no regard is had to the pecuniary circumstances and relations of the individual owners, is so difficult a problem that it is impossible to ascertain the truth of the matter by this method, except in a very imperfect way. It is only under circumstances where the customary methods of business favor the ascertainment of the facts in the way they do for the house tax, that the task of ascertaining the produce of land can be accomplished easily and in a tolerably satisfactory manner. If the practice of leasing prevails extensively in agriculture or if sales of land are very frequent, this will afford reliable and accessible facts as to the produce, or at least afford ground for an inference as to the produce and value of land much preferable to the laborious and, in the last analysis, fictitious computations of the cadaster.

§ 383. It is characteristic of these classes of taxes, and of the method of assessment required by them, that these, as well as the subjective taxes, necessarily involve an element of self-administration.

In the assessment of the Prussian house tax, as well as in

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the construction of the cadaster for the Prussian land tax, the assistance of experts is always counted on. The alternative method of assessment, modeled after the English pattern and advocated by Kries (sec. 305), also rests, substantially, on the services of men intimately acquainted with the affairs of the neighborhood.

This fact itself suggests the relative difficulty of assessing this class of taxes as compared with the others presently to be taken up, which can and do dispense with the services of "experts." It is not for the detection of the intricate facts of private life and circumstances, but only of the facts of the taxpayer's business activity that we do and must employ business men, men who have gained experience in the business world and especially in local business affairs.

This is particularly evident in the case of the trade-license tax, where, as is the case in Prussia (sec. 302) the taxing authorities shrink from the difficulties of the French method (sec. 302) and reluctantly adopt the methods of subjective taxation. In this case we have an assessment after the manner of the class tax, being partly effected by professional officials and partly by the members of the commune; the tax being at the same time restricted to a certain rate, somewhat after the fashion of the repartition tax, by the requirement of an average rate to be paid by the members of the class on whom the tax is levied. It is to be added that this method of administering the trade-license tax has been less production of results than the French license tax precisely because it occupies a vacillating position between the subjective and the objective tax. The French tax does not employ personal assessment of any kind, but has recourse exclusively to definite external indications - the number of inhabitants of the place, the character of the industry, the rental of the buildings and grounds occupied by the establishment. The difficulties which arise out of this purely "objective" treatment of the license tax, and which have to be overcome by extremely minute and detailed provisions, remind us of the difficulties of the land-tax cadaster; any advantage that may belong to the

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license tax depends on the fact that a single assessment is not required to serve for a long term of years, but is renewed from year to year.

In the one case as in the other, the inadequacy of the assessment is shown by the fact that we content ourselves with a simple class tax because an adequate ascertainment of the net produce of any industry is practically unattainable.

§ 384. The problem of assessment is greatly simplified if the facts to which the tax attaches are obvious and tangible. This is habitually the case as regards taxes on consumption and on transactions. It is especially true in case the law applies to the most obvious facts only. The substitution of specific for *ad valorem* duties, for example, is such a case of simplification in the tax administration; neglect of differences in quality, other than the most tangible ones, is a grave fault in point of equity, but is often highly expedient as a practical measure.

In the same spirit a selection is sometimes made of the simplest and most obvious factors in the process of production in order to the laying of a tax on articles of consumption produced within the country; the taxation of the raw material of beet-sugar, or of spirits, or of beer (secs. 272, 274) seizes upon the most accessible of the stages into which the process of producing these goods resolves itself, - of course not without raising a question as to the expediency of this method on other grounds.

Viewed from the standpoint of industrial progress, the incitement to a fuller utilization of the raw material, afforded by a tax on raw material, may of course recommend itself; but as seen from the standpoint which is immediately concerned in the question of taxation, it must be set down as a defect of the method that this incitement not only involves an advantage to the stronger producer over the weaker, but also a failure to collect the full tax income aimed at by the legislator. Experience of this kind accordingly urges to the supplementing of this simple method of taxation by extending the tax to other portions of the process of production or circulation.

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Taxes of this class will, of course, continue to enjoy the advantage that in their employment the tax administration has only to take thought for the ascertainment of the presence of the special facts in question, and the necessary supervision is facilitated by this fact that the tax need attach only to facts that are easily ascertainable. Goods may be taxed at their entrance into the country in case the conformation of the national boundary favors or admits of the proper supervision of imports. The articles of consumption produced at home are taxed by this method if of such a nature that their production (or circulation) may be readily controlled. This class of taxation, therefore, selects those articles and those steps in their production or circulation that can be assessed with ease and accuracy.

tax on transactions derives an advantage from the use it can make of the courts, notaries and other officials, very analogous to the advantage which taxes on consumption enjoy in the accessibility of the process of production or circulation. The stamp used for purposes of public registration, or simply as an evidence of the payment of the tax (as happens in the case of many consumption taxes), aids in the ascertainment of taxable objects by the requirement of publicity.

### III. THE COLLECTION OF TAXES.

§ 385. In the method of collecting taxes, at least so far as concerns indirect taxes - internal taxes on consumption and import duties - we are confronted with an historical growth of the same character as what we have met with in other departments of national life, - a development from the performance of public functions by private enterprise to their performance by a state organization in the full sense:

In the states of classical antiquity, as well as in the tax administration of the *ancien régime*, and, under analogous circumstances, in the countries of Eastern Europe at the present time, and even in certain special instances in the modern kingdom of Italy, we have the institution of Tax Farming. This method of collecting taxes turns over to private business men a function

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which is assumed as a matter of course by the financial administration of any fully developed modern state. Even Frederick the Great, in his effort to increase the revenues of the Prussian state after the Seven Years' War, made an attempt to reorganize and strengthen the tax system by calling French farmers of the taxes to his aid.

It is not to be denied that expedients of this sort may find some justification if we consider the relative efficiency of private enterprise as compared with an undeveloped official class for the performance of services of this kind, together with the teaching of past experience in the administration of the taxes. In this, as in other cases, the self-seeking of private individuals may be made use of to accomplish those purposes of the community for whose adequate performance the state officials of the time are not possessed of a sufficiently mature intelligence and sense of duty.

But there is also a second, and perhaps often a stronger argument for the farming of the taxes, viz., the state's need of advances for which it will, in such a case, pawn the taxes for a number of years. Even in the case of Italy's granting a lease of her tobacco monopoly to a joint-stock company this was the decisive reason; and in France this was the decisive inducement to a farming of the taxes down to the reorganization of the finances after the Revolution. From time immemorial, says Taine,<sup>1</sup> it had been the custom to eat the corn in the ear and to anticipate the income of the succeeding year. Even Colbert<sup>2</sup> tried to break with the practice of alienating the national revenues and to annul the contracts already made; but without any permanent result.

It is therefore readily intelligible that theoretical writers should have condemned the farming of taxes at an early date. Montesquieu<sup>3</sup> says that the royalty (i. e., collection of taxes by state officials) is the management of a prudent householder who takes up his revenues in an orderly and economic manner; he

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<sup>1</sup> *Les origines de la France contemporaine*, p. 403.

<sup>2</sup> *Zeitschrift für die gesammte Staatswissenschaft*, 1870.

<sup>3</sup> *De l'esprit des lois* (1748), book xiii. chap. 19.

saves the state the enormous gains of the tax farmers, who consume the substance of the country in a thousand years; he saves the people a multitude of evil laws which the greed of the tax farmers imposes on them. Montesquieu's historic sense, however, leads him to admit the possible utility of a tax lease in introducing a new tax where the resourceful self-seeking of private interest would detect and prevent tax frauds that would escape the state officials.

Justi,<sup>1</sup> who in so many things has a modern air, sets up the general rule that royalties cannot be farmed out without some detriment, and applies the statement particularly to customs duties and tolls. It is impossible that a farmer of the taxes should pay more for the lease than the revenue which would be obtained through officials, unless he enriches himself by illegal exactions from the public. But Justi falls short of Montesquieu in breadth of view, in that he does not recognize the importance of a self-seeking private enterprise, which may be made use of to prepare the way for administration by state authority in this field in much the same way as it is useful in modern improved industry and business.

The experiences which were present to the writers of the eighteenth century, especially in France, must have been quite unfavorable to the farming of taxes, since this method is so peremptorily condemned even by Adam Smith, from whose general standpoint it might be expected that he would show a certain predilection for it. The best and most economical way of collecting the taxes, says he,<sup>2</sup> can never be by the use of the tax lease. The large capital required for the purpose excludes any active competition, so that the state granting the lease has to deal with a combination instead of with competitors outbidding each other, and the profits of the tax farmers are consequently enormous; they are the richest people in the country; stir up the hatred of the public by their extravagance and their heartless oppression of the taxpayers, for whom it is impossible that they

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<sup>1</sup> *Staatswirthschaft*, vol. ii. p. 141.

<sup>2</sup> *Wealth of Nations*, book v. chap. ii. (ed. Playfair, vol. iii. p. 403).

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should feel the sympathy which the officials feel towards subjects. Even a very bad prince has more sympathy with his people than can ever be expected of the farmers of taxes; hence the tax laws are harshest in countries where the farming of taxes is practiced; the sovereign has an interest in dealing gently with his people, the farmer of the taxes, never.

§ 386. The qualification of the state officials for the collection of taxes, just as the adaptation of the state officials generally for any function, is the product of a development which gradually brings out the requisite intellectual characteristics of the people. The official class, and more particularly the tax officials of the half-civilized states of today, afford us a living example of this in the contrast they offer to what we find in civilized states. In these half-civilized states there are no accomplished results ready to hand - the goal has to be reached by a process of gradual approach. The question as to whether the Russian state is better served by the kind of administration which it can get through an official class of the grade of development actually to be found in that country, or through an administration carried on by joint-stock companies and private enterprise, is a question to which an answer can be found only by experience.

For the state of the higher stages of development this question has been solved. Its official class has reached a maturity corresponding to the cultural stage occupied by the community, and possesses the qualities which the state's work requires of it. It is safe to assume this fact as the basis of tax administration and tax collection and to simply make allowance for such infirmities of "human nature" as are unavoidable, or at least unavoidable at the present stage of development. This public function is adequately performed by the official staff simply as part of its public duties, without recourse to those motives of private interest which the immature political organism of the Middle Ages and the formative period of the absolute state found so useful.

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Viewed from this standpoint it becomes a question of detail only how far the organs of local self-government are to assist the organs of the central administration in the collection of taxes. There are no reasons in favor of a participation of the organs of local self-government in the collection of taxes, of equal urgency with those which speak for participation in the assessment of taxes. And in point of fact the national government does not so frequently employ those organs for the former purpose. The case where it will most obviously and most frequently occur is that of a tax levied for the purposes of state and commune both, when the commune may be entrusted with its collection for both; or in the analogous cases where, in a federal state, a member of the confederacy, as being the public body in closest contact with men and affairs, may be entrusted with the collection of a tax levied for the member and the confederation in common, - as, for example, is done in Switzerland, since 1879, with the military-compensation tax, one-half of which goes to the canton and the other half to the confederation.

§ 387. The period of recurrence in the collection of taxes is of considerable importance in connection with the various forms of taxation.

In the case of the direct taxes (taxes on income and produce) it is customary to concede so much to the circumstances and habits of the less well-to-do classes as to collect the tax in as small quotas, and therefore at as short intervals (monthly and the like) as possible. The aggregate sum to be paid is not reduced by this process; but, the burden of taxation being to a large extent an emotional fact, it is to be remarked that the poor man who is not in the habit of keeping large sums on hand (except under circumstances of an unusual industrial maturity) finds it harder to pay the entire annual tax once for all than to pay it in twelve monthly installments.

It answers more nearly to the habits of the well-to-do classes to collect the tax in quarterly, semi-annual or even annual installments. But even in the case of these well-to-do classes the



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degree of economic maturity and the consequent habits vary greatly from one country to another. It is by no means a matter of pure accident that in the canton of Zurich the state tax is paid in a single annual installment by all classes of taxpayers, and the communal tax in semi-annual installments by all classes alike, whereas in Prussia the class tax payable to state and commune is collected monthly, and the income tax quarterly.

If no such considerations of leniency toward straitened circumstances and an undeveloped economic sense are taken into account, it is certainly most convenient, for the tax collector and for the taxpayers both, to make the tax payable in a single yearly sum. The circumstances controlling the collection of indirect taxes, and especially of taxes on consumption, are quite different.

The point of practical utility in this form of taxation lies, to a great extent, in the fact that in the collection of the tax the producers (merchants, etc.) advance the tax in a lump sum, with the expectation of recouping themselves from the persons who ultimately bear the tax. This method of payment is a necessary feature of this form of taxation, the hardship of which cannot be avoided although it can be reduced. Measures may be taken which will, as far as possible, reduce the interval between the payment of the tax and the recovery. The more nearly we succeed in making these two points of time coincide, the less legitimate ground will there be for the complaint (not ungrounded though often exaggerated for purposes of free-trade advocacy) of a burdensome interference with production and trade by taxes of this kind.

Measures intended to serve this purpose are: (1) Extension of the time of payment, for a proper term and with proper security; (2) the laying of the tax in such a manner as will (so far as other requirements permit require the payment of the tax at a point in the process of production or of circulation that shall be as little removed from the time of sale to the consumers as may be; (3) bonded warehouses (*entrepôts*) where goods may be held in bond until the tax is paid and the goods removed for

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actual entrance into domestic consumption, or until they are removed for re-export; of course with all due precautions against abuses and discrimination.

Under this third head are comprised especially dutiable articles of import which at the same time enter largely into a transit trade with other countries; for this reason there is frequently (where the political circumstances permit) a protracted struggle against including these markets within the tariff boundaries. The remedy in such a case, after the modern state has once carried its irresistible tendency to unity and centralization so far as to include them within the tariff boundary, is that of great places of deposit (free ports under customs supervision). Such are to be found in the commercial cities of Great Britain, France, and latterly also in the politically independent seaports of the German Empire.

Something analogous may also occur with respect to consumption taxes on domestic products in case the tax is levied on the finished product. Very much as is done with the goods imported from abroad, these domestic products may be held in bond under the charge of the tax officials until the goods are thrown on the domestic market or are exported.

The difficulty is much greater in case the tax is levied at a stage in the productive process at which no determination with respect to the destination of the goods has been taken. Under the Prussian-German law, the potatoes intended for distillation, the barley intended for beer, the beets which are to be converted into sugar represent the stage at which the tax is collected, whereas the decision as to their ultimate use, whether for home consumption or for export, will not be made until they have passed through the manufacturing process and assumed their finished form. For, it is to be remarked, this manufacture plays a very important part in the national industry and produces in excess of the home demand.

The consequence is that a tax is paid on the raw material which is reimbursed in case the product can be shown to have been exported (drawback). So that we have, instead of a place

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of deposit exempt from taxation (bonded warehouse), an actual payment and reimbursement of the tax. The objectionable features of this method are (apart from the tax supervision), in the first place, a burdening of the industry by the tax, and in the second place, the difficulty of an accurate computation, for the purpose of the drawback, of the ratio of the raw material to the finished product. If the drawback is placed at too low a figure the result is a hardship to the producers; if it is placed too high it involves a drain on the public revenues which goes to the producers as a virtual exorbitant bounty, and may under given circumstances result in all the detriment involved not only in the enrichment of a number of individuals at the public expense, but also in an abnormal growth of certain branches of production through artificially overstimulating them, as has happened of late in the case of the beet-sugar industry.

§ 388. To this national character of taxation and tax collection there corresponds a system of coercive measures, in the shape of tax inspection and penalties adopted to secure the payment of taxes.

The methods of tax inspection are so closely connected with the character of the various forms of taxation, that the adoption and the successful employment of a given tax, as we have seen, largely depends on the kind and the possibility of the measures of control to be adopted. The entire system of income taxation is dependent on the feasibility of certain methods of superintendence, the characteristic features of which have already been touched upon; the question as to whether taxes involving certain annoyances and difficulties are feasible at all, what results may be expected from them, and how much it is expedient to require of them, all these are questions the answer to which depends on the existence of practicable means of supervision and control. Whether and what taxes on consumption are to be employed, on what particular articles they are to be levied, whether on imported goods or on domestic products, and at what rates, depends (aside from the question of the need of revenue and

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of equitable distribution) on the practical conditions imposed by the measures of supervision and control necessary to be adopted.

Hence we have a variety of methods of supervision employed in the various classes of taxes, as well as a further variation in detail between the individual kinds of taxes made necessary by differences in the details of production and circulation. The practical exigencies of the processes of production and distribution, therefore, give rise to special practices in tax collection; we find instances of this in the taxation of distilled liquors and in the sugar tea; and the progressive centralization of the business of supplying a great city by rail has, for example, resulted in a centralized control of the octroi in Paris and other similar places.

The strictness with which measures of superintendence and control are applied answers in some degree to the height of the rate of taxation; so that an increase in the demand for a tax revenue is followed by a fresh accentuation of the measures of control, which sometimes takes the form of the substitution of a new method of tax collection (a tobacco monopoly instead of a tobacco tax levied on private producers).

The principle involved in the question is the discovery of the most effective weapon that can be brought to bear upon the taxpayers' undeveloped sense of public duty; the greater the demands, the severer, *cæteris paribus*, in this struggle between the public demand and the tax-payers' reluctance, and the severer the struggle the greater the need of an effective weapon.

Penalties for failure to pay the taxes are the *ultima ratio* in this struggle, just as the legal penalty is always the *ultima ratio* in the struggle between the public authority and the individual in the execution of the public will. And the tax penalties can do nothing beyond applying to the special purpose contemplated the penalties which are at the disposal of the law generally, and by the usual methods. The distinction between different degrees of offense and the consequent difference in the penalties imposed, etc., have their place in the field of taxation as elsewhere. The

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distinction between this field and the field of criminal law generally lies in a difference not of principle but of practical application. The difference lies in this, that the penalties with which the modern state visits tax frauds are relatively very light, the very name and implication of fraud being avoided in the wording of the law, out of consideration for the very prevalent feebleness of the sense of civic duty.

The law has got into the habit of taking active cognizance of only a very moderate proportion of the cases of such frauds as actually take place. Probably in no sphere is the proportion so very low as in the field of frauds on the taxes.

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BOOK III.  
GERMAN TAX LEGISLATION OF  
THE PRESENT TIME,  
IS OMITTED FROM THIS TRANSLATION.

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BOOK IV.  
THE PUBLIC CREDIT.





## CHAPTER I.

### THE HISTORY OF PUBLIC CREDIT.

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#### I. THE EARLY DEVELOPMENT OF PUBLIC DEBTS IN EUROPE.

§ 470. Credit is a fruit of advancing civilization. It is a precipitate from the moral atmosphere of a people and an epoch

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which finds the transfer of the usance of capital advantageous (vol. i. sec. 418). The resulting historical development takes the form of a succession of stages within the history of any given people, and the form of a succession of phases in the history of the various peoples concerned. The degree of industrial efficiency, the productivity of industry and commerce, the degree of accumulation of capital, all these furnish the material basis for some one stage in the course of this development. Political and civil activities, as the visible manifestation of the degree of moral culture achieved, constitute the hyperphysical basis. The importance of this last factor is especially great, and is on the increase, within that sphere of credit where the state figures not simply as the keeper of the law, but is itself the recipient of loans - the field of public credit. The stage of industrial and political development, both, therefore, decides what shall be the degree of development of public credit. The early development of credit in the city republics of Italy gave the first impetus to this growth in the modern European world; and afterwards the other European states in succession, each in turn as it reached its prime, followed the example of that ancient home of civilization. In this spread of public credit, as happens so often in analogous cases where a cultural advance is transmitted from one people to another, the hand of the business men and adventurers of the land of its origin was active in introducing the institution into foreign lands. The Italians taught the people of the North the unfamiliar methods of credit and of financiering, the lottery and the tontines; adventurers bent on gain made the capitals of Europe the scene of their activity even as late as the close of the last century. Indeed the great world-market of capital and of credit which has been supplying the world with loans for a century past still bears the name of those Lombards who came to England seven hundred years ago on the business of collecting tolls and taxes and of loaning money on the security of those sources of income.<sup>1</sup>

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<sup>1</sup>Schanz, *Englische Handelspolitik gegen Ende des Mittelalters* (1881), p. 551.

§ 471. The business of the Italian *campsores* began quite early to extend itself beyond the simple exchange of coin (money-changing in the strict sense), so as to include the making of remittances to distant places, and more especially to include the deposit business. It had been the custom for a long time past, traceable to the business methods of ancient Rome, to place money in banks for security. The deposits which accumulated in this fashion as *depositu irregulare* afforded the banker an opportunity to make a profit. The Roman-Canonical dogmas, however, forbade the derivation of any profit from such deposits on loans by the payment of interest, and the representatives of this doctrine, even as late as the middle of the seventeenth century, were unable to find any justification for such interest. Hence arose the custom of entering such money nominally as a partnership investment, in which case a participation in the gains from the money would be legitimate; and so the partnership method gradually replaced the form of a deposit. These partnership banks are to be conceived of as a number of powerful and respectable family establishments, some of them very old, which played a very important part in the money market. The name *Bancherii* had gradually come to replace that of *Campsores*.

At the same time there was in existence a deposit business in the strict sense, which was even developing into the chief business of the banks. This gave the state, as guardian of the public interests, and in much the same manner as the exchange business of the *campsores* formerly, occasion to require an official concession as a condition of doing business; whereby the state would have an opportunity to guard against frauds on the public conscience on the part of the banks. From all this there resulted a supervision on the part of the state and a giving of bonds on the part of the banks; all of which afforded the state a leverage for fiscal exactions.<sup>1</sup> In the case of Venice there is documentary evidence going back to the second half of the fifteenth century<sup>2</sup> to show that certain banking houses had loaned

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<sup>1</sup> Endemann, pp. 423-431.

<sup>1</sup> Nasse, pp. 339-342.

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the state sums amounting to 1,200,000 ducats, for which they received no interest and, according to the views of that time, could not receive interest. Whenever the fiscal administration of the state was in a strait it seems to have turned to the banks as the most obvious resource. It is conceivable that the government's power of supervision and control over the city's commerce may have been made use of to indemnify the bank. But the banking business found the arrangement unprofitable; the banks gradually came to refuse credit to anyone whom they suspected of the intention of withdrawing the amount credited to him instead of letting it remain in the Bank. So the government enjoined the banks by law from declining to make any transfer that might be demanded.

§ 472. Besides this abusive conversion of the bank deposits to national loans there was also some borrowing of a permanent character. Since the doctrine on usury prohibited interest, the state paid "rents" in return for the loans, and these rents were secured by special branches of the national income.

The origin of the *montes* which were by accepted usage the means of placing these loans, and the relation of the *montes* to the development of the Italian banking system, have to this day not been thoroughly cleared up. It seems certain that the relation was a close one. The common bond between them is the state's need of loans and its use of compulsion in order to secure loans from private parties. The *montes* had this in common with the bank partnership, that both of them were in possession of an accumulation of capital which was made up of a number of shares.<sup>1</sup>

<sup>1</sup> *Mons argenti, mons auri*, occur in the Latin comedians of the classic period. Prudentius (*Hymnus II. in honorem Laurentii*) relates, in the early years of the fifth century, that in the third century the pagan *præfectus urbi* had made a demand on the Deacon Laurentius for the church treasure (*fulgidæ montes monetæ conditos*). Certain writers as H. C. Senkenberg and Beckmann take this as a proof that the usage was already in vogue at that early date, and that the term *mons* was applied to the treasure of the Christian church. This does not seem to me to be proven by the passage in question, as the church treasure is here first spoken of as *arca* (*exquirat arcam ditibus massis refertam*), followed by the above words used as a poetic figure.

In the thirteenth century, it is said, the government of Florence having to pay a number of its own citizens a debt of seventy marks in gold, and being without money, adopted the expedient of assigning its creditors a fixed annual income to be paid out of the state's revenues, the rate being first fixed at 15 per cent. and then successively lowered to 10 and 5 per cent. Out of this beginning there grew up a permanent financial system; the debt of the republic increasing in times of war and diminishing 3n times of peace. These annuities also became objects of purchase and sale, their price fluctuating, like that of other goods, according to the seasons, the fancy of purchasers, etc.<sup>1</sup>

As in Florence, so in Genoa, Rome, Naples and other cities; these fiscal institutions are said to have come into general use, gradually spreading over the country in the fourteenth and fifteenth centuries. The *montes pietatis* (pawnbrokers' shops established for some charitable purpose) seem to have come into vogue later than these *montes (profani)*.<sup>2</sup>

The *montes* are said to owe their origin, in Florence as elsewhere, to forced loans (*præstantiæ*), but they presently came to be taken up to some extent voluntarily, as a business, by capitalists. The spread of this method of loans furnished occasion for the canonical doctrines to consider the question of its permissibility. The voluminous literature of learned monks and jurists bears testimony to the importance and the prevalence of the *montes* in Italy. The inclination was, more and more, - to admit the legitimacy of this method of loan. Ecclesiastical authorities who ordinarily anathematized all countries and cities that borrowed and paid usury on their loans, advocated the full free-

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Leonardus Aretinus says (*Histor. Florentinarum*, lib. vii. p. 145): "*Quantitates vero ipsas in unum coacervatas a similitudine cumulandi vulgo montem vocavere. Idque in civitate postea servatum.*"

<sup>1</sup> Leonardus Aretinus, *loc. cit.* On Venice in the Sixteenth Century, cf. also Nasse, p. 350; Endemann, p. 433; Beckmann, vol. iii. p. 344.

<sup>2</sup> The meaning of the name *monte di pietà*, *mont de piété*, was afterward in its turn lost sight of, as shown, e.g., by Savary s. h. v. According to Savary, the original meaning of the word *mons* seems to have been retained in Rome as late as the eighteenth century, being used to designate *une creation de rentes lorsque la chambre apostolique a besoin d'argent .... ces rentes se payant très régulièrement.*

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dom of interest payment for the Florentine, Genoese and Venetian *montes*.

Then, during the course of the fifteenth and sixteenth centuries, there is a typical development of the details of business methods in this fiscal institution, whereby the different permutations of chance and circumstance are exploited by means of a specialization of the mechanism. Data and experiences were carefully collected and then adopted as guiding principles for the routine of the business and handed on to later generations.

The annuities assigned to creditors were for the most part funded on particular sources of public revenue. The shares of these annuities (*appoints, loca montium*) were adapted to the varying demands of purchasers. They were sometimes life annuities terminating at the death of the creditor (*montes vacabiles*), sometimes terminating only on repayment of the capital, and capable of being inherited (*montes non vacabiles*), these latter being computed at a lower rate than the former; sometimes the annuity was terminable at the instance of the creditor (*montes redimibiles*), sometimes non-terminable (*non redimibiles*). The modification of the annuities which in the time of Louis XIV. was introduced into France and Northern Europe, and associated with the name of the Neapolitan Tonti, had long been well known in Italy (and in the German towns) - the principle of this form of annuity being that the value of annuities falling void is to accrue to the surviving annuitants.

§ 473. The connection of these institutions with forced loans, which during their early days had served to exempt the sale of annuities from the canonical condemnation of usury, presently declined in importance. It came to be more and more a matter of interest voluntarily entered into between capitalists and the state. The popes themselves made use of it after the beginning of the sixteenth century. The name employed (*mons religionis, mons fidei*), which carried a suggestion of the war against the infidel or of the defense of the faith in the protection of the city of Rome, and which was thus calculated to cover up

whatever might be questionable about this money transaction,<sup>1</sup> this form of name gradually came to be accepted as the everyday designation for those domains or taxes which were mortgaged to the state's creditors (*montes farinæ, carniæ, vini*); or the loans were sometimes named for the popes who contracted them (*mons Julius*) or were designated by the length of time which the annuity had to run (*mons novennialis*). In the seventeenth century it was, especially in Rome, that the *montes* came to be a permanent institution; about the middle of the eighteenth century these papal annuities were accounted an especially safe and popular investment.<sup>2</sup>

The shares (*loca montis*) became subject to inheritance and transfer. The state when in need of a loan matched its opportunity to place them advantageously on the market just as the various states have placed their bonds on the market in later times. The price of these *loca* fluctuated according to the fortunes of war and peace, and according to the security and productiveness of the hypothecated sources of revenue. An obvious further step was that this mortgaging of the future revenues from taxes and duties to the state's creditors should bring with it a leasing of these sources of revenue to the creditors, and a consequent collection of the taxes by farmers. The *mons* was therefore very often a tax-farming business, and the farmers of the taxes were a detested class of people in Italy, as they afterwards were in France and other countries.

About the close of the fifteenth and the beginning of the sixteenth century, Macchiavelli testifies to the influence which public credit at that time had on the course of political affairs. When the Venetians entered into alliance with the King of Naples against Florence, Cosimo di Medici, by means of a loan operation, drained Venice and Naples of money to such an extent that those states were obliged to accept the terms of peace dictated

<sup>1</sup> Sixtus V. (Bull of 1585) established a *mons non vacabilis* which was based on an agreement manifestly more questionable under the doctrine of usury than that involved in the *mons vacabilis*.

<sup>2</sup> Cf. Savary, *Dictionnaire de commerce*, article "Mont;" Endemann, p. 436; Beckmann, vol. iii. p. 346.

to them by Florence. And still the Medicis were only one of the wealthy families of Florence; besides them there were many, other families that were noted for enormous wealth. Great productivity of industry, of trade and of the banking business on the one hand, and a standing mercenary army, frequent wars, large payments of tribute to the great states of the north, on the other hand, gave rise to the habitual use of credit by the Italian states and their capitalists.

§ 474. The German cities of the Middle Ages<sup>1</sup> also show a striking similarity in the evolution of their public credit to the city republics of Italy.

Even as early as the latter half of the fourteenth century (in Basle beginning 1365-66) municipal loans occur as a constantly recurring transaction, loans being taken up year after year. One reason for this is the fluctuations in public expenditures, the greater part of which cannot be fixed beforehand. If a war came on unexpectedly, or an opportunity to acquire prerogatives or domains, or to extend the municipal territory, then the public credit offered a means of supplementing the revenues. In this way the growth of political power was, here also, just as in the case of the Italian republics, largely bound up with the employment of public credit.

A second reason may (according to Sohm's hypothesis) have been - the first reason offered being insufficient to explain the permanent character of these loans - that the city carried on a banking business in order to profit by the fact (founded in law) that its credit alone was sufficiently stable for such a business. The city became a banker; it looked upon the contracting of liabilities in the way of annuities and the like, not primarily as a means of covering extraordinary public expenditures, but as an ordinary constituent factor in the municipal administration; because the city was in possession of a virtual bank monopoly for certain purposes, in much the same way as it possessed a

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<sup>1</sup>G. Schönberg, *Finanzverhältnisse der Stadt Basel im 14. und 15. Jahrhundert*, (1879). Rud. Sohm, "Städtische Wirtschaft im 14. und 15. Jahrhundert," Conrad's *Jahrbücher*, 1880, vol. xxxiv, pp. 261-266.



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legal monopoly of the salt business. Interest-bearing debt was here employed side by side with annuities; debts with a high rate of interest were also converted into new debts with a lower rate of interest.

All this was of course useful as preparing the way for profitable employment of the municipal credit in case of public need, and served therefore as a substantial support of the city's political power.<sup>1</sup>

§ 475. The center of gravity of the world's trade shifted, during the era of discoveries, from Italy to the countries which lay on the new high road of the world and were able to seize the advantage of their position. There resulted a northern counterpart to the commercial prosperity of Italy in the Netherlands, whose gains were drawn from the more productive sources of the all-inclusive world market.

The money market of the Netherlands developed a luxuriant growth along the lines of the traditional fiscal methods, and at the same time brought forth new forms beside the old. The

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<sup>1</sup> The public credit as employed in the German principalities during the Middle Ages is treated of in *Der öffentliche Kredit im Mittelalter nach Urkunden der Herzogthümer Braunschweig und Lüneburg*, by A. von Kostanecki (*Staats- und sozialwissenschaftliche Forschungen*, vol. ix. p. 1, 1889), containing details as to the early development of public credit. The documents of the duchies of Brunswick and Lüneburg show nearly 300 ducal debentures issued during the period 1293-1405. In by far the greater number of cases the creditors are secured by a grant of the usufruct of property or franchises. Three-fourths are mortgages on castles [*Schlossverpfändungen*]. The occupant of a large estate in pawn was, as a very general rule, vested with the power to appoint the officials of the district (*Amtleute*, *Vögte* etc.); or at any rate the old incumbents must *mit Eiden Sicherheit leisten*.

As regards the towns of Brunswick and Lüneburg (Brunswick, Lüneburg, Hanover, Göttingen) the facts given in this publication supplement what was already known from other sources (especially from Schönberg's book). Here, as in Basle, the prevalent form of credit is that of the sale of annuities. These were at the outset founded on sources of revenue in kind (real estate), afterward on income in money (taxes and the like). In particular cases there occur, here as in Basle, phenomena properly belonging to a more highly developed stage of public credit; so, for example, in Brunswick there occurs between 1396 and 1406 a progressive reduction of interest (first from 10-11 per cent. to 8 per cent., and afterward gradually down to 3 per cent.). And, as was also the case in Basle, we find both life annuities and perpetual annuities. And as applied to the life annuities, we find the method of the tontine in use.

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bourse of Amsterdam was, in the early part of the seventeenth century, a money market of the same significance for its day as the London money market became some 200 years later. The buying and selling of securities here for the first time developed to considerable proportions, with all the excitement and the excrescences of speculation. The business spread abroad about it an atmosphere of reckless thirst for gain, which presently led to the extension of the business methods of the exchange from transactions in securities to commercial transactions in all kinds of goods. A development which in point of technical efficiency is admirable, in point of morality problematical, and in its economic bearings not fairly comprehended to this day.<sup>1</sup> The Dutch East India Company was founded in 1602. Its shares directly became such a favorite object of speculation on change that a decree of the States General was issued in 1610 prohibiting the sale of these securities in blank. The same thing was repeated in connection with the West India Company founded shortly afterward. The occasion for these prohibitions was the solicitude felt for the credit of the companies and for the state interests closely bound up with them. The extended participation of the public in investments of this kind is evident from these acts; even in these early decrees there is mention of the property of widows and orphans, which was afterward so frequently declared to be bound up with the interests of these joint-stock companies. In like manner as the investments of private individuals in the company's stock served to strengthen Holland's world-wide trade, so the same wealth invested in the state securities did service in the national struggle for a position as a political and commercial power. What had been done on a small scale by the Italian republics and by the German towns at the height of the Middle Ages, repeats itself in the Netherlands on a much broader scale; the public credit is constantly made to serve as a resource of the national finances and for carrying on war. The

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<sup>1</sup>G. Cohn, "Zeitgeschäfte and Differenzgeschäfte," Hildebrand's *Jahrbücher für Nationalökonomie und Statistik*, 1866, vol. vii. pp. 395-403.

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accumulation of capital and the security of the public credit both developed in such a high degree that the rate of interest declined in the course of the seventeenth century to the point at which it commonly stands in the wealthiest and soundest nations of today.<sup>1</sup> As early as the second half of the seventeenth century the rate of interest had declined to 3 - 2 ½ per cent., and even the shares of the East India Company paid no more than 3 ½ per cent. This low rate of interest drove the superfluous capital to foreign countries, where it could obtain twice as much. In the American War of Independence Dutch capital fought both on the English and on the American side. Amsterdam sided with the one party, Rotterdam with the other. The greater risk of investments abroad made itself felt as an advantage to the increasing national debts; these served to keep the money from going out of the country and to bind the creditors to the state.

§ 476. The usual form in which national and municipal debts were contracted in the Netherlands, too, was the sale of annuities.

In this the earlier examples, which we are already acquainted with, were followed. But the occasion for so doing which was afforded by the canonical doctrine of usury was not present in this case;<sup>2</sup> the decisive reasons were reasons of financial administration. The annual payments were employed to cancel the principal of the debt. This form of payment moreover afforded an opportunity for a reduction of the rate of interest, of which the finance administration made profitable use. Under the Stadtholder Maurice the rate of interest in Holland and West Friesland was reduced from 6.25 per cent. to 5 per cent.; in 1655, under John de Witt, it was reduced from 5 to 4 per cent., in order to reorganize the finances and to lighten the burden on the citizens by redeeming the debt or to place new war loans on more advantageous conditions. This measure was of course not applied to the life annuities; but these were looked on with all the more favor as canceling the principal of the debt in a short

<sup>1</sup> Laspeyres, *Geschichte der Niederländer*, pp. 248-253.

<sup>2</sup> *Ibid.*, pp. 256-270.

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time. The principal of interest-reduction, too, found less application in the eighteenth century, as the rate of interest on state loans had then fallen to 2.50 per cent. With respect to the life annuities, the question was then coming up as to whether the state or private enterprise had best take this branch of the insurance business in hand. Projects for carrying on the business by private enterprise were put forward as early as the close of the seventeenth century, but the private establishments for this purpose seem not to have been particularly successful in the Netherlands.<sup>1</sup> Even as late as the close of the eighteenth century there is evidence that the business was thought very unfavorably of.<sup>2</sup> Tontines and life annuities, says *De Koopman*, are good as state institutions; as private undertakings they for the most part profess to be charitable institutions, but their sole real basis is greed of gain, and in the most favorable cases the poor results are due to incompetence rather than to fraudulent management.

§ 477. As we approach the present we naturally turn to the country - which at present is the center of the world's money market - Great Britain.

With the unity and centralization of its general development during the past eight hundred years this country affords us also in the growth of its national debt administration a clear and conspicuous example of the development of public credit, from infancy - upward through many intermediate stages to the mature vigor based upon a controlling position in the world's commerce, which England inherited from the Netherlands, and then, since the close of the eighteenth century, strengthened and increased to gigantic proportions by the aid of the modern efficiency of industry. And all this rests upon a political system whose basis is not the narrow ground of a city-republic or a collection of several city republics, but has all the breadth and scope of a great modern state.

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<sup>1</sup> Laspeyres, pp. 252-253.

<sup>2</sup> De Koopman, vol. iii. pp. 24-28.

Down to the closing years of the eighteenth century England was dependent, on Dutch capital even for its public credit, so much so that during the English war against the American colonies the people of Amsterdam could seriously ask the question how long England would be able to go on paying interest on its debts. The stupendous effort put forth in the struggle against France was a marvelously successful test of England's wealth of capital and of its credit; so that after the great war closed English capital was already in position to render the same service to the states of the continent as Holland had rendered to England shortly before. During the progress of the American war every successive loan was obtained on more onerous terms than the next preceding; quite the contrary was the case during the war at the close of the century, when every successive loan was obtained on easier conditions.<sup>1</sup> And when, in 1783, a man of great consequence exclaimed: "Either the nation must put an end to its debts or the debts will put an end to the nation,"<sup>2</sup> the historian of English finances, Sir John Sinclair,<sup>3</sup> replied with prophetic words, then as he did twenty years later: "Posterity will laugh at the foolishness and shortsightedness of the statesmen of today who venture to assert that we have entirely exhausted our resources."

§ 478. But it is a long way that has to be accomplished before this point is reached. Want, violence, breach of faith, straitened finances, these are the conditions amidst which the evolution must proceed for centuries before the requisite legal basis of public credit and the free movement of capital which comes of law and order can be achieved. So long as the authority of the sovereign, like all other public authority during the Middle Ages, is still encumbered with the swaddling bands of private law and private-law rela-

<sup>1</sup> William Playfair, the editor of Adam Smith's work, writes to this effect in the year 1805, and adds (vol. iii. p. 445, note): "An effect has taken place in England which nobody expected and which it is not easy distinctly to explain."

<sup>2</sup> *Hints Addressed to the Public on the State of Our Finances* (1783).

<sup>3</sup> *The History of the Public Revenue*, vol. iii. p. 211 (3<sup>d</sup> ed., 1804).

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tions, so long does the public credit also continue to lie latent under the form of the king's private credit, and this latter bears all the characteristic marks of its time, in the way of indebtedness and pecuniary straits. The first king whose debts history records is Henry III.; he had pawned everything, crown jewels, robes of state, even the casket containing the relics of St. Edward; he was so beset with debts that he could scarcely appear in public without being assailed by the shouts of his creditors; he is even reported to have publicly declared his want to be so great that it would be a greater deed of charity to give money to him than to a beggar at the door.

A hundred years later Edward III. (1340) disclosed to Parliament that he had borrowed so much money on his personal security while abroad that in case it were not repaid he would be obliged to return to Brussels and stay there as a pledge to his creditors. The grandson of Edward III., Richard II., was the first king<sup>1</sup> who applied to Parliament for aid in raising the money necessary for a campaign against France. But in vain; the Lords declared that they were willing to accompany him to the war in person, but they had no money, and the merchants were unwilling to lend except on the most unquestionable security. A further attempt to raise the required sum (£60,000) from foreign merchants by granting them the privilege of trade in England failed, and so the war had to be given up. Among the grievances on which the deposition of this king was based there stands out prominently the complaint that he had extorted money under pretense of borrowing.

Henry V. succeeded in obtaining from Parliament (1416) a subsidy of £,60,000 to cover pressing necessities in the war in France. But as it was feared that the money would not come in fast enough, the attempt was made to borrow the money on hypothecation of the subsidy, at the same time giving three royal princes as hostages. Scarcely one-fourth of this loan could be obtained; the king was obliged to mortgage the crown and the crown jewels to raise the remainder.

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<sup>1</sup> *Rot. Parl.*, vol. iii. p. 122; *Sinclair*, vol. i. p. 384.

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§ 479. With Henry VII. and the House of Tudor begins a new era.

The fiscality introduced by him was violent in the means it employed and hypocritical in its professions, but profitable to the commonwealth in its substantial effects, and it gradually reduced the public finances to order. Henry VII. left behind him a national treasure of £1,800,000. By an exercise of sagacity in the punctual payment of debts he improved his credit. Henry VIII., it is true, repeatedly resorted to the dubious expedient of having a pliant Parliament absolve him from his obligations. But the modern order and method of things comes more clearly into the foreground, in this department also, under Elizabeth's rule. In 1575 the Chancellor of the Exchequer was able to assure Parliament that the whole of the old debt, which went back at least four years before the death of Henry VII., had been paid, with interest; and that Her Majesty's credit had hereby grown stronger both at home and abroad than that of any other prince, because she had kept her word to everybody, which many princes had not done. In return for this the queen desired that her prerogative of granting monopolies should be left intact, as being "the most beautiful flower in her garden and the richest jewel of her diadem." For this purpose she also revived an old law, of the second year of Richard II., which recognized the right of the crown to levy forced loans and left the decision as to what constituted a "reasonable excuse" in the discretion of the crown. For this purpose she had to go into the money markets of the continent - Hamburg, Cologne, Antwerp - and pay high interest (10-12 per cent.) even for small sums, which could even then be obtained only on the security of the City of London and the personal security of her own ministers. Such was the case until the increasing wealth of the country, the parsimony of the administration and the growing credit of the crown made capital available at home. The turbulent times of the seventeenth century involved the English national credit in vicissitudes of the same kind as the rest of the political system. This came to a close with the Revolution of

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1688, and an orderly system then began to be introduced into the management of the public debt, such as to inspire its historian with the conviction,<sup>1</sup> quite in the spirit of the time, that Henry V. would never have been hindered in his glorious campaign by lack of funds if the system of funded debts had been in existence in his time.

§ 480. The struggle against the French power in Europe and in the colonies, the struggle against the independence of the English colonies, and, finally, the struggle against the French republic and empire, were the causes which kept the English national credit on the stretch throughout the course of the eighteenth century and down into the beginning of the nineteenth, and so occasioned the search for and the finding of new resources in the use of it. These sources of revenue only gradually reached the full productivity which they had at the beginning of the nineteenth century. The stability of the public credit, as well as the country's wealth of capital, had to develop for a full hundred years before the point of saturation was reached, before the state could stand independently on its own credit and the country on its own domestic capital.

The reign of William III, opened amidst financial difficulties which had been aggravated by the war. The English were not accustomed to heavy burdens of taxation, and "did not know that no nation has ever enjoyed civil and political liberty without paying dearly for these blessings." Moreover, the customary revenues declined in consequence of the war. The same taxes which yielded net receipts of £2,000,000 before the Revolution, yielded in 1693 only £1,100,000, and in 1695 only £812,000. Of taxes previously in existence, the hearth money alone had been remitted; new duties and excise taxes had been introduced, which in 1693 yielded not half a million, so that the aggregate receipts of earlier times were not nearly equaled. The growth of political parties was one cause of this result. Davenant computes that the sudden changes in the administration of

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<sup>1</sup> Sinclair, vol. i. p. 401.



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the excise, due to the revolution in political parties (to cite one out of a great number of instances in the national administration, brought about a decrease of more than one quarter of a million pounds. Great defalcations came to light. In 1701 the lower house found it necessary to pass a resolution that: "It is notorious that many millions have been paid to His Majesty for public purposes without their being, so far, accounted for in any way."

We can comprehend the necessity of the debts that were incurred, even without resorting to the explanation afterwards brought forward by Bolingbroke that they were incurred in order to bind the propertied classes to the new government. In 1710, writes Davenant, the government was in the position of a debtor reduced to such extremities that the creditors were squeezing the very blood out of it; the citizens had withdrawn from trade and given up commerce because the wars interfered with the business, and had become usurers, lending their money, to the government. As early as 1697 Parliament passed a law to control the brokers, who were put under oath in order to remedy the ill consequences of the unfortunate traffic in securities.

§ 481. At the outset the form of public credit employed was that in vogue under Charles II.; the taxes granted by Parliament were anticipated by pledging them. Presently a change was made to the system of rents or annuities, patterned after the Dutch model. In 1692 an attempt was made to borrow one million by this method, on annuities to run ninety-nine years, at 10 per cent. until 1700, and 7 per cent. after that date; but it was impossible to raise the full amount on these conditions. The following year one million was borrowed on annuities of sixteen years' term, with annual payments of 14 per cent, and a lottery feature added. Life annuities were also sold (at 14 per cent. to terminate with the life of a single person, at 12 per cent. for the life of two persons, and to per cent. for three, no regard being had to the age of the person taking up the annuity). The

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lottery also came into vogue; the opposition, even at that time, styled it the destroyer of industry and sobriety, and ascribed to the Dutch the intention of undermining the virtue and thrift of the English by introducing this institution among them. In 1697 the Chancellor of the Exchequer, Montagu, invented the exchequer bills, issued to some extent in denominations of five and ten pounds, as an expedient for remedying the scarcity of money while the recoinage was going forward. The government borrowed from the Bank of England and the East India Company, on occasion of granting them their privileges, 1.2 million and 2 million pounds respectively, for which they received 8 per cent. interest. The entire national debt at the close of 1701 amounted to 16.4 million pounds, and the annual interest charge on the debt to 1.3 million pounds. Only so much of this was accounted a permanent debt as was borrowed from the two companies above mentioned, together with a sum of .66 million pounds carried over from the reign of Charles II.

Anticipation of future tax revenues and the sale of annuities remained the staple forms of public credit. The rate of interest declined gradually; at times during the reign of Queen Anne it was only 6-5 per cent. By the end of 1714 the permanent debt to the companies (to which had now been added the South Sea Company) amounted to 20.50 million pounds; to which is to be added annuities to the amount of 26 millions (one-half of this being lottery annuities of thirty-two years' term); and finally there was a floating debt of five million pounds, which it was estimated might be converted into a funded debt of an additional two millions. The debt therefore aggregated 54 million pounds, with an interest payment of 3.35 million pounds.

Next followed several decades of improvement in the national credit and of decrease of the debt. At the close of 1727 the debt amounted to 52 millions, with an interest charge of 2.2 millions; by the end of 1739 it was only 47 millions, with a yearly charge of 1.96 millions. In 1737 Sir John Barnard was able to submit a scheme for reducing the interest on the greater part of the redeemable annuities from 4 to 3 per cent., a measure which

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was adopted ten years later.<sup>1</sup> The 3 per cent. stock, during the succeeding years, stood nearly at par, never below 89. About this time it became the fashion to issue stock with an integral rate of interest and at a fluctuating price; the 3 per cent. securities continued to be used even at a later time, when the state could sell these securities only at a discount of 40 or 50 per cent. The use of life annuities and lotteries still continued, especially in seasons of great expenditure and straitened finances; they were held to contain something of the nature of *douceurs* to the creditors, spices to tickle the palate of the investing public. Also loans from the privileged companies, who received in return new privileges or an extension of the term of the old, continued to be a fiscal expedient which could be of but relatively slight profit to a state whose credit was good. In return for the extension of the privileges of the East India Company for fourteen years (1766-80), the state received £1,000,000 at 3 per cent. interest; this was in 1743 when 3 per cent. stock stood at 97.

§ 482. From this time on heavier demands on the state's credit occur from time to time, on account of war expenditures; the heavier demand pushes the rate of interest up above the normal rate of 3 per cent., sometimes very considerably; but greater and greater sums were continually demanded, and the influence of this demand to injure the national credit grew relatively less as time went on.<sup>2</sup> Contemporaries were readily led to see only

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<sup>1</sup> Montesquieu (*Esprit des Loix*, livre xxii. chap. 18) points to the interest reduction effected by England as an example to be followed. If, says he, a state is in possession of a credit which has never been shaken it can do what one of the states of Europe has so successfully accomplished, viz., lay in a great stock of ready money and offer all its creditors payment in full, with the alternative that they may accept a reduction in the rate of interest.

<sup>2</sup> Justi (*Staatswirthschaft*, vol. ii. p. 432) speaks of this with admiration: "when a state's credit is perfect it is generally true that nothing is easier than to raise any sum required, whatever necessity may arise; it need only be published that the state wishes to raise so or so much money, and creditors enough will appear and freely offer their money." He cites Holland and England as examples. Although the state was already burdened with very large debts it is to be noticed that, especially in England, when the government, "during the late war," opened a subscription for a loan, there were within a few hours so many creditors offering to subscribe that several millions had to be declined.

the dark side of these increasing burdens; but for the historian it is not difficult to recognize a great advance in the fact that such increasing burdens could be borne at all, and that a constantly increasing strain on the public credit can be met. More than that, from the historical point of view it is possible to see the mutual relation of cause and effect between this increasing capacity of the public credit and the increasing demands of the state; it is possible to perceive that these national demands could not have grown as they have done if the state had not had such a credit to fall back on. The Seven Years' War (1755-1762) burdened the nation with a yearly interest charge of 2.50 million pounds, but at the close of the war the country was in a flourishing condition. The American War of Independence with its consequences, during the years 1776-1784, created a new interest charge of 5.20 millions, so that the entire interest charge by that time amounted to 9.70 millions, and the principal of the debt to 257 millions. But during the years 1793-1801 alone the debt increased by 327.50 million pounds (face value, for 215.40 millions actually received). And finally, during the years 1802-1815 the debt increased by 260 million pounds.

The growth of the debt was as follows:

YEAR	PRINCIPAL (million pounds)	INTEREST (million pounds)
1792	239.66	9.43
1802	537.65	25.30
1815	861.04	32.65 <sup>1</sup>

During the period 1793-1815 the taxes rose by a steady progression from 20 million pounds to 72 million pounds. We can appreciate the magnitude of this burden of taxation if we call to mind that it is only very lately (since 1883) that an annual amount of 72 million pounds has been raised by taxation in Great Britain; and this after an interval of seventy years, during which the population of Great Britain (exclusive of Ireland) has increased from

<sup>1</sup>The lowest point reached by the three-per cents was 47-47 ½, in 1797-8. - Leroy-Beaulieu, *Traité de la Science des Finance*, vol. ii, p. 435. Compare this table with more detailed computations given by Porter, *Progress of the Nation* (1838), sec. 4, chap. ii. p. 291.

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12.50 millions to 31 millions, and the country's wealth increased in an unparalleled manner, while at the same time the value of money has very appreciably declined.

§ 483. During the severest test to which the national credit of England has been subjected, the appeal to the public credit was accompanied by a remarkable strain on the people's tax-paying capacity. A hundred years before that time the government was engaged in great financial efforts to cancel its debts.

In the course of development of its credit every civilized state reaches a point where the necessity of redeeming its debt is no longer present to the thoughts of its creditors. It is the point at which, in the course of history, the public credit diverges in its essential character from that of private credit, where confidence in the permanence, the immortality of the state (as contrasted with the physical person) comes to prevail. The necessity previously present, of providing for the claims of creditors by securing the redemption of the debt in some specific way, is replaced by a free choice of redeeming the debt or not. Annuities with a short term and life annuities have, in England, since the beginning of the eighteenth century given place to long-term (ninety-nine years') annuities and the like. The ever-recurring and ever-increasing need of loans swells the aggregate sum continually until it has now become an important duty of the financial administration to take thought and put a stop to its overgrowth by a systematic payment of the debt.

Radical schemes for this purpose were brought forward as early as the times of Queen Anne and George I. The expedient of a reduction of interest was first applied on a large scale by Robert Walpole, when, in 1716, he converted the 6 per cent. debt to a 5 per cent., and with such success as to have no need of the capital which he had secured from the bank for the operation. This conversion made so favorable an impression even on the creditors that one of the largest capitalists told the minister<sup>1</sup> that while he lost in the rate of interest it seemed to him that his

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<sup>1</sup> Sinclair, vol. i. p. 485.

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capital was all the more securely invested. His operation had appended to it a provision that the sum hereby saved in interest was to apply to the redemption of the debt, and from this measure, therefore, dates the sinking fund.

The principle of the sinking fund is a statutory provision imposed by the government upon itself as if to bring the external pressure of the law to bear upon the vacillations of the times and of its own resolutions. It is a good resolution seeking support in a formal declaration, and continues to be practiced until it presently appears from experience that this formality is too feeble to resist the force of circumstances, though it may be strong enough to act as a vexatious obstruction,

From 1716 to 1728, for example, 2.70 million pounds of the debt was canceled, but in the next succeeding years new needs came up, so that in 1732 Walpole himself was constrained to cover the shortage in the land tax (which he had reduced in order to gain the support of the landlords by taking half-a-million from the sinking fund. So (wrote Price at a later time) the sinking fund, the only hope of the nation, was murdered prematurely and cruelly by its own father.

§ 484. The superstitious belief in the mechanism of the sinking fund retained such a hold, however, that even as late as 1783 an authority in finance could assert that it was immaterial how high a rate of interest a nation had to pay for its debts, inasmuch as the higher the interest the sooner will a properly organized sinking fund cancel the principal. Eminent authorities in finance, though differing somewhat in detail, were enthusiastic for the plan, - Sinclair, Price, the younger Pitt. Price created something of a sensation by his mathematical exposition of the scheme; Sinclair was agreed with him in the astounding calculation by which he showed that the state, by means of a sinking fund of one million a year at compound interest, would in sixty years cancel a principal of 317 millions of 3 per cent. stock. Pitt clothed the idea in the form of law and made one of his eloquent speeches<sup>1</sup>

<sup>1</sup> *Speeches of the Right Honorable William Pitt in the House of Commons* (2<sup>d</sup> ed, 1808), vol. i. pp. 217-237.

in the House of Commons (March 29, 1786) in support of the proposition that "a sum of one million annually be granted the Commissioners of the Sinking Fund to be applied to the purchase of national securities with a view to discharging the public debt of the country." This contrivance had been the wish and the hope of all men, said Pitt; he himself was proud that his name was to be inscribed on this strong pillar of the national credit and prosperity. A few years later these brave hopes were brought to grief by the war which Pitt waged against France, and the national expenditures which it involved. Even as early as 1772 a reply to Price's scheme had well remarked that taxes are taken not from a dead, insensible fund, but from the living source of the labor and tax-paying capacity of the people.<sup>1</sup> Sinclair had himself anticipated the bolder objection that the increase of the wealth of the English people which went hand in hand with the increase of the debt might make it more advantageous to apply the amount to the promotion of industry and wealth under state supervision instead of to the sinking fund,<sup>2</sup> and had in this connection made a sharp attack on Adam Smith, in defense of what the latter had named the Mercantile System.

The most effective method for reducing the debt during the first half of the eighteenth century continued to be that adopted by Walpole in 1716, namely, the reduction of the rate of interest, effected by terminating the terminable bonds and by conversion. But when the 3 per cent. rate had been reached it became the custom to regard this as the normal rate and gradually to bring the entire debt formally to this rate, in spite of any fluctua-

<sup>1</sup> *Remarks on Dr. Price's Appeal to the People* (1772), pp. 8-10. In scientific literature this view gains ground only very gradually. Sismondi, Nebenius and Lotz advocated the view. Sismondi (*Nouveaux principes d'économie politique*, 1819, vol. ii. pp. 241 et seq.) says: "*Quelque indépendance qu'on prétende assurer à une caisse d'amortissement, elle fait toujours partie de l'État, elle est toujours soumise aux lois; et l'expérience a déjà prouvé que dans les moments de détresse un emprunt à la caisse de l'amortissement, un emploi irrégulier de ses fonds, sont des ressources si faciles, qu'aucun gouvernement ne saurait se promettre d'avoir assez de fermeté pour s'y refuser toujours.*" On Nebenius and Lotz see below (secs. 512, 513).

<sup>2</sup> Vol. i. p. 522.

tions of credit. Sinclair criticises the loans placed during the war of 1755-62 because they were issued at 3 per cent. interest and much below par.<sup>1</sup> If these debts had been contracted at a high rate of interest, according to Sinclair, the country might have saved 12.50 millions; since it would in that case have been possible to borrow at a lower rate after the return of peace, and so pay off the old debt.<sup>2</sup>

§ 485. As a contrast to the mature development of public credit which England shows us during this era, we will turn now to the youngest among modern civilized states, youngest in point of political power as well as in the development of its industry and credit, but for our purposes practically the most important, viz., the Prussian state. While Great Britain exhibits the characteristic features of a stable and productive national credit as early as the first half of the eighteenth century; while that country came out of the Seven years' war in a flourishing condition at the middle of the century, after having contracted enormous loans; while it was able even during the first half of the eighteenth century to relieve its finances by a reduction of interest that resulted in the adoption of 3 per cent. as the normal rate, and its retention for a century-and-a-half since; while it has consequently outgrown all the primitive methods of covering extraordinary expenditures of the state, and retains but a single one of the expedients handed down from earlier stages of growth - the suspension of specie payments by the Bank of England on February 26, 1797 - an expedient which, even at the end of another century, has not been made obsolete by the financial development of the most advanced nations; while all this is true of England, a comparison (which

<sup>1</sup> Vol. i. p. 464.

<sup>2</sup> R. Pauli (*Geschichte Englands seit den Friedensschlüssen von 1814 und 1815*, vol. i, p. 329) says: "It makes one's head swim to be confronted with proofs of the disproportion which has always existed between the nominal value of the securities and the actual receipts from the loans; the loans issued between 1793 and 1816 amounted to £586,697,433 on paper, but they actually fielded only £339,131,500." This overstatement is probably due to the fact that to the historian, simply as such, this class of facts are not very clear.



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will carry its several centuries backwards in English history will show us the youthful German nation meeting the fiscal demands of its struggle for national existence by means that belong to an essentially earlier period.

The expenses of the first two Silesian wars<sup>1</sup> were for the most part defrayed out of the war treasure which Frederick William I. had left to his son, amounting to 8.70 million thalers. To this is to be added funds in the two treasuries of more than one million thalers. But 1.50 million thalers in plate, which the royal palace contained, also gradually took their way into the melting-pot and were converted into coin. The King contracted a debt of 1.35 millions to the Electorate for the second Silesian war, which he discharged after the close of the war. Preparatory to the third war there had again been (1756) accumulated in the treasury a sum of 13.38 millions, and a new loan of 3.57 millions was had from the Electorate. Apart from about one million contained in the "new" treasure, and set apart for the mobilization of the army, the funds with which the great war was begun amounted to 18 million thalers. These funds were exhausted by the end of 1757.

§ 486. The fiscal expedient which was next resorted to is a barbaric one. It marks the cultural level of a state with no credit and struggling for existence with brute violence. Resort was now had to debasement of the coin. First gold and then silver coins of light weight were struck, in the expectation that a debasement carried out in secret would pass unnoticed do the strength of the confidence which the Prussian coins had earned, and with the further intention of sparing the home country as far as possible and of issuing the money in the territory of the enemy. Any scruples entertained by the king and the higher officials as to this measure affected them but slightly; more than half-a-thousand years earlier the German Emperor, Frederick II., had aptly characterized the curse of uncertainty of the coinage in a rescript to the citizens of Nuremberg.<sup>2</sup> But the necessity of the

<sup>1</sup> Riedel, *Der brandenburgisch-preussische Staatshaushalt*, pp. 80, *et seq.*

<sup>2</sup> In talibus similitudinibus et tanquam indemnitatibus monetarum damna latent

state was pressing. The contrast at this point with England and Holland is as instructive for the historical study of the public credit as it is serviceable for the pedagogic purposes of the reformer. While the debasement of the coin by Frederick the Great was aimed at the neighboring German states, it is to be added that these states presently found themselves tempted to meet him and even outbid him on this treacherous field. In Wurtemberg, on the Rhine, in hither Pomerania, in Brunswick, etc., the governments sought to make head by the use of the same expedient against the inundation of Prussian coin. Quite naturally, in the course of the long continued war, the Prussian countries were also not spared the infliction of the debased coin. After the close of the war the light-weight coin was formally rated at its bullion value, and as a measure of transition a "new Brandenburg money" was introduced, which was to be employed in the discharge of the obligations entered into before March 1, 1759, but at a rate 41 per cent. above its nominal value.

The officials suffered in an especial degree from this calamity. Since the close of 1757 they had received no payment of salary, but only treasury certificates to be redeemed upon the return of peace, which declined in value constantly from year to year. In 1763 the redemption of these certificates began, but only in the "new Brandenburg money" in which for the time being current payments of salaries were also paid (consequently at 40 per cent. reduction).

Besides the debasement of the coin, some help was also derived from war contributions (which fell especially on Saxony and Mecklenburg), from the English subsidies (£670,000 annually, 1758-61), and finally from the quasi-contributions of corporations within the country. Under this latter head are to be named the loans which the King obtained from all bishoprics and chapters, from the towns, and, towards the close of the war, from the provincial estates of Magdeburg.

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universalia et ex ipsis generalius provenit dispendium provinciis et hominibus quam ex guerra vel causa aliqua temporis sive aeris particulari (Ried, *Cod. Ratisb.* vol. i. p. 325). Cf. K. W. Nitzsch, *Ministerialität und Bürgerthum im 11. und 12. Jahrhundert* (1859), p. 386.

§ 487. After the war the financial policy of the great king was permeated by the conviction<sup>1</sup> that more effective provision must be made against such exigencies in the future. He saw such a provision in the accumulation of a national treasure which should go farther than the last one. He sought a means for the accumulation of such a treasure in a more effectual administration of the excise and the tax monopolies; into which he introduced the more highly developed methods of foreign countries and which he to some extent supplemented with fiscal expedients that - as, e.g., the lotteries - had been discarded by more advanced states, especially by England.<sup>2</sup>

By 1766 the greater treasure of the king contained 18 million thalers and the petit treasure over one million. Down to 1780 the great treasure increased till it nearly reached the sum of 32 millions; at the same time the petit treasure, destined for the mobilization of the army, had received 4.33 millions. In 1786 Frederick II. left behind him a national treasure aggregating 55 million thalers.<sup>3</sup> In the meantime he had carried on the war of the Bavarian succession, which, according to the king's own account, had cost 17 millions. During the later years of his reign the national income reached a yearly net average of nearly 20 million thalers.<sup>4</sup> Of this 2-3 millions were turned over to the treasure; for military expenses during the years 1784-1786 12.50 millions a year were appropriated, for the civil service and the court not quite 4 millions, for the crown about 220 thousand thalers.

Income and expenditure remained in somewhat the same relation under Frederick's successor. During 1786-1796 about one million yearly, on an average, was turned in to the national treasure. But the art of carrying on wars and still replenishing the national treasure had, as so much else, disappeared with Frederick the Great. The unsuccessful wars against France, in

<sup>1</sup> Riedel, *Staatshaushalt*, pp. 96 *et seq.*

<sup>2</sup> Cf. William Pitt, *Speeches*, vol. i. p. 230.

<sup>3</sup> Büsching gives (what is an exaggeration) 110 million thalers; others give similar sums.

<sup>4</sup> Riedel, p. 122. Less reliable accounts place it as high as 46 million thalers.

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1792-1795 especially, called for great expenditures, and so the national treasure was exhausted by 1794. The financial support which had been looked for from England, Holland and the German Empire failed, and Prussia therefore had to face the necessity of resort to extraordinary measures.<sup>1</sup>

Frederick William I, had, in 1715, relinquished the right of collecting the poll tax, which had so frequently been resorted to by his predecessors in times of need, but with the reservation<sup>2</sup> that it might be levied in case he had to go to war for the preservation of his own territory. This poll tax which had even in the days of the Great Elector been, in point of fact, a progressive income tax, was now advocated by persons who stood near the throne, because they were anxious to avoid the alternative of a contraction of debts. It was at the time when the income tax was called upon to play a great part in England to meet the war expenditures. In Prussia the imposition of such a burden upon the subjects was sought to be avoided and a loan was preferred; this means was now for the first time employed on a moderately large scale. The king had *seinem väterlichen Herzen die Genugthuung verschafft, Dero getreue Unterthanen von Auflagen und Lasten, die ihnen sonst zur Führung dieses überaus kostbaren Krieges, wie in anderen Staaten, hätten aufgebürdet werden müssen, glücklich befreit zu haben, und im Gefolge dieser wohlwollenden Gesinnungen gehet auch jetzt Allerhöchstdero Absicht dahin, beide Zwecke, Abzahlung der Zinsen und Abzahlung der Capitalien, mit fernerer Beiseitesetzung eines Beitrages der Unterthanen, bloss durch Anwendung eines Theiles der Staatseinkünfte erfüllen zu lassen.*"<sup>3</sup>

In the foreign money-markets, in 1794, eight million gulden of the debt was placed in Holland; and in Frankfort on the Main, in 1794 and 1795, five million gulden was placed each of the

<sup>1</sup> Riedel, pp. 192 *et seq.*

<sup>2</sup> Riedel, p. 63.

<sup>3</sup> *Allerh. Cab.-Ordre*, of January 20, 1796. Riedel is quite at one with this position: "Des Königs staatswirthschaftliche Einsicht wie seine landesväterliche Gesinnung sträubten sich gleichmässig gegen eine solche Massregel" (*viz.*, the capitation tax).

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two years; at home the Society of Maritime Commerce took up two to three million thalers. This, together with a few smaller loans, seems to have touched the limas of the national credit, and before the year was out an attempt was made to supply the missing funds by the dubious method to which the great king had resorted in the financial straits of the Seven Years War - the issue of light coin (the minor coins). These light coins were, now as in the former instance, especially intended for foreign countries, where they were put in circulation by being paid to the troops; but the light coin presently returned to the Prussian territory. It is true, the plan of the Minister Struensee embodied a provision that this money would be received in sums of 25 thalers, 50 thalers, etc., in payment for national bonds bearing 4 per cent. interest; but this simply served all the luore certainly to insure their return home. The conclusion of peace at Basle, April 5, 1795, was to some extent brought about by the financial straits of Prussia.<sup>1</sup>

§ 488. The national debt which Frederick William II. left to his successor in 1797 amounted to forty-eight million thalers. Twelve millions of this had come down from the reign of Frederick the Great, 5.75 millions had been assumed by the state in connection with the new acquisition of territory, and 2.33 millions were arrears of subsidies, granted but not yet disbursed, for the assistance of certain provinces, communes and individuals; this had been occasioned especially by the distress of 1794-95.

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<sup>1</sup> Riedel holds this to be a justification of the conclusion of peace at Basle, as opposed by J. von Müller, who taxes the king with betraying German interests. On the other hand Von Sybel (*Geschichte der Revolutionszeit von 1789 bis 1795*, vol. iii., 4<sup>th</sup> ed., 1877, p. 367.) points to the relative magnitude of the exertions which were put forth by various nations at that time, and also indicates what are the moral and spiritual qualities which go to make a nation more or less capable of meeting the demands made upon them at such times and in such circumstances, when he says: "The financial and military exhaustion of the state was imminent and was apparent enough to restrain the government from any fight for a foreign interest; but as regards the question of efforts put forth for self-preservation it is to be said that the exertions made by Prussia during the period since 1792 did not amount to one-third of the exertions by which France had risen in the course of a single year from absolute impotency to the leading position in Europe."

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The remaining twenty-eight millions consisted of three approximately equal parts: the debt held at home, foreign loans, and floating obligations for army supplies. It is to be added that an additional three millions had been canceled during the king's lifetime. The revenues from the salt business were set apart for the gradual discharge of the debt, the management of the business being connected with the Society of Marine Commerce, but on account of previous appropriation of these revenues for other purposes there was but half a million yearly (1796-97) left for the discharge of the debt. This was to be supplemented by the revenue from the lately revived tobacco monopoly, estimated at four to five millions, but this revenue came to an abrupt end with the change in the government.

The discharge of the debt proceeded very slowly from this time on, so that during the years 1797-1805 there were redeemed in all seven millions. In addition to this it was found impossible to meet the maturing obligations of the foreign loans without contracting new debts. The second Frankfort loan, for example, which matured January 1, 1796, was a lottery loan payable at the rate of one million gulden a year, and therefore to be discharged in five years, beginning January 1, 1797. The first Frankfort loan of five million gulden bore interest, but it, too, was payable at the rate of one million gulden a year, and therefore to be discharged in five years, beginning February 1, 1799. The case of the Dutch loans was similar. The first of these, contracted June 1, 1793, was payable at the rate of one million gulden a year, beginning June 1, 1799; the second, dated April 1, 1794, was payable 800,000 gulden a year, beginning April 1, 1800. Similarly with respect to the loans of Kassel and Hardenberg. These were managed by the Society of Marine Commerce (under the direction of the Minister Struensee) as a banking establishment the purpose of which was partly to find new creditors and partly to furnish the funds for the new loan out of its own capital. The society placed 4 per cent. securities on the market, payable after one year on notice from either the creditor or the debtor, and in this way secured

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considerable sums for the state from private parties; it was able gradually to reduce the interest to 3 per cent. and had, by the end of 1805, loaned the state more than thirteen million thalers.

But when the peace came to an end the government was again brought face to face with the traditional fiscal expedients of distress. Besides obtaining two loans in Kassel and Danzig, aggregating about two million thalers, resort was had to the issue of five millions of treasury notes (Order in Council of February 4, 1806), of which one million had already been presented for redemption by June 1, 1806, and the government then turned with renewed energy to the ancient practice of issuing light coin (minor coins). From December 1, 1797, to the end of October 1805, there were coined 14.70 million thalers, and from October 1805 to 1806 an additional 3.50 millions; altogether rather over 18 million thalers (for the most part groschens)<sup>1</sup> on the issue of which the treasury computed a profit of six million thalers.

Then, when the misfortune came and reduced the Prussian territory by three-fifths, this mass of depreciated treasury notes and minor coin and a debt of 48 million thalers were crowded together within the reduced boundaries, and the exhausted national treasury was in addition required to pay a war indemnity of 120 million francs to the victorious enemy.

§ 489. The raising of this war indemnity served to show the full wretchedness of a nation subjected to a foreign conqueror and with its wealth and credit in an undeveloped condition.

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<sup>1</sup> The mark of fine silver was coined into a nominal value of z t thalers, while it was actually worth only 13 1/3 thalers. Struensee persuaded the king that "the issue of minor coin to any amount whatever, so long as the public accepted them, would not alter the essential character of the currency if there only were good, full-weight silver coin in circulation." A Prussian correspondent of the *Allgemeine Zeitung* (September 28, 1798) says: "An effort is being made in Prussia to bring up the treasure again, and to make some respectable preparation for an emergency; among the measures taken for this purpose is the minting of minor coins, which undoubtedly means a reduction of their value, and by which means, as we are assured by experts in finance, the king will gain half a million yearly. In point of fact the worst money is the best, inasmuch as it does not go out of the country and we are therefore sure always to retain an adequate circulating medium of exchange in the country. Base money alone has created the army and the manufactures of Prussia."

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The indemnity was the price to be paid for the evacuation of the country in September 1808, but this price could be paid only in promises, and as security for its payment the enemy continued to garrison the fortifications on the Oder.

It was stipulated<sup>1</sup> that of this sum 70 million francs was to be paid in mortgages on domains, and the remaining 50 millions in bills of exchange. The domanial mortgages were issued in 1809 by the various provincial establishments, after the king had abrogated the edict making the domains inalienable, and had handed over a suitable proportion of them to these establishments as security. The bills of exchange were issued by the bankers and merchants of the country, and were payable in monthly instalments of four million francs, beginning with November, 1808.

The difficult task of raising these sums fell upon the Altenstein ministry, after Stein had resigned in November 1808. The new ministry succeeded only to a slight extent. On December 27, 1808, they issued a domestic premium loan of one million thalers (scarcely one month's instalment), but only 0.75 million had been disposed of by 1811. Then an order was issued, February 12, 1809, requiring the delivery of all articles of gold and silver in return for certificates payable in coin; anyone who paid one-third of the value of the articles in question as a tax to be exempt from the entire amount of this forced loan. By 1812 there had been turned over to the government a bullion value of not quite 1.50 million thalers; the one-third tax yielded less than one million, by far the greater portion of this (as much as 110,645 thalers) being paid in coin certificates, which were of no avail for meeting the immediate demand. On February 12, 1810, the government issued a loan which embodied a very peculiar mixture of free choice and compulsion. It demanded 1.50 million thalers which might be paid in the minor coins, and bearing 5 per cent. interest; in case the amount were not forthcoming voluntarily the residue would be raised by compulsion. This alternative was not employed, as nearly the whole amount was obtained (1.39 millions).

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<sup>1</sup>Krug, *Geschichte der preussischen Staatsschulden*.



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Negotiations had been in progress with Holland since the fall of 1807. These negotiations came to a conclusion in March 1810. But while the request had been for 32 million gulden, the transaction brought in by 1812 an aggregate of scarcely four million gulden.

So it happened that of the aggregate of 50 million francs payable prior to November 1809, in monthly instalments of four million francs, only 41.30 million francs had been paid by May 1810. There were arrears (aside from interest) of something more than nine million francs. Further, after the payment of the 50 million francs, the 70 million francs secured by the mortgages on domains were to be paid off in monthly instalments beginning November 8, 1809, and closing April 8, 1811. Napoleon's importunity in the midst of this embarrassment led Altenstein into the scheme of ceding the province of Silesia to France in lieu of the remainder of the debt. But at this joint Altenstein was replaced by Hardenberg.

Then the property of the church was confiscated in order to be sold along with the national domains. But the outcome of this transaction, too, was insignificant. In order to find buyers at all the government accepted national bonds in payment of not more than two-thirds of the price. Still, the sales amounted (January 7, 1809, to June 1, 1813) to not more than eight millions, and of this not one-tenth was paid in cash. The new taxes imposed since 1811 were scarcely sufficient to help cover the current expenses of the government, to pay the salaries of the government officials, to discharge the interest on the national debt, and to pay for the keep of the French garrisons (1807-1812, 5.84 million thalers).

Hardenberg therefore was able to discharge during the year (1810-11) not more than 25 million francs of the indemnity, and at the end of May 1811 there was still left unpaid 59 million francs, toward which only slight payments were afterwards made.

§ 490. There remained the liquidation of arrears as promised to the Prussian subjects in the edict of October 27, 1810. As

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there was no cash on hand, payment was made in interest-certificates which were to mature in 1814 (3.75 million thalers). In salaries and pensions there were still about whve million thalers of arrears dating back of March 1809, the date at which regular payments recommenced. To cover this, too, bonds were issued to mature in 1814, besides an issue of about 1.50 millions in treasury notes. Finally, there were arrears payable on claims for supplies furnished the Russian army (1805-1807), amounting to nearly 13 million thalers. These were covered by bonds to mature in 1816, but which were in the meantime receivable at the treasury in payment of not more than two-thirds of the purchase price of national domains and the like.

Along with this vent a consolidation of the funded national debt, which was also completed on the basis of the free consent of the creditors. The edict of October 27, 1810, consolidated the various earlier obligations incurred into a new 4 per cent. security, the national bonds [*Staatsschuldscheine*]. These were not terminable at the option of the creditors; but it was stated that after the payment of the indemnity to France and the payment of the arrears of interest, a given Pearly sum has to be devoted to their redemption. The measure was a compulsory conversion, whereby the more advantageous conditions originally secured by the creditors (rate of interest and repayment) were altered. among these may be named the debts to the Society of Marine Commerce, which mere originally terminable on short notice and had originated as a kind of bank account, and had afterwards, through the unbusiness-like amalgamation of the national funded debt with the banking business of the Society, been changed into ordinary government securities, so that they now partook of the universal distress in which the national credit was involved. At the beginning of 1813 there were 20 million thalers of these new debentures outstanding. The remainder of the indemnity to France was cancelled by Prussia's undertaking the maintenance of the French and allied armies in their transit through the country on the expedition to Russia, February 12, 1812. By June 1812, 35 million francs had in

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this way been paid off in supplies. France then returned the mortgages on the domains. The chief means of revenue which was now employed was a mixture of a property-tax and a forced loan. The tax was to be paid at the rate of 3 per cent. on the property, that is, not much less than the full annual income; those who paid 2 per cent., however, were granted a remission of one-half of the remaining one-third per cent., and received in addition, to the amount of 1 ½ per cent. of the tax, a mortgage on the public domain bearing interest at the rate of 4 per cent.; they would therefore have paid, in point of fact, only 1 per cent. on their property as a tax, together with 1 ½ per cent. as a forced loan. It has already been noticed (sec. 312) how far the receipts from this tax fell short of the estimates (25 million thalers); there were actually received only 4.50 million thalers. Besides this property tax there was also levied a tax on personal income (5 per cent.).

In anticipation of the revenue from this tax there were issued at the middle of 1812 one million thalers of treasury notes and 3.50 million thalers of non-interest-bearing bills redeemable after January 1, 1813. These flowed back into the treasury in the payment of the property tax.

The supplies to the army from March 1, 1812, to March 1, 1813, amounted, so far as claims were allowed by the government, to nearly 25.50 million thalers. Of this 4.50 millions were placed to the account of the property tax, and what was called "pay-certificates" [*Kompensationserkenntnisse*] were issued to cover the rest.

§ 491. With the beginning of the year 1813 all energies had to be directed to the struggle against France; resort was then had - besides discontinuing the payment of interest to the creditors of the state - to an issue of paper money with forced circulation. Up to this time the treasury notes issued had circulated without coercion; during 1812 they had fluctuated between 80 and 48 per cent., and at the middle of January 1813 they stood

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at 48. January 19, 1813, an edict increased the issue of these treasury notes to 10 million thalers and made them full legal tender for all sums payable by the state. Their redemption was to be secured by the receipts from a new property and income tax which was to be paid quarterly, beginning with May 1813 and running for a year and a half, and at half the rate fixed for the tax of 1812. Although the government discontinued the further issue of treasury notes on March 5, 1813, when eight million thalers had already been issued, while at the same time some mitigation was made in the rigor of their legal-tender quality, they stood at 25 per cent. in July 1813. Supplies for the army were paid for with these notes, while officials were obliged to accept them in part payment (salaries and pensions of more than 400 thalers a year were paid one-fourth in treasury notes. On the other hand the treasury notes were received in payment of the property tax.

The property tax had to be given up. The voluntary payments brought in but a very inconsiderable revenue. The sale of domains, which had been facilitated by the ordinance of March 5, 1813, was equally ineffective in bringing cash into the treasury, because it had been decided to accept national bonds and treasury notes in payment of the domains in order to mend the national credit.

There was therefore nothing left but the forced loan and the requisition of contributions in kind to the maintenance of the army. The former expedient brought in four million thalers. The courts were formally enjoined from entertaining complaints for supplies seized for the use of the army. Not until July 1, 1814, were cash payments again made. Supplies obtained previous to that time were paid for in non-interest-bearing warrants, which were redeemable within the year (in 1814, one million thalers; beginning with 1815, two millions a year), but in point of fact they were exchanged for government securities under an ordinance of March 1, 1815, at a time when the government securities stood at 83-86 per cent.

The legal-tender paper money was redeemed after the fortu-

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nate turn of events that began in 1814. The ordinance of March 1, 1815 made the sum then in circulation (about six million thalers, worth 85-90 per cent.) receivable at its face value in all payments to the government, and full legal-tender.

The second victorious campaign against Napoleon was carried through without any funds for the maintenance of the troops. Resort was had to requisitions, even in the enemy's territory; while the English army paid for its supplies in cash.

But here with the feeble powers of the youthful commonwealth had passed what was, for a long time to come, to be the last severe test. Now succeeded a long period of growth and gathering of strength, during which Prussia's national credit gradually came to maturity.

§ 492. Let us now take a look at the disposition made of the Prussian debt after the close of the war.

In spite of the favorable termination of the war, in spite of the not inconsiderable share coming to Prussia (145 million francs) out of the war indemnity (500 million francs;) exacted from France, beside the indemnification received from friendly powers for the maintenance of their troops (50 million thalers), the exhausted country succeeded only very gradually (1815-1820) in bringing order into its debt, and even then only by the help of repeated loans obtained on onerous conditions from foreign countries.

The settlement of a great number of floating obligations had to be postponed. The first successful effort was that directed to bringing the treasury notes to par; they reached par January 13, 1816. On the other hand, it proved impossible to discharge the Russian bonds which matured in 1816 (issued in 1811, to an amount of nearly 13 million thalers, to cover the maintenance of the Russian army during the year 1806-7), a further extension of three years being required for this purpose. Something similar is true of the smaller loans issued during the war. In warrants issued for war supplies in 1812-1814 the government owed nearly 36 million thalers; the payment of these was not begun until the

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latter part of 1815. By the same time the option was offered of exchanging these warrants for 4 per cent. national bonds, and after the redemption of the warrants had come to a standstill in 1817 the government ordered (May 7, 1818) the compulsory exchange of the warrants for bonds which were at that time worth only 66-68 per cent., and so reduced the debt by about one-third.

And still it was necessary to obtain several foreign loans. In 1817 a loan of five million gulden was obtained from the banking house of the Rothschilds at 5 per cent. interest, in order to meet earlier obligations outstanding in South Germany. A much larger loan had to be contracted on account of pressing pecuniary embarrassments in 1818; this was arranged for with the Rothschilds in London by the Counsellor of the Finances, Rother: This amounted to five million pounds sterling and was disposed of at 71.86 per cent., with interest at the rate of 5 per cent., redeemable in early instalments within twenty-eight years and secured by mortgage on a correspondingly large extent of domains. These conditions were accepted because the terms offered by German contractors were still more disadvantageous to the state than those obtained in London, the terms offered being interest at 7 per cent., collateral security in the domains, and payment within a short term.

Still the government continued to draw on the Prussian bank, which had been a fellow-sufferer with the government ever since 1807 and had for this reason been prevented from meeting its obligations; it was not until 1817 that the bank succeeded in returning to a payment of interest, which had been discontinued in 1807. Still, the year 1819 closed with a deficit of 13.50 million thalers, and for the years 1820-22 the deficit was computed at 27 million thalers.

§ 493. The royal ordinance of January 17, 1820, sought to explain the state of the national debt and to strengthen the public credit by appealing to the people for support, referring in express terms to the control to be exercised by the "Estates of the Realm," which had been talked of ever since the reform period.

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At that date the national debt amounted, in round numbers, to 218 million thalers,<sup>1</sup> and was made up of the following obligations:

(1) The foreign loans of 1817 and 1818 from the Rothschilds, in round numbers 36 million thalers; (2) the old obligations of the Electorate, dating back of 1807, amounting to 3.23 millions; (3) domanial mortgages, 5.50 millions; (4) national bonds (the consolidated national debt), 119.50 millions, of which 56.60 millions were outstanding in 1820 and the remainder was intended to cover the floating debt. The national debentures in circulation before this time had for the most part originated in a forced conversion of the obligations incurred during the war period (15.70 millions for securities and stock of the Society of

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<sup>1</sup> The report submitted by the commissioners of the national debt, which was appended to this ordinance, says that an aggregate debt of 239 million thalers would be shown to exist [*motivirt sein würde*], and reports the following amounts:

(1) War indemnity to France and the expenses of armament down to 1813, 86.60 million thalers; (2) maintenance of the French garrisons for five years in the three forts on the Oder, 5.80 million thalers; (3) supplies and services rendered the French army in the campaign of 1812, 52 million thalers; (4) expenditures of the campaigns of 1813-1815, 61.60 millions; (5) expenses of general reorganization of the government 1815-1819, 50 millions; (6) sums required to cover the deficits in 1820 and succeeding years, 31.50 millions. That is to say, altogether 287.50 million thalers. Of this amount there had been raised up to date: (1) by extraordinary taxes, 23.50 millions; (2) by forced loans which were afterward converted into national securities, one million (forced loans, inclusive of amounts reimbursed or compensated for, amounted to 17.60 million thalers); (3) compensation received from friendly powers for maintenance of troops, 50.27 millions; (4) war indemnity from France and maintenance of Prussian troops in hostile territory, 65.50 millions; (5) sale of domains and secularized estates, 25.30 million thalers. That is to say, the receipts from extraordinary sources aggregated 165,50 millions, leaving 122 million thalers to be covered by other means.

To this is to be added: (1) the debts outstanding at the close of 1806, exclusive of the debts assigned to the territory lost in 1806, amounting to 49 million thalers; (2) the debts resting on the territory acquired since the Peace of Paris, amounting to nearly 68 million thalers. This makes up the aggregate debt of 239 million thalers which the commissioners of the national debt in 1820 counted up as "*motivirt*." It is to be remarked that in point of fact this statement of the obligations outstanding in 1820, as amounting only to two millions, omits many items of the floating debt. On the other hand there is included in these 217 millions 35.50 million thalers of which 27 millions were to cover the deficit of the succeeding years, 1820-1822, and also 4.50 millions intended to replenish the national treasure and four millions of non-interest-bearing debt.

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Marine Commerce alone); (5) the provincial public debts, 26 millions; (6) claims still unliquidated, 15.20 millions; (7) non-interest-bearing debts, 11.20 millions (,including six millions of treasury-notes outstanding); (8) sundry minor items.

Speaking of this national debt the ordinance of January 17, 1820, said (Art. II): "We declare this statement of the national debt to be definitively closed. No national bond nor national debt paper of any kind may be issued in excess of the sum herein given. Should the state hereafter be placed under the necessity of taking up a new loan for its own preservation or for the furtherance of the public good, such a step can be taken only with the advice and assent of the estates of the realm in assembly."

The national bonds were to be paid off at the rate of one per cent. a year. The yearly interest-charge<sup>1</sup> amounted to 7.60 millions, the charge for the redemption of the debt to 2.50 millions. The funds realised from the sale of domains were

<sup>1</sup>A review of F. Nebenius's work (*Der öffentliche Kredit*, 1820) in *Hermes* (1821, p. 160) computes the annual payments of interest by the various European states at that date. The amounts, expressed in millions of dollars-banco (= 3 marks-banco = 4.50 imperial marks = \$1.07), are:

Great Britain	145.
France	33.
Austria	7.
Russia	5.2
Prussia	5.
Holland	5.
Spain, Portugal, Italy, Sweden, Denmark and the minor German states	50.
Total	250 million dollars-banco.

Bender (*Der Verkehr mit Staatspapieren*, 2. Aufl. 1830, pp. 149 *et seq.*) computes that for the year 1829 the proportion of the interest-charge on public debts to the entire national income was as follows:

Great Britain	Three-fifths.
France	Five-nineteenths.
Russia	One-ninth.
Austria	One-sixth.
Prussia	One-fifth.
Hanover	
Baden	
Bavaria	
Württemberg	One fourth.
	One-sixth.



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devoted to this redemption, the amount being placed provisionally at one million a year; but in point of fact there was more than seven million thalers drawn from this source during the next three years. There still remained a yearly charge for interest and redemption of 4.50 millions. To meet this was the purpose of the tax reform of 1818-1820 (secs. 272, 275, 307, 308).

The 54.50 millions of national bonds which the government had to convert into cash in order to pay off the floating debt, were not disposed of without some trouble and shrewd management. Thirty millions were disposed of through various banking houses, but this was accomplished only by combining the feature of a premium lottery with the loan; in this way the bonds were sold at their face value. The remaining 24.50 million thalers were taken by the Society of Marine Commerce at 66.66 per cent., the Society obtaining the necessary funds by negotiating a loan of 3.50 million pounds from the Rothschilds in London, bearing interest at 5 per cent.; this loan being placed at a discount of 16 per cent., and with the national bonds as collateral security.

§ 494. The promise contained in the royal ordinance of January 17, 1820, went too far in one direction at least. There was a miscalculation (subjective or objective) with respect to the difficulties involved in getting the *Zuziehung der künftigen reichsständischen Versammlung*, or else with respect to the necessary recurrence of an occasion for borrowing on the part of the Prussian government.

The result was that the actual needs of the state during the next succeeding decades led to financial methods intended to mask the fact of a new national debt, and pressing necessities which could be met only by a public loan were not met at all by the government.

The first extraordinary armament in time of peace (1831), it is true, was covered by the national treasure of 1 t million thalers. But before that time (1824) the Society of Marine Commerce had built 125 miles of public highways for which they

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had not been paid. In order to place funds at the disposal of this institution it was authorized by an order in council of July 27, 1832, to contract a loan of 12.60 millions in the form of premium-bonds of 50 thalers each, bearing interest at 5 per cent. and payable between 1833 and 1857.

At the same time there were many undertakings properly belonging to the government which had to be neglected or left to private enterprise. The chief example of this is afforded by the beginnings of the railroad business in Prussia.

The redemption of the old debt went on; but the sale of domains was called on to contribute much more to this end than had been counted on in 1820. During the thirteen years 1820-1833 the funds actually derived from this source amounted to 24 millions, instead of the estimated 13 millions; the funds from the tax revenues amounting only to six millions. The later progress of the redemption was very similar; during the years 1833-1847, 38 millions were applied on the debt, of which 20.70 millions came from the sale of domains, 11.50 from taxes and six millions from interest saved on the discharged debt.

In 1848 the national debt amounted to 9.66 thalers per capita of the population (16.30 million inhabitants), as compared with 20 thalers in 1822 (11.66 million inhabitants). Still more gratifying was the case of the interest-charge. The growth of the credit of the Prussian state between 1820 and 1848, together with a favorable condition of the money market, made it possible in 1830 to convert the 5 per cent. debt to 4 per cent., and to convert these 4 per cent. bonds again to 3 ½ per cent. in 1838. The total interest-charge in 1833 was 6.40 million thalers, and in 1848 4.35 million thalers. The first loan, formally recognized as such, which the government attempted to contract, came up in connection with the calling of the United Diet (1847) and was intended for the construction of the Eastern Railway [*Ostbahn*]. But, on constitutional and fiscal-political grounds, it was refused, and so, together with so much else of the business brought before the United Diet, was laid over until succeeding years.

## II. OUTLINES OF THE EVOLUTION OF THE PUBLIC CREDIT.

The purpose of the foregoing survey has been to give a realistic picture of the actual course of development of public debts. For this purpose we have selected countries which are of great importance in this development, or which stand for typical stages of the evolution, such as Italy, Holland and Great Britain, making our account of the development in these countries the point of departure for a discussion of the affairs of our own commonwealth and the later growth of its public credit along the same lines. Our next task is to bring out the most important facts in the history of the development, so as to indicate the successive stages in the growth of public credit.

There are two features in which the public credit differs from private credit. The first of these is the relation of public authority to the loans negotiated for public purposes. The second is the relative permanency of the public body in quest of a loan.

The sequence of development with which we are occupied depends on the development of these two factors through the process of differentiation by which public credit comes to depart from its original identity with private credit.

In the first place, then, as regards the relation of the public control to the public credit, there is obviously a long step taken in advance when this public control comes to be so employed as to not discriminate in its own favor. A long course of experience may be required to inculcate the expediency of using this power of control with moderation, because only in this way will confidence in the government's good faith be firmly established. But the memory is not retentive of experiences of this kind, and recurring necessity is ever anew suggesting recourse to this treacherous use of power. And while it is true that after a great advance has been made along this line the public power is used with great regard for the demands of morality, it is also true that necessity and its temptations can never be quite done away; so that even at the height of the maturity of the state

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and of the public credit there always remains an undissolved residuum, within which breach of faith backed by force must of necessity remain triumphant.

As regards the other phase of the matter - the permanence of the commonwealth as compared with the individuals who make up the state; it is not on the fact of permanence alone, but quite as much on confidence in the continued existence of the state, that the growth of public credit depends. Long centuries of interminable struggles for supremacy precede the final recognition of such a stable continuity as is raised above all the changes and vicissitudes of sovereignty and of the lives of individuals. It is to be added that it also requires a long-continued growth of the commonwealth before the rulers for the time being come to recognize an element of permanency in their own government, such as to impose the necessity of honoring the obligations of the past while they may themselves in turn transmit new obligations to the future.

§ 496. The weight of these two elements will explain why private credit may reach a fair degree of development under the circumstances of a time and a people where the public credit is still in its infancy.

The element of force acts as a hindrance until it has passed through the refining evolutionary process. The element of permanence, while in its nature favorable to a growth of public credit as compared with private credit, cannot exert its favorable influence at this early period because it is as yet unrecognized.

On the other hand, there exist for a long time only oases of credit, lying within the restricted circle of commercial relations, while in the world outside the fraud and knavery of untamed natural man are constantly confounding the struggling growth of credit.<sup>1</sup>

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<sup>1</sup>The *Romancero del Cid* gives an instructive account of what were the knightly notions of honor that prevailed among the chivalry at the height of the Middle Ages, and that exerted an influence long after that time. The ideal of Spanish chivalry, Don Rodrigo de Vibar, had no money for his journey into exile. He accordingly called in

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The first of these striking facts in the historical development of the public credit is therefore the part played by the pledge in credit transactions.

At the outset, the pledge, in public as in private credit, must be a dead-pledge, so as to secure the creditor against any attempt on part of the debtor to violate the contract by physical force. Progress is seen in the fact that the articles which serve as pledges presently come to be delivered into the hands of the creditor, not *de facto*, but only *de jure*; then, little by little, comes an assignment of certain specified income devoted to having the interest on a given debt or to discharging the principal. So long as the creditor takes over the collection of this income (farming of taxes) there is an actual, and not only a virtual, pledge or pawn, though its terms may be laxer than those of the dead-pledge. As soon as the collection of the pledged income comes to be placed in the hands of the state, the creditor's security is removed from its previous physical basis, and this step therefore serves as introductory to the stage of the mature national credit where there is no longer any mention of such a pledge. The obligation of the state and the financial means at its disposal are, at this highest stage, securities that replace any and all pledges.

§ 497. The second feature of the development is the length of the term for which the loan is to run.

With respect to this point the change accomplished by the course of historical development is very great. At the outset, before the peculiar elements of strength belonging to the public credit have come into view, the condition is always made that, just as in private credit, the debt must be discharged very shortly - after a few months or years; the creditor has good ground

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two Jews and begged them with many blandishment to lend him a thousand gulden. As a pledge he left with them, as he said, two chests of plate which they were authorized to sell in case they were not redeemed within a year. The chests were locked, and contained sand. In full confidence, the Jews loaned him twice what he asked. The poet clears the honor of his hero by having him arraign the "*neccesidad infame*," "*á cuantos honrados fuerzas – á que por salir de ti - hagan mil cosas mal hechas.*" - *Romancero del Cid* (ed. A. Keller, 1840), p. 174.

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for anxiety and naturally wants to be paid. On the other hand, in the more advanced stages of growth it is the creditor that is anxious to postpone the repayment; there is no longer ground for the solicitude at one time entertained, the stability of the public credit has grown so great that all limitations of time are in contradiction to the growing financial strength and maturity.

In this evolution, as in all others, there are transition stages we have debts of long term, but secured by the pledging of public property or of income from the taxes. Then we have a long period of redemption without such a pledge. The plan of discharging the debt simply on the ground of financial expediency, to which the debtor state has accustomed itself, presently takes the place of redemption simply at the instance of impatient creditors. Finally the question of redemption comes by mutual consent to be left entirely undetermined.

Within this field, as on the broader field of credit generally, disturbances are constantly occurring; there may be a temporary relapse occasioned by disturbances of the peace, by wars, and the like, but after a brief interruption the progressing development resumes its wonted course. A war loan may perhaps be contracted on conditions of much the same kind that were the normal conditions in the same country some generations earlier, and after the lapse of a few years the special circumstances may again have disappeared. But the result of these variations of circumstance may be a very complicated and diversified practice in respect of the conditions on which loans are obtained, combining survivals of the past and the beginnings of future institutions (e.g., redemption within a given term but not until the end of another given term).

§ 498. The third great feature in the evolution of public credit is the progressive development of occasions and inducements to the contraction of public debts.

At this point the earlier public credit very closely resembles early private credit. In the early days it is usually distress, embarrassment, that leads to the contraction of debt. It is not

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as in the modern state when extraordinary circumstances may lead to the contraction of a loan; this necessity is in our day always associated with the consciousness that the ordinary financial energies are always, in the long run, adequate to meet this extraordinary demand. But where financial straits are the chronic condition, where the ordinary regular revenues are never sufficient to meet the regular expenses, still less to meet any extraordinary exigency, the case is very different.

The result is that in the early days of public credit we have the situation which is characteristic of the credit relation in early times - distress on one side and usury, either as actual fact or as a supposed fact, on the other side. The result for the state is partly that it finds itself compelled by circumstances to violate the traditional injunction of past centuries against usury (or to betray others into violating it), partly it yields to the ever present temptation to make use of its sovereign power to punish the usurers.

Under such circumstances it is of course impossible to have even a moderate development of public debt. The Italian republics, German towns of the later Middle Ages, the Netherlands of the seventeenth century, England in the eighteenth century, all these had long since passed this stage. The relatively orderly system of the finances, the abundant supply of loanable capital, and habituation to the institution of public credit, had removed the notion of usury outside the sphere of the public debt. All that is left is the notion itself, and the letter of the law with which scholastic legal erudition occupies itself in an attempt to harmonize two contradictory assumptions: the interdiction of interest, and the sovereign authority of the state.

In the course of the approach to a mature development there results not only harmony between the state's need of loans and its ability to repay them, but there presently comes into view a particular use of public credit which sets out with opening a source from which the means of paying the debt is to be derived; this is the productive credit of the state, the counterpart to that form of private credit which, both in theory and practice, most violates the prohibition of usury.

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§ 499. The fourth typical feature is the contrast between coercion and free choice in public loans - the varying degrees and stages of the coercion employed.

To the superficial view there is no continuity of sequence with respect to this point. At one end of the course of development we have an unscrupulous use of compulsion accompanying extreme scantiness of pecuniary means; at the other end of the course there is progressive substitution of the compulsory tax for the voluntary loan, coincident with a plentiful supply of loanable capital. In the former case compulsion is the result of physical need, in the latter case it is the result of a qualitative change in the moral factors on which the public economy rests.

This consummation of the development has so far remained an unattainable ideal even for the maturest of modern states, to which some approach has been made only here and there during periods of heightened patriotic sentiment (as in Great Britain at the beginning of this century); but be this as it may, on looking to the past growth of public credit we find that there has been a progress from compulsion to voluntarism, in the course of which compulsion has been dispensed with, and that gladly, as fast as it has lost usefulness in the negotiation of loans. This progress reaches its highest point where the great abundance of voluntary loans acts like a sweetened poison and tempts to the accumulation of debts. This stands out in extreme contrast to that scantiness of resources which tempts the undeveloped public economy to resort to compulsion, without being able to surmount its necessities even by this means.

If we compare Prussia with Great Britain at the beginning of the nineteenth century we have before us an instructive contrast between these two stages of development.

Enormous sums are voluntarily offered to the national credit of Great Britain on very moderate terms; whereas Prussia can scarcely obtain the minimum of necessary financial means by the method of voluntary loans, and the inevitable resort to compulsion, for the most part in the shape of redeemable forced loans and war contributions, never avails to cover the state's necessities. This condition of



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things in Prussia is of course not merely a consequence of poverty and of the disturbance of business that results from war; the difficulty is quite as much a lack of any productive national credit, which, if it existed, would not be restricted to domestic capital alone.

Under such circumstances the state, whose privilege and duty it is to assert and preserve itself at any cost and by any means available, has recourse, besides its unavoidable neglect of its financial obligations, to those expedients which are always ready to the hand of the national authority. It exploits its sovereign right of coinage, in order by this forcible means to obtain advances in the readiest way which the circumstances permit. With regard to this point, again, the growth of public credit and of public morals creates a succession of stages of development. The issue of light coin, the forced circulation of great quantities of the minor coins in place of the larger coins of full weight, the issue of paper money with forced circulation as a legal-tender on equal terms with coin, - these follow one another as successive stages in the growth of the Prussian national and military administration, crowded into the short space of half a century.

Each of these several stages may reach a more definite and characteristic development if the condition of the finances and of financial morals favor it. Or a relapse may occur even at a relatively high stage of the development, the degree of such a relapse being determined by the general political situation of the time. Compare the employment of the Assignats of the French Revolution with the forced circulation of the Bank of England. The former was a system of plunder whose basis was terror; the latter was an abnormality in the currency, perhaps avoidable, but at any rate appreciably mitigated by financial stability and a strong public credit, and not sufficient to hinder the growth of national wealth.

§ 500. The fifth characteristic feature in the development of public debts lies in the use and disuse of "relishes," gambling

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risks which are added in order to commend a public loan to the taste of creditors. Adam Smith pointed to the difference between England and France in this respect, to prove by an example of his own time that habits of productive industry and the sober commercial spirit favor those forms of public debts which promise a permanent, safe investment of capital; while an industrial dilettanteism naturally takes to the more doubtful forms of life annuities tontines, lotteries, premium-loans and the like. Even those who (as I conceive, too realistically) hold very different views as to the desirability of discontinuing the use of these "relishes," cannot deny the historical fact that the various countries with great unanimity discard the infusion of this gambling element in proportion as their national credit approaches a mature development. This implies a recognition of the principle that, under the presence of an undeveloped credit and the onerous conditions which attach to public loans under those circumstances, the state is not above employing these dubious fiscal expedients in order to adapt its credit to the circumstances and get its loans on easier terms. But so soon as the state reaches the stage of development where its credit no longer has need of this bait, and where capital is to be had in abundance at a moderate rate of interest, it discards these expedients as something unworthy of the present, and a discreditable reminder of the past.

In Great Britain this class of expedients fell into disuse about the middle of the eighteenth century, in Prussia and Germany not until the middle of the nineteenth century. In Russia they flourish today. The Central American republics, however, which (in the words of an English parliamentary committee) "are states in name only," consider themselves to have carried out a successful financial operation if they are able to obtain a loan for a term of years even by this means.

Even during the eighteenth century the Dutch had reached an appreciation of the fact that the national sale of life annuities involved a legitimate element of life insurance, besides the gam-

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bling element already alluded to; they had also, as we are aware, reached the point of view, which strikes us as extremely modern today, that it is proper and desirable even apart from financial reasons, that the state should undertake this class of business as an insurance business, rather than leave it to private enterprise. But it is to be added that we are today standing at a stage of the historical development where the private undertakings that replaced the rudimentary attempts made by the public finances, are enjoying a well-earned reputation for their services in this line; it is only the peculiarly restricted circumstances of the laboring classes that has latterly induced the state to enter this field.

§ 501. As a healthy body needs no medicine, so also it needs no physician. The feebler and less developed the national credit is the more does it need these stimulants and the physician to administer them.

In the character of the organs which serve the public credit, accordingly, lies a sixth characteristic trait which marks the stage of development of the public credit. One such characteristic of the modern stage of development of capital and of an international market for capital is the growth of organs with an abnormal fatty development, which owe their existence to the presence of great accumulations of capital on the one hand and needy states in search of loans but with poor credit on the other hand. These organs are, with great benefit to the state, sloughed off as the national credit approaches maturity.

The Barings, Hopes, Rothschilds are such organs. The enormous brokerage which they receive, as evidenced by their accumulations of wealth, is a mark of the unripe condition of things under which it has been acquired. They have received this broker's commission for pledging their own private credit in cases where the public credit of the state in search of a loan was insufficient; private credit in this case is therefore superior to the public credit, and this fact is sufficient evidence of the immaturity of the latter.

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This contrast is broadest, and the consequences most striking, where a state crosses its boundaries in search of a loan and, as has been customary ever since the Middle Ages, seeks out a country which is its superior in point of wealth and in the development of credit. Put this is a phenomenon which recurs, with typical constancy, to the same extent to which the various states and nations differ in the degree of civilization.

The individual state in the end attains to a degree of credit and accumulation of capital such that the very simplest organs and methods suffice to satisfy its need of loans on reasonable terms. Taking the aggregate of states together, there is every reason to expect that for an indefinite time to come differences will exist between individual states such as to make an exchange of deficiency and surplus advantageous or even necessary. The means of carrying out this exchange are at hand in the above mentioned organs of the unripe national credit. The greater the interval between the states in question, physically, culturally or financially, the more indispensable are these organs.

The exponent of this interval, for the purposes of the money-market, is the rate of interest charged. Just as a high price for corn attracts the cheap corn of another country and overcomes the cost of transportation, so a high rate of interest draws the surplus capital of a wealthy country with a lower rate of interest into the country which is in need of capital. The interests of the exporting and of the importing country go hand in hand in this matter, as they do in the case of other trade relations between different countries or regions. The difference lies only in this, that in an exchange of goods there is no other obstacle to be surmounted than the interval of space, whereas in the case of a transfer of capital this element of remoteness is of a much more complex character; it is not a question of physical distance only, but involves also both subjective prejudices and objective differences of culture, both of which may be of very different magnitude even where the physical distance intervening is the same. The interval of space between the United States of America and Europe is much greater than the distance between

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Egypt and Europe; but the demand for capital on part of the former country which Europe met during the war of the secession was backed by a state of civilization which placed that country in much closer contact with Europe, and which has by this time even put the United States in position to afford loans of capital to European states. It is a consequence of the historical nature of economic life that this exchange, just like every other international exchange relation, is forever subject to change. Even as late as the end of the eighteenth century Dutch capital was being invested in English public loans; since the beginning of the nineteenth century English capital is being loaned to all other countries. Prussia, once so needy of capital as we have seen it to have been even after the wars of liberation, has very lately been investing large amounts of capital in Russian securities.

Just as, in general, war sets a nation's industrial life back for the time being, so also on this particular point does rear bring out symptoms of an earlier stage of development. The great need of loans to pay the war indemnity, etc., during the years 1871-72, obliged the French Republic to fall back on what was to it an obsolete stage of growth, and go into the English market for funds; and in addition to capital borrowed from abroad it was chiefly French capital which had long been invested in foreign countries that was now under the stimulus of an enhanced rate of interest, brought home and put into French securities.

§ 502. If it can be said that History in any part of our scientific field favors us with an exhibition, in the present, of the varied phases of its past development, the proposition will hold with especial force in the case of the public credit.

In fact, the situation of the various nations of the world today shows us the entire diversity comprised in all the various characteristic phases which have prevailed in the history of the past.

If we look for the first crude beginnings we will find them in those volcanic national structures which, under a strong

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European stimulus, have developed a caricature of a civilized state, but whose future possibilities, it is to be remarked, are not to be denied by any impartial historical discussion.

Examples of such rudimentary structures have been brought before the public by the parliamentary inquiries concerning "Foreign Loans" (1875) in the states of Spanish America - Honduras, Santo Domingo, Costa Rica, Paraguay. Honduras was, upon the dissolution of the Central American Union, apportioned its share of one-sixth of a national debt incurred by the Union in London and Paris in 1825, amounting to 163,000 pounds sterling, but had, down to 1867, made no payment whatever, either on principal or interest. Still, this state entered the English market in 1867 to place a loan of one million pounds sterling (partly to pay off the old debt, partly for an ostensible construction of railways). The loan was negotiated by diplomatic agents, who either saved themselves from imprisonment only by the fact of their official position as ambassadors, or who had already been in custody. Banking houses in London and Paris lent them their aid, to the detriment of their credit and their good name. All the domains and the public lands of the state of Honduras were pledged; redemption was to take place within fifteen years, with interest at 12 per cent. The most questionable means were employed to tempt the investing public into the loan on the London exchange. Under similar circumstances and on similar conditions a loan of 2.50 million pounds was placed in 1870. The terms of the contract were observed only so long as was necessary in order to place the loans. In 1872 a further loan was attempted but failed. The securities declined in June 1872, from 72 to 44 per cent., and by July 1875 to six per cent. By this latter date Honduras was owing 1.25 million pounds in interest and nearly 5.50 million pounds as principal. Much the same is true of the republics of Santo Domingo, Costa Rica and Paraguay.<sup>1</sup>

There is here presented to us a complete clinic, including all the pathological phenomena of primitive national credit. What

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<sup>1</sup> Cf. *Zeitschrift für die gesammte Staatswissenschaft*, vol. xxxii., 1876, pp. 410-447.

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occurs in the history of the civilized states of Europe of a hundred years ago is here repeated and all exaggerated in an enormous degree. Financial straits, deception, default, eventuating in a hopeless nullity for the creditors. Where else than in France during the Terror of the Revolution is it possible to find in modern times a monetary system to equal that of the Black Republic of Hayti,<sup>1</sup> which has depreciated its paper dollars to a ratio by one to 6500?

Intermediate stages between these crude beginnings of national credit and the high degree of development which we find in modern Great Britain or in Germany and France, are to be found in the states lying geographically and culturally between Europe and Asia. These states present to our eyes the spectacle of what prevailed in middle and western Europe one or more centuries ago.

### III. THE DEVELOPMENT OF PUBLIC CREDIT AS REFLECTED BY CONTEMPORARY THEORY.

§ 503. It is the office of every science that deals with public life to be more than a simple reflection of facts and events. But it falls to the portion of every new science to be little more than that.

The writers of the age during which the science of finance and political economy came forward as a new science show us a reflection of the events of the time in the current theory of national credit. It is the historical facts that prepare the way for a broader theory, not the theory that prepares the way for the events. The process of development within this special field and the occasioning causes of the development are very similar to what we have found in the case of the income tax. The efforts of the English nation in its struggle against the French Revolution carried both these financial expedients to a height of efficiency such as to shame the theory of Adam Smith. Even Montesquieu, whose broad view in historical and political matters so greatly exceeds the horizon of many of the

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<sup>1</sup> Sir Spencer St. John, *Hayti or the Black Republic* (2<sup>d</sup> ed. 1889), p. 388.

thinkers of the eighteenth century, takes a deprecatory attitude towards public debts.<sup>1</sup> In his continual comparison of nations and peoples, it is true, he recognizes and acknowledges the advantageous position of a commonwealth such as the English state was even at his time, in comparison with other contemporary states. But while he enumerates the manifold disadvantages of public debts, and among them some which are frequently dwelt on even today,<sup>2</sup> he has nothing to say to the fact that there may be circumstances which will oblige the state to borrow.<sup>3</sup>

If we now turn to the authorities in financial science and economics we shall find that at the dawn of the scientific era there is by no means a dearth of profound discussion on the public credit. In England the practical importance of state debts had by the middle of the eighteenth century necessarily led the theoretical writers to go into the question. Not only Adam Smith (1776), but even to a much greater extent, his predecessor, Sir James Steuart (1767), denotes a considerable portion of his voluminous work<sup>4</sup> to this phase of finances.

The half century which separates this writer from Charles Davenant finds a summing up of its experiences in Steuart's works. Davenant, living at the time of the painful efforts put forth by the new régime, about the close of the seventeenth and the beginning of the eighteenth century to make use of the national credit, has a thoroughgoing abhorrence of state debts. He asserts that England's industry will not flourish until the greater part of the national debt has been canceled. A poor prophet; the growing prosperity of England during the next century years accompanied by a stupendous increase of the national debt, compared with which the amount which Davenant contemplated was but an insignificant beginning.

Not so Steuart. He gives a definition of the public credit which brings out the essential characteristic that distinguishes

<sup>1</sup> *Esprit des Lois* (1748), livre xxii. chap. xvii., xviii.

<sup>2</sup> "On ôte les revenus véritables de l'État à ceux qui ont de l'activité et de l'industrie, pour les transporter aux gens oisifs."

<sup>3</sup> "Voilà les inconvénients; je n'en connais point les avantages."

<sup>4</sup> *Inquiry into the Principles of Political Economy*.



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public from private credit. The public credit is confidence in a public body which borrows money on the condition that repayment of the principal can not be exacted, but that a yearly payment will be made, either as interest or as an instalment to apply toward the cancellation of the debt.

With this conception of the public credit Steuart takes a position directly opposed to Davenant, whom he considers the best informed man of his time, but who held to the view that a nation's debt, just like those of a private person, had best be redeemed within the year; the current view at that time being that the nation was in much the same position as a private individual, and the contracting of debts by the nation was consequently deprecated.

Steuart shows even a profounder insight into the new course of events in that he regards the development of public credit as an element of national strength which must be made use of by every state that is to assert itself in the struggle for national power. If a state resorts to a new contrivance, says Steuart, by which it is able to raise more money than before, the other states will be compelled to apply the same method. This is a truth which also today serves to explain so many things in the domain of European public debts and of the development of power by European nations; and on the other hand, it also serves to show the groundlessness of all excessive solicitude for the welfare of the people and finances of the several states, by inculcating the doctrine that financial exertion and its progressive growth is the elastic basis on which the development of power rests, instead of being an effect of power attained.

Indeed, Steuart possesses so large a gift of historic sense as to enable him to explain the views of Davenant on the ground of the economic and financial circumstances prevalent during his time. From a detailed comparison of the French national credit with the English he draws the conclusion that France has not yet reached the stage occupied by England.

While it is true that Steuart affords a faithful reflection of the brilliant advance of the English national credit at the middle of

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the eighteenth century, it is also to be said that his exposition shows conspicuous traces of the newness and unsettled condition of this financial institution. The dangers which he points out as surrounding the use of the public credit in his own country, the precautionary measures which he thinks necessary to be taken against bankruptcy or the repudiation of the debt, show the limitations of his view even though that view is prevailingly favorable.

§ 504. The different view of the state and its functions entertained by Adam Smith, as it appears in his discussion of the national economy, is probably the cause of his being more disinclined to the employment of national debts than his predecessor.

The standpoint of destructive criticism from which Smith is fond of regarding the doings of governments and Princes in general, characterizing them as spendthrift, foolish, arrogant, etc., could not be expected to incline him to a favorable view of national debts and the luxuriant growth of debts during his time. His radical view of wars and the occasions of wars must necessarily carry with it a radical view of the financial means requisite for them.

This fact infuses into the views entertained by Smith and his school on public credit a peculiar theoretical element, not an element fated to conquer and direct the facts, but one which the march of events has disregarded and passed over.

A lack of parsimony in times of peace, according to Smith; is the cause of the necessity of contracting debts in time of war.<sup>1</sup> When war supervenes there is no money in the national treasury. He extols the two Prussian kings (Frederick the Great and his father) as the only two among the greater princes of Europe who, since the death of Henry IV. of France, have laid by a considerable national treasure. The parsimony necessary to this purpose had been lost through the influx of luxury and the love of pleasure which had everywhere else followed in the wake of

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<sup>1</sup>Wealth of Nations, book v, chap. iii., vol. iii. p. 417.

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the development of industry and commerce. The Italian republics and the United Provinces of the Netherlands were in debt, just as the monarchical states were. The canton of Berne alone possessed a national treasure. For the lust of pomp and luxury holds sway in the senate of a small republic as well as at the prodigal court of the greatest of kings.

But while a flourishing industry and commerce hinder the accumulation of a national treasure, they foster a superabundance of business people who are always able to loan their own or foreign capital to the government. But this means a diversion of capital from the employment of productive laborers to the sustenance of unproductive laborers. The comforting doctrine that the payment of interest on the debt is merely a paying into the left hand out of the right<sup>1</sup> is a mercantile sophism, proceeding on the assumption that all the state's creditors are residents of the country; a supposition which will not hold for England, whose securities are in large part held by the Dutch and various other nations.

But even if it were true that the entire English Debt was held by inhabitants of the country alone, it would be none the less pernicious. Taking the greater part of the income from land and capital out of the hands of their owners in order to enrich the unproductive class of state creditors must in the long run result in neglect of the land and a wasteful expenditure or exportation of capital.

And this is proved by history. Genoa, Venice and the Netherlands were exhausted by their debts. Will the debt which has brought exhaustion or annihilation upon every other country prove harmless in Great Britain alone?

How far Adam Smith, in his criticism of the public credit,

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<sup>1</sup> The writer who formulated this sophism in the time of Adam Smith was Jean François Mélon, John Law's secretary, in his *Essai politique sur le commerce* (1734; 2<sup>d</sup> ed., 1736), reprinted in *Économistes financiers du XVIII<sup>e</sup> siècle*, published by E. Daire (Paris, 1843, pp. 707-835). Here we read: "Les dettes d'un État sort des dettes de la main droite à la main gauche, dont le corps ne se trouvera point affaibli, s'il a la quantité d'aliments nécessaire et s'il sait les distribuer" (p. 802). Voltaire, too, somewhere says: "Un État qui ne doit qu'à lui-même, ne s'appauvrit pas, et ses dettes même sont un encouragement pour l'industrie."

is affected by the conceptions of an earlier period is shown by the fact of his agreeing, to some extent even literally with his older friend, David Hume. Hume, in 1752, in his essay on "Public Credit," criticises the use of national debts in a decidedly hostile manner. "It would scarcely be more imprudent," wrote Hume,<sup>1</sup> "to give a prodigal son a credit in every banker's shop in London, than to empower a statesman to draw bills, in this manner, upon posterity." Hume had also remarked that the taxes which are levied to pay interest on the debt must either raise the price of labor or depress the working class; and that the national debt gives a great impetus to idle and unproductive living, since the greater part of it is always in the hands of idle people. He had also answered the sophism about the right and the left hand by pointing to the distinction of social classes which vitiates this seductive argument. He had denounced the strange equanimity with which all classes regarded the increasing national debt, and had made use of these strong words: Either the nation must destroy the public debt or the public debt will destroy the nation.<sup>2</sup>

<sup>1</sup> *Essays Moral, Political and Literary*. By David Hume. Edited by T. H. Green and T. H. Grose, London, 1875, vol. i. p. 362.

<sup>2</sup> A view similar to that held by Smith and Hume is also entertained by the third member of this group of Scottish scholars, Adam Ferguson. In the chapter on "National Waste" (part v. sec. v., *Essay on the History of Civil Society*, 1767; 7<sup>th</sup> ed., 1814, p. 391), he says: "States have endeavored, in some instances, by pawning their credit, instead of employing their capital, to disguise the hazards they ran. They have found, in the loans they raised, a casual resource, which encouraged their enterprises.

.... They have by these means proceeded to the execution of great national projects, without suspending private industry, and have left future ages to answer, in part, for debts contracted with a view to future emolument. So far the expedient is plausible, and appears to be just. The growing burden, too, is thus gradually laid; and if a nation be to sink in some future age, every minister hopes it may still keep afloat in his own."

Benjamin Franklin, too (Richard Hildebrand, *Jahrbücher für Nationalökonomie*, 1863, p. 648), is one of the writers who recognizes no difference between private and public credit.

On the other hand, it is worthy of remark that the philosopher Berkeley, a contemporary of Davenant's (*The Querist*, 1735, No. 233, 234) took a view of the English public credit similar to that afterward held by Sinclair and Pinto. He regards it as the chief advantage which England had over France and all other countries of Europe; hence all measures were to be scrupulously avoided which could diminish this credit. - Cf. Sinclair, *History of the Public Revenue*, vol. i. p. 355.

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§ 505. Adam Smith's question and Hume's prophecy were answered by events a generation after, but not in the way Adam Smith and Hume expected. Sir John Sinclair, the English writer on finance, who lived during the succeeding generation and was immediately occupied with public affairs as a member of Parliament, is consequently the representative of views on the public credit of a very different nature from those entertained by Adam Smith.

To begin with, Sinclair, looking at the matter from the standpoint of the new development and use of credit, denies the expediency of the national treasure which Adam Smith had so greatly commended. For a state with a slightly developed credit, says this writer,<sup>1</sup> a national treasure may perhaps be a necessity, on account of the difficulty with which any considerable sum is to be obtained at a critical juncture. But apart from such special cases it is more expedient to sink the surplus of the people's income in useful public works, or even in the building of useless pyramids (as in Egypt), than in a public treasure, laid by as a lifeless hoard, without interest and without circulation.

The experience of the latest times has shown that he went altogether too far in his estimate of what the public credit is capable of. And with respect to his polemic against David Hume, the succeeding century has shown the older writer, and not Sinclair, to be in the right (cf. sec. 169 above). Hume<sup>2</sup> says, in words which might have been written today, that the opening of the public treasure, as it produced an uncommon affluence of gold and silver, served as a temporary encouragement to industry, and atoned, in some degree, for the inevitable calamities of war."

But Sinclair's optimism is proved to have been in the right in contending, against Hume and Smith, that the public debt is, financially considered, a necessity and, economically considered, an indication of increasing wealth and confidence. For a thoughtful observer, says he,<sup>3</sup> it is scarcely possible to deny the

<sup>1</sup> *History of the Public Revenue of the British Empire* (3<sup>d</sup> ed., 1803), vol. i. p. 332.

<sup>2</sup> *Essays*, vol. i. p. 362.

<sup>3</sup> *History of the Public Revenue*, vol. i. p. 354

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beneficial results of the use of the public credit in the conduct of a just and unavoidable war. England's credit was the chief advantage of England over France and all the other states of Europe; it was a gold mine for England. If a state is enabled to raise great sums of money without difficulty, it can put forth the greatest efforts with the highest probability of a successful issue.

The limit which the men of Sinclair's time observed in their praise of the national credit lay in the dogma of an inviolable sinking fund. He commends - quite in the spirit of the full-grown public credit - the employment of perpetuity funds, leaving it optional with the state after a term of five to seven years to reduce the interest or repay the principal, it being a recognized fact that under circumstances of increasing wealth the rate of interest constantly declines. But for the preservation of the nation's credit a sinking fund is indispensable;<sup>1</sup> it should be entrusted to an independent commission, which is to be entirely distinct and disconnected from the officials who have to do with the placing of the debt. The sinking fund should be based on a large, stable and productive tax, bearing some relation to the wealth and to the debts of the nation. Peculiarly appropriate for this purpose is an inheritance tax, amounting to at least one-half the yearly income of the property. In addition to this, every means should be used to induce wealthy persons with no near relatives to bequeath their property to the state; "The effects of such a measure, especially in wealthy and commercial nations, would be almost incredible."

§ 506. Even before Sinclair's time, the anonymous but well-known author of the *Traité de la Circulation et du Crédit*,<sup>2</sup> the hitch writer Pinto, reflects in his writings the marvels of the Dutch and English public credit of those times.

Pinto is the practical man of the money market of the eighteenth century. His method of thinking on economic subjects

<sup>1</sup> Vol. i. pp. 377-378.

<sup>2</sup> Par l'auteur de l'essai sur le luxe, etc. Amsterdam, Marc Michel Rey, 1771.

betrays the experience and impressions of the world's money-market. His polemic, principally directed against the Physiocrats, is effective at those points where practical experience is opposed to abstract ideas of reform; he is one of the most decided and readiest opponents of the *impôt unique*.<sup>1</sup> But his discussion is less felicitous and shows the limitations of practical business logic, when employed on the profounder questions of principle. The wide interval there is between Pinto's discussions on money, circulation, etc., and the lucid exposition of Turgot's work,<sup>2</sup> which preceded Pinto by a few years, will serve also to explain the oft-mentioned exaggeration with which Pinto speaks of the importance of the public credit.

This exaggeration is, in fact, to be taken as nothing more than the reflection of contemporary phenomena in the brain of a man without scientific training; in part the exaggerated statements are to be construed in their proper organic relation to the world as a whole, and the work taken as a whole goes to show that so shrewd a man of affairs does not readily make nonsensical statements of the kind often imputed to Pinto. His work is in substance a panegyric of the English national debt, and he clearly comprehends the basis, presuppositions and limitations of this debt, and sets himself the task of explaining England's advantage over other states, especially over France, from these circumstances.

Pinto makes the rash statement that the public securities become capital, just like a piece of land or a building; they yield interest without expenditure for repairs, or cultivation.<sup>3</sup> In another place he says:<sup>4</sup> With every loan which it places, the government of England, by setting apart a portion of the taxes as security for the interest, creates a new artificial capital which did not previously exist, which is enduring, stable and sound, and

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<sup>1</sup> He combats the Marquis de Mirabeau especially, pp. 129 *et seq.*, 149 *et seq.*, 157, 162 *et seq.*, 186, 200, 203 *et seq.*, 207 *et seq.*, 214-219.

<sup>2</sup> *Reflexions sur la formation et distribution des richesses* (1869).

<sup>3</sup> "Les fonds publics deviennent des biens fonds, tout comme une terre et une maison; ils portent intérêt sans exiger ni réparation ni culture," p. 148.

<sup>4</sup> P. 44.

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which, on the strength of the public credit, circulates among the public with the same advantage to them as if it were a veritable hoard of coin which the country had acquired.

This preposterous notion might serve to enforce upon the "practical" men, as well as the "historians," that in order to resolve economic phenomena into their simplest elements it is necessary to have been trained to economic thinking. But Pinto is far from drawing the rash conclusions warranted by such a position, or even admitting them.

In all these statements he is always speaking of the English national credit of his time. It is not the public credit, says he in answer to Mirabeau, which has destroyed France, but simply the fact that no such regard has been paid to the necessary conditions of public credit in France as in England; it is therefore the lack of credit that has injured the French finances. Foremost among these conditions is the sacred observance of all obligations,<sup>1</sup> and, further, the appropriation of certain specified revenues to the punctual payment of the principal of the debt and unreserved publicity, by which the government may gain and retain the public confidence. The means of lightening the burdens resting on the people are not<sup>2</sup> primarily a radical tax reform, least of all the Physiocratic scheme, so much as a protracted period of peace and an economic administration of the finances.

Even as regards the English administration of the public debt he takes exception to the fact that it made no provision for a permanent sinking fund; that if wars, and consequently national loans, were to follow one another in rapid succession so as not to leave time for the greater part of the debt to be canceled during the interval, the machine might collapse and bring ruin upon the country.<sup>3</sup>

The substance of Pinto's thinking on the public credit, what he means by his obscure statements concerning a "newly created capital," is really the well-founded conviction that, in the first

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<sup>1</sup> P. 170-173, 102.

<sup>2</sup> P. 165.

<sup>3</sup> Pp. 102-104.



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place, certain conditions must be fulfilled in order to a plentiful public credit, and, in the second place, that the employment of this credit would enhance the efficiency of the available capital. Even a hundred years after Pinto's time the English writer Macleod and others have identified this moral power of credit with actual capital (by the aid of the untenable notion of an "immaterial capital").

§ 507. Leaving the English national credit and the theories built upon it, we come now to a writer on finance who reproduces in his writings the results of French financial practice of the pre-revolutionary times. This is the French minister, Necker. With Pinto and the English writers the French national credit serves as a contrast to the English, and brings home to the enthusiastic admirers of the English national credit the conditions and limitations of all public credit. With the French finance minister it is his own experience that serves to bring out the dark side of this new and brilliant institution.

Necker<sup>1</sup> not only opposes the favorable view of national debts that was coming into vogue in his time so far as regards the French finances. He goes on to generalize, and extends his criticism and objections to all national debts, and applies his objections especially to the English debts. He points out the disadvantages attaching to the English public credit as compared with the French. So, for example, he remarks that England owes more to foreign countries than France, with the consequence that a great part of the interest paid is consumed in foreign countries.

Necker lays great stress on the divergence of interest between the state's creditors and the taxpayers. In answer to the light-hearted view that the payment of taxes to the creditors of the state amounts to nothing more than a change from one hand to the other, he remarks that the relations between the different members of society are not like the relations between the individual grains in a heap of sand, which can be altered at will.

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<sup>1</sup> *De l'administration des finances de la France* (1785), vol. ii. pp. 371-383.

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Is it a matter of indifference, he asks, if great changes in ownership are wrought, whereby the property of those who are attached to the soil and to the country is diminished and new accessions of wealth are created for the class of people known as annuitants, who can readily become citizens of any country? The growth of national debts has done much to destroy public spirit, by increasing the number of those persons whose interest is opposed to the public welfare.

Within moderate limits the use of the public debt might become a means of enlarging institutions of public utility. But the debts have been made an instrument of political and military ambition. They have made it possible to expend two or three hundred millions, where forty or fifty millions could perhaps have barely been raised by means of extraordinary taxes. Nations ought to enter into a compact never to contract loans in order to carry on war against one another. A very amiable wish! One might just as well propose that the different governments should agree to discontinue the use of cannon. There is better reason to hope that the greatness of the evil itself would set a limit to it and that the nations overburdened with enormous debts, and taxes to correspond, would be compelled to call a halt.<sup>1</sup>

How very different is this discourse on public debts from what the financiers of England and Holland have to say on the same topic!

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<sup>1</sup> It may be remarked by the way that loans were spoken of in France a few decades later as unnecessary and objectionable, in an official document of Napoleon's. In the decree on the establishment of the tobacco monopoly, of December 29, 1810 (*Anlagen* to the Report of the Tabak-Enquête-Commission des Deutschen Reiches, vol. iii. *Anlage* xii. p. 114), there is a pompous declaration to the effect that: The most enlightened nations had resorted to national loans as an expedient under extraordinary circumstances; this expedient, however, is both immoral and fatal; it imposes a tax on future generations, undermines the state, etc. We, it goes on to say, have adopted a different principle. We have established a system of taxation in times of peace, which is constructed out of a variety of taxes at moderate rates, and rates that are not oppressive, but that can be increased in case of a war, and so are capable of meeting the vicissitudes of the bitterest war. Such is the salt monopoly, and such is also now the tobacco monopoly.

Along with the public loan, extraordinary war taxes were also to be superseded by this system, for the reason that the latter are both unproductive and, at the same time, likely to fail at the critical moment.

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A similar attitude of opposition is taken by a considerably later French writer, Jean Baptiste Say,<sup>1</sup> who took the lead in introducing the political economy of Adam Smith into his country.

So far as regards the detriment to the taxpayer, there is, according to Say, no difference between a public loan and a tax; the former is somewhat the worse in that the taxpayer has to pay not only the entire amount of the principal but the costs involved in discounting future taxes. The increase of taxes raises the price of all articles, which is equivalent to a general impoverishment (*appauvrissement général*) generally. The conclusion is therefore that public loans doubly impoverish the future. Against the claim that public debts encourage people to save, say objects that it could much more truly be said that public debts dissipate capital by drawing into "the abyss of the public expenditures" capital which would otherwise be employed, though at a lower rate of interest; for some purpose of human use or comfort.<sup>2</sup>

Proceeding still further in his opposition to the views then in vogue, say, quite in the spirit of the orthodox school, rejects the argument that public loans serve to keep capital within the country. He says: Let the capital go abroad, by all means, rather than that it should stay and oppress our taxpayers!

Say follows Necker almost to the letter in charging national loans with having greatly favored the lust for conquest and war.

§ 508. We come now to the German writers on finance, the first one to be mentioned being J. H. G. von Justi.<sup>3</sup>

Justi, the ablest of all the German Cameralists, approaches the questions involved in the public credit from the standpoint of a man who is familiar with the remarkable results achieved by the Dutch and English through the employment of national debts during his time, and has at the same time intelligently studied the peculiar and divergent circumstances of the German

<sup>1</sup> *Cours complet d'économie politique pratique* (1829), vol. vi. pp. 128-167.

<sup>2</sup> "à des placements dont le revenu serait l'utilité ou l'agrément des familles."

<sup>3</sup> *Staatswirthschaft* (1755), 2. Theil, pp. 428-444, 587-608.

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states, as he has encountered the facts in his own rich and varied experience.

This point of departure is the question of the alternative which offers itself to the state under unusual circumstances and exigencies: extraordinary taxes, or state debts. He is disinclined to the usual forms of extraordinary taxation, especially the property tax (the ascertainment of the property of all subjects would take time, and in case the attempt were not to be nugatory this ascertainment must be under oath, which would require still more time; and even then there would be no end of perjury, not to speak of the fact that the publication of their pecuniary circumstances would be very detrimental to merchants and many other subjects, and would be highly distasteful and objectionable to all). In all this he describes the facts as we meet with them in Prussia half a century after his time.

Hence the necessity of public debts. If the government has no credit, says Justi, the state suffers from a great and pervading injury. It is therefore one of the first principles of action for any wise government to keep its credit perfect. And this purpose is served almost exclusively by the prompt payment of interest. For every creditor considers his money safe and has no desire to make any change so long as interest is punctually paid. In this respect the case of the state's creditors is very different from, that of the creditors of a private person. No one is concerned about the question whether the state is able to pay all its debts; if only the interest is properly paid the creditor can transfer his claim to some other person, so that the claim is always as good as coin. The astounding debts owed by the state in England and Holland are well known all over the world, and everybody knows that it would be impossible to redeem these debts in case all the creditors demanded payment at once. But these states do not on this account suffer for lack of credit, and they could readily, at any hour, add many millions of new loans to the old debts if necessary, simply because the interest is punctually paid. Justi, too, strongly favors an independent sinking fund commission, like the other writers of the `Vest of Europe whom we

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have already mentioned. It would be better, in his opinion, if the business of paying the debt, in great states where there are large debts, were entirely disconnected with the exchequer, and a special commission were appointed, to consist one-half of skilled financiers and the other one-half of learned and conscientious men trained in the law. Such an arrangement, he says, is to be found in the Austrian states, and its usefulness is very evident.

If, therefore, the national credit is perfectly good, nothing is easier than to raise any required sum under all circumstances. It needs only to publish the fact that the state will receive so and so much money, and creditors in abundance will present themselves and freely offer their money even beyond what the state desires. The experience of Holland and England is evidence of this fact.

§ 509. While Justi points to the highest perfection of the public credit to be found in Holland and England as the goal of the development, he falls short of this level by several degrees in his discussion of details, and takes us back, on this head, into a different and remote age.

The bridge by which the higher development is to be reached is to be constructed out of financial expedients which had already been discarded by this more highly developed public credit, but which were yet to be introduced into German and Austrian finance administration. Annuities, tontines, lotteries - the essential principle of all these, the spice of chance which they contain, is treated by Justi with characteristic expressions of approbation. Many respectable writers, says he, have made what are in fact specious objections to the morality of institutions of this sort (referring particularly to the lotteries; but it is not opposed even to the strictest principles of ethics to entrust a superfluous portion of one's property to the chances of fortune, otherwise we should be able to carry on but very few branches of trade. The state may properly assume that everyone will make use of these institutions according to the dictates of duty; at any rate it is not the state's

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duty, nor does it lie within its power, to prevent their using them to excess; and in case it were to block this road, they would find a hundred other ways of misusing their wealth. And in case the government were to exclude establishments of this kind from its own territory, it would by so doing accomplish nothing more than to divert a great deal of money to other states.

Justi counts this fiscal expedient among those which a government must use when in possession of a "perfect credit." But where such a credit is absent, what is then to be done?

One of the most usual means in such a case is that of farming out all the revenues of the state and receiving the farm-rent in advance. Such a method was in almost constant use in France, but that was an evil state of affairs and the French farmers general were looked upon by everybody as leeches sucking the blood of the people. Very similar is the method of pledging the domains or leasing them for a long term. It is preferable to pawn the royal heirlooms and crown jewels, or even to sell them, as it is easy to replace them when times are better again, and probably at a lower price, as the supply of jewels is constantly increasing.

The most desperate of all expedients is for a state in financial straits to raise money, as a last resort, by the alienation of territories, provinces, cities, or fortifications, to other states. During the Middle Ages this occurred quite frequently, and many dominions grew great by this method; but nowadays the claims of national sovereignty and integrity are regarded as quite priceless and not to be offset by any sum of money. In order to avoid such extreme necessities a national treasure must be accumulated. It is a great misfortune to any state not to be in possession of an adequate treasure. Circumstances do not always admit of the state's obtaining the necessary funds from its subjects, or by the use of its credit. At any rate the state may suffer the greatest misfortunes before it is able effectively to do so. Hence it is imperative to make a seasonable provision for the accumulation of a treasure, and this work must take precedence of all expenditures that are calculated simply to serve some purpose of use or convenience. It is true, certain

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writers had expressed the opinion that the devotion of the subjects might take the place of a treasure, through the subjects coming to the assistance of the sovereign with their possessions in time of need. But Justi would advise no sovereign to depend on such a support in case of real necessity.

The extravagant importance which Justi ascribes to a national treasure shows how far behind Sinclair and others he still stands, and how greatly he is bound by the circumstances of the German principality of his day. The whole substance of the power and suzerainty of a monarch, according to Justi, rests on this national treasure; all his negotiations will carry an added weight when it is known that his power is sufficiently backed by force. Here again what holds true of a person in private life holds true of the sovereign: where there is money it is possible to accomplish something.

§ 510. The German Science of Finance, which followed in the footsteps of Justi and Cameral Science for a hundred years after his day, down to Rau and Roscher, followed him very closely also on the head of the national credit.

There is a painstaking collation and comparison of the various facts of political and financial affairs, of the experience of foreign countries, especially England, with the experience of the German states, in all of which the homespun practicality of the writers gives a preponderant importance to the homely facts of their own immediate surroundings. This characteristic also furnishes an element of moderation, as contrasted with the dogmatism fostered by Adam Smith and his school, especially as opposed to their one-sided disapproval of all development of state activity and of the development of the financial means necessary to such activity.

Theodor Schmalz<sup>1</sup> may be taken as one of the most radical of these writers. He was a campfollower of the Physiocrats and

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<sup>1</sup> *Handbuch der Staatswirthschaft* (1808), secs. 419-432. The book is full of extravagant statements. The following is a sample: "Nothing but a straining after paradox, or the most inveterate bigotry, could lead anyone to defend the tobacco monopoly" (sec. 382).

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the representative of the science in the new University of Berlin. And still, even his judgment is influenced by his Prussian surroundings and by the circumstances of the time.

A statesman, says Schmalz, must always look upon debts as a great evil, to which he can resort only under stress of great necessity, viz., the impossibility of meeting extraordinary demands by means of taxes. But in such a case he must not fear the evil, as it can be rendered quite harmless by a proper exercise of sagacity. For the fact is that the oppressive character of debts is simply a result of the manner in which they are contracted and the method by which they are redeemed.

Schmalz accordingly sets up the requirement that the debt must be paid by the generation by whom it was contracted, and that a sinking fund must therefore be established; and if the state is in so fortunate a position as to have paid off its debts, then it should turn its attention to preventing future debts by accumulation of a treasure. What has been said in derogation of such accumulated treasure originated in the erroneous notions of the Mercantilists, who conceived money alone to be capital, and then, on the ground of this premise, talked about capital lying idle.

§ 511. More moderate, and more nearly approaching the facts of the case, is the view of Ludwig Heinrich von Jacob.<sup>1</sup>

While Schmalz still adhered to the opinion that public debts could be avoided by the accumulation of a war treasure, Jacob, on the other hand, makes the war treasure his point of departure, and argues from the limitations and inadequacy of such a treasure to the indispensability of public loans.

Jacob enumerates the reasons for and against a national treasure in the fashion which K. H. Rau's usage has since made typical, and concludes that the reasons against preponderate. He admits that many good financiers had proposed to provide themselves for times of war with a treasure large enough not only to

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<sup>1</sup> *Die Staatsfinanzwissenschaft, theoretisch und praktisch dargestellt*, vol. i. (1821), secs. 728-825.



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cover everything that is required for the opening of a campaign, but even to defray the expenses of several campaigns. But as contrasted with the savings of private persons, such treasures lie idle, to the detriment of the finances and of industry.

Accordingly, if a state is able to provide the means for an expeditious conduct of war in other ways, then it may properly dispense with the treasure. Such is the case with any wealthy nation, where there is a great accumulation of capital and an unquestioned confidence in the government. Under different circumstances the accumulation of a treasure in times of peace is desirable and necessary. But in our day such a treasure will probably never be large enough to go far. For one thing our states are generally not in a position to think of accumulating a treasure, and for another, the wars of our time are much more expensive than formerly. The state will accordingly always have use for its credit. It is therefore a matter of the first importance for every state to establish its credit on a firm basis.

Jacob enumerates the means by which this firmer basis for the public credit is to be established, in the same long-winded fashion as Justi, who preceded him by two generations. These long and elaborate prescriptions, which rehearse what is matter of course to the German state of today and to the English state of that time, are but the symptoms of those diseases of childhood from which the German public credit of that time suffered. The ever-recurring asseveration that public debts, although a necessity, are an evil, that the public creditors live on the product of the people's industry, that national debts have a detrimental effect on production, that they are a dangerous financial engine in the hands of an ambitious or wasteful government - all these are little else than evidences of the influence of the Smithian school.

On the other hand, a decided progress on the part of the German political and financial organization since the days of Justi is indicated by Jacob's position, that a powerful state will not readily resort to any other method than that of borrowing on its own credit simply, without the pledging of specific portions

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of its property or revenues. A similar progress is indicated by the position that "the principles of sound policy demand" that the state should dispense entirely with annuities, tontines, and other like means of raising funds, and rather place its loans in such a way that the creditors, instead of being repaid their capital, will receive simply the interest on it. It is also to be considered a relative advance that the "funding method invented in England" is commended as an indispensable means of maintaining a perfect national credit, the method consisting in this, that a loan is not put upon the market until a specific source of revenue has been set apart for the payment of the interest and the establishment of a sinking fund.

§ 512. The work of Friedrich Nebenius (*Ueber die Natur und die Ursachen des öffentlichen Kredits*<sup>1</sup>) is in the form of a monograph on the subject, which it treats in the school-book fashion so much in vogue in Germany at that time. It is also in point of its content a faithful expression of the circumstances of the author's time and surroundings, but somewhat clearer and more definite than is to be found in the works of his contemporaries.

We are told that the expenditures demanded by a modern war are too great to be met by an accumulation of treasure, and at the same time the greater activity of industrial life, which now absorbs all available capital, has made such accumulation inexpedient on other grounds. Credit enables a nation to employ its energies on the offensive or the defensive, and to concentrate them upon a given point at the decisive moment. In cases where no lucky turn of the fortunes of war shifts the burden to the losing party alone, it will always be necessary to draw on the future. Credit, therefore, adds to the political power of the state.

After the events of the successful war against Napoleon there was added ground for the admiration with which the German

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<sup>1</sup> *Der öffentliche Kredit. Zweite Auflage, Erster, allgemeiner Theil* (1829). The second part, not published, was to treat of the History of Public Debts, while the first part is occupied with the general discussion. The First edition (1820) contained both parts in one volume.

<sup>2</sup> Chap. v. sec. 7. pp. 249 *et seq.*

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Cameralists had looked upon the English national credit even as early as the middle of the eighteenth century. Without prejudice to the gratitude due the liberator of Europe, says Nebenius, we may well ask if, in the absence of the credit which the British government was able to use to such stupendous effect at the critical moment, events would not have taken a different turn in Europe, unfavorable to the independence of the European nations.

Every state should therefore take thought to maintain and strengthen its credit. Upon the conclusion of a war the next step is to proceed to the redemption of the debt; history teaches that it very rarely happens that a single generation is exempt from this disease of human society. And this method will moreover conduce to greater moderation, because the same generation which has contracted the debt must count on contributing to its redemption. Experience also teaches that representative institutions are no defense against a progressive accumulation of debts, but they are good security for a faithful observance of obligations entered into.

Nebenius is a writer who solemnly emphasizes the importance of good faith and honesty for maintaining and strengthening the public credit, and this makes the unconstrained way in which he (quite different from many of his contemporaries) judges of the sinking fund all the more remarkable. What is of avail is not those schemes that are constructed to run for several generations and are never adhered to; but rather, the point of importance is the relation in which the interest on the debt and the other national expenditures stand to the resources of the country, that is to say, the means available for the redemption of the debt after these other demands have been satisfied. People are prone to believe that they have cleared themselves of the debt as soon as they have made provision for the interest and the sinking fund; but they forget that the values which the public accounts present as an increasing sinking fund are not a product of the amortization office, but are drawn annually from the people's income.<sup>1</sup>

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<sup>1</sup> Similarly Lotz, *Handbuch der Staatswirthschaftslehre* (2<sup>d</sup> ed. 1838), vol. iii. pp. 475-477. About the time the second edition of Nebenius's work appeared obligatory redemption was abolished in England, by a law of June 1, 1829.

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But Nebenius is all the more the spokesman of a bygone age when in a painstakingly elaborate chapter on the sundry aims of operations in public credit, he remarks with regard to loans for productive purpose,<sup>1</sup> or what we have called "productive credit" in the stricter sense (sec. 162), that experience condemns the undertaking by the financial administration of such productive enterprises as come into competition, ordinarily into disastrous competition, with private industry. The few exceptions which must be admitted are, taken as a whole, of no consequence. And even of these (highways, canals, etc.) it has become possible, through a progressive accumulation of large bodies of capital in the hands of single individuals, and through the increasing facility of combination, to relegate a good portion to private industry.

What Nebenius has in view in his reflections on the influence of public loans upon the industrial situation, is the German industry of his own time and its scanty supply of capital, and he views this situation in the light of that exaggerated sense of the importance of private production which was then so much in vogue in economic science. This is the ground of the proposition<sup>2</sup> that: Public loans destroy capital which has been accumulated by industry and thrift, and in so doing they deprive society of an important means to the improvement of its condition; just as the beginning of all civilization is conditioned upon the capacity of men for the accumulation of capital, so it is also true that all progress of any people in welfare and happiness essentially depends on changes which take place in their fund of accumulated capital. The very existence of a considerable national debt, says he, affects production detrimentally, particularly by the resulting increase in the number of persons who withdraw their energies from the services of production - that is to say, on the one hand the creditors of the state, with the persons who serve their luxurious mode of life, and on the other hand the numerous official class who perform the unproductive labor of collecting the taxes.

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<sup>1</sup> Pp. 29, *et seq.* (chap vi. sec. 2).

<sup>2</sup> Chap. x. secs. 5 *et seq.* pp. 669 *et seq.*

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Further it is worthy of remark that Nebenius approves<sup>1</sup> of lottery loans (on the lines of the financial practice of Baden,<sup>2</sup> 1820, 1840, 1845) provided that no great favors are conceded to the lucky numbers, no more, for example, than the interest on their investment, and provided that the principal remains unimpaired, and also provided that the shares are not altogether too small. The third of the lottery-loans issued by Baden, during Nebenius's lifetime, contracted in 1845 in order to provide means for railway-building, consisted of 400,000 shares of 35 gulden, to be redeemed by means of four drawings a year and canceled within forty years; this loan was issued at 3 ½ per cent. interest and was taken up at considerably above par (110 ½ per cent.). Regenauer, in fact, remarks that "the demand for interest-bearing obligations was for the first time fully met by the loan of 1842; the demand for lottery shares should in all reason be decidedly more active. Still this was Baden's last lottery loan.

§ 513. C. A. von Malchus (Royal Finance Minister of Wurtemberg) wrote<sup>3</sup> unreservedly from the standpoint of the financial practice of his time.

According to Malchus, in the existing state of all political relations, internal and external, a more or less extended use of credit is a necessity for all states, and especially for the larger states; it is a necessary and effective means for consolidating political power. Still, a large national debt is "a canker which consumes the political energy and the wealth of a nation," and will sooner or later destroy it. It is, of course, less detrimental where there is a sufficient surplus of capital to prevent the contraction of a national loan from trenching on the increment of capital demanded by industry; but it is all the more disastrous in countries not so favorably placed. There is, accordingly, no financial measure which is less confidently to be justified

<sup>1</sup> Chap. vii. sec. 9, pp. 343-353.

<sup>2</sup> Regenauer, *Der Staatshaushalt des Grossherzogthums Baden* (1863), pp. 689, *et seq.*; cf. also pp. 206 *et seq.*

<sup>3</sup> *Handbuch der Finanzwissenschaft und Finanzverwaltung*, (1830), *Erster Theil*, secs. 80 *et seq.*

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on the simple plea of its successful employment in other countries.

The idea of a national treasure is, for Malchus, an obsolete notion, just as it was to the greater number of his contemporaries and to the financial administrations of his time. He discusses the various forms of national debts dispassionately and concisely, and explains the nature of annuities and lotteries also with considerable breadth of view. He lays stress on the requirement that loans must not be made terminable at the pleasure of the creditors, but insists also on the great value of the sinking fund.

Johann Friedrich Eusebius Lotz,<sup>1</sup> the contemporary of Malchus, Nebenius and Jacob, goes into a detailed criticism of the expedience of a national treasure. The example of the ancients, says he, cannot be appealed to with any effect; their treasures were accumulated from a source which is available only in the very rarest cases in our time, viz., the spoils of a conquered enemy. And the possession even of the richest treasure cannot afford a modern nation the same degree of security that a nation derives from its wealth and culture; and these factors in turn presume as low a rate of taxation as possible.

Of all expedients in times of need the contracting of debts is the least objectionable. This means has the advantage over forced loans, anticipation of revenues, and the levying of extraordinary imposts, that it ordinarily diverts to the government only the floating capital and especially that belonging to the wealthier classes. It can, therefore, "never have a particularly detrimental effect upon the regular course of the nation's industry." Indeed, if it brings out capital which has previously been lying idle, or brings in capital from abroad, it is even conceivable that it will act to quicken industry for the time being.

It is however to be added that the loan results in a heavy burden of taxation, and the ease with which they can borrow has tempted many governments into a wanton contraction of debts. It is a sore grief to any one who has the welfare of the nation at heart to see that individual politicians have so far forgotten

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<sup>1</sup> *Handbuch der Staatswirthschaftslehre* (2<sup>d</sup> ed. 1838), vol. iii. sec. 146.

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themselves as to incite our governments to an unnecessary contraction of debts, by advocating the doctrine that public debts always increase the wealth of a people, and that there is no sounder means of furthering the nation's wealth and welfare than to borrow without stint.

Lotz accuses Pinto particularly of this "scarcely intelligible nonsense;" of course this is an overstatement, as we have already seen. For it is not only true that Pinto emphasizes the limitations of the public credit, but, more than that, it needs only a charitable construction of his exposition in order to see that, though clumsily expressed, his meaning is that the development of credit as a substitute for metallic money increases the efficiency of a people's industry.

The most powerful motive to the contraction of public debts which is usually cited, viz., the assertion of independence and political power, may, as a matter of fact, have a result the contrary of that desired if, as so often happens, the government places its loans abroad and so becomes a tributary to a foreign country. At the same time, national debts which are owned at home are a very effective lever for political revolutions, because they give the capitalists too great an influence in all the affairs of the nation, and too great a preponderance over the landowners and professional classes, who are the real support of the existing order.<sup>1</sup>

As an offset to the wonderful results wrought by the English

<sup>1</sup>How slight a support this apprehension, so frequently expressed by financial writers of that and earlier times, derives from the facts of actual life, may be seen from the following figures. In Great Britain the number of persons who drew interest on the national debt was as follows:

£ PER YEAR	1833	1848
Under 5	85,142	96,415
5- 50	141,021	140,962
50-100	25,446	24,462
100-500	21,941	20,516
500-2000	1,799	1,550
2000 and over	183	177
Total	<u>275,532</u>	<u>284,127</u>

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national credit, Lotz not very felicitously remarks that while England had contracted a debt of 706 million pounds between 1688 and 1813, she could in case of need scarcely contract an equally large debt during the next 124 years, because the wealth of the English nation had already been trenched on too seriously by previous loans. He puts the responsibility of England's large debt on her representative form of government; the representatives of the people made use of loans in order to avoid the sacrifices which would have been required of them to meet extraordinary demands by taxation. But he forgets the great sacrifices in the way of taxes which England bore in addition to the debt during the long period of the war (sec. 482).

§ 514. To the group of German writers on finance already spoken of belongs also Karl Heinrich Rau. In the successive editions of his work on the Science of Finance he stands as the exponent of the views of that age, even down to a date very near the present.<sup>1</sup> His method of treatment, collecting and collating the views of other writers with the same industry as he does the varied facts of the fiscal and industrial field, is as far removed from the harsh radicalism of Lotz as it is from the sober lucidity of Nebenius. His work, which was in progress for a generation, during which it was pushed on to completeness with painstaking industry, places in juxtaposition doctrines and facts which mutually contradict one another. For example, he is of opinion that: "Under the circumstances of today, when governments as well as private individuals can find the necessary

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In France, in 1845, the payments of interest to private creditors on the 5 per cent. securities were:

Under 100 francs	36,833
100- 500 "	40,186
500-1000 "	13,424
1000-2000 "	9,710
2000 and over	9,009

Cf. Rau, *Finanzwissenschaft* (5<sup>th</sup> ed. 1865), sec. 480.

<sup>1</sup> *Grundsätze der Finanzwissenschaft* (5<sup>th</sup> ed. 1864-1865), secs. 464-529. (Vol. iii. of the *Lehrbuch der politischen Oekonomie*.) The first edition of the *Grundsätze der Finanzwissenschaft* appeared in 1832.



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credit with the owners of capital, it is unnecessary to accumulate a national treasure, because the state can easily get along by loans in case of need; and it is moreover unwise, because the lying idle of considerable sums of money works an injury to the industry and income of the people, as well as because the presence of such large funds will easily tempt to unnecessary expenditure." But in a note to this proposition, in the last edition of the book, he says: "Latterly it has been claimed with respect to the Prussian state that a national treasure has great value, in that it affords a speedy resource in case of a sudden emergency, and probably also because it enables the government to dispense for the time being with parliamentary consent to a loan. ... This treasure amounted in 1862 to 12 million thalers, in 1863 to 20 millions." Which of the two was in the right, the text or the note, became evident the following year. And it is probable that in case of a sixth edition the note would have found its way into the text and the text into the note.

Rau considers national debts the unavoidable means of meeting great expenditures in time of war or under other extraordinary circumstances. With the rate of taxation already at a given height it seems to him "beneficent" for the government to make use of its credit to meet such demands. But at the same time he hedges this necessity about with all manner of precautions, and in the course of so doing he brings under view all the many unfavorable circumstances connected with state debts that have ever been discovered. He cites as a commendable example the "Pragmatic Sanction on Public Debts," of November 18, 1808, issued under Charles Frederick of Baden. This provides that a public loan must not be contracted except on occasion of an actual and immediate public necessity, such as a permanent improvement of the situation of the country, or the redemption of an honest debt, or the rescue of the state, the prince or his successor from some great danger or calamity.

Quite in the spirit of the *Aufklärung* is the proposition that the history of national debts goes to show how little the nature of public credit and the best manner of employing it have been

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understood in the past; but during the present century an understanding of this matter has reached maturity, with the result, on the one hand, that the sacrifices demanded of the taxpayers have been reduced, and, on the other hand, that the rights of the public creditors have been better secured.

In point of fact, the history of public debts shows a gradual development of the finances and of the national credit, which is not by and means due to "insight" alone. It shows a mature development in several countries long before the insight of the nineteenth century came to its aid. It attained, especially on the classic soil of modern economic life and economic theory, a high degree of perfection half a century if not a whole century before the insight of the nineteenth century impressed its seal of approval. It is particularly to be noticed that the insight of Adam Smith and his school falls so fully short of the practical development of English national credit in their time.

§ 515. During the first half of the nineteenth century, German writers on finance are substantially agreed in a position of a more positive character and more nearly in accord with existing institutions than that of Smith and his school; although in recognizing the necessity of public debts they for the most part recognize them as a necessary evil. About the middle of the nineteenth century there comes a change in the attitude of German writers which at a single stroke shifts the position quite appreciably nearer to a full recognition of the nature of public debts, and makes an effort to bring the developments of the new era into harmony with certain fundamental points of theory insisted on by the old school.

The representative of this new departure is Carl Dietzel.<sup>1</sup>

First as to the fundamental points of theory.

Among the doctrines of the Smithian school (vol. i. secs. 143-146) the concept of productivity has, ever since the beginning, been the occasion of a great deal of discussion. These

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<sup>1</sup> *Das System der Staatsanleihen, im Zusammenhang der Volkswirtschaft betrachtet* (Heidelberg, 1855).

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discussions are in line with the efforts of the Physiocrats to reach a clear comprehension of the essential nature of economic life, and are influenced by the advancing development of method on the one hand and by the shifting phases of practical life on the other. On the one-hand we have the gradually unfolding doctrine concerning the nature of net product and income, which came down from the Physiocrats through the hands of Adam Smith and Ricardo, and reached a relatively definitive conclusion in the writings of Hermann. On the other hand we have the practical question as to the proper order of precedence of the industrial classes in the modern society, as judged by the standard of their relative importance to the social welfare; the interest in this question, setting out from the peculiar and frequently misapprehended views of the Physiocrats, acquired a continually wider and more philanthropic scope until it so seriously violated the boundary lines of the neighboring fields of science as to bring on a reaction, represented particularly by Theodor Bernhardi.<sup>1</sup>

For the purpose in hand, and as bearing on C. Dietzel's work here under discussion, this literary growth becomes important at the point where the doctrine of "immaterial production" and "immaterial capital" Say, Macculloch, List comes into prominence and seeks to terminate the ancient controversy by conceding the invaluable character of "productivity" to every useful activity. Possessed of the conception, quite natural to a new scientific system, that all and every human action must be measured by its measure and be ranked accordingly, the new departure magnanimously spreads its protecting mantle over the highest as well as the lowest of human activities. As Bernhardi with a noble indignation has pointed out (though going too far in restricting the idea of productivity to the production of material goods alone), the error of this view lies in its seeking to bring every human aspiration under the yoke of the economic end. We are told,<sup>2</sup> says he, about the

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<sup>1</sup> *Versuch einer Kritik der Gründe, die für grosses und kleines Grundeigenthum angeführt werden* (St. Petersburg, 1849). Cf. especially pp. 67-157.

<sup>2</sup> Pp. 141 *et seq.*

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righteous judge who defends the cause of the innocent, and about the soldier who fights for his country at the frontier, and so protects the house and home of the individual citizen; and it is taken for granted that the trade of these persons, especially of the latter, is not a little improved in reputability when it is declared to be no less useful than any other occupation; military service is a form of production; it is quite proper that other producers should pay the security-producing soldier the value of the product of his work. Bernhardt goes on to say the defense of house and home is certainly of great importance; but is property the only thing for which the fighting is done? House and home might often be preserved by simple submission - a kind of prudence which has frequently been put in practice by sensible, calculating people. On the other hand the world's history teaches that hearth and home have frequently been forfeited in war in order to preserve things which belong under quite another head, for a future which the men who take part in the struggle cannot hope to see or to enjoy, and which cannot well come within the scope of the eudemonism of the individual.

It may be set down as an accepted tenet of the political economy of today (apart from such reactionary tendencies as always occur) that the importance attached to the economic point of view and to economic standards in the aggregate of human activity, is a phenomenon of an essentially psychological and therefore historical nature; and that its scope and degree of influence on the aims of human life and activities vary. Its influence is relatively strong in our century, but assuredly not so strong as to leave no room for other and higher interests. Even at lower stages of culture this is never the sole consideration; kinship, religion, independent national life, are interests possessing a powerful influence even there; so much so that the economic interest must yield to them in part.

The state, as comprising all the highest interests of civilization, is in a special degree the stage upon which this truth comes into view and is realized in any people. But the state is not the only form in which it expresses itself. Its expression in the

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state is but a repetition of what is present in private life as well. When the bold discoverer, bent on research, ventures his life and his property, both, on a polar expedition, he undergoes an economic sacrifice which is not repaid by any pecuniary results. When the fatherland calls out its sons to defend the highest of human interests and at the same time puts into the venture those expensive material equipments which are indispensable in modern warfare, then there is done in the name of the community something analogous to what is done by the individual investigator spoken of above. After full allowance is made for the economic interests which, among others, are served by these public activities, there still remains a residuum which is not to be resolved into economic elements, but must be classed under a different head. There is a consumption of economic goods for purposes of another class, which yields no economic results.

From this it follows that a national expenditure of economic goods, whether they are obtained by loans or taxation, may yield an economic equivalent if it is undertaken for an economic end, but that where no such aim is present (as happens in the case of the greatest of all expenditures), there the production of an economic equivalent is not to be looked for, except as a possible incidental result under specially favorable circumstances (war indemnity). A theory, therefore, which insists on forcing taxes and national loans into the mould of a pecuniary equivalent will accomplish nothing further than is accomplished by that mathematical method in economic science, which is able to begin its work only after elimination of all the real character of the matter in hand. In point of fact, the question between the state and the individual concerns an exchange of economically incommensurable benefits and economically incommensurable obligations.

§ 516. The foregoing brief reflections have been introduced in order to indicate the theoretical standpoint from which Dietzel's view of public loans is to be regarded, as well as to show what influence he has had upon later writers on finance.

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According to Dietzel<sup>1</sup> the only expedient method of transferring capital from private economy to the national economy is by the use of national loans. By this method private individuals are led to put their disposable capital into the permanent capital of the community as a means of obtaining a permanent income, just as soon as it commends itself to them as a profitable investment.

The collective capital [*Nationalkapital*] is that portion of a nation's aggregate capital by means of which the collective business of the people is carried on. It consists of those permanent works and establishments, and those immaterial relations and things, whose presence is necessary in order to the emergence of the useful results which the nation has to accomplish by this method of collective production. The cause<sup>2</sup> of all perverse and derogatory opinions and sentiments with regard to public loans lies in a one-sided conception of the nature of the nation's economy, according to which the aggregate costs of production include nothing but the expenditures which are made by each private economy in detail, and which reappear more or less palpably in new products; this view overlooks the fact that the national organization is the prime requisite of all economic development, and that the ever-recurring expenditures which this national establishment requires are properly to be included in the aggregate costs of production of the nation's industry.

The view<sup>3</sup> which is expressed by most writers, that a system of public loans destroys capital, will not bear inspection. Aside from its defective apprehension of the nature of capital, this opinion is an inference from the proposition that everything which is consumed by the collective economy is consumed unproductively.

If the position were sound that national loans are an iniquitous imposition of a burden upon future generations by the present generation, then it should also hold that no one engaged in

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<sup>1</sup> *System der Staatsanleihen*, pp. 148 *et seq.*; cf. pp. 84 *et seq.*

<sup>2</sup> P. 155.

<sup>3</sup> P. 167.

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industry, who is at the same time the father of a family ought to borrow capital in order, e.g., to add to his fixed capital a much needed and probably very profitable supplement in the form, say, of a new machine.<sup>1</sup>

The line of demarkation between public loans and taxes is determined as follows.<sup>2</sup> Taxes are to serve for meeting the ordinary running expenses and cost of repairs of the national establishment; whereas all expenditures for permanent public improvements, for the extension and maintenance of the state establishment must be met by means of loans. How much is to be regarded as ordinary expenditure in the sense here understood is easily determined by finding if it recurs invariably in each successive industrial period.

These propositions, given almost word for word in Dietzel's language, sufficiently characterize his doctrine of public debts. It is seductively simple, and brings the irresistible rise of the public debt in European countries into harmony with the plausible doctrines of the old school. It falls short at two points. It rests on an unsound theoretical basis, as I have already attempted to show; and as a practical scheme, even if its theoretical soundness be conceded, it affords but a very dubious footing for any actual system of national debts:

Viewed from the historical standpoint it must be conceded that this doctrine reflects the later phases of the public debt administration more faithfully than any previous formulation of doctrine does. It does not suffer from the vicious economics of Pinto and his contemporaries; - though it is to be added that the doubtful economic doctrines of these latter writers serve to cover a much more moderate position with respect to the public debts than that of Dietzel.

§ 517. Lorenz von Stein<sup>3</sup> so far lends his countenance to

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<sup>1</sup> *System der Staatsanleihen*, pp. 182 *et seq.*

<sup>2</sup> P. 152.

<sup>3</sup> *Lehrbuch der Finanzwissenschaft. Zweiter Theil: Die Finanzverwaltung Europas. Dritte Abtheilung: Das Staatsschuldengesetz* (5<sup>th</sup> ed. 1886), p. 427. Cf. especially pp. 41 *et seq.*, 212 *et seq.*

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Dietzel's position as to reckon the third and concluding epoch in his scheme of the theory of public credit as having begun with Dietzel.<sup>1</sup>

The characteristic feature of this third epoch is that the public debts are now judged of in a much profounder way. The position now is that a "public debt is debt only in form; in point of substantial fact every loan is an independent method of taxing the future for all those government expenses which go to build up permanent government establishments for the benefit of the future by means of advances furnished by the present." To those who hold this view, therefore, Stein goes on to say, the placing of a debt has come to be not a manifestation of straitened finances, but simply an obligation of the state, which, by the payment of interest and the gradual redemption of such debts, shifts to the coming generation a part of the burdens incurred for the joint

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<sup>1</sup> The first epoch of "speculations upon the public credit" contains as yet, according to Stein (pp. 40 *et seq.*), no conception of an organic connection between the national credit and the rest of the finances, nor any conception of the difference between financial credit and the national debt. This first epoch regards every debt as the result of mismanagement and misfortune. There is at this period no demand for a systematic administration of the national credit; consolidation is still unknown, and there is no question of the method of redemption. This period begins with Adam Smith, although Smith's fundamental principles have in part survived down to the present. The second epoch begins even before the beginning of our century and its characteristic features are that, in the first place, it incorporates the entire subject of national debts into the body of the science of finance, and, in the second place, it seeks to ascertain the principles of a wise administration of the national credit as a whole. This second epoch begins with Sonnenfels, and its most characteristic exponents are Malchus and Nebenius.

This scheme of Stein's has the dubious feature not only that it constructs a second epoch which comes upon the stage before its first epoch (Adam Smith 1776, Sonnenfels 1765, but it also overlooks the fact that there is quite a respectable literature antedating Smith and Sonnenfels which gives evidence of a broader comprehension of the national credit. In England, for example, James Steuart (1767) preceded - Smith, in Germany and Austria Justi (1755) preceded Sonnenfels. The praise which Stein (p. 44) lavishes on Sonnenfels should go not to Sonnenfels but to Justi. Also, as we are aware, it is incorrect to say that from Adam Smith's time "unto this day" the English literature has been unanimous in absolutely condemning national debts." It needs only mention Sinclair. The reason given for this condemnation is that "the English national debt, have been employed almost exclusively for purposes of war"; - surely a curious explanation in view of the fact that the English finances afford the standing illustration of a great public debt during times of peace.



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benefit of the present and the future. Hereby for the first time is a basis established for the organic connection of the national credit with the national finances, and in so doing we are also shown the bond which exists between the national administration and the national credit. "Dietzel was unquestionably the pioneer in this work."

In order to a closer appreciation of this position, it may be well to give some attention to Stein's remaining propositions.<sup>1</sup> Every debt contracted by the state, says he, increases the state's "productivity,"<sup>2</sup> that is to say, every debt pays its own interest in the useful purpose which it serves. A national debt is directly productive if its expenditure results in income, and indirectly productive if its productivity consists simply in increasing the taxpaying capacity of the people. The former is calculable, the latter not. The former completes itself and may be measured within a period of one year; the latter, as e.g., in the resumption of specie payments or the establishment of penal or educational institutions, will often demand several generations for the full accomplishment of its purpose. Instead of a computation, therefore, we must in this latter case fall back on a general principle. This principle can be no other than the principle which holds for all national income and expenditure, The national administration must see that in the contraction of any national debt the expenditure of the funds shall provide for interest payment and redemption of the debt, at the same time that its application works out the moral and economic results for which the debt was incurred. If this is not done then every public debt becomes a consumption of the people's capital instead of becoming an element in the productive power of private capital.

So far Stein. He agrees in substance with Dietzel's theory of production, and what has already been said of Dietzel's view of the public credit will hold true in the main of Stein's view.

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<sup>1</sup> *Lehrbuch der Finanzwissenschaft*, pp. 230 *et seq.*

<sup>2</sup> The quotation marks are Stein's own; but they do not recur in his subsequent use of the term.

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His writings constitute the summit to which the doctrinal reflex of the development of public debts gradually attained during the course of two centuries. The economic science of the past rendered valuable service in this presentation of facts and views relating to public credit; it may in a similar way be the privilege of the science of today, by seeing these reflections of past events I from its own modern standpoint, to reach such an understanding of the matter as shall do justice to the present and the past alike.<sup>2</sup>

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<sup>1</sup> For criticisms of Stein see Adolph Wagner, *Ordnung des österreichischen Staatshaushalts* (Vienna, 1863), pp. 17 *et seq.*, and "Staatsschulden," in Bluntschli's *Deutsches Staatswörterbuch* (1867).

<sup>2</sup> Cf. secs. 157-169 above (book i. chap. vi., "Order and Sequence in the Public Economy").

## CHAPTER II.

### THE PUBLIC CREDIT OF THE PRESENT TIME.

LITERATURE. Friedrich Nebenius, *Ueber die Natur und die Ursachen des öffentlichen Kredits, Staatsanleihen, die Tilgung der öffentlichen Schulden, den Handel mit Staatspapieren und die Wechselwirkung zwischen den Kreditoperationen der Staaten und dem ökonomischen und politischen Zustande der Länder* (2. Auflage. Erster, allgemeiner Theil, 1829). Lorenz von Stein, *Lehrbuch der Finanzwissenschaft; Zweiter Theil: Die Finanzverwaltung Europas; Dritte Abtheilung: Das Staatsschuldenwesen* (5. Auflage, 1886). Adolph Wagner, *Ordnung des Österreichischen Staatshaushalts* (1863). The Same, "Staatsschulden," Bluntschli and Brater's *Deutsches Staatswörterbuch* (1867). The Same, "Die Ordnung der Finanzwirtschaft und der öffentliche Kredit," Schönberg's *Handbuch der politischen Oekonomie*, vol. iii. (2<sup>d</sup> ed. 1885). Paul Leroy-Beaulieu, *Traité de la science des finances* (1877), vol. ii. G. Ricca-Salerno, *Teoria generale dei prestiti pubblici* (Milan, 1879). Henry C. Adams, *Public Debts* (New York, 1887). F. von Reitzenstein, "Das kommunale Finanzwesen," Schönberg's *Handbuch der politischen Oekonomie* (2<sup>d</sup> ed. 1885), vol. iii, pp. 649-657.

For statistics on the present state of national and municipal debts, cf. *Finanzarchiv*, 1884-1889. Richard von Kaufmann, "Finanzstatistisches zu den Schulden der europäischen Grossmächte," Conrad's *Jahrbücher für Nationalökonomie und Statistik*, 1887 ( N. F. vol. xv.). The Same, "Die öffentlichen Ausgaben der grösseren europäischen Länder nach ihrer Zweckbestimmung," *ibid.*, 1889 ( N. F. vol. xviii.)

SPECIALLY ON PAPER MONEY. T. Tooke and W. Newmarch, *History of Prices* (German Translation by C. W. Ashen 1859). Adolph Wagner, "Papiergeld," *Deutsches Staatswörterbuch* (1862). The Same, "Zur Geschichte der österreichischen Bankozettelperiode," *Zeitschrift für die gesammte Staatswissenschaft*, 1861, 1863. The Same, *Die russische Papierwährung, eine volkswirtschaftliche und finanzpolitische Studie nebst Vorschlägen zur Herstellung der Valuta* (Riga, 1868). J. A. R. Helferich, "Die österreichische Valuta seit dem Jahre 1848," *Zeitschrift für die ges. Staatsw.*, 1855, 1856. Carlo Ferraris, *Moneta e corso forzoso* (Milan, 1879).

#### I. THE PRESENT STATE OF THE PUBLIC CREDIT.

§ 518. What the far-seeing philosopher Berkeley said, a century and half ago, in speaking of England, that the discovery

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of public credit was the discovery of a new gold mine, and what James Steuart, and more particularly Sinclair, had to say of its efficiency as an instrument of political power, all this has been realized in actual fact during the course of a hundred years after their time. The debts of the nations of Europe, the magnitude of which at the close of the wars with which the nineteenth century began, filled the most sensible of our financial writers with astonishment and dismay, have gone on increasing during a further couple of generations in a degree to correspond with the progress in industrial productivity accomplished during the century.

It is true that the wealthiest and most deeply involved of all the nations - Great Britain - was able not only to come to a halt in its career of national debts, but even to cancel a considerable portion of its old debts. But at the same time it is to be noted that the other states which have attained a similar abundance of credit and capital, have, as fast as the circumstances have permitted, also found occasion for the contraction of large national debts; so that we have today the following situation.

While, according to computations given above (sec. 493), the interest payable on debts in 1820 by the various states of Europe amounted to 1,125 million marks, later computations show that by 1865-66 this sum had nearly doubled, and by 1885-86 had increased nearly fourfold.<sup>1</sup> From the principal of the debt (1885-86, 108,431 million francs) is to be deducted so

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<sup>1</sup> The Société de Statistique computes that the payments for interest and redemption in 1865-66 amounted to 2438 million francs; for 1885-86 Paul Boiteau computes it at 4864 million francs (Conrad's *Jahrbücher*, 1887, p. 145). According to an official Italian document (*Finanzarchiv*, 1885, pp. 847 *et seq.*) the interest-charge on the public debt of the seven states (the individual states of the German Empire being included under Germany, France, England, Italy, Austria-Hungary, Spain, Russia and Germany, in 1882, amounted to 3957 million francs; that is to say, three times as much as the computed expenditure of all European states in 1820. Henry C. Adams (*Public Debts*, 1887) finds that the civilized countries of today, with a population of 1170 millions and an area of 37.4 million square miles, have an aggregate burden of debt amounting to 27,000 million dollars. This does not include municipal or communal debts. Converted into francs this would be 143,000 millions, as contrasted with an aggregate of 108,431 million francs for European public debts alone according to the French calculation cited above.

much as is covered by productive investments, as, e.g., the Prussian railway loans. But as against this there is to be added the municipal and communal debts, of which but a very modest portion are so invested as to cover their own interest-charge. In Prussia alone the urban and rural communes together paid, in 1883-84, 34.50 million marks in interest and in discharge of the principal of their debts; in the kingdom of Italy the communes and provinces in 1880 paid 41.50 million francs as interest on their debt (on a principal of 745.40 million francs).<sup>1</sup>

The national debt of England, the interest-charge on which amounted to 32.50 million pounds in 1820, has been gradually redeemed, so that the interest-charge in 1852 amounted to only 28 millions, and in 1885-86 only 22 millions.<sup>2</sup> Instead of amounting to three-fifths of the national expenditures, as in 1820, the interest-charge now amounted to only one-third or one-fourth of the total.

But in most other countries (with the exception of the German states, especially Prussia) the public debt has increased with great rapidity.

Austria-Hungary in 1820 paid only 31 million marks in interest, as compared with 395 millions in 1882; Russia 23 millions in 1820, and 640 millions in 1882; France 148 millions in 1820, and 790 millions in 1882. Italy paid 410 million marks in interest on its public debt in 1882, while in 1820 all the Italian states, together with Spain, Portugal, Sweden, Denmark and the minor German states paid only 225 million marks interest. It is especially in the case of states like Austria-Hungary and Russia, which had exhausted all their resources, including their credit, at the close of the great war, that the contrast between the relatively slight amount paid after the Napoleonic wars and the large interest-charge of today brings out the great advance that has taken place in the growth of the public credit and of the financial strength of the states. Even in the case

<sup>1</sup> *Finanzarchiv*, 1884, pp. 760, 244-253.

<sup>2</sup> *Statistical Abstract for the United Kingdom*. 1868. 1888.

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of France, which, it is true, was treated with leniency at the re-establishment of peace in Europe, but was still subjected to burdens that were very great for that time, - even in France the increase of the interest-charge by more than sevenfold is evidence of a great development of industrial productivity and wealth during the nineteenth century.

§ 519. Let us take up, somewhat in detail, the development of the public credit in Prussia and Germany. In so doing we shall (here as in the discussion of the tax system) avoid comparison of multifarious facts and figures taken from various systems of legislation and various nations, and will be able to confine our attention to definite facts regarding the community immediately under consideration. We shall in this way get a conception much truer to life than is attainable by the old-fashioned method of discussion.<sup>1</sup>

A survey of the Prussian public debts, and their development since the middle of this century, is calculated to impress us with the worthlessness of the customary arithmetical comparison of our state with other of the larger states. What everyone understands in speaking of the debts of any private person, viz., that the degree of indebtedness depends on the purpose for which the debts have been contracted and the assets to be set off against them, - this important fact is left out of consideration in speaking of public debts. This is to some extent due to the influence of unsound theory. During the years 1848-1866 the Prussian national debt increased from 158.50 million thalers to 290 millions, that is to say, by 131.50 million thalers. The amount invested in the state railways built or bought during this period (inclusive of the stock held by the state in private roads amounted to 124.33 million thalers. This leaves a remainder of only 7 million<sup>2</sup>

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<sup>1</sup> Even Nebenius (*Der öffentliche Kredit*, 2<sup>d</sup> ed. vol. i. pp. 289 *et seq.*) made some acute and noteworthy remarks on the subject of the prevalent method of comparing figures taken from different countries. His remarks have seldom received due consideration.

<sup>2</sup> E. Richter, *Das preussische Staatsschuldenwesen*, pp. 63 *et seq.*

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thalers not covered by the value of the railways. The national treasure at the end of 1865, moreover, amounted to 20 million thalers (1848, 19.40 millions).

The interest-charge on the national debt in 1865 was 11 million thalers, whereas the railroads turned in funds to meet this charge amounting to 9.6 million thalers.

The latest changes in the national railway policy have appreciably altered this condition of things for the better. The national debt has greatly increased in aggregate amount, and, through productive investment, it has not only afforded the funds necessary for interest and redemption, but has even yielded a progressively increasing surplus above these requirements.

The debt has increased as follows:

Year	Population (millions)	Principal of Debt (million marks)	Interest and Redemp- tion Charge (million marks)
1867	24.	1135	42.78
1881-82	27.30	1995	98.49
1886-87	28.30	4073	181.88
1889-90	[28.30]	4457	196.60 <sup>1</sup>

But the net receipts of the state railway business have developed at such a rate that from 1878-79 they nearly equaled the interest-charge on the entire national debt, and since 1879-80 they have even exceeded the interest-charge.<sup>2</sup> The figures are as follows:

Year	Interest-Charge (million marks)	Net Receipts (million marks)
1881-82	72.40	95.10
1883-84	107.60	141.90
1886-87	161.10	201.70
1887-88	170.90	209.90
1889-90	165.60	278.60

According to this showing the public debt of Prussia during the last forty years has been in a radically different situation from what we find in Austria, France, Russia, Italy and even the United States, and differs likewise from the debts contracted by

<sup>1</sup> Cf. *Anlagen zum Staatshaushaltsetat* for 1889-90, vol. ii. No. 1, *Beilage B. Staatsschuldenverwaltung.*

<sup>2</sup> *Finanzarchiv*, 1887, pp. 294 *et seq.* and *Anlagen zum Staatshaushaltsetat*, for 1889-90, vol. i.

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Great Britain in the eighteenth century and such remnants of the great national debt as have survived down to the present part from slight and, relatively to the great average of the the Prussian debt, quite insignificant exceptions, this debt does not answer to the description of the data which the history and the theory of the public debt has had to struggle with for the past century-and-a-half; it is not the same either in its good or in its bad features. In place of a nebulous conception of an immaterial productivity due to the national loans, we have here an imposing example of a true productive credit, which while it far exceeds the conceptions of a past age (Nebenius), is but the prelude to a further development of the national and communal economy in the same direction in the future.

It is-of course to be remembered that this clear and unhampered development of the Prussian national debt system in the direction indicated has been greatly favored by a general situation favorable to the national life as a whole. The events of the years 1864-1866 and 1870-71, so fortunate in every respect, were of course also fortunate in their financial bearing. The wars, being brought to a victorious conclusion, have paid their own expenses and have consequently not left the usual traces in the way of a national debt. If, nevertheless, there has been a vigorous beginning made (not in Prussia, but in the Empire) towards a debt for military equipment, that is to be taken simply as testifying to a growth of the military requirements and a resort to the customary financial expedients.

§ 520. The state of the public debts in the minor German states is much the same as in Prussia. In Wurtemberg the history of the national debt is the history of the railways.<sup>1</sup> The "general" debt amounted in 1845 to 36 million marks, in 1885 to 47.50 millions. Almost the entire increase of these forty years falls under the head of railway debt, amounting to 381.50 million marks. As we are aware, the relation between the surplus earnings of the railways and the interest-charge on the railway debt

<sup>1</sup>Riecke, *Finanzarchiv*, 1885, pp. 823 and 815 *et seq.*



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is different in Wurtemberg from what it is in Prussia; the interest-charge on the railway debt amounted in 1883-84 to 15.39 million marks, while the surplus earnings of the railways were only 13.64 million marks, so as to leave 1.75 millions to be met by other revenues (according to the estimates for 1884-85 and 1885-86 the uncovered interest-charge was 2.32 millions and 2.40 millions respectively). But in spite of this difference in detail, in which respect an improvement may take place in the course of years, there is after all a great difference between a debt which draws on the national finances for only one-eighth or one-tenth of its interest-charge, and one which calls for the payment of the whole of the interest.

In Baden the situation is much the same as in Wurtemberg. The debt contracted for railways and for the Bodensee shipping amounts (1888) to 334.20 million marks, while the remaining interest-bearing debt is 17.30 millions.<sup>1</sup>

In the Kingdom of Saxony the national debt on January 1, 1888, was 659 million marks, by far the greater portion being railway debt. The interest-charge amounted to 22.30 millions, while the net earnings of the state railway business amounted to 28 millions. Finally, as to the Kingdom of Bavaria. In 1870 its aggregate national debt was 850 million marks. Of this the railway debt made up to 379 millions, and the debt contracted for the enfranchisement of landed property [*Grundentlastungsschuld*] to 163 millions. On April 1, 1884, the entire debt was 1347 millions, of which 947 millions was railway debt and 163 millions enfranchisement debt. The remaining debt was, during the years 1870-1884, reduced from 308 millions to 237 millions.

§ 521. The predominantly military character of the imperial finances is shown also by the character of the imperial debt.

It has already been noticed in another connection that the progressively increasing provision made for the defense of the Empire has resulted in constantly recurring financial sacrifices

<sup>1</sup> *Gothaischer Hofkalender*, 1889.

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(which will undoubtedly continue to increase) that can properly be called "extraordinary" expenditures only in a very circumscribed sense of the word. It is further to be noticed that this designation of "extraordinary" must be made to serve as an excuse for loans which would be replaced, wholly or in part, by taxes, in case the Empire possessed a more adequately developed tax system.

At the end of 1871 the debt of the German Empire, inclusive of the debts of the North German Confederation, amounted to 766.50 million marks (of which 692 millions were interest-bearing). The war indemnity paid by France enabled the Empire to discharge this debt, so that by the end of 1873 there was only some two millions left. Since 1877 loans have been repeatedly issued, for the most part in small amounts; latterly, to meet the increased requirements of army and navy, the amounts of the loans have somewhat increased.

On January 1, 1886, the Empire had a debt of 427 millions. In the imperial estimates for 1889-90<sup>1</sup> the figures for the aggregate debt are given as follows:

Imperial Debt		Interest-Charge	
4 per cent.,	450 millions		18. millions
3 ½ per cent.,	565 "	(Jan. 1, 1890)	18.48 "
Total -	1015 millions		36.48 millions

Until a few years ago - in a manner similar to what happens in the individual states of the Empire - the earnings of the imperial railways afforded an offset to this interest-charge, but these receipts have been considerably exceeded by the interest-charge since the larger loans of the last few years.

The net earnings of the railways for 1889-90 are estimated at 19.20 million marks.<sup>2</sup> The consequent remaining interest-charge to be covered by taxes (17 millions) is a small sum compared with the analogous

<sup>1</sup> *Anlage X., Denkschrift, betreffend den Geldbedarf für die Verzinsung der Reichsschuld.*

<sup>2</sup> Receipts 49.10 millions, expenditures 29.90. *Anlage XVIII. Etat für die Verwaltung der Eisenbahnen auf das Etatsjahr 1889-90.*

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demands on the finances of the greater neighboring states; - France 1291 million francs (principal of the debt 31,718 millions) according to the budget of 1888,<sup>1</sup> Russia 281 million rubles according to the published balance for 1887, and 288 million rubles according to the budget for 1888 (with a deduction of 53 millions for railway earnings).<sup>2</sup>

§ 522. Municipal (communal) credit [*Gemeindekredit*], as is evident from some facts already cited, has of late made considerable growth, both in Germany and in other states. There are several points in this connection that call for special discussion, as, for example, the purposes for which municipal debts are incurred, and the relation of dependence in which the municipalities stand to the state.

As concerns the purposes for which loans are issued, by municipal bodies of high and low degree, they are (because of the similarity of the functions devolving on the state and on the municipality) partly productive, partly unproductive, just as in the case of the state, water-works, gas-works, slaughter-houses, markets; street railways are ordinarily in position (if the town is large enough) to pay interest on their cost out of their net earnings.<sup>3</sup> Hospitals, poor houses and schoolhouses belonging

<sup>1</sup> *Gothaischer Hofkalender*, 1889, pp. 667, 935.

<sup>2</sup> The principal of the debt of the Russian Empire on Jan. 1, 1888, was:

Rubles (specie)	391.50	millions
Rubles (paper)	3105.	"
Dutch Gulden	66.	"
Pounds Sterling	122.30	"
Francs	552.	"

<sup>3</sup> The debt of the city of Berlin is chiefly of a productive character. The aggregate amount in 1883 was 136.36 million marks, against which is to be set off the following investments:

Gas-works	20.61	million marks
Water-works	38.21	" "
Canals	52.87	" "
Slaughter-houses	11.18	" "
Markets	1.92	" "
Total	124.79	million marks

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to the communes, and highways and insane asylums belonging to larger civil divisions, can produce no such net earnings if they are gratuitous and are open to the lower or indigent classes of the population. Various improvements and embellishments of modern towns (the opening of new streets, paving, lighting, etc.) can in the nature of things not repay their cost out of their own earnings.

We therefore find side by side, here as in the case of the national debts, loans for productive and unproductive purposes. The position of the commune and of all communal and municipal bodies relatively to the state involves on the one hand a supervision of the municipal contraction of debts by the state (if the latter has attained the maturity requisite for this function, and on the other hand the state may be of assistance to the municipal body in obtaining the loans desired.

In the orderly and well-governed states of today there is ordinarily nothing of that adventurous element to be found in the use of the municipal credit which is so frequently seen in any experimental democracy (where, among other things, demagogical railway politics have sometimes led to municipal insolvency). Still it is always possible that the responsibility of the national administration for the acts of minor civil bodies may, in case of a catastrophe of any kind, leave the national government morally answerable for the obligations of an insolvent commune. Hence the unquestionable right of the state to exercise a supervision and control of municipal indebtedness. Supervision is exercised in this case as in that of taxation generally, but for more urgent reasons. We accordingly find that in Prussia and the other German states, in Austria, France, Great Britain, Belgium and other countries, no municipal loans are permitted without the approval of officials having the matter of Charge. The relation of the municipalities to the state also involves state also to the municipalities in obtaining loans. Large and

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*Statistisches Jahrbuch der Stadt Berlin*, 1884, p. 319. The net earnings of the gas-works in 1882-83 amounted to 5.46 million marks, the net earnings of the water-works to 1.46 million marks.

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favorably situated municipalities need no such assistance;<sup>1</sup> but the majority of the small municipalities need it all the more. In the German Empire this purpose is served, as a subsidiary purpose, by the Reichsinvalidenfonds;<sup>2</sup> in Belgium a special institution (the Crédit Communal) has been erected (1860) for this particular purpose.

In Great Britain there prevails, in this respect, a strongly centralized management.<sup>3</sup>

Municipal authorities have three ways of obtaining funds. They may apply to Parliament for permission to issue a loan for a particular object (special local act); for certain public purposes they may apply to the Exchequer through the Board of Public Works Loan Commissioners; or finally they may go into the market for loans for similar objects under the general act governing municipal loans (1875). The last-named method has been used to but a slight extent; whereas loans to a

<sup>1</sup> The loan lately (1889) effected by the city of New York may be cited as the highest achievement hitherto attained by municipal credit. This loan bears interest at 2 ½ per cent. and was issued at 1 ¼ per cent. above par. Shortly before that time the neighboring city of Brooklyn placed a 3 per cent. loan at 8 ½ per cent. above par. These favorable terms are in some slight degree due to a lately enacted law of the state of New York, which permits insurance companies to deposit these municipal bonds as legally satisfactory security. But the main reason is after all to be sought in the high degree of credit enjoyed by these two municipalities, together with the presence of a plentiful supply of capital. Cf. *The Economist*, June 22, 1889.

This high municipal credit - which contrasts so strikingly with the abuses that prevail in America - is in its turn largely due to a law of the State of New York which limits municipal debts to one-tenth of the value of the real property as assessed for the property tax. Even as early as 1887 the city of New York paid no more than 3 per cent. in interest on its loans.- *Message of Abram S. Hewitt, Mayor, to the Board of Aldermen, January 10, 1888* (New York, 1888), p. 9.

The city of Berlin has lately (July, 1889) effected a conversion of its 4 per cent. loan (of 123 million marks) to 3 ½ per cent. Its 3 ½ per cent. bonds were quoted on July 26, 1889, at 102.80. The city of Zurich has issued a 3 ½ per cent. loan which has been quoted at 99.10 per cent. on the Berlin exchange from the date of issue.

The city of Hildesheim placed (July, 1889) a loan of 1.50 million marks, bearing interest at 3 ½ per cent., with a syndicate of bankers on a basis of 101.25.

<sup>2</sup> On March 31, 1884, the amount of the loans to communes was 202.30 million marks, bearing interest at 4 - 4 ½ per cent.

<sup>3</sup> Phillips, *Local Taxation in England and Wales (Local Government and Taxation in the United Kingdom*, edited by J. W. Probyn, 1882) p. 479.

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considerable amount have been obtained from the Exchequer (the rates of interest since 1879 are as follows: 3 ½ per cent. payable in 20 years; 3 ¾ per cent. payable between 20 and 30 years after the date of issue; 4 per cent. for loans payable between 30 and 40 years after the date of issue; 4 ½ per cent. for loans of a longer term than 40 years).

The aggregate amount of the municipal debts has greatly increased of late years. In 1872-73 its amount in England and Wales was only 80 million pounds, and in 1879-80, 137 million pounds. Of the latter amount only 30 millions were funded on special items of revenue (tolls, dues, rents); the whole of the remaining 107 millions rested on taxes. The control exerted by Parliament or by the Board of Public Works Loan Commissioners seems to be very lax and to unduly facilitate the contraction of debt, especially it has little effect to enforce seasonable discharge of the debt.

## II. THE VARIOUS KINDS OF PUBLIC DEBTS.

§ 523. The facts relating to public debts which we have reviewed have so far been distinguished into classes only according to two principles of classification. (1) According as the loan is made for productive or for unproductive purposes, and (2) with respect to the kind of public body which issues the loan.

We shall now have to make a further distinction.

If we examine the debts of the German Empire we shall find that they were, March 31, 1887,<sup>1</sup> made up of the following classes:

Interest-bearing bonds	504.2	million	marks
Non-interest-bearing Treasury Bills	54.15	"	"
Imperial Treasury Notes	133.87	"	"

We have here three typical forms of public loans differing in respect of the term for which they are to run, and this difference in duration is in its turn determined by the differing causes and purposes of the loan.

<sup>1</sup> *Statistisches Jahrbuch für das deutsche Reich*, 1888, p. 198.

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Just as we distinguish between long and short credit in private business, and just as the credit employed assumes various forms to correspond to the object for which it is employed, so also in the case of the public credit. We make a distinction between mortgage-loans advanced to a land-owner for a long term of years, answering to the permanency of his tenure of the land, and loans made on bills of exchange or on personal security, the short term of which corresponds to the rapidity of circulation with which goods pass through the various stages of the productive process. Similarly occasions arise in the public economy which demand the use of a longer term of credit, at the same time that there are also objects for which a short credit is sufficient.

§ 524. It has appeared from the historical survey that the great body of public debts, whether contracted for productive or unproductive purposes, is always of some considerable duration, and the mature development of the public credit even enforces the conviction that an unlimited duration is the essential characteristic of the public credit. The essential nature of the great body of requirements which occasion the use of the public credit is on this point at one with the essential nature of the state. The fiscal demands which the national economy makes through the loan market are in this respect of the same nature as the ethical-political demand which we know it is competent for the state to assert. And this demand is no longer reluctantly complied with; the experience of the various states, for a long time past, goes to prove that the money market is always ready to meet such demands, if only the state and the nation's industry have reached the requisite degree of maturity.

Some of these experiences have been outright triumphs for the public credit, in which confidence in the permanency of the state and in its financial soundness has mastered all doubts arising from the changing fortunes of a growing state and the changes and succession of constitutions and of dynasties. The

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stability of the national unity has proved itself so indubitable that all the alterations have seemed trifling in comparison.

The fiscal need of obtaining loans of a long term must always come prominently into view when large sums have to be raised for carrying on a great war, or even when more moderate sums are wanted for establishing great productive institutions.

The name "funded debt" which has usually been applied to this best known class of public debts is itself an evidence of the growth of the public credit at this point. The term came into general use in England during the eighteenth century, and was there used to designate the practice of setting apart certain specified public revenues for the payment of a debt and its interest-charge. This was a further development of the earlier practice of pledging certain crown estates and crown revenues, only that the setting apart of certain revenues by a legislative act now took the place of an earlier quasi-private hypothecation of property by an act of the crown. By a further step in the development, this close relation between a particular expenditure and a particular source of revenue fell into disuse, and the annual payment for interest and redemption of the debt took its place among the other national expenditures; and this led to the "funding" of all the state's expenditures, so that all expenditures without distinction have come to depend on the aggregate of the national revenue.

The original meaning of this old term has therefore been lost, so far as regards any modern state with a mature system of national credit. The term funded debt has come to signify only so much of the original content of the term as has survived in practice, viz., a debt intended to run for a long time.

§ 525. To distinguish it from the funded debt the rest of the public debt is designated as a "floating" debt. This latter is ordinarily of slight consequence as compared with the funded



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debt, especially in countries with a large funded debt;<sup>1</sup> it is made up of so great a diversity of items, and is incurred for such a variety of purposes, as to require some detailed consideration.

This subject has already been touched upon in the general exposition dealing with the relation between taxes and national debts in meeting the public expenditures (sec. 168). It will now have to be taken up somewhat more in detail.

A national economy with an undeveloped credit system is like an ill-ordered private economy; it will incur debts of whose necessary term of duration it has no adequate conception, at the same time that it does not possess the means for their speedy discharge. It may even be that the debts arise out of a simple disproportion between expenditures and income, such as cannot be remedied either by an increase of revenue or by any available recourse to credit. This may fairly be designated a "shiftless" credit system.

Under this system, in the public as in private finances, arrears will drag on from year to year, increasing as time goes on through the persistence of the causes out of which they originated, and in the absence of an increase of ordinary revenues they can be liquidated only by facing the facts squarely and recognizing that this multitude of small over-due liabilities amounts to the same thing as a considerable body of debt, for the discharge of which, and for the payment of interest on which adequate provision must be made.

This is the oldest and therefore, under conditions of an inadequately organized public economy, the most prevalent form in which the floating debt occurs.

But even the shrewd manager, whether in public or in private

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<sup>1</sup> The national debt of Great Britain on March 31, 1888, consisted of the following items (Statistical Abstract for the United Kingdom, 1888, p. 29):

(1) Funded Debt	£ 609,740,743
(2) Terminable Annuities	78,149,230
(3) Unfunded Debt	17,385,100
(4) Savings Funds Deficiencies	1,346,176
(5) Exchequer Balances at the banks of England and Ireland	7,647,072
(6) Sundry Debts (local loans, Suez Canal Shares, etc.)	5,522,917

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life, must come to recognize that debts of this character will occur even where there is no such shiftlessness in the keeping of accounts.

Even the best administrator cannot avoid the carrying over from one fiscal period into the next unliquidated claims for supplies and services rendered in the course of the former period.

There may moreover occur unforeseen shortages in the estimated revenues, or unforeseen items of expenditure which will not admit of delay.

Moreover, the regular revenues and the regular expenditures do not always coincide in point of time. Considerable sums may be required for the payment of officials, troops, etc., whose equivalent in the shape of revenues from taxes, domains, rents and the like, will regularly be received after an interval of some months or quarters.

But it is especially the administrative activities of the government that give rise to floating debts due to other than financial reasons.

We will now take a closer look at the chief kinds of these administrative expenditures.

§ 526. The chief source of a floating debt of this kind is the issue of government paper money. All financial abuses apart, this paper money in any country with a silver currency serves the purpose of a more easily portable substitute for silver for the payment of amounts the transportation of which in silver would be burdensome, at the same time that the bank notes in circulation are, and properly should be, of too large denominations to serve for this particular purpose. A typical illustration of the need of such a paper currency is afforded by the practice of the German states; previous to the imperial law of April 30, 1874, they kept notes in circulation of one, five, and ten thalers (gulden), - amounting to 184,298,500 marks at the time the law went into effect; and the Empire inherited from them the institution of the imperial treasury notes of a normal amount of 120 million marks. In addition to this, as a measure of transition,

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the right to issue 54.74 millions was conceded to the individual states, to be redeemed between 1876 and 1890, so that at the end of March, 1887, there were still 133.86 millions in circulation, of different denominations as follows:<sup>1</sup>

2,041,823	imperial	treasury	notes	of	5	marks
1,000,038	"	"	"	"	20	"
2,073,172	"	"	"	"	50	"

A second provocation to the contraction of a floating debt, also incidental to the administrative duties of the government, is afforded by national (imperial) savings banks where such exist. This is especially apt to be the case under the modern practice of combining savings banks with the post-office, which involves the contraction of a large debt payable on demand. In Great Britain and Ireland the amount owed by the state on March 31, 1887, was 53.97 million pounds sterling.<sup>2</sup>

§ 527. Whether the causes of the floating debt are of one kind or another, whether the occasion out of which the debt arises may be said to be an active cause or an occasion simply, in any case the management of the debt by the fiscal administration will necessarily differ, according as the debt results directly and immediately from the occasioning cause or originates as an indirect consequence.

If supplies furnished to the state are not duly paid for, or if the postal savings banks bring large deposits to the state, this fact itself immediately gives rise to a floating debt. On the other hand, if the equilibrium aimed at in the financial estimates is disturbed by unforeseen shortages in the revenue or by unforeseen expenditures, so as to leave a shortage in the funds available for meeting immediate expenditures, then it becomes necessary to incur a floating debt. Halfway between these two classes lies the issue of national treasury notes. A sufficient ground for such an issue is to be found in circumstances affecting the

<sup>1</sup> *Statistisches Jahrbuch für das deutsche Reich*, 1888, p. 123.

<sup>2</sup> *Statistical Abstract*, 1888, p. 180. In the statement of the national debt (see note to preceding section) this item does not appear.

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currency, as we have already seen. But neither as an historical fact nor in point of practical expediency is this the sole or most important ground of such issue. The outstanding imperial treasury notes which are at present to be found in circulation in the Empire, under the law of April 30, 1874, represent a legacy from the monetary habits and abuses of the states of Germany; the institution owes its origin to the eagerness of (at least some of) these governments to exploit to the utmost the advantages of a non-interest-bearing debt. As a result Prussia found herself compelled as early as 1856 to reduce her paper-money issue by one-half,<sup>1</sup> and the imperial government was again compelled to reduce the amount from the 184.30 million marks outstanding at the beginning of 1874 to 120 million marks (at the same time introducing the gold standard.

Treasury notes (paper money in the widest sense are therefore one of the usual means by which a temporary deficit in the available funds is supplied. Under what circumstances, within what limits, and with what special danger will appear later on. Besides paper money there are (especially in countries which do not make use of this expedient, as, e.g., Great Britain and France) other forms of floating debt which serve the same purpose. As we have seen, Prussia, especially in seasons of financial or political straits, fell back on the Society of Marine Commerce, which helped out the abnormalities of the public credit by means of a permanent floating debt. In Great Britain there have existed ever since its foundation certain financial relations between the exchequer and the Bank of England; also the privileged trading companies (the East India and the West India Companies) stood in a somewhat similar relation to the English public credit. The mixture of diverse forms of credit which resulted from these financial relations, and the conversion of cash deposits in the hands of these financial institutions into a permanent national debt, marks an immature, and therefore unsound stage of development of the public credit after these aberrations of the early days are past, banks of this kind come

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<sup>1</sup> Law of May 7, 1856, reducing the issue from 30.7 million thalers to 15.7 millions.

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to assume their legitimate function in a developed system of public credit, viz., the maintaining of a running account for the purposes of the floating debt. The indebtedness of the English government on this account to the Banks of England and Ireland amounted, on March 31, 1887, to £7,647,072.<sup>1</sup>

An important form of floating debt which is likewise native to England and has lately been introduced into Continental countries is Exchequer Bills [*Schatzscheine*]. These differ from treasury notes [*Kassenscheine*] much as commercial bills differ from bank notes. While treasury notes and bank notes are issued as a substitute for coin and are therefore intended to serve the everyday purposes of circulation, basing their acceptance in the circulation on their redeemability in coin on demand, commercial bills and exchequer bills on the other hand are adapted for temporary investment of money, as contrasted with the relatively permanent investment in funded securities, mortgage loans and the like. As investments the exchequer bills, just like commercial bills, pay interest, and this interest being of the nature of interest on short loans (discount) has the characteristics of a discount, which differs somewhat from the interest paid on loans of a long term.

§ 528. We come now to a consideration of the various kinds of public debts in detail. The line of demarkation between the funded and the floating debt is determined by the form in which the debt is owed. The tendency in every ill-ordered financial system is to increase the amount of the floating debt and so lessen that of the funded debt. This is done partly to conceal the actual amount of the latter, partly in order to enjoy the fiscal advantages there are in a floating debt (no interest, or a low rate of interest); but this advantage finds its offset in the loss which it involves of all the advantages of a funded debt.

These advantages are the long term of credit and the less

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<sup>1</sup> During the fifteen years 1873-87 it was on an average six million pounds at the close of the fiscal year. - *Statistical Abstract*, 1888, p. 29.

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importunate requirement of discharging the debt; whereas the floating debt, maturing from day to day or from month to month, may, if it grows very large, exert a great pressure on the finances, such as the funding of the national debt is devised to obviate. In case of an orderly and well-developed national credit, such an excessive accumulation of floating debt may exist in good times without evil consequences; but if confidence in the state is shaken, as in case of a threatened war, when alarm may easily take possession of the public, such a mistaken policy may plunge the country into embarrassments at the precise moment when it is least able to cope with them. If in such an emergency the state is unable to meet its obligations, this failure will in its turn react on the public confidence and so increase the general alarm.

There is therefore great danger in an excessive issue of substitutes for money (treasury notes and the like) whose acceptance and value rest on their being redeemable in coin on demand. If this convertibility fails at the decisive moment the result will be precisely the contrary of what was aimed at in the issue of the paper money. The paper money which is issued in the expectation that it will float on the strength of an unshaken confidence in its ready convertibility into coin, is now importunately presented to the treasury for redemption at a time when redemption is impossible. There is in such a case a great temptation for the state to help out its credit by the use of compulsion. While the acceptance of the paper as a means of payment had previously rested almost exclusively on public confidence, it comes now, when public confidence has failed, to rest on the legal-tender quality of the paper, at the same time that this legal-tender quality is unable to save it from depreciation.

Something similar has happened in cases where the state has not itself issued paper money but has incurred a floating debt in the form of short bills due to privileged banks of issue, and where, instead of being able to discharge this debt in a time of financial stringency, it has been obliged to incur additional debts. In consequence of such a situation the banks have been unable

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to meet their own obligations, with the result that a continually increasing pressure has been brought to bear upon the state to use its authority to suspend specie payments. It is, however, quite impossible to draw a hard and fast line between the floating and the funded debt.

There were in the German Empire, on March 31, 1887, 133.87 million marks of imperial treasury notes, 54.15 million marks of exchequer bills [*Schatzanweisungen*], which being non-interest-bearing, just like commercial bills, were discounted at their issue (at an average of 3 per cent). The amount of these exchequer bills outstanding at the close of each fiscal year between 1877 and 1887 varied between 10 and 70 million marks. In earlier years (1868-1875) the form employed was usually that of interest-bearing exchequer bills, which, it is to be remarked, were not exempt from the fluctuations of discount by virtue of their bearing interest. Exchequer bills were especially used to a very great extent in connection with the monetary reform of the German Empire.

Since 1868, the date when exchequer bills were first employed both in Prussia and in the North German Confederation, the amount of exchequer bills which may be issued during the year, as well as the interest-charge on them, is determined by the budget from year to year. The imperial budget for 1889-90<sup>1</sup> provides for an issue of 78.50 millions, and allows a sum of 350,000 marks for interest. The Prussian estimates<sup>2</sup> contain the provision that "for the payment of interest on the exchequer bills issued for the temporary reinforcement of the funds at the disposal of the general treasury during 1889-90 there are appropriated 600,000 marks."<sup>3</sup>

§ 529. Funded debts are of various kinds, differing and varying according to the progressive development of the chief

<sup>1</sup> *Anlage X., Etat der Reichsschuld auf das Etatsjahr 1889-90.*

<sup>2</sup> *Anlagen*, vol. ii. No. 1, "Staatsschuldenverwaltung."

<sup>3</sup> "Zur Verzinsung der zur vorübergehenden Verstärkung des Betriebsfonds der Generalstaatskasse durch Ausgabe von Schatzanweisungen zu beschaffenden Mittel für 1889-90 = 600,000 Mark vorgesehen werden."

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characteristics which mark the funded debt as such. The more the feature of permanency in the credit of the state (empire or commune) comes into prominence, the more does the legal claim of the creditors to a repayment of the principal of the debt decline; the state's obligation to redeem the debt is postponed or entirely done away; the dates and the amount fixed upon for the redemption of the debt, whether by the terms of the contract with the state's creditors or by legislative enactment, are gradually less and less regarded, or entirely disregarded.

The earlier Prussian loans, at the beginning of the nineteenth century, were issued for a term of only 3-8 years, and their redemption was accordingly divided into 3-8 instalments. Even in the midst of the distress under which the ill-ordered national finances labored, payments continued to be made towards the discharge of national obligations; one million thalers a year being expended for this purpose in 1818 and 1819. On the first English loan (to Prussia, 1818) there were to be paid, on the principal of the debt, 3 per cent. during the first year and 2 ½, 2, 1 ½ and 1 per cent. in succeeding years.

Premium loans, the attraction of which lies largely in the gambling element infused into them, belong, in the history of Prussian debt, chiefly to this period, and recur from this time down to the middle of the nineteenth century. In England this fiscal expedient went out of use about the beginning of the century. The first Prussian premium loan was issued in 1796, the second in 1821, the third in 1832, the fourth and last in 1855. The terms of these loans bind the state, by the specifications of the lottery scheme which they embody, to the payment of fixed annual installments; in order to heighten the allurements of the loan the drawing of lots for the release of bonds is arranged to take place as soon after the issue of the bonds as may be, and with as large prizes as may be. But the scheme for the release of the bonds by lot always covers a considerable term of years, so that there is even yet (1889) a remnant of the Prussian premium loan of 1855 outstanding. The same is the case with the

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<sup>1</sup> Richter, *Das Preussische Staatsschuldenwesen*, p. 222.



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premium loans issued by Baden, Bavaria, Brunswick, Dessau, Hamburg, Lubeck, Meiningen and Oldenburg, 20, 30 and 40 years ago.

It is not only the form of this class of loans, but also the substance of the method, viz., the hard and fast scheme of redemption, which is to be regarded as a transitional stage in the course of development that results in the full-fledged funded debt. While this method was abandoned in England in 1828, in France in 1848, and in Austria in 1859 - for reasons already suggested by our historical survey of the facts - it is still retained in Prussia. A motion was introduced in 1856 in the Upper House to abolish the requirement of redemption by a fixed scheme; in 1867, in the Reichstag of the North German Confederation, Twisten made a similar proposition; but neither of these projects came to anything. The productive character of the compact body of the Prussian national railway debt has occasioned (Law of March 27, 1882) an adherence to a fixed scheme of redemption, at the rate of three-fourths of one per cent., to be paid out of the annual net receipts, It is instructive to note that this obligation, which the brilliant results of the railway business have made it possible to meet, has in point of fact been met not by an actual cancellation of existing debts, but by contributions to new expenditures made by the state, which would otherwise have been covered by new loans.

§ 530. The funded debt of an unlimited term, without obligatory redemption, or, at any rate, with no other obligation than that imposed by legislative enactment, logically leads up to the form of the annuity (*rentes*).

In this form of debt the obligation of the state which owes the debt does not include repayment of the principal, but only the annual payment of interest.

We have seen that this most highly developed form of national debt, which goes back to the beginning of public debts in the city republics of Italy and Germany, is related to the life

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annuities of earlier times and has gradually developed in England into the typical form of a national debt.

While this form answers in all respects to the essential nature of a developed national credit, it still suffers a few limitations. In the first place this highest development of national credit, and the resulting abolition of all obligation to repay the principal, does not abolish the fact that individual creditors may sometimes find it desirable to withdraw their loans in order to use the capital which they represent for other purposes. It follows, therefore, that a public debt in the form of annuities presupposes the stock exchange where the national bonds can always find buyers, and which will, by virtue of this fact, act as a substitute for redemption by the state.

But while this restriction applies not only to the public debt in the form of annuities, but to every extensive debt owed by the state, there is still another and more important limitation to be mentioned. The interests of the state which issues the loan demand that it take the form not simply of a perpetual rent payment, but that it must take the form of interest on a certain specified capital which the state reserves the privilege of repaying sooner or later; for the reason that future circumstances affecting the national credit or the money market may make it possible to borrow at a lower rate of interest and so effect a reduction or conversion.

In the late adoption of the annuity form for the public debt in Prussia and other German states, as well as in Austria, it has accordingly been thought best that the securities should still retain the form of an obligation to pay a certain principal. In England this form has been readopted since 1866. In France the form in which the *rentes*<sup>1</sup> are issued leaves it an open question whether there is any principal, and, consequently, whether the state has a right to redeem the debt. But the decree of March 14, 1852, (dealing with the conversion of the 5 per cent. *rentes* into 4 ½ per cent.) established the principle<sup>2</sup> that this right

<sup>1</sup> Stein, *Finanzwissenschaft*, vol. ii. (5<sup>th</sup> ed. 1886), pp. 265-267.

<sup>2</sup> Block, *Dictionnaire de l'administration française* (1877), p. 774.

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is "inherent in the nature of an obligation engaging to pay a perpetual annuity." In practice considerable departures from the annuity form of the public debt have been made in France; in 1878 a loan of about 500 million francs was issued for railways, the loan being in the form of a 3 per cent. *rente*, but not convertible, and payable in 75 yearly installments at the face value of the principal. The immediate reason for this arrangement was that the securities issued by the private railway companies, and to cover which this loan was incurred, were likewise redeemable within a term ending between 1950 and 1960; and this for the reason that the, railway lines would at that time become the property of the state.<sup>1</sup>

§ 531. Connected with this development is the introduction of the Ledger of the Public Debt [*Staatsschuldbuch*] in Prussia and other German states.<sup>2</sup>

Ever since the edict dealing with the Prussian finances, dated October 22, 1810, the principle has been adhered to of making all the bonds of the Prussian public debt payable to the bearer. By an ordinance of January 17, 1820, dealing with the future management of the public debt, all obligations then outstanding, electoral, provincial and municipal, and bearing the name of a specified creditor of the state, were retired. After the acquisition of the new provinces in 1866 it was provided by laws of February 29, 1868, and of February 11, 1869, that public obligations issued by these provinces and bearing the name of the creditor need not be converted into obligations payable to the bearer, but the central administration of the national debt was authorized to make, such securities payable to the bearer at the request of their holder.

The case is different in other countries. In England, France, Holland, Austria, and also in some of the German states, in Hamburg and in the United States of America the practice has been, even down to the very latest times, either to write the

<sup>1</sup> *Finanzarchiv*, 1884, pp. 269

<sup>2</sup> E. Francke, *Finanzarchiv*, 1884, pp. 265-303. Löbe, *ibid.*, 1885, pp. 194-216.

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public obligations payable to a creditor specified by name, or, more generally, to register them in a book kept for this purpose. In England the state's creditor receives only the amount of interest agreed upon the nominal principal of the debt being entered against his name in the Great Ledger, in which the Bank of England enters the names of all holders of the consolidated debt. The creditor receives no bond in evidence of the debt. In France the Revolution, at the same time that it achieved the consolidation of the funded debt, also created, by a law of August 24, 1793, the Grand Livre de France, in which every item of debt must be entered if the claim is to be binding on the state. The holder of the public debt receives an abstract (*inscription*) of the entry in the Grand Livre (in which he is usually mentioned by name), certifying the entry. The Receiver-General of each of the eighty-six departments keeps a subsidiary ledger, in which he likewise makes entries of *rentes*. The items of debt entered in this subsidiary ledger may, on request, be transferred to the corresponding ledger kept in any other department, or to the Great Ledger in Paris. Interest is paid on presentation of the "inscription." This reads either in the name of the creditor, or payable to bearer (being in the latter case provided with interest coupons).

A desire for a change of the same kind has repeatedly been expressed in Prussia also, even as early as the enactment of the law of December 19, 1869, dealing with the consolidation of the public debt. More particularly a proposal was brought forward in the Chamber of Deputies during the session of 1880-81, which led the Prussian government to take up the matter, and, by a proposition presented to the Chamber in 1882, to prepare the way for the law of July 20, 1883, dealing with the Ledger of the Public Debt. This example was followed by the Kingdom of Saxony in its law enacted April 25, 1884.

§ 532. The decisive argument for this step was the following: While the mobility of capital was adequately provided for and satisfied by the practice which had been in vogue in Prussia

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since the beginning of the century of issuing national bonds payable to the bearer, it is also true that there is a large body of capital seeking investment which is not best served by this form of securities.

Foundations, trusts, church property, and the like, seek a form of investment which affords the greatest possible security against loss, at the same time that it dispenses with administration or superintendence on part of the owner. Moreover, as the accumulation of capital goes on there is a constant increase of the number of persons seeking a form of investment that is permanent, safe and free from care. The expedient resorted to in the past, of depriving securities payable to the bearer of transferability, had proved inadequate; it does not afford the requisite security and also involves difficulties and complications.

Sufficient security is to be found only in a provision abolishing the transferability of bonds employed for investments of this class. This can be accomplished by substituting a registration of the debt in a ledger in place of an issue of bonds. At the same time the practice of issuing bonds payable to the bearer may be continued in order to meet the demand for a class of public securities that are easily transferable. The law provides that bonds of the 4 per cent. consolidated debt may be converted into a book-debt due to a particular creditor specified by name; the conversion is to take place upon presentation of the bonds and by means of an entry in the book kept by the central administration of the public debt. A notice of the entry, in due form, is given the creditor. Interest is paid to the creditor or to his attorney. The fee for entering the debt on the ledger is 25 pfennigs per 1000 marks (with a minimum fee of one mark. For the issue of transferable bonds, in case the debt is withdrawn from the ledger, the fee is 50 pfennigs per 1000 marks.

The disadvantages of the new scheme are closely related to its advantages. There are inconveniences in the way of any change of ownership; any transfer to a third party involves more trouble than is the case with obligations payable to the bearer.

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The re-conversion into the form of a bond involves certain formalities, and so long as the claim remains in the form of a book-debt the creditor is not possessed of any evidence of debt which will unquestionably satisfy any third party of the existence of the book-debt, and the creditor frequently has occasion to prove the fact of his claim on the state (as e.g., in proving assets, in giving security or mortgage). The Ledger of the Public Debt, moreover, is on other grounds not open to the public.

Still, the new arrangement has come into use more and more. The Ledger of the Public Debt was opened October 1, 1884, and the number of creditors who have made use of it has increased with each succeeding year since that time.

The entries on April first of each year have been as follows:

1885	643	entries	of	52,192,700	marks
1886	2918	"	"	155,533,900	"
1887	4491	"	"	206,642,150	"
1888	5929	"	"	334,442,700	"
1889	6781	"	"	387,804,400	"

Of this last named number of entries about

33	per	cent.	are	4,000	marks	and	under
20	"	"	"	4,000	"	"	"
31	"	"	"	10,000	"	"	10,000 marks
8	"	"	"	50,000	"	"	50,000 "
8	"	"	"	100,000	"	"	100,000 "
						"	over

Of these entries 4230 were to the account of physical persons, 1025 were to the account of legal persons, and 1493 to the account of estates not possessed of a legal personality.<sup>1</sup>

### III. THE STOCK EXCHANGE AND THE MANAGEMENT OF THE PUBLIC DEBT.

§ 533. It is with the public credit as with credit in general; the employment of credit gives rise to special kinds of transac-

<sup>1</sup> *Amtliche Bekanntmachung der Hauptverwaltung der Staatsschulden*, April 8, 1889. The following items are taken from the same publication: The interest on 3481 of the entries was paid by check or postoffice money-order sent by the officials in charge directly to the address of the creditor, 727 by credits at the Imperial Bank, and 4215 by direct payment at the central or branch offices of the government.

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tions in credit, and the resulting special branches of the credit business in their turn give rise to special organs and organizations, which become a necessity to the existence of the business in any highly developed form.

The modern organization of credit in general is represented by two classes of institutions known in the language of modern business life by the names "Bank" and "Bourse" or "Exchange." The distinction between these two kinds of institutions (see vol. i. sec. 423) lies in this, that the bank receives and advances money, so that the bank's business originates the paper with which transactions in credit have to do (such as deposits, bills of exchange, bank notes, drafts, mortgages, public bonds); whereas the bourse is occupied with the circulation of credit-paper already in existence - its business is buying and selling of securities.

The development of both these organs goes hand in hand with the development of business activity. It is only gradually that these organs succeed in absorbing the credit business and that, in so doing, they react upon the credit business and increase its volume. The course of development is analogous to that of productive industry.

Productive industry, too, only gradually develops the methods proper to a high division of labor, and so advances from the stage of household industry to that of production on a large scale, from the stage of barter to that of money. The market upon which productive industry places its products is at the outset some adjacent center of exchange, which is presently succeeded by a larger market with a wider tributary area, until finally great world-markets are established, whose influence extends over many countries and vast areas, and acts to further specialize production.

The case is similar with the business of transfers of the usance

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of the owners of the registered debt 6073 live in Prussia, 637 in other German states, 13 in England, 11 in America, eight in France, seven each in Austria and Russia, five in Asia and two in Africa.

The use of the Ledger by guardians and courts of ward for the safe-keeping of the property of minors, invested in Prussian consols, has hitherto been relatively inconsiderable. Only 416 entries of this kind have so far (1889) been made.

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of capital. Answering to the stage of production by household industry we have a stage at which credit is entirely absent, any capital which one household may be unable to use productively being hoarded, while other households may suffer for want of borrowed capital. When the employment of credit begins to develop and the transfer of capital becomes recognized as a usual thing, it is at first simply a transfer between neighbors, burdened with all the annoyance and inconvenience which must always characterize a business relation so entirely local and bound up with such close personal relations. The effort to make the demand and supply of capital correspond in volume, length of term, rate of interest, security, etc., can be only partially successful so long as the effort is not seconded by the presence of a wide-reaching money-market and the proper business organization.

Just as the development of trade first establishes an easy, regular and safe exchange of commodities, and thereby relieves the producers and consumers of the trouble of seeking each other out and reaching an adjustment of their mutual needs, so, as regards the exchange of capital, a like purpose is served by the development of independent business organs whose specialized function is trade in the use of capital. When this development is accomplished the new organs undertake the work previously done by those in need of and those in possession of capital. It is of course true, as in the nature of the case is true of all historical development, that even after this stage has been reached there is still a considerable volume of circulation of capital by the old method; widespread usage, individual habits and inclinations change only very slowly, and the circumstances and customs, both of social life and of business, vary greatly from place to place. But the tendency in any progressively developing industrial community is constantly toward a growth of these intermediary organs whose logical purpose is a progressive centralization of the money market.

§ 534. The public credit partakes of this development in an eminent degree.



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The great volume of its demand for capital on the one hand, and the long or unlimited term for which it requires its loans on the other hand, both contribute to make the public debt a very considerable item in the business done by these great organs of credit, and also to bring the public debt relatively early into the organized money market.

The banks, by their great accumulations of deposits, have, at the outset, a virtual monopoly of the means necessary to raise those great sums which a public loan demands. As a result of the vague and uncertain ideas prevalent in the early, undeveloped stages of banking, the banks often turned over to a borrowing state capital which had not been entrusted to them for such a purpose. The mixing up of the earlier bank of issue with the business of the public debt, and the part which the Marine Commerce of Prussia played in its day as an intermediary between private persons and the administration of the public debt, belong to the stage of undeveloped banking. Mature development results in differentiation. Modern usage in England (affording a significant contrast to the usage on the Continent) has for a generation past gone so far as to restrict the term bank to those establishments alone which carry on a trade in short paper. Enterprises which deal in paper of a longer term, with the placing of public loans and the like are known by other names. This sharp distinction of names is an expression of the clear distinction observed between the two kinds of business. The mature public credit presently outgrows its dependence on the Bank. It applies directly to the Bourse, the second organ of the credit business, by long usage the indispensable intermediary for long loans.

The requirement of perpetuity for its loans develops hand in hand with the demand for very large loans by the state, but it is to be noticed that there has been no corresponding development on the part of the capitalists who furnish, the loans to the state. The discrepancy which arises from the presence of these two incompatible requirements may be and has been removed by the establishment of a daily market for securities. This is

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the meaning of the Stock Exchange. And this function of the stock exchange is performed with increasing efficiency as the sphere of the stock exchange widens and the number and variety of securities dealt in increases, and as the number of buyers and sellers of securities in the daily market increases.

To illustrate these general remarks by facts taken from tire actual business life of today, there is given in what follows a survey of the exchanges of Berlin and London and the business which is transacted from day to day in such securities as are quoted on these exchanges.

§ 535. The number of securities of which daily quotations are permitted<sup>1</sup> on the Berlin stock exchange is at present (1889), according to expert computation,<sup>2</sup> 985. This number of course includes items of very various degrees of importance, as e.g., a public loan of a few million marks on the one hand, and a public loan amounting to hundreds of millions on the other. The total number of items appreciably exceeds the corresponding figure for the previous year (883 on May 10, 1888). The face value of the entire aggregate of securities quoted is 54,573 millions (as against 52,563 millions on May 10, 1888); the market value being 55,669 millions.

Of this total by far the greater portion is made up of public loans:

55 German Imperial, State, and Municipal Loans	9,294	million	mark
108 foreign State and Municipal Loans	<u>28,359</u>	"	"
Total	37.653	"	"

This figure of course does not represent the volume of business done on the Berlin exchange; for it takes no account of what proportion of the total amount of any given securities enters the market of this one center of the traffic in securities.

<sup>1</sup> Besides those securities whose quotation is officially permitted there is also a considerable number which are dealt in without being officially quoted.

<sup>2</sup> *Handelsblatt der Nationalzeitung*, Supplement to No. 316, May 22, 1889, The day for which this compilation was made was the tenth of May, 1888 and 1889. I have not been able to revise the computation, and I am inclined to question many of the items.

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This is especially true as regards foreign national bonds. But so long as we view this presentation of facts simply as indicating what takes place on a representative stock exchange it answers the purpose satisfactorily. The information it affords is especially significant if we take note of the market value and the rate of interest of the various securities, and the relation between the two.

The aggregate market value of all German, imperial, state, and municipal bonds was 9797 millions (105 per cent. of the nominal value) and the aggregate annual interest was 358 millions 3.85 per cent.

The market value of foreign, state, and municipal bonds amounted to 28,360 million marks (100 per cent.), the aggregate annual interest being 1218 millions (4.26 per cent.).

Beside public securities (163 altogether) there were 822 others, issued by private concerns. While the aggregate of public securities was 37,653 millions, the private securities amounted to only 16,920 millions, including (as is also true of the state bonds) a considerable number not owned in the country, especially foreign railway bonds and railway shares (9624 millions) and foreign mortgage loans (1087 millions). The number and diversity of enterprises whose paper is quoted is very great: railways, banks, mines, breweries, sugar factories, gas and water works, machine shops, chemical factories, spinning mills and dye works, building societies, and insurance companies. The papers were partly shares, partly bonds.

The shares of Ion banks, of a nominal aggregate value of 1449 million marks, paid a dividend of 100 millions and were sold at an average price of 146.25 per cent. The dividend amounts to 7.6 per cent. of the nominal value, or 5.2 per cent. of the actual market value of the stock. The shares of 84 mines, of a nominal value of 452 millions, with a dividend of 22.7 millions, were quoted at 524 millions; that is to say, the dividends were 5 per cent, of the nominal value, or 4.2 per cent. of the market value of the stock. Shares of 38 breweries, of a nominal value of 75 million marks, with a dividend of 6.1 millions,

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were quoted at 131.2 millions; that is to say, the dividends amounted to 8.1 per cent. of the nominal value, or 4.6 per cent. of the market value of the stock.

§ 536. The number of securities quoted daily on the London stock exchange<sup>1</sup> is about twice as great as the number quoted on the Berlin exchange, viz., about 1800.

Of this number 340 are bonds of states, provinces, colonies and cities. Nearly two-thirds of these belong within the British Empire, and some 140 are from foreign countries. Interest on the greater number of these latter securities is paid in London, only 16 of which this is not true being quoted on the London exchange, and these 16 are for the-most part the bonds of great states, such as France, Italy, Prussia and the United States.

The second great class, following the public securities, is made up of railway paper, comprising some 650 different kinds. Of these, 600 belong to railways in the British Empire, including India and the Colonies; the remainder represent foreign railways.

The third and final class comprises shares and obligations issued by concerns of the most diverse kinds: banks, insurance companies, canals and docks, mines, gas and water works, street cars, telegraph companies, breweries, and a variety of other industrial and commercial concerns, numbering in all some 800.

There is no computation at hand showing the nominal amount and the market value of these securities. Nor would a comparison of their aggregate value with the corresponding figure for the Berlin exchange yield any valuable results, unless the degree of intensity represented by the figures in both cases were also determined; that is to say, unless we could also determine to that extent each of the securities that are dealt in on the stock exchange is actually employed as an investment of capital and so is an object of purchase and sale.

We may, however, supplement the general figures given above by a few data of a more special character, of undoubted accuracy, and very significant for the purpose in hand.

<sup>1</sup> *Economist*, July 6, 1889, pp. 883-886.

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English consols bearing interest at the rate of  $2\frac{3}{4}$  per cent. until 1903 and  $2\frac{1}{2}$  per cent. after that date, and redeemable at the option of the government after 1923, were sold at  $98\frac{1}{2}$ . The bonds of the great English railway companies (Great Eastern, Great Western, Great Northern, Midland, London and Northwestern, Northeastern), bearing interest at the rate of 4 per cent., are quoted at 130-135.

The shares of the London banks of deposit and the London and Westminster Bank, paying 15 per cent. dividends, are quoted at 355 per cent.; London Joint-Stock Bank, paying  $12\frac{1}{2}$  per cent. dividends, are quoted at 277 per cent.; London and County Bank, paying 20 per cent. dividends, are quoted at  $467\frac{1}{2}$  per cent.

On the other hand, the Russian 5 per cent. bonds are quoted at 101-103; the Greek loans of 1881 and 1884, paying 5 per cent. interest, at 92 per cent.; Hungarian 5 per cent. bonds at 100-101; Mexican 6 per cent. bonds, at 95; Japanese 7 percents., at 110; Santo Domingo 6 per cent. bonds of 1869, at  $17\frac{1}{2}$ .

These figures (July 6, 1889) may be compared with some of the items of the Berlin exchange list (August 1, 1889).

The German imperial loan, bearing interest at  $3\frac{1}{2}$  per cent., is quoted at 104; the Prussian national loan, bearing interest at  $3\frac{1}{2}$  per cent., is quoted at 105.

The bonds of the East-Prussian Southern railway, bearing  $3\frac{1}{2}$  per cent. interest, are quoted at 102 per cent.; the shares of the same road, which in 1887 and 1888 paid 6 per cent. dividends, are quoted at  $108\frac{1}{4}$ . The shares of the bank of the Berlin Kassenverein ( $5\frac{1}{3}$  per cent. dividends) are quoted at 129; the shares of the German Bank (9 per cent.), at 172 per cent.; the shares of the Discount Company (12 per cent.), at  $233\frac{1}{2}$ ; the shares of the Tivoli Brewing Company (7 per cent.), at 145; the shares of the Patzenhofer Brewing Company (55 per cent.), at 738.

Taking all the securities together which are quoted on the Berlin exchange, it, appears on computation (as already indicated above) that in the course of the last year (May 10, 1888 to May 10, 1889) there has been an advance in the market value in the proportion of 48 to 53; i.e., about 10 per cent.

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§ 537. The few figures here given from these two great money markets are intended to show two things.

In the first place, the figures of aggregates are intended to give some idea of the extent to which this form of investment affects the body of investments taken as a whole.

In the second place, the juxtaposition of securities selected as types of different classes, together with the variation of market value between these different types, may serve to suggest what are the determining factors of the market value of securities, and consequently of the rate of interest. It is intended to bring out the manner and the causes by which the price of securities, or what is the same thing the rate of interest, is determined in the modern developed money market through the medium of the great stock exchange, - how this rate of interest is determined for the great multitude and variety of investments, not only within the limits of a single industrial community, but within the wider limits of the world-market. It is therefore intended to bring out for our special purpose what are the determining factors that decide the conditions on which public loans are obtained.

Let us now take a look at the exchange list of the London exchange, with a view to comparing the quotations of the various securities which it names.

Consols pay all income of  $2\frac{3}{4}$ , and this is paid for at a capitalized value of  $98\frac{1}{2}$ . The annual amount of this income is to remain unchanged until 1903, after which date it falls to  $2\frac{1}{2}$  per cent., and may then, after another twenty years, in case a further reduction of interest should make the transaction profitable for the government, be redeemed at its nominal value of 100. The rate of  $2\frac{3}{4}$  per cent. paid on consols is an expression of the value in use of capital under the conditions prevalent in a wealthy country with a high tax-paying capacity and a highly developed public credit.

The loans of the great English railway companies are obtained on conditions closely approximating the low rate of interest achieved by the public debt. Having been issued many years

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ago, when the rate of interest for this class of securities stood at 4 per cent., these railway bonds have appreciated by about one-third, for the reason that, as shown by later loans issued by the same railway companies, the present rate of interest for securities of this class is only 3 per cent., whereas these bonds secure the continued receipt for the future of the 4 per cent. originally stipulated. It appears, therefore, that the difference in rate of interest on English consols and that on English railway bonds is only one-quarter of one per cent.; the general situation of the English money market is very much the same for both classes of obligations, while the peculiar circumstances affecting the standing of one class and of the other are pretty evenly balanced, the security offered by a flourishing railway business (6-8 per cent dividends) on the one side nearly balancing the security offered by the English public credit on the other. Dividends range higher among the London banks of deposit. A share of their stock brings a yearly profit of 12 ½, 15 or 20 per cent. The price of the shares is consequently much higher than it was at the outset - 277,355 and 467 ½ per cent. But even at these prices the shares still yield interest at about 4 1/3 per cent. The difference in price between these shares and the securities enumerated above is due to the fact that while the same abundance of capital is available for these enterprises, and while the banks enjoy the highest degree of confidence and do a flourishing business, the rate of the annual profits is uncertain, because these shares represent not a loan, as in the case of the railway bonds, but a share in the business, The fact of this uncertainty affects the value of the securities all the more sensibly where, as in this case, the profits are very high, and where, consequently, the chance of a decline in the rate of profits is relatively great as compared with an investment yielding a low rate of profits.

Lastly, there are the foreign public loans. Russian and Hungarian loans pay, nominally and actually, 5 per cent. interest. The nominal 5 per cent. Greek loan is quoted at 92, and conse-

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quently yields an actual interest on the investment of  $5\frac{1}{2}$  per cent.; the Mexican loan of nominally 6 per cent. sells at 95, and accordingly yields an actual interest of  $6\frac{1}{3}$  per cent. on the investment; the Japanese 7 per cent. loan sells at 110, the actual interest on the investment being consequently  $6\frac{1}{3}$  per cent.; the 6 per cent. loan of Santo Domingo, finally, is quoted at  $17\frac{1}{2}$ , which goes to say that in this case there is no regular payment of interest. If we compare them with the case of the English debt, the varying rate of interest at which the Russian, Greek, Mexican and Japanese obligations are capitalized argues, that in each and all of these countries the financial and political conditions requisite to a high national credit are not present in the same degree as in England, and, further, that the transfer of surplus capital from a country possessed of a large accumulation of capital, such as England, to a very distant country meets with a certain peculiar element of distrust on the part of the owners, which hinders a free and uniform distribution of capital.

§ 538. We may now proceed to compare the selected securities of the London exchange, one by one, with the corresponding securities on the Berlin exchange. Relatively to one another the various classes of paper on the Berlin exchange range in much the same fashion as those on the London exchange. In the one case as in the other the price of a railway obligation bearing the same rate of interest is approximately the same as that of the corresponding state paper. The difference between the market value of shares in dividend-paying business enterprises and that of a state or railway-bond bearing interest at the same rate, recur in Berlin as in London, but in this case as in the former the difference is quite moderate so long as the stock in question is that of non-speculative undertakings doing a steady and un Hazardous business; such, e.g., as the bank of the Berlin Kassenverein, whose shares, then counted at their market price, yield a dividend of about 4 per cent., that is to say, only some one-half per cent. more than the national bonds. In the case of speculative banking enterprises with less invariable



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dividends the market price is lower relatively to the dividends; that is to say, the interest on the investment in these securities is higher. Investments in the German Bank and in the Discount Company pay more than 5 per cent. interest. In case the dividends are uncommonly high, as in the case of the Patzenhofer Brewery, the risk of a decline in the dividends reacts on the market price of the stock, with the consequence that investments in such securities are made at an unusually high rate of interest ( $7\frac{1}{2}$  per cent.). All the cases cited are fair typical examples of what occurs in both the markets in question.

The great difference between the London exchange and that of Berlin lies in this, that the normal level of the rate of interest in London is a little lower. This normal level is indicated by the market value of consols in London and of the Prussian bonds in Berlin. Consols bear interest at  $2\frac{3}{4}$  per cent., and may be bought at  $98\frac{1}{2}$ ; the Prussian bonds bear interest at  $3\frac{1}{2}$  per cent. and are sold at 105. The English government, consequently, pays its creditors interest at a rate some two-thirds of one per cent. lower than the Prussian government pays its creditors.

The ground of this cannot be sought in the different degree of credit enjoyed by the governments of the two countries; for the other securities which we have cited as typical examples from the two countries in both cases stand in somewhat the same relation to the state paper of their respective countries. The reason must therefore be sought in general causes which decisively affect the general money market of Germany as distinct from the English money market.

These grounds are to be sought in peculiar circumstances affecting the money market of each of the two countries; peculiarities which may be expected gradually to disappear with the progressive development of an international money-market, in a manner similar to that in which discrepancies of price in other commodities between one country and another are disappearing. The limit to the discrepancy in question is determined by the obstacles, physical and psychological, in the way of a transfer of capital from one country to another.

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§ 539. The foregoing remarks are intended to show that the course of prices of securities, or what is the same thing, the rate of interest on securities, depends on two factors; first, the general condition of the money market, which will vary with the peculiarities of the industrial development from which it results, and second, the peculiar circumstances affecting the standing of each particular investment in detail. Both these factors are in constant process of change and growth. If we compare the situation today in the money market of London or Berlin with the condition and circumstances of the same market ten or twenty years ago, we find a difference between the present and the past which is common to both markets, and which runs as a characteristic feature through the money-markets of all countries; this characteristic feature is the higher average rate of interest paid at the earlier period. What we have already taken note of as a difference existing between England and Germany reappears as a difference in time between the money-market of today and that of earlier years. The rate of interest on English consols twenty years ago was  $3\frac{1}{3}$  per cent.; the rate of interest on Prussian state paper was  $4\frac{1}{2}$  per cent. The rate of dividends or interest on railway bonds, bank stock and railway stock, relatively to the rates obtained on public securities, was the same then as now. On an average for the years 1830-1875 the interest on English consols was  $3\frac{1}{5}$  per cent.; on an average for the years 1839-1876 the income from the shares of the banks of deposit (London and Westminster Bank, London and County-Bank) was 5 per cent.,<sup>1</sup> and the dividends on the shares of the great railway companies averaged about the same. The income from these securities today is  $3\frac{1}{2}$  -  $3\frac{3}{4}$  per cent.<sup>2</sup> The highest rate on investments being yielded by those railways which declare high dividends.

As is true of the money market in general, so also with respect to each particular class of securities in detail; the conditions have changed in the course of years. At any rate it is

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<sup>1</sup> William Farr, *Journal of the Statistical Society*, 1876, vol. xxxix. pp. 528-530.

<sup>2</sup> *Whitaker's Almanack*, 1889, p. 670.

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impossible to prove conclusively in any particular case that the standing of any one has remained entirely unchanged, while the presumption always is that the current of time wherein all living things lie will have had its effect at every point.

It might be a very difficult matter to ascertain whether the last few decades have brought fresh developments that have affected the credit of Great Britain. On the other hand, there is ever-presumption in favor of the position that the progressive consolidation of the German Empire and of Prussia during this period has affected their credit favorably. It is a fact which no one will question that Great Britain or the German Empire will be able to obtain credit on better terms during an era when they are making but slight use of their credit than at a time when the contrary is true. It is likewise beyond question that the extended credit operations carried through by the Prussian state for the eminently productive purposes of its state railway system must make quite a different impression on the money market than that produced by loans of the same amount for war purposes, especially by loans issued during the war. It is certain that the credit of the French nation was lower during and immediately after the last great war, when large loans were placed at a rate of about 6 per cent. interest, than at present, when France pays 3 ½ per cent. interest (3 per cent. *rentes* being quoted at 85).

The case is much the same with other securities. English railway shares approach the level of consols much more nearly at present; the interval twenty or thirty years ago was 1 ¾ per cent., it is now scarcely 1 per cent. It is safe to assume that the ground of this lies in the increasing consolidation of these great enterprises, and in their continued productivity and a conviction of their permanence. The bonds of the railway companies, as well as the shares, have approached nearer to the rate of interest received on investments in consols; the figures were formerly 4 and 3 1/3 per cent. respectively, while they are now 3 and 2 ¾ per cent. respectively.

In all this no notice has been taken of the obvious fact that

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any alteration in the productivity of industry will have its influence on the rise and fall of the market values of securities, especially of such securities (shares) as derive their returns directly from the earnings of the business which they represent. It is also to be remarked that we have here been comparing the income yielded by securities simply as interest on an hypothetically invariably amount of capital, and computed at so much per hundred of nominal capital, whereas on the stock exchange the basis of operation is always the actual value of the securities and not the nominal value.

§ 540. The relation of capitalists to the stock exchange is determined, in a general way, by the degree of attractiveness of the securities offered for investment, and secondarily by the degree of centralization attained, in virtue of which the exchange governs, to a greater or less extent, the entire field of investment. Their relation to the exchange is governed, as regards details, by special circumstances affecting each particular class of securities.

It is only through the centralizing force of the trade in securities that the business community has reached the point of affixing a single market value to any given investment, and of correcting any aberrations by a revision from day to day. So long as investment has not developed into the form of securities the centralising force of the trade in investments either fails of its effect, or works out its results slowly and painfully through intermediate steps. The obligations of a German railway enjoy a credit equal to that of German state paper and are therefore only obliged to pay  $3\frac{1}{3}$  per cent. interest, but it will take years before equally secure mortgage loans on urban real estate can be brought below  $4\frac{1}{2}$  per cent. interest. If these loans can be thrown into the form of securities of the ordinary kind, as has been the aim for more than a hundred years past of the Prussian Mortgage Loan Associations, by the formation of a corporation competent to issue such securities, then this interval between mortgage loans and railway obligations in point of the rate of

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interest will vanish. But if it hereby appears that the interests of the persons in need of capital are on the side of securities of a marketable form, it is also true that the adoption of such a marketable form for mortgage securities is also very attractive to capitalists. Through the progressive division of labor, this form of securities will relieve the capitalists of all the trouble of selecting investments; all the details of this process of selection being shifted to those specially engaged in the business, leaving the investor nothing beyond the decision as to the kind and price of securities desired. Instead of partnership in distant enterprises we shall have joint-stock shares; instead of mortgage loans, debenture bonds; instead of all private loans whatever, state paper.

The question as to the character of each of the securities, as compared with its price and as compared with the price and character of all other securities, taken in conjunction with the effect produced by the influx and withdrawal of capital from stock exchange investments, offers capitalists a world-wide field for speculation; and this speculative activity in its turn, by a further specialization and division of labor, comes to the aid of the traffic in securities in making the requisite adjustments.

§ 541. The activity of the stock exchange in its present developed form effects, for one thing, a most painstaking scrutiny of those classes of investments that can be thrown into the form of marketable securities. This scrutiny, which is, in the first place, effected within the field of a particular stock exchange, is immediately and constantly made available for all the various exchanges in all countries by the help of the modern developed means of communication (telegraph, telephone).

The decision reached by means of this complex and wide-reaching scrutiny expresses itself in the quotations of the various securities on change. The incessant fluctuations to which these quotations are subject, and the growing minuteness of the fluctuations, increasing with the increasing rapidity of fluctuation, are consequences of an ever-increasing nicety of discrimi-

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nation. Instead of strong and sudden perturbations we have (here as in the case of any developed trade) a gentle but incessant ripple. And this result is possible only in so far as an ever-watchful anticipation of coming events (speculation) comes in to retard the action of causes that make for a sudden rise or fall.

The moral indignation with which this phase of modern business life is looked upon by so many, and which must perforce serve in lieu of a knowledge of the facts for large portions of the public, can never be satisfied until the truth is generally accepted, that any highly developed technical process in business life is sure to be accompanied by phenomena that are questionable on moral grounds and call for efforts at reform.<sup>1</sup>

The quotations which embody the judgment of the trade on the marketable securities express: (1) the aggregate of the features which go to make up the character of each particular security, such as the rate, degree of permanence and certainty of the interest payment, and therefore of the investment itself; (2) the rank of the individual securities relatively to another securities, and finally (3) the relation of the particular investments in question to the general condition of the money market. The selected figures from the Berlin and London exchanges given above express the influence exerted by all these factors upon the securities in question. The relation existing between the market value of any given security and the rate of interest paid by it depends in part on the varying reliability of the investment, in part on the varying circumstances affecting each, and in part on the degree of general development of the money market; this relation varies incessantly, but the fluctuations are always the outcome of a close scrutiny of facts. In any orderly national economy the obligations of the state will ordinarily stand for a normally perfect security, as well as for the lowest normal rate of interest. The administration of the public debt is aware that the price of securities, or the rate of interest at which a given

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<sup>1</sup> Cf. a paper by the present writer on "Differenzgeschäfte" (*Volkswirtschaftliche Aufsätze*, 1882, pp. 671 *et seq.*) and the literature there cited.

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loan contracted for a given purpose can be placed, depends on all the factors which we have enumerated: the condition of the national credit for the time being, the extent of its demand for loans, the situation of the general money market, the amount of available capital, and other circumstances affecting investments at home and abroad.

In issuing a public loan, therefore, the effort is to place it in such a way as to best allow for the fluctuations in the rate of interest and the price of securities which result from the action of these various factors. The points to be considered in this connection in issuing a loan are (1) the nominal rate of interest, (2) the term for which the loan is negotiated, or in other words the question as to whether it is to be terminable on the motion of the creditors, and if so, after how long a time.

The nominal rate of interest coincides with the real rate in the case of short loans, where the loan is terminable at the option of either party, so that the rate of interest originally agreed upon can readily be adjusted to the fluctuations of the market. The fluctuations of the rate of discount in such cases lead to readjustment between the creditor and debtor by a simple direct alteration of the terms of the contract, just as happens in all analogous contracts (lease) when one of the parties, on discovering an alteration in current prices favorable to himself, brings on a raising or lowering of the price previously agreed upon by terminating the old contract.

The process is more complicated in cases where this direct means of adjustment is wanting, where the agreement is either not terminable or terminable only at the option of one party, or at least not terminable until after a period of years. In such cases, inasmuch as the original agreement continues in force for a long time, the necessity of an adjustment to the altered conditions of the money market is constrained to find some other way. The market value of the loan rises or falls according as the rate of interest originally agreed upon exceeds or falls short of the rate obtainable for the time being. It is the office of a developed stock exchange to insure that these fluctuations in value find the

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most exact possible expression in the market quotations from day to day.

Since the length of time for which the loan is negotiated affects the course of the state's obligations, it clearly follows that the terms of the loan, as to whether it is to be terminable, and how soon it is terminable, and whether it may be terminated on the motion of one or of both parties, - all these considerations will influence the rate of interest at which public loans can be placed. It is for the interest of the creditors to secure the privilege of terminating the loan at their own option, while the interest of the debtor state, on the other hand, is to secure for itself the fullest discretion with regard to terminating any of its obligations. But, as we have already seen, the creditor's right to terminate a loan tends on independent grounds to vanish with the development of the public credit; this leaves no other protection for the interests of the creditor than such measures as will limit the right of the state to terminate its obligations.

The state for its part will find itself obliged to make certain concessions in this direction, for the reason that without these concessions the terms on which it could place its loans would be still more disadvantageous. All this holds with added force during a season of distress, when loans can in any case be obtained only on less favorable terms, and when the great amount of loans required may itself give rise to additional difficulty.

§ 543. The outcome of all these considerations is almost always a compromise. The creditors are assured a given rate of interest for a series of years, which implies the chance of a rise in market value wherever the national credit improves or money gets "easier." But the state sets certain limits to these advantages granted the creditors by reserving the right of redemption after the lapse of a series of years.

One method by which this result is accomplished is that which was employed in the great French loans of 1872. The state engaged to pay its creditors interest at the rate of 6 per cent. in point of fact, but this was accomplished by issuing obligations



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bearing a nominal interest of 5 per cent. and selling them at 83. Since these obligations have a face value of 100 the state cannot pay less than 100 when it comes to redeem them. That is to say, the creditors can be deprived of their 6 per cent. rate of interest only at the cost of 17 per cent. increase of the principal of the debt. This provision was sufficiently attractive to the capitalists to bring a superabundance of offers for the state securities; while if the French government had reserved the right of redemption after a year's time a good share of the readiness manifested by the capitalists would have disappeared. But the concession made by the government also lies entirely within the limits set by this discount of 17 per cent. The government can not be held to pay more in discharge of the debt than 100. Consequently as soon as it can place loans of less than 5 per cent. (when this loan will rise above 100) the government is able to redeem it at 100.

The meaning of the so-called low rate loans is that a relatively long time will elapse before the state can exercise its right of redemption. If, e.g., the French loan of 1872 had been issued at a nominal rate of interest of three per cent. and obligations of a face value of 100 had been disposed of at 50, then these obligations would today stand at 85 instead of the 50 per cent. discount at which they were issued. The state would therefore, after a lapse of seventeen years, and in spite of a great reduction in the normal rate of interest on government paper, not be able to discharge the debt without suffering a loss, while as regards the creditors they would still have a chance of gaining a further 15 per cent. after having already made a profit of 35 per cent.

The opposite extreme to this method would have been the placing of a six per cent. loan at par; this would have conceded to the creditors no chance of making a profit above the interest and no chance of permanently drawing interest at the rate agreed on in case the normal rate of interest should decline, unless, indeed, the state had bound itself in some other way to suspend its right to redeem.<sup>1</sup>

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<sup>1</sup>As a peculiar but unusual case it may happen that the government is in receipt

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§ 544. At a season when there is an abundance of capital, when the public credit is gaining, and when the present has in addition the advantage of being compared with a recently preceding period of war loans (France in 1870-1873, the United States in 1862-1865) such as we have witnessed of late, the advantages to be gained through a reduction of the rate of interest brings on an era of interest reduction,<sup>1</sup> the result is a lightening of the burden of the nation and a reduction of the income of the capitalists. This process of reduction of the rate of interest may be viewed from three distinct points of view: of legality, of equity, and of expediency.

As to the question of legality, it is to be accepted as a matter of course that any modern state must reserve to itself, in the terms on which the loan is issued, all the rights and privileges which it wishes to exercise at all. The state can exercise no right of redemption, and therefore effect no reduction of interest, unless on the basis of the terms of the contract.

The question of equity is somewhat more difficult. It is a matter of experience that, even in the case of loans in which the state has no interest, considerations of fairness and equity will modify the tendency to a reduction of interest in special cases. This serves to illustrate the truth that the determining factors in business life are not mechanical but moral forces. An example of this is afforded by the funds which have been loaned out by benevolent institutions and have afterwards not been repaid by the benevolent debtors of the institution when the normal rate of interest has declined. The fact may be cited as a case

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of a large surplus revenue which might advantageously be applied to the discharge of the debt, except for the obstacle that the terms on which the loan was negotiated prevent redemption of the debt until a later date, while the bonds in question bearing interest at a rate above the present normal rate have advanced in price so that they could be bought in the open market only at a considerable premium. This exceptional state of things exists at present (1889) in the United States of America.

<sup>1</sup> G. Schanz "*Die Konvertirung preussischer Staatsschulden*," Finanzarchiv, 1885, pp. 1085 *et seq.* M. Ströll, "Ueber die neueste Konversions-Aera in Deutschland," Conrad's *Jahrbücher*, 1886, N. F. vol. xiii, pp. 422 *et seq.*

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in point that the Professors' Widows' Fund of Gottingen has been able to draw interest at 4 ½ per cent. on a good share of its capital because the debtors, out of a regard for the benevolent purpose of the loan, have declined to take advantage of the reduction that has occurred in the normal rate of interest and so insist on a reduction or a discharge of the debt. There is all the more urgent reason for the demand that the state shall, in a similar manner, have regard to other considerations than the course of the market; for we are accustomed to measure the doings of the state by a higher standard than that which governs the relations of the market-place.

But even if we concede the justice of this view, or rather if we lay stress on it, we shall by no means come to the conclusion that attention to the financial advantage of a reduction of interest is incompatible with the higher considerations of equity or of benevolence - in short the social-political bearing of the question.

In all the activity which the state (or the commune) puts forth in the field of financial and industrial policy, the decision that has to be made does not concern the question what is right or equitable absolutely, but rather what is the aggregate of interests to be taken into consideration on one side and on the other.

An improvement of the conditions on which the state obtains its loans means a lightening of the burdens of the taxpayers; and regard for the public creditors is only a regard for one part of the taxpayers, if it is not, as is sometimes the case, a regard for interests lying entirely outside the compass of the state. Now, the constitution of the tax-paying body of citizens being what it is, and the tax burdens being distributed in the manner in which they are distributed under existing systems of taxation, a very considerable portion of the tax burden falls on the shoulders of people who never, or, at the best, very seldom, are in position to hold any share in the national securities.

Relatively speaking, the most favorably situated with respect to such participation are the lower classes of the population in France; but even as concerns that country the fact does not admit of question that the preponderant body of interests con-

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cerned in the question of taxation is not to be sought in the holdings of *rentes* among the lower classes.<sup>1</sup>

But even under an imaginary condition of things, where participation in the ownership of the public debt among the lower classes prevails to the very greatest possible extent, it is impossible to comprehend why we should disregard the plain dictates of justice, which demand that the burden of the debt and of tax payment should be reduced to the lowest figure that the state of the money-market and of the public credit will admit. Regard for the great number of households in moderate circumstances which depend entirely or mainly on income from the public funds, must not blind us to the fact that there is always a much greater number of households that have to contribute out of the product of their labor in order to pay interest on the funds.<sup>2</sup> It may be added that the familiar catch-words about "widows and orphans" are very frequently nothing but a cloak to the selfish greed of great capitalists.

§ 545. The question of expediency, as regards any reduction of interest on the public debt, depends chiefly on the consideration that in order to a successful move in this direction the state of the money-market and of the public credit must be such as to enable the state to raise the funds required at the lower rate of interest aimed at. A conversion is not an unmixed success if the previous holders of the public securities are not content to continue holding the government paper at the lower rate of interest;

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<sup>1</sup> Of the English public debt fully one-third (34.2 per cent.) is held in small amounts (incomes of less than five pounds sterling); a further one-sixth (15.5 per cent.) in amounts of 5-10 pounds sterling, and still another third in amounts of 10-50 pounds income. Still the whole of the debt was (1870) distributed among only 231,349 different holders, while the number of taxpayers in Great Britain and Ireland at the same date was nearly to millions. - *Finanzarchiv*, 1884, p. 266. Leroy-Beaulieu (*Traité de la science des finances*, 1877, p. 450) estimates the number of holders of *rentes* in France in 1869 at 7-8 hundred thousand, and is of the opinion that the number had been decupled during the period 1830-1869, although the amount of the public debt during the same time had only doubled. But the number of taxpayers in France, too, is some 10 millions, and therefore fully ten times as many as the holders of *rentes*.

<sup>2</sup> Cf. the debates in the Prussian Landtag, 1884-85. Printed in the *Finanzarchiv*, 1885, pp. 1092 *et seq.*

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that is to say, if the funds offered by the state in payment of the debt are, in whole or in part, actually paid over to the creditors and so have to be replaced out of loans from a new set of creditors. It has been estimated, e.g., that the sum paid over in the conversion of the Russian public debt to the German creditors alone, amounts to 260 million marks.<sup>1</sup>

The more highly the public credit of any community is developed, the more plentiful the supply of capital, and, especially, the greater the influence of the owners of capital and public funds upon the national administration, the more rarer will a mistake of this kind be made, and the more frequently will a mistake of the opposite character be made.

The reduction of interest in such cases is apt to follow the state of the money market only tardily. Apart from certain very striking examples of this (such as the long postponed reduction of the interest on the French 5 per cent. loan, which, when finally effected in 1883,<sup>2</sup> reduced the interest only by the inadequate figure of one-half per cent.), this measure has been resorted to with extreme caution also in Germany.

The Prussian 4 ½ per cent. public loan created by the Consolidation Act of December 19, 1869, was, by the terms of the Act, redeemable after January 1, 1885. The 4 ½ per cent. consols had by 1883 advanced to 106, and had then declined in view of the approaching redemption. The 4 per cent. consols had gone above par as early as 1880, and had advanced to 102 in 1883 and to 103 ½ in 1884. Due regard for the aggregate of taxpayers demanded (such is the language of the *Begründung* of the government's bill) a reduction of the rate of interest. Of the 4 ½ per cent. consols 545.78 million marks were outstanding at the beginning of 1885, requiring a yearly interest payment of 24.56 million marks. A reduction of the rate of interest by ½ per cent. would mean a relief of 2.73 million marks for the taxpayers. The government was content to effect this much of a reduction, although the rate at which the 4 per cent. bonds were

<sup>1</sup> *Nationalzeitung*, August 3, 1889.

<sup>2</sup> *Finanzarchiv*, 1885, p. 1094. The 5 per cent. *rentes* had risen to 120. The annual saving from a reduction of one-half per cent. in the rate of interest amounts to 34 million francs.

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quoted was proof that a further reduction could have been successfully carried out. The reason for this course was, partly, "consideration for the creditors," partly a solicitude lest capital should be transferred to more alluring but less secure speculative investments.

These were the considerations upon which the law of March 4, 1885, was based. A majority of the Landtag sided with the government. There was a scattering opposition<sup>1</sup> (on part of the Ultramontanes and the Conservatives) which even went the length of denouncing convertible public loans as vicious in principle. But this position was deprecated by the government as an "altogether infelicitous idea" [*überaus unglücklicher Gedanke*]. On the other hand, the upper house advocated a more sweeping reduction of interest on the ground that a gift to the state's creditors, such as was implied in offering them the 4 per cent. bonds (then quoted at 104.70) was entirely unjustifiable. This view was advocated more especially by the former Finance Minister Camphausen.

The fact is that the 3 ½ per cent. Prussian public funds which were nearly at par in 1885 have since then advanced to 105 and even over that figure.<sup>2</sup> By October 1886 a reduction from 4 per cent. paper to 3 ½ per cent. (and even in part to 3 per cent.) had been effected in other German securities, especially in mortgage bonds, railway securities and railway bonds; the entire amount of securities converted being not less than 1450 million marks.<sup>3</sup> It is of course evident that in the case of these securities the motives of everyday business life would act with less hindrance or scruple than in the case of the public securities.

The great body of 4 per cent. paper is made up of loans issued by the Empire and the individual states, Of these securities there were outstanding at the end of 1886 about 6200 million marks, which were still awaiting conversion to 3 ½ per cent.; that is to say, relief might be afforded the German taxpayers by this means to an amount of 30 million marks annually. But the question of a transition from 4 to 3 ½ per cent. is evidently the same as the earlier question of a transition from 4 ½ to 4 per cent.

<sup>1</sup> Cf. the defense of this position offered by M. Ströll, Conrad's *Jahrbücher*, 1886.

<sup>2</sup> Quoted on the Berlin exchange August 6, 1889, at 105.20.

<sup>3</sup> Ströll, Conrad's *Jahrbücher*, 1886, N. F. vol. xiii. p. 424.

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§ 546. The fiscal measure of a reduction of the rate of interest is more frequently spoken of by the name of "conversion" or "refunding," because of the change by which paper bearing interest at a higher rate is replaced by paper bearing interest at a lower rate. This measure comprises both of the operations which bring the public credit of today into relation with the money market, viz., the negotiation and the discharge of debt.

The more thoroughly centralized and organized the money market is, the more unavoidably is every considerable transaction in credit dependent on this central organ, whether in borrowing or in repaying borrowed capital.

The reason for this is very simple. In proportion to the efficiency with which the market for securities performs its work will it become the focus both of the demand and of the supply of capital. The market gathers, as it were into a central reservoir, all manner of securities, varying in point of the rate of interest, the degree of security of the paper, domestic or foreign, in point of kind, etc. By this means it offers an opportunity to choose between different forms of investment, and consequently an opportunity to withdraw from any one and transfer the investment to any other. The result is that any new demand for capital or for an opportunity to invest capital on entering the market is confronted with a great body of material from which it can pick and choose, and on which it can work out its own effect.

The latest fashion in the redemption of public debts, which has long since left obligatory redemption behind it as obsolete, and which redeems or not, or redeems more or less from year to year according to the general situation of the finances - this latest method of redemption can in no way effect its purpose better than by a purchase of the securities in the open market.

In placing the public loans, choice may be made either of this method, or of a direct application of the public administration to the investing public. Of this latter kind was the employment of the Grand Livre in France, above referred to, and the ramification of that institution through the provinces; the like is true of all those forms of public debt which are of the nature of a

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savings-bank for the people. But these forms of public debt afford no adequate reliance for the public finances on account of (their irregularity and uncertainty; the stock exchange, on the other hand, in proportion to the degree of its development, offers an effective means of obtaining large amounts of capital in a consolidated form. All this holds true with added force if the magnitude of the sums demanded, or any other circumstance affecting the situation, makes it necessary for the state to go outside its own boundaries for a loan. In such a case the exchange is the only organ possessed by the world's money market by which to obtain control of the funds required. A striking example of this is afforded by the great French loan negotiated after the late war.

#### IV. GOVERNMENT PAPER MONEY AND THE RESUMPTION OF SPECIE PAYMENTS.

§ 547. The experience of, the United States of America during the Civil War is full of instruction and warning for the nations of Europe; it shows that the sudden demands of a great war may not only plunge a state whose credit and finances have previously been in the most prosperous condition, deeply in debt, but may bring on the further related calamity, of far-reaching significance for the whole of the nation's industrial life - a régime of paper money. This experience serves to show, especially, that apart from any of those abuses of the permanent fiscal machinery (e.g., debts, taxes) that are apt to accompany a war epoch, there is a distinct financial danger involved in the employment of bank notes, paper money, etc. This financial danger threatens any financial system, however stable and orderly, if only the political exigencies are present that are calculated to give rise to it.

A discussion of paper money, therefore, has more than an historical interest, as dealing with one stage or one form of the development of public credit; - a stage which has been passed through and left behind, at least by the national economics of more mature growth. Such a discussion may be of practical



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value in shedding light upon conditions which exist in many states today, and which may recur in other states as well, even in spite of all known precautionary measures.

§ 548. Reference may here be made to the observations contained in the introductory portion of this work (Vol. i. sec. 412), where, in speaking of money in general, some attention is given to the subject of substitutes for money and the degeneration to which such substitutes are liable. Even in the days of ancient Greece both debasement of the coin and the use of substitutes for coin were resorted to as fiscal expedients. Even Solon remarked that many of the Hellenic states made use of silver money with an alloy of lead or copper, which was received only at a heavy discount, if at all, in foreign trade. When the Clazomenians were twenty talents in arrears in the pay due their mercenaries and were unable to raise the money, they, in order to save interest on the debt, minted iron coins to the amount of twenty talents, ascribed to them the value of silver coins, and distributed them among the wealthiest men in return for silver, with which they discharged the debt. Within the country the iron coins served the same purpose as silver, and the latter could therefore be turned to use in foreign trade. To this extent, says August Böckh,<sup>1</sup> iron served the purpose for the Clazomenians which paper money serves in our day.

Even at that early day this expedient profited by the confused notions prey alert with regard to the nature of money. The two opposite views on this subject, and the wrongheadedness of both, were recognized as early as Aristotle's time.<sup>2</sup> Now we are told, says he, that wealth consists in money. Then, again, that money is nothing but a name; that of itself it is of no value, and what value it possesses is due to the law alone, without which it would be of no use. Plato is of the latter view, and the money which he wishes to employ in his republic is of a nature to correspond to this principle.<sup>3</sup>

The Utopias of later

<sup>1</sup> *Die Staatshaushaltung der Athener* (2<sup>d</sup> ed., 1851, vol. i. p. 768.

<sup>2</sup> *Politica*, i. 3, 6.

<sup>3</sup> Büchschütz, *Besitz und Erwerb im griechischen Alterthum* (1869), p. 480.

socialistic writers are affected with a bias of the same kind. J. G. Fichte is of the opinion that a closed commercial state can make anything whatever its money by declaring that it will accept nothing in payment but this money.<sup>1</sup> Of French writers, Boisguillebert is to be cited before all others as an advocate of the view that "if men would agree among themselves they could easily abolish money altogether."<sup>2</sup> H. D. Macleod has reaffirmed the same view within the last generation.<sup>3</sup> The apostles of Rousseau who tried to put his ideas in practice in the French Revolution (St. Just) wanted to adopt a coin that could never circulate in foreign countries.<sup>4</sup> Indeed, an eminent German historian has in very recent times expressed the opinion that "the best exponent of value, in itself considered, is a token money with the least possible intrinsic value, which, in its most perfect development, would measure the value of other articles almost as exactly as a clock measures time or a yard-stick measures space."<sup>5</sup>

§ 549. In measuring space with a yard-stick the use a (previously determined) extent of space as a measure for another extent of space (to be determined). In measuring economic value we can no more employ as a standard anything that is as nearly devoid of intrinsic value as may be, than we can measure space by means of something that is as nearly devoid of extension as may be. As length can be measured only by length, so value can be measured only by value.

The seductive promise contained in this erroneous theory is especially dangerous because it sets up as an ideal what is in point of fact only a derangement of any orderly monetary system, and due entirely to extraordinary financial exigencies.

A well-ordered monetary system admits the use of such substitutes for money only as confine themselves to serving in place

<sup>1</sup> *Der geschlossene Handelsstaat* (1800), p. 91.

<sup>2</sup> *Zeitschrift für die gesammte Staatswissenschaft*, 1869, p. 395

<sup>3</sup> *Dictionary of Political Economy* (London, 1863), Art. "Credit."

<sup>4</sup> Sybel, *Geschichte der Revolutionszeit* (4<sup>th</sup> ed. 1877), vol iii, p. 159.

<sup>5</sup> Mommsen, *Geschichte des römischen Münzwesens* (1860), p. vi.

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of specie for purposes of payment and circulation, without departing from the specie basis. They are substitutes for money for certain purposes, without arrogating to themselves those functions of money which they are not capable of performing. They are substitutes for money as a circulating medium, not as a standard of value. They may serve as a symbol of value, but they cannot serve as a standard of value without assuming a function that is beyond their competency. It follows from their character as substitutes for money that they possess value only in virtue of the belief that they will be redeemed in specie, and only to the amount of the specie obtainable for them. They cease to be evidences of debt when it is attempted to erect them into money independent of a specie basis.

A distinction is accordingly to be made between paper money in the broad sense and paper money in the strict sense.

The former category comprises - to follow the usage of every day life - those substitutes for money that are employed in a well-ordered monetary system. Paper money - in the stricter sense comprises only such substitutes for money as attempt to supplant specie currency by force of legal enactment, by suspension of specie payments and the assigning of a legal tender quality to the paper, the paper in this way taking the place of coin as money.

It is this final step that is unsound. The idea is untenable that anything not possessed of intrinsic value can be made into money-paper can maintain its position in the monetary system only so long as the fact is not lost sight of that it is in origin and essential nature an evidence of debt; its function as circulating medium rests on its credit, and this credit is impaired by a suspension of specie payments. True paper money is therefore a degenerate credit money.

§ 550. That the value of paper money is an open question is shown by the unavoidable fluctuations in its value. These fluctuations may be masked for the time by certain legislative provisions, but in point of fact they can no more be avoided in the

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case of paper money than in that of debasement of the coin or substitution of the minor coins for standard coin. By suspension of the convertibility into coin the identity of value between paper and coin is brought to an end. In place of an identity we have a divergence in value between paper and specie, the extent of which is not to be determined beforehand. For, inasmuch as the paper has no intrinsic value, but acquires a value solely on the strength of a hope of its future redemption in specie, the question as to how far the value of the paper will depart from that of specie depends on the degree of confidence which exists as to its convertibility.

If the state's credit is exceptionally good and the period of suspension is a relatively short one, then it may happen, in a favorable case, that the divergence in value between paper and specie is inappreciable; such was the case in France during and immediately after the last war. But this happens only by rare exception. The most recent experiences with paper currency in Austria, Russia, and the United States have been much less favorable. Forced circulation and inconvertibility of the paper money, together with an enormous issue of the paper, the depreciation of which only affords occasion for a still greater issue, - all this has resulted in an extreme depreciation, with the secondary consequence of a great fluctuation of values.

The first requirement of any standard of measurement is that it must remain constant, so as to afford a reliable unit for the measure of other things. This requirement is binding on money as a measure of value. The thought given to the question of what is the best specie standard and the debate about the different possible standards (silver, gold, or double standard) turns, in the last analysis, on the question which of them answers most satisfactorily to this requirement of a fixity of value. It must be conceded at the outset that in the nature of things a paper currency does not meet this requirement. Paper can of course have no stability; it flutters in the wind of public opinion and expectation regarding its value relatively to specie. Paper also differs from a specie currency in this, that it is deprived

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of the support and regulation which the latter enjoys in the influx and withdrawal of the specie circulating in foreign countries; gold and silver have an international value, but that is not the case with a paper currency, which has no intrinsic value, and circulates only in virtue of the enactment and compulsion of the state in question.

§ 551. The historical data bearing on the employment of paper money and its mischievous effects may be found in sufficient abundance in the history of modern countries. It is of course a one-sided economic position to assert that we should "rather let the state perish than resort to forced circulation."<sup>1</sup> This view overlooks the fact that economic institutions are only means, and not the end of the national life. But apart from exaggerations of this sort, the testimony of history is well agreed that a paper-money régime is an abnormal condition of the political and industrial life of any nation, and that it is to be justified only as an expedient in the state's direst necessity, and is to be avoided by all means if it possibly can be avoided.

The most extravagant known example of a paper-money régime was that of the French Revolution.

As the regular sources of revenue failed and repeated exactions yielded a progressively slighter result, the successive governments of the Revolution found themselves all the more irresistibly pushed to a paper currency with forced circulation (assignats) as their last resort. Down to January 1, 1793, 3600 million francs had been put in circulation. The year 1793 doubled this amount, and the first half of 1794 added a further increment of 1000 millions. The assignats, which at the beginning of 1793 had stood at 61, declined from week to week in spite of all the penal enactments of the Terror until they reached 17 per cent., although every payment and every increase of price aggregating more than 500,000 francs was watched by spies and visited with the penalties of imprisonment and death. The Committee of Safety itself was obliged to violate its own law, in that

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<sup>1</sup> This expression marks the climax of the German free-trade school and of their Economic Congress (Hanover, 1864).

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it both paid prices for goods corresponding to the rapid depreciation of the assignats, and also obtained specie on the very most onerous conditions for use in its purchases abroad.<sup>1</sup> By the end of 14 May, 1795, the amount of paper money issued had risen to nearly ten milliards, and its value had declined to 7 per cent. The depreciation constantly led to further issues. By the end of August, 1795, there were 16 milliards in circulation, at a market value of 2 ½ per cent. Consequently anyone who had obtained a loan of 10,000 francs in 1790 would discharge it in the summer of 1795 by paying it in assignats of the same nominal value, but which could be bought for 250 francs in specie. A tenant who paid his rent in assignats would be able to discharge the annual rent of an entire estate with a single sack of corn.

The experience of Austria with its "bank bills" [*Bancozettein*] at the beginning of the nineteenth century was not much more gratifying. At every succeeding conclusion of peace there was an increasing amount in circulation: Campo-Formio, 150 million gulden; Luneville, 340 millions; Pressburg, 450 millions; Vienna, 860 millions. The value of the bank bills in December 1810, fell below 1200 paper gulden to 100 gulden in silver; and thenceforward fluctuated rapidly and violently by hundreds of points above and below that level.<sup>2</sup>

The continued growth of public credit, and the greater political stability and wealth which have been achieved in the course of the nineteenth century, have acted to diminish these extreme manifestations of the paper-money system. The fluctuations in the value of paper money as compared with specie in Austria, Russia and the United States during the last generation, have moved within a narrower range. During the years 1854-1855 the depreciation of the Austrian paper money amounted to 20-30 per cent., the very highest being 42 per cent.;<sup>3</sup> and at the same time the Russian paper money, originating from the same cause (the Crimean War), showed a considerably less depreciation,

<sup>1</sup> Von Sybel, *Geschichte der Revolutionszeit* (1877), vol. iii. pp. 175, 331, 407; Ramel, *Finances de la France en l'an IX*.

<sup>2</sup> Wagner, *Zeitschrift für die gesammte Staatswissenschaft*, 1861, p. 593

<sup>3</sup> Helferich, *Zeitschrift für die gesammte Staatswissenschaft*, 1856, p. 429.

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about 16 per cent., a phenomenon which has since recurred<sup>1</sup> with the recurrence of a war situation (1859, 1866, 1870, 1877); in Austria it has recurred twice, in 1859 and 1866.

But even when the depreciation and the fluctuations in the value of paper money are confined, as they latterly have been; within these relatively narrow limits, the results are still so dubious as to call for a closer consideration of the effects of a paper-money régime and the remedies for it.

§ 552. The fundamental fact in the fluctuation of the value of paper money (depreciation of paper, premium on specie; or discount is the loss of confidence in the nominal value of the paper which on its face is the equivalent of a specified amount of the specie previously in circulation. This loss of confidence occurs because specie payments are suspended under circumstances which afford ground for reasonable doubt as to the ability of the government issuing the paper money to redeem it in the future. The result is a divergence between the real value and the nominal value, based on the degree of probability of a future redemption, and also affected by the amount of paper money issued.

The legal fiction by which the government is apt to try to conceal this divergence, viz., the recognition of both specie and paper as equally competent means of payment, cannot prevent payments from being, in point of fact, made in the cheaper money. Paper money is offered to everyone who has a payment to receive, while specie is hoarded, is hidden away, or goes abroad, for it is only the international currency, specie; and not the national currency, paper money, that has any purchasing power in transactions between one country and another. The result is similar (only more strongly marked) to what occurs in the case of a double standard (vol. i. sec. 413) when, a preference is shown between two legally equivalent metals, or when the circulation is flooded with light-weight coin (debased, by intention or by inattention) or with the minor coins; the coin

<sup>1</sup>Wagner, *Die russische Papierwährung* (1868), p. 142.

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of full value is in such cases crowded out because the law authorizes payment in the cheaper coins,

The difference in degree of severity of these pathological phenomena in the case of an unhomogeneous metallic currency as contrasted with a mixed currency of paper and specie is due to the fact that the cheaper coins have stable intrinsic value, though less than that of the dearer, while the paper has no intrinsic value whatever. The result is that the divergence of the paper from the value of specie is potentially unlimited, its degree depending entirely on the degree of confidence with which it is regarded and the amount in circulation. Debased coin, or the cheaper metal in a double standard, possesses a norm in its own intrinsic value which fixes its purchasing power. Paper money has no such intrinsic stability, and consequently fluctuates in value back and forth.

The evil of which paper money is capable is therefore, as it were, a multiple of that wrought by a coin that is below standard. The latter inflicts damage but once and for a short time on those who have payments to receive, viz., during the interval while the facts about the base coin are penetrating into the popular knowledge and appreciation. With paper money this interval is an indefinite period, lasting as long as specie payments are suspended. Every shock to the public credit lowers the value of the paper; every fresh depreciation of the paper is an occasion to the government for fresh issues; and every fresh issue acts in the direction of a further decline.

§ 553. An absolutely unvarying standard of value is an unattainable ideal, even with the best possible provision for a metallic currency, because all valuable objects, including the precious metals, vary in intrinsic value, as the effect of general causes. But this difficulty is accentuated in an extreme degree in the case of a paper currency, because such a currency has no independent value whatever.

The shortcoming of even the most perfect standard of value lies in this, that it is compelled to assume as a fixed norm what



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is in the nature of things a variable; and the result of this imperfection, for the business of the community, is that all pecuniary relations, between private parties among themselves and between private parties and the state, have to proceed on the assumption of invariability in a basis which is essentially variable. All future payments due in virtue of a contract entered into today, for loans, rent, wages, salaries, etc., will consequently not represent just the same value when it falls due. This uncertainty is increased indefinitely under a régime of paper money. A sudden outbreak of war, even when the state in question is not a participant except as an interested third party, may cause a depreciation of the state's paper money to the extent of 20-30 per cent. (Russia in 1870); and recent loans negotiated for a short term will be found by the creditors on maturity to have shrunk by 20-30 per cent. in spite of their nominally unaltered amount.

The consequence is that the entire system of pecuniary relations and transactions is permeated with an element of risk. All monetary affairs are suspended in a shimmering atmosphere of advance and decline, so that everyone concerned in business becomes perforce a participant in a game of chance, in which he gains and loses with varying fortune. Even the expedient of making all contracts payable in specie is no protection against the evil. In the great proportion of cases one's interests are better protected against the fluctuations of paper money by making contracts in terms of paper. The reason for this is to be sought in the circumstances which go to neutralize the abruptness of the fluctuations of value, viz., the tardiness with which variations in discount are propagated from the great centers of business, of the foreign exchanges, the export and import trade, through the lesser ramifications of the business community into the affairs of everyday life. The case affords an illustration of the general principle that prices are not fixed with the precision observable in physical phenomena, their determination being effected through the instrumentality of less calculable human factors - customs, opinions, transactions. For a short term,

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therefore, the employment of the paper currency would in most cases afford a relatively greater security against fluctuations than the use of specie, as the point of importance to those who receive the payments would, after all, commonly lie in the relation of the payment to prices as expressed in terms of paper.

§ 554. An incidental effect of a paper currency is that it brings certain temporary benefits and gains to certain classes of the people, but only at the expense of the rest of the community. The chief case to be cited of this kind is the quasi-protective effect resulting from the fact that the discount on the paper money does not correspond precisely to the rise of domestic prices due to the use of the paper currency. As already pointed out, the discount which manifests itself so obviously in all business on a large scale translates itself but slowly into the prices of domestic products; all the more slowly the more remote the locality is from the great business centers, and the less highly developed the means of communication are. In such situations the prices fixed under a specie currency may maintain themselves for years under a paper-money régime.<sup>1</sup> The result is that those branches of business which are occupied with buying products in the remote country districts at the old price and selling them at the centers of trade at the new price, augmented by the discount on paper, enjoy an exceptional advantage. This advantage is obviously greatest in cases where the depreciation of paper is great and rapid, especially if it takes place by a sudden drop, to which the prices prevalent in remote districts are able to adjust themselves but slowly if at all. The resistance offered to a resumption of specie payments by the interests that have got used to the quasi-protective advantages secured them by the paper-money régime is to be explained on like grounds. The retention of the paper currency is demanded as a measure of protection (United States, Austria, etc.), and viewed in this light the demand is quite intelligible. The decline of the premium on specie brings a decline of the

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<sup>1</sup> Cf. Wagner, *Die russische Papierwährung* (1868), pp. 103 et seq.

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prices (in paper) of articles of export, and so makes them compare unfavorably with the prices of the same articles in the primary markets, which have been gradually advancing under the pressure of the premium. With a return to specie payments, therefore, the supply of products for export can be obtained only at a relative advance. What has been said of the export trade will be found to hold in much the same manner of the import of goods from abroad: As the premium advances import prices (in paper) advance, and the corresponding advance in retail prices can be effected only gradually. After this adjustment has once been effected, a resumption of specie payments will lower the import, price and so give foreign an advantage over domestic goods in the home market. This advantage will be more pronounced the more fully domestic prices have been adjusted to the premium during the régime of paper money.

The premium accordingly acts as an export bounty on the home products and as a protective tax against foreign competition. This protective feature of a paper currency has something in common with the measures of industrial policy employed (at times quite legitimately) with the same end in view. But there is in sundry respects a difference unfavorable to the paper currency. In the first place, a protective duty or an export bounty is placed where a deliberate canvass of the situation shows that it will be of advantage. A blindly accidental secondary effect, following undesignedly from financial distress, is not to be compared with such an intelligently constructed measure of protection, even if it does produce a result of the same general nature.

But in the second place, this circuitous way of reaching the desired end is altogether too unwieldy and costly; for it is always to be recognized that a paper-money system is very detrimental to the general economic interests of the community. If special advantages are to be afforded particular branches of industry by state interference, the direct method is cheaper and more effective.

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§ 555. The governments of the great states of today whenever they have become involved in a paper-money system, have, without exception, made efforts to clear themselves of it.

An instance of the greatest magnitude is that of the United States after the Civil War. The efforts of the kingdom of Italy have also been successful. Austria has (1889) for a long time been near accomplishing the same end, and has only been prevented from successfully solving the problem by its being complicated with the presence of a silver standard. Russia is the farthest in arrears, and the ill success of her monetary policy for a generation past is but a feature of the incongruity that exists between her financial development and her growth in political power; her position closely resembles that of the other European states in the seventeenth and eighteenth centuries.

The United States at the close of the Civil War had a debt of 2846 million dollars (August 31, 1865), 684 millions being paper money,<sup>1</sup> with funds in the treasury amounting to 88 millions. As early as December 3, 1866, Secretary McCulloch declared that specie payments could be resumed by July 1, 1868. He was filled with the conviction that a nation which adopts paper money as a standard of value "violates the financial laws of the universe" and will inevitably suffer for the offense. This expectation was not fulfilled. But by a vigorous redemption of the great war debt (some \$100,000,000 annually) a rapid approach to its accomplishment was made. The gold value of the paper money on an average for the year was, in 1865, 63 per cent.; in 1868, 71.6 per cent.; in 1869, 75.2 per cent.; in 1870, 87 per cent.; in 1871, 89.5 per cent.<sup>2</sup> During the succeeding years the value of the paper closely approached that of gold, and specie payment was resumed January 1, 1879. During the years 1865-87 the entire debt was reduced from 2846 millions to 1175 million dollars (July 1, 1887). Against the 630 millions of notes outstanding in 1887 there was specie in the treasury amounting to 482 million dollars.

<sup>1</sup> *Annual Report of Secretary of the Treasury* (McCulloch), November 30, 1867. Cf. *Report of the Secretary of the Treasury*, December 3, 1866.

<sup>2</sup> *Quarterly Report of the Chief of the Bureau of Statistics*, September 30, 1878.

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In Italy<sup>1</sup> forced circulation was introduced May 1, 1866. The paper money in circulation (notes of the National Bank, etc.) reached 940 million lire by the end of 1875. The premium on specie reached its maximum of 20 ½ per cent. the first year of the depreciation (during the war), and ranged during the years 1867-1879 between 10 and 15 per cent. Toward the close of 1880 the Italian government came forward with a proposition for the discontinuance of forced circulation, and the premium fell directly to a minimum of 2-1 per cent. (January and February, 1881).

The moderate premium which prevailed seems to have exerted but a slight influence on the course of prices and wages in the country; that is to say, the depreciation of the paper money was inconsiderable. The premium seems to have been little else than an expression of the depreciation of the paper relatively to gold, and to have had an influence mainly on foreign trade.

On September 30, 1880, the aggregate of legal-tender notes issued on account of the government and the banks amounted to 1665 million lire, while the gold and silver currency was 444 million lire.

The government's project, which was accepted by Parliament early in 1881, contemplated the negotiation of a loan of 644 million lire as a means to resumption; 400 millions of this loan, at least, to be made up of gold coin. By this means 600 million lire of paper was to be retired, while the remaining 340 million lire was to be retained in circulation (being first converted into national paper money, instead of its existing form of legal-tender bank notes) convertible on demand into gold or silver.

§ 556. The examples of America and Italy cited above show what is the accepted method of resumption in modern states.

The path which has been followed in the descent during a season of financial embarrassment is retraced in the reascent. The premium which has arisen under the influence of a forced circulation, an impaired national credit and an inflated paper cur-

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<sup>1</sup>W. Lexis, Conrad's *Jahrbücher*, 1881, N. F. vol. ii. pp. 520-541.

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rency, is gradually reduced as the influence of improved credit, the expectation of a speedy resumption and the reduction of the volume of paper money makes itself felt, until the normal level is reached, when paper and specie coincide.

This temperate procedure, in which the cure reverses the steps by which the disease was contracted and developed, best answers the requirements of equity for the course of prices throughout the great body of business activity. The premium does not penetrate current prices with mechanical precision, but rather breaks against the circumference of the business world and makes its way through the system slowly, partially and fragmentarily. It is therefore also not expedient to seize upon the quotation of the premium at any given point of time as the one by which to effect resumption, and then by a single drastic measure restore specie payments at this level.

This latter method (devaluation) can properly be resorted to only where there is a very serious depreciation of long standing, so that the entire system of pecuniary relations has become adjusted to the depreciated standard. If this rule is applied, it appears that the legitimate use of devaluation is essentially a thing of the past. A notable example is the reduction of bank bills in Austria in 1811 to one-fifth of their nominal value, and of the paper currency in 1820 to two-fifths. Likewise the reduction of the paper money of Russia in 1839 to two-sevenths of its nominal value, and the probable further reduction of the Russian paper money in the future; this has of late reached a depreciation of nearly one-half, and has suffered a premium of 35-40 per cent: since 1877.

A measure still more extreme than devaluation is that of simple national insolvency, where all attempt at rehabilitating the paper currency is abandoned (as, e.g., in the case of the assignats issued during the French Revolution. But this is a phenomenon of such an ultra-barbarous nature as places it without the pale of civilized public policy, though it is but the practical outcome of a seemingly inoffensive theory.

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