Effect of the War Economy on Financing Public Assistance*

THE WAR ECONOMY, which has greatly increased war production and at the same time has curtailed the production and sale of consumer commodities, should have a pronounced effect on State revenues and, therefore, on financing public assistance. The effect in individual States will depend on the tax sources used for these programs. Programs financed from income, inheritance, and other progressive taxes or from relatively stable revenues, such as general-property taxes, should not be affected adversely. Financing of these programs may even be more nearly adequate as employment and wage levels rise.[1] On the other hand, further curtailment in the production and sale of consumer goods may reduce State revenues from general and selective sales taxes. General sales-tax yields from rationed goods will be particularly affected, as will taxes on alcoholic beverages and gasoline. There are some indications, however, that reductions in revenues because of rationing may be offset by increased sales and prices of nonrationed goods.

Influence of the War Economy on General and Selective Sales Taxes

The first effect of accelerated production and rising prices under the defense program was a substantial increase in sales-tax collections. Total State tax collections in 1941 reached the unprecedented sum of $4.5 billion. As a result, many States accumulated surpluses and others reduced taxes.[2] Sales-tax collections, which represented a substantial part of the total, increased 11 percent from the fiscal year 1938–39 to 1939–40 and an additional 15 percent in 1940–41.[3]

There are indications, however, that such increases have not continued in 1942, when war needs have necessitated the sharp curtailment of nonmilitary production. Data for seven States on sales-tax collections in April 1942 show that increases over April 1941 averaged only 8 percent, in contrast to an 18-percent rise for the first 10 months of the fiscal year.[4] Further deceleration of the rise in such collections may result from

*Prepared in the Division of Operating Statistics and Analysis, Bureau of Public Assistance.

[1] Alabama, Arizona, and Nevada finance the old-age assistance program from the property tax; Connecticut finances old-age assistance and aid to the blind from the poll tax. The District of Columbia, Louisiana, Maryland, New York, South Carolina, Tennessee, and Wisconsin finance all programs, and Massachusetts finances aid to dependent children and aid to the blind, from general funds, of which more than nine-tenths are derived from taxes on income and/or on relatively stable bases such as property.

[2] See "How to Use State Surpluses," *State Government*, March 1942, p. 7; *Tax Administrators News*, January 1942.

[3] Federation of Tax Administrators, *State Sales Tax Collections in the War Economy*, Memorandum RM-212, Chicago, June 6, 1942, p. 1.

[4] Ibid, p. 2.

Table 1.—*States financing public assistance entirely from earmarked revenues: Proportion of State funds derived from specified source*

State	Program	Proportion of non-Federal funds provided by State[1]	Proportion of State funds derived from specified source[2]				
			Total	General-sales and use taxes	Gasoline taxes	Alcoholic-beverage taxes	All other
Arizona	Old-age assistance	100	100	----	----	----	[3]100
	Aid to dependent children, aid to the blind.	100	100	31	----	----	69
Arkansas	Old-age assistance, aid to dependent children, aid to the blind.	100	100	62	----	26	12
Colorado	Old-age assistance	100	100	68	----	31	1
	Aid to dependent children, aid to the blind.	50	100	76	----	24	([4])
Kansas	Old-age assistance	51					
	Aid to dependent children	33	100	100	----	----	----
	Aid to the blind	33					
Nebraska	Old-age assistance, aid to dependent children, aid to the blind.	100	100	----	50	31	19
Nevada	Old-age assistance	50	100	----	----	----	100
New Mexico	Old-age assistance, aid to dependent children, aid to the blind.	100	100	20	----	46	34
Oklahoma	Old-age assistance, aid to dependent children, aid to the blind.	100	100	100	----	----	----
Texas	Old-age assistance, aid to dependent children, aid to the blind.	100	100	----	([5])	([5])	([5])
Utah	Old-age assistance	70					
	Aid to dependent children	76	100	100	----	----	----
	Aid to the blind	72					

[1] Data from "Source of Funds Expended for Public Assistance, 1941," Social Security Board, Bureau of Public Assistance, Mar. 25, 1942, mimeographed release.
[2] Based on annual report of public assistance agency for 1941 (Arizona, Arkansas, Nebraska, New Mexico), for 1940 (Colorado), and biennial report for 1938–40 (Utah); *Handbook of Kansas Social Welfare Laws, December 1941* (Kansas); *Tax Systems of the World: 1940* (Oklahoma); and "Characteristics of State Plans—characteristics cards" (Nevada, Texas).
[3] Special levy on real property to cover estimate of agency.
[4] Less than 0.5 percent.
[5] "Omnibus Tax Bill," enacted in 1941, provides funds for public assistance and certain other State functions through a variety of taxes including gasoline sales, sale of automobiles, and luxuries.

several new factors in the war economy—the imposition of price ceilings, greater reduction of nonmilitary production, and stricter controls over installment buying.

Despite these factors, however, no immediate decrease in sales taxes is likely. "Balancing the imposition of price control and reductions in the supply of consumers durable goods on one hand, against expected moderate increases in the supply of food and other nondurable goods and the existence of record inventories, it may be predicted that general sales tax revenues will flatten out, but not slump, in the next several months. Collection experience will vary from State to State, depending on the relative importance of restricted foods in the tax base, but in general no quick decline seems likely." [5]

The extent to which the general-sales tax may be affected by curtailed production and rationing of automobiles, tires, and gasoline is indicated in part by the distribution of retail sales-tax revenues by class of commodity. In 1936, automotive commodities (including filling stations) represented 21 percent of the total; food, 32 percent; general merchandise, 27 percent; and other commodities, 20 percent.[6] These data indicate that, if sales of automotive commodities were cut to practically nothing, revenues might decrease as much as 20 percent. Offsetting probable declines in automotive sales, however, are recent increases in food sales, which will probably continue to expand.

Through 1941, tax receipts on both alcoholic beverages and gasoline also continued to increase.[7] However, many distilleries have been converted to war purposes, and States relying on taxes on distilled spirits may find their revenues falling off sharply when present inventories are exhausted. Gasoline taxes also should decrease sharply as rationing is extended.

Changes in General and Selective Sales-Tax Revenues

Many public assistance administrators have been particularly concerned about the effect that decreases in gasoline taxes may have on financing public assistance. These taxes, which probably will be seriously affected by rationing, are unimportant, however, both as a revenue specifically earmarked for financing the public assistance programs and as a revenue source of State general funds. Only Nebraska uses the gasoline tax as the major revenue earmarked for public assistance; in Texas this tax is one of several revenues so earmarked. Only Florida, New York, Ohio, and Pennsylvania derive part of their general funds from gasoline taxes.[8] In all other States, gasoline taxes are earmarked, principally for highways and, in a few instances, for education. It is doubtful that decreases in gasoline-tax yields will divert general funds from public assistance to highways, since highway construction is restricted by Federal war agencies and would tend to decrease, in any case, with rationing of automotive products. The effect of sharp decreases in revenues from gasoline taxes, therefore, will be confined to a few States which may have to find other sources of funds for the public assistance programs. It is interesting to note, however, that in Nebraska, the one State which earmarks the gasoline tax as the major revenue for public assistance, the State assistance director has stated that he thinks "the situation regarding assistance won't be any more crucial with gas rationing than it is now." The director pointed out that "liquor and beer taxes are yielding far more than normal this year . . . and during the first five months of 1942 replaced gasoline taxes as the biggest source of assistance income." [9]

Public assistance programs in 38 States [10] will be affected in varying degrees by changes in revenues from sales taxes. The importance of such changes depends on the proportion of funds for public assistance derived from sales-tax revenues [11] and the degree to which the funds are limited to such revenues by earmarking.

Sales-tax revenues account for half or more of

[5] Ibid, p. 6.

[6] Jacoby, Neil H., *Retail Sales Taxation*, Chicago, 1938, p. 230.

[7] U. S. Bureau of the Census, *State Tax Collections*, 1941, p. 15.

[8] See *Tax Systems*, Tax Research Foundation, Commerce Clearing House, 1940. In Florida, old-age assistance, aid to dependent children, and aid to the blind are financed primarily from earmarked revenues, so that the gasoline tax has a negligible influence on funds for these programs.

[9] *Journal*, Lincoln, Nebr., June 4, 1942.

[10] The other 11 States include the District of Columbia, Louisiana, Maryland, New York, South Carolina, Tennessee, and Wisconsin, in which all programs are financed from general funds, of which more than nine-tenths is derived from taxes on income and/or on property and other relatively stable bases; Nevada, where old-age assistance, the only program administered under a plan approved by the Social Security Board, is financed from the property tax; and Massachusetts, North Dakota, and Texas. Data are not available on the amount of public assistance funds derived from general-sales and alcoholic-beverage taxes for all programs in North Dakota and Texas and for old-age assistance in Massachusetts; aid to dependent children and aid to the blind in Massachusetts are financed from general funds, of which less than one-tenth is derived from general-sales and alcoholic-beverage taxes.

[11] Appropriations from the general fund for public assistance programs are assumed to have been derived from sales taxes in the same proportion as the total general fund is derived from this revenue source.

the State funds used for public assistance in 20 States. More than a third of these States finance each of their programs entirely from earmarked funds derived in major part from sales-tax revenues (table 1). Programs will be most directly affected, therefore, in these States, i. e., Arkansas, Colorado, Kansas, Nebraska, New Mexico, Oklahoma, and Utah. Three additional States—Alabama,[12] Florida,[13] and Oregon—finance programs from both earmarked and general funds, of which at least half is comprised of revenues from sales taxes (table 2). In these States, increases or decreases in sales-tax revenues may be balanced by changes in general-fund revenues and appropriations therefrom. The other 10[14] of the 20 States finance their programs entirely from the general fund (table 3); changes in revenues from sales taxes in this group of States may be compensated by changes in other revenue sources of the general fund.

In 18 additional States, sales taxes account for less than half although more than one-tenth of funds used for public assistance programs. Arizona [12] alone finances its programs entirely from earmarked funds (table 1), and only Connecticut, Iowa, and Maine use both earmarked and general funds.[15] Programs are financed entirely from general funds in the other 14 States.[16]

[12] Sales taxes are used for aid to dependent children and aid to the blind only; old-age assistance is financed from the property tax.

[13] Information is for aid to the blind only; data are not available on the amount of funds for old-age assistance and aid to dependent children derived from taxes on general sales and alcoholic beverages.

[14] California, Illinois, Indiana, Michigan, Missouri, Ohio, South Dakota, Washington, West Virginia, Wyoming.

[15] Information on sales taxes is for aid to dependent children only, in Connecticut; aid to the blind only, in Iowa; and aid to dependent children and aid to the blind, in Maine. In Connecticut, old-age assistance is financed from the poll tax, and aid to the blind, from other relatively stable revenues. Data are not available for Iowa and Maine on the amount of funds for old-age assistance derived from taxes on general sales and alcoholic beverages.

[16] Delaware, Georgia, Idaho, Kentucky, Minnesota, Mississippi, Montana, New Hampshire, New Jersey, North Carolina, Pennsylvania, Rhode Island, Vermont, Virginia.

Table 2.—*States financing public assistance from both earmarked and general revenues: Proportion of State funds derived from specified source*

State	Program	Proportion of non-Federal funds provided by State [1]	Proportion of State funds derived from specified earmarked source [2]: Total	General-sales and use taxes	Gasoline taxes	Alcoholic-beverage taxes	All other	General funds	Proportion of State general fund derived from specified source [3]: Total	General-sales and use taxes	Alcoholic-beverage taxes	Income taxes	Property taxes	All other
Alabama	Old-age assistance	57	100	-------	-------	(4)	100	(4)						
	Aid to dependent children	50	100	-------	-------	31	-------	69	100	31	14	12	20	23
	Aid to the blind	50	100	-------	-------	62	-------	38						
Connecticut	Old-age assistance, aid to the blind.	100	100	-------	-------	-------	78	22	100	-------	18	14	17	51
	Aid to dependent children	50	100	-------	-------	-------	-------	100						
Florida	Old-age assistance	100	100	-------	-------	(5)	(5)	(6)	-------	-------	-------	-------	-------	-------
	Aid to dependent children	100	100	-------	-------	(5)	(5)	(6)	100	-------	23	-------	13	64
	Aid to the blind	100	100	-------	-------	100	-------	(6)	-------	-------	-------	-------	-------	-------
Iowa	Old-age assistance	100	100	(5)	-------	-------	(5)	-------	-------	-------	-------	-------	-------	-------
	Aid to the blind	45	100	-------	-------	-------	-------	100	100	-------	25	-------	40	35
Maine	Old-age assistance	100	100	-------	-------	-------	(5)	(6)						
	Aid to dependent children	47	100	-------	-------	-------	-------	100	100	-------	28	-------	41	31
	Aid to the blind	100	100	-------	-------	-------	-------	100						
Massachusetts	Old-age assistance	67	100	-------	-------	(5)	(5)	(6)	100	-------	8	8	32	52
	Aid to dependent children	48	100	-------	-------	-------	-------	100						
	Aid to the blind	100												
North Dakota	Old-age assistance	85	100	(5)	-------	-------	(5)	(6)	100	-------	11	9	52	28
	Aid to dependent children	51	100	(5)	-------	-------	-------	(6)						
	Aid to the blind	100												
Oregon	Old-age assistance, aid to dependent children.	60	100	-------	-------	85	-------	15	100	-------	-------	64	-------	36
	Aid to the blind	61												

[1] Data from "Source of Funds Expended for Public Assistance, 1941," Social Security Board, Bureau of Public Assistance, Mar. 25, 1942, mimeographed release.

[2] Based on annual report of public assistance agency, 1941 (Alabama, Florida); "Characteristics of State plans—characteristics cards" (Connecticut—aid to dependent children; Maine—old-age assistance, aid to dependent children; Massachusetts—old-age assistance, aid to the blind; North Dakota, Oregon); *Tax Systems of the World, 1940;* and memorandum from Division of Finance and Economic Studies, Bureau of Research and Statistics (old-age assistance, Connecticut; aid to the blind, Florida); "Earmarking Tax Funds for Welfare Purposes," *Social Security Bulletin*, January 1940 (Iowa, Maine—aid to the blind, Massachusetts—aid to dependent children).

[3] Data for 1940 compiled by Division of Finance and Economic Studies, Bureau of Research and Statistics, Social Security Board.

[4] Less than 0.5 percent.

[5] Unknown.

[6] Deficits made up from general fund.

Table 3.—*States financing public assistance entirely from general revenues: Proportion of State funds derived from specified source*

State	Program	Proportion of non-Federal funds provided by State [1]	Proportion of State general fund derived from specified source [2]					
			Total	General-sales and use taxes	Alcoholic-beverage taxes	Income taxes	Property taxes	All other
California	Old-age assistance, aid to the blind Aid to dependent children	50 57	100	53	7	23	4	13
Delaware	Old-age assistance Aid to dependent children	100 50	100		18	40		42
District of Columbia	Old-age assistance, aid to dependent children, aid to the blind.	100	100		4	6	57	33
Georgia	Old-age assistance Aid to dependent children Aid to the blind	88 87 87	100		13	36	30	21
Idaho	Old-age assistance, aid to dependent children, aid to the blind.	100	100		16	24	37	23
Illinois	Old-age assistance, aid to dependent children	100	100	56	16		(3)	28
Indiana	Old-age assistance, aid to dependent children Aid to the blind	60 100	100	65	14		8	13
Kentucky	Old-age assistance	100	100	(3)	26	17	21	36
Louisiana	Old-age assistance, aid to dependent children, aid to the blind.	100	100		(3)		15	85
Maryland	Old-age assistance Aid to dependent children Aid to the blind	67 80 30	100		1	28	27	44
Michigan	Old-age assistance, aid to the blind Aid to dependent children	100 85	100	68	17		1	14
Minnesota	Old-age assistance Aid to dependent children Aid to the blind	67 39 100	100		16		37	47
Mississippi	Old-age assistance, aid to dependent children, aid to the blind.	100	100	37	4	10	14	35
Missouri	Old-age assistance, aid to dependent children	100	100	50	12	15	9	14
Montana	Old-age assistance Aid to dependent children Aid to the blind	68 70 69	100		42	12	26	20
New Hampshire	Old-age assistance Aid to dependent children, aid to the blind	50 100	100		29		14	57
New Jersey	Old-age assistance Aid to dependent children Aid to the blind	75 35	100		42			58
New York	Old-age assistance, aid to the blind Aid to dependent children	51 29	100	(3)	8	32	1	59
North Carolina	Old-age assistance Aid to dependent children Aid to the blind	55 53 51	100	31	6	30	5	28
Ohio	Old-age assistance Aid to dependent children Aid to the blind	100 43 33	100	39	26		7	28
Pennsylvania	Old-age assistance, aid to dependent children	100	100	(3)	19	14	13	54
Rhode Island	Old-age assistance, aid to the blind Aid to dependent children	100 59	100		37			[4] 63
South Carolina	Old-age assistance, aid to dependent children, aid to the blind.	100	100		1	22	9	68
South Dakota	Old-age assistance, aid to dependent children, aid to the blind.	100	100	37	20	(3)	13	30
Tennessee	Old-age assistance, aid to the blind Aid to dependent children	75 67	100		8	19	9	64
Vermont	Old-age assistance, aid to the blind Aid to dependent children	100 50	100		28	16		56
Virginia	Old-age assistance, aid to dependent children, aid to the blind.	62	100		28	18	10	44
Washington	Old-age assistance, aid to dependent children, aid to the blind.	100	100	39	18		11	32

See footnotes at end of table.

Table 3.—*States financing public assistance entirely from general revenues: Proportion of State funds derived from specified source*—Continued

State	Program	Proportion of non-Federal funds provided by State[1]	Proportion of State general fund derived from specified source[2]					
			Total	General-sales and use taxes	Alcoholic-beverage taxes	Income taxes	Property taxes	All other
West Virginia	Old-age assistance, aid to dependent children, aid to the blind.	100	100	59	12	5	3	21
Wisconsin	Old-age assistance, aid to the blind Aid to dependent children	61 52	100		9	35	20	36
Wyoming	Old-age assistance Aid to dependent children Aid to the blind	55 56 100	100	51	15		13	21

[1] Data from "Source of Funds Expended for Public Assistance, 1941," Social Security Board, Bureau of Public Assistance, Mar. 25, 1942, mimeographed release.
[2] Data for 1940 compiled by Division of Finance and Economic Studies, Bureau of Research and Statistics, Social Security Board.
[3] Less than 0.5 percent.
[4] Apparently includes part of gasoline tax which, according to *Tax Systems of the World: 1940* and *Supplement: 1941*, is earmarked for unemployment relief.

Under present trends in sales-tax collections, programs in all these States probably can be more nearly adequately financed than under pre-war conditions. If, as the war economy deepens, greater restrictions on the production of consumer commodities result in decreases in sales-tax revenues, these States may have to curtail their programs or find other sources to offset or take the place of decreased sales-tax collections. However, the present improved fiscal condition of the majority of States may mean that losses of revenue from sales taxes, if they occur, can be absorbed either from accumulated surpluses or from increased collections of other taxes.

Income taxes may provide an important source of State revenue during periods of increased business activity and employment. Income-tax yields should continue to increase with the rising volume of war production. Such increases, however, may be limited in several States which permit deductions for Federal income taxes from the State tax base. It is possible that States which do not levy income taxes may find it necessary to substitute them for sales taxation.