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TAX BASES IN LAND, HOUSE AND BUSINESS TAXES

FOREWORD

The land, house and business taxes are the principal ones of the taxes on products or real taxes and are the most important local taxes in all civilized countries today. They are also extensively adopted as national taxes. In Japan, the house tax is imposed only as a local tax. On the other hand, both land and business taxes are levied as national as well as local taxes, both occupying an important position in the tax system of the country. These taxes are ancient and their tax bases which have been contrived from time to time have always been the subject of discussion. Their tax bases have remained and still are the subject of much discussion even today. Recently, changes have been made as regards these taxes, but these changes cannot necessarily be thought to be desirable. Viewed from the actual tax system of our country, the land tax has its tax basis products-value

(Ertragswert). (It is expected that this will be changed to products-capacity or Ertragsfähigkeit.) The basis of the business tax is actual products, or rather actual revenue; whereas that of the house tax, which is a local tax, is products-capacity. One may object to the divergences in the tax bases; but it may be said that such divergences are exactly what are appropriate to the tax system. At any rate, a study of the propriety of these tax bases will be of much theoretical interest.

I. TAX BASIS OF THE LAND TAX

In modern times, external indications (for example, the area of lands) do not become an issue as a tax basis of the land tax. Either land products (Ertrag) or land value (Gemeiner Wert) must be chosen as the tax basis. But before comparing their respective merits and demerits, it is desirable to make a comparative study of their essences. I shall therefore first take up this study.

(1). Comparison of the essences of land products and land values.

(A). Manifold forms of land products. Manifold forms of land products have been chosen as tax bases in the past. A preliminary discussion of this point seems desirable.

(a). Actual land products—this is one form. It is a concrete and subjective product which one derives from the use of land, instead of being an objective and average product; it can be either gross revenue or net revenue. When it is net product, it can correspond with income in the income tax and also can be brought into harmony with net profit as the basis of the business tax. On the other hand, when it is gross product, it becomes harmonious with the tax basis of the class-2 income tax in our income tax system as well as with that of the capital interest tax. It is not impossible to make actual products the tax basis of the land tax. But it seems that actual products need not be the basis of a real tax. Moreover, serious inconveniences may arise from its

adoption as the tax basis, and may lead to intentional tax evasion, in some circumstances.

(b). *Products-capacity*—it may take this form. This also may be either gross product or net product. In our new tax bases, the gross product is adopted. As the basis of the tax on products, its adoption is permissible. It differs from an actual product in that an objective and average product is derived therefrom, after the personal and accidental elements have been eliminated. For example, the differences in the amount of products from the changes in the cultivators of land or the differences of crops in different years are eliminated. This elimination of personal and accidental elements is proper in the land tax.

(c). *Productsvalue*—This is the land value reduced from net product, or the intermediary between gross and net products by means of a proper interest rate. For instance, it may be a value equal to 25 times the foregoing objective and average product. Thus, this product is not an actual product but rather the one reduced from products-capacity, especially net products-capacity. If the rate of the interest from which the reduction is made is proper, the result will be the same as products-capacity.

(B). *Comparison between product and value.*

(a). *Similarities*—Here, by value is meant the ordinary value (market value). It is not an individual, concrete and actual value. It is not the value of the land actually bought or sold between individuals. It is the value which all will agree to be proper in the market. Thus, it does not contain any subjective element; it is the objective value of land. Suppose a piece of land is sold by a person to his relative comparatively cheaply; or again, suppose one has paid a comparatively high price for a piece of land because it perpetuates the fond memories of ones ancestors. All such personal elements are eliminated from consideration in arriving at the market value. But since such value is nothing but the real income reduced by means of the proper interest rate, the result will be the same as the products-value. And

so long as the products-value corresponds to the net products-capacity, the ordinary value of land may be said to be about the same as its products-capacity.

(b). Differences—However, the results cannot be the same. The ordinary value is not the same as the products-value; on the contrary, it is usual that the ordinary value (market value) is higher than the products-value. In the first place, whereas in the case of the products-value only tangible products are taken into consideration, in the case of the ordinary value consideration is given to all possible factors tangible, intangible and prospective, as well as to all elements that are accompanied by the operation of the law of supply and demand. (I shall dwell on this point more fully later). Secondly, although the interest rate coefficient used in the reduction of the products-value must vary in various places in the country and with the various pieces of land in the same locality (inasmuch as it is to be applied to tangible products), usually the same and uniform coefficient is used; for instance, it may be 25 times or 4 percent. In this respect, too, the products-value differs from the ordinary value. (True, if the tangible as well as intangible products are added together and made the basis of computation, then the same rate may be applied in all cases in the same locality. They need only differ in different localities).

(2). Comparative study of the merits and demerits of product and value.

(A). From Point of View of Justice in Taxation.

(a). Viewed from the element of value.

(i). The merits of the product system and the demerits of the value system.

a. Ability to pay as manifested by the ownership of a piece of land. This is revenue in the form of land rent. When the rent is economized, it is equal to the amount one would have to pay as rent. Thus, it may be either a natural revenue, or an amount equal to that revenue when the land is not used by the owner, or even when no one is allowed to use it by him. We can reasonably suppose the existence

of such a revenue, because there is actually such a revenue. But we cannot regard the ability to pay on the part of the owner of a piece of land as something more than this, or something other than this. One may object to the supposition of the existence of such a revenue when the owner of the land in question neither uses it himself nor lets others use it. But it is his own fault that he does not derive a revenue from his land. He has to blame himself for the failure to use the land or let others obtain a revenue from it; and we need not make an exemption on that account. Such exemption would result in the encouragement of tax evasion and in the disuse of land. When a piece of land is used by its owner and not rented out to anyone else, it may not be possible to specify unmistakably such a revenue among his other revenues. But such a revenue may be inferred by fiction. Its amount would be the same as the rent he would have received had he rented his land out to some one else. Equity can be secured only by such a method. And inasmuch as the rent is taken not as an actual amount but as an average and objective amount (products-capacity), then it may inevitably prove more or less than the actual amount of rent. However, such an apparent discrepancy is permissible in the case of the land tax as a real tax or a tax on products.

b. Thus, the adoption of a tangible product as the tax basis of the land tax may be regarded as corresponding to the actual capacity of the owner to pay. On the other hand, suppose elements other than the tangible product are taken into consideration. There will arise no serious problem while such elements are insignificantly small. But when they operate powerfully, and especially when they operate differently on different pieces of land, then the tax burden based upon them could be something radically different from that based upon the tangible product. This will obviously be an injustice when viewed from the actual capacity to pay, and in some cases would be well nigh intolerable for the taxpayer. Especially in the case of the arable lands around cities, the

market value basis may result in an unbearable tax burden for their owners; the adoption of a tangible product in such cases is highly desirable. Even supposing that the market value and in consequence an element other than the tangible product is taken into consideration, in the case of the lands around cities, either the value of the product is adopted solely or the intermedium between the products-value and the market value may be adopted as the basis of the land tax.

(ii). The merits of the value system and the demerits of the product system.

a. A closer enquiry will reveal that it is wrong to consider the tax-capacity of land from only tangible products, either actual, or average and objective, because its capacity involves much more complicated and divergeant elements. It must be noted that there are degrees of certainty in the productivity of land. Even when the same amount of tangible product is derived from two different lands, their values may be different. In some instances, productivity is said to be more certain than in other instances, so that the owner of such a land is satisfied with a smaller tangible product; he knows that his smaller product in the long run will be as good as some other pieces of lands whose productivity is not so certain though the size of their tangible products is larger. He derives an intangible benefit in addition to a tangible product because of the certainty of the production. To be more precise, there are differences in the productivities of different lands. To give an extreme case, there is much difference in the values of the lands lying in an earthquake belt and those lying outside of such a belt, although their productivity may be the same. Moreover, there is a difference in the degree of honour, rights and cravings associated with the ownership of land, according to different localities and ages. Even today, these social phenomena and sentiments are more closely associate with land than with any other forms of property; they also constitute intangible products. Some individuals may not attach im-

portance to these ; but so long as they are held important by the general public in a given community, they must be taken into consideration. Moreover, the general tendency is that the value of land is comparatively higher than other forms of property in view of the fact that its supply is limited, is more or less monopolised, and it must meet the ever-increasing demand, though its extent is not unlimited. People show greater reverence towards land and that means that land possesses another intangible value. Some small pieces of land are more preferred by people to other larger tracts of land, and in consequence their value is higher ; herein also is found another form of invisible value. Again, the pieces of land lying close to urban districts have the possibility of being used some day for residential purposes. Such pieces of land have greater productivity than mere farm land ; in fact their productivity is the same as the urban land actually used as building sites or residential lots : they thus have greater value than the farm lands. In addition to their tangible values, they also possess an intangible value. Furthermore, the value of land has always been on the increase. For this reason the owner of land expects this increase in the future and is quite satisfied though the value of it at present may not be great. This quality of land should also be taken into consideration in taxation. All of the foregoing qualities are not the same everywhere and it would be a difficult task to decide on each case in each locality. However, the fact remains that they all exercise some influence on the value of land. There is the possibility that because of all these elements, land yields less profits than other invested objects, and all these elements which are difficult to specify are found as an indivisible whole, unified and diffused and synthesized in the market value. There is no other natural basis by which the real products-capacity of land could be compared with those of other things.

b. Instead of adopting as tax basis the market value of land, if the tangible product or tangible products-capacity is adopted, there will be injustice in taxation, because all the

elements other than the tangible products are disregarded. True, reduction may be made by taking a due interest rate coefficient ; but this rate cannot be the same everywhere and therefore if it is arbitrarily fixed for all cases, a greater injustice will arise.

(b). Viewed from the psychology of the owner.

(i). The merits of the product system and the demerits of the value system. Some landowners in country districts do not care about commercial transactions in land ; their psychology is averse from the sale or purchase of land, and they prefer to derive revenue from ownership only. There are such landowners also in urban districts. For these persons, the land tax based upon the market value would be felt as an unjustifiably heavy burden and as being unfair. The product system would be fairer in such circumstances.

(ii). The merits of the value system and the demerits of the product system. The existence of this psychological factor cannot be denied. On the other hand, the fact remains that even such landowners hold their land because of its value and have a valuation of their landed property. Moreover, this fact is becoming more and more significant so that the taxation of land on the product system will be unjust. Thus, neither system can remain absolutely fair. We must, therefore, decide which method of valuation is more universally acted upon in actual practice. This would favour the value system, inasmuch as the latter method is acted upon almost everywhere in urban districts and to a considerable extent also in rural districts. However, the existence of some doubts cannot be lost sight of. I would rather apply the product system as an exception in the case of arable lands. The adoption of the value system with such an exception may be a moderate scheme.

(c). Viewed from relations with other taxes.

(i). The merits of the product system and the demerits of the value system.

a. If the land tax is to be levied as a tax on products

and on the same level with such other taxes as the house tax, the capital interest tax, and the business tax, we must take rent, or product or rather products-capacity as the basis of the land tax; such a tax basis would correspond to the value of rent in the case of the house tax, to the amount of interest in the case of the capital interest tax, and to net profit in the case of the business tax. True, strictly speaking, net profit in the business tax is not the same as the value of rent; but at any rate the difference is very slight. Moreover, the difference between them may be met by considering the rate of each tax. In the land tax, the value of rent may rather be held as a better basis. Even when the value system (the market value) is adopted as tax basis, the same result as in the product system may be obtained by adopting some proportion between the value of land and its rent, and by giving consideration to its tax rate. However, it would be all the more difficult to find any proportion because of the great difference that may, for example, exist between net product and value, especially when such a perplexing element as the interest rate coefficient enters into the problem.

b. Moreover, where a property tax exists, the market value may be taken as basis in both the property tax and the land tax. This may result in the frequent use of the same tax basis for the two taxes, and may encourage tax evasion. In such circumstances, it is desirable that in the case of the land tax, the product system should be adopted. However, this difficulty is not in question in this country.

(ii). The merits of the value system and the demerits of the product system. Where the land tax is a direct tax and the main direct tax, the product system may be justified. But where the income tax is the main tax and the land tax is regarded as a supplementary tax only, as in contemporary Japan, the imposition of the land tax according to the rent which stands near by income would give rise to evasion and omission in taxation, and would defeat its own end. The object in view may be more

adequately realized by adopting as the tax basis the value system.

(d). Studied from the point of view of improvement of the tax quality.

(i). The merits of the product system and the demerits of the value system. The product system may be adopted just as well when the land tax is intended as a tax on products and therefore as a real tax.

(ii). The merits of the value system and the demerits of the product system. Even supposing the land tax to be a real tax or a tax on products as well as a supplementary tax, an attempt should be made to include the personal element therein, so as to make it as consistent as possible with the taxpayer's capacity to pay. There is tendency to include in real taxes as much of the personal element as possible in the taxation systems everywhere in the world; the recent changes made in the business tax in Japan may be regarded as a manifestation of this tendency. Because of these reasons, the land tax may as well be based upon the value system, which will give to the land tax the element of a personal tax; moreover, consideration will be taken of debts and personal circumstances, while the application of progression could be made to a greater degree than under the product system.

(B). From Tax Technique.

(a). The merits of the product system and the demerits of the value system.

(i). Products may be actually found through the existing concrete rental contracts in an extensive area of land. But what is known as the existing value is largely an abstract thing. In very rare cases, it represents the latest value: in the majority of cases, however, it represents the value of land in the remote past. It is estimated by inferring from the past values and thus it is necessarily uncertain and dubious.

(ii). The market of the products of land exists more definitely and realistically than the market of land and can

be more easily estimated, although in cities the market of lands is becoming more definite. Moreover, the products of land does not constitute a problem in the case of urban lands.

(iii). It is possible to set a standard, in many localities, of the products of land, rent in particular; but it is difficult to find such a standard in case of the value of land for the simple reason that transactions in land take place rather infrequently, and the value is sometimes reached by inference from the products. Thus, from the standpoint of tax technique, the product system seems to be better than the value system.

(b). The merits of the value system and the demerits of the product system.

However, the market value has been showing much progress. Although it is far from being perfect, it has been making steady progress toward a very fair perfection. Where transactions in land take place frequently, it is possible to make an objective estimate that will appear rational to many persons, out of the actual cases, after special elements have been eliminated therefrom. Where such a process of valuation is difficult of accomplishment, the products-value may be reached by multiplying the product by some interest rate coefficient. This method of assessment may be substituted in such an exceptional case.

(C). From the State Financial Revenue.

(a). Viewed from the amount of revenue, the value system may be said to be superior to the product system inasmuch as it is based upon more numerous elements, and thus it has a greater possibility of increasing the amount of the state's revenue.

(b). Viewed from the degree of elasticity of taxation, the value system is better than the product system. The tax basis will increase with the progress of the times as well as with the increase in the expenditure of land administration. It will also be able to vary according to the variation in prices more adequately than does the product system. The

state revenue will also be elastic and will vary according to changes in the amount of national expenditure. On the other hand, it may be said in favor of the product system, especially of the products-capacity system, that the revenue under such a tax basis would be comparatively stationary; there will be little hope of increasing the amount of revenue, but there is also little possibility of a decrease in the amount.

(D). From the Viewpoint of Economic Policy and Social Policy.

(a). The merits of the value system and the demerits of the product system.

(i). Under the product system, it is impossible to impose a heavy tax on the land owned for speculative purposes and from which only a little or no revenue at all is derived. It will not be so under the value system. The lands utilized as gardens for wealthy citizen's residences may similarly be taxed heavily, and thus the use of lands for such luxurious purposes may be discouraged, whereas under the products system only a light tax can be imposed on such lands. The natural increment in the value of lands can also be more adequately taxed under the value system than under the products system, when viewed from the standpoint of social justice. Thus, the value system is more desirable from the point of view of social policy.

(ii). When the products-capacity or products-value of one's piece of land is taken as the basis of this tax, it is not objectionable; but when the actual products of the land are taken as such, one's personal endeavors are taxed and thus economic development is discouraged. There will be no such danger in the case of the value system which is based upon the average and objective value of land. Thus, from the point of view of economic policy, the value system is more desirable than the product system.

(b). The merits of the product system and the demerits of the value system. If actual products are taken as the basis of the land tax, those who derive no products need

not pay any tax. But under the value system, everybody will have to pay whether he derives any product from his land or not, and those who have no means to pay will be required to shoulder the tax burden. This may result in trespassing on their property principals. From this economic standpoint, the products system may be regarded as better than the value system. In actual practice the products system will mean either the products-capacity or the products value. If it is imposed even where there is no actual product, the system will amount to the value system. But the value system is liable to trespass on the property principals to a greater degree than does the products system inasmuch as the former also grasps elements other than the tangible one. But a deeper enquiry will reveal that even where a heavy tax is levied on a piece of land yielding but little or no revenue at all, its owner will be able to pay such a tax if he would only utilize the land properly. Even when he is unable to do this, he would be owning the land so long as he can maintain it for speculative purposes with the revenue he derives from some other sources, so that there is no reason for fearing injustice in taxation on that account.

(E). From Culture Policy and Health Preservation Policy.

Under the products system—whether according to actual product, products-ability, or the products-value—such things as gardens which are necessary for culture and the preservation of public health can be dealt with more liberally than by the value system. In this respect, the products system is better than the value system.

As I have endeavored to show, both systems have their respective merits and demerits, so that it is almost impossible to decide which is the better system. However, personally, I am inclined to give any vote to the value system as better than the product system.

II. TAX BASIS IN THE HOUSE TAX

(1). Various tax bases in the house tax.

There are the following three principal bases in the house tax: product, value and external indications. Each of these three bases has several varieties. For instance, product or rental value may take one of the following forms: actual net revenue (revenue from a house), actual gross revenue, and products-capacity (estimated house rent). The value of a house may be either building value or market value (Verkehrswert, Gemeiner Wert). External indications may be either the door and window tax, the tax on lots (tax on ground area or the tax on building area and lots attached to a building) or the class tax (various compositions of different external indications). Thus, the basis of the house tax may be chosen from a variety of items.

(2). Comparison between rental value and other tax bases.

Of the foregoing various tax bases, product, or, to be more specific, products-capacity, should be adopted by this country in all cases hereafter. Estimated gross products should be adopted and I am of the opinion that this would furnish a fitting system. One may urge that actual products be taken just as well. However, inasmuch as the house tax is intended as a tax on products or a real tax which is to be imposed side by side with the income tax and the surtax both of which are based on the net revenue, it is more desirable that it be based on some other tax basis, such as products-capacity. It is desirable that the various tax bases should be adopted so that one's capacity to pay is reached as perfectly as possible. I shall discuss the various tax bases with products-capacity as the centre.

(A). From justice in taxation.

(a). Estimated rental value. This would be the best conceivable basis for the taxes on products or real taxes, if it is known unmistakably, for it will then represent most

fairly the real capacity of the house owner. And if the land tax is also based upon rental value, a fair distribution of the tax burden between the land owner and the house owner would be assured. It is comparatively easy to grasp the rental value in urban districts where many houses are rented out. The assessment of the tax of a house which is not rented out may be inferred from the rental value. But in rural districts not many houses are rented out so that it is difficult to know the rental value. Moreover, even in urban districts, it would be difficult to grasp the rental value of factories, although it is comparatively easy to know their value. If rental value is adopted in these cases, there will necessarily be some injustice. Where it is impossible to ascertain at a glance the rental value of a house, it may be calculated by multiplying its value by some suitable interest rate coefficient or by adopting some external indication such as the tax on lots, the class tax, or the tax on value. The former method (where rental value is derived by multiplying the value of a house by some interest rate coefficient) amounts to the value system, while the latter is based upon bases other than rental value. Thus, taken as a whole, it would be impossible to find a unified tax basis throughout the entire country, and in consequence the system is bound to give rise to injustice in taxation. But it is adopted from other viewpoints, as comparatively good; wherever its application is impossible, the rental value must be calculated from the house value. In the rural districts in Japan, it is often observed that some people have their own houses in size or value out of proportion to their revenue, having inherited such big houses from their ancestors, so that the tax based upon the house rent would inevitably be over-burdensome to them. But such an evil is bound up with the house tax itself; it will not be eliminated no matter what tax basis is adopted, so long as the house tax remains in existence.

(b). Other tax bases.

(i). Actual net revenue. This is one way. If it is grasped adequately, the result will be equity. However,

the possibility of tax evasion is very great under this system. Inasmuch as the income tax and other personal taxes are based upon this system, its adoption in the case of the house tax will encourage further tax evasion. Thus, actual net revenue may be objected to from justice in taxation. One may argue that actual net revenue is more conducive to justice in taxation than is actual gross revenue, as it will be more in consistence with one's real ability to pay. However, in the case of such a real tax as the house tax, gross revenue or an intermediary between net revenue and gross revenue may be endurable. Moreover, actual revenue cannot cover the whole field. Those houses which do not yield an actual revenue must necessarily have a revenue inferred from an estimated rental value, and in so far they must depend upon the system of products-capacity.

(ii). The value of the house. This will enable the grasping of capacity which may be evaded under the products system. It can also follow the variation in capacity, and has a greater merit than the products system in playing the role of a supplemental tax to the income and other personal taxes that exist side by side with it.

It can be adopted for the houses in urban as well in rural districts, and thus a uniformity in the tax basis may be attained. In the case of houses, the failure of a correspondence between value and rent occurs less frequently than in the case of land. Of course, it is possible that an inequality of the tax burden in different parts of the country may result. Owners of houses in a locality where the interest rate is higher, and in consequence the revenue from their houses is higher, would have to pay comparatively a lighter tax than under the products system; whereas the owners of houses in a locality where the interest rate is lower and in consequence the revenue from their houses is lower, would have to shoulder a tax burden which will be heavier than under the products system. Another view will reveal the fact that the mere amount

of revenue will not be an adequate basis for ability to pay; the risks and difficulties one has to face in deriving revenue must be taken into consideration together with the value of the house, so that the tax may be more consistent with the house-owner's real ability. It may be said that when the house tax is based upon the value of a house, it ceases to remain a tax on products and becomes a partial property tax. But if the land tax which is levied along with the house tax is also based upon the value of land, it would be desirable to adopt the value system, so that a sort of harmony may exist between the two related taxes. But when rental value is adopted as the basis of the land tax as in our tentatively decided tax plan, then the adoption of house rent rather than house value would be more acceptable.

(iii). External indications. Justice to a certain degree may be maintained by adopting this method. Under this system, precision cannot be obtained and thus, when viewed from the standpoint of equity in taxation it is much inferior to the systems of products and value. Of the three external indications, the class tax which incorporates various external indications is more conducive to justice in taxation than either the door and window tax or the tax on lots. It is, however, inferior to either the products system or the value system. The tax on lots may be endurable where economy is simple and there is not much difference in the lives of different individuals as in rural communities; but it will prove intolerable where society is somewhat more complex and advanced. Nor does the door and window tax show any greater aptitude, so far as compatibility with the tax payer's ability to pay is concerned.

(B). From tax technique.

(a). Estimated rental value. This may be reached comparatively easily in urban districts. The rental value of an unrented house can be inferred from the rents of other houses. This is difficult in the case of big factories but not impossible. It is very difficult to reach the estimated rental

value in rural districts where there are only a few rented houses, the majority of the houses being used by the owners themselves. The number of rented houses is not usually sufficient in number to form an estimated rental value therefrom. An exception may be found in resorts and spas, but this does not affect the general proposition that it is very difficult to reach an estimated rental value in country districts. I have already dwelt on this point from the standpoint of justice in taxation.

(b). Other tax bases.

(i). Actual net revenue. As we have already pointed out, this is difficult to reach in tax technique.

(ii). Value. This is easier to be reached in tax technique than is actual net revenue, but more difficult than are external indications on which I shall dwell later. It is on the same level with the estimated rental value when considered from tax technique. However, it is better than the latter in so far that it may be adopted in rural districts as well as in cities, whereas as we have seen rental value is difficult to get at in rural districts.

(iii). External indications. They are easily reached in tax technique. This hardly needs any explanation.

(C). From state financial revenue.

(a). Estimated rental value. If this tax basis be adopted, the financial revenue of a state may be secured in considerable amount. Moreover, it may make the receipt of revenue more stable and constant than under the principle of taxing actual revenue. But when the period covered by the estimate is let stand too long at a time, it would be impossible to secure a natural increase in the revenue.

(b). Other tax bases.

(i). Actual net revenue. Under this system, natural increase may be great and thus the financial revenue of a state may be increased. But it may give rise to a financial deficit during a business depression.

(ii). Value. Revenue may be great under this system, and natural increase may be secured to a certain extent.

But when the period covered by the estimate is long, this increase would not be possible. On the other hand, this method secures the stability of the revenue, which is an obvious merit of the system.

(iii). External indications. The receipt of considerable revenue will be possible under this system, and natural increase can be also arranged for and in this latter respect it is better than other tax bases.

(D). From economic, social and hygienic considerations.

(a). Estimated rental value. So long as this system results in a heavier tax burden than under the actual rent, it will oppress the economy and industry of the taxpayer ; and inasmuch as the tax may be shifted to house tenants, it will menace their economic life which is already in a pitiable condition. However, it is possible that the estimated value may be lighter than the actual rental value and in consequence it may result in a cheaper tax burden upon taxpayer. The difficulty of the shifting of tax burdens is true more or less with all tax bases, and is not limited to this particular one. Moreover, this tax can be mitigated by abatement in favour of the houses of poor people. The objection may be made to the effect that this basis will encourage people to choose small houses which will prove harmful morally and hygienically to their occupants. Such an evil, however, is more or less bound up with all tax bases ; and we may say that we must be content with the system so long as it does not involve that hygienic inefficacy which is found in the door and window tax.

(b). Other tax bases.

(i). Actual net revenue. Under this system, the tax would not be so burdensome upon the bearer ; economic oppression can be limited to a minimum.

(ii). Value. The effects that will be obtained under this system will be substantially the same as that which was described under the estimated rental system.

(iii). External indications. It is possible that a measure of injustice will be seen under this system. Thus, it

may cause economic oppression and give rise to social difficulties. The imposition of the door and window tax may cause people to make their doors and windows as small as possible ; this undoubtedly will be harmful to their health.

The foregoing discussion has revealed the fact that the principle of taxing estimated rental value is not an ideal one and in a sense it may even be held as inferior to the principle of taxing value (current price). However, it possesses merits which make it a tolerable system. None of the tax bases seems to be predominantly superior to the others ; they are all, *ceteris paribus*, of the same intrinsic value.

(3). The substance of the estimated rental value.

Supposing the estimated rental value be adopted as the basis of the house tax, let us see what is the substance of this value.

(A). Relations with the actual value of rent.

The estimated rental value is a value arrived at objectively and by taking averages, and thus is not a real or actual value. This basis is an equitable one for real taxes or taxes on products. When a house is rented out, its owner is required to make a report thereon, and the report is taken into consideration but it is not adopted as a basis for the house tax. All special circumstances of the owner are excluded and the house rent is fixed as objectively equitable and proper. In the case of those houses which are occupied by their own owners, the rent is inferred from other similar houses which are rented out.

(B). Special method of estimating rental values in country districts. In the urban districts, the discovery of an objective rental value is easily made by taking the standard of averages. But in the country it is impossible and the only method is to calculate the rental value by multiplying the value of each house by some proper interest rate coefficient. That the rate is to be fixed arbitrarily and the adoption of a uniform rate, though conditions in different places are not

the same, will be held as being conducive to injustice. But so long as the principle of taxing rental value is adopted, such defects are unavoidable. It may be contended that for the country districts, the tax on lots or the product of the unit of a building lot and its accessory lands be taken as the tax basis (as in Bayern, and in Mecklenburg-Strelitz). But this method cannot escape the charge of inequality between the tax burdens of several places and between those of the rural and urban districts.

(C). Questions of calculation.

(a). Maintenance and depreciation expenses. Although their deduction may appear to be desirable from the standpoint of the faculty principle, they cannot be deducted under our law. It may be held as tolerable as a real tax or a tax on products and the deduction of these expenses would be very difficult of realization; their calculation would not be precise. Rather a lump sum should be taken and allowance be made in the rate of the tax. This allowance would prevent injustice to a certain extent. However, the maintenance and depreciation expenses are comparatively larger for the houses of the poor than for those of the rich, and for this reason non-deduction of these expenses may result in a comparatively larger burden on the poor, and in consequence may be held as unsocial.

(b). Ground rent. In actual life, the so-called house rent includes ground rent. But in this country the house-owner shoulders the land tax also, and therefore this ground rent should be deducted from the house rent in arriving at the proper house tax, which is imposed side by side with the land tax. The rental value in our house tax is the value of rent minus the ground rent, or the value for the use of the house plus the superficies. But the question remains as to whether this ground rent should be a concrete individual ground rent or an estimated ground rent. But inasmuch as the rental value of the house itself is an estimated value, the ground rent should be also an estimated value. On the one hand, the land tax is to be based upon the estimated

ground rent; on the other hand, in the case of the house tax, it should be based upon the total estimated rental value minus the estimated ground rent.

(c). Capital invested in houses. This need not be deducted from the house rent. One may argue that, if ground rent is deducted from the house rent, the money invested in the house should also be deducted. But so long as no capital interest tax is levied on the entire investment in houses, no deduction should be made of the capital invested. If such a deduction is made, there will remain no taxable object for the house tax. If, however, such a deduction is to be made, it should be limited to the loans which have been invested in the houses, and for which the lender has paid the capital interest tax on it. In the case of the house tax, this deduction should be limited in the technique of taxation to the interest which is paid for the loan for which the house is held as mortgage. Now, one may borrow money not necessarily for his house but for his other business interests or because of his domestic or personal reasons. But the deduction of interest in the case of the house tax should be limited only to that of the loans used for the house. But in actual practice this is difficult to distinguish, so that although desirable it will not be practicable. But in Japan, there is no capital interest tax among the local taxes on products that are levied side by side with the house tax, so that there is no need of deducting the interest whether it be of loans or of one's own capital.

III. TAX BASIS IN THE BUSINESS TAX

Thus, in both the land and house taxes, a certain tax basis should be chosen for each. But when it comes to the business tax, not a single tax basis is to be chosen exclusively; on the other hand, several different ones may be adopted side by side.

(1). The tax bases at issue and the methods of their combination. They are: actual products or rather revenue

and external indications. Either one of them must be adopted in all cases. As to the method of their combination, about one half of the total taxable amount is to be based upon net revenue or income, while the remainder should be based on external indications. In regard to the former portion, wherever the announcement of net revenue is regarded as reliable (as in those of corporations and banks which are required by law to publish their balance-sheets), net revenue or income is accepted as the tax basis. But where such announcement is not regarded as reliable (as in the case of individual businesses) the estimated net revenue is obtained by multiplying a pre-determined net profit coefficient on the total amount of revenue (total gross revenue, the amount of compensation, or the amount of contracts, etc.) on which taxpayers are asked to make a report. This estimated net revenue is to be adopted as tax basis. This estimated net revenue is not to be made by revenue officials' personal discretion as is done in Japan but should be legally prescribed so that it may be made without a shadow of doubt as to its legality. As to the external indications, the amount of capital (where this is not known the rent of the business building should be taken) and the amount of the salaries of employees (where this is impossible the number of employees) should be taken. When these two external indication are taken together, the former or real element as opposed to the personal element of the latter, should be given preponderance.

(2). Reasons for adopting the foregoing method.

(A). Underlying fundamental principle. There are the following underlying reasons for the joint adoption of the tax bases of net revenue and external indications.

(a). Factors common to both the national and local taxes.

(i). Where net revenue is recommended in principle.

a. From the faculty principle. It is required that taxation should be made according to men's faculty to pay. Especially in national taxes, the income tax is levied as the

central tax according to this principle with such supplementary taxes as the business and other taxes on property or products or the partial income tax, so that property income is taxed rather heavily. In this, the faculty represented by business is best shown by net revenue. Thus, the business tax is levied according to the amount of net revenue, progression being adopted in its rate. From the standpoint of the faculty principle, external indications cannot be satisfactory; they are likely to be unfair. At first sight, external indications may appear adequate for estimating the amount of net revenue, but in reality the nature of net revenue is more dependent upon men's faculties and outer changes than on external indications which do not directly correspond with net revenue.

b. From the policy of financial revenue. The adoption of external indications for the basis of the business tax may induce the law makers to make the rate as high as possible and this may prove a financial oppression for those who derive comparatively small profits. On the other hand, if the law makers should attempt to forestall such oppression by making the rate bearable, the result will be a financial deficit to the State. But if net revenue is adopted, those who derive a large profit will be able to shoulder their business tax, while those who get little profit will have to pay a correspondingly small tax on their business. All will be able to bear the tax even if its rate be comparatively high. For this reason, it would be easier to secure government revenue under the tax basis of net revenue than under that of external indications.

c. From economic policy. Whereas under the system of external indications, the business tax may prove oppressive for those whose business profit is small, there will be no such apprehension under the system of net revenue. This is clear from what has already been said above. When an external indication takes the form of gross revenue, it may happen that the tax oppresses a merchant who adopts the policy of selling his goods in large quantities at cheap

prices.

d. From social policy. The policy of selling goods in large quantities at cheap prices is one way of preventing the rise of prices and therefore is desirable from the standpoint of social policy. But if the business tax is based upon gross revenue and not on net revenue, it will discourage such a business policy and thus would be undesirable from the standpoint of social policy. If the amount of the salaries of employees is taken as the tax basis, it will tend to check the increase of pay; while the adoption of the number of employees as tax basis would make the business tax a sort of poll tax.

(ii). The necessity of adopting external indications side by side with the system of net revenue.

a. From tax technique. I have already explained that in principle net revenue should be preferred as tax basis to external indications. When considered from the standpoint of tax technique, external indications are easier of access than net revenue, so that the former is adopted side by side with the latter. But a closer enquiry will reveal the fact that not all of the external indications are easy to reach in the same degree. Such external indications as the gross proceeds of sales, the amount of capital or of salaries are more difficult to reach than the rental value of buildings or the number of employees. Moreover, some net incomes, notably those which are required by law to be published, are more accessible. The net revenue of some local business may be more easily found by local officials, although it is not required by law to be published. Thus, the system of net revenue as tax basis may profitably be used. If net revenue only is adopted, there will be the danger of tax evasion even among some of those whose revenues are required to be published by law. This danger is all the more pronounced in the case of corporations whose officials are composed of members of the same family; they are more liable to resort to tax evasion by some dishonest method, even though they are required to publish their accounts, which they may

secretly tamper with. For instance, an attempt may be made for tax evasion by paying some members of the same family unnecessarily high salaries and compensations thereby reducing the company's net revenue. In order to prevent such dishonest practices, the adoption of external indications side by side with net revenue is advisable. This is all the more desirable in the case of an individual business whose net revenue is difficult to discover.

b. From the faculty principle. From this standpoint external indications are inferior to net revenue in principle. But considered from tax technique, this is not necessarily so, for the fact that tax evasion is discouraged more under the system of external indications than under that of net revenue may be taken as showing that the former is quite consistent with the faculty principle. Moreover, external indications help the apprehension of the net revenue, so that they may roughly correspond to justice in taxation. Thus, the system of external indications may be desirably adopted as a supplement to that of net revenue, though it by itself cannot be adequate.

c. From the states financial revenue. The revenue of a state is more stable under the system of external indications than under that of net revenue. The net revenue of business is changeable and thus the tax based upon this changeable source is ipso facto unstable. But external indications are less changeable than net revenue.

d. From economic policy. Under the system of net revenue, the revenue officials may light upon business secrets and this will cause unpleasant feelings to the taxpayers in the course of the collection of the tax. This may be regarded as interference in business. No such fear exists in the case of external indications.

e. From the nature of the tax. If the business tax is based solely on net revenue, it will lose its objectivity, will become a partial income tax, and may double with the existing income tax. It is desirable for the basis of the business tax which is to be imposed in co-ordination with the income tax that something other than income such as

external indications should be adopted.

(b). Matters that the business tax should consider as a local tax.

(i). External indications are indispensable.

a. Necessity of including the benefit principle. It is necessary that local taxes should include the benefit principle in addition to the faculty principle. Business receives some special benefits from the government of the locality in which it is situated. When some business exists in a given locality, it receives the benefits of the roads over which its materials and manufactured goods are conveyed; is protected by the fire guards of that locality; and its employees receive the benefits of its educational facilities, relief work, police and health institutions. For these services and facilities, the local government spends money. The degrees of benefit the various businesses receive in localities are not equal, but all receive some benefit. In consequence, the basis of the business tax should be decided with an eye on the amount of compensation due for such services and benefits. Not only where net revenue is difficult to perceive but also where it is easily discernible, external indications should be partly used in the business tax. Whether a business has received any net revenue or not, and disregarding the amount of such revenue if any, it ought to pay some tax according to some external indications, so long as it has received some benefit from, or caused some expense to, the locality in which it is situated. It would be unfair not to pay the tax on the ground that no net revenue has been gained. When considered only from the faculty principle, the imposition of the tax where there is no net revenue would be held as unjust. But when considered from the benefit principle, the failure to impose the tax would be unjust.

One may say that since the benefit principle is to be applied as a supplementary principle, it need not be treated as important. However, I am in favor of dividing the importance equally between the two bases, because as I have pointed out above, net revenue is not sufficient even when

the tax is considered only from the faculty principle and it is desirable to adopt external indications as a supplement from the standpoint of tax technique. On the other hand, it may be said that if a business receives benefits from the locality in which it operates, the locality also receives benefits from the business. Because of the existence of the business, the locality prospers, its people are given work, other businesses in the locality are expanded and increased, and the values of land and houses there are increased. It may appear that there is no need of any compensation for the benefits received by the business from the locality as the benefits of the two are cancelled against each other. However, generally speaking, businesses are located at certain places not because of the wishes of the localities, but for the convenience of the enterprisers. True, there are some towns or cities that invite enterprisers to establish their business there. But such towns or cities usually give some compensation at the initial stage, and various conveniences are given to the owner of a business when the benefit from it to the town or city is realized by its officials. Usually some allowance is made in the tax on such an enterprise. Thus, the benefits a locality receives from an enterprise is amply compensated for. When the benefits an enterprise receives from the government of the town in which it is located exceeds this compensation, the tax levied on the enterprise must give special consideration to the benefits.

b. Convenience in local discrimination. In the case of a national tax, difference in the location of revenue does not constitute a problem. (Here I am not concerned with international taxation). But in the case of local taxes, discrimination must be made so far as they are concerned with that locality. But this discrimination is difficult to be made under the system of net revenue. It may be more easily made under the system of external indications. Thus, this latter system has a merit when considered from the point of view of local taxes.

(ii). Net revenue should also be used. It has been

argued that considered from the standpoint of tax technique, net revenue cannot be easily discoverable. On the other hand, it may be said that local governmental bodies are so closely associated with the people that it is comparatively easy for them to find the net revenue of the latter. Thus, this tax basis may be used in the case of the local special taxes. Its adoption as the basis of a surtax may enable the state to reach the sources of taxes with comparative certainty.

(B). Reasons for fixing details.

(a). When net revenue is adopted. When net revenue is not discoverable, it is imperative from the standpoint of tax technique that it should be estimated by applying a net revenue coefficient. But this is to be fixed by law and executed openly and in the full view of all, and not to be made arbitrarily at the discretion of revenue officials.

(b). When external indications are adopted.

(i). The joint adoption of personal and real elements is desirable. By attaching a greater importance to the real element than to the personal element, a heavy tax on property income can become possible. The adoption of the real element only may seem to result in a heavy tax on property revenue, but business includes both real and personal elements. Moreover, the degree of the proportions between the two is not the same for all cases, and for this reason the adoption of the two tax bases is highly desirable. This is advisable from the standpoint of the benefit principle, also.

(ii). Such personal and real elements as the number of employees in business establishments, the rental value of buildings, are easily discoverable from the standpoint of tax technique. The fact that business enterprise receives benefits from the locality in which it is situated, thereby necessitating compensation, will make the adoption of these tax bases desirable as well as appropriate. However, when the tax basis is regarded as a means of discovering net revenue, it may be said that the amount of salaries in the

case of the personal element is better than other personal elements, and that the amount of capital is similarly better in the case of real elements. In the case of corporations, banks, and industries in which these two elements are easily discoverable, they should be adopted as tax bases.

(c). Apportionment of tax rates.

(i). Tax rates should be so apportioned that the revenue from the taxation of net revenue will equal that from the taxation of external indications. In the case of external indications, the tax rate on personal elements should be made lighter than that on real elements.

(ii). Strictly speaking, it is not fair to discriminate between corporations and individuals in the matters of tax rates. It may be said that lighter rates should be imposed on individuals for whom it is easier to evade taxes than on corporations, so that the former would be encouraged to make more truthful reports on their incomes. But since this argument is based upon the supposition of tax evasion, such a tax differentiation is not desirable. It is again contended that individuals should be allowed lower rates than corporations because the deduction of the business expenses of individuals is not so adequate as in the case of corporations. This does not justify such a discrimination. If such an inadequacy is a fact, the equality of the estimate of business expenses should be established, so that there will remain no injustice from such a fact. All these arguments in favor of discrimination for the benefit of individuals cannot stand on their legs. We may, however, find justification in a discrimination in favor of individuals over corporations in the following argument: capitalistic bodies may be taxed more heavily than individuals, and since corporations are capitalistic bodies they may be taxed more heavily. Moreover, the tax on corporations falls indirectly on their members, and consequently heavier tax is more feasible than in the case of individuals on whom the taxes fall directly.

CONCLUSION

I shall now summarise what I have set forth above.

1. Both products and value have their respective theoretical merits as the basis of the land tax. However, I am inclined to believe that the taxation on the value of land is more consistent with justice in taxation and is more desirable when considered from the standpoints of state revenue, economic policy and social policy. It seems that the difficulty involved in tax technique has been more and more removed, making the taxation of land value more practicable than before. I would adopt land value in principle at least, and to a certain extent the products-value as an exceptional and temporary measure during the present transitory period.

2. Of the three tax bases of products, value and external indications for the house tax, the first named, especially in the form of products-capacity, seems to be the best, although each of them has its respective merits. The adoption of this tax basis is difficult in the rural districts where houses are not rented out in any number, in which case it would be necessary to find the products-capacity of each house by means of an interest rate coefficient. So long as the land tax is levied on the ground on which a house stands, the ground rent must be deducted from the so-called house rent in order to derive the revenue which is to be the basis of the house tax. The maintenance and depreciation expenses need not be deducted from the house rent; an arrangement to the same effect may be made in the rates of the house tax. The interest on the capital invested in a house should not be deducted, provided there is no capital interest tax levied.

3. In view of the respective merits and demerits of net revenue and external indications, and considering the benefit principle in the case of local taxes, it is desirable that both should be adopted side by side as the bases of the business tax, instead of adopting either of the two to the exclusion of

the other. And where net revenue is adopted, individual businesses should be required to make reports of the amounts of their gross revenues (gross sale, the amount of remunerations, or the amount of contracts) and an estimated net revenue should be discovered by applying a prescribed net profit coefficient. The net revenue thus calculated should be taken as the basis of the tax. In the case of external indications, the personal and real elements should be jointly adopted. In the former case, the amount of the salaries of employees should be taken whenever it is discoverable; when this is impossible, the number of employees should be taken. In the case of the latter (real elements), the amount of capital invested should be taken whenever possible; but if this is impossible, the rental value of buildings should be taken. Of these two elements, the personal elements should be more lightly taxed than the other.

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