

# DELAWARE STATE FINANCE: THE POST-WAR RECORD

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## 1. *Introduction*

EARLY IN 1955 Governor J. Caleb Boggs appointed an advisory committee on educational needs in Delaware.<sup>1</sup> The purpose of the committee was to prepare for the White House Conference on Education to be held in the late autumn of 1955. Incidental to the committee's main function, however, was the highlighting of a need for strengthening the state's revenue system. That a study of the education needs of Delaware should lead one into a serious consideration of state finances should come as no surprise. In the fiscal year ended June 30, 1954, for example, outlay on education accounted for about 48 per cent of state expenditures for general functions, as reported by the Census Bureau.<sup>2</sup>

A subcommittee of the Governor's Advisory Committee (designated as Group 6 and chaired by Dr. John A. Perkins, of the University of Delaware) received the assignment of studying financial requirements of education. Early in their investigation Group 6 members were faced with a policy decision: should the financial requirements of education be considered in detachment, or should they be considered only as a part of the entire picture of state finances? The decision was in favor of the latter course as the more realistic of the two alternatives.<sup>3</sup> The report of Group 6 was thus not only a survey of the financial requirements of an adequate education program in Delaware, but also an interesting commentary

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<sup>1</sup> The full name of the committee was the Governor's Citizens Advisory Committee for Study of Needs and Problems of Education. Hereafter, the shortened form "Governor's Advisory Committee" will be used.

<sup>2</sup> Bureau of the Census, *Compendium of State Government Finances in 1954* (Washington 1955), p. 26.

<sup>3</sup> This decision presented certain difficulties since it meant assembling data and making projections not only for education costs, but also for costs of other state functions. For this purpose, Group 6 relied on data contained in the 1954 McKinsey study, although these data are not entirely satisfactory.

on the public finance of the state.<sup>4</sup> However, the report made no particular claim to originality. For some time it has been apparent to many people that things are happening in Delaware which are making the state revenue system inadequate.

In 1953 Governor Boggs appointed a Committee on Revenue and Taxation under the chairmanship of Mr. George Edmonds.<sup>5</sup> The committee members were requested to present their findings on necessary additional revenue. Such findings were to be used by the Governor in recommending new tax legislation to the 117th General Assembly. As a result, the General Assembly increased personal income, liquor, tobacco, pari-mutuel, and insurance taxes, as well as certain licenses. The 1953 measures did bring the fiscal 1954 general fund budget into balance, after substantial deficits in fiscal 1952 and 1953. They did not, however, check the rise in the state debt attributable to capital outlay requirements. In the summer of 1954, the management consultant firm of McKinsey and Company undertook a survey of state revenues and expenditures, with projections through fiscal 1960. The result of this survey was a set of findings as to possible additional sources of revenue. These findings are contained in a report entitled "Fiscal Affairs in Delaware" issued in November 1954.

In 1954 also, Public Administration Service made a survey of accounting and related fiscal practices in the state government. In the same year, Dr. John A. Perkins, aided by Professor Paul Dolan, investigated the matter of a central purchasing agency for the state and reported their findings to the Governor. As has already been pointed out, the Governor's Advisory Committee contributed its findings in 1955.

Thus, it is evident that state finance in Delaware has been examined from two points of view: increasing revenues to meet the growing and more costly responsibilities of state government, and seeking more efficient administration with a view toward reducing

<sup>4</sup> The report of Group 6 entitled "Financing an Adequate Program of Education in Delaware" was completed in May 1955 and submitted to the parent Governor's Advisory Committee. Group 6 members were Dr. John A. Perkins, Chairman; Mr. Walter S. Carpenter, Jr.; and Mr. James H. Snowden. Associated with Group 6 as consultants and staff members were Mr. Ira J. Ellis and Mr. Edward R. Caffrey, Du Pont Company economists, and Professors Herbert Newman and Matthew Pillard from the University of Delaware Faculty.

<sup>5</sup> This committee did not publish a report. Its recommendations were made directly to Governor Boggs. Minutes of the full committee were kept by Mrs. Lillian I. Martin, who served as secretary.

the "housekeeping costs" of state government. The emphasis in this paper is on the first point of view. This is not to deny the importance of good administration and the necessity for improving organization and procedures. However, as the subsequent pages should show, the Delaware problem is more than one of administrative detail. Rather, it is one of meeting growing responsibilities in a state whose economic and social structure is becoming more complex.

It is the purpose of this paper to provide background information, rather than to make recommendations for changes in the Delaware revenue system. It is believed that a review of the post-war decade (1945-1955) will put the state's revenue problem in proper perspective and thereby aid in arriving at sounder solutions to its fiscal requirements. It is apparent from recent studies, to which reference has been made, that there is a general awareness of revenue inadequacy. The full extent of this inadequacy can only be ascertained by reviewing just what has occurred since the end of World War II.

## 2. *Factors Affecting the Financial Needs of Delaware*

In considering the financial needs of state government in Delaware, there are certain factors (favorable and unfavorable) which should be kept in mind.

a. *Population Growth.* In the first place, Delaware is a state which has a rather rapidly growing population. Between 1940 and 1950, the state's population increased from 267,000 to 318,000, or somewhat more than 19 per cent. The national increase was about 14½ per cent.<sup>6</sup> Group 1 of the Governor's Advisory Committee made the estimates contained in Table I for the decade 1955-1965. Regarding the distribution of population by counties, the Group 1 report states:

It will be noted . . . that no appreciable growth is forecast for the Wilmington area. New Castle County exclusive of Wilmington will increase from 145,400 at present to 230,400 population by 1965 or an increase in population of 58%. Kent County will increase from 45,200 to 63,000 or 39%, and Sussex County will increase from 73,400 to 102,200 or 39%. We are less certain of specific county populations than the state as a whole but are relatively sure that the least growth will be in

<sup>6</sup> *Statistical Abstract of the United States* (1954 edition), p. 19.

Wilmington and the most growth in New Castle County. However, some time in the future as New Castle County approaches saturation, as Wilmington already has, Kent and Sussex Counties will share the major increase in population growth.

TABLE I

POPULATION FORECAST FOR THE STATE OF DELAWARE, BY COUNTIES,  
SELECTED YEARS 1950-1965

Year	New Castle	Kent	Sussex	Total
1950	218,900	37,900	61,300	318,100
1955	258,400	45,200	73,400	377,000
1960	299,500	53,500	87,500	440,500
1965	348,400	63,000	102,200	508,600

Source: Governor's Advisory Committee, Report of Group 1.

The rate of growth estimated for the state as a whole during the decade 1955-1965 is about 34 per cent, which is in excess of the estimates for the country as a whole. The Census Bureau, for example, in one projection used by the staff of the Joint Congressional Committee on the Economic Report estimated an increase in United States population from 165 million to 190 million.<sup>7</sup> This would be an increase of about 9 per cent.

The Group 1 report points out that for a twenty-year period prior to 1937, Delaware school population was about constant. Since 1937, however, the number of births has increased at a rate of about 300 per year, so that the number of births now is more than twice the number in 1937. Furthermore, it is expected that this increase (at the rate of 300 per year) will continue. By the school year 1964-1965, public school enrollment is expected to be double what it was in the year 1949-1950. The members of Group 1, in their report, were thus led to observe that "the basic problem facing education in Delaware is that of sheer numbers." Nor is the "sheer numbers" problem confined to the public school system. In the decade 1955-1965, the enrollment in the state's institutions of higher education is expected to grow from approximately 2,100 to 3,800 undergraduates.

The effect of such population growth upon education require-

<sup>7</sup> Staff of the Joint Committee on the Economic Report, *Potential Economic Growth of the United States during the Next Decade*, 83rd Congress, 2nd Session (Washington 1954), p. 35.

ments is fairly obvious. Not so obvious, perhaps, are the effects upon other aspects of government. As more people inhabit a given area, their needs for governmental services are likely to increase more rapidly than their own number. Greater concentration of population brings new problems of traffic control, health, recreation facilities, etc., in addition to greater needs of education.

As indicated in Table I, population growth in New Castle County (outside Wilmington) will be at a more rapid rate than in the two lower counties during the next decade. In one respect this may be unfortunate, since it may tend to widen the conflict in interests and point of view that is supposed to exist between the two sections of the state. This, with a legislative apportionment that favors the lower counties, may lead to a neglect of the urbanized area's needs.

One possibly unwanted effect stemming from legislative neglect of more densely populated and socially complex areas in a state is the tendency of such areas to look to the Federal Government for more of the services and controls which they desire. These areas may find that the Congress is more representative of their needs and points of view than their own legislative bodies in state capitals.<sup>8</sup> Otherwise the states themselves must assume more financial responsibility (or empower their local units to do so) for the increased needs of any section of a state affected by significant economic growth. Delaware will be no exception to this requirement. This may not actually require legislative reapportionment, but it does suggest the absence of any regional schism in the legislative body of the state.

b. *Delaware is a Small State.* Because Delaware is a small state, it is probably more costly per person or per unit of service rendered to maintain a full complement of services than for, say, adjacent New Jersey or Pennsylvania.

Actual comparisons here are difficult, if not impossible, because the kinds and quality of services are not necessarily identical in Delaware and nearby states. However, it seems likely that the state government is affected by the problems of a relatively small constituency in much the same way as is the University of Delaware, where the problem is well known to University administrators.

As the population of the state grows over the next decade, the

<sup>8</sup> The Commission on Intergovernmental Relations, *A Report to the President for Transmittal to the Congress* (June 1955), p. 40.

"overhead cost" problem may be reduced somewhat. Also, the problem may not be so serious for the state as it could be due to the fact that there is greater degree of concentration of government activity in the state government than is true in most other states.<sup>9</sup>

c. *State Government is More Important in Delaware Than in Most States.* One test of the relative importance of state and local government is to be found in employment and payroll data. The Census Bureau has provided such data, using October 1953 as its test month.<sup>10</sup> For the nation as a whole, 24 per cent of total state and local employes (full-time equivalent number, including school teachers) worked for state governments. In Delaware, on the other hand, 54 per cent of such employes were state government workers. On the basis of payrolls, rather than the number of employes, the distribution was about the same.<sup>11</sup> In other words, on the basis of employes and payrolls, state government in Delaware is twice as important, as compared with local government, as in the nation as a whole.

Another test is the relative importance of state and local taxation. This point is developed in 2c below. However, it can be stated here that on the basis of this approach, too, Delaware state government bulks large in relation to the local units.

Two functions of government which in many states are divided between state and local governments are, in Delaware, concentrated in the state government. These two functions are highways and education. In the case of the former, the highway network of Delaware is strictly a state undertaking, county participation in this function having been terminated in 1935. In the case of education, the extent of concentration is not as marked as it is in highways. However, some idea of the state's role can be had from the fact that in the year ended in June 1954, 89 per cent of the operating cost of the public school system was covered by state funds. Only 9.5 per cent came from local sources, and the remaining 1.5 per cent represented federal funds.<sup>12</sup>

Naturally, where state government looms so large (relatively speaking), the cost will seem high. This has one unfortunate aspect,

<sup>9</sup> This point is discussed further in 2c below.

<sup>10</sup> Bureau of the Census, *State Distribution of Public Employment in 1953* (Washington 1954).

<sup>11</sup> *Ibid.*, p. 17.

<sup>12</sup> Report of Group 6, Governor's Advisory Committee (May 1955), p. 3.

in that it is likely to create an added obstacle of public resistance when it becomes necessary to elicit public support for still larger state revenues. People are likely to point to the seeming high cost of state government, without at the same time realizing that local government costs and taxes are much lower than they would otherwise be if Delaware were nearer the average for the nation as a whole in the state-local balancing of functions. Viewed in this light, for example, the fact that Delaware has the highest per capita state debt in the nation is perhaps not quite so alarming as some residents of the state seem to think.<sup>13</sup>

From an administrative standpoint, concentration of activities such as education and highways in state agencies may make for greater efficiency in a small state such as Delaware. As pointed out in 2b above, Delaware, because of its size and population, is probably an expensive state for providing a full complement of government services. In fact, from an administrative standpoint, one might be able to make a fairly good case for the abolition of all local government in the state, leaving everything other than federal matters to the state regime.

d. *Delaware Is a High-Income State.* Delawareans are accustomed by now to being reminded that their state has the highest or close to the highest per capita income in the nation. To repeat the fact here may seem unnecessary, but the income picture is important in any discussion of ability to finance government.

The attempt to measure (or find some index of) the financial capacity of a state is, as one might expect, a subject which interests students of public finance.<sup>14</sup> Per capita income has come to be rather extensively used, not only as a measure of capacity, but also (as will appear later) as a basis for estimating the burden of existing taxation.<sup>15</sup>

<sup>13</sup> In 1953, according to the Census Bureau, net long-term state debt (full faith and credit only) for Delaware was \$179.14 per capita, as compared with \$26.26 for the nation as a whole and \$78.25 for the second-highest state (Massachusetts). Bureau of the Census, *Compendium of State Government Finances in 1953* (Washington 1954), p. 41. In the same publication, page 5, the Bureau warns: "Caution must be used in attempting to draw conclusions from direct comparison of financial amounts for individual State governments. The States vary widely in the scope and intensity of their responsibilities."

<sup>14</sup> See Selma Mushkin and Beatrice Crowther, *Federal Taxes and the Measurement of State Capacity* (U. S. Department of Health, Education, and Welfare, Washington 1954; mimeographed), pp. 1-7.

<sup>15</sup> In some of the federal grant-in-aid programs, per capita income is also used as a basis for determination of allocation and matching requirements.

For the calendar year 1954, Delaware per capita income was \$2,372, as compared with a national average for the continental United States (District of Columbia included) of \$1,770 and a low of \$873 (Mississippi).<sup>16</sup> During the period 1940-1954, however, Delaware per capita income increased less than the rate for the nation as a whole (1.4 times in the case of Delaware, as compared with 2.0 times for the nation). In fact, the most rapid growth occurred generally in the ranks of the twelve lowest-income states. For example, between 1940 and 1954, Mississippi's per capita income increased 3.0 times.<sup>17</sup>

In a high-income state such as Delaware, where there is perhaps some sensitivity on the subject, one is likely to hear various objections to the use of per capita income data for fiscal analysis. In Delaware, one of these objections is the argument that Delaware is a small state with a number of very wealthy men, with the result that per capita income figures are distorted and misleading. This would appear to be true, however, only to the extent that anyone would be naive enough to believe that an average is also reflective of every item or individual involved in the averaging process. In this case, the "distortion" would merely seem to suggest that the state's tax system be somewhat different from what it would be if total income payments to individuals were more equally divided among the citizenry.

A more serious criticism is the argument that per capita income is not an adequate measure of state fiscal ability unless it is adjusted for federal taxes. The Council of State Governments has stated, for example: <sup>18</sup>

Unadjusted per capita income should not be used as a measure of fiscal capacity. At the very least, federal tax withdrawals should be reflected by the deduction of individual income tax collections.

There are several technical difficulties in "adjusting" per capita income figures for any given calendar year to allow for federal taxes.<sup>19</sup> Thus, to "adjust" a state's personal income for the inci-

<sup>16</sup> U. S. Department of Commerce, *Survey of Current Business* (September 1955), pp. 16-17, table 2.

<sup>17</sup> *Ibid.*, p. 18.

<sup>18</sup> Council of State Governments, Committee on Federal Grants-in-Aid, *Federal Grants-in-Aid* (Chicago 1949), p. 117.

<sup>19</sup> Mushkin and Crowther, *op. cit.*, pp. 33-34.

dence of the federal corporate income tax in that state would be to deduct some amount from an income base which does not itself include the source of the tax. A rough method of allowing for differences in the incidence of federal taxes among the states would be to correct per capita income figures for federal personal income tax withdrawals only. This, as can be seen in the excerpt quoted above, is the suggestion of the Council of State Governments.

The Mushkin and Crowther study (to which reference has already been made) undertook such an adjustment of calendar 1950 per capita income payments.<sup>20</sup> The results for the ten highest income states and the District of Columbia are shown in Table II below. Briefly, according to these data, the federal personal income tax takes a bigger "bite" (percentagewise) from Delaware's income payments to individuals than in any other state.<sup>21</sup> Furthermore, Delaware's margin is a considerable one. In terms of per capita income, the adjustment for federal personal income tax dropped Delaware from first position to sixth position among the states in 1950 (from second to seventh, if the District of Columbia is included).

A more recent study by the Economist's Office of the Du Pont Company is based on Commerce Department personal income data for 1954 and personal income tax liability estimated for the same calendar year.<sup>22</sup> Salient facts from this study are given in Table III below.

The Du Pont study estimates that federal personal income tax liability was slightly in excess of 14 per cent of personal income in Delaware in 1954. For the nation as a whole, the percentage was 9.8. In second place after Delaware was the District of Columbia with a figure of 13.3 per cent. Thus, as in the earlier Mushkin-Crowther study, it is shown that Delaware residents, as a group, contribute a larger percentage of personal income to the Federal Government as personal income taxes than do the residents of any other state. However, it should also be noted from Table III that Delaware remains a relatively high-income state, even after allow-

<sup>20</sup> *Ibid.*, pp. 35-37.

<sup>21</sup> Only the ten highest income states plus the District of Columbia are included in Table II. However, the inclusion of the remaining 38 states would not affect the conclusions reached in this paragraph.

<sup>22</sup> "Personal Income and Federal Personal Taxes, by States: Estimates for 1954," released by Economist's Office, Du Pont Company, November 1955. Referred to hereafter as "Du Pont Company Study."

TABLE II

EFFECT OF FEDERAL PERSONAL INCOME TAX WITHDRAWALS ON PER CAPITA INCOME  
OF TEN HIGHEST INCOME STATES, AND DISTRICT OF COLUMBIA

CALENDAR 1950

STATE	PER CAPITA INCOME		FEDERAL PERSONAL
	Before Adjustment	After Adjustment	INCOME TAX AS PERCENTAGE OF INCOME PAYMENTS
District of Columbia.....	\$1,955	\$1,778	9.1%
Delaware.....	1,897	1,598	15.8
New York.....	1,875	1,719	8.3
Nevada.....	1,863	1,702	8.7
Connecticut.....	1,776	1,641	7.6
California.....	1,758	1,621	7.8
Illinois.....	1,756	1,614	8.1
New Jersey.....	1,710	1,580	7.6
Washington.....	1,622	1,513	6.7
Massachusetts.....	1,604	1,476	8.0
Montana.....	1,591	1,493	6.2
United States *.....	1,439	1,332	7.5

\* Including District of Columbia.

SOURCE: Selma Mushkin and Beatrice Crowther, *Federal Taxes and the Measurement of State Capacity* (U. S. Department of Health, Education and Welfare, Washington, 1954; mimeographed), pp. 36, 38.

TABLE III

ESTIMATES OF PER CAPITA PERSONAL INCOME BEFORE AND AFTER FEDERAL  
PERSONAL INCOME TAX LIABILITY, 1954

STATE	PER CAPITA PERSONAL INCOME		RELATIVE POSITION	
	Before Taxes	After Taxes	Before Taxes	After Taxes
Nevada.....	\$2,414	\$2,157	1	1
Delaware.....	2,372	2,035	2	3
Connecticut.....	2,361	2,087	3	2
District of Columbia.....	2,220	1,924	4	7
New Jersey.....	2,219	1,997	5	4
New York.....	2,163	1,930	6	6
California.....	2,162	1,939	7	5
Illinois.....	2,155	1,912	8	8
Michigan.....	2,017	1,806	9	9
Ohio.....	1,983	1,755	10	10
National Average.....	1,770	1,596	—	—

ance for federal income taxes. This, together with the relatively low state-local tax burden discussed in 2e, should effectively answer any argument that Delaware cannot keep pace with her sister commonwealths in state and local developments because of an impossible burden of federal taxation.<sup>23</sup>

e. *Delaware Has a Low State-Local Tax Burden.* One method of showing state and local tax burden would be to express taxes on a per capita basis. For comparative purposes, however, such a method may be misleading. A per capita state and local tax of, say, \$100 may represent far greater "tax effort" on the part of one state than it does in the case of another state. This may be true because of significant differences in the income of the two states. Hence, it is more usual to relate state and local taxes to individual income of state residents by expressing the former as a percentage of the latter.

Even this second method is not entirely satisfactory as an index of burden. For one thing, there is the question of geographic incidence. Not all the taxes paid to government in a particular state are in the long run borne by residents of that state. The burden of some taxes may be "exported" to other states. In the case of Delaware, it seems reasonable to believe that the burden of the very important corporate franchise tax is not on Delaware residents to any appreciable extent.

Also, states differ among themselves as to the use they make of such non-tax revenues as liquor store profits, highway and bridge tolls, etc. Charges for services, for example, ranged all the way from 3.4 per cent (Vermont) to 21.0 per cent (Delaware) of total state and local general revenue in the fiscal years ending in 1953. During the same period taxes varied from 59.0 per cent (New Mexico) to 83.4 per cent (Massachusetts) of such revenue.<sup>24</sup> The apparent burden in some instances may reflect a decision to finance out of general tax revenues a service which, in other states, is put on a quasi-commercial basis. Comparisons among the states are thereby further complicated.

<sup>23</sup> It is not suggested that the federal tax burden should be dismissed lightly. The effect of federal taxation at current levels on such things as saving and capital formation is an important consideration today. However, the point made here is that in relation to other states Delaware is actually in a better position than most to increase state revenues, despite the burden of federal taxation.

<sup>24</sup> Bureau of the Census, *State and Local Government Revenue in 1953* (Washington 1954), p. 18, table 5.

In addition, federal grants-in-aid affect the states in unequal fashion. In the fiscal year ended in calendar 1953, for example, grants-in-aid ranged all the way from 6.2 per cent (New Jersey) to 29.8 per cent (Nevada) of state and local tax collections.<sup>25</sup> It would have been necessary to increase tax collections by these rather widely varying percentages to offset the loss of federal grants.

Finally, to express total state and local taxes as percentages of personal income, even assuming that the incidence of such taxes is wholly within the state is to err in logic. This is because some of the taxes involved do not have as their source the income base (personal income) being utilized. This would be true of corporate income taxes to the extent that such taxes are not shifted to individual income recipients in the state in question. This same point, it may be recalled, was mentioned in 2d above in the discussion of adjusting per capita income for federal tax withdrawals. Nevertheless, despite these objections and some others which could be raised, the use of this particular method for comparative burden analysis has sufficient currency to warrant its cautious usage here. Two such comparisons will be cited.

The first of these is contained in a study by Roger A. Freeman.<sup>26</sup> Freeman's estimates are for the latest fiscal year for which local data were available at the time (fiscal 1950 or 1951). State tax collections were derived from the Census Bureau's *Compendium of State Finances*. Local tax collections (a weak spot in fiscal reporting) were based on questionnaires to local officials and such data and estimates as the Census Bureau was able to supply. These fiscal-year tax collections were then expressed as percentages of the preceding calendar year's income payments to the residents of the states. The second comparison is a more recent one made by the Census Bureau.<sup>27</sup> In this study, state and local taxes combined, as well as total general revenues from own sources, for fiscal 1953, are expressed as amounts per \$1,000 of calendar 1953 income payments to individuals.

In both cases, Delaware's combined state and local tax burden appears to be smaller than that of any other state.<sup>28</sup> The Freeman

<sup>25</sup> The Commission on Intergovernmental Relations, *op. cit.*, p. 114, table 3.

<sup>26</sup> Roger A. Freeman, "The State and Local Tax Burden," *State Government* (April 1953), pp. 116-119, 127-128.

<sup>27</sup> Bureau of the Census, *State and Local Government Revenue in 1953* (Washington 1954), p. 28.

<sup>28</sup> For reasons of space, no data from either of the two studies of state-local

study also shows the much greater importance of state, as compared with local taxation in Delaware. It is true, of course, that Delaware's low state-local tax burden is coupled with a relatively high federal tax burden. As brought out in 2d above, Delaware has a very substantial federal tax bill. However, as also previously brought out, too much should not be made of this fact. As noted earlier, Delaware's per capita income remains high even after adjustment for federal taxes.

In concluding this brief consideration of tax burden, one other point should be noted: taxes are for the purpose of providing governmental services of various types. So far as state taxes are concerned, their imposition brings about a burden which may be more than offset by the benefits which the government programs make possible. Particular individuals may feel that on net balance they are losers. For the group as a whole, however, if government programs are intelligently planned and executed, welfare should be greater by virtue of the tax and expenditure programs.

### 3. *Trends in Delaware State Finance in the Post-War Decade*

In the preceding section, some of the general factors affecting Delaware state finance were listed. These factors are of significance in terms of past and future developments. In this section, some pertinent trends occurring during the decade following World War II are presented. Later, an attempt will be made to evaluate these trends in the light of the factors enumerated in section 2 and to relate them to the future needs of the state's revenue system.

The United States became an active participant in World War II at a time when there were still evidences of depression. Two years of war brought an end to unemployment, and gross national product mounted to a new high. In general (and despite the dips of 1949-1950 and 1953-1954), the full employment and rising production continued in the post-war decade. The predicted post-war depression, with estimated unemployment of eight million, did not materialize. How much of the continued high level of economic activity (especially since the Korean episode) has been due to the stimulus of a heavy armament program is problematical. In any case, public

burden are reproduced here. For further details the reader is referred to the sources quoted in the two preceding footnotes.

finance since the close of World War II has had a vigorous economy as its background.

During the war years, inevitably federal finance superseded state and local finance. This was not an entirely new development for even during the depression years of the 1930's the financing of the Federal Government was assuming increasing importance.<sup>29</sup> However, the financing of World War II gave substantial impetus to the upward course of federal fiscal requirements. The states, barred from capital outlay and at the same time profiting taxwise from an expanding economy, were in most instances able to put their financial houses in some order, following the strain of the depression decade. Thus for example, between 1942 and 1946 (fiscal year basis) net long-term debt (full faith and credit issues) declined from \$3.1 to \$1.4 billion.<sup>30</sup>

With the close of the war, the states encountered various problems. Population in the 48 states increased about 15 per cent between 1942 and 1952. More than this, shifting patterns of economic development among the states were accompanied by even more striking geographic redistribution of population. In the same decade (1942-1952), the states of the Southwest and Northwest showed population increases of as much as 65 per cent (Arizona), whereas in New England, for example, with the exception of Connecticut, the increase was less than half that of the 48 states as a group. In some states (Arkansas and North Dakota), there was actually a net reduction in population.<sup>31</sup> Still a third phase of population changes were the movements out of urban to suburban fringe areas.

The war-time curtailment of expenditures on capital improvements (highways, schools, etc.) reduced only temporarily the spending of state governments. Once the war and its various controls passed, the race was on to catch up on both new capital outlay and deferred maintenance of existing items.

An outstanding feature of postwar state finance has been the problem of providing for needed capital improvements. Partly this capital outlay problem resulted from the inability of the states to do much along this line in the war years. Partly also it was due

<sup>29</sup> R. A. Musgrave and J. A. Culbertson, "The Growth of Public Expenditures in the United States, 1890-1948," *National Tax Journal* (June 1953), p. 104.

<sup>30</sup> Bureau of the Census, *Revised Summary of State Government Finance, 1942-1950* (Washington 1953), p. 4, table 1.

<sup>31</sup> *Ibid.*, p. 55, table 3. Population figures are July 1 estimates exclusive of armed forces overseas.

to the various population changes and to the sustained economic development mentioned in the preceding paragraphs. In any case, however, the postwar needs of the states have bumped up against the scarcity of resources which characterizes a period of generally prosperous conditions, and against a governmental structure in which the requirements of the Federal Government still loom large.

The story of this decade, as it relates to state finance in general and to Delaware state finance in particular, is brought out in Table IV.<sup>32</sup> Comparisons among the states in the matter of receipts and expenditures is subject to some danger, since (as pointed out in 2b and 2c above) the states differ among themselves as to scope and quality of services offered. In this case, however, we are not so much concerned with a comparison of differences in scope and quality of state functions as we are with the (apparent) degree of willingness to meet the cost of whatever functions are undertaken.

An examination of Table IV reveals several things. It appears that in the decade following the war, population and expenditures in Delaware have tended to increase more extensively than in other states, whereas taxes (except for personal income taxes) have tended to lag behind other states' collections. It may also be noted in passing that Delaware has not fared as well, relatively speaking, as other states in the matter of federal grants-in-aid which supplement other state sources of revenue.<sup>33</sup>

Delaware's attempts to improve the state revenue sources have concentrated largely (though not wholly) on increasing personal income tax collections. This is evident from an inspection of series 4 in Table IV, where the effect of the two-year increase of 1949 and the permanent increase in 1953 are reflected in the data for fiscal years 1950 and 1954. The marked change in total tax collections in the two latter years is a result also of these income-tax developments.

<sup>32</sup> The basis of table 4 is the Census Bureau's series on state finance as revised effective with data for the fiscal year 1951. This series brings together all the receipts and disbursements of all state agencies (including, for example, state institutions of higher education) in a non-duplicative fashion. State government and its finance is thus viewed in a broad sense. The Bureau's data provide a basis for some comparison among the states, although as pointed out in the text such interstate comparisons are dangerous unless cautiously handled. See footnote 13 above, and H. E. Newman and E. W. Smith, "Federal Grants-in-Aid to the State of Delaware," *Delaware Notes* (Twenty-eighth Series, 1955), pp. 7-14.

<sup>33</sup> On the matter of federal grants-in-aid in Delaware state finance, see H. E. Newman and E. W. Smith, *op. cit.*

TABLE IV

PERCENTAGE CHANGE IN POPULATION AND SELECTED STATE GOVERNMENT FINANCE  
SERIES, 48 STATES AND DELAWARE, FISCAL YEARS 1942-1954

(1942 = 100)

Series	1942	1944	1946	1948	1950	1952	1953	1954
1. Population:	48 States 100	101	99	108	112	115	118	119
	Delaware 100	103	104	111	115	120	123	130
2. Sales & Gross Receipts Taxes:	48 States 100	97	126	132	211	258	280	296
	Delaware 100	146	119	132	196	225	245	284
3. License Taxes:	48 States 100	99	111	141	173	208	230	241
	Delaware 100	102	112	130	144	161	193	213
4. Individual Income Taxes:	48 States 100	127	156	200	291	367	389	403
	Delaware 100	73	97	124	488	304	203	722
5. Total Taxes	48 States 100	104	126	173	203	253	270	284
	Delaware 100	116	139	137	236	221	235	385
6. Total Federal Aid:	48 States 100	115	100	205	284	297	320	333
	Delaware 100	117	87	164	238	252	282	240
7. Expenditure, Education:	48 States 100	114	124	223	289	341	371	394
	Delaware 100	109	118	171	259	386	452	498
8. Expenditure, Public Welfare:	48 States 100	104	116	176	258	261	275	280
	Delaware 100	81	89	150	231	271	323	356
9. Expenditure, Highways:	48 States 100	74	84	178	235	290	316	364
	Delaware 100	57	88	166	525	558	577	370
10. Expenditure, Health and Hospitals:	48 States 100	112	144	225	335	405	422	451
	Delaware 100	95	114	215	271	365	390	394
11. Expenditure, Capital Outlay:	48 States 100	51	57	227	348	414	443	521
	Delaware 100	21	53	172	682	781	819	638
12. Expenditure, Total General:	48 States 100	99	115	208	269	301	323	347
	Delaware 100	92	109	172	385	416	459	434
13. Net Long-Term Debt Outstanding, End of Fiscal Year:	48 States 100	82	67	114	166	219	246	307
	Delaware 100	88	79	839	1344	1585	1930	2166
14. Same, Full Faith and Credit Only:	48 States 100	81	65	115	159	188	192	211
	Delaware 100	89	80	137	672	784	1162	1473

SOURCE: Percentages computed from the following:

Data for 1942-1950 from U. S. Dept. of Commerce, Bureau of the Census, *Revised Summary of State Government Finances, 1942-1950*, State and Local Government Special Studies No. 32 (Washington 1953); for 1952, U. S. Dept. of Commerce, *Compendium of State Government Finances in 1952* (Washington 1953); for 1953, *Compendium, etc.*, for 1953 (Washington 1954); for 1954, *Compendium, etc.*, for 1954 (Washington 1955).

Of the ten highest-income states in 1954 (per capita basis), only three (California, Delaware, and New York) were among the 31 states in that year using some form of personal income taxation. The tax on individual incomes produced about 8 per cent of California's total tax collections, about 24 per cent in the case of Delaware, and about 30 per cent in the case of New York. Since both California and New York also have corporate income taxes, their reliance on income taxation in all forms is greater than the figures just shown.<sup>34</sup> For the 48 states as a group, about 9 per cent of taxes in 1954 were of the individual income variety and about 7 per cent came from corporate income taxes.<sup>35</sup>

Delaware, in other words, relies more on personal income taxation than do the 48 states as a group, and to a greater extent than any other state in the top ten (per capita income basis) except New York. This is especially significant when it is recalled that state government is generally more important in Delaware than elsewhere.<sup>36</sup> By the criteria of progressiveness usually accepted by students of public finance today, Delaware's state tax system would score a rather high mark. The criticism one can make of tax developments in Delaware during the post-war decade is not so much in the content of those developments, but rather in their failure to exploit to the extent necessary the tax resources of the state.

The major tax changes in 1949 and 1953 did little more than to enable the balancing of general fund. They did not come to grips with the capital outlay problem. This is apparent from an examination of series 11 through 14 in Table IV. The surging capital outlay on schools and highways and public institutions, reflecting accumulated needs from the war years and post-war population and economic development factors, resulted in a state-debt trend which is probably not in the best interest of the state. The fact that Delaware has the highest per capita debt in the group of 48 states is not, *per se*, an alarming condition. As has already been indicated, state governments vary among themselves as to the scope and content

<sup>34</sup> Bureau of the Census, *Compendium of State Government Finance in 1954* (Washington 1955), p. 11. One other state (Connecticut) among the ten with highest per capita incomes employs a corporate income tax, but no individual income tax. This leaves six which, in 1954, employed no form of income taxation: Illinois, Michigan, Nevada, New Jersey, Ohio, and Washington.

<sup>35</sup> *Ibid.* See also Tax Institute, Inc., "Total Tax Collections in 1954," *Tax Policy* (October 1955), p. 4.

<sup>36</sup> See section 2c above.

of their functions; and in Delaware, the scope and content of those functions seem well above average. However, the trend in Delaware's state debt does suggest some cause for concern.

There seems to have been a too easy acceptance in the state of the idea that capital improvements represent long-term projects, and that it is only proper that their cost should be spread out over the life of the improvements. To put it another way, there seems to have been reluctance on the part of present taxpayers (or their legislative representatives) to pay the entire cost of a school or a new highway whose benefits would extend to future groups of taxpayers.

Such reasoning would be more plausible if capital improvements were isolated and non-recurring in nature. But in a state fortunate (or unfortunate?) enough to experience above-average population growth and a tempo of economic development generally above that of its somewhat more tranquil past, so-called capital improvements become virtually current expenditures. If, for the state as a whole, one has to add a school building each year (in addition to replacing old ones), then there is nothing of an isolated or non-recurring nature about school construction.<sup>37</sup>

A rapidly growing state debt presents two problems which may be noted here. In the first place debt service charges tend to become an increasing percentage of the state's budgeted expenditures. In fiscal 1955 debt service already amounted to more than 11 per cent of general fund disbursements and it is estimated that during fiscal 1957 this figure will go above 15 per cent.<sup>38</sup> Such a development introduces an element of rigidity and inflexibility into budgeting.

The second problem has to do with the credit of the state. To date there is no evidence that the mounting state debt has seriously impaired the state's credit position. But a continuation of the trend evidenced in the past decade could weaken that position, particularly if an economic recession of any significance should develop.

The post-war decade has been one of generally high and rising levels of employment, income, and production. It should have been a decade favorable to substantial pay-as-you-go in the capital out-

<sup>37</sup> For a discussion of this point, see W. J. Shultz and C. L. Harriss, *American Public Finance* (New York 1954; Sixth Edition), pp. 572-576.

<sup>38</sup> Circular dated August 23, 1955, issued by the Secretary of State soliciting bids on \$7 million of new capital improvement bonds.

lay field, with a reservation of the state's credit for any future period of economic recession. In this connection it should be recalled that a state (even a relatively "rich" state such as Delaware) has a limited borrowing capacity at any given time. The Federal Government has enormous aids in its taxing powers and control over the money supply in dealing with its own debt problems. Not so the states, which come closer to the position of individuals and business concerns in the matter of credit limitations.<sup>39</sup>

#### 4. *Summary and Conclusions*

A review of Delaware state finance in the post-war decade as a means of assessing the present and future financial requirements of the state leads one to the following conclusions:

The cost of Delaware state government in the years ahead will be affected by five factors: (1) Population growth will increase the cost and will tend to increase it by more than the rate of growth itself. (2) As a small state, Delaware may expect to pay more per unit of service than larger areas providing comparable programs. (3) Unless a radical change occurs in the functional distribution between state and local government, the cost of state government may appear unusually high to Delawareans, higher, in fact, than it actually is when the division of duties between the two levels of government is borne in mind. (4) On the other hand, while the preceding factors tend to increase costs of state government in Delaware, the fact that it is a high-income state makes Delaware better able to meet the requirements of state government. (5) State and local tax burdens combined are relatively low as measured by commonly employed tests. It is true that total tax burden (federal tax incidence included) is quite high. However, per capita income (even after allowance for all taxes) is still such that Delaware should be better able to cope with needs than many sister states.

The five factors enumerated in the preceding paragraph, and discussed at greater length in section 2 above, were present during the post-war decade. They will be influencing factors in the years

<sup>39</sup> The states do have one advantage in marketing their securities: the exemption of interest on those securities from the sharply progressive federal income tax on individuals. This is a major explanation of how Delaware has been able to market 20-year bonds at rates generally below the rates paid by the U. S. Treasury on issues of comparable maturity.

ahead. The conclusion one draws from them is that state government in Delaware will be relatively expensive, but at the same time one must also conclude that the state is quite capable of meeting its financial needs.

The actual record of state finance in the years following the end of World War II is not a commendable one. Briefly, the state's legislators and officials have contented themselves with sporadic efforts (notably in 1949, 1953, and 1955-1956) which have for the most part done little more than keep the general fund balanced (or restore it to a balanced condition).

It is the argument of this paper that the great weakness in Delaware state finance in recent years is the failure adequately to deal with the issue of capital outlay on improvements. It is perhaps unrealistic to think that a complete pay-as-you-go policy should have been pursued. However, a better record than the one to date should have been earned. In this connection, it may be noted that the so-called McKinsey study of state finances in 1954 recommended that the state aim toward financing about half of capital outlay in the next few years from tax receipts.

Any attempt to cover general fund disbursements and a substantial share of capital outlay from current taxes will mean a significant upward revision in state tax collections, over and above any increase attributable to general economic growth. As pointed out in the introductory section, it is not the purpose of this paper to suggest specific revenue solutions. It is to be hoped that solutions adopted will not weaken the generally progressive tone which has characterized taxation in Delaware. In any case, the state has the ability to meet its needs, and the solutions should not prove too difficult or elusive.