It was a taxing situation during the Depression

By Jerry Bowen

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In my last column we began to take a brief look at some of the history of the Depression of the 1930s. A look at our elected officials performance gives us reason to wonder if they have learned anything from the past.

From 1914 to 1934, Californians paying taxes of all kinds increased an amazing 538 percent. Beginning in 1929, the state's deficit increased in spite of the many new taxes enacted during the previous six years.

Under the political thinking of the day, the federal government decided it was morally prudent to pursue a balanced budget. As tax revenue was plummeting along with economic activity in the period from 1929 to 1932, the political "worthies" decided to raise taxes to cover the mushrooming deficit.

In 1932, President Herbert Hoover, with the support of the newly elected Democratic majority in the House of Representatives, passed the largest peacetime tax increase in the history of the United States. Marginal income tax rates were raised from 1.5 percent to 4 percent at the low end and from 25 percent to 63 percent at the top of the scale. This was a huge tax increase by any measure.

It would have taken 25 percent of all the wages and salaries received by wage earners in California to pay the taxes in 1934.

That rate of tax increase was almost three times the rate of increase in basic income and almost four times the rate of increase in population. Even though the outlook was for a general fund deficit of $79 million, at the end of 1935 the California Legislature enacted $97 million dollars in new taxes.

That doesn't sound like much by today's standards, but it was a huge increase then. The total bonded debt of the state, counties and districts in California, coupled with California's per capita share of the federal public debt, was equal to 33 percent of the total assessed valuation of all tangible property in the state. With all of the bloated actions of the politicians, government costs approached the danger line of economic safety during the 1930s.

The tax increases were generally associated with decreases in demand for goods and services and the incentive to earn. At that point the situation was becoming so severe that anybody that still had a job was motivated to keep it. If you earned money, you saved as much as you possibly could. With bank failures everywhere, many folks hid their savings so they would have access to the money. Quite likely the main obstacle to demand then was probably fear of spending.

Paying more out in taxes and out of sight fees to let the government spend it for you to stimulate the economy was the idea promoted by politicians then much as it is again today. But the tax increase took money out of people’s hands that could have been spent more “efficiently” if not equitably. Many considered that to be a factor that prolonged the downturn.

So what were some of the factors contributing to the severity of the Great Depression? Was it a highly stimulated economic exhilaration of the 1920s? Was it the monetary policy pursued by the Federal Reserve Bank from 1930-1933? Was it a sudden rise of global protectionism leading to the collapse of world trade? Did the dramatic rise of income taxes in 1932 prolong the downturn? Did the Work Projects Administration (WPA) provide efficient relief or did it prolong the depression?

It isn’t particularly amusing to witness policy debate over such actions by politicians these days that have forgotten the Depression. When times are good, they spend like reckless fools. Perhaps it takes a Great Depression once in a while to remind us that we are all cut from the same cloth.