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# CONGRESSIONAL REGULATION OF STATE TAXATION OF INTERSTATE COMMERCE

PAUL F. MICKEY AND GEORGE B. MICKUM, III\*

## INTRODUCTION

In the 1958 term the Supreme Court of the United States decided in three cases that a properly apportioned state net income tax may be validly applied to activities within a taxing state which are exclusively in furtherance of interstate commerce.<sup>1</sup> Since interstate businesses already feel harassed by a myriad of state taxes, the decisions created some consternation in business circles. Among state tax officials faced with lagging revenues, the decisions received an enthusiastic welcome. Some states have rushed to enact new net income tax laws.<sup>2</sup>

Business countered these decisions by obtaining from Congress the enactment of federal legislation intended to draw a line for state taxation of interstate commerce at the point reached by *Northwestern States Portland Cement Co. v. Minnesota*<sup>3</sup> and providing for further joint study by the House Judiciary and Senate Finance Committees for the purpose of formulating broader legislation.<sup>4</sup> Since the Court had never before sustained a tax so levied and since Congress had never before legislated to restrict state taxation of interstate commerce, it is understandable that these cases have been regarded as ushering in a new era in state taxation.<sup>5</sup>

While passage of this legislation limiting to some extent the power of the states to impose taxes is a major development, of more vital significance is the possibility of further congressional action regulating the states in their taxation of interstate businesses. Having entered the

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<sup>1</sup> *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450 (1959) (consolidated for hearing with *Williams v. Stockham Valves & Fittings, Inc.*), and *E T & W N C Transp. Co. v. Currie*, 359 U.S. 28 (1959).

<sup>2</sup> Idaho (IDAHO CODE ANN. §§ 63-3001 to -3087 (Supp. 1959)); Tennessee (TENN. CODE ANN. §§ 67-2701 to -2727 (Supp. 1959)); and Utah (UTAH CODE ANN. §§ 59-13-1 to -77 (Supp. 1959)) have added themselves to the thirty-one states which imposed a net income tax prior to the decisions.

<sup>3</sup> 358 U.S. 450 (1959).

<sup>4</sup> S. 2524, 86th Cong., 1st Sess. (1959) was signed by the President on September 14, 1959. 73 Stat. 555 (1959), 15 U.S.C.A. § 381 (Supp. 1959). To distinguish the legislation from various other bills which were proposed it will be referred to as S. 2524.

<sup>5</sup> See Silverstein, *State Taxation of Interstate Commerce: A First Look at the "Net Income" Cases*, XI TAX EXECUTIVE 200 (1959); *The New Tax Grip on Interstate Income*, XXVIII P-H Corporation Reporter § 2 (April 15, 1959); Maun, *Stockham, Northwestern States, End Long Fight But Raises Numerous Business Problems*, 10 J. TAX. 280 (1959).

field in a flurry,<sup>6</sup> it is conceivable that Congress eventually may undertake to establish general rules of limitation and uniformity for taxation of interstate commerce by the states, with revolutionary consequences. Although such regulation is badly needed and long overdue, the suggestion presages a battle with politically powerful state revenue officials and governors, the outcome of which is doubtful.

With the stage thus set for such legislation, it is worthwhile to examine the power of Congress to regulate state taxation of interstate commerce, the scope of its first effort, the magnitude of the problem which hundreds of haphazard state laws and nearly a century of judicial tinkering with individual factual situations have generated, and the avenue to solution.

#### THE POWER OF CONGRESS TO CONTROL STATE TAXATION OF INTERSTATE COMMERCE

The Constitution itself was a direct outgrowth of a need to end interferences with the free flow of commerce among the states, arising in part from burdensome taxation which the Articles of Confederation had permitted.<sup>7</sup> Differences which arose over the effort to prescribe the governing provisions were resolved by limiting specific restrictions upon the states' taxing power to those forbidding any imposts or duties on imports or exports and by giving Congress the power to regulate commerce among the states.<sup>8</sup>

<sup>6</sup> To our knowledge Congress has in the past never passed legislation of this character and has formally considered it only infrequently, and then, for the most part, only in restricted areas: *e.g.*, uniform allocation formulae for airlines: S. 2453, 80th Cong., 2d Sess. (1948); S. 420, 81st Cong., 1st Sess. (1949); H.R. 1241, 80th Cong., 1st Sess. (1947); sales taxes: S. 2897, 73d Cong., 2d Sess. (1934); see also *Hearings Before Senate Subcommittee on Interstate Commerce on S. 2663 and 2897*, 73d Cong., 2d Sess. (1934); general legislation authorizing state taxes of all kinds on interstate business to the same extent as on intrastate business: S. 3074, 72d Cong., 1st Sess. (1932).

<sup>7</sup> See Webster's argument in *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 12-13 (1824), that the "entire purpose" of the Constitutional Convention "was to devise means for the uniform regulation of trade." See also Justice Johnson's concurring opinion in *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) at 222-39, elaborating on the causes leading to adoption of the Constitution. Justice Miller, dissenting in *Philadelphia & R.R.R. Co. v. Pennsylvania*, 82 U.S. (15 Wall.) 284 (1873), refers to the same origin of the Constitution, commenting that "the reluctance of the little State of Rhode Island to give up the tax which she thus levied on the commerce of her sister States through the harbor of Newport . . . was the reason that she refused for nearly two years to ratify that instrument." 82 U.S. (15 Wall.) at 297. And Justice Stone, in *Western Livestock v. Bureau of Revenue*, 303 U.S. 250 (1938), speaking of unapportioned gross receipts taxes says: "The multiplication of states taxes measured by the gross receipts from interstate transactions would spell the destruction of interstate commerce and renew the barriers to interstate trade which it was the object of the Commerce Clause to remove." 303 U.S. at 255-56.

<sup>8</sup> See Hellerstein and Henefeld, *State Taxation in a National Economy*, 54 HARV. L. REV. 949 (1941). This clearly is the only possible inference to be drawn from Marshall's discussion of the commerce clause vis-a-vis the explicit restrictions on state taxing power in *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 201-03 (1824). See

Congress did not prior to 1959 exercise any regulatory authority in respect to state taxation of commerce; but for nearly a hundred years the Supreme Court has upheld or struck down innumerable state tax statutes, most often challenged under the commerce clause, and less frequently under the due process clause of the Constitution. In the *State Freight Tax Case*,<sup>9</sup> decided nearly a decade after the Civil War, the Court squarely encountered the problem of the effect of the commerce clause on a state revenue measure where no congressional legislation on the subject had been passed. Pennsylvania's tax on each ton of freight carried in the state as applied to interstate freight was held to be an invalid regulation of commerce between the states. The Court laid down the basic rule that,

Transportation is essential to commerce; and every burden laid upon it is *pro tanto* a restriction. Whatever, therefore, may be the true doctrine respecting the exclusiveness of the power vested in Congress to regulate commerce among the States, we regard it as established that no State can impose a tax upon freight transported from State to State, or upon the transporter, because of such transportation.<sup>10</sup>

In response to the contention that the tax was a revenue measure which did not discriminate against interstate commerce and was, accordingly, not regulation, the Court said:

Nor can it make any difference that the legislative purpose was to raise money for the support of the State government, and not to regulate transportation. It is not the purpose of the law, but its effect, which we are now considering. Nor is it at all material that the tax is levied upon all freight, as well that which is wholly internal as that embarked in interstate trade. We are not at this moment inquiring further than whether taxing goods carried because they are carried is a regulation of carriage.<sup>11</sup>

Justices Swayne and Davis dissented because the tax was on all freight without regard to its origin or destination and was therefore not discriminatory. This fact they said was "conclusive" in favor of the constitutionality of the tax.<sup>12</sup>

also Hamilton in *THE FEDERALIST* No. 32, at 206 (Dunne ed. 1901): "I am willing here to allow, in its full extent, the justness of the reasoning which requires that the individual States should possess an independent and uncontrollable authority to raise their own revenues for the supply of their own wants. And in making this concession, I affirm that (with the sole exception of duties on imports and exports) they would, under the plan of the convention, retain that authority in the most absolute and unqualified sense; and that an attempt on the part of the national government to abridge them in the exercise of it, would be a violent assumption of power, unwarranted by any article or clause of its Constitution."

<sup>9</sup> *Philadelphia & R.R.R. v. Pennsylvania*, 82 U.S. (15 Wall.) 232 (1873).

<sup>10</sup> *Id.* at 281-82.

<sup>11</sup> *Id.* at 276-77.

<sup>12</sup> *Erie Ry. v. Pennsylvania*, 82 U.S. (15 Wall.) 282 (1873), was decided on the

Thus, the Court was induced to invalidate a state tax on the basis of the commerce clause, notwithstanding that the clause apparently was designed not to be in itself a restriction on the states' power to tax commerce, but to give Congress power to eliminate arbitrary restrictions on the flow of commerce by the several states. Obviously, non-discriminatory taxation for revenue purposes is not a direct regulation of commerce even though it burdens it; but whether or not such a rule was intended by our forefathers is a question for historians. For nearly a century since the *State Freight Tax Case* it has been the rule that some nondiscriminatory tax burdens on commerce are prohibited regulation even in the absence of congressional action of any kind.<sup>13</sup>

A corollary to this rule must be that Congress has the power under the commerce clause to regulate state taxation of interstate commerce. For if state taxation is held to be "regulation," congressional supervision of state taxation should be held to be "regulation" within the language of the commerce clause. While the Supreme Court has never had occasion directly to uphold any such legislation, it has repeatedly assumed that congressional action would be proper.

In *Northwestern Cement*<sup>14</sup> Justice Clark speaking for the majority twice specifically mentions congressional failure "to regulate taxation" by the states of interstate commerce, stating at one point,

It has long been established doctrine that the Commerce Clause gives exclusive power to the Congress to regulate interstate commerce and its failure to act on the subject in the area of taxation nevertheless requires that interstate commerce shall be free from any direct restrictions or impositions by the States.<sup>15</sup>

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same day as the *State Freight Tax Case* and involved the tonnage tax on a foreign corporation. As might be expected the tax was held invalid. Here, however, Justices Field and Miller dissented, while Justices Swayne and Davis did not. A third case, *Philadelphia & R.R.R. v. Pennsylvania*, 82 U.S. (15 Wall.) 284 (1873), also decided on the same day as the others, involved a tax on the gross receipts of railroads incorporated in Pennsylvania. This tax was upheld, apparently because the taxpayer was chartered by Pennsylvania and because the burden on interstate commerce did not seem as direct as had been thought in the case of the tonnage tax, inasmuch as at the time the tax was levied the gross receipts had become "part of the mass of property of the State." Justices Miller, Field and Hunt dissented from this decision, contending that the tonnage tax could not be distinguished from the gross receipts tax on the corporation's revenues derived from carrying freight.

<sup>13</sup> The Court's action in this field is in marked contrast to the general rule that the states are free to legislate in respect of matters over which Congress has, but has not exercised, power and that upon congressional entry state action inconsistent therewith falls under the supremacy clause, U.S. CONST. art. VI. As has been observed elsewhere, "the Court's assumption of the power to strike down state taxes for this reason constitutes an exercise of the very power to regulate commerce delegated to Congress . . ." Hellerstein and Hennefeld, *supra* note 8, at 953 n.12.

<sup>14</sup> 358 U.S. 450 (1959).

<sup>15</sup> *Id.* at 458; see also *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157, 170 (1954).

Justice Whittaker in his dissenting opinion in that case clearly states his view that Congress has the power to regulate state taxation of interstate commerce. He says, "The Commerce Clause denies state power to regulate interstate commerce. . . . Direct taxation of 'exclusively interstate commerce' is a substantial regulation of it and, therefore, in the absence of congressional consent, the States may not directly tax it."<sup>16</sup> Justice Frankfurter, also in dissent, calls for a congressional policy stating, "Congress alone can provide for a full and thorough canvassing of the multitudinous and intricate factors which compose the problem of the taxing freedom of the States and the needed limits on such state taxing power."<sup>17</sup> Thus, the entire present Court appears committed to the principle that Congress can regulate state taxation of interstate commerce.

Long ago in *Woodruff v. Parham*<sup>18</sup> the Court, invalidating a tax on sales of merchandise made in interstate commerce, observed:

There is also . . . the unquestioned power of Congress, under the authority to regulate commerce among the States, to interpose, by the exercise of this power, in such a manner as to prevent the States from any oppressive interference with the free exchange of commodities by the citizens of one State with those of another.<sup>19</sup>

Later, in *Lyng v. Michigan*,<sup>20</sup> the Court held:

We have repeatedly held that no State has the right to lay a tax on interstate commerce in any form, whether by way of duties laid on the transportation of the subjects of that commerce, or on the receipts derived from that transportation, or on the occupation or business of carrying it on, for the reason that such taxation is a burden on that commerce, and amounts to a regulation of it, which belongs solely to Congress.<sup>21</sup>

And on one occasion, despairing of effective judicial solution, the four dissenting Justices in *McCarroll v. Dixie Greyhound Lines, Inc.*<sup>22</sup> called for broad congressional study and "exercise of its plenary constitutional control over interstate commerce."<sup>23</sup>

<sup>16</sup> 358 U.S. at 496.

<sup>17</sup> 358 U.S. at 476; see also *Gwin, White & Prince, Inc. v. Henneford*, 305 U.S. 434, 441 (1939) (Butler, J., concurring); *Gwin, White & Prince*, 305 U.S. 434, 442 (1939) (Black, J., dissenting); *J. D. Adams Mfg. Co. v. Storen*, 304 U.S. 307, 316 (1938) (Black, J., dissenting).

<sup>18</sup> 75 U.S. (8 Wall.) 123 (1869).

<sup>19</sup> 75 U.S. (8 Wall.) at 140.

<sup>20</sup> 135 U.S. 161 (1890).

<sup>21</sup> 135 U.S. at 166; see also *Crutcher v. Kentucky*, 141 U.S. 47, 57 (1891).

<sup>22</sup> 309 U.S. 176, 183 (1940).

<sup>23</sup> The dissenters said: "Judicial control of national commerce—unlike legislative regulations—must from inherent limitation of the judicial process treat the subject by the hit-and-miss method of deciding single local controversies upon evidence and information limited by the narrow rules of litigation. Spasmodic and unrelated

There is, accordingly, little room for doubt that reasonable congressional efforts under the commerce clause to legislate concerning state taxation of interstate commerce will be sustained. Nor is there any basis for a claim that such power is limited in any practical sense, for the Court has held that the grant to Congress of the power to regulate commerce is "plenary and may be exerted to protect interstate commerce 'no matter what the source of the dangers which threaten it.'"<sup>24</sup> Even where a matter is intrastate in character Congress may legislate with reference to it in order to protect interstate commerce to which it is substantially related.<sup>25</sup>

In view of all the dicta suggesting, and in the practical sense requesting, congressional action, attacks on the existing or prospective federal legislation regulating state taxation of interstate commerce are foredoomed. The Collector of Taxes of Louisiana is reported to have announced that the 1959 statute would be attacked by Louisiana on constitutional grounds.<sup>26</sup> Such an effort may be desirable in order to settle the issue directly at an early date, but it can have but one outcome.

#### THE NEW STATUTE

The first congressional stir resulting from *Northwestern Cement* and its related cases was the issuance by the Senate Select Committee on Small Business on June 30, 1959, of a *Report on the Problems Faced by Small Business in Complying With Multi-State Taxation of Income Derived From Interstate Commerce*.<sup>27</sup> This committee was

instances of litigation cannot afford an adequate basis for the creation of integrated national rules which alone can afford that full protection for interstate commerce intended by the Constitution. We would, therefore, leave the questions raised by the Arkansas tax for consideration of Congress in a nation-wide survey of the constantly increasing barriers to trade among the States. Unconfined by 'the narrow scope of judicial proceedings' Congress alone can, in the exercise of its plenary constitutional control over interstate commerce, not only consider whether such a tax as now under scrutiny is consistent with the best interests of our national economy, but can also on the basis of full exploration of the many aspects of a complicated problem devise a national policy fair alike to the States and our Union." 309 U.S. at 188-89. See also *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157, 166 (1954); *Northwest Airlines v. Minnesota*, 322 U.S. 292 (1944).

<sup>24</sup> *NLRB v. Jones & Laughlin Steel Corp.*, 301 U.S. 1, 36-37 (1937), and cases therein cited.

<sup>25</sup> *United States v. Darby*, 312 U.S. 100 (1941); *United States v. Rock Royal Co-op.*, 307 U.S. 533 (1939); *Mulford v. Smith*, 307 U.S. 38 (1939); *NLRB v. Jones & Laughlin Steel Corp.*, 301 U.S. 1 (1937); *Railroad Comm'n v. Chicago, B. & Q.R.R.*, 257 U.S. 563 (1922); see also *Houston, E. & W.T. Ry. v. United States*, 234 U.S. 342 (1914), in which the Court sustained Congress' right to regulate intrastate freight rates because of their effect on interstate through rates.

<sup>26</sup> Address of Robert L. Roland, Louisiana Collector of Revenue, to Tax Executives Institute meeting in French Lick, Indiana, reported in *CCH State Tax Review*, vol. 20, No. 40 (Oct. 5, 1959).

<sup>27</sup> S. Rep. No. 453, 86th Cong., 1st Sess. (1959). This report was the outgrowth of hearings held April 8, May 1 and June 19, 1959. *Hearings Before the Senate Select Committee on Small Business, State Taxation of Interstate Com-*

primarily concerned with the problems which confront small businesses engaged in interstate selling activities but lacking sales offices or employees in all states in which they sell, although it recognized that large as well as small businesses shared the multi-state tax problem. It recommended legislation which, as a "temporary minimum standard," drew the line for state taxation of income at the point to which *Northwestern Cement* had advanced it. Under the so-called minimum standard a state or political subdivision thereof could not "impose a tax upon the income of any business" unless such business "maintained a stock of goods, an office, warehouse, or other place of business in such State or has had an officer, agent or representative who has maintained an office or other place of business in such State."<sup>28</sup> Thus, under the proposal of the Select Committee, *Northwestern Cement*, in which the taxpayers maintained sales offices and resident salesmen and employees, would have been left undisturbed for the time being. However, the recommended legislation proposed to create a Commission on State Taxation of Interstate Commerce to study the problem resulting from multi-state taxation of income, as well as the problem of assuring the states that interstate commerce bears its fair share of the tax burden, and to formulate a concrete proposal for the solution of these two problems.<sup>29</sup>

In its report the Committee stressed the problems confronting business, among which were the "difficulty of knowing what constitutes 'doing business,'" the "lack of uniform State laws and formulas for apportioning income to the various taxing jurisdictions, and the burdens of complying with the multiplicity of State and municipal laws and regulations,"<sup>30</sup> the possible resulting evasion by smaller concerns,<sup>31</sup>

*merce*, Parts I, II and III, 86th Cong., 1st Sess. (1959). On a broader basis, and perhaps with differing ultimate aims, the Senate and House Committees on Government Operations have reported favorably bills establishing a permanent Advisory Commission on Intergovernmental Relations. S. 2026, 86th Cong., 1st Sess. (1959); H.R. 6904, 86th Cong., 1st Sess. (1959); H.R. 6905, 86th Cong., 1st Sess. (1959); see S. Rep. No. 584, 86th Cong., 1st Sess. (1959); H.R. Rep. No. 742, 86th Cong., 1st Sess. (1959); *Joint Hearings Before Committee on Government Operations on H.R. 6904, H.R. 6905 and S. 2026 to Establish an Advisory Committee on Intergovernmental Relations*, 86th Cong., 1st Sess. (1959). These bills provide that the Commission is to "recommend, within the framework of the Constitution, the most desirable allocation of governmental functions and responsibilities among the several levels of Government." S. 2026, 86th Cong., 1st Sess. § 2(6) (1959).

<sup>28</sup> S.J. Res. 113, 86th Cong., 1st Sess. § 101 (1959). The temporary minimum standard was intended to apply with respect to taxable years ending after December 31, 1958, and beginning before January 1, 1961—approximately the period during which the Commission would conduct its study and report to Congress.

<sup>29</sup> Two other bills, S. 2213, 86th Cong., 1st Sess. (1959) and S. 2281, 86th Cong., 1st Sess. (1959), were introduced. In essence these bills, although permanent in nature, utilized the language of the "temporary minimum standard" but did not set up a study commission.

<sup>30</sup> S. Rep. No. 453, 86th Cong., 1st Sess. 2 (1959).

<sup>31</sup> *Id.* at 4.



and, in addition, the waste of tax revenues to the states as well as the federal government.<sup>32</sup> The report states that largely because of differences in apportionment formulae and thirty-five different definitions of what is a sale (a factor in most formulae), there are instances where businesses are taxed "on more than 100 percent of their income."<sup>33</sup> It concludes that the *Northwestern Cement* case opens the door to retroactive assessment of taxes from any prior years, and as a result may impair the financial position of firms likely to be so taxed.<sup>34</sup>

Observing that a uniform apportionment statute is "one of the essential keystones in the final solution of the multi-state taxation problem," the report states that "it [the Select Committee] is not now in a position to draft a satisfactory formula."<sup>35</sup>

The Senate Committee on Finance held hearings on the pending legislation on July 21 and 22, 1959.<sup>36</sup> Thereafter the Finance Committee sponsored S. 2524 which provided that for any taxable year ending after the enactment of the bill no state or subdivision thereof would have power to impose "a net income tax" on the income derived within such state by any person from interstate commerce if the business activities within such state by or on behalf of such person during the taxable year were limited to any or all of the following:

(1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and

(2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective client or customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1); and

(3) the maintenance and operation by such person, or by his representative, in such State of an office the primary purpose and use of which is to serve representatives of such person who are engaged in the solicitation of orders described in paragraphs (1) or (2), or both, and to receive, process, and forward such orders.<sup>37</sup>

<sup>32</sup> *Id.* at 5.

<sup>33</sup> *Ibid.*

<sup>34</sup> *Ibid.*

<sup>35</sup> *Id.* at 11.

<sup>36</sup> *Hearings Before the Senate Finance Committee on S.J. Res. 113, S. 2213 and S. 2281—State Taxation of Interstate Commerce*, 86th Cong., 1st Sess. (1959).

<sup>37</sup> S. 2524, 86th Cong., 1st Sess. §§ 101(a)(1) to (3) (1959). There is no prohibition against taxing a corporation chartered in the taxing state or an individual domiciled or resident in such state, §§ 101(b)(1), (2). However, under § 101(c) a tax may not be imposed merely as a result of sales via an independent contractor.

Thus, under the Finance Committee bill, the *Northwestern Cement* and *Stockham* cases in which the local activity or "nexus" consisted exclusively of maintaining sales offices and soliciting orders in the taxing states would have been overturned.<sup>38</sup> Furthermore, section 103 of the committee bill enlarged the phrase "net income tax" used in section 101 to include "a tax measured by net income," thus extending the prohibition to a variety of taxes other than pure income taxes—for example, a privilege or franchise tax measured by net income, which quite a few states now impose.<sup>39</sup>

Other provisions of S. 2524 prohibited retroactive assessment of a tax on the basis of the activities exempted by the bill. However, the bill did not attempt to affect taxes already collected for prior years or prohibit collection of such taxes where assessed for a taxable year ending on or before the date of the act.

Title II of S. 2524 called for a temporary fourteen-member Commission on State Taxation of Interstate Commerce and Interstate and Intergovernmental Problems, to be made up of three members of the Senate Finance Committee, three members of the House Ways and Means Committee, three officers of the executive branch of the federal government and five members to be appointed by the Conference of Governors.<sup>40</sup> This commission was directed to study "all matters pertaining to the taxation by the States of income" for the purpose of "recommending to the Congress proposed legislation providing uniform standards to be observed by the States in imposing income taxes on income" derived from interstate commerce.<sup>41</sup>

S. 2524, as drafted by the Senate Finance Committee, ran into difficulties when it reached the Senate floor for debate. Fundamentally, the dispute centered around section 101(a)(3) relating to maintenance of an office which, the Chairman of the Committee on Finance frankly conceded, was intended to overrule *Northwestern Cement*. After two days of debate the Senate passed S. 2524 but, as a result of amendment, minus the controversial provision overruling the Supreme Court decision.<sup>42</sup> Although a number of criticisms of S. 2524 were made, the principal arguments against passage were that it was premature and

<sup>38</sup> See S. Rep. No. 658, 86th Cong., 1st Sess. 1, 6-7 (1959).

<sup>39</sup> *Id.* at 1, 5.

<sup>40</sup> S. 2524, 86th Cong., 1st Sess. §§ 101, 202 (1959).

<sup>41</sup> *Id.* at § 203. Detailed instructions to the Commission appear in the bill and the Commission was also directed to study the relation of the federal and state revenue laws so as to eliminate overlaps and competition for revenue and to simplify the laws and improve their administration at all levels of government. This commission would therefore have overlapped the commission contemplated by S. 2026, discussed note 27 *supra*.

<sup>42</sup> 105 Cong. Rec. 15134-36 (daily ed. Aug. 20, 1959). The debate appears at 105 Cong. Rec. 14985, 14987, 14989-15004, 15011-23, (daily ed. Aug. 19, 1959) and 105 Cong. Rec. 15091, 15097-15107, 15108-15, 15121-34 (daily ed. Aug. 20, 1959).

hasty legislation which would adversely affect the states in their fiscal operations.

Meanwhile a number of bills and a joint resolution were introduced in the House. All of the proposed House legislation followed the general pattern of the legislation originally proposed in the Senate; it did not disturb *Northwestern Cement*, and prohibited taxation only where the business maintained no inventory, office, warehouse, etc. in the taxing state.<sup>43</sup> H.R.J. Res. 450 emerged from these proposals and provided for a temporary minimum standard in language virtually the same as section 101 of S.J. Res. 113, quoted at note 28 above. To use the language of the House Report on H.R.J. Res. 450, "In terms of case law, this bill would not affect fact situations such as those in the *Northwestern* and *Stockham* cases. In both of those cases the out-of-State business maintained an office in the market State and under the standard in this bill they would remain subject to taxation."<sup>44</sup>

However, departing from the Senate proposals, H.R.J. Res. 450 did not provide for formation of an independent study commission but provided rather that the Senate and House Judiciary Committees

[S]hall conduct studies and investigations of pertinent State revenue laws and the effect and implications of the Supreme Court decision in *Northwestern States Portland Cement Co. against Minnesota and T. V. Williams*, as State Revenue Commissioner, against *Stockham Valves and Fittings, Inc.* (358 U.S. 450), as well as other decisions in the Federal courts with respect to the authority of States to tax income derived exclusively from interstate commerce and shall report to Congress with their proposals for permanent legislation on or before February 1, 1961.<sup>45</sup>

When the Senate bill, S. 2524, reached the House, the House, which had not yet passed any bill, amended it by striking it in its entirety, and substituting the provisions of H.J. Res. 450. As thus amended, S. 2524 was passed by the House. Out of the resulting conference came the first attempt by Congress in the history of the United States to regulate state taxation of interstate commerce.<sup>46</sup>

The conference measure retained the provisions of title I of S. 2524 as passed by the Senate but adopted title II of the House bill which provides for further study by committees of Congress instead of a specially formed independent commission.

<sup>43</sup> A majority of the bills contained only the permanent prohibition of the tax and did not provide for further study. *E.g.*, H.R. 8019, 86th Cong., 1st Sess. (1959); H.R. 8175, 86th Cong., 1st Sess. (1959); H.R. 8270, 86th Cong., 1st Sess. (1959); H.R. 8389, 86th Cong., 1st Sess. (1959); H.R. 8470, 86th Cong., 1st Sess. (1959). H.R. 8148, 86th Cong., 1st Sess. (1959) and H.R.J. Res. 450, 86th Cong., 1st Sess. (1959) imposed the temporary minimum standard and provided for further study.

<sup>44</sup> H.R. Rep. No. 936, 86th Cong., 1st Sess. 3 (1959).

<sup>45</sup> H.R.J. Res. 450, 86th Cong., 1st Sess. § 201 (1959).

<sup>46</sup> 73 Stat. 555 (1959), 15 U.S.C.A. § 381 (Supp. 1959).

The study presently called for by S. 2524 is limited to state taxes measured by net income. However, some requests have been made that the study be broadened to encompass all state taxes affecting interstate commerce and this pressure might be expected to increase. An examination of the present decisions on all the major forms of state taxation upon interstate commerce will demonstrate the need for a comprehensive approach. Net income taxes are only a small part of the tax maze through which interstate business must wend its way. Judicial control has produced inconsistencies, vacillation and confusion in the whole gambit of taxes, which will perforce continue until we have legislative prescription of a general policy and operating rules.

#### EXISTING CASE LAW

An attempt to synthesize all the Supreme Court decisions pertaining to taxation of interstate commerce would be foredoomed by the Court's inconsistency.<sup>47</sup> The "quagmire" of judicial decisions to which Justice Clark referred in *Northwestern Cement* is too real to permit such an exercise. For present purposes, it will be sufficient to refer briefly to development of what appears to be the current state of the law with respect to application to interstate commerce of various types of state taxes. It is important to consider each tax separately, because some are based on theories of taxation not applicable to others, and the grounds for sustaining or invalidating one tax may not be applicable to another. The failure of the Court to preserve such distinctions has contributed to the confused state of the authorities.

##### 1. *The Drummer Cases*

One of the firm peaks of decisions stated in the *Northwestern Cement Co.* opinion was that "a State 'cannot impose taxes upon persons passing through the state, or coming into it merely for a temporary purpose' such as itinerant drummers. *Robbins v. Taxing District*, 120 U.S. 489, 493-494 (1887)."<sup>48</sup> The itinerant drummer, it seems, has occupied a special niche in the law for almost a century. As Justice Rutledge has pointed out, "the drummer is a figure representative of a by-gone day. But his modern prototype persists under more euphonious appellations. So endure the basic reasons which brought about his protection from the kind of local favoritism which the facts of the case typify."<sup>49</sup> The

<sup>47</sup> In *Memphis Natural Gas Co. v. Stone*, 335 U.S. 80 (1948), the Court, per Mr. Justice Reed, made an elaborate analysis of many of its prior decisions in an attempt to rationalize them. But this opinion clearly demonstrates the difficulty of even a limited survey of the cases.

<sup>48</sup> 358 U.S. at 458.

<sup>49</sup> *Nippert v. City of Richmond*, 327 U.S. 416, 435 (1946). The tax involved was a license tax upon solicitors of orders for goods at the rate of a flat fifty dollars per annum and one-half of one per cent on the gross earnings and commissions of

"more euphonious" name for the modern prototype of the drummer is "traveling salesman," and the basic reasons for the *Robbins* holding that a tax may not be levied on the sale of goods (for example by sample) where the goods are to be delivered from another state has always endured and probably always will. For, like the North Carolina tax invalidated in *Best & Co. v. Maxwell*,<sup>50</sup> the "drummer" taxes normally were intended to and did discriminate against out-of-state suppliers. They were explained as involving discrimination taxes in *McGoldrick v. Berwind-White Coal Mining Co.*,<sup>51</sup> and again in *Best & Co.* Obviously discrimination against traveling salesmen cannot be countenanced.

However, despite explanations in the later cases, the opinions in *Robbins* and many of its progeny were not predicated upon the existence of discrimination against interstate commerce, but rather upon the generalization that the negotiation of contracts for interstate sale of goods was protected from licensing and taxation by the commerce clause; and *Robbins* has been cited for this general proposition in numberless cases in which discrimination was not present, the tax applying to local and interstate activity alike.<sup>52</sup>

For present purposes the interesting aspect of the *Robbins* case is that the drummer there has today been replaced by a group of salesmen whose function and activity are precisely the same as the drummer's. And the taxation of the employer under modern statutes is an extension of the earlier laws, but without any discrimination. The question which gave rise to concern on the part of interstate business and which led to the recent legislation is whether a nondiscriminatory tax on the net income of a business produced by its traveling salesmen would today be sustained by the Court. Later, we indicate that the Court may have been on the verge of holding that systematic solicitation through salesmen, without other presence in the taxing state, was sufficient to support a net income tax upon the employer. So long as the new legisla-

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the drummers in excess of 1,000 dollars. See also *Memphis Steam Laundry v. Stone*, 342 U.S. 389 (1952), invalidating a Mississippi privilege tax upon persons soliciting business for a laundry not licensed in the state.

<sup>50</sup> 311 U.S. 454, 455, n.1 (1940).

<sup>51</sup> 309 U.S. 33 (1940). Even under *Robbins* resident citizens, domestic corporations selling products shipped from out-of-state, and resident agents of nonresident firms have always been taxable in all respects. *Banker Bros. v. Pennsylvania*, 222 U.S. 210 (1911); *Kehrer v. Stewart*, 197 U.S. 60 (1905); *Ficklen v. Shelby County Taxing Dist.*, 145 U.S. 1 (1892). Section 101(b) (1) of the new legislation expressly exempts from its coverage domestic corporations and individuals who are residents of the state. However, a license tax applicable only to sellers of goods manufactured outside the state is discriminatory and unlawful. *Bethlehem Motors Corp. v. Flynt*, 256 U.S. 421 (1921); *Welton v. Missouri*, 91 U.S. 275 (1876).

<sup>52</sup> *E.g.*, *Caldwell v. North Carolina*, 187 U.S. 622 (1903); *Real Silk Hosiery Mills v. City of Portland*, 268 U.S. 325 (1925); *Heyman v. Hays*, 236 U.S. 178 (1915); *Rearick v. Pennsylvania*, 203 U.S. 507 (1906); see also *Norfolk & W. Ry. v. Sims*, 191 U.S. 441 (1903).

lion is in effect, a tax measured by income and predicated solely on solicitation is prohibited. But the legislation has no bearing upon any other type of tax which might be applied to sales activity.

## 2. Taxes on Goods in Commerce: Sales and Use Taxes

Since the *State Freight Tax Case*,<sup>53</sup> state taxation of goods moving in interstate commerce has been prohibited. A nondiscriminatory tax may be levied if the goods either have not begun the interstate journey or have completed it and come to rest in the taxing state. The Court affirmed this rule in another case decided the same day as *Northwestern Cement*.<sup>54</sup> The same rule applies to a state tax on property where there is an interruption in the transit; and where the interruption is not a necessary incident of the transportation, the goods may be taxed.<sup>55</sup>

By the same token taxes on the sale of property brought into a state from another state have been held to be valid even where such goods were thereafter to be used in interstate commerce.<sup>56</sup> And state taxes on the use and storage of gasoline brought into the state and stored there for use in interstate trains and airplanes<sup>57</sup> and similar "use and storage" type taxes have frequently been upheld.<sup>58</sup> However, where the commodity, such as gasoline, has not come to rest in the state, but is purchased in another state for use in interstate commerce through the state, a use tax directly thereon, as distinguished from a charge for using the highways, is invalid.<sup>59</sup>

For a long time it was assumed that a sales tax could not be imposed by the state in which delivery was made where the sale was made pursuant to a contract calling for shipment from another state.<sup>60</sup> But in

<sup>53</sup> *Philadelphia & R.R.R. v. Pennsylvania*, 82 U.S. (15 Wall.) 232 (1873).

<sup>54</sup> *Youngstown Sheet & Tube Co. v. Bowers*, 358 U.S. 534 (1959); see also *Heisler v. Thomas Colliery Co.*, 260 U.S. 245 (1922); *Coe v. Errol*, 116 U.S. 517, 527 (1886); *Brown v. Houston*, 114 U.S. 622 (1885); *Woodruff v. Parham*, 75 U.S. (8 Wall.) 123 (1869).

<sup>55</sup> *Independent Warehouses v. Scheele*, 331 U.S. 70 (1947); *General Oil Co. v. Crain*, 209 U.S. 211 (1908).

<sup>56</sup> *Eastern Air Transp., Inc. v. South Carolina Tax Comm'n*, 285 U.S. 147, 152-53 (1932).

<sup>57</sup> *Edelman v. Boeing Air Transp., Inc.* 289 U.S. 249 (1933); *Nashville, C. & St. L. Ry. v. Wallace*, 288 U.S. 249 (1933).

<sup>58</sup> See, e.g., *Pacific Tel. & Tel. Co. v. Gallagher*, 306 U.S. 182 (1939); *Southern Pacific Co. v. Gallagher*, 306 U.S. 167 (1939); *Monamotor Oil Co. v. Johnson*, 292 U.S. 86 (1934).

<sup>59</sup> *McCarroll v. Dixie Greyhound Lines, Inc.*, 309 U.S. 176 (1940); *Bingaman v. Golden Eagle Western Lines, Inc.*, 297 U.S. 626 (1936); *Helson v. Kentucky*, 279 U.S. 245 (1929).

<sup>60</sup> See *Sonneborn Bros. v. Cureton*, 262 U.S. 506 (1923); *Banker Bros. v. Pennsylvania*, 222 U.S. 210 (1911); *Ware & Leland v. Mobile County*, 209 U.S. 405, 412 (1908). Thus, in *Henneford v. Silas Mason Co.*, 300 U.S. 577, 583 (1937), the Court, speaking of a "compensating tax" imposed on the use of articles imported from other states where the article had not previously been subject to a sales tax, said: "A tax upon a use so closely connected with delivery as to be in substance a part thereof might be subject to the same objections that would be applicable to a tax upon the sale itself."

1940 in *McGoldrick v. Berwind-White Coal Mining Co.*<sup>61</sup> the Court upheld the New York sales tax as applied to coal shipped pursuant to contract from Pennsylvania to New York, where title passed, and said that any "distinction . . . between a tax laid on sales made, without previous contract, after the merchandise has crossed the state boundary, and sales, the contracts for which when made contemplate or require the transportation of merchandise interstate to the taxing state" was unsupported by "reason or authority."<sup>62</sup> Rather, the Court held, the *Robbins* case (on which the distinction was predicated) is "narrowly limited to fixed-sum license taxes imposed on the business of soliciting orders for the purchase of goods to be shipped interstate . . ."<sup>63</sup>

Four years later in *McLeod v. J. E. Dilworth Co.*<sup>64</sup> a divided Court ruled that a sales tax could not be validly imposed on sales which were consummated by acceptance of orders in and shipment of goods from another state in which the title passed.

The Court's original treatment of use taxes followed the premise that interstate sales were not subject to tax. They were upheld on the theory that a use tax was not levied upon the "operations of interstate commerce" but upon the "use after the property is at rest",<sup>65</sup> and they were collected solely from the purchaser or user. Later the Court sustained a requirement that the tax be collected by an extraterritorial vendor. In *General Trading Co. v. State Tax Comm'n*<sup>66</sup> a nonresident seller carrying on no operations in Iowa other than solicitation of orders by traveling salesmen was held liable for collection of an Iowa use tax on goods sold by it to Iowa residents, even though the orders were forwarded for acceptance to Minnesota, where they were filled by direct shipment to Iowa customers. It upheld this use tax on the very day that it invalidated a sales tax upon transactions which were practically identical.<sup>67</sup> Thus in substance the Court permitted the state to collect a sales tax from an extraterritorial vendor if the tax was denominated a use tax.

But ten years later, in *Miller Bros. v. Maryland*,<sup>68</sup> *General Trading Co.* was limited. The Court held that in order for a state to compel

<sup>61</sup> 309 U.S. 33 (1940).

<sup>62</sup> *Id.* at 53-54.

<sup>63</sup> *Id.* at 57.

<sup>64</sup> 322 U.S. 327 (1944). We are not aware of a Supreme Court case dealing specifically with a sales tax imposed by the state of origin on goods to be delivered in another state after title passes. Presumably, such a tax could be invalid as being imposed directly on commerce. Cf. *Heyman v. Hays*, 236 U.S. 178 (1915).

<sup>65</sup> *Henneford v. Silas Mason Co.*, 300 U.S. 577, 582-83 (1937). The Court stressed the fact that such products as had already been subjected to an equal or greater tax were exempted from the use tax.

<sup>66</sup> 322 U.S. 335 (1944).

<sup>67</sup> *McLeod v. J. E. Dilworth Co.*, 322 U.S. 327 (1944).

<sup>68</sup> 347 U.S. 340 (1954).

an out-of-state seller to collect and pay over a use tax, the seller must engage in a regular and "continuous local solicitation" of business in the taxing state. Newspaper advertisements, the Court said, were not sufficient to validate the use tax there involved.

In *Miller Bros.* the Court really was concerned with the question of taxing jurisdiction, which it said was absent for want of "continuous local solicitation" of the type found in *General Trading Co.* It applied a barrier to state taxation of interstate commerce which seemingly is independent of any restrictive effect of the Commerce Clause. The Court's position raises the question whether Congress would have the power under the Commerce Clause to confer a taxing jurisdiction which is otherwise absent. Apparently it is this question of jurisdiction which underlies the Court's reference to the activities of Northwestern Cement Company as providing a sufficient "nexus" with the taxing state. While the Court is far from articulate on this point, it would seem that the question of taxing jurisdiction is now hopelessly intertwined with any discussion of state taxation of interstate commerce.

In all of these sales and use tax cases the activity of the seller in the taxing state was similar to that in *Northwestern Cement*. In each the commerce involved some form of solicitation of orders which were accepted and filled in another state. But the in-state activity was less in *Dilworth*, *General Trading Co.* and *Miller Bros.* because the sellers there did not maintain an office, stock of goods or warehouse in the taxing state, whereas in *Northwestern Cement* the taxpayers had sales offices in the taxing states. Since the lack of an office in the taxing state did not preclude the state from requiring an out-of-state seller to collect and pay it use taxes,<sup>69</sup> where there was systematic solicitation, sufficient to confer taxing jurisdiction, it is quite possible that, except for the new legislation prohibiting it, the Court would uphold an income tax on an interstate business where the activity is merely sufficient to confer taxing jurisdiction. At this point the commerce clause would impose no limitation. But there would remain the uncertainty inherent in judicial definition, on a case-by-case basis, of the kind and volume of activity which would provide taxing jurisdiction.

The fear of Congress that the Supreme Court had reached or would soon reach just this conclusion was one of the clearly expressed reasons for passage of the temporary legislation.<sup>70</sup>

<sup>69</sup> *General Trading Co. v. State Tax Comm'n*, 322 U.S. 335 (1944). In *Felt & Tarrant Mfg. Co. v. Gallagher*, 306 U.S. 62 (1939), *Nelson v. Montgomery Ward & Co.*, 312 U.S. 373 (1941), and *Nelson v. Sears, Roebuck & Co.*, 312 U.S. 359 (1941), the out-of-state seller maintained offices and the use tax was also upheld.

<sup>70</sup> The various reports refer to *International Shoe Co. v. Fontenot*, 359 U.S. 984 (1959), and *Brown-Forman Distillers Corp. v. Collector of Revenue*, 359 U.S. 28 (1959). The Court denied certiorari in the first and dismissed the appeal in the



### 3. *Privilege, License, Occupation or Franchise Taxes*

In *Northwestern Cement* the Court held it to be fundamental that "a State may not lay a tax on the 'privilege' of engaging in interstate commerce, *Spector Motor Service v. O'Connor*, 340 U.S. 602 (1951)."<sup>71</sup>

In *Paul v. Virginia*,<sup>72</sup> decided in 1869, prior to the *State Freight Tax Case*, the Court held that a foreign corporation could do business in a state only upon such terms and conditions as the state "may think proper to impose."<sup>73</sup> This holding was sapped of all vitality in *Leloup v. Port of Mobile*,<sup>74</sup> less than two decades after it had been announced. The Court held that the states may not tax the privilege of engaging in interstate commerce. The inquiry of the Court with regard to the validity of privilege, license, occupation and franchise taxes became whether the privileged activity is local or interstate in character. It could be privileged by a state only if it were "local."

From such an *ad hoc* process it was inevitable that confusion would emerge. In its efforts to restrict these taxes to "local" activities without impairing state revenues, the Court more and more sought ways to separate some part of the interstate business which had a local appearance and sustained the tax wherever the statute and its construction by the state court permitted, as being levied only on that local activity.

With *Western Union Tel. Co. v. Kansas ex rel. Coleman*,<sup>75</sup> the Court began evolving what might be called the "solely intrastate" doctrine. Later in *Sprout v. City of South Bend*,<sup>76</sup> *East Ohio Gas Co. v. Tax Comm'n of Ohio*,<sup>77</sup> and *Cooney v. Mountain States Tel. & Tel. Co.*<sup>78</sup> the doctrine was crystallized into the following test:

latter. In neither case did the taxpayer maintain an office in the taxing state but in both the Louisiana Supreme Court upheld the net income tax involved. These cases will be discussed more completely below.

<sup>71</sup> 358 U.S. at 458.

<sup>72</sup> 75 U.S. (8 Wall.) 168 (1869).

<sup>73</sup> *Id.* at 181.

<sup>74</sup> 127 U.S. 640, 645 (1888). The Court relied in part on a federal statute conferring certain privileges upon the telegraph company. Thereafter in *Crutcher v. Kentucky*, 141 U.S. 47 (1891), the same result was reached sans support of a federal statute. The Court said: "To carry on interstate commerce is not a franchise or privilege granted by the State; it is a right which every citizen of the United States is entitled to exercise under the Constitution and laws of the United States . . ." 141 U.S. at 57.

<sup>75</sup> 216 U.S. 1 (1910). There, because the Kansas tax was upon the total capitalization of the foreign corporation and not on that justly attributable to the state, it was invalidated. Seven years later, in *Looney v. Crane Co.*, 245 U.S. 178 (1917), a similar Texas tax on an Illinois corporation was invalidated where the corporation engaged in its manufacturing operations in its home state but maintained in Texas depots and warehouses from which orders were filled and sales were made.

<sup>76</sup> 277 U.S. 163, 171 (1928).

<sup>77</sup> 283 U.S. 465, 470 (1931).

<sup>78</sup> 294 U.S. 384, 392-93 (1935).

It is elementary that a State can neither lay a tax on the act of engaging in interstate commerce nor on gross receipts therefrom. . . . And, while a State may require payment of an occupation tax by one engaged in both intrastate and interstate commerce, the exaction in order to be valid must be imposed solely on account of the intrastate business without enhancement because of the interstate business done, and it must appear that one engaged exclusively in interstate business would not be subject to the imposition and that the taxpayer could discontinue the intrastate business without withdrawing also from the interstate business.<sup>79</sup>

Many cases invalidate state license or privilege taxes because the impact of the tax is upon an activity too closely related to interstate commerce.<sup>80</sup> For example, in *Ozark Pipe Line Corp. v. Monier*<sup>81</sup> a privilege tax on an oil pipe line doing an exclusively interstate business was invalidated, although the activity (including maintenance of pumping stations in the taxing state) was indistinguishable from that involved in *Coverdale v. Arkansas-Louisiana Pipe Line Co.*<sup>82</sup> and *Memphis Natural Gas Co. v. Stone*.<sup>83</sup> Nor was the occupation tax on operating and maintaining telephone lines and furnishing telephone service struck down in *Cooney v. Mountain States Tel. & Tel. Co.*<sup>84</sup> essentially different from those upheld in those two cases. Likewise, a Massachusetts excise tax on the doing of business in the state where the foreign corporation had an office there for the transaction of interstate business was held unlawful as an attempt to license interstate business in *Alpha Portland Cement Co. v. Massachusetts*,<sup>85</sup> but a New York privilege tax on a British brewery which did no brewing in the state but imported ale and merely maintained branch sales offices located in New York City and Chicago was upheld as valid in *Bass, Ratcliff & Gretton, Ltd. v. State Tax Comm'n.*<sup>86</sup>

<sup>79</sup> *East Ohio Gas Co. v. Tax Comm'n of Ohio*, 283 U.S. 465, 470 (1931).

<sup>80</sup> *Railway Express Agency, Inc. v. Virginia*, 347 U.S. 359 (1954); *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157 (1954); *Spector Motor Serv., Inc. v. O'Connor*, 340 U.S. 602 (1951); *Joseph v. Carter & Weekes Stevedoring Co.*, 330 U.S. 422 (1947); *Puget Sound Stevedoring Co. v. State Tax Comm'n*, 302 U.S. 90 (1937); *Fisher's Blend Station, Inc. v. State Tax Comm'n*, 297 U.S. 650 (1936); *Cudahy Packing Co. v. Hinkle*, 278 U.S. 460 (1929).

<sup>81</sup> 266 U.S. 555 (1925); see also *State Tax Comm'n v. Interstate Natural Gas Co.*, 284 U.S. 41 (1931), holding a privilege tax on a pipe line selling gas transported from another state and sold for resale to be invalid. Compare *Southern Natural Gas Corp. v. Alabama*, 301 U.S. 148 (1937).

<sup>82</sup> 303 U.S. 604 (1938), dealt with at note 87 *infra*.

<sup>83</sup> 335 U.S. 80 (1948), dealt with at note 88 *infra*.

<sup>84</sup> 294 U.S. 384 (1935).

<sup>85</sup> 268 U.S. 203 (1925).

<sup>86</sup> 266 U.S. 271 (1924). Compare *Anglo-Chilean Nitrate Sales Corp. v. Alabama*, 288 U.S. 218 (1933), holding unconstitutional a franchise tax on a foreign corporation whose business in the state included landing and storing as well as selling goods imported by it from abroad. But the same tax was held valid as to an interstate pipeline in *Southern Natural Gas Corp. v. Alabama*, 301 U.S. 148 (1937).

At the same time, while appearing to adhere to early doctrines prohibiting state privilege taxes on interstate commerce, the Court actually sustained many levies on activity which was directly connected with interstate activity. Thus, taxes on the production of mechanical energy in connection with compressing natural gas for interstate transmission;<sup>87</sup> the maintenance of a natural gas pipe line engaged exclusively in interstate commerce;<sup>88</sup> the generation of electricity transmitted immediately and without interruption to another state;<sup>89</sup> and producing natural gas where the gas moved directly and without pause into interstate commerce<sup>90</sup> have all been upheld on the ground that such activities were sufficiently localized or sufficiently severable from non-local activity to permit imposition of the particular tax.

Some cases decided during the period 1910-1935 do not seem to accept the "solely intrastate" test;<sup>91</sup> and a year after the *Cooney* decision Justice Brandeis stated in *Pacific Tel. & Tel. Co. v. Tax Comm'n*<sup>92</sup> that "no decision of this Court lends support to the proposition that an occupation tax upon local business, otherwise valid, must be held void merely because the local and interstate branches are for some reason inseparable."<sup>93</sup>

Notwithstanding inconsistencies in application, what we have chosen to call for convenience the "solely intrastate" doctrine has maintained a very real vitality. One of the latest examples of this doctrine appeared in *Michigan-Louisiana Pipe Line Co. v. Calvert*,<sup>94</sup> where Justice Clark said, "Here it is perhaps sufficient that the privilege taxed, namely the taking of the gas, is not so separate and distinct from interstate transportation as to support the tax."<sup>95</sup>

But another test has been formulated—the multiple burden test—and this is used in combination with the "solely intrastate" test since the lack of separateness between inter- and intrastate commerce more easily leads to multiple taxation. Thus, Justice Reed in *Memphis Natural Gas Co. v. Stone* states:<sup>96</sup>

The cases just cited in the note show that, from the viewpoint of the Commerce Clause, where the corporations carry on a local activity sufficiently separate from the interstate commerce, state

<sup>87</sup> *Coverdale v. Arkansas-Louisiana Pipe Line Co.*, 303 U.S. 604 (1938).

<sup>88</sup> *Memphis Natural Gas Co. v. Stone*, 335 U.S. 80 (1948).

<sup>89</sup> *Utah Power & Light Co. v. Pfost*, 286 U.S. 165 (1932).

<sup>90</sup> *Hope Natural Gas Co. v. Hall*, 274 U.S. 284 (1927).

<sup>91</sup> *Hump Hair Pin Mfg. Co. v. Emmerson*, 258 U.S. 290 (1922); *Kansas City, Ft. S. & M. Ry. v. Botkin*, 240 U.S. 227 (1916); *Baltic Mining Co. v. Massachusetts*, 231 U.S. 68 (1913).

<sup>92</sup> 297 U.S. 403 (1936).

<sup>93</sup> *Id.* at 415.

<sup>94</sup> 347 U.S. 157 (1954).

<sup>95</sup> *Id.* at 170. It was applied to invalidate the Texas tax on the privilege of gathering gas for transmission in interstate commerce.

<sup>96</sup> 335 U.S. 80 (1948).

taxes may be validly laid, even though the exaction from the business of the taxpayer is precisely the same as though the tax had been levied upon the interstate business itself. But the choice of a local incident for the tax, without more, is not enough. There are always convenient local incidents in every interstate operation . . . . The incident selected should be one that does not lend itself to repeated exactions in other states. Otherwise intrastate commerce may be preferred over interstate commerce.<sup>97</sup>

More recently, in the *Calvert* case<sup>98</sup> Justice Clark applied the test in conjunction with the solely intrastate test, stating:

But additional objection is present if the tax be upheld. It would "permit a multiple burden upon that commerce," . . . for if Texas may impose this "first taking" tax measured by the total volume of gas so taken, then Michigan and the other recipient states have at least equal right to tax the first taking or "unloading" from the pipeline of the same gas when it arrives for distribution. Oklahoma might then seek to tax the first taking of the gas as it crossed into that State. The net effect would be substantially to resurrect the customs barriers which the Commerce Clause was designed to eliminate. "The very purpose of the Commerce Clause was to create an area of free trade among the several States. That clause vested the power of taxing a transaction forming an unbroken process of interstate commerce in the Congress, not in the States."<sup>99</sup>

Comments upon the effect of *Northwestern Cement* on this doctrine are reserved for a later point.

In a number of cases, the privilege, occupation or franchise taxes were measured by income or gross receipts. In an early case, *Maine v. Grand Trunk Ry.*,<sup>100</sup> the Court upheld an annual excise tax for the privilege of exercising corporate franchises in Maine as applied to a Canadian railroad engaged in interstate commerce. The tax was upon the railroad's gross receipts allocated to Maine by a track mileage formula. In a throwback to *Paul v. Virginia*,<sup>101</sup> the majority upheld the tax on the following basis:

As the granting of the privilege [of exercising the franchises of a corporation within the state] rests entirely in the discretion of the State, whether the corporation be of domestic or foreign origin, it may be conferred upon such conditions, pecuniary or otherwise, as the State in its judgment may deem most conducive to its interests or policy.<sup>102</sup>

<sup>97</sup> *Id.* at 87.

<sup>98</sup> 347 U.S. 157 (1954).

<sup>99</sup> *Id.* at 170, quoting from *McLeod v. J. E. Dilworth Co.*, 322 U.S. 327, 330-31 (1944).

<sup>100</sup> 142 U.S. 217 (1891).

<sup>101</sup> 75 U.S. (8 Wall.) 168 (1869).

<sup>102</sup> 142 U.S. at 228. This view, of course, is flatly contradictory to *Crutcher v.*

In 1917, however, the Court distinguished *Maine v. Grand Trunk* when it struck down a Pennsylvania mercantile license tax imposed upon all of the gross receipts of a domestic corporation engaged in exporting merchandise to foreign countries.<sup>103</sup> This holding, that an unapportioned privilege, license or franchise tax on the gross receipts of a business engaged in interstate commerce is invalid, has been followed,<sup>104</sup> and a tax of this nature is referred to as a classic example of an unconstitutional tax.<sup>105</sup> Even where a gross receipts privilege tax appears fairly apportioned it recently has been held unconstitutional as to an exclusively interstate business.<sup>106</sup>

Yet, some taxes measured by income or receipts have been sustained although the apportionment formula was questionable. *Bass, Ratcliff & Gretton, Ltd. v. State Tax Comm'n*,<sup>107</sup> a decision cited by the Court in *Northwestern Cement*, involved a New York privilege tax on net income apportioned to New York on the basis of the ratio between the value of specified classes of property in the state to the total value of such property everywhere. Bass was a British corporation which brewed and sold ale. All brewing and a large part of its sales were in England; but some ale was imported and sold through branch offices in New York City and Chicago. Holding the tax valid on the ground that the state was entitled "to attribute to New York a just proportion of the profits earned by the Company from such unitary business," the Court dismissed as irrelevant the contention that, as the corporation had no net income in New York during the year for which the tax was computed, the apportionment formula was arbitrary.

Similar results were reached in *Matson Nav. Co. v. State Bd. of Equalization*<sup>108</sup> and *Butler Bros. v. McColgan*,<sup>109</sup> where a tax by California on the privilege of exercising corporate franchises in the state measured by allocated net income was upheld as applied to a domestic corporation and, in the latter case, to an out-of-state corporation. In *Matson* the state, in addition to taxing intrastate income, attributed to itself 22.2 per cent of income from interstate and foreign commerce, while in *Butler Bros.* standard cost accounting showed that the taxpayer

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Kentucky, quoted note 74 *supra*, decided in the previous term, and *Leloup v. Port of Mobile*, discussed in note 74 *supra*, and this fact was pointed out by the four dissenting Justices.

<sup>103</sup> *Crew Levick Co. v. Pennsylvania*, 245 U.S. 292 (1917).

<sup>104</sup> *Gwin, White & Prince, Inc. v. Henneford*, 305 U.S. 434 (1939); *Fisher's Blend Station, Inc. v. State Tax Comm'n*, 297 U.S. 650 (1936).

<sup>105</sup> See *Railway Express Agency, Inc. v. Virginia*, 347 U.S. 359, 363 (1954), referring to "prohibited taxation of gross receipts from interstate commerce."

<sup>106</sup> *Railway Express Agency, Inc. v. Virginia*, 347 U.S. 359 (1954).

<sup>107</sup> 266 U.S. 271 (1924). Although this is the first "privilege" tax case based on net income of which we are aware, the Court had already upheld taxes imposed directly on net income in prior cases.

<sup>108</sup> 297 U.S. 441 (1936).

<sup>109</sup> 315 U.S. 501 (1942).

sustained a loss in its California operations. In each instance the tax was upheld against challenge grounded on both the commerce and due process clauses.

In *Matson* stress was laid on the fact that the taxpayer was a domestic corporation.<sup>110</sup> But the California tax also was upheld as to a foreign corporation in *Butler Bros.*

In *Spector Motor Service, Inc. v. O'Connor*,<sup>111</sup> the latest net income privilege tax case, the governing factor was stated to be whether the taxpayer is engaged exclusively in interstate commerce or engages in a combination interstate-intrastate operation. If the latter situation obtains, "a state may tax the privilege of carrying on intrastate business and, within reasonable limits, may compute the amount of the charge by applying the tax rate to a fair proportion of the taxpayer's business done within the state, including both interstate and intrastate."<sup>112</sup> In *Spector* a nondiscriminatory, fairly apportioned privilege tax on the net income of an exclusively interstate business was held unconstitutional.

*E T & W N C Transp. Co. v. Currie*,<sup>113</sup> decided by the Court on the authority of *Northwestern Cement*, involved North Carolina's net income tax levied on a purely interstate trucking business identical to that involved in the *Spector* case. When one remembers that *Spector* was cited by Justice Clark in *Northwestern Cement* as one of the "firm peaks of decision" establishing that the states could not tax the privilege of engaging in interstate commerce, the height of the Court's confusion becomes apparent. The contrasting results of *Spector* and *E T & W N C* not only emphasize at once the difficulty of applying a consistent rationalization of the decisions in this field but suggest the possibility of overturning *Spector*. As the law now appears to stand, a state may impose a tax directly on the apportioned net income of a foreign trucking company engaged exclusively in interstate commerce but may not do so if it labels the tax a privilege tax. A similar tax may be collected by calling it a property tax. "One must comprehend, however, the difference between the use of magic words or labels validating an otherwise invalid tax and their use to disable an otherwise constitutional levy. The latter this Court has said may sometimes be done."<sup>114</sup>

<sup>110</sup> "Appellants' franchises, including the right to be corporations empowered to do business in corporate form in accordance with California law, were granted to them by the State, and undoubtedly the State may tax the privilege of exercising the franchises . . . [A] State may tax net income derived from a domestic corporation's business—intrastate, interstate and foreign." 297 U.S. 443-44.

<sup>111</sup> 340 U.S. 602 (1951).

<sup>112</sup> *Id.* at 609-10. At note 6 on page 609 the Court apparently limited the holding in *Memphis Natural Gas Co. v. Beeler*, 315 U.S. 649 (1942), stating that a direct tax on earnings derived wholly from interstate commerce would be invalidated; but as is now clear, that promise has not been fulfilled.

<sup>113</sup> 359 U.S. 28 (1959).

<sup>114</sup> *Railway Express Agency, Inc. v. Virginia*, 358 U.S. 434, 441 (1959).

The difference is sometimes explained on the ground that payment of a privilege tax is a prerequisite to doing business, and the penalty for non-payment is fine and exclusion from the state, while only civil collection procedures are invoked for collection of other taxes. But non-payment of the tax in *Spector* did not result in any attempt by Connecticut to preclude Spector from carrying on its interstate business. From all that appears, the Connecticut "privilege" tax would be collected only via ordinary collection processes. The fact that the consequence of non-payment of what was essentially the same Connecticut tax as that involved in *Spector* would not preclude a protesting taxpayer from continuing to engage in interstate commerce was adverted to as a ground for upholding the tax in *Underwood Typewriter Co. v. Chamberlain*.<sup>115</sup>

Moreover, there is no difference of substance between an unused claim by Connecticut of a right to revoke Spector's privilege of carrying on interstate activities there and North Carolina's right to attachment or distraint against E T & W N C's trucks or facilities to satisfy delinquent taxes. The effect on either company's ability to carry on interstate commerce would be the same, and in either event the ordinary result would be a payment of the tax under protest and suit for its recovery.

In the case of a purely interstate transportation business, however, the Court seems to have established an exception to the general trend of narrowing the immunity of interstate commerce to privilege taxes by construing the tax as levied upon local activities. Local incidents such as gathering up, loading, putting down or unloading of commodities as an integral part of their interstate movement are not adequate grounds for a state privilege or occupation tax.<sup>116</sup> But where a taxpayer is engaged in both interstate and intrastate activity of a non-transportation character, a state may tax the privilege of carrying on the intrastate business and may apply the tax to the total of all of the taxpayer's business, interstate as well as intrastate, which is fairly allocable to the state, and may utilize gross receipts for this purpose.<sup>117</sup> Whether even the transportation industry—buses, trucks, pipelines, airlines—will continue to be so protected depends upon whether the Court adheres to the

<sup>115</sup> 254 U.S. 113 (1920).

<sup>116</sup> *Railway Express Agency, Inc. v. Virginia*, 347 U.S. 359 (1954); *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 347 U.S. 157 (1954); *Spector Motor Serv. v. O'Connor*, 340 U.S. 602 (1951); *Joseph v. Carter & Weekes Stevedoring Co.*, 330 U.S. 422 (1947); *Puget Sound Stevedoring Co. v. State Tax Comm'n*, 302 U.S. 90 (1937); *United Fuel Gas Co. v. Hallanan*, 257 U.S. 277 (1921); see also *Memphis Steam Laundry Cleaner, Inc. v. Stone*, 342 U.S. 389 (1952). Compare *Matson Nav. Co. v. State Bd. of Equalization*, 297 U.S. 441 (1936).

<sup>117</sup> *International Harvester Co. v. Evatt*, 329 U.S. 416 (1947); *Ford Motor Co. v. Beauchamp*, 308 U.S. 331 (1939); *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250 (1938).

distinction repeated in *Northwestern Cement* between privilege and direct income taxes.

The temporary minimum standard imposed by S. 2524 applies to any tax "measured by" net income (section 103) and would, therefore, inhibit a privilege tax so measured. But the temporary restriction upon the states in respect to net income taxation applies only where the sole activity in the state is the solicitation of orders and the transportation industry does not fall in this category.

The study provision of S. 2524 (section 201), read literally, does not appear to contemplate consideration of taxes measured by income as distinguished from taxes directly upon income. While this is obviously subject to change, it is clear that if the Congress should pass a law dealing only with taxes laid directly upon income, the states may be left the opportunity to utilize privilege taxes to impose levies which in the last analysis will be duplicative.

#### 4. Taxes on Gross Receipts

The Supreme Court generally has regarded taxes levied upon acts of interstate commerce irrespective of profit to be more burdensome and therefore even more objectionable than those imposed only where the commerce has produced a profit.<sup>118</sup> As always, it is impossible to say that *no* tax on gross receipts derived wholly from interstate commerce has been sustained, for, as already observed, the Court sustained a privilege tax measured by gross income as applied to a Canadian corporation in *Maine v. Grand Trunk Ry.*,<sup>119</sup> while a similar privilege tax as applied to a Pennsylvania corporation was held invalid in *Crew Levick*.<sup>120</sup> And only seventeen years after *Maine v. Grand Trunk*, in *Galveston, H. & S.A. Ry. v. Texas*,<sup>121</sup> the Court struck down a Texas gross receipts tax modeled upon the Maine tax which it had upheld, because the receipts taxed by Texas were derived in part from interstate commerce. The Court relied upon *Philadelphia & S.S.S. Co. v. Pennsylvania*,<sup>122</sup> in which a gross receipts tax on a domestic steamship company was held invalid because such receipts were obtained from commerce between the states and with foreign nations. The conviction expressed in *Galveston* that a tax "directly" on "receipts from interstate commerce" was inherently bad<sup>123</sup> certainly has no application to net income taxes

<sup>118</sup> See the Court's discussion of this point in *Robbins v. Shelby County Taxing Dist.*, 120 U.S. 489 (1887), and in *United States Glue Co. v. Town of Oak Creek*, 247 U.S. 321 (1918).

<sup>119</sup> *Maine v. Grand Trunk Ry.*, 142 U.S. 217 (1891).

<sup>120</sup> *Crew Levick Co. v. Pennsylvania*, 245 U.S. 292 (1917).

<sup>121</sup> 210 U.S. 217 (1908).

<sup>122</sup> 122 U.S. 326 (1887).

<sup>123</sup> 210 U.S. at 227-28. Justice Harlan dissented on the ground that the state court had called the tax an occupation tax and, accordingly, the tax was not directly upon receipts from commerce.



after *Northwestern Cement*. In *Galveston* Justice Holmes distinguished *Main v. Grand Trunk* on the ground that the Texas tax was not a privilege tax, while Justice Harlan, in dissent, said that the Texas tax was valid because it was a privilege tax. These views are diametrically opposed to the views of the present Court if, as the dictum in *Northwestern Cement* indicates, *Spector* still represents the law. In 1937, in *J. D. Adams Mfg. Co. v. Storen*,<sup>124</sup> the Court struck down an Indiana tax directly on unapportioned gross receipts as applied to a domestic road equipment manufacturer whose sales were eighty per cent in interstate commerce. The same Indiana tax was still later held invalid as applied to the gross receipts of an interstate sale of securities by the trustee of an estate in *Freeman v. Hewit*.<sup>125</sup>

In 1948 New York's unapportioned gross receipts tax was held invalid as applied to the transportation of passengers by Central Greyhound Lines between points in New York, where part of the journey was through other states.<sup>126</sup> However, the Court said that if the tax were apportioned, apparently on the basis of mileage, it would be valid.<sup>127</sup>

### 5. Taxes on Net Income

The discussion of the development of net income taxes in the Court's various opinions in *Northwestern Cement* is so detailed that lengthy analysis here is unwarranted.

*William E. Peck & Co. v. Lowe*<sup>128</sup> upheld a tax on the entire net income of a domestic corporation engaged in purchasing commodities in several states and exporting them, against the contention that the tax was a duty on articles exported from the state forbidden by article I, section 9, clause 5, of the Constitution. The Court compared the tax with levies on gross income, saying:

The words of the act are "net income arising or accruing from all sources." There is no discrimination. At most, exportation is affected only indirectly and remotely. The tax is levied after exportation is completed, after all expenses are paid and losses adjusted, and after the recipient of the income is free to use it as he chooses.<sup>129</sup>

<sup>124</sup> 304 U.S. 307 (1937). The Court distinguished *American Mfg. Co. v. City of St. Louis*, 250 U.S. 459 (1919), where a privilege tax measured by the gross receipts of a local manufacturer was upheld on the ground that the St. Louis tax was for the privilege of engaging in a local manufacturing activity.

<sup>125</sup> 329 U.S. 249 (1946). At page 257 the Court cites a number of unapportioned gross receipts tax cases invalidating such taxes.

<sup>126</sup> *Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653 (1948).

<sup>127</sup> *Id.* at 663-64.

<sup>128</sup> 247 U.S. 165 (1918).

<sup>129</sup> *Id.* at 174-75. It is noteworthy that *Crew Levick Co. v. Pennsylvania*, 245 U.S. 292 (1917), and *Philadelphia & S.S.S. Co. v. Pennsylvania*, 122 U.S. 326 (1887), differ from *Peck v. Lowe* only in the fact that the Pennsylvania tax was on gross receipts.

*United States Glue Co. v. Town of Oak Creek*<sup>180</sup> sustained a direct tax on the net income of a domestic corporation derived from sales of goods outside the taxing state of goods delivered from a factory in such state, and from sales to customers outside the taxing state of goods delivered from sources outside the state. The taxable net income was apportioned on the basis of a formula to ascertain the portion attributable to the taxing state. Again distinguishing gross receipts taxes, the Court said:

The difference in effect between a tax measured by gross receipts and one measured by net income, recognized by our decisions, . . . affords a convenient and workable basis of distinction between a direct and immediate burden upon the business affected and a charge that is only indirect and incidental. A tax upon gross receipts affects each transaction in proportion to its magnitude and irrespective of whether it is profitable or otherwise . . . . A tax upon the net profits has not the same deterrent effect, since it does not arise at all unless a gain is shown over and above expenses and losses, and the tax cannot be heavy unless the profits are large.<sup>181</sup>

The next case approving a direct net income tax was *Memphis Natural Gas Co. v. Beeler*.<sup>182</sup> Memphis, a foreign corporation, was licensed by Tennessee to do business there, managed its business from offices in Tennessee and, according to the Court, had "established a commercial domicile in Tennessee." Citing numerous cases, the Court upheld the tax as follows: "[E]ven if taxpayer's business were wholly interstate commerce, a nondiscriminatory tax by Tennessee upon the net income of a foreign corporation having a commercial domicile there . . . is not prohibited . . . ."<sup>183</sup>

Subsequently in *West Publishing Co. v. McColgan*,<sup>184</sup> in a per curiam order, the Court upheld a California tax on net income of a wholly interstate business. This case furnished the primary basis for the result in *Northwestern Cement*, since West's only activity in the state was selling activity by salesmen who had office space with attorneys. The California court had upheld the tax upon the ground that it was levied directly on net income "as distinguished from a tax on the privilege of engaging in interstate commerce," and the Supreme Court apparently accepted this rationale.<sup>185</sup>

<sup>180</sup> 247 U.S. 321 (1918).

<sup>181</sup> *Id.* at 328-29.

<sup>182</sup> 315 U.S. 649 (1942). While the tax was apparently described in the statute as an excise tax, the state court interpreted it as a direct tax on net income.

<sup>183</sup> 315 U.S. at 656.

<sup>184</sup> 328 U.S. 823 (1946).

<sup>185</sup> See the Court's comment on the *West* case in *Northwestern Cement*. 358 U.S. at 461.

Considered against this setting the 1959 net income tax decisions should not have come as a surprise. In the income tax cases as well as in the cases dealing with other types of state taxes, the area of immunity of interstate commerce from state taxation had been shrinking. Northwestern States Portland Cement Company and Stockham Valves and Fittings Company each maintained offices and permanent personnel in the taxing states and engaged in systematic solicitation of orders there. This was "substantial income-producing activity" the Court held, providing a "sufficient 'nexus'"<sup>136</sup> or "fiscal relation" to the taxing states to warrant subjection of the companies to a net income tax on the portion of net income fairly allocable to the states. Consequently, there was less room for surprise that in *E T & W N C* the income of a trucking company with terminals and permanent employees in North Carolina was held taxable.

The Court's search for a "nexus" or income-producing activity suggests strongly that it is not yet ready to approve a tax on sales only, unaccompanied by some presence. This hesitation is traceable to the confusion noted above between the commerce clause problem and absence of taxing jurisdiction, or due process. It appears certain only that, at the present, intermittent or casual solicitation alone (without offices or permanent personnel, and not on a substantial regular basis) would not be acceptable to the Court as a predicate for a state tax.<sup>137</sup>

On the other hand systematic solicitation of orders through employees or agents, without more, may provide an adequate basis for taxation. Such activity in Louisiana by salesmen employed by International Shoe Company, and the presence of so-called "missionary men" who did not solicit orders but helped wholesalers display the products of Brown-Forman Distillers Corporation, appear to have been the only connection of these companies with Louisiana. But both were held liable by the State Supreme Court for Louisiana's net income tax, and review of both of these cases by the Court was sought but not obtained. Certiorari was denied in *International Shoe Co. v. Fontenot*<sup>138</sup> and the

<sup>136</sup> 358 U.S. at 464, quoting from *Wisconsin v. J. C. Penny Co.*, 311 U.S. 435 (1940). The reference to "nexus" has to do with jurisdiction to impose a tax, a question under the due process clause of the Constitution. The test as stated by the latter case is: "whether the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the state. . . whether the state has given anything for which it can ask a return." 311 U.S. at 444. While we have seen numerous references to the nebulous character of this "nexus" (see, e.g., S. REP. No. 658, 86th Cong., 1st Sess. 2-3 (1959)), we have noted above that this may be a question beyond legislative power. Moreover, even granted the power, a comprehensive and detailed statute could hardly cover the myriads of possible fact situations.

<sup>137</sup> *International Shoe Co. v. Washington*, 326 U.S. 310 (1945).

<sup>138</sup> 359 U.S. 984 (1959). Ordinarily, a denial of certiorari cannot be taken as indicating the Court's view as to the correctness of the decision below, and it would be unwise to depart from this principle in this instance. However, systematic

appeal in *Brown-Forman Distillers Corp. v. Collector of Revenue* was dismissed.<sup>139</sup>

However, the recent sales and use tax opinions<sup>140</sup> and the opinions in all the 1959 cases substantiate the view that solicitation by mail, radio, newspaper or magazine advertisement probably would not support a state tax. S. 2524 certainly precludes state net income taxation where such solicitation, even though systematic, is the only activity in the state. Thus, S. 2524 clearly prohibits the further collection of the tax involved in the *International Shoe* case and would, of course, prevent any tax based upon non-personal solicitation. However, the act is so narrowly drawn as not to affect the state court's decision in *Brown-Forman*, although the taxpayer's activity there was less directly related to sales than the activity in *International Shoe*.<sup>141</sup>

#### 6. *Tangible and Intangible Property Taxes*

Taxes on tangible personal property, as well as real property, located in the taxing jurisdiction are, and have been from time immemorial, recognized as the fundamental avenue by which any sovereign obtains revenues.<sup>142</sup> In modern times taxes on intangible personal property have been added to the state's tax arsenal.<sup>143</sup> As to taxes upon property used in interstate commerce the Supreme Court said in *Postal Tel. Cable Co. v. Adams*:<sup>144</sup>

[P]roperty in a State belonging to a corporation, whether foreign or domestic, engaged in foreign or interstate commerce, may be taxed, or a tax imposed on the corporation on account of its property within a State, and may take the form of a tax for the privilege of exercising its franchises within the State, if the ascertainment of the amount is made dependent in fact on the value of its property situated within the State (the exacting, therefore, not being susceptible of exceeding the sum which might be leviable

solicitation of orders in a state has provided a sufficient basis for requiring foreign corporations to collect and pay to a state use taxes, and on this basis such solicitations would appear to support a net income tax also. See cases cited at notes 68 and 69 *supra*.

<sup>139</sup> 359 U.S. 28 (1959). A review of the record in this case indicates that the appeal was probably dismissed because the monies involved had been allowed by the taxpayer to pass into the general treasury of the state, and under state law it was no longer possible for the taxpayer to recover back the money paid. In such circumstances the Court's opinion, had it rendered a decision, would have been advisory. There is certainly no basis for considering this to be a decision by the United States Supreme Court on the merits.

<sup>140</sup> *Miller Bros. v. Maryland*, 347 U.S. 340 (1954); *McLeod v. Dilworth*, 322 U.S. 327 (1944); *General Trading Co. v. State Tax Comm'n*, 322 U.S. 325 (1944).

<sup>141</sup> Compare *James v. Dravo Contracting Co.*, 302 U.S. 134 (1937).

<sup>142</sup> *Robbins v. Shelby County Taxing Dist.*, 120 U.S. 489 (1887).

<sup>143</sup> See *Atlantic Lumber Co. v. Commissioner*, 298 U.S. 553 (1936).

<sup>144</sup> 155 U.S. 688, 696 (1895); see also *United States Express Co. v. Minnesota*, 223 U.S. 335, 344 (1912); *Atlantic & Pacific Tel. Co. v. Philadelphia*, 190 U.S. 160, 163 (1903).

directly thereon) and if payment be not made a condition precedent to the right to carry on the business, but its enforcement left to the ordinary means devised for the collection of taxes.

Because property taxes have been so generally upheld against attacks based upon the commerce clause, litigants have often used the due process clause as the springboard for challenging state property taxes. It was determined early that property not in the state could not be taxed.<sup>145</sup> As to tangible personal and real property this doctrine goes far toward eliminating multiple taxation.<sup>146</sup> In the case of intangibles such as corporate stock, debts, investments, dividends, and the like, the situs of the property is often uncertain and the danger of double taxation is always present.<sup>147</sup> While taxation of intangibles as a matter of due process undoubtedly has a large bearing on the problems of the burden which multiple state taxation of interstate commerce creates, it requires more detailed consideration than can be given here.<sup>148</sup>

In the property tax cases the problem has been apportionment. The first reference to apportionment appeared in property tax cases. In 1888 Massachusetts was sustained in taxing Western Union on such proportion of its capital stock as the length of the company's lines in Massachusetts bore to the length of lines everywhere.<sup>149</sup> Three years later the Court sustained a tax on the stock of the Pullman Palace Car Company. The portion attributable to Pennsylvania, the taxing state, was determined by the ratio of mileage Pullman cars traveled in Pennsylvania to mileage everywhere,<sup>150</sup> and the apportioned property tax has never since been seriously challenged.

<sup>145</sup> *Union Refrigerator Transit Co. v. Kentucky*, 199 U.S. 194 (1905).

<sup>146</sup> *Cf. Northwest Airlines, Inc. v. Minnesota*, 322 U.S. 292 (1944).

<sup>147</sup> For a time it seemed that the Court would not permit multiple taxation of intangibles. *Farmers Loan & Trust Co. v. Minnesota*, 280 U.S. 204 (1930); *Brown, Multiple Taxation by the States—What Is Left of It?*, 48 HARV. L. REV. 407 (1935). More recently it appears that the Court may find sufficient relationships between intangible property and several states to warrant taxation by each such state and permit multiple taxation, although this is still considered by some to be an open question. See *Wisconsin v. J. C. Penney Co.*, 311 U.S. 435 (1940); *Graves v. Elliott*, 307 U.S. 383 (1939); *Curry v. McCannless*, 307 U.S. 357 (1939).

<sup>148</sup> As will be developed below, the Court has sustained in a commerce clause context property taxes which, by reason of the inclusion of "intangible values" are inflated far beyond what such a tax might produce if applied to the actual physical worth of the property in the taxing state. In response to the argument that "the intangible values" reached by the tax were derived from interstate commerce, the Court announced what it described as the "cardinal rule" in this area: "[W]hatever property is worth for purposes of income and sale it is also worth for purposes of taxation." *Adams Express Co. v. Ohio*, 166 U.S. 185, 220 (1897), *denying rehearings of* 165 U.S. 194 (1897). The Court has repeatedly held that going concern value of property can validly be measured by "fairly apportioned gross receipts." *Railway Express Agency, Inc. v. Virginia*, 358 U.S. 434, 441 (1959), and cases therein cited.

<sup>149</sup> *Western Union Tel. Co. v. Massachusetts*, 125 U.S. 530 (1888).

<sup>150</sup> *Pullman's Palace Car Co. v. Pennsylvania*, 141 U.S. 18 (1891).

Gross receipts from within and without (but fairly apportioned to) the taxing state may be used as a measure of the portion and value of a foreign corporation's property to be taxed, especially where such a tax is "in lieu of" other taxes.<sup>151</sup> All of a domestic corporation's movable or moving property has been held to be taxable by the chartering state. Thus in *Northwest Airlines, Inc. v. Minnesota*,<sup>152</sup> where Minnesota was the "home port" of the company, the Court upheld a tax upon the entire fleet of planes even though other states collected property taxes on portions of the fleet, which touched down in those states. The doctrine of apportionment was said to be inapplicable because the taxing power of the domiciliary state had a different basis than that of a non-domiciliary state. Subsequently, however, in *Standard Oil Co. v. Peck*,<sup>153</sup> an Ohio tax on the full value of the boats and barges of a domiciliary corporation was invalidated even though all of the vessels were registered in Cincinnati, Ohio, as the "home port." The reason given by the Court for its holding was that the tax was not apportioned. Only in the dissent was *Northwest Airlines* cited.

To complete the circle, the Court in 1954, in *Braniff Airways, Inc. v. Nebraska State Bd. of Equalization*,<sup>154</sup> upheld a Nebraska tax on a portion of the aircraft of a foreign corporation whose home port was elsewhere. The amount of property to be taxed was determined on the basis of a three-factor formula using arrivals and departures, revenue tons and operating revenues. *Northwest Airlines* was distinguished but not overruled.

S. 2524 does not appear to affect the property tax cases. It is quite clear, however, that this area should be included in the congressional study and that some attempt should be made to prescribe uniform rules designed to avoid duplicate taxation.

## 7. Miscellaneous Taxes

Obviously there are other kinds of state exactions which we have not discussed specifically but which impose a real burden upon interstate commerce, particularly the transportation industry. Among these are fuel and other types of taxes imposed for the privilege of using the state's roads and state vehicle license and registration fees.<sup>155</sup> These exactions on interstate commerce are not to be confused with general sales and use taxes as applied to fuels, which are discussed elsewhere.

<sup>151</sup> *Railway Express Agency, Inc. v. Virginia*, 358 U.S. 434 (1959), and cases therein cited; see also *United States Express Co. v. Minnesota*, 223 U.S. 335 (1912).

<sup>152</sup> 322 U.S. 292, 295 (1944).

<sup>153</sup> 342 U.S. 382 (1952).

<sup>154</sup> 347 U.S. 590 (1954).

<sup>155</sup> See, e.g., *Capital Greyhound Lines v. Brice*, 339 U.S. 542 (1950); *International Shoe Co. v. Washington*, 326 U.S. 310 (1945).

Rather the miscellaneous taxes are separate taxes which the interstate commerce must also bear and which are frequently doubly burdensome in that an interstate carrier's vehicles are in a particular state only a portion of the time whereas an intrastate competitor may use the roads one hundred per cent of the time for the same fee. However, the classes of state taxes we have discussed provide a sufficient basis upon which to assess the need for congressional action and perhaps also will furnish a basis upon which to consider in its broadest aspects the kind of regulation Congress should undertake.

#### APPORTIONMENT AND THE PROBLEM OF DUPLICATE STATE TAXATION

The Supreme Court has recognized from the outset that it was functioning as the architect not only of federal policy but of the federal system itself in respect of the regulation of the states' taxation of interstate commerce. The Court has in its decisions formulated a whole body of law with no direct constitutional or statutory basis. But the lines of this structure have been cloudy, irregular, incongruous and shifting. In no field of constitutional law has the application of the basic principles been shrouded in more uncertainty.

The reasons are simple. Changes in the personnel of the Court brought different philosophies of federal-state intergovernmental relations to focus in a field vague enough to give them freedom to function. Changes in the nature of commerce and the needs of the states for revenue created new pressures. But the most substantial reason was the negative nature of the judicial process. Without power to prescribe an affirmative pattern, the Court could only pass upon a conglomeration of statutes presented by the various economic and political demands and ingenuities of forty-eight separate governments. Its definition of the limits of state power to tax is essentially a series of negatives. Only Congress can furnish an affirmative. Justice Rutledge once observed:

For cleanly as the commerce clause has worked affirmatively on the whole, its implied negative operation on state power has been uneven, at times highly variable . . . . Into what is thus left open for inference to fill, divergent ideas of meaning may be read much more readily than into what has been made explicit by affirmation. That possibility is broadened immeasurably when not logic alone, but large choices of policy, affected in this instance by evolving experience of federalism, control in giving content to implied negation.<sup>156</sup>

Judicial decisions are made in the context of a single state tax levy so that the validity and impact of the taxes and allocation formulae in other states which may and do result in duplicative or multiple taxation of the

<sup>156</sup> Prudential Life Ins. Co. v. Benjamin, 328 U.S. 408, 418 (1946).

revenues, properties, franchises and sales of interstate businesses—the very thing the Supreme Court has consistently sought to guard against—are not and perhaps cannot be brought to the Court's attention.

The task of protecting an extensive interstate business from disproportionate and duplicate taxes by means of litigation is virtually impossible. In any given state there may be half a dozen different types of taxes: license, privilege, fuel, sales, use, gross receipts, net income, property. Among the states there are variations in the kinds of taxes and in the terms and definitions of any particular type of tax. For example, the Senate Select Committee on Small Business reported that there are thirty-five different definitions of "sale" in the state statutes. In deciding whether a particular tax is valid as imposed upon and apportioned to activity attributable to a particular state, a business must look to the irreconcilable state and federal decisions in litigated cases. The number of different taxes which are imposed by the same state, and the great lack of uniformity among the states in the same type of tax, impose burdens upon persons wishing to engage in interstate commerce which are in fact restrictive. Every large interstate business is confronted with myriads of state taxes and corresponding record-keeping and reporting requirements. These cannot be homogenized into an orderly arrangement. A decision to contest any particular tax must be made not only with the ordinary uncertainties of success but also with the assurance that success probably will engender imposition of a new tax attempting to reach the same business through another channel.

The duplicate or multiple tax is also a very real problem. A domestic corporation, for example, an airline with movable property, may be taxed by the home state on all of its property, and all other states into which such property travels may tax an apportioned share of the same property again.<sup>157</sup> Property taxes may be measured in one state by gross income from all traffic originating and terminating in the state, while other states are free to impose a property tax measured by gross receipts apportioned according to mileage traveled within their borders.<sup>158</sup> Different states may impose both net or gross income taxes on the same concern<sup>159</sup> although even a properly apportioned gross receipts tax may create a burden on commerce since it does not depend upon whether or not the business done in the taxing state is profitable. Sales taxes upon

<sup>157</sup> *Braniff Airways, Inc. v. Nebraska State Bd.*, 347 U.S. 590 (1954); *Northwest Airlines, Inc. v. Minnesota*, 322 U.S. 292 (1944).

<sup>158</sup> *Railway Express Agency, Inc. v. Virginia*, 358 U.S. 434 (1959); *Wisconsin & M. Ry. v. Powers*, 191 U.S. 379 (1903).

<sup>159</sup> *Northwestern States Portland Cement Co. v. Minnesota*, 358 U.S. 450 (1959). Cf. *Western Live Stock v. Bureau of Revenue*, 303 U.S. 250 (1938); *Maine v. Grand Trunk Ry.*, 142 U.S. 217 (1891).



gasoline purchased in one state for use in buses, trucks and airplanes may be repeated in the form of use taxes in the states where it is used.<sup>100</sup>

These illustrations are only some of the possibilities. They suffice to depict the vice of isolated Court decisions without reference to the whole tax framework in which an interstate operator is ensnared.

As the Court itself has recognized, the primary difficulty is that there is no general framework in which to place a particular state tax so as to view it in total perspective and measure the over-all burden it may place upon interstate commerce. But duplicate taxation does not begin and end with the nature of the tax. More difficult is the duplication which arises from the heterogeneous apportionment formulae used by the states. The opinion in *Northwestern Cement* recognizes the broad problem of possible multiple taxation, but then illustrates the weakness of judicial control by voicing a strict rule for meeting this question on a case-by-case basis. Justice Clark states that the Court will not be influenced by multiple taxation as a possibility, but only where it is an existing fact as to the litigant concerned, established clearly by evidence.<sup>101</sup> Yet Justice Clark wrote the opinion in *Michigan-Wisconsin Pipe Line Co. v. Calvert*<sup>102</sup> in which the mere possibility of multiple taxation was assigned as a secondary reason for invalidating a Texas tax on gathering natural gas.

The full import of this language is not clear, but the prospects are disturbing unless the matter is covered by comprehensive legislation. The opinion suggests that a litigant may escape from multiple taxes only by proof that two statutes actually tax the same income from interstate operations, but this places on the taxpayer the burden of choosing for attack that one (or more) of the taxes which has the wrong allocation formula. It suggests further that a tax invalid as to one taxpayer who does business in a state having a conflicting tax may yet be valid as to other taxpayers not doing business in the second state and that these latter then might escape the tax levied by the first upon entering into commerce in the second. Such an approach is intolerable.

Apportionments and formulae for arriving at them go back to a trilogy of cases—*Western Union Tel. Co. v. Massachusetts*,<sup>103</sup> decided in 1888, *Pullman's Palace Car Co. v. Pennsylvania*,<sup>104</sup> and *Maine v. Grand Trunk Ry.*,<sup>105</sup> both decided in 1891. There, by applying a ratio of local mileage to total mileage to the taxpayer's capital stock or income, a figure was derived which was taken to be the equivalent of the taxable

<sup>100</sup> *Bingaman v. Golden Eagle Western Lines, Inc.*, 297 U.S. 626 (1936); *Eastman Air Transp., Inc. v. South Carolina Tax Comm'n*, 285 U.S. 147 (1932).

<sup>101</sup> 358 U.S. at 463.

<sup>102</sup> 347 U.S. 157 (1954).

<sup>103</sup> 125 U.S. 530 (1888).

<sup>104</sup> 141 U.S. 18 (1891).

<sup>105</sup> 142 U.S. 217 (1891).

property or receipts situated within or earned within the taxing state. These were relatively simple formulae and have survived the test of time in property and privilege tax cases as well as income tax cases.<sup>166</sup> However, more complex apportionment formulae were adapted for application to manufacturing and other types of businesses.<sup>167</sup>

Emphasizing either location of property, maintenance of payrolls, or receipts from the consummation of sales, or any combination thereof, multiple-factor formulae emerge as perhaps the most direct avenue to multiple taxation. In large measure, this is because of the so-called "unit rule" that the business of a company in one state contributes to the valuation of its property or activities in another. Thus, in *Adams Express Co. v. Ohio*<sup>168</sup> the Court held that the value of property within a state included its tangible worth and, in addition, a percentage of the value attributable to its interstate activities as a going concern. On this basis, property worth less than 70,000 dollars was valued at more than 500,000 dollars as a result of the ratio of in-state to total mileage. Later, manufacturing and selling businesses were brought within the "unit rule" and allocations which did not produce completely rational results were frequently upheld.<sup>169</sup>

While complete accuracy of apportionment is impossible and has never been required by the Court,<sup>170</sup> the earliest decisions required a formula fair on its face and a reasonable result.<sup>171</sup> The results in some of the later cases are questionable. The Court has permitted taxation of a company by a state where it incurred a loss, on the basis of the assumption that as a unitary operation the company benefited from its unprofitable operations in the state.<sup>172</sup> Similarly, a tax on income of a company was sustained even though nearly a quarter of the income taxed

<sup>166</sup> *Central Greyhound Lines, Inc. v. Mealey*, 334 U.S. 653 (1948) (gross receipts tax); *Wisconsin & M. Ry. v. Powers*, 191 U.S. 379 (1903) (property tax).

<sup>167</sup> *Western Cartridge Co. v. Emmerson*, 281 U.S. 511 (1930); *Hump Hairpin Mfg. Co. v. Emmerson*, 258 U.S. 290 (1922); *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113 (1920).

<sup>168</sup> 165 U.S. 194, *petition for rehearing denied*, 166 U.S. 185 (1897).

<sup>169</sup> For some examples of the application of the unit rule see *Butler Bros. v. McColgan*, 315 U.S. 501 (1942); *Ford Motor Co. v. Beauchamp*, 308 U.S. 331 (1939); *Matson Nav. Co. v. State Bd. of Equalization*, 297 U.S. 441 (1936); *Bass, Ratcliff & Gretton v. State Tax Comm'n*, 266 U.S. 271 (1924); *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113 (1920); *United States Glue Co. v. Town of Oak Creek*, 247 U.S. 321 (1918).

<sup>170</sup> *International Harvester Co. v. Evatt*, 329 U.S. 416, 422-23 (1947); *Norfolk & W. Ry. v. North Carolina ex rel. Maxwell*, 297 U.S. 682, 684-85 (1936), and cases therein cited.

<sup>171</sup> *Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell*, 283 U.S. 123 (1931); *Cudahy Packing Co. v. Hinkle*, 278 U.S. 460 (1929); *Southern Ry. v. Kentucky*, 274 U.S. 76 (1927); *Union Tank Line Co. v. Wright*, 249 U.S. 275 (1919); *Looney v. Crane Co.*, 245 U.S. 178 (1917); *Fargo v. Hart*, 193 U.S. 490 (1904).

<sup>172</sup> *Bass, Ratcliff & Gretton v. State Tax Comm'n*, 266 U.S. 271 (1924); see also *Butler Bros. v. McColgan*, 315 U.S. 501 (1942).

was derived from concededly interstate commerce.<sup>173</sup> In one case<sup>174</sup> the Court sustained an apportionment formula which allocated to the taxing state eight times the actual value of the property located within its borders. By contrast, in an older case where the company introduced evidence to show that only seventeen per cent of its income was derived from activities in North Carolina, an assessment of a tax on eighty-five per cent of the company's income—only five times that earned from sources within the state—was held unlawful.<sup>175</sup>

Others have written on the variety of apportionment formulae presently in vogue and the possible impact of their interplay. There is no need here to go into such detail.<sup>176</sup> A recent study suggests that the older apportionment formulae worked fairly and should be retained, since few corporations contacted in a survey claimed that more than one hundred per cent of their income was taxed as a result of varying apportionment formulae.<sup>177</sup> But the same writers seem to concede that apportionment formulae are now producing duplicate taxation of many businesses engaged in interstate commerce.<sup>178</sup>

The standard needed by commerce would not permit income from out-of-state activity to be taxed merely because it is not presently being taxed in the state where it is earned. To permit such taxation places a premium upon tax aggression, fosters litigation, and penalizes states which seek to attract industry by maintaining a minimal tax structure. An orderly system requires that each state be restricted to taxation of revenues or property properly attributable to it.

#### CONCLUSION: NECESSITY FOR BROAD CONGRESSIONAL LEGISLATION

From the maze of past litigation, some basic considerations cry out for attention in the formulation of a congressional policy for state taxation of interstate business. First, the states' needs for revenue demand that the original purpose of the Constitution be respected by preserving to them the maximum taxing power with respect to interstate commerce that is consistent with development of our economy. Second, an effort should be made to simplify the tax burden by encouraging or requiring uniformity in the kind and the terms of state levies, and by reducing their variety and number. Third, uniform standards should be adopted

<sup>173</sup> *Matson Nav. Co. v. State Bd. of Equalization*, 297 U.S. 441 (1936).

<sup>174</sup> *Ford Motor Co. v. Beauchamp*, 308 U.S. 331 (1939).

<sup>175</sup> *Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell*, 283 U.S. 123 (1931).

<sup>176</sup> See Silverstein, *Problems of Apportionment in Taxation of Multistate Business*, 4 TAX L. REV. 207 (1949).

<sup>177</sup> Studenski and Glasser, *New Threat in State Business Taxation*, Harv. Bus. Rev. Nov.-Dec. 1958, p. 77.

<sup>178</sup> *Ibid.* See also S. Rep. No. 453, 86th Cong., 1st Sess. (1959), which points out that all thirty-five income tax states differ in their interpretation of the word "sale" with the result that two states may tax the same sale.

for allocating to each state its fair share of the total taxable revenue from the interstate enterprise. Such goals cannot be achieved without some rather sharp changes in the present catch-as-catch-can system, nor can they be accomplished if federal regulation is restricted to income taxes.

It would be premature to attempt, before thorough investigation of the views of the state governments and of business, to say that workable legislation must take any specific form. Moreover, as is so often the case, political considerations indicate that changes probably will come slowly. Nevertheless, the stated objectives suggest ultimates that can be posted as a target for thought.

Our consideration suggests as the ultimate target a system which limits state taxation of interstate business to uniform net income and property taxes.

For example, Congress might prescribe as a policy that the states could not impose any tax upon income of an interstate business except a net income tax, that each state must use as a measure of the income to be taxed the net income of the interstate business as determined for federal income tax purposes, that the proportion of that income taxed by any state should be the proportion of gross receipts from sales within the state to the total sales everywhere, that location of a sale should in each case be determined by a uniform rule, and that the tax collected by any state under this formula should not exceed a specified maximum rate. At the same time, Congress could prescribe that states in which the fixed physical assets of an interstate business are located should have the right to impose property taxes on fixed assets, but at rates not to exceed those imposed upon the properties of purely local businesses. The policy would permit the taxation of personal property on an apportioned basis, using either net income (for businesses engaged in manufacturing, selling, etc.) or miles traveled within the state (for transportation businesses such as truck, bus and airline companies). License and privilege taxes and sales and use taxes on interstate transactions should be prohibited.

Beyond question, such legislation presents technical, economic and political problems of great complexity. Perhaps they are too severe to expect any comprehensive legislation in the near future. But the tax problems faced by interstate business are also severe and will continue to grow. Therefore, every effort should be made to induce the Congress to enlarge its study with a view toward legislation that will establish a simpler and more equitable pattern for all state taxes on interstate transactions.