Local Income Taxation

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INTRODUCTION

During the last two decades governmental activity in the United States has expanded greatly at all levels. A recent attempt to catalogue functions performed and services rendered by government produced a list of some 400 items, many of which include sub-activities.[1] The demands made upon local government since the war by the backlog of capital projects and enlarged service requirements have been unprecedented in volume and costliness. An obvious concomitant is the need for additional revenues.

In the scramble for public revenue the position of local government is doubly difficult. Beyond the ever-present economic aspects of taxation, the local unit, as the legal creature of the state, must, by and large, assume public burdens imposed from above and at the same time confine itself to such means of raising revenue as the state makes available. It is a commonplace for a state legislature to impose an additional burden as by requiring a three-platoon in lieu of a two-platoon system in a fire department, without concern over the means of paying the piper.[2]

The problem has been aggravated in a number of states by constitutional limitations upon ad valorem taxation adopted during the depression years. In a state like West Virginia, where the limits are absolute, the effect, as to locally-rendered services, which the community would not suffer to be curtailed, was state assumption of some of the services, state subsidy of others, and a search for new non-property tax local revenues to support the rest.[3] Even in Ohio, where the composite ten mill limitation upon all levies on real property can be exceeded by a local taxing authority with

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[1] Chatters and Hoover, AN INVENTORY OF GOVERNMENTAL ACTIVITIES IN THE UNITED STATES (Municipal Finance Officers Association 1947).

[2] Luhrs v. Phoenix, 52 Ariz. 438, 83 P. 2d 283 (1938); People *ex rel.* Moshier v. Springfield, 370 Ill. 541, 19 N.E. 2d 598 (1939); State *ex rel.* Strain v. Houston, 138 Ohio St. 203, 34 N.E. 2d 219 (1941).

[3] See Sly and Shipman, *Tax Limitation in West Virginia,* in PROPERTY TAX LIMITATION LAWS, 77 *et seq.* (Pub. Admin. Serv. No. 36, 1934).

electoral approval, special voted levies for both debt service on bonds and current expenses have not, in most centers, begun to reflect the increase in cost of local government. Some indication of this is given by the fact that the three Ohio cities between 250,000 and 500,000 population, as of the 1940 census, have the lowest tax rates of the 23 cities in that population group.[4] We are witnessing in Ohio and other states the significant spectacle of the incidence of a mounting local revenue burden being shifted from property despite the demands of the federal and state governments upon other so-called tax sources. Portsmouth, Ohio, represents an interesting cross-current. A Portsmouth income tax ordinance, adopted in 1948, was subjected to referendum by petition backed by organized labor. The city fathers proposed as an alternative an additional ad valorem levy. The voters approved the special levy. Council responded by repealing the income tax ordinance.[5]

Local units other than municipalities have traditionally had little recourse to non-property taxation. Ad valorem levies have been their mainstay. That is still largely the case but there have been significant developments. In the realms of education and welfare one notes heavy state support of local agencies.[6] Counties and townships and various special function units as well have resorted increasingly to direct service charges in such activities as garbage collection. Except for the recent Pennsylvania experience, which is yet to be discussed, power to levy non-property taxes has not, however, been more than sparingly devolved upon such units.

Considering the country as a whole, aid from state and federal governments, resort to service charges and the levying of additional non-property taxes have all figured substantially in the effort to pay for municipal services. With the first two sources of revenue we are not primarily concerned in this paper. It is to be recognized, of course, that the service charge device has important possibilities beyond the so-called public enterprise area. It may be used in connection with such matters as garbage collection. It has the advantage of being keyed directly to benefit and, in the case of public enterprises involving substantial capital outlay, has been employed increasingly as a means of project financing by way of issuing revenue bonds in anticipation of collection of project revenues. While special assessments are employed largely to finance capital im-

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[4] *Tax Rates of American Cities* 1949, 39 NAT. MUN. REV. 17, 23 (1950).

[5] Letter to the writers from Lowell C. Thompson, City Solicitor of Portsmouth, Ohio, dated Nov. 29, 1949. The Portsmouth Income Tax Ordinance was Ordinance No. 81 (1948).

[6] See, *e.g.*, Abraham and Greeley, FEDERAL AND STATE GRANTS IN AID, PART II (Cambridge 1947).

provements, in some states they are used for current operating purposes, such as street cleaning.[7] The use of fees to cover the cost of regulation under the police power has been stretched to the point of providing funds for the general support of government. While it is not easy to document, we are confident that this has not uncommonly been the case with parking meter charges.[8]

The policy implications involved in seeking state and federal aid as against imposing more local taxes are too weighty for adequate consideration in this introductory statement. We do venture to say that there are occasions on which such aid to local government can be strongly supported as a matter of policy. If it be assumed that there is proper national or state interest in the performance of a local function on at least a minimum quantitative and qualitative basis and if there are actually low spots in local ability to meet the expense, the device of federal or state grants in aid does rationally tend to meet the objective. There is such diversity, however, in the bases upon which state funds are allocated to local government that it is difficult to observe any consistent strain of policy.[9] Expediency has played a dominant role in the matter. The grant in aid is more sensitive to local need than a simple tax-sharing program; the latter may channel money into a local unit whose income is already adequate.[10] The former, moreover, may exact matching of funds and, thus, keep local responsibility for fund-raising in the picture.

There is an important body of opinion which supports the thesis that the governmental unit charged with the expenditure of funds should bear the responsibility for raising them. The logic of this is that local units of government should have broader powers of taxation than has been traditionally granted and should, for the most part, be left to the exercise of that authority to raise needed funds. At the time of the present writing the American Municipal Association is waging a battle in favor of municipal resort to admissions taxes. One A.M.A. spokesman has urged that

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[7] OHIO GEN. CODE §§ 3842-3852. For a general discussion see Hillhouse, WHERE CITIES GET THEIR MONEY 152-153 (Municipal Finance Officers Association 1945).

[8] See Hillhouse, *op. cit. supra* note 7 at 89-93. THE MUNICIPAL YEARBOOK 1949, 437-439 (International City Managers Association 1949).

[9] But see, N. Y. STATE FINANCE LAW § 54. This law makes provision for an annual state per capita allocation to each city ($6.75), town ($3.55), and village ($3.00). Each local unit may spend the money as it deems best.

[10] See the analysis of the Ohio situation in A STUDY OF THE TAX AND REVENUE SYSTEM OF THE STATE OF OHIO AND ITS POLITICAL SUBDIVISIONS, Ch. 3 (Report of The Tax Commissioner to The Governor and the 97th General Assembly 1947).

the twenty per centum federal tax be so adjusted that it, plus any municipal levy, would not exceed the present federal rate.[11]

While hard-pressed municipalities have been glad to seize upon admissions and other levies of rather limited revenue potential, there undoubtedly has been, shall we say, poignant yearning for a revenue mainstay other than the general property tax.[12] New York City in 1934 and New Orleans, a few years later, found relief in the retail sales tax. Recently a swarm of California municipalities have had recourse to the sales tax.[13] In other parts of the country, notably Ohio and Pennsylvania, local income taxes now enjoy the spotlight.

THE "PHILADELPHIA STORY"

The pioneer in the field of local income taxation has been the City of Philadelphia.[14] Pennsylvania does not grant constitutional home rule to her municipalities; there is provision, however, for what we may call statutory home rule.[15] In 1932 the legislature, through the adoption of the "Sterling Act," authorized the city council of a city of the first or second class to levy taxes on persons, transactions, occupations, privileges, subjects and personal prop-

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[11] The American Municipal News, March, 1950, 3.

[12] See, for example, the statement of Gilbert Burnett, Director of Law of Louisville, Kentucky:

"We had long ago reached our constitutional limit on *ad valorem* taxes . . . We had tried practically everything. We still could not get along, with increased demands on the city, and the lowered revenue."

"A scientific reassessment is a slow and expensive thing. Possibly basically that is where we ought to go. We tried every character of license tax permitted to us. But we said 'Why bite off these little hunks? Why not go at it whole hog,' and that is what we proceeded to do." MUNICIPALITIES AND THE LAW IN ACTION 45-46 (National Institute of Municipal Law Officers 1949).

Criticism of the general property tax is not a new phenomenon. "The City of Chicago is forced by the State of Illinois, through the Constitution, to exist under an antiquated taxing system. This system, the general property tax, with its principle of so-called uniformity, presses its thorns deeply into only one form of wealth, real estate, and allows larger items of wealth, represented by personal property, to escape. Such a system was long ago outmoded for urban communities." Hodes, LAW AND THE MODERN CITY 21 (1937).

[13] It has been reported that over 120 California municipalities had adopted sales taxes as of Jan. 1, 1949. Campbell, *The Experience of California Cities with the Local Sales Tax*, 23 MICH. MUNIC. REV. 5 (Jan. 1950).

[14] The first Philadelphia Income Tax was ordained by the Philadelphia Ordinance approved Nov. 26, 1938. New York City enacted a local income tax in 1934 which was repealed before it became effective. The rate of this tax was set at 15 per centum of the income tax paid to the federal government. Hillhouse, WHERE CITIES GET THEIR MONEY 107 (Municipal Finance Officers Association 1945). Prior to 1941 Montreal had a local income tax. *Id.* at 108.

[15] PA. CONST. Art. XV, § 1.

erty within the limits of the city not subjected to a state tax or license fee.[16] The authority so conferred upon cities of the second class expired June 1, 1935. Thus, the act, now applies only to Philadelphia, the lone city of the first class. Philadelphia relied on the Act in 1938 in levying a sales tax.[17] Strong opposition of local merchants led to repeal of the ordinance the following year.[18]

It was late in 1938 that Philadelphia first resorted to income taxation by imposing a flat rate one and one-half per centum levy on earned income. The validity of the measure was promptly tested in a taxpayer's suit to enjoin its enforcement. The tax was upheld.[19] In January 1939 the ordinance was repealed.

In December, 1939, a comprehensive earned income tax ordinance was enacted.[20] This ordinance deserves somewhat detailed attention because it has served as a model for Toledo and other income tax cities. The ordinance levied a tax of one and one-half per centum on earned income. It applied to salaries, wages and other compensation, and the net profits from business and other activities of residents and non-residents of Philadelphia. Corporations were excluded. No personal exemptions were allowed, no deductions were allowed against earnings of employed persons and no attempt was made to tax investment income or capital gains.[21] In a key administrative provision collection at the source was provided; employers were required to withhold and account for the tax on salaries and wages. Collection was made a responsibility of the Receiver of Taxes. The ordinance granted him rule-making and certain investigatory powers. It made information gained by a municipal officer or agent under the ordinance confidential and imposed a penalty for disclosure. Enforcement was supported by both civil and penal sanctions. Provision was made for interest and financial penalties to be imposed on delinquent taxpayers and for suit to collect unpaid taxes. Penal sanctions took the form of a fine of $100, enforceable by imprisonment if not paid in ten days, for each violation of the ordinance. The closing sections excluded persons and

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[16] PA. STAT. ANN. tit. 53, § 4613 (Supp. 1949).

[17] Green and Wernick, *The Philadelphia Income and Wage Tax*, in MUNICIPALITIES AND THE LAW IN ACTION 148 (National Institute of Municipal Law Officers 1944).

[18] *Id.*

[19] Butcher v. Philadelphia, 333 Pa. 497, 6 A. 2d 298 (1938). It is interesting to note, however, that the court struck down the $1,000 basic exemption provided by the ordinance on the ground that it was contrary to the Uniformity Clause of the State Constitution. PA. CONST. Art. IX § 1.

[20] Philadelphia Ordinance approved Dec. 13, 1939. (This ordinance will be referred to throughout this article as "Philadelphia Ord.").

[21] Philadelphia Ord. § 2 set the initial rate of the tax and specified those upon whom it was imposed.

property beyond the council's power to tax and ordained separability.

The rate of the tax was reduced to one per centum after a time to adjust it to revenue needs. In December, 1949, it was fixed at one and one-quarter per centum.[22] It has been an extremely effective revenue-producer. Responsible authority has gone so far as to declare unequivocally that the tax saved the city from bankruptcy.[23]

Administration of the Philadelphia ordinance has called for hundreds of rulings by the city solicitor and much revising and refining of the administrative regulations.[24] The measure has, moreover, been subjected to very thorough scrutiny by the courts in a series of cases. Down to this year the city had successfully beaten off all substantial attacks upon the levy as an impost upon earned income. Recently, however, the city has met with serious reverses in attempting first to apply the earnings tax to investment income and capital gains on the theory that the taxpayer was engaging in business in producing this income[25] and later in attempting, by express amendment, to extend the application of the ordinance to all income not included within the meaning of "earned income."[26] All that need be added at this juncture with respect to these cases is that the state supreme court has interpreted that provision of the Sterling Act which excludes municipal taxation of "a privilege, transaction, subject or occupation or . . . personal property which is now or may hereafter become subject to a State tax or license fee"[27] very strictly against the city. The effect appears to be to confine the Philadelphia income tax largely to earned income. More particular reference will be made to these recent cases as well as the other Philadelphia income tax decisions at appropriate points in the discussion which follows.

In 1947 the Pennsylvania General Assembly adopted the famous Act No. 481, which extended to 3,600 of the 5,200 local units in the commonwealth substantially the same broad powers of taxation devolved by the Sterling Act upon Philadelphia.[28] Over 800 of the

[22] The provision fixing the tax at one and one-quarter per centum was upheld in Murray v. Philadelphia, 71 A. 2d 280, 289 (Pa. 1950).

[23] ACT. 481: ITS FIRST TWO YEARS OF OPERATION 25 (Bureau of Municipal Affairs, Department of Internal Affairs of Pennsylvania 1949).

[24] Hillhouse, WHERE CITIES GET THEIR MONEY 105 (Municipal Finance Officers Association 1945).

[25] Breitinger v. Philadelphia, 363 Pa. 512, 70 A. 2d 640 (1950); Murray v. Philadelphia, 363 Pa. 524, 70 A. 2d 647 (1950).

[26] Philadelphia Ordinance approved Dec. 9, 1949, was invalidated, except as to the provision increasing the tax rate (see note 22 *supra*), in Murray v. Philadelphia, 71 A. 2d 280 (Pa. 1950).

[27] PA. STAT. ANN. tit. 53, § 4613 (Supp. 1949).

[28] PA. STAT. ANN. tit. 53, § 2015.1 *et seq.* (Supp. 1949) is Act 481 of 1947, Pamphlet Laws 1145, as amended.

3,600 eligible units have imposed in excess of 1,000 taxes under the act,[29] but, of these, nearly 200 (largely school districts) levied severance taxes on the mining of coal,[30] a form of tax now expressly denied them by a 1949 amendment to the act.[31] Apart from severance taxes, the bulk of the levies under the act have been (1) admissions taxes, (2) per capita levies, (3) mercantile license taxes on retailers and wholesalers measured by gross receipts, (4) taxes on mechanical amusement devices, (5) deed transfer taxes and (6) income taxes.[32] Nearly 200 units, including a few cities, boroughs and townships and many school districts, have levied flat rate income taxes.[33] Thus exercise of the power devolved has not been vagrant. Whether the act heralds a new day in state-local relationships is a question we shall pretermit for the moment.[34]

Following the lead of Philadelphia, six Ohio cities have levied income taxes.[35] Louisville, Kentucky, has a so-called occupational license tax measured in terms of wages, salaries or business net profits.[36] St. Louis has an earnings tax[37] based upon an express statutory grant of power made after a broad home rule charter provision on taxation was declared to fall short of authorizing in-

[29] ACT 481: ITS FIRST TWO YEARS OF OPERATION 2 (Bureau of Municipal Affairs, Department of Internal Affairs of Pennsylvania 1949); TAXES LEVIED UNDER ACT 481, SUPPLEMENT—FEB. 1, 1949 TO NOV. 15, 1949 2 (Bureau of Municipal Affairs, Department of Internal Affairs of Pennsylvania 1949).

[30] ACT 481: ITS FIRST TWO YEARS OF OPERATION 3 (Bureau of Municipal Affairs, Department of Internal Affairs of Pennsylvania 1949).

[31] Pa. Act 246 of 1949, Pamphlet Laws 898, PA. STAT. ANN. tit. 53, § 2015.1 *et seq.* (Supp. 1949). There has been evidence of judicial antipathy to severance taxes since the decision in English v. School District of Robinson Township, 358 Pa. 45, 55 A. 2d 803 (1947) which upheld the validity of Act 481. For a discussion of the later cases see Rose, *Pennsylvania's Experiment in Home Rule Taxation as it Affected the Coal Industry*, 11 U. OF PITTS. L. REV. 228 (1950).

[32] ACT 481: ITS FIRST TWO YEARS OF OPERATION 4, 5 (Bureau of Municipal Affairs, Department of Internal Affairs of Pennsylvania 1949).

[33] *Id.* at 4.

[34] The Pennsylvania Bureau of Municipal Affairs has taken a very *favorable* view as to the statute. *Id.* at 1, 25.

[35] Columbus Ord. No. 658 (1947); Dayton Ord. No. 16614 (1949); Springfield Ord. No. 4741 (1948); Toledo Ord. No. 18 (1946); Warren Ord. No. 3839 (1949); Youngstown Ord. No. 49349 (1948). (In these footnotes the local income tax ordinances will be identified hereafter by reference to the name of the local unit after the ordinance citation has been given once.)

Portsmouth Ord. No. 81 (1948) was repealed before it became effective. See note 5 *supra*. The City of Garfield Heights, Ohio, does not levy an income tax even though it is listed as a city which does levy such a tax in THE MUNICIPAL YEAR BOOK 202 (International City Managers' Association 1949). Letter to the writers from Joseph L. Zelazny, City solicitor of Garfield Heights, Ohio, dated Dec. 5, 1949.

[36] Louisville Ord. No. 112 (1948) as amended by Ord. No. 165 (1948) and by Ord. No. 6 (1949).

[37] St. Louis Ord. No. 44678 (1948).

come taxation.[38] A Portland, Oregon, ordinance levying a license tax akin to that of Louisville was defeated on referendum at the May 1950 primary.[39] A proposed amendment to the home rule charter of the City of Minneapolis, which, significantly enough, would have authorized a graduated income tax was lost by a tie vote in Council in 1948.[40]

Home Rule Power in Ohio—The Preemption Doctrine

In Ohio we must look first to the home rule amendment of the state constitution as a possible source of municipal authority to impose income taxes. It is clear enough that so far as counties and other non-municipal types of local units are concerned there is no direct constitutional grant of power to levy taxes of this character and appropriate enabling legislation has not been enacted.

It should be observed at once that the Ohio cases down to 1948 have been very ably discussed in a previous number of this *Journal* by C. Emory Glander and Addison E. Dewey.[41] They will be re-examined here only to the extent necessary to give the reader the general picture and to permit of expression of certain views, which differ from those of the authors of the previous article.

Article XVIII of the Constitution of Ohio, popularly known as the municipal home rule amendment, by Section 3 confers upon municipalities "authority to exercise all powers of local self-government and to adopt and enforce within their limits such local police, sanitary and other similar regulations, as are not in conflict with general laws." While there is substantial basis, as an original matter, for interpreting the qualifying clause, which appears at the end of this Section, to modify both grants of power made by the Section,[42] the settled interpretation is that the clause qualifies only the second grant of power.[43]

When the home rule amendment was adopted in 1912, there was already to be found in the constitution a provision command-

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[38] Mo. Rev. Stat. Ann., §§ 7780.4-7780.12 (Supp. 1949) constitutes express provision for St. Louis to levy its tax. The abortive tax levied under the St. Louis Charter provision was invalidated in Carter Carburetor Corp. v. St. Louis, 356 Mo. 646, 203 S.W. 2d 438 (1947).

[39] The [Portland] Oregonian, May 22, 1950, Sec. 2, Page 10, Col. 3, reports the final vote at 31,840 for and 85,241 against the proposal.

[40] Letter to the writers from John F. Bonner, City Attorney of Minneapolis, Minnesota, dated December 9, 1949.

[41] Glander and Dewey, *Municipal Taxation: A Study of the Pre-emption* Doctrine, 9 Ohio St. L. J. 72 (1948).

[42] See the discussion of this matter in Fordham and Asher, *Home Rule Powers in Theory and Practice*, 9 Ohio St. L.J. 18, 23-25 (1948).

[43] See State *ex rel.* Arey v. Sherrill, 142 Ohio St. 574, 578-579, 53 N.E. 2d 501, 504 (1944).

ing the General Assembly to restrict the power of municipalities to levy taxes, impose assessments, borrow money, contract debts and lend credit.[44] The draftsmen of Article XVIII evidently thought that the positive grants of power in Article XVIII might be deemed unaffected by the older restrictive provision, for they expressly wrote into the home rule amendment a Section 13 which authorizes the legislature to pass laws to limit the power of municipalities to levy taxes and incur debts for local purposes. If the mandate of the earlier restrictive provision had been expected to survive the adoption of Article XVIII, what would have been the occasion for including in Article XVIII a permissive section simply conferring power upon the General Assembly to limit municipal tax levies? This point has not been rationalized in the cases; it has simply been held, without explanation, that Article XVIII did not repeal by implication the earlier restrictive section.[45]

The first case in which the state supreme court was called upon to decide whether municipalities have home rule power to levy non-property taxes reached the court in 1919.[46] The question presented was whether Cincinnati had authority to impose occupational excises upon persons pursuing osteopathy and various other occupations. There was no similar state tax. The court upheld the levy. The opinion did not provide a clear explanation for the result. At one point it was broadly laid down that, apart from the provisions of Section 13 of Article XVIII, the home rule grant in Section 3 of Article XVIII conferred upon municipalities as complete taxing power as the General Assembly had received under the broad grant of legislative power made by Section 1 of Article II of the Constitution. Here the court signfiicantly pointed out that the grant of all powers of local self-government would be an empty affair unless it embraced the power of taxation. A little further on, however, the opinion intimates that the legislature might impliedly limit municipal taxing power by invading a particular field of taxation itself. The opinion closed with a pronouncement that unless and until the state itself invaded the field or expressly interdicted the exercise of the power, the authority of a municipality to utilize subjects of taxation as in that case must be upheld. Since the state had not imposed a tax on occupations the reference in the opinion to limitation by implication was *obiter*. It was unfortunate, however, that once having referred to it the court did not explain why the mere levy of a similar state tax would necessarily constitute a

[44] OHIO CONST. Art. XIII, § 6.

[45] State *ex rel.* Osborne v. Williams, 111 Ohio St. 400, 145 N.E. 542 (1924); Berry v. Columbus, 104 Ohio St. 607, 136 N.E. 824 (1922); State *ex rel.* Toledo v. Cooper, 97 Ohio St. 86, 119 N.E. 253 (1917).

[46] State *ex rel.* Zielonka v. Carrel, 99 Ohio St. 220, 124 N.E. 134 (1919).

limitation by implication upon municipal taxing power.

It is not too clear whether the court was suggesting that the restriction by implication would be based on an interpretation of the state tax statute or would be explained as a limitation implicit in the very home rule grant of taxing power. The language used seems to be a little more suggestive of the former, although we are not told how it is that a state tax statute can be said to interdict municipal taxation when all it does as a matter of positive enactment is impose a state levy without any mention of municipal taxation.

We find it very interesting that in the first case in which the incipient preemption doctrine was actually applied the supreme court did not proceed on the theory that the state tax law was to be interpreted as limiting municipal taxation, but embraced the theory that the taxing power conferred by the home rule grant simply did not extend to any field of taxation occupied by the state.[47] There was no mention of Section 6 of Article XIII or Section 13 of Article XVIII. The rationalization of the decision is largely embodied in the statement that the state should be deemed to have preempted the field "to the end that the sovereignty of the state may be superior to that of any of its subdivisions in a matter so essential to that sovereignty as that of taxation."[48] This, we suggest, is a highly vulnerable rationalization. It is by way of saying that the court is interposing to preserve state supremacy even though the legislature has two independent provisions of the constitution upon which it could draw to achieve that objective. Certainly the legislature would not be without strings to its bow if either the mandate of Section 6 of Article XIII to "restrict" municipal taxing power or the permissive authority of Section 13 of Article XVIII to "limit" municipal power to levy taxes is broad enough to enable the General Assembly substantially to forbid or interdict municipal taxation in this or that field.

There has been little discussion of the content of the words "restrict" and "limit" as used in these provisions of the constitution. It is clear enough that legislative control is not confined to ad valorem taxes. Property tax limitations are spelled out in the taxation article of the constitution.[49] It would be anomalous, moreover, to accord the express reference to "taxation" and "taxes" in the limitation sections a narrower application than the power to tax drawn from the general grant of home rule power.

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[47] Cincinnati v. American Telephone and Telegraph Co., 112 Ohio St. 493, 147 N.E. 806 (1925).

[48] *Id.* at 499, 147 N.E. at 808.

[49] OHIO CONST. Art. XII, § 2.

Do the terms "restrict" and "limit" refer to the placing of ceilings on rates or amounts or do they embrace the idea of prohibition or exclusion? In the initial home rule non-property tax case the question was mentioned but there was, of course, no occasion for a judicial commitment on the point.[50] The later cases simply take it for granted that the second meaning is the true one and offer no explanation. In ordinary usage both "restrict" and "limit" are relative terms;[51] here they are given an absolute quality. The General Assembly on this basis may expressly deny any form of taxation, with the possible exception of property levies, to a municipality. The logical extreme of this is the negation of home rule power to tax, since if the legislature may deny a city or village one form of taxation it may proscribe another.

Hardly a month after the court embraced the theory that the concept of state preemption was an implicit limitation in the home rule grant,[52] Section 13 of Article XVIII was invoked and limitation by implication applied.[53] The City of Cambridge had imposed a "license fee" on the owner of a motor vehicle of one-fourth of the state excise tax and provided that the net proceeds be used for street maintenance. The state tax law required half of the receipts of the state tax to be returned to the municipality of origin for street repair purposes. It will, thus, be seen that there was present in this case the additional factor of state tax-sharing with municipalities. Whether that makes a substantially stronger case for implying a limitation is a point which we shall reserve for the moment. What strikes us as especially noteworthy about the case is the early and unexplained shift in theory.

Questions were bound to arise as to whether an existing state tax actually covered the same area as a municipality proposed to occupy. It is easy to perceive that questions of this character are likely to lead us into an inquiry into the economic incidence of state and municipal taxes. This type of problem was first presented to the supreme court in 1931.[54] The case, however, was one where legal form rather than economic burden governed. The state, of

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[50] State *ex rel.* Zielonka v. Carrel, 99 Ohio St. 220, 228, 124 N.E. 134, 136 (1919). State *ex rel.* Toledo v. Cooper, 97 Ohio St. 86, 119 N.E. 253 (1917) related to home rule power to levy property taxes; the *Carrel* case was the first involving non-property taxation under the Home Rule Amendment.

[51] WEBSTER'S INTERNATIONAL DICTIONARY (2d Ed. 1948) defines "restrict" in part as follows: "1. To restrain within bounds; to limit; to confine; as, to *restrict* words to a particular meaning . . ." The same work defines "limit" in part as follows: "2. To apply a limit to, or set a limit or bounds for. . ."

[52] See note 47 *supra.*

[53] Firestone v. City of Cambridge, 113 Ohio St. 57, 148 N.E. 470 (1925).

[54] Cincinnati v. Oil Works Co., 123 Ohio St. 448, 175 N.E. 699 (1931).

course, had a gasoline tax. The City of Cincinnati adopted an ordinance imposing an occupational excise of $100 per year upon operators of gasoline filling stations in the city. The city insisted that the gasoline tax was actually imposed upon the consumer; it certainly was passed on to him in economic fact. The court, however, interpreted the gasoline tax statute to impose the tax upon the seller, that is, the filling station operator, and it accordingly held that the state had preempted the field to the exclusion of the municipal tax. It will be seen that it was considered enough to establish peemption that the gasoline tax was technically imposed on the dealer, although it was obvious that he would pass it on to the consumer and that the city license covered activity beyond selling gasoline. Whether the dealer could effectively shift the burden of the municipal excise was an entirely different matter. The marked difference in the measure of the two taxes is obvious.

Fifteen years later the court had before it a case in which the respective state and municipal taxes were clearly imposed on different subjects of taxation and different taxpayers but the measure was substantially the same.[55] The state sales tax expressly exempted sales by public utilities of utility services and commodities but applied to their sales of merchandise and appliances. At the same time, the three per centum state tax on the gross receipts of public utilities excepted receipts from sales which were subject to the sales tax. In other words, those two state taxes were integrated. The City of Youngstown came along and adopted a tax ordinance which imposed a tax of two and one-half per centum on the net rate charged for natural gas, electrical energy, water and local telephone service and equipment furnished in the city. The ordinance required that the tax be added to the consumer's bill and the amount collected along with the charges for service. The pertinent statutes provided that substantial portions of both the sales tax and gross receipts tax on public utilities be allocated to municipalities. Again the preemption doctrine prevailed and the municipality went empty-handed. The court was impressed by the legislative design to avoid "double taxation" of gross utility receipts, whether from ordinary utility service and commodities or from merchandise and appliances. This, it was thought, warranted the inference that the General Assembly was, by a combination of sales and gross receipts taxes, preempting the field. It was not considered necessary to explain that preemption occurred notwithstanding the fact that the sales tax was imposed on the consumer whereas the gross receipts tax was imposed upon the utility. It was apparently deemed

[55] Haefner v. City of Youngstown, 147 Ohio St. 58, 68 N. E. 2d 65 (1946).

enough that the taxes were "similar," that each was measured by gross receipts. Nothing was said as to whether, as an economic fact, the gross receipts tax was passed on to the consumer.

The *Youngstown* case[56] did not clarify the preemption doctrine although it assuredly extended its application. About the only concession which had been made to municipal autonomy down to the time of that decision was a ruling, not previously mentioned herein, to the effect that a state charge imposed as an incident to a regulation under the police power and not to produce revenue for the support of government is not enough to constitute state preemption.[57] Apart from this, it would appear that no matter how nominal a state tax it will be deemed automatically to exclude municipal taxation on the same person and technical tax bases, and even of municipal taxes not technically imposed on the same persons and subjects if they be measured by the same economic factors. Thus, in the *Youngstown* case, the state gross receipts tax was imposed on public utilities and the subject of the tax was the privilege of doing business; gross receipts were the measure of the tax. Under the city tax the consumer was the taxpayer and the privilege of buying and using utility service and commodities was the subject of the tax. The measure of the tax, however, was, in effect, the same as that employed in the state levy.

If similarity in the measure of state and municipal taxes is to be enough to ground preemption that alone would serve to becloud municipal taxation of the income from intangibles since the state property tax on productive intangibles is measured by reference to their income yield.[58] Yet, in theory at least, the state levy is clearly a property tax.

The intangibles tax situation suggests another problem. Suppose, instead of covering a so-called field of taxation, whether heavily or lightly, the state merely camps on a part of the area as by taxing income from investments but not earned income. Should this be deemed to exclude local taxation of earned income? Surely "preemption" does not carry so far as to preclude the local levy.

Messrs. Glander and Dewey's study of the preemption doctrine led them to the conclusion that the decisions employing it have

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[56] The *Youngstown* case referred to throughout this article is the case cited in note 55 *supra*.

[57] Loan Co. v. Carrel, 106 Ohio St. 43, 138 N. E. 364 (1922).

[58] OHIO GEN. CODE §§ 5323, 5388, 5389. *See* Angell v. Toledo, 153 Ohio St. 179, 186-187, 91 N.E. 2d 250, 253-254 (1950) (concurring opinion) for an able discussion of this problem by Taft, J. See, a STUDY OF THE TAX AND REVENUE SYSTEM OF THE STATE OF OHIO AND ITS POLITICAL SUBDIVISION 19-21 (Report of The Tax Commissioner of Ohio to The Governor and The 97th General Assembly 1947) for a summary of the state tax on intangible personal property.

been eminently correct.[59] They were content to insist that the General Assembly may by express provision permit municipal taxation in an area occupied by the state.[60] It is not evident that there could be any serious question about the latter proposition. The preemption doctrine itself, however, is another matter. What it does, we suggest, is turn the constitutional pattern around.[61] The constitution grants municipal taxing power subject to legislative limitation; the preemption doctrine denies municipalities access to all non-property forms of taxation employed by the state unless the legislature expressly opens the door to them.

Both theories employed in the cases are vulnerable. It is not necessary to labor what has already been said about the implicit limitation theory, which is dedicated to the cause of maintaining state supremacy. The express legislative power of limitation appears adequate for that purpose. This much may be added—while it is not lightly to be supposed that the people would give local units taxing power co-eval with that of the state government there is nothing in the nature of things to preclude their doing so. It is not to be forgotten that we are talking about a constitutional grant of municipal home rule.

The other theory must be supported, if at all, as a matter of statutory interpretation, since it stems from the constitutional provisions empowering the legislature to limit municipal taxation. The legislature, let us say, imposes an admission tax in order to raise funds to meet current expenses of the state government. The statute makes no mention of municipal taxation. Certainly the prime concern is the positive objective of financing state business. On what basis can it realistically be said that the statute does more, that it is also a law to limit municipal taxation? What intrinsic or extrinsic aid to interpretation points toward such a secondary purpose? Raising state revenues is one thing, limiting municipal taxation to prevent abuse and effect coordination with the over-all revenue system of the state is another. It seems scarcely more farfetched to say that here are two subjects which should be dealt

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[59] Glander and Dewey, *Municipal Taxation: A Study of the Pre-emption Doctrine*, 9 OHIO ST. L.J. 72, 88, 89 (1948).

[60] *Id.* at 89, 90.

[61] Professor Knight, one of the delegates to the Ohio Constitutional Convention of 1912 who contributed most to the content of the Home Rule Amendment, pointed out in the Convention that it was desired to reverse the rule that municipalities have only those powers granted by the legislature, so that by direct constitutional grant they would have the power to do things which were not denied to them. 2 PROCEEDINGS AND DEBATES, OHIO CONSTITUTIONAL CONVENTION 1433 (1912). For an analysis of the action of the Convention in regard to the Home Rule Amendment see Fordham and Asher, *Home Rule Powers in Theory and Practice*, 9 OHIO ST. L.J. 18, 19-24 (1948).

with by separate statutes in view of the single subject matter clause of the constitution,[62] than to interpret the hypothetical amusement tax statute to preclude a municipal amusement tax.

A statute levying a tax goes into effect immediately and is not subject to referendum.[63] A law authorizing or limiting local taxation is subject to referendum and cannot take effect until the expiration of 90 days after filing in the office of the Secretary of State.[64] If a statute levying a state tax contained express provisions limiting local taxation would not the latter be subject to referendum?[65] If they would, does not the preemption doctrine have the effect of imposing immediate limitations on municipalities without fear of referendum—something that could not be done by express enactment? If there is any force in these points, they provide an additional basis for questioning the preemption doctrine.

The bugaboo of double taxation is not at all alarming. Is it double taxation, in the first place, for local, state and national governments to tap the same revenue source, each for its own purposes? The term will have more content if we confine it to cases where one government digs a second time into particular taxpayer pockets for the same purposes. Even if we choose to label concurrent state and local taxation of the same subject "double taxation" that does not, *per se*, confront us with legal questions. The same property may be subject to ad valorem taxation by a plethora of overlapping units of government. Almost equally commonplace is non-property taxation of a subject by a number of independent levying authorities. If, as a matter of policy, the General Assembly of Ohio should choose to minimize this sort of thing it would have the authority to do so, and that without benefit of the preemption doctrine.

In the *Youngstown* case emphasis was laid upon the legislative intent to avoid double taxation of utility receipts. That there was a design to avoid simultaneous sales and gross receipts taxation by the state measured by the same gross receipts was evident. That is a substantial objective in itself. The fact that not a word was said about municipal taxation provides a much more compelling basis for concluding that it was unaffected than the levy of integrated state taxes affords for determining that municipal taxation is banned.

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[62] OHIO CONST. Art. II, § 16.

[63] OHIO CONST. Art. II § 1d.

[64] State *ex rel.* Keller v. Forney, 108 Ohio St. 463, 141 N.E. 16 (1923).

[65] OHIO CONST. Art. II § 1g requires any initiative, supplementary or referendum petition to be presented in such a manner that there may be a separate affirmative or negative note on each section. It is apparent that a difficult problem would be raised if an express limitation upon municipal taxation were placed in the same section which levies a tax.

Should the fact that a state tax law provides for sharing the tax revenues with municipalities be deemed to weight the scales in favor of preemption? Our answer is "No." Consider certain variations in the tax-sharing pattern. Suppose the sharing was with counties or some other non-municipal type of local unit. The tax-sharing would add little, if any, force to the fact of a state levy since it would be without municipal relevance. Assume state allocation of receipts from a state tax to a particular muncipal purpose and that a municipality proposes to resort to a similar levy for a different purpose. It will be recalled that the situation in the *Cambridge* case presented a municipal tax for the same purpose and it is of interest that the closing sentence of the opinion read: "No municipality has power to levy such a tax in addition to that levied by the state for similar purposes."[66] That was a stronger case because the General Assembly was making the state levy serve the particular municipal end in view. This, however, is not a very satisfying distinction. A municipality might obviate it by earmarking the proceeds of its tax for a different purpose and drawing more heavily on the general fund, if need be, to finance the object aided by the state levy.

In brief, the problem of interpretation is more difficult where tax-sharing is involved, particularly where the allocation and a municipal levy are for the same purpose, but the case for preemption is still not convincing. The legislature can, with relative ease, articulate a policy of limitation by express provision. Why is there not more reason to infer from silence a want of purpose to preempt the field than to imply from the state levy a policy not merely of limitation but of complete exclusion of municipalities from the field?

The present preemption doctrine is a very blunt instrument. It operates to exclude a municipality from a particular tax field even where the state levy is nominal, where the state levy in law, but not economics, burdens the same class of persons and, at least in some cases, where the classes of taxpayers are legally different but either the measure or the economic incidence of state and municipal levies are much the same. If, on the other hand, the courts were to leave the burden of correlating state and municipal taxes to the legislature the job could be done with deliberation and whatever precision and refinements were deemed desirable. Affirmative measures by the municipalities would be calculated to prod the legislature into action defining the respective areas of state and municipal taxation. Under the preemption doctrine legislative inertia works against the municipalities; if they desire to impose

[66] Firestone v. Cambridge, 113 Ohio St. 57, 67, 148 N.E. 470, 473 (1925).

levies similar to state taxes they must get what amounts to enabling legislation. This is not home rule; it is traditional pre-1912 legislative supremacy.

The preemption doctrine is not realistic; it is not sensitive to the fact that all taxes are imposed on people and that government simply varies the incidence by its choices of tax subjects and measures. Thus, the adoption of property tax limitations is calculated to redistribute the burden on us taxpayers but can hardly be relied upon to keep down public expenditure. To say that a municipality may not act because the state has invaded the field is to explain a result by resort to what is anything but a clearly-defined idea. Taxation is a pretty arbitrary business at best. Are we not deluding ourselves to talk in tones of finality about a given tax preempting a field of taxation when what it does is seize upon a particular human relationship or pattern of relationships as a funnel through which to draw revenue from persons?

We come now to the contention that the constitution preempts the income tax field for the state and, thus, municipal income taxation is entirely excluded without regard to whether the state has levied an income tax. It is necessary to look to the constitutional background.

There can be little doubt that the General Assembly had the power to levy an income tax under the Constitution of 1851. The broad grant of legislative power made by Section 1 of Article II renders true of Ohio the familiar theory that state legislative power is plenary except as limited. What, then, was the occasion for the 1912 amendments which expressly authorized the taxing of inheritances and incomes?[67] Doubtless, the explanation is that it was thought necessary to amend the constitution in order to empower the legislature to levy graduated inheritance and income taxes. In 1895 the Ohio Supreme Court had held invalid an inheritance tax law which taxed estates of larger value at higher rates on the entire valuation than smaller ones.[68] The act was considered in conflict with the equal protection clause of Section 2 of Article I of the Constitution. While the crude form of graduation employed was a far cry from making the rates progressively higher upon higher brackets of the tax base and, thus, taxing all corresponding brackets alike, the case seems to have caused concern about the permissibility of any type of graduation.

The 1912 amendments did not, however, stop with authorizing graduation. They proceeded to require that at least half of state income and inheritance tax proceeds be returned "to the county, school district, city, village, or township in which said income or

[67] OHIO CONST. Art. XII, §§ 7, 8.

[68] State *ex rel.* Schwartz v. Ferris, 53 Ohio St. 314, 41 N.E. 579 (1895).

inheritance tax originates, or to any of the same, as may be provided by law."[69] What effect, if any, does this allocation provision have upon municipal taxing power? The journal of the constitutional convention does not record any reference to the point or any discussion, for that matter, of the provision. A separate section authorizing state excise, franchise and severance taxes, also added in 1912, does not require sharing with local units.

In the opinion in, *State* ex rel. *Zielonka v. Carrel,*[70] the initial case upholding home rule power to tax, there was a dictum that by implication from the allocation clause municipalities are clearly without power to levy an income or inheritance tax. No further rationalization was offered. The supposed implication is by no means clear to us. The matter can be put this way—the people have said to their representatives in the legislature: "you may impose income and inheritance taxes and graduate the rates but if you do so you must share the proceeds with local governments." The tax-sharing feature is, in terms, simply a limitation upon state taxation. The delegates, as has already been noted, chose to deal expressly and in a more appropriate place with the subject of municipal tax limitation.

It is significant that the tax-sharing clause does not require sharing with municipalities. The clause, in effect, tells the legislature it may share with counties, for example, to the exclusion of municipalities located within their boundaries. Are we to say that since the legislature might or might not, entirely at its discretion, share with municipalities, the clause must be read as a limitation upon the home rule grant of municipal taxing power?

What has been said thus far with respect to the Ohio problem was written prior to the decision of the Supreme Court of Ohio in *Angell v. The City of Toledo,*[71] announced on March 8, 1950, in which the Toledo tax on earned income was upheld. Mr. Angell, who resided in the county outside the corporate limits of Toledo, was employed in Toledo.[72] He sought to enjoin enforcement of the tax. The primary question in the case was whether Toledo had authority to provide for the imposition of an income tax on earned

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[69] OHIO CONST. Art. XII, § 9.

[70] 99 Ohio St. 220, 228, 124 N.E. 134, 136 (1919).

[71] 153 Ohio St. 179, 91 N.E. 2d 250 (1950).

[72] The court pointed out that the ordinance was in effect when the plaintiff commenced his employment in Toledo and concluded that therefore, plaintiff's contract of employment was not impaired. The contract clause objection does not strike us as formidable in any case. A contract is conditioned by existing power to tax, just as is property ownership. Collection at the source does not obscure this basic idea; it is hardly a difference of substance that the taxing authority does not wait for one to have his wage envelope in hand before exacting tribute.

income. The majority opinion, written by Judge Turner, took note at the outset that the power of the General Assembly, unlike that of the Federal Congress, is plenary except as limited. The grant of home rule powers to municipalities did, in effect, limit state sovereignty to the extent of the sovereign authority conferred upon municipalities. The court recognized that the power so conferred upon municipalities embraced the power to raise revenue.

The opinion does not attempt extended rationalization in rejecting the contention that the income tax provisions of the constitution operated *per se* to preempt the field. Judge Turner simply dismissed the dictum in the *Carrel* case as *obiter,* pointing out that if the legislature enacted an income tax it would have to do so within the restrictions of Sections 8 and 9 of Article XII of the constitution and reiterated the doctrine of statutory preemption by saying that a municipality could levy an income tax in the absence of a state levy preempting the field. There was obviously no occasion to re-examine the statutory preemption doctrine.

It is significant that Judge Taft thought it necessary to write a separate opinion[73] in the *Angell* case to make it clear that statutory preemption was not involved. The second paragraph of the syllabus laid it down categorically that the state had not preempted the field of income taxation authorized by Sections 8 and 9 of Article XII of the constitution and that the General Assembly had not, under authority of Section 13 of Article XVIII or Section 6 of Article XIII of the constitution, passed any law limiting municipal power to levy and collect income taxes. All that it was necessary to determine was that the legislature had not acted in such a way as to deny to a municipality power to levy the Toledo type of income tax on earned income. While Judge Taft was careful to say that state occupation of a small part of a field of taxation does not necessarily indicate a design to exclude municipalities from the rest of it, he wanted to make it clear that the case had no real bearing on the question whether the legislature had preempted parts of the income taxation field by, for example, adopting a state excise tax, a state franchise tax and a state intangibles tax. Even if the Toledo tax had overlapped such state levies, Mr. Angell did not have standing to assert the invalidity of the Toledo tax on that account since there was no preemption so far as earned income was concerned and the ordinance would not stand or fall as a unit because the court would give effect to the separability clause.

The separate opinion of Judge Taft serves to point up afresh some of the difficulties of the preemption doctrine already discussed in this paper. He was quite understandably accepting the

[73] *See* Angell v. Toledo, 153 Ohio St. 179, 186, 91 N.E. 2d 250, 253 (1950).

doctrine as gospel. The very matters with which he was concerned in his opinion, however, emphasize to us the unsatisfactory character of this doctrine as a device for marking out respective areas of state and municipal taxation.

At the came time that the city fathers of Toledo received the glad tidings about their income tax the Dayton commissioners heard the bleak word that their income levy had been invalidated for want of electoral approval.[74] In 1945 the voters had added a Section 171 to the Dayton charter, the heading or guide line of which reads as follows: "Limitation of the total tax rate which may be levied without a vote of the people for all of the purposes of the municipality." The first six paragraphs of the section, true to the heading, relate unmistakably to ad valorem taxes and to no other kind of levy. They deal with ad valorem tax rates in terms of millage and control the use of the over-all maximum millage for debt service, permanent improvements and general fund purposes. The seventh paragraph reads:

> Unless authorized and approved by a vote of the electors conformably with the general laws of this State, the City Commission shall levy no tax outside of the limitations set forth in this Section. Provided, however, that the City Commission shall annually levy, to the extent necessary, outside the limitations provided in this Charter and by general law a sufficient sum to pay the interest, sinking fund and retirement charges on all bonds and notes of the City of Dayton heretofore or hereafter lawfully issued,
> the tax for which by general law or by this Charter has been or shall be authorized to be levied outside of tax limitations.

In a brief per curiam opinion the court expressed doubt as to whether the first sentence of this paragraph related solely to ad valorem taxation. The doubt was resolved against the income tax ordinance largely in reliance upon the rule that tax laws are to be strictly constructed against the levying authority. Actually, the only thing in all of the eight paragraphs of Section 171 to afford support for this conclusion is the absence of the modifying word "ad valorem" before "tax" in the first sentence of the quoted paragraph. That sentence, however, is hardly less clear without them. All that went before related to ad valorem tax limitations and the provision under scrutiny forbids a tax outside those limitations unless approved by a vote of the people. The only kind of tax with respect to which limitations of that character have any relevance is an ad valorem levy; it would be incongruous to speak of levying an income, admissions or occupational license tax, for example,

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[74] Zimmer v. Hagerman, 153 Ohio St. 187, 91 N.E. 2d 254 (1950).

"outside of" ad valorem tax limits. It is apparent that Section 171, and particularly its seventh paragraph, was drawn with an eye to the restrictions upon ad valorem taxation set out in Section 2 of Article XII of the constitution. Finally, the proviso in the seventh paragraph of Section 171 is addressed to ad valorem taxes to provide for debt service.

In sum, the doubt which troubled the court is so fully dispelled by the context that, to use the familiar parlance of statutory interpretation, the section was free from ambiguity in this respect.[75] The governing body of the city is left in the unhappy position of being unable to impose any tax whatever, other than ad valorem, without electoral approval. A referendum is compulsory, not merely voluntary or optional. On May 23, 1950, Dayton voters approved an income tax substantially the same as the original Dayton levy.

State Preemption in Pennsylvania

In Pennsylvania the concept of preemption has been written expressly into the Sterling Act and Act No. 481 of 1947. The original statute in each case ordained that the local authorities to which they pertain should not have authority to levy and collect any tax on a privilege, transaction, subject or occupation or personal property which was then or might thereafter become subject to a state tax or license fee.[76]

So long as Pennsylvania local units acting under one or the other of these two statutes confined their income levies to earned income, they did not run afoul state preemption. In December 1949, however, the City of Philadelphia so amended its income tax ordinance as to provide for taxation of non-earned income from any source whatsoever which was within the legal power of the city to tax.[77] It was broad enough to apply to corporations as well as individuals.

In February 1950 two suits were entertained in the original jurisdiction of the state supreme court, the object of which was to

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[75] While this is not the place to undertake a critical evaluation of rules of interpretation in the nature of presumptions, it is hardly amiss to stress that those rules are, at best, but court-made aids to interpretation which, if used unimaginatively, may obscure instead of reveal statutory meaning. It is not convincing simply to invoke such a rule without careful analysis of the language of the charter provision in relation to its purpose. To illustrate, the guide line of the provision was a part of the proposal approved by the voters as a charter amendment. Thus, it should have been considered in attempting to resolve the asserted ambiguity. See Fordham and Leach, *Interpretation of Statutes in Derogation of the Common Law*, 3 VAND. L. REV. 438 (1950).

[76] PA. STAT. ANN. tit. 53 § 4613 (Supp. 1949) (the "Sterling Act"); Act 481 of 1947 § 1, Pamphlet Laws 1145.

[77] Philadelphia Ordinance approved Dec. 9, 1949.

enjoin enforcement of the ordinance.[78] One suit was brought by an individual and his wife and the other by a corporation. A number of parties were allowed to join in the attack upon the ordinance by intervention. It was urged that the ordinance was not valid as to various classes of income and in every instance the court sustained the attack. The general theory upon which the court proceeded was that the Sterling Act banned municipal taxation of a "thing" or "subject" taxed by the state. It should be particularly noted that the emphasis was upon the "subject" of a tax.

The individual plaintiffs received dividends from domestic corporations which paid a state capital stock tax and from foreign corporations which paid a franchise tax. To sustain the conclusion that the income and corporate taxes were imposed upon the same subject the court treated the capital stock tax as, at once, a levy on corporate property and on the stock in the hands of shareholders and the income tax as an imposition on the property producing the income, that is, the stock. The franchise tax was placed on a footing with the capital stock levy. It was declared that when a corporation pays dividends out of the property on which the capital stock tax has been paid the city may not tax the dividend income to the stockholders because it would be taxing the same subject as the state had taxed. One can understand a line of thought which treats corporate income in a broad sense as corporate property, but the way the court finds identity of subject here is to say that the city was, in effect, taxing the stock of the stockholders. The opinion does not suggest that the city was taxing corporate property.

We run into this same confusion in connection with the next class of income which was involved in the case. The individual plaintiffs had received income from corporations which paid the state excise tax measured by their net income. The court insisted that it would look to reality rather than to the label "excise." It had no better explanation, however, for determining that the municipality could not tax the income than to say that the state excise was paid out of corporate property and would become a preferred lien on that property if not paid when due. It is far from clear what this demonstrates since any tax on a corporation is paid out of some kind of corporate property. The question remains whether, as in the case of the capital stock tax, the city was taxing the same subject when it taxed an individual's income from stock and the state imposed an excise on the privilege of doing business and used corporate net income as the measure of the tax.

When it came to the income of the individual plaintiffs from

[78] Murray v. Philadelphia, 71 A. 2d 280 (Pa. 1950) (two cases).

real estate, there was no basis for invoking preemption; the state had not levied a property tax. The city lost just the same. The explanation was that the income tax was, in effect, a tax on the real estate itself and the state had by separate enactment made provision for local taxation of property. The court cited the largely discredited *Pollock*[79] case for the proposition that the tax on the income from land is a tax on the land itself. It took no note of the Federal Supreme Court's repudiation, in 1937, of the notion that to tax income is the same as taxing the source. In *New York* ex rel. *Cohn v. Graves* the Court sustained the application of a New York income tax to rents received by residents from out-of-state real property.[80] Harlan F. Stone, perhaps our greatest tax judge, wrote the majority opinion. The following passage is particularly pertinent:

"Neither analysis of the two types of taxes, nor consideration of the bases upon which the power to impose them rests, supports the contention that a tax on income is a tax on the land which produces it. The incidence of a tax on income differs from that of a tax on property."[81] Yet the Pennsylvania court insists that it is a principle of economics that a tax on income produced by property is a tax on the property itself. The court carried this thought to the point of declaring that even if the Sterling Act purported to authorize such a levy it would be unconstitutional as a violation of the uniformity requirement of the state constitution.[82]

Graduation of Rates

In the two leading local income tax states, Ohio and Pennsylvania, there are legal clouds over progressive levies. The Pennsylvania constitutional requirement of uniformity of taxation is not, as in most states, confined to ad valorem taxation, but applies to "all taxes," including local income levies. The state supreme court invalidated the $1,000 personal exemption under the original Philadelphia ordinance on this ground.[83] This bears scant promise that the court would sustain graduated levies.

We have already seen that an old Ohio case, invoking the equal protection clause of the state constitution, was deemed to call for

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[79] Pollock v. Farmers Loan & Trust Co., 157 U. S. 429, 158 U. S. 601 (rehearing 1895).

[80] 300 U.S. 308 (1937). Counsel for the city in the second *Murray* case were at pains to point up the *Cohn* case to the court. Brief for Defendants, pp. 9, 14, Reply Brief for Defendants, p. 7, Murray v. Philadelphia, 71 A. 2d 280 (Pa. 1950).

[81] 300 U.S. 308 at 314.

[82] Murray v. Philadelphia, 71 A. 2d 280, 287 (Pa. 1950).

[83] Butcher v. Philadelphia, 333 Pa. 497, 6 A. 2d 298 (1938).

constitutional amendments in 1912 to permit the legislature to levy graduated inheritance and income taxes.[84] Since these amendments apply only to state levies and since municipalities have no specific constitutional grant of power to levy any sort of income tax, there remains a question as to whether they can impose progressive rates. It is elementary that the equal protction clause of the Fourteenth Amendment does not preclude graduated state income tax levies. It is not evident why the Ohio provision should be interpreted to do so. Were graduated taxation in its modern guise of different rates for different brackets of income now put to the judicial test the old case should be overruled or distinguished.

Persons and Income Subject to the Tax

Individuals

Residents and Non-residents. One of the principal reasons for resort to income taxation is to compel the "daylight citizen" to pay toward the support of those services and that protection which he enjoys in the locality where he is employed. Even if an income tax is adopted for other reasons, the revenue possibilities of taxing those non-residents who are employed or engaged in business or professional activity within the city are immediately apparent. All of the municipal income tax measures examined in the preparation of this paper tax the income of non-residents as well as residents.[85]

That a local unit of government may be given jurisdiction to tax its own residents is too clear to require extended comment. If its authorization is sufficiently broad, the local unit may use as a tax base all of the income earned by its residents without regard to the place where it is earned. With the exception of the Louisville, Kentucky, "occupation" tax all of the local income taxes studied do so impose the tax upon their residents as such.[86] In the case of a general function local unit, an adequate tax nexus between the taxing unit and the taxpayer is clearly present. The resident taxpayer has available for his use the "benefits" and "protection" provided by the local unit. In return the local unit may require financial support by taxation.

A local unit in levying a tax on the income of non-residents is in a position analogous to that of a state taxing the income of non-

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[84] See note 68 *supra.*

[85] School districts in Pennsylvania, however, are on a different footing. Act 481 of 1947, § 1A5 as amended by Act 246 of 1949, Pa. Stat. Ann. tit. 53, § 2015.1 (Supp. 1949) specifically prohibits school districts from levying income taxes on the salaries or other income of non-residents.

[86] Louisville Ord. § 1 imposes the tax only on those who are "engaged in an occupation, trade, profession, or other activity in the City."

residents and must stay within the limits of Fourteenth Amendment due process of law which are applicable to the states.[87] State taxation of this character is a commonplace.

In the recent landmark case, *Angell v. Toledo*,[88] the Supreme Court of Ohio upheld the validity of the Toledo earnings tax as applied to a salary earned in the city by a non-resident. The court readily concluded that there was jurisdiction to tax the non-resident's earnings within the city because the municipality had rendered benefits in the form of a place to work and protection for the non-resident. *Wisconsin v. Penney Co.*,[89] which was cited in the opinion, supports the result but actually goes well beyond the facts presented in the *Angell* case. The *Penny* case dealt with a Wisconsin tax "for the privilege of declaring and receiving dividends, out of income derived from property located and business transacted" in Wisconsin;[90] the dividends involved were actually declared by a Delaware corporation at its principal office in New York and the stockholders may or may not have been residents of Wisconsin. The Court held that the levy was, in effect, an income tax on earnings within Wisconsin and that the granting of the privilege of doing business to the foreign corporation supported the tax on the income earned from the business.[91] It is to be noted, as emphasized in the dissenting opinion,[92] that the formal subject of the tax was an out-of-state transaction and if the levy was to be regarded as a tax on income it amounted to an impost on non-resident stockholders.

The Philadelphia income tax is applied to all wages, salaries or compensation for work done or services performed in the city.[93] If a non-resident is paid on a unitary basis for business transacted or work done partly in and partly outside the city the taxable amount is the portion of the total compensation that the "in-city" business done or days worked bears to the total.[94] It is not consid-

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[87] Thus, in Milwaukee County v. White Co., 296 U. S. 268 (1935), the plaintiff was simply treated as though it were the state.

A state income tax on non-residents must be non-discriminatory and cannot deprive them of exemptions equivalent to those allowed residents though it may limit the deductions of non-residents to those occurring within the state. Travis v. Yale & Towne Mfg. Co., 252 U. S. 60 (1920); Shaffer v. Carter, 252 U. S. 37 (1920).

[88] See note 71 *supra*.

[89] 311 U. S. 435 (1940).

[90] Wis. Laws 1935, c. 505, § 3 as amended by Wis. Laws 1935, c. 552.

[91] 311 U. S. 435 at 444, 445.

[92] 311 U. S. 435, 446 (dissenting opinion).

[93] Philadelphia Ord. § 2 as amended.

[94] Philadelphia Income Tax. Regs. Art. II-2. (In these footnotes the local income tax regulations will be identified hereafter by reference to the name of the local unit.)

ered practicable to insist on strict application of the pro rata rule in all cases. For example, where the non-resident simply comes to town to report and get instructions or is employed on a train which regularly passes through the city and his services performed within the city are incidental to those performed without the city, he is not treated as engaged in a taxable activity within the city.[95]

The taxability of earnings of a non-resident of Philadelphia was first clearly determined in *Kiker v. Philadelphia.*[96] Plaintiff, a resident of New Jersey who worked in the Philadelphia Navy Yard and commuted by boat on the Delaware without going through Philadelphia proper, asked that enforcement of the ordinance against him be restrained. The Navy Yard is on League Island, which is within the city limits. Among other things Kiker contended that he received no protection or benefit from the city. In upholding the tax as applied to non-residents, the court stated that the recession by Congress to the state of power to tax in the Navy Yard area[97] carried with it the obligation to make available the usual services provided by the municipality to residents and citizens. This potential benefit was considered enough to support taxing jurisdiction even though the city did not actually provide governmental services on the island. The court judicially noticed, moreover, that the city cut ice in the Delaware and thus enabled plaintiff to go to work by boat in the winter!

Prior to the 1949 Amendments to Pennsylvania Act 481, school districts taxed the income of non-residents which was earned within their boundaries and no judicial difficulty was encountered. It was clearly implied in the then credit provisions of the statute[98] that school districts could tax the income of non-residents earned within their boundaries. A school district is an ad hoc unit performing a single function. Does benefit exist if the taxpayer is a non-resident and his children go to school elsewhere? Obviously general benefits are enough; a resident might be a confirmed bachelor. Is it not true, moreover, that one derives general benefits from the promotion of literacy, if not erudition, in the community where he works?

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[95] *Id.* at Art. II-2 (a).

[96] 346 Pa. 624, 31 A. 2d 289 *cert. denied,* 320 U. S. 741 (1943). In Guerra v. Philadelphia, 30 F. Supp. 791 (E.D. Pa. 1940) a resident of New Jersey who was employed in Philadelphia raised the question of applicability of the tax to non-residents by asking an injunction against the enforcement of the tax. The court refused to examine the question saying that the jurisdictional amount was not present and that the existence of a plain, speedy, and efficient remedy in the Pennsylvania courts also prevented it from taking jurisdiction.

[97] 54 STAT. 1059 (1940) as reenacted by 61 STAT. 641 (1947), 4 U.S.C. 106 (1949).

[98] Act 481 of 1947 § 5.

Where the non-residents reside in another state there may well be special problems of enforcement in cases where the tax cannot be collected at the source. For example, where the impact of the tax is on business profits the taxing local unit may have occasion to sue for the tax in the state of residence. The judicial disposition against enforcing foreign revenue laws renders it advisable to obtain judgment in the mother state of the taxing unit, if jurisdiction of the taxpayer can be had and, then, rely on the full faith and credit clause in suing on the judgment in the state of residence.[99]

The Toledo ordinance took the lead in spelling out a formula for allocating earned net profits of non-residents.[100] This is the formula: First compute the percentage of (1) the value of the taxpayer's corporeal property in Toledo to that of all his corporeal property, (2) the taxpayer's gross receipts from sales made and work done in Toledo to his total and (3) of his non-executive payroll for employees in the city to the total. Then, determine the average of these percentages. The result is the percentage figure to use in allocating net income to Toledo. The formula is permissive; the Board of Review established by the ordinance may substitute other factors where the formula would not produce a just and equitable result. Several other cities have borrowed this device,[101] but Columbus, St. Louis and Youngstown use it only where the records of the taxpayer do not show what net income is reasonably attributable to business or other activity in the city.[102]

EARNED INCOME. (a) *Regular employment—wages and salaries.* Many laymen and some lawyers on first encountering a local income tax will almost automatically think of it in terms of the progressive and graduated Federal Income Tax with which they are already familiar. The local income taxes which have been levied in this country in the wake of the Philadelphia experiment bear little similarity to the Federal Tax except that they may also be classified as income taxes. Local income taxation, in fact, follows a markedly uniform pattern of flat rates without substantial exemptions or, in the case of salaries and wages, even of deductions.

The local income taxes have uniformly imposed the tax rate on the gross income from wages and salaries on the net income

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[99] In Milwaukee County v. White Co., 296 U. S. 268 (1935), the Court stressed the difference between an original action and a cause of action based on a judgment.

[100] Toledo Ord. § 3.

[101] See, *e.g.*, the following ordinances which use substantially similar formulas: Dayton Ord. § 2; Louisville Ord. § 2 (only two factors are used in the Louisville formula); Warren Ord. § 2.

[102] Columbus Ord. § 2; St. Louis Ord. § 3; Youngstown Ord. § 2.

from business activities.[103] This distinction between the taxation of employees and the taxation of business profits has been upheld as reasonable classification, usually on the basis that business profits are uncertain.[104] It would seem that the classification could be more persuasively supported on the ground that, in a rough sense, gross wages and salaries are net income, whereas the gross income of a business or profession is likely to be substantially offset by expenses incurred in producing it. The Philadelphia Income Tax regulations make detailed provision for the taxation of those who receive wages, salaries, commissions and other income arising out of an employment relation. Bonuses and incentive payments are treated as taxable income.[105]

The Philadelphia Regulations formerly classified marriage fees and other monies received by clerics for religious services as income from a profession.[106] This was successfully attacked by a Roman Catholic priest. Under the canons of his church he could not exact a charge for such services but was free to receive offerings. The Superior Court, two judges dissenting, ruled that the offerings were gratuities and not "earned income" within the meaning of the ordinance.[107] The dissenting opinion[108] was, we believe, on sounder ground; the dissenters said the nub of the matter was whether the transfer was made for services rendered. The tip has become a characteristic American institution. Quite commonly the person who receives the *pourboire* is not in a position to exact it, but that it is compensation for service is hardly debatable.[109]

Disability and accident benefits are treated as income only where the employee has an enforceable right to receive the benefits.[110] Because of the unusual method of contracting for the services of professional musicians special provision has been made which requires the purchaser of the music to withhold the taxes of

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[103] See, *e.g.*, Philadelphia Ord. § 2. The amendments to § 2 of the ordinance have retained the basic classification.

[104] See, *e.g.*, Louisville v. Sebree, 308 Ky. 420, 214 S.W. 2d 248 (1948); Dole v. Philadelphia, 337 Pa. 375, 11 A. 2d 163 (1940).

[105] Philadelphia Regs., Art. II-1 (a) & (b).

[106] Philadelphia Income Tax Reg. promulgated Nov. 2, 1940.

[107] Ross v. Philadelphia, 149 Pa. Super. 33, 25 A. 2d 834 (1942).

[108] *Id.* at 41, 25 A. 2d at 835 (dissenting opinion).

[109] Some municipalities have specifically included tips as earned income. See, *e.g.*, Philadelphia Regs. Art. II-1 (e); Columbus Regs. Art. II-1 A (e); Dayton Regs. Art. II-4-2 (e); Louisville License Fee Regs. Art. II-1, §1, e, 1 (a); Springfield Regs. §II-1 F (1); Toledo Regs. Art. II-1 (e); Warren Regs. Art. II-1 (e); Youngstown Regs. Art. II-1 (e). And some have refused to follow the logic of the Pennsylvania court and continue to include marriage and similar fees as earned income. See, *e.g.*, Warren Regs. Art. II-1 (d).

[110] Philadelphia Regs. Art. II-1 (e) (2).

the musicians except in the case of "name bands," where the leader or owner is made responsible for withholding.[111] Full time life insurance agents are taxed on all commissions received from policies placed with the company with which the agent has a full time employment status.[112] Part time insurance agents and general insurance agents, who are residents, are taxed on all commissions received.[113] Their non-resident fellows are taxed on commissions received on policies sold to residents and on those sold to non-residents if they, the agents, conduct their business in Philadelphia offices and do not maintain outside offices for sales of policies to non-residents and the keeping of records on them.[114]

(b) *Self-employment.* We have already seen that employees and the self-employed are separately classified for local income tax purposes and that the latter are taxed on net profits of "businesses, professions or other activities."[115] In this second category one might expect to find, along with business and professional people generally, independent contractors,[116] professional fiduciaries[117] and persons who buy and sell real property or securities as a business or are in the business of owning and operating or simply managing such properties.[118] The line between administering or managing one's own investments as good husbandry in personal affairs and being in the business of property ownership and management is not sharply defined. The Philadelphia regulations treat operation of loft buildings, apartment hotels, hotel buildings, office buildings and similar structures, as well as apartment houses over three stories in height, unequivocally as taxable activities. In the case of lesser dwelling structures the regulations permit consideration, in determining "business activity vel non," of the number of properties operated, the employment of labor in the operation and the ratio of income of the properties to all other income of the owner or person for whom the properties are operated.[119] The regulations declare the buying and selling of securities a taxable activity where the transactions "are not isolated and few, but are extended so as to constitute an activity."[120]

In two cases decided in January, 1950, the Supreme Court of

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[111] *Id.* at Art. II-1 (f).

[112] *Id.* at Art. II-1 (g), § II.

[113] *Id.* at Art. II-1 (g), § III.

[114] *Id.* at Art. II-1 (g), §§ II and III.

[115] Philadelphia Ord. § 2 as amended.

[116] Philadelphia Regs. Art. II-3 (d) 3.

[117] *Id.* at Art. II-3 (d) 2.

[118] It is evident that the business of buying and selling realty is a taxable business activity within the meaning of Philadelphia Regs. Art. II-3.

[119] Philadelphia Regs. Art. II-3 (b) 3.

[120] *Id.* at Art. II-3 (d) 1.

Pennsylvania determined that the investment operations of a lawyer[121] and a retired businessman[122] were not taxable activities under the Philadelphia ordinance. The lawyer employed real estate agents to conduct his real estate transactions for him. This included original purchase and sale, repairs, insurance and rentals. His real estate holdings were very substantial. No structure exceeded three stories. He provided electricity to certain properties and janitor service to another and that was all. The retired businessman owned two buildings, each of three stories. He furnished no services; all he did was collect rents, pay taxes and maintain insurance. Both dealt some in securities through brokers but the layman was far more active — he averaged ten purchases and eleven sales a year but these included, as separate items, sales executed at different times pursuant to a single order and purchases and sales in connection with the receipt and disposal of stock rights, stock dividends and securities redeemed. The conclusion in both cases was that the tax did not apply because only unearned income on investments was involved. This was achieved without invalidating the somewhat flexible regulation as to real estate.[123] Nor did the court expressly impeach the securities transactions regulation although it declared the regulation's use of "activity" inconsistent with the ordinance.[124]

Some years before the Pennsylvania Court had upheld the application of the tax to the net profits of a corporate trustee engaged in operating real estate as a mortgagee in possession or as owner protecting trust assets pending litigation.[125] It appeared from the trustee's own illustrations of its operations that it furnished services consisting of labor, light, heat, power or supervision.

As recently as February, 1950, the Pennsylvania court has invalidated, so far as pertinent here, a December, 1949, amendment to the Philadelphia ordinance which was clearly broad enough to reach simple investment income.[126] We have already ventured to criticize that tribunal's view that a tax on income is a tax on the source.[127] Obviously, if a tax on the income of realty is a

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[121] Breitinger v. Philadelphia, 363 Pa. 512, 70 A. 2d 640 (1950).

[122] Murray v. Philadelphia, 363 Pa. 524, 70 A. 2d 647 (1950).

[123] *Id.* at 530, 70 A. 2d at 650. The realty regulations are Philadelphia Regs. Art. II-3 (b).

[124] Murray v. Philadelphia, 363 Pa. 524, 531, 70 A. 2d 647, 650 (1950). The securities transaction regulation is Philadelphia Regs. Art. II-3 (d) 1.

[125] Pennsylvania Co. v. Philadelphia, 346 Pa. 406, 31 A. 2d 137 (1943).

[126] Murray v. Philadelphia, 71 A. 2d 280 (Pa. 1950) invalidated Philadelphia Ordinance approved Dec. 9, 1949, except for the provision increasing the rate of the tax.

[127] See note 80 *supra.*

property tax uniformity is denied.[128] The question here is this — since income from the business of operating properties is attributable in very substantial part to the capital investment will the factor of business activity continue to control and, thus, leave the way clear for local income taxation? Certainly, the corporate trustee case has not been overruled. The patent moral of the cases to the investor is that he should minimize his services in relation to rental property, for example, if he would avoid the city income tax.

There has been no reported judicial experience with these problems outside of Pennsylvania. The Ohio municipalities utilizing income taxes have followed the basic Philadelphia pattern whereby the tax is imposed on the gross income of wage earners and on the net profits of the self-employed. They, too, impose the tax on earned income. Their ordinances, that of Dayton excepted,[129] define the earned net profits on which the tax is imposed on the self employed in such a way that the net profits must be earned in the course of a regular profession, business or other enterprise.[130] The various municipal income tax regulations in Ohio are generally limited to earned income.[131] However, a number of these municipalities include rental income as taxable.[132] The implication is that rental income is taxable because earned, and yet, except for Toledo[133] and Youngstown[134] there is no attempt to relate rental income to services rendered or supervision performed in connection with the rental property. In short, only a minority of these municipalities have not faced up to the problems encountered recently by Philadelphia.[135]

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[128] It is evident that there would be inequality of treatment as between income producing property and non-productive property.

[129] Dayton Ordinance § 1 defined "net profits" in part as follows: "[t]he gross income derived from any *transaction*, venture or activity . . . whether permanent, temporary or non-recurring in character to the extent that it can be made by the City of Dayton . . . " (writers' emphasis).

[130] Columbus Ordinance § 1; Springfield Ordinance § 1; Toledo Ordinance § 2; Warren Ordinance § 1; Youngstown Ordinance § 1.

[131] Columbus Regs. Art. II-3, 4 & 5; Springfield Regs. § II-3, 4 & 5; Toledo Regs. Art. II-3, 4 & 5; Warren Regs. Art. II-3, 4 & 5; Youngstown Regs. Art. II-3, 4 & 5.

[132] Columbus Regs. Arts. II-7-3-3, II-10 (m); Dayton Arts. I-1 (g), II-9 (h); Springfield Regs. § II-3 E; Toledo Regs. Arts. II-6-3-3, II-9 (j); Warren Regs. Arts. II-6-3-3,II-9 (n); Youngstown Regs. Arts. II-6-3-3, II-9 (n).

[133] Toledo Regs. Art. II-9 (j).

[134] Youngstown Regs. Art. II-9 (n).

[135] The City Attorney of Columbus has concluded that a trustee of realty who only has authority to receive rents and distribute them to beneficiaries, and who does not control or manage is not taxable on trust income from the realty. Opinion of the City Attorney of Columbus to the City Auditor dated May 24, 1949. The conclusion of the city attorney does not appear to be reflected in the Columbus Income Tax Regulations.

(c) *Casual and irregular employment.* The local income tax ordinances do not refer specifically to intermittent employment. The terms in which the taxes are imposed, however, are usually sufficiently broad to include employment of this character.[136] There can be no doubt but that employment of brief duration is taxable. Even isolated instances of employment for only a few hours at a time are subject to the tax.[137] As a practical matter, however, strict enforcement at this level may not be worth the candle.[138]

Investment Income

There is, of course, nothing in the nature of things to preclude local taxation of investment income. In Pennsylvania, however, the uniformity clause[139] and statutory preemption have, between them, pretty well excluded local units from this part of the field. As we have seen, taxability of the income of various types of investments were recently considered in the second *Murray* case[140] and the city lost at every turn. Thus, Pennsylvania local units can get at the income from property only where the taxpayer can be said to be engaged in the business of operating properties which would place the income in the earned category.

We venture to prophesy that the Ohio Court would not treat a tax on investment income as a tax on the source.[141] In Ohio, moreover, the uniformity requirement applies only to land and improvements thereon.[142] On the other hand, intangibles are not taxed locally but are subject to a state tax the proceeds of which are shared locally.[143] The tax on productive "local situs" intangibles is measured by their income yield.[144] Thus, so long as the Ohio pre-

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136 See, *e.g.*, Philadelphia Ord. approved Dec. 13, 1939, § 2 and amendments thereto; St. Louis Ord. § 2; Youngstown Ord. § 2. The catch-all phrase employed in most of the ordinances is, "and other compensation earned."

137 See, *e.g.*, Income Tax Regulations for City of Sharon, Sharon School District, Farrell School District, Borough of Sharpsville, Sharpsville School District, Wheatland School District, and Hickory Township School District Art. I-1. (These local units are all located in Pennsylvania. Their income tax regulations will hereafter be cited as "Sharon Uniform Regs.")

138 Some municipalities have possibly been influenced by enforcement considerations in specifically exempting the earnings of minors under specified ages. Columbus Ord. § 16-6; Dayton Ord. § 16-5; Springfield Ord. § 15 (f).

139 Kelley v. Kalodner, 320 Pa. 180, 181 Atl. 598 (1935).

140 Murray v. Philadelphia, 363 Pa. 524, 70 A. 2d 647 (1950).

141 *See* State *ex rel.* Zielonka v. Carrel, 99 Ohio St. 220, 224, 124 N.E. 134, 135 (1919).

142 Ohio Const. Art. XII § 2. State *ex rel.* Struble v. Davis, 132 Ohio St. 555, 9 N.E. 2d 684 (1937).

143 Public libraries, municipalities and counties are the primary beneficiaries. Ohio Gen. Code § 5639 (Supp. 1949).

144 See note 58 *supra.*

emption doctrine survives, there is a question whether the state has preempted the field as to these intangibles. Pointed reference was made to this in the separate opinion of Judge Taft in the recent *Toledo* case.[145]

Aside from the possible problems raised by the impact of the preemption doctrine, there is nothing to prevent Ohio municipalities from taxing investment income in the exercise of their home rule powers.

Capital Gains

In Philadelphia the situation as to capital gains and losses was, down to December, 1949, the same as that with respect to income from property; they were to be taken into account only if classificable as business or earned income or losses.[146] This appears to be the case now under the Louisville ordinance and some of the Ohio ordinances.[147] The Columbus, Youngstown and Warren regulations, on the other hand, declare that capital gains and losses shall not be taken into account in arriving at "net profits earned."[148] The December 9, 1949, amendatory ordinance of Philadelphia was clearly broad enough to cover any class of unearned income.[149] Its validity in this respect was not specifically in issue in the second *Murray* case, but the court declared all the provisions of the ordinance other than that raising the rate on earned income, too vague to be enforceable.[150] It is not evident that the uniformity requirement stands in the way. In federal income tax lore there is nothing more commonplace than that a capital gain levy is not imposed on the property with respect to which gain is realized. Thus, intergovernmental immunity does not preclude taxation of capital gains on public securities.[151]

The home rule taxing power of Ohio municipalities would, we believe, extend to income taxation of capital gains, whether classifiable as earned or unearned income. There is no similar state levy which can be said to preempt the field.

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[145] See note 73 *supra*. See Springfield Regs. §§ II-1 F & II-7 C (3) which exclude from the municipal income tax the income from property subject to the Ohio Intangible Personal Property Tax.

[146] Philadelphia Regs. Art. II-7 (j).

[147] Louisville Regs. Art. II-5 (j); Dayton Regs. Art. II-9 (e); Springfield Regs. § II-8 C; Toledo Regs. Art. II-9 (j).

[148] Columbus Regs. Art. II-10 (j); Warren Income Tax Regs. Art. II-9 (j); Youngstown Income Tax Regs. Art. II-9 (j).

[149] Philadelphia Ord. approved Dec. 9, 1949 § 3 which provides for the imposition of the tax, *inter alia*, "on all other net income derived . . . from any source whatsoever . . . "

[150] Murray v. Philadelphia, 71 A. 2d 280, 289 (Pa. 1950).

[151] Willcuts v. Bunn, 282 U.S. 216 (1931).

Partnerships

It is obvious that local income levies would reach income from partnership activities. The method, however, varies. In Philadelphia the primary rule is to exact the tax from the partnership as an entity.[152] To the extent, however, that partnership income is non-Philadelphia it can be reached only as to resident members and that is done on the basis of their distributive shares.[153] The Columbus and St. Louis patterns are similar.[154] Neither city requires partnership information returns. The late Dayton ordinance expressly rejected taxation as an entity [155] and the regulations, accordingly, exacted information returns.[156]

Corporations

Philadelphia first undertook to apply its income tax to corporations as such by its amendatory ordinance of December 9, 1949. The effort went aground on the shoals of preemption. The state franchise tax and corporate income tax barred the way as to foreign corporations.[157] The capital stock and corporate income taxes did as much with respect to domestic corporations.[158] Pittsburgh and other units operating under Act No. 481 have found a way to obviate the preemption difficulty with respect to what is at least a substantial class of corporations. Pittsburgh has an excise, a mercantile license tax, measured in terms of gross income, which has been sustained in its application to domestic and foreign corporations.[159]

The Ohio income tax cities and Louisville and St. Louis, as well, do tap corporate income.[160] No effort is made to base the tax on total corporate net profits without regard to source, even in the case of domestic corporations. Instead, the design is to apply the tax simply to income attributable to business conducted in the taxing unit. Thus, all business corporations, domestic and foreign, are placed on the same footing. For this purpose an allocation formula,

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[152] Philadelphia Regs. Art. II-4.

[153] *Id.* at II-3 (a).

[154] Columbus Regs. Arts. II-3, II-4; St. Louis Regs. §§ 10 & 11.

[155] Dayton Ord. (1949) § 2 (1).

[156] Dayton Regs. Art. IV-1-3. Sharon Uniform Regs. Art. II-A 1 also requires an informational return.

[157] Murray v. Philadelphia, 71 A. 2d 280, 286 (Pa. 1950).

[158] *Id.* at 284, 285.

[159] Federal Drug Co. v. Pittsburgh, 358 Pa. 454, 57 A. 2d 849 (1948).

[160] Columbus Ord. § 2 (5); Dayton Ord. § 2 (3); Louisville Ord. § 1; Springfield Ord. § 2 (5); St. Louis Ord. § 2 (e); Toledo Ord. § 3 (5); Warren Ord. § 2 (5); Youngstown Ord. § 2 (5).

like that employed by Toledo in the case of a non-resident individual,[161] is used. Under the Columbus ordinance and regulations if the business in Columbus of a corporation is so departmentalized that actual records of it will disclose the net profit derived wholly from business done within the city and such records are actually kept under a usual accounting system, which is acceptable for federal income tax purposes, those actual records must be used.[162] Otherwise, resort is to be had to the allocation formula. St. Louis has a similar pattern.[163]

The Columbus and Toledo regulations, influenced, doubtless, by the *Youngstown* case,[164] authorize the exclusion of gross receipts of public utility corporations, upon which the state excise tax is paid, in determining net profits for purposes of the tax.[165] The ordinances do not speak to the point; the exclusion is apparently achieved by very liberal interpretation.

Cooperatives

Many cooperatives engage in what are functionally business activities within the meaning of local income tax ordinances. That seems clear enough. Whether they realize "net profits" is the vital question. Apparently most of the local units levying income taxes have taken the label "non-profit corporation" at face value. Several Ohio cities have, however, proceeded on the basis that there may be net profits in fact.[166] Columbus took the lead. Her regulations declare the tax applicable to income of a "non-profit organization" determined by deducting from gross receipts (1) all costs and expenses of doing business and (2) patronage refunds paid in cash within ninety days after close of the taxpayer's accounting period with respect to which they were made.[167]

Estates and Trusts

To the extent that an estate or trust earns net profits in like fashion as a business corporation, there appears to be no reason why it should not be taxed on such income. The Philadelphia reg-

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161 See note 100 *supra*.

162 Columbus Ord. § 2 (6); Columbus Regs. Art. II-5-3 (a).

163 St. Louis Regs. § 12 C (1) & (2).

164 See note 55 *supra*.

165 Columbus Regs. Art. II-5-4; Toledo Regs. Art. II-5-4. Columbus and Toledo both prescribe that no deduction shall be allowed for expenses incurred in producing the gross receipts so excluded.

166 Columbus Regs. Art. II-6; Dayton Regs. Art. II-6; Springfield Regs. Art. II-6.

167 Columbus Regs. Art. II-6-1.

ulations proceed on just this basis as to a trust estate.[168] And the supreme court has upheld the application of the tax to estate income produced by a corporate trustee engaged in operating real estate, sometimes as mortgagee in possession and sometimes as owner, for the purpose of protecting the assets of the estate pending liquidation and sale.[169] Trust or estate income which is properly to be classified simply as investment income could be reached in Pennsylvania only in the unlikely possibility that neither the uniformity clause nor state preemption stood in the way.[170]

The definition of "business" in the Toledo regulations excludes "the ordinary administration of a decedent's estate by the executor or administrator, and the mere custody, supervision and management of trust property under a passive trust, whether inter vivos or testamentary, unaccompanied by the actual operation of a 'business' as herein defined."[171]

Columbus,[172] Springfield,[173] and Warren, Ohio,[174] all have substantially similar provisions. Dayton achieved the same result as to the income of decedents' estates during the period of administration by exempting such income, not earned in the operation of a business, from the tax.[175] It, thus, appears that these cities are not trying to reach unearned investment income of estates and trusts, whether distributed or undistributed. The same is true of the Louisville impost, which, as we have seen, is formalized as a license tax measured by earned income.[176]

Exemptions and Deductions

Most local income taxes allow no personal exemptions nor deductions for dependents at all. Two exceptions have been observed. The Springfield, Ohio, levy does not apply to earnings of $1040 or less per annum[177] of any taxpayer, individual or corporate. If, however, a taxpayer's total "taxable" income exceeds $1040 he is taxed upon all of it. This largely nullifies the exemption. Warren, Ohio,

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168 Philadelphia Regs. Art. II-3 (c).

169 Pennsylvania Co. v. Philadelphia, 346 Pa. 406, 31 A. 2d 137 (1943).

170 Sharon Uniform Regs. Art. II-C 3 is an attempt to tax trust income.

171 Toledo Regs. Art. I-1 (b).

172 Columbus Regs. Art. I-1 (b).

173 Springfield Regs. § I-2.

174 Warren Regs. Art. I-1 (b).

175 Dayton Regs. Art. XVI-1-7.

176 Louisville Regs. Art. II-2, § 2 (b) provides that, "[w]henever a trust estate is engaged in an enterprise, activity or business which is productive of income, said income shall be considered subject to the license fee."

177 Springfield Ord. § 15 (g).

has an outright exemption of $1200 per annum.[178] This is as close as any of the local income taxes come to relating burden to ability to pay.

A few cities have excluded personal earnings of minors below certain ages outright.[179] Columbus and Springfield exclude funds received from local, state or Federal Government because of service in the armed forces of the United States.[180] In the case of the minor an adequate personal exemption would be a better approach. Why exempt all the earnings of a minor who has a demonstrated adult earning capacity? Nor is it apparent that the tax should not reach military service earnings — at least during a non-hot-war period.

Various types of receipts, some of which could hardly be considered earned income in any event, have been expressly excluded. Within this category are (1) poor relief benefits, (2) public or charitable pensions or assistance to the aged or disabled, (3) pensions, disability benefits annuities or gratuities from any source, (4) copyright and patent royalties and (5) compensation for personal injury.[181]

Salaries, wages and commissions of employed persons are taxed without deductions for expenses incurred in producing the income or any other items. This is, of course, a rather crude pattern. Whatever justification can be mustered for it would probably amount to this — salaries and wages are largely net to begin with and to allow deductions would create an unwarranted administrative burden.

In determining professional and business net profits, allowable deductions under the Columbus tax, for example, include (1) all ordinary and necessary business (or professional) expenses, (2) depreciation, depletion, obsolescence and losses from theft or casualty, not otherwise claimed, (3) bad debts for the year ascertained worthless and charged off or a reasonable addition to a reserve for the purpose and (4) taxes directly connected with the business (or profession).[182] Capital gains are, as a general rule not included on the income side, nor may capital losses be deducted,[183] Income from the sale, as a dealer, of securities or real property is, however, taxable

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[178] Warren Ord. § 2.

[179] Columbus Ord. § 16-6 (under 18 years of age); Dayton Ord. § 16-5 (under 16 years of age); Springfield Ord. § 15 (f) (under 16 years of age).

[180] Columbus Ord. § 16-1; Springfield Ord. § 15 (a).

[181] Exclusions of the type listed in the text may be found in the following regulations: Columbus Regs. Arts. II-1 & II-10; Dayton Regs. Art. XVI-1; Louisville Regs. Art. II-1, § 1 (e) 2; Springfield Regs. § XV; Toledo Regs. Arts. II-1; Warren Regs. Arts. II-1 & II-9.

[182] Columbus Regs. Art. II-10 (f), (g), (h) and (i).

[183] *Id.* at Art. II-10 (j). But see Philadelphia Regs. Art. II-7 (j).

business income.[184] Presumably all costs of such activity can be set off against all receipts but it is not clear that a net loss could be deducted from earned income received in another activity or in an employee capacity.

Intergovernmental Relations

There is, of course, no longer any constitutional difficulty about subjecting the salaries and wages of federal officers and employees to state and local income taxation.[185] It is of interest that in one of the Philadelphia cases it was argued that the Sterling Act did not enable the city to tax the salaries of federal personnel since at the time the Act was adopted the doctrine of intergovernmental immunity was still deemed by the Supreme Court of the United States to apply to such income.[186] The superior court proved a poor market for such an idea; that court relied upon the prospective character and operation of the Sterling Act.[187] The Act was designed to enable the city to impose substantially any kind of a tax which the state did not and it was implicit that a subject which subsequently became amenable to city income taxation would automatically fall within the sweep of the power conferred.[188]

There is, apart from the erstwhile immunity of federal salaries, a separate question as to state and local taxing jurisdiction over federal areas. In 1940 Congress enacted legislation expressly consenting to state and local taxation of income received by federal employees residing or working in federal areas.[189]

It is clear that the federal act carries far enough to permit of municipal taxation of income earned in a federal area by one resid-

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[184] Philadelphia Regs. Art. II-3 (d) (1) classifies the business of buying and selling securities as taxable. It is apparent that one engaged in the business of selling either securities or realty is engaged in a taxable activity within the meaning of an income tax based on earned income without regard to whether the particular businesses are expressly stated to be taxable.

[185] Graves v. New York *ex rel.* O'Keefe, 306 U.S. 466 (1939) (state taxation of federal employee).

[186] Philadelphia v. Schaller, 148 Pa. Super. 276, 25 A. 2d 406, *cert. denied*, 317 U.S. 649 (1942).

[187] *Id.* at 281, 25 A. 2d at 410.

[188] The net income of a contractor from work performed under a federal contract is subject to state and local income taxation. James v. Dravo Contracting Co., 302 U.S. 134 (1937). It has been held recently that federal employees are subject to the provisions of the Louisville License Fee Ordinance. Cook v. Commissioners of the Sinking Fund of Louisville, 312 Ky. 1, 226 S.W. 2d 328 (1950). (The quotation at 226 S.W. 2d 329, 330, from the concurring opinion of Frankfurter, J., in the O'Keefe case was inadvertently ascribed to Chief Justice Hughes.)

[189] 54 Stat. 1059, 1060 (1940) as reenacted by 61 Stat. 641, 644-645 (1947), 4 U.S.C. 106 (1949).

ing in the municipality outside the area as well as income earned by a resident of the area outside of it but in the city.[190] It is clear, moreover, that a state may reserve for itself and its local units taxing jurisdiction over territory ceded to the Federal Government.[191] Where jurisdiction is so reserved the authority to tax does not depend upon the federal statute.

The question has arisen in Pennsylvania whether Philadelphia could impose an income tax upon a non-resident working in a federal area situated within the geographical limits of the city exclusive jurisdiction of which had been ceded by the state to the Federal Government.[192] The question arose in relation to a person employed at the League Island Navy Yard. The state had ceded exclusive jurisdiction of the island to the Federal Government reserving only the authority to execute civil and criminal process in the area. The Supreme Court of Pennsylvania decided that the federal statute consenting to state taxation of persons living or receiving income in a federal area constituted, in substance, a recession of taxing jurisdiction to Pennsylvania and that the effect of the recession was to impose upon Philadelphia the obligation to provide all the usual governmental services and protections to those receiving income from working on League Island. The court did not think it made any difference that the Federal Government was not looking to Philadelphia to provide those governmental services for persons working on the island. The Supreme Court of the United States denied certiorari.[193]

As for collecting a local income tax upon earnings at the source the local units have no hope of being able to require the Federal Government to withhold the tax in the case of federal employees. This device cannot be used without the consent of Congress.[194]

Intergovernmental immunity as between a state and its local units is, of course, a matter of state policy. Even where local units have a measure of constitutional home rule the state-local relationship is not closely comparable to the federal system. The local units are creatures of the state and the state can take steps to adjust any unbalance.

A state employee who resided in Philadelphia sought to enjoin

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190 *But see* Kiker v. Philadelphia, 346 Pa. 624, 640, 31 A. 2d 289, 298 (1943) (dissenting opinion).

191 James v. Dravo Contracting Co., 302 U. S. 134 (1937).

192 Kiker v. Philadelphia, 346 Pa. 624, 31 A. 2d 289, *cert denied.*, 320 U. S. 741 (1943).

193 *Ibid.*

194 The Comptroller General has ruled that withholding of the salaries of federal employees could not be required under an Oregon income tax law. Comp. Gen. Dec. B — 72432, Jan. 6, 1948.

the collection of the city's income tax from her.[195] The grant of power to tax made by the Sterling Act is couched in very broad language and there is no exception favoring state personnel. The city prevailed. The statute covered the case and so did the ordinance since it applied to "residents of Philadelphia."[196] Intergovernmental immunity was rejected on substantially the same reasoning as we have employed in the preceding paragraph.

Collection from state personnel may not be effected by the withholding device unless the state is willing to play ball. Pennsylvania refused to withhold for Philadelphia, nor would the state furnish the city a list of state employees.[197] The court, in the case last cited, observed that the city could not "command" action by a superior power,[198] but that merely affected the difficulty of collecting the tax and not the validity of the levy. The court would not accept the contention that enforcement would, by reason of state non-cooperation, be so uneven as to state personnel as to render the levy fatally unreasonable. This does, however, pose a substantial practical problem of tax administration and tax equity.

A good many land-going "sea-lawyers" like to think that a state area, such as the state capitol building and grounds, is a political island in the city in which it is located and, thus, the earnings of a non-resident of the city works in the area or of a person who both works and resides in the area are not subject to the taxing jurisdiction of the city. This, we suggest, is a mistaken notion. The money is, technically, earned in the city. Usually, it will be found that the municipality bears the responsibility for providing one or more services, such as fire protection, in the area. That is responsive to the benefit theory of jurisdiction to tax. The Pennsylvania court considers it enough that there be potential benefits as where a city has the governmental responsibility to provide one or more services although another government is actually doing the job.[199] One working in a state area, such as a state office building, will receive substantial city benefits in the form of protected access to his place of

[195] Marson v. Philadelphia, 342 Pa. 369, 21 A. 2d 228 (1941).

[196] Philadelphia Ord. § 2. The provision of the ordinance of Dec. 13, 1939 in this respect, of course, has not been changed by the amendments.

[197] Marson v. Philadelphia, 342 Pa. 369, 21 A. 2d 228 (1941). It has been reported that Toledo received "very fine cooperation from the federal offices as well as the county and the school board" in compiling lists of taxpayers. Tillman, *Actual Problems Involved in Setting Up Local Income Tax Administration* in INCOME TAX ADMINISTRATION 324 (Symposium conducted by the Tax Institute 1948). The same writer states that some firms located outside of Toledo have withheld the tax from employees who are residents of Toledo at the request of those employees. *Id.*

[198] 342 Pa. 369 at 375, 21 A. 2d 228, 231.

[199] Kiker v. Philadelphia, 346 Pa. 624, 31 A. 2d 289, *cert. denied,* 320 U.S. 741 (1943).

work and the availability of the various public and private facilities of urban living.

What has been said concerning state personnel is equally applicable to officers and employees of local units other than the levying authority. Without the aid of statute it is not likely that a city might compel a county, for example, to withhold the city tax on the salaries of county personnel.[200] Here it is more a matter of one local unit placing a burden upon a separate governmental agency on roughly the same level than of giving orders to a superior. But, even so, the levying unit should be called upon to point to some authority for requiring such assistance.

The 1949 amendment to Pennsylvania Act No. 481 authorizes local units levying taxes under the act to make joint agreements for their collection and to use the same person or agency to do the collecting.[201]

In the area of investment income the constitutional immunity of the income received by individuals by way of interest on United States securities still survives.[202] Here again Congressional consent would be necessary to pave the way for effective state or local action. The income from "municipals," obligations of states and of local units of government, is quite another matter. There is no implicit constitutional immunity, even in the case of local taxation of the income from securities of the parent state. The matter depends entirely upon actual exemption effected by positive law.

A not insignificant aspect of intergovernmental relations at the local level is the problem of multiple local taxation of the same income. Thus far it has not become acute in Ohio; only a scattering of Ohio municipalities have income levies. Nor is there any state regulation of the subject. The Dayton ordinance allowed a credit to residents for taxes paid to any other city on income subject to the Dayton tax but only to the extent of the Dayton tax attributable to that income.[203] The other Ohio cities make no allowance for taxation by another city.

The Pennsylvania situation is more complex; various types of local units, some of which may physically overlap, have the authority to impose income taxes.[204] Philadelphia, the only Sterling Act city, has the inside track. There is nothing in that act on multiple

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200 *But cf.* Wilkinsburg Borough v. School District of Wilkinsburg, 40 PA. MUN. L. R. 221 (1949) to the effect that a municipality may require school district officials to collect and pay over a municipal amusement tax.

201 Act 481 of 1947 § 4, as amended by Act 246 of 1949, PA. STAT. ANN. tit. 53, § 2015.4 (Supp. 1949).

202 See Fordham, LOCAL GOVERNMENT LAW 178 (1949).

203 Dayton Ord. § 17.

204 Act 481 of 1947 as amended by Act 246 of 1949, Pamphlet Laws 398, PA. STAT. ANN. tit. 53, § 2015-1 *et seq.* (Supp. 1949).

local taxation, but Section 5 of Act No. 481 of 1947 provides that payment of any tax to a local unit under an ordinance or resolution passed or adopted prior to the effective date of Act No. 481 shall be credited to and allowed as a deduction from liability for any like tax on earned income or for any income tax imposed by any local unit under Act No. 481. This, in effect, leaves Philadelphia with undisturbed precedence over Act No. 481 local units under the Philadelphia income tax ordinance as amended down to the effective date of Act No. 481.[205] This applies to Philadelphia income of non-residents and all income of residents of the city. Doubtless, a later amendment increasing the rate of the tax would enjoy priority but an amendatory ordinance extending its application would not.

With respect to non-overlapping Act No. 481 local units it is first to be observed that the 1949 amendments denied to second, third and fourth class school districts authority to impose taxes on earned income of non-residents, whether taxed by the unit of residence or not.[206] Section 5 of Act No. 481 deals with the situation where both the unit of residence and that of the production of income seek to tap earned income by giving the local unit of residence priority; the taxpayer is allowed a credit for the amount paid the unit of residence against his liability for a like tax of any other unit under the act. It is significant that the credit is not, in terms, confined to that part of the tax of the unit of residence attributable to income subject to tax by the other unit. This could obviously become important in a situation where the unit of residence had a lower rate. There has been no reported judicial ruling on the question. It has been decided that where the unit of residence levies the maximum one per centum rate and the taxpayer's place of work lies in two other units, which are coterminous and each of which has a one per centum levy, he is entitled to the full credit against the tax of each of the latter units.[207] In a companion case the facts were reversed; the taxpayer lived in two coterminous units and worked in a third. He tried unsuccessfully to pay just one of the two units of residence and credit that against the tax of the coterminous unit as well as that of the unit of employment.[208]

As indicated in the case last cited, a taxpayer may not credit payments to the unit of his residence against his liability to an overlapping unit of residence. The same would be true under Act No.

[205] It has been pointed out that the result of this situation is that no other local income taxes have been levied in the Philadelphia area. Smedley, LEGAL PROBLEMS INVOLVING ACT 481, 9 (Bureau of Municipal Affairs, Department of Internal Affairs of Pennsylvania, undated).

[206] Act 481 of 1947 § 1 A (5), as amended by Act 246 of 1949, PA. STAT. ANN. tit. 53, § 2015.1 (Supp. 1949).

[207] Morgan v. Glen Alden Coal Co., 165 Pa. Super. 203, 67 A. 2d 756 (1949).

[208] Glen Alden Coal Co. v. Thomas, 165 Pa. Super. 199, 67 A. 2d 754 (1949).

481 with respect to two overlapping units in which a non-resident's place of work was located. The 1949 amendments to Act No. 481 take a fresh tact as to overlapping units; they simply confine each of two such units levying a tax to one-half the statutory maximum rate or to such share of the maximum as the two may determine by agreement.[209]

Administration

Administrative organization for local income tax purposes has generally been provided by placing the responsibility for administration and enforcement upon the holder of an existing office and leaving him to add the necessary additional staff. Philadelphia proceeded in this wise,[210] although the Sterling Act authorizes the creation of such bureaus and provision for such personnel as may be deemed necessary.[211] There is a similar provision in Act No. 481 of 1947 which has been made use of.[212] The City of Sharon ordinance, for example, creates a "Sharon income tax bureau" and establishes an office of chief clerk of the Sharon income tax bureau, who is constituted at the same time receiver of the taxes levied by the ordinance.[213]

Most of the Ohio income tax cities have rested the administrative responsibility upon the holders of existing offices but have, in addition, established a new administrative agency called a board of review or a board of tax appeals. The function of these boards will be discussed at a little later juncture in this paper.

The City of Springfield income tax ordinance established a department of income taxation headed by the city manager and consisting, in addition, of a board of review and a commissioner of taxation together with such staff as might be provided.[214] The commissioner of taxation is made the primary tax administrator. There is a legal question in Ohio as to the manner of exercising home rule powers with respect to the organization of municipal government. As applied to the Springfield ordinance the question would be whether the organization it establishes was properly set up by ordinance or should have been provided for by home rule charter amendment. If one accepts the "bare bones" theory of charter-making the Springfield ordinance is clearly valid in this respect. Judi-

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[209] Act 481 of 1947 § 1 E, as amended by Act 246 of 1949, Pa. Stat. Ann. tit. 53, § 2015.1 E (Supp. 1949).

[210] Philadelphia Ord. § 5. 6.

[211] Pa. Stat. Ann. tit. 53, § 4613 (Supp. 1949).

[212] Act 481 of 1947 as amended by Act 246 of 1949 § 4, Pa. Stat. Ann. tit. 53, § 2015.4 (Supp. 1949).

[213] Sharon Ord. No. 1190 (1948) § 3, 4.

[214] Springfield Ord. § 13.

cial experience with the problem has not been such as to mark a sharp line.[215] The attorney general has indicated that the establishment of a civil service commission of a city is something that must be done by charter instead of ordinance.[216] It is our thought that an administrative organization set up to administer a municipal income tax would fall on the other side of the line on the theory that it is not so closely joined to the basic framework of municipal government.

The Philadelphia ordinance authorizes the receiver of taxes to "prescribe, adopt, promulgate and enforce rules and regulations relating to any matter or thing pertaining to the administration and enforcement of the provisions of this ordinance, including provision for the re-examination and correction of returns and payments alleged or found to be incorrect or as to which an overpayment or underpayment is claimed or found to have occurred."[217] Here again the Quaker city has set the pattern; we have found similar language in every ordinance reviewed. There are, of course, variations. Thus, the City of Sharon, Pennsylvania, confers the rule-making power upon the city solicitor instead of the tax administrator.[218] In Toledo the rules are subject to the approval of the city manager and the board of review.[219] In Columbus and Springfield they are subject to the approval of the board of review alone.[220] Springfield attempts to be a little more specific by defining a regulation as something not in conflict with the provisions of the ordinance.[221] While the effect is to confer upon the rule- making officer some power to fill in the content of the ordinance his authority is what would conventionally be described as power to make interpretative rules as distinguished from sub-legislation.[222]

What amounts to broader rule-making power as to a particular problem has been conferred by several ordinances. The Toledo ordinance, in order to take care of the situation where only part of the business activity of the individual or corporation is conducted in the city, provides a formula for the allocation of net profits and adds that in the event a just and equitable result cannot be obtained by use of the factors set out in the ordinance the board of re-

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215 See Fordham and Asher, *Home Rule Powers in Theory and Practice*, 9 OHIO ST. L. J. 18, 27 *et seq.* (1948).

216 1941 OPS. ATT'Y. GEN. (Ohio) No. 3846.

217 Philadelphia Ord. § 6.

218 Sharon Ord. § 11 A.

219 Toledo Ord. § 8, 13.

220 Columbus Ord. § 14; Springfield Ord. § 13 (b).

221 Springfield Ord. § 1.

222 The Pennsylvania Supreme Court has so described the rule-making power under Philadelphia Ord. § 6. Murray v. Philadelphia, 71 A. 2d 280 (Pa. 1950); Pennsylvania Co. v. Philadelphia, 346 Pa. 406, 31 A. 2d 137 (1943).

view should have authority to substitute factors calculated to effect a fair and proper allocation.[223] The St. Louis ordinance confers similar authority upon the collector but expressly sets as a ceiling the amount of tax which would be arrived at by the application of the methods of allocation spelled out in the ordinance.[224] The Toledo provisions are somewhat more vulnerable since they would permit of the substitution by an administrative board of factors of allocation which would result in a higher tax than that to be arrived at by use of the specific allocation provisions of the ordinance.

Returns—Taxpayer Accounting

The Philadelphia ordinance, as amended down to December, 1949, has a separate scheme of returns for three different classes of taxpayers. A person taxed on his net profits makes an annual return on or before March 15 or within 75 days after the end of his fiscal period if it is other than the calendar year.[225] A person who is an employee on a salary, wage, commission or other compensation basis, who is subject to the tax but is not affected by the withholding provisions, or being affected, whose tax is not withheld and paid to the city by his employer, must file a return and pay quarterly.[226] Employers in Philadelphia must withhold and pay the tax quarterly with respect to employees whose compensation is subject to the levy.[227] Employees who have income subject to the tax which is covered by employers' returns required by the ordinance do not have to file as to that income.[228] With respect to all classes of taxpayers affected by the ordinance the forms of returns are prescribed by the receiver of taxes.

Columbus, Ohio, has a system of returns more nearly paralleling the federal plan. Columbus requires collection at the source and quarterly return and payment.[229] The actual taxpayers, however, whether their income be net profits from business or professional

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223 Toledo Ord. § 3 (5) b.

224 St. Louis Ord. § 3 (c).

225 Philadelphia Ord. § 3 (a), as amended March 31, 1948.

226 Philadelphia Ord. § 3 (b), as amended March 31, 1948.

227 Philadelphia Ord. § 4 (a), as amended March 31, 1948. It has been held that an employer must withhold pursuant to regulations of the Receiver of Taxes promulgated under the ordinance. Philadelphia v. Westinghouse Electric Co., 55 Pa. D. & C. 343 (1945).

228 Philadelphia Ord. § 3 (b), as amended March 31, 1948. Section 4 (b), as amended March 31, 1948, which permits the receiver of taxes to accept the returns of employers as those required of the employees when the income from that source is the sole income subject to the tax, presumably covers situations where the employer is not legally bound to withhold and file a return but does so voluntarily.

229 Columbus Ord. § 5.

activities or be compensation as employees, must file only one return a year and that on or before March 15.[230] In addition, a taxpayer who anticipates any income which is not subject to collection at the source must file a declaration of estimated tax for the current year on or before March 15 and pay at that time at least one-fourth of the estimated tax for the full period.[231] The remainder of the estimated tax must be paid quarterly on the same footing as the federal tax.

Mandatory provision has been made for taxpayer accounting on an accrual basis in certain circumstances. Where a taxpayer who is taxable on net business profits keeps his books on an accrual basis or uses such a basis for Federal Income Tax purposes he is required to use it for returns made pursuant to the local tax.[232]

Taxpayers taxable on net business profits are not restricted to using the calendar year accounting period. A fiscal year which ends on the last day of some calendar month and which is acceptable for Federal Income Tax purposes may be used by such taxpayers.[233]

Inventories must be used where necessary to reflect accurately net business profits. The same basis of valuation used for Federal Income Tax purposes is generally required.[234] Two methods very commonly used are "cost" and "cost or market, whichever is lower." In any event consistency is more important than the method selected. The Federal Internal Revenue Code prescribes that inventories shall be used whenever they are necessary to determine clearly the income of any taxpayer.[235] There is reason to believe that local units will follow this general rule.

Collection at the source is a common feature of the local income tax measures which have been examined in the preparation of

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230 *Id.* at § 4. A taxpaper reporting on the basis of a fiscal year other than the calandar year must file on or before the fifteenth day of the third month after the close of his fiscal year. See note 233 *infra.*

231 *Id.* at § 6.

232 Columbus Regs. Art. II — 10 (b); Dayton Regs. Art. II — 3 —3 (b) ("the usual accounting system of the taxpaper"); Louisville Regs. Art. II — 5 (b); Philadelphia Regs. Art. II — 7 (b); Springfield Regs. § II — 8 A; Toledo Regs. Art II—9 (b); Warren Regs. Art. II—9 (b); Youngstown Regs. Art. II — 9 (b).

233 Columbus Regs. Art II—9; Dayton Regs. Art. II—1; Louisville Regs. Art II—4; Philadelphia Regs. Art. II—6; St. Louis Regs. § 13; Sharon Uniform Regs. Art. III — B — 4 (by implication); Springfield Regs. § III — 3; Toledo Regs. Art. II — 8; Warren Regs. Art. II — 8; Youngstown Regs. Art. II — 8.

234 Columbus Regs. Art II — 10 (a); Louisville Regs. Art. II — 5 (a); Philadelphia Regs. Art. II—7 (a); Springfield Regs. § II—8 E; Toledo Regs. Art. II — 9 (a); Warren Regs. Art. II — 9 (a); Youngstown Regs. Art II — 9 (a).

235 INT. REV. CODE § 22 (c).

this paper. As a matter of fact that device, copied from the federal system, is one of the things which makes the tax attractive to local units. It greatly facilitates administration for the levying authority and, in most instances, actually keeps down the cost of administration by imposing the burden of collection upon the employer without making any allowance to him for his trouble.[236] It is significant in this connection that the St. Louis enabling statute expressly gives the employer the right to keep three per centum of the amount collected to offset the expenses of collection.[237]

There is a common provision that any tax collected by the employer by withholding at the source shall be deemed a trust fund in the hands of the employer for the benefit of the levying unit until it is payed to the latter.[238] Until the payment to the local unit is actually made, the employee still has an interest since he is entitled to full payment of his compensation either to himself or to some other party legally entitled to take through him. So far as he is concerned there is nothing but a simple contract obligation. It is not evident that as between him and the employer the city can change the contract relationship to a trust nexus. The employer is not required to earmark any funds and as a matter of practice he would be expected simply to pay the levying unit with one check for the full amount to be collected from all employees subject to the tax. The withholding each pay day is merely a bookkeeping matter. In view of these circumstances it would appear rather difficult to lay hand at any stage of the game upon something which could be labeled a trust *res*. This conclusion is reinforced by the fact that the ordinances carefully provide that non-payment by the employer does not excuse the employee. Are we to permit the levying unit to say in the same breath that the employer without earmarking any funds holds something in trust for the unit but that until actual payment to the city the employee remains liable?

Administrative Review

The Philadelphia ordinance makes no provision for administrative review. Nor do the Louisville and St. Louis measures. The

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[236] See, *e.g.*, Toledo Ord. § 6. For a commentary on the burden imposed on employers see Homuth, *The Taxpayer Angle on Local Income Tax Administration*, in INCOME TAX ADMINISTRATION (Symposium conducted by the Tax Institute 1948).

[237] MO. REV. STAT. ANN. § 7780.8 (Supp. 1949).

[238] Columbus Ord. § 5; Dayton Ord. § 5; Springfield Ord. § 5; Toledo Ord. § 6; Warren Ord. § 5; Youngstown Ord. § 5. The withholding provisions of the following municipalities do not employ trust terminology: Louisville Ord. § 3; Philadelphia Ord. § 4 as amended; St. Louis Ord. § 6; Sharon Ord. § 10.

Ohio cities which have, as we have seen, been drawing upon home rule power in levying income taxes, do provide a scheme of administrative review. The Columbus ordinance is generally illustrative, if not typical. Under it the city auditor, who is the administrator of the tax, issues a proposed assessment to any taxpayer or an employer who has failed to pay the full amount of the tax due or of funds withheld.[239] When the proposed assessment is served upon a taxpayer or employer, he is allowed 20 days within which to make written protest. If the protest is filed the auditor must allow him an opportunity to be heard. After the hearing the auditor issues a final assessment. A proposed assessment automatically becomes final in the event the protest is not filed within the time allowed. In either case the final assessment must be served upon the taxpayer and he is allowed 30 days to file a written notice of appeal with the board of appeals. In Columbus this board consists of the city attorney, or his designate, the city auditor, or his designate, and a representative citizen appointed by the mayor. If a notice of appeal is duly filed with the board, the taxpayer is allowed a hearing at the conclusion of which the board examines, reviews or modifies the final assessment. Presumably one who is subject to the tax would have to exhaust this process of administrative review before seeking judicial redress.

ENFORCEMENT

Where the power to levy the tax depends upon enabling legislation, the same will be true of means of enforcement. In Pennsylvania the Sterling Act empowers a levying unit to fix and enforce penalties for non-payment or for violation of the provisions of a tax ordinance.[240] Act 481 of 1947, as amended in 1949,[241] has a similar provision, except that it authorizes "reasonable" penalties. No mention is made of civil suits but it must be implicit that the taxpayer may be subjected to personal liability enforceable by civil suit. Likewise, the exaction of interest at not exceeding the legal rate is no more than claiming damages for delay in payment, authority for which may be reasonably implied. The Philadelphia ordinance accordingly expressly provides for recovery of unpaid taxes, with interest and penalties, like any other debt.[242] This has set a

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239 Columbus Ord. § 9.

240 PA. STAT. ANN. tit. 53, § 4615 (Supp. 1949).

241 Act 481 of 1947 § 7, as amended by Act 246 of 1949, PA. STAT. ANN. tit. 53, § 2015.7 (Supp. 1949). The question as to whether the Pennsylvania Local Tax Collection Act of 1945, PA. STAT. ANN. tit. 72, § 5511.1 *et. seq.* (Supp. 1949), applies to taxes levied under Act 481 as amended is apparently an open one. The writers express no opinion on it.

242 Philadelphia Ord. § 8.

pattern followed by other local units levying income taxes.

The Pennsylvania statutes speak of penalties; they do not refer to imprisonment.[243] The Philadelphia ordinance provides for a $100 fine and for imprisonment for non-payment of the fine within ten days. This is in keeping with the historic notion that a fine imposed by a local by-law is a civil liability to be enforced primarily by civil action but supported, in turn, by the sanction of imprisonment.[244] The Wisconsin court has recently gone so far as to say that a statute which authorized a local unit to define a misdemeanor or to make imprisonment a primary punishment for a forbidden act would be unconstitutional.[245] The explanation was that only the state may define a crime or provide for its punishment. This is a juristic "throwback" which has been justly criticized.[246] What difference is there, if the purpose of the fine is punitive?

The Ohio ordinances expressly make violations misdemeanors punishable by fine or imprisonment, or both. There is little doubt that home rule power carries this far.[247] Ohio has not been troubled about the devolution upon municipalities of power to define misdemeanors and provide for their punishment.[248] The Columbus, Ohio, ordinance is unique among the many Ohio and other measures we have examined in expressly making wilfulness an element of the conduct for which one may be penalized.[249] All ordinances examined subject a person who "knowingly" makes an incomplete, false or fraudulent return to penalty but all save that of Columbus penalize simple failure, neglect or refusal to make a return or to pay the tax, interest and penalties due.

Most of the ordinances reviewed make no specific reference to sanctions directed to employers who are required to withold the tax with respect to salaries and wages. They do provide penalties for failure, neglect or refusal "of any person" to make a required return, for refusal to permit official examination of his books, records and papers or for attempts to do anything to avoid the payment of the whole or any part of the tax. The original Philadelphia ordinance is typical in this respect.[250] It doubtless applied to an employer

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243 PA. STAT. ANN. tit. 53, § 4615 (Supp. 1949) (the "Sterling Act"); Act 481 of 1947 § 7 as amended by Act 246 of 1949, PA. STAT. ANN. tit. 53, § 2015.7 (Supp. 1949).

244 Dillon, MUNICIPAL CORPORATIONS § 625 and n. 3 (5th Ed. 1911).

245 State *ex rel.* Keefe v. Schmiege, 251 Wis. 79, 28 N.W. 2d 345 (1947).

246 1 VAND. L. REV. 262 (1948).

247 Fordham and Asher, *Home Rule Powers in Theory and Practice*, 9 OHIO ST. L. J. 18, 68 (1948).

248 OHIO GEN. CODE § 3628. Greenberg v. Cleveland, 98 Ohio St. 282, 120 N.E. 829 (1918).

249 Columbus Ord. § 13.

250 Philadelphia Ord. § 9.

with respect to all of the matters mentioned. When it comes to non-payment of the tax only the taxpayer himself is subject to penalty. The Columbus, Ohio, ordinance expressly makes it a misdemeanor for any employer wilfully to fail, neglect or refuse to deduct, withhold and pay the tax.[251] It is less drastic in requiring wilfuness, but more exacting in covering withholding and payment as well as the filing of returns, access to records and conduct designed to avoid full disclosure.

No instance of an attempt to make a local income tax a lien upon the property of the taxpayer has been encountered. It is arguable that a local unit with home-rule power to levy an income tax may, by way of implementation, make the tax a lien upon the property of the delinquent taxpayer as well as make him subject to penal sanctions. Municipalities in Ohio have home rule powers to operate public utilities[252] and it has been determined that in the exercise of this power a municipality may impose upon a property owner a liability to pay a tenant's water bill.[253] If this be true, why may not home rule power be said to be broad enough to permit of the imposition of a lien for utility charges or for income taxes? While it must be evident that home rule power does not extend broadly to the enactment of private law, it is not considered a distortion to go as far as suggested here even though civil relations are directly affected.

Generally speaking, problems of enforcement are the same with respect to residents and non-residents. Thus, if a non-resident is in default on a municipal income tax imposed on income earned within the municipality, he, as well as the resident, can be subjected to penalty. The Supreme Court of Pennsylvania had no difficulty in reaching this conclusion with respect to residents of New Jersey working at the League Island Navy Yard, which is located within the geographical limits of the City of Philadelphia.[254]

With respect to the civil liability of a non-resident we are faced with the pronouncement in *Dewey v. Des Moines*[255] to the effect that a state is without legislative jurisdiction to impose personal liability upon a non-resident owner for a special assessment. Actually, there was no provision for personal service in that case and none was made upon the non-resident. It is not evident why personal liability may not be imposed on the basis of personal jurisdiction of the non-resident being obtained in the enforcement pro-

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[251] Columbus Ord. § 13.

[252] OHIO CONST. Art. XVIII, § 4. See Comment, 9 OHIO ST. L.J. 141 (1948).

[253] Pfau v. Cincinnati, 142 Ohio St. 101, 50 N.E. 2d 172 (1943).

[254] Kiker v. Philadelphia, 346 Pa. 624, 31 A. 2d 289, *cert. denied*, 320 U. S. 741 (1943).

[255] 173 U.S. 193 (1899).

ceeding.[256] Certainly this must be true as to a tax upon income earned within the taxing unit, since this involves the presence of the taxpayer within the jurisdiction. We venture to say that it would be so as to a levy upon income from property within the unit.

Taxpayers' Remedies

The redoubtable Teufelsdröckh was no more amenable to the charge of prolixity than are the authors of this paper.[257] Thus, it is proposed largely to pretermit the topic of taxpayers' remedies. Under the head of administration we have already touched upon the efforts of Ohio cities to provide a scheme of administrative review.[258]

Under Pennsylvania Act No. 481, as amended in 1949, a local tax measure may not take effect for at least 30 days after adoption and in the interim "aggrieved" taxpayers of the unit may "appeal" to the court of quarter sessions.[259] While the court is charged by the act not to interfere with the reasonable discretion of the local governing body as to tax subjects or rates, it has authority to determine whether a tax is excessive or unreasonable and may even reduce the rates of tax. An appeal may be taken to the Supreme or Superior Court as in other cases. Since the statute sets a maximum of one per centum for taxes on earned income of individuals it is hardly likely that a charge of excessiveness or unreasonableness would be sustained as against a levy within the stated limit. It is unusual to empower the judiciary to reduce tax levies; certainly in some jurisdictions it would present a troublesome separation of powers question.

The recent invalidation of the Dayton, Ohio, levy has bred some nice questions with respect to previous collections. It is being contended, we understand, that collection at the source should be considered involuntary payment not governed by the general statutory provision for filing written protest to ground recovery on the ground of illegality.[260]

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[256] See Nickey v. Mississippi, 292 U. S. 393 (1934) which allowed resort to property other than that taxed to enforce collection of a non-resident's ad valorem taxes. See also Rubin, *Collection of Delinquent Real Property Taxes by Action in Personam*, 3 Law and Contemp. Prob. 416, 422 (1936).

[257] Carlyle, Sartor Resartus 22 (Edinburgh Edition 1903).

[258] See page 263 *supra*.

[259] Act 481 of 1947 § 3, as amended by Act 246 of 1949, Pa. Stat. Ann. tit. 53, § 2015.3 (Supp. 1949). The "aggrieved" taxpayers are those "representing 25% or more of the total valuation of real estate in the political subdivision or assessed for taxation purposes, or taxpayers of the political subdivision not less than 25 in number aggrieved by the ordinance or resolution. . ." *Id.*

[260] Ohio Gen. Code §§ 12075, 12077 are applicable generally to suits to recover taxes paid. See Alaska Packers Ass'n. v. Hedenskoy, 267 Fed. 154

Some Policy Implications

It seems fairly safe to say at once that considerations of expediency have had important influence in the resort by a local government to income taxation. It calls to mind state experience with the sales tax during the gloomy depression period of the early 1930s. A number of states turned to retail sales taxes during that period because of the urgent need of revenue without concerning themselves too much with the broader implications of the levy. Somewhat parallel has been the resort by a growing number of local units to income taxation in recent years. The case for the levy has been more that it is a good revenue producer than that it is an equitable method of taxation which fits as well as may be into the existing tax melange. It is understandable that flat rate income tax would have its appeal to hard pressed local units.

In support of the flat rate local income tax, several factors can be mustered. (1) The levy involves the assumption of local responsibility for raising the money to be expended in local public administration. There is certainly much to be said for imposing responsibility for raising local revenue upon those who are to spend it rather than encouraging resort to state and federal governments for shared taxes and grants in aid. This point is grounded upon the assumption that there is a strong nexus between local responsibility for tax levies and a high quality of stewardship in local expenditure.

(2) A favorable factor which has already been noted is that the tax is a good producer. Since it is usually imposed as a flat rate on gross salaries and wages without exemptions or deductions, it is not likely, moreover, to be affected as much as a true graduated net income tax by fluctuations in economic conditions.

(3) The tax enables a local unit to draw some financial support from so-called "daylight citizens." A municipality as we have seen, would not have much difficulty in making a substantial case, in terms of benefits conferred, for taxing non-residents who receive the benefits of its governmental services from day to day in conducting their business or professional activities within its confines.[261] This is particularly true of the commuter who does not own taxable property within the unit.

(4) The fact that a municipality can reach the daylight citizen by the levy of an income tax has significant implications with respect to the relation of peripheral municipalities and unincorporated

(9th Cir.), *cert. denied*, 254 U.S. 652 (1920). (Suit by employee against employer who withheld tax from wages.)

[261] See note 96 *supra*. Angell v. Toledo, 153 Ohio St. 179, 91 N.E. 2d 250 (1950) involved imposition of the tax on a non-resident.

suburbs to a primary city. The use of an income tax by the primary city is calculated to overcome some of the resistance to the extension of the city limits to the actual borders of the metropolitan area.[262] In our view this is a very favorable factor since we believe that it is in the public interest to foster the type of metropolitan development just mentioned. By and large, the boundaries of the primary general function local unit of government should conform to the metropolitian area in which services of the type it renders are expected to be administered.[263] Not the least objection to the present unhappy hodgepodge of local units in a given metropolitan area is the fact that thousands of the best trained and most influential people of the major community do not live in the primary city and have no direct political voice in or responsibility for its affairs.

(5) While the tax imposes a considerable burden upon employers engaged in collection at the source the cost of administration to the taxing unit is relatively low. In the City of Toledo, Ohio, for example, the cost has been 3.3c per tax dollar collected.[264] This figure is for the first three years of operation and includes the total original expense for equipment. There is reason to believe that the cost will be substantially less during the next three years.

(1) One of the most disturbing criticisms of the local income tax in the form employed thus far is the charge that the levy is regressive. The levy is not graduated; it is imposed at a flat rate. Most of the local units which have employed it apply the flat rate to gross earnings of wage earners and salaried persons without either deductions or exemptions. In the case of business or professional people, however, the tax is imposed on net earnings. While we cannot document the statement, we believe that the general effect of this is to favor people of larger incomes.

It is clear that the tax is regressive in that it means more as a deduction from gross income for federal income tax purposes the greater the income of the individual. The fact that little investment income has been taxed by local income taxes is favorable to widows and orphans dependent upon that type of income but, as between wage earners and people of larger income, the latter are more likely to have investments and, thus, to enjoy income not affected by the tax.

A flat tax rate of the sort under scrutiny hardly deserves the

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262 Anderson, *Income Tax Aids Annexation*, 38 NAT. MUN. REV. 443 (1949).

263 In the prevalent situation where the primary units' boundaries are more restricted than those of the metropolitan area, it is well known that devices such as functional consolidation, service contracts and ad hoc units are necessarily utilized.

264 *Report of the Citizens' Income Tax Committee*, 34 TOLEDO CITY JOURNAL 822 (1949).

name in modern parlance, of an income tax. The complications of a graduated levy such as that employed by the Federal Government would present difficult administrative problems to an ordinary local unit and it may not be expected to have the human and other resources required for competent administration of such a tax. The difficulties of administration of a graduated tax do not provide convincing justification for a flat rate tax, however, if the operation of the latter results in serious inequalities. There is an interesting possibility here which was considered in connection with the St. Louis levy and ultimately rejected.[265] Where the state itself imposes an income tax, local units might be authorized to impose an additional levy on the income of persons subject to their taxing jurisdiction. It would constitute a "supplement" to the state levy and both would be administered by state tax authorities. On that basis the local unit would bear the responsibility for its levy but the state would be the administrator and would simply return to the local unit the fruits of its "tax supplement." Thus, that kind of an arrangement could be geared to a graduated income levy which made proper allowance for expenses incurred in producing income, for dependents, and so on.[266] In this connection it has been observed that a municipality is too narrow a base for a corporate income tax in view of the difficulty of allocating corporate income.[267] Toledo and other cities which have followed her lead have obviously not considered this difficulty of allocation insurmountable in levying a flat rate tax, but that does not, without more, invalidate the objection.

(2) Does a local unit embrace an adequate territorial and economic base for an individual or corporate income tax? Even at the state level income producing activity pays little heed to boundary lines on a map. On the local scene this is all the more evident. The result is that, in the case of residents, there may be taxation of large "outside" income on a basis not at all proportioned to benefit, and, in the case of non-residents and corporations, a difficult problem of allocation of income may be confronted. The cry of "no taxation without representation" has also been voiced in this modern context, particularly by non-residents, but we are not disposed to dignify it. In this day taxation without representation is

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[265] See, PERMISSIVE TAXATION VERSUS STATE SUBSIDY (Missouri Public Expenditure Survey, January 1948).

[266] The Montreal Income Tax, which was based on a proportion of the income tax paid to the Dominion, utilized graduated rates. Hillhouse, WHERE CITIES GET THEIR MONEY 108 (Municipal Finance Officers Association 1945). Mississippi municipal sales taxes are collected by the state tax commission and returned to the cities after deduction of five per centum for cost of administration. FROM THE STATE CAPITALS (prepared by Bethune Jones) May 1950, p. 1.

[267] Sly, *Tax Supplements For Municipalities*, 8 TAX REVIEW 7 (1947).

inevitable; reference to taxation of corporations is enough to make this clear.

(3) Many of the vagaries of the ad valorem property tax are common knowledge and its faults in general are so great there is no disposition here to urge that its use be extended. There is a question, however, whether or not the type of local income tax we have been discussing provides too ready an escape from responsibility to make the best use of the ad valorem tax system within its present framework. There is enough information at hand to make one doubt most seriously whether the general property tax is as productive as it should be in some of the cities which have levied income taxes. In Columbus, Ohio, for example, property tax assessments were less in 1948 than they were in 1925.[268] At the same time, the tax rate is one of the lowest in the United States among cities of comparable size.[269] It would take electoral approval to increase ad valorem levies beyond the constitutional 10 mill limit but one might suppose that the matter of additional revenue to keep essential services going could be effectively enough brought home to the voters to get support for a levy required to prevent serious disruption of local public services.[270] To point to an extreme case, taxable values in Fayette County, Ohio, in 1948 were approximately 25 per centum below the 1911 total.[271] Ready recourse by a local unit to an earnings tax is hardly calculated to stimulate efforts to make the most effective use of the existing ad valorem tax system.

(4) Collection of an earnings tax at the source imposes a heavy burden upon employers for which, under the usual scheme, no financial allowance is made. In many instances the expense of administration imposed upon an employer will exceed the amounts collected, particularly where it is required that the employer file information returns on all employees.[272]

(5) The difficulty of getting a complete list of all persons liable to pay a local income tax, whether they be residents or non-residents in public or private activities, employees or self-employed, is a

[268] In 1925 realty and utility assessments were $464,166,050 and in 1948, $419,863,020. There has been but little variation in the figure for the intervening years during which prices have increased markedly. Letter to the writers from Dr. L. E. Smart of the Ohio Department of Taxation dated May 23, 1950.

[269] *Tax Rates of American Cities* 1949, 39 NAT. MUN. REV. 17, 23 (1950).

[270] Portsmouth, Ohio, was able to obtain electoral approval of such an ad valorem levy on the understanding that the municipal income tax would be repealed if the levy passed. See note 5 *supra*.

[271] Columbus (Ohio) Dispatch, March 19, 1950, p. 6 B, Cols. 5, 6.

[272] It has been suggested that employers not be required to file information returns for employees. Homuth, *The Taxpayer Angle on Local Income Tax Administration*, in INCOME TAX ADMINISTRATION 329, 346 (Symposium conducted by The Tax Institute 1948).

drag on enforcement. Unless it is substantially overcome uneven enforcement, which means unequal taxation, will be the order of the day.

(6) A closely related objection is based on the doubt that most smaller local units have the resources for efficient income tax administration. It is a question whether several small levying units can obviate the difficulty by joining together for the purpose as under Pennsylvania Act No. 481 as amended.[273]

(7) Another difficulty with local income levies is that in the absence of some form of reciprocity the same income may be tapped by more than one local unit. Since the difficulty can be overcome by statute or by reciprocity provisions in local tax measures, this objection is not fundamental in character. It does, however, present administrative complications.[274]

(8) There has been no effort to think through the implications of the tax in its relation to the state and federal tax systems. Instead, as we have already seen, it sprang from the matrix of expediency and its impact in distributing the tax burden was not anticipated in terms of the relation of tax burden to governmental benefits and to ability to pay.

These are but a few meagre comments upon policy. The real task of evaluation remains to be done.

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[273] Act 481 of 1947 § 4, as amended by Act 246 of 1949, PA. STAT. ANN. tit. 53, § 2015.4.

[274] See the discussion of some of the problems presented in, ACT 481: ITS FIRST TWO YEARS OF OPERATION 21, 22 (Bureau of Municipal Affairs, Department of Internal Affairs of Pennsylvania 1949).