Unlawful Property and Activities as Subjects of Taxation

Statutes in Ohio make the keeping or exhibiting of a gambling device subject to penalty and property so used may be confiscated and destroyed.[1] Although slot machines are not gambling devices per se,[2] if they are used improperly they clearly fall within these statutes and become property of an illegal character.

Acting under the Ohio law which imposes a tax on "all property located and used in business in the state,"[3] the tax commissioner added the value of certain slot machines to a taxpayer's list of assessable personal property. In *Ellery v. Evatt*[4] the court sustained the commissioner over the taxpayer's objection that the machines were mere gambling devices, not subjects of ownership as defined by statute.[5] This appears to be the first decision in Ohio treating the validity of a tax imposed upon chattels of an illegal nature. The absence of similar cases in other jurisdictions indicates either that such property is not taxed or that the owners choose not to litigate the matter.

It is the form of the tax rather than the nature of the property subjected thereto which presents the novelty, for under the Revenue Act of 1918, which laid a federal tax on certain enumerated sporting goods and other "games and parts of games," slot machines were held taxable.[6]

The validity of classifying slot machines as games may well be questioned,[7] but the case illustrates that gambling devices, as such, are not immune to taxation.

In the two preceding cases the legislative intent to tax the particular article was an issue, but once this was decided the court had no trouble in sustaining the tax although it fell on the sale and manufacture of objects tainted with illegality.

It is not unusual to find occupation or license taxes levied

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[1] OHIO GEN. CODE §§ 13066 and 13430-8.

[2] *In re* Estate of Weisenberg, 147 Ohio St. 152, 70 N.E. 2d 269 (1946).

[3] OHIO GEN. CODE § 5325.

[4] 140 Ohio St. 249, 42 N.E. 2d. 979 (1942).

[5] The statute, Ohio Gen. Code § 5325, defines personal property as "every tangible thing being the subject of ownership" (with certain exceptions not pertinent here).

[6] Mills Novelty Co. v. United States, 50 F. 2d 476 (Ct. Cl. 1931).

[7] See Feitler v. Harrison, 126 F. 2d 449 (7th Cir. 1942) (where under a similar act punchboards held not taxable since no contest was involved).

upon businesses or activities that are in violation of the law; for example: a license tax on punchboards was upheld in Alabama, although the display of the boards was illegal.[8] The usual argument of the taxpayer in such cases is that the tax necessarily amounts to a grant of authority inconsistent with the prohibition. The United States Supreme Court rejected this argument very early in the License Tax Cases,[9] and the state courts have generally followed the high court whether the taxpayer is objecting to the payment of the tax,[10] or attempting to use payment as a defense to prosecution under the prohibiting statute.[11]

The contention that a taxing unit has no authority to tax that which is forbidden has been frequently raised in cases involving state and federal liquor taxes with little success. Ohio liquor taxes have been sustained even though levied upon traffic forbidden by local ordinance[12] or the state constitution.[13] During the federal prohibition era the federal courts were in conflict as to the congressional intent,[14] but there was general agreement that Congress still had the *power* to tax liquors. Similarly the income derived from illicit liquor traffic was held subject to federal income taxes.[15]

There is some support, however, for the theory that a thing unlawful in itself cannot be subject to any taxation; thus it was decided in Texas that the state could not levy an occupational tax on the business of selling liquor in a county in which such an occupation was forbidden by local option.[16] Likewise, in a recent Kentucky decision a proposed municipal ordinance to levy an occupation tax on slot machine and handbook operation was found to be illegal because statutes outlawed such occupations.[17]

In a recent Ohio case,[18] again involving a property tax on slot machines, the taxpayer proposed an interesting theory. He

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[8] Casmus v. Lee, 236 Ala. 396, 183 So. 185 (1935); see 118 A.L.R. 822 (1939) (Taxing Unlawful Activities).

[9] 72 U. S. 462 (1866) (federal license taxes on unlicensed dealings in lottery tickets and liquors upheld).

[10] Youngblood v. Sexton, 32 Mich. 406, 20 Am. Rep. 654 (1875); Brannan v. Schartzer, 4 Ohio App. 356, 35 Ohio Cir. Ct. Rep. 626 (1915).

[11] Palmer v. State, 88 Tenn. 553, 13 S.W. 233 (1890); State v. Caldwell, 3 La. Ann. 435 (1848); for general discussion see 110 A.L.R. 827 (1937).

[12] Conwell v. Sears, 65 Ohio St. 49, 61 N.E. 155 (1901).

[13] Kenich v. McClearly, 103 Ohio St. 457, 134 N.E. 462 (1921).

[14] Compare: Kelchun v. United States, 270 Fed. 416 (8th Cir. 1921) with Skilken v. United States, 293 Fed. 923 (8th Cir. 1923).

[15] United States v. Yuginovich, 256 U. S. 450 (1920); United States v. One Ford Coupe, 272 U. S. 321 (1926).

[16] State v. Texas Brewing Co., 106 Tex. 121, 157 S.W. 1166 (1913).

[17] Beierle v. City of Newport, 305 Ky. 477, 204 S.W. 2d 806 (1947).

[18] Capitol Novelty Co. v. Evatt, 145 Ohio St. 205, 61 N.E. 2d 211 (1945), *cert. denied* 326 U. S. 738 (1945).

complained that his interest or ownership in the machines in Ohio was without benefit, and to compel him to pay taxes without in turn granting him benefits similar to those granted like taxpayers was a denial of the rights guaranteed by both state (Art. 1 Sec. 2) and federal (IV Amendment) constitutions. This "benefits" argument is by no means unique in the field of taxation but was given an unusual application in this case. The Ohio court followed a long line of federal cases[19] and flatly rejected the contention. It is not uncommon in the field of taxation to impose a tax upon a class or upon individuals who enjoy no direct benefit from its expenditures.[20] Indeed if each tax had to be apportioned to the direct benefits received few taxes could be sustained. The familiar argument that taxation and protection are reciprocal was raised in an early Ohio case and rejected.[21]

The taxpayer's contention in *Ellery v. Evatt* that the slot machines were mere gambling devices and so not subjects of ownership as defined by the statute raises an interesting question. Lower courts in Ohio have found that no property right exists in gambling devices.[22] Courts of other jurisdictions have held that such devices cannot be replevied by a former possessor if used solely for gambling purposes,[23] but can be replevied if they are capable of any legitimate use.[24] To make such a distinction is to recognize a property right in the gambling device measured by its capacity for legal use.

In some jurisdictions where by statute gambling devices may be seized and destroyed, the constitutionality of such statute is based on the theory that gambling devices are dangerous to public welfare and are not property within the meaning of the due process clause. One would not expect to find a property tax on a slot machine in a jurisdiction where this concept obtains.

Under the Ohio statutes it is not an offense to possess a gambling device unless it is kept or exhibited for gain, and the express authorization to destroy the device is dependent upon conviction for *illegal* possession. It is difficult logically to maintain that property, which has been rendered contraband and subject to immediate seizure by the illegal use to which it has been put, can, at the same time, be owned by anyone. It would seem valid, rather, to contend that the legal ownership of a gambling device is forfeited

[19] Carmichael v. Southern Coal and Coke Co., 301 U.S. 495 (1936); Carley v. Hamilton and Snook, 281 U.S. 66 (1930); Thomas v. Gay, 169 U.S. 264 (1897).

[20] For example: 115 Ohio Laws 26 (1933) (gasoline taxes used for unemployment relief); OHIO GEN. CODE § 6212-491 (beer taxes used for unemployment relief).

[21] Stevenson v. Hunter, 2 Ohio N.P. 300 (1892).

[22] Akron v. Stoganovic, 24 Ohio N.P. (ns) 479 (1923).

[23] Mullen v. Moseley, 13 Idaho 457, 90 Pac. 986 (1907).

[24] Wagner v. Upshur, 95 Md. 519, 52 Atl. 509 (1902).

the moment it is put to the use which the statute prohibits, because such machines can be confiscated immediately upon their being so used. Indeed, one lower court in Ohio permitted destruction of a machine irrespective of its present use, on the ground that it was possible to transform it into a gambling device by removing a part.[25] If it be true that one's property in a device ceases upon its being improperly employed, the property in the slot machines, which were the subject of controversy in *Ellery v. Evatt*, had fled, the use of the machines in that case being admittedly entirely for gambling purposes. The court, however, found that the "subject of ownership" portion of the defining statute was satisfied by the taxpayer's having purchased and paid for the machines and having maintained and put them to use for gain.

It is possible that the imposition of a tax on property, ownership of which has been forfeited by reason of the illegal use thereof, results from a failure properly to distinguish between taxation of the illegal *occupation*, and taxation of the *property* used in such illegal occupation. With respect to the tax on the property, to state the proposition is to illustrate the apparent fallacy; a property tax on chattels of an illegal nature compels one to pay a duty, based on ownership, on property which is legally incapable of being owned. This objection is not present with respect to taxes levied on occupations or uses.

In the final analysis, however, whether that which is unlawful shall or shall not be taxed rests upon a policy basis. The argument against such a tax is that the attraction of the additional revenue derived therefrom tends toward a laxity of law enforcement, at least on local levels.[26] The support of the opposite view lies in the theory that taxing the unlawful is a deterrent to the crime, which supplements rather than discourages enforcement of criminal statutes. It is well known that merely prohibiting an activity seldom causes it to cease altogether, and the policy of continuing a tax cannot be regarded as unsound, since to allow the argument to prevail that a tax is a license would tend to encourage participation. Nor should the tax be withheld because no benefit is derived when it is the taxpayer who deprived himself of those benefits. Thus it appears that whether an individual is using his property in a manner forbidden by law, or engaging in an illicit business he continues to be subject to taxes of all forms.

C. Stanley Taylor and Joseph S. Wise

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[25] Steed v. Tate, Sheriff, No. 331, Greene County, Ohio, May 1930, cited in Miller v. Warren, 20 Ohio L. Abs. 443 (1935).

[26] Beierle v. City of Newport, 305 Ky. 477, 204 S.W. 2d 806 (1947). (The court condemning a local occupation tax on gambling. "Where a city's treasury is found, there may its heart be found also.")