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Charles Butler

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**BISHOP V. DISTRICT OF COLUMBIA:
TAXATION OF UNINCORPORATED
PROFESSIONALS' NET INCOME
VIOLATES HOME RULE**

The District of Columbia Self Government and Governmental Reorganization Act of 1973 (Home Rule Act)¹ is the product of one hundred years of congressional debate.² In the 1970's alone, proposals for governing the District ranged from retrocession to Maryland and Virginia³ of all but the federal enclave to statehood for the District.⁴ The District today has characteristics of a territory,⁵ a state,⁶ a city-state,⁷ and a local government.⁸ Despite such similarities, however, the District lacks several important powers common to most sovereignties.⁹ For example, Congress has retained the power to veto, by concurrent resolution, any legislative act

1. Pub. L. No. 93-198, 87 Stat. 774 (1973) (codified at D.C. CODE §§ 1-121 to 1-171 (1973 & Supp. V 1978)).

2. Since the first bill was introduced in the 43d Congress on June 1, 1874, more than 40 bills to provide some form of local government for the District have been introduced. The Senate has approved seven of them, only to have them fail in the House. S. REP. NO. 219, 93d Cong., 1st Sess. 3 (1973). See H.R. REP. NO. 482, 93d Cong., 1st Sess. 67-81 (1973). See generally Newman & Depuy, *Bringing Democracy to the Nation's Last Colony: The District of Columbia Self Government Act*, 24 AM. U.L. REV. 537 (1975).

3. A referendum on the retrocession proposal was originally included in the drafts of the Home Rule legislation. HOUSE COMM. ON THE DISTRICT OF COLUMBIA, 93D CONG., 2D SESS., HOME RULE FOR THE DISTRICT OF COLUMBIA § 1108 at 121 (1974). See H.R. 10,693, 93d Cong., 1st Sess. 33-43 (1973) (Title II — Self Government); *Proposals to Retrocede Part of District of Columbia to Maryland: Hearings on H.R. 12,823, H.R. 355, H.R. 9881, H.R. 12,922, House Comm. on the District of Columbia*, 92d Cong., 2d Sess. 252 (1972).

4. *House Comm. on the District of Columbia, Hearings on H.R. 9197 and H.R. 9599*, 92d Cong., 2d Sess. 23-28 (1972).

5. *District of Columbia v. John R. Thompson Co.*, 346 U.S. 100, 105 (1953) (the grant of legislative power to "all rightful subjects of legislation" is substantially identical with the grant of legislative powers to territories). See also Home Rule Act § 302, (codified at D.C. CODE § 1-124 (1973 & Supp. V 1978)).

6. H.R. REP. NO. 482, 93d Cong., 1st Sess. 120 (1973) (the Home Rule Act will expand the District's legislative authority to that of a state).

7. 119 CONG. REC. H8715 (daily ed. Oct. 9, 1973) (H.R. 9682 creates a city-state) (remarks of Rep. Nelson).

8. H.R. REP. NO. 482, 93d Cong., 1st Sess. 1 (1973) (the purpose of the Home Rule Act is to provide a charter for local government). See also Home Rule Act § 102, (codified at D.C. CODE § 1-102 (1973 & Supp. V 1978)).

9. The prohibitions peculiar to the District are contained generally in Title VI of the Home Rule Act. The specific legislative limitations are contained in § 602 of the Act. D.C. CODE § 1-147 (1973 & Supp V. 1978).

of the District government.¹⁰ Although to date the validity of this legislative veto power has not been seriously challenged in the courts,¹¹ another significant limitation upon the District's legislative power has already engendered considerable legal controversy.

Section 602(a)5 of the Home Rule Act prohibits the District from imposing "any tax on the whole or any portion of the personal income, either directly or at the source thereof, of any individual not a resident of the District. . . ."¹² Unable to tax the personal income of nonresidents, the District has sought to expand its revenue base by broadening the applicability of local taxes not prohibited by the Home Rule Act.¹³ One such tax is the District of Columbia Unincorporated Business (DCUB) tax.¹⁴ As enacted by the Congress in 1947, the DCUB tax is on the privilege of doing business¹⁵ or receiving income from sources within the District.¹⁶ It

10. D.C. CODE § 1-127 (1973 & Supp. V 1978). As a result, two separate legislative bodies, the city council and Congress, review the substantive merits of the proposed legislation. The effect is to give groups opposed to particular legislation two opportunities to thwart its passage: once before the city council and again before Congress. There are, however, exceptions to the congressional veto provisions. For example, § 602(c)1 provides that acts which come under the Budget and Accounting Act of 1921 (codified at 31 U.S.C. § 1 (1976), the 90 day "emergency circumstances" exception of § 412(a), and proposals to amend the charter itself (Title IV of the Home Rule Act), all require separate procedures for adoption.

11. That Congress has not vetoed any District legislation raises the question whether courts should assume Congress has acquiesced in this area.

12. While the Act defines "individual" to mean "all natural persons (other than fiduciaries), whether married or unmarried," "person" is defined as "individuals, fiduciaries, partnerships, associations, corporations, and unincorporated businesses." D.C. CODE § 47-1551c (1973). Note that Congress could have prohibited taxing the personal income of any *person* not a resident, which would have prohibited taxation of non-resident corporations and unincorporated businesses. See D.C. CODE § 47-1551c(e) (1973).

13. The prohibition against taxing the "personal income" of nonresidents is the only taxing prohibition in the Home Rule Act. Sen. Eagleton, one of the sponsors of Home Rule legislation, said:

The present . . . council [has] jurisdiction over taxes — to wit [*sic*]— the real property tax. . . . [A]s to all other taxes, including franchise taxes, sales taxes, local taxes, that jurisdiction is in Congress. We transfer the jurisdiction of taxation to the elected City Council and the elected mayor — holding back, as I said before — the commuter tax.

119 CONG. REC. 35,747 (1971) (remarks of Sen. Eagleton).

14. The tax was originally enacted as part of the District of Columbia Income and Franchise Tax Act of 1947, Pub. L. No. 80-195, 61 Stat. 331, 345 (1947), and has been a part of the District's tax structure ever since. See D.C. CODE § 47-1574 (1973). See also note 42 *infra*.

15. In this Note, *doing business in the District* refers to the carrying on of business operations in the District or receiving revenue from sources within the District.

16. The tax extended to any unincorporated trade or business engaged in or carried on in the District. The "professional exemption" provided:

The words "unincorporated business" do not include any trade or business which

applies uniformly to businesses conducted in the District by both residents and nonresidents. The scope of the tax had been limited, however, by a provision of the original act exempting nonsalaried professionals and personal service businesses.¹⁷ In 1975, the District removed the professional exemption to the DCUB tax, thereby taxing uniformly all enterprises doing business or receiving income in the District.¹⁸

Because it is uncertain whether, for example, fees earned by physicians and lawyers in the District represent income to an unincorporated business or "personal income" within the meaning of the section 602(a)5 prohibition, nonresident professionals have challenged removal of the exemption as *ultra vires*. Recently, in *Bishop v. District of Columbia*,¹⁹ the Court of Appeals for the District of Columbia, *en banc*, held that the Council's removal of the professional exemption violated section 602(a)5 of the Home Rule Act.²⁰ This Note will examine the evolution of the DCUB tax in light of section 602(a)5 and the *Bishop* case.

I. THE DCUB TAX: INCOME OR FRANCHISE TAX?

Franchises confer rights which go beyond the rights and privileges of citizens generally.²¹ In return for granting a franchise, the government gains the right to impose a tax on the franchise. Probably the most com-

by law, custom, or ethics cannot be incorporated, any trade, business, or profession which can be incorporated only under Chapter 11 of Title 29 (the Professional Corporation Act), or any trade or business in which more than 80% of the gross income is derived from the personal services actually rendered by the individual or members of the partnership or other entity in the conducting or carrying on of any trade or business, and in which capital is not a material income producing factor. D.C. CODE § 47-1574 (1973). The reference to the Professional Corporation Act was added by Congress in 1971. *See* note 103 *infra*.

17. *See* note 16 *supra*. It should be understood from the outset that the professional exemption, as well as the DCUB tax itself, applies only to nonsalaried income earners (i.e., sole proprietors or partners). The taxation of salaried employees is not at issue, since the District government has not attempted such a tax.

18. 22 D.C. Reg. 2091, 2113. The District may have done what Congress had previously refused to do in removing the exemption for professionals. *See* H.R. REP. NO. 508, 92d Cong., 1st Sess. (1971).

19. 105 DAILY WASH. L. REP. 2013 (D.C. Super. Ct., Oct. 18, 1977), *modified*, DAILY WASH. L. REP. 2013 (Oct. 27, 1977), *rev'd* 401 A.2d 955 (D.C. App. 1979), *aff'd on rehearing en banc*, 411 A.2d 997 (D.C. App. 1980), *cert. denied*, No. 79-1568 (May, 1980).

20. *See* note 13 and accompanying text *supra*; notes 88-96 and accompanying text *infra*.

21. *See, e.g.*, *People's R.R. v. Memphis R.R.*, 77 U.S. 38, 50-51 (1869); *In re Southern Neb. Power Co.*, 109 Neb. 683, 192 N.W. 317 (1923). The "privilege" of doing business has been cited as grounds for imposing a tax, there being no "right" recognized in common law to do so. *See* *Pure Oil Co. v. State*, 244 Ala. 258, 12 So.2d 861 (1943); *State ex rel. Short v. Riedell*, 109 Okla. 35, 233 P. 684 (1924); *Philadelphia v. Samuels*, 338 Pa. 321, 12 A.2d 79 (1940); *In re Watson*, 17 S.D. 486, 97 N.W. 463 (1903).

mon type of franchise tax is that imposed on corporations. Doing business in a corporate form is a right which citizens generally do not enjoy; however, corporate franchises are by no means the only type of franchise taxed.²² Banking and private mail delivery services, for example, are typically subject to franchise taxes. The common thread among franchises appears to be that when an entity engages in a privileged activity, it becomes subject to being classified and taxed on the privilege.²³

There is a wide array of methods for assessing the value of the taxed privilege. The entity subject to a franchise tax may be assessed a flat license fee,²⁴ or may be taxed on the basis of either gross²⁵ or net income.²⁶ When earnings or net income are taxed, the inevitable argument is that the tax is really an income tax rather than a tax on a franchise measured by income. Courts have done little to clarify the distinction between a franchise tax and an income tax, stressing that the nature of the tax, judged by its substance and effect, is controlling, and not necessarily the legislative designation.²⁷ The lack of a clear distinction between the two types of

22. *See, e.g.*, *Western Union Tel. Co. v. City of Visalia*, 149 Cal. 744, 87 P. 1023 (1906) (privilege of constructing and operating telegraph lines); *First Fed. Sav. & Loan Ass'n of Boston v. State Tax Comm'n*, 372 Mass. 478, 485-87, 363 N.E.2d 474, 480-81, (1977) (privilege of banking); *People ex rel. Pennsylvania Gas Co. v. Saxe*, 186 A.D. 28, 174 N.Y.S. 102 (1919) (privilege of piping gas).

23. *See, e.g.*, *Mosig v. New Jersey Chiropodists*, 122 N.J. Eq. 382, 385, 194 A. 248, 250 (1937) (franchises are grants that citizens cannot enjoy without legislative grant). Of course a tax does not automatically flow from the granting of a franchise; it merely becomes a possibility.

24. A franchise may be construed to be a license. The issue may arise when a sovereign is granted the power to levy one type of tax but not another. *See, e.g.*, *Copt-Air, Inc. v. City of San Diego*, 15 Cal. App. 3d 984, 93 Cal. Rptr. 649 (1971); *People ex rel. Fitzhenry v. Union Gas & Elec. Co.*, 254 Ill. 395, 398 N.E. 768, 771 (1912); *Ex parte Polite*, 97 Tex. Crim. 320, 323-24, 260 S.W. 1048, 1050 (1924).

25. *See, e.g.*, *State v. Boston & Portland Express Co.*, 100 Me. 278, 282, 61 A. 697, 698 (1905); *Tri County Elec. Assoc., Inc. v. City of Gillette*, 584 P.2d 995, 1001 (Wyo. 1978). Some unincorporated business taxes are assessed on gross income. *See, e.g.*, *Foosaner v. Dir. Div. of Taxation*, 58 N.J. 57, 59-60, 275 A.2d 129, 131 (1971); *Lougee v. New Mexico Bureau of Rev. Commr's.*, 42 N.M. 115, 76 P.2d 6 (1937); *Davis v. Ogden City*, 117 Utah 315, 215 P.2d 616 (1950).

26. The net income taxation model is most common in corporate franchise taxation. *See, e.g.*, D.C. CODE § 47-1571 (1973). In 1890, the Supreme Court said, "[t]he validity of the tax can in no way depend upon the mode which the State may deem fit to adopt in fixing the amount for any year which it will exact for the franchise." *Home Ins. Co. v. New York*, 134 U.S. 594, 600 (1890). Unincorporated businesses are also subject to a tax on net income in some jurisdictions. *See City of Louisville v. Sebree*, 308 Ky. 420, 214 S.W.2d 248 (1948); *Carter Carburetor Corp. v. City of St. Louis*, 356 Mo. 646, 203 S.W. 438 (1947); *Dole v. Philadelphia*, 377 Pa. 375, 11 A.2d 163 (1940).

27. *See, e.g.*, *Dawson v. Kentucky Distilleries*, 255 U.S. 288, 292 (1921); *Commissioner v. American Metals Co.* 221 F.2d 134, 137 (2d Cir.), *cert. denied*, 350 U.S. 829 (1955); *New York and Honduras Rosario Mining Co. v. Commissioner* 168 F.2d 745 (2d Cir. 1948). *See*

taxes has given rise to some unlikely consequences.

In *City of Louisville v. Sebree*,²⁸ the city had imposed what purported to be a license fee for the "privilege of engaging in Louisville in occupations, trades, businesses, and other activities."²⁹ The fee was assessed on the amount of wages paid, or in the case of businesses, on net income.³⁰ Without ruling on whether this was in fact an income tax,³¹ the Kentucky Court of Appeals construed the ordinance to impose a license fee, even though no licenses were issued and the income of every wage earner and business in the city was subject to tax. Although the court noted that a similar tax had been declared an income tax in Philadelphia,³² and "a species of income or excise tax" in St. Louis,³³ it regarded the operative distinction to be the subject of the taxation, not the unit of measure.³⁴ Since the Louisville tax was based on the privilege of doing business in the city, it was a license fee.

Four years later, the same court came to a different conclusion regarding the same tax in *Commissioners of the Sinking Fund of Louisville v. Howard*.³⁵ Pursuant to congressional authorization,³⁶ the city was permitted to levy local income taxes, defined as "any tax levied on, with respect to, or

note 108 *infra*. The mere fact that a court may refuse to accept the legislative designation does not mean that the court will be any more adept than the legislature at defining the tax. *See, e.g.*, *Eugene Theater Co. v. City of Eugene*, 194 Or. 603, 243 P.2d 1060 (1952). *See also* note 33 *infra*.

28. 308 Ky. 420, 214 S.W.2d 248 (1948).

29. Louisville, Ky., Ordinance 83. The tax was imposed pursuant to a specific grant of legislative power to the city to raise revenue from taxes "based on income, licenses and franchises." KY. REV. STAT. § 91.200 (1970).

30. 308 Ky. at 424, 214 S.W.2d at 250-51. Net income for businesses included businesses conducted by individuals, partnerships, or any other entity. *Id.*

31. *Id.* at 428, 214 S.W.2d at 252-53. *See* note 28 and accompanying text *supra*.

32. The Philadelphia unincorporated business tax, enacted in 1939, was an income tax and a business net profits tax imposed on both residents and nonresidents. It was a model for statutes in St. Louis and Louisville. The tax was challenged and upheld where Philadelphia had the charter power to exact taxes. *See Dole v. City of Philadelphia*, 337 Pa. 375, 11 A.2d 163 (1940). However, it was struck down in St. Louis where the statute authorized only license taxes. *See Carter Carburetor Corp. v. City of St. Louis*, 356 Mo. 646, 203 S.W. 438 (1947).

33. *Carter Carburetor Corp. v. City of St. Louis*, 356 Mo. 646, 203 S.W. 438 (1947). In *Cincinnati, Ohio*, a similar tax was upheld as an excise tax. *State ex rel. Zielonka v. Carrel*, 99 Ohio St. 220, 124 N.E. 134 (1919).

34. 308 Ky. at 430, 214 S.W.2d at 254. The court also considered the fact that the tax was on net, not gross income. The Court of Appeals of Kentucky noted that in delegating local taxing power to the city, the state legislature failed to specify a standard of measure; in the absence of a legislative mandate, the court would not impose one. *Id.* at 430-31, 214 S.W.2d at 254.

35. 248 S.W.2d 340 (Ky. 1952), *aff'd*, 249 S.W.2d 816, *aff'd*, 344 U.S. 624, 628-29 (1953).

36. 4 U.S.C. § 106(a) (1976).

measured by net income, gross income, or gross receipts"³⁷ upon employees at newly annexed federal land adjacent to Louisville. The license fee was challenged by a worker in the annexed area as a license tax rather than a local income tax. In finding the tax an income tax, the Court of Appeals emphasized that a tax could be construed as an excise tax within the meaning of the Kentucky Constitution and as an income tax for federal tax purposes.³⁸ Consequently, the improbable result of *Sebree* and *Howard* is that the Louisville tax is a license fee for municipal purposes and an income tax for federal purposes. On a more basic level, however, these cases illustrate that a tax must be judged within the context of the challenge made against it.

A. Evolution of the DCUB Tax

The District of Columbia Income and Franchise Tax Act of 1947³⁹ was the first local statute recognizing unincorporated businesses as taxable entities.⁴⁰ Prior to the 1947 enactment, unincorporated business income passed directly to its partners, as in the federal taxation scheme.⁴¹ The Act imposed a tax "for the privilege of carrying on or engaging in any trade or business within the District and of receiving income from sources within the District. . . ."⁴² The tax sought to capture revenue from businesses that refrained from incorporating as a means of avoiding the corporate franchise tax. Under the Act, partners conducting the business are jointly and severally liable for payment of the tax and must file a return indicating their distributive share of the net income, whether distributed or not.⁴³

37. 4 U.S.C. § 110(c) (1976).

38. 248 S.W.2d at 342.

39. Pub. L. No. 80-195, ch. 258, 61 Stat. 336 (1947).

40. *Id.* (income from unincorporated business). Previously, the states of Connecticut and New York both had unincorporated business statutes. *See* note 45 and accompanying text *infra*. Connecticut's unincorporated business tax applies to gross income defined as "all receipts, whether in the form of money, credits or other valuable consideration received during the income year in connection with any business subject to taxation under the provisions of this chapter." CONN. GEN. STAT. ANN. § 12-270 (West 1972).

41. *See* note 43 *infra*.

42. D.C. CODE § 47-1574b (1973). The same language was used by Congress in imposing a tax on corporations. *Id.* § 47-1571a (1973). Under the District's Revenue Act of 1937, a general tax on the privilege of doing business was imposed at a rate of two-fifths of one percent of gross receipts for each person, whether an "individual, firm, copartnership, joint adventure, association, corporation . . . or other group . . . acting as a unit." Pub. L. No. 75-314, 50 Stat. 673, 688-90 (1937). This tax was repealed in 1939. Under the District of Columbia Revenue Act of 1939, there was no tax on unincorporated businesses. Partners were individually responsible for their pro-rata share of the partnership net income. Pub. L. No. 76-225, ch. 367, § 25(a), 53 Stat. 1085, 1099 (1939).

43. Under I.R.C. § 701, partners rather than the partnership are taxed. This was the

The 1947 Act was based upon a New York statute which also imposed a net income tax on unincorporated businesses.⁴⁴ Both statutes exempted professionals⁴⁵ because professionals had traditionally not incorporated and, in fact, were not permitted to incorporate until 1971.⁴⁶ Failure to incorporate, therefore, was not a tax avoidance scheme, as might have been the case with other unincorporated businesses.⁴⁷

Although comparison among local tax schemes is necessarily tenuous, an examination of New York's unincorporated business tax is helpful in understanding the nature of the DCUB tax. Like the DCUB tax, the New York tax recognized unincorporated businesses as taxable entities and, until 1966, exempted nonsalaried professionals from its operation.⁴⁸ The tax was alleged to be a franchise tax in *People ex rel Froelic v. Graves*,⁴⁹ a case involving a partner in an unincorporated business who sought to deduct unincorporated business taxes from his personal return.⁵⁰ Under New

scheme of the District's code. The aspect of joint and several liability distinguishes the DCUB tax from the federal scheme which creates only several liability. Compare I.R.C. § 701 with D.C. CODE § 47-1574d (1973).

44. The law was originally enacted as a temporary measure by New York in 1935. 1935 N.Y. Laws, ch. 33, art. 16-A (currently codified at N.Y. TAX LAW § 701-23 (McKinney 1975 & 1978 Supp.)).

45. The New York law specifically exempted doctors, lawyers, dentists, and "any other profession in which capital is not a material income producing factor and in which more than eighty per centum of the unincorporated business gross income . . . is derived from personal services . . ." N.Y. TAX LAW § 703(c) (McKinney 1975).

In 1966, New York delegated its taxing powers over unincorporated businesses to the cities. Ch. 772, 1966 Laws of New York. Then, pursuant to express authority from the state, New York City repealed the professional exemption. See Local Law No. 36, reprinted in the City Rec., July 2, 1977. Removal of the exemption was upheld in *Shapiro v. City of New York*, 67 Misc. 2d 1021, 325 N.Y.S.2d 787, *aff'd*, 32 N.Y.2d 96, 196 N.E.2d 230, 343 N.Y.S.2d, *appeal dismissed*, 414 U.S. 804.

46. See D.C. CODE § 29-1101 to 29-1121 (1973 & Supp. V 1978). Interestingly enough, unincorporated professional associations were not subjected to the DCUB tax until 1975. See note 17 *supra*.

47. In urging imposition of the tax, the governor stated, "[i]n my view, it is eminently fair that a business carried on at a profit by a sole proprietor or by a group of partners should pay a tax upon its net earnings corresponding to the franchise tax on business corporations." See Legislative Docket No. 56, 1935, 22-25 (New York). See also *Thompson v. Mealey*, 290 N.Y. 230, 232, 48 N.E.2d 499, 501 (1943); *Tower v. State Tax Comm'n.*, 282 N.Y. 407, 26 N.E.2d 955 (1940).

48. Compare D.C. CODE § 47-1574 (1973) with N.Y. TAX LAW § 703(c) (McKinney 1975). A critical distinction between New York and the District is that under New York law, the taxation statutes are to be construed consistently with federal law. See N.Y. TAX LAW § 702 (McKinney 1975).

49. 259 A.D. 30, 18 N.Y.S.2d 418 (1940).

50. Froelick was a partner owning 5% of the stock in a brokerage firm. He argued that the unincorporated business tax should have been deducted by the firm before arriving at its distributive net income upon which he would be taxed personally. 259 A.D. at 30, 18 N.Y.S.2d at 419.

York law, a taxpayer may not deduct income taxes on his personal return but may deduct franchise taxes.⁵¹ The New York Court of Appeals held that unincorporated business taxes were income taxes and as such could not be deducted on personal returns.⁵² In doing so, the court looked to the legislative intent, New York's overall taxation scheme, and the well-established principle that deductions are never presumed.⁵³ Thus, at least within the ambit of New York tax law, unincorporated business taxes are considered to be income taxes.

B. Section 602(a)5: Prohibition of Nonresident Income Taxes

The Home Rule Act transferred Congress's taxing jurisdiction over the District of Columbia to the City Council, with the caveat that the District may not impose a tax on the personal income of nonresidents.⁵⁴ It has been said that this so-called "commuter tax" prohibition was the price the District had to pay to get the Home Rule Act through Congress.⁵⁵ Depriving the District government of the power to tax nonresidents was in fact a reaction to the District's attempts, prior to Home Rule, to do just that. On several occasions, District leaders sought congressional approval for a commuter tax on salaried nonresident workers.⁵⁶ Similarly, the District petitioned for removal of the professional exemption from the DCUB tax.⁵⁷ Congress rejected both proposals.⁵⁸ Moreover, as a result of these initiatives, drafts of the Home Rule legislation began appearing with what

51. N.Y. TAX LAW § 360(3) (McKinney 1975).

52. 259 A.D. at 32, 18 N.Y.S.2d at 420.

53. In contrast, Bishop argued that the DCUB tax was an income tax. See Brief for Appellant at 12-23, *District of Columbia v. Bishop*, 401 A.2d 955 (D.C. 1979), *aff'd on rehearing en banc* No. 12871 (Feb 12, 1980). See also note 83 and accompanying text *infra*. The New York court noted the high degree of integration between the unincorporated business and the personal tax schemes. Further, the New York legislature had not designated the tax as either a franchise or excise tax. Compare this with the congressional designation of the DCUB as a franchise tax. Pub. L. No. 80-125, ch. 258, § 2(b)(10), 61 Stat. 336 (1947). See also note 48 *supra*.

54. Home Rule Act § 602(a)5, (codified at D.C. CODE § 1-147(A)5 (1973 & SUPP. V 1978)).

55. See Brief for the District of Columbia on rehearing *en banc* at 11, *District of Columbia v. Bishop*, 401 A.2d 955 (D.C. 1979), *aff'd on rehearing en banc*, 411 A.2d 997 (D.C. 1980).

The fact that Home Rule may have been held hostage by suburban legislators, who allowed its passage only at the cost to the District of the commuter tax prohibition, may explain why § 602(a)5 is in the Home Rule Act, but does not explain how it should be construed. See note 113 *infra*. The District is probably right.

56. There were three separate attempts by the District in three successive Congresses, and three dismal failures. See note 113 *infra*.

57. See H.R. REP. NO. 508, 92d Cong., 1st Sess. (1971). The District argued that passage of the District of Columbia Professional Corporation Act, D.C. CODE § 29-1101 to 29-

eventually became section 602(a)5 of the Home Rule Act.⁵⁹ Because removal of the exemption for professionals from the DCUB tax would result in the taxation of nonresident as well as resident nonsalaried professionals working in the District, it has been argued that section 602(a)5 was aimed at prohibiting the repeal of the professional exemption.⁶⁰ It has also been argued that section 602(a)5 prohibits only a tax on the personal income of salaried nonresidents.⁶¹

Long before the section 602(a)5 prohibition in the Home Rule Act was even conceived, the DCUB tax was levied upon non-professional unincorporated businesses, including those owned by nonresidents.⁶² Like professionals, non-professionals derive their personal income from unincorporated businesses doing business in the District. Yet, since 1947, these non-professionals, some of whom are nonresidents, have been subject to the DCUB tax. There were no proposals to amend the DCUB tax when the Home Rule Act was enacted or afterwards to prohibit exaction of the tax from nonresidents. Thus it would appear that since the passage of the Home Rule Act, the DCUB tax has violated that Act.⁶³

C. Judicial Response to the DCUB Tax

In 1949, just 2 years after the DCUB tax was enacted, the District of Columbia Circuit Court of Appeals in *District of Columbia v. Pickford*,⁶⁴ considered the nature of the tax. At issue was whether the DCUB tax was

1121 (1973 & Supp. V 1978), eliminated the reason for the exemption; therefore, the District urged repeal of the exemption.

58. See notes 56-57 and accompanying text *supra*.

59. The Home Rule Act went through three drafts in the House Committee on the District without the § 602(a)5 prohibition. The Senate bill contained the prohibition beginning in 1969. See note 113 *infra*. See also STAFF OF THE HOUSE COMM. ON THE DISTRICT OF COLUMBIA, 93d Cong., 2d Sess., Home Rule for the District of Columbia 1973-1974: Background and Legislative History of H.R. 9056, H.R. 9682 and Related Bills 366 (Comm. Print 1973).

60. See Supplemental Brief for Appellant Axel-Felix Kleiboemer Before the Court *en banc* at 17. Congress specifically maintained the exemption when it passed the District of Columbia Professional Corporations Act, Pub. L. 92-180, 85 Stat. 576 (1971), thus ensuring that professionals would be taxed under neither the DCUB tax nor the corporate franchise tax. See note 103 *infra*. The report stated that the exemption was necessary to avoid what is really a commuter tax upon a group of people. H.R. REP. NO. 508, 92d Cong., 1st Sess. 4 (1971).

61. See, e.g., H.R. REP. NO. 482, 93d Cong., 1st Sess. 37 (1973). See note 86 and accompanying text *infra*.

62. Pub. L. No. 80-195, 61 Stat. 328 (1947). Although title VI of the Act refers to a tax on residents and non-residents, the DCUB tax is the only portion of the 1947 Act which was levied against nonresidents. *Id.* at 343-45.

63. See notes 101-03 and accompanying text *infra*.

64. 179 F.2d 271 (D.C. Cir. 1949).

intended to tax net income of owners of unincorporated businesses derived from any source in the District, or only that income derived from the business itself.⁶⁵ The court held that the tax was only upon income derived from the business. Furthermore, the court noted that the DCUB tax was inapplicable to nonresidents' income from sources within the District.⁶⁶ Thus, the court clearly distinguished unincorporated business income, which was subject to tax, from other income, which was not.⁶⁷

In 1957, the Maryland Court of Appeals rendered a decision much closer to the heart of the income/franchise tax issue. In *Gardella v. Comptroller of Maryland*,⁶⁸ the Maryland court considered whether DCUB taxes paid by a Maryland resident could be credited against personal income taxes due the state.⁶⁹ Since Maryland grants a credit for income taxes paid to other jurisdictions,⁷⁰ the court had to consider whether the DCUB tax was, in fact, an income tax. In finding the tax to be a franchise tax, not an income tax, the court reasoned that it was so designated by Congress, that it was imposed for the privilege of doing business in the District, and that it was imposed upon the entity "unincorporated business."⁷¹ The court concluded that the taxpayer could claim a deduction for the taxes paid as an ordinary business expense, but not as a tax credit.⁷²

Subsequent to the Home Rule Act, a Virginia court considered the character of the DCUB tax. In *Groom v. Forst*,⁷³ the Arlington County Court reached a conclusion opposite that in *Gardella*. Subsequent to removal of the professional exemption from the DCUB tax, the petitioner, a Virginia

65. Pickford, a nonresident, owned an apartment building from which he derived rents and a hotel which he leased to a corporation for a percentage of the gross receipts. The apartment rents were considered income to an unincorporated business, while the hotel rents were not. 179 F.2d at 272.

66. *Id.* See also *Capital Holding Corp. v. District of Columbia*, 374 A.2d 573 (D.C. 1977).

67. The tax is only upon work done in the District. The rules on apportioning work between the District and other jurisdictions are set out in D.C. CODE § 47-1580 (1973 & Supp. V 1978).

68. 213 Md. 1, 130 A.2d 752 (1957).

69. *Gardella* was an unincorporated partner in a retail sales store. He included all of the income from the store in his gross income computation for his Maryland return. He then excluded the income already subject to the DCUB tax, giving him, in effect, a tax credit for the DCUB taxes paid. 213 Md. at 2, 130 A.2d at 752-53. See note 78 *infra*.

70. See MD. ANN. CODE art. 81, § 286 (1957). The Code provides that "whenever a resident of this state has become liable . . . upon such part of his net income . . . as is properly subject to taxation in such state" he may reduce his tax by that amount. *Id.* See also note 74 and accompanying text *infra*.

71. 213 Md. at 2, 130 A.2d at 753.

72. 213 Md. at 3, 130 A.2d at 754.

73. *Groom v. Forst*, No. 18809 (Arlington County Cir., filed, March 30, 1978), *aff'd on rehearing mem.* No. 18809 (Oct. 23, 1978) (appeal stayed pending D.C. litigation).

resident working as a nonsalaried partner in a District of Columbia law firm, became liable for payment of the DCUB tax. He paid the tax, and like the taxpayer in *Gardella*, sought to claim the payment as a credit against Virginia income taxes due, pursuant to a Virginia tax credit scheme similar to Maryland's.⁷⁴ In this case, however, the court allowed the tax credit. The Arlington court found that to be classified as an income tax, the tax in question had to meet the definition of an income tax used by the federal government to determine whether taxes paid to a foreign government may be credited against federal income taxes due.⁷⁵ Under the federal test, foreign taxes are income taxes if they "seek out a net gain or profit."⁷⁶ Since the DCUB tax is one on net income, the court held that it is an income tax and creditable on Virginia returns.

The Arlington County Court did not need to construe the DCUB tax in light of the Home Rule Act and expressly declined to do so.⁷⁷ Neither the Maryland court in *Gardella* nor the Virginia court in *Groom* had to determine whether unincorporated business income under the DCUB tax was personal income under section 602(a)5 of the Home Rule Act. The facts that gave rise to the controversy, however, reveal the underlying complaint of both professional and non-professional unincorporated owners: Virginia and Maryland residents receive a tax credit for income taxes paid to other jurisdictions but may claim only a deduction for franchise taxes.⁷⁸ The dilemma is clear: if the DCUB tax is an income tax, it is creditable but illegal; if it is a franchise tax, it is legal but not creditable.⁷⁹

74. VA. CODE § 58-151.015 (1974). While no attempt is made here to define the reasoning of the Arlington Circuit Court, its inconsistency with the holding in *Gardella* may have some logical basis independent of the stated rationale. Virginia's tax credit statute was amended in 1972 to allow a resident to take a credit for taxes on "earned or business income." This should be compared with Maryland's credit statute. See notes 70-71 *supra*.

75. I.R.C. § 901(a) & (b)(1). The issue was whether the DCUB was the "substantial equivalent" of an income tax for credit purposes. *Groom v. Forst*, slip op. at 4 (Arlington County Cir., filed March 30, 1978). The *Gardella* court was likewise of the opinion that federal definitions were relevant in determining the nature of the DCUB tax. See note 117 and accompanying text *infra*.

76. See *Groom v. Forst*, No. 18809, slip op. at 6 (Arlington County Cir., filed March 30, 1978). See also IRC § 901. See generally *Bank of America v. United States*, 459 F.2d 513 (Ct. Cl. 1972).

77. *Groom v. Forst*, No. 18809, slip op. at 8 (Arlington County Cir., filed March 30, 1978).

78. Compare MD. TAX CODE ANN. art. 81, § 290 (Supp. 1978) with VA. CODE § 58.151.015 (1974). There is ample evidence that if no residents had been permitted to take a tax credit for DCUB taxes paid, the litigation never would have arisen. H.R. REP. NO. 508, 92d Cong., 1st Sess. 4 (1971).

79. See Home Rule Act § 602(a)5, (codified at D.C. CODE § 1-147(c) (1973 & Supp. V 1978)) (prohibiting taxation of nonresident income without addressing franchise tax based

II. *Bishop v. District of Columbia*

In *Bishop v. District of Columbia*,⁸⁰ the District of Columbia courts considered whether the DCUB tax is a tax on personal income, thereby violating the Home Rule Act. Subsequent to the removal of the professional exemption from the DCUB tax, the petitioner, a Virginia resident practicing law in the District, paid the tax and sued for a refund in the Superior Court for the District of Columbia.⁸¹ In addition to other arguments raised,⁸² Bishop claimed that the tax was on his personal income, and that the City Council had acted outside its authority under the Home Rule Act by removing the professional exemption and subjecting his personal income to taxation.⁸³

The argument failed in the superior court⁸⁴ where Judge Penn reasoned

on income). See also MD. ANN. CODE art. 81, § 286 (1957); VA. CODE § 58-151.015. Both Maryland and Virginia allow credits for income taxes paid to other jurisdictions.

80. 105 DAILY WASH. L. REP. 2013 (D.C. Super. Ct., Oct. 18, 1977), *revised mem.* (Oct. 27, 1977), *rev'd*, 401 A.2d 955 (D.C. 1979), *aff'd*, 411 A.2d 997 (D.C. 1980) (en banc), *cert. denied*, No. 79-1568 (May, 1980).

81. The *Bishop* case was not the first attack on the DCUB by a nonresident professional. An earlier case, *Committee for Fair Taxation of Professionals v. District of Columbia*, 104 DAILY WASH. L. REP. 749 (D.C. Super. Ct., April 15, 1976), was dismissed by the court for failure to sue in the tax division and because the Superior Court could not grant injunctive relief. *Id.* See D.C. CODE § 47-2410 (1973). In *Virginia v. District of Columbia*, Civil No. 76-0533 (D.D.C. June 1, 1976) (motion to vacate and reconsider denied June 22, 1976), the attorney general of Virginia brought suit as *parens patriae* for all Virginia non-salaried professionals subject to the tax seeking a declaratory judgment, but the suit was dismissed. Virginia has thus stood on both sides of the issue in *Bishop*, arguing that it was an income tax in *Virginia v. District of Columbia* and that it was a franchise tax in *Groom v. Forst*, No. 18809 (Arlington County Cir., filed March 30, 1978), *aff'd on rehearing mem.* No. 18809, Oct. 23, 1978.

82. Petitioners also argued that the exemption was repealed without adequate notice as required by D.C. CODE § 1-144(c) (Supp. 1978) and Council Resolution 1-1-2 (adopted Jan. 7, 1975). The District argued that notice published in the D.C. Register on March 10, 1975, saying that the Committee on Finance and Revenue would consider "new and alternative methods of raising revenue for the District of Columbia" was sufficient. 21 D.C. Reg. 2173 (March 10, 1975). In fact, the proposed budget did not include repeal of the professional exemption, but did contain an overall one percent gross receipts tax. Notice of the exemption repeal did not appear until the July 11, 1975 Revenue and Finance Committee Report. The Superior Court found this notice to be adequate. 105 DAILY WASH. L. REP. at 2020. The petitioners also argued that the DCUB violates the Privileges and Immunities Clause and the Equal Protection Clause of the United States Constitution. These arguments also failed. *Id.* at 2022. See generally *Austin v. New Hampshire*, 420 U.S. 656, 658, 665 (1975); *Travis v. Yale & Towne Mfg. Co.*, 252 U.S. 60 (1920); *Travellers Ins. Co. v. Connecticut*, 185 U.S. 364 (1902).

83. Bishop sued on his own behalf and was joined by Axel-Felix Kleiboemer, who obtained class action certification for the case. The class consisted of nonresident taxpayers who had paid the DCUB tax. 105 DAILY WASH. L. REP. at 2013. The court order of Oct. 27, 1977 does not distinguish between professionals and nonprofessionals. *Id.* at 2019.

84. *Id.* at 2021.

that unlike an income tax, a minimum tax is assessed upon all unincorporated businesses.⁸⁵ He also noted that the *Gardella* court construed the DCUB tax to be a franchise tax, and he interpreted section 602(a)5 to prohibit imposition of a "personal income tax" as that term is commonly used.⁸⁶ Thus, since the DCUB tax was a franchise tax, not an income tax, it was valid. The court focused upon the entity taxed, recognizing a congressionally intended distinction between unincorporated businesses and individuals. Moreover, Judge Penn interpreted the legislative history of the Home Rule Act to indicate that Congress intended section 602(a)5 to prohibit only a personal income tax on nonresidents, not a nonresident franchise tax.⁸⁷

A three judge panel of the Court of Appeals for the District of Columbia disagreed, finding the District's removal of the professional exemption to be *ultra vires*.⁸⁸ Judge Kelly, writing for the unanimous court, adopted the *Groom* rationale, distinguishing taxes on net income from those on gross receipts. Holding that the former is properly termed an income tax and the latter a franchise tax,⁸⁹ the court interpreted section 602(a)5 to prohibit a tax based on net income because it would tax consumable wealth, while a tax on gross income would tax the franchise without regard to its profitability.⁹⁰ In observing this distinction, the court failed to consider that the DCUB tax as amended in 1975 allowed professionals to deduct seventy percent of their net income as a salary allowance, thereby minimizing the

85. *Id.* The minimum tax is \$25.00. D.C. CODE § 47-1574b (1973).

86. 105 DAILY WASH. L. REP. at 2021.

87. *Id.* Judge Penn cited a House Report describing § 602(a)5 as prohibiting "the imposition of a personal income tax upon nonresidents of the District." This is in contrast to Senator Eagleton's comment, when home rule was being debated on the House floor, that § 602(a)5 was "a specific prohibition as to the imposition of a commuter tax, a reciprocal income tax, or any other tax on nonresidents of the District of Columbia." 117 CONG. REC. 42,498 (1971).

88. 401 A.2d 955 (1979). The panel was composed of Judges Kelly, Gallagher, and Pair. The unanimous opinion addressed only the authority of the Council. *See* note 82 and accompanying text *supra*. While the court held that removal of the professional exemption was *ultra vires*, it did not imply that the District cannot tax nonresident professionals operating unincorporated businesses. This indeed is the most confusing aspect of the division opinion. *See* note 104 and accompanying text *infra*.

89. 401 A.2d at 959.

90. *Id.* at 959-60. *See* note 76 and accompanying text *supra* and note 106 and accompanying text *infra*. The court stated:

A tax on gross receipts offers a very different result. Since a gross receipts tax can be collected even if the taxpayer has no funds remaining . . . the tax cannot be one on personal wealth. Rather a gross receipts tax is levied for the purpose of either taxing a privilege, such as the right to do business, or simply raising revenue, as in the sales tax.

401 A.2d at 960. *See* note 104 and accompanying text *infra*.

impact of the tax upon consumable wealth.⁹¹

Perhaps because of the impact of the court's holding upon future District finances, a majority of the Court of Appeals for the District of Columbia agreed to rehear the *Bishop* case *en banc*.⁹² On rehearing, Judge Kelly again wrote for the majority in an eight to one decision holding the DCUB tax in violation of section 602(a)5.⁹³ In this opinion, Judge Kelly stressed the legislative history of the Home Rule Act, indicating that section 602(a)5 was expressly intended to forbid repeal of the DCUB exemption for professionals.⁹⁴ Further, the court *en banc* limited the reach of the panel's earlier *Bishop* opinion as to the potential legality of a tax on gross income, referring to its previous discussion as merely "an illustrative device."⁹⁵ In so doing, the future of the DCUB tax in any form is left open to doubt,⁹⁶ and further litigation would appear inevitable.

Dissenting, Judge Mack viewed the issue not as whether the Home Rule Act prohibited the Council's repeal of the professional exemption, but rather whether unincorporated professionals constituted business entities for tax purposes.⁹⁷ She saw "no reason in law or logic" why a professional

91. D.C. CODE § 47-1557b(a)(15)(A) (1973 & Supp. V 1978). The percentage deductible by owners as a salary allowance has undergone several changes. When professionals were exempt from the tax, the allowance was 20% of net income. D.C. CODE § 47-1557b(a)(15) (1973). After passage of the Revenue Act of 1975, the City Council raised the allowance to 55%. 22 D.C. Reg. 2547 (Nov. 13, 1975). Then, while repeal of the Revenue Act was being considered in the House, and, in light of H.R. 9471, which would have not only raised the salary allowance to 80%, but also would have removed the income exclusion feature available only to District residents, the Council agreed to compromise. It agreed to a 70% allowance for professionals, but reduced the allowance for non-professional unincorporated owners to 30%. D.C. CODE § 47-1557b(a)(15) (1973 & Supp. V 1978). Undoubtedly the argument that the tax is one on personal income would have been much stronger had the Council retained the 20% salary allowance.

92. 401 A.2d at 962. The *en banc* court also vacated the opinion of the three-judge panel pending the rehearing *en banc*. *Id.*

93. Appeal docketed, No. 12871 (D.C., Feb. 12, 1980) (*en banc*).

94. *Bishop v. District of Columbia*, No. 12871, slip op. at 6 (D.C. 1980). In the three-judge panel opinion, Judge Kelly similarly found that § 602(a)5 was intended to prohibit a commuter tax. Judge Kelly sought to distinguish the DCUB tax from the corporate franchise tax. She noted that "if there is a sufficient nexus between that individual and the jurisdiction, such as a corporation which does business exclusively within the jurisdiction, then the tax is no longer a commuter tax. For that and other obvious reasons, a commuter tax could be levied only on natural persons." 401 A.2d at 958 n.9. This kind of acute reasoning was not extended to unincorporated businesses, even though they are no more natural persons than are corporations.

95. *Bishop v. District of Columbia*, No. 12871, slip op. at 5 (D.C. Super. Ct. 1979). *See* note 90 *supra*.

96. *See* note 110 *infra*. At present, the District is still undecided on whether to attempt collection of the tax against nonresident shareholders in professional corporations. *See* note 112 *infra*.

97. *Bishop v. District of Columbia*, No. 12871, slip op. at 9 (D.C. Super. Ct. 1979). This

doing business in the District is not an entity that can be made subject to a franchise tax.⁹⁸ Regarding the DCUB tax as a franchise tax, not an income tax, Judge Mack found application of the tax to nonresidents within the District's authority under the Home Rule Act. The problem with the majority's holding, she noted, was that it removed the tax from nonresident professionals but continued to tax resident professionals, making the DCUB tax vulnerable on constitutional grounds.⁹⁹ Judge Mack's opinion quite accurately predicts an administrative nightmare in the wake of the opinion.¹⁰⁰

III. TOWARD AN EQUITABLE TAXING SCHEME: REPEAL OF THE PROFESSIONAL EXEMPTION TO THE DCUB TAX

A. *Alternative Interpretations of the Bishop case*

1. *The Court of Appeals en banc*

The decision of the court of appeals *en banc* in *Bishop* raises many questions about the validity of the DCUB tax in light of section 602(a)5 of the Home Rule Act. These questions stem, in part, from alternative classification schemes used by Congress and the District in drafting legislation.

The local tax scheme in the District of Columbia distinguishes between salaried and nonsalaried income earners.¹⁰¹ Prior to 1975, the DCUB tax had distinguished between professionals and non-professionals.¹⁰² The Home Rule Act distinguishes between residents and nonresidents. Although repeal of the professional exemption occasioned the challenge, the foundation of the *Bishop* challenge lies in the Home Rule Act's resident/nonresident distinction. Thus, if the DCUB tax violates section 602(a)5, it does so with respect to *all* nonresidents, both professionals and non-professionals working in the District. The court's opinion grants relief

view presumes that unincorporated businesses are separate taxable entities and that the DCUB is a franchise tax measured by net income. See notes 65-68 and accompanying text *infra*.

98. *Id.* at 9-10.

99. *Id.* at 12. The Professional Corporation Act, D.C. CODE § 29-1101 to 29-1121 (1973 & Supp. V 1978), eliminated the rationale for the professional exemption. See note 103 *infra*. Since 1971, therefore, this tax has been vulnerable on Equal Protection grounds.

100. The District must decide whether to continue to collect the tax against nonresident non-professionals, resident professionals, and nonresident shareholders in professional corporations. Moreover, the District must refund taxes paid by nonresident professionals since 1975, estimated at approximately 58 million dollars. See Wash. Post, Feb. 13, 1980, § A, at 1; see note 103 *supra*.

101. See D.C. CODE § 47-1574 (1973).

102. D.C. CODE § 47-1502a (1973). The income tax applies only to residents; the business franchise taxes apply to residents and nonresidents. D.C. CODE § 47-1567 (1973).

only to the class of nonresident professionals which Bishop represented. Nonresident non-professionals and resident professionals — two classes that remain subject to the tax — have compelling arguments that will undoubtedly be litigated in the near future.

Resident professionals can argue that although they must compete on an equal footing with nonresident professionals working in the District and derive the same benefits from the District government as their nonresident counterparts, they alone are subject to the DCUB tax.

Similarly, nonresident non-professionals can argue that there is no reasoned basis for taxing them while exempting nonresident professionals. The effect of the court of appeals *en banc* decision in *Bishop* is to reinstate the professional exemption for nonresident professionals. A substantial element in the former rationale for the exemption no longer exists, however, because professionals have been able since 1971 to incorporate in the District.¹⁰³ Thus, the absence of a viable rationale for the exemption again raises strong equal protection arguments.

2. *The Three Judge Panel*

In the earlier decision in *Bishop*, the three judge panel focused on the DCUB tax as a tax on net rather than on gross income, thus determining that it was an income tax.¹⁰⁴ However, the distinction between taxes on gross and net income is an artificial one. It is true that there is an established body of federal case law making this distinction on the creditability of foreign taxes.¹⁰⁵ This case law, however, is of little value in construing a local statute such as section 602(a)5 prohibiting taxes on "personal income."

The court of appeals *en banc* apparently recognized the weakness of the three judge panel's decision. In endorsing a gross income tax and prohibiting a net income tax, the panel failed to address the issue of whether the

103. District of Columbia Professional Corporations Act, Pub. L. No. 92-180, 85 Stat. 576 (1971) (codified at D.C. CODE § 29-1101 to 29-1121 (1973 & Supp. V 1978)). With removal of the professional exemption from the DCUB tax, the Council amended the Professional Corporations Act to include a tax on professional corporations and unincorporated businesses. See D.C. CODE § 29-1121 (Supp. V 1978). The *Bishop* opinion leaves the District vulnerable to a suit under the Equal Protection Clause.

104. It is ironic that this distinction would be used to invalidate the tax. In its initial consideration of the Revenue Act of 1975, the City Council examined a 1% overall gross receipts tax, but abandoned it in favor of removing the professional exemption. See Proposed Budget, 21 D.C. Reg. 2359, 2372. See also notes 42 & 90 *supra*.

105. See, e.g., *New York & Honduras Rosario Mining Co. v. Commissioner*, 168 F.2d 745 (2d Cir. 1948); *Keasbey & Mattison Co. v. Rothensies*, 133 F.2d 894, 897 (3d Cir.), *cert. denied*, 320 U.S. 739 (1943).

DCUB tax was a tax on personal income. This may explain why the court converted what was essentially the rationale for the earlier holding in *Bishop* into mere dicta.¹⁰⁶ But in so doing, the court left open the question of what other tax measures are permissible.¹⁰⁷

Moreover, the panel identified "unincorporated businesses" as the taxable entities, thus eliminating the need to consider that Congress enacted the DCUB tax as a franchise tax.¹⁰⁸ This differentiation supports the proposition that references to federal income tax definitions, regulations, and rulings in construing local taxes are often inappropriate.¹⁰⁹ Finally, by reasoning that the DCUB tax is one on net income, the three judge panel side-stepped the main issue of the case: whether a tax on net income is necessarily a tax on personal income within the meaning of the section 602(a)5 prohibition.¹¹⁰

3. *The Superior Court*

The superior court, on the other hand, correctly acknowledged that the language of section 602(a)5 was the crux of the issue in *Bishop*. In understanding the term "a personal income tax" as that term is "commonly used,"¹¹¹ Judge Penn failed to address the definitional problem at the heart of the controversy: the scope of the section 602(a)5 prohibition. Al-

106. See note 90 and accompanying text *supra*. Using the federal foreign tax credit analysis, the court concluded that taxes on gross income are taxes on franchises or other privileges, while taxes on net income are income taxes. *Bishop v. District of Columbia*, 401 A.2d at 959. See note 74 *supra*. This was the premise that enabled the court to conclude that the DCUB tax was an income tax.

107. See notes 129-31 and accompanying text *infra*.

108. Pub. L. No. 80-195, 61 Stat. 343, 346 (1947). One trend in the law considers legislative clarification as irrelevant in determining the nature of the tax. See, e.g., *Dawson v. Kentucky Distilleries & Warehouse Co.*, 255 U.S. 288, 292 (1921); *Commissioner v. American Metal Co.*, 221 F.2d 134, 137 (2d Cir.), *cert. denied*, 350 U.S. 829 (1955). An alternative view gives great weight to legislative classification of taxes. See, e.g., *Flint v. Stone Tracy Co.*, 220 U.S. 107, 145 (1910); *County Comm'rs v. English*, 182 Md. 514, 531, 35 A.2d 135, 143 (1943).

109. Reference to federal definitions may have been appropriate in *Groom v. Forst*, No. 18809 (Arlington County Cir., filed March 30, 1978), because the Virginia tax scheme relies upon federal tax definitions. The *Bishop* court, however, lost sight of the fact that in construing the DCUB tax it was construing a local tax statute that did not depend on federal tax law as do some state tax statutes. See [1979] ALL STATES TAX GUIDE (P-H) ¶ 221.

110. The court fails to support this conclusion. For example, corporate income taxes are frequently considered to be corporate franchise taxes based on net income. The court's conclusion that a tax on net income is a tax on personal income begs the question. See 401 A.2d at 961. See generally *Lever Bros. Co. v. District of Columbia*, 204 F.2d 39 (D.C. Cir. 1953); 1 A. COOLEY, TAXATION ¶ 49 (4th ed. 1903).

111. 105 DAILY WASH. L. REP. at 2021. Judge Kelly was satisfied that § 602(a)5 prohibited a personal income tax but not a franchise tax based on income. See note 87 *supra*.

though the statute obviously attempts to avoid allowing a commuter tax, the scope and extent of the commuter tax ban remain issues in need of judicial interpretation.¹¹²

The District attempted to have a reciprocal income tax enacted in three sessions of Congress prior to home rule.¹¹³ Simultaneously, the District was also seeking removal of the professional exemption to the DCUB tax. In refusing to remove the exemption, it has been argued that Congress viewed maintaining the professional exemption in the DCUB tax as necessary to avoid imposing what would be, in effect, a commuter tax.¹¹⁴

On the other hand, there is no evidence in the legislative history of the Home Rule Act that Congress ever conceived of the DCUB tax, which was then taxing nonresident nonprofessionals, as running afoul of the section 602(a)5 prohibition.¹¹⁵ Moreover, pursuant to the Home Rule Act, Congress is given thirty days to veto Council legislative action.¹¹⁶ After hearing extensive debate on the same issues raised by the *Bishop* case, the House Committee on the District of Columbia decided not to object to the Council's removal of the professional exemption.¹¹⁷ Therefore, if Con-

112. *Bishop v. District of Columbia*, No. 12871, slip op. at 13 (D.C. 1980). No one on either side of the debate doubts that § 602(a)5 prohibits a commuter tax, but neither side can agree on what constitutes a commuter tax for the purposes of § 602(a)5. See note 87 *supra*. The strongest argument that the intent of § 602(a)5 was to preserve the professional exemption in the DCUB tax can be found in the legislative history of the Professional Corporations Act. See note 114 and accompanying text *infra*.

113. In 1967, Rep. Minchall introduced a bill that would have imposed a flat 2% tax on wages. H.R. 7473, 90th Cong., 1st Sess. (1967). It failed. In 1968, the District unsuccessfully attempted to remove the professional exemption from the DCUB tax and change its designation to a "business income" tax to enable nonresidents to avail themselves of the credit provisions of their home state statutes. See H.R. 16361, 91st Cong., 2d Sess. 202 (1968). In 1969, the proposals from 1967 and 1968 were put together but were defeated with no small amount of help from suburban congressmen. See *Revenue Proposals: Hearings before the House Subcommittee on the District of Columbia*, 91st Cong., 1st Sess. (1969). See also notes 70 & 74 *supra*.

114. H.R. REP. NO. 508, 92d Cong., 1st Sess. 4 (1971). See note 60 *supra*. Interestingly, reference to a commuter tax ban as prohibiting repeal of the professional exemption appears in the legislative history of the Professional Corporations Act of 1971, but nowhere in the legislative history of the Home Rule Act.

115. The exemption was preserved in the Professional Corporation Act by Congress. See D.C. CODE § 47-1574 (1973). The vitality of the exemption may indicate the lobbying strength of nonresident professionals on Capital Hill at the time the Professional Corporation Act was passed. See *Bishop v. District of Columbia*, 105 DAILY WASH. L. REP. at 2021 ("petitioners overlook the fact that the exemption was merely granted by way of legislative grace.").

116. Home Rule Act § 602(c)1, (codified at D.C. CODE § 1-147(c)1 (1973 & Supp. V 1978)). See also note 11 *supra*.

117. See *Subcommittee on Fiscal Affairs of the Comm. on the District of Columbia: Hearings and Disposition on H. Con. Res. 370, to disapprove the Revenue Act of 1975, and H.R. 9471, to amend the District of Columbia tax laws applicable to unincorporated business in-*

gress intended section 602(a)5 to prohibit repeal of the professional exemption to the DCUB tax, it is difficult to understand why it failed to act in the face of the Council's action doing just that.

B. Implementing an Equitable Tax Scheme

Nonresidents may justifiably complain about paying taxes to the District in that they have no voting representation on the City Council. Congress, however, showed little concern for the problem of taxation without representation when, in 1947, it authorized taxing nonresident, non-professional unincorporated businesses in the DCUB tax.¹¹⁸ Nonetheless, any inequities created by the DCUB classification system were resolved in 1975 when the City Council removed the professional exemption.¹¹⁹ The combined effect of section 602(a)5 and what is left of the DCUB tax results in an inequitable distribution of the local tax burden. Under the current arrangement, professional unincorporated business owners who reside outside the District are not subject to the DCUB tax, but nonprofessional nonresidents are taxed.¹²⁰ This distinction may cause patent inequities. For example, in a given hypothetical unincorporated District law firm, a senior partner living in Virginia will not be subject to the DCUB tax, while the senior partner living in the District will be subject to the tax. Further, the unincorporated supplier of office furniture for the firm living in Virginia will pay the DCUB tax, but the law firm's salaried junior associate living in the District will not. An arrangement as dizzying as this bears only the most tenuous relationship to the value of city services actually consumed, or to the ability of the entity taxed to pay — two rationales most often advanced for taxing nonresident workers.

Even nonresident professionals have conceded that they are inequitably benefited by the *Bishop* decision and, as an alternative, have advocated a reciprocal income tax.¹²¹ A reciprocal income tax would apply to all sala-

come, 94th Cong., 1st Sess. (1975) [hereinafter cited as 1975 *Congressional Veto Hearings*]. Congress did not reserve for itself line-item veto power over the Council's budget. Thus, Congress would have had to veto the entire budget for it to exercise its veto power over the removal of the exemption.

118. Pub. L. No. 80-195, 61 Stat. 331 (1947). The Supreme Court has rejected the argument that a state may not tax nonresidents who earn income within its borders. *See* *Travis v. Yale & Towne Mfg. Co.*, 252 U.S. 60 (1920).

119. An obvious inequity was created when Congress preserved the professional exemption in the DCUB tax while enacting the Professional Corporation Act, Pub. L. No. 92-180, 85 Stat. 576 (1971), thereby removing the only rationalization for the exemption. *See* note 103 and accompanying text *supra*.

120. This is because *Bishop* only represented the class of nonresident professionals. *See* note 96 *supra*.

121. *See Hearings and Markup of H.R. 11579 and H.R. 14621 Before Subcomm. on Fiscal*

ried and nonsalaried individuals working in the District but residing elsewhere. These workers would pay an income tax to the District and credit the amount paid on their home state returns.¹²² An obvious disadvantage of such a scheme, often cited by legislators from Maryland and Virginia, is that income taxes paid by their residents to the District would result in less tax revenue to their respective states. Thus, areas of Maryland and Virginia outside the Washington metropolitan region would be required, in effect, to subsidize the District, while commuters reap the benefits.¹²³ As an alternative, neighboring Congressmen have proposed increasing the federal payment to the District.¹²⁴ This solution, in addition to being administratively burdensome, essentially leaves the District's finances in the hands of Congress, depriving the District of the autonomy purportedly granted by Home Rule.¹²⁵

Since a reciprocal income tax may be politically impossible,¹²⁶ or at least undesirable, District officials must examine other taxing alternatives in light of *Bishop* and section 602(a)5. The District is one of the few jurisdictions recognizing an unincorporated business as a taxable entity.¹²⁷ In failing to exempt nonresidents from the DCUB tax when it passed section 602(a)5, Congress implicitly chose not to recognize unincorporated business income as personal income. For a court to deny the District a taxing power that Congress apparently approved, and to do so in unequivocal terms,¹²⁸ constitutes judicial interventionism warranted by neither section 602(a)5 nor by the facts of the *Bishop* case. Further, if section 602(a)5 is to

Affairs and the Comm. on the District of Columbia, 94th Cong., 2d Sess. 476-78 (1976) [hereinafter cited as *Commuter Tax Hearings*] (statement of Dr. Shuford, Pres. of District of Columbia Dental Society, and Mr. Daniel, Pres. of District of Columbia Bar). See also *id.*, at 483-84 (statement of Ben Fischer, past Pres., Federal Communications Bar Ass'n).

122. This is assuming the reciprocal income tax would pass both Maryland and Virginia's tax credit statutes. See note 74 *supra*. The state of Virginia has estimated its revenue loss from a reciprocal income tax in the District at 21 million dollars per year as of 1978. See *Commuter Tax Hearings*, *supra* note 121, at 265. Maryland estimates its yearly loss at 25 million dollars. *Id.* at 179.

123. *Id.*

124. See 1975 *Congressional Veto Hearings*, *supra* note 117, at 196 (statement of Hon. N. Steers state Sen. - Md.) and 228 (statement of Cong. Harris - Va.). This solution is discussed in *Washington Post*, March 2, 1980 § A, at 1.

125. See *id.*

126. See *Commuter Tax Hearings*, *supra* note 121. "Even the most ardent advocates for the city know that this Congress is not going to pass a commuter tax. . . . I am at a loss to explain why we are here today holding these hearings." *Id.* at 11 (remarks of Rep. Gude - Md.).

127. The New York Unincorporated Business Tax, for example, will be phased out in 1982, with the proviso that the cities may retain it. See N.Y. TAX LAW § 701 (McKinney 1975).

128. See notes 88-91 and accompanying text *supra*.

stand as an absolute bar to nonresident taxation, as the court has implied, more than the DCUB tax has been brought into question.¹²⁹ The broad consequences flowing from the court's interpretation of section 602(a)5 in *Bishop* suggest that Congress never intended "personal income" to have such a far-reaching and potentially destructive meaning. After *Bishop*, the District will have to examine closely any new revenue scheme.¹³⁰ Although the District will waste no time finding some other way to tap revenue from nonresidents working in the District,¹³¹ the success of such efforts is highly speculative in light of the convoluted logic of the court of appeals in *Bishop v. District of Columbia*.

IV. CONCLUSION

In the Home Rule Act, Congress conferred sweeping powers on the District government, with certain important caveats. One key power withheld was the right to tax the personal income of nonresident workers. The extent of this reservation, however, is ambiguous. In *Bishop v. District of Columbia*, the court of appeals *en banc* construed the prohibition very broadly. In finding the application of the DCUB tax to nonresident non-salaried professionals to be a violation of section 602(a)5 of the Home Rule Act, the court raised more questions than it answered. Not only has the applicability of the DCUB tax to nonresident non-professionals and resident professionals become unclear, but other District taxes affecting nonresidents' personal income may soon be challenged. In future opinions interpreting section 602(a)5, courts should seek to narrow the broad and uncertain construction rendered in *Bishop v. District of Columbia*.

Charles Butler

129. See *District of Columbia v. Bishop*, Petition for Certiorari at 8. All taxes, except perhaps the real property tax, in some indirect way apply to nonresidents when they attach to goods rather than to individuals.

130. The Court of Appeals has created a trap for the unwary. Each revenue package the District enacts will now be subject to the uncertainties of enormous potential liability.

131. See *Washington Post*, March 7, 1980 § A, at 1.

