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State Taxation of Interstate Businesses: A More Liberal Trend

Judy F. Pierce

In conclusion, an argument can be made, based on historical, constitutional, and practical considerations, that misdemeanor defendants having a right to counsel at trial should, if their conviction is unappealable, also have a right to counsel in seeking a writ of review to the Louisiana Supreme Court. However, until statutory or jurisprudential action is taken, these criminal defendants may continue to face the situation of having access to an important and complex legal procedure without the aid of counsel to adequately implement that right.[41]

Jerry Glen Jones

STATE TAXATION OF INTERSTATE BUSINESSES: A MORE LIBERAL TREND

Plaintiff, an interstate carrier of petroleum products, sued to recover taxes paid under the Louisiana corporation franchise tax,[1] challenging the tax as an unconstitutional levy on the privilege of doing interstate business. Plaintiff owns and operates over two hundred fifty miles of pipeline

REV. 783 (1961). The need for counsel to insure an effective application for review has already been recognized at the federal level. FED. R. CRIM. P. 44(a). *See also* Note, 9 WAKE FOREST L. REV. 579, 587-88 (1974).

41. For a further examination of indigent defendants in Louisiana, see Erickson, *The Standards of Criminal Justice in a Nutshell*, 32 LA. L. REV. 369 (1972); Powell, *Extending Legal Services to Indigents and Low Income Groups*, 13 LA. BAR J. 11 (1965); Slovenko, *Representation for Indigent Defendants*, 33 TUL. L. REV. 363; Smith, *Indigent Representation by Law Students: Forum Juridicum*, 30 LA. L. REV. 476 (1970); Note, 33 LA. L. REV. 740 (1973); Note, 33 LA. L. REV. 731 (1973); Note, 47 TUL. L. REV. 446 (1973); Note, 16 LOY. L. REV. 495, 496-97 (1969-70).

1. LA. R.S. 47:601 (1950), *as amended by* La. Acts 1970, No. 325, § 1, provides in pertinent part: "Every domestic corporation and every foreign corporation, exercising its charter, or qualified to do business or actually doing business in this state, . . . shall pay an annual tax . . . on any one or all of the following alternative incidents: (1) The qualification to carry on or do business in this state or the actual doing of business within this state in a corporate form. The term 'doing business' as used herein shall mean and include each and every act, power, right, privilege, or immunity exercised or enjoyed in this state, as an incident to or by virtue of the powers and privileges acquired by the nature of such organizations, as well as the buying, selling or procuring of services or property. (2) The exercising of a corporation's charter or the continuance of its charter within this state. (3) The owning or using any part or all of its capital, plant or other property in this state in a corporate capacity."

within Louisiana but is engaged exclusively in interstate business, having no administrative offices in Louisiana and neither buying nor selling products in the state. The franchise tax was imposed upon plaintiff for its voluntary qualification to do business in the state in a corporate form. Finding the tax to have been levied on the local incident of doing business in a corporate form and not on interstate commerce itself, the United States Supreme Court *held* the tax a constitutionally permissible exaction for the benefits and protections afforded plaintiff's local activities in the corporate form. *Colonial Pipeline Co. v. Traigle*, 421 U.S. 100 (1975).[2]

The commerce clause of the Federal Constitution grants to Congress the power "[t]o regulate Commerce . . . among the several States. . . ."[3] Although the clause, on its face, is only an affirmative grant to Congress of the power to regulate interstate commerce, the United States Supreme Court early decided that it was also a tacit restriction on state regulation.[4] Since taxation is a form of regulation,[5] the commerce clause is also considered a restriction on the exercise of the taxation power by the states;[6] nevertheless, the Supreme Court has long recognized that not all state taxation of interstate business is prohibited.[7]

In distinguishing between prohibited and permitted taxes, the United States Supreme Court has used various approaches over the years and has demonstrated considerable inconsistency in reasoning.[8] Initially, the Court had a rigid attitude toward all state taxation of interstate business,

2. The jurisprudence in the area of state taxation of multi-state businesses is extensive. This note focuses on the United States Supreme Court's treatment of the subject.

3. U.S. CONST. art. I, § 8, cl. 3.

4. Reading R. R. v. Pennsylvania, 82 U.S. 232, 276 (1872) (commerce clause prevents states from interfering with the privilege to carry on interstate business).

5. McCulloch v. Maryland, 17 U.S. 316 (1819).

6. *See* Reading R. R. v. Pennsylvania, 82 U.S. 232 (1872) (state tax that constituted a burden on or regulation of interstate commerce was contrary to the power granted Congress, and, therefore, unconstitutional).

7. *E.g.*, Western Live Stock v. Bureau of Revenue, 303 U.S. 250 (1938) (upholding state tax on multi-state advertising business); Southern National Gas Corp. v. Alabama, 301 U.S. 148 (1937) (upholding state franchise tax on interstate carrier of petroleum products).

8. For a general discussion of approaches used by the Supreme Court in this area, *see* J. HELLERSTEIN, STATE AND LOCAL TAXATION, 163-69 (3d ed. 1969) [hereinafter cited as HELLERSTEIN].

reasoning that states may not tax a privilege granted by the federal government.[9] However, as states' income needs grew and multi-state businesses increased in number, the Court became more willing to examine each specific tax instead of laying down blanket restrictions. If a state tax was a direct tax on interstate commerce, the Court found it unconstitutional, in line with its earlier reasoning that a state cannot tax a privilege granted by the federal government;[10] however, if the tax was indirect, *i.e.*, levied on a local incident, it was not prohibited.[11]

Concentration on the practical effect or burden on interstate commerce of even an indirect tax has overshadowed the direct-indirect test. If a state tax does not create an undue burden on interstate commerce, it will generally be upheld against a commerce clause challenge.[12] A court examining the disputed tax will usually focus on three requirements. First, a state must not impose a tax that discriminates against interstate commerce in favor of intrastate commerce.[13] Second, a state may tax only those activities that are

9. Reading R. R. v. Pennsylvania, 82 U.S. 232 (1872); HELLERSTEIN at 164.

10. *E.g.*, Memphis Steam Laundry Cleaner, Inc. v. Stone, 342 U.S. 389 (1952) (state tax on the privilege of soliciting interstate business unconstitutional); Spector Motor Service, Inc. v. O'Connor, 340 U.S. 602 (1951) (tax on truckers found to be engaged only in interstate commerce invalid); Alpha Portland Cement v. Massachusetts, 268 U.S. 203 (1925) (excise tax on foreign corporations doing exclusively interstate business invalid); Galveston H. & S. Ry. v. Texas, 210 U.S. 217 (1908) (tax on railroads' gross receipts which included receipts from interstate activities unconstitutional).

11. *E.g.*, Stone v. Interstate Natural Gas Co., 103 F.2d 544 (5th Cir.), *aff'd*, 308 U.S. 522 (1939) (upholding franchise tax levied on incidents of business carried on within state by foreign corporations); Southern Natural Gas Corp. v. Alabama, 301 U.S. 148 (1937) (upholding franchise tax, apportioned to corporation's capital within state, on the doing of *local* business); HELLERSTEIN at 165.

12. *E.g.*, Northwestern States Portland Cement Co. v. Minnesota, 358 U.S. 450, 461 (1959) (upholding state income tax on foreign corporations, finding no "undue burden" placed on the business); Ott v. Mississippi Valley Barge Line Co., 336 U.S. 169, 174 (1949) (upholding Louisiana tax on freight carrier, finding no "cumulative effect" on the interstate commerce).

13. *E.g.*, Memphis Steam Laundry Cleaner, Inc. v. Stone, 342 U.S. 389 (1952); Nippert v. City of Richmond, 327 U.S. 416 (1946) (tax on soliciting business placed a heavier burden on interstate than on intrastate businesses); Best & Co. v. Maxwell, 311 U.S. 454 (1940) (tax unconstitutional because it levied a higher payment on out-of-state merchants than on local ones); Welton v. Missouri, 91 U.S. 275 (1875) (holding invalid a tax on peddling products made out-of-state but not on peddling those made locally).

located within the taxing state; therefore, the state must fairly apportion the measure of its tax.[14] Third, a state may tax only those local incidents having such a nexus with the taxing state that the possibility of multiple taxation of the same incident by several states is precluded[15] and the tax will be a fair exaction only for benefits and protections provided by the taxing state.[16]

The trend toward a liberal treatment of state taxes that do not, as a practical matter, unduly burden interstate business was evident in 1948 when in *Memphis Natural Gas Co. v. Stone*[17] the Supreme Court upheld a tax similar to the Louisiana corporation franchise tax. The Mississippi tax in question in *Memphis* was a franchise tax levied on corporations doing business within Mississippi and was measured by the amount of capital used in the state, for which the state gave "the benefit and protection of the government and laws of the state."[18] The Mississippi statute further defined "doing business" as including every activity or benefit exercised or enjoyed in the state by reason of the corporate form.[19] The

14. *Compare* Standard Oil Co. v. Peck, 342 U.S. 382 (1952) (non-apportioned tax on river traffic unconstitutional) *with* Ott v. Mississippi Barge Line Co., 336 U.S. 169 (1949) (Louisiana tax on barge traffic measured by the number of miles traveled within the state as compared with the number of miles traveled in entirety, constitutional).

15. *E.g.*, Northwestern States Portland Cement Co. v. Minnesota, 358 U.S. 450 (1959) (upholding income tax fairly apportioned to foreign corporation's business activities within the state); Michigan-Wisconsin Pipe Line Co. v. Calvert, 347 U.S. 157 (1954) (holding unconstitutional a tax on the gathering of gas intended for shipment out of state); Memphis Natural Gas Co. v. Stone, 335 U.S. 80 (1948) (upholding franchise tax fairly apportioned on basis of capital within state); Joseph v. Carter & Weekes Co., 330 U.S. 422 (1947) (holding invalid a tax on stevedoring because loading and unloading are separable sections of interstate commerce, taxable by both the state of origin and that of destination); Western Live Stock v. Bureau of Revenue, 303 U.S. 250 (1938) (upholding tax on gross receipts from advertising sales within state).

16. *E.g.*, General Motors Corp. v. Washington, 377 U.S. 436, 441 (1964) (upholding tax on wholesale businesses, stating that "the question is whether the State has exerted its power in proper proportion to appellant's activities within the State and to appellant's consequent enjoyment of the opportunities and protections which the State has afforded"); Wisconsin v. J. C. Penney Co., 311 U.S. 435, 444-45 (1940) (Court held valid state tax on corporate earnings, finding that the state gave in return the "substantial privilege of carrying on business").

17. 335 U.S. 80 (1948).

18. Miss. Code § 9314 (1942).

19. *Id.* § 9312 (1942).

Court found that the tax in *Memphis* was levied on a local incident, the maintenance of one hundred thirty-five miles of pipeline within the state,[20] and that the state in return gave appellant the protection of its laws in carrying on such activities.[21]

However, that a tax does not place an undue burden on interstate commerce does not of itself render the tax constitutionally valid. For example, in *Spector Motor Service, Inc. v. O'Connor*[22] a tax was struck down because it was not levied on a local incident; the challenged tax purported to be levied merely on "the privilege of carrying on or doing business."[23] Making only a passing reference to *Memphis*, the United States Supreme Court distinguished that case on the ground that the *Memphis* tax was on an activity that was "local in nature."[24] Much of the *Spector* decision was devoted to an explanation of the separation of taxing powers between the states and the federal government.[25] The Court pointed out that in the commerce clause the states gave Congress the exclusive power to tax the privilege of engaging in interstate commerce[26] and concluded its opinion by stating that "there is not only reason but long-established precedent for keeping the federal privilege of carrying on exclusively interstate commerce free from state taxation."[27]

The tax in *Spector* seems no more burdensome on interstate commerce than that upheld in *Memphis*. The only significant distinction between the two taxes was the terminology used to describe their subjects. The *Memphis* tax purported to tax corporations engaged in business;[28] the *Spector* tax purported to tax only the privilege of doing business.[29] The Court's emphasis on terminology was made further evident in the *Railway Express Agency* cases, *Railway I*[30] and *Railway II*,[31] and again in the instant case. The

20. Memphis Natural Gas Co. v. Stone, 335 U.S. 80, 86 (1948).

21. *Id.* at 96.

22. 340 U.S. 602 (1951).

23. Conn. Gen. Stat. § 354(e) (Cum. Supp. 1937).

24. Spector Motor Service, Inc. v. O'Connor, 340 U.S. 602, 610 (1951).

25. *Id.* at 608-10.

26. *Id.* at 608.

27. *Id.* at 610.

28. Miss. Code § 9314 (1942).

29. Conn. Gen. Stat. § 354(e) (Cum. Supp. 1937).

30. Railway Express Agency, Inc. v. Virginia, 347 U.S. 359 (1954) [hereinafter cited as Railway I].

31. Railway Express Agency, Inc. v. Virginia, 358 U.S. 434 (1959) [hereinafter cited as Railway II].

state tax challenged in *Railway I* was levied on the privilege of carrying on interstate business in the state[32] and was held unconstitutional.[33] However, the Virginia legislature redrafted the law, and the new version was challenged in *Railway II*. The amended law provided for a franchise tax measured by gross receipts and did not purport to tax the privilege of doing business.[34] In upholding the new tax, the United States Supreme Court in *Railway II* stated that a state legislature cannot make an unconstitutional tax valid by changing the words used, but can make a constitutional tax invalid by choosing the wrong words.[35]

In the instant case, the United States Supreme Court accepted the Louisiana Supreme Court's reasoning that the Louisiana franchise tax relates to a corporation's local activities and that the state provides benefits and protections[36] for those activities for which it is justified in asking a fair return.[37] In reconciling its decisions with *Spector* and *Railway I*, the Court emphasized that the Louisiana legislature rephrased the franchise tax law in 1970, repealing an unconstitutional basis for the tax[38] and substituting another basis, thereby making the law "constitutional by limiting its application to operating incidences of activities within Louisiana for which the State affords privileges and protections. . . ."[39]

32. Va. Code § 58-546-47 (1950).

33. Railway I at 369.

34. VA. CODE ANN. § 58-546 (1950) *as amended by* VA. ACTS 1956, ch. 612: "Each express company doing business in this State shall, on or before the first day of June of each year, pay to the State a franchise tax which shall be in lieu of taxes upon all of its other intangible property and in lieu of property taxes on its rolling stock."

35. Railway II at 441. The Court cites *Railway I* and *Spector* as authority. For a further treatment of the *Railway Express* cases and *Spector*, *see* Hellerstein, *State Taxation of Interstate Commerce: Roadway Express, the Diminishing Privilege Tax Immunity, and the Movement Toward Uniformity in Apportionment*, 36 U. CHI. L. REV. 186 (1968); Marsh, *Interstate Commerce: State Taxation of Motor Carriers*, 41 A.B.A.J. 603 (1955).

36. Colonial Pipeline Co. v. Agerton, 289 So. 2d 93, 100 (La. 1974). Such benefits include the right to sue and be sued, continuity of business, the right to transfer property by stock disposition, advantages due to control by corporate directors, and the absence of individual liability.

37. Colonial Pipeline Co. v. Traigle, 421 U.S. 100, 109 (1975).

38. Colonial Pipeline Co. v. Mouton, 228 So. 2d 718 (La. App. 1st Cir. 1969), *cert. denied*, 231 So. 2d 393 (1970) (LA. R.S. 47:601, *as amended by* La. Acts 1958, No. 437, § 2 held unconstitutional as applied to plaintiff). Section 601 then provided that the tax "is due and payable for the privilege of carrying on or doing business. . . ."

39. Colonial Pipeline Co. v. Traigle, 421 U.S. 100, 113 (1975).

Whereas the taxes in *Spector* and *Railway I* were levied expressly on the privilege of doing interstate business, the Louisiana tax is levied on a local activity, the qualification to do business in the corporate form.[40]

The dissent in *Colonial Pipeline* criticized the majority's distinction between taxing interstate commerce and taxing the form in which it is conducted. It failed to find a consistency between the instant case and prior decisions and suggested that if the Court upheld the instant tax, it would be more reasonable to overrule the decisions in *Spector* and *Railway I*.[41]

Although the precedents in the area are inconsistent,[42] if the prior cases are viewed in light of the purposes of the commerce clause, a definite pattern emerges. On a practical level, the commerce clause was designed partly to fulfill the need for free trade on a national level, unfettered by burdensome state regulation.[43] As interpreted by the Supreme Court, the clause has fulfilled this need by requiring that state taxes bearing upon interstate commerce be nondiscriminatory,[44] fairly apportioned,[45] and sufficiently related to local activities for which the state provides benefits in return.[46]

However, conformity with the Court's three-factor test is not enough to satisfy constitutional requirements. An examination of the federal-state implications of the commerce clause should make the reason for the insufficiency obvious; not only was the commerce clause intended as a restriction on

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40. *Id.* at 112-14.

41. "I could understand if the Court today were forthrightly to overrule these precedents and hold that a state franchise tax upon interstate commerce is constitutionally valid, so long as it is not discriminatory." *Id.* at 116 (Stewart, J., dissenting).

42. Justice Blackmun's concurring opinion shared some of the dissent's views and also pointed out the obvious inconsistences among precedents. He recognized the need for clear guidelines in the area of state taxation of interstate commerce and suggested that "a state franchise tax that does not threaten interstate commerce by being discriminatory, or unfairly apportioned, or devoid of sufficient nexus, passes constitutional muster under the Commerce Clause and may be imposed in the absence of Congressional proscription." *Id.* at 114-16 (Blackmun, J., concurring).

43. *See* General Motors Corp. v. Washington, 377 U.S. 436, 440 (1963); Parker v. Brown, 317 U.S. 341, 363 (1943).

44. *See* cases cited in note 13, *supra.*

45. *See* cases cited in note 14, *supra.*

46. *See* cases cited in notes 15 & 16, *supra.*

the power of the states to burden interstate commerce, it is primarily a grant of power to Congress.[47] As pointed out in the *Spector* decision, the commerce clause gives Congress the exclusive power to regulate interstate commerce, and its power must be kept free from state interference.[48] If a state is allowed to tax interstate commerce, by implication it may control and eventually destroy it, for the power to tax is the power to control and destroy.[49] Thus, although the *Spector* tax was not likely to burden interstate commerce to a greater extent than the tax challenged in the instant case, the *Spector* tax was apparently objectionable because, by claiming to tax the privilege of carrying on interstate commerce, the tax suggested that the state could exercise control over interstate commerce. The tax in the instant case does not run afoul of the commerce clause because it does not purport to tax the privilege of doing interstate business, and thus does not suggest state control of that federal privilege. Although the distinction between taxing the privilege of doing business and taxing the form of doing business may make "no practical sense,"[50] it does make "constitutional sense."[51] In our federal system, the power to regulate interstate commerce belongs exclusively to Congress, and the states may not share in that control.

The decision in the instant case has clarified the Supreme Court's position. Although the Court has shown a liberal attitude toward state taxes that bear upon but do not burden multi-state businesses unfairly, it has shown a strict adherence to the tenet that states may not reach, or at least purport to reach, the forbidden fruit of interstate commerce. Thus, a four factor test emerges: a state tax statute which burdens interstate commerce must be non-discriminatory, be fairly apportioned, demonstrate a sufficient nexus to local activity and return, and be worded in such a manner that it does not purport to tax the privilege itself of carrying on interstate business.

The last restriction is, in fact, little more than a phantom. The decisions in *Spector, Railway I* and *II*, and the instant

47. Spector Motor Service, Inc. v. O'Connor, 340 U.S. 602, 608 (1951).

48. *Id.* at 608-10; Nippert v. City of Richmond, 327 U.S. 416, 425 (1946).

49. Nippert v. City of Richmond, 327 U.S. 416, 424 (1946); McCulloch v. Maryland, 17 U.S. 316, 431 (1819).

50. Colonial Pipeline Co. v. Traigle, 421 U.S. 100, 115 (1974) (Blackmun, J., concurring).

51. *Id.*

case seem to indicate that a state legislature can make an otherwise unconstitutional tax constitutional by rephrasing a statute so that it purports to tax a local incident, such as the form of doing business, rather than the privilege of doing interstate business. This distinction is, however, justified as a means of safeguarding the federal-state taxing dichotomy created by the commerce clause, as construed by the United States Supreme Court.

Judy F. Pierce

CONDITIONS FOR THE APPLICATION OF ACTIO DE IN REM VERSO

Defendant, A-Second Mortgage Co., which held a second mortgage on the plaintiff's property, agreed to accept the property in full settlement of its claim and to pay the plaintiff's first mortgage notes on the property as they matured.[1] A-Second was relieved of the additional obligation when the first mortgage was satisfied from proceeds of a life insurance policy which the plaintiff had previously purchased from and assigned to the first mortgagee. Realizing that she had lost both the insurance proceeds and the property, plaintiff sued the first and second mortgagees for recovery of the amount of insurance proceeds applied to the first mortgage. Reversing the First Circuit Court of Appeal,[2] the Louisiana Supreme Court *held* that A-Second had been unjustifiably enriched and that the plaintiff could recover the sum on the basis of an *actio de in rem verso*.[3] *Edmonston v. A-Second Mortgage Co.*, 289 So. 2d 116 (La. 1974).

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1. Whether A-Second legally assumed the mortgage was never determined. The trial court judge stated that such a determination was not material to the ultimate issues in dispute. Trial Record, 22d J.D.C., Parish of St. Tammany, #28,064 at 106 (Wallace A. Edwards Div. "B"; June 9, 1972) [hereinafter cited as Trial Record].

2. Edmonston v. A-Second Mortgage Co., 273 So. 2d 707 (La. App. 1st Cir. 1973).

3. The *actio de in rem verso* derives from Roman law, which provided the action for the recovery of necessary expenses incurred by a slave, as an unauthorized agent, for the benefit of his master. W. HUNTER, A SYSTEMATIC AND HISTORICAL EXPOSITION OF ROMAN LAW IN THE ORDER OF A CODE 616 (3d ed. 1897) [hereinafter cited as HUNTER].