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Constitutional Law: Taxation of Interstate Commerce

R. H. Moseley

procedure offered by the wire recorders is a very practical aid to both sides in a lawsuit, and especially to law enforcement officers, in preparing the evidence for presentation in the case, but the ultimate importance lies in the opportunity afforded the court and the jury to consider the sounds or conversations themselves rather than rely upon the mere recitals of the fact.[7]

CHARLES R. JONES
University of Oklahoma

CONSTITUTIONAL LAW: TAXATION OF INTERSTATE COMMERCE

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

Petitioner, a nonresident corporation, engaged solely in interstate business within the state of Connecticut. It maintained an office and staff as well as a small fleet of pick-up trucks to facilitate the pick up of items to be shipped to points in other states. The petitioner contested a ruling of liability under the Connecticut Corporations Business Tax Act of 1935. On certiorari to the United States Supreme court,[1] HELD, the imposition of a tax by a state, irrespective of the measure, on the corporate franchise for the privilege of engaging in interstate commerce is invalid under the Commerce Clause.

The Court rested its decision on the theory that the states may not tax a right which is not theirs to give — that interstate commerce is the exclusive concern of the Federal Government.[2] The opinion lacks the convincing logic that might be expected or at least hoped for in so important a decision. It seems clearly to be a return to the old "subject" test — to the dogma of half a century ago which pro-

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[7]"The wire recorder which reproduces the actual voice of the accused and those who may be questioning him should be of much more value to the court and the jury than a confession taken in shorthand and later reduced to writing, especially where an issue has been raised as to whether the confession was voluntarily made." *Ibid.*

[1]The case had spent eight years in the courts.

[2]At page 608.

claimed that interstate commerce could not be the subject of taxation by the states. For this reason *Spector Motor Service v. O'Connor* is a most significant case.[3]

That the Court returned to the subject test, and disregarded intervening cases which had attempted a more realistic analysis of the injury, if any, to interstate commerce, may be seen from an examination of the statute with which the Court was dealing. Section 41 (c) of the Act provided in part:

> "Imposition of the tax. Every . . . corporation or association carrying on business in this state . . . shall pay, annually, a tax or excise upon its franchise for the privilege of carrying on or doing business within the state, such tax to be measured by the entire net income as herein defined received by such corporation or association from business transacted within the state during the income year and to be assessed at the rate of two per cent . . . ."

The Supreme Court accepted as controlling the determination by the Supreme Court of Errors of Connecticut that the tax was "upon the franchise of corporations for the privilege of . . . doing business in the state . . . ."[4] This was found fatal to the cause of the respondent tax commissioner.

The measure of the tax, though considered by the Court to have no bearing, should be noted. It was to be determined by the application of an allocation formula to the net income of the corporation. The formula used a fraction which was the average of three ratios: (1) the ratio of tangible property of the taxpayer in the state to all tangible property everywhere, (2) the ratio of wages and salaries paid in the state to all wages and salaries, and (3) the ratio of gross receipts assignable to the state to all gross receipts.

It is evident that this measure was fairly and carefully drafted so

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[3]Although the principal case will come as a surprise to many, its possibility had not been overlooked. See Overton, *Taxation of Interstate Commerce,* 19 TENN. L. REV. 870, 873 (1947): "At the present time there are some indications that . . . a return to the original 'subject' test may become the technique of the Court." The article is a comprehensive and perspicacious analysis of the problem.

[4]Spector Motor Service v. Walsh, 135 Conn. 37, 56 (1948). The court there found the tax valid.

that it would avoid the deficiencies which earlier decisions had found in similar tax structures. Such a measure, even if used by other states, would result in no multiple burdens on interstate commerce.[5] The statute and its measure reflected, moreover, the economic realism of an approach that required interstate commerce to pay its own way.[6]

It is believed that the authority of the modern decisions, as well as an analysis based on economic fact, would have supported a finding of validity of the tax in the principal case. In *Memphis Natural Gas Co. v. Stone*[7] a Mississippi franchise tax measured by the portion of capital invested within the state was sustained on a nonresident corporation engaged only in interstate commerce within the state. The Court said that there were localized activities which were taxable and found that the tax was not on the privilege of doing business but was on the things done in Mississippi. The Court has also sustained a net income tax on a corporation whose receipts were almost entirely taken from interstate commerce.[8] Of course, it was early held that a tax on net income *from* interstate commerce was not *on* interstate commerce. Gross receipts, properly apportioned, have also been found valid tax instrumentalities where applied to a business which was both interstate and intrastate.[9] The logical conclusion of these decisions, it seems, should have supported a finding of validity of the tax although it was upon a corporation doing only interstate business, since there was no discrimination, no multiple burdens, no possibility of duplication, and no extraterritoriality.[10]

It can be hoped that we shall soon see a judicial miracle of the

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[5]This was the basis of the decisions in Gwin, White & Prince v. Henneford, 305 U.S. 434 (1939), and McGoldrick v. Berwind-White Coal Mining Co., 309 U.S. 33 (1940). The evil results from an improper measure, which may cause multiple burdens when used by other states. Such a result is always bad in a federal system, where we are concerned alike with the integrity of the whole and the stability of the component parts.

[6]In this connection Chief Justice Stone had said, ". . . even if taxpayer's business were wholly interstate commerce, a nondiscriminatory tax by Tennessee upon the net income . . . is not prohibited by the commerce clause . . . ." He spoke for a unanimous court, Memphis Natural Gas Co. v. Beeler, 315 U.S. 649, 656 (1942).

[7]335 U.S. 80 (1948).

[8]See note 6 *supra*. Interstate commerce provided 85% of the corporation's earnings.

[9]Central Greyhound Lines v. Mealy, 334 U.S. 653 (1948).

[10]Western Live Stock v. Bureau of Revenue, 303 U.S. 250 (1938); Adams Mfg. Co. v. Storen, 304 U.S. 307 (1938).