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## Indiana Gross Income Tax Act-Interstate Commerce

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INDIANA GROSS INCOME TAX ACT—INTERSTATE COMMERCE.—The Indiana Gross Income Tax Act imposes a tax on the gross income of residents and domestic corporations derived from transactions conducted in interstate commerce except that which Indiana is prohibited from taxing by the Constitution of the United States. In a recent decision, the Indiana Supreme Court held a manufacturer taxable for the gross income which he received from sales in interstate commerce.<sup>1</sup>

It is elementary constitutional law that a state cannot by taxation or otherwise interfere with the power of Congress to regulate foreign or interstate commerce.<sup>2</sup> Any possible state taxation may conceivably have some slight effect upon interstate commerce;<sup>3</sup> but if state taxation goes too far it will be prohibited either because it would interfere with the federal government's regulation, or it would be regulation in itself.<sup>4</sup> The problem is to what extent the state may go without unreasonably burdening interstate commerce. In the principal case the Indiana court interpreted the present constitutional law to be that interstate commerce is exempt from only unreasonably discriminatory taxation by the states. This, however, does not seem to follow the decisions of the United States Supreme Court, the rule of which appears to be: states may tax property used in interstate commerce, but they cannot levy a direct tax on that commerce.<sup>5</sup> A state tax which affects interstate commerce only remotely is valid so long as it does not impose a discriminatory or unreasonable burden on that commerce.<sup>6</sup>

If the tax is to be justified in the principal case, it must come under the latter rule; that is, the tax must be one that affects interstate commerce only

<sup>1</sup> *Storen v. J. D. Adams Co.* (Ind. 1937), 7 N. E. (2d) 941; construing the Gross Income Tax Act of 1933, Burns '33, sec. 64-2606(a), not altered by amendment in Acts of 1937, Ch. 117, sec. 6 (a).

<sup>2</sup> Willis, *Constitutional Law*, p. 304. But see *Brown, When is a Tax not a Tax?*, 11 *Indiana L. J.* 399, maintaining that if an act is not for the purpose of raising revenue it is not a tax, but an exercise of the police power.

<sup>3</sup> *Brown, State Taxation of Interstate Commerce*, 81 *U. of Pennsylvania L. Rev.* 247.

<sup>4</sup> *State Tax on Gross Receipts* (U. S. 1872), 15 *Wall.* 284, 21 *L. Ed.* 230; *Western Union Tel. Co. v. Kansas* (1910), 216 *U. S.* 180, 30 *S. Ct.* 190, 54 *L. Ed.* 355; Willis, *loc. cit.*, *supra*, note 2.

<sup>5</sup> The first decision on the subject upheld a tax on the gross receipts of a transportation company, *State Tax on Gross Receipts*, (U. S. 1872), 15 *Wall.* 284, 21 *L. Ed.* 164. But the Supreme Court refused to follow this case by distinguishing it in *Fargo v. Michigan* (1887), 121 *U. S.* 230, 7 *S. Ct.* 861, 30 *L. Ed.* 893; and in *Philadelphia S. S. Co. v. Pennsylvania* (1887), 122 *U. S.* 326, 7 *S. Ct.* 1113, 30 *L. Ed.* 1200 repudiated it. See *Brown, Restrictions on State Taxation Because of Interference with Federal Functions*, 17 *Virginia L. Rev.* 325. Cases in accord with *Philadelphia S. S. Co.* case: *Galveston etc. Ry. Co. v. Texas* (1908), 210 *U. S.* 217, 28 *S. Ct.* 638, 52 *L. Ed.* 1031; *Crew Levick Co. v. Pennsylvania* (1917), 245 *U. S.* 292, 38 *S. Ct.* 126, 62 *L. Ed.* 295; *N. J. Bell Tel. Co. v. State Board* (1930), 280 *U. S.* 338, 50 *S. Ct.* 111, 74 *L. Ed.* 463; *Peck and Co. v. Lowe* (1918), 247 *U. S.* 165, 38 *S. Ct.* 432, 62 *L. Ed.* 1049; *Meyers v. Wells, Fargo Co.* (1912), 223 *U. S.* 298, 32 *S. Ct.* 218, 56 *L. Ed.* 445.

<sup>6</sup> *American Manufacturing Co. v. St. Louis* (1923), 261 *U. S.* 330, 43 *S. Ct.* 266, 67 *L. Ed.* 682; *U. S. Exp. Co. v. Minnesota* (1912), 223 *U. S.* 335, 32 *S. Ct.* 328, 56 *L. Ed.* 459; *Cudahy Packing Co. v. Minnesota* (1918), 246 *U. S.* 450, 38 *S. Ct.* 373, 62 *L. Ed.* 827; *Postal Tel. Co. v. Adams* (1895), 155 *U. S.* 688, 15 *S. Ct.* 268, 39 *L. Ed.* 34.

remotely. The U. S. Supreme Court has held that for a gross receipts tax to be other than a direct tax on interstate commerce, the tax must be in fact a property or excise tax on subjects within the taxing power of the states. Then the tax is not on the gross receipts, but such receipts are merely used as a measure of value of the property or privilege taxed.<sup>7</sup> The majority of the Indiana court held the instant tax to be in effect a property tax since the purpose of its enactment was to relieve the burden upon property. However, any tax law is passed in the expectation that the burden of other taxes will be relieved. To determine whether the tax is a property or a license tax, we must look at the practical operation and general affects of the tax.<sup>8</sup> If the tax is in addition to all other taxes it is invalid as a direct tax, since it is obviously not an attempt to reach the value of property or privileges which is by law already valued and taxed in a different manner.<sup>10</sup> Whereas section 19 of the act decrees: "The tax imposed by this act shall be in addition to all licenses and taxes imposed by law . . ." it is submitted that the law imposes a direct tax on interstate commerce.<sup>11</sup>

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<sup>7</sup> *Ibid.*

<sup>8</sup> *Pullman Co. v. Richardson* (1923), 261 U. S. 330, 43 S. Ct. 366, 67 L. Ed. 682; *Galveston etc. R. C. v. Texas* (1908), 210 U. S. 217, 28 S. Ct. 638, 52 L. Ed. 1031.

<sup>9</sup> *American Manufacturing Co. v. City of St. Louis* (1919), 250 U. S. 459, 39 S. Ct. 522, 63 L. Ed. 1084, was largely relied upon by the majority in the principal case. It held that a license tax on a manufacturer as a condition precedent to doing business was valid, even though the tax was measured by the value of the goods manufactured. This value was computed by the gross receipts from their sales which were largely to customers in other states. The court explicitly held that there was no direct tax on the commerce in the goods manufactured. This was more dramatically displayed in *Utah Power & Light Co. v. Pfof* (1932), 286 U. S. 165, 52 S. Ct. 548, 76 L. Ed. 1038, where power generated in one state and immediately transmitted to another state was held taxable in the state where generated. It was a license tax and measured by the power reaching consumers, many of whom were in foreign states. The power company should not complain that it was not taxed on leakage in transmission. *Pullman Co. v. Richardson* (1923), 261 U. S. 330, 43 S. Ct. 366, 67 L. Ed. 628; *U. S. Express Co. v. Minnesota* (1912), 223 U. S. 355, 32 S. Ct. 328, 56 L. Ed. 459 (property tax); *Cudahy Packing Co. v. Minnesota* (1918), 246 U. S. 450, 38 S. Ct. 373, 62 L. Ed. 827 (tax in lieu of all other taxes of a given percentage on gross earnings sustained); *Foster v. Hart etc. Mining Co.* (1913), 52 Colo. 459, 122 P. 48; *Culliton v. Chase* (1933), 174, Wash. 363, 25 P. (2d) 81. *Brown, Constitution Limitation on Progressive Taxation of Gross Income*, 22 *Iowa L. Rev.* 246.

<sup>10</sup> *Meyers v. Wells, Fargo Co.* (1912), 223 U. S. 298, 32 S. Ct. 218, 56 L. Ed. 445. *Brown, Restrictions on State Taxation Because of Interference with Federal Functions*, 17 *Virginia L. Rev.* 325. Also see notes in 28 *Harvard L. Rev.* 93, 28 *Michigan L. Rev.* 1062, and 39 *Yale L. J.* 750. The importance of this is shown in the dissent of Holmes, J., *N. J. Bell Tel. Co. v. State* (1930), 280 U. S. 338, 50 S. Ct. 111, 74 L. Ed. 463.

<sup>11</sup> The majority opinion used as its authority *Am. Mfg. Co. v. St. Louis*, supra note 9, *Pullman Co. v. Richardson*, supra note 9, and *Galveston etc. Ry. Co. v. Texas*, supra note 8. The first case held the tax questioned to be a license tax, see supra note 9, and the latter two cases held the taxes on gross receipts there questioned to be direct burdens on interstate commerce, and therefore unconstitutional.

Neither will comparison of the gross income tax law with net income taxes save the tax on interstate commerce. The Supreme Court, as pointed out in the dissent of Treanor, J., has drawn the distinction. Gross receipt taxes affect each transaction in proportion to its magnitude, irrespective of whether it is profitable or otherwise. This may make the difference between a profit and a loss, or it may so diminish profit as to impede and discourage the conduct of commerce. Net income taxes do not arise unless a profit is shown over and above all expenses, and the tax cannot be heavy unless the profit is large. A gross income tax is therefore a direct and immediate burden on interstate commerce, and hence prohibited, while a net income tax is a charge that is only indirect and incidental.<sup>12</sup>

The present state of the law may seem to be technical, but it is supported by a degree of common sense. Since it is established that any law affecting commerce regulates it, and whereas interstate commerce is purely a legal concept, the limits thereof must be fixed by practical lines. Thus the court drew that line on the assumption that when a state is attempting to value property it is less likely to attempt to effect injurious regulations than when it is aiming directly at the receipts from interstate commerce.<sup>13</sup>

However, the logic of the present view is predicated upon the major premise established by Chief Justice Marshall in the memorable case of *McCulloch v. Maryland*:<sup>14</sup> viz. it is undesirable to grant states unlimited power of taxation of interstate commerce because it would enable them to stop this function of the federal government—the power to tax involves the power to destroy. But, as shown by Justice Holmes, this idea is founded upon the falacious assumption that there cannot be distinctions of degree.<sup>14a</sup> The power of taxation does not involve the power of destruction; only unreasonable or discriminatory taxes destroy. The purpose of the commerce provisions of the Constitution was to prevent discrimination among the states,<sup>15</sup> not to exempt those engaged in interstate commerce from their fair share of the expenses of government of the states in which they operate.<sup>16</sup>

Until recent times the courts' interpretation of the commerce clause did not seriously impede the machinery of taxation. Businesses engaged in

<sup>12</sup> U. S. *Glue Co. v. Oak Park* (1918), 247 U. S. 321, 328, 329, 38 S. Ct. 499, 62 L. Ed. 1135, Ann. Cas. 1918E, 748.

<sup>13</sup> *Galveston etc. Ry. Co. v. Texas* (1908), 210 U. S. 217, 28 S. Ct. 638, 52 L. Ed. 1031.

<sup>14</sup> (U. S. 1819), 4 Wheat. 316, 4 L. Ed. 579.

<sup>14a</sup> Holmes, J., dissent, *Panhandle Oil Co. v. Mississippi* (1928), 277 U. S. 218, 223, 72 L. Ed. 857, 48 S. Ct. 451: "(concerning Marshall's statement) In those days it was not recognized as it is today that most of the distinctions of the law are distinctions of degree. If the States had any power it was assumed that they had all power, and that the necessary alternative was to deny it altogether. But this Court which so often has defeated the attempt to tax in certain ways can defeat an attempt to discriminate, or otherwise go too far without wholly abolishing the power to tax. The power to tax is not the power to destroy while this Court sits."

<sup>15</sup> Perkins, *The Sales Tax and Transactions in Interstate Commerce*, 12 North Carolina I. Rev. 99, p. 104, notes 23, 24.

<sup>16</sup> See Stone, J., concurring, *Helson v. Kentucky* (1929), 279 U. S. 245, 253, 49 S. Ct. 279, 73 L. Ed. 683.

interstate commerce had not reached their present proportions. The principal form of taxation was property taxes, and property engaged in interstate commerce was always a proper subject of state taxation. But modern business has necessitated modern methods of government finance. Increased state functions require increased revenues. An increased proportion of the wealth of the community is represented by intangibles, and this makes the use of Nineteenth Century tax methods economically unsound. Sales taxes and income taxes have become more important. The increase of nation wide business in competition with state and local businesses together with modern facilities of transportation and communication have accentuated the effect of a tax which must discriminate in favor of the former. As a matter of policy there is no reason why business in interstate commerce should not pay its own way in the form of non-discriminatory state taxes.<sup>17</sup>

There are two ways in which states might get this much needed power—either the Supreme Court might reverse its previous decisions and uphold the rule set forth in the principal case, or Congress might give states permission to extend general application of certain types of taxation to businesses operating in interstate commerce. Should the Supreme Court effect the change, it would be acting in no more revolutionary a manner than it did when it alleviated the acute situation in regard to multiple taxation by the states.<sup>18</sup> If Congress should take the initiative it could enact a law similar to the one relative to state taxation of national banks.<sup>19</sup> Some might contend that if the United States Constitution prohibits the states from levying a direct tax on interstate commerce, Congress does not have the power to effect a change. However the restrictions upon the states' power to tax interstate commerce are no greater than those on the states' power to tax federal instrumentalities,<sup>20</sup> and Congress has been allowed to delegate to the states the power to impose certain taxes on national banks.

Pending the decision of the Indiana Supreme Court in the principal case taxpayers were permitted to defer the payment of gross income taxes upon gross receipts which were derived from transactions made in interstate commerce, but they were required to keep a separate account of such gross receipts.<sup>21</sup> Although the Indiana Supreme Court has now decided that these transactions are taxable, since the plaintiff in this case now contemplates appealing the decision to the United States Supreme Court, the Gross Income Tax Division has extended the privilege of deferrment of payment of the tax on such gross receipts, but has cancelled the privilege of deferring the reporting thereof. As a condition to the privilege of deferring payment, taxpayers have been required to file information reports on their

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<sup>17</sup> *Ibid.*

<sup>18</sup> *Farmers L. and T. v. Minnesota* (1930), 280 U. S. 204, 50 S. Ct. 98, 74 L. Ed. 371; *Baldwin v. Missouri* (1930), 281 U. S. 586, 50 S. Ct. 436, 74 L. Ed. 1056; *Beidler v. Commission* (1930), 282 U. S. 1, 51 S. Ct. 54, 75 L. Ed. 131. *Brown, Multiple Taxation by the States*, 48 *Harvard L. Rev.* 407.

<sup>19</sup> R. S. 5219.

<sup>20</sup> *Brown, Restrictions on State Taxation Because of Interference with Federal Functions*, 17 *Virginia L. Rev.* 325.

<sup>21</sup> *Regulations under Indiana Gross Income Tax Act of 1933, Regulation 190.*

gross receipts from transactions in interstate commerce since May 1, 1933.<sup>22</sup> It is hoped that an early decision will settle this matter of doubt to the taxpayers of Indiana.

-H. A. F.

**TEACHER TENURE CONTRACTS—DISCRIMINATION AGAINST MARRIED WOMEN TEACHERS.**—Appellee, a married woman, was a tenure teacher in the schools of Michigan City, Indiana. Due to economic conditions, the school trustees adopted a new salary schedule which discriminated in amount of compensation paid married women teachers. Appellee instituted this action to collect additional compensation for her services on the theory that the schedule was void as to married women teachers. The trial court found the schedule invalid. The Appellate Court held that discrimination in fixing women teachers' salary because of marriage would be capricious to a teacher who was as competent and efficient after marriage as before; and transferred the case to the Supreme Court with a recommendation that *McQuaid v. State ex rel. Sigler*, holding marriage "good and just cause" for cancellation of a teacher's contract, be overruled. The Supreme Court held that the discrimination was unreasonable, but that the *McQuaid* case was inapplicable to the facts of the principal case.<sup>1</sup>

There is an honest difference of opinion on the public policy of allowing married women to teach. In England, the power of educational authorities to remove women teachers who are married has been sustained.<sup>2</sup> In the United States, in the absence of any statutory provisions, marriage of a woman teacher has generally been held to be not in itself grounds for discharge,<sup>3</sup> and under statutes giving power to discharge for reasonable grounds has usually been held not to be a reasonable ground.<sup>4</sup> In recent years the trend of public opinion has been against allowing married women to teach, and some statutes have been interpreted as giving school boards authority to dismiss them.<sup>5</sup> This trend is due, no doubt, to the economic conditions which have turned many men and single women out of work.

The *McQuaid* case,<sup>6</sup> undoubtedly the outgrowth of this public opinion, repudiated two leading Indiana decisions which held marriage in itself

<sup>22</sup> Temporary regulation 3801 (approved June 25, 1937).

<sup>1</sup> *State ex rel. Hutton v. Gill* (Ind. 1937), 8 N. E. (2d) 818 (Sup.), 7 N. E. (2d) 1011 (App.).

<sup>2</sup> *Short v. Poole* (1926), 1 Ch. 66, 14 British Rul. Cas. 641, note.

<sup>3</sup> 56 C. J. 403.

<sup>4</sup> *State ex rel. Pittman v. Barker* (1934), 113 Fla. 865, 152 So. 682, 94 A. L. R. 1481; *School Dist. of Wildwood v. State Board of Education* (1936), 116 N. J. Law 572, 185 A. 664 (N. J. act is quite similar to the Indiana act); *People v. Board of Education of N. Y.* (1914), 212 N. Y. 463, 106 N. E. 307; *People v. Maxwell* (1904), 117 N. Y. 494, 69 N. E. 1092; *Richards v. District School Board* (1916), 78 Or. 621, 153 P. 482, Ann. Cas. 1917B, 226, L. R. A. 1916C, 789; *State v. Board of School Directors of City of Milwaukee* (1923), 179 Wis. 284, 191 N. W. 746. See also 56 C. J. 403, 88 A. L. R. 1103, and Stephenson, *Handbook of Indiana School Law* (1929), p. 181.

<sup>5</sup> *Rinaldo v. Dreyer* (Mass. 1936), 1 N. E. (2d) 37; *Ansofrage v. City of Green Bay* (1929), 198 Wis. 320, 224 N. W. 119; 24 R. C. L. 612ff.

<sup>6</sup> *McQuaid et al. v. State ex rel. Sigler* (Ind. 1934), 6 N. E. (2d) 547.