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STATE TAXATION OF INTERSTATE COMMERCE, AND
FEDERAL AND STATE TAXATION IN INTERGOVERNMENTAL RELATIONS—1932-1935

ROBERT C. BROWN *

IT IS well known that the Federal Constitution gives to Congress the power "To regulate Commerce with foreign Nations and among the several States and with the Indian Tribes." 1 This clause of the Constitution (usually referred to as the "Commerce Clause") is one of the most important provisions of the original Constitution. In fact, one of the chief purposes of forming our national government was to give Congress this power, and thus put a stop to a very frequent and vicious feature of the old confederacy, namely, interference by the different states with commerce involving other states or countries. It will be noted that the clause covers not only commerce involving more than one state (interstate commerce in the strict sense), but also commerce with the Indian tribes, and also foreign commerce. Commerce with the Indian tribes is today of comparatively slight importance, but foreign commerce still remains of considerable consequence. The power of Congress is exactly the same with respect to foreign and Indian commerce as it is with respect to interstate commerce in the strict sense; and no distinction can justifiably be made, or has in fact been made, with respect to these different kinds of commerce within the regulatory power of Congress. In this article, following a usual and convenient, if somewhat inaccurate, practice, the phrase "interstate commerce" will be used to cover not only commerce between the states, but also foreign commerce and, if need arise, commerce with the Indian tribes.

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1 Art. I, § 8, Cl. 3.

All that is said in the Constitution is that Congress has power to regulate such commerce. From this, it would certainly not follow that the states are precluded from similar regulation, though some court decisions have seemed to indicate an idea that such is the case. However this may be, it is entirely certain that the states may not discriminate against interstate commerce (in the broad sense previously explained), nor may they unreasonably burden it. The court decisions to this effect are innumerable. Furthermore, it is a fair inference from the commerce clause that any state power to regulate such commerce is clearly subordinate to the power of Congress.

The mere words of the commerce clause, however, certainly do not demand, even if they possibly justify, the ruling that states may not burden, or discriminate against, interstate commerce. The correctness of the numerous decisions of the Federal Supreme Court to that effect is, however, hardly doubtful. As already pointed out, one of the primary purposes of the formation of our national government was to put an end to such interferences by the individual states. To construe the commerce clause as including a prohibition against such state interference is, therefore, reasonable, and in accordance with the intent of the makers of the Constitution. Furthermore (and this is the problem with which we are definitely concerned here), such improper interference by the states may be through taxation as well as by other methods.

But another restriction upon the power of the states also merits consideration. This is, that the states may not burden the functions of the Federal Government. And conversely, the Federal Government may not burden state functions. For neither of these well-settled propositions is there even a shadowy verbal justification in the terms of the Constitution, as is the case with respect to interstate commerce. The truth is that this whole doctrine is purely a judicial invention, but one which is believed to be both theoretically and practically justified. Even the original terms of our Constitution clearly contemplated a dual form of government, with both nation and states existing and operating effectively in their respective spheres. The very early Tenth Amendment also reenforces this theory. And it

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3 This amendment, ratified in 1791 as one of the original ten amendments to the Constitution, provides, “The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively or to the people.”
is entirely evident that such a dual form of government is workable only if in governmental relations the respective members of the partnership—the nation and the several states—are restricted from burdening, and thereby potentially destroying, the operations of the other. It is possible that the Federal Government has somewhat greater powers to interfere with the states than have the states to interfere with the Federal Government, but, in general, the Federal Supreme Court has wisely striven to keep a perfect balance between states and nation.

Again it is obvious that such prohibited interference may be accomplished by sundry methods; but the method of taxation, with which we are here concerned, is certainly not one of the least effective. It is, in fact, one of the most frequently used—and condemned. We are concerned, then, with the rule that the states may not unreasonably burden interstate commerce in the broad sense by taxation, and that neither the states nor the nation may impose taxes which unreasonably burden the functions of the other.

However, the word "unreasonably" is used advisedly, for any statement of the rule which left out this word (even though such statement occasionally appears in judicial opinions) would be merely ludicrous. For example, if it were the law that no state could impose a tax which by any possibility imposed a burden upon interstate commerce, the states would be precluded from imposing any corporation or excise taxes, as all such would affect interstate business and, therefore, would burden interstate commerce. In fact, we may go further and say that the states could impose no taxes at all, for even a land tax may burden activities upon the land, and such activities may affect interstate commerce. Furthermore, a rule that the states could not impose any tax in any way affecting the Federal Government would have a similar result. And conversely, a rule that the Federal Government could impose no tax in any way affecting state functions would wipe out one hundred per cent of the federal taxing power.

Fortunately, the Federal Supreme Court, which is, of course, the supreme authority in this matter, whatever it may at times have said, has rarely in fact attempted to enforce rigid rules bringing about such utterly impossible results. The problem is

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a practical one, and is necessarily one of adjustment rather than complete prohibition. The Court has at times taken the position that the prohibition of taxes affecting the other member of our dual system of government is more rigid than the restriction upon the power of the states to impose taxes affecting interstate commerce; but the truth seems to be that the problem is essentially the same in both cases. For reasons already pointed out, complete rigidity would result in the destruction of both the state and Federal Government. The problem lacks the dramatic force of the important constitutional questions now arising out of the unprecedented activities of the Federal Government during the present administration; but basically it involves the same contention as to what are the proper respective spheres of activity of the nation and the states.

Since this is a problem of practical adjustment, it is one which recurs constantly in different forms. This means that it has never been settled in all its aspects, and very probably never will be. However, as in other branches of constitutional law, the piling up of precedents has at least delimited the field of judicial and practical uncertainty. This has been going on since the beginning of our government, but the tax problem has become more serious, if anything, in the last decade or so. Accordingly, we find that contemporary decisions on this point are quite numerous and are of enormous importance. It is the purpose of this article to consider Supreme Court decisions upon state taxation affecting interstate commerce, and federal and state taxation in intergovernmental relations during the three terms of the Supreme Court beginning in October, 1932, and ending with the close of the October, 1934, term.

5 See, e. g., Gillespie v. Oklahoma, 257 U. S. 501 (1922), where the Court, speaking through Mr. Justice Holmes, said at p. 505, "The criterion of interference by the States with interstate commerce is one of degree. It is well understood that a certain amount of reaction upon and interference with such commerce cannot be avoided if the States are to exist and make laws. . . . The rule as to instrumentalities of the United States on the other hand is absolute in form and at least stricter in substance."


7 See, for a discussion of the earlier authorities on the topics of this article, Brown, Restrictions on State Taxation because of Interference with Federal Functions (1931) 17 Va. L. Rev. 325; State Taxation of Interstate Commerce, and State and Federal Taxation in Intergovernmental Relations—1930-1932 (1933) 31 U. of Pa. L. Rev. 247.
The Interstate Commerce Cases

The first problem with regard to interstate commerce is obviously as to what may be regarded as such commerce. It is certain that there may be facilities for such commerce which are not themselves commerce, and therefore have no immunity from state taxation.

This problem was presented to the Court in a case involving the question of the power of the state of Michigan to impose a franchise tax upon a domestic corporation, the sole asset of which was an international bridge between Michigan and Canada. The contention of the taxpayer was that it was immune from tax, upon the ground that its only asset was a facility of foreign commerce, and that, accordingly, such a tax would effect a direct burden upon that commerce. The Court dismissed this contention on the short ground that the certificate of incorporation of the taxpayer gave it broader powers than the construction and maintenance of the bridge in question, and that, therefore, it could not be shown that its franchise was restricted to the maintenance of a facility of foreign commerce. However, in the second appeal of the same case, nearly three years later, the taxpayer had removed any basis for this decision by amending its charter so as to restrict its powers to the operation of the bridge.

However, the taxpayer was again denied relief, on the theory that the maintenance of the bridge was not engaging in foreign commerce. The Court relied upon a much older case where it was held that a state could impose a property tax upon that portion of an interstate bridge situated within the state, notwithstanding the fact that the bridge was a facility of interstate commerce and could be used only for that purpose. In reaching this conclusion, the Court said:

"Clearly the tax was not a tax on the interstate business carried on or by means of the bridge, because the bridge company did not transact such business. That business was carried on by the persons and corporations which paid the bridge company tolls for the privilege of using the bridge. The fact that the tax in question was

10 Henderson Bridge Co. v. Kentucky, 166 U. S. 150 (1897).
to some extent affected by the amount of the tolls received, and therefore might be supposed to increase the rate of tolls, is too remote and incidental to make it a tax on the business transacted." 11

Obviously, this language is applicable, and indeed conclusive, with respect to the situation in the Michigan case. However, the very language which has been quoted is an admission that such a tax does to some degree burden interstate, or foreign, commerce, as the case may be. Presumably, the tax must be paid out of tolls collected for passage over the bridge, and therefore, in theory, such tolls would be lessened if the state were precluded from collecting the tax. A sardonic, but probably accurate, answer to this argument would be that the tolls are put at all the traffic will bear, and would not actually be reduced if the tax were not collected from the owner of the bridge. Be that as it may, these cases are sufficient proof that the Court is continuing its previous very wise practice in dealing with this problem. Often, it purports to decide the case before it by relying upon some technical distinction (as in this case, between a facility of commerce and the commerce itself), but in the last analysis, the problem is not whether or not the state tax theoretically, or even actually, burdens such commerce (for it nearly always does), but whether such burden is really substantial.

This consideration is made even more explicit in the case of Liggett v. Lee, 12 which upset a chain store tax imposed by the state of Florida upon grounds not here applicable. The Court, however, refused to accept the taxpayer's argument that the chain-store tax was necessarily invalid, as a burden upon interstate commerce, merely because more chain store dealers buy from wholesalers from outside the state than do individual dealers. The answer was made that, assuming the truth of this statement, there was no intentional discrimination by the state against interstate commerce, and that the burden was trifling. 13

Growing out of the problem of taxing directly or indirectly the facilities of interstate commerce, is the problem of taxing such property as railroad cars and similar assets which actually move in interstate commerce. In one sense, these are mere facilities of such commerce, but their relationship to the com-

11 Id. at 153.
12 288 U. S. 517 (1933).
13 Id. at 538-539.
merce actually carried on is obviously much closer than a mere right of way.

The Court, by its decision in Johnson Oil Refining Co. v. Oklahoma, adhered to its opinion many times previously reiterated, that cars may be taxed by a state where they are, even though their usual, or perhaps, sole use is in interstate commerce. Here the plaintiff, an Illinois corporation, had an oil refinery in Oklahoma at which all its tank cars were loaded and to which empties were returned. The cars were used in interstate commerce, and each car was in Oklahoma only a small part of the time. The chief problem was as to the extent of the tax, which was limited by the Court to the average number of cars in Oklahoma during the year; but the Court, nevertheless, refused to accept the taxpayer's argument that the cars were wholly exempt from tax, on the ground that they were used exclusively in interstate commerce. The Court, speaking by Mr. Chief Justice Hughes, said as to this:

"The basis of the jurisdiction is the habitual employment of the property within the State. By virtue of that employment the property should bear its fair share of the burdens of taxation to which other property within the State is subject." 16

Here again we have the Court sustaining a state tax which is a burden on interstate commerce—strictly limited, to be sure, but a burden nevertheless. And in Virginia v. Imperial Coal Sales Co., the Court applied the same principle to intangible property within the state, but shown to be used solely in interstate commerce, because the owner's activities were exclusively such commerce.

The next step is a consideration of the power of the states to tax property which is, or at least alleged to be, not merely moving in interstate commerce, but actually the subject thereof. As to this problem, probably the most important case in this period is Minnesota v. Blasius. 18

14 290 U. S. 158 (1933).
16 290 U. S. 158, 162 (1933).
17 293 U. S. 15 (1934).
18 290 U. S. 1 (1933).
In this case the plaintiff was a trader in live stock in Minnesota. On the tax day, he had there cattle which had been shipped from outside Minnesota, and which he expected to sell and ship outside the state, as he, in fact, actually did later. The cattle were subjected to local property taxation in Minnesota, and the Court held that this was proper.

The chief argument which the plaintiff had in this case was that cattle so handled were within the "stream of commerce" and therefore subject to federal regulation for purposes of anti-trust activities and for protecting agriculture. On this basis, he argued that the cattle must be considered to be the subjects of existing interstate commerce, and, therefore, immune from taxation by the states. However, the Court had already held that cattle thus in the "stream of interstate commerce" may, nevertheless, be subjected to non-discriminatory property taxation by the states. And in this case it adhered to the same view, stating very expressly:

"But because there is a flow of interstate commerce which is subject to the regulating power of the Congress, it does not necessarily follow that, in the absence of a conflict with the exercise of that power, a State may not lay a non-discriminatory tax upon property which, although connected with that flow as a general course of business, has come to rest and has acquired a situs within the State."

The same doctrine was applied in Federal Compress Co. v. McLean. Here the basis of the state tax was cotton which was in the hands of the plaintiff company for the purpose of compressing and forwarding it by railway to other states. The plaintiff had been expressly designated as the railway agent for this purpose. The tax was not strictly a property tax, but was a license tax measured by the amount of property. The Court recognized, however, that the tax burdened the property, but held that such property was within the taxing power of the state, though it was being held by the plaintiff solely for the purpose of being shipped in interstate commerce. In fact, the case was

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21290 U. S. 1, 8 (1933).

somewhat easier than *Minnesota v. Blasius*,\(^{23}\) because the cotton had been grown in the same state and as yet had not entered interstate commerce.\(^{24}\) But here, too, there is a burden upon interstate commerce, but one which is not merely non-discriminatory but also not really very heavy.

Another form of state taxation affecting interstate commerce is a tax upon the use of commodities within the state, even though such commodities have been produced outside the state and, therefore, brought within it by some form of interstate commerce, and even though they are actually used exclusively in carrying on interstate commerce. Here, too, the federal courts generally sustain the tax, in the absence of substantial discrimination.

This principle, while applied to various commodities,\(^{25}\) has its most frequent application with respect to gasoline. As to this, probably the leading case during this period was *Nashville, Chattanooga & St. Louis Ry. Co. v. Wallace*.\(^{26}\) The plaintiff railroad company was engaged mainly in interstate commerce and, therefore, objected to an excise tax imposed by Tennessee upon the use of gasoline within the state, measured by the amount so used. The argument was that while the use was in Tennessee, yet that was only a step in interstate commerce, and that, accordingly, such commerce was burdened. The Court rather clearly admitted the theoretical soundness of this argument, but sustained the tax as a matter of degree, stating that the burden, while existing, is not direct or heavy. It said:

"But interstate rail carriers are not wholly immune from other forms of non-discriminatory state taxation, even though the burden of the tax is thus indirectly or incidentally imposed upon the interstate commerce in which they are engaged. It cannot be doubted that, when the gasoline came to rest in storage, the state was as free to tax it, notwithstanding its prospective use as an instrument of interstate commerce, as it was to tax appellant's right of way, rolling

\(^{23}\) 290 U. S. 1 (1933).

\(^{24}\) See *Coe v. Errol*, 116 U. S. 517 (1886).

\(^{25}\) Thus, a state tax on the sale of oleomargarine was sustained in *Magnano Co. v. Hamilton*, 292 U. S. 40 (1934). In applying the tax, no regard was paid to whether or not the oleomargarine was manufactured in the state.

\(^{26}\) 288 U. S. 249 (1933).
A similar Wyoming statute was upheld, and upon similar reasoning, in *Edelman v. Boeing Air Transport,* the tax here being applied to gasoline used in aeroplanes flown exclusively in interstate commerce. And the same result was reached with reference to a Louisiana statute of the same nature, and applied in a similar manner.

The Iowa tax sustained in *Monamotor Oil Co. v. Johnson,* was very similar in substance, though somewhat different in form. Here, all gasoline brought into the state was subjected to the tax, but a refund was given of that part of the gasoline sent out of the state. The Court, speaking through Mr. Justice Roberts, reached the sensible conclusion that the practical result of this scheme was to tax only that gasoline used in the state, and that the tax could, therefore, be sustained upon the same reasoning that has already been summarized.

Gasoline taxes have been traditionally imposed as compensation for the use of the roads by motor carriers. As has already appeared, however, they may be sustained even though the user of gasoline does not use the roads, as in the case of aeroplanes. However, it still remains true that the states may exact a tax from persons using the road, though in interstate commerce, providing the tax is at least roughly proportionate to their use of the roads.

On this point, the leading case during the period under consideration is *Hicklin v. Coney.* Here, a South Carolina tax

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27 Id. at 267. It should be noted that this same Tennessee tax had already been before the Court in an appeal from the decision in American Airways, Inc. *v. Wallace,* 57 F. (2d) 887 (M. D. Tenn. 1932), which upheld the tax. The Supreme Court affirmed the decision without opinion, 287 U. S. 565 (1932).

28 289 U. S. 249 (1933).


31 292 U. S. 86 (1934).

32 To tax gasoline not produced or used in the state would be an unconstitutional burden upon interstate commerce. *Helson v. Kentucky,* 279 U. S. 245 (1929).


34 290 U. S. 169 (1933).
imposed on carriers by motor vehicle was upheld, even though the plaintiff was engaged solely in interstate commerce. The tax was graduated, and based upon the "carrying capacity" of the vehicles. The tax was spent exclusively for the construction and maintenance of roads, which the plaintiff used, though with no settled route.

The chief difficulty of the Court, however, was to distinguish this case from *Interstate Transit, Inc. v. Lindsey*, where the Court had invalidated a Tennessee tax upon interstate motor busses, upon the ground that it was not reasonably proportioned to the use of the roads and was, therefore, an improper burden upon interstate commerce. The Tennessee tax was graduated and based upon carrying capacity—the same basis as the South Carolina tax now upheld. The Court, however, distinguished the cases upon the ground that the South Carolina tax was used exclusively for roads, whereas the Tennessee tax was not.

It is submitted that this distinction will not do. It can hardly be said that a state must use all of the taxes which it exacts for the use of its roads, upon the roads. The real question is whether the tax is reasonably proportioned to the use made of the roads. No doubt the use of the tax money by the state has some evidentiary bearing upon the subject, but it is not conclusive. The truth seems to be that the test of carrying capacity usually has a reasonable relation to the use of the roads, particularly where the taxpayer does not follow a prescribed route. It is probable, therefore, that this case really overrules *Interstate Transit, Inc. v. Lindsey*, at least on this particular point.

A similar, but somewhat less important, case is *Aero Mayflower Transit Co. v. Georgia*, where a state tax on private carriers of $25 for each vehicle was upheld as applied to a carrier engaged solely in interstate commerce. Here, too, the entire tax was to go to the road fund. The plaintiff claimed that interstate commerce was discriminated against because, as he alleged, local carriers use the roads in the state more than interstate carriers. The Court's answer was that there was no real discrimination in fact, as the question of how much the plaintiff used the roads was a matter solely in its own discretion.

35 283 U. S. 183 (1931).
36 See Note (1933) 42 *Yale L. J.* 402 (*State Taxation of Motor Vehicles Engaged in Interstate Commerce*).
As already pointed out, even a corporation tax imposed upon a corporation engaged in interstate commerce does, to a greater or less degree, burden such commerce. Usually, the burden is too slight or indirect to result in the invalidation of the tax. But in the important case of Anglo-Chilean Corp. v. Alabama, a state tax was invalidated upon this ground.

The plaintiff was a New York corporation engaged in importing nitrate into Alabama, the nitrate being sold only in original packages. The plaintiff had secured permission to do business in Alabama, but in fact did no other business than that already stated. It was held not subject to an Alabama tax on the capital of foreign corporations employed in Alabama, on the ground that it was doing no intrastate business in Alabama, but was engaged only in foreign commerce. The opinion, by Mr. Justice Butler, relied upon certain previous decisions of the Court, to the effect that a state has no power to tax a foreign corporation whose only activities within the state are in interstate commerce, or directly connected therewith. The first decision in the Detroit International Bridge Company case was distinguished on the ground that the Alabama statute confined the tax to cases where business was actually done.

While the cases already cited do justify the result in this case, the decision is not very satisfactory. In all these cases, the measure of the tax is concededly valid, and the tax could probably be sustained in full if the corporation performed any activity in the state apart from interstate or foreign commerce, no matter how trifling. Furthermore, the tax is not discriminatory and does not impose a substantially greater burden upon such commerce than would be the case if some such slight amount of intrastate commerce were carried on. Accordingly, the dissenting opinion of Mr. Justice Cardozo (concurred in by Mr. Justices Brandeis and Stone) seems more desirable. His reliance upon the fact that the corporation had power to do intrastate business, while perhaps somewhat technical, seems substantially justifiable. This point is made explicit in the following language in this dissenting opinion:

38 288 U. S. 218 (1933).
40 287 U. S. 295 (1932). The later decision in this case, cited in note 9, supra, had not yet been rendered.
41 Notes 39 and 40, supra.
"Moreover, what was done under the franchise one day might not be done under it the next. Another franchise tax would not be owing for a year. In the meantime the appellant might transact its business as it pleased. If some of its sales, however few and trifling, had been made in broken packages, there would be no denial by any one that the privilege of making them would be subject to taxation by one measure or another. This court has never held that the measure in such circumstances would be arbitrary and unlawful because determined by the value of all the local capital, and not merely the proportion necessary for sales in broken lots." 42

This line of cases, unfortunately, departs from the realistic test which the Court had ordinarily applied in this problem of state taxation of interstate commerce. In most of these commerce cases the Court explicitly, or at least impliedly, uses the test of substantial burden rather than theoretical burden. There is no more real justification for using the extreme doctrinal test in this class of cases than in others, and it is to be hoped that the Court will abandon its attempt to do so.

The folly of attempting to adhere to the doctrinal test is made the more evident by the fact that the Court is compelled to admit explicitly in many cases that there is always a burden upon interstate commerce if the taxpayer is at all engaged in such commerce, and that the problem is, therefore, one of degree; that the burden cannot be entirely avoided, though it must not be permitted to be too heavy. 43 Even an apparent discrimination against interstate commerce may not invalidate a state tax if, on analysis, the discrimination substantially disappears in fact. This is made clear in State v. Wilson & Co. 44 a case coming up from the Supreme Court of Louisiana, where the Federal Supreme Court dismissed the appeal without opinion "for want of a substantial federal question." The state imposed a 1½% per cent tax on gross sales of meat and a much lower tax on slaughtering of animals in Louisiana. The apparent joker was that the payment of the slaughtering tax exempted the taxpayer from the payment of the higher gross sales tax. The defendant claimed that the gross sales tax was, on its face, a discrimination against interstate commerce, since sales in Louisiana would unquestionably in part result in interstate commerce, whereas

42 238 U. S. 218, 235 (1933).
43 See Minnesota v. Blaisius, 290 U. S. 1 (1933).
44 179 La. 648, 154 So. 636 (1934), appeal dismissed, 293 U. S. 518 (1934).
the slaughtering would, of course, take place entirely within the state. The state court admitted that the tax was discriminatory on its face, but held that it could be sustained by construing it so that the wholesale dealer always had to pay the tax on gross sales. The lower tax on slaughtering was thus confined to one who slaughtered but did not wholesale. The result was that anyone who engaged in interstate commerce would have to pay the higher tax whether or not he engaged in slaughtering in Louisiana; therefore, there could be no discrimination against interstate commerce. As already stated, the Federal Supreme Court accepted this view without deeming it necessary to write a further opinion.

Another important case where a state tax concededly affecting interstate commerce was, nevertheless, sustained, is *Wiiol Corp. v. Pennsylvania.* The taxpayer was a wholesale distributor of liquid fuels in Pennsylvania. It ordered fuel from Delaware which was to be delivered to purchasers at Philadelphia or Essington, Pennsylvania. The price included the Pennsylvania tax on the use or sale of liquid fuels. In this litigation, testing the validity of the tax on these shipments, the state court held that the sale took place in Pennsylvania, and the taxpayer did not dispute this. The state court, therefore, held the sales subject to the Pennsylvania tax, and the Federal Supreme Court affirmed this decision. The opinion, by Mr. Justice Butler, pointed out that there was no discrimination against interstate commerce by the tax, and furthermore, that, so far as the purchaser was concerned, no interstate commerce was required, as the fuel could have been obtained from Pennsylvania sources. It was further held to be immaterial that the products were delivered in tank cars, which constitute original packages. The following language from the opinion of the Court makes especially clear that the whole problem, at least disregarding the question of actual discrimination, is a matter of degree:

“Our decisions show that, if goods carried from one State have reached destination in another where they are held in original packages for sale, the latter has power without discrimination to tax them as it does other property within its jurisdiction.”

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47 *Id.* at 175.
On the other hand, *Cooney v. Mountain States Telephone & Telegraph Co.* holds invalid a state tax on a flat amount on each telephone in the state, the tax being payable by the telephone company. The ground for this decision is that the tax necessarily burdens interstate commerce to the degree that such commerce is carried on by the use of such telephones. The tax was called by the statute, an "occupation tax," and the Court held that it could be sustained as such, so far as intrastate business was concerned. However, the tax "being indivisible and indiscriminate in its application, necessarily burdens interstate commerce." It might be said that this is not an excessive tax, even with respect to the intrastate business; but the answer is that it must necessarily burden the interstate business, because intrastate and interstate business are inseparable. The remedy of the state is to impose another form of taxation (for example, on the gross receipts of the telephone company)—which will permit some division upon the intrastate and interstate business. The ruling may seem harsh with respect to the state, but permission to tax in this manner would enable the states to burden interstate commerce almost without limit.

This review of the interstate commerce tax cases during this period demonstrates that the Court has, in general, adhered to the principles which it has previously applied, and has perhaps made those principles even more explicit. These principles are that the states may not by taxation discriminate against interstate commerce, nor substantially burden it; but that a state tax will not be invalidated merely because, like practically any conceivable state tax, it may possibly affect interstate commerce. Only with respect to corporate taxes upon foreign corporations carrying on solely interstate activities within the state has any substantial departure from these general principles been recognized in the last three years. It is to be hoped that this unfortunate doctrine will be brought to an end, or at least so minimized as to avoid its present effect in unjustly precluding state taxation in that situation. On the whole, however, the Court has, in general, reached a position in this whole matter which is both logically defensible and practically desirable.

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49 Id. at 394.
The Intergovernmental Cases

In the cases involving state and federal taxation which is alleged to burden improperly the activities of the other member of our dual system, the test has been said to be somewhat stricter.\(^5\) Perhaps that is the case; nevertheless, the history of the past three years has shown a definite tendency toward applying the same practical test as has appeared in the inter-state commerce cases. In general, the Court has in the intergovernmental cases repudiated in fact, if not always in word, the test of doctrinal immunity; the test is, as it ought to be, one of practical burden.

It may be said in the first place that no matter how great the right of the Federal Government to immunity from state taxation on its functions, such immunity may not only be given up (at least with some limitations) but is also at least partly dependent upon Congressional assertion of such immunity. The Court has recently said that:

"Immunity of corporate government agencies from suit and judicial process, and their incidents, is less readily implied than immunity from taxation."\(^5\)

But it is still true that such tax immunity can only result from Congressional action, express or implied.

Thus, in *Trotter v. Tennessee*,\(^5\) it was held that a federal statute, exempting moneys paid to war veterans by the United States from state taxation, did not exempt real estate purchased with such money. The Court, in an opinion by Mr. Justice Cardozo, intimates that Congress could insist upon this further exemption, but clearly holds that it has not, in fact, done so. And, in *Gillis v. California*,\(^5\) this idea was carried so far as to hold that an oil company receiver appointed by a federal court must comply with a law of Congress requiring the giving of a bond to the state to insure the payment of state gasoline taxes. In this case it appeared that the receiver was unable to give the bond, but the Court only said that, if so, he must give up the

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\(^5\) 290 U. S. 354 (1933).

\(^5\) 293 U. S. 62 (1934).
business. The Court admitted that the effect of the Congressional Act was substantially to give priority to the state tax, but stated that this was within the power of Congress.

On the other hand, it was held that California could not tax sales of gasoline to the Post Exchange at the Presidio at San Francisco. Here the Court found that the state had ceded this property absolutely (with the exception of service of state process) to the United States, and had, therefore, precluded itself from imposing any tax upon, or with respect to, activities within the boundaries of the property.

Though authorities on the point seem to be lacking, at least during this period, the same general rules would seem to apply to the necessity of state action in asserting, or perhaps explicitly giving up, immunity from federal taxation upon its agencies. In either case, however, it would seem that an intention to assert all the tax immunity possible would usually be a reasonable and fair implication, in the absence of express language to the contrary.

However, there is at least one situation where the tax immunity does not seem to be reciprocal. This is, that state activities not regarded by the Court as carrying on a strictly governmental function, are not exempt from federal taxation, no matter how direct is the state action in question. This principle, first applied to a state liquor business many years ago in South Carolina v. United States, was reiterated during this period as to the same activity in Ohio v. Helvering. The Court, speaking through Mr. Justice Sutherland, said:

“If a state chooses to go into the business of buying and selling commodities, its right to do so may be conceded so far as the Federal Constitution is concerned; but the exercise of the right is not the performance of a governmental function, and must find its support in some authority apart from the police power. When a state enters the market place seeking customers it divests itself of its quasi sovereignty pro tanto, and takes on the character of a trader, so far, at least, as the taxing power of the federal government is concerned.”

This is all very well; and it must be conceded that state socialism might, if state immunity from taxation was literally

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56 199 U. S. 437 (1905).
57 292 U. S. 360 (1934).
58 Id. at 369.
applied, result in no scope being left for the federal taxing power.\textsuperscript{59} Still, it seems that the argument is not altogether applicable in this situation. It is absurd to contend that a state government which carries on the liquor business is doing so exclusively for reasons of revenue. One obvious and important purpose is to regulate and limit the business, exactly as private liquor business is regulated, in the interest of public health, order, and good morals. The bland assumption of the Court that immunity in this case means logically the possibility of total immunity of all activities within the state from federal taxation is subject not only to the criticism that it is another application of the well-known "parade of imaginary horribles," but also that it is not even applicable, in that such regulation is not a real step toward state socialism.

Furthermore, if this is a justifiable restriction upon state immunity from federal taxation, it would seem that the rule would work both ways, and that the states would be entitled to tax federal activities not strictly governmental. As yet, however, the federal officials have absolutely denied such state power of taxation, even in activities having far less connection with traditional governmental functions than liquor regulation. So far as judicial decision upon this point is concerned, however, it seems entirely in the future, at least so far as the Supreme Court is concerned.

However, in adhering to this doctrine, the Court held in \textit{Helvering v. Powers} \textsuperscript{60} that the compensation of the trustees of the Boston Elevated Railway was subject to federal income tax, even though the state (Massachusetts) had taken over the operation of the railroad, and the trustees were concededly state officers. The Court, relying upon the cases already cited in this connection, holds that the state itself would have been directly taxable on such income and therefore had no difficulty in holding that the plaintiffs, as trustees, were taxable.

Some slight, but very slight, weakening of this concept appears in \textit{A. Magnano Co. v. Hamilton},\textsuperscript{61} where, however, the state did not carry on the activity in question (the manufacture and sale of oleomargarine) but rather taxed it. The Court held

\textsuperscript{59} This idea is emphasized in \textit{South Carolina v. United States}, 199 U. S. 437 (1905).
\textsuperscript{60} 293 U. S. 214 (1934).
\textsuperscript{61} 292 U. S. 40 (1934).
that such a tax did not unconstitutionally interfere with the taxing power of the United States, merely because it was intended to, and might actually wipe out the oleomargarine industry in the state, and thereby eliminate that source of federal taxation. The truth seems to be that this alleged tax, being intended as prohibitive, is actually an exercise of the police power of a state rather than a taxing power.

Another limitation on intergovernmental immunity from taxation, and one which seems to be applied reciprocally, is the refusal to exempt a mere independent contractor. Thus, a tax by Louisiana on the use of gasoline in the state was sustained, even as applied to a contractor with the Federal Government who used the gasoline exclusively in carrying out that contract, for the construction of levees. The opinion, by Mr. Justice Butler, lays much stress upon the rigidity of intergovernmental immunity from taxation, saying:

"The appellant seeks reversal on the ground that the contracts are federal means or instrumentalities, that the enactments referred to impose a direct burden upon them and that the State was without power to impose the tax. And on that basis it seeks to invoke the rule that, consistently with the Federal Constitution, a State may not tax the operations of an instrument employed by the government of the Union to carry its powers into operation. That principle, while not expressly stated in the Constitution, necessarily arises out of our dual government. It has often been given effect. And reciprocally it safeguards every State against federal tax on its governmental agencies or operations. Its application does not depend upon the amount of the exaction, the weight of the burden or the extent of the resulting interference with sovereign independence. Where it applies, the principle is an absolute one wholly unaffected by matters or distinctions of degree. Indian Motorcycle Co. v. United States, 283 U. S. 570, 575, and cases cited. Its right application is essential to the orderly conduct of the national and the state governments and the attainment of justice as between them."}

But all this roaring quickly becomes as gentle as a sucking dove when the Court actually goes on to hold that the burden upon the Federal Government is too remote to justify immunity. This idea is buttressed by pointing out that the machinery itself could concededly be taxed by the state. This is all true, and it is good sense. Nevertheless, the result is a denial of that doc-

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63 Id. at 470-471.
trinal immunity which the Court so strenuously and vociferously (but only verbally) asserts in the above question.

This doctrine that an independent contractor with the United States normally is not exempt from state taxation (and presumably *vice versa*) is reiterated in several cases coming up from state or federal district courts sitting locally, which the Supreme Court affirmed without opinion. The most interesting and important of these cases is *Tirrell v. Johnston*, coming up from the Supreme Court of New Hampshire. The opinion in the state court was extremely long, elaborate and carefully reasoned, reaching the conclusion that a rural mail carrier, paid by the government at so much a mile, is subject to New Hampshire gasoline tax for gasoline thus used by him in his car. The opinion first argues at some length that this tax is not a tax but a payment for services rendered. This does not seem very convincing, and the court largely abandons it in connection with the second argument, which is much more forceful. This argument assumes that this exaction is a tax, but contends that it is still a question of degree, and that there is no direct or substantial burden on the Federal Government. It is explicitly pointed out that the government pays the man just so much, irrespective of how much tax he pays to the state.

It might be answered that the government could supposedly reduce its payment to the carrier if he were immune from state taxation. Indeed, this is the only method of sustaining *Panhandle Oil Co. v. Knox*, where the Court, several years ago, held that sales of gasoline made by the plaintiff to the United States for use of the Coast Guard and a Veterans' Hospital, were immune from state taxation. This was a five to four decision, and the dissenting opinion of Mr. Justice Holmes has acquired a lasting fame from his rather curt remark that "The power to tax is not the power to destroy, while this Court sits."  

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65 86 N. H. 530, 171 Atl. 641 (1934), *aff'd without opinion*, 293 U. S. 533 (1934).

66 277 U. S. 218 (1928).

67 Id. at 223.
Of course such purchasers are rather more direct federal agencies than in the New Hampshire case, but the actual burden on the Federal Government is hardly greater, or more direct. The New Hampshire court in its opinion criticized the Panhandle Oil case, and says that it thinks the doctrine of that case should not be extended. It seems difficult to reconcile these cases on any realistic basis, and, in affirming the New Hampshire court without opinion, the Supreme Court seems, in fact, to have overruled the Panhandle Oil case. At any rate, the doctrine of Tirrell v. Johnston seems much more desirable.

Even more clearly should such tax immunity be absolutely denied where the taxpayer's activities, while carried on under a license of the state or Federal Government, as the case may be, is yet primarily for his own private advantage. This proposition, already clearly enunciated in previous cases, was reiterated, during the period now under consideration, in Broad River Power Co. v. Query. Here the plaintiff was subject to a South Carolina excise tax on the generation of electricity by water power. The plaintiff claimed immunity, on the ground that it was acting under a license of the Federal Power Commission. The Court held, however, that the plaintiff was acting for its own benefit, and not as an agent of the United States. Accordingly, the state tax was unobjectionable. The same result was reached in Federal Compress Co. v. McLean, where the taxpayer was carrying on its business of compressing and forwarding cotton under a federal license. This, too, was held not to give any immunity from state taxation.

Another prolific cause of litigation of this general scope is state taxation of national banks. It is clear that such banks are agencies of the Federal Government, and that as such they are immune from state taxation, except to the extent that such taxation is permitted by Congress. However, the Congressional statute, withdrawing in part such immunity, and thereby subjecting the banks to state taxation, has in recent years been much broadened. But such state taxation is still definitely limited.

69 288 U. S. 178 (1933).
70 291 U. S. 17 (1934).
71 McCulloch v. Maryland, 4 Wheat. 316 (1819).
In *Domenech v. National City Bank*, it was held that this statute limited the power of a territory (Puerto Rico) to tax the branch of a national bank in that territory; that the taxing power of a territory was limited exactly the same as that of a state. The Court, speaking by Mr. Justice Roberts, said:

"Puerto Rico, an island possession, like a territory, is an agency of the federal government, having no independent sovereignty comparable to that of a state in virtue of which taxes may be levied. Authority to tax must be derived from the United States. But like a state, though for a different reason, such an agency may not tax a federal instrumentality. A state, though a sovereign, is precluded from so doing because the Constitution requires that there be no interference by a state with the powers granted to the federal government. A territory or a possession may not do so because the dependency may not tax its sovereign. True the Congress may consent to such taxation; but the grant to the Island of a general power to tax should not be construed as a consent. Nothing less than act of Congress clearly and explicitly conferring the privilege will suffice. Not only do we find no such statutory consent but we are confronted by R. S. 5219, which *proprio vigore* extends to territories, and the Congressional declaration that it, like other statutes of the United States shall, if not locally inapplicable, apply to Puerto Rico."  

While it is well-settled that the states may not discriminate against national banks by taxing them at a higher rate than other capital actually competing with the national banks is taxed, the Court has recently reiterated the proposition that a state tax will not be invalidated upon this ground unless actual competition is shown, and to a substantial amount. The mere power of a national bank to go into activities carried on by more lightly taxed capital does not invalidate the tax on the bank, unless it is shown that the bank actually exercises this power.

On the other hand, the strict prohibition against the states' discrimination against national banks may result in the necessity of discrimination in their favor. This is shown by *Union Bank & Trust Co. v. Phelps*. Here the plaintiff was a state bank of deposit. It was subjected to a tax on its stock, which was not imposed on various other state financial institutions which substantially competed with it. The state statute imposing the tax

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74 Id. at 204-205.
77 288 U. S. 181 (1933).
purported to tax national bank stock in the same way; but this provision was stricken out as contrary to the Federal Constitution by the state supreme court, and the state authorities acquiesced, thus, in practice, exempting national banks entirely from this tax. On appeal to the Federal Supreme Court, it was held that the plaintiff had no grounds for complaint. The Court said that the discrimination as regards other state institutions may have been justified, because of the circumstances, and certainly was not shown to violate the Fourteenth Amendment. More important for our purposes, the Court held that the discrimination with respect to national banks was actually compulsory. The Court, speaking of national banks, said:

"Such instrumentalities are exempted from state taxation without the express consent of Congress, by the Federal Constitution. They are of a class wholly distinct from the property of ordinary corporations or individuals, and this fact cannot be disregarded by the State. If the State sees fit to tax unrestricted property within her jurisdiction and to omit National Bank shares, the classification cannot be said to be arbitrary and wholly unreasonable—the basis of it is plain enough. It may be vastly more important for the State to omit National Bank shares and tax ordinary moneyed capital according to a plan not permissible in respect of National Bank shares rather than conform to the standard prescribed by Congress. There is nothing to indicate that Congress ever supposed that mere establishment of a National Bank within a State could upset the scheme for taxation, therefore entirely proper, by producing conflict with the XIV Amendment. This view would subject the taxing power of the State to the will of Congress far beyond what is necessary for the protection of federal agencies. The constitutional inhibition against taxing these agencies does not abridge the taxing power of the several States in respect of other property. The implied exemption is a shield for federal agencies—not the source of congressional power to control State action in respect of other matters." 78

The situation with respect to national banks, then, is one which seems reasonably fair to the states; but if it is not, Congress alone can change the situation. As to state banking and other financial institutions, the situation may not be so fair; but here again the Court is helpless. If there is any substantial unfairness, only Congress can cure it, for it is clear that the states may not tax national banks at all, except under, and to the extent of, express Congressional permission.

78 Id. at 187.
With respect to state taxation affecting Indians, the situation may not be quite the same, because of the imperative necessity of careful federal protection of the Indians against probably unfriendly local activities. As to federal taxation of the Indians and their property (which, of course, does not really affect intergovernmental relations), there would seem to be a moral obligation at least to limit such taxation, but certainly there is no legal obligation which the courts can enforce. Thus, it was recently held that income from investments of funds received from Indian lands is subject to federal income tax. In fact, there seems no reason why the Indians should have as complete immunity from taxation as they claimed in that case; at any rate the Court has sustained practically complete subjection of the Indians to federal income tax.

With respect to state taxation, the only case found during this period is *Indian Territory Oil Co. v. Board.* Here it was held that the State of Oklahoma could impose a property tax on oil produced on restricted Indian lands on which the royalty to the Indian owners had been paid. The principal difficulty in reaching this result was the previous decision in *Jaybird Mining Co. v. Weir,* where it was held that ore taken from restricted Indian property, under the terms of a governmental lease, was not subject to the ordinary state property tax so long as in the hands of the lessee. This case was distinguished from the *Indian Territory Oil Co. case* on the ground that the Indian superintendent had actually been paid, so that there was no possible burden upon the United States. The Court said in the latter case:

"Such immunity as petitioner enjoyed as a governmental instrumentality inhered in its operations as such, and being for the protection of the Government in its function extended no farther than was necessary for that purpose."
It is submitted, however, that the case represents at least a step in the opposite direction from the *Weir case*,\(^5\) which should probably be overruled, on the ground that the burden upon the United States, as regards its Indian wards, is too theoretical and, at any rate, unsubstantial to justify a complete denial of the state power to tax.

Another case involving leases, but this time a state lease—as affecting federal taxes, was decided during this period. This case was *Burnet v. A. T. Jergins Trust*\(^6\). The case arose as follows: Oil was discovered on land owned by the City of Long Beach, California, and used by it for its water supply. The petitioner secured an oil lease on the land, the oil to be sold by it and the city jointly. The profits were to be shared, sixty per cent to the petitioner and forty per cent to the city. The former claimed immunity from federal income tax upon its share of the proceeds, but this claim was denied by the Court. Much of the argument of counsel seems to have been as to whether the supplying of water is a governmental or a private function of the city, but the Court does not decide this. Its conclusion is predicated upon the very sensible ground that there cannot be any real burden upon the city, since the city got its share of the profits, no matter what taxes had to be paid by the petitioner on its share. Still, it cannot be denied that there was at least a theoretical burden upon the city, but the Court properly holds that this is immaterial.

In *New York ex rel. Northern Finance Co. v. Lynch*,\(^7\) the Court, without opinion, sustained a New York franchise tax measured by corporate net income which included interest from United States bonds and dividends from national banks. The decision is clearly contrary to the famous—or perhaps notorious—case of *Macallen Co. v. Massachusetts*,\(^8\) holding that a state may not compel a corporation to pay an income tax upon that part of its income derived from United States bonds and Federal Farm Loan bonds held by it. However, the *Macallen case* had already been substantially overruled in a decision previous

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\(^5\) 271 U. S. 609 (1926).
\(^6\) 288 U. S. 508 (1933).
\(^7\) 262 N. Y. 477, 188 N. E. 27 (1933), (memorandum), *aff'd without opinion*, 290 U. S. 601 (1933).
\(^8\) 279 U. S. 620 (1929).
to the period under consideration. The *Northern Finance Company* case is, therefore, only another spadeful of earth thrown upon the grave of the *Macallen case*. It is to be hoped that the Court will soon entirely close the grave by explicitly overruling that most unfortunate decision.

Only one other case on this topic remains for discussion; but this is perhaps the most significant of all. It is *Board of Trustees of the University of Illinois v. United States*. The facts of the case were that the University of Illinois imported certain scientific apparatus for use in its laboratories, both for teaching and for research purposes. Upon this importation, a duty was exacted, against the protests of the University authorities. Suit was subsequently brought by the University to recover the amount of the tariff which it had thus been compelled to pay.

It would seem, at least at first glance, that this is nearly an open-and-shut case of where the tax was improper. There was a direct burden upon a corporate agency of the state carried on exclusively for educational purposes. No one would seriously contend that education is not a governmental function of a state; indeed, the Supreme Court did not attempt to rely upon any such absurd proposition as this. And yet the Court upheld the collection of the tariff, upon the somewhat surprising ground that the tariff is a regulation of foreign commerce, and not a tax.

Two excerpts from the opinion, written for a unanimous Court by Mr. Chief Justice Hughes, will make sufficiently clear the principle upon which it proceeded. These are as follows:

"The principle of duality in our system of government does not touch the authority of the Congress in the regulation of foreign commerce," 81

"The principle invoked by the petitioner, of the immunity of state instrumentalities from federal taxation, has its inherent limitations. *Fox Film Corp. v. Doyal*, 286 U. S. 123, 128. It is a principle implied from the necessity of maintaining our dual system of government. . . . Springing from that necessity it does not extend beyond it. Protecting the functions of government in its proper province, the implica-

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81 *Id.* at 57.
tion ceases when the boundary of that province is reached. The fact that the State in the performance of state functions may use imported articles does not mean that the importation is a function of the state government independent of federal power. The control of importation does not rest with the State but with the Congress. In international relations and with respect to foreign intercourse and trade the people of the United States act through a single government with unified and adequate national power. There is thus no violation of the principle which petitioner invokes, for there is no encroachment on the power of the State as none exists with respect to the subject over which the federal power has been exerted." 92

From one point of view this is a distinctly realistic decision. Everyone knows that the chief, though undoubtedly not the sole, purpose of our tariffs is not to raise revenue but to protect our supposedly weak infant industries. This fundamental purpose, it may well be said, cannot be permitted to be interfered with even for the benefit of strictly governmental activities of the states.

However, this argument may also lead to an absurdity, as has been pointed out by the counsel for the University in that case. 93 Accepting the doctrine of South Carolina v. United States, 94 and applying it to other state functions, what is to prevent the United States from completely taxing certain or all state functions out of existence under the guise of regulating foreign—or possibly even interstate—commerce? The case certainly does open up rather startling possibilities from this point of view.

It is improbable, however, that these results will be actually reached, at least within the very near future. The Court was chiefly thinking that the real purpose of tariffs is not to raise revenue, and that, therefore, a state should no more be permitted to evade tariffs than it would be permitted, say, to import explosives for its own use without complying with federal restrictions in the interest of public safety. As already said, the concept of the tariff as a non-revenue regulation of our foreign commercial relations has a certain basis of realism, though by no means completely so. If the case is to be supported, however, it seems that it can only rest upon that founda-

92 Id. at 59.
93 Sveinbjorn Johnson, Federal Taxation Affecting State Instrumentalities (1934) 68 U. S. L. Rev. 248, 261 et seq.
94 199 U. S. 437 (1905).
tion. As a tax case, it certainly permits the Federal Government to impose a direct and substantial, and therefore unjustified, burden upon an important governmental function of a state.

Conclusion

The past three years have shown a tendency with respect to these topics which, in general, is in accordance with, and to some extent even more distinct than, the previous authorities. With respect to interstate commerce, the Court has, in general, adhered to the sensible, though perhaps somewhat illogical, position which it has previously taken; namely, that a state tax is not to be invalidated merely because it affects interstate commerce, but rather that it is to be sustained unless it discriminates against such commerce or at least burdens it to a substantial degree. The only case decided during this period which seems difficult to reconcile with that general theory is Anglo-Chilean Corp. v. Alabama, which reiterated the unfortunate doctrine that a foreign corporation, authorized to do business in the state, but which confines its activities to interstate or foreign commerce, is entirely immune from any license tax by the state. Here is an application of the doctrinal immunity which the Court has otherwise not in fact adhered to.

With respect to taxation in intergovernmental relations, the same tendency is evident. No longer does the Court apparently make any appreciable distinction between interstate commerce and intergovernmental relations. In both situations, the test is the practical one of discrimination and substantial burden rather than the theoretical one of possible effect. Even direct tax burdens upon non-governmental activities are permitted, at least so far as the Federal Government is taxing state activities. In the University of Illinois case, indeed, a direct burden by the Federal Government upon a governmental activity of the state was permitted upon the somewhat dubious theory that the tariff is not a tax but a regulation of foreign commerce.

On the whole, however, the Court seems to be going in the right direction with respect to these problems. Interstate commerce is entitled to be protected from state taxation which is discriminatory or substantially burdensome; and both state gov-

95 288 U. S. 218 (1933).
96 289 U. S. 48 (1933).
ernments and the Federal Government are to be protected from the other side with respect to taxes which directly and substantially discriminate against, or substantially burden, their own necessary governmental activities. Beyond this, the Court ought not to go; for to do so means not protection of the nation and the states, but potential destruction of one, or both, of them. It seems that the Court has really seen and applied this principle, even though it sometimes talks as if it had not. The decisions, in general, take the intermediate position, which may be difficult to justify in logic, but which is not only practical but necessary if the states and nation are to continue to exist and operate separately.