The Tax Burden of the 1935 Supreme Court

Charles L. B. Lowndes
NOWHERE is the increasing importance of the law of Taxation better reflected than in the decisions of the United States Supreme Court. At the last term, the Court decided over sixty tax cases, if you exclude orders, petitions for certiorari and rehearings, and count as single opinions cases which were consolidated and disposed of together. The whole field of Taxation passed in review before the critical appraisal of the Court. Some decisions, of course, turned on petty points of evanescent interest, but there were a substantial number of “peak” cases which mark notable steps in the development of this field.

I  **LIMITATIONS ON THE POWER TO CONGRESS TO REGULATE INTRASTATE ACTIVITIES THROUGH ITS TAXING AND SPENDING POWERS**

The most dramatic development of the past term was the decision in *United States v. Butler*,¹ which held the Agricultural Adjustment Act unconstitutional. So much has been said about the *Butler* case that there is no occasion for extended comment here. From a technician's point of view, prescinding from its social and economic aspects, the decision is the first to lay down any definite limitation upon the spending power of the national legislature. Apparently it stands for the broad proposition that Congress cannot regulate intrastate matters through the use of the spending power. Of course that leaves open the really important questions of what are the intrastate matters which Congress cannot regulate and what is meant by regulation. Another intensely practical question which is not decided by the *Butler* case is whether it will be possible to raise judicially the question of an unconstitutional exertion of the federal spending power in a future situation, where the tax and the unconstitutional appropriation are not tied up as tightly as they were in the Agricultural Adjustment Act. It may or may not be significant that the Court in the *Butler* case did not overrule *Massachusetts v. Mellon*² but distinguished it with every evidence of sincere affection and respect.

The bearing of the *Butler* case upon the Social Security Act, the Soil Conservation program, and what remains of the so-called New Deal legislation is happily beyond the scope of this paper. The most pressing problem for the average tax practitioner is whether the processors are

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¹ Professor of Law, Duke University, School of Law.

going to be able to recover the taxes which were held to be unconstitutional in the Butler case, or whether the device of requiring them to prove that they neither passed on nor passed back the taxes as a condition precedent to refunds, will prove successful. The only case before the Court at the last term which might have shed some light on this question was completely neutral. Rickert Rice Mills, Inc. v. Fontenot,3 in which the Supreme Court granted a temporary restraining order against the collection of processing taxes and after the decision in the Butler case ordered the taxes impounded under this order to be returned to the processors,4 carefully refrained from passing upon the constitutionality of the procedure which requires the processors to prove absorption of the taxes as a condition precedent to their recovery. Several District Courts have held that this is constitutional.5 What the Supreme Court will say remains to be seen.

There is little doubt but that the Bankhead Act, which was a frankly coercive measure, was unconstitutional in the light of the decision in United States v. Butler. In Moor v. Texas & N. O. R. Co.,6 however, the Court refused to consider this question. Moor sued the railroad for a mandatory injunction to compel it to carry his cotton, on which he had not paid the taxes due under the Bankhead Act. The lower courts refused the injunction on the ground that he had not shown that he could not have paid the tax and then sued for a refund. The Supreme Court upheld their decisions on the ground that the plaintiff had made out no case for equitable intervention and escaped the constitutional issue.

As a matter of accurate analysis, it is important to distinguish an unconstitutional exertion of the taxing power from misuse of the spending power. United States v. Butler imposed a limitation upon the spending power. The processing taxes were held invalid not because they were not revenue raising measures, but because the proceeds of the taxes were expended in an effort to regulate agriculture. On the other hand, there were several decisions at the last term where federal taxes were held to be bad, not because the proceeds of the taxes were used to regulate in a field where Congress had no power to regulate, but because the taxes themselves were designed to coerce

4. Cf. Bailey v. George, 259 U. S. 16 (1922) which was decided the same day as the famous Child Labor Tax Case, Bailey v. Drexel, 259 U. S. 20 (1922). The Supreme Court held in Bailey v. George that the fact that a tax was unconstitutional did not justify granting injunctive relief, but the taxpayer must pay the tax and sue for a refund.
or repress conduct over which the Federal Government had no constitutional power of control. In *United States v. Constantine*\(^7\) and the companion case of *United States v. Kesterton*,\(^8\) for example, it was held that a federal excise of $1,000 upon dealers retailing liquor in dry states was a penalty and not a tax, and, since the repeal of the Eighteenth Amendment had taken from Congress its power over the liquor traffic, was unconstitutional. Although the tax on dealers in liquor in wet states was only $25, Mr. Justice Cardozo, who had the backing of Justices Brandeis and Stone, could see nothing on the face of the statute to show that this was a penalty, rather than a higher tax on an illegal occupation. According to Mr. Justice Cardozo, as a result of the majority opinion “the process of psychoanalysis has spread to unaccustomed fields,”—which is certainly not an encouraging prospect for the lawyer.

A somewhat similar situation arose in connection with *Carter v. Carter Coal Co.*,\(^9\) another of the New Deal cases which the government lost. The Bituminous Coal Conservation Act of 1935, or as it is popularly called the Guffey Act, provided for a tax of 15 per cent. on producers of bituminous coal with a drawback of 90 per cent. to producers who agreed to abide by a code regulating prices and conditions of labor. This was the bill which Mr. Roosevelt urged Congress to pass regardless of reasonable doubts as to its constitutionality. There must have been some justification for those doubts, because the Court held that the statute was unconstitutional. Although the Court divided on the point of whether the Federal Government could regulate prices and labor conditions in the bituminous coal industry, they were pretty well agreed that the tax provided for by the Act was not a tax but a penalty designed to enforce compliance with a code.

## II IMMUNITY OF INTERSTATE COMMERCE FROM STATE TAXATION

The immunity of interstate commerce from state taxation continued to provide a fertile field for litigation. At the last term there was the usual crop of cases involving the usual problems. For the most part the answers returned by the Supreme Court were the orthodox answers, but at least one group of decisions seems to indicate a rather radical deviation from past precedent.

*Pacific Telephone & Telegraph Co. v. Tax Commission of Washington;*\(^10\) *Great Northern Railway Co. v. Washington;*\(^11\) and *Northern Pacific Railway Co. v. Washington*\(^12\) were disposed of in a single opinion. *Great Northern Railway Co. v. Washington* will illustrate the problem

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10. 297 U. S. 403 (1936).
11. Ibid.
12. Ibid.
which was involved. The State of Washington imposed an occupation
tax of one and one-half per cent. upon the gross income of a railroad
which did both an interstate and an intrastate business. Although the
tax was a privilege tax for engaging in local business and was measured
exclusively by receipts from such operations, the intrastate business
was conducted at a loss, so that as a matter of fact, the tax was paid
out of the profits from the interstate operations. Since the Great
Northern was required by law as well as practical considerations to
continue the local service, it contended that the tax was unconstitutional.
With singular unanimity however, the Court concurred in an opinion
by Mr. Justice Brandeis, who held that the tax was constitutional.
Although he admitted that the tax came out of the profits of the in-
terstate business, Mr. Justice Brandeis denied that this burdened inter-
state commerce, since the tax would not "induce the company to with-
draw from the local business, even if it were permitted by law to do so." He
distinguished an earlier statement by Mr. Justice Brandeis in
Sprout v. City of South Bend\textsuperscript{13} to the effect that in order for a state license tax for doing local business to be valid "it must appear that . . .
the person taxed could discontinue the intrastate business without with-
drawing also from the interstate" on the ground that the tax in the Sprout
case "made no distinction between buses engaged exclusively in in-
terstate commerce, those engaged exclusively in intrastate commerce,
and those engaged in both classes of commerce." Nothing is more
dangerous than generalization from a case of this type. However, it
would appear that in the future it will be immaterial whether a taxpayer
engaged in both intrastate and interstate commerce is free legally and
factually to withdraw from the local business. A tax whose subject
is the privilege of doing local business, and whose measure is restricted
to gross receipts from such operations, would appear to be valid if the
tax is not so burdensome that the taxpayer would prefer to pay the tax
and continue the local service rather than relinquish intrastate operations
entirely.

Fisher's Blend Station, Inc. v. State Tax Commission\textsuperscript{14} involved a
novel application of old principles. The Court held that a state occupa-
tion tax measured by gross receipts from a broadcasting station within
the state, which was licensed to broadcast and did in fact broadcast to
points outside the state was an unconstitutional burden on interstate
commerce. The State Supreme Court in sustaining the tax had taken
the position that the broadcasting station was not engaged in interstate
commerce, but was carrying on the purely local activity of making its
facilities available to commercial advertisers. It would, of course, be
quite as logical to argue that an interstate telephone or telegraph com-

\textsuperscript{13} 277 U. S. 163, 171 (1928).
\textsuperscript{14} 297 U. S. 250 (1936).
pany is not engaged in interstate commerce but is simply selling its facilities to people who wish to telephone or telegraph. The Supreme Court of the United States took this view, and held that the broadcasting company was really broadcasting the programs of its advertisers, and engaging in interstate commerce, so that the tax was unconstitutional. *Atlantic Lumber Co. v. Commissioner of Corporations & Taxation* was another case involving a privilege tax for doing business within the taxing state. The Court held that a Delaware corporation which was engaged exclusively in interstate commerce, but which had its principal office in Massachusetts, kept its books and bank account there, held directors meetings there and paid dividends from its office there, was doing a sufficient local business to sustain the tax.

In still another franchise tax case, *Matson Navigation Co. v. State Board of Equalization*, the Court upheld a California franchise tax upon a local corporation which was doing both an interstate and an intrastate business. The tax was measured by a percentage of the corporation’s net income from both classes of business, properly allocable to its operations in California. The taxpayer attacked the tax on the grounds that it imposed an unconstitutional burden on interstate commerce and created an unconstitutional classification in that corporations engaged exclusively in interstate business were not subject to the tax. The Court denied that measuring the tax by net income from interstate commerce unconstitutionally burdened such commerce, and further found that the classification was constitutional, since the tax could not be applied to corporations engaged exclusively in interstate commerce, and therefore the classification was compelled by the Constitution. It may be worth noting that the *Matson* case does not necessarily hold that a state cannot tax the net income derived from the taxing state by a corporation engaged exclusively in interstate business. The tax in the *Matson* case was a franchise tax. Clearly such a tax cannot be exacted from a corporation which does no intrastate business. A direct tax upon the net income of a corporation doing an exclusively interstate business might present a very different question from a privilege tax measured by such income. *Bingaman v. Golden Eagle Western Lines Inc.*, was another in the series of cases involving the validity of a tax upon the use of gasoline consumed in interstate commerce. Gasoline was purchased outside of New Mexico, put in tanks attached to buses engaged exclusively in interstate transportation, and used to propel the buses through New Mexico. New Mexico attempted to tax the gas which was used in the state, but the Court held that the tax was unconstitutional.

15. 56 Sup. Ct. 887 (1936).
17. 297 U. S. 626 (1936).
Another case from New Mexico, Morf v. Bingaman, involved the distinction between a tax and a fee. The state statute provided that cars driven in the state for purposes of sale should get a special permit which costs $7.50 in the case of a vehicle propelled by its own power, and $5 for a vehicle which was towed. Morf, who was engaged in the business of buying cars outside of New Mexico, transporting them through the state in caravans and reselling them outside the state, contended that the statute imposed an unconstitutional burden on interstate commerce and created an unconstitutional classification. The Court held, however, that this was not an unconstitutional tax upon commerce but a reasonable fee for policing the caravans and repairing the wear and tear they inflicted on the state roads, despite the fact that the proceeds were not specifically appropriated for such purposes. Nor, according to the Court, was Morf denied the equal protection of the laws. It was reasonable to treat cars travelling in caravans for purposes of sale and single cars driven for pleasure differently. The only possible discrimination in the statute was against single cars driven for sale as contrasted with single cars driven for pleasure. However, since Morf transported his cars in caravans he was not within the class discriminated against and therefore he could not raise this question.

Another case at the last term involved the distinction between a tax and a fee, in connection not only with a tax on commerce but with a tonnage duty. In Clyde Mallory Lines v. Alabama, a charge of $7.50 per vessel was made for ships above a certain tonnage entering the port of Mobile. The Court held that this was not a tonnage duty nor a tax on commerce, but a reasonable fee for policing the harbor, regulating traffic and so on. Although this is not the first case where the Court has distinguished an unconstitutional duty upon tonnage and a valid fee the earlier cases required a particular benefit in order to have a fee. The Clyde Mallory case seems to extend the earlier decisions somewhat by holding that an exaction may be made for a general benefit and still be a fee rather than a tax upon tonnage.

The last case of this group attempted to raise an interesting point upon which the Court will be compelled to pass eventually. The Twenty-first Amendment tried to protect dry states from a flood of liquor from wet states which was sure to follow Repeal, by embodying the principle of the Webb-Kenyon Act in the amendment itself. The second Section of the Twenty-first Amendment forbids “the transportation or importation into any state... for delivery or sale therein of intoxicating liquors in violation of the laws thereof.” Some states which tolerate the sale of liquor have regarded this as a license to discriminate against foreign liquor in favor of the domestic product. The inferior federal courts have

18. 56 Sup. Ct. 756 (1936).
reached divergent results as to the validity of this type of legislation.\textsuperscript{20} In *Premier-Pabst Sales Co. v. Grosscup*,\textsuperscript{21} a Pennsylvania statute required dealers in beer manufactured outside the state to pay a license fee of $900 and give bond in the sum of $2,000, while dealers in domestic beer were only required to pay $400 for a license and to give bond for $1,000. The District Court upheld the statute denying that it violated either the commerce clause or the Fourteenth Amendment. The Supreme Court, however, held that the dealer in foreign beer, who alleged that it was aggrieved by the statute, would not have been entitled to a license in any event, since its directors and stockholders did not have the requisite residential requirements of the statute, and refused to consider the constitutional question.

III Reciprocal Exemption of State and Federal Instrumentalities From Federal and State Taxation

The precise boundaries of the doctrine that immunizes the instrumentalities of the states against federal taxation and those of the national government against state taxes, continued to embarrass the Court. At the last term six cases raised this problem. Curiously enough, all of them involved the scope of federal immunity from state or territorial taxation.

Although the most publicized decision was *Baltimore National Bank v. State Tax Commission*,\textsuperscript{22} which held that Section 5219 of the Revised Statutes authorized a tax on shares of stock in national banks belonging to the Reconstruction Finance Corporation, even upon the assumption that the RFC was a governmental agency, a much more significant case from a doctrinal viewpoint would appear to be *Schuylkill Trust Company v. Pennsylvania*\textsuperscript{23} Pennsylvania assessed a tax against shares of stock in trust companies, which was paid by the corporation as the agent of the shareholders. In arriving at the value of the shares, for the purpose of the tax, shares of stock in other corporations which had already been taxed by Pennsylvania and shares in corporations which were exempt from tax under the Pennsylvania law, were deducted from the capital of the trust company. The purpose of the former deduction was to eliminate double taxation; of the latter, to carry out a consistent state policy of exempting certain corporations from taxation. Federal securities and stock in national banks were not deducted. The majority of the Court held that the tax was unconstitutional in that it discriminated

\textsuperscript{21} 56 Sup. Ct. 754 (1936).
\textsuperscript{22} 297 U. S. 209 (1936).
\textsuperscript{23} 296 U. S. 113 (1935).
against federal securities, and provided for an additional tax upon shares of stock in national banks which had already been taxed in a manner specified by Section 5219 of the Revised Statutes. The minority in an opinion by Mr. Justice Cardozo, which was concurred in by Justices Brandeis and Stone, felt that the tax was valid as far as the inclusion of federal securities was concerned, since the discrimination was not "so marked as to justify the inference that it was unfriendly in design" and it did not favor forms of investment "in substantial competition" with federal securities. The decision pushes the prohibition against state taxation of federal securities to an extreme. It seems to add to the rule that the stock of a corporation which owns federal bonds may be taxed the flat qualification that if anything is deducted in computing the tax, federal securities must be exempted too.

Graves v. Texas Co.,25 raised an interesting question in connection with an Alabama tax upon gasoline sold to the Federal Government for governmental purposes: Mr. Justice Brandeis and Mr. Justice Cardozo (Mr. Justice Stone did not participate in the decision of the case) felt that the tax was upon storage rather than sale and did not therefore impose an unconstitutional burden upon a federal instrumentality. However, the majority concurred in an opinion by Mr. Justice Butler, who first doubted whether the tax was really upon storage rather than sale, and then held that even upon the assumption that it was imposed upon storing it was unconstitutional. "Plainly," said Mr. Justice Butler, "the sales and deliveries by the company to the United States necessarily include storing and withdrawal from storage. A tax upon anything so essential to the sale of gasoline is as objectionable as would be a tax upon the sale itself."

Other cases on intergovernmental immunities were of less general interest. Posados v. National City Bank of N. Y.26 held that the Philippines could not impose a tax on national banks which was not authorized by Section 5219 of the Revised Statutes.27 State v. Barnsdall Refineries Inc.,28 found that an Oklahoma gross production tax on oil from Osage lands did not conform to the conditions of the congressional waiver of immunity from state taxation and was invalid. Leahy v.

25. 56 Sup. Ct. 818 (1936).
27. In Domenech v. National City Bank, 294 U. S. 199 (1935) the Court held that Puerto Rico could not tax a national bank except as provided by R. S. 5219. The Posados case simply adds that there is nothing in the Organic Act of the Philippines which differentiates its position from that of the other dependencies of the United States.
State Treasurer sustained an Oklahoma tax upon the income of an emancipated Osage Indian from restricted tribal lands. The Court reasoned that the Indian had a certificate of competency and that his income could be taxed like that of any other taxpayer. The case reaches a sensible result and seems perfectly consistent with precedents like Gillespie v. Oklahoma where a state income tax upon the income of a lessee of Indian lands was held unconstitutional. Although the lessee in the Gillespie case was as emancipated as the Indian in the Leahy case, still a tax on the lessee's income would tend to make leases of Indian land less desirable and slightly prejudice the position of the wards of the nation. A tax upon an emancipated Indian's income, however, can only prejudice the Indian whose income is taxed, and presumably since he has been emancipated he is no longer a concern of the federal government.

IV THE FOURTEENTH AMENDMENT

A. Freedom of the Press

One of the late Senator Long's legislative experiments consisted of a Louisiana tax of two per cent. upon the gross receipts from advertising of newspapers and periodicals with a weekly circulation of 20,000 or more. The constitutionality of this measure was challenged in Grosjean v. American Press Company upon the grounds that it deprived the larger papers of equal protection of the laws, since periodicals with slightly smaller circulations were not taxed, and that it violated the due process provision of the Fourteenth Amendment. Somewhat to the surprise of those who had been watching the case, the Supreme Court did not concern itself with the problem of classification, but directed its attention to due process. Starting with the premise that due process in the Fourteenth Amendment includes the fundamental liberties guaranteed by the first eight amendments to the Federal Constitution, including liberty of the press, the Court found that the tax abridged the freedom of the press by curtailing revenues from advertising and restricting circulation and was unconstitutional. Although Mr. Justice Sutherland was careful to observe that "It is not intended by anything we have said to suggest that the owners of newspapers are immune from any of the ordinary forms of taxation," the case leaves considerable doubt as to just what forms of taxation a newspaper may be subjected constitutionally. It is possible that some taxes directed specifically at newspapers and similar periodicals which are not dis-

criminatory might be sustained,\textsuperscript{32} although it would appear that any such tax would be jealously scrutinized by the Court.

\textbf{B. Chain Store Taxes}

Recently a lower federal court upheld the constitutionality of the Louisiana chain store tax which bases the rate of tax upon the total number of units in the chain, regardless of whether they are located in Louisiana or not, although only the units in Louisiana are taxed,\textsuperscript{33} and both the Florida Supreme Court and an inferior federal court held that a progressive Florida gross receipts tax on chain stores, which was graduated according to the number of units in the chain, rather than the volume of receipts, was unconstitutional.\textsuperscript{34} At the past term of the Supreme Court, however, there were no notable developments in the field of chain store taxation. \textit{Gulf Refining Co. v. Fox} \textsuperscript{35} came before the Court for the second time. In a previous decision the Court had upheld the constitutionality of the West Virginia chain tax as applied to filling stations and remanded the case to determine whether the Gulf Refining Company's "Authorized Licensed Dealer" stations were "stores . . . owned, operated, maintained and/or controlled by the same person, firm, corporation, copartnership or association" within the tenor of the statute. The lower court held that they were, and the Supreme Court refused to disturb the decision. Another case disposed of by the same opinion, \textit{Ashland Refining Co. v. Fox} \textsuperscript{36} involved a similar point and the Court again sustained the decision of the lower tribunal that certain dealer stations connected with the Ashland Refining Company were taxable as part of the Ashland chain.

These were the only cases on chain store taxation. Their significance perhaps lies in the fact that they narrow the sphere for avoidance of chain taxes. A carefully drafted statute should be able to marshall into a single chain units which have a substantial economic or factual connection, regardless of the form of their technical legal affiliation.

\textbf{C. Privileges or Immunities}

\textit{Colgate v. Harvey}\textsuperscript{37} is noteworthy as the first case to hold a state statute unconstitutional under the privileges or immunities clause of the

\begin{footnotes}
\textsuperscript{33} Great Atlantic \& Pacific Tea Co. \textit{v. Grosjean}, decided by the District Court for the Eastern District of Louisiana, July, 1936.
\textsuperscript{34} State \textit{v. Simpson}, 166 So. 227 (Fla. 1935); \textit{Lane Drug Stores, Inc. v. Lee}, Comptroller, 11 F. Supp. 672 (N. D. Fla. 1935).
\textsuperscript{35} 297 U. S. 381 (1936).
\textsuperscript{36} \textit{Ibid.}
\textsuperscript{37} 296 U. S. 404 (1935).
\end{footnotes}
Fourteenth Amendment, although this question had been presented to the Supreme Court on at least forty-four previous occasions. Under the Vermont Income Tax, dividends from foreign corporations were taxed, while dividends from domestic corporations were not, and interest from loans made without the state were taxed, while interest from loans made within the state at not more than five per cent. was not. Both of these provisions were challenged on the grounds that they violated the equal protection and the privileges or immunities provisions of the Fourteenth Amendment. The Court agreed that the tax on dividends was constitutional, since the exemption of domestic dividends was compensated for by the tax which domestic corporations paid Vermont on their income. However, the Court divided upon the constitutionality of the tax upon interest from loans made without the state. Six of the Justices in an opinion by Mr. Justice Sutherland held that this part of the statute was invalid. Justices Brandeis and Cardozo concurred in an opinion by Mr. Justice Stone upholding the validity of the Vermont tax in its entirety. The majority thought that the tax violated both the equal protection and privileges or immunities provisions; the minority that it transgressed neither. Their differences were sharply defined. Mr. Justice Sutherland held that the statute did not make a reasonable classification, since the legislature failed to disclose affirmatively any public interest which would be furthered by the exemption of interest on loans made within the state. This approach contradicts the time-honored presumption of constitutionality and the minority seemed on much firmer ground when they took the position that the statutory classification might promote the investment of capital within the state and therefore it could not be assumed to be unreasonable. "Surmise," was the way that the majority characterized this reasoning. However, the minority felt compelled to such surmises by a proper respect for the action of a state legislature. The attitude of the majority toward the privileges or immunities guaranteed by the Fourteenth Amendment was amazing. Since the *Slaughter House Cases* it has seemed settled that "privileges or immunities" under the Fourteenth Amendment do not include those "fundamental immunities" which are protected against discriminatory action of the States under Article IV, but are limited to the privileges and immunities of United States citizenship, which are guaranteed by some other part of the Constitution or a federal statute. Admittedly this nullifies the privileges or immunities provision of the Fourteenth Amendment, since it simply guarantees protection of those things which are independently protected by some other clause of the Constitution. In *Colgate v. Harvey*, however, the majority of the Court rejected the narrow construction of the *Slaughter House Cases* which was vigorously contended for by the minority, and held that the right to lend money in a state other

38. 83 U. S. 36 (1873).
than that in which the lender resides is a privilege of national citizenship. The case clearly goes beyond the previous precedents on privileges or immunities under the Fourteenth Amendment and suggests new and undesirable encroachment of Supreme Court control over the intimate concerns of the states.

D. Jurisdiction to Tax

The outstanding decision on jurisdiction to tax was *Wheeling Steel Corporation v. Fox.* The Wheeling Steel Corporation is a Delaware corporation with its principal headquarters at Wheeling, West Virginia. Its office in Delaware is a purely nominal affair designed to conform to the minimum requirements of the corporation laws of that state. The real seat of corporate control is Wheeling. Although the principal plants of the company are located in Ohio, the business is controlled from the Wheeling office. There the officers reside, directors and stockholders hold their meetings, orders are ratified, disbursements are ordered and dividends are declared. The corporation has bank accounts in West Virginia and in the states where its plants are located. Except for disbursements for payrolls, however, payments from these accounts are controlled from the Wheeling office. West Virginia imposed an *ad valorem* tax upon all the receivables of the company, including bank deposits, although some of the bank accounts which had been assessed by Ohio were excluded as a matter of the proper construction of the West Virginia statute. The corporation challenged the tax, broadly upon the ground that its intangibles could only be taxed at the technical corporate domicile, Delaware. The State countered with the argument that these receivables had acquired a business situs in West Virginia. The Supreme Court upheld the tax in an equivocal opinion which leaves the precise grounds of decision obscure. The Court stressed the "commercial domicile" which the corporation had acquired in West Virginia and referred to Wheeling as the "actual seat of its corporate government." Moreover, the corporate domicile in Delaware was referred to as a "technical one" and not a "principal office so far as the actual conduct of business is concerned;" while it was said that to allow Delaware to tax these credits to the exclusion of West Virginia "is to make a legal fiction dominate realities."

It is barely possible that the case may be the starting point for a doctrine that would make the corporate domicile for tax purposes the "seat of the corporate government" rather than the technical place of incorporation. Apart from such considerations, however, the case constitutes an important precedent on the doctrine of business situs. It is the first case which has discovered such a situs where the business situs

40. 56 Sup. Ct. 773 (1936).
was not also the domicil of the debtors. There is moreover a strong
intimation that a tax upon the basis of such a situs will exclude another
tax by the corporate domicil, since the Court seemed to feel that it
had to make a competitive choice between Delaware and West Virginia.
This, of course, has still to be squarely decided, but it seems to be a fair
inference from the opinion.

In another case involving domicil, the representatives of the Dorrance
estate made another futile appeal to the Supreme Court. As you are
doubtless aware, in the now famous Dorrance cases, both Pennsylvania
and New Jersey claimed Dorrance as a domiciliary and proceeded to
assess inheritance taxes on that basis. Repeated recourse to the state
courts and to the Supreme Court of the United States failed to bring relief
from either tax. In *Hill v. Martin* 41 an attempt was made to enjoin
the New Jersey tax in a federal district court. The injunction was denied
and the Supreme Court upheld the decision of the district court on the
ground that the proceedings in New Jersey had passed from an admin-
istrative into a judicial stage.

*Norfolk & Western Ry. Co. v. North Carolina* 42 the last case on
jurisdiction to tax, involved a unitary assessment by North Carolina in
connection with a tax upon the net income of an interstate railway. The
part of the railway's net income which was subject to the tax was deter-
mined by allocating to the state the gross operating revenues within the
state including the mileage proportion of the interstate business and
deducting a proportionate average of operating expenses. The railroad
sought to sustain its contention that this resulted in allocating an un-
constitutional proportion of its income to North Carolina by introducing
evidence to show that its actual operating expenses in the state exceeded
its average operating expenses. However, the Court upheld the assess-
ment because the railroad had failed to show that its actual gross income
from within the state did not exceed the amount which it was obliged to
return from the purpose of the tax. In other words, an assessment based
upon a portion of average income and average expenses will not be in-
validated simply because actual expenses exceed average expenses, unless
the taxpayer shows that this is not compensated for by a discrepancy
between actual receipts and average receipts.

E. Assessment

In *Great Northern Railway v. Weeks* 43 the Supreme Court enjoined
an assessment of railroad property which was based upon pre-depression
values on the ground that this violated due process. Hitherto the Court
has consistently held that it would not interfere with an assessment sim-

41. 296 U. S. 393 (1935).
42. 297 U. S. 682 (1936).
43. 297 U. S. 135 (1936).
ply because it was too high. Mr. Justice Butler, who delivered the majority opinion, attempted to preserve a verbal consistency with past precedent by declaring that "overvaluation is not of itself sufficient to warrant injunction against any part of the taxes based on the challenged assessment" while he purported to find "the equivalent of intention or fraudulent purpose to overvalue the property" because the assessors who had previously based their assessments partially upon the market value of the railroad's securities refused to consider the depreciation caused by the depression. Needless to say this equivalence was not apparent to the minority who in the words of Mr. Justice Stone felt that the "Constitution guarantees no immunity from taxation even though the tax because of its amount may be burdensome . . . or because it is as high in a year of depression and falling property values as in years of prosperity." According to the minority the railroad had shown nothing beyond overvaluation and had failed to "present any case for invoking the protection of the Constitution."

The only other case involving an assessment was Georgia R. R. & Electric Company v. City of Decatur,44 where the Court held that a street railway could constitutionally be required to pay for paving a street which it used without any showing of special benefits.

V Extrastate Enforcement of Tax Obligations

Although the Supreme Court had never passed upon the point, it had been generally assumed that full faith and credit did not require one state to enforce the taxes of another, even though the obligation to pay the tax had been reduced to a judgment. Milwaukee County v. M. E. White Co.45 dissipated this assumption by deciding that a district court sitting in Illinois must enforce a judgment for taxes recovered in Wisconsin.

The desirability of the decision cannot be questioned. However, the case still leaves open the problem of whether a tax obligation of one state which has not been reduced to a judgment, must be enforced by the courts of another state. As a matter of principle and policy it should. In the event of an adverse decision on the point, however, there would appear to be no possible constitutional objection to a statute such as that recently enacted in North Carolina,46 which provides in substance that the courts of North Carolina enforce taxes due other states, where those states extend a similar comity to North Carolina.

VI The Federal Income Tax

The bulk of the Supreme Court's tax work at the last term as usual concerned itself with the Federal Income Tax. Koshland v. Helvering47

44. 297 U. S. 620 (1936).
45. 296 U. S. 268 (1935).
47. 56 Sup. Ct. 767 (1936).
was perhaps the most perplexing case which the Court decided. A taxpayer owned shares of preferred stock on which she received common stock as dividends. The preferred stock was later redeemed. In computing the taxpayer's profit upon the redemption of the preferred stock, the Commissioner allocated the cost of the stock between the preferred stock and the common stock, which, of course, reduced the taxpayer's basis and increased the amount of her taxable gain. The taxpayer appealed to the Board of Tax Appeals, which reversed the Commissioner and held that the stock dividends were taxable as income in the years in which they were received and could not be applied to reduce the basis of the original stock. The Circuit Court of Appeals in turn reversed the Board on the ground that the stock dividends were not taxable as income and therefore the cost of the original stock must be apportioned. The Circuit Court of Appeals was in turn reversed by the Supreme Court, in an opinion by Mr. Justice Roberts from which Justices Stone and Cardozo dissented. Mr. Justice Roberts first considered the question of whether or not the stock dividends were taxable as income in the years when they were received. This involved two questions: whether they could constitutionally be taxed in view of *Eisner v. Macomber*, and whether they were taxed under the Acts in force in those years which provided that "A stock dividend shall not be subject to tax." The Court said that the dividends were constitutionally taxable, because the stockholder acquired a new interest in the corporation. While *Eisner v. Macomber* was limited to a stock dividend under which "the pre-existing proportionate interests of the stockholders remain unaltered." With respect to whether the statutes as a matter of fact taxed dividends like those in the *Koshland* case, the Court said that as an original proposition it might think that it did, and that the proper construction of the phrase excluding stock dividends from taxation was only to exclude that type of dividend which could not be taxed constitutionally under *Eisner v. Macomber*. However, the Court added that the long administrative interpretation of the statutes to exclude all stock dividends should be given proper deference, although it did not explicitly define the degree of deference, because it said that this was not a question which it had to decide. The reason why the Court did not feel called upon to decide this question was that the stock dividends in the *Koshland* case were income and not capital, and therefore the regulations which required the basis of the original stock to be reduced by such dividends were not authorized by the statute. Mr. Justice Roberts does not squarely say that it is beyond the constitutional power of Congress not to tax income in the year in which it is realized but to use it to reduce the basis of the capital asset which produces the income, although it is possible to infer from his language that there may be some difficulty about this. It is difficult at this stage to estimate the

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exact significance of the holding in the *Koshland* case. However, a few suggestions may perhaps be ventured. Since the Sixteenth Amendment only authorizes a tax upon income, we are familiar with the importance of distinguishing capital from income. The *Koshland* case makes it important to distinguish income from capital. It is possible that there is some constitutional inhibition against using income which is not taxed to reduce the basis of a capital asset which is subsequently sold. If this can be done under explicit statutory authorization, it certainly cannot be done where there is no explicit congressional mandate. Not only will the Department be unable to collect a tax now on many stock dividends which they made no attempt to tax, but it will have to go over the situations where tax exempt distributions have been used to reduce the basis of a capital asset, to see just how many of them will stand in the light of *Koshland v. Helvering*.\(^4^9\)

Another important decision on the nature of income was *Douglas v. Willcuts*,\(^5^0\) which put an end to a conflict in the Circuit Courts of Appeals by holding that income from a trust established to pay alimony was taxable to the settlor of the trust, rather than to the former wife, who actually received the income. The broad principle underlying the decision seems to be that a payment in discharge of an obligation is income to the taxpayer. The decision in the *Douglas* case was followed in two *per curiam* decisions. In *Helvering v. Schweitzer*\(^5^1\) it was held that income from a trust which had been established by a father for the support of minor children was taxable to the father, and in *Helvering v. Blumenthal*\(^5^2\) it was held that the income from a trust established to liquidate a debt was taxable to the debtor.

Everyone who has followed the development of the Federal Income Tax knows of the difficulties which have arisen in determining whether a so-called Massachusetts trust was to be taxed as a trust or an association. The Regulations for the most part have reflected the confusion of the cases. The last Regulations, however, came out squarely for a test based upon the purpose of the trust. If the purpose was merely to hold and conserve property, it was taxable as a trust. If the purpose was to carry on some business it was to be taxed as an association. It is a safe assumption that the general current of professional opinion felt the regulations had gone too far; that they had achieved simplicity at the expense of including some trusts as associations which would not be so classified by the courts. However, in four cases, the Supreme Court

\(^{49}\) Section 115 (f) (1) of the Revenue Act of 1936 provides: "A distribution made by a corporation to its shareholders in its stock or in rights to acquire its stock shall not be treated as a dividend to the extent that it does not constitute income to the shareholder within the meaning of the Sixteenth Amendment to the Constitution."

\(^{50}\) 296 U. S. 1 (1935).

\(^{51}\) 296 U. S. 551 (1935).

\(^{52}\) 296 U. S. 552 (1935).
affirmed the Department's latest position. In Swanson v. Commissioner,\textsuperscript{53} Helvering v. Coleman-Gilbert Associates,\textsuperscript{54} Helvering v. Combs,\textsuperscript{55} and Morrissey v. Commissioner,\textsuperscript{56} the Court adopts as the controlling test of a trust or an association, the purpose of the trust. A trust to be taxable as such must be designed to hold and conserve property without more. If the purpose of the trust is to carry on a business, it is taxable as an association. Transferability of certificates of beneficial interest, meetings of the beneficiaries, continuity of existence, the election of directors and officers, and so on, are all makeweights in determining whether there is a trust or an association. But the controlling test is purpose.

Another important aspect of these decisions is this: In the past some confusion has been engendered by a tendency to test the existence of a trust or an association by the character of the business done during the taxable period. A change in the business done by the trust might result in its being held to be a trust in one year and an association in another. Under the recent decisions what seems to be important is not what the trust actually does during the taxable year, but what it is authorized to do. If it is created to carry on a business, it will be taxed as an association, regardless of the fact that its activities in a given year may consist of little more than holding and conserving property.

There were other decisions in connection with the income tax at the past term of less general interest perhaps, but which still raised interesting and important questions. General Utilities & Operating Co. v. Helvering,\textsuperscript{57} for example, raises a nice point in connection with corporate distributions. General Utilities purchased 2,000 shares of stock of the Islands Edison Company for $2,000. After the stock had appreciated in value, Southern Cities Utilities Company desired to purchase it. If General Utilities sold the stock directly to Southern Cities Utilities a taxable gain would, of course, have been realized upon the sale. To avoid this tax General Utilities wrote the stock up on its books to its market value. Then it declared a dividend of $1,071,426.25 which was made payable in the stock of the Islands Edison Company at a valuation of $56.12\(\frac{1}{2}\) a share, and the General Utilities stockholders undertook to sell this stock to Southern Cities Utilities. The Commissioner contended that the corporation realized a gain by the distribution of the stock to the extent of the difference between the cost of the stock and the amount of the declared dividend, on the theory that the declaration of the dividend created a debt which was discharged by the distribution

\textsuperscript{53} 296 U. S. 362 (1935).
\textsuperscript{54} 296 U. S. 369 (1935).
\textsuperscript{55} 296 U. S. 365 (1935).
\textsuperscript{56} 296 U. S. 344 (1935).
\textsuperscript{57} 296 U. S. 200 (1935).
of the stock. The Board of Tax Appeals held that there was no taxable profit to the corporation upon the distribution of the stock. The Circuit Court of Appeals agreed with the Board upon this point, but held that the corporation had realized a profit because it was in substance the seller of the stock to Southern Cities Utilities. The Supreme Court agreed with the two lower tribunals that no profit was realized by the corporation by the distribution of the stock to its own stockholders, and it reversed the decision of the Circuit Court of Appeals because in deciding that there was a sale by the corporation, they decided a point upon which there was no finding by the Board of Tax Appeals. The interesting feature of this decision is its possible implications. If a corporation has stock which has appreciated in value it can distribute this stock without showing any taxable gain by a distribution or dividend in kind. On the other hand if the corporation has stock which has depreciated in value, it would seem possible to show a tax loss by declaring the dividend without mentioning the stock and then distributing the stock in payment of the dividend. It is not certain that a loss would be recognized in this case, but at least it could be argued that the declaration of the dividend creates a debt, and the corporation realizes a taxable loss when it distributes the stock to liquidate this debt.

A more certain device for minimizing income taxes appears from United States Trust Company v. Commissioner. It is, of course, obvious that the total tax liability of separate trusts for several beneficiaries will usually be less than that of a single trust for the same beneficiaries. This is particularly true if part of the trust income is to be accumulated. In addition to the added one thousand dollar exemption for each trust, the income from the separate trusts will fall into lower surtax brackets. In United States Trust Company v. Commissioner, a trust was originally created for three beneficiaries. Later it was amended to provide that the trust should be divided into separate trusts for each beneficiary. Although the trustee proceeded to set up separate cash accounts for each of the beneficiaries, and separate accounts of their undivided interests in the other trust property, there was no actual physical severance of the trust property. However, the court held that the amendment converted the trust into three distinct trusts for purposes of the income tax. Helvering v. McIlvaine was a companion case which reached a similar conclusion.

There was the usual run of cases dealing with basis. McFeeley v. Commissioner held that personal property is acquired from a decedent at the date of the decedent's death, rather than the date of distribution for the purpose of determining the holding period necessary for a

58. 296 U. S. 481 (1935).
60. 296 U. S. 102 (1935).
capital asset under the capital gains provisions of the 1928 law. *Helvering v. San Joaquin Fruit & Investment Co.* held that realty which was leased with an option to purchase was acquired when the option was exercised, rather than upon the date when the lease commenced. *Helvering v. Salvage* involved the basis of stock which had been acquired by the taxpayer at less than its market value in consideration of his agreement not to compete with the issuing corporation. The Court held that the proper basis of the stock was the market value at the time it was acquired, rather than the cash price, since the taxpayer's agreement not to compete was part of the consideration for the purchase of the stock. However, with respect to a part of the stock which the corporation had retained an option to repurchase at a figure below the current market value, the Court held that the basis could not exceed the price at which the corporation was entitled to exercise its option.

*United States v. Safety Car Heating & Lighting Company* involved property held on March 1, 1913. The taxpayer acquired a patent in 1907. In 1912 it brought an action for an infringement. Originally the suit sought to recover both damages and loss of profits, but later the taxpayer elected to sue only for loss of profits. An infringement was found in 1915. An accounting followed for eight years. Finally an award was made which was affirmed by the court and appeals were taken from the decision. In 1925 while the appeals were pending the taxpayer settled for $200,000 or about half the original award. The taxpayer contended that part of the settlement which was referable to profits accrued before March 1, 1913 was capital and not income. It also contended that it had sustained a loss in 1925 when the settlement was made for less than the amount of the judgment which had been recovered. However, the Supreme Court found that the entire settlement (less costs of prosecuting the action) was income in the year when it was paid, and that the taxpayer had not sustained any loss. The claim was not clear and unconditional on March 1, 1913 and therefore it had not become capital. Income, which was taxable, was realized when the settlement was made. No loss was sustained because before the settlement was made it was not clear how much the taxpayer would recover. Mr. Justice Sutherland, together with Justices Butler and Roberts dissented upon the ground that the claim had an ascertainable value on March 1, 1913 and therefore the part of the profits accruing before that date could not be taxed.

There were a group of cases which undertook to define a reorganization under the 1924, 1926 and 1928 Acts. Prior to the 1934 Act a reorganization was defined to include a merger or consolidation. In the

61. 297 U. S. 496 (1936).
63. 297 U. S. 88 (1936).
1934 Act the qualification was added that the merger or consolidation must be a "statutory" merger or consolidation. In five cases, Helvering v. Minnesota Tea Co.; John A. Nelson Co. v. Helvering; Helvering v. Watts; G. & K. Mfg. Co. v. Helvering and Bus & Transport Securities Corporation v. Helvering, the Supreme Court was called upon to construe the definition of a reorganization under the earlier acts. The Court held that a technical merger or consolidation was not a prerequisite to a reorganization under those statutes, but that there might be a reorganization, if the selling corporation acquired a substantial interest in the affairs of the purchasing corporation. Of course, these decisions are not controlling under the present law.

A point of practical importance to those concerned with corporate financing arose in Great Western Power Co. v. Commissioner. A corporation redeemed an issue of bonds with new bonds. The Court held that the unamortised discount on the old bonds and the expense of issuing and exchanging the new bonds for the old should not be deducted in the year when the new bonds were issued but should be amortised and deducted over the life of the new bonds.

The last case on the income tax, Hulburd v. Commissioner, involved a deficiency assessment against the estate of a stockholder in a corporation which had distributed its assets without paying its income tax. An attempt was made to collect the assessment from an executor and legatee of the estate. The Court held that the assessment could not be collected against the legatee because the deficiency had not been assessed against the legatee but against the estate. Nor could the executor be held liable because under the Illinois law, where the estate was administered when an executor is discharged his official existence ceases, and this assessment was made after the discharge. The fact that the executor had not notified the Commissioner of his discharge did not affect the situation, because under the Act in force at that time, notice was not required.

VII The Federal Estate Tax

There were notable developments in connection with the federal estate tax at the last term. In Helvering v. City Bank Farmers Trust Company, the Court in a five to four decision held that a trust which was revocable by the settlor in conjunction with a beneficiary of the trust

64. 296 U. S. 378 (1935).
65. 296 U. S. 374 (1935).
68. 296 U. S. 391 (1935).
69. 297 U. S. 543 (1936).
70. 296 U. S. 300 (1935).
71. 296 U. S. 85 (1935).
was taxable as part of the gross estate of the settlor under the federal estate tax. This ended a conflict in the inferior courts. It came as a distinct shock to professional opinion which had about concluded that such trusts could not be taxed under the federal estate tax, either because the Court would construe the provision providing for a tax where the trust was revocable in conjunction with "any person" to mean in conjunction with any person not having a substantial adverse interest, in conformity with a somewhat similar provision in the income tax; or because a tax on such a trust was without the constitutional power of Congress. The reason that the tax in the City Bank Farmers Trust Company case appeared to be unconstitutional was that it was difficult to find any testamentary transfer here, and since Heiner v. Donnan it seemed settled that there must be a testamentary transfer to sustain an estate tax. The remarkable thing about the decision in Helvering v. City Bank Farmers Trust Company, however, is that there is no talk about testamentary transfers. Congress, said Mr. Justice Roberts, speaking for a majority of the Court, "may adopt a measure reasonably calculated to prevent avoidance of a tax. The test of validity in respect of due process of law is whether the means adopted is appropriate to the end. A legislative declaration that a status of the taxpayer's creation shall, in the application of the tax, be deemed the equivalent of another status falling normally within the scope of the taxing power, if reasonably requisite to prevent evasion, does not take property without due process." In other words a tax designed to prevent tax avoidance does not necessarily have to fit into any preconceived judicial pattern. If it is a reasonable means of preventing tax avoidance, it will be constitutional.

The language in Helvering v. City Bank Farmers Trust Company readily fits taxes other than death taxes. It suggests an entirely new constitutional theory of taxes designed to prevent tax avoidance, foreshadowed perhaps, but not nearly so explicitly stated in Burnett v. Wells. No longer need prophylactic taxes conform to any judicial conception of a certain type of tax, but any tax which is reasonably calculated to prevent tax avoidance may be sustained as a complement to the tax whose avoidance it is designed to prevent.

The decision in Helvering v. City Bank Farmers Trust Co. was qualified somewhat by White v. Poor and Helvering v. Helmholtz which were decided the same day.

White v. Poor involved a situation where a decedent during her lifetime had conveyed property in trust to three trustees, who were the decedent herself, her son, who was also a beneficiary, and a third
person who was not beneficially interested. It was provided that the trust could be terminated by the trustees. After the creation of the trust the settlor resigned as a trustee and was replaced by her daughter. Then the daughter resigned and was replaced by the settlor, who continued to serve as a trustee until her death. The Court held that the trust was not taxable as part of the settlor’s gross estate. There were two grounds for the decision. The first was that the settlor had the power to terminate the trust only as a trustee and not in her capacity as settlor, and therefore as a matter of construction the trust fell without the terms of the statute. The second ground was that if the tax applied it would be unconstitutionally retroactive. Although a revocable trust can be subjected to a death tax under a statute which is passed after the creation of the trust, the trust must really be revocable. A trust which is revocable by the settlor in conjunction with a beneficiary is within the statutory definition of a revocable trust, but as far as a retroactive tax is concerned it is a complete transaction, which cannot be reached constitutionally. Mr. Justice Brandeis, Mr. Justice Stone and Mr. Justice Cardozo concurred in the result. It may be of interest to note that the 1936 Act explicitly provides for a tax in a situation like that in *White v. Poor*.

In *Helvering v. Helmholtz* the Court held that a trust which had been created by the decedent and her relatives and which was revocable with the consent of all the “then beneficiaries” was not taxable as part of the decedent’s gross estate under the federal estate tax. The reasoning of Mr. Justice Roberts which involves a very dubious premise from the point of view of the Law of Trusts was that the trust could have been revoked by the action of all the persons in interest, without any explicit retention of a power of revocation, and since, therefore, the reserved power added nothing to what would exist without the reservation, the trust was not subject to tax. An added ground for the decision was that the transfer in trust had been fully completed before the passage of any statute taxing such transactions, and therefore even if the statute could be construed to apply it would be fatally retroactive. Justices Brandeis, Stone and Cardozo limited their concurrence to the second ground of the decision.

In further contrast to the Court’s attitude on constitutional points were two decisions involving another problem of construction. In *Klein v. United States*, it was held that where there was a gift of a life estate

76. Revenue Act of 1936, § 805.
77. The trust was revocable with the consent of all the “then beneficiaries.” It is not at all clear, however, that “then beneficiaries” was synonymous with all the persons beneficially interested in the trust. It might well have been construed to mean those persons who were then entitled to the income from the trust and to exclude a charity and the issue of the subscribers who had contingent interests.
78. 283 U. S. 231 (1931).
with a remainder in fee, contingent upon the donee surviving the donor, that the remainder was taxable as a part of the donor's gross estate, as a transfer intended to take effect in possession or enjoyment upon death. It seemed almost incredible that the tax could be avoided by changing the form of the gift without altering the substance of the transaction, and the Regulations assumed that a gift of a fee subject to a reverter to the donor, if the donee failed to survive the donor, would likewise be taxable. However, in Helvering v. St. Louis Union Trust Co. and Becker v. St. Louis Union Trust Co. five of the Justices held that a gift of a fee which was subject to revert to the donor, if the donee failed to survive the donor, was not subject to the estate tax. The result of these decisions is that two transactions identical in substance and differing only verbally receive different tax treatment. It is worth noting that no effort was made to correct this situation in the 1936 Act.

There were two rather interesting decisions dealing with the application of the federal estate tax to policies of insurance, which followed the St. Louis Union Trust Company cases. In Bingham v. United States a deceased had, prior to the 1918 Act, taken out policies of insurance payable to his wife provided that she survived him. He retained no power to change beneficiaries, to pledge, assign or surrender the policies. The Court held that the policies were not taxable as part of the decedent's gross estate under the 1918 Act. There were two grounds for the decision. The first upon which the Court were unanimous, was that the tax provided for by the 1918 Act was not retroactive and did not apply to these policies. The second ground, which followed the St. Louis Trust Company cases and was not assented to by Justices Brandeis, Cardozo and Stone, was that there was no taxable transfer upon the death of the decedent merely because he had retained a possibility of reverter in the policies, if his wife predeceased him.

Industrial Trust Co. v. United States involved substantially the same situation, except that the insured died while the 1926 Act was in force. Despite the fact that the tax on insurance seems to be made explicitly retroactive under the 1926 Act, the Court held that the case was controlled by Lewellyn v. Frick and refused to construe the statute retroactively in order to avoid grave constitutional difficulties.

The only other case on the federal estate tax was McCaughn v. Real Estate Land Title & Trust Co. McFarlan made a transfer of a substantial portion of his estate within two years of his death. The Com-

80. 296 U. S. 48 (1935).
81. 296 U. S. 211 (1935).
82. 296 U. S. 220 (1935).
83. 268 U. S. 238 (1925).
84. 297 U. S. 606 (1936).
missioner assessed and collected a tax on the theory that the transfer was in contemplation of death. The representatives of the estate sued for a refund but the District Court found as a fact that they had failed to rebut the statutory presumption that the transfer was in contemplation of death and upheld the tax. The Circuit Court of Appeals weighed the evidence and reversed the District Court, to be in turn reversed by the Supreme Court, which held that the Circuit Court of Appeals had no jurisdiction to decide this question, but was limited to passing upon whether or not the finding of the District Court was supported by evidence.

VIII THE FEDERAL STAMP TAX ON STOCK TRANSFERS

There was one very important decision upon the federal stamp tax on stock transfers. In *Raybestos-Manhattan, Inc. v. United States*, Raybestos-Manhattan Incorporated issued stock to the stockholders of two other corporations in return for the assets of those corporations. A tax of five cents a share was assessed under Section 800 Schedule A-3 of the Revenue Act of 1926 upon the original issue of the stock and a tax of three cents a share upon the transfer of the right to receive the stock. The Raybestos-Manhattan company admitted liability for the five cent tax, but they sued in the Court of Claims to recover the tax of three cents a share on the transfer of the stock. Both the Court of Claims and the Supreme Court denied recovery. The Supreme Court said that the stockholders' rights to receive the stock originated in the transfer of the assets of the two corporations to Raybestos-Manhattan, and since the stock could only be issued to someone other than these corporations with their consent, the rights of the stockholders derived from the corporations and in substance there was a transfer of the right to receive the stock to them. The case is close. It has the practical advantage that there will be the same tax liability whether a selling corporation transfers its assets for stock in another corporation in return for stock which it distributes to its stockholders, or whether it transfers its assets in return for stock issued directly to its stockholders. In other words the same results are subjected to the same tax liabilities. Since the tax was not upon the transfer of stock, but upon the transfer of the right to receive stock, it would appear that the decision can probably be sustained not only as a matter of policy but as a matter of technical legal analysis.

CONCLUSION

The purpose of this paper has been to present a brief and objective review of the tax work of the Supreme Court at the last term. The temptation to praise or to condemn has perhaps, been too sternly repressed.
In conclusion, however, a word of caution may be in point. Excesses in judicial decision tend to correct themselves. A case may prove much less revolutionary in the healing hands of time, than it appears on the surface. There were some surprising departures from precedent at the last term, but nearly every one carried with it the potential seeds of its own destruction. To be more explicit:

United States v. Butler\(^86\) held that there were constitutional limitations on the spending power of Congress. But in view of the deference expressed for Massachusetts v. Mellon,\(^87\) it is highly doubtful whether these limitations can be invoked if the unconstitutional appropriation is formally divorced from the tax which is designed to feed it. The Constantine\(^88\) and the Kesterton\(^89\) cases appeared to the minority to foreshadow judicial psychoanalysis in dealing with regulatory taxes. But they still leave the the court free to sustain such legislation, where the regulatory character of the tax does not appear on the surface of the questioned statute.

Schuylkill Trust Company v. Pennsylvania\(^90\) does push the doctrine of the immunity of federal instrumentalities from state taxation to an extreme, but anyone who knows the vagaries of decision in this field will not be unduly alarmed.

Grosjean v. American Press Company\(^91\) broke new ground when it held that a tax which abridges the freedom of the press transgresses the guaranties of due process. But the Court left the widest latitude for the future determination of the taxes which fall into this category.

Colgate v. Harvey\(^92\) read a new and hitherto unsuspected meaning into the privileges or immunities clause of the Fourteenth Amendment. However, that decision does not necessarily mean any great extension of judicial power. Tampering with "fundamental immunities" has hitherto been rectified under the due process clause. It is quite possible that in the future the Court will continue to prefer a due process rather than a privileges or immunities technique, and it is highly doubtful in any event, whether the newly discovered potencies in the privileges or immunities provision will add greatly to the sum total of judicial encroachment which has already been achieved in the name of due process.

Wheeling Steel Corporation v. Fox\(^93\) may entirely revolutionize the existing rules of jurisdiction to tax corporate intangibles. It is just as

\(^{86}\) See note 1, supra.
\(^{87}\) See note 2, supra.
\(^{88}\) See note 7, supra.
\(^{89}\) See note 8, supra.
\(^{90}\) See note 23, supra.
\(^{91}\) See note 31, supra.
\(^{92}\) See note 37, supra.
\(^{93}\) See note 40, supra.
likely, however, that it will finally be found to be just another precedent on the somewhat muddled subject of "business situs."

It is almost incredible that *Great Northern Railway v. Weeks*\(^4\) really stands for the broad proposition that an assessment which is too high violates due process. The vigorous attack of the minority coupled with the cautious language of the majority suggest that in the future course of decision, the *Great Northern* case will be found to possess a great number of individuating circumstances which will enable the court to confine the decision of the case very narrowly.

*Koshland v. Helvering*\(^5\) caused the gentlemen of the Department of Internal Revenue severe mental anguish, just as *Helvering v. City Bank Farmers Trust Company*\(^6\) was the spark that touched off wild revelry. But both the sorrow and the rejoicing of the minions of Government may prove premature. It is quite possible that the *Koshland* case will be found not to stand for any broad principle that income cannot constitutionally be applied to reduce capital basis, but simply for the prosaic proposition that less creative imagination is desirable in writing the regulations for the income tax. The *City Bank Farmers Trust Company* case does suggest a new and wise approach to the problem of tax avoidance, but there is still considerable latitude to knock out a tax avoiding tax under the constitutional prescription of that case.

The unhappiest expression in the lawyer's vocabulary from the point of view of clear and realistic thinking is the "Supreme Court." There is no reality paralleling this conception. There are the nine justices, but there is no objective reality apart from them, no collective mind which dictates their opinions. Judicial decisions are individual expressions of opinion which usually succeed in masking the precise identity of the individual whose opinion they express. Supreme Court cases are a compromise between nine very wise, somewhat disillusioned, always overworked, and lately angry old gentlemen. Supreme Court opinions are vulnerable from the viewpoint of logic and consistency because the Court does not get the easy questions. As a matter of necessity the lawyer must use the decisions of the Court as tentative premises in his legal syllogisms. But he must remember that they are only tentative, experimental propositions, subject to revision and rejection at the next term of the Court.

\(^{94}\) See note 43, *supra*.
\(^{95}\) See note 47, *supra*.
\(^{96}\) See note 71, *supra*. 