Constitutional Law—Taxation—Immunity of Federal Employees from State Income Taxation—[Federal].—The State of New York sued to collect an income tax levied by it upon the salary of an employee of the Home Owners Loan Corporation. *Held*, judgment for the State. Without deciding whether the HOLC is an essential activity of the federal government, the Court found that a tax on the income of employees is not a substantial burden upon a governmental activity. *Graves v. O'Keefe.*[1]

The instant case[2] is a significant step in the current reconsideration and restatement[3] of the tax immunity doctrine by means of which essential activities of the state governments are exempted from taxation by the national government, and activities of the national government are exempted from taxation by the states.[4] This implied limitation on the taxing power of both the state and national governments was originated by the Supreme Court in *McCulloch* v. *Maryland*[5] as an incident to the supremacy of federal legislation, and was extended some fifty years later in *Collector v. Day*[6] to preserve the sovereignty of the states at a time when it was threatened by a strengthened nationalism.[7] As the doctrine developed, the Court has distinguished between proprietary (non-essential) activity and governmental (essential) activity,[8] denying immunity to the former and exempting the latter from

[1] 59 S. Ct. 595 (1939).

[2] Expressly overruled by this decision is the line of cases including Dobbins v. Comm'n of Erie County, 41 U.S. 434 (1842); Collector v. Day, 11 Wall. (U.S.) 113 (1870); New York *ex rel.* Rogers v. Graves, 299 U.S. 401 (1936); and Brush v. Commissioner, 300 U.S. 352 (1936).

[3] This decision is a corollary to Helvering v. Gerhardt, 304 U.S. 405 (1938), which held that salaries of employees of the Port of New York Authority were taxable by the federal government since the burden of the tax upon the government of New York was merely speculative. See also James v. Dravo Contracting Co., 302 U.S. 134 (1937), and Helvering v. Mountain Producers Corp., 303 U.S. 376 (1938), overruling Gillespie v. Oklahoma, 257 U.S. 501 (1922) and Burnet v. Coronado Oil Co., 285 U.S. 393 (1932). See 5 Univ. Chi. L. Rev. 679 (1938).

[4] McCulloch v. Maryland, 4 Wheat. (U.S.) 316 (1819); Collector v. Day, 11 Wall. (U.S.) 113 (1871); Indian Motorcycle Co. v. United States, 283 U.S. 570 (1930).

[5] 4 Wheat. (U.S.) 315 (1819) (prohibiting the state of Maryland from levying a tax on notes of the Bank of the United States). The national government was deemed supreme in the sense that the part must not be allowed to govern the whole. A tax levied on the activities of the national government by a state is truly "taxation without representation." Mr. Justice Stone in Helvering v. Gerhardt, 304 U.S. 405, 412 (1938).

[6] 11 Wall. (U.S.) 113 (1871) (federal tax on income of a state judge held invalid).

[7] Collector v. Day has been much criticized. See, *e.g.*, the dissenting opinion in that case by Mr. Justice Bradley: "In my judgment, the limitation on the power of taxation in the general government which the present decision establishes, will be found very difficult of control. . . . . I cannot but regard it as founded on a fallacy, and that it will lead to mischievous consequences . . . . no concession of any of the just powers of the general government can easily be recalled." 11 Wall. (U.S.) 113, 129 (1871).

[8] The measure of an "essential" governmental activity is not a simple one. The confusion of the cases may be due to a conflict on the basic premise. One view holds that the concept is one of changing content, as expressed by Mr. Justice Black, concurring in the Gerhardt case, "There is not, and there cannot be, any unchanging line of demarcation between essential and nonessential governmental functions." Our form of government provides that the people have

"direct"[9] although not from "indirect" or "conjectural" burdens.[10] Since every immunity granted of necessity results in a deprivation of revenue to the taxing body, a denial to either government of the power to tax in order to safeguard "some remote antecedent benefit"[11] to the other would seem an unjust encroachment upon the sovereign power to tax. Inasmuch as the policy behind national immunity is the maintenance of national supremacy, and the policy behind state immunity is the prevention of interference with activity essential to the preservation of the state governments, the immunities are not, in the strict sense of the term, "reciprocal."[12]

The instant case, by its statement that the problem of "burden" is a question of fact, implicitly adopts Mr. Justice Brandeis' contention[13] that a distinction should be drawn between an interpretation or construction of the Constitution by the Court and the application of that construction to the particular case, the former being a question of law, the latter of fact.[14] Thus, the determination by the Court of a fact should be open to reconsideration at any time in view of the presence of new and more precise data, a new approach, or a change in general conditions. In addition the opinion follows a dual system of *stare decisis* also propounded by Mr. Justice Brandeis.[15] Strict adherence to

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the "power to determine as conditions demand, what services and functions the public welfare requires." On the other hand, Mr. Justice Stone, in the same case, contends that the concept is fixed and that the restriction on national taxing power was "devised as a shield to protect the states from curtailment of the essential operations of government which they have exercised *from the beginning*" (italics added). Cases are collected in 17 N.C. L. Rev. 62, 66 (1938).

[9] Pollock v. Farmers' Loan and Trust Co., 157 U.S. 429 (1895) (holding invalid a federal income tax on state and municipal bonds); Indian Motorcycle Co. v. United States, 283 U.S. 570 (1930) (federal excise tax on sale of motorcycles to police department of municipality prohibited).

[10] Metcalf and Eddy v. Mitchell, 269 U.S. 514 (1925) (upholding a federal tax on net income of consulting engineer for municipal works); Willcuts v. Bunn, 282 U.S. 216 (1931) (upholding a federal tax upon income derived from the sale of municipal and county lands); James v. Dravo Contracting Co., 302 U.S. 134 (1937) (wherein a state tax upon the gross income of an independent contractor engaged exclusively in federal construction was sustained).

[11] Language of Mr. Justice Stone, dissenting in Burnet v. Coronado Oil Co., 285 U.S. 393, 403 (1932).

[12] Chief Justice Marshall pointed out in the McCulloch case that there are certain political checks on national taxation of the states, but that a tax levied on national agencies by a state government is a tax levied without adequate representation. Although the court has intimated otherwise, it would seem that the test of "essential" function is inapplicable to the national government. By the very nature of the federal system of delegated powers in the national government, all activity is "necessary" that is constitutional. See notes 5, 6, and 8, *supra*.

[13] Dissenting in Burnet v. Coronado Oil Co., 285 U.S. 393, 412 (1932).

[14] Other examples given by Mr. Justice Brandeis of questions of fact: (1) in cases under the due process clause whether the legislation is unreasonable, arbitrary, or capricious, (2) in cases under the equal protection clause whether there is any reasonable basis for the classification made by the statute, (3) in cases under the commerce clause whether the admitted burden laid by the state statute is so substantial as to be deemed direct. The issue in these cases resembles the use and application of the reasonable man standard in torts.

[15] Note 13, *supra*.

precedent makes for the desirable end of certainty in the law, but also for rigidity. In the field of legislation, an undesirable precedent is readily remedied by statute; but a "wrong" interpretation of the Constitution, unless the Court is willing to overrule itself, requires the prolonged process of amendment for rectification. In controversies involving the interpretation of the Constitution, therefore, the Court should "bow to the lessons of experience[16] and the force of better reasoning."[17]

With the recognition of "burden" as a question of economic fact, the way is open for a reconsideration of the cases involving taxation of income from government bonds and allied problems.[18] As long as the tax is non-discriminatory and not direct[19] there seems to be little danger of "destruction" of essential activity.[20]

The scope of the decision is narrowed somewhat by the express reservation for later determination of the situation where Congress by legislation in terms has expressly exempted federal employees from income taxation by the states. In a footnote to the *Gerhardt* case[21] the Court intimated that such an exemption might be possible. It has been argued that the basis of the *McCulloch* case is the finding by the Court of an implied intent in Congress to declare the national bank notes exempt from state taxation.[22] However, since the instant case and the cases it overrules have never regarded the non-consent of the federal government as relevant (it impliedly being always present), the rationale of the possible immunity is difficult to see.[23] The present Congress, for obvious political reasons, has not seen fit to follow the suggestion of the

[16] Mr. Justice Brandeis probably uses the word advisedly in the sense of public opinion.

[17] Note 13, *supra*. *Cf.* Taney, C. J., in The Passenger Cases, 7 How. (U.S.) 282, 470 (1849): "I . . . . am quite willing that it be regarded hereafter as a law of this court, that its opinion upon the construction of the Constitution is always open to discussion when it is supposed to have been founded in error, and that its judicial authority should hereafter depend altogether on the force of the reasoning by which it is supported."

[18] Pollock v. Farmers' Loan and Trust Co., 157 U.S. 429 (1895). See discussion of the application of the Sixteenth Amendment by Mr. Justice Black, concurring, in Helvering v. Gerhardt, 304 U.S. 405, 427 (1938).

[19] Mr. Justice Roberts, dissenting, in Brush v. Commissioner, 300 U.S. 352, 375 (1936), observes that the reciprocal rights and immunities of the state and national governments may be adequately safeguarded by these two limitations on the taxing power. His statement that any additional exemption is unsound because state and federal business ought to bear their proportionate share of taxation "in order that comparison may be made between the cost of conducting public and private business" is interesting when applied to the contemporary controversy over the T.V.A. "yardstick."

[20] In his concurring opinion in the instant case, Mr. Justice Frankfurter traces the tax immunity confusion to the "seductive *cliché*" of Chief Justice Marshall in the McCulloch case that "the power to tax is the power to destroy." Mr. Justice Holmes, dissenting in Panhandle Oil Co. v. Knox, 277 U.S. 218, 223 (1928) introduced the modern view when he wrote, "The power to tax is not the power to destroy while this Court sits."

[21] 304 U.S. 405, 411 (1937).

[22] See opinion of Mr. Justice Stone in the instant case.

[23] Any exemption of salaries would probably be based upon the "necessary and proper" clause. It would have to contend with the statement by Hamilton in the Federalist, No. 33 that "a law for abrogating or preventing the collection of a tax laid by the authority of the State (unless upon imports and exports), would not be the supreme law of the land, but a usurpation of power not granted by the Constitution."

Court and to immunize federal employees by express legislation. With the way opened by the decisions in the *Gerhardt* case and the instant case, Congress has passed legislation to permit reciprocal income taxation by the federal and state governments.[24]

Taxation—Domicil—Interpleader of Rival Claimants to Inheritance Taxes—[Federal].—The state of Texas filed in the United States Supreme Court an original bill in the nature of interpleader[1] against three other states, asking a determination of the domicil of the decedent for the purpose of deciding which of the four states could impose death taxes upon the decedent's intangibles. The decedent's next-of-kin was joined as defendant. The total taxes claimed by the several states were in excess of the total net value of the estate. *Held* (Justices Frankfurter and Black dissenting), the Court has jurisdiction of the cause and the special master's finding that the decedent was domiciled in Massachusetts at the time of his death should be confirmed. *State of Texas v. State of Florida.*[2]

In the notable case of *First National Bank v. Maine*,[3] the Supreme Court established the rule that a state statute imposing death taxes upon intangibles of decedents not domiciled in the state infringes the Fourteenth Amendment.[4] Shortly thereafter, there arose in the *Dorrance* cases[5] the problem of the constitutionality of multiple taxation of the same intangible estate based upon conflicting determinations by state courts as to the place of the decedent's domicile. These cases, however, failed to settle the problem since the appeal to the United States Supreme Court from one of the state courts was dismissed on the ground that the federal question "was not properly presented to . . . . the Supreme Court of Pennsylvania,"[6] and a later action to enjoin the collection of the New Jersey tax was dismissed as contrary to the federal statute forbidding a stay of any proceedings in a state court.[7]

In *Worcester County Trust Co. v. Riley*[8] an executor filed a bill under the Federal Interpleader Act[9] joining tax officials of two states and seeking a determination of

[24] 33 Time No. 17, at 14 (1939).

[1] The Court said: "The essential of the bill in the nature of interpleader is that it calls upon the Court to exercise its jurisdiction to guard against the risks of loss from the prosecution in independent suits of rival claims where the plaintiff himself claims an interest in the property or fund which is subjected to the risk." State of Texas v. State of Florida, 59 S. Ct. 563, 568 (1939).

[2] 59 S. Ct. 563 (1939). [3] 284 U.S. 312 (1932).

[4] The rule grew out of the cases of Farmer's Loan and Trust Co. v. Minnesota, 280 U.S. 204 (1930) overruling Blackstone v. Miller, 188 U.S. 189 (1903); Baldwin v. Missouri, 281 U.S. 586 (1930); Beidler v. South Carolina Tax Comm'n, 282 U.S. 1 (1930); and has been followed in City Bank Farmers Trust Co. v. Schnader, 293 U.S. 112 (1934).

[5] See Dorrance's Estate, 309 Pa. 151, 163 Atl. 303 (1932) *cert. denied* Dorrance v. Pennsylvania, 287 U.S. 660 (1932); New Jersey v. Pennsylvania, 287 U.S. 580 (1933); *In re* Dorrance, 115 N.J. Eq. 268, 170 Atl. 601 (1934); *In re* Dorrance, 116 N.J. Eq. 204, 172 Atl. 503 (1934) aff'd Dorrance v. Thayer-Martin, 13 N.J. Misc. 168, 176 Atl. 902 (1935); Hill v. Martin, 296 U.S. 393 (1935).

[6] Dorrance v. Pennsylvania, 287 U.S. 660 (1932).

[7] Hill v. Martin, 296 U.S. 393 (1935).

[8] 302 U.S. 292 (1937). [9] 49 Stat. 1096 (1936), 28 U.S.C.A. § 41 (26) (Supp. 1938).