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# Taxation -- Discriminatory License Classifications - - Limitations of Equal Protection and Commerce Clauses

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the surety in executing an official bond is presumed to know the terms of the statute under which he executed the bond.<sup>17</sup>

In certain respects the case is unusual; it is a strong holding in that the statute specifically provided that the bond be "not more than \$15,000"; and it was decided on the basis of estoppel, which basis might be seriously questioned since it is difficult to see wherein the surety was estopped as to the state.

It is of especial interest to note that the case involved a summary proceeding under the statute. The summary remedy has been declared constitutional in North Carolina,<sup>18</sup> but its use has been denied where the penalty superseded the statute<sup>19</sup> as in the present case, the reason assigned by the court being that since the bond was not in conformity with the statute, it was not a statutory bond to which the summary remedy would apply. As there is no essential difference between the then existent statute on summary remedy<sup>20</sup> and the one now in force, the present case is apparently a direct reversal of the previous holding.

FRANK P. SPRUILL, JR.

#### Taxation—Discriminatory License Classifications—Limitations of Equal Protection and Commerce Clauses.

The 1931 General Assembly of North Carolina imposed a license tax of \$50 per truck upon persons, firms or corporations who sell fresh fish, fruits or vegetables and who do not maintain a permanent place of business in the State, but exempted persons, firms or cor-

<sup>17</sup> See *Fogarty v. Davis*, 305 Mo. 288, 264 S. W. 879; 880 (1929) (school contractor's bond); *Crawford v. Ozark Insurance Co.*, 97 Ark. 549, 134 S. W. 951, 952 (1911) (statutory bond); 9 C. J. 34, §56.

<sup>18</sup> Anonymous Case, 2 N. C. 29 (1794) (judgment against receivers of public monies); *Oats v. Darden*, 5 N. C. 500 (1810) (summary remedy against a sheriff); *Broughton v. Haywood*, 61 N. C. 380 (1867) (summary proceeding against sureties for Clerk and Master in Equity).

<sup>19</sup> *State Bank v. Twitty*; *Henderson v. Matlock*; *Governor v. Witherspoon*, all *supra* note 5.

<sup>20</sup> Acts of North Carolina Assembly of 1795, c. VIII, §5: "And be it further enacted that when any constable or constables in any county within this state shall or may have received any money in virtue of his office or appointment as constable, and shall fail to pay the same to the person or persons entitled to receive it, that then and in that case it shall and may be lawful upon motion made in the court of the county in which said constable resides for said court to give judgment against said constable or constables and his or their securities for all sum or sums of money so received and collected, together with costs, and to award execution thereon in the same manner as other executions issuing from said court, *provided*, such constable has ten days previous notice of such motion. . . ."

porations selling these products if they are grown in this State or the fresh fish taken in the waters of this State.<sup>1</sup> A specially constituted three-judge federal court declared the tax unconstitutional since it discriminates against the products of other states and so constitutes a burden upon interstate commerce.<sup>2</sup> It is surprising that, in face of many emphatic decisions enforcing this constitutional prohibition of State legislation discriminatory against other States' products, such legislation actuated by local interests and flagrantly violative of the commerce clause is still enacted. This tax which is so clearly discriminatory raises the question of discrimination in license taxes generally.

License classifications which discriminate against either products<sup>3</sup> of other States or residents<sup>4</sup> of other States are promptly condemned by the courts. The equal protection of laws and the equal privileges and immunities clauses which prohibit legislation aimed at non-resident persons have augmented the commerce clause to prevent the States from harassing each other with rival and spiteful measures. A State may tax the sale within its borders of produce brought from other States if the tax applies impartially to produce from within as well as from without the State,<sup>5</sup> and it may tax business within the State conducted by non-residents, but the tax must not be unlike that imposed upon business conducted by residents.<sup>6</sup>

When interstate commerce and non-resident considerations are not involved in the classification, the courts recognize considerable discretion in the legislature to classify business for license taxes. De-

<sup>1</sup> N. C. PUB. LAWS (1931) c. 427, §121½. "The Finance Committee several times rejected a tax proposal similar to this, but in the long, drawn-out session this modified section was enacted." Commissioner of Revenue A. J. Maxwell, U. S. Daily, Aug. 22, 1931, at 1430. Merchants in several South Carolina towns threatened to boycott North Carolina goods in protest against the tax.

<sup>2</sup> *Gramling v. Maxwell*, 52 F. (2d) 256 (W. D. N. C. 1931). Suit to enjoin the Revenue Commissioner from enforcing the act. Complainant operated trucks selling South Carolina peaches in North Carolina. A temporary restraining order was obtained from the District Judge and an interlocutory injunction granted by the three-judge court. No appeal was taken.

<sup>3</sup> *Welton v. Missouri*, 91 U. S. 275, 23 L. ed. 347 (1875); *Webber v. Virginia*, 103 U. S. 344, 26 L. ed. 565 (1880); *Walling v. Michigan*, 116 U. S. 446, 29 L. ed. 691 (1886). Nor may a tax discriminate against the products of the taxing State. *State v. Hoyt*, 71 Vt. 59, 42 Atl. 973 (1899).

<sup>4</sup> *Bethlehem Motors Co. v. Flynt*, 256 U. S. 421, 41 Sup. Ct. 571, 65 L. ed. 1029 (1921), reversing 178 N. C. 399, 100 S. E. 693 (1919).

<sup>5</sup> *Wagner v. City of Covington*, 251 U. S. 95, 40 Sup. Ct. 93, 64 L. ed. 157 (1919).

<sup>6</sup> *Chalker v. Birmingham and N. W. Ry. Co.*, 249 U. S. 522, 39 Sup. Ct. 366, 63 L. ed. 748 (1917).

cisions under the equal protection of laws clause require that persons who are similarly situated shall be similarly taxed.<sup>7</sup> Although the North Carolina constitutional provision for taxation by a uniform rule<sup>8</sup> applies expressly only to taxes on property,<sup>9</sup> the decisions have established the rule that a license tax not uniform upon persons in substantially the same situation is inconsistent with the intent so apparent in the provision and that its collection would be restrained as unconstitutional.<sup>10</sup> As such equality is guaranteed under the federal constitution, these decisions do not promulgate a new rule. The requirement of reasonable classification is satisfied when the court can conceive that the legislature could regard the classification as having a "connection with the duties of citizens as taxpayers."<sup>11</sup> Thus, differences in types of business, volume of business, opportunities afforded the business, or burdens which the business places upon government are held to afford reasonable bases for classification, whereas personal attributes would not justify classification. The differences may be minute; they are invalid only when they are palpably arbitrary.

This equality which the courts require may be termed "formal equality," for a classification is legal if there is a genuine difference in business organization. This difference may not actually be an economic justification for the dissimilar tax treatment which results. For example, it is legal to impose a license tax on hand laundries without imposing one on steam laundries.<sup>12</sup> The legislature may select a number of businesses for special taxes, and because those types of business are unlike others in external appearances they are legally subject to a tax not imposed on the others. In the 1931 Revenue Act license taxes are laid on piano dealers<sup>13</sup> and radio dealers,<sup>14</sup> while there is not a tax on furniture dealers; manufacturers

<sup>7</sup> See *Toyota v. Hawaii*, 226 U. S. 184, 33 Sup. Ct. 47, 57 L. ed. 180 (1912).

<sup>8</sup> N. C. CONST., Art. V, §3.

<sup>9</sup> *State v. Williams*, 158 N. C. 610, 73 S. E. 1000 (1912).

<sup>10</sup> *Gatlin v. Tarboro*, 78 N. C. 119 (1878); *Worth v. Petersburg Ry. Co.*, 89 N. C. 301 (1883); *State v. Carter*, 129 N. C. 560, 40 S. E. 11 (1901); *State v. Williams*, *supra* note 9; *Tea Company v. Doughton*, 196 N. C. 145, 144 S. E. 701 (1928).

<sup>11</sup> See *American Sugar Refining Co. v. Louisiana*, 179 U. S. 89, 21 Sup. Ct. 43, 45 L. ed. 102 (1900).

<sup>12</sup> *Quong Wing v. Kirkendall*, 223 U. S. 59, 32 Sup. Ct. 192, 56 L. ed. 192 (1912).

<sup>13</sup> N. C. PUB. LAWS (1931) c. 427, §147a.

<sup>14</sup> N. C. PUB. LAWS (1931) c. 427, §147d.

of ice cream<sup>15</sup> and of bottled drinks<sup>16</sup> are taxed, while other manufacturers are not; a tax is imposed on electricians, plumbers and gas-fitters,<sup>17</sup> but not on carpenters or brickmasons. Here is a departure from a natural interpretation of equality.

It appears that this system of taxes in North Carolina has developed from a few fees imposed in 1715 for regulation of "Ordinary Keepers and Tippling Houses," and in 1752 extended to "Traders, Peddlers and Petty Chapmen,"<sup>18</sup> with random and illogical additions to the present time. A license system framed judiciously would seem to have a valuable function in a revenue system. There is a group of occupations which the State desires to restrict, and to accomplish this it imposes a heavy tax upon them.<sup>19</sup> Again, there are enterprises in which State inspection is considered necessary, and a license fee can be imposed to defray this expense.<sup>20</sup> Also, where an occupation causes the State an extra expense not connected with inspection a license tax can be used for reimbursement.<sup>21</sup> License taxes can be utilized to correct inequalities in taxation. There are some enterprises which have very little taxable property but which nevertheless earn large profits, and the license tax is a way to offset this escape from other taxes.<sup>22</sup> These latter enterprises which cause extra expense or which escape other taxes present peculiar differences from other forms of business as taxpayers, and to require a special tax from them is not a departure from equality. The use of a license tax merely to curtail an undesired activity is a departure from actual equality, and it is a questionable use of the taxing power.

If there is to be more than a formal equality in license taxes, the system should be confined to enterprises with real differences of obli-

<sup>15</sup> N. C. PUB. LAWS (1931) c. 427, §161.

<sup>16</sup> N. C. PUB. LAWS (1931) c. 427, §134.

<sup>17</sup> N. C. PUB. LAWS (1931) c. 427, §155.

<sup>18</sup> PARKER, HISTORY OF TAXATION IN NORTH CAROLINA DURING THE COLONIAL PERIOD (1928) 129. CLARKE, LAWS OF NORTH CAROLINA, Vol. 23, p. 79, 371-375.

<sup>19</sup> Among these are phrenologists, fortune tellers, peddlers, employment agents, trading stamps. N. C. PUB. LAWS (1931) c. 427 §116, §124, §121, §154, §156.

<sup>20</sup> Licenses on hotels, restaurants, soda fountains and barber shops would come within this classification. N. C. PUB. LAWS (1931) c. 427, §126, §127, §144, §140.

<sup>21</sup> For example, a business which conducts frequent sales may place an extra burden upon the police; in like manner carnivals and circuses will cause extra expense. Heavy trucks cause greater injury to the roads than lighter motor vehicles, and the tax upon them is accordingly greater. N. C. PUB. LAWS (1931) c. 427, §165.

<sup>22</sup> Real estate agents, peddlers, traveling carnivals.

gation to the state, or, if business as such owes an extra obligation,<sup>23</sup> the tax should be on all business.

In addition to a lack of actual equality in classification the license system is subject to criticism as regards the measure of the tax on enterprises within the same formal classification. In effect, when the same tax applies to firms of diverse ability to pay this is a discrimination against the smaller firms. Some taxes are flat rates without regard to extent of activity;<sup>24</sup> others are graduated according to the population of the town in which the business operates,<sup>25</sup> which manifestly is an inaccurate gauge of ability; other licenses are measured by various external signs which may not be good criteria for the levying of taxes.<sup>26</sup> If the license tax is not imposed for revenue but for regulation, in which the ability principle is not an important consideration, the measure should be selected with regard to the purpose in view.

E. M. PERKINS.

### **Taxation—Exemption of Property Bought with Federal War Risk Insurance or Compensation Money.**

An act of congress<sup>1</sup> provides that the money payable to veterans of the World War shall be exempt from "all taxation." A later section<sup>2</sup> adds that "no sum payable under this chapter . . . shall be subject . . . to national or state taxation." Three state supreme

<sup>23</sup> T. S. Adams, *The Taxation of Business*, PROC. NAT. TAX ASSN. (1917) 185. "A large part of the cost of business is traceable to the necessity of maintaining a suitable environment." ". . . business ought to be taxed because it costs money to maintain a market and those costs should in some way be distributed over all the beneficiaries of that market."

<sup>24</sup> Of 131 license taxes in the 1931 Revenue Act, 37 are flat rates, 25 are measured according to population, and 69 have various measuring devices such as type and size of equipment used, gross receipts, persons accommodated, persons employed.

At first thought net income would seem to be the most equitable and efficacious measuring device. However, administrative difficulties of a tax measured by net income might prohibit such a device.

<sup>25</sup> Moving pictures, soda fountains, laundries, and automotive service stations are among those measured by population. N. C. PUB. LAWS (1931) c. 427, §105, §144, §150, §153. Obviously the individual enterprises within these groups are of diverse profitableness.

<sup>26</sup> Various measures have been sustained. *Gatlin v. Tarboro*, 78 N. C. 119 (1878) (volume of business); *State v. Stevenson*, 109 N. C. 730, 14 S. E. 385 (1891) (amount of purchases); *Cobb v. Commissioners*, 122 N. C. 307, 30 S. E. 338 (1898) (gross receipts); *State v. Carter*, 129 N. C. 560, 40 S. E. 11 (1901) (population); *Clark v. Maxwell*, 197 N. C. 604, 150 S. E. 190 (1929) (tonnage of trucks).

<sup>1</sup> 43 Stat. 613 (1924), 38 U. S. C. A. §454 (1928).

<sup>2</sup> 43 Stat. 125 (1924), 38 U. S. C. A. §618 (1928).