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Taxation—Ships, Boats and Watercraft—Application of Mileage Apportionment Doctrine

Taxation of ships, boats, and various watercraft has had some rather peculiar twists over the years. Steamships running between New York, New Orleans, Galveston, and Havana were allowed to be taxed by the state of Kentucky,[1] notwithstanding the fact that none had ever been in the state, nor ever were likely to be. This result was accomplished because none of the vessels had ever acquired a tax situs elsewhere, and Kentucky was the domicil of the owner. This has been the general rule, with the exception being the case where a vessel engaged in interstate commerce had acquired an actual situs in a state other than the place of the domicil of the owner;[2] and in order to have acquired a new tax situs other than the domicil of the owner, the vessels must have spent their time wholly within the new jurisdiction.[3] The rule, with the exception, has been applied to vessels trading in interstate commerce on the navigable rivers and waterways of the United States.[4]

Recently a new tax pattern affecting transportation on inland waterways was enunciated. The United States Supreme Court has decided that the principle of mileage apportionment heretofore used in taxing railroads or railroad cars[5] and telephone, telegraph and express companies[6] may be used to tax watercraft engaged in transportation on inland waters.[7]

The state of Louisiana and the city of New Orleans levied *ad valorem* taxes on tugs and barges belonging to foreign corporations engaged in carrying freight up and down the Mississippi and Ohio rivers, stopping only for unloading, reloading, and necessary repairs in New Orleans. Of the total time spent in interstate commerce for preceding years the amount spent by these vessels in Louisiana ranged from 2.2% to a maximum of 17.5%. The tax was apportioned on the ratio between the total number of miles of the corporations' lines in Louisiana to the total number of miles of the entire line. The Supreme Court reversed decisions of the district court[8] and the circuit court of appeals[9] whose

[1] Southern Pacific Co. v. Kentucky, 222 U. S. 63 (1911).

[2] Ayer & Lord Tie Co. v. Kentucky, 202 U. S. 409 (1905).

[3] Old Dominion S.S. Co. v. Virginia, 198 U. S. 299 (1905).

[4] Ayer & Lord Tie Co. v. Kentucky, 202 U. S. 409 (1905).

[5] Pullman's Palace-Car Co. v. Pennsylvania, 141 U. S. 18 (1890); Pittsburgh C. C. & St. L. R. Co. v. Backus, 154 U. S. 421 (1893). In addition to the mileage apportionment doctrine, the Supreme Court has held that railroad cars may be taxed according to the average number of cars which are found to be physically present within a state. Johnson Oil Refining Co. v. Oklahoma, 290 U. S. 158 (1943).

[6] Adams Express Co. v. Ohio State Auditor, 165 U. S. 194 (1896).

[7] Ott v. Mississippi Valley Barge Line, 69 S. Ct. 432 (1949).

[8] American Barge Line v. Cave, 69 F. Supp. 30 (E. D. La. 1946).

[9] Ott v. De Bardeleben Coal Corp., 166 F. 2d 509 (C. C. A. 5th 1948).

decisions that the tax was invalid under the due process clause of the 14th amendment were based upon the finding that the taxed boats and barges had never acquired a tax situs in Louisiana.

The rulings of the lower courts are bolstered by the argument in *Northwest Airlines, Inc. v. Minnesota*,[10] where Mr. Justice Frankfurter, speaking for the majority said: "But the doctrine of apportionment has neither in theory nor in practice been applied to tax units of interstate commerce visiting for fractional periods of the taxing year. . . . The continuous protection by a state other than the domiciliary state—that is, protection throughout the tax year—has furnished the constitutional basis for tax apportionment in these interstate commerce situations, and it is on that basis that the tax laws have been framed and administered."

The Supreme Court in the principal case distinguished the cases stating the general rule, saying the element of apportionment was not involved or considered in those earlier cases.[11] On the element of employment of the vessels in Louisiana for the whole of the taxable year, the court said it would not stop to resolve the question, as the Attorney-General for Louisiana stated in his brief that the Louisiana tax statute was intended to cover and actually covered an average portion of property permanently within the state, and by permanently was meant throughout the taxing year. Thus the decision overruled nothing, but it certainly makes available a new tax formula whereby states along an inland waterway may tax commerce which was heretofore taxable only at the owner's domicil or at an actual tax situs.

The meaning of the language used by the court, "an average portion of property permanently within the state," is not clear. It obviously cannot mean that in order for Louisiana to tax a tug or barge, that the tug or barge must be at all times within the borders of Louisiana. If a tug or barge remains in Louisiana throughout the taxing year, no problem arises, for automatically a tax situs in Louisiana is acquired,[12] and the state of Louisiana has full taxing power.

If the language means that Louisiana must determine the average number of vessels within the state in a given year, give that average

[10] 322 U. S. 292, 297 (1943). And again at page 298: "But no judicial restriction has been applied against the domiciliary state except when property (or a portion of fungible units) is permanently situated in a state other than the domiciliary state, and permanently means continuously throughout the year, not a fraction thereof, whether days or weeks. Such was the unanimous decision in the Miller case (N. Y. Central & H. R. R. Co. v. Miller, 202 U. S. 584 (1906)) or the Miller case decided nothing."

[11] Hays v. Pacific Mail S.S. Co., 17 How. 596 (1854); City of St. Louis v. Wiggins Ferry Co., 11 Wall. 423 (1870); Morgan v. Parham, 16 Wall. 471 (1872); Ayer & Lord Tie Co. v. Kentucky, 202 U. S. 409 (1905); Southern Pacific Co. v. Kentucky, 222 U. S. 63 (1911).

[12] Old Dominion S.S. Co. v. Virginia, 198 U. S. 299 (1905).

number a valuation, and then superimpose the mileage apportionment doctrine before determining the tax, the state is unduly restricted in the assessment valuation. It is the view of the writer that if the words of the court are construed literally, such an interpretation will result. However, the probable meaning is otherwise, and if interpreted with a common sense view, this decision permits a just apportionment of tax among states affected by inland water transportation. The court was not attempting to lay down any detailed formula for a tax system, but only the broad principle that inland water vessels engaged in interstate commerce may be taxed on the same basis as railroad cars.

The difficulty in applying this broad principle lies in the fact that while railroads operate on daily schedules, sending a large number of cars through a state on a day-to-day basis, tugs and barges are irregularly operated, and the number of units, if any at all, inside the borders of any given state at a particular time will vary widely. Consequently, the words *continuous protection* must either be omitted from expressions of the constitutional basis for tax apportionment referring to inland water commerce, or else be interpreted to mean continuous protection to the right to carry on business within a state.

In working out a tax method which will fit within the framework of this decision, one must consider first of all, that if vessels only incidentally and sporadically visit a port or ports within a state, that state cannot[13] and should not tax such vessels. Assuming a degree of regularity and continuity of visits, what is an equitable tax basis which allows a reasonable source of revenue to the state and which will not be a burden on commerce because of a cumulative effect of several states imposing such a tax? A logical and fair system, and one within a reasonable interpretation of this case, would be: (1) a determination of the value of all tugs and barges belonging to a company doing a regular business in a state, and then excepting from that valuation all tugs and barges used exclusively outside the state; (2) apply to the remaining valuation the fraction obtained by putting the total number of miles of the company's lines within the state over the total number of miles of the company's entire line;[14] (3) apply the appropriate property tax figure to the result.

For example, assume a company owns 20 tugs and 100 barges, whose total value is $1,000,000. Ten tugs and 50 barges never enter the state proposing to tax. If the tugs and barges never entering the state were one-half of the total value, then the taxing state has left $500,000 in step (1). If the tugs and barges run 100 miles into the

[13] Hays v. Pacific Mail S.S. Co., 17 How. 596 (1854).
[14] Or as an alternative, if the average number doctrine is used in a state as a tax basis, the mileage apportionment should be omitted.

state, and the total miles of their entire run is 500 miles, then a figure of 100 over 500, or 1 over 5 is the figure for step (2). Applying one-fifth to $500,000, the state has a valuation of $100,000 which it can tax. If the tax rate is one dollar on $100 valuation, then the tax to be assessed against the company results as $1,000 in step (3).

Since 1905, North Carolina has had a statute[15] providing for taxing of canal and steamboat companies in the same manner as provided for railroads, and so would seem to be in line with this latest decision of the United States Supreme Court on the point. No cases seem to have arisen under the North Carolina statute.

Only one North Carolina case dealing with the tax situs of boats has been found. In *Texas Co. v. Elizabeth City*[16] boats were employed by the Texas Co., a Delaware corporation, to haul oil products on North Carolina rivers and sounds and into Virginia. Elizabeth City was allowed by our court to levy an *ad valorem* tax on the boats on a finding by the jury in the lower court that for tax purposes the situs of the boats was in Elizabeth City. That this decision failed to square with prior federal decisions is pointed out in a prior note in this REVIEW.[17]

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Trusts—Charitable Bequests—Application of Cy Pres Doctrine

The testator, Ackland, willed the bulk of his fortune to his executors as trustees for the purpose of building and maintaining a memorial art museum on the campus of Duke University. Duke declined the "benefits, burdens and responsibilities" of the trust and the heirs sued the trustees, claiming the fortune resulted to them, but the trust was upheld by the invocation of the *cy pres* doctrine.[1] The court ordered the trustees to investigate to see whether the University of North Carolina or Rollins College or either of them should be selected as the new site.[2] The trustees, after two years of investigation, recommended North Carolina because of its similarity to Duke in size, financial status, location, cultural influence, faculty and curricula. The trial court, however, selected Rollins as the site because of evidence of its more prominent art department and Rollins' contention that the University of North

[15] N. C. GEN. STAT. §105-371 (1943).
[16] 210 N. C. 454, 187 S. E. 551 (1936).
[17] 15 N. C. L. REV. 217 (1937).

[1] Noel v. Olds, 138 F. 2d 581 (App. D. C. 1943), *cert. denied*, 321 U. S. 773 (1944). The court found that the testator's primary purpose was to benefit art education in the South. The fact that a previous will had named Duke, University of North Carolina and Rollins, in that order, tended to show that he had no special interest in Duke nor any intent to benefit it exclusively.

[2] See note 1 *supra*.