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DOUBLE TAXATION IN INCOME AND INHERITANCE TAXES

The "Due Process" clause of the Fourteenth Amendment of the United States Constitution, in so far as it controls substantive laws rather than procedure, requires such laws to be reasonable. The question then arises, what constitutes reasonableness? When can a state reasonably exercise taxing jurisdiction? *Union Refrigerator Transit Co. v. Kentucky*¹ answers the question by applying the benefit theory of taxation: where the taxpayer gets protection of his person and property, or the value of such property becomes greater, or he is benefited by the maintenance of public conveniences in which he shares, such as roads, bridges or schools, the state then has the power to tax. But if the taxing state is in no position to render these services or benefits to the person or his property taxed, and the property is wholly within the taxing power of another state to which it looks for protection, the taxing of such property is an extortion rather than a tax, and is a taking of property without due process of law. In other words, property which is wholly and exclusively within the jurisdiction of another state receives none of the protection for which the tax is supposed to be the compensation. Therefore, if the state is in no position to render benefits to the object taxed, the exaction is unreasonable and jurisdiction to tax does not exist.

The above standard is applied in determining the proper jurisdiction of all forms of taxation. In the case of real estate, the state in which the land lies is in a position to tax, for it can render protection and benefit to the real estate.² Likewise in taxing personalty, the state where the tangible personalty is permanently situated can tax, for that state gives protection to the property.³ The rule as to inheritance taxes for tangible property is the same as the rule for property taxes: the state where the property is located may tax, others may not.⁴

When we come to the question of income taxes, it is natural to feel that the recipient of the income gets the benefit of protection and enjoyment of the income from his domiciliary state, and therefore that state should be allowed to tax it. On the other hand, the state where the business is carried on, from which the income is derived, or the state where the property is located, may tax on the theory that it is rendering services to the income-producing property.

¹ 199 U.S. 194, 26 Sup. Ct. 36, 50 L.Ed. 150, 4 Ann. Cas. 493 (1905).

² *Paddell v. City of New York*, 211 U.S. 446, 29 Sup. Ct. 139, 53 L.Ed. 275, 15 Ann. Cas. 187 (1908).

³ *Old Dominion Steamship Co. v. Virginia*, 198 U.S. 299, 25 Sup. Ct. 686, 49 L.Ed. 1059 (1905).

⁴ *Frick v. Pennsylvania*, 268 U.S. 473, 45 Sup. Ct. 603, 69 L.Ed. 1058, 42 A.L.R. 316 (1925).

The courts have recognized the taxing jurisdiction of both the domiciliary state and that in which the business is located. *Shaeffer v. Carter*⁵ holds that part of the income of a non-resident which was derived from oil lands owned and operated within its boundaries was taxable in Oklahoma, the state where the property was located. *Maguire v. Trefry*⁶ permitted a tax on income received by one of its residents as the beneficiary of a trust of intangibles, created and administered in another state, because the resident receives benefits with regard to the income, from his domiciliary state. The income from a trust is to be distinguished from the equitable interest in a trust which can not be taxed in a domiciliary state if the object of the trust is in another state.⁷ It has also been held that a state might tax the income of a resident although such income was earned in a business conducted outside of the state.⁸ It is reasonable to conclude from the latter case that the decision would not be otherwise, if the state in which the business was located also taxed the income, derived from that business, thus allowing multiple taxation which would approach double taxation.

In a recent case, *New York ex rel. Cohn v. Graves*,⁹ the taxpayer, a resident of New York, owned real estate in New Jersey from which she received rents as part of her income. New York taxed her entire income and she was denied a refund of the tax on the portion which was attributable to the rents from the New Jersey real estate. The court here denies any double taxation, making a distinction between a tax on the land and a tax on income from land, but no reference is made to the possibility of both states taxing the income. The argument is set forth that a state cannot tax real property beyond its bounds, and that a tax on income derived from the real property is a tax on the real property itself. It follows that if a state taxes the income from real property beyond its jurisdiction, it is really taxing the property, which it cannot do according to an accepted interpretation of the Fourteenth Amendment. *Pollack v. Farmers Loan & Trust Co.*¹⁰ is cited as authority for the proposition that a tax on income from real estate is a tax on the real estate. The court denied that the *Pollack v. Farmers Loan & Trust Co.*¹¹ case so held, but rather held that for purposes of apportionment such a tax is a "direct tax," and it did not say it is a tax on the real estate.

⁵ 252 U.S. 37, 40 Sup. Ct. 221, 64 L.Ed. 445 (1920).

⁶ 253 U.S. 12, 40 Sup. Ct. 417, 64 L.Ed. 739 (1920).

⁷ *Safe Deposit & Trust Co. v. Virginia*, 280 U.S. 83, 50 Sup. Ct. 59, 74 L.Ed. 180, 67 A.L.R. 386 (1929).

⁸ *Lawrence v. State Tax Comm.*, 286 U.S. 276, 52 Sup. Ct. 556, 76 L.Ed. 1102, 87 A.L.R. 374 (1932).

⁹ 300 U.S. 308, 57 Sup. Ct. 466, 81 L.Ed. 668 (1937).

¹⁰ 157 U.S. 429, 15 Sup. Ct. 673, 39 L.Ed. 759 (1895).

¹¹ *Ibid.*

The issue as to whether double taxation will be tolerated was brought squarely before the court in the case of *Guaranty Trust Co. of New York v. Virginia*.¹² There was an imposition of an income tax under a Virginia statute on income received by a resident of Virginia as beneficiary of a discretionary trust established in New York, notwithstanding the fact that the trustees had been required to pay a tax on the income in New York under New York statutes. It was argued that the tax was upon the same income and would amount to double taxation and infringe the due process clause. Many of the cases cited in this discussion were used to support that proposition. The court says: "that those cases go on the theory that the taxing power of a state is restricted to her confines and may not be exercised in respect of subjects beyond them. Here, the thing taxed was receipt of income within Virginia by a citizen residing there. The mere fact that another state lawfully taxed funds from which the payments were made did not necessarily destroy Virginia's right to tax something done within her borders." The court cites *Lawrence v. State Tax Commission*¹³ and *New York ex rel. Cohn v. Graves*¹⁴ as authority and says there is no distinction between the cases. The court apparently tolerates what seems to be a double tax in income taxation.

As to the question of double taxation in inheritance taxes, two cases that have recently been decided seem to weaken the rule set down in *Farmers Loan & Trust Co. v. Minnesota*¹⁵ in which the court held that double taxation would not be tolerated in inheritance tax cases. A debtor and a creditor state attempted to tax intangible property, and the court held that only the creditor state, or the domicile of the owner of the intangibles, could impose the tax. We now have two recent decisions that hold that more than one state may levy inheritance taxes. These decisions, of course, should be interpreted only with reference to the fact-situations involved, although they give an indication of the leanings of the court in any future double taxation questions.

In *Curry v. McCanless*,¹⁶ both Alabama and Tennessee were allowed to impose death taxes upon the transfer of an interest in intangibles which were held in trust by an Alabama trustee but passing under the will of a deceased beneficiary domiciled in Tennessee. The decedent reserved control of the trust during her life and power to revoke it by will, which was not exercised. The court held that both the state in which the trustee and trust are located and the state of the domicile of the settlor may impose an inheritance tax. Four justices dissented.

¹² 305 U.S. 19, 59 Sup. Ct. 1, 83 L.Ed. 16 (1938).

¹³ *Supra*, note 11.

¹⁴ *Supra*, note 9.

¹⁵ 280 U.S. 204, 50 Sup. Ct. 98, 74 L.Ed. 371, 65 A.L.R. 1000 (1930).

¹⁶ 307 U.S. 357, 59 Sup. Ct. 900, 83 L.Ed. 1339 (1939).

The court denies that authority requires the acceptance of the rule that the Fourteenth Amendment precludes the taxation of any interest in the same intangible in more than one state. The court states that when the taxpayer extends his activities with respect to his intangible so as to avail himself of the protection and benefit of the laws of two states, and his person or property is within reach of the taxing authorities, the reason for a single place of taxation no longer holds. The dissenting opinion has the statement that legal title was in the trustee, and only the state of the trustee has jurisdiction to tax.

In the companion case, *Graves v. Elliot*,¹⁷ the same property is subjected to an inheritance tax by two states, as above. Decedent created a trust in Colorado. She reserved the power of revocation, but died without having exercised such power. Prior to her death, the decedent established a domicile in New York, while the trust continued to remain in Colorado. Both New York and Colorado were allowed to tax, the court basing its ruling on the reasoning in *Curry v. McCanness*.¹⁸ In the dissenting opinion it was contended that there was an effective localization of the intangibles in Colorado, and that the trustee held legal title to such intangibles. The dissenting justices feel that only Colorado should tax, and the principle of *Mobilia sequuntur personam* must yield to the established fact of legal ownership. The argument made in the majority of opinions of *Curry v. McCanness*¹⁹ and *Graves v. Elliot*²⁰ seems applicable to the dissenting opinion of *Blodget v. Silberman*²¹ and moves in the direction of implying the allowance of double taxation as in *Blackstone v. Miller*,²² which case *Blodget v. Silberman*²³ overruled.

The consideration of the cases wherein the right of several states to impose income and inheritance taxes on the same object has been determined reveals a definite tendency of the modern courts. A change of ideas has taken place, possibly corresponding to the change of personnel in the United States Supreme Court. That tendency and change in principles are toward judicial acknowledgment of the right of several states to impose income and inheritance taxes on the same object. This is an indication that the liberal viewpoint of the courts is encroaching upon the doctrine of double taxation.

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¹⁷ 307 U.S. 384, 59 Sup. Ct. 913, 83 L.Ed. 1359 (1939).

¹⁸ *Supra*, note 16.

¹⁹ *Ibid.*

²⁰ *Supra*, note 17.

²¹ 277 U.S. 1, 48 Sup. Ct. 410, 72 L.Ed. 749 (1928).

²² 188 U.S. 189, 23 Sup. Ct. 277, 47 L.Ed. 439 (1903).

²³ *Supra*, note 21.