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Clark J.A. Hazelwood, *Full Faith and credit Clause as Applied to Enforcement of Tax Judgments*, 19 Marq. L. Rev. 10 (1934).
Available at: <http://scholarship.law.marquette.edu/mulr/vol19/iss1/2>

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FULL FAITH AND CREDIT CLAUSE AS APPLIED TO ENFORCEMENT OF TAX JUDGMENTS

CLARK J. A. HAZELWOOD

RECENTLY it was discovered by the Wisconsin Tax Commission that a corporation located in Chicago, Illinois, but licensed to conduct business in Wisconsin, had earned enormous profits during a short period of operation in Wisconsin, had then withdrawn from this state all its property and business, leaving behind an indebtedness to the state, county, and city, wherein its business had been carried on, in the sum of approximately \$50,000.00 for state income taxes.

The legal departments of the county and state determined to enforce payment of this substantial claim, but their initial efforts have been curtailed by a decision of the United States District Court of the Northern District of Illinois, in *Milwaukee County v. M. E. White Company, a corporation*.¹ The case is now pending upon an appeal to the United States Circuit Court of Appeals.

The question of law presented therein is of considerable interest to tax collecting authorities of many of the states. A discussion on the subject was recently held at the conference of Attorneys General at the Milwaukee meeting of the American Bar Association.

The issue can be observed by reviewing the proceedings taken in the White Company case. After the tax assessment was determined by the Tax Commission and due notice thereof was given to the tax debtor, and after the tax debtor failed to take an appeal from the Commission's determination of the amount of the assessment and the time for appeal by the debtor to the Wisconsin courts had expired, an action against the M. E. White Company was filed in the Milwaukee County Circuit Court, jurisdiction having been obtained by the service of process within the State of Wisconsin.

The debtor company failed to defend this suit. Milwaukee County, as plaintiff in said action on behalf of the state, city, and county, was awarded a default judgment, the same being duly entered and docketed in the Circuit Court of Milwaukee County. The judgment still remains of record and no attempt has been made to disturb it.

The suit in the District Court was commenced upon a complaint asking for a judgment against M. E. White Company of Chicago, based upon the judgment of the Wisconsin Circuit Court. The court was asked to enforce this Wisconsin judgment, the plaintiff relying upon the so-called "Full Faith and Credit" provision of the United States

¹ --- F. Supp. --- (1934).

Constitution.² Under the powers invested in it by this Section, Congress in 1790 provided for the authentication of records and judicial proceedings of the courts of the States, and prescribed the effect of such authenticated record.³

Since the Wisconsin judgment which formed the basis of the action was properly authenticated and exemplified in the manner prescribed by the Act of Congress above cited, it becomes material to inquire what limitations or restrictions, if any, are or should be imposed upon the apparently universal and all-embracing requirement that "full faith and credit" be given to judgments of sister states.

In *National Surety Co. v. Milligan*,⁴ the court said, in touching upon this point:

"The only defenses that can be made to a judgment obtained in another state, when sued upon here, are that the court of our sister state did not have jurisdiction of the person or of the subject-matter; that it was fraudulently procured, or had been paid."⁵

As a corollary to the rule that judgments of sister states can be attacked only on the three grounds above stated, namely (1) lack of jurisdiction in the original state court where the judgment was entered, (2) fraudulent procurement or (3) payment, it has been generally held that the merits or validity of the claim upon which the judgment is founded cannot be re-examined in the court of the sister state.⁶

But the District Court in the White Company case apparently holds that there is a fourth ground on which the judgment of a court of a sister state can be successfully attacked, namely that where the demand

² U.S. Const. Art. IV, Section 1.

³ Act of May 26, 1790, ch. 11; 28 U.S.C.A. § 687 (1926), providing,

"The acts of the legislature of any State or Territory, or of any country subject to the jurisdiction of the United States, shall be authenticated by having the seals of such State, Territory, or country affixed thereto. The records and judicial proceedings of the courts of any State or Territory, or of any such country, shall be proved or admitted in any other court within the United States, by the attestation of the clerk, and the seal of the court annexed, if there be a seal, together with a certificate of the judge, chief justice or presiding magistrate, that the said attestation is in due form and the said records and judicial proceedings, so authenticated, shall have such faith and credit given to them in every court within the United States as they have by law or usage in the court of the State from which they are taken."

⁴ 105 N.J.L. 336, 341, 146 Atl. 372 (1929).

⁵ See, *Mutual Life Ins. Co. v. Harris*, 97 U.S. 331, 335, 24 L.Ed. 959 (1877); *Christmas v. Russell*, 5 Wall. 290, 302, 18 L.Ed. 475 (1866).

⁶ *Christmas v. Russell*, 5 Wall. 290, 302, 18 L.Ed. 475 (1866); *Thompson v. Whitman*, 18 Wall. 457, 461, 21 L.Ed. 897 (1873); *Knowles v. Longsport Gas & Coke Co.*, 19 Wall. 58, 60, 22 L.Ed. 70 (1873); *Hanley v. Donaghue*, 116 U.S. 1, 6 Sup. Ct. 242, 29 L. Ed. 535 (1885); *Renaud v. Abbott*, 116 U.S. 277, 297, 6 Sup. Ct. 1194, 29 L.Ed. 629 (1886); *Huntington v. Attrill*, 146 U.S. 657, 666, 13 Sup. Ct. 224, 36 L.Ed. 1123 (1892); *Faunileroy v. Lum*, 210 U.S. 230, 236, 28 Sup. Ct. 641, 52 L.Ed. 1039 (1908); *Kennedy v. Supreme Lodge*, 252 U.S. 411, 415, 40 Sup. Ct. 371, 64 L.Ed. 638 (1920); *Roche v. McDonald*, 275 U.S. 449, 48 Sup. Ct. 142, 72 L.Ed. 365 (1928).

is by a sister state itself, or a political subdivision thereof, and where it is revealed that the original demand in the court of the sister state was on a cause of action created by the law of said state as a method of furthering its own governmental interests, by taxation or otherwise, such revelation is fatal to the plaintiff's reliance upon the "full faith and credit" clause.

It is reasoned that since the "full faith and credit" clause cannot be extended to cover such cases as the claim against the White Company, the suit must then fall under the rule barring original suits for tax claims outside of the state which imposes the taxes. Where, for example, John Doe owes the State of Wisconsin \$500.00 for income taxes, although he can be sued in Wisconsin for the \$500.00, if he has moved to Illinois, no Illinois court and hence no federal court in Illinois will entertain an original suit against him. This doctrine is upheld, apparently, upon the reasoning that a state is more than sufficiently occupied in the enforcement of its own revenue laws, without being called up to assist in the enforcement of the revenue laws of a sister state. This doctrine arises from ancient rules barring the courts of one country to the revenue agencies of another. It is difficult to see why, with respect to tax laws, states of this Union should be regarded as separate nations.

It is difficult to see why a tax indebtedness owing to any state in the Union should not be considered in courts of other states to be a debt with as high standing as any other indebtedness owing to citizens and residents of sister states. In other words, while Wisconsin is barred from the use of Illinois courts for tax suits, an individual from anywhere can enter the Illinois courts and sue to collect his just debts.

Yet a tax indebtedness is no less an obligation with a quid pro quo than other debts. Persons assessed with taxes have received the protection of the state government. The tax is the price they are called upon to pay for that protection.

There is cooperation between states in the enforcement of criminal laws through extradition. It seems that a similar spirit is needed in the matter of revenue laws.

Yet there is a line of decisions barring suits by taxing authorities of one state in sister states, regardless of the merits of the claims.⁷ The

⁷ *Moore v. Mitchell*, 30 F. (2d) 600 (C.C.A., 2d, 1929), 65 A.L.R. 1352; affirmed on other grounds by the United States Supreme Court, 281 U.S. 18, 50 Sup. Ct. 175, 74 L.Ed. 673 (1930); *Colorado v. Harbeck*, 232 N.Y. 71, 133 N.E. 357 (1921); *In the matter of Bliss*, 202 N.Y.S. 185 (1923); *State of Maryland v. Turner*, 132 N.Y.S. 173 (1911); *Estate of Martin*, 240 N.Y.S. 393 (1930); *N. Y. Trust Co. v. Island Oil & Transport Corp.*, 11 F. (2d) 698 (C.C.A., 2d, 1926); *Municipal Council of Sidney v. Bull*, [1909] 1 K.B. 7; and cases collected in Note, 65 A.L.R. 1360.

rule of these cases however has not been directly affirmed by the United States Supreme Court.

But this has been a digression from the main issue, namely that, assuming the rule of the Harbeck⁸ and similar cases to be the law, is not a sovereign state or subdivision thereof entitled to the benefit of the "full faith and credit" clause after its tax claim has been reduced to judgment?

Formulators of the Restatement of the Law on Conflict of Laws,⁹ have prepared the following statement:

"ACTION ON JUDGMENT ON GOVERNMENT CLAIM. No action can be maintained on a foreign judgment which has been obtained in favor of a state, a state agency, or a private person on a cause of action created by the law of the foreign state as a method of furthering its own governmental interests."

The following was added to the above statement in June, 1934:

"*Comment:*

"The rule stated in this Section is not applicable to a judgment upon a claim for payment for a privilege given or service rendered by the state for a price.

"*Illustration:*

"A, a foreign corporation, applies for permission to do local business in State X. Permission is granted by X on terms, among others, that a certain fee be paid by A. A fails to pay the fee. X sues A and secures a judgment for the amount of the fee. X may sue A in Y upon the judgment and may recover thereon."

The addition of the above comment was made by the committee after their attention was called to the case of *People v. Coe Manufacturing Company*.¹⁰ The court, in that case, held that the state of New York might bring an action in a New Jersey court on a New York judgment obtained for taxes imposed by a New York statute. In his very illuminating opinion in the New Jersey Supreme Court case, Judge Caffrey pointed out,¹¹

"Of course, if this were an original suit for the collection of taxes due to the state of New York, the plaintiff would be without relief, because the principle is well settled, without the need of citation, that the courts of one state will not enforce a claim for taxes as such in any other jurisdiction than that in which the taxes are due. *Colorado v. Harbeck*, 232 N.Y. 71, 133 N.E. 357.

"*As I view this matter, the suit in this court is not for the collection of taxes, but for the collection of a judgment which is based on a tax*

⁸ *Colorado v. Harbeck*, 232 N.Y. 71, 133 N.E. 357 (1921).

⁹ Draft 34 (Oct. 16, 1930) Sec. 621.

¹⁰ 10 N.J. Misc. 116, 162 Atl. 872 (1932), [affirmed in 172 Atl. 198 (1934)].

¹¹ 10 N.J. Misc. 116, 162 Atl. 872, 873 (1932).

claim, and the original character of the claim has been merged in the judgment. In so holding I am not unmindful of *Huntington v. Attrill*, 146 U.S. 657, 13 S.Ct. 224, 36 L.Ed. 1123, nor *Wisconsin v. Pelican Insurance Company*, 127 U.S. 265, 8 S.Ct. 1370, 32 L.Ed. 239." (Italics ours.)

The New Jersey Supreme Court thus makes a distinction between an action brought by one state in the courts of another state to enforce a claim for taxes as such and an action brought on a judgment obtained for taxes.

The New Jersey Court of Errors and Appeals, being the highest court of that state, on the appeal of the *Coe* case, affirmed the same in all respects on April 12, 1934,¹² and it was stated by Judge Lloyd, who delivered the opinion of that court that:

"The right of the state of New York to exclude corporations of other states cannot be open to question, and its right to admit such corporations for the transaction of business within its borders upon such terms as it deems wise is likewise not open to question. When, therefore, as a privilege of transacting its business therein the state exacted for that privilege a franchise tax or sum of money proportioned to the earning power of the corporation, it was wholly within its rights. *Bass, Ratcliff & Gretton v. State Tax Commission*, 266 U.S. 271. It was then optional with the corporation to avail itself of the privilege accorded or to refrain from doing so. When it did avail itself of the opportunity thus afforded it did so under the implied obligation that it would comply with the conditions upon which it was permitted to enter.

"Its own action carried with it, under the interpretation as given to the statute by the courts of that state (binding here) the obligation to personally see that the license fees or franchise taxes were paid. It could not accept the benefits without incurring the burdens. It is true the statute imposed certain penalties for failure to comply with the obligation thus assumed, but these were nothing more than the obligation frequently imposed in ordinary contracts between individuals and became as it were liquidated damages for the breach.

"The state of New York, having in its own court recovered judgment against the appellant, (the appellant having been personally served and present therein), jurisdiction of the person was obtained. When it was there determined that the statute imposed a personal liability upon the corporation it was the construction by the court of that state of its own laws. Having been so determined the appellant was concluded on those two phases of the litigation and could not thereafter deny jurisdiction either of the subject matter or of the person; nor could it assert another interpretation of the act.

"Our added view is that even though the door to contend that the statute creates penalties which may not be enforced outside the state of New York be open to the appellant in this state, (which may be de-

¹² (N.J. Errors & Apps., 1934) 172 Atl. 198.

batable) the action was not to collect such penalty, but to collect a debt which the appellant had impliedly agreed to pay.

"If such claims as are here presented were not enforceable against foreign corporations wherever found, the states of the Union would be subject to grave wrongs from without, inasmuch as corporations establish important connections in states other than those of their incorporation, and transact large business therein without the investment of a dollar or the placing of tangible property within their borders whereby redress may be had against corporations in default."

Thus the decision of the District Court in the *White Company* case is in almost direct conflict with the above quoted New Jersey decision.

An examination of authorities and text-writers shows that the odds should be in favor of a reversal of the *White Company* case when and if the same reaches the United States Supreme Court.¹³

In general the courts in refusing to enforce revenue claims arising in other states rely merely upon the reiteration of the rule "that one state does not enforce the revenue laws of another."¹⁴ The reasons (additional burden placed upon the courts, difficulty in making an assessment in conformity with the complex foreign statutes and the fact that the nature of the tax might be inconsistent with established local policy) for refusing to entertain a foreign tax suit are not applicable where the tax claim has been reduced to judgment, as the local court would have to consider only matters of jurisdiction or collateral defenses which might be raised in the taxing state.¹⁵ Some courts have advanced so far as to recognize penal judgments of sister states under the "full faith and credit" clause, to allow claims by another state for accrued and unpaid corporate franchise taxes, and in the case of executors, administrators and corporate receivers seeking reimbursement for payment of foreign taxes, to recognize foreign revenue laws.¹⁶ The difficulty of enforcing judgments is increased by the present concentration of wealth in the form of easily transportable intangibles.¹⁷ Corporations having their property located and business conducted in other states than the one in which incorporated, can in most cases escape satisfaction of judgments for its franchise tax.¹⁸ Where pernicious results flow from the application of an arbitrary rule to situations where the reason for the rule does not apply, it is reasonable to presume

¹³ Comment (1933) 42 Yale L. J. 1131; Note and Comment (1933) 18 Cornell L. Q. 581; Note (1929) 29 Columbia L. Rev. 782; Leflar, *Extrastate Enforcement of Penal Governmental Claims*, (1932) 46 Harv. L. Rev. 193.

¹⁴ Note and Comment (1933) 18 Cornell L. Q. 584.

¹⁵ Comment (1933) 42 Yale L. J. 1131.

¹⁶ Note (1929) 29 Col. L. Rev. 782, 790-791.

¹⁷ Comment (1933) 42 Yale L. J. 1131.

¹⁸ Leflar, *Extrastate Enforcement of Penal Government Claims*, (1932) 46 Harv. L. Rev. 193, 215.

that the United States Supreme Court will hold that a revenue judgment must be given "full faith and credit."

In support of the claim that the constitutional mandate as to "full faith and credit" ought not apply to suits on tax judgments, much reliance is placed on *Wisconsin v. Pelican Insurance Co.*¹⁹ In that case a Wisconsin statute imposed a penalty of \$500.00 a month upon any fire insurance company which transacted business in the state without depositing with the commissioner of insurance an annual statement of its business and property. The state of Wisconsin in a Wisconsin court sued a fire insurance company of Louisiana which was doing business in Wisconsin, alleged a violation of the statute and demanded the penalties provided thereunder. A judgment was rendered and the state then instituted an original action thereon against the defendant in the United States Supreme Court. The defendant pleaded that the judgment was founded upon a punitive and penal claim, and that the original jurisdiction of the United States Supreme Court extended only to controversies of a civil nature. This contention was sustained by the court and judgment was entered for the defendant. It is apparent that the actual decision in this case went no further than to hold that the United States Supreme Court had no original jurisdiction of a suit brought by a state upon a judgment for a penal claim, and the construction of Art. III, Sec. 2 of the United States Constitution, relating to the original jurisdiction of the Supreme Court, was alone involved. However, the court discussed the application of the "full faith and credit" clause, and made various statements, such as that "the courts of no country execute the penal laws of another" and that this rule applied "to all suits in favor of the state for the recovery of pecuniary penalties for any violation of statutes for the protection of its revenue * * * and to all judgments for such penalties."

Giving these statements their full weight, although they appear to be only dicta in the case, it will be noted that the cause of action in the Pelican case was not the same as a tax claim. It was a "pecuniary penalty" or punishment for doing a prohibited deed. A tax, on the other hand, is, in the writer's opinion, a debt of a higher nature than the obligation to pay a forfeiture. But the Pelican case, so far as it might apply to the issue here discussed, has been revised in later United States Supreme Court decisions in such a way as to eliminate it as authority upon the applicability of the "full faith and credit" provision of the Federal Constitution.

In *Huntington v. Attrill*²⁰ a New York statute was involved which imposed liability upon officers and directors of a New York corpora-

¹⁹ 127 U.S. 265, 8 Sup. Ct. 1370, 32 L.Ed. 239 (1888).

²⁰ 146 U.S. 657, 13 Sup. Ct. 224, 36 L.Ed. 1123 (1892).

tion for all debts of the corporation, if they made and filed any false certificate. The defendant, a director of a New York corporation, signed and recorded a certificate which falsely stated that all the capital stock of the company had been paid in. The plaintiff, a creditor of the company, sued the defendant in New York under the New York statute and secured a judgment. The plaintiff then brought a bill in equity in Maryland, setting up the New York judgment and seeking to set aside an alleged fraudulent transfer of property by the defendant to another. The Maryland court dismissed the bill on the ground that since the New York judgment was based upon a penalty it was not entitled to enforcement in the courts of another state. The United States Supreme Court *reversed* the decision of the state court and held that the judgment was entitled to full faith and credit.

Mr. Justice Gray also rendered the opinion of the court in this case, and stated that the doctrine enunciated in *Wisconsin v. Pelican Insurance Co.*, applied only to claims which were "penal in the international sense," the test being whether or not the law was one which imposed "punishment for an offense committed against the state, and which the executive of the state has the power to pardon."

The action involved in *Huntington v. Attrill* was held not to fall within the said defense, because although penal in a sense, it was, nevertheless, not a criminal or *quasi*-criminal law. It was penal in imposing a burdensome liability on the officers for their unlawful act, but it gave a civil remedy in which recovery was measured by the amount of the debt due to the creditor, and in this sense was clearly remedial. A judgment upon such claim was, therefore, held to be entitled to full faith and credit in the courts of sister states.

In *Fauntleroy v. Lum*²¹ the plaintiff and the defendant entered into a gambling transaction in Mississippi involving cotton futures. This transaction was void under the law of Mississippi. A controversy thereafter arising over a loss was submitted to arbitration in Missouri, and an award was rendered for the plaintiff. The plaintiff brought suit on this award in Missouri and recovered a judgment. The plaintiff then sued upon this judgment, in Mississippi. The court gave judgment for the defendant, on the ground that the original cause of action arose in Mississippi, by whose law it was illegal and against public policy. The Supreme Court of the United States reversed the judgment of the state court. Mr. Justice Holmes, in delivering the opinion of the court, said (at page 236) :

" * * * We proceed at once to the further question, whether the illegality of the original cause of action in Mississippi can be relied upon there as a ground for denying a recovery upon a judgment of another state.

²¹ 210 U.S. 230, 28 Sup. Ct. 641, 52 L.Ed. 1039 (1908).

"The doctrine laid down by Chief Justice Marshall was 'that the judgment of a state court should have the same credit, validity, and effect in every other court in the United States which it had in the state where it was pronounced, and that whatever pleas would be good to a suit thereon in such state, and none others, could be pleaded in any other court in the United States.' *Hampton v. M'Connel*, 3 Wheat. 234, 4 L.Ed. 378. There is no doubt that this quotation was supposed to be an accurate statement of the law as late as *Christmas v. Russell*, 5 Wall. 290, 18 L.Ed. 475, where an attempt of Mississippi, by statute, to go behind judgments recovered in other states, was declared void, and it was held that such judgments could not be impeached even for fraud.

"But the law is supposed to have been changed by the decision in *Wisconsin v. Pelican Ins. Co.*, 127 U.S. 265, 32 L.Ed. 239, 8 Sup. Ct. Rep. 1370. That was a suit brought in this court by the state of Wisconsin upon a Wisconsin judgment against a foreign corporation. The judgment was for a fine or penalty imposed by the Wisconsin statutes upon such corporations doing business in the state and failing to make certain returns, and the ground of decision was that the jurisdiction given to this court by Art. 3, Sec. 2, as rightly interpreted by the judiciary act, now Rev. Stat. Sec. 687, U.S. Comp. Stat. 1901, p. 565, was confined to 'controversies of a civil nature', which the judgment in suit was not. The case was not within the words of Art. 4, Sec. 1, and, if it had been, still it would not have, and could not have, decided anything relevant to the question before us. It is true that language was used which has been treated as meaning that the original claim upon which a judgment is based may be looked into further than Chief Justice Marshall supposed. But evidently it meant only to justify the conclusion reached upon the specific point decided, for the proviso was inserted that a court 'cannot go behind the judgment for the purpose of examining into the validity of the claim.' 127 U.S. 293. However, the whole passage was only a dictum and it is not worth while to spend much time upon it.

"A judgment is conclusive as to all the media concludendi (*United States v. California & O. Land Co.*, 192 U.S. 355, 48 L.Ed. 476, 24 Sup. Ct. Rep. 266); and it needs no authority to show that it cannot be impeached either in or out of the state by showing that it was based upon a mistake of law. * * *."

Kennedy v. Supreme Lodge,²² involved a suit in Illinois upon an Alabama judgment recovered for the wrongful death of the plaintiff's intestate. The defendant set up a statute of Illinois which provided that no action could be brought in that state for wrongful death caused in another state. The Supreme Court of the United States held that this statute could not constitutionally be applied to judgments, and that the Alabama judgment was entitled to full faith and credit, even though the original cause of action could not have been maintained in Illinois.

²² 252 U.S. 411, 40 Sup. Ct. 371, 64 L.Ed. 638 (1920).

In *Roche v. McDonald*²³ a judgment was recovered in Oregon upon a Washington judgment, more than six years after the judgment had been rendered. Suit was thereafter brought in Washington upon the Oregon judgment, and the defendant set up a statute of Washington which provided that after six years from its rendition, a judgment should cease to be a charge against the judgment debtor. The United States Supreme Court held that the full faith and credit clause of the Constitution required the judgment be enforced even though the cause of action upon which it was based could not have been sued on in Washington. Mr. Justice Sanford stated that since the court which rendered the Oregon judgment had jurisdiction of the parties and of the subject matter of the suit, the judgment was as valid and conclusive in the courts of the state where it was sued upon as it was in the state where it had been rendered.

From the foregoing it would seem reasonable to conclude that an indebtedness founded upon a judgment for taxes in any state ought to be enforceable in the courts of all other states and in the Federal courts wherever jurisdiction of the debtor can be obtained.

²³ 275 U.S. 449, 48 Sup. Ct. 142, 72 L.Ed. 365 (1928).