St. John's Law Review

Volume 6
Issue 1 *Volume 6, December 1931, Number 1*

Article 32

June 2014

Chain Stores--History and Growth--License Tax Legislation--Constitutionality--Effect

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TAX COMMENT

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CHAIN STORES—HISTORY AND GROWTH—LICENSE TAX LEGISLATION—CONSTITUTIONALITY—EFFECT.—The Chain Store is a development of modern business.[1] The first of existing Chain Stores seems to have been the Great Atlantic and Pacific Tea Company, which was established in 1858. Jones Brothers Tea Company came into existence in 1872; Woolworth's Five and Ten Cent Stores in 1879; James Butler Company in 1882; and S. S. Kresge in 1885.[2] There are now probably more than ten thousand Chain Store Systems, and in the year 1929 it was estimated that Chain Store volume of all kinds made up eighteen per cent of the total trade of the country.[3]

This growth in the development of Chains and their spreading to the less urban regions of the country caused the local tradesman, unable to cope with the competition to induce the local representative in the legislature to introduce a bill imposing a license tax on all Chain Stores. The years 1927 and 1928 marked the beginning of such legislation by the states to curb the progress of the Chains.

Such statutes were passed by the legislatures of Georgia,[4] Maryland,[5] North and South Carolina,[6] and Indiana.[7] The Maryland statute was the first to be tested and held unconstitutional by the Courts of that state.[8] The North and South Carolina statutes were

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[1] NYSTROM, CHAIN STORES (revised ed. 1930) p. 3.

[2] HAYWARD AND WHITE, CHAIN STORES, THEIR MANAGEMENT AND OPERATION (1928) p. 16.

[3] *Supra* note 1, p. 4.

[4] GA. LAWS (1927) §§108, 109, p. 59 imposes a tax of $250 on each store more than five, owned, operated, or maintained, by one person, firm or corporation.

[5] MD. LAWS (1927) c. 554, §§1–3 prohibited the operation by one owner of more than five stores in a single county and imposed a tax of $500 on each store, if they were found to be members of a national chain organization.

[6] N. C. LAWS (1927) c. 80, §162 provides that any person, firm or corporation operating six or more stores in the state shall pay a license tax of $50 for each store.

S. C. ACTS (1928) no. 574, §24 taxes any person, firm or corporation operating five or more stores in the state at the rate of $100 per each store.

[7] IND. LAWS (1929) act no. 207, §5 provides that any person, firm or corporation operating one or more stores shall pay the following license fee: Upon one store, $3; upon two stores but not to exceed five, $10 for each additional store; upon each store in excess of five but not to exceed ten, $15 for each additional store; upon each store in excess of ten, but not to exceed twenty, $20 for each additional store; upon each store in excess of twenty, $25 for each additional store.

[8] Keystone Stores Corporation v. Huster, decided by the Circuit Court of Allegany County, Md., April 1928 (Unreported).

likewise held to be in violation of the equal protection clause of the constitution and were declared invalid.[9] The Indiana Federal Court followed suit and declared the license tax statute of that state to be purely discriminatory and therefore void.[10] Applying the principle that,

> "The law is firmly established that the power of classification is within the discretion of the legislature. The motives which may have actuated in the enactment of such legislation do not concern the court. It may enact legislation so as to favor some industry or industries. It must however apply the same means and methods impartially to all persons of the same class, so that the law will operate equally and uniformly upon all persons under similar circumstances, and must rest upon some ground of difference having a fair and substantial relation to the object of the legislation. It cannot arbitrarily select a certain class of persons for taxation and justify the acts by calling it classifications," [11]

the unanimous tribunal agreed that the act in question was unconstitutional in that there was no real or substantial grounds upon which a law could be upheld which adopted a different measure of taxation for stores known as Chain Stores from that applied to individual stores. At the same time, the state Supreme Court of North Carolina upheld [12] a second license tax statute, passed by the legislature [13] after the previous one had been held unconstitutional [14] which enforced a tax of $50 per store on all stores in excess of one owned and operated by one person. Of this statute, the court said that there was a substantial difference between the business of operating one store and the carrying on of the business of more than one store.

The Chains, undaunted, and backed by their powerful millions and determined to have a final ruling by the highest Court of the land on their contention that a license tax statute on Chain Stores violated the equal protection clause of the constitution, appealed to the United States Supreme Court. The state of Indiana, feeling that it had been deprived unjustly of a source of income, did likewise.

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[9] Great Atlantic and Pacific Tea Company v. Daughton, 196 N. C. 145 144 S. E. 701 (1928); Southern Grocery Stores, Inc. v. W. G. Query, decided by the Court of Common Pleas, S. C. (Unreported).

[10] Jackson v. State Board of Tax Commissioners, 38 F. (2d) 652 (S. D. Ind. 1930).

[11] *Supra* note 10.

[12] Great Atlantic and Pacific Tea Co. v. Maxell, 199 N. C. 433, 154 S. E. 838 (1930).

[13] N. C. LAWS 1929, c. 345, §162 provides that any person, firm or corporation operating two or more retail stores shall pay a $50 license tax on each store in excess of one.

[14] *Supra* note 9.

The equal protection clause of the fourteenth amendment has been subject to much interpretation by the Supreme Court. It has applied the principle that the Constitution does not detract from the right of the state to justly exert its taxing power or prevent it from adjusting its legislation to differences in situation, or forbid classification in that connection, but it does require that the classification be not arbitrary but based on a real and substantial difference, having a relation to the subject of the particular legislation.[15] Past decisions of the Court have made it clear that such difference need not be great.[16] Thus railroads more than fifty miles in length may be prohibited from using wood stoves for heating purposes, while roads less than fifty miles long may continue their use;[17] proprietors of warehouses, situate on the right of way of a railroad may be compelled to secure a license and pay a tax, while warehouses not situate on such a right of way are exempt;[18] hand laundries may be taxed while steam laundries are not;[19] theatres charging a higher admission price but having less revenue may be taxed on a higher basis than theatres exacting a smaller price of admission but having a greater revenue;[20] sellers of oleomargarine may be subject to a tax, while sellers of butter are not;[21] sewing machine merchants who employ selling agents and use vehicles in the promotion of their sales may be taxed, while merchants selling sewing machines at their established place of business are exempt;[22] merchants who use profit-sharing certificates to promote their sales may be subjected to an additional tax, while merchants not offering such coupons are exempt.[23] Applying the same principle, however, the Supreme Court in 1928 held a Pennsylvania statute,[24] taxing the gross receipts of taxicabs owned by corporations, while exempting the total receipts of cabs owned by individuals and partnerships, and a Kentucky statute[25] providing for a tax on mortgages not maturing within five years while exempting from taxation mortgages

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[15] Royster Guano Co. v. Virginia, 253 U. S. 412, 40 Sup. Ct. 560 (1920); Air Way Corporation v. Day, 266 U. S. 71, 45 Sup. Ct. 12 (1924); Palmer Co. v. Saunders, 274 U. S. 490, 47 Sup. Ct. 664 (1927); Quaker City Cab Company v. Commonwealth of Pennsylvania, 277 U. S. 389, 48 Sup. Ct. 553 (1928).

[16] Gulf Colorado and Santa Fe Ry. Co. v. Ellis, 165 U. S. 150, 17 Sup. Ct. 253 (1897); American Sugar Co. v. Louisiana, 179 U. S. 89, 21 Sup. Ct. 43 (1900); Citizens Telephone Co. v. Fuller, 229 U. S. 322 ,33 Sup. Ct. 833 (1912).

[17] New York, New Haven and Hartford R. R. Co. v. New York, 165 U. S. 628, 17 Sup. Ct. 418 (1897).

[18] Cargill v. Minnesota, 180 U. S. 452, 21 Sup. Ct. 423 (1901).

[19] Quong Wing v. Kirkendall, 223 U. S. 59, 32 Sup. Ct. 192 (1912).

[20] Metropolis Theatre Co. v. Chicago, 228 U. S. 61, 33 Sup. Ct. 441 (1913).

[21] Hammond Packing Co. v. State of Montana, 233 U. S. 331, 34 Sup. Ct. 596 (1914).

[22] Singer Sewing Machine Co. v. Brickell, 233 U. S. 304, 34 Sup. Ct. 493 (1914).

[23] Rast v. Van Deman, 240 U. S. 342, 36 Sup. Ct. 370 (1916).

[24] PA. LAWS 1889, 420, 431; PA. STAT. 1920 §. 20, 388.

[25] KY. STAT. §§4019a-9 (Carroll, 1922).

maturing within that period, to be in violation of the equal protection clause and hence unconstitutional.[26]

It is evident from the foregoing cases that the Supreme Court would uphold the license tax on Chain Stores only if it found that there was a very substantial and significant difference between the business and operation of the two kinds of stores. The Court found [27] that the Chain differed from the individual store in many respects. Quantity buying, buying for cash and thus obtaining the advantages of a cash discount, distribution from a single warehouse, a greater turnover, a different sales and pricing policy, cheaper and better advertising, superior management, special accounting methods, and standardization of store management and sales policies are some of the advantages and distinguishing features between the two. In upholding [28] the Indiana statute, the Court concluded as a fact that the Chain Store was a distinctly different enterprise from the individual store and hence presented a different taxable entity.

What will be the effect of this decision? Chain Store systems are here to stay.[29] What the effect of a tax upon them will be is conjecture. It is a certainty that it will not put an end to the growth and development of the system. Let us bear in mind that in certain lines and in some communities the Chain Store has reached the limit of its growth.[30] A "Chain Menace" does not exist, it is merely a fiction originated by the competing independent, so as to enlist the aid of the public in his struggle with the more competent Chain Store.

From the standpoint of the public, the question in this Independent-Chain Store controversy is which system can provide the desired goods and the proper service at the lowest price. Everything else is subsidiary to this. Legislatures should be wary lest a prohibitive tax on the Chain Store be too easily shifted to the consumer.[31]

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INCOME TAXATION—DEDUCTION FOR OBSOLESCENCE—GOODWILL.—Section 234 (a) (7) of the Revenue Act of 1918,[1] and

[26] Quaker City Cab Company v. Commonwealth of Pennsylvania, *supra* note 15; Louisville Gas and Electric Company v. Coleman, 277 U. S. 32, 48 Sup. Ct. 423 (1928).

[27] State Board of Tax Commissioners of the State of Indiana v. Lafayette A. Jackson, 283 U. S. 527, 51 Sup. Ct. 540 (1931).

[28] *Supra* note 27.

[29] *Supra* note 1, p. 21.

[30] NYSTROM, ECONOMICS OF RETAILING (1930) p. 213.

[31] Address of Robert M. Haig before the 1930 Convention of the National Chain Stores Association on Business Taxation.

[1] REV. ACT OF 1918, c. 18, 40 stat. 1077, 1078.