

Extent to Which Corporate Stock is Subject to Double Taxation

William H. Shapiro

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EXTENT TO WHICH CORPORATE STOCK IS SUBJECT TO DOUBLE TAXATION.—Much scholarly research and painstaking labor has been done regarding the problem of taxation of intangibles.¹ There is no doubt of its instant and looming importance. The law at present has shown some definite tendencies to obviate multi-state taxation of intangibles in several of the recent cases decided by the Supreme Court,² but there still is much speculation and uncertainty concerning the future.³

Until a few years ago, since there was and still is no definite constitutional limitation against multi-state taxation of intangibles,⁴ it was clearly the rule that intangible chattels were taxable at the domicile⁵ and might also be taxed wherever they were to have a "situs."⁶ Until the momentous decision in the case of *Farmers Loan and Trust Co. v. Minnesota*⁷ there were four different jurisdictions that had the power to subject the transfer of intangibles to taxation. Beginning in 1929 with the intimations found in *Safe Deposit and Trust Co. v. Virginia*,⁸ the Supreme Court indicated a new attitude concerning multi-state taxation. Following the cases of *Farmers Loan and Trust Co. v. Minnesota*, *Baldwin v. Missouri*⁹ and *Beidler v. South Carolina Tax Comm.*,¹⁰ multi-state taxation of intangibles was considered an evil, not to be further tolerated.¹¹ Gen-

¹ Beale, *Jurisdiction to Tax* (1919) 32 HARV. L. REV. 587; Carpenter, *Jurisdiction Over Debts in Purpose of Administration, Garnishment and Taxation* (1918) 31 HARV. L. REV. 905; Mason, *Jurisdiction for the Purpose of Imposing Inheritance Taxes* (1931) 29 MICH. L. REV. 324; Rottschaeffer, *State Jurisdiction of Income for Tax Purposes* (1931) 44 HARV. L. REV. 1075; Lowndes, *Bases of Jurisdiction in State Taxation of Inheritances and Property* (1931) 19 MICH. L. REV. 850. Besides these leading articles there is also available a host of law review notes and comments.

² Lowndes, *Recent Tendencies in the Taxation of Intangibles* (1930) 17 VA. L. REV. 146; Nossaman, *The Fourteenth Amendment in Its Relation to State Taxation* (1930) 18 CALIF. L. REV. 345.

³ Peppin, *The Power of the State to Tax Intangibles or Their Transfer* (1930) 18 CALIF. L. REV. 638.

⁴ *Fidelity and Columbia Trust Co. v. Louisville*, 245 U. S. 54, 38 Sup. Ct. 40 (1917); *Blodgett v. Silberman*, 277 U. S. 1, 48 Sup. Ct. 410 (1928); see *Citizens National Bank v. Durr*, 257 U. S. 99, 42 Sup. Ct. 15 (1921).

⁵ *Corey v. Baltimore*, 196 U. S. 466, 25 Sup. Ct. 297 (1905).

⁶ *Hawley v. Malden*, 232 U. S. 1, 34 Sup. Ct. 201 (1914); *Matter of Bronson*, 150 N. Y. 1, 44 N. E. 707 (1896); *Matter of Hallenbeck*, 231 N. Y. 409, 132 N. E. 131 (1921).

⁷ 280 U. S. 204, 50 Sup. Ct. 98 (1930). This case definitely overruled the law which sustained an inheritance tax by the state of the debtor's domicile on intangibles of a non-resident whose state had imposed a like tax. *Blackstone v. Miller*, 188 U. S. 189, 23 Sup. Ct. 277 (1903); see note (1930) 15 CORN. L. Q. 457; Note (1930) 4 ST. JOHN'S L. REV. 322.

⁸ 280 U. S. 83, 50 Sup. Ct. 59 (1930).

⁹ 281 U. S. 586, 50 Sup. Ct. 436 (1930); see (1930) 5 ST. JOHN'S L. REV. 136.

¹⁰ 282 U. S. 1, 51 Sup. Ct. 54 (1930); Note (1930) 5 ST. JOHN'S L. REV. 288, 290.

¹¹ Rottschaeffer, *Power of the State to Tax Intangibles* (1931) 15 MINN. L. REV. 741, at 745 *et seq.*; see Peppin, *supra* note 3.

erally, the cases said, the doctrine of *mobilia sequuntur personam* which governed in taxation of tangibles should also be applied to intangibles.¹² Intangibles should be taxed at the state of the owner's domicile and should enjoy immunity from further taxation in another state. It should be remembered that although all of these revolutionary decisions involved inheritance taxes, their principles apply as well to property taxes, and to base distinctions on this ground is of little practical significance.¹³ For that reason, cases involving both forms of taxation are indiscriminately cited.

There is, however, still to be decided the validity of multiple taxation of shares of stock. Since intangibles include stock, at first blush it would seem that there is even greater merit in protecting corporate intangible wealth than capital investments represented by debtor's obligations in various forms.¹⁴ Yet it seems clear that the courts are not quite prepared to admit the implications of the recent tax cases.

In *Benson v. State*,¹⁵ a Minnesota taxing statute¹⁶ imposed a transfer tax on corporate shares of that state regardless of ownership by residents or non-residents. Lund died a resident of Wisconsin owning stock in the corporation having a domicile in Minnesota. Benson, administrator, petitioned to have the stock exempt from the tax. The petition was denied since the situs of the property interest represented by the stock was still within Minnesota, which, therefore, had jurisdiction. The decision is a blunt and clear-cut denial of the Minnesota Supreme Court to extend the doctrine of *Farmers Loan and Trust Co. v. Minnesota* to stock. That there is a fundamental difference between bonds and stocks is too well known to require explanation.¹⁷ Bondholders are creditors while stockholders own undivided interests in corporate property. Furthermore, since the corporation is the creature of the state, stockholders, whether non-

¹² See opinion of Mr. Justice McReynolds in *Farmers Loan and Trust Co. v. Minnesota*, *supra* note 7.

¹³ The inheritance tax is levied on the right to transfer property while the property tax impinges upon property. *HANDY, INHERITANCE AND OTHER LIKE TAXES* (1929) §35; see also *Buck v. Beach*, 206 U. S. 392, 27 Sup. Ct. 712 (1907); *Wheeler v. Sohmer*, 233 U. S. 434, 34 Sup. Ct. 607 (1914). There are many examples where cases of one category have been cited in decisions involving the other. *Union Transit Co. v. Kentucky*, 199 U. S. 194, 26 Sup. Ct. 36 (1905); *Frick v. Pa.*, 268 U. S. 473, 45 Sup. Ct. 603 (1925). However, it is generally conceded that the distinction is still valid in cases involving reciprocal exemptions from state and federal taxation. *U. S. v. Perkins*, 163 U. S. 625, 16 Sup. Ct. 1073 (1896).

¹⁴ "The ultimate economic interest evidenced by a corporate share derives its value from the business and assets of the corporation and, therefore, bears a closer economic relation to the states in which the assets are situated and the business conducted than it bears to the other states whose claims rest on the factors of corporate domicile or the share owners' domicile." *Rottschaeffer*, *supra* note 11, at 754.

¹⁵ 236 N. W. 626 (Minn. 1931).

¹⁶ Minn. Stat. (1 Mason 1927) §§2292, 2302.

¹⁷ *DEWING, FINANCIAL POLICY OF CORPORATIONS* (1929) c. I.

residents or residents should be aware of the right of the state granting the franchise to tax the transfer of the stock. It is obvious then that since the incorporating state has jurisdiction to tax non-residents and since the domicile of the owner is doubtless entitled to tax,¹⁸ double taxation of corporate shares will continue for some time to come.

The nearest approach to the solution of this vexing problem has been a recent decision of the Supreme Court, which ultimately side-stepped the embarrassing issue. In *Susquehanna Power Co. v. State Tax Comm.*,¹⁹ a tax on all shares of stock of domestic corporations owned by non-residents was upheld. A Maryland statute²⁰ provided that such tax considered as a debt of the owners of the shares, can be collected from the corporation. In valuing the shares, account of the market value, the net earning, and the net value of the corporate assets were considered, but in no case was the stock of any corporation to be valued at less than the full value of the real estate and chattels, minus all valid exemptions. The plaintiff, a Pennsylvania corporation, owned all the shares, did business in Maryland, but argued that Maryland had no control of the "situs" of the shares to be entitled to tax them. The state court upheld the tax, asserting the method of valuation to be constitutional and since Maryland had power to create the corporation it could fix the situs of the corporate shares within the state, thus exhibiting a striking similarity to the decision of the court in the *Benson* case. On appeal to the Supreme Court, the decision was sustained but on the different ground of being an indirect tax on the corporation.

By refusing to see through the subterfuge that the tax was actually on the shareholders and not on the corporation, an embarrassing situation was avoided and the extent to which shares are subject to multi-state taxation still left undetermined. The plaintiff corporation tried in vain to extend the implications of the *Farmers Loan and Trust Co. v. Minnesota* case to corporate shares. Because of the great lengths to which the court had gone in avoiding a definite ruling by dealing with the case as involving the tenuous distinction of tax measure and tax subject,²¹ and by its ready acceptance of Maryland State Court constructions, it is not improbable that in the future the state of incorporation may be denied the right to collect property taxes on shares of stock, should such tax not also be viewed as a levy on the corporation.

The writer does not attempt to deal with the advisability of multi-state taxation nor with the factors that determine its utility,²²

¹⁸ *Tappan v. Merchants Nat. Bank*, 86 U. S. 490 (1873); *Corey v. Baltimore*, *supra* note 5.

¹⁹ 283 U. S. 297, 51 Sup. Ct. 436 (1931).

²⁰ Md. Code Anno (Bagly 1924) art. 81, §§1, 2, 4, 154, 163.

²¹ Isaacs, *Subject and Measure of Taxation* (1926) 26 COL. L. REV. 939.

²² For a scholarly article see Rottschaeffer, *Power of the States to Tax Intangibles* (1931) 15 MINN. L. REV. 741.

nor with the policies that determine the situs of corporate shares. That these are related problems is obvious. At present, however, none of these factors have influenced the court to announce a definite stand in regard to the limitation of multi-state taxation of stock. The *quaere* is still left open as to whether the taxpayer's convenience would best be served by localizing the tax at the corporate domicile or whether the interests and economic claims of the state where the property happens to be located is paramount.

WILLIAM H. SHAPIRO.

LIABILITY OF STOCKHOLDER OF DISSOLVED CORPORATION FOR UNPAID TAXES.—In 1919, the Coombe Garment Company, a Pennsylvania corporation, distributed its assets among its stockholders and then went into voluntary dissolution. Thereafter, the Commissioner of Internal Revenue made deficiency assessments against the corporation for income and profits taxes for the years 1918 and 1919. A small part of these taxes was collected, with an unpaid balance remaining of \$9,306.36. I. L. Phillips, of New York City, had owned one-fourth of the company's stock and had received \$17,139.61 as his distributive dividend. Pursuant to section 280 of the Revenue Act of 1926, the Commissioner sent due notice to Phillips that he proposed to assess against and collect from him the entire remaining amount of the deficiencies. No notice of such deficiency was sent to any of the other stockholders nor were any proceedings instituted against them. Upon appeal by the executors of Phillips for a redetermination, the Board of Tax Appeals held that the taxpayer was liable for the full amount. This decision was subsequently affirmed by the United States Circuit Court of Appeals for the Second Circuit. Because of conflicts in the decisions of the lower courts a writ of *certiorari* was granted by the Supreme Court. *Held*, that section 280 of the Revenue Act of 1926, providing for the collection of revenue by summary administrative proceedings, is constitutional. *Phillips et al. v. Commissioner of Internal Revenue*, 51 Sup. Ct. 608 (1931).

The lower federal courts have often questioned the constitutionality of employing summary administrative proceedings to enforce the liability of a transferee stockholder for the unpaid taxes of a corporation.¹ It has been argued that the power given the

¹ *Owensboro Ditcher and Grader Company v. Lucas*, 18 F. (2d) 798 (D. C. Ky. 1927): " * * * section 280 of the Revenue Act of 1926, if enforced, * * * will result in denying to the plaintiff due process of law within the meaning of the Fifth Amendment to the Constitution of the United States." See also *Elmhurst Investment Co. v. U. S.*, 24 F. (2d) 561 (D. C. Kan., 1928); *Mid-Continent Petroleum Corp. v. Alexander*, 35 F. (2d) 43 (D. C. Okla., 1929).