IS CORPORATION TAX CONSTITUTIONAL?

(Continued from Page 5.)

the law imposing this federal tax is before the Supreme Court of the United States for its consideration and it is the general expectation that this court will decide the question before the time arrives to pay the tax. If the court should declare the law unconstitutional, of course no further attempts would be made by any of the federal officers to collect the tax and nothing would remain to be done by the companies which have made their returns.

But if, for any reason, the decision should be delayed, or if the decision should sustain the law in some particulars and declare it invalid in other particulars, then it behooves companies paying their taxes to do so under proper protest and to follow that procedure required by the federal statutes as a basis for any subsequent effort to recover the taxes so paid or any part of them.

Previous Income Tax Laws.

It is not the purpose of this article to attempt to forecast the decision of the Supreme Court but a brief statement of the outlines along which that make clear the form of protest which should be used in the event that it should be necessary for companies, for their own protection, to pay their taxes under protest.

Income taxes levied by the federal government are no novelty. Such taxes were levied during the period of the Civil War by various statutes enacted between 1861 and 1870. The income taxes levied in those times were subsequently abolished. In 1894, in a time of profound peace, another income tax was levied and the law imposing this tax was declared unconstitutional by the United States Supreme Court in 1895 in the case of Pollock vs. Farmers' Loan and Trust Co. The income tax of 1894 imposed a percentage tax on all incomes, whether derived from business transacted or invested capital and whether earned by individuals or corporations. The tax was thus imposed upon incomes derived from the following sources:

1. Income from real property.
2. Income from business property.
3. Income from business transacted (including earnings of professional men), and
4. Income by way of interest on state or municipal bonds.

The Decisions in the Pollock Case.

There were two hearings and two decisions in the Pollock case, and at both hearings and in both decisions the Supreme Court was unanimously of the opinion that, in so far as the income tax of 1894 taxed income derived as interest on state or municipal bonds, the law was invalid. Beyond this point, in the first decision, the court went no further than to hold that the tax was invalid in so far as it taxed income derived from real property. Upon this latter point the court divided by a vote of six to two, Mr. Justice Jackson not participating in the hearing. In the second decision of the Pollock case, the court was still unanimously of the opinion that the tax was invalid in so far as it taxed interest derived from state or municipal bonds, and also held that the tax was invalid in so far as it taxed income from real property and income from personal property. Upon this last point the court divided five to four. Mr. Justice Brown joining and Mr. Jackson reinforcing the ranks of the minority. The majority having reached the above conclusion held that the income tax of 1894, being valid in the particulars noted, must fall as a whole, although the suggestion was made that a tax levied upon income derived solely from the transaction of business or the exercise of a profession might be good under the federal constitution as an excise tax, if it stood alone.

Possibility of Law Being Held Invalid Only In Part.

It is apparent and, indeed, is a matter of common notority, that the Congress in passing the law imposing a federal tax on corporations and other companies intended to profit by the suggestion made in the Pollock decision and make this tax strictly a excise tax. The law itself characterizes the tax imposed as a "special excise tax with respect to the carrying on or doing business." But in describing the income which forms the basis of the amount of the tax, the law provides, with reference to American companies that "income from all sources" shall be included and provides, with reference to foreign companies doing business in America, that their income shall include income from business transacted and capital invested in America. "Income from all sources" and "income from capital invested" would certainly include income from real property, from personal property and by way of interest on state and municipal bonds. It would therefore appear, at first blush, as though the federal tax of 1894, held invalid in the Pollock case.

But if the Pollock decision did not expressly overrule prior adjudications of the Supreme Court upon the income tax laws passed during the period of the Civil War, and other analagous cases, it at least reached a conclusion at variance with the under-standing of those prior adjjudications by such eminent legal writers, to mention only a few, as Chancellor Kent, Judge Story, and Prof. Pomeroy. And a factor in the case which may have some weight is that the personnel of the Supreme Court, as it exists today, is so changed, that of the nine members of the present court, only four were on the bench when the Pollock case was decided, of whom two sided with the majority while the other two wrote long and vigorous dissents

[Note: Since this article was written, the death of Mr. Justice Brewer removes from the Supreme Bench one of the two survivors of the majority in the Pollock case.]

If the Pollock case is to be overruled by the Supreme Court at this time, the federal tax on corporations, in the opinion of the writer, will probably be sustained, as the objections to that tax, such as lack of uniformity, want of power in the federal government to tax corporations, and the like objections, do not appear to rest on a sound foundation, so far as the writer has been enabled to examine into the question. Without overruling the Pollock case, however, the Supreme Court especially in view of the language in the law which recites that the tax imposed is a special excise tax with respect to the carrying on or doing business, may attempt to distinguish the present law from the income tax law is valid in so far as it imposes a tax on income derived from business transacted and holding that in so far as it attempts to impose a tax on income derived from real property, personal property or by way of interest from state or municipal bonds, it is valid. In other words, instead of condemning the law as a whole, as was done in the Pollock case, the court may sustain that part of the law which, in the Pollock case, it was intimated might have imposed a valid tax if standing alone, and only reject that portion of the present law which appears to be so clearly opposed to the conclusions reached in the Pollock case. And it may justify this severence of the valid, from the invalid parts of the law in the present case by reason of the reference in the law itself to the tax as an excise tax.

What Parts of Taxes Should Be Paid Under Protest.

If the time arrives to pay taxes under protest and no decision has been rendered by the Supreme Court, it would be the proper course to pay the entire tax under protest. But should the court render its decision before the time for the payment of the taxes comes around and should it hold any part of the tax imposed by the present law unconstitutional, that part of the tax ought to be refused to the Collector of Internal Revenue or at least paid under proper protest, so that it might be recovered. If the taxes are paid under protest before the decision is rendered by the Supreme Court not only should the entire tax be paid under protest but each of the items thereof should be paid under protest which may, by any possibility, be held invalid, so that due advantage might subsequently be taken of such portion of the decision as might be to the company paying the tax.

What Constitutes an Involuntary Payment.

In California those who have grown accustomed to paying State or City and County taxes under protest are familar with the practice which requires as the only basis for a suit to recover the taxes so paid under procise tax with respect to the carrying test, the filing with the tax collector of a notice of protest at he time of paying the taxes, in which the points of protest are specificially urged. This, it should be remembered, is the appropriate procedure in California with reference to State or city and county taxes only by grace of the California statute. Ordinarily one who pays taxes voluntarily is not entitled to recover them back subsequently even if erroneous or illegal; and ordinarily one is, in the eyes of the law, regarded as paying his taxes voluntarily unless he does so under coercion; and ordinarily, in the absense of a statute the mere filing of a written protest, and a payment thereunder or thereafter is not a payment under coercion.

Federal Decisions Defining Involuntary Payment.

It therefore becomes necessary to examine the federal statutes and learn from them what is the proper procedure to follow as a basis for the recovery of taxes. The law imposing the federal tax on corporations specificially provides that all laws relating to the collection, remission and refund of internal revenue taxes so far as applicable to the federal taxes on corporations. There is nothing in the California law.

After a careful examination of the cases of Chesebrough vs. United States, 192 U. S. 253, and Herold vs. Kahn, 159 Fed. 608, with previous decisions the writer has reached the conclusion that it is quite doubtful whether the mere payment of taxes, accompanied with a written protest, is sufficient to make the payment involuntary and to form the basis of a right of recovery under the federal statutes. It is therefore advisable not to pay these taxes until after June 30th of this year and then only after formal demand by the local Collector of Internal Revenue, so that there may be no question but that the taxes are paid under coercion.

Pay Taxes Under Protest Only.

Second Notice.

The law imposing federal taxes on corporations provides that all companies shall be notified of the amount of the assessments for which they are respectively liable on or before the first day of June. This is the first notice which the company will receive. The tax is then payable on or before the thirtieth day of June. If not paid by that time, it is the duty of the collector to give the company a second notice and make a demand for the payment of the tax. If the tax is not paid within ten days after this second notice and demand a penalty is incurred which amounts to five per cent of the taxes and interest thereon at the rate of one per cent per month from the thirtieth day of June. If the company, before paying the tax, awaits the receipt of this second notice and demand and then, within the ten days after its receipt, to avoid the penalty and interest, pays the tax under protest, it will be just such an involuntary payment of the tax as was held in the Herold case was sufficient to constitute involuntary payment of the tax and basis of a right of recovery.

What Form the Protest Should Take.

No particular form of protest is required so long as the protest advises the collector that the party paying the taxes claims that they are being illegally exacted and gives the collector notice that he intends to institute proceedings or suit to compel their repayment. The notice of protest should conclude with a demand on the collector for the repayment of the taxes so paid under protest. In the protest, where part of the taxes are to be protested (like taxes on the income and realty), should be a statement of the amount of income derived from real property, and the amount of the tax on that income when the tax on it is to be protested. A like statement should be made with reference to income derived from personal property or income derived as interest from state or municipal bonds, if the taxes on the income from those sources are to be protested. Although the law apparently does not require that the protest be in writing, it is clearly advisable that it should be.

Appeal to Commissioners and Suit.

After taxes have been paid under protest, if the Collector of Internal Revenue does not refund the taxes an appeal must be made to the Commissioner of Internal Revenue at Washington for the refund of these taxes. This appeal is made upon forms and subject to, the regulations prescribed by the Secretary of the Treasury and may be made by a delivery to the local collector for transmission to the commissioner. If the decision of the verse decision by the Commissioner of Internal Revenue, suit may be brought to recover the taxes within two years after the time when the tax was paid under protest. If the Commissioner of Internal Revenue delays to render his decision upon the appeal for more than six months from the date of appeal, suit may be brought without awaiting an adverse decision of the cimmissioner. If the decision of the commissioner is favorable, the taxes will be refunded without suit. Suit to recover taxes may be brought in the apropriate United States Circuit Court against the local Collector of Internal Revenue, or a suit may be instituted against the United States in the Court of Claims or in any United States District or Circut court according to the amount involved.

Income From United States Bonds.

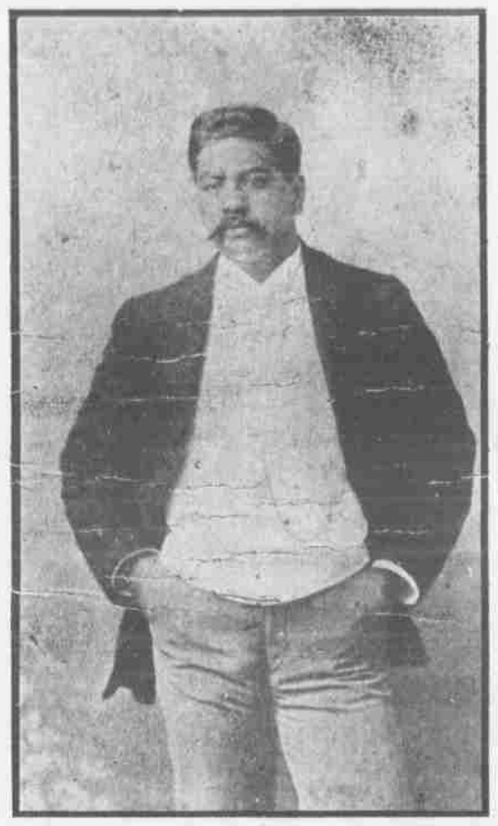
In the course of this article nothing has been said about income derived as interest from United States bonds. Congress, if it has power to tax incomes at all, in the manner attempted by the Federal Tax on Corporations, has the power to tax income by way of interest from United States bonds. Many of the United States bonds, however are issued under a statute which distinctly provides that they shall be exempt from all taxes or duties of the United States, as in the case of the recent statute of 1902, authorzing the Panama Canal bonds. As repeals by implication are not favored in the law, it is probable that the statute which authorized bonds and provided that they should be exempt from taxation would be construed with the statute imposing the federal tax on corporations and that the court would hold that income derived as interest from United States bonds was not subject to the federal tax on corporations, where such bonds had been issued under federal statutes exempting them from taxation. Any companies holding such bonds would therefore want to refer to the income derived from that source in the same way in its protest and appeal as it would refer to income derived from state or municipal bonds.

DELEGATE KALANIANOLE ISSUES A CHALLENGE

Hilo Tribune, April 26:

Delegate Kalanianaole has written a letter to Supervisor Stephen Desha in which he issues a challenge to Editod Ewaliko of te Malamalama, the Democratic paper published in Hawaiian in this city, to debate on the land law amendments. It appears that for some time past the Malamalama has been criticizing the attitude taken by the Delegate in reference to his stand on the land law proposition, and the friends of the delegate, who are able to read Hawaiian, state that these attacks have been very bitter and have hinted that the delegate was not purely disinterested in his motives.

In his letter to Desha the delegate states that he on his return to Hawaii will come to Hilo, when he will call a mass meeting of the citizens of this city. He will then challenge Ewaliko to appear on the platform with him and to make his charges, when the delegate will answer them.



DELEGATE KALANIANAOLE.

In discussing the amendments the delegate writes, referring to the defeat of the clause, providing for advances to be made by the government to homesteaders as follows:

"Congress wants the people to be self-supporting and not to be dependent on others. What the government wants is people who can work for themselves, and that kind of people who work themselves up and look after themselves are the kind who make good citizens and good Americans. Another objection to the amendment was that such a method had never been employed here before(and that they did not see why they should use it even for Hawaii."

The delegate also explains his stand on the prohibition measure at great length. The bulk of the letter is in Hawaiian, and parts of it read about as follows:

"Possibly the Hawaiians do not understand about these questions. Now they leave the matter to the people here is what I want to explain to the people of Hawaii The main reason is; believe in home rule, and if I had not worked hard to try to defeat the bill introduced in Congress, the door would have been opened for further legislation by Congress in purely local matters in other instances, and the impression would have been given that the people of Hawaii were not capable of running their own affairs.

"I went before them and explained to them that the people were capable of making a good law themselves. History has shown, even before annexation, that the Hawaiians were able to run their own government, and I feared that if the door were thus opened, the next thing might be government by commission. I had to explain the local situation to open the eyes of some of the Congressmen with regard to these matters

"By thus closing the door a good thing has been accomplished for Hawaii, and a precedent has been set by Congress themselves that we as a people are capable and able to run our own affairs They not only leave it to us to vote for the plebiscite, but go further and say that after we have decided what we want to do, it is up to our own legislature whether to enact a prohibition bill or not This, you will see, shows the high opinion in which we are being held as to our fitness to legislate for ourselves It has been shown, not only to Congress, but to the whole world, that we are able to run our own home affairs.

"Had the prohibition bill been passed by Congress the enemies of the welfare of Hawaii could use this precedent in the future This on the face of it would be the opening wedge for anybody to come here and ask Congress to pass legislation for Hawaii, but as it is now, I have stopped it for good, of course unless we should go to the extent of passing laws detrimental to the interest of the Territory and the people therein.

"The question was, not as to whether we wanted prohibition or not, but as to whether we wanted home rule or not."