TAX EXEMPTIONS WITH SPECIAL REFERENCE

TO OREGON

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PART I

PUBLIC INSTRUMENTALITIES

A. Presumption of Exemption from Taxation

Generally speaking, public property that belongs to any unit of government is held by the courts to be exempt from taxation unless expressly made taxable either by the constitution or a statute.[1] However, there are a few states, such as Illinois, where all property is taxable unless specifically exempted. In these states the courts construe the constitutional provision granting the legislature power to exempt as being merely permissive. Thus the legislature must by affirmative action exempt property, or all property is taxable;[2] or the exemptions specified in the constitution are exhaustive, as is the case in Nebraska.[3]

The Oregon Supreme Court has held that all state or local public school property can be taxed by the legislature, but that, due to public policy, property owned by the state or its political subdivisions will be exempt from taxation even though such exemption is not expressly stated in the law. Nevertheless, the express exemptions in the Motor Vehicle Act as to licenses for automobiles of

1. James D. Barnett, "The Taxation of Public Property," Commonwealth Review of the University of Oregon (N.S.), Vol. XII, November, 1930, pp. 262-264.

2. Krause v. Peoria Housing Authority 19 N.E. (2d) 193, 198 (Illinois, 1939). People v. University of Illinois, 328, 211. 377, 159 N.E. 811, 814 (1928). Blue-Jacket v. Commissioners of Johnson County, 3 Kan. 299, 342 (1865).

3. Droll v. Furnas County, 108 Neb. 85, 187 N.W. 896 (1922).

the United States government, farm tractors, road rollers, fire wagons, invalid chairs and baby buggies are held to be exclusive and do not include a Ford automobile that is owned by a municipality.[1]

1. State v. Preston, 103 Or. 631, 635-6; 206, P. 304 (1922). Portland v. Kozer, 108 Or. 375, 379-384, 217 P. 833 (1923) held that municipalities must pay the tax on gasoline as the statute levying that tax did not expressly exempt municipalities.

B. Governmental Self-Taxation

A unit of government does not tax its own properties, it is said, because "it is obvious that in taxing its own properties, an authority would merely be transferring its own money (obtained by taxing its private citizens) from its general fund to its tax account and from its tax account back again to its general fund".[1] But it is often urged that this bookkeeping process be retained by a publicly-owned utility so that it can be placed upon a more equal footing with private corporations. Such bookkeeping enables the people to determine whether the publicly-owned public utility is as efficiently operated as one that is privately owned.[2]

Each grade of government may, in the absence of a constitutional restriction, tax or exempt its own agencies, or permit one of its political subdivisions to tax its property.[3] For example, in Evans v. Gore,[4] the United States Supreme Court held unconstitutional an act taxing the salary of a federal judge whose appointment and compensation were fixed prior to the passage of the Congressional Act. Even though the judge was a federal officer and the tax a federal tax, still it was held that his salary could not be taxed as the Constitution of the United States provides that a judge's salary shall not be reduced during his term of office; but

1. New York State Constitutional Convention Committee, Problems Relating to Taxation and Finance (1938), Vol. X, p. 193.
2. Oregon Report of the Committee on Assessment and Taxation of Municipal Utilities (1933), pp. 8-27.
3. National Industrial Conference Board, State and Local Taxation of Property (1930), pp. 40-41.
4. 253 U.S. 245, 64 L.ed. 887 (1920).

where the Congressional Taxing Act precedes the appointment of a federal judge, it is valid and he must pay an income tax the same as any other citizen.[1]

> A diminution of the compensation of certain officers during their term of office is prohibited under these constitutional provisions--Federal with relation to certain Federal officers--State with relation to certain State officers.[2]

The government of England and most progressive governments of the world which have income taxes tax the salaries of its own employees. In the United States a government taxes its own employees except when a constitutional provision interferes. A proposed remedy is a constitutional amendment authorizing an income tax to be levied upon the salaries of governmental officers. In support of such an amendment, it can be said that the amount of income irrespective of source should be used as the factor in determining their ability to pay a tax. The officials have the same obligations to support the government as have private individuals. Moreover, taxation will make them more tax conscious and tend to promote economy in government expenditures. In opposition to such an amendment, the most important argument is that the abolition of the tax exemption of government employees' salaries would result in destroying the independence of the officers from the legislative branch of the government. Through taxation the officers would be entirely dependent upon the legislature for a livelihood. This would be particularly true of the members of the judiciary, which is

1. O'Malley v. Woodrough, 30 U.S. 277, 83 L.ed. 1289 (1939).
2. Idem. 1, p. 3, Constitutional Convention Committee, New York, p. 466.

the weakest branch of the government. Still the independence of the governmental officers from the legislature could be maintained by public opinion.[1]

The state taxation of the income of its employees does not come within the rule that a state should not tax itself, as the governmental employees' salary is as much a private one as any other individual's salary. An argument for exemption from taxation is that state salaries are low. Adams, in his work on Public Finance, declares that the taxation of a public salary maintains the parity between that and the industrial remuneration for a similar position. Actually the public salary is lower than the industrial salary on account of the prestige and civic pride involved in the public position.[2] When a salary is not subject to taxation, the salary need not be as large as one that is subject to taxation.

In Wieder v. Hoss[3] it was held that property which was not owned but merely controlled or operated by the state is not exempt from state taxation as public property unless a statute so specifically provides. Thus the property controlled or operated by the Oregon State Hydro-Electric Power Commission is subject to taxation by the state of Oregon.

Securities of the state or of its political subdivisions are in Oregon and many other states exempt from state taxation; but in Connecticut, Illinois, Massachusetts, New York, and some other states, they are not. Where the securities are not exempt from taxation, it is because of a

1. Idem., p. 467; 493-93.
2. J. H. Gilbert (from class notes in Public Finance).
3. 143 Or. 57, 61, 21 P. (2d) 227 (1933).

constitutional provision or a statute of that state which strictly limits exemptions from taxation.[1] By statute in Oregon the property of the Peoples' Utility Districts is now subject to state taxation.[2]

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1. State v. Page, 100 West Virginia, 426, 130 S.E. 426. 44. A.L.R. 501 (1925). See also note on Tax Exempt Securities, 86 A.L.R. 547, 552.

2. Peoples' Utility Districts impliedly exempt from taxation. Oregon Constitution, Article XI, Section 12. Oregon Supplement, 1935, 56-3401; 56-3460; Laws, 1937, Ch. 276. Real and Personal Property subject to taxation, Laws, 1939, Ch. 387, Section 10, p. 739.

C. Taxation of the Instrumentalities of One Unit of Government by Another Unit of Government

(1) Real Property

The Oregon Supreme Court has held, in the absence of statute, that the property of one unit of government is generally exempt from taxation by another unit of government whether that property is located within or without the limits of the unit of government that owns the said property. However, in the absence of a constitutional restriction, the legislature may provide for the taxation of the property of one unit of government by another.[1] There is at present in Oregon no such constitutional restriction.[2]

Where the property of one unit of government is located within the limits of another, tax exemption of such property works inequality. The property should be taxed by the servient unit as it protects that property at an expense, and the exemption of the property increases the burden on that property which remains to be taxed. The dominant unit receives the benefits from the tax exempt property that it owns, but none of the burden. When, however, the property is not taxed, payment by the dominant unit of a contribution in money in lieu of taxes should be made not only on the basis of the damages inflicted but also on the basis of the benefits received from the servient unit. For example, a county court house located within the

1. City of Eugene v. Keeney, 134 Or. 393, 397-8, 293, P.924 (1930). City of Portland v. Multnomah County, 151 Or. 504, 510-11, 50 P. (2d), 1145 (1935).
2. Oregon Constitution, Article 1, Sec. 32.

boundaries of a city should be paid for by the county by a money contribution in lieu of the taxes, the amount of which contribution should be determined by the burden that it places upon the city to protect it and also by the benefits that the county receives from the city because of that protection.

Due to the greater value of urban over rural property, it is urged that exemptions work to the benefit of the owner of urban property. On the other hand, it is argued that the taxation of urban property would cause it to bear a disproportionate share of the total taxes, as compared with the rural areas. However, most of the wealth is in the urban areas and thus the owners thereof should pay more because they have the ability to do so. It is agreed that while burdens are added to the local government through tax exemptions, nevertheless the increase in population, finances and social advantages due to the presence of the tax-exempt area or institution often outweigh those burdens. However, the costs of government in a city increase faster than population or property values.[1]

There should be a presumption of universal taxation as between the units of government. There should be no exemption except where two units have common boundaries.[2] The English common law exempts property "occupied by the crown" from taxation. The scope of this exemption has been difficult to define. Parliament now grants the localities sums in lieu of the taxes, the amount thereof being

1. Barnett, _op. cit._, pp. 262-264.
2. _Idem._

computed on the assessed value of the exempt property. In England the national income tax applies to the local governments, individuals and corporations alike.[1]

> So that, practically speaking, with some exemptions, it is very largely a case of taxation all around--the nation now taxes the localities, the localities practically tax the nation, and the various localities tax each other.[2]

There are two chief remedies for inequalities caused by tax exemption. The first is the removal of the exemption. But this would be a dangerous procedure. It would permit of the taxation of the whole state by a part of the state, of a political subdivision of the state by another political subdivision of the state, or of the federal government by a state. The local assessor is often inclined to discriminate against the property of the general or larger unit of government. The local authorities may also be tempted to go on a spending spree. The more centralized the control of assessment is, the less will be the abuses on the part of the local authorities against the property of the general or larger unit of government. According to the second method, the higher unit of government substitutes money compensation in lieu of the taxes that would have been received from the exempt property. This method is more satisfactory than the first named as it is free from the abuses that exist when a subdivision of a government taxes the property of the government. The contribution method is used in England, Massachusetts, New York and California. An attempt is made to compute the money contribution according to the value of the tax exempt property and its relation to

1. Idem., pp. 275, 257-58.
2. Idem.

the total ratable property of the locality.[1] H. L. Lutz contends that a grant by the state to the localities in lieu of taxes on the state property is indefensible because it merely prolongs the existence of localities that should be reorganized to exclude the state land and imposes an unnecessary burden on the people.[2] New York state grants a money contribution to the localities wherein the state Forest Preserves are located.[3] And in New York state, the city of New York is given the power to tax state property that lies within its borders.

The exemption of federal lands has long been a grievance of the Pacific states. It deprives them of a very large source or revenue. However, it is offset to a great extent by provision that the states concerned shall share in the proceeds of the sale of the lands, to be applied to roads and schools. Moreover, twenty-five percent of the gross revenue from the sales of the timber, grazing fees and the like received within the state are given to them for similar purposes. In addition, Congress makes appropriations for roads and also often builds roads within the national forests. A few states that have forest reserves of their own grant money compensation to the localities, due to the losses in taxes caused by the exemption of the state forest lands within the borders of the localities affected.[4]

1. H. L. Lutz, Public Finance, New York: D. Appleton-Century Company, 1936, pp. 276-278.

2. Idem., pp. 549-550.

3. New York Constitutional Convention Committee (1938), op. cit., pp. 194, 196, 200.

4. Barnett, op. cit., p. 275. National Industrial Conference Board, op. cit., pp. 22, 23-28.

One-fifth of the United States is owned by the federal government. In 1939 the total federal lands were 400,000,000 acres, with a value of about $4,500,000,000. The total value of all realty in the United States is about $113,000,000,000. The tax-exempt federal lands are about four percent of the national total. Most of the federal lands are rural. The bulk of these lands are located in the west. In Nevada, the federal government owns eighty-three percent of the state's area; in Arizona, sixty-three percent; in Utah, sixty percent; in Idaho, fifty-six percent; and in Oregon, forty-six percent of the total state area.[1]

It is urged that the taxation of the federal lands would increase the burden on the eastern federal taxpayer. This result would be achieved because the majority of the federal lands are located in the west and would be taxed by the western states. In addition, the majority of the federal revenues are collected from the eastern taxpayers. Thus the eastern taxpayer would be unjustly taxed.[2]

The United States Supreme Court has held that lands owned by the federal government for the Indians are exempt from state taxation; but if the land has been deeded to the Indians, then the lands so held by the Indians are not exempt from state taxation. Oregon has a statute which, in pursuance of this case, exempts the property of all Indians residing on reservations from taxation exeption that acquired by them through purchase or inheritance.[3]

1. *Oregonian*, July 9, 1939, I, 4 (2).
2. Lutz, *op. cit.*, pp. 548-549.
3. 291 U.S. 466, 472, 78 L.ed. 918 (1933).

It has been held by the United States Supreme Court that a state may tax a railroad used by the federal government which serves some of the mines of the Choctaw nation, for "the mere fact that ... property is used among others by the United States as an instrument for effecting its purpose does not relieve it from state taxation".[1]

The Supreme Court has held that while Congress makes or authorizes contracts to be made with individuals or corporations or grants aids by money or land to them for services rendered to the government, the property of such agencies is nevertheless subject to state taxation unless expressly exempted by Congress. The decision is based on a distinction between the taxation of the agency used by a unit of government and the taxation of the property of such an agency. It is permissible to tax the property of such an agency since the corporation is organized and holds property by virtue of state law. To exempt that property from taxation would unduly embarrass and limit the taxing power of a state. But the agency of the federal government, such as a corporate franchise, cannot be taxed by a state.[2] A federal franchise given to a private business and used by the business to its own advantage and profit is subject to state taxation. But if the franchise is used for a governmental purpose and not for a private one, the property is then exempt from taxation by the state. The power of taxation must be so construed as not to impair either the government levying the tax or the one taxed or affected by the tax.[3]

1. Choctaw, Oklahoma, and Gulf R. Co. v. Mackey, 256 U.S. 531, 536, 65 L.ed. 1076 (1920).
2. Thomson v. Pacific Railroad, 76 U.S. 579, 19 L.ed. 792 (1869).
3. Susquehanna Co. v. Tax Commission, 283 U.S. 291, 294, 75 L.ed. 1042 (1931).

Moreover, the mere extension of control or regulation over a business, as for example a cotton warehouse, by the federal government does not withdraw such business from local taxation.[1]

A tax levied by a state on the property of an United States naval officer has been held valid by the United States Supreme Court.[2]

The exact volume of tax exemptions has never been determined and is thus not known in the United States. A few states, such as New York and Connecticut, have fairly accurate records as to the amount of property that is tax exempt. But most states either require no assessment of the tax-exempt property or where an assessment of such property is made, it is not accurate either as to the completeness of the records or the value of the property.[3]

The privilege of unlimited tax exemption of one grade of government from another would endanger the federal system just as much as the unrestricted taxation by one government of the agencies of the other would do. The burden is great at either extreme.[4]

"There has always been a well-founded objection to tax exemption because it in effect places a mortgage on possible sources of necessary future revenue."[5] Thus wrote the 1924 Congressional Committee on Taxation and Tax Exempt Income in its report to Congress.

1. Federal Compress Co. v. McLean, 291 U.S. 17, 78 L.ed. 622 (1933).

2. Dyer v. City of Melrose, 215 U.S. 594, 54 L.ed. 341 (1910).

3. Barnett, op. cit., p. 275. National Industrial Conference Board, op. cit., pp. 22, 23-28.

4. Alden L. Powell, National Taxation of State Instrumentalities, University of Illinois, 1936, pp. 11-13.

5. Report on Taxation and Tax Exempt Income to 67th Congress (1924), pp. 15, 25, 46. Report of the Committee on Tax Investigation of the State of Oregon (1923), pp. 32-36.

(2) Public Utilities

In recent years a demand for the taxation of municipally-owned public utilities has arisen in California, Oregon, Washington, and elsewhere. The movement is supported by the public service corporations and the granges. However, the granges are advocating further public ownership but without tax exemption in order to obtain lower service rates without an increase in taxes on their land. The public utility corporation opposes further public ownership as the extension of public ownership will end the privately-owned public utility. The corporations complain of the disadvantages they suffer due to the tax-exempt utilities. The farmers complain of the higher taxes they must pay because of the exemptions. The municipalities themselves favor exemption as they fear that in taxation of the publicly-owned utility would end it. Exemption is a stimulus to the socialization of industry movement. It is claimed that tax exemption or a subsidy in lieu of exemption reduces the rate; but it has been denied that reduction of rate is due to the fact of public ownership alone. Private corporations stress the fact that publicly-owned utilities being exempt from taxation can borrow at lower rates of interest. But the advocates of public ownership answer that this is more than balanced by the limits placed on public bond issues and the requirements for a sinking fund.[1]

As between local units of government, the taxation of the property of the dominant unit contained within the borders of the servient

1. Barnett, op. cit., pp. 273-275.

unit is often only just and fair. It is not a mere pocket transferring process. In New York state the municipal property located outside of a city is taxed by the municipality within which it is located. In Michigan each locality taxes the property of the other locality that is located within its borders. Oregon exempts from taxation property owned and used by a municipality for a public purpose. Municipal exemptions in Oregon in 1933 were not large enough to be serious. They might become so when they are greatly increased by such projects as the Bonneville Dam and the like. Inclusion of the municipal property now exempt in Oregon would amount to an increase on the tax roll of 2.15 percent of all property, which would lower the county tax 2.11 percent. The total value of exempt municipal property in 1933 was $22,934,766. By adding this total to the tax roll, a reduction of about one mill in the taxes would occur.[1]

A tax on the exempt municipal utility would increase the service rates, which increase would fall primarily on the small consumer. The large consumer of power would not feel the increase in service rates so greatly as the small consumer because the more power that is consumed the cheaper the rate, and because the municipal utility's property would be taxed the amount of the larger consumers' general property tax would be lowered. Moreover, the large consumer of power is generally the one most able to pay for that power. A large taxpayer, on the other hand, may not use any of the service, and thus the lower rates due to the tax exemption of a municipally-owned public

1. Oregon Report of the Committee on Assessment and Taxation of Municipal Utilities, (1933) pp. 6-27.

utilities would not benefit him. But the large consumers of service who might not be heavy taxpayers would benefit from the lower rates made possible by tax exemptions.[1] When the utility is not taxed, the service rates are lower but the burden is shifted upon the payer of the general property tax. However, the real difficulty lies in the fact that the consumer of the utility's product and the taxpayer are not always the same persons, as the utility often extends its services far beyond the limits of the taxing unit. Its exemption causes a higher state, county and private public utility tax.

Most of the utilities do not at their present service rates receive a sufficient surplus to enable them to pay the additional tax without raising their service rates. The chief obstacle to taxation without an increase in service rates in Oregon is the local requirement that a publicly-owned utility must pay off its debts within twenty years after they are incurred. A privately-owned public utility is exempt from this requirement.

It was recommended in 1933 by the Oregon Committee on Assessment and Taxation of Municipal Utilities that Oregon retain the law as it then existed in regard to the exemption of municipal utilities, for the following reasons:

(1) The amount of exempt property owned by municipal utilities in Oregon was inconsiderable.

(2) The continued exemption would tend to encourage hydro-electric power development during its early stages.

1. Calvin Crumbaker, "Shall Oregon Tax Its Municipally Owned Utilities?", Commonwealth Review of the University of Oregon, Vol. XIV, January, 1933, pp. 247-248.

(3) A tax would unduly burden the publicly-owned utility because of the strict legal requirements for the reduction of its debts.

(4) Tax exemption of the part of the municipal plant located outside of the city should be continued because of the evils to which taxation of such property is subject. For example, the outside property of the utility may be subjected to excessive special levies for the support of local schools. The levies are voted by those who have little property. Thus the utility patron must often pay tribute to rural school districts that are located many miles away but within which is located the utility's dam site property, or the like.

(5) The bondholders purchased the municipal utility bonds in reliance upon the continued exemption of the municipal's utility's plant from taxation.

(6) The surplus is often insufficient to pay a tax without an increase in the rates of service. Without a tax, the surplus can be used to make rate reductions possible, or to improve the plant, or it can be paid into the common fund.[1]

Calvin Crumbaker has stated a few additional arguments in favor of the tax exemption of publicly-owned utilities as follows:

(1) The publicly-owned utility is generally an agency of a municipality which is in turn an arm of the government and therefore should be free from taxation.[2]

1. Oregon Report of the Committee on Assessment and Taxation of Municipal Utilities (1935), pp. 8-27.
2. Crumbaker, op. cit., pp. 241-249.

(2) Publicly-owned utilities are more hampered by legal restrictions than those that are privately owned. The publicly-owned utility must usually wait for a vote of the people authorizing them to act. The publicly-owned plants are publicly managed and as such open to much interference. Every step in the management must conform to statutes, charters and ordinances.[1]

(3) Publicly-owned utilities, through tax exemption, force the privately owned utilities to reduce their service rates if they wish to remain in business.[2]

(4) The low rates bring industry into the municipality because of the cheap power. With the increase in industry the population of the municipality increases and results in higher values for municipal property.[3]

(3) Public Securities

Pollock v. Farmers Loan and Trust Company,[4] decided in the United States Supreme Court, held that "the national government must not impose a tax on the income derived from bonds issued by the states or their political divisions." The United States Supreme Court has, however, permitted a federal excise tax on corporations, although the interest derived from municipal bonds is included in determining the amount of the franchise tax. The Court has permitted such a tax because the tax does not interfere with a governmental

1. Idem.
2. Idem.
3. Idem.
4. 157 U.S. 429, 39 L.ed. 759 (1895).

power such as the power of borrowing money.[1] Further, the Supreme Court has held that the rent paid by a municipality and the interest on an award given for property taken through condemnation proceedings by a municipality are both taxable under the national law.[2] Moreover, it has been held that profits made on the exchange or sale of state or municipal bonds are taxable by the national government and also the interest on money borrowed to buy and sell such bonds.[3] The United States Supreme Court has held that public securities of the states and their political subdivisions are subject to the national inheritance tax.[4] The inheritance tax is a tax upon the right to receive property upon the death of a person and is not a tax upon the property itself.[5]

It has been urged by A. L. Powell that a national tax on state obligations may be justified because the early cases that denied the validity of such a tax dealt only with a special discriminatory tax on federal securities. For example, in McCulloch v. Maryland[6] the state tax held to be invalid was actually a discriminatory one levied upon the notes of the Second United States Bank, which was a federal instrumentality. Thus a non-discriminatory tax should be valid. Moreover, the national tax may be only incidental, as in the case of a corporate franchise tax that is measured by all the corporate income including that from the exempt bonds.[7]

1. Willcuts v. Bunn, 282 U.S. 216, 75 L.ed. 304 (1930).
2. Idem.
3. Idem.
4. Powell, op. cit., pp. 33-42.
5. Idem.
6. 4 Wheaton 316 (1819).
7. ~~Powell,~~ op. cit., pp. 118-124.

From a phrase of Chief Justice Marshall's, which occurs in the decision of McCulloch v. Maryland,[1] to the effect that "the power to tax involves the power to destroy," an implied national constitutional prohibition against the federal government's taxation of state instrumentalities and against the state's taxation of federal instrumentalities has been derived by the United States Supreme Court.[2]

The doctrine laid down in the McCulloch case "that notes issued by the National Bank were not taxable by the States" has been extended by the courts to the national securities,[3] salaries of federal officers[4] (now taxable[5]), federal franchises,[6] patents,[7] copyrights,[8] and public lands.[9]

In Collector v. Day[10] the doctrine of McCulloch v. Maryland[11] was applied to prevent federal taxation of state instrumentalities. It was held that on the same principle that the federal government was protected from taxation by the state, that the state should be protected from federal taxation.[12]

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1. 4 Wheaton 316 (1819).
2. Barnett, op. cit., pp. 262-264.
3. Securities. Weston v. City of Charleston, 2 P. 449 (1829).
4. Federal Salaries. Dobbins v. Erie Commissioners, 16 Pet. 435 (1842).
5. 306 U.S. 466, 83 L.ed. 927 (1939).
6. Franchise. California v. Central Pacific R. R. Co., 127 U.S.1(1888).
7. Patents. Long v. Rockwood, 277 U.S. 142 (1928).
8. Copyrights. People v. Assessors, 156 N.Y. 417 (1898).
9. Lands. Gillespie v. Oklahoma, 257 U.S. 501 (1922); Van Brocklin v. Tennessee, 117 U.S. 151, 29 L.ed. 845 (1886); Wisconsin Central R.R. Co. v. Price County, 133 U.S. 496, 33 L.ed. 687 (1890).
10. 11. Wall. 113 (1871).
11. 4 Wheaton 316 (1819).
12. Powell, op. cit., pp. 131-133.

The United States Supreme Court has held that a state cannot tax the gross income of a corporation derived from all sources, including exempt United States bonds, as the tax imposes a burden on the federal government that is beyond the state's power.[1] But in a recent decision the Court has permitted a state tax on the net corporate income, a part of which was derived from copyright royalties--a federal instrumentality.[2] In this case, the Court considered the burden upon the federal government caused by taxing the income from a federal instrumentality to be slight compared to the burden upon the state if the power to tax that income had been denied the state. For example, the power of a state to tax the shares of a national bank is granted and limited by a congressional act. Under this act a state can tax the capital shares of such banks, provided that they are assessed at the same rate as other capital shares of a similar kind located within the state, but not otherwise.[3]

A state tax on federal obligations such as checks and warrants available for immediate use was held to be valid as it did not burden the operations of the federal government. The checks and warrants are the same as money--the government is not burdened in its functions through the limitations on its agency. Further, a state tax on interest checks derived from federal bonds was held valid.[4]

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1. Northwestern Ins. Co. v. Wisconsin, 275 U.S. 136, 140-141, 72 L.ed. 202 (1927).
2. Educational Films Corp. v. Ward, 282 U.S. 379, 388, 75 L.ed. 400 (1930).
3. Owensboro National Bank v. Owensboro, 173 U.S. 664, 43 L.ed. 850 (1898); Citizen's National Bank v. Board of Equalization, 109 Or. 669, 672; 222 Pac. 341 (1924).
4. Hibernia Savings Society v. San Francisco, 200 U.S. 310, 315, 50 L.ed. 495 (1906).

The United States Supreme Court has held that the exemption from taxation granted veterans by the United States does not extend beyond the money or pension actually received from the government. Thus, a veteran must pay the state tax on lands purchased by him with the money received from the federal government. "Exemptions from taxation are not to be enlarged by implications if doubts are nicely balanced."[1] A deposit of warrants or checks received from the federal government by veterans is exempt from local taxation by Congressional Act[2] when the deposits are made in the ordinary manner so that the veteran may subject the proceeds of collection to demand draft.[3]

A New York case in 1923 held that money due to an individual from the federal government, as for bonds issued to buy gas masks during the World War, is not subject to state taxation since this would interfere with the federal powers to borrow money, declare war, and raise and support armies.[4] There is no federal case on this point.

In 1930, $17,091,000,000 worth of obligations of the states and their subdivisions were exempt from national taxation.[5] In 1935 the amount of national, state and local securities exempt from the national income tax was about $46,922,000,000.[6] In 1937, over $65,000,000,000

1. Trotter V. Tennessee, 290 U.S. 354, 356, 78 L.ed. 358 (1933).
2. World War Veteran's Act, 522, and Act of August 12, 1935, ff. 3 and 5.
3. Lawrence v. Shorn, 300 U.S. 245, 81 L.ed. 623 (1936).
4. People ex. rel. Astoria Light, H & P Co. v. Canton, 236 N.Y. 417, 141 N.E. 901, 30 A.L.R. 1498, (1923).
5. Powell, op. cit., pp. 54-64, 64-66, 97. C. O. Hardy, Tax Exempt Securities and the Surtax, New York: The Macmillan Company, 1926. L.T. Beman, Tax Exempt Securities, The Reference Shelf, New York: ~~H.W.~~ Wilson Company, 1925.
6. Idem.

of tax exempt securities existed in the United States. Of these, the banks owned forty-one percent. The life insurance companies and the banks together held about fifty-three percent of the tax-exempt securities.[1] It is this vast amount of tax-exempt securities that is causing the United States Supreme Court to limit so drastically the field of implied exemptions from taxation. Further, the need for revenue has vastly increased over what it was in the past.

The following are arguments for the abolition of tax-exempt securities:

(1) The limits thus placed on the taxing power of the nation and of the states are the cause for a net loss of revenue.[2]

(2) The exemption results in an undesirable distribution of investments because the wealthy invest in those securities that are tax exempt and the poor in those that are taxed. However, there are actually enough exempt bonds for all as the wealthy cannot corner all of them.[3]

(3) The exemption of public securities increases the cost of the distribution of the industrial securities. This is because the wealthy invest in the public securities that are exempt and leave the industrial for the small investor who buys in small lots, thus increasing the handling charges of the industrial securities. However, there is a compensatory effect since either the public or the

1. H. M. Groves, Financing Government, New York: Henry Holt & Company, 1939, p. 478 (pp. 475-492).

2. Tax Exemption in New York, Report of Joint Committee (1927), pp. 89, 90-92, 93-94, 94-95, 128. The Menace of Tax Exemption, pamphlet, 1921. Robins, K. N., The Menace of Tax Exemption, pamphlet, 1919.

3. Idem.

industrial security must bear the handling charges involved in sales to the small investor. Under tax exemption of public securities, it is the industrial security that bears this handling charge.[1]

(4) A privileged class is created by means of the exemption but members of all classes object to the tax exemption of public securities.[2]

(5) There is a violation of the principle of "ability to pay" a tax. Earned income has to pay a heavier tax than unearned, which is based largely on interest from tax-exempt government bonds.[3]

(6) Such an exemption causes a decline in the effectiveness of the surtaxes. Those individuals with a large income invest that income in the tax-exempt securities, thus causing their <u>taxable</u> income to fall from a high to a low bracketed income.[4]

(7) The exemption from taxation of public securities causes a scarcity of capital for private enterprise whose securities are <u>not</u> tax exempt. It is claimed that this is balanced to a large extent by the fact that the governments spend their money rather rapidly.[5] But private business is forced through the exemption of governmental securities to seek capital at higher rates of interest than the government need pay.[6]

(8) Extravagance and wasteful expenditure by the governments is caused by tax exemption of public securities. But it is doubtful if the abolition of the exemption would change the amount of governmental expenditure.[7]

1. <u>Idem</u>.
2. <u>Idem</u>.
3. <u>Idem</u>.
4. <u>Idem</u>.
5. <u>Idem</u>.

6-7. <u>Idem</u>.

(9) The advantage to the government of tax exemption has been exaggerated. Government bonds have had a good market and low rates of interest because they are generally considered to be a safe and secure investment.[1]

The following arguments are presented in favor of the continuance of the tax exemption of public securities:

(1) "Abolition of tax exempt securities would infringe on the principle of (national or) state sovereignty."[2] But the states may tax each other's securities.[3] A national tax on these securities would not be a greater burden. The national government would tax all states alike. That government would be the one most benefited as the amount of tax-exempt state and local securities is much more in amount than is the amount of tax-exempt national securities.[4]

(2) Abolition of exemption would increase the value of the outstanding exempt securities. However, only the sellers of the outstanding exempt securities would gain. The buyers would have large incomes subject to the income tax.[5]

(3) The loss of revenue to the federal government because of the exempt securities amounts to an actual subsidy for good roads, schools, and the like, to the states. If these securities were taxed, the national income taxpayer would have to make up the difference.[6]

1. Idem.
2. Report of Joint Committee, Tax Exemption in New York, pp. 89, 90-95, 128. "The Menace of Tax Exemption, 1921. Robins, op. cit.
3. Powell, op. cit., pp. 54-66, 97. Hardy, op. cit. Beman, op. cit.
4. Powell, op. cit., pp. 33-42.
5. Cf. footnote 2.
6. Idem.

The exemption of the local obligations from state taxation is also a subsidy to such political subdivision of the state.[1]

(4) Tax-exempt public securities result in lower interest rates on the bonds of the government and thus save the taxpayer money. The lower interest rates are a compensation for the diminished revenues. But it has never been shown that the reduction in interest rates was sufficient to offset the loss in taxes.[2]

At the present time the majority of the writers oppose any "further exemption from national taxation of the interest derived from state and local obligations".[3]

New York state exempts federal securities, its own and those of its political subdivisions when the securities are owned by individuals or partnerships. However, corporations must pay a franchise tax on the interest derived from these exempt securities.[4]

(4) Public Salaries

In 1871 in *Collector v. Day*[5] involving a tax on a state judicial officer's salary, "the court decided that Congress did not have the power to levy such a tax upon the compensation of a state officer".[6]

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1. Report of the Joint Committee (1927), *op. cit.*, pp. 89-93, 128. *The Menace of Tax Exemption*, 1921. Robins, *op. cit.*
2. *Idem.*
3. Powell, *op. cit.*, p. 97.
4. Cf. footnote 1.
5. 11 Wall. 113 (1871).
6. Powell, *op. cit.*, pp. 17-22. *Collector v. Day*. This case arose during a period of the revival of State's Rights following the Civil War. It was a period of reaction. Between 1870-73, six congressional acts were declared null and void by the Court. This was more than in the whole preceding period.

> The Court concluded that it is both reasonable and logical that whatever means the state may employ to carry on the operations of their governments should be as free and unimpaired by national taxation as the means employed by the national government to carry into operation the powers granted to it are exempt from taxation by the states. Such exemption is necessary as "the power to tax involves the power to destroy".[1]

In the dissenting opinion a different view prevailed, which, since March 27, 1939, is in effect the law. The dissent argued that all are citizens of the United States including the state officers; they are also under the protection and power of the national government and should be taxed as all should be treated equally.[2]

The doctrine of immunity of state officers from the national income tax has long been attacked.

> It is axiomatic that taxation should be universal and that every person in the jurisdiction of a government should contribute to the support of that government ~~in a proper proportion.~~[3]

Thus spoke the Committee on Tax Exemption of the National Tax Association in 1920. Further, the exemption is uneconomic because it is based on the source of income rather than on the amount which is the true criterion of ability to pay a tax.[4] At different times there have been before Congress proposals to amend the constitution in order to allow taxation of the salaries of state officers. The arguments here presented are also applicable to the immunity of national officers from state income tax.

1. Powell, *op. cit.*, p. 17.
2. *Idem.*, pp. 17-22.
3. *Idem.*, pp. 29-32, 111-116.
4. *Idem.*

In the United States no titles of nobility are allowed, but a group of untaxables exists in the public officers. Therefore, all should be taxed alike, as the officials are no better in this respect than private persons. The theory of tax exemption of state or federal governmental agencies rested on the nature of our dual system of government. Yet there is no reason to suppose that the people would consent to a tax that would destroy either the state or the national governments. Therefore all exemptions should end. This is true especially as to the national revenue laws, since they will affect all state officers' incomes of the same amount alike and at the same rate. But the taxing of federal official incomes by the states may not be proper because the tax rate will vary on the same amount of income from state to state. It will not be a uniform or equal rate as between all the states that a federal employee or officer would have to pay under a state income tax on the same amount of income. In addition to the protection afforded by the public opinion of the country against the abuse of taxation of public officials' incomes, the United States Supreme Court can protect the states and the federal government from destruction at the hands of one or the other government,[1] since statutes respecting the taxation of one grade of government by another grade of government are subject to review by the United States Supreme Court.

In Graves v. New York,[2] decided in March, 1939, the Court permitted taxation of the salary of a federal office by a state. In this case New York applied its income tax to the salary of the attorney for the Home Owner's Loan Corporation. The New York courts

1. Idem.
2. 306 U.S. 466, 83 L.Ed. 927 (1939).

held the respondent's salary to be free from taxation on the ground that the Home Owner's Loan Corporation was a federal instrumentality owned by the government and exempt from taxation by Congress. However, Congress did permit the states to levy surtaxes, estate, inheritance and gift, and realty taxes upon the corporation. The tax here is held to be non-discriminatory as it applies to all salaries whether governmental or industrial at a specified rate. It is not a tax upon the Home Owner's Loan Corporation or its property or income, nor is the tax one paid by the corporation or the government.

> It is laid upon income which becomes the property of the taxpayer when received as compensation for his services; and the tax laid upon the privilege of receiving it is paid from his private funds and not the funds of the government, either directly or indirectly. The theory, which once won a qualified approval, that a tax on income is legally or economically a tax on the source, is no longer tenable (citing cases) and the only possible basis for implying a constitutional immunity from state income tax of the salary of an employee of the national government or of a governmental agency is that the economic burden of the tax is in some way passed on so as to impose a burden on the national government tantamount to an interference by one government with the other in the performance of its functions.[1]

In a prior case, that of Rogers v. Graves,[2] the United States Supreme Court had held a state income tax on the salary of an employee of the Panama Railroad Company, a federal instrumentality, to be invalid. This case the present one overruled.

In the four cases that had granted immunity from taxation to the officers or employees of the government or its instrumentality, the Court had first found the instrumentality to be exempt from

1. Idem.
2. 299 U.S. 401; 81 L.ed. 306 (1936).

taxation and had then just assumed that the salary of an officer or employee of the government or instrumentality was exempt from taxation.[1] However, it was pointed out in Helvring v. Gerhardt[2] that the implied immunity between the grades of governments should be narrowly restricted.

> For the expansion of the immunity of the one government correspondingly curtails the sovereign power of the other to tax, and where that immunity is invoked by the private citizen it tends to operate for his benefit at the expense of the taxing government and without corresponding benefit to the government in whose name the immunity is claimed.[3]

The immunity from taxation should not confer benefits on the employees of the government through exempting their salaries from taxation or enable the government itself to engage its employees at a lower salary because of the exemption; "but (the exemption from taxation is) to prevent undue interference with the one government imposing on it the burdens of the other".[4]

The opinion of the Gerhardt case was to the effect that the employees of the New York Port Authority, an instrumentality created by the states of New York and New Jersey, were not immune from the federal income tax for these reasons: (1) the employees thus taxed enjoyed the benefits and protection of the United States government and were under a duty to contribute as citizens even though they were state employees; (2) the tax was not a burden on the Port Authority but rather on its employees; (3) the tax was a non-discriminatory one

1. 306 U.S. 466, 83 L.ed. 927 (1939).
2. 304 U.S. 405, 82 L.ed. 1427 (1937).
3. 306 U.S. 466, 83 L.ed. 927 (1939).
4. Idem.

and could not be held to obstruct the function for which the Port Authority was created; and (4) "immunity would do no more than relieve the taxpayers from the duty of financial support to the national government in order to secure to the state a theoretical advantage; speculative in character and measurement and too unsubstantial to form the basis of an implied constitutional immunity from taxation".[1] The reasons set forth in the Gerhardt case for denying tax immunity apply equally to the Graves case because

> the burden on government of a non-discriminatory income tax applied to the salary of the employee of a government or its instrumentality is the same, whether a state or national government is concerned.[2]

In both the Gerhardt case and the Graves case, the tax in question is not levied on the governmental instrumentality but rather on its employees' incomes and therefore the immunity of a governmental instrumentality is not really in question.[3]

The case of Utah v. Van Cott[4] held that it would be proper for Utah to tax the income of the attorney for the Reconstruction Finance Corporation and the Regional Agricultural Credit Corporation, both of which are federal instrumentalities.

It was further stated in Graves v. New York that there is

> no difference in result whether the taxed income be salary or some other form of compensation, or whether the taxpayer be an employee or an officer of either a state or the national government, or of its instrumentalities. In no case is there basis for the assumption that any such tangible or

1. Idem.
2. Idem.
3. Idem.
4. 306 U.S. 511, 83 L.ed. 950 (1939).

> certain economic burden is imposed on the government concerned as would justify a court's declaring that the taxpayer is clothed with the implied constitutional tax immunity of the government by which he is employed.[1]

The cases of Collector v. Day and Rogers v. Graves, above referred to, are overruled insofar as regards the immunity of the salaries of officers or employees of one grade of government from taxation by the other grade. Thus the ultimate result of the case of Graves v. New York is that there is no longer an implied constitutional immunity so far as the taxation of government salaries is concerned; that such a tax levied by the state is not a burden on the federal government; and that the silence of the Constitution or of Congress gives no tax immunity unless a burden upon government results.[2]

Justice Frankfurter rendered a concurring opinion in which he states that the Court's reversal of its prior decisions was due largely to the presence of new members upon the bench. For one hundred and twenty years this Court had dealt with immunity from taxes. The tax immunity was based upon the dictum in McCulloch v. Maryland that "the power to tax involves the power to destroy". Justice Frankfurter continued stating that the dissent in Collector v. Day has become the law at the present time so that a state officer is subject to the federal income tax. Opposition increased against the decisions until they were finally overruled by Graves v. New York. "The ultimate touchstone of constitutionality is the Constitution itself and not what we have said about it."[3]

1. 306 U.S. 466, 83 L.ed. 927 (1939).
2. Idem.
3. Idem.

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Justices Butler and McReynolds rendered a dissenting opinion upholding the tax immunity of the federal salaries from state taxes. They also insisted that under the majority opinion the rates for taxation "depend on legislative discretion not subject to judicial revision". They said the vague intimations that this Court will prevent excessive or destructive taxation are valueless. "... it may be said that presently marked for destruction is the doctrine of reciprocal immunity that by recent decisions here has been so much impaired."[1]

Before the decision of the recent case of Graves v. New York, it had been contended that a federal constitutional amendment to give Congress the power to tax the salaries of state officers and to tax state securities was not necessary because a clause of the Sixteenth Amendment giving Congress the power to tax incomes "from whatever source derived" conferred this power upon Congress. H. Hubbard wrote in the Harvard Law Review for April, 1920, that the members of Congress meant by this clause of the Sixteenth Amendment to grant the power to Congress to tax the salaries of state officers and to tax state securities; that these members knew that the state, county and municipal treasuries were an overflowing source of income which it had been illegal to tax before the amendment; and that the members knew that such could be authorized only by a constitutional amendment.[2] Governor Charles E. Hughes of New York in 1910 opposed the amendment when it was up for ratification by New York state because he believed

1. Idem.
2. Powell, op. cit., pp. 31-32.

that under it Congress would be given power over an essential right of the state; that is, the power to tax the hitherto exempt income of state officers.[1] The opposite view was held by Elihu Root, Senator Borah, and Governor Fort of New Jersey.[2] A few years later the United States Supreme Court in Brushaber v. Union Pacific Railroad Company[3] held that the Sixteenth Amendment did not extend the taxing power of Congress but merely set aside the apportionment rule for direct taxes on the basis of population as between the states in respect to a levy of an income tax by Congress. Thus Congress could not, under the Sixteenth Amendment, tax a state instrumentality or salary of a state officer or employee.[4] In Graves v. New York no reference is made to the Sixteenth Amendment.

The state officers have always had to pay the federal taxes on tobacco, oleomargarine and gasoline.[5]

In Metcalf and Eddy v. Mitchell,[6] decided by the United States Supreme Court in 1925, it was held that "persons engaged by a state whose duties were prescribed by contract and held no office, were not entitled to national income tax exemption". This decision was a limitation upon tax immunity, even though the burden of taxation

1. Idem.
2. Idem.
3. 240 U.S. 1, 17; 60 L.ed. 493 (1915).
4. Powell, op. cit., pp. 31-32.
5. Idem., pp. 28-29; 124-131; 67-85.
6. Barnett, op. cit., pp. 276-278.

on the state was no less because the function was performed by a contractor rather than by an officer. Likewise, the income of an independent contractor for the federal government has been held by the United States Supreme Court to be subject to state taxation.[1] However, the decisions of Graves v. New York and Helvering v. Gerhardt permit the taxation of the salaries of governmental officers whether state or national. The person taxed may be an officer of the government or an independent contractor for the government. Thus, for all practical purposes, the distinction between a governmental officer and an independent contractor for purposes of taxation is at an end.

> The application of the principle (now overruled) which denied the validity to such a tax has required the observing of close distinctions in order to maintain the essential freedom of government in performing its functions, without unduly limiting the taxing power which is equally essential to both nation and state under our dual system.[2]

In Trinityfarm County v. Grosjean[3] the United States Supreme Court held that a state tax on the gasoline used by an independent contractor of the federal government was valid, as the burden it imposes "is consequential and remote and not one that is necessary or immediate or direct".

1. Silas Mason Co. v. Tax Commission of Washington, 302 U.S. 186, 197-201, 82 L.ed. 187 (1937). Atkinson v. State Tax Commission of Oregon, 303 U.S. 20, 22-25; 87 L.ed. 621 (1938).
2. James v. Dravo Contracting Company, 302 U.S. 134, 150, 82 L.ed. 155 (1937).
3. 291 U.S. 466, 472, 78 L.ed. 918 (1933).

B. Public and Private Instrumentalities

(1) Public and Private Instrumentalities Distinguished

All "public" property of a state or its political subdivisions is exempt from national taxation. But the so-called "private" property of a state or its political subdivision is subject to national taxation.[1] All property owned by the federal government is exempt from state taxation.[2]

The meaning of the word "public" varies greatly, depending upon the circumstances under which it is used and upon the changes in social conditions. There are several tests that determine what is "public" and what is "private". One is simply an historical test. Under this test it is determined whether the function is one generally performed by a private or governmental agency. If it is generally performed by a private agent, such as a private corporation, it is taxable; but it is not taxable if the function is one generally performed by governments.[3] Another test consists in ascertaining whether the state enterprise is for profit, and therefore private, which makes it subject to taxation.[4] The distinction between "public" and "private" is illogical, because a government can actually perform only public functions.[5]

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1. Collector v. Day, 11 Wall. 113 (1871). South Carolina v. United States, 199 U.S. 437, 50 L.ed. 261 (1905). Metcalf v. Mitchell, 269 U.S. 514, 70 L.ed. 384 (1926). Jamestown and Newport Ferry Co. v. Commissioner of Internal Revenue, 43 Fed. (2d) 929 (1930).

2. Gillespie v. Oklahoma, 257 U.S. 501 (1922). Van Brocklin v. Tennessee, 117 U.S. 151, 29 L.ed. 845 (1886); Wisconsin Central R. R. Co. v. Price County, 133 U.S. 496, 33 L.ed. 687 (1890).

3. Barnett, _op. cit._, pp. 268-73; 264-8; 260-1; 258-60.

4. _Idem._

5. _Idem._

Among the private or proprietory agencies of a state subject to national taxation are publicly-owned hospitals, state-owned banks,[1] and the like.[2]

State officers "engaged in the exercise of proprietory non-governmental functions of state or local government" are not immune from taxation under the national income tax law. Officers engaged in such proprietory non-governmental functions are those of irrigation districts, public parks, public hospitals, state-owned banks, and the like.[3]

The distinction between "governmental" functions which are exempt from taxation and "private" functions which are subject to national taxation was taken from the law of torts in respect to liability of a municipality for the torts that it or its agents had committed. A municipleity is liable for the torts committed in its "private" capacity, but not those in its "public" or "governmental" capacity. The distinction was taken from the law of tort liability of municipalities and applied to tax exemptions in the case of South Carolina v. the United States,[4] in 1905, in which it was held that a state liquor monopoly is subject to the federal income tax. The distinction was applied to prevent a burden arising on the federal government through this possible exemption of

1. Banks. State of North Dakota v. Olson, Collector, 33 Fed. (2d) 848 (1929). Appeal denied 280 U.S. 528 (1929).
2. Powell, op. cit., pp. 67-85.
3. Idem.
4. 199 U.S. 437, 50 L.ed. 261 (1905).

all state enterprises from federal taxation. However, in spite of the principle established in the South Carolina case, the distinction adopted is faulty in that it is extremely indefinite and uncertain. Just what functions are "governmental" or what functions are "private" cannot be foretold, but each situation must be decided as it arises. However, in Graves v. New York[1] it was held that an officer of the national government must pay a state income tax whether the officer performed a proprietory or governmental function. In Helvering v. Gerhardt[2] it was held that state officers must pay a federal income tax no matter whether the function performed by the state officer was proprietary or governmental. Thus, for all practical purposes, the distinction between "governmental" and "proprietary" function in the law of tax exemption has been abolished.

(2) Education

> Although the educational functions of a State are *per se* of a governmental nature, there are occasions when the state through its educational institutions ventures into the realm of private business as, for example, when conducting athletic exhibitions and concerts for profit, or operating extensive farm lands and public markets. In these latter functions, the educational institution is subject to national taxation.[3]

In Group No. 1 Oil Corporation v. Bass[4] it was held that the lease of Texas school lands to a private corporation for purposes

1. 306 U.S. 466, 83 L.ed. 927 (1939).
2. 306 U.S. 405, 82 L.ed. 1427 (1937).
3. Powell, *op. cit.*, p. 86.
4. 283 U.S. 279, 75 L.ed. 1032 (1931).

of developing the land for the production of oil was subject to national taxation as under Texas law the lease was a sale of the oil to the private corporation and therefore the production of oil was not carried on by a state instrumentality. A contrary result was reached in Burnett v. Coronado Oil and Gas Company[1] in respect to the lease of Oklahoma school lands to a private corporation for the production of oil. It was held that the lease was for the benefit of the public schools and thus a state instrumentality. Therefore, the private lessee corporation was exempt from national taxation. The tax was levied upon both the state's and the corporation's share of the proceeds. In Gillespie v. Oklahoma[2] the United States Supreme Court decided that, since the Indian lands were federal property and exempt from state taxation, the net income derived from these lands by a private lessee was not taxable by the state. The Coronado case seems to have extended the immunity from national taxation to agencies used by an educational institution to raise revenue for education even though the agency was used as a private business. This appears to be an encroachment upon the distinction between governmental and proprietary function insofar as state education is concerned.[3] In regard to the taxation of incomes of government employees, this distinction has been recently entirely abandoned, as has been shown before. But in 1937, in Helvering v. Mountain Producers Corporation,[4] it was

1. 285 U.S. 393, 76 L.ed. 815 (1932).
2. 257 U.S. 501, 66 L.ed. 338 (1922).
3. Powell, op. cit., pp. 86-93, 93-96.
4. 257 U.S. 501, 66 L.ed. 338 (1922).

held by the United States Supreme Court that a tax, either state or federal, on the income of a lessee, derived from a lease of government-owned or controlled lands is valid as it does not interfere with the governmental activities of the government concerned, and Gillespie v. Oklahoma and Burnett v. Coronado Oil and Gas Company were expressly overruled.

(3). Municipal Activities

In Oregon, by statute all the property owned and used by a political subdivision of the state is exempt from taxation.[1] The Oregon Supreme Court has declared:

> Property of a municipal corporation used for public or corporate purposes is exempt from taxation by the state or county in which it is situated whether the property is within or without the municipality by which it is owned.[2]

Oregon requires that municipal property be both owned by a municipality and used for a municipal purpose in order to be exempt from taxation. Thus it was held that where land owned by a municipality was rented at a nominal annual rental for a long period of time, the land is not exempt from taxation because although municipally owned it was not used for a municipal purpose.[3] However, in a later decision, the Oregon Court has held that where the city has the power to lease a fire station and does so for a short period of time to an individual for use as a store and receives a substantial rental, the fire station is nevertheless considered to be used for a corporate purpose and thus exempt from taxation.[4]

1. Oregon Code, 1930, Supplement 1935, 69-105.
2. City of Eugene v. Keeney, 134 Or. 393, 397-8; 293 P. 924 (1930).
3. Idem.
4. City of Portland v. Multnomah County, 151 Or. 504, 510-11, 50 P. (2d) 1145 (1935).

Oregon statutes also exempt county roads and municipal streets from state taxation so long as the roads and streets are used by the public.[1] Furthermore, by Oregon statutes, a city is exempt from the interest and penalty imposed upon a delinquent taxpayer's property which is acquired by the city through foreclosure or settlement of the tax lien on the property. The state by statute has a similar exemption although the tax lien on the property so acquired continues until it is paid in full.[2]

1. Oregon Code 1930, 69-109.
2. Oregon Code, Supplement 1935, 69-780a; Oregon Laws 1937, Ch. 331, Sec. 4.

B. Taxation of Transitional Property

The United States Supreme Court has held that land owned by the federal government is free from state taxation unless it has been transferred to private hands by a patent or final certificate.[1] By statute in Oregon, the assessor is to assess all the improvements made on federal Homestead Lands as personal property, and when the certificate is issued for the land, the land also is to be assessed.[2] In 1915 the Oregon Supreme Court in Cannon v. Hood River Irrigation District[3] declared that

> where a homestead entry has been made under the laws of the United States, final proof submitted, and final certificate issued, it operates to transfer an equitable estate, and immediately renders the land liable to taxation, although the United States holds the title until the patent issues.[4]

The Oregon Supreme Court has held that upon the exchange of lands by the United States with a railroad, no tax by the state can be levied on the land as long as equitable and legal title remain in the United States. A receipt for payment in full for the land is sufficient to make the land subject to state taxation.[5] The Oregon Court has held that

> lands earned, and the selected indemnity lands to which the railroad is entitled to receive a patent, are subject to taxation the same as the lands for which it has received a patent. . .[6]

But unselected lands are exempt until selected by the railroad company.

1. Van Brocklin v. Tennessee, 117 U.S. 151, 29 L.ed. 845 (1886). Wisconsin R.R. Co. v. Price County, 133 U.S. 496, 33 L.ed. 687 (1889). Trimble v. Seattle, 231 U.S. 683, 58 L.ed. 435 (1913).
2. Oregon Code 1930, 69-110.
3. 79 Or. 71, 76, 154 Pac. 397 (1916).
4. Idem.
5. Johnson v. Crook County, 530 Or. 329, 331-2, 100 Pac.294 (1909).
6. O & C. R.R. CO. v. Lane County, 23 Or. 386, 31 Pac. 964 (1893).

In Oregon, by statute, the purchaser of lands from the state is the owner, even though the lands are held by him under a contract for the purchase thereof from the state or any political subdivision of the state. However, if the contract of purchase is cancelled prior to the assessment roll's becoming the tax roll, the assessment must be cancelled, and the land and improvements on the land become state property again and therefore exempt from taxation.[1]

The United States Supreme Court has held that lands owned by the federal government for the Indians are exempt from state taxation, but if the land has been deeded to the Indians, then the lands so held by the Indians are not exempt from state taxation.[2]

The Oregon Supreme Court has held that realty, the title to which is vested in the state or held in trust for the state's sole benefit, is exempt from taxation, but not that in which the state has an indirect interest, such as the interest of a mortgage.[3] The exemptions of charitable, educational and benevolent institutions are based solely on statute and are not in point where a building is given in trust to the University of Oregon, a state instrumentality. Exemption from taxation may depend on either ownership or use, or both.[4] The ultimate test for the exemption of public property owned by a political subdivision of Oregon is the use made of that property. But property owned by the state, and even though it is

1. Oregon Supplement 1935, 69-109; 69-716.
2. McCurdy v. U.S. 264 U.S. 484, 68 L.ed. 801 (1923).
3. Security Savings & Trust Co. v. Lane County, 152 Or. 108, 140-6, 53 Pac. (2d) 33 (1935).
4. Idem.

not used by the state it aids in maintaining the state functions. The University of Oregon is a state agency and property owned by it is exempt from taxation, irrespective of the use made of that property.[1] According to the decision in this case, title to the Miner Building in Eugene, Oregon, is in the Security Savings and Trust Company and not in the state. The income from the building goes directly through the state to a professional chair at the University. The state neither possesses title to the building nor does the state have control over the sole beneficial use of the income derived from the building.[2] Thus, the building was not in 1935 exempt from taxation; but since then, the state has been granted title and the building is now tax exempt.

1. *Idem.*
2. *Idem.*

V. Summary and Conclusions

At present public property that belongs to any unit of government is generally presumed to be exempt from taxation. A government should not tax its own property because such taxation would merely be a bookkeeping process. On the other hand, a government should tax the income of its officers and employees because a tax should be levied according to one's ability to pay and not in respect to the source of his income. Furthermore, the payment of an income tax by an officer of one grade of government to another grade of government which levied that tax does not in any way burden the grade of government whose officer's income is being taxed.

The property of one unit of government is, in the absence of statute, exempt from taxation by another unit of government. But such an exemption places an unnecessary burden upon the servient unit to protect the property exempted and gives the dominant unit a benefit from the property it owns but without the burdens of taxation or protection. Thus it is that the dominant unit should at least pay a money contribution in lieu of the taxes to the servient unit.

Municipally-owned public utilities are generally exempt from taxation. This exemption is granted because the municipally-owned utility is a part of the state, results in lower service rates, and, as in Oregon, the utilities must meet rigid debt limitation requirements.

A privately-owned public utility has no such requirement. This legal requirement also makes it hard to tax the public utility without resulting in an increase in the service rates. However, the exemption of public utilities from taxation should be abolished because the exemption shifts the tax burden onto the other taxpayers. Furthermore, the consumer of the utility's product and the taxpayer are not always the same person, as the utility often extends its services far beyond the limits of the taxing unit.

Public securities are generally exempt from taxation whether the security be that of the taxing government itself or of another unit of government. Such immunity arises from the idea that "the power to tax involves the power to destroy". However, the national government can tax the interest derived from municipal bonds or subject the state obligations and those of its political subdivisions to the national inheritance tax. Likewise, the state can tax the net income of a private corporation even though a part of that income is derived from a federal copyright royalty. Tax exemption of government bonds is supposed to result in lower rates of interest for bonds. But public securities should be taxed because exemption places a limit on the state and national taxing power, results in waste and extravagance in government and the advantage to the government of tax exemption has been exaggerated since the good market and low interest rates for government bonds depend upon their reputations as a safe investment and is not due to the exemption from taxation.

The "public" property of a state is exempt from national taxation but not its "private" property or "proprietary" agencies such as public hospitals, state-owned banks, and a state liquor monopoly. The distinction was created by the United States Supreme Court to prevent a burden upon the federal government through the possible exemption of all state enterprises from federal taxation. The income of the lessee of government-owned lands is subject to a state or federal tax. In Oregon municipally-owned property, to escape taxation, must also be used for a municipal purpose. Property procured from either the state or nation to which the private individual has either equitable or legal title is subject to state taxation. In Oregon, by decision, realty, the title to which is vested in the state or held in trust for the state's sole benefit, is exempt from taxation.

From these considerations, the writer has come to the conclusion that all exemptions of public property should be abolished, except that a government should not tax its own property, as that would be a mere transfer of money from one pocket to another. Aside from this, taxation of public property should be the rule.

PART II

PRIVATE PROPERTY

A. In General

The exemption of private property from taxation becomes a most important problem during a period of stress, such as the recent depression of 1929.[1] The power to tax includes the power to make reasonable exemptions of property therefrom except as limited by the Constitution.[2] In 1917 the Oregon Constitution, Article IX, Section 1, was amended so that the part of the original article which provided for the exemption of municipal, educational, literary, scientific, religious or charitable property was omitted, leaving all exemptions to the discretion of the state legislature.[3]

In Oregon the tax day is the all-important time for determining whether a given piece of property is taxable or not. If the property on the tax day is owned by persons who are taxable, then the property is taxable for the current fiscal year even though on the following day the property is conveyed to persons who possess the privilege of exemption from taxation. Likewise, if the property is owned by persons who are exempt from

1. C. J. Tobin, The Exemption from Taxation of Privately Owned Real Property Used for Religious, Charitable and Educational Purposes in New York State, 1934, pp. 13,15,19-20,21-27,27-29,29-33, 34-64.

2. W. W. Soper, Legal Limitations on Rights and Powers of School Boards, Columbia University, 1929, pp.46-55,71,69-70,55-62,62-69.

3. Oregon Constitution, Article IX, Section 1 (1917).

taxation and is used by them for the exempt purposes only on the tax day, then the property is exempt from taxation for the current fiscal period, even though it be transferred to persons who are not so exempt by law on the following day.[1]

The power to exempt property from taxation may be delegated by the state to a political subdivision of the state.[2] This delegation must be done by express grant of the state constitution or of a statute as the power to exempt property from taxation is not implied from the grant of the power to a political subdivision of a state to tax property.[3] Exemption is based upon the concurrence of ownership and use.[4]

Statutes granting exemptions are to be strictly construed with any uncertainty that may arise being resolved in favor of the state. "But there is a tendency to a more liberal construction when religious, charitable, benevolent, and educational institutions are concerned."[5] However, no exemption is implied and it must be expressly stated in the constitution or statute.[6] The law does not favor the exemption of private property. The Oregon Supreme

1. Oregon Laws 1937, Ch. 351, Sec. 1.
2. Soper, loc. cit.
3. Whiting v. Town of West Point, 88 Va. 905, 14 S.E. 698, 15 L.R.A. 860, 29 Am. St. Rep. 750 (1892).
4. Soper, loc. cit.
5. State ex. rel. Hatch v. Phipps, 136 Or. 454, 459-62, 299 P. 1009 (1931). Ballou v. Fisher, 154 Or. 548, 553, 556, 61 P. (2d) 423 (1936).
6. Soper, loc. cit. Corporation of Sisters of Mercy v. Lane County, 123 Or. 144, 152-156, 261 P. 694 (1927).

Court has held that "exemption from taxation must rest upon some substantial difference between the income exempted and that taxed".[1] In other words, the classification between taxed and exempted property must be reasonable, or the equal protection of the laws as guaranteed by the Fourteenth Amendment of the Federal Constitution will be violated.[2] In Oregon the requirement for a reasonable classification for tax exemption is necessary also under Article IX, Section 1, and Article I, Section 32, of the state constitution, both sections requiring that the rules of assessment and taxation shall be uniform on the same class of subjects.[3]

An exemption from taxation is a privilege personal to those to whom it is granted and cannot be transferred with a conveyance of the property unless the new purchaser is one who is also exempt in his own right. Furthermore, taxes become payable that have already accrued, and at the time of the enactment of an exemption statute are not freed from payment by that statute.[4] The source of an exemption from taxation varies as it is found sometimes in the Constitution, sometimes in a statute, and sometimes in a special charter.[5]

1. State ex. rel. Harth v. Phipps, 136 Or. 494, 459-62, 299 P. 1009 (1931). Ballou v. Fisher, 154 Or. 548, 553, 556, 61 P. (2d) 423 (1936).
2. Idem.
3. Corporation of Sisters of Mercy v. Lane County, 123 Or. 144, 152-56, 261 P. 694 (1927).
4. Cooper, loc. cit.
5. State and Local Taxation of Property, National Industrial Conference Board (1930), p. 34. J. P. Jensen, Tax Exemption as Means of Encouragement to Industry, Kansas Studies in Business, No. 10 (May, 1929), pp. 7, 9, 10-11, 12, 13-40, 42-51, 54-60.

In 1930, in the state of New York, the exemptions for religious and charitable purposes were not great. The churches then owned $670,000,000 worth of exempt realty, or about ten percent of the total, and the charities owned $108,000,000 of the exempt realty, or one and six-tenth percent of the total exempt realty. About one-fourth of the total exempt realty was privately-owned. In 1930 the total exempt realty in New York state was $6,700,000. This is about twenty-three percent of the taxable real estate in New York state.[1] In 1934 the total exempt private property in New York state was twenty-three percent of all exempt property and was five and eight-tenths percent of all the assessed property.[2] Tobin makes the statement that the New York State Tax Commission's figures showing the relation between the exempt and the taxable property is not accurate, since no complaint is ever made if the exempt property is assessed at an over-valued amount.[3]

In 1932, in Iowa, sixteen percent of all taxable tangible property was exempt from taxation. Fifty-four percent of the exempt property is governmental, and adding in the universities, the amount of public exempt property is sixty percent. Thus only forty percent of the exempt property is private. If all the exempt property were returned to or put upon the tax base, it is estimated

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1. Report of New York State Commission for the Revision of the Tax Laws, 1932, pp. 27, 120-123.

2. New York State Constitutional Convention Committee, Problems Relating to Taxation and Finance, 1938, Vol. X, pp. 201-206, 211, 212-219, 219-222.

3. Tobin, loc. cit.

that in Iowa the property tax could be reduced ten percent without affecting in any way the amount of revenue.[1]

In 1925, in Connecticut, one-sixth of all the taxable property was exempt from taxation. About one-half of the exempt property was private. Even so, this was a better situation than existed in many other states. This was probably due to the fact that the state of Connecticut was a pioneer in the study of the effects of exempting property from taxation and in keeping a record of the amount of property so exempted.[2] There are even yet very few states that have made such a study. No such study has been made in Oregon.

One-fifth of the national wealth was tax exempt in 1921, leaving the remainder of the wealth to bear a greater burden due to that exemption.[3] Schwab states: "Exemptions exist either from direct statutory action, from defective, ineffective and slovenly legislation, and finally from poor administrative methods."[4]

The inefficient administration is due largely to the obsolete, obscure and outgrown statutes, and is not necessarily due to the inefficiency of the officials. The laws should be strictly enforced. The strict enforcement of the laws would show those that are antiquated and thus result in their repeal. Another proposed

1. Survey of Administration in Iowa, Institute for Government Research of Brookings Institution, Washington, D. C., 1933, pp. 30-34, 115, 126-127.

2. State of Connecticut, Quadrennial Statement by the Tax Commissioner of Property Exempted from Taxation, 1926, pp. 3-21.

3. Soper, loc. cit.

4. J. S. Schwab, Exemption of Personal Property in New York, New York: J. B. Lyon Company, 1914, pp. 1-14.

remedy is a standardization of the methods of assessment and collection under the control of a central agency such as the State Tax Commission.[1] The Connecticut Tax Commission recommended in 1926 that the statutes granting exemptions from taxation should be clarified so that the property exempted might be clearly and definitely stated and that all exemptions from taxation should be strictly limited to the statutory provisions.[2]

The New York State Commission for the Revision of the Tax Laws recommended in 1932 that no further exemptions from taxation should be granted and that the future increases in the value of present properties of tax exempt bodies should be subjected to taxation.[3]

In New York the following reasons have been found as to why real property exemptions increased from 1925 to 1930:

(1) Growth of practice of assessing exempt property as well as taxable property at more nearly its true value.

(2) Flow of property from the taxable class to the exempt class through legislative mandate or statute.

(3) Normal yearly increase in exempt buildings.[4]

For example, such buildings as those for schools, court houses, administration, and the like, greatly increased in number during the five-year period.[5]

1. Schwab, op. cit.
2. State of Connecticut report, op. pp. 3-21.
3. Report of New York State Commission for the Revision of the Tax Laws, 1932, pp. 27, 120-123.
4. B. Bailey, Tax Exemption in New York, Memorandum Number Nine; Report of the New York State Commission for the Revision of the Tax Laws, p. 7.
5. Idem.

The Connecticut Temporary Commission to Study the Tax Laws of the state in 1934 made the following classification of exemptions from taxation:

(1) Illegal exemptions, as for example, those granted by the cities to certain industries if they would locate in the city concerned, although the city was not authorized by the state legislature to make such an exemption. This type of exemption is now rapidly disappearing.

(2) Technical exemptions are those exemptions from the general property tax of certain properties only because they are taxed in other ways. Such an exemption is really a method of taxation rather than an exemption therefrom.

(3) True exemptions are those granted by law to certain properties because of their character, ownership or use. The property is usually exempt because it may be performing a public service without profit or be used for a public purpose, or in order not to deprive an individual or his family of the means of livelihood.[1]

A New York Joint Committee found in 1927 that little substantial injustice was done the localities because of the exempt real estate. The harm was more apparent than real. A tax assessor looks with envy upon exempt property and compares the total exempt property with the total taxable property. In a majority of

1. Report of the Connecticut Temporary Commission to Study the Tax Laws of the State and to Make Recommendations Concerning Their Revision, 1934, pp. 233-236.

the cases the locality actually derived a benefit from the tax exempt property, such as a charitable institution or university. In some cases, the benefit even goes so far that the entire local prosperity depends upon the exempt institution and its continuance in that locality. But where there is no local benefit, some measure of relief from the burden of the tax exempt property should be granted.[1]

While exemption may not cost anything, still it does not offer a solution for obtaining the aid of private individual or institutions in the performance of a public service. Railroads, grocery stores, and banks that are as necessary to the community as are those institutions, are not exempted from taxation.[2]

Every year demands are presented to the legislatures for tax exemptions; but they are always opposed by the tax officials.[3] A common reason for the position taken by the tax officials is that stated by the Connecticut Tax Commissioner: "Tax exemptions is a form of bounty which can never be regarded as a dignified way of meeting a felt public obligation."[4]

From 1909 to 1929 in Connecticut there has been a vast increase in exemptions from taxation amounting to about two hundred percent. This increase was largely due to the weakness of administration. It is only recently that the state of Connecticut has

1. Report of the Joint Committee on Tax Exemption in the State of New York, 1927, pp. 10-12, 79-80.
2. Idem.
3. Schwab, op. cit., p. 5.
4. State of Connecticut report, op. cit., p. 13.

required that applications for tax exemptions be submitted before any exemption will be granted. Most exemptions have been allowed without such an application until recently. After once the property was exempted, the property was never checked to see that it was still continuing to be used for the purpose for which the exemption was granted. But this periodic check-up should exist. Furthermore, the assessors are untrained men, often part-time officers, and are elected for short terms with meager salaries.[1]

A general change in property tax exemptions under present conditions (during the depression of 1929) would probably cause great hardships. The shrinkage of private incomes and the increases in taxes for the relief of the unemployed have reduced considerably the income of private charitable institutions since they no longer receive the large donations or bequests from wealthy individuals, as in the past. A taking away of the exemption from taxation from them at this time might end their very existence.[2]

1. Report of the Connecticut Temporary Commission to Study the Tax Laws of the State and to Make Recommendations Concerning Their Revision, 1934, pp. 236-240, 243-248, 270-271, 275, 342, 349, 447, 514-515.

2. Idem.

B. Literary, Benevolent, Charitable, Scientific, Educational and Religious Institutions

Either by constitutional or statutory provision in all the states, property used exclusively for religious, educational or charitable purposes is exempt from general taxation.[1]

An Oregon statute expressly exempts from taxation the personal property of all literary, benevolent, charitable and scientific institutions and also such real estate as they own and occupy for the purpose for which the said institutions were created. In addition, Oregon by statute grants tax exemption to the amount of all gifts made to institutions, fraternal societies, associations, funds, trusts, or corporations engaged in benevolent, charitable, educational or religious purposes. The exemptions is extended to gifts made to war veteran organizations that are organized within the state of Oregon.[2] Further, Oregon by statute grants exemption to all religious properties and burial lots and crematory association's properties so long as they are used only for religious, burial or crematory purposes.[3] Thus, land used for a store or shop owned by these institutions is subject to taxation.

In accordance with these statutes the Oregon Supreme Court has held that a part of a building owned by a benevolent society but not

1. C. L. Bartlett, The Tenure of Parochial Property in the United States of America, Catholic University of America, 1926, p. 97.
2. Oregon Laws 1937, Ch. 350, p. 356.
3. Oregon Code Supplement 1935, 69-104, 3-4.

used by the society for its benevolent objects is subject to taxation.[1]

Special assessments levied for the payment of public improvements or a particular type of public service are a special type of tax and are thus not included within an exemption from general taxation and must be paid.[2]

The Oregon Supreme Court has held that property bequeathed to the Christian Science Board is exempt from the state inheritance tax as the bequest is to a charitable and religious organization.[3]

The exemption of church property, composed mostly of real estate, from taxation is actually a grant by the state in support of the church. The same result is attained as though the government appropriated money from the public treasury expressly for the church.[4] The reasoning presented herein in regard to the exemption of church property applies equally to the property of fraternal societies and of educational, benevolent, literary, charitable, and scientific institutions. Every dollar the church is exempted increases the burden on the remaining taxpayer. Nor does the fact that the church does social good through conducting charities, teaching morality, and the like, provide a sufficient reason for its exemption any more than should philanthropists, scientists, inventors, or educators be entitled to exemption from taxation. All receive

1. Benevolent Society v. Kelly, 28 Or. 173, 193, 42 P. 3 (1895).
2. Bartlett, loc. cit.
3. Poe v. State Treasurer, 144 Or. 561, 571, 25 P. (2d) 925 (1933).
4. But the Oregon Constitution, Article I, Section 5, states that no money is to be drawn from the public treasury for the benefit of any religious or theological institution.

their share of social advantages from the state and should be willing to pay for them and not force the state to raise its revenues from the baser elements of the population. While democracy is hostile to special privilege, still such a privilege is claimed by and is given to the church by reason of the exemption from taxation of its property.

Exemptions of church property from taxation should end for the following reasons:

(1) The church receives definite and regular services from the state the same as other organizations, and persons and should therefore be willing to pay their share of the taxes.

(2) Nor should a church be exempt merely because it makes no money any more than is a retired business man who is engaged in philanthropic enterprises.

(3) "Let the church be supported by those who accept its offer, and who desire to profit by its privileges."[1] It is no affair of the state or any other person.

(4) The church is actually commercial through its means of creating religious hysteria and then obtaining collections or pew fees. Since the church is commercial, it should pay taxes the same as any other commercial enterprise.

(5) Further, the church should pay taxes the same as other social or recreative institutions. None of these institutions is for profit.

1. J. F. Morton, Jr., Exempting the Churches, New York: The Truth Seeker Company, 1916, p. 56.

(6) The exemption of property owned by the church from taxation causes the church to accumulate vast amounts of property with great rapidity. As the church holdings that are exempt from taxation increase, so does the burden of the common citizen as a taxpayer increase.

Tax exemption of church property is a survival of the unity of the church and state. However, many persons today believe that the church should be exempt from taxation even though it has been separated from the state, and they base their position on the following reasons:

(1) The church discourages crime through its moral and religious teachings. But the home also does this and does not claim any exemption from taxation for this reason. Nor is the mere fact that one goes to church a sign that he is not a criminal, as it has been found that many of the criminals were church-goers. Further, it has been found that religion appeals to the higher intellectual men, few of whom are the criminals. Thus admitting that the church lessens crime, still it does not reach the rank and file of the criminal class. The church is only one of many institutions that morally uplifts the community. Still it is the only one that is tax exempt.

(2) The social and philanthropic activities of the church would be sorely crippled by a removal of the privilege of tax exemption. However, all churches would not be hurt by taxation but only the parasite churches: those with large surpluses that at

present do little or no social work. Even if the church were destroyed that did all of the social work, the persons in the church that carried on this social work would find other channels for social work. In addition, the church should be taxed since it uses its social services as a means of advertising itself and to spread its gospel to the injured or needy whom it cares for.

(3) It is urged that churches enhance the value of real estate. But if this is true, the exemption only aids a few individuals who own the surrounding properties at the expense of the public since the increase in value in the property is an unearned increment as the increase is due to society and the building up of the surrounding area. But not all adjoining owners desire the presence of a church and they might move away, thus causing a drop in the value of the land through depopulating the surrounding area.

(4) Precedent is against the taxing of the churches. This is an upholding of the old at the expense of new ideas of progress.

(5) As to the exemption of the country churches from taxation, it is based upon the cry of poverty, and in addition it is urged that without exemption the churches could not exist. This is an unsound argument, because the taxable property of the country church is of very low value, and thus the taxes thereon are extremely light. But the city churches are wealthy and there is more reason

that they be reached by taxation. They own the greater part of all the church property, and have at the same time a smaller membership in proportion to their wealth than do the country churches. In 1919 the property owned by the churches was estimated at $1,500,000,000. The services drawing upon this wealth performed by the churches use only a small part of the income therefrom. There would be enough left to pay the taxes, as would be only just.[1]

The blind, indigent, and orphaned persons are exempted from taxation because the state supports them and if they were taxed, the state would have to pay the tax to itself.[2]

It is contended that the taxation of educational or philanthropic institutions would result in driving private wealth in the form of donations or bequests from them and would thus result in the increase in the tax burden since the government would have to assume the functions that would otherwise have been carried on by private individuals; that private and public schools should be exempt because of the vast importance of education to a democracy; that the people must be educated in order that they may vote intelligently on the issues submitted to them and for the candidates that they are to elect.[3] But, in spite of all this, educational and philanthropic institutions should be taxed because they receive the benefits of government and by exempting them from taxation, the tax burden of those who pay the taxes is increased.

The property of a Greek letter house is not exempt from taxation as a charitable institution. Nor is it a benevolent society, as the latter aids others while the Greek letter house is beneficial to its

1. Morton, _op. cit._, pp. 1-84.
2. Soper, _op. cit._, p. 59.
3. _Idem._

members only. The house is only incidentally educational and scientific. The Greek letter house association merely prepares students for their life's vocation. The house is not legally connected with the educational institution.[1]

By decisions fraternal orders and social clubs are not exempt from taxation except as to their property used exclusively by them for public charity because most of their sick and death benefits apply only to their own members and in addition much of their property is not devoted to public charity.[2]

In Oregon properties of libraries, museums, and asylums are exempt from taxation by statute.[3] Private hospitals not operated for profit are exempt from taxation, but this exemption is unwise because it shifts the tax burden upon those who still pay taxes. Furthermore, institutions that derive income from the fees of their inmates are usually in a position to pay taxes and have no claim to state aid. A hospital not for profit is exempt by law in Oregon as being a literary, benevolent, charitable or scientific institution, and its property used therefore is likewise exempted. The exemption of a hospital as a charitable institutions is not affected by the acceptance of pay patients, as least when proceeds therefrom are devoted to hospital upkeep and to the extending of free treatment to pauper patients. Whether a hospital is charitable or not depends on whether it is one operated

1. Kappa Gamma Rho v. Marion County, 130 Or. 165, 174-79, 279 P. 555 (1929).

2. In re. Masonic Temple Society, 90. W. Va., 441, 111 S.E. 697, (1922). People ex. rel. Loyal Order of Moose v. Clark, 210 N.Y. S. 393 (1924); Appeal of Scottish Rite Building Co., 106 Neb. 95, 182 N.W. 574 (1921); New Standard Club v. [illegible], 111 Miss. 92, 71 S. 289 (1916).

3. *Oregon Code Supplement* 1935, 69-104 (3-6).

4. Soper, *op. cit.*, pp. 65-66.

for profit or for social service only. If it is operated for profit, it is taxable. All land or buildings belonging to a private charitable hospital that are reasonably necessary for the accomplishment of the hospital's purpose are exempt from taxation.

By an Oregon decision property held by a charitable institution such as a hospital was exempt from taxation, but once title passed from it to the First National Bank of Junction City as trustee for the bondholders, the exemption ended.

> Purchaser of exempt property at judicial sale does not acquire the privilege of exemption, unless the statute in terms provides therefore, or unless the exemption is appartenant to the particular property.[1]

In 1934 the property was sold to the Pacific Hospital Society, which is a benevolent and charitable institution incorporated in this state, and the property so sold is used for charitable purposes and is therefore exempt.[2]

The Oregon attorney-general is of the opinion that the Eastern Oregon Livestock Association, Incorporated, is exempt from taxation because it is a non-profit literary, benevolent, charitable or scientific institution for the betterment of the breeding and rearing of livestock.[3]

Since there is no means of measuring the value to society of the exempt property of an institution or of the institution

1. Waller v. Lane County, 155 Or. 160, 63 P. (2d) 214 (1936).
2. Idem.
3. Oregon Attorney-General Opinions, 1936-38, p. 444.

itself, a grant in aid should be allowed by the state rather than an exemption as the people will then know the exact amount of aid given to <u>the tax exempt institution</u>. With this knowledge the people can then determine whether the benefit received is worth the aid given to the tax exempt institution. Tobin claims that the benefit from tax exemption of private institutions far outweighs its cost to the public in New York state.[1]

Charitable, religious, educational and similar property should, it has been urged, ~~be exempt from~~ taxation because:

(1) Theyperform a meritorious service for the public. However, despite this, the exemption is opposed because it promotes the taking of property from the tax roll. Tax exemption increases the burden on those individuals who pay the taxes. In addition, there is a tendency for the exempt property to remain such even though it has passed from the hands of the exempted person or institution.

(2) Tax exemption relieves the public of costs for services that it would otherwise have to perform. However, the services within the proper sphere of government should be performed by it or by private groups that pay taxes. Tax exemption is usually for the benefit of a small group, while taxation is itself for the benefit of all.[2]

(3) There is an historical justification for the exemption of private property that has performed a public service. This is an

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1. C. J. Tobin, <u>The Exemption from Taxation of Privately-Owned Real Property Used for Religious, Charitable and Educational Purposes in New York State</u>, 1934, pp. 13,15,19-20,21-27,27-29,29-33,34-44. <u>Report of the Connecticut Temporary Commission to Study the Tax Laws of the State and to Make Recommendations Concerning Their Revision</u>, 1934, pp.236-40,243-48,270-271,273,342.

2. National Industrial Conference Board, <u>op. cit.</u>, pp. 38-39.

argument based on the theory that what has been should continue. However, such reasoning would stifle progress and should therefore be discarded.[1]

It seems clear, therefore, that taxation rather than exemption is the better policy.

War veterans are generally tax exempt by statute on sentimental grounds; and their widows are exempted for the same reason. In Oregon the war veterans' property is exempted up to a thousand dollars, and this exemption extends to his widow upon his death. In addition, the widow who remains unmarried after his death has a five hundred dollar exemption on the homestead.[2] But such exemption ~~is to be condemned~~, for it shifts the tax burden upon those who still pay taxes and such an exemption overlooks an individual's ability to pay a tax as shown by the size of his income or the amount of property that he owns.

1. Tax Exemption on Real Estate, Westchester County Chamber of Commerce, 1922, p. 80.

2. Oregon Laws 1937, Ch. 34, Sec. 1; Oregon Laws 1937, Ch. 241, Sec. 1.

C. Homesteads

Exemptions of homesteads from taxation ordinarily range from $2500 to $5000.[1] During the years 1936 and 1937 the homestead exemption from taxation had been rapidly spreading among the states of the American Union; but as yet Oregon has not adopted such an exemption.[2]

"Homestead exemption would appear in many cases to aggravate the present tax inequalities unless careful provision is made for replacement."[3] There are in general four methods for the replacement of lost revenues, as follows:

(1) A reduction in the number of public services rendered by the government.

(2) An increase in the assessment ratio in relation to the actual value of the property.

(3) Increase the levies on the remaining assessed property after deducting the exempt property.

(4) The use of other sources of revenue for the replacement of the lost revenue.

In regard to the above methods, the first one is not practical, the next two methods are often limited in their scope and operation by a constitutional tax limitation clause, and the fourth

1. H. L. Lutz, Public Finance, New York: D. Appleton-Century Company, 1936, pp. 550-551.

2. Dan E. Clark II, "Homestead Exemptions in Oregon," The Commonwealth Review of the University of Oregon, Vol. XX, November, 1938, pp. 641-691.

3. Homestead Tax Exemption, Research Department, Kansas Legislative Council, Supplementary Report, 1936, pp. 3-4.

method is thus the only one available. By this method state aid may be given to a local unit of government. For replacement the amount of revenue lost by the locality should be the basis for the compensation from other sources of revenue and not the amount of revenue needed by the locality. However, rather than the exemption of any class of property from taxation, all property should be reassessed on a scientific basis in order that the tax burden might be equalized among the taxpayers.[1]

The arguments in favor of the tax exemption of homesteads appear to be many, a few of which are stated below:

(1) Tax exemption of homesteads tends to aid the poorer classes in owning their own homes.[2]

(2) The homestead exemption is also an aid to real estate dealers in the selling of homes.[2]

(3) It is urged that the homestead exemption makes the legislators "expense conscious" since through the exemption the state loses revenue and must therefore curtail governmental activities or increase the tax rates.[2]

(4) Exemption of homesteads from taxation stimulates home building.[2]

(5) The tax exemption of homes has in it much of political appeal and value.[2]

(6) The exemption opens new fields to investments and makes mortgages more secure.[2]

1. Kansas Legislative Council report, op. cit., pp. 344.
2. Dan E. Clark, II, op. cit., pp. 641-651.

In opposition to the granting of homestead exemptions the following may be urged:

(1) Home ownership will not be promoted, since the amount of the exempted tax on the property will be added to the purchase price of the property. Furthermore, the buyer of a home does not concern himself to a very great extent as to what the amount of taxes is on the property.[1]

(2) The tenant laborer will pay more taxes because the home owner pays less. The homestead exemption applies only to the small home owner. Thus the tenant of a large land-owning landlord will pay more taxes because the taxes on the large land-owners' property will be raised by the exemption of the small home. The tenant will bear this increased tax because the increase in the large land-owners' taxes will be shifted to the tenant in the form of higher rents. In addition, the tenant laborer will also have to pay a replacement tax, such as the sales tax, etc. This is an application of the principle that tax exemption of one group of taxpayers increases the tax burden on those who remain.[1]

(3) The homestead tax exemption is a serious blow to the productiveness of the property tax, and even imperils the maintenance of governmental functions, especially in the localities.[2]

(4) Freed from taxes, the home owners would become indifferent to governmental spending.[3]

1. Idem.
2. Lutz, op. cit., pp. 552-553.
3. Clark, op. cit., pp. 641-651.

(5) Homestead exemptions are undemocratic since they favor a certain class only.[1]

(6) Furthermore, the tax on homes is only a small part of the home expense, which is made up largely of the actual building costs, the costs of subdividing the area, and the costs involved in the sales promotion.[2]

Thus from this study, it can be seen that arguments support taxation rather than exemption.

1. Idem.
2. Lutz, op. cit., pp. 552-553.

D. Business Property

Property owned and used by a particular class of business is often exempted from taxation in order that the business may be encouraged to locate in a certain place. The exemption is sometimes granted to prevent double taxation on growing crops and young stock, and to provide a subsistence level of living. It was used during the depression to guarantee the subsistence level of living by inducing an industry to remain in the locality because of exemption from taxation and thus enabled the locality to prevent unemployment. The exemption has also been used to promote agricultural fairs. Exemption has been used to improve or generate an industry. For example, the exemption from taxation of registered sires of any breed of animals should aid in the improvement of the livestock in that area.[1]

There are many different kinds of industries exempted, such as flax plants, steel companies, railroads, etc. The list varies from state to state. Such an exemption increases the burden on those who own the property that is taxed. In the west, constitutional restrictions limit tax exemptions very strictly; but as has been stated, there are no restrictions in Oregon.[2]

The assessing officers often illegally grant a partial exemption through the undervaluation of the business property assessed.

1. National Industrial Conference Board, State and Local Taxation of Property, 1930, pp. 32-53. J. P. Jensen, op. cit., pp. 7, 9, 10-11, 12, 13-40, 42-51, 54-60.
2. Idem.

The classified property tax is thus often used in an attempt to remedy the undervaluation of the property.

Industrial property under the classified property tax is taxed at a lower rate than other property, whereas under the general property tax it bears the same rate of taxation as does other property. Or in the place of the property tax on industry, a substitute tax may be used, such as a tax on income, or output, or a privilege tax. It often happens that when tangible property is fully assessed in spite of the fact that the statute exempts the mortgage from taxation. Further, there is sometimes allowed a deduction from the personal property tax of some part of the property included within the general property tax. This deduction is allowed even though it involves the cost of placing the property on the assessment roll and then striking it from that roll. This is a wasteful procedure both as to time and money.

An increase in exemptions from taxation is opposed generally by most economists. All property should be taxed equally without favoritism. Industry will tend of its own accord without tax exemption to find its best locations. "Commercial tax exemption is the local equivalent of the national tariff."[1]

It has been urged occasionally that for a short period of time there may be a very few industries that might possibly receive aid in the form of tax exemption. The infant industry argument is the best one for industrial exemption. By means of exemption from taxation it becomes easier to establish a new business in the locality

1. *Idem.*

granting the exemption. But the exemption should be withdrawn after a reasonable period of time. Because of inter-city or inter-state rivalry for industry, it is possible that tax exemption for industry might have to be resorted to in order to have industry come to the locality in question or in order to compete with other localities that granted tax exemptions to the industry. An exemption of a new industry should not deprive an old established one of its security. Exemption from taxation should not be used to attract migratory industries that leave the city or state as soon as the exemption is withdrawn. The exemption should be granted to the permanent industries only, if at all.[1] Many writers urge that tax exemption will bring industry to the city or state which grants the exemption, cause an increase in the property values and in the population, and so result in a reduction in the tax rate. But these writers overlook the fact that costs for police, fire, schools, and streets will also increase with the increase in population, and that increase in such expenditures must be at a higher rate than the increase in property values or population.[2]

In order to promote the reforestation of privately-owned land, a few states like Connecticut have by statute granted exemptions from taxation to the land replanted with trees for a ten-year period.[3]

1. Idem.
2. Idem.
3. Report of the Connecticut Temporary Commission to Study the Tax Laws of the State and to Make Recommendations Concerning Their Revisions, pp. 236-40, 243-248, 270-71.

E. Income and Inheritance Tax Exemptions

It is largely a matter of public policy as to how large the exemption is to be from the income and inheritance taxes. Incomes up to a certain annual amount are exempted by both the state and federal governments.[1] In Oregon, the exemption for the income tax is $800 for a single person and $1500 for a married person.[2] Such an exemption is granted to allow to each person a subsistence of living and because of the cost involved in collecting a tax from such a small income.[3] Opponents of the exemption claim that by taxing all incomes irrespective of amounts the taxpayers would become more conscious of the cost of government. Since practically everyone would be conscious of governmental expenditures, the people would be more sparing in the voting of extravagant expenditures.[4] Moreover, the revenues from the tax would thus be increased. Similar principles apply to the amount to be exempted under the inheritance tax. However, the exemption from the inheritance tax should be lower than that from the income tax, since the amount received by an heir is unearned in that he receives it through an accident of birth and the death of his ancestor. The legacy is not the result of effort or ability on the part of the recipient thereof. Charitable or educational institutions are generally exempted from the inheritance tax.

1. Survey of Administration in Iowa, Institute for Government Research of Brookings Institution, Washington, D. C., 1933, pp. 30-34.
2. Oregon Laws 1939, Ch. 488, Sec. 10, pp. 972-4.
3. Survey of Administration in Iowa, pp. 115, 126-127.
4. National Industrial Conference Board, Incorporated, Current Tax Problems in New York State, 1931, pp. 49-50.

The federal government in 1921 permitted certain exemptions from its income tax, many of which still continue. The income of churches, charities, the interest from tax exempt securites, and the like, was exempt from the income tax.[1] The amounts of the deductible exemptions from the income tax are generally expressed in terms of income. It is urged that this favors persons with large incomes over those with small incomes, since it enables those with a large income to escape the surtax on the higher progressive rates of the income tax. Wisconsin corrects this situation by permitting the exemption allowed to be expressed in terms of amount of tax rather than in those of income received.[2]

In a few states, such as Connecticut, certain corporations are exempt from the income tax, as, for example, the savings banks, building and loan associations, and insurance companies.[3]

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1. Report on Taxation and Tax-Exempt Income to 67th Congress, 1924, p. 19.
2. Survey of Administration in Iowa, pp. 126-127.
3. Report of the Connecticut Temporary Commission to Study the Tax Laws of the State and to Make Recommendations Concerning Their Revision, 1934, pp. 349, 447, 514-515.

F. Personal Property

Exemption from the general property tax does not necessarily mean exemption from taxation, as other taxes may be substituted therefore.[1]

It has been urged that the personal property tax be abolished because the poorer classes of the people should be exempted from taxation as they are now in fact; and in addition, the high cost of administering the tax plus the ease of its evasion makes it rather unproductive as a source of revenue. Yet it is better to continue this tax as the amount it returns lessens the burden on the other taxable property. Moreover, if the tax should be abolished, a vast amount of valuable property would be left untaxed. The classified property tax is a qualified remedy, whereby personal property is taxed at a lower rate than is other property.[2]

The argument has also been made that the intangible personal property tax should be abolished since it involves an unjust form of double taxation. The property itself is taxed under the tangible property tax and then the documentary evidences (mortgages, etc.) of that property are also taxed under the intangibles property tax. Much of the intangible property consists only of equities in tangible property that is thus doubly taxed as follows: Mortgages, bills and

1. National Industrial Conference Board, <u>State and Local Taxation of Property</u>, 1930, pp. 32-53.
2. <u>Idem</u>.

notes; money, other than gold, bank deposits; and corporate securities. However, all of these intangibles have a value separate and apart from the tangible property with which they are connected and should therefore be separately taxed.[1]

In Oregon there is no tax on intangible property, but there is an income tax on such property. The Oregon Supreme Court has held that an income tax on income generally and another on the income from intangible property alone is valid because such a classification is reasonable. The legislature has the right to levy a tax providing for different rates on different classes of property. "The Constitution does not require that either exemptions or rates shall be the same in all classes. It is satisfied with uniformity in each class."[2]

In those states that do not have the personal property tax, especially on intangibles, a substitute tax is used. But this tax is seldom satisfactory because it is hardly ever levied simply in lieu of the tax on the property exempted. It is often broader in scope and falls on some individuals who do not benefit from the exemption. In addition, the substitute tax may yield less revenue than was derived from the exempted property and thus increases the tax burden on the balance of the taxpayer's property.[3]

Automobiles or musical instruments are in the same states exempted from taxation because of the difficulty of an equitable administration of taxes in such cases.[4]

1. Idem.

2. McPherson v. Fisher, 143 Or. 615, 621-22, 23 P.(2d) 913 (1933). Oregon Constitution, Article IX, Sec. 1: "The legislative assembly shall, and the people through the initiative may, provide by law uniform rules of assessment and taxation. All taxes shall be levied and collected under general laws operating uniformly throughout the state." See Art. I, Sec. 32)

3. Lutz, <u>op. cit.</u>, p.550.

4. <u>State and Local Taxation of Property</u>, p.34.

In Oregon by statute the personal property of those persons who are infirm, aged, or in poverty, is tax exempt if he is "in the opinion of the assessor" considered to be unable to contribute his share to the tax fund.[1]

Moreover in Oregon by statute the household furniture and wearing apparel that is in actual use is exempted from taxation.[2]

Some states, such as Connecticut, by statute exempt the tools of the workmen and the food of their families from taxation, so that the individuals concerned may not be hampered in obtaining a livelihood.[3]

Oregon, in 1917, exempted all real and personal property of water cooperatives used for the transportation of water for domestic and irrigating purposes from taxation. But the water cooperative must be a non-profit organization.

Upon the close of the World War, in order to promote the American merchant marine, Oregon by constitutional amendment exempted all ships over fifty tons' capacity from taxation excepting those used for state purposes, until January, 1939. In 1935 the legislature passed an act exempting all vessels of fifty tons or more registered in Oregon from taxation from a rate higher than ten percent of the current consolidated tax levy; but ships in intercoastal or foreign trade shall be taxed only at the rate of one-fifth of one percent of the current consolidated tax levy.[4]

1. Oregon Code 1930, Supplement 1935, 69-104 (7-8)
2. Idem.
3. State of Connecticut, Quadrennial Statement by the Tax Commissioner of Property Exempted from Taxation, 1926, pp. 3-21.
4. Oregon Constitution, Article IX, Section b; Oregon Supplement 1935, 69-207.

In a state that has a personal or poll tax, such as Connecticut, there are many classes of persons exempted from its operation; as, for example, firemen, students and members of the militia.[1]

1. National Industrial Conference Board, *op. cit.*, p. 33. *Report of the Connecticut Temporary Commission to Study the Tax Laws of the State and to Make Recommendations concerning Their Revision*, pp. 514-515.

C. Limitations upon the Power of Exemption

Authorities on tax exemption have advanced many arguments for the limiting of the power of a legislature over the granting of exemptions from taxation. The arguments, in addition to some already mentioned, are as follow:

(1) Tax exemption is being carried too far and is not being limited to property used for public purposes only.[1]

(2) Tax exemption limits the amount of taxable property available for local revenues.

(3) A limitation on the power of the legislature to exempt property from taxation will provide an easier transition to a better policy.[2]

There is also much to be said in opposition to limiting a legislature's power over tax exemption, as follows:

(1) It is dangerous to limit the legislative powers as an unforeseen emergency might arise.[3]

(2) An abuse of power does not justify its denial.[4]

(3) A direct subsidy or tax exemption may be better in one case than in another. The determination of which is to be used should be left to the discretion of the legislature.[5]

(4) A direct subsidy would cost the public authorities substantial sums of money annually. Exemptions, it is claimed, do not increase the cost of government.[6]

1. New York State Constitutional Convention Committee, Problems Relating to Taxation and Finance, 1938, Vol. X, pp. 201-204, 211, 212-219, 219-222.

2-3. Idem.

4-5-6. Idem.

The New York constitution was amended in order to limit the legislature's power over the granting of exemptions from taxation. The amendment prohibited the use of special acts for exemptions. However, the effect of this amendment was to make the situation worse because the legislature now passed general acts whose scope is much wider than was that of the old special act. Thus, the attempted limitation was a failure.[1]

However, it is possible to lay down certain principles for a legislature to follow in the granting of exemptions from taxation, if exemptions are not completely abolished in that state. These principles, if followed, would do away with much of the injurious effects of tax exemption. The principles are:

(1) No exemption should be granted unless the legislature would be willing to make a direct grant of an equal amount to the exempt activity.

(2) The activity should be exempt from taxes only in the locality that it benefits.

(3) The amount of the tax exemption should be strictly limited.

(4) All exempt property should be assessed and entered upon the assessment rolls.[2]

1. *Idem.*
2. *Survey of Administration in Iowa*, Institute for Government Research of Brookings Institution, Washington, D. C., 1933, pp. 126-127.

H. Summary and Conclusions

Private property is presumed to be subject to taxation unless specifically exempted by a constitutional or statutory provision.

The property of literary, benevolent, charitable, scientific, educational and religious institutions is exempt from taxation because it performs a meritorious service for the public and relieves the public of the costs for services that it would itself otherwise have to perform. But the property of such institutions should not be exempt from taxation because it increases the burden on those who still pay the taxes and the services within the sphere of government should be performed by the government or by groups who pay taxes.

Homestead exemptions have been granted in order to aid the small home owner. However, it is urged that such a exemption from taxation would not greatly aid the small home owner as taxes are only a small part of the total home expense. But the real danger of such an exemption lies in the fact that the exemption deprives the local government of a large part of its revenues since the local government is largely dependent upon the property tax for its revenues.

Business property is sometimes exempted from taxation in order to get an industry to locate within the borders of the exempting unit of government. But this is a bad policy as all private property should be taxed. Further, industry will tend of its own accord without tax exemption to find the locations to which it is best suited.

The determination of the amount of the exemption from the income and inheritance taxes is a matter of public policy. The amount that is exempted from the income tax is granted to insure a subsistence of living to each person. Taxation of all persons no matter what the amount of their incomes would make all of the people conscious of the expenditures of the government and accordingly more careful in granting them. The amount exempted from the inheritance tax should be much less than that from the income tax because one's inheritance is due to an accident of birth and is not "earned".

Exemption from the personal property tax has been justified because of the cost of administering the tax plus the ease of its evasion. However, through such an exemption, a vast amount of valuable property would be left untaxed.

The writer has come to the conclusion that all private property should be subject to taxation, and that without exception. The reason is that equality of the tax burden is best served by denying tax exemption altogether.

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