Pennsylvania Constitution - Uniformity Clause - Excise Tax - Foreign and Domestic Corporations

Jolene M. Grubb

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Pennsylvania Constitution—Uniformity Clause—Excise Tax—Foreign and Domestic Corporations—The Pennsylvania Supreme Court has held the Excise Tax on Foreign Corporations unconstitutional since disparate tax treatment based solely on a taxpayer’s place of incorporation is an unreasonable classification and is therefore violative of the uniformity clause of the Pennsylvania Constitution.

_Columbia Gas Transmission Corp. v. Commonwealth, 360 A.2d 592 (Pa. 1976)._  

Columbia Gas Transmission Corporation (Columbia) is a foreign corporation authorized to do business in Pennsylvania.¹ Pennsylvania, pursuant to an act entitled Excise Tax on Foreign Corporations,² levied upon foreign corporations an excise tax of one-third of one percent on the amount of any increase of capital actually employed within the Commonwealth.³ Domestic corporations were taxed in the same period in which the tax on foreign corporations accrued under the Bonus on Capital Stock Act.⁴ This tax on domestic corporations was only one-fifth of one percent on the amount of stated capital and any increase in the same.⁵  

Columbia filed suit in the Commonwealth Court of Pennsylvania seeking to enjoin imposition of the foreign excise tax. It alleged, among other things, that the tax was violative of both the uniformity clause of the Pennsylvania Constitution and the equal protection clause of the United States Constitution.⁶ The commonwealth court

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³ The statute reads in relevant part:
   
   [E]very foreign corporation, in addition to complying with all the laws of the Commonwealth now or hereafter in effect, shall, for the privilege of exercising its franchises in Pennsylvania, pay . . . an excise tax of one-third of one per cent upon the amount of any increase of capital actually employed within this Commonwealth . . . .

_Id._ § 8002.

⁶ Columbia also contended that the foreign excise tax violated the commerce clause of the United States Constitution as a tax on interstate commerce, that its increases in capital were not properly apportioned under the applicable statutory formula, and that the credit Columbia received for domestic excise taxes paid by its predecessor was improperly computed. 19 Pa. Commw. Ct. at 526-27, 339 A.2d at 915. The supreme court rested its decision solely on the uniformity clause and found it unnecessary to deal with Columbia’s other contentions. 360 A.2d at 594 n.3. Cf. notes 34-38 and accompanying text _infra._
rejected Columbia's contentions of constitutional invalidity. It started from the premise that Pennsylvania accepted, as a reasonable distinction, a classification based solely on place of incorporation. Without referring to any justification offered by the Commonwealth for the different rates of taxation, the commonwealth court declared that the foreign excise tax involved a reasonable classification and therefore did not contravene any constitutional provisions.

In an opinion written by Justice Roberts, the Pennsylvania Supreme Court unanimously reversed the commonwealth court and declared the Excise Tax on Foreign Corporations violative of the uniformity clause. The court recognized that foreign and domestic corporations, as a practical matter, cannot be taxed identically. Absolute or perfect uniformity is not demanded by the uniformity clause. Rather, the state has broad taxing authority which includes the power to classify subjects differently for tax purposes. In order to meet the requirements of the uniformity clause, however, a classification must be based upon a reasonable difference between the

8. Id. at 538-43, 339 A.2d at 921-23.
9. 360 A.2d at 597. The Pennsylvania Supreme Court has never held that the parameters of the Pennsylvania uniformity clause and the federal equal protection clause are identical, but has generally looked to federal equal protection cases when a disparity in tax treatment is presented. See, e.g., Commonwealth v. Life Assurance Co., 419 Pa. 370, 374 n.8, 214 A.2d 209, 213 n.8 (1965) (so far as the reasonableness of classifications for purposes of taxation is concerned, uniformity clause and equal protection clause are "in pari materia"). See also Commonwealth v. Budd Co., 379 Pa. 159, 167, 108 A.2d at 563, 566 (1954) (corporate net income tax declared violative of the uniformity and equal protection clauses); Commonwealth v. Fireman's Fund Ins. Co., 369 Pa. 560, 565, 87 A.2d 255, 258 (1952) (license tax imposed upon foreign insurance companies held nonviolative of the uniformity and equal protection clauses since the tax merely created equality between foreign and domestic companies); Commonwealth v. Lukens, 312 Pa. 220, 224, 167 A. 167, 169 (1933) (classifying freight and baggage transporting companies apart from passenger transporting companies not violative of uniformity and equal protection clauses); Commonwealth v. Girard Life Ins. Co., 305 Pa. 558, 562, 158 A. 262, 263 (1932) (tax levied against insurance companies based on their corporate structure did not contravene either clause).
classes of taxpayers; otherwise, the distinction would be arbitrary and capricious and constitutionally infirm.\textsuperscript{11}

Justice Roberts observed that the Commonwealth had not posited a justification for the variant rates of taxation other than a corporation's place of incorporation. He relied on the United States Supreme Court's decision in \textit{WHYY, Inc. v. Borough of Glassboro}\textsuperscript{12} for the proposition that such a distinction, without more, was an insufficient basis for differing tax rates and did not pass "constitutional scrutiny."\textsuperscript{13} Since the Commonwealth had not met its burden of demonstrating a valid reason for the disparate rates, the foreign excise tax violated the uniformity clause and was therefore unenforceable.\textsuperscript{14}

It is well established, in Pennsylvania and elsewhere, that classifying domestic and foreign corporations for tax purposes is within a state legislature's broad discretionary power subject only to constitutional limitations.\textsuperscript{15} The traditional test evolved for determining the validity of any classification is whether there is a reasonable basis for the distinction, or whether any set of facts can reasonably be conceived to sustain it.\textsuperscript{16} This minimal scrutiny standard places

\textsuperscript{11} See 360 A.2d at 595, and cases cited therein. In \textit{WHYY, Inc. v. Borough of Glassboro}, 393 U.S. 117 (1968), a nonprofit Pennsylvania corporation was authorized to do business in New Jersey. Although New Jersey allowed exemptions to domestic nonprofit organizations, it did not exempt similar organizations incorporated outside the state. The New Jersey Superior Court held that the tax classifications did not violate the equal protection clause. 91 N.J. Super. 269, 219 A.2d 893 (1966). The United States Supreme Court reversed, finding no rational basis for the distinction. The Court concluded that appellant had been denied equal treatment because the distinction was based solely on the different residence of the owner and not because of any difference in the state's relation to the decisive transaction. 393 U.S. at 120. For further analysis of the relationship between \textit{Columbia} and \textit{WHYY} see text accompanying notes 34-38 \textit{infra}.

\textsuperscript{12} 393 U.S. 117 (1968). See note 11 \textit{supra}.

\textsuperscript{13} 360 A.2d at 595.

\textsuperscript{14} Id. at 597.


the burden upon the taxpayer challenging the tax to prove that no rational basis for the classification exists. Absent such a showing, the classification will not be deemed arbitrary and capricious and in violation of constitutional standards. In some instances, courts themselves have discerned a reasonable basis even when the legislature has not stated the purpose for a particular classification. The

(1926) (corporate and individual taxicab owners). As early as 1905, the Pennsylvania Supreme Court, in sustaining the constitutionality of a classification of real estate having the same market value into three different classes stated: "It is too late in the day in Pennsylvania to question the power of the legislature to classify subjects of taxation on broad lines and within certain limitations. The reasons for such classification, based upon imperious necessity, are . . . numerous, and have been . . . frequently discussed by the higher courts . . . ." Jermyn v. Scranton City, 212 Pa. 598, 602, 62 A. 29, 31 (1905).


There have been instances where no rational basis for a classification was found and the tax was therefore invalidated. See, e.g., WHYY, Inc. v. Borough of Glassboro, 393 U.S. 117 (1968) (foreign and domestic companies of similar nature). The test of reasonableness is applied on a case by case basis. It has been stated repeatedly that there is no "iron rule" of equal taxation. That is, each classification will be examined and if a reasonable justification exists for it, it will be upheld. See Allied Stores, Inc. v. Bowers, supra at 526, and cases cited therein.

In Life Assurance, the Pennsylvania Supreme Court summarized the purpose and guidelines of the test for reasonableness and its effects:

The essential question in testing the validity of [legislative determinations of classifications] is whether the distinctive treatment accorded rests upon substantial differences between the subjects so classified. . . . And where such distinctions rest upon differences recognized and acted upon by the business world, it is not within the province of the courts to intrude. . . . So long as the classification is neither capricious nor arbitrary, there is no denial of the equal protection of the law. 419 Pa. at 378-79, 214 A.2d at 215 (citations omitted).

Cases involving the constitutionality of tax classifications have placed the burden on the taxpayer to prove there is no reasonable justification for the distinction in question. See, e.g., State Bd. of Tax Comm'rs v. Jackson, 283 U.S. 527 (1931) (classification based upon number of retail stores owned); Quong Wing v. Kirkendall, 223 U.S. 59 (1912) (classification of hand and steam laundries); Philadelphia v. Depuy, 431 Pa. 276, 244 A.2d 741 (1968) (municipal electric and gas companies); Commonwealth v. Lukens, 312 Pa. 220, 167 A. 167 (1933) (classification of operations transporting passengers and freight).

See Allied Stores, Inc. v. Bowers, 358 U.S. 522 (1959), and cases cited therein. In Allied, the bases for the classification were not posited by the defendant, but the Court observed that a state legislature need not explicitly declare its purpose and went on to discuss
commonwealth court's employment of the minimal scrutiny test in *Columbia* to determine whether the foreign excise tax was an arbitrary and capricious classification was therefore consistent with past judicial standards for determining who should bear the burden of demonstrating the absence or existence of a constitutional justification for the particular tax measure.\(^{20}\)

Although the Pennsylvania courts have upheld a multitude of classifications involving the taxation of domestic corporations and businesses,\(^{21}\) the propriety of classifying foreign and domestic taxpayers has not been extensively litigated in Pennsylvania. Nonetheless, existing case law in Pennsylvania seemed to support the view that a tax classification based on a corporation's state of incorporation would pass muster under the uniformity clause regardless of whether the Commonwealth presented any other justification for the uneven tax treatment. *Germania Life Insurance Co. v. Commonwealth,*\(^{22}\) cited by the commonwealth court in *Columbia,* was one of the earliest decisions examining the foreign-domestic distinction. *Germania,* a nineteenth century case, involved a foreign corporation doing business in Pennsylvania that was taxed at a rate different than the rate for domestic corporations.\(^{23}\) The Pennsylvania Supreme Court held that foreign corporations may be placed in a class and taxed apart from domestic corporations.\(^{24}\) The *Germania* court did not address the question of who was to bear the burden of establishing a justification for distinctive tax treatment, but the clear implication was that the foreign-domestic distinction was constitutionally justified where similar companies were incorporated in different states.

Had *Germania* been the only relevant precedent, perhaps the commonwealth court would have questioned the decision's continuing vitality. The court perceived that decision to have been revital-

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\(^{20}\) The Supreme Court found a conceivable basis the legislature could have intended. The Supreme Court found a conceivable basis for the classification and held the tax enforceable. *Id.* at 528-30.

\(^{21}\) Compare *id.* at 528, with 19 Pa. Commw. Ct. at 542, 339 A.2d at 923: "Further, the classifications will be upheld if any set of facts reasonably can be conceived that would sustain them. The Foreign Excise Tax on Corporations meets these tests."

\(^{22}\) *See* cases cited at note 16 supra.

\(^{23}\) Germania, a foreign insurance corporation, was taxed at a rate of three percent on premiums paid to the corporation while domestic insurance companies were taxed only one half mill for each one percent of dividends made. *Id.* at 514.

\(^{24}\) *Id.* at 519.
ized, however, by more recent Pennsylvania cases which did not involve a distinction between domestic and foreign corporations but arguably reaffirmed the result as well as the standard of review used in Germania. In both Commonwealth v. Life Assurance Co.\textsuperscript{25} and Alco Parking Corp. v. Pittsburgh,\textsuperscript{26} the Pennsylvania Supreme Court upheld taxing classifications using a rational basis standard.\textsuperscript{27} The court in both of these cases stated that the burden of showing a classification employed by the Commonwealth to be not reasonable lies with the party attacking the tax.\textsuperscript{28} Life Assurance cited Germania as precedent for sustaining distinctive tax treatment due to bona fide differences between corporations,\textsuperscript{29} and in Alco the court added that a taxpayer's burden of proving that a particular classification is unreasonable is "a heavy one."\textsuperscript{30}

The supreme court's opinion in Columbia appears to represent a break from its prior view on the relationship between the state's taxing power and those subject to the tax. Although it was not expressly overruled, it seems clear Germania cannot stand alongside the Columbia court's approval of the Supreme Court reasoning in WHYY, Inc. v. Borough of Glassboro.\textsuperscript{31} The court in Columbia did not address the question whether the commonwealth court had properly interpreted the prior decisions in Life Assurance and Alco, but rather distinguished Life Assurance factually\textsuperscript{32} and did not refer to Alco. Yet, from the standpoint of assigning the burden of proof, these three cases are difficult to reconcile. The taxpayer in Columbia showed no more than a disparity in taxing rates,\textsuperscript{33} and the

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\item \textsuperscript{25} 419 Pa. 370, 214 A.2d 209 (1965).
\item \textsuperscript{27} See notes 16 & 17 and accompanying text supra.
\item \textsuperscript{28} 419 Pa. at 376-77, 214 A.2d at 214; 453 Pa. at 255, 307 A.2d at 857.
\item \textsuperscript{29} 419 Pa. at 379, 214 A.2d at 215-16.
\item \textsuperscript{30} 453 Pa. at 255, 307 A.2d at 857. See note 18 supra.
\item \textsuperscript{31} 393 U.S. 117 (1968). See note 11 supra; note 38 infra. See also Hanover Fire Ins. Co. v. Harding, 272 U.S. 494 (1926) (net receipts tax on foreign corporations held an unlawful discrimination against foreign companies in favor of domestic companies of the same class and therefore violative of the equal protection clause); Southern Ry. v. Greene, 216 U.S. 400 (1910) (franchise tax based upon foreign corporation's stock within the taxing state is an arbitrary classification based only on place of incorporation).
\item \textsuperscript{32} The court stated that Life Assurance was inapposite because there a rational basis existed for the tax rate distinction. 360 A.2d at 596. A rational basis for the disparate tax treatment also existed in Alco, since certain traffic-related problems were engendered by commercial parking lot operations which justified classifying them separately from public parking lots for tax treatment. 453 Pa. 245, 257, 307 A.2d 851, 858 (1973).
\item \textsuperscript{33} See 360 A.2d at 595.
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supreme court seems to have relegated to the Commonwealth the onus of setting forth valid reasons for taxing one class of subjects differently than another class. Without directly confronting the issue of the continued vitality of Germania, the court relied on WHYY to effectively emasculate Germania’s holding that a distinction based solely upon place of incorporation was a reasonable classification. In WHYY, the United States Supreme Court held that a classification based solely on state of incorporation was not a rational basis for distinction and therefore was in contravention of the fourteenth amendment equal protection clause. The Columbia court apparently accepted the principle that foreign corporations, once allowed entry into a state, are to be treated uniformly with domestic corporations; a distinction based merely upon the place of incorporation is an arbitrary standard of classification. Although the Columbia court said only that the foreign-domestic classification violated the Pennsylvania uniformity clause, it probably could have reached the same result relying exclusively on the Supreme Court’s application of the equal protection clause in WHYY.

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34. There is language in the court’s opinion indicating that in future cases, the Commonwealth must affirmatively come forth with justifications for a particular taxing scheme. After noting that “[n]o justification is offered by the Commonwealth for the disparity in tax rates,” 360 A.2d at 596, the court acknowledged the state’s “[failure] to point to any rational reason for the difference in tax treatment.” Id. The court summarized in its concluding paragraph: “The Commonwealth has shown no valid reason for imposing a higher tax rate on . . . foreign corporations . . . . We therefore conclude that the tax . . . violates the uniformity clause . . . .” Id. at 597.

35. 393 U.S. at 120.

36. The WHYY Court found no rational basis for the tax classification. Without such a showing, and absent any basis which the Court itself could discern, it held that a classification based solely on the place of incorporation was an arbitrary classification and was violative of the equal protection clause. 393 U.S. at 120.

37. 360 A.2d at 594 n.3, 597.

38. Columbia’s treatment of the appellant’s argument that the tax measure in question violated both the Pennsylvania uniformity clause and the Federal Constitution’s equal protection clause leaves unclear the supreme court’s position on the relationship between the two constitutional provisions. The court found the appellant’s equal protection argument “meritorious,” and the Supreme Court’s reasoning in WHYY “equally applicable” to the case before it. Id. at 594, 597. By expressly basing its holding on only the uniformity clause the Columbia court may, however, be suggesting that in deciding future allegations of unequal tax treatment the court will look to the state constitution, formulating its own standards. Perhaps the supreme court concluded that reviewing state taxing schemes under the equal protection clause, which would necessitate consideration of the United States Supreme Court’s treatment of identical or analogous claims, is unnecessary since the Commonwealth’s uniformity clause provides a ready means of assessing the legality of a particular tax. Although it was relatively clear under WHYY that classifying corporations by their state of
By placing the burden on the Commonwealth to justify its tax classifications, *Columbia* raises questions as to what the state must show in order to justify a particular taxing scheme. While it is clear that a classification based solely on place of incorporation is not enough, beyond that, little is certain. The court did not deal with whether there were any other justifiable reasons for the classification which would establish a rational basis for taxing domestic and foreign corporations differently. It is possible the Commonwealth could have demonstrated that regulating foreign corporations is more costly than overseeing domestic businesses and therefore a higher taxing rate is justified. Although there are indications in *Columbia* that the Commonwealth might have met its burden had it attempted to justify the disparate tax rates,39 Justice Roberts' observation that the court could not itself discern any justification for the classification40 may indicate that under no circumstances could this different treatment pass constitutional scrutiny under the uniformity clause. More importantly, Justice Roberts' opinion may indicate that the court is not yet willing to completely abandon the past practice of seeking a legitimate basis for the classification and upholding the scheme if it finds that such a basis exists.41 Since the court did not expressly state that it would no longer provide conceivable justification for the Commonwealth's taxing measures, such a possibility remains open. It would nonetheless seem prudent that in structuring future taxing classifications, the General Assembly should, through House or Senate debates, or by some other means, articulate its reasons for a particular classification to ensure that it survives judicial scrutiny.

Placing the burden on the Commonwealth to demonstrate some actual justification for tax classifications should be encouraged.42

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39. See id. at 596-97: "But in the absence of some concrete justification for differences in tax treatment, an arbitrary difference in tax rates cannot be tolerated." Justice Roberts also observed: "The Commonwealth has shown no valid reason for imposing a higher tax rate . . . . We therefore conclude that the tax is not . . . 'uniform . . .'" Id. at 597.
40. Id. at 595.
41. See note 19 and accompanying text supra.
42. See Gunther, *In Search of Evolving Doctrine on a Changing Court: A Model for a Newer Equal Protection*, 86 HARV. L. REV. 1 (1972), where the author analyzed the United States Supreme Court's use of the minimal and strict scrutiny standards in relatively recent decisions and identified a middle ground—means scrutiny—which he perceived as a standard whereby the Court has determined whether the legislative means substantially furthered
The minimal scrutiny standard has been regarded as an important safeguard to the structure of the political process, allowing legislative value choices to stand without unwarranted judicial intervention.\textsuperscript{43} However, when a tax statute is challenged on constitutional grounds, it may further the safeguarding of the political process, and improve the substantive validity of legislative value choices, to place the burden upon the Commonwealth to come forward with some justifications for distinctive tax treatment.\textsuperscript{44} Not only does such a standard promote legislative accountability, but it also avoids judicial second-guessing of legislative ends. Columbia’s break from the traditional minimal scrutiny test might therefore have salutary effects on the relationship between the judicial and legislative branches, and on those lawmakers most concerned that taxing classifications withstand possible constitutional challenges.

\textit{Jolene M. Grubb

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legitimate legislative ends. Gunther suggested that this means scrutiny approach has been utilized over the years to a limited extent, but putting a “new bite” into this old standard would mean the courts would not be as willing to exercise their own “judicial imagination” to supply justifying rationales. \textit{Id.} at 21.  
\textsuperscript{43} \textit{Id.} at 21-22.  
\textsuperscript{44} The means scrutiny test, as well as the standard utilized by the supreme court in \textit{Columbia}, could improve the quality of the political process by encouraging an airing of the grounds for legislative action, thus directly promoting public consideration of the benefits assertedly sought by the proposed legislation. \textit{See id.} at 44. 
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