THE FRANCHISE TAX.

NOTABLE DECISION OF THE SUPREME COURT—ESTABLISHES A LEGAL PRINCIPLE VITAL TO THE FUTURE.

(*For the Review.*)

The Supreme Court of the United States upheld the validity of the "special franchise tax" law of the State of New York in a decision handed down May 29th. The court held that the law does not violate the Federal Constitution, since it neither impairs the obligation of a contract nor does it deny to the owners of the franchise the equal protection of the laws or due process of law, and that the sum paid by the grantee on a franchise, either in a lump sum or the annual privilege of gross receipts, is merely the consideration of the grant of the said tax, and not in any sense a tax.

This case was an appeal by the Metropolitan Street Railway Company from the decision of the Court of Appeals of the State, which had decided that the law did not conflict with the State Constitution. The public service corporations of the large cities have nearly all refused to pay taxes under this law during the six years' fight in the courts.

The special franchise taxes claimed by the City of New York to be due amount to some $24,000,000. It is not likely, however, that the corporations will pay this entire sum, as for three years it is based upon an assessment at full value, whereas the assessment of ordinary real estate was less than 70%, according to the Board of Equalization, and in the original decision on this law (that of former Judge Earle as Referee, which has been upheld) it was held that the corporations were therefore entitled to a pro rata deduction. The assessment of real property in the City of New York now being at full value, there will not be any inequality between these assessments and those of special franchises.

Because of the loose use of the term "franchise taxation," there is much confusion in the general understanding of these tax laws, and a history and description of the law under consideration is pertinent at this time.

Since 1880 the State of New York has imposed so-called franchise taxes based upon the dividends paid by all corporations and upon the gross earnings of various public service corporations. These taxes are imposed only on corporations, on the theory that they should pay for the franchise of being a corporation; while the "special franchise tax" applies to individuals as well as to corporations, being really an assessment as real estate of the value of the right to use a public highway for private profit.

The real estate of corporations has always been assessed locally in New York in the same manner as that of individuals. The personal property of corporations has been assessed for taxation by computing the value of the capital stock. In determining this value it had been the custom of the local assessors to take into consideration the market value, to some extent, and this resulted in putting on the rolls some of the intangible value included in the special franchise assessment. But after a ruling of the Court of Appeals in 1891 (Union Trust Co. case), the Manhattan Railway Company appealed from its personal property assessment, and in 1895 obtained a decision to the effect that only the actual value of its capital stock could be assessed, which forbade the assessors to include the value of the privilege to use streets for railway purposes. Its tangible property in the streets, such as rails and structure, was defined as real estate in the tax law and was so assessed, as were the rails, pipes and wires of other corporations or individuals.

An agitation was at once begun for the taxation of the intangible property of public service corporations. Senator John Ford introduced a bill to amend the tax law by inserting after the words "all surface, underground or elevated railroads" in the definition of real estate, "including the value of all franchises, rights or permission to construct, maintain or operate the same in, under, above, on or through the streets, highways or public places," and similar words relating to the pipes, conduits, wires, etc., for gas, electric, telegraph and other purposes. This bill was passed but not signed. Because of the protests of the corporations, Governor Roosevelt convened the Legislature in extra session and a new bill was passed. This bill amended the definition of real estate as proposed by Senator Ford, defined such franchises and rights for the purpose of taxation as "special franchises," and further provided that such special franchises should include the value of the tangible property used in connection with the special franchise. Other sections were added providing for the assessment of special franchises by the State Board of Tax Commissioners, who certify the value as ascertained by them to the local assessors, who then place it upon the assessment rolls to be taxed as ordinary real estate. This provision was added at the request of the corporations, who claimed that otherwise they would be unfairly treated by local assessors, and this very provision was one of the main grounds of attack by the same corporations before the Court of Appeals of the State.

The chief credit for the enactment of the special franchise tax law has been given to Governor Roosevelt. But while this measure was under consideration in March, Governor Roosevelt sent a special message in which he said: "Whether these franchises should be taxed as realty, or whether it would be wiser to provide that after the gross earnings equal say 10% of the actual original cost, then 5% of all the gross earnings over and above this shall be paid into the city treasury, or whether some yet dif-

ferent plan should be tried, can only be settled after careful examination of the whole subject." And he recommended a legislative committee of investigation to report at the next session. One month later, when public opinion had been aroused in favor of the bill, Governor Roosevelt sent a message urging its adoption. He did, it is true, resist great pressure from those who wished him to veto the bills, and served notice on the corporations that if they blocked the passage of the second bill, he would sign the first one.

It is interesting to note that a 5% tax on all gross earnings of street railways would not amount to half their special franchise tax in the City of New York, and as to how much it would be after the corporations had been allowed to compute a deduction equal to 10% of the actual original cost, it is not hard to guess. Even under the present law the Brooklyn Rapid Transit Company claimed that the car licenses it paid should be offset against the tax, and that the city really owed it money. And a gross earnings tax is a very unjust discrimination against smaller companies.

The special franchise assessment in 1904 for the entire State was $302,688,757, and for the City of New York $251,521,450. It must be borne in mind, however, that this includes the value of tangible property in the streets which has always been taxed. There is no way of ascertaining how large a part this is of the total assessment. By comparing the first special franchise assessment with the assessment of the previous year, it would seem that only 50% or 60% of the special franchise assessment represents the value of the intangible right to the use of the highway. The entire sum for Manhattan Borough is nearly $190,000,000, of which $75,000,000 is a low estimate for tangible property, leaving only $115,000,000 for the privileges of the street and elevated railways, gas, telephone and electric companies. The under-assessment is obvious. Still, it is a beginning.

It is objected that to tax these privileges as real estate is to admit that they are property. However, the New York courts have held that franchises to use streets are estates in perpetuity, so to tax their value does not add to the legal obstacles in the way of rescuing highways from private ownership.

The special franchise tax does not apply to steam railroads unless they use a public street longitudinally (their crossings over highways were specifically exempted in 1901 after attempts to assess them); private roadbeds are taxable as any other real estate by local assessors.

Without waiting for the Supreme Court decision or an amendment to their tax laws, the Baltimore assessors this Spring put the Consolidated Gas Company of that city on the rolls for $6,000,000 additional for the value of its easement or the use of the beds of public streets, computing this upon the basis of the market value of the company's stock and bonds, and then subtracting the value of the property upon which it paid taxes. The Court of Appeals of Maryland has set aside this assessment, saying, "Whilst we hold the easements in question to be taxable, we determine that the method followed in valuing them cannot obtain under the statutes in force." This is probably for the reason that not all of the differences in value between the value of the taxed property and the market value of stocks and bonds is easement or special franchise value; some of it may be good-will or similar improvement value rather than land value. It is important, however, that the court holds such a use of the street to be a taxable easement, for this will open the way in many cities for the placing of such value upon the rolls without further legislation.

In Pennsylvania public service corporations have matters so arranged that they will not be affected by either of these decisions. Under the laws of that state the real estate of quasi-public corporations essential to the use of their franchises is exempt from local taxation (there is no State tax upon real estate), and therefore there is no way, apparently, of assessing the easement value for taxation. The value of their franchises is supposed to be reached by the State tax, but that is computed upon gross earnings, and is entirely unrelated to the actual value of the use of highways. The real estate of steam railroads in Philadelphia and Pittsburg is subject to local taxation by special law, and there may be special laws relating to some other corporations. But the general law is as stated.

A. C. PLEYDELL.

Mayor Dunne of Chicago has appointed Emil W. Ritter president of the Referendum League of which organization our valued contributor, James P. Cadman, is secretary, member of the Board of Education of that city. Mayor Dunne has begun a campaign to compel property owners to pay for the side walk space monopolized.

W. D. Lamb, of Plumas, Manitoba, ordered from his bookseller a copy of Patrick Edward Dove's Elements of Political Science. The bookseller canvassed 4,000 dealers and finally secured a copy for Mr. Lamb, which copy had been in the Edinburg Library.

In the Universalist *Leader*, of April 22, is a poem entitled, "What are we Here For.' The answer is,

"To hold earth's bounty equal prize
Of every child that's born."