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## State Taxation

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## STATE TAXATION

The most significant state tax legislation passed in 1962 was the simplification of the Massachusetts corporate tax laws and the addition of an incentive to encourage investment in new machinery in that state.<sup>1</sup>

The new legislation was the result of an intensive two year study by the Massachusetts State Tax Commission which was conducted to analyze possibilities of simplifying the corporation excise tax applicable to business and manufacturing corporations and of distributing the corporate tax burden more equitably.<sup>2</sup>

The Massachusetts corporation excise tax, which was first enacted in 1919,<sup>3</sup> is a tax on domestic and foreign business and manufacturing corporations for the privilege of corporate existence in the Commonwealth. It is the third most important single tax in Massachusetts. In 1960 it yielded 88.1 million dollars or 7.25 per cent of a total 1.2 billion dollar state budget.<sup>4</sup> Of the taxes that support the state rather than local government, the corporation excise tax ranks second and is surpassed only by the personal income tax.<sup>5</sup> Like taxes in most states it is interlaced with a series of "temporary" levies which, considering both their longevity and importance in the governmental fiscal structure, one can safely assume to be, in reality, permanent.

In order to understand the innovations made by the new law and their significance, it will be necessary to consider the previous method of taxing corporations.

The tax was divided into two parts. First, there was a corporate income tax based on taxable net income<sup>6</sup> allocable to Massachusetts. The rate of taxation was five and one-half per cent.<sup>7</sup> Second, there was the much criticized "corporate excess" tax. The basis of this tax was the "fair value" of the capital stock allocable to Massachusetts (minus certain deductions).<sup>8</sup> The rate was \$5 per \$1000. To the sum of these two parts was added an

<sup>1</sup> Laws, 1962, ch. 756, adopted July 25, 1962, effective for taxable years ending after December 31, 1962.

<sup>2</sup> Mass. Resolves 1960, ch. 103.

<sup>3</sup> Mass. Stat. 1919, ch. 355 (now Mass. Gen. Laws Ann. ch. 63, § 32 (Supp. 1961)).

<sup>4</sup> These figures originated primarily in the office of the Comptroller of the Commonwealth and the Department of Corporations and Taxation.

<sup>5</sup> The property tax, which is the largest single tax in Massachusetts, is collected by the local rather than state government.

<sup>6</sup> Deductions are roughly analogous to those allowed by the Federal Internal Revenue Act. Mass. Gen. Laws Ann. ch. 63, § 32 (Supp. 1961).

<sup>7</sup> 2½% is "permanent" and was provided for in the original act, 1½% was added as "temporary" in 1946, Mass. Stat. 1946, ch. 581, and an additional 1½% "temporary" tax was added in 1948, Mass. Stat. 1947, ch. 598. The above cited acts are now incorporated in Mass. Gen. Laws Ann. ch. 63, § 32 (Supp. 1961).

<sup>8</sup> The method of ascertaining the fair value was not provided in the original act and was left to administrative rulings. The method of arriving at the value varied over the years but was essentially the value of the company's stock represented by their property located in, and business done in, Massachusetts. From this figure was deducted the value of property subject to local taxation. Large amounts of corporate property is not subject to local taxation, however, among which is machinery for a manufacturing corporation and inventories for all corporations. A complete list of such property is found in Mass. Gen. Laws Ann. ch. 59, § 5 (Supp. 1961).

additional twenty-three per cent of that sum.<sup>9</sup> The foregoing provisions were subject to four minimum amounts below which the tax paid to the Commonwealth could not fall. The first minimum was, in reality, a substitute for the corporate excess tax. It was based on the value of all tangible property located in Massachusetts and not subject to local taxation. The rate was \$5 per \$1000.<sup>10</sup> In short, if the value of the above tangible property exceeded the "fair value of the capital stock" after deductions, the former would be paid in lieu of the latter. The other three minimums were in lieu of both the "corporate excess" and the "net income" provisions. The first was one-twentieth of one per cent of the fair value of the capital stock *without any deductions*, plus a three per cent tax on net income allocable to Massachusetts.<sup>11</sup> The second taxed gross receipts at the rate of one-twentieth of one per cent and net income at three per cent in so far as each is allocable to Massachusetts.<sup>12</sup> Third was a flat rate of twenty-five dollars which, of course, applied only to corporations with little income and practically no tangible property.<sup>13</sup> All of the above minimums were subject to the twenty-three per cent surtax.

In January, 1961, the tax commission filed a preliminary report with the General Court.<sup>14</sup> They recommended that the tax be replaced by (1) a tax measured by net income only or (2) a tax measured in part by net income and in part by tangible property not subject to local taxation. They also recommended that the complicated minimums be replaced by either a tax based on gross receipts or a flat sum of fifty dollars.<sup>15</sup> The legislature directed the commission to continue its study but to limit it to the second recommendation and the second part of the first.<sup>16</sup>

In 1962, after considering the commission's new report, the legislature enacted the new tax law. The corporation excise tax is now the greater of:

- (1) The sum of 6.765 per cent of net income and \$7.65 per \$1,000 upon the value of tangible property in Massachusetts not subject to local taxation;<sup>17</sup> or (2) .0615 per cent of gross receipts allocable to Massachusetts plus 3.69 per cent of net income; or (3) One-hundred dollars.<sup>18</sup>

The old corporation excess measure of taxation was abolished.<sup>19</sup>

<sup>9</sup> This additional tax first appeared in 1935 as a 10% "surtax." It was ostensibly "temporary." Mass. Stat. 1935, ch. 480. In 1941 the legislature passed an additional 3% tax which was classified as permanent. Mass. Stat. 1941, ch. 729. In 1950 the 10% temporary tax was increased to 20% and the increase was also classified as "temporary." Mass. Stat. 1949, ch. 674. The above cited acts are now incorporated in Mass. Gen. Laws Ann. ch. 63, § 32 (Supp. 1961).

<sup>10</sup> Mass. Gen. Laws Ann. ch. 63, § 32(a)(1) (Supp. 1961).

<sup>11</sup> Mass. Gen. Laws Ann. ch. 63, § 32(b) (Supp. 1961).

<sup>12</sup> Mass. Gen. Laws Ann. ch. 63, § 32(c) (Supp. 1961).

<sup>13</sup> Mass. Gen. Laws Ann. ch. 63, § 32(d) (Supp. 1961).

<sup>14</sup> Printed as Mass. Senate Doc. 512 (1962).

<sup>15</sup> *Ibid.*

<sup>16</sup> Mass. Resolves 1961, ch. 65.

<sup>17</sup> Local tax exemptions are discussed briefly in note 8 *supra*.

<sup>18</sup> *Supra* note 1. A provision for lowering the above rates by 1964 was also included in the act, provided revenue requirements permit such a reduction.

<sup>19</sup> *Supra* note 1.

## CURRENT LEGISLATION

Corporations having little tangible property in Massachusetts are now classified as "intangible property corporations" and net worth allocable to Massachusetts is substituted for the tangible property considered in (1) above.<sup>20</sup> The legislature further provided for a five year exemption to all new investments in machinery and equipment with a useful life of eight years or more.<sup>21</sup> This is particularly significant in Massachusetts since much of the machinery in question is also exempt from local taxation.<sup>22</sup> The net result is that it is not taxed at all for five years. Massachusetts appears to occupy a unique position among the fifty states in this innovation and, in fact, has adopted a plan that has been suggested should be part of the policy of the federal government.<sup>23</sup> It is obviously designed to encourage new investment in capital equipment and, if successful, will result in a much larger tangible property base after the five year exemption period expires, thus reaping for the Commonwealth considerably more revenue than will be temporarily lost during the period of exemption, not to mention the increase in other forms of state revenue that would result from increased investment in capital equipment in the Commonwealth.

In evaluating the rest of the new legislation, it would be best to examine the various methods other states use to tax corporations. Interestingly enough five states have either a low flat rate or no tax at all.<sup>24</sup> This alternative, of course, is impractical in Massachusetts if one considers the importance of the tax in the state budget. A majority of the states base their tax on some form of the value of the capital stock.<sup>25</sup> However, in most of these states the means of determining that value, in short the true basis of the tax, rests on property, income or business done.<sup>26</sup> Often, as in Massachusetts, the law does not provide a precise method of determining the value and thus it is left to administrative rulings and negotiation between the state and the taxpayer. This method is unsatisfactory since it lacks definiteness, certainty and clarity. Fourteen states, on the other hand, have some form of corporate income tax.<sup>27</sup> Of these, seven tax corporations solely

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<sup>20</sup> If the ratio between the tangible assets in Massachusetts not subject to local taxation and the total assets not taxed locally is less than 10%, the corporation is an intangible property corporation.

<sup>21</sup> *Supra* note 1.

<sup>22</sup> See note 8 *supra*.

<sup>23</sup> In 1962 Congress partially adopted such a policy. See the discussion of the federal investment tax credit, Legislation 4 B.C. Ind. & Com. L. Rev. 131-35 (1962).

<sup>24</sup> Alaska, flat rate—\$15; Arizona, no tax; Indiana, no tax—\$2 annual report fee; Nevada, no tax—\$10 annual report fee; South Dakota, no tax—\$1 annual report fee.

<sup>25</sup> Alabama, Arkansas, Colorado, Connecticut, Delaware, District of Columbia, Florida, Georgia, Kansas, Kentucky, Louisiana, Maine, Maryland, Michigan, Mississippi, Missouri, Nebraska, New Hampshire, New Mexico, North Carolina, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, Tennessee, Virginia, Washington and West Virginia.

<sup>26</sup> Delaware, the "corporate haven," is a notable exception. One of its two alternative bases of taxation rests on the number rather than the value of outstanding shares. The other alternative, however, is based on the value.

<sup>27</sup> California, 5½%; Connecticut, 5%; Hawaii, graduated; Idaho, 9.5%; Iowa, 3%; Minnesota, 9.3%; Montana, 4½%; New Jersey, 1¾%; New York, 5½%; North Dakota, graduated; Pennsylvania, 6%; Tennessee, 3¼%; Utah, 4%; Wisconsin, graduated.

on the basis of income,<sup>28</sup> three tax income if it yields more than an alternative tax,<sup>29</sup> and four, like Massachusetts, employ an income tax as well as other forms of franchise tax.<sup>30</sup> Straight taxation of income alone is probably the simplest method of corporate taxation and also the most equitable, all other things being equal. In Massachusetts, however, things are something less than equal. Large amounts of corporate property are exempt from local taxation. Therefore, if they are not taxed by the state government, they will escape taxation altogether. Their inclusion within the purview of the corporate excise tax is a fiscal necessity.

In conclusion, the Massachusetts General Court has taken a step in the right direction both as to simplifying and equalizing the tax laws and as to providing an investment incentive. It is a step that could well be emulated by her sister states.

JOHN M. TOBIN

## TRADE REGULATON

Congress has recently enacted the Antitrust Civil Process Act<sup>1</sup> which enables the Department of Justice to obtain compulsory production of documentary evidence in civil antitrust investigations. The act thus places the Department on a parity with other federal agencies which have the power to obtain documents for purposes of investigation.<sup>2</sup> This seems eminently desirable since the Department is the primary enforcer of the antitrust laws. Nonetheless, similar proposals had been submitted, without success, to Congress for the last four years.<sup>3</sup>

Prior to this enactment, the Department had three methods to obtain evidence in civil antitrust investigations, all of which were generally unsatisfactory and inherently unenforceable.<sup>4</sup> First, voluntary cooperation of prospective defendants could be sought. This procedure is subject to obvious defects and needs no extended discussion, suffice it to say that there were many instances where cooperation was not forthcoming.<sup>5</sup> As the applicable House Report points out, "this method . . . is unsatisfactory since it leaves

<sup>28</sup> California, Hawaii, Idaho, Minnesota, Montana, North Dakota and Wisconsin.

<sup>29</sup> Connecticut, New York and Utah.

<sup>30</sup> Iowa, New Jersey, Pennsylvania and Tennessee.

<sup>1</sup> Pub. L. No. 87-664, 76 Stat. 546 (1962); 15 U.S. Code Cong. & Ad. News 3095 (1962).

<sup>2</sup> A partial list of such agencies is contained in H.R. Rep. No. 1386, 87th Cong., 2d Sess. (1962). They include the Departments of Agriculture, the Army, Labor, Treasury, as well as the Veterans Administration and the Federal Maritime Commission.

<sup>3</sup> For a legislative history of these proposals, see H.R. Rep. No. 1386, *supra* note 2.

<sup>4</sup> Dissatisfaction with the evidence producing powers of the Department was the main topic of the Hearing on Current Antitrust Laws, Att'y Gen. Nat'l Comm. Antitrust Rep. 345 (1955). For additional discussion concerning the previous inadequacies of civil antitrust enforcement by the Department of Justice, see H.R. Rep. No. 2966, 84th Cong., 2d Sess. 267 (1956), cited in 59 Colum. L. Rev. 1089 (1959); 19 Md. L. Rev. 326 (1959).

<sup>5</sup> See Hearings on S. 167 Before Senate Subcommittee on Antitrust & Monopoly, 87th Cong., 1st Sess. (1961) (remarks of Asst. Att'y Gen. Loevinger).