Louisiana Law Review

Volume 14 | Number 3
April 1954

Constitutional Law - Commerce Clause - Validity of State Tax on the "Taking of Gas"

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CONSTITUTIONAL LAW—COMMERCE CLAUSE—VALIDITY OF STATE TAX ON THE "TAKING OF GAS"

A Texas statute[1] placed an occupational tax on gas gathering, defined as "the first taking or the first retaining of possession of such gas for other processing or transmission."[2] Appellants, the Michigan-Wisconsin Company, bought their entire supply of gas from a Texas producer. The gas was processed, then was taken into the company's line, and was compressed so that it would flow through the interstate pipes. The tax was upheld by Texas courts in a suit to test its validity.[3] On appeal the United States Supreme Court held the taking to be an inseparable part of interstate commerce, the gas being in continuous flow from well to pipes and that the tax, as applied to appellants, was invalid. *Michigan-Wisconsin Pipe Line Co. v. Calvert*, 74 Sup. Ct. 396 (1954).

Since Louisiana has a statute[4] almost identical to that of Texas, the decision will be of considerable importance to this state. The problem facing the Court in this case was whether or not the tax, under the broad definition of gas gathering in the statute, was delayed until the gas became a part of interstate commerce itself.[5] The rules of state taxation of interstate commerce are highly complicated, confusing and seemingly contradictory. No attempt, however, is made here to present a complete

1. Tex. Laws 1951, c. 402, § 23(2): "In addition to all other licenses and taxes levied and assessed in the State of Texas, there is hereby levied upon every person engaged in gathering gas produced in this State, an occupation tax for the privilege of engaging in such business, at the rate of 9/20 of one cent per thousand (1000) cubic feet of gas gathered."

2. Tex. Laws 1951, c. 402, § 23(1)(c): ". . . the term 'gathering gas' means the first taking or the first retaining of possession of such gas for other processing or transmission whether through a pipeline . . . or otherwise after such gas has passed through the outlet of such [original processing] plant."

3. Calvert v. Michigan-Wisconsin Pipe Line Co., 255 S.W.2d 535 (Tex. Civ. App. 1953).

4. LA. R.S. § 47:671 (1950): "In addition to all other licenses and taxes levied and assessed in the State of Louisiana, there is hereby levied upon every person engaged in gathering gas produced in this state, an excise, license or privilege tax, for the privilege of engaging in such business, at the rate of one cent (1¢) per thousand (1,000) cubic feet . . . of gas gathered."

According to LA. R.S. § 47:673 (1950), gathering gas means "the first taking or the first retaining of possession of gas produced in Louisiana for transmission through a pipe line, after the severance of such gas, and after the passage of such gas through any separator, drip, trap or meter that may be located at or near the well. In the case of gas containing gasoline or liquid hydrocarbons that are removed or extracted in commercial quantities at a plant by scrubbing, absorption, compression, or any similar process, the term 'gathering gas' means the first taking or the first retaining of possession of such gas for transmission through a pipe line after such gas has passed through the outlet of such plant. . . ."

5. Michigan-Wisconsin Pipe Line Co. v. Calvert, 74 Sup. Ct. 396, 401 (1954).

analysis of this topic.[6] A brief outline of the basic developments will be sufficient to locate the position of the instant case within the overall framework. Indeed, the problem of state taxation is but a part of the entire subject of residual powers of the states with regard to the Commerce Clause and other powers delegated to the federal government.

The United States Supreme Court has announced certain standards which a state tax affecting interstate commerce must meet before it will be sustained. First, the tax cannot discriminate against interstate commerce.[7] In the instant case, the levy was not discriminatory, for it was laid on all gas gathering within the state, regardless of whether the gatherer was engaged in interstate or intrastate commerce.[8]

Until 1938, the Court would not allow a state tax to stand if it constituted a direct burden on interstate commerce;[9] although it was valid if it only placed an indirect burden on it.[10] However, this test seems unfair to the states. Interstate commerce derives certain benefits from the states; it should be obliged to pay its own way, as is local commerce. Realizing this, Mr. Justice Stone formulated the multiple burden doctrine, which controlled from 1938 until 1946.[11] Under this rule a state could not lay a tax which could be duplicated by the other states through which the articles of commerce flow. This rule seems to be the more equitable one. It does not entirely relieve interstate commerce from payment of its due share to the states, yet it prevents double taxation of the commerce. The multiple burden doctrine appears to be in line with Madison's opinion:

"A very *material* object of this power [regulation of inter-

6. For recent comprehensive analyses of the subject, see Barrett, *State Taxation of Interstate Commerce*, 4 VAND. L. REV. 496 (1951); Note, *State Taxation and Interstate Commerce*, 54 COL. L. REV. 261 (1954).

7. Nippert v. Richmond, 327 U.S. 416 (1946); Best & Co. v. Maxwell, 311 U.S. 454 (1940).

8. 74 Sup. Ct. 396, 400 (1954).

9. Minnesota v. Blasius, 290 U.S. 1 (1933). *Accord*: Pacific Tel. & Tel. Co. v. Tax Commission, 297 U.S. 403 (1936); Alpha Portland Cement Co. v. Massachusetts, 268 U.S. 203 (1925); Ozark Pipe Line Co. v. Monier, 266 U.S. 555 (1925).

10. Southern National Gas Corp. v. Alabama, 301 U.S. 148 (1937); Atlantic Lumber Co. v. Commissioner of Corporations and Taxation, 298 U.S. 553 (1936); Matson Navigation Co. v. State Board of Equalization, 297 U.S. 441 (1936); Virginia v. Imperial Coal Sales Co., 293 U.S. 15 (1935); Hope Natural Gas Co. v. Hall, 274 U.S. 284 (1927); Postal Telegraph-Cable Co. v. Richmond, 249 U.S. 252 (1919); Watters v. Michigan, 248 U.S. 65 (1918).

11. Western Live Stock Bureau of Revenue, 303 U.S. 250 (1938). *Accord*: Memphis Natural Gas Co. v. Stone, 335 U.S. 80 (1948); McGoldrick v. Berwind-White Coal Mining Co., 309 U.S. 33 (1940); Southern Pacific Co. v. Gallagher, 306 U.S. 167 (1939).

> state commerce] was the *relief* of the States which *import and export through other States* from the *improper* contributions levied on them by the latter. Were these at liberty to regulate the trade between State and State, it must be foreseen that ways would be found out to *load the articles* of import and export *during their passage through their jurisdiction* with duties. . . ."[12] (Italics supplied.)

Thus, it was a main purpose of the Commerce Clause to prevent multiple taxation by those states through which commerce flows.[13] Conversely, it was not intended to make it immune to all state taxation.[14] However, where the states have attempted to tax foreign corporations which are engaged merely in transporting goods through the state (as, for example, a pipeline,[15] a branch office in the state,[16] the loading and unloading of vessels,[17] and motor vehicles[18]), the taxes have been invalidated.

Since gathering gas was defined as the first taking of the gas after production,[19] and since there could be but one such instance, it would seem that the tax could not be duplicated by other states on gas produced in Texas. Furthermore, the statute also required that the gas be produced within the state.[20] Although other states might enact similar legislation, it would not seem to affect appellant's gas, regardless of how many times it was gathered after leaving Texas. Nevertheless, the Court indicates a fear that this would happen.[21]

Since *Freeman v. Hewit*[22] in 1946, the decisions of the Court have not been in agreement as to which rule would be followed.[23] That case completely ignored the multiple burden doctrine and struck down an Indiana tax on gross incomes on the sole basis

12. THE FEDERALIST, No. 42 at 274 (Madison) (Mod. Lib. ed.).
13. Western Live Stock v. Bureau of Revenue, 303 U.S. 250, 258, 259 (1938).
14. Western Live Stock v. Bureau of Revenue, 303 U.S. 250, 258, 259, 260 (1938); Postal Telegraph-Cable Co. v. Richmond, 249 U.S. 252, 259 (1919).
15. Ozark Pipe Line Corp. v. Monier, 266 U.S. 555 (1925).
16. Alpha Portland Cement Co. v. Massachusetts, 268 U.S. 203 (1925).
17. Puget Sound Stevedoring Co. v. State Tax Commission, 302 U.S. 90 (1937).
18. McCarroll v. Dixie Greyhound Lines, 309 U.S. 176 (1940).
19. Tex. Laws 1951, c. 402, § 23(1)(c). See note 2 *supra* for text.
20. See note 1 *supra* for text.
21. 74 Sup. Ct. 396, 403 (1954).
22. 329 U.S. 249 (1946).
23. The theory of *Western Live Stock v. Bureau of Revenue* is followed in: Interstate Oil Pipe Line Co. v. Stone, 337 U.S. 662 (1949); Memphis Natural Gas Co. v. Stone, 335 U.S. 80 (1948). The theory of *Freeman v. Hewit* is followed in: Joseph v. Carter & Weekes, 330 U.S. 422 (1947). See also the dissent in Interstate Oil Pipe Line Co. v. Stone, 337 U.S. 662, 669 (1949).

that it was a direct imposition on interstate commerce,[24] a reversion to the pre-1938 doctrine. The next year, the Court invalidated a gross receipts tax which could not be duplicated in its effect by other states, because the occupation burdened, though carried on entirely within the state, was essentially a part of interstate commerce itself.[25] This is, then, another way of stating the direct burden theory.

In the instant case the Court states the principle that a tax on the "local activity related to interstate commerce is valid if, and only if, the local activity is not such an integral part of the interstate process . . . that it cannot realistically be separated from it."[26] This is the theory which has prevailed for over a hundred years.[27] The Court decided that the first taking of the gas by appellants could not be separated from the interstate commerce because the gas was already moving in interstate commerce, being in continuous flow from the well into the pipes. But if continuity of flow is the basis for finding the gas to be an integral part of interstate commerce, it would appear that it should also be such from the time that it began its upward movement from the interior of the earth, and a state could not tax it at any point thereafter. Moreover, in *Utah Power & Light Co. v. Pfost*,[28] the Court had held that an Idaho tax on all electrical energy generated within the state was valid, even though about eighty-five percent of the energy went to other states.

24. Freeman v. Hewit, 329 U.S. 249, 256 (1946): A "State has various means of obtaining legitimate contribution to the costs of its government, without imposing a direct tax on interstate sales. While these permitted taxes may, in an ultimate sense, come out of interstate commerce, they are not, as would be a tax on gross receipts, a *direct imposition* on that very freedom of commercial flow which for more than a hundred and fifty years has been the ward of the Commerce Clause." (Italics supplied.)

In a dissenting opinion to this case (*id.* at 285-86) Mr. Justice Douglas said: "Any receipt of income in Indiana from out-of-state sources involves, of course, the use of interstate agencies of communication. That, alone, however, is no barrier to its taxation by Indiana. Western Live Stock v. Bureau of Revenue. . . . For a local activity which is separate and distinct from interstate commerce may be taxed though interstate activity is induced or occasioned by it. . . .

"The present tax is not aimed at interstate commerce and does not discriminate against it. . . . The tax is on the proceeds of the sales less the brokerage commissions and therefore does not reach the revenues from the only interstate activities involved in these transactions. . . .

"I would adhere to the philosophy of our recent cases [Western Live Stock v. Bureau of Revenue, 303 U.S. 250 (1938), and McGoldrick v. Berwind-White Coal Co., 309 U.S. 33 (1940)] and affirm the judgment below."

25. Joseph v. Carter & Weekes Stevedoring Co., 330 U.S. 422 (1947).

26. 74 Sup. Ct. 396, 401 (1954).

27. Cooley v. The Board of Wardens of the Port of Philadelphia, 12 How. 299 (U.S. 1851).

28. 286 U.S. 165 (1932).

In the *Pfost* case it was found that "the generator and the transmission lines perform different functions";[29] thus, that tax fell only on a local aspect of the commerce.[30] The object of the tax, then, could realistically be separated from the interstate process. But, in view of the fact that electricity travels almost instantaneously, it would seem that the first taking of gas (which was its entrance into the Michigan-Wisconsin Company's pipes from the producer's pipes), as well as its compression, can be separated as realistically as can the generation of electricity. It may be added that as the generator and lines perform different functions, so do the compressor and pipes. Furthermore, the apparent impossibility of the tax being duplicated on appellants by other states has already been brought out.[31]

Moreover, in *Coverdale v. Arkansas-Louisiana Pipe Line Co.*,[32] the Court upheld a privilege tax on the production of power to run a compressor, used for the same purpose as the one in the principal case. The tax fell about the same place in transit in both instances—in fact, in the *Coverdale* case, it came *after* the taking, for the tax was on the production of the power used in the compression of the gas. Such power production would seem to be as much an integral part of interstate commerce as the taking, for without the compression, the gas would not flow through the pipes.

An interesting point about the instant decision is its unanimity. Mr. Justice Black has usually been hesitant to strike down non-discriminatory state legislation alleged to be a regulation of interstate commerce, in the absence of congressional action to the contrary.[33] He would uphold the state law, even if the tax might possibly be duplicated by other states.[34] Moreover,

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29. *Id.* at 180.
30. *Id.* at 181.
31. See page 693 *supra*.
32. 303 U.S. 604 (1938).
33. For analyses of the position usually taken by Mr. Justice Black on this subject, see Barnett, *Mr. Justice Black and the Supreme Court*, 8 U. OF CHI. L. REV. 20 (1940); FRANK, MR. JUSTICE BLACK 154-191 (1949).
34. In the dissenting opinion in Gwinn, White & Prince, Inc. v. Henneford, 305 U.S. 434, 445 (1939), it was stated: "While there are strong logical grounds upon which this Court has based its invalidation of state laws actually imposing unjust, unfair and discriminatory burdens against interstate commerce as such, the same grounds do not support a judicial regulation designed to protect commerce from validly enacted non-discriminatory state taxes which do not—*but may sometime*—prove burdensome. . . . So here, if national regulation to prevent 'multiple taxation' is within the constitutional power of this Court, it would seem to be time enough to consider it when appellant or some other taxpayer *is actually subjected* to 'multiple taxation.'" (Italics supplied.)

he has expressed the view that it is for Congress, not the Court, to decide how far a state may go in regulating interstate commerce if such regulation is not discriminatory.[35] Has he relinquished this view by his asquiescence in this decision?

In conclusion, it is easy to formulate the proposition that a state tax on interstate commerce is valid if it is on a separable, local incident and invalid if on an inseparable, integral part of the commerce. The difficulty arises when this abstract proposition is applied to a concrete case, and one is called upon to decide whether the object of the tax in question is separable or inseparable, local or national in scope. Reasonable minds can well differ as to when the object becomes inseparable from, and a direct part of, interstate commerce, for in making that determination it is easy to point out distinctions where they apparently do not exist.

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CONSTITUTIONAL LAW—INTER-GOVERNMENTAL TAXATION—IMMUNITY FROM STATE SALES TAX OF CONTRACTORS UNDER "COST-PLUS-A-FIXED-FEE" CONTRACTS WITH THE UNITED STATES

Two tractors to be used in the construction of a government project were purchased by private contractors as "purchasing agents for the Government."[1] An Arkansas "gross receipts" tax[2] was levied on the sale and paid by the contractor's vendor under protest. The plaintiff vendor alleged that the tax was, in effect, a tax on the federal government and therefore invalid. The Arkansas Supreme Court upheld the tax.[3] On appeal to the

35. Gwin, White & Prince, Inc. v. Henneford, 305 U.S. 434, 452 (1939): "Congress is the only department of our government—state or federal—vested with authority to determine whether 'multiple taxation' is injurious to the national economy. . . ."

Id. at 455: "I would return to the rule that—except for state acts designed to impose discriminatory burdens on interstate commerce because it *is* interstate—Congress alone must 'determine how far [interstate commerce] . . . shall be free and untrammelled, how far it shall be burdened by duties and imposts, and how far it shall be prohibited.' [Welton v. Missouri, 91 U.S. 275, 280 (1875).]"

1. Kern-Limerick, Inc. v. Scurlock, 74 Sup. Ct. 403, 409 (1954).

2. Ark. Gross Receipts Tax Act of 1941, ARK. STAT. §§ 84-1901, 84-1902(e), 84-1903, 84-1908 (1947).

3. Parker v. Kern-Limerick, Inc., 254 S.W.2d 454 (Ark. 1953). The Arkansas Supreme Court relied on Alabama v. King & Boozer, 314 U.S. 1 (1941), holding that the *legal incidence* of the tax fell on the private contractor. When the *incidence*, which refers to the specific person or agency