

1960

# The Denver and Rio Grande Western Railroad Co. v. State Tax Commission of Utah : Brief of Respondent

Utah Supreme Court

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Walter L. Budge; F. Burton Howard; Attorneys for Respondent;

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# IN THE SUPREME COURT OF THE STATE OF UTAH

THE DENVER AND RIO GRANDE  
WESTERN RAILROAD  
COMPANY, a Corporation,

*Petitioner,*

— vs. —

THE STATE TAX COMMISSION  
OF UTAH,

*Respondent.*

FILE

DEC 1 0 1960

Clk. Case Court, Utah  
No. 9312

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## BRIEF OF RESPONDENT

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# IN THE SUPREME COURT OF THE STATE OF UTAH

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WESTERN RAILROAD  
COMPANY, a Corporation,

*Petitioner,*

— vs. —

THE STATE TAX COMMISSION  
OF UTAH,

*Respondent.*

Case  
No. 9312

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## BRIEF OF RESPONDENT

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### STATEMENT OF THE CASE

The parties herein will be designated in the same manner as adopted by petitioner, the Denver and Rio Grande Western Railroad Co., as the “Rio Grande,” and respondent, State Tax Commission of Utah, as the “Tax Commission.”

The State Tax Commission of the State of Utah has levied an assessment against the Denver and Rio Grande Western Railroad Co. for a sales tax on the amount charged by Rio Grande for repairs to cars and

locomotives of other railroads which are repaired by Rio Grande pursuant to “Rules of the Association of American Railroads.” The pertinent facts are set forth in a stipulation of facts heretofore filed in the above proceeding and are not in dispute.

Section 59-15-4, Utah Code Annotated, 1953, as amended, provides in pertinent part as follows:

“From and after the effective date of this act there is levied and there shall be collected and paid: . . . (e) A tax equivalent to 2% of the amount paid or charged for all services for repairs or renovations of tangible personal property rendered in connection with other tangible personal property.”

The present controversy arises out of an attempt by the Tax Commission to apply this statute to the amount charged by Rio Grande for repairs to cars and locomotives of other railroads.

The only question raised by this appeal is whether or not a tax upon these charges constitutes an unlawful burden on interstate commerce. Assuming, without conceding, the validity of petitioner’s argument on pages 8-10 of its brief, it is submitted that this Court is not obliged to construe the issue in the manner advocated by petitioner — the tax *was* imposed upon the *amount charged for repairs*. The validity or application of Tax Commission Sales Tax Regulation 78 was not considered in the formal decision of the Tax Commission nor raised at any time prior hereto by petitioner. Neither should this regulation be used to adduce the intention of the Legislature in enacting Section 59-15-4.

## STATEMENT OF POINTS

### POINT I

THE SALES TAX IN UTAH IS A TRANSACTION TAX.

### POINT II

THE ASSESSMENT OF SALES TAX ON THE AMOUNTS CHARGED BY RIO GRANDE FOR REPAIRS TO CARS AND LOCOMOTIVES OF OTHER RAILROADS IS NOT A BURDEN ON INTERSTATE COMMERCE PROHIBITED BY THE COMMERCE CLAUSE OF THE UNITED STATES CONSTITUTION.

### POINT III

THE FACT THAT RIO GRANDE IS PROHIBITED BY FEDERAL LAW FROM MOVING DEFECTIVE CARS DOES NOT REQUIRE THAT A TAX UPON REPAIRS OF SUCH CARS BE DEEMED AN ILLEGAL INTERFERENCE WITH INTERSTATE COMMERCE.

## ARGUMENT

### POINT I

THE SALES TAX IN UTAH IS A TRANSACTION TAX.

Any analysis of a tax problem must first begin with a determination of the kind of tax involved. Clearly, rules applicable to the decision of a use tax case may not necessarily apply to a sales tax problem.

The majority of decided cases in this area involve what is hereby denominated as the retail sales tax — the

most restricted type — which is imposed only upon sales of tangible personal property at retail. However, the sales tax has been expanded in Utah to include sales of tangible personal property at retail as well as certain sales of services by business enterprises. See 59-15-4, Utah Code Annotated, 1953, as amended. This type of sales tax may properly be categorized as a general sales tax.

However, both of these forms of taxation can and should be distinguished from other taxes, the basis of which may be an amount charged or paid. In Utah the sales tax is not a tax on property but rather a tax upon the transaction. The amount of consideration involved in the sale or transaction is the measure to which the rate is applied. *W. F. Jensen Candy Co. v. State Tax Comm.*, 90 Utah 359, 61 P. 2d 629 (1936); *Union Stock Yards v. State Tax Commission*, 93 Utah 174, 71 P. 2d 542 (1937).

The use tax is a tax upon the storage, use or consumption of tangible personal property within the state of Utah. *Southern Pac. Co. v. Utah State Tax Comm.*, 106 Utah 451, 150 P. 2d 111 (1944).

A gross receipts tax, although foreign to Utah law, is a tax upon gross receipts received from the total business operation of a taxpayer and not upon any particular transaction. Such a tax based wholly or in part upon receipts derived from interstate commerce is unconstitutional because it is a direct burden on benefits to be derived from such commerce. *Cooley, Taxation*, 4th Ed. § 395.



It becomes apparent that, given a valid basis of distinction, decisions involving gross receipts or use taxes cannot be used to resolve the problem in the instant case. It is submitted that the only possible way in which the apparently conflicting decisions in this area can be reconciled is to recognize the type of tax involved and the general principles governing its application.

It is contended that the basic principles governing the decision of the instant controversy should be the same as are applied to the retail sales tax. Whether the article sold is intangible service or tangible personal property should have no bearing upon the taxability of such a sale assuming a valid application of taxing powers.

## POINT II

### THE ASSESSMENT OF SALES TAX ON THE AMOUNTS CHARGED BY RIO GRANDE FOR REPAIRS TO CARS AND LOCOMOTIVES OF OTHER RAILROADS IS NOT A BURDEN ON INTERSTATE COMMERCE PROHIBITED BY THE COMMERCE CLAUSE OF THE UNITED STATES CONSTITUTION.

The petitioner contends that the imposition of the tax assessed by the Commission is a burden on interstate commerce prohibited by the Commerce Clause of the Federal Constitution, and cites as authorities for this proposition *Union Pacific Railroad Co. v. Utah State Tax Commission*, 110 Ut. 99, 169 P. 2d 804 (1946), and *Southern Pacific Co. v. Utah State Commission*, 106 Ut. 451, 150 P. 2d 110 (1944).

The *Union Pacific case*, *supra*, involved engines purchased by the taxpayer used by it in switching operations and hauling of interstate and intrastate cars in the state of Nebraska which were subsequently transferred by it, under their own power to Utah. They were inspected, refueled and repaired at the Salt Lake City roundhouse, and following this procedure, the engines were placed in switching services, both interstate and intrastate in Utah. The Supreme Court in this case ruled in favor of the taxpayer and found that no taxable moments not involved with interstate commerce existed and, therefore, no tax was due. The Court held that the transfer of switching engines from Nebraska to Utah was a furtherance of interstate commerce and did not establish a withdrawal of engines from interstate activities during the course of their movement so as to subject them to a state use tax when they came to rest in Utah for servicing, inspection and overhauling before commencing switching operations here.

The *Southern Pacific Co. v. Utah State Tax Commission case*, *supra*, was one where the Commission had assessed use tax against the food carried on trains of the taxpayer for the purpose of feeding dining car stewards and other employees. In that case, the Court held that the storage of consumption of said foods within the state of Utah was in furtherance of interstate commerce and, therefore, taxation of the same was forbidden by the Commerce Clause. The food involved was purchased outside of the state of Utah. The Court, speaking through Mr. Justice McDonough, said :

“The furnishing in Utah of the prepared meals for the crew differs then from an event which takes place before transportation in interstate commerce of goods in relation to which the event occurs, or one which occurs in relation thereto after such transportation ceases. The event here sought to be taxed is one in furtherance of interstate commerce, the consumption of the goods not merely in the course of an interstate journey but in interstate commerce.”

Generally, both cases were given a similar interpretation: the Court held that the Commerce Clause of the Constitution foreclosed the taxation involved because the subject matter of each was in the course of movement in interstate commerce. Both cases involved the use tax. It is respectfully submitted that the instant case does not fall within the same category, but rather should be treated as a tax imposed upon local business activity and applicable to all transactions on the same basis, not intending, nor in fact discriminating against interstate commerce.

Several efforts have been made to apply sales and use tax to articles used in interstate commerce. In *Helson and Randolph v. Kentucky*, 279 U. S. 245, 49 S. Ct. 279, 73 L. Ed. 683 (1929), cited by petitioner, the United States Supreme Court faced for the first time the validity of use taxes as applied to articles used in interstate commerce. There, Kentucky levied a tax upon all gasoline used or sold within the state. The objecting taxpayer was a citizen and resident of Illinois where it had its place of business. Taxpayer did an exclusively interstate ferry

business, and the gasoline used to create the motive power of the ferry was purchased outside Kentucky, although 75 per cent of it was actually consumed within the borders of Kentucky. Using familiar doctrinal declarations, the Court condemned the use tax as a "direct burden" upon the "privilege of using an instrumentality of interstate commerce." See 279 U. S. at p. 252.

Other cases to the same effect followed, including the *Union Pacific* and *Southern Pacific* cases heretofore mentioned and relied upon by petitioner.

Following the immunity from use taxes granted by the *Helson* case and those that followed, an escape from sales tax on articles to be used in interstate commerce was attempted in *Eastern Air Transport, Inc. v. South Carolina Tax Comm.*, 285 U. S. 147, 52 S. Ct. 340, 76 L. Ed. 673 (1932).

The court refused, however, to expand the zone of tax immunity in this field. In the *Eastern Air Transport* case, South Carolina had imposed on all dealers in gasoline a license tax measured by the number of gallons of gasoline sold in the state. The complaining taxpayer operated planes only in interstate commerce. Purchases of gasoline were made in the taxing state for use of its planes, and the seller added the amount of the tax to the price which the purchaser had to pay. In refusing an injunction against the collection of the tax as an alleged violation of the Commerce Clause, the court sustained the validity of the tax as applied to the taxpaying

carrier, although engaged exclusively in interstate commerce. It said:

“Mere purchase of supplies or equipment for use in conducting interstate commerce is not so identified with that commerce as to make the sale immune from a non-discriminatory tax imposed by the state upon intrastate dealers.”

The court found no difficulty in distinguishing the sales tax involved in the Eastern Transport case from the use struck down in the Helson case, on the ground that a use is “manifestly different from . . . a tax upon purely local sales.”

A state taxing statute can be invalidated under the Commerce Clause only if it subjects interstate commerce to such a burden as is tantamount to an interference with the power of Congress to regulate commerce among the several states. *Gibbons v. Ogden*, 9 Wheat. 1. Whether or not it interferes with interstate commerce is a question of fact. *Hump Hairpin Co. v. Emerson*, 258 U. S. 290, 42 S. Ct. 305, 66 L. Ed. 622 (1921); *Kansas City Bell Ry. Co. v. Kansas*, 240 U. S. 227, 36 S. Ct. 261, 60 L. Ed. 617 (1915).

A tax imposed upon a local activity, or imposed on an interstate transaction before the interstate movement has commenced or after it has come to rest, is valid because it cannot be imposed in more than one state. *American Mfg. Co. v. St. Louis*, 250 U. S. 459, 39 S. Ct. 522, 63 L. Ed. 1084 (1919); *Western Livestock v. Bureau*, 303 U. S. 250, 58 S. Ct. 546, 83 L. Ed. 823 (1937); *Coverdale*

v. *Pipe Line Co.*, 303 U. S. 604, 58 S. Ct. 736, 82 L. Ed. 1043 (1937); *Gregg Dyeing Co. v. Query*, 286 U. S. 472, 52 S. Ct. 631, 76 L. Ed. 1232 (1931). The tax here is upon a sale of services rendered, a local event which can take place in only a single state. It is imposed not upon the seller but upon local buyers, who cannot be taxed in any other state. *Wiloil v. Penna.*, 294 U. S. 169, 55 S. Ct. 358, 79 L. Ed. 838 (1934); *Utah Power Co. v. Pfofost*, 286 U. S. 165, 52 S. Ct. 548, 76 L. Ed. 1038 (1931). A similar case considered by the Utah Supreme Court was that of *Union Stockyards v. State Tax Commission of Utah*, 93 Ut. 174, 71 P. 2d 542 (1937). In that case the plaintiff was a corporation engaged in the business of unloading, feeding, watering and reloading livestock intransit in interstate commerce as an agent of interstate railroads operating in and through Ogden. A primary duty of feeding and resting livestock was with the shipper, but ~~the~~ the carrier was subject to penalty if it failed to furnish proper facilities and opportunity for the unloading, feeding and resting of the animals so moving in interstate commerce. The State Tax Commission levied against a plaintiff a tax on the value of the hay, grain and straw furnished by plaintiff to livestock under such contracts. *The tax levied included a small amount assessed for the furnishing of hay, grain and straw to livestock moving in interstate commerce.* (Emphasis supplied) It was therein stated:

“It may be conceded without discussion that the livestock in question were intransit in interstate commerce and that the carriers provided for the feeding of such livestock by plaintiff pursuant to the federal statutes. The tax cannot be dismissed because the feed sold is consumed by animals in

the course of shipment in interstate commerce. *The incidence of the tax is before the interstate commerce began, as applied to the articles taxed.* The Utah sales tax is a tax on the transaction. (Citing cases.) Here the hay, grain, and straw did not become a part of interstate commerce until after it had been fed to the livestock. The situation is analogous to that in the case of *Nashville, C. & St. L. Ry. v. Wallace*, 288 U. S. 249, 53 S. Ct. 345, 77 L. Ed. 730, 87 ALR 1191, where gasoline purchased by the carrier outside of the state of Tennessee was brought into that state in tank cars, unloaded and placed in carrier's own storage tanks. It was withdrawn and used by the carrier as motive power in interstate operation. The United States Supreme Court held that the gasoline on being unloaded and being stored ceased to be a subject of interstate commerce and lost its immunity as such from state taxation. The state tax was imposed on the withdrawal of the gasoline for use by the carrier." (Emphasis supplied)

The Court added that the principles of the *Union Stock Yards* case were reaffirmed in *Edelman v. Bowing Air Transport, Inc.*, 289 U. S. 249, 53 S. Ct 591, 77 L. Ed. 1155 (1932), and it then said:

"It is not contended that the hay, grain and straw, before being used by plaintiff in feeding the livestock in question had any interstate commerce status. We think it did not become a part of interstate commerce until after it was fed to the livestock. *The tax was on the sale in this state and not on the use of these products in interstate commerce.*" (Emphasis supplied)

That even a use tax case may be distinguished on a "local event" theory is the holding of *Southern Pacific v. Gallagher*, 306 U. S. 167, 59 S. Ct. 389, 83 L. Ed. 586



(1938), where it was said that activities and events indispensable to interstate commerce have been recognized by the Court as local privileges for tax purposes, even though the taxable moment is most brief. It was there held that the retention and installation of property are intrastate taxable events, and that there is a taxable moment when the property has reached the end of its intrastate haul and has not yet begun to be consumed in the interstate operation of the railroad. The Court there said, "... prohibited is state interference with commerce, a matter distinct from the expense of doing business."

Although the tax herein is a sales or excise tax, an analogous problem has been considered in the area of gross receipt taxes. It has been held that using gross receipts to determine the value of a local activity or event for tax purposes is proper. This has been applied to a wide variety of business activities, including manufacturing, production and extraction of natural resources. These activities in themselves are not interstate commerce for tax purposes. See *Utah Power & Light v. Pfof*, 286 U. S. 165, 52 S. Ct. 548, 76 L. Ed. 1038 (1932). The tax is considered as levied on a local activity distinct from interstate commerce and has been upheld in addition to an ad valorem tax. *American Mfg. Co. v. St. Louis*, 250 U. S. 459, 39 S. Ct. 522, 63 L. Ed. 1084 (1919). In *Department of Treasury v. Ingram-Richardson Mfg. Co.*, 313 U. S. 252, 61 S. Ct. 866, 85 L. Ed. 1313 (1940), a tax on enameling of stove parts in interstate commerce was upheld, very closely analogous to the present case.



However, in the present case the activity taxed is not an interstate commerce activity but is wholly intrastate. It is conditioned upon local activity, that is, the repair of locomotives performed by petitioner entirely within this state. This repair service is purchased by foreign railroads and is conditioned upon performance within this state. It is an activity which apart from its effect on commerce because of the very nature of the purchaser is subject to the state taxing power. The effect of the tax even though on services measured by interchange rules is neither to discriminate nor obstruct interstate commerce more than numerous state taxes which have repeatedly been sustained as involving no prohibitive regulation of interstate commerce. See *Aero Mayflower Transit Co. v. Board of R. R. Commrs.*, 332 U. S. 495, 68 S. Ct. 167, 92 L. Ed. 99 (1947), where a gallonage tax imposed upon gasoline purchased within a state was applied to a wholly interstate carrier and was held to be not an unconstitutional burden. And in the case of *McGoldrick v. Berwind White Coal Mining Co.*, 309 U. S. 33, 60 S. Ct. 388, 84 L. Ed. 565 (1940), it was held:

“Sales tax conditional on delivery of possession to purchaser within this state is based on local business activities, which apart from its effect on interstate commerce, is subject to the taxing power of the state, and hence such a tax does not discriminate against interstate commerce.”

In this same case, it was held that the test is, does the tax have a tendency to prohibit the commerce or place it at a disadvantage as compared to intrastate commerce.

### POINT III

THE FACT THAT RIO GRANDE IS PROHIBITED BY FEDERAL LAW FROM MOVING DEFECTIVE CARS DOES NOT REQUIRE THAT A TAX UPON REPAIRS OF SUCH CARS BE DEEMED AN ILLEGAL INTERFERENCE WITH INTERSTATE COMMERCE.

Petitioner contends that because of the federal law regulating the transporting of defective railroad cars and because of the fact that the nature of the repair as well as the amount charged therefor is regulated by the Association of American Railroads by its "Interchange Rules," that the tax imposed is a direct interference with congressional legislation now occupying the field for the regulation of commerce. This argument assumes that the tax imposed herein does interfere with commerce. If it does not constitute an illegal interference with interstate commerce, it does not matter that some aspects of railroad operation are regulated by the Federal government. There is no showing that the sales tax which is the subject of this appeal interferes with duties imposed by the Federal government any more than does the use tax which petitioner admits is a valid and proper exercise of the taxing power. As long as the tax is not imposed upon an agency of the Federal government, it matters not that the company sought to be taxed is regulated in other areas of its business life by the government. See *Alabama v. King & Boozer*, 314 U. S. 1, 62 S. Ct. 43, 86 L. Ed. 3 (1941).

Petitioner contends that because it is forbidden by Federal law from operating defective equipment that, therefore, it is impliedly required by the same law to

make repairs and perform services. Assuming the validity of this logic, it is next contended that the Tax Commission seeks to impose a tax burden upon the performance of required duties, and that such a tax is a direct burden upon interstate commerce.

The fallacy of this logic becomes apparent upon examination of its premises:

1. A tax upon repair as a local incident is not necessarily a tax on interstate commerce nor need it unduly burden such commerce.
2. Purchases or sales in accordance with governmental requirements or specifications are not exempt from state taxation unless the purchaser or seller partakes of the governmental immunity of the agency making the requirements. See *Alabama v. King & Boozer, supra*.

Petitioner implies that the state of Utah is seeking to regulate the activities of railroads. Such is not the case. The Tax Commission only attempts to impose a tax upon a service transaction completed entirely within this state. In so doing, the Commission is complying with a valid grant of legislative authority.

It is significant to note that the Utah Supreme Court has spoken concerning this particular matter. In the *Union Stock Yards case, supra*, at page 179, the court said:

“So here, the fact that plaintiff was licensed and under regulation of the Federal Government did

not convert it into an agency or instrumentality of the Government or confer immunity from the payment of the state sales tax on provender sold by it to be used in interstate commerce. We think it no different from any other sale by a local merchant of articles to an interstate carrier, even though such articles are immediately attached to trains or buses for the purpose of engaging in or becoming a part of interstate transactions. *The sale is complete within the state before the article commences its journey in interstate commerce.*" (Emphasis supplied)

Petitioner cites several cases in support of its contention, all of which are clearly distinguishable on their facts in that none of these cases deals with a sales or transaction tax as does the instant case.

The most important of these cases is that of *Joseph v. Carter & Weekes Stevedoring Co.* 330 U. S. 422, 67 S. Ct. 815, 91 L. Ed. 993 (1947). The decision in that case was reached after the Court professed to apply a multiple burden or multiple taxation doctrine, and upon a failure to find stevedoring distinct enough from interstate commerce to permit the tax on a "local event" theory, the New York gross receipts tax was invalidated.

This case is important because it illustrates the theory of the Commerce Clause and its relationship to taxation. Commerce is not to be subjected to the multiple burdens of taxation by the various states so as to place it at a competitive disadvantage with local business.

It cannot be stressed too greatly that in the case presently before this Court the incident of taxation, i.e.,

servicing or repairing, clearly cannot be reached, tax-wise, by another state. The activity of repairing and furnishing service is confined exclusively to the state of Utah which imposed the tax. No other state has jurisdiction to impose a tax on these services. The risk of multiple taxation does not exist in the present case.

Local business in Utah, including servicing and repair of planes, trucks, buses, etc., presumably must pay the sales tax involved herein. Therefore, interstate commerce would not be placed at a competitive disadvantage with local business by reason of the tax. In fact, the effect of petitioner's claimed exemption gives to interstate commerce a large tax immunity as compared with the tax burden on local business. To grant petitioner's claim will be to not equalize the tax burden as between interstate and local business but to give interstate business a competitive advantage. Such would be to grant a discriminating preference to this interstate business — a result which it is exceedingly difficult to believe the Commerce Clause ever was intended to achieve.

## CONCLUSION

The trend in recent years has been away from a strict construction of the Commerce Clause. As late as 1939, a preponderance of government activities were deemed exempt from sales or use tax for varying reasons. The Commerce Clause had been an oasis of exemption, and probably the most prolific source of exemptions has been the area of interstate commerce. Up until the early 1930's it was very strictly construed. Beginning with

the case of *Western Livestock v. Bureau*, 303 U. S. 250, 58 S. Ct. 546, 82 L. Ed. 823 (1938) where the court said, "Even interstate commerce must pay its way," a gradual lessening of this construction has been noted. Recent pronouncements by the Court evidence no change from the pervading liberal interpretation. *Scripto, Inc., v. Carson*, ..... U. S. ...., 80 S. Ct. ...., 4 L. Ed. 2d 660, Decided March 21, 1960.

In summary, it is the position of the Commission that the repairs made by the Rio Grande to cars, locomotives and other rolling stock of foreign lines are a local business activity, the incidence of which is before the beginning of interstate commerce, as applied to the article or the service which is taxed. That the Utah sales tax is a tax upon a transaction, and the transaction in the present case was completed before it became part of interstate commerce. That the cases cited by petitioner are clearly distinguishable on their facts from the instant case. It is respectfully submitted, therefore, that the taxation of such repairs is not forbidden by the Commerce Clause but should properly be upheld against petitioner.

Respectfully submitted,

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