

1960

University Heights, Inc. v. State Tax Commission of The State of Utah : Brief of Respondent

Utah Supreme Court

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IN THE SUPREME COURT OF THE STATE OF UTAH

UNIVERSITY HEIGHTS, INC.,
a Utah Corporation,

Petitioner,

— vs. —

STATE TAX COMMISSION OF
UTAH,

Respondent.

Case
No. 9313

FILED
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Clark, Supreme Court, Utah

BRIEF OF RESPONDENT

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TABLE OF CONTENTS

	Page
STATEMENT OF THE CASE.....	1
STATEMENT OF FACTS.....	2
STATEMENT OF POINTS.....	3
ARGUMENT	3
POINTS:	
I. The Tax Commission is not bound by a county asses- sor's determination of value of property for property tax purposes, but may properly make its own deter- mination of fair value for purposes of the franchise tax	3
II. The Utah franchise tax is not a property tax and therefore is not subject to the constitutional require- ment of taxation according to value.....	9
CONCLUSION	13

Authorities Cited

Cases

American Investment Corp. v. State Tax Comm. of Utah, 101 Utah 189, 120 P. 2d 331 (1942).....	6
American States Water Service Co. of Calif. v. Johnson, 31 Cal. App. 2d 606, 88 P. 2d 770 (1939).....	7
Atlantic and Pacific Tel. Co. v. Philadelphia, 190 U. S. 160, 23 S. Ct. 817, 47 L.Ed. 995 (1902).....	7
Blackrock Copper Mining & Milling Co. v. Tingey, 34 Utah 369, 98 Pac. 180 (1908).....	11
Commonwealth v. Ford Motor Co., 350 Pa. 236, 38 A. 2d 329, App. dismissed 324 U.S. 827, 65 S. Ct. 857, 89 L.Ed. 1394 (1944)....	11
Douglas Aircraft Co. v. Johnson, 13 Cal. 2d 545, 90 P. 2d 572 (1939)	10
Emerald Oil Co. v. State Tax Comm., 1 Utah 2d 379, 267 P. 2d 772 (1954).....	6
Jersey City v. Martin, 126 N.J.L. 353, 19 Atl. 2d 40 (1941).....	10
J. M. & M. S. Browning Co. v. State Tax Comm., 107 Utah 457, 153 P. 2d 993 (1945).....	6
Kaiser Land & Fruit Co. v. Curry, 155 Cal. 638, 103 Pac. 341 (1909).....	10

TABLE OF CONTENTS — (Continued)

	Page
Phoenix Carpet Co. v. State, 118 Ala. 143, 22 So. 627, 72 Ann. St. Rep. 143 (1897).....	10
Standard Underground Cable Co. v. Attorney General, 46 N. J. Eq. 270, 19 Atl. 733, 19 Ann. St. Rep. 394 (1890).....	10
State v. Maine Cent. R. Co., 74 Me. 376 (1882).....	10
State v. Western Union Tel. Co., 73 Me. 518 (1882).....	10
Utah-Idaho Sugar Co. v. Salt Lake County, 60 Utah 491, 210 Pac. 106 (1932).....	5

Statutes

Constitution of Utah

Article 13, Section 2.....	6
Article 13, Section 3.....	9
Article 13, Section 12.....	5

Utah Code Annotated, 1953, as amended

Section 59-3-20(6) (f)	8
Section 59-5-1	2
Section 59-5-46.1	8
Section 59-5-46(9)	2
Section 59-5-47	4
Section 59-13-3	8, 12
Section 59-13-26	4
Section 59-13-52	4

Texts and Treatises

Cooley, Taxation, 4th Ed., Volume II

Section 849	10
Section 850	10

American Law Reports, Annotated

71 A.L.R. 266	11
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IN THE SUPREME COURT
OF THE STATE OF UTAH

UNIVERSITY HEIGHTS, INC.,
a Utah Corporation,
Petitioner,

— vs. —

STATE TAX COMMISSION OF
UTAH,
Respondent.

Case
No. 9313

BRIEF OF RESPONDENT

STATEMENT OF THE CASE

This is a proceeding to review an order and decision of the Tax Commission imposing additional corporation franchise tax upon petitioner, University Heights, Inc., as a result of a disagreement as to the method of determining the value of the petitioner’s corporate franchise.

The statute imposing the tax provides that it shall be equivalent to 4 per cent of the net income of the corporation, or 1/20th of 1 per cent of the fair value during the next preceding taxable year of the corporation’s tan-

gible property, whichever is greater. The petitioner determined in the present case that the tax should be paid upon the property base and filed its return accordingly. The question presented, therefore, is when the tax is paid on the property base, whether the fair value of such tangible property shall be computed from a determination made by the county assessor for property tax purposes, or on the other hand should consist of an evaluation of the corporate property as determined by the Tax Commission, the latter being greater.

No attempt will be made to defend the constitutionality of Sections 59-5-46(9) and 59-5-1, Utah Code Annotated, 1953, as such sections were not considered by the Tax Commission in its determination of this matter.

STATEMENT OF FACTS

The Tax Commission agrees substantially with the facts as set forth by the appellant. However, in the interests of clarification and amplification the following brief statement is submitted.

A corporation franchise tax deficiency was proposed against the petitioner for the years 1956, 1957 and 1958. The corporation in filing its returns computed the tax on the property base arriving at the fair value of its tangible personal property in Utah by considering the assessed value, as determined by the county assessor, to represent 40 per cent of the fair value of the corporation. The petitioner reported and paid a tax in the amount of \$707.79. The State Tax Commission refused to accept this meth-

od of determining the value of the property in question, and in lieu thereof the said Tax Commission determined the value of said property by reference to depreciated book values as shown by the balance sheets on returns filed by the taxpayer for the years in question. Thereupon the Tax Commission assessed an additional \$619.70, plus interest in the amount of \$59.71. There is no showing that the respondent acted in an arbitrary manner in making said assessment or that it departed in any way from standard valuation procedures.

STATEMENT OF POINTS

POINT I

THE TAX COMMISSION IS NOT BOUND BY A COUNTY ASSESSOR'S DETERMINATION OF VALUE OF PROPERTY FOR PROPERTY TAX PURPOSES, BUT MAY PROPERLY MAKE ITS OWN DETERMINATION OF FAIR VALUE FOR PURPOSES OF THE FRANCHISE TAX.

POINT II

THE UTAH FRANCHISE TAX IS NOT A PROPERTY TAX AND THEREFORE IS NOT SUBJECT TO THE CONSTITUTIONAL REQUIREMENT OF TAXATION ACCORDING TO VALUE.

ARGUMENT

POINT I

THE TAX COMMISSION IS NOT BOUND BY A COUNTY ASSESSOR'S DETERMINATION OF VALUE OF PROPERTY FOR PROPERTY TAX PURPOSES, BUT MAY PROPERLY MAKE ITS

OWN DETERMINATION OF FAIR VALUE FOR PURPOSES OF THE FRANCHISE TAX.

The taxpayer contends that it is proper to use the assessed value of property for property tax purposes to determine the "fair value" of its property for franchise tax purposes. In this regard, petitioner contends that the Tax Commission is bound to accept the County Assessor's determination of "value" for purposes other than which it was intended. With this contention the Tax Commission must respectfully disagree. The Tax Commission is not bound to accept any valuation of the County Assessor. Section 59-5-47, Utah Code Annotated, 1953, provides that the Commission "may of its own initiative order or make an assessment or re-assessment of any property which it deems to have been over-assessed or under-assessed or which it finds has not been assessed." The County Assessor is not charged with the duty of determining the value of corporate franchises. The Tax Commission alone has the responsibility to determine the correct amount of tax due. See Section 59-13-26, Utah Code Annotated, 1953. The Tax Commission alone is empowered to examine the taxpayer's records for the purpose of ascertaining the correctness of any return. Section 59-13-52, Utah Code Annotated, 1953. In fact, it would be intrepid for the Commission to adopt the petitioner's contentions and to do so would be unfair to the petitioner itself. The County Assessor by experience and profession is prepared to determine the value of property. However, as will more fully appear later, a tax upon the corporate franchise in Utah is not a property tax, but rather is a tax upon the

privilege of doing business within the state. This is true even though the tax be computed upon the property base. The Tax Commission maintains an experienced staff, the sole function of which is to determine the value of property for purposes of the franchise tax. It should be apparent that more accurate valuations may be obtained by such a staff than could be obtained by following determinations made by a County Assessor motivated by entirely different purposes. In fact, because of certain pronouncements by the Utah State Supreme Court, the Tax Commission could prudently assume no other course. In the case of *Utah-Idaho Sugar Co. v. Salt Lake County*, 60 Utah 491, 210 Pac. 106 (1932), Mr. Justice Thurman stated in a concurring opinion that a certain tax was an income tax and that taxation as a property tax was excluded “. . . by the provision of the State Constitution (Article 13, § 12) which reads as follows:

‘Nothing in this Constitution shall be construed to prevent the Legislature from providing a stamp tax, or a tax based on income, occupation, licenses or franchise.’ ”

That opinion continued:

“From the section just quoted nothing can be clearer than that the constitutional convention regarded a property tax as one thing and a tax based on income as another. The tax on property was provided for in the preceding sections of the article, while a tax based on income was provided for as a separate and distinct subject of taxation in the section quoted. (As is the franchise tax.) With this provision of the Constitution staring him in the face, what right or power had the assessor of Salt Lake County to assume that the

income or earnings from the management of physical property not reduced to tangible form could be assessed as property the same as physical property may be assessed?”

The court held that the franchise to be a corporation was not taxable property under the meaning of the Utah Constitution, Article 13, Section 2 and, therefore, could not be assessed in the same manner as tangible property.

In the case of *American Investment Corp. v. State Tax Comm. of Utah*, 101 Utah 189, 120 P. 2d 331 (1942), it was held that the tax imposed by a statute requiring corporations annually to pay the state for the privilege of exercising its corporate franchise or doing business in the state, based on its net income allocated to the state, was not a “property tax” nor an “organization tax” but a “tax on the privilege of exercising the corporate franchise,” or, in other words, on the privilege of doing business in the state. The court reiterated this doctrine in the case of *J. M. & M. S. Browning Co. v. State Tax Comm.*, 107 Utah 457, 153 P. 2d 993 (1945). The court said:

“The use of net income allocated to Utah as a measure for the amount of tax to be paid by a corporation for the privilege of doing business has a reasonable common sense basis. The more net income realized from doing business in Utah, the more valuable the privilege and the higher the tax.”

See also, *Emerald Oil Co. v. State Tax Comm.*, 1 Utah 2d 379, 267 P. 2d 772 (1954).

This position is in accord with that taken by the Supreme Court of the United States when it held in the case of *Atlantic and Pacific Tel. Co. v. Philadelphia, Pa.*, 190 U.S. 160, 23 S.Ct. 817, 47 L.Ed. 995 (1902), that a corporate franchise is valuable entirely apart from, or in addition to, the corporation's other property or assets.

Modern cases generally sustain this view. In the case of *Commonwealth v. Ford Motor Co.*, 350 Pa. 236, 38 A. 2d 329, App., dismissed 324 U.S. 827, 65 S. Ct. 857, 89 L.E. 1394, (1944), it was held that being an excise tax, the State may fix as a measure of the corporation franchise the value of the corporation's property, even property which would not ordinarily be amenable to property tax. And the California High Court has held that a franchise tax differs materially from a property tax, as levied for state and municipal purposes, in the basis prescribed for computing the amount of the tax. *American States Water Service Co. of California v. Johnson*, 31 Cal. App. 2d 606, 88 P. 2d 770 (1939).

It is apparent that whether the franchise tax is computed upon the basis of net income or the basis of tangible property that it cannot be considered a property tax. It should follow that an independent evaluation of property for franchise tax purposes should be made. To accept petitioner's contentions in this regard is to say that the County Assessor's determination should also be binding in other non-property tax areas, such as the determination of value for inheritance tax purposes. To rule accordingly is to completely disrupt established procedures.

It seems fairly evident from the Utah statutes alone that the legislature intended the valuation of corporate franchises to be placed on a different basis from the regular property tax assessment. The Utah Code Annotated, Section 59-5-46.1 provides that the State Tax Commission in cooperation with the various county assessors shall make an evaluation of all taxable property in the county at least once every five years. However, in regard to corporate franchise taxes, Section 59-13-3 provides in part:

“Every bank or corporation . . . for the privilege of exercising its corporate franchise or for the privilege of doing business in the state, shall annually pay to the state a tax equal to four per cent of its net income for the preceding taxable year computed and allocated to this state in a manner hereinafter provided, or 1/20th of one per cent of the fair value *during the next preceding taxable year* of its tangible property in this state, whichever is greater . . .” (Emphasis supplied)

Section 59-3-20(6)(f), Utah Code Annotated, 1953, as amended, provides:

“The value of a corporation’s tangible property for the purpose of this section shall be the *average value of such property during the taxable year*.” (Emphasis supplied)

It is evident from these statutory provisions that it was intended by the legislature that the value of a corporate franchise be determined more often than every five years, whereas tangible property need only be re-evaluated once every five years. It is also apparent that a fair and accurate picture of the value of a corporation franchise cannot be had by relying on an outmoded figure

reached by a County Assessor. Real property values tend to remain constant. The value of business property is a product of many factors and may fluctuate rapidly. The legislature was aware of this and provided valuation procedures accordingly. The Tax Commission should not be bound by the County Assessor's determination for non-property tax purposes.

POINT II

THE UTAH FRANCHISE TAX IS NOT A PROPERTY TAX AND THEREFORE IS NOT SUBJECT TO THE CONSTITUTIONAL REQUIREMENT OF TAXATION ACCORDING TO VALUE.

Petitioner contends that a franchise tax imposed upon the "fair value" of its assets violates the Utah Constitution, Article 13, Section 3. It is contended that the addition of the word "fair" to modify the value in money or cash value standard set by the Utah Constitution is unconstitutional and renders the section void.

Assuming the validity of this argument for property tax purposes, it is submitted that petitioner fails to take into consideration the fact that there are several constitutional provisions relating to taxation which apply to property taxes but not to excise taxes. It is respondent's position that Article 13, Section 3, is such a provision. In Utah the franchise tax is an excise tax or a privilege tax and need not be based on the value of the franchise. Indeed, such a franchise tax is not subject to constitutional provisions regarding taxation according to cash

value. In Utah the franchise tax is imposed upon the privilege of doing business within the state. This proposition and the underlying principles concerned therewith is succinctly stated by Cooley in his work on Taxation, Volume II, Section 849, pg. 1714:

“Very often a tax would be unconstitutional and void if a ‘property’ tax while it would be constitutional and valid if in reality an excise. It is natural, therefore, in such cases, that corporations seek to have such taxes declared a property rather than an excise tax. If the tax is held to be an excise rather than a property tax, it is not subject to the constitutional requirement of equality and uniformity of taxation, or the requirement of taxation according to value.”

Section 850 of the same work provides:

“The constitutional provision that taxation shall be according to value applies to property taxes and not to excise taxes. It follows that if a tax on franchises is a property tax it must be based on the value of the franchise, while if the tax on franchises is an excise tax it need not be based on their value.”

The following also furnish support for the above proposition: *Phoenix Carpet Co. v. State*, 118 Ala. 143, 22 So. 627, 72 Am. St. Rep. 143 (1897); *Kaiser Land & Fruit Co. v. Curry*, 155 Cal. 638, 103 Pac. 341 (1909); *State v. Maine Cent. R. Co.*, 74 Me. 376 (1883); *State v. Western Union Tel. Co.*, 73 Me. 518 (1882); *Standard Underground Cable v. Attorney General*, 46 N.J. Eq. 270, 19 Atl. 733, 19 Am. St. Rep. 394 (1890); *Douglas Aircraft Co. v. Johnson*, 13 Cal. 2d 545, 90 P. 2d 572 (1939); *Jersey City v. Martin*,

126 N.J.L. 353, 19 Atl. 2d 40 (1941); Annotation 71 ALR 266.

As the standard of “value” for purposes of the franchise tax need not and cannot be the same as “value” for property tax purposes and as the constitutional provision that taxation shall be according to value does not apply to the franchise tax, it should follow that petitioner’s argument herein must fail. Indeed, this may well be the lesson of an early Utah case. In 1908 the Utah Constitution provided:

“All property in the state, not exempt under the laws of the United States, or under this constitution shall be taxed in proportion to its value, to be ascertained as provided by law. The word ‘property’ as used in this article, is hereby declared to include . . . franchises . . .”

In construing the then existing constitutional provision, the Utah Supreme Court in the case of *Blackrock Copper Mining & Milling Co. v. Tingey*, 34 Utah 369, 98 Pac. 180, held that the constitutional provision did not apply to a license tax on the privilege of existing as a corporation as distinguished from a license tax on the franchise to carry on a particular business. *It had been contended that inasmuch as franchises were declared to be property by the Constitution that it included all corporate franchises, and therefore no franchise tax could be imposed except by valuation and assessment by the regular method.* (Emphasis supplied) The court said:

“We cannot agree with this contention. To our minds it is clear that the legislature did not in-

tend the license tax imposed by the act in question as a property tax notwithstanding that the constitution provides, in the section quoted from, that franchises are property. Nor did the framers of the constitution, in our opinion, intend to limit the right of the legislature to impose any other than a property tax by valuation upon franchises by what is said in Section 2, Article 13. If such had been the intention of the framers of that instrument, all that was necessary to say was said in Section 2 of that article. Why therefore specially refer to franchises again in Section 12 of the same article, and there expressly state that the legislature may impose a license tax upon franchises, if it was intended that no tax other than a direct valuation tax could be imposed upon corporate franchise? In our view these two provisions are not even conflicting, but if they were, it would be our duty to harmonize them and to give each one its proper effect so far as possible under the rules of construction.”

The present-day constitutional provisions have changed, but it would appear that the Utah Court has adopted the rules as stated by Cooley and as set forth in Point I, *supra*. If this is true, then the requirement that all property must be assessed at 40 per cent of its value does not apply to an assessment for franchise tax purposes. The legislature may fix a different rate for such purposes and has in fact done so by the enactment of Section 59-13-3, Utah Code Annotated, 1953. As corporate property is not subject to an assessment of 40 per cent for franchise tax purposes, it should follow that corporate franchise values cannot be determined by subjecting them to a faulty and illogical algebraical ratio based on pre-

determined property tax values. Value for corporation franchise tax purposes cannot be obtained by multiplying a property tax by two and one-half. It is, therefore, apparent that if the Utah franchise tax is not a “property” tax that the tax in itself is not subject to the requirement of taxation according to value and that the addition of the word “fair” as found in 59-13-3, Utah Code Annotated, cannot possibly constitute a violation of the Utah State Constitution.

CONCLUSION

If “value” for property tax purposes and “value” for purposes of the franchise tax need not be the same, it would appear that the various cases interpreting the meaning of “fair value,” “actual value,” “cash value,” etc., in different contexts, are meaningless in the present case. Therefore, assuming the general rules as stated are correct, it follows that because the Utah courts have determined that a franchise tax is not a property tax, it should also determine that the constitutional provisions as to taxation and assessment of real properties should not apply in this area.

The decision of the Tax Commission should be upheld.

Respectfully submitted,

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