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Walker Center Corporation, A Utah Corporation v. State Tax Commission of Utah : Appellant's Brief

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IN THE SUPREME COURT OF THE STATE OF UTAH

WALKER CENTER CORPORATION,
a Utah Corporation,

Plaintiff-Appellant,

— vs. —

STATE TAX COMMISSION
OF UTAH,

Defendant-Respondent.

} **Case
No. 10847**

APPELLANT'S BRIEF

CERTIORARI
TO THE STATE TAX COMMISSION OF UTAH

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18 1967

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IN THE SUPREME COURT OF THE STATE OF UTAH

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a Utah Corporation,
Plaintiff-Appellant.

vs.

STATE TAX COMMISSION
OF UTAH,
Defendant-Respondent.

Case
No. 10847

APPELLANT'S BRIEF

STATEMENT OF THE KIND OF CASE

This is a proceeding by certiorari to the State Tax Commission of Utah to review a decision of that agency sustaining a deficiency assessment in state corporate franchise tax for the year 1966 against the Plaintiff, Walker Center Corporation.

DISPOSITION BELOW

After a formal hearing before the State Tax Commission of Utah based in part upon the testimony of a witness and in part on stipulated facts the Commission entered its decision sustaining a deficiency assessment of

\$7,465.18 plus interest for state corporate franchise tax for the year 1966 against the Plaintiff.

RELIEF SOUGHT IN THIS PROCEEDING

Plaintiff seeks reversal of the decision below.

STATEMENT OF FACTS

On or about March 27, 1959, Walker Center Corporation was duly incorporated under the laws of the State of Utah. From the date of its incorporation and for all taxable periods up to and including December 31, 1965, it filed all corporation franchise tax returns and paid all corporation franchise taxes due the State of Utah. It did not file a corporation franchise tax return for 1966 based on its net income during the calendar year 1965 or based on the fair value of its tangible property in Utah during the year 1965. (R. 80)

From its incorporation through 1965 Walker Center Corporation had substantial operating losses and no net income which would have resulted in the imposition of a corporate franchise tax based on income, except that in March of 1965 substantially all of the assets of the Corporation were sold at a price which, if a franchise tax for 1966 based on 1965 income were found to be due, would result in a taxable gain against which gain the operating losses for 1965 and prior years could not be offset and which, if the corporation filed a return for 1966, would result in a tax due thereon of \$7,465.18, plus interest. The result of the operations of Walker Center

corporation through its history and including the sale of its assets in 1965 was a substantial economic loss to the stockholders of Walker Center Corporation. (R. 81)

On December 21, 1965, Walker Center Corporation duly delivered to the Secretary of State of the State of Utah its Statement of Intent to Dissolve by Written Consent of Shareholders, and as of that date all of the assets of Walker Center Corporation had been sold and distributed and, to the extent of available funds and assets, all creditors of the Corporation were paid with the exception of claims made by the State Tax Commission of Utah hereinafter referred to. The stockholders did not recover any part of their investment in the stock of the Corporation. (R. 81-82)

As of December 21, 1965, Walker Center Corporation was not engaged in the conduct of any business nor has it ever since said date conducted any business. (R. 82)

On December 23, 1965, the supervising auditor of the Corporate Franchise Tax Division of the State Tax Commission received notification from the office of the Secretary of State of the submission of the Statement of Intent to Dissolve above referred to (R. 8) and on December 27, 1965, the State Tax Commission sent a letter, under signature of auditor Horace Gailey, requesting that a copy of Form A-66, which is an information return, be filed. (R. 9) It contained the following language:

Upon receipt of this completed form, we shall start our investigation as to tax liabilities, and either issue a tax clearance certificate or advise you, as soon as possible, of any delinquencies or deficiencies which must be satisfied.

If dissolution proceedings are not complete prior to December 31, 1965, it will be necessary for you to file a corporation franchise tax return for the period then ended and pay the tax shown to be due thereon before we can issue a clearance. . . . (R. 90)

This letter was a form letter to which the second paragraph quoted above, the paragraph about the likelihood of a return becoming due, was added.

When the Tax Commission's audit of the Plaintiff was completed after December 31, 1965, it was ascertained that Walker Center Corporation owed no unemployment compensation taxes, no sales tax, only a use tax of \$40.10 which was paid on February 10, 1966, and no additional corporate franchise tax, except the 1965 corporate franchise tax based on 1965 net income which is here contested. (R. 82)

The dissolution proceedings of Walker Center Corporation have not yet been completed and the Statement of Intent to Dissolve above described has not been revoked by the corporation.

The procedure which the State Tax Commission used in processing the tax clearance of the Plaintiff was as follows: The Corporate Franchise Tax Division received notification from the Secretary of State that the Plaintiff had entered dissolution proceedings. It then notified all other taxing departments of the dissolution proceedings and requested that they search their records to determine whether any additional taxes were owing by the corporation or if any unfilled returns were due.

(R. 8) The plaintiff was not required by the procedure and did not attempt to contact the Tax Commission to say it had a deadline or a preference that clearance be issued before the end of the year. (R. 14) Only after audit showing no additional tax to be due would the Commission have issued a clearance for Walker Center Corporation to the Secretary of State. (R. 8)

Forced dissolution does come up in a number of instances with other corporations and on other occasions the State Tax Commission has applied a different procedure and has issued a tax clearance prior to the completion of the procedure which is described above and which the Commission required in the case of the Plaintiff. In such instances the clearance has been issued where the corporation has filed a bond and requested the speedy clearance. The Plaintiff or its counsel was not informed and could not have informed itself through any printed regulation or other official source, and was not advised of the possibility of obtaining or of filing such a bond in order to complete the proceedings prior to the end of the year. (R. 13-14)

The Commission did not, prior to December 31, 1966, advise Plaintiff or its counsel that the Tax Commission would be unable to issue its tax clearance prior to the end of the year. (R. 14)

ARGUMENT

I. THE DECISION BELOW IN THIS CASE AND THE WRITTEN AND PUBLISHED AND THE UNWRITTEN AND UNPUBLISHED

REGULATIONS AND THE INTERPRETATIONS AND PRACTICES OF THE STATE TAX COMMISSION OF UTAH VIOLATE THE DUE PROCESS AND EQUAL PROTECTION CLAUSES OF THE STATE AND FEDERAL CONSTITUTIONS, AND, IF, THEY ARE SUPPORTED BY STATUTE, THEY CONSTITUTE AN UNCONSTITUTIONAL DELEGATION OF THE TAXING POWER.

The due process clauses in the State and Federal Constitutions, Utah Const. Art. I, § 7; U. S. Const. Amend. XIV, require that a tax must be collected through procedures which constitute "the usual manner as provided by law"; *State ex rel. Jennings Bros. Inv. Co. v. Armstrong*, 19 Utah 117, 56 Pac. 1076, 1079 (1899); see *Jenkins v. Ballantyne*, 8 Utah 245, 249, 30 Pac. 760, 761 (1892) ("administrative process of the customary sort"); *Untermeyer v. State Tax Comm'n*, 102 Utah 214, 129 P.2d 881 (1942); and which are therefore made available to all taxpayers without discrimination. Due process also affords protection from laws which are unreasonable, arbitrary, or capricious, requiring that the means selected shall have a real and substantial relation to the object sought to be obtained, *e.g.* *Garrett Freight Lines, Inc. v. State Tax Comm'n*, 103 Utah 390, 135 P.2d 523 (1943); *Nebbia v. New York*, 291 U.S. 502, 78 L.Ed. 940 (1934). These requirements of due process have been violated by the Respondent, Tax Commission, on several grounds.

First, the guarantee of due process has been denied the Plaintiff by the failure of the Tax Commission to announce a regulation which the Plaintiff could have fore-

policy to avoid any claim by the Tax Commission for the 1966 franchise tax here in question. We refer to the commission's policy of granting tax clearance on filing a bond, thus permitting corporations in year-end dissolution proceedings to proceed rapidly to statutory dissolution and void any claim for an additional year's corporate franchise tax. The record discloses that the commission has not published, filed or otherwise made public this speedy tax clearance procedure, nor is it customarily made known to corporations in year-end dissolution through the regular correspondence of the Tax Commission. It is available only to those corporations which may have heard of the procedure or which the Tax Commission sees fit to advise of the procedure. The record contains the following testimony by the supervising auditor of the Corporate Franchise Tax Division:

Q. [O]n occasion in the past have you issued a tax clearance from your office prior to completion of an audit if the corporation has filed a bond?

A. It has been done only when the counsel or the corporation requests that this be done.

Q. I notice that in your letter of December 27th, 1965, . . . that you referred to as your action you took after you received notice of this corporation's intent to dissolve and in this letter of December 27th you didn't advise the corporation or its representatives of the possibility of obtaining or or filing such a bond in order to complete the proceedings prior to the end of the year?

A. This is true. . . .*[I]t is not customary to make these arrangements without having it sought by the corporation or its counsel.* (R. 13-14) (Emphasis added)

We do not contend that the Tax Commission may be required to give each taxpayer personal notice of regulations, but we do assert that the Commission is obligated by due process to give the taxpaying public some notice of its procedures which affect substantially the tax liability of a taxpayer. It is not proper for Commission to have two procedures for tax clearance — one in which the taxpayer must wait for Tax Commission action and one in which the taxpayer must make application and file bond — where it neglects to give public notice of one of the procedures. With respect to its speedy tax clearance procedure, the Respondent has been almost secretive and has failed to give adequate notice of the procedure, thereby violating due process.

The failure of the Respondent to publish or otherwise make known its speedy tax clearance procedure also has the effect of making the Commission's printed and published regulations and interpretations affirmatively misleading to the injury of the Plaintiff. The published regulations make tax clearance a prerequisite to the filing of a Certificate of Dissolution and to termination of corporate franchise tax liability. They provide that the taxpayer has no control over such procedure and that nothing the taxpayer can do will hasten or otherwise influence the tax clearance procedure. Corporate Franchise Tax Regulation No. 1, paragraph 9, provides:

9. For Utah corporation franchise tax purposes, a corporation which is incorporated under the laws of this state terminates its corporate existence and/or the privilege of exercising its cor-

porate franchise for which the franchise tax is
levied on the date on which:

- (a) A certificate of dissolution is issued by
the Secretary of State pursuant to a voluntary
dissolution under the provisions of Sec-
tions 16-10-77 or 16-10-78 to 16-10-88 of the
Utah Code;

Under 16-10-80 of the Utah Code, referred to in the above
citation, a corporation is required to deliver a State-
ment of Intent to Dissolve to the Secretary of State and
“with a ‘tax clearance from the state tax commission’”
before it can obtain a certificate of dissolution. In this
case after the Plaintiff had filed its Statement of Intent
to Dissolve, it was notified through a letter from the
State Tax Commission as follows:

[W]e shall start our investigation as to tax lia-
bilities and either issue a tax clearance certificate
or advise you, as soon as possible, of any delin-
quencies or deficiencies which must be satisfied.

If dissolution proceedings are not completed
prior to December 31, 1965, it will be necessary
for you to file a corporate franchise tax return
for the period then ended and pay the tax shown
to be due thereon before we can issue a clear-
ance. . . . (R. 90)

The regulation, the corporation code and the letter do
not offer the taxpayer any control over the tax clear-
ance procedure or suggest that it might file a bond. The
clear implication is that the Tax Commission in its own
time and at its own convenience will finish the procedure.
Indeed, the supervising auditor of the Corporate Fran-
chise Tax Division, after admitting that the Commission

did not notify the Plaintiff that it would be unable to issue its tax clearance prior to December 31, 1965, testified:

Q. Now in the ordinary course of dissolution proceedings by a corporation is it not the fact that . . . the notice of dissolution comes to you from the Secretary of State's office rather than from the corporation?

A. This is correct.

Q. And so in other words the procedure is the corporation files its notice of intent to dissolve with the Secretary of State, the Secretary of State in the ordinary course of its procedure notifies the Tax Commission and then the Tax Commission goes through the audit procedure and issues the tax clearance?

A. There are other departments involved other than the Tax Commission but after they issue their approval and we have found there is no taxes due, then we do issue a tax clearance to the Secretary of State. (R. 14-15)

The effect is affirmatively misleading to the taxpaying public, since the taxpayer is directed away from acts which might lead it to discover the Commission's unannounced procedure for speedy tax clearance, which procedure requires the filing of an application and bond by the taxpayer and which is customarily permitted by the Commission only if it has been "sought by the corporation or its counsel," (R. 14) and the Plaintiff has thereby been deprived of the opportunity to save itself a considerable tax by filing a bond. Therein it has been deprived of due process.

The procedure used in his case is not only improper because it is affirmatively misleading but also because it is itself constitutionally defective. The conclusion reached by the Tax Commission depends upon its interpretation of "tax clearance" as it appears in Section 94 to 96. In the case of the Plaintiff it interpreted the phrase to require a full scale audit and settlement with the taxpayer of all taxes imposed by the State before it could issue clearance and before the imposition of the franchise tax would terminate. Once the Plaintiff's statement of Intent to Dissolve had been submitted, and notice thereof had been transmitted from the office of the Secretary of State to the State Tax Commission, the taxpayer was informed by the Respondent, "[W]e shall start our investigation as to tax liabilities, and either issue a tax clearance certificate or advise you, as soon as possible." (R. 90) Thereafter the Corporate Franchise Tax Division notified all other taxing departments of the dissolution proceedings and requested that they search their records to determine whether any additional taxes were owing by the corporation or if any unfiled returns were due. (R. 8, 14) All of this procedure was entirely outside the control and management of the Plaintiff; however, the speed, exercise of discretion, efficiency, work load and other administrative factors of each individual agent and functionary of the State involved in the process of preparing and communicating tax clearance could have, and in this case did have, the effect of imposing an additional year's corporate franchise tax upon the Plaintiff.

In effect under the procedure used against the Plaintiff, the Respondent can impose a tax by its mere delay. The tax consequence is determined, not by statute, but by the Legislature, but by the Tax Commission, the Secretary of State or any employee of those agencies, or any unforeseen cause of delay in those agencies. For example, the personal vendetta of an auditor, the misfiling of a piece of correspondence in any department, fluctuations in the work load of the Tax Commission could result in an additional tax. The termination of liability for franchise tax is dependent upon the time of the issuing of tax clearance is directly dependent upon and influenced by the speed and course of administrative action and may be delayed, without being subject to any time limit within which the respective agencies are required to act. Such fortuitous determination of ultimate taxing events with respect to the Plaintiff is capricious, arbitrary and unreasonable and clearly contrary to due process.¹

Of course it is the Legislature, not the State Tax Commission, that is given the power to tax; Utah Const. Art: VI, § 1; Art: XIII, § 2; and it is an unconstitutional delegation to permit the Tax Commission to effect the imposition of a corporate franchise tax by the exercise of discretion and authority of the type found, under Respondent's interpretation, in Section 16-10-80. In *Western Leather & Findings Co. v. State Tax Comm'n*, 87 Utah 227, 48 P.2d 526, 528 (1935), it is stated:

The Legislature is not permitted to abdicate or transfer to others the essential legislative func-

¹ Compare the procedural safeguards which qualified "tax clearance" in an earlier statute. Laws of Utah 1951, ch. 58, § 1, formerly, U.C.A. 1953 78-42-6.

tion with which it is thus vested. The imposition of a tax and the designation of those who must pay the same is such an essential legislative function as may not be transferred to others. . . .

See also Carter v. Beaver County Service Area No. One, 774 P.2d 280, 399 P.2d 440 (1965), and *Tite v. State Tax Commission*, 89 Utah 404, 57 P.2d 734 (1936), in which the court has struck down unconstitutional delegations.

The Legislature may not delegate to an administrative agency arbitrary power or uncontrolled discretion. *Cotton v. Earle v. Wilson*, 15 Utah 67, 48 Pac. 150, 112 (1897); *Amos*, 79 L.Ed. 474 (1935). Construed as the Respondent has done, Section 16-10-80 of the Utah Code vests upon it absolute and uncontrolled discretion to tax or not to tax, to require extensive audit prior to tax clearance or to make summary tax clearance. As construed by the Commission there is no completeness of the statute and no setting of appropriate standards and limits upon the exercise of discretion, *Duhamel v. State Tax Commission*, 179 P.2d 252, 171 A.L.R. 684 (Ariz. 1947), and to preserve its constitutionality it must not be construed, as it has been, to grant uncontrolled discretion to the Tax Commission.

Plaintiff's rights under the equal protection clauses of the State and Federal Constitutions and the equality clause of the State Constitution have also been denied, Utah Const. Art. I, §§ 2, 24; U.S. Const. Amend. XIV, because it is being subjected to taxes not imposed upon others of the same class. While the equal protection clause does not impose an iron rule of equality, pro-

hibiting the flexibility and variety that are appropriate to reasonable schemes of state taxation, "there is no point beyond which the State cannot go without violating the Equal Protection Clause," and it "must proceed upon a rational basis and may not resort to a classification that is palpably arbitrary. . . ." *Allied Stores, Inc. v. Bowers*, 358 U.S. 522, 527, 3 L.Ed. 2d 480, 485 (1959). In *Untermeyer v. State Tax Comm'n, Inc.*, 307 U.S. 214, 129 P.2d 881, 886 (1942), the Court held that the uniformity clause, as applied to taxation statutes, requires that "the tax shall fall equally upon all similarly situated." In *Township of Hillsborough v. Cromwell*, 326 U.S. 620, 90 L.Ed. 358 (1946), the court said that the equal protection clause protects a taxpayer "from state action which selects him out for discriminatory treatment by subjecting him to taxes not imposed on others of the same class. . . ." See *State v. Mason*, 34 Utah 501, 78 P.2d 920 (1938); *Sioux City Bridge Co. v. Dakota County*, 260 U.S. 441, 67 L.Ed. 340 (1923); *Cumberland Coal Co. v. Board of Revision*, 284 U.S. 23, 7 L.Ed. 146 (1931); *Baldwin Constr. Co. v. Esser County Bd. of Taxation*, 108 A.2d 598 (N.J. 1954); *Delaware Lackawanna & W. Ry. Co. v. Kingsley*, 189 F. Supp. 32 (D.N.J. 1960).

The Respondent's procedure in issuing tax clearance, a requirement which it deems to be a prerequisite to the discontinuance of the corporate franchise tax, results in an arbitrary classification of taxpayers. The imposition of corporate franchise tax for an entire additional year in the case of the Plaintiff is dependent upon the delay, or the haste, with which the Respondent's

agents and functionaries conduct reviews and audits, exercise their unlimited discretion, and send their recommendations; and the taxpayer is not protected by a constant or reasonable limit of any kind. The supervising auditor of the Respondent's Corporate Franchise Tax Division testified as follows:

A. I received a notification from the Secretary of State dated December 21st, 1965, that an application had been submitted to that department to enter dissolution proceedings.

Q. When you receive such a notice what is your practice?

A. We notify all other taxing departments that a statement of intent to dissolve had been filed with the Secretary of State and request that they make a search of their records to determine whether any additional taxes are owing by the corporation, any unfiled returns are due and if they find it to be in good order and upon audit of the records find no additional tax to be due, we then issue a clearance to the Secretary of State.

Q. Is this clearance a condition precedent to dissolution, in other words does a corporation have to be so cleared before it can dissolve?

A. Yes, the law requires that the tax Commission must issue a tax clearance to the Secretary of State before a corporation can be dissolved.

Q. This is done as a matter of course in connection with every corporation?

A. Yes. (R. 8-9)

The effect of such tax clearance procedure is to subject some unfortunate taxpayers, including the plaintiff corporation, to taxes not imposed upon others of the same

class and similar circumstances which are fortunate enough to have the administrative action result in a year-end tax clearance. The unequal treatment to which Plaintiff and others have been subjected is "intentional" and "discriminatory," *Delaware Lackawanna & W. R.R. Co. v. Kingsley, supra*, and, hence of the type clearly proscribed by the State and Federal Constitutions.

A further denial of equal protection results from the fact that in the case of a favored group of corporations, who somehow learn of the bond procedure permitted by the Tax Commission, tax clearance can be granted as soon as the Statement of Intent to Dissolve is delivered for filing; whereas, in the case of the Plaintiff, the Tax Commission would not issue such tax clearance until after lengthy and involved administrative action has occurred. The result is that some corporations, similarly situated to Plaintiff, have not been subjected to the same tax as is now asserted against Plaintiff; thereby subjecting Plaintiff to taxes not imposed on others of its same class and injuring it in deprivation of its right to equal protection. Furthermore, it cannot be fairly asserted that the speedy tax clearance and hence the ^{avoidance of the} additional tax would have been extended to Plaintiff if it or its counsel had petitioned for such action. Plaintiff cannot have been expected to know that which it could discover only by rumor, by chance or by good fortune, because to require that would be to penalize reliance on published procedures and written correspondence of the Commission.

II. THE DECISION OF THE STATE TAX COMMISSION OF UTAH IN THIS CASE AND THE PRIOR INTERPRETATION AND APPLICATION OF THE FRANCHISE TAX BY THAT AGENCY IS CONTRARY TO THE APPLICABLE STATUTE LAW OF THE STATE.

There are conceptual differences between the corporation law and the tax law of the State, and, of course, the tax statute and not the corporation law of the State must be utilized to define the time and events as of which liability for corporate franchise tax is determined. Under § 13-13-2 of the Franchise Tax Act the imposition of the tax terminates when a corporation no longer has a privilege to "exercise" its franchise. In its present interpretation of the Franchise Tax Act the Respondent has concluded that the tax imposed thereby is not terminated until after it issues its "tax clearance," required by 16-10-80 of the Business Corporation Act and such clearance has been filed with the Secretary of State and the Certificate of Dissolution issued (16-10-88); and it assumes that "tax clearance" means a lengthy administrative process of audit and review. This interpretation suffers from the constitutional defects we have previously discussed. Recognizing the fundamental rule that statutes must be construed so as to avoid constitutional infirmities, we here propose interpretations of the statutes which we contend are reasonable and proper and eliminate these constitutional problems.

Some states have imposed their corporate tax only on corporations "doing business" in the state, see *Annot.*

18 A.L.R. 700, 702 (1922), while others have broadly extended their taxes to all corporations having bare corporate charter existence. For example, an earlier Utah corporate tax was imposed upon "all corporations organized under and by virtue of the laws of this state. . . ." Laws of Utah 1907, ch. 107, p. 126. This was characterized as a tax on the privilege to "exist" in the case of *Blackrock Copper Min. & Mill. Co. v. Tingey*, 34 Utah 369, 98 Pac. 180 (1908). See also *Federal Crude Oil Co. v. State*, 169 S.W. 2d 283 (Tex. Civ. App. 1943). The present franchise tax statutes of Utah and statutes of a number of other states contain provisions between the two extremes above, using neither bare corporate charter existence nor doing business as the limiting criteria for imposing the tax. Thus Section 59-13-3, provides:

Every . . . 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. . . . (Emphasis added)

The term "corporation" as used in that section is not defined to include all chartered corporations but rather it includes "every corporation . . . organized for profit and doing business in this state . . ." (59-13-1(3)); and "doing business" is defined to include "the right to do business," (59-13-1(5)). Utah's present law does not, then, place a tax on mere charter existence but it does impose a tax upon the privilege of "exercising" — upon the existence of a privilege to do business for profit whether that privilege is actually exercised or not. It is a tax on *active charters*. In *American Inv. Corp. v. State Tax Comm'n*, 101 Utah 189, 120 P.2d 331, 332-3-

(1941), overruled on another point, *J. M. & M. S. Brown-
ing Co. v. State Tax Comm'n*, 107 Utah 457, 154 P.2d
603 (1945), the Court said:

The tax imposed by this section is not a property
tax, nor an organization tax, but a tax on the
privilege of exercising the corporate franchise
... This is a franchise tax, a tax on the right or
privilege of doing business in the state ... lawful
business; business it may do without violating the
law. ...

The tax is not imposed on corporations which are
prevented or limited by state law from doing business
in this state. The present tax is not one on the right to
"exist," as the license tax was in the *Blackrock Copper*
case, *supra*, but upon the right to transact business ac-
tively. Cases in other jurisdictions having similar active
charter statutes have held that the franchise tax termi-
nates as soon as under state law the privilege of doing
business becomes limited. *In re Commercial Safe De-
posit Co. of Buffalo*, 266 N.Y.S. 627 (1933); *People of*
New York v. Irving Trust Co., 87 F.2d 295 (2d Cir.
1937); *Johnson v. Johnson Bros.*, 80 Atl. 741 (Me. 1911);
McKinney, Marsh & Cushing, Inc. v. Jackson Health
Resort, Inc., 56 F.2d 285 (W.D.N.Y. 1932). *Annot.*,
85 L.Ed. 656, 678 (1941); *Annot.* 76 L.Ed. 1141, 1146
(1932). Part of Respondent's regulations follow this
interpretation, although others are inconsistent with it.²

Corporate Franchise Tax Regulation No. 1, paragraph 9(d), in accord-
ance with the "active charter" requirements of the Franchise Tax Act,
specifies that suspension of corporate rights for failure to pay taxes under
59-13-61 is an event terminating the imposition of the franchise tax.
It is clear from Section 59-13-63 that such suspension does not termi-
nate charter existence. *C.f.* Prudential Fed. Sav. & Loan Ass'n v. Hart-

Prior to December 21, 1965, when Walker Center Corporation duly delivered its Statement of Intent to Dissolve by Consent of Shareholders it had ceased to engage in any business, and since that time it has not conducted any business. Also prior to December 21, 1965, it had sold and distributed all of its assets and paid all claims of creditors, except a \$40.10 claim of the State Tax Commission. The decision to dissolve was reached by the unanimous consent of all of the shareholders of the corporation. (R. 29) The act of delivering a Statement of Intent to Dissolve was an official affirmative act in the process of dissolving the corporation under the corporation law and once performed effectively limited any further corporate action to the winding up of its affairs. Walker Center Corporation has given public notice to the world and to its creditors that its existence would soon terminate. At any time after

ford Acc. & Indem. Co., 7 Utah 2d 366, 325 P.2d 899 (1958). But in paragraph 7 of the Regulation it is suggested that the tax is imposed upon mere existence, "until the corporation itself ceases to exist under the law," and in paragraph 9 "corporate existence" is equated to the statutory phrase "the privilege of exercising its corporate franchise." In paragraph 9(a) and (b) the formality of entering a Decree of Dissolution or of issuing a Certificate of Dissolution is designated as the event terminating tax liability, although under Section 16-10-101 after such events a corporation is deemed to continue to exist indefinitely for some purposes.

With the exception of paragraph 9(d) the events specified in paragraph 9 as terminating imposition of the tax are not the events by which the corporation laws of the State withdraw the privilege of exercising the corporate franchise. They do not, therefore, define appropriate tax events. For example, in voluntary dissolution proceedings, the privilege of "exercising" is withdrawn under Section 16-10-81 upon the filing by the Secretary of State of the Statement of Intent to Dissolve, since thereafter the statute says "the corporation shall cease to carry on its business except in so far as may be necessary for the winding up thereof. . . ." As the privilege of a corporation, subject to either voluntary or involuntary dissolution proceedings in court may have terminated prior to the entering of the decree of dissolution, either by a limitation of the authority of a receiver in an order issued pursuant to 16-10-93 or by 16-10-92 which applies through 16-10-92(c).

in filing the Statement to be filed, the taking of any corporate action was at the risk that the right to so act had been terminated, since the Secretary of State could at any time and without notice have "filed" the Statement pursuant to 16-10-80, and after such "filing" the corporation would be limited by 16-10-81 and could do nothing with its franchise except to wind up its affairs. The corporation had become a "worthless derelict" of no value to no one, *People of New York v. Irving Trust Co.*, 87 F.2d 295 (2d Cir. 1937).

We agree with cases which hold that taxability is dependent upon the exercise of the franchise granted, *American Inv. Corp. v. State Tax Comm'n*, 101 Utah 189, 120 P.2d 331, 334 (1941), overruled on other grounds, *J.M. & M.S. Browning Co. v State Tax Comm'n*, 707 Utah 457, 154 P.2d 993 (1945), but the present case is distinguishable because the Plaintiff's charter had become useless, and abandoned and the shareholders had performed official, affirmative acts prescribed under the corporation law for its termination. The charter existence of the Plaintiff was, as of December 21, 1965, a mere legal technicality and not a business reality. The franchise tax is imposed upon the actual privilege of exercising a franchise to do business for profit, not upon a formality of legal existence. The thing taxed must exist as a practical matter and the mere possibility that the statutory dissolution proceedings of Walker Center Corporation could have been revoked under Sections 16-10-83 to -86 does not in itself preserve the franchise or constitute a taxable franchise. In administering the franchise tax laws it is "quite impractical to

place emphasis on technical form," *Bennett Assoc., Utah State Tax Comm'n*, Docket No. 10682 (April 2, 1967). In *Weiss v. Stearn*, 265 U.S. 242, 68 L.Ed. 1001, 1005 (1924), the court said:

Questions of taxation must be determined by viewing what was actually done, rather than by declared purpose of the participants; and when applying the provisions of the 16th Amendment, and income laws enacted thereunder, we must regard matters of substance, and not mere form.

In *Griffiths v. Helvering*, 308 U.S. 355, 357, 84 L.Ed. 319, 322 (1939), the court stated:

We cannot too often reiterate that "taxation is not so much concerned with the refinements of title as it is with actual command over the property taxed — the actual benefit for which the tax is paid." . . .

As of the beginning of the 1966 tax year, Walker Center Corporation did not possess an active charter of the type which is taxable under the Utah Corporate Franchise Tax although as an empty formality its charter was still in limited existence.

Even if it is assumed, however, that it is necessary to look to the technicalities of the corporation law in deciding this case, the same result can be reached. The Tax Commission has construed the corporation statutes to require issuance of a tax clearance before tax liability terminates. The term "tax clearance" is defined in the statute, but the phrase must be given a reasonable interpretation within the context in which it is used.

The Tax Commission as to Plaintiff interpreted the term to mean audit by the Tax Commission and other agencies of the State before the document, a "tax clearance," would be issued; however, as previously discussed, the Commission has not been consistent in this interpretation, for "tax clearance" has been issued upon filing a bond, thereby interpreting the term to require summary procedure which does not contemplate final audit and payment of all of the State's tax claims prior to its issuance. In view of this inconsistency, the court should not feel inhibited by administrative construction of the phrase in defining the proper interpretation. Certainly the court may construe the phrase with as much leeway as the Tax Commission has done.

We can gain insight into the present statutes by considering their history. The franchise tax as pertinent here has not been changed for many years. The corporation laws were changed in 1961 when Utah adopted a version of the Model Business Corporation Act. One of the changes from the former law was in the procedures for dissolution. The former law required application to a court for a decree of dissolution. The draftsmen of the new act, doubtless recognizing the rather meaningless formality of court involvement where the shareholders wished to dissolve, permitted voluntary dissolution by filings and certifications made with and to the Secretary of State. Can we reasonably assume the Legislature intended to change the liability for the franchise tax by adopting this new dissolution procedure?

The former law (Chapter 42 of Title 78, P. S. 1953) provided in part:

78-42-6. . . . [I]n no instance shall the court declare the corporation dissolved until proof, in the form of a certificate from the state tax commission, has been filed by the corporation applying for dissolution that all fees, taxes, penalties, interest and costs due the state have been satisfied and discharged. If the said state tax commission refuses or fails to give such tax clearance within ninety days from the request therefor by the dissolving corporation and from the date of the filing of a verified copy of the resolution hereunto referred to, the court may, upon request for the corporation or upon its own motion, require the tax commission to appear in the proceedings and show cause at a time appointed by the court why the corporation should not be allowed to be dissolved. The court thereupon [determines] the tax liability of the corporation, and upon payment of any sums found by the court to be due to the tax commission, the court shall order the corporation dissolved. The tax liability of the corporation shall be determined as of the date the corporation formally resolved in a proceeding to quit doing business as corporation provided, however, that if a corporation does business other than in the normal course of liquidation, and winding-up its affairs, after the date determined in said resolution, the tax liability of said corporation shall be fixed as of the date the corporation actually ceased doing business. The corporation shall furnish to the secretary of state and to the state tax commission a verified copy of the resolution showing the date when the corporation resolved to cease doing business.

The former law expressly provided franchise tax liability ceased when the corporate resolution to cease doing business was adopted. The present law substitutes a Statement of Intent to Dissolve which must certify in fact that the corporation had resolved to dissolve by action of its directors and shareholders (16-10-79) or by written consent of its shareholders (16-10-78). The former law permitted corporate existence to continue for liquidation and winding up of affairs even after adoption of the resolution and the present law provides the same by permitting liquidation, winding up and payment of creditors after the Statement of Intent to Dissolve has been filed (16-10-81). The former statute like the present statute contemplates a "tax clearance" before corporate existence is terminated by the decree of dissolution, now the certificate of dissolution. It is also important to note that the former statute contemplated a lapse of time between the issuance of a tax clearance and the termination of corporate existence by the entry of a decree of dissolution. The only significant change is the omission of the provision of the former law which permitted the court to require the Tax Commission to act in assessing back taxes or, failing that, to **determine** the tax liability itself. Surely the failure to include this procedural safeguard in the new corporation law should not change the tax result.

With so many similarities between the statutes, it is unreasonable to assume that the Legislature intended to do anything more than change the agency through which the dissolution is accomplished from the courts to the Secretary of State. Certainly it is unlikely that

the Legislature, in enacting these sections as part of a basic revision of the corporation laws, intended to change or affect the liability for the franchise tax. Accordingly, the franchise tax liability of Plaintiff terminated December 21, 1965, and the receipt of a tax clearance from Respondent was not a prerequisite to such termination.

It is true that the new corporation laws do not go forward the express requirement that franchise tax liability ceases when the corporate action is taken to initiate dissolution. From this it might be argued that a different termination date for franchise tax liability was intended. But does this justify the Tax Commission asserting that the new termination date is the issuing of the Certificate of Dissolution? We think not.

The term "tax clearance" is again used in the statute. Clearance connotes review of past liability. How can one be cleared of future liability? It is retrospective in operation not prospective. Certainly the term was not intended as a means to extend tax liability. It is defined as "a certificate from the Utah State Tax Commission certifying that the named corporation has satisfied and discharged all fees, taxes, penalties, interests and costs due to the State of Utah." (16-10-2 (o)). It is not intended and is not defined to be the event as of which tax liability for the corporation franchise tax ceases. It is a mere formality in the process of dissolution which may frequently be delayed until after the liability of the corporation for the corporate franchise tax has ceased and terminated. Upon issuance of a certificate of tax clearance the State's Intent to Dissolve would

can be "filed" by the Secretary of State and the corporation would be required to cease doing business (16-10-81), must notify its creditors, liquidate its business and affairs and pay or adequately provide for payment of its obligations (16-10-82). The latter is important for if the corporation did owe any past franchise taxes or other taxes, the Tax Commission as well as other creditors would have to be paid or provision made for payment before the final dissolution could be achieved. Once all these steps have been taken and a verified statement of such facts is made to the Secretary of State pursuant to 16-10-87, the certificate of dissolution is issued and the corporate existence is terminated, except as provided in 16-10-101.

Construed in this manner the statutes make sense, eliminate the constitutional problems mentioned in Point I, and avoid the ridiculous and unfair result reached by the Tax Commission in this case. ~~When the Plaintiff filed its Statement of Intent to Dissolve, the Tax Commission would have issued its "tax clearance". The issuance of this document would terminate franchise tax liability for 1966 and subsequent years but~~

I^t would not prevent the Tax Commission from making whatever audit and review it wished over whatever period of time was reasonably required for such purpose. If any tax was found due, it would have to be paid before the dissolution could be concluded. Here the plaintiff could not properly certify that it had paid or adequately provided for all its debts until it had paid the \$40.10 use tax asserted by the Tax Commission. Even the Tax Commission bond procedure fits into this frame-

work for in a proper case the filing of a bond or "adequately providing" for payment of debts due to state for taxes. Both the concept and the fact requiring payment of state taxes before the corporation goes out of existence and makes collection difficult is carried forward under this interpretation.

Furthermore, such an interpretation does not result in unequal treatment to taxpayers. It does not require that Plaintiff be subjected to a \$7500 franchise tax liability because the Tax Commission did not (or could not) determine before year end that Plaintiff owed a \$400 use tax. It does not result in a continuing liability for franchise tax while the taxpayer is contesting an assessed tax liability, for note that if the Tax Commission theory is adopted the Plaintiff will be required to pay 1967, as well as 1966, franchise taxes, since its existence has not terminated and a tax clearance has not been issued. In addition, this interpretation prevents tax liability from being dependent upon action by the assessing authority. If this court upholds the Tax Commission theory and Plaintiff pays the 1966 and 1967 franchise taxes, there would still be no assurance that its "tax clearance" would be issued prior to January 1, 1968, when Plaintiff would become liable for 1968 franchise taxes, and the circle could continue *ad infinitum*.

Thus, there is no conceptual difficulty in terminating tax liability for corporation franchise tax purposes on a different official date than termination of the existence of the corporation for corporation law purposes. Whether it is considered that plaintiff in 196

... a new certificate of incorporation which could be taxed or that the legislature intended no change in the corporation franchise tax law when it revised the corporation laws or

that the requirement of a "tax clearance" refers to past liability and is not the official act or event which ends tax liability under the Utah Corporate Franchise Tax Act, on any of these grounds, the decision of the Tax Commission should be reversed.

FROM ASSESSING OR COLLECTING THE TAX.

An estoppel may be applied against the State if its application is necessary to prevent manifest injustice; *Kearns v. Bremerton*, 155 P.2d 493, 496 (Wash. 1945), overruled on other grounds, *Hutton v. Martin*, 252 P.2d 781 (Wash. 1953); *Walsonovich v. United States*, 335 F.2d 96, 101 (3d Cir. 1964); and the Utah Supreme Court has expressed a willingness to apply the theory against a city in its attempts to collect a tax, stating that "estoppel is the device by which courts prevent their processes from being used for unjust ends." *Peterson v. Ogden City*, 111 Utah 125, 176 P.2d 599, 604 (1947).

In *Peterson v. Ogden, supra*, Justice Wolfe stated that before an estoppel would apply against the city "the estoppel would have to be such that if the City attempted to collect the tax . . . a court of equity would enjoin the City from so doing." *Id.* 176 P. 2d at 604. He also drew the following quotation from Section 1044 of Lawrence on Equity Jurisprudence:

The most direct and effective method of averting injury through legal proceedings is one applied by the court whose process is invoked, where the party seeking any form of judicial relief, remedy, judgment or decree, affirmative or defensive, legal or equitable, to which he is not factually entitled, is prevented from accomplishing the result by the simple process of denying his right. He is barred or "estopped" from using judicial machinery for unjust ends.

While the early rule prevented application of the doctrine of estoppel to the sovereign — "the king cannot be estopped for it cannot be presumed the king would do wrong to any person," 15 *Halsbury's Laws of England* 215 (1956), quoting from *Bacon's Abridgements* — one can not now readily defend that broad statement which is based upon reason or upon recent cases. The government in its dealings should be subject to the same rule of fairness that the courts apply to others. In *Strom v. Commissioner*, 190 F.2d 283 (D.C. Cir. 1951), disapproved in a part not applicable to the instant case *Automobile Club of Michigan v. Commissioner*, 352 U.S. 180, 183-84, 1 L.Ed. 2d 746, 750 (1957), the court in holding that the Commissioner of Internal Revenue was estopped noted, "[N]o one should be permitted to found any claim upon his own inequity or take advantage of his own wrong. . . ." It then stated:

It has been well said that the government should always be a gentleman. Taxpayers expect, and they are entitled to receive ordinary fair play from tax officials. We regard as unconscionable the Commissioner's claim of authority to assess a tax in 1948 because of failure to file a return for

1938, when the Commissioner himself was responsible for that failure.

The Commissioner of Internal Revenue has also been estopped by the federal courts in other cases. See, e.g., *First Nat. Bank v. Commissioner*, 152 F.2d 132 (D.C. Cir. 1945); *Boone v. United States*, 86 F.2d 798 (6th Cir. 1936); *Jordan, Eckelberger & Co. v. Commissioner*, 88 F.2d 874 (7th Cir. 1937).

According to Respondent's interpretation of Section 10-10-80, it has power expressly conferred by law to issue tax clearances to the Secretary of State in cases of corporations in dissolution proceedings, and its acts or omissions when acting within the scope of that authority may be the basis for the application of estoppel. See *People v. Gustafson*, 127 P.2d 627, 634 (Calif. 1942), wherein it was stated:

A State, as well as an individual, may be estopped where the necessary elements or grounds of estoppel are present . . . ; it may be estopped when acting in its proprietary capacity as distinguished from its governmental capacity . . . ; and it may be estopped by the acts of its public officials done in the exercise of powers expressly conferred by law, and by their acts or omissions when acting within the scope of their authority.

See also *Annot.* 1 A.L.R. 2d 338, 346 (1948); *Ritter v. United States*, 28 F.2d 265 (3d Cir. 1928).

It would be manifestly unjust to permit the Respondent to collect the tax asserted under the decision below, because it failed to notify the Plaintiff that it

could participate in the tax clearance procedure, petition for and receive a speedy tax clearance by the end of 1965, by filing a bond. Such failure is sufficiently important to require an estoppel; because Respondent had not publicly announced its regulations permitting such petition and bond, and it was under no obligation to make its procedures known where they affected the rights of taxpayers generally; because it had "temporarily" extended such speedy clearance only to "clairvoyant" taxpayers who discovered the existence of the procedure and requested it; because the statutes governing corporate dissolution (16-10-80 to -82, -88) do not expressly provide for any contact whatsoever with the Tax Commission in dissolution proceedings and do not suggest that such a petition and bond could be filed with the Respondent; because the published regulations of the State Tax Commission appear on their face to be a complete statement of the regulations of the Respondent with respect to termination of Franchise Tax Liability of a corporation in process of dissolution (Corporate Franchise Tax Regulation No. 1, paragraphs 5, 6, 7 and 9) and such regulations do not suggest or imply that a taxpayer may have anything to do with hastening the process of receiving a tax clearance; and because the letter of the Respondent of December 27, 1965, had the effect of reinforcing the misconception already created by the regulations that the taxpayer was completely subject to the course of action of the various agents of the Respondent in preparing the tax clearance and could do nothing to hasten their procedures. The letter stated: "If dissolution proceedings are not completed prior to

January 31, 1966, it will be necessary for you to file a corporate franchise tax return for the period then ended and pay the tax shown to be due thereon before we can issue a clearance." Respondent's own communications were in effect affirmatively misleading and the Plaintiff's reliance on them effectively prevented it from obtaining the pre-year-end tax clearance which it would otherwise have obtained. Furthermore, it was entirely within the Respondent's power to give tax clearance at the time, which it failed to do, and it failed to advise Plaintiff that clearance would not be forthcoming before the end of the year. In view of these representations and omissions by the Respondent it must be estopped to collect the 1966 Franchise Tax which it claims herein, to avoid reaching "unjust ends."

CONCLUSION

We ask this court to rule on grounds of due process, equal protection, delegation of authority, statutory construction and estoppel that the corporate franchise tax for the year 1966 should not be imposed upon the Plaintiff-Appellant. No other disposition would give the Plaintiff the relief to which it is entitled by its constitutional guarantees and by the equity doctrine of estoppel, and such disposition can also be better harmonized with the Utah Franchise Tax Act than the interpretation applied by the Respondent in its decision below. The statutory construction which we suggest in Point II of our argument is not new but is in effect an extension and refinement of the interpretation adopted by the

Respondent in its policy of issuing speedy tax clearance upon filing bond. The construction we propose as to collection of unpaid state taxes before a corporation is dissolved, avoids constitutional infirmities and operates equally and fairly on all taxpayers.

For the foregoing reasons, the decision of the Tax Commission should be reversed and this Court should determine that Plaintiff's franchise tax liability terminates as of December 22, 1965.

Respectfully submitted,

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