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Cases Cited.

STATUTES.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1938.

No.

MARK GRAVES, JOHN J. MERRILL and JOHN P. HENNESSY, as Commissioners constituting the State Tax Commission of the State of New York,

Petitioners,

v.

THE PEOPLE OF THE STATE OF NEW YORK, upon the relation of JAMES B. O'KEEFE.

PETITION FOR WRIT OF CERTIORARI TO THE SUPREME COURT OF THE STATE OF NEW YORK.

To the Honorable the Chief Justice and Associate Justices of the Supreme Court of the United States:

Your Petitioner, John J. Bennett, Jr., Attorney General of the State of New York, on behalf of Mark Graves, John J. Merrill and John P. Hennessy, as Commissioners constituting the State Tax Commission of the State of New York, respectfully prays for a writ of certiorari herein to review a certain final order and judgment of the Supreme Court of the State

of New York, Albany County, entered and filed Aug. 19, 1938, affirming the final order of the Court of Appeals of the State of New York, being the highest court of said State, in the above entitled proceeding, the opinion and decision of said Court of Appeals having been rendered and filed July 7, 1938, affirming an order of the Appellate Division of the Supreme Court of the State of New York in the Third Judicial Department in said State, entered December 29, 1937, which annulled, on certiorari, a determination of the State Tax Commission denying an application by the taxpayer therein (the above named James B. O'Keefe) for a revision and resettlement or computation of his personal state income tax for the year 1934 and for a refund of the tax paid for that year.

Opinions Below.

The decision of the Court of Appeals of the State of New York is reported in the New York Advance Sheets Number 1962, for August 6, 1938, as page 2210, Volume 278 of New York Reports, with the notation: "Order affirmed with costs on the authority of *People ex rel. Rogers v. Graves,* (299 U. S. 401). No opinion." The order of the Appellate Division in the Third Judicial Department of the State of New York (R. ff. 191-214), was reported in 253 App. Div. (N. Y.) 91, with the memorandum: "Relator is the regularly retained attorney for the Federal Home Owners' Loan Corporation. His salary is not subject to tax under *People ex rel. Rogers v. Graves* (299 U. S. 401)."

A dissenting opinion was filed in the Appellate Division of the Supreme Court by Justice Crapser (R. f. 210), on the ground that:

> "The business of the Home Owners' Loan Corporation is a business that has always been carried on by private corporations or individuals."

The determination of the State Tax Commission and the opinion of Graves, Commissioner, are also set forth in the record. (R. ff. 22-48.)

Jurisdiction.

The order of the Supreme Court below was entered on August 19, 1938 (R.). The jurisdiction of this Court is invoked under Section 237 (b) of the Judicial Code, as amended by the Act of February 13, 1925, Chapter 229; 43 Stat. 936; 28 U. S. C. A. Sec. 344:

> "Sec. 237 (b). It shall be competent for the Supreme Court, by certiorari, to require that there be certified to it for review and determination, with the same power and authority and with like effect as if brought up by writ of error, any cause wherein a final judgment or decree has been rendered or passed by the highest court of a State in which a decision could be had where is drawn in question the validity of a treaty or statute of the United States; or where is drawn in question the validity of a statute of any State on the ground of its being repugnant to the Constitution, treaties, or laws of the United States; or where any title, right, privilege, or immunity is specially set up or claimed by either party under the Constitution, or any treaty or statute of, or commission held or authority exer-

cised under, the United States; and the power to review under this paragraph may be exercised as well where the Federal claim is sustained as where it is denied. Nothing in this paragraph shall be construed to limit or detract from the right to review on a writ of error in a case where such a right is conferred by the preceding paragraph; nor shall the fact that a review on a writ of error might be obtained under the preceding paragraph be an obstacle to granting a review on certiorari under this paragraph."

Question Presented.

Whether the compensation received by the taxpayer for services performed during the year 1934 as an employee of the Home Owners' Loan Corporation is exempt from taxation by the State of New York on the ground that such a tax would be an unconstitutional burden on the Federal Government.

Statutes Involved.

The pertinent statutory provisions involved will be found in the appendix *infra,* pages 34 to 52. They are Section 359 of the Tax Law of New York State; and Chapter 64, 48 U. S. Stat. at Large, 128, being the Home Owners' Loan Act of 1933.

Statement.

The taxpayer, a resident of New York during the year 1934, was employed as an examining attorney (R. f. 64) by said Home Owners' Loan Corporation

and started work on January 12th, 1934, at a compensation of $80.00 per month (R. f. 66). His duties as examining attorney included the reading of titles, *i. e.*, the examination of certificates sent in by Title Companies before sending the file to the closing attorney (R. ff. 68, 69), to see if there were any defects in title, to examine the certificates of title after the return of the file by the closing attorney prior to the loan closing, and various similar legal services (R. ff. 31, 32, 126, 127).

He duly made a personal income tax return pursuant to the Tax Law of the State of New York and paid an income tax of $57.28 for the year 1934. Thereafter, on August 16, 1935 (Stip. R. ff. 170, 171) he made application, pursuant to Section 374 of the Tax Law, for a refund of the foregoing tax upon the grounds that his salary from the Home Owners' Loan Corporation in the sum of $2246.66 (R. ff. 29, 71, 83; Stip. R. f. 169) was earned by him as an employee of the Federal Government engaged in the performance of a governmental function and therefore was exempt from New York State Income Tax. He was paid semi-monthly by check of the Home Owners' Loan Corporation, signed by the Treasurer of the Home Owners' Loan Corporation, drawn on the Treasury of the United States (R. ff. 77, 105).

Under the statutory authority of Section 4, Subdivision (j) of the Home Owners' Loan Act of 1933 (June 13, 1933, Chap. 64, 48 U. S. Stat. at Large, 128; U. S. Code, Tit. 12, Sections 1461-1468), Mr. O'Keefe

received a verbal appointment as attorney (R. f. 73) from the Home Loan Bank Board through its Metropolitan District Council (R. f. 72), without competitive civil service examination (R. ff. 74, 128). By this statute the Corporation had power to employ such officers and employees without regard to provisions of law applicable to the employment or compensation of officers, employees, attorneys or agents of the United States. U. S. Code, Tit. 12, sec. 1463 (j).

The law creating the Home Owners' Loan Corporation as amended is entitled "Home Owners' Loan Act of 1933". It provides in Section 4-(a) thereof that the Federal Home Loan Bank Board (created by Congress under the Federal Home Loan Bank Act) was authorized to create a corporation to be known as the Home Owners' Loan Corporation (R. f. 34) and when created became a distinct entity (R. f. 4).

The Home Owners' Loan Corporation was empowered to issue bonds in an aggregate amount not to exceed $4,750,000,000 and stocks to be sold to the public by the corporation to obtain funds for carrying out the purposes of the Section (R. ff. 37, 41). The bonds were to be fully and unconditionally guaranteed both as to principal and interest by the United States (R. f. 37).

Among the other purposes for which the corporation was organized were the following:

(a) For a period of three years after the date of the enactment of the Act

(1) To acquire in exchange for bonds issued by it, home mortgages and other obliga-

tions and liens secured by real estate recorded or filed or executed prior to the date of the enactment of the law and

(2) In connection with any such exchange to make advances in cash to pay the taxes and assessments on the real estate, to provide for necessary maintenance and make necessary repairs, to meet the incidental expenses of the transaction and

(b) For a period of three years from the date of the enactment of the Act to make loans in cash in cases where property is not otherwise encumbered, but in no case should such loan exceed fifty per centum of the value of the property securing the same; such loan to be secured by duly recorded home mortgage bearing interest and

(c) In a case where the holder of a home mortgage or other obligation or lien eligible for exchange for the corporation bonds does not accept such bonds in exchange, to make cash advances to such home owner in an amount not to exceed forty per centum of the value of the property (R. ff. 38-40).

The operations of the Home Owners' Loan Corporation are now carried out in each of the forty-eight states by separate state organizations (R. f. 94). Over the state offices there is a Regional Office; each Regional Office supervising state offices of several states. The Regional Office has nothing to do with the approval or disapproval of loans. The state office is a complete functioning office (R. f. 99).

The Corporation refunds, refinances and loans monies on mortgages at interest rates of five (5%) per centum and six (6%) per centum per annum (R. ff. 107, 134-135) on properties upon which are built homes for

not more than four families and having a value of not more than Twenty-five Thousand ($25,000) Dollars (R. ff. 107-108). The rate of interest is so fixed that the difference between the rate charged and the rate paid on account of the bonds is to pay for the operating costs of the corporation (R. f. 132). Congress has the power to reduce the rate of interest if the Corporation shows profit (R. f. 135). It makes advances to home owners for repairs under the supervision of a Reconditioning Division of the Home Owners' Loan Corporation (R. ff. 92, 111, 112-113, 143-144) and for additions to houses or for new heating systems upon those premises on which the Home Owners' Loan Corporation has a mortgage or is about to refund an existing mortgage (R. ff. 113-115). In return for the advances, the Home Owners' Loan Corporation takes back a mortgage or other obligation from the owner (R. ff. 114-115). Loans are made up to eighty (80%) per centum of the Corporation's appraised value of the property, the maximum loan being Fourteen Thousand ($14,000) Dollars (R. f. 122). The corporation also pays real estate taxes on property actually owned by itself (R. f. 101).

The Home Owners' Loan Corporation work is carried on by full time salaried employees and also by fee personnel who are paid a certain amount per case. Outside experts are retained to appraise property and to appraise the cost of reconditioning or repairing. Title closings are handled by outside attorneys on a fee basis. Title searches are made for the Corporation by title or abstract companies or by outside fee attorneys (R. ff. 124-125).

Specifications of Errors to be Urged.

The Court of Appeals erred:

1. In holding that the taxpayer was an official or employee of the United States.

2. In failing to hold that the functions of the Home Owners' Loan Corporation were not essential to the preservation of the Government of the United States and that, consequently, the salary received by the taxpayer was not immune from taxation by the State of New York.

3. In failing to hold (within the rulings of this Court in *Helvering v. Gerhardt,* 82 Law Ed. Adv. Ops. 962) that the burden of the tax in question on the Government of the United States was speculative and uncertain and that, consequently, the salary received by the taxpayer was not immune from taxation by the State of New York.

4. In failing to hold (within the rulings of this Court in *Helvering v. Gerhardt)* that the tax in question would be substantially or entirely absorbed by a private person and that, consequently, the salary received by the taxpayer was not immune from taxation by the State of New York.

5. In holding that the functions exercised by the Home Owners' Loan Corporation during the year in question were governmental functions of the United States.

6. In failing to hold that the Home Owners' Loan Corporation was performing proprietary functions.

7. In failing to hold that the law creating the Home Owners' Loan Corporation is unconstitutional.

8. In holding, if the decision can be so construed, that the compensation received by the taxpayer for services rendered during the year 1934 as an employee of the Home Owners' Loan Corporation was exempt by statute from the income tax of the State of New York.

9. In holding, if the decision can be so construed, that said compensation received by the taxpayer as aforesaid, was constitutionally immune from the income tax of the State of New York.

10. In affirming the decision of the Appellate Division of the Supreme Court in the Third Judicial Department of the State of New York.

Reasons for Granting the Writ.

A decision by this Court is necessary to determine whether or not salaries, wages, and other compensation received by employees of the Home Owners' Loan Corporation and other similar corporations of the Federal Government are taxable under the New York State Income Tax Law. This question of constitutional law is one of first and pressing importance in many States.

The questions which require decision are: (1) whether the Courts below should not have found the employee taxable by the State of New York under the

recent decision of this Court in *Helvering v. Gerhardt,* 82 Law Ed. Adv. Ops. 962; (2) whether the Court below was in error in following the decision of this Court in *New York ex rel. Rogers v. Graves,* rather than the more recent principles of intergovernmental immunity enunciated in *Helvering v. Gerhardt, supra,* within the meaning of that case; (3) whether or not the burden on the Federal Government of a state tax on the salary of an employee of the Home Owners' Loan Corporation would not be so speculative and uncertain, and so substantially absorbed by a private person, as not to be prohibited by the limitations on the doctrine of implied immunity; (4) whether the activities of the Home Owners' Loan Corporation are essential to the preservation of the Federal Government; (5) whether or not the activities of the Home Owners' Loan Corporation were proprietary, rather than governmental; (6) whether the taxpayer herein who claims immunity from the common burdens of taxation which rest equally upon all, brings himself clearly within the statutory exemptions and the language relied upon therein as creating such exemptions; and (7) whether the salary, wages or compensation of an employee of certain Federal instrumentalities is immune from a state income tax when the Congress has clearly undertaken the task of expressly declaring exemptions from state taxation and in so doing has omitted income taxation from its enumerated exemptions.[1]

[1]The State of New York appeared as amicus curiae in **Helvering v. Gerhardt,** 82 Law Ed. Adv. Ops. 962 and submitted certain arguments concededly inconsistent with certain of those herein expressed. While still adhering to the arguments made in that case, at least during the pendency of a petition for a re-hearing therein, the state proceeds here upon the provisional assumption that the Gerhardt opinion expresses the law as it now stands on those points and that it has disposed of the state's original contentions in that case. Other arguments for review herein are, of course, not dependent on the Gerhardt decision.

WHEREFORE, your petitioners pray that a writ of certiorari may be issued out of and under the seal of this court, directed to the Supreme Court of the State of New York to review the determination of the Court of Appeals, the court of last resort of the State of New York, as provided by law, and that your petitioners have such other and further relief as may be deemed appropriate. A certified copy of the record in the courts below is submitted herewith, together with the remittitur of the Court of Appeals, in support hereof.

Dated, October 24th, 1938.

Respectfully submitted,

MARK GRAVES, JOHN J. MERRILL and JOHN P. HENNESSY, constituting the State Tax Commission of the State of New York,
Petitioners,

By—

JOHN J. BENNETT, JR.,
Attorney General, State of New York,

HENRY EPSTEIN,
Solicitor General, State of New York,
Solicitor for Petitioners.

ARGUMENT IN SUPPORT OF PETITION.

I.

Under the Rule of Helvering v. Gerhardt, the Respondent Is Clearly Taxable by the State of New York.

The Courts below rested their decision solely upon *New York ex rel. Rogers v. Graves,* 299 U. S. 401.

We submit, however, if *Helvering v. Gerhardt,* 82 Law. Ed. Adv. Ops. 962, is to stand unreversed, it enunciated entirely new rules in these cases of intergovernmental immunity as applied to employees. It eliminates the old test of whether or not the activity in question was governmental or proprietary. That test was determinative of the Courts' decision in the *Rogers* case. The unanimous opinion of the Court in that case is devoted solely to the inquiry whether the functions of the Panama Rail Road Company were governmental or proprietary. Thus we find (299 U. S. 401, 404):

> "In order to reach a correct determination of the question whether the railroad company is exercising functions of a governmental character, the railroad and ships are to be considered not as things apart, but in their relation to the Panama Canal; * * *."

The Court, in order to answer this question, felt called upon to determine the answer to the further question:

> "* * * whether the canal is such an instrumentality of the federal government as to be immune from state taxation; and, if so, are the operations of the railroad company so connected with the canal as to confer upon the company a like immunity?"

And again (page 407-408):

> "We attach no importance to the fact that the railroad company has utilized both its ships and railroad to carry private freight and passengers. The record shows that this is done to a limited extent compared with the government business; and that it is only incidental to the governmental operations. The primary purpose of the enterprise being legitimately governmental, its incidental use for private purposes affords no ground for objection.[1] United States v. Chandler-Dunbar Water Power Co., 229 U. S. 53, 73; Ashwander v. Tennessee Valley Authority, 297 U. S. 288, 333. * * *"

It is quite clear, therefore, that this case was decided by the Courts below solely on the basis of a rule of constitutional law, as formulated by this Court *prior* to the *Gerhardt* case, that the salary of a state or federal employee was immune on the sole showing that he was engaged in the performance of a governmental function.

The necessity of such an inquiry in the case of public employees appears to have been abandoned in the *Gerhardt* opinion. The decisions of the Court below should therefore be reversed.

The fundamental change in the rule of immunity evidenced by the *Gerhardt* decision, becomes clear upon

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[1]The Court in summing up the reason for its opinion (p. 408) said:
"The rule is well established; and the reasons upon which it is based and the authorities sustaining it have been so recently reviewed by this court, Indian Motorcycle Co. v. United States, 283 U. S. 570, that further discussion is unnecessary."
When we turn to page 575 of the **Indian Motorcycle** case, we find the distinction between governmental and proprietary functions with respect to the taxation of both federal or state employees is emphasized in the statement of the rule:
"It is an established principle of our constitutional system of dual government that the instrumentalities, means and operations whereby the United States exercises its **governmental** powers are exempt from taxation by the states, and that the instrumentalities, means and operations whereby the states exert the **governmental** powers belonging to them are equally exempt from taxation by the United States." (Boldface ours.)

examination of the arguments and opinion in that case. The Attorney General of the United States admitted that under the then existing rule the employees of the Port Authority must be held immune if they were engaged in the performance of a governmental function. (*Helvering v. Gerhardt* and related cases, October Term, 1937, Nos. 779-781; Brief for Petitioner, pp. 30, 31.)[1]

On the other hand, the respondent's brief and argument in the *Gerhardt* case were confined to the contention that the activities of the Port Authority were in fact governmental. Both sides, therefore, rested their case on the determination of that question.

The Court, however, found it unnecessary to decide it. Instead, a new rule was announced. The new rule questioned the entire basis of employee implied immunity, as that doctrine had theretofore been formulated. In its place, the Court stated two new guiding principles. First, that implied immunity would not be recognized where the function was not essential to the preservation of the government. The second new principle would, we submit, appear to end all employee immunity—for it declares that the burden of a tax on employees is speculative and uncertain, and that even though a function might be important enough to demand the immunity for the government itself, a tax on its employees is "substantially or entirely absorbed by private persons."[2]

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[1]See also Transcript of Argument of Assistant Solicitor General, pages 8, 32.

[2]It may still be argued upon the proper showing of facts that in a given case the burden is not speculative and uncertain "or substantially absorbed by a private person". But in this case the record corresponds in all respects with that in the Gerhardt case on this point.

The applicability of the first of these rules will be developed in our subsequent Reasons. We need only state here, as a comment obviously so well founded that it should hardly require extended development—that, if there is any function which is not "essential to the preservation" of the Federal Government, it is the banking, mortgage and real estate business of the Home Owners' Loan Corporation.

Here we are primarily concerned with the second principle, that the burden of a tax on employees is so speculative and uncertain and has only a remote, if any, influence upon the exercise of functions of government, that it does not give rise to immunity. Such a principle would seem to be quite clear in its consequences. It simply abolishes the former rule of employee immunity.[1]

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[1]This would appear to be the view of the Attorney General of the United States, for in a Study made by the Department of Justice at the direction of the Attorney General himself, entitled "Taxation of Government Bondholders and Employees", and forwarded to the Treasury Department on June 24, 1938, the Attorney General says (pages 67 to 71):

"Finally, the doctrine of tax immunity of state employees appears largely if not entirely to have been swept away on May 23, 1938, by the decision in **Helvering v. Gerhardt.** * * * The opinion, by Mr. Justice Stone, proceeded on a broad front. * * * Earlier cases were distinguished. * * *

"The **Gerhardt** case seems probably to settle that the state or municipal employee is subject to federal taxation. The entire discussion in the opinion, apart from the introductory statement of facts, contains only one reference to the fact that the taxpayers were employed not by the state but by The Port of New York Authority. * * * The affirmative reasoning of the Court is directed entirely to state employees generally. It seems, therefore, a reasonably safe prediction that all salaries paid to employees of state and local governments, * * * may be subjected to the federal income tax. * * *.

"It is probable that the care with which the opinion distinguishes the officer from the employee is due to a desire to escape the necessity of reexamining **Collector v. Day,** rather than to approval of its result. * * *

"Since the Court seemed studiously to refrain from approving **Collector v. Day,** and since every reason which it advanced to sustain taxation of the state employee is equally applicable to the state officer, it is at the least a reasonable conclusion that the Court viewed the federal taxing power as reaching to officers as well as to employees of the states.

"Finally, the analysis of the present authority of **Pollock v. Farmers' Loan & Trust Co.** is fully applicable to **Collector v. Day.** Every reason which the Court has articulated for declaring invalid a nondiscriminatory tax on a private person who deals with the government seems to have been abandoned or contradicted by subsequent decisions; * * *

"It seems, therefore, to be more probable than not that the federal income tax may be applied to the salary received from a state or municipal government, whether the taxpayer serve as an employee or as an officer."

In the case of *Indian Motorcycle Co. v. United States,* 283 U. S. 570, 580 (1930) Justice Stone in a dissenting opinion, with Justice Brandeis concurring, said:

> "The implied immunity of one government, either national or state, from taxation by the other should not be enlarged. Immunity of the one necessarily involves curtailment of the other's sovereign power to tax. The practical effect of enlargement is commonly to relieve individuals from a tax, at the expense of the government imposing it, without substantial benefit to the government for whose theoretical advantage the immunity was invoked.
>
> "'* * * it is not clear how a recovery by a taxpayer would benefit directly the government supposed to be burdened; and the assumption of individual benefit in the case of a tax of this type necessarily rests upon speculation rather than reality.'"

If the burden of a tax on an employee's salary is speculative and uncertain, it is equally so whether the taxpayer be an employee of the state or the federal government. The quality of the relationship is precisely the same in either case. In both cases human beings serve as the instruments of government. In both cases there is the same contract to devote human brains and human hands to the performance of a service for an agreed salary. In both cases the employees receive the benefits and protection extended by the other government which seeks to impose the tax.[1] In both cases the salary may be considered to have been diminished by the tax.

[1]See Helvering v. Gerhardt, U. S. ; 82 Law. Ed. Adv. Ops. 962.

But how can it conceivably be contended that in the case of a state employee the resultant burden on the state is "speculative and uncertain," whereas in the case of the federal employee the burden would be "definite and certain?" How can it be contended, with any semblance of plausibility, that the federal tax is "substantially or entirely absorbed by private persons," but that a similar state tax would have to be absorbed by the Federal Government itself? And, when in all cases the question is simply one of a tax on a salary, how can it be contended that a "speculative" effect of the burden differs with the function?

Why is a tax on the salary of a President, a Judge, or a Governor any less speculative than a tax on the salary of a policeman, a port employee, or a federal clerk?

These are questions which we submit should commend this Court's review of the decision below. They demonstrate that the rule of the *Rogers* case, relied on by the Courts below, should not have been accepted as persuasive. On the contrary, the applicability of the principles now established by the *Gerhardt* case, would have held the salary of the respondent taxable by the State of New York.

The respondent will, no doubt, reply that all of the Court's reasoning in the *Gerhardt* case should be jettisoned when the state attempts to tax the salary of a federal employee. On the contrary, we question whether the dicta in the Court's opinion in the

Gerhardt case, with reference to federal employees, justifies any such distinction. Prior decisions of the Court would seem to negative any intention to abandon the reciprocal character of the rule of immunity. And in any event such a claim raises a serious question of constitutional law which this Court ought now to decide.

In a long series of cases the immunity rule has been expressly held to be reciprocal as between state and federal governments.

Collector v. Day, 11 Wall. 113, 127 (1817);
Pollock v. Farmers' Loan & Trust Co., 157 U. S. 429, 584 (1895);
Ambrosini v. United States, 187 U. S. 1, 7 (1902);
South Carolina v. United States, 199 U. S. 437, 451, 452 (1905);
Metcalf & Eddy v. Mitchell, 269 U. S. 514, 521 (1926);
Burnet v. Coronado Oil & Gas Co., 285 U. S. 393, 400 (1932);
Trinityfarm Construction Co. v. Grosjean, 291 U. S. 466, 471 (1934).

As the Supreme Court has recently expressed it in *Indian Motorcycle Co. v. United States,* 283 U. S. 570, 579 (1930):

> "Under the constitutional principle the exertion of such a function by a state or a state agency has the same immunity from Federal taxation that like exertions by the United States or its agencies have from state taxation."

In all of the foregoing cases, and particularly at the pages noted, the Court has emphasized the constitutional necessity that the rule of immunity be applied reciprocally. The logic of that conclusion would seem inescapable if the dual sovereignty of state and federal governments is to be preserved. If taxation is incompatible with sovereignty, no distinction can be drawn between the two divisions of government in America, the one recognized and preserved, the other created by the Constitution.

It is certainly no answer to say that the states are represented in Congress. We are dealing with a question of the reserved sovereignty of the states. Representation in Congress has nothing whatsoever to do with such a question. It seems elementary to have to state that the reserved rights of the states can only be overthrown by constitutional amendment, and not by the action of their representatives in Congress.

If representation in Congress may ever be interposed as an answer to the complaint based upon the sovereignty of the states, it should be obvious that the last remnants of independence will then have been stripped from the states. Under the Constitution their sovereignty *may* be impaired with the acquiescence of three-fourths of the states—but *not* by a congressional majority. The question is one of constitutional right and not one of dubious political protection.

We also petition for certiorari in order that the state may place before this Court its contention that

the mere power of Congress to create such instrumentalities does not of itself give rise to a federal immunity.

The state also seeks an opportunity to present to the Court its contention that even if the employees of the Home Owners' Loan Corporation would enjoy an implied immunity, that such an immunity has been waived by Congress' failure to include the employees of the Corporation among the subjects expressly declared exempt in Section 1463 (c) of the Act.

In the case of *Baltimore National Bank v. State Tax Commission* of Maryland, 297 U. S. 209, the Court decided against the Petitioner's contention that the following section in the Reconstruction Finance Corporation Act,

> "The corporation, including its franchise, its capital, reserves, and surplus, and its income shall be exempt from all taxation * * * except that any real property of the Corporation shall be subject to * * * taxation to the same extent according to its value as other real property is taxed. 47 Stat. at L. 5, 9, 10; chap. 8, U. S. C. A. title 15, section 610,"

provided for an exemption from state taxation of shares in a national bank wholly subscribed and owned by the Reconstruction Finance Corporation. The Petitioner insisted that the tax in controversy was impliedly forbidden by that section. The Court, at page 214, stated:

> "The contention is plausible, yet it will not prevail against analysis. For the tax now in controversy whatever its indirect effect, is not laid

> directly upon the capital, reserves, or surplus of the corporation claiming the immunity or accorded the exemption."

The Court therefore refused to agree with the Petioner's contention that this Congressional declaration of immunity covered taxation of national banks' shares.

The Home Owners' Loan Corporation Act, section 1463 (c), has a like provision, as follows:

> "The bonds issued by the Corporation under this subsection shall be exempt, both as to principal and interest, from all taxation (except surtaxes, estate, inheritance, and gift taxes) now or hereafter imposed by the United States or any District, Territory, dependency, or possession thereof, or by any State, county, municipality, or local taxing authority. *The Corporation, including its franchise, its capital, reserves and surplus, and its loans and income, shall likewise be exempt from such taxation; except that any real property of the Corporation shall be subject to taxation to the same extent, according to its value, as other real property is taxed.*" (Italics ours.)

It is this Petitioner's contention, therefore, that Congress intended to declare immune from state taxation only those subject matters stated in the Home Owners' Loan Act as above set forth. Congress has clearly undertaken the task of expressly declaring what subject matters are exempt from state taxation and in so doing has omitted income taxation of the Corporation's employees from its enumerated exemptions. The authority of the *Baltimore National Bank case* is binding upon the employee herein in answer to

any proposition urged by him with respect to the possible Congressional implied immunity under the Home Owners' Loan Act.

If such considerations of the entrance of government into new fields of activities never dreamed of when the Constitution was adopted, were found by this Court to be a persuasive argument against the states in *Helvering v. Gerhardt,* they should be given similar weight when the states seek to impose a tax on an employee of the Federal Government whose functions in the field of private banking and real estate have always been taxable by the states. Indeed, there is a graver reason for protection of the states than of the Federal Government. The immunity of a state activity can, at most, be deemed to interfere with the power of the Federal Government to raise revenue. But with the vast powers and resources of the central government, the power to tax the states is the most direct road to federal control and to the ultimate centralization of our government.[1]

The doctrine of tax immunity is a necessary development of our dual system of state and federal government. It must be given a practical construction which permits both governments to function with the minimum of interference each with the other. Limitations

[1]In this connection the extent to which the Attorney General of the United States hopes to carry the **Gerhardt** decision, is rather alarmingly indicated by his recent statement in an official document, that

> "For on May 23, 1938, the Court in **Helvering v. Gerhardt** seems to have rejected the reciprocal test of tax immunity and returned to Chief Justice Marshall's understanding that the principle of immunity protected the federal government against taxation by the states but **did not necessarily shield the states against the exercise of the delegated, and supreme, taxing power of the central government.**" (Boldface ours.) "Taxation of Government Bondholders and Employees," **supra, pp. 9-10.**

cannot be so varied or extended as seriously to impair the taxing power of the government imposing the tax or the appropriate exercise of the functions of government affected by it.

The state and national governments must co-exist. Each must be supported by taxation of those who are citizens of both. The fact that the economic burden of taxes may be passed on to the other government and thus increase to some extent, here wholly conjectural, the expense of its operation, infringes no constitutional immunity. Such burdens are but normal incidents of the organization within the same territory of two governments, each possessed of the taxing power.

II.

The Activities of the Home Owners' Loan Corporation are not Essential to the Preservation of the Federal Government.

As appears from the foregoing statement *(supra*, page 15), the Home Owners' Loan Corporation was created by the Federal Home Loan Bank Board, as a distinct and independent corporate entity. It issued its own stock and sold bonds to the public. Its operations were conducted by its own board of directors. By statute, the provisions of law applicable to officers and employees of the United States had no application to the employment of the taxpayer. The Home Owners' Loan Corporation was created as a temporary agency to aid distressed owners during a period of

economic depression. However praiseworthy those motives, it may be questioned whether the Federal Government has the constitutional power to undertake such an enterprise. In any event, it is obvious, particularly in view of the absence of any power in the Federal Government to make private loans on mortgage security, to undertake the repair of private houses or to go into the real estate business on a huge scale, that such functions are not, within the test prescribed in the *Gerhardt* case, essential to the preservation of the Federal Government. The mere fact that its activities are performed for what the Federal Government conceives to be a public benefit does not establish the immunity of the corporation's employees. See *People ex rel. Rogers v. Graves,* 299 U. S. 401, citing therein *Indian Motorcycle Co. v. United States,* 283 U. S. 570, 575, *et seq.* and the authorities therein referred to.

The entire reasoning of this Court in the *South Carolina* and the *Powers* cases[1] makes it clear that neither the state nor the Federal Government may engage in a traditionally private business, such as the real estate and mortgage business here involved, and by so doing withdraw that business from the taxing power of the other government. Clearly, the business in which the Home Owners' Loan Corporation is engaged in the State of New York was previously a source of large tax revenues to the State of New York. If the Federal Government is not free to tax proprietary activities of the states, but can also deprive the state of such sources of revenue, and if it can come

[1]South Carolina v. United States, 199 U. S. 437; Helvering v. Powers, 293 U. S. 214.

into a state, as it has done throughout the Tennessee Valley, and erect huge power plants, distributing systems, and engage in the wholesale and retail distribution and sale of electric power and other businesses formerly carried on by private utilities, the states can rapidly be reduced to pauperized geographical divisions of a central government and be dependent for their continued existence upon its charity or bounty.

As was pointed out by the two dissenting Justices in the Appellate Division below:

> "The business of the Home Owners' Loan Corporation is a business that has always been carried on by private corporations or individuals.
>
> "The tax has been imposed on the income of the relator who is neither an officer nor an employee of the United States Government, and whose only relation to it is that he has contracted with the Home Owners' Loan Corporation to furnish his services to them.
>
> "It cannot be said that the tax imposed upon the relator is imposed upon an agency of government from any technical sense, and the tax itself cannot be deemed to be an interference with government or an impairment of the efficiency of its agency in any substantial way. *(Fidelity & Deposit Co. v. Pennsylvania,* 240 U. S. 319, *Railroad Co. v. Peniston,* 18 Wall. 5; *Gromer v. Standard Dredging Co.,* 224 U. S. 362; *Baltimore Ship Building Co. v. Baltimore,* 195 *id.* 375.)" *People ex rel. O'Keefe v. Graves, supra,* p. 95.

That the tax in the instant case is not a tax on the corporation—the instrumentality itself—is evident. It does not cast a direct burden on the corporation's operations within the requirements of the *Gerhardt*

case. The tax, if it in fact affects the operations of the corporation, could do so only remotely and would not constitute an interference with a federal instrumentality or be an encroachment upon the sovereignty and supremacy of the Federal Government.

III.

The Activities of the Home Owners' Loan Corporation are Proprietary.

The Home Owners' Loan Corporation is engaged in no activity which can be declared to be other than proprietary. An analysis of its powers and purposes forces one to the conclusion that the Corporation performs no governmental function.

All of the capital stock of the Corporation is subscribed for by the Secretary of the Treasury on behalf of the United States, U. S. C. A. Tit. 12, Sec. 1463 (b). Surplus or accumulated funds are to be paid into the Treasury of the United States. Tit. 12, section 1463 (k). The purpose for which the Corporation was created was to provide emergency relief with respect to mortgage indebtedness upon homes, Tit. 12, section 1463 (g); to refinance mortgaged properties, Tit. 12, section 1463 (f); and to acquire in exchange for bonds issued by it, home mortgages and other obligations or liens secured by real estate and to make advances in cash to pay taxes and assessments, Tit. 12, section 1463 (d).

These purposes and activities of the Home Owners' Loan Corporation seem to the Petitioner to be clearly proprietary in character. *Helvering v. Powers*, 293 U. S. 214. In the conduct of its business it may enter into contracts with individuals, firms, or corporation in a like manner as any private lending institution. All of the above enumerated characteristics are characteristics of any ordinary mortgage loan corporation.

The Petitioner urges that this case demands the application of the principle announced by this Court that the doctrine of intergovernmental tax immunity is not to be applied in a manner so as to cripple the taxing power of the other sovereignty. *Willcuts v. Bunn,* 282 U. S. 216, 225; *James v. Dravo Contracting Co.,* 302 U. S. 134. The Court should not deprive the State of New York of a source of revenue because the Federal Government has engaged in activities which are proprietary and which would produce revenues had the activities been carried on by private institutions.

IV.

Respondent was neither an Officer nor an Employee of the United States, nor did he receive his Salary from the United States.

The respondent cannot establish exemption under Section 359, Paragraph 2-f of Article 16 of the Tax Law of the State of New York. That section excludes from gross income:

> "Salaries, wages and other compensation received from the United States of officials or employees thereof, including persons in the military or naval forces of the United States."

The respondent is not an employee of the United States. The Home Owners' Loan Corporation is merely a corporate creation of the Federal Home Loan Bank Board. The taxpayer was appointed by an officer of that corporation and became its employee. The corporation was an entity distinct from the United States and from any of its departments.

In this connection it is significant that both the Court of Appeals and the Appellate Division rested their decions below, not upon the foregoing statute, but upon the arguments for constitutional immunity as they were formerly set forth by this Court in *People ex rel. Rogers v. Graves,* 299 U. S. 401. The opinion of this Court in that case nowhere makes any claim for the statutory exemption of Mr. Rogers, General Counsel of the Panama Rail Road Company, as an officer or employee of the United States, although by Point IV of his Brief, the Appellant, Rogers, stated that while he was not a direct employee of the United States Government, it seemed to him that he fell within the exception from state taxation of "salaries, wages and other compensations received from the United States of officials or employees thereof." (Sec. 359-f, New York Tax Law.)

In the case of *Pomeroy v. State Board of Equalization of Montana,* 45 P. (2d) 316 (Mont.); the taxation

of the income of a citizen-resident taxpayer of that State who was an employee of the Reconstruction Finance Corporation, was upheld. Section 7 of Chapter 181, Laws of Montana, 1933—Montana Income Tax Law—declares that:

> "The term 'gross income'— * * * (2) * * * does not include the following items * * * (f) salaries, wages and other compensations received from the United States or officials or employees thereof, including persons in the military or naval forces of the United States."

The Court stated that the word "or" after the words "United States" was a typographical error and should be "of," basing this finding on the fact that the Montana statute was probably copied from the New York Act or the "model" act drafted in 1921 for the National Tax Association.

The Court pointed that the Reconstruction Finance Corporation was similar to the Inland Waterways Corporation, United States Shipping Board Emergency Fleet Corporation, and Federal Intermediate Credit Banks. Citing the authority of *United States v. Walter,* 263 U. S. 15; 44 S. Ct. 10, 11; 68 L. ed. 137, wherein this Court held that the Fleet Corporation, although an instrumentality of the Government exercising governmental functions, was a private corporation "government owned" whose employees are not agents of the government, the Reconstruction Finance Corporation employee was deemed to be in a similar category and not entitled to the exemption under Section 7 of the Montana Income Tax Law.

In the recent case of *Parker v. Mississippi State Tax Commissioner,* 178 Miss. 680; 170 So. 567, the salary

of the Vice-President of a Federal land bank was held not to be exempt from state income tax. In considering the question of tax exemption, the Court said (page 684):

> "* * * the principle should be kept in mind that exemptions from taxation will not be presumed; the burden is on the claimant to establish clearly his right; the statute is strictly construed against the claim. (Citing authorities.)"

The taxpayer applied for a writ of certiorari to this Honorable Court. The certiorari was denied 302 U. S. 742; 82 Law. Ed. Adv. Ops. 105. It is to be noted that the taxpayer's petition set forth Laws of Mississippi, 1934, Chapter 120, Section 7 (6), providing that "gross income" shall not include

> "salaries, wages and other compensations received from the United States Government or officials or employees thereof, including persons in the military or naval forces of the United States."

The petitioner did not rely upon this statute and frankly stated that this provision did not bear on the issues in the case but was incorporated only because it was referred to in the defendant's demurrer in the state Court.

We respectfully submit, therefore, that under the authorities given, the taxpayer is not in receipt of a salary from the United States as an officer or employee so as to come within Section 359, Subdivision 2 (f) of the New York Tax Law.

Conclusion.

We feel that it is desirable, in view of the vital implications of the instant case, that this Honorable Court determine once and for all the taxability of the salaries of employees of the Home Owners' Loan Corporation and similar governmental agencies. Every tax, irrespective of its nature, cannot be said seriously to interfere with the primary purpose for which an instrumentality is created. The Home Owners' Loan Corporation presents only one of a constantly mounting number of new operations which have come to be regarded as having some relationship to government. Although it may be of the greatest social and economic wisdom to create agencies of this type, it must be obvious to the most casual observer that, if the immunity of an employee of the Home Owners' Loan Corporation and similar agencies is upheld, the states will lose substantial revenues.

If the taxation of this employee represents an interference with a federal agency, the interference is certainly too remote to warrant an application of the immunity which the taxpayer attempts to derive from the sovereign nature of the Federal Government.

Above all, we submit that only through the traditional reciprocity as between the states and the Federal Government can the constitutional purpose of "an indestructible union of indestructible states" be fulfilled. We are confident that this Court will extend to the states as well as to the Federal Government, an equal protection of its sovereign rights and immunities.

WHEREFORE, it is respectfully submitted that this petition for a writ of certiorari should be granted.

October 25, 1938.

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