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Conflict of Laws - Comity - Extraterritorial Enforcement of State Tax Claims - Nelson v. Minnesota Income Tax Div.

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CASE NOTES

CONFLICT OF LAWS—Comity—Extraterritorial Enforcement of State Tax Claims. Nelson v. Minnesota Income Tax Div., 429 P. 324 (Wyo. 1967).

The State of Minnesota, by its Attorney General,[1] sued in the district court of Fremont County, Wyoming for collection of a state income tax assessed against the defendant Nelson, while he resided in Minnesota. Nelson was a resident of Wyoming at the time this suit was instituted. Holding that the State of Wyoming should enforce the tax laws of sister states on principles of comity,[2] the judge of the district court granted the plaintiff's motion for summary judgment, and judgment was thereby entered against defendant in the sum of $581.87 plus costs. The judgment included a penalty for failure to file a tax return, in addition to the amount of the assessed tax.[3] The defendant appealed, contending that taxation is a legislative function, and therefore an improper subject for comity to be extended by the courts. In remanding the case with instructions to modify, the Wyoming Supreme Court *held* that Wyoming courts would, on principles of comity, enforce the tax laws of a sister state by entertaining suit for taxes due, but that the penalty provisions of the Minnesota tax law could not be enforced.

Until 1946,[4] there had been almost universal application by the American states of the rule enunciated by Lord Mansfield in 1775[5] that "'no country ever takes notice of the revenue laws of another.'"[6] This decision stemmed from a dicta in an earlier case where Lord Hardwicke had refused to recognize the validity of a Portuguese revenue measure.[7] The Portuguese statute outlawed export of gold from Portugal. A contract was made for shipment of gold from Portugal to England in violation of the statute. In a suit to require

1. MINN. STAT. ANN. § 290.48(1) (1962).
2. "The principle in accordance with which the courts of one state or jurisdiction will give effect to the laws and judicial decisions of another, not as a matter of obligation, but out of deference and respect." H. BLACK, LAW DICTIONARY 334 (4th ed. 1951).
3. MINN. STAT. ANN. § 290.53(3) (1962) provides for assessment of a penalty up to an amount equalling 50% of the face amount of the assessed liability.
4. State *ex rel.* Oklahoma State Tax Comm'n. v. Rodgers, 238 Mo. App 1115, 193 S.W.2d 919 (1946).
5. Holman v. Johnson, 98 Eng. Rep. 1120 (K. B. 1775).
6. *Id.* at 1121.
7. Boucher v. Lawson, 95 Eng. Rep. 53 (K.B. 1734).

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performance of the contract, the contract's validity was upheld, and the statute ignored. From these rudiments developed a well-settled rule of law in England that foreign revenue laws were unenforceable.

The early American courts immediately followed suit and applied the rule of the mother country in analogous cases.[8] Once the rule had become entrenched in this country there began an expansion of its application to diverse fact situations. *Maryland v. Turner*[9] was the first in a line of significant New York cases[10] to establish the rule that tax claims of sister states would not be enforced. In that case, the State of Maryland brought an action in New York for collection of a personal property tax. The New York court held that the claim was penal in nature, and that it was not "bound by any rule of comity to enforce the tax laws of Maryland."[11] Subsequently, in *Colorado v. Harbeck*,[12] the leading New York case, the court disallowed a suit on a transfer tax claim against a former resident's estate. Although the decision was based on a constitutional issue, the court gained wide notice for its dictum that one state will not enforce the revenue laws of another.[13] A substantial line of precedent evolved from these two cases in New York expounding the logic underlying non-enforcement of sister-state tax claims.[14] Thereafter, the rule enjoyed extensive acceptance throughout the state jurisdictions.[15] That extraterritorial tax claims were unenforceable became a universally accepted rule of law.

The issue was first adjudicated by a federal court in

8. Ludlow v. Van Rensselar, 1 Johns. 92 (N.Y. 1806); Henry v. Sargent, 13 N.H. 321 (1843).
9. 75 Misc. 9, 132 N.Y.S. 173 (Sup. Ct. 1911), noted 12 COLUM. L. REV. 60 (1912).
10. City of Philadelphia v. Cohen, 11 N.Y.2d 401, 184 N.E.2d 167, *cert. denied*, 371 U.S. 934 (1962); Wayne County v. American Steel Export Co., 277 App. Div. 585, 101 N.Y.S.2d 522, (1950); *In re* Buckley's Estate, 31 Misc.2d 551, 220 N.Y.S.2d 915 (Sur. Ct. 1961); *In re* Bliss' Estate, 121 Misc. 773, 202 N.Y.S. 185 (Sur. Ct. 1923). *See also* cases cited in note 8 *supra*.
11. Maryland v. Turner, *supra* note 9, at 175.
12. 232 N.Y. 71, 133 N.E. 357 (1921). The statement was a dictum, but the case seems to be the one cited most often for the rule.
13. *Id.* at 85, 133 N.E. at 360.
14. *See* cases cited note 10 *supra*.
15. *Cf.* Annot., 165 A.L.R. 796 (1946). *See generally* Leflar, *Extrastate Enforcement of Penal and Governmental Claims*, 46 HARV. L. REV. 193 (1932); Ruby & Pyle, *Extraterritorial Enforcement of Tax Claims*, 16 HASTINGS L. J. 101 (1964); *Extrastate Collection of Taxes*, 33 VA. L. REV. 179 (1947).

1929.[16] The United States Court of Appeals for the Second Circuit denied enforcement of a tax claim prosecuted in New York by the Treasurer of Grant County, Indiana. Judge Learned Hand, in a concurring opinion,[17] rationalized the rule of non-enforcement on the premise that to enforce another state's tax laws, a forum state would initially have to inquire if such laws were contrary to its public policy. Such determination, it was argued, would require a scrutiny of the taxing state's relations with its citizens, and might result in commission of the forum "to a position which would seriously embarrass its neighbor."[18] The United States Supreme Court affirmed the decision of the Court of Appeals on other grounds, expressly leaving unanswered the question of extra-state enforcement.[19] However, in later cases, dicta of the Court have indicated a favorable attitude toward enforcement of tax liabilities arising in sister states.[20]

An important modification of the rule resulted with the United States Supreme Court's decision in *Milwaukee County v. M. E. White Co.*;[21] the Court held that under the full faith and credit clause of the federal constitution,[22] where a tax claim has been reduced to judgment, a sister state must allow action on the judgment in its courts. The original claim in that case was for income tax and the Court reasoned that since the liability of the taxpayer was quasi-contractual in nature, no policy of the forum state could have sufficient weight to counteract the interests of the taxing state and the policy of the full faith and credit clause of the constitution. However, the Court once again declined to decide "whether one state must enforce the revenue laws of another."[23] There the issue presently rests.

16. Moore v. Mitchell, 30 F.2d 600 (2d Cir. 1929), *aff'd on other grounds*, 281 U.S. 18 (1930), noted 5 IND. L. J. 625, 5 WISC. L. REV. 494.
17. *Id.* at 608.
18. *Id.* at 604.
19. Moore v. Mitchell, 281 U.S. 18 (1930).
20. "With respect to the character of the claim now urged, we are not advised that Missouri would close its courts to a civil action brought by Massachusetts to recover the tax alleged to be due from the trustees." Massachusetts v. Missouri, 308 U.S. 1, 20 (1939). "Still the obligation to pay taxes is not penal. It is a statutory liability, *quasi*-contractual in nature, enforcible, if there is no exclusive statutory remedy, in the civil courts by the common law action of debt or *indebitatus assumpsit*." Milwaukee County v. M. E. White Co., 296 U.S. 268, 271 (1935).
21. 296 U.S. 268 (1935).
22. U.S. CONST. art. IV, § 1.
23. Milwaukee County v. M. E. White Co., *supra* note 21, at 275. It has been argued that since the forum must accord full faith and credit to a *judgment* under the statute of a sister state, the forum must also necessarily

As previously stated, until 1946 the uncontroverted weight of authority was, without exception, that such extra-territorial claims as herein involved were unenforceable. In that year, the Supreme Court of Missouri rendered a decision in the case of *State ex rel. Oklahoma v. Rodgers*[24] holding for the first time that a state court would extend comity to another state in order to enforce a tax claim. The Missouri court reasoned that the doctrine promulgated by Mansfield and Hardwicke had been applied to situations beyond the scope of the probable anticipation of those eminent jurists. The court distinguished those cases on the grounds that they involved no attempt to collect a tax, but commercial considerations, by which forum courts refused to enforce foreign revenue laws as a means of invalidating contracts which were perfectly legal in the forum. The court reasoned that as a result of the failure to recognize this distinction, courts had applied the rule blindly without reference to the wisdom of its results.

Rodgers was heavily relied upon by the Wyoming Supreme Court in the principal case. After reviewing *Rodgers,* Mr. Justice McIntyre paraphrased the philosophy of the Missouri court "that a taxpayer who enjoys the protection of government should bear his share of the expense of maintaining the government, and should not be permitted to escape his obligation by crossing state lines."[25] Said the Wyoming court in *Nelson,* "There is no longer any valid justification for not permitting a suit in one state for a tax lawfully levied by another."[26]

An analysis of *Nelson v. Minnesota Income Tax Division* demonstrates the lack of any sound basis for refusing to extend comity. As the court in the *Rodgers* case pointed out, the earliest English and American cases involved fact situa-

accord full faith and credit to the *statute* of the sister state. *See* 49 HARV. L. REV. 490 (1936). In addition a 1948 revision of the statute which implements the full faith and credit clause may have some impact in dictating greater full faith and credit to *causes of action.* 1 Stat. 722 (1790) was amended by 62 Stat. 947 (1948), 28 U.S.C. § 1738 (1964) to specify that the *public acts* of sister states must be given the same faith and credit in every state as is accorded to judgments of sister states.

24. 238 Mo. App. 1115, 193 S.W.2d 919 (1946). An earlier case allowing enforcement did not clearly hold that state tax claims could be extraterritorially enforced on the basis of comity. J. A. Holhauser Co. v. Gold Hill Copper Co., 138 N.C. 248, 50 S.E. 650 (1905).
25. Nelson v. Minnesota Income Tax Div., 429 P.2d 324, 325 (Wyo. 1967).
26. *Id.* at 325.

tions totally dissimilar to the fact situation of the principal case. Such decisions as were therein rendered provided the courts with an indirect means of giving effect to a contract and preserving the commercial convenience of the forum nation. In addition, another significant ramification existed: During the period in which the cases recognized as giving birth to the doctrine were decided, England was at war with the nations whose revenue laws were involved. These bases for the formation of the rule are obviously inapplicable in the present context,[27] yet courts have applied the ancient axiom of non-enforcement without giving due consideration to the significance of such circumstances at that time and to their manifest irrelevancy at present.

The other major premise upon which refusal to extend comity has consistently been based, is the erroneous categorization by the courts of revenue laws as penal. Support for this contention has by analogy been drawn to the field of criminal law.[28] It has been the position of many courts that both criminal and revenue laws serve primarily governmental purposes in assessing liability, and therein lies their penal nature. In truth, however, the only parallel philosophy which an analysis of the two bodies of law reveals is the fact that each is in the nature of governmental regulation of civic duties.[29] Justice Cardozo has elucidated the test of a law's penal nature. To be penal within the rules of international law, a statute must have as its purpose, "not reparation to one aggrieved, but vindication of the public justice."[30] In that context, a revenue law, totally lacking any vindictive purpose as the basis of its creation, can hardly be viewed as penal. In *Milwaukee County v. M. E. White Co.*,[31] discussed *supra,* the Supreme Court said "still the obligation to pay taxes is not penal. It is a statutory liability *quasi*-contractual in nature."[32] A revenue law in no way punishes: it rather defines the extent of a citizen's obligation to the government, in return for which the citizen is afforded protection of his rights.

27. State *ex rel.* Oklahoma Tax Comm'n. v. Rodgers, *supra* note 24.
28. *See* note 15 *supra,* Loucks v. Standard Oil Co., 224 N.Y. 99, 120 N.E. 198 (1918).
29. *Id.*
30. Loucks v. Standard Oil Co., *supra* note 28.
31. 296 U.S. 268 (1935).
32. *Id.* at 271.

Another reason for the decisions in the English cases was the desire by the courts of the forum to maintain and perpetuate the sovereign status of a nation and its laws. This motive no longer has any pertinence in light of the limited extent to which state sovereignty exists in the context of American federalism, especially under the mandates of the full faith and credit clause of the federal constitution.[33]

There also exists a basic weakness in Judge Hand's contention that scrutiny by one state of another state's relations with its citizens might lead to the forum placing its sister state in an embarrassing position; the sister state in bringing the action has indicated a willingness to risk the possibility of embarrassment to collect tax.

The Wyoming Supreme Court reversed that portion of the district court judgment awarding the State of Minnesota a penalty for failure to file a tax return.[34] The relevant provision of the Minnesota revenue law clearly designates that the amount in question is to be assessed as a penalty for failure to file a tax return. There is voluminous precedent for a refusal to enforce the penalty provisions of another state's laws.[35] Futhermore, it has been the perpetual philosophy of retributive justice that one state should not undertake to vindicate violations of the laws of another state.[36] Yet it should be noted that in the present case, the penalty provision, if enforced, would have accomplished nothing more than to compensate the State of Minnesota for the costs incurred in locating the whereabouts of the defendant and prosecuting the suit for collection of the tax. Considering the nature of the defendant's initial liability for the tax, that being in the nature of a debt,[37] and the expenses and inconvenience incurred by the plaintiff as a result of the defendant's failure to satisfy the debt, it is conceivable that the judgment served not as a penalty, but as a component of the debt itself. Had the provision been framed in the

33. *Id.* at 276: "The very purpose of the full faith and credit clause was . . . to alter the status of the several states as independent foreign sovereignties, each free to ignore obligations created under the laws or by the judicial proceedings of the others, and to make them integral parts of a single nation . . . ."
34. Nelson v. Minnesota Income Tax Div., *supra* note 25, at 325.
35. *See* authorities cited notes 15, 28 *supra*.
36. *Id.*
37. Milwaukee County v. M. E. White Co., *supra* note 20.

context of an interest assessment, the court's refusal to enforce it would be somewhat more vulnerable to criticism. In light of the sum being specifically designated as a penalty in the statute, however, there is uncontroverted authority for the court's decision.

Complexities of modern civilization have resulted in the creation of a greater need among the states to raise revenue to better meet the needs of their citizens. Modern mobility enables those who would cast off their legal duties to evade the law, conveniently aided in their flight by rules created in times when the implication of their present strict applications could hardly have been envisaged. The philosophies of the law in a nation such as ours have nullified the underlying foundations of many older rules. More important in contemporary America than the so-called sovereign character of state governments is the realization by state courts that evasion of valid tax laws with impunity by such people as the defendant in the present case causes a substantial increase in the burden of the conscientious citizen. In the words of Justice Cardozo, the courts "are not free to refuse to enforce a foreign right at the pleasure of the judges, to suit the individual notion of expediency or fairness." They should not "close their doors, unless help would violate some fundamental principle of justice, some prevalent conception of good morals, some deep-rooted tradition of the common weal."[38]

The refusal of the Wyoming Supreme Court to perpetuate the doctrine of non-enforcement of a sister state's tax claim is wholly commendable. Yet, despite the unimpeachable logic underlying such a decision as was here rendered, Wyoming is only the fifth jurisdiction to adopt the rule.[39] That extraterritorial tax claims will not be enforced is yet the view of an overwhelming majority of state jurisdictions.

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38. Loucks v. Standard Oil Co., *supra* note 28.

39. Oklahoma *ex rel.* Oklahoma Tax Comm'n. v. Neely, 225 Ark. 230, 282 S.W.2d 150 (1955), noted in 9 VAND. L. REV. 389 (1956); Ohio *ex rel.* Duffy v. Arnett, 314 Ky. 403, 234 S.W.2d 722 (1950), noted in 39 KY. L. J. 472 (1951); City of Detroit v. Gould, 12 Ill. 2d 297, 146 N.E.2d 61 (1957), noted in CHI.-KENT L. REV. 71 (1959), 7 DE PAUL L. REV. 243 (1958); California *ex rel.* Houser v. St. Louis Trust Co., 260 S.W.2d 821 (Mo. Ct. App. 1953), approving its earlier decision in *Rodgers*, but distinguishing the case on its facts.