# The Municipal Occupational Tax: A Source of Revenue for the Central City

*THE MUNICIPAL OCCUPATIONAL TAX: A SOURCE OF REVENUE FOR THE CENTRAL CITY examines the statutory and constitutional aspects of an occupational tax imposed upon employees for the privilege of working within the city. The article focuses particular attention on such a levy's application to city nonresidents, and concludes that such a tax can and should be enacted by central cities.*

In light of the growing fiscal crises which face major cities, municipalities are searching for additional means of generating revenue.[1] A variety of factors contribute to the growing socioeconomic pressures responsible for the central city's[2] fiscal problems.[3] Those more heavily dependent on city services—the poor, the undereducated, the aged—comprise an increasing segment of the central city's total

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[1] The municipal revenue crisis has long been a topic of discussion and, although it has become a cliche, it remains a serious problem. As traditional sources of municipal revenue—property and sales taxes—are becoming inadequate to meet future needs, city officials are turning to new austerity measures and increasing state and federal assistance to maintain the ability of municipal government to render effective services. For example, New York City received national attention in 1975 when it was on the verge of bankruptcy. N.Y. Times, Dec. 10, 1975, at 1, col. 7. Unable to meet its financial obligations, the city precariously remained solvent through the receipt of federal assistance. N.Y. City Seasonal Finance Act, 31 U.S.C. §§ 1501-15 (1975). Congressional testimony suggests that New York City's fiscal problems are not so unique as to preclude similar crises in other cities. *New York City Financial Crises: Hearings on* S. 1862, S. 2372, S. 2514, and S. 2523. *Before the Senate Comm. on Banking, Housing, and Urban Affairs*, 94th Cong., 1st Sess. 529-32 (1975) [hereinafter cited as *Senate Hearings*]. A New York Times' multi-city survey of budget officials revealed that at least seven other major U.S. cities were considered to be in similar "shaky financial shape." N.Y. Times, May 27, 1975, at 1, col. 1.

[2] The term central city as used in this article refers to the largest city within a Standard Metropolitan Statistical Area (SMSA) as the term is defined by the U.S. Office of Management and Budget. See U.S. BUREAU OF THE CENSUS, DEPT OF COMMERCE, 1970 CENSUS OF POPULATION XIII - XIV (1972). Generally, a central city is to be distinguished from the townships, unincorporated areas, and other small and large cities located within the designated SMSA.

[3] For example, the percentage of increase in city expenditures for selected services during the three-year fiscal period from 1972 to 1975 is as follows:

population.[4] Coupled with a continued migration of middle- and upper-income groups to the suburbs and a shift in local economic activity away from the central city,[5] the tax base fails to grow as rapidly as city revenue requirements.[6]

One factor contributing to the city's problems is the daily influx of nonresident employees. These individuals who are gainfully employed in the city, but reside elsewhere, receive a variety of municipal benefits[7] for which they pay little.[8] Traditionally, property and

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| | SERVICES | | |
|---|---|---|---|
| CITY | Police | Fire | Education (on county basis) |
| Los Angeles | 38.2 | 32.2 | 124.4 |
| Oakland | 19.9 | 22.3 | 94.7 |
| Sacramento | 24.1 | 25.0 | (19.5)* |
| San Diego | 50.0 | 33.3 | 129.5 |
| San Jose | 53.3 | 29.5 | 60.3 |
| San Francisco | 24.7 | 24.7 | 19.0 |

*(decrease)

U.S. BUREAU OF THE CENSUS, DEP'T OF COMMERCE, LOCAL GOVERNMENT FINANCES IN SELECTED METROPOLITAN AREAS AND LARGE COUNTIES 76-78 (1974); U.S. BUREAU OF THE CENSUS, DEP'T OF COMMERCE, LOCAL GOVERNMENT FINANCES IN SELECTED METROPOLITAN AREAS AND LARGE COUNTIES 93-96 (1976) [hereinafter cited as LOCAL GOVERNMENT FINANCES].

[4] For example, in the Oakland-San Francisco urbanized area the percentage of persons over age 65 rose from 8.2 to 9.7 percent between 1950 and 1970. Those persons with incomes below the area's median income level rose from 40.4 to 48.1 percent. U.S. DEP'T OF COMMERCE, U.S. CENSUS OF POPULATION, CALIFORNIA, Tables 5-51, 5-128 (1950); U.S. DEP'T OF COMMERCE, U.S. CENSUS OF POPULATION, CALIFORNIA, Tables 6-79, 6-646 (1970).

[5] It is useful to distinguish between the short and long-term factors that have precipitated the fiscal crisis many central cities face. The short-term factors are linked to local economics—unemployment, inflation, interest rates, investor confidence, bond indebtedness, and sources of city revenue. The long-term factors reflect national socioeconomic trends such as population and industrial migration patterns. *Senate Hearings, supra* note 1, at 521-528.

[6] For example, with the growth of expenditures, bond indebtedness of California cities nearly tripled between 1960 and 1974.

Bond Indebtedness of California Cities
(in millions of dollars)

| 1960 | 1965 | 1970 | 1974 | Percentage change from 1960 to 1974 |
|---|---|---|---|---|
| $1,352 | 1,804 | 2,831 | 3,536 | 262% |

CALIFORNIA STATISTICAL ABSTRACT, FINANCIAL TRANSACTIONS CONCERNING CITIES, Tables N-21 (1970), N-12 (1972), N-9 (1975).

[7] Expenditure categories that benefit nonresident employees directly include police and fire protection, health care, parks and recreation, highways, and sanitation. W. HIRSCH, P. VINCENT, H. TERRELL, D. SHOUP, A. ROSSET, FISCAL PRESSURES ON THE CENTRAL CITY 18-22 (1971).

[8] There have been few empirical studies of the hypothesis that the central city provides services to nonresidents for little or no compensation. What research has been undertaken on this "exploitation thesis" has resulted in differing conclusions. For studies which support the thesis, *see, e.g.*, Hawley, *Metropolitan*

general sales taxes have supplied a large portion of the revenue used to support services such as police, fire, and sanitation.[9] Since nonresident employees do not pay property taxes to the city in which they work, a large part of the cost for these services falls on residential taxpayers.

One method of raising additional revenue is an occupational tax levy on the privilege of working in the city.[10] A number of cities across the country have imposed various forms of the occupational tax.[11] This has significantly increased local tax revenue,[12] while at the same time exacting a substantial tax contribution from nonresidents.[13] While several California cities are affected by commuter influx[14] and a shrinking revenue base, to date, relatively few have at-

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*Population and Municipal Government Expenditures in Central Cities*, 7 J. SOC. ISSUES 100 (1951); Neenan, *Suburban-Central City Exploitation Thesis: One City's Tale*, 23 NAT'L. TAX J. 117 (1970). For reports that find no strong evidence that the suburbs exploit the cities, *see, e.g.*, Margolis, *Metropolitan Finance Problems*, in J. BUCHANAN, PUBLIC FINANCES: NEEDS, SOURCES, AND UTILIZATION 256 (1961); H. BRAZER, CITY EXPENDITURES IN THE UNITED STATES (1959). For studies which refute the thesis *in toto*, *see, e.g.*, J. BANORETZ, GOVERNMENTAL COST BURDENS AND SERVICE BENEFITS IN THE TWIN CITIES METROPOLITAN AREA (1965); Vincent, *The Fiscal Impact of Commuters*, in HIRSCH, *supra* note 7, at 41.

[9] The percentage of total city tax revenue generated from property and general sales taxes in 1974-75 are as follows: Los Angeles 68.0, Sacramento 96.1, San Diego 83.9, Oakland 80.6, San Francisco 79.7, and San Jose 72.7. LOCAL GOVERNMENT FINANCES, *supra* note 3, at 93-96.

[10] While an occupational tax is generally a gross receipts tax on earnings, there are many differences in detail, particularly with respect to scope, definition of tax base, tax credits, methods of collection, and general administration. For a further discission of these aspects, *see* R. SIGAFOOS, THE MUNICIPAL INCOME TAX (1955). An example of one such tax is that enacted by the City of Oakland that provides for a license fee of one percent of the yearly gross income of persons employed therein. OAKLAND, CALIF., ORDINANCE NO. 9021 (1974). At the time of this writing the validity of the ordinance is the subject of litigation. The trial court held the tax invalid as an income tax. The appellate court reversed, stating that while the tax had some of the characteristics of an income tax, it was more akin to a license tax. The California Supreme Court has recently granted a hearing in this case. Weekes v. City of Oakland, 64 Cal. App. 3d 907, 926, 134 Cal. Rptr. 858, 869 (1st Dist. 1976), *hearing granted*, Feb. 11, 1977 (1 Civ. 37873).

[11] As of 1969 a form of the occupational tax had been adopted by over 1,900 local governments in the United States. Stephens, *The Suburban Impact of Earnings Tax Policies*, 22 NAT'L. TAX. J. 313 (1969).

[12] In the 34 cities sampled by Sigafoos, the percentage of total city revenue from occupational taxes ranged from 7 to 37 percent, with a mean of 22.4 percent. SIGAFOOS, *supra* note 10, at 72.

[13] It should be noted that growing fiscal demands make it unlikely that a tax reduction, in absolute terms, would inure to the benefit of city property taxpayers. A relative reduction would be realized by virtue of the new group of nonresident taxpayers since distributing the total tax burden over a larger group of individuals necessarily reduces the burden on any one taxpayer.

[14] R. SMITH, LOCAL INCOME TAXES: ECONOMIC EFFECTS AND EQUITY 104-105 (1972).

tempted to impose an occupational tax.[15]

It is the thesis of this article that the fiscal dilemma of California's central cities may be resolved in part by the imposition of a municipal occupational tax. Such a tax is not only fair and necessary but, moreover, can withstand judicial scrutiny if its drafters are mindful of statutory as well as federal and state constitutional limits on the municipal taxing authority.

Through a bifurcated analysis, this article considers the potential statutory and constitutional challenges to an occupational tax, with particular focus on its application to nonresidents. Part I examines the statutory authority of municipal taxing powers, while part II considers the state and federal constitutional constraints of a city's power to levy an occupational tax. The discussion is limited to charter cities, since most central cities in California are chartered.[16]

## I. STATUTORY AUTHORITY TO IMPOSE AN OCCUPATIONAL TAX

Generally, a charter city municipality derives its substantive governing authority from state constitutional grants augmented by statutory provisions.[17] In California, a municipality's power to levy an occupational tax can be found in two statutory provisions. Govern-

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[15] San Francisco, citing statistics indicating a nearly twenty percent commuter population, made an unsuccessful attempt to impose an occupational tax in 1969. *See* County of Alameda v. City and County of San Francisco, 19 Cal. App. 3d 750, 97 Cal. Rptr. 175 (1st Dist. 1971). Currently, the city of Oakland is attempting to impose an occupational tax on residents as well as on nonresidents. *See* Weekes v. City of Oakland, 64 Cal. App. 3d 907, 134 Cal. Rptr. 858 (1st Dist. 1976).

[16] Of the sixteen California cities with populations over 100,000 fourteen are charter cities. ABSTRACT Table B-6 (1976; CALIFORNIA ROSTER 93 (1975-1976). Furthermore, the elimination of the general law city from the discussion is predicated on the assumption that the imposition of a nonresidential occupational tax is of lesser concern to the general law city because of its size, limited industrial and commercial base, adequate fiscal finances, and limited nonresidential employees. This is not to suggest that the general law city does not have the power to impose similar taxes, but merely that the fine distinctions between powers of a charter city and a general law city in imposing an occupational tax are beyond the scope of this article. For a discussion of these distinctions *see* Sato, *Municipal Occupational Taxes in California: The Authority to Levy Taxes and the Burden on Intrastate Commerce*, 53 CAL. L. REV. 801, 805-810 (1965) [hereinafter cited as Sato, *Municipal Occupation Tax* ].

[17] Generally, California municipalities are organized as charter or general law cities. Article 11, section 5 of the California Constitution, permits a city to adopt a charter for its own government. Such chartered cities have the power to "make and enforce all ordinances and regulations in respect to municipal affairs." CAL. CONST. art XI, § 5(a). In contrast, general law cities do not have charters. They derive their authority from the general state law rather than from their own charter. For a further discussion of this distinction and its applicability to an occupational tax, *see* note 64 *infra*.

ment Code section 37101[18] provides that a city may license and tax every lawful business transacted in the city; Business and Professions Code section 16000[19] permits incorporated cities to license any business transacted within its jurisdiction.

In examining the scope of this statutory taxing power, courts focus on three aspects: (1) the nature of the business being taxed, (2) the local nexus of the taxable event, and (3) the measure of the tax. An occupational tax must pass all three criteria before it will be held valid.

### *A. The Nature of the Business Being Taxed*

Section 37101 of the California Government Code and section 16000 of the Business and Professions Code authorize municipalities to tax "any business" conducted within its territorial limits. The courts have given a liberal construction to the term "business" under these statutes, defining it to include "all manner of occupation or means by which persons earn a livelihood."[20] In this context the term "occupation" has received an equally expansive interpretation by the courts, which have stated that it encompasses "any business, trade, profession, pursuit, vocation or calling."[21]

Typically, cities have chosen to exercise their statutory taxing authority by levying a license fee on commercial enterprises. Such a tax has received judicial approval when applied in a variety of busi-

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[18] CAL. GOV'T CODE § 37101 (West Supp. 1977). Section 37101 provides that:

> The legislative body may license, for revenue and regulation, and fix the license tax upon, every kind of lawful business transaction in the city, including shows, exhibitions, and games. It may provide for collection of the license tax by suit or otherwise. If the legislative body levies a sales tax under the authority of this section, it may impose a complementary tax at the same rate upon use or other consumption of tangible personal property. If the legislative body imposes a sales or use tax, it shall do so in the same manner and use the same tax base as prescribed in Part 1.5 (commencing with Section 7200) of Division 2 of the Revenue and Taxation Code.

[19] CAL. BUS. & PROF. CODE § 16000 (West 1964). Section 16000 provides that:

> The legislative bodies of incorporated cities may, in the exercise of their police power, and for the purpose of regulation, as herein provided, and not otherwise, license any kind of business not prohibited by law transacted and carried on within the limits of their jurisdictions, including all shows, exhibitions and lawful games, and may fix the rates of such license fee and provide for its collection by suit or otherwise.

[20] *In re* Diehl, 8 Cal. App. 51, 54, 96 P. 98, 99 (3d Dist. 1908).

[21] City of Los Angeles v. Rancho Homes, Inc., 40 Cal. 2d 764, 767, 256 P.2d 305, 306 (1953). The court also noted that the term trade had been defined as "equivalent to occupation, employment or business whether manual or mercantile. Whenever any occupation, employment or business is carried on for the purpose of profit or gain or livelihood, not in the liberal arts or learned professions, it is constantly called trade. (citations omitted.)" *Id.*

ness settings.[22] Cities, however, have on occasion applied the tax to certain service professions.[23] California decisions suggest that a charter city's occupational taxing powers may extend to virtually all income-producing activities, occupations, businesses and professions, carried on within its borders.[24]

It is still an open question, however, whether such an expansive interpretation would allow cities to impose an occupational tax on all wage earners. A possible limitation was suggested by one early California Supreme Court decision,[25] which reversed the conviction of an attorney for failure to pay a municipal license tax levied against "every attorney at law."[26] The defendant attorney, who refused to pay the tax, claimed that the tax was imposed upon him personally rather than upon the carrying on of his "law business." Arguably, a tax on the individual as an employee would be more akin to an income tax, whereas a tax upon a person conducting a business is more like a license tax. The court held that a city cannot levy license tax upon a person nor upon individual acts that fall short of carrying on a business.[27] While this case involved a license tax the same argument can be raised against occupational taxes.

While providing little guidance as to what constitutes the carrying on of business, the court apparently drew a distinction between an attorney maintaining her own office and thereby carrying on a "law business," and an attorney practicing law in an employee capacity. If the court intended to uphold occupational taxes as to attorneys because they maintain their offices but not as to attorneys who are employees, the distinction is dubious at best. No inherent reason justifies the distinction among an associate who works for a large law firm in a wage earning capacity or a sole practitioner with an office

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[22] *See, e.g.*, Willingham Bus Lines, Inc. v. Municipal Court, 66 Cal. 2d 893, 428 P.2d 602, 59 Cal. Rptr. 618 (1967) (license tax on busline); Fox Bakersfield Theater Corp. v. City of Bakersfield, 36 Cal. 2d 136, 222 P.2d 879 (1956) (license tax on amusements); Clarke v. City of San Pablo, 270 Cal. App. 2d 121, 75 Cal. Rptr. 726 (1st Dist. 1969) (license tax on apartment operator); Hirsch v. City & County of San Francisco, 143 Cal. App. 2d 313, 300 P.2d 177 (1st Dist. 1956) (license tax on auctions).

[23] *See, e.g., In re* Galusha, 184 Cal. 697, 195 P. 406 (1921) (license tax on attorneys); City of Redding v. Dozier, 56 Cal. App. 590, 206 P. 465 (3d Dist. 1922) (license tax on physicians).

[24] *In re* Groves, 54 Cal. 2d 154, 351 P.2d 1028, 4 Cal. Rptr. 844 (1960) (carrying on any business, vocation, profession, calling, show, exhibition or game); City of Los Angeles v. Belridge Oil Co., 42 Cal. 2d 823, 271 P.2d 5 (1954) (privilege of engaging in the activity of selling); *Ex parte* Braun, 141 Cal. 204, 74 P. 780 (1903) (license tax upon various trades and occupations); Marsh & Mclennan of Calif., Inc. v. City of Los Angeles, 62 Cal. App. 3d 108, 132 Cal. Rptr. 798 (2d Dist. 1976) (any person engaged in any trade, calling, occupation, vocation, profession or other means of livelihood as an independent contractor).

[25] City of Sonora v. Curtin, 137 Cal. 583, 70 P. 674 (1902).

[26] *Id.* at 584, 70 P. at 674.

[27] *Id.* at 585, 70 P. at 675.

or a partner in a small professional law corporation. Presumably, all receive the benefit of the governmental services rendered by the municipality in which they are employed.

It is not self-evident that a distinction, although permissible, between independent business entrepreneurs and those employed by others is mandatory before a tax can be levied on the privilege of engaging in an occupation.[28] On the contrary, since the courts have defined the terms business and occupation broadly to include all means of making a livelihood or obtaining a profit, nothing appears to preclude a municipality from imposing an occupational tax on wage earners as well as business entrepreneurs. Thus, while cities have historically imposed occupational taxes in limited settings, their statutory authority to impose such taxes extends to virtually all occupations.

### *B. The Geographic Limitation and Measure of the Tax*

A second statutory requirement is that charter cities may only impose a tax on occupations and businesses "transacted and carried on within the limits of their jurisdiction."[29] Taxation of any extraterritorial activities are proscribed by the state Constitution.[30] When an occupational tax is imposed on residents who work solely within the city there is no jurisdictional problem because both the place of employment and residence are within the city.[31] Problems do arise, however, when the tax is applied to nonresidents employed within the city, or to individuals, whether residents or nonresidents, who work both within and without the city's geographical boundaries.

The courts have not directly dealt with these problems in the context of sections 16000 of the Business and Professions Code and 73101 of the Government Code. There is, however, a line of license and occupational tax cases from which one can draw some general

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[28] The imposition of an occupational tax appears to be limited only by the constitutional and statutory exceptions carried out in favor of certain groups. For example, the California Constitution exempts banks and insurance companies from local license taxes. CAL. CONST. art XIII, §§ 27 and 28, respectively. Statutory provisions exempt cafe musicians, CAL. BUS. & PROF. CODE § 16100.5 (West Supp. 1977), and veterans, CAL. BUS. & PROF. CODE § 16102 (West 1964).

[29] CAL. BUS. & PROF. CODE § 16000 (West 1964), set forth in note 19 *supra*. A similar provision is found in CAL. GOV'T CODE § 37101 (West Supp. 1977), set forth in note 18 *supra*. *See generally* 11 CAL. JUR. 3D *Business and Occupation Licenses* § 30 (1974).

[30] Article XI, section 11, of the California Constitution provides: "Any county, city, town or township may make and enforce within its limits all such . . . . regulations as are not in conflict with general laws." This provision has been held to forbid extraterritorial application of local ordinances. City of South Pasadena v. Los Angeles Terminal Ry., 109 Cal. 315, 321, 41 P. 1093, 1095 (1895).

[31] A charter city's taxing authority over individuals so situated has its basis in section 5 of article XI of the California Constitution. The discussion of the city's taxing authority in this article is limited to taxation for revenue purposes and does not include regulatory taxation.

analogies. These cases are significant for two reasons. First, they address the issue of what would constitute sufficient employment activity to justify the imposition of an occupational tax. Second, assuming the city's taxing power can properly be invoked, the cases give guidance concerning the question of what relationship the measure of the tax must have to the taxable event. Each question is, in fact, part of a two-prong test used by courts in analyzing the validity of occupational taxes. California courts have held that before an occupational tax can be validly imposed (1) the event to be taxed must be more than an occasional activity within the jurisdiction;[32] and (2) the measure of the tax must bear a reasonable relationship to the taxable event.[33]

Generally, before an occupation or business can be taxed, courts insist that more than an occasional transaction of the activity must occur within the municipality seeking to impose the tax.[34] The ratio of work done in the city to the total hours of business activity undertaken provides a simple measure of whether an activity is merely occasional and therefore not subject to the tax. For example, if attorney $A$ works twenty hours of a fifty-hour work week in city $X$ and the remaining thirty hours in city $Y$, then the business transacted in city $X$ would constitute forty percent of $A$'s work time.

Although the courts have not defined the precise point at which a city may invoke its taxing authority, the cases suggest that minimal activity is sufficient. In one case, for example, the court found that one-sixth of the total volume of a business transacted within the city was sufficient to enable the city to tax the activity.[35] In another case, the court held that thirty-four deliveries to one customer in the city during a five-month period was more than an occasional transaction.[36] While these two cases involve license taxes on non-city-based businesses, one court has implied that the same occasional transaction test will apply to an occupational tax on nonresidents.[37] Since most nonresident employees spend one-third of the weekday in the city in which they are employed, this contact is sufficient to

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[32] Security Truck Line v. City of Monterey, 117 Cal. App. 2d 441, 451, 256 P.2d 366, 373 (1st Dist. 1953).

[33] City of Los Angeles v. Shell Oil Co., 4 Cal. 3d 108, 124, 480 P.2d 953, 963, 92 Cal. Rptr. 1, 11 (1971), *cert. denied*, 404 U.S. 831 (1971).

[34] *See* Security Truck Line v. City of Monterey, 117 Cal. App. 2d 441, 451-52, 256 P.2d 336, 373 (1st Dist. 1953).

[35] Arnke v. City of Berkeley, 185 Cal. App. 2d 842, 847, 8 Cal. Rptr. 645, 648 (1st Dist. 1960).

[36] People v. M. V. Nurseries, Inc., 40 Cal. App. 3d Supp. 1, 2, 115 Cal. Rptr. 326, 327 (App. Dep't Super. Ct., Los Angeles 1974).

[37] County of Alameda v. City and County of San Francisco, 19 Cal. App. 3d 750, 97 Cal. Rptr. 175 (1971). While not directly applying the occasional transaction test, because it was not at issue in the case, the court cited with approval cases that apply the two-prong test. *Id.* at 754-55, 97 Cal. Rptr. at 177-78.

bring them within the city's taxing authority.[38]

In addition to a sufficient nexus of activity, courts have also required that there be fair and reasonable relationship between the taxable event and the measure of the tax.[39] In one case, a non-city-based company challenged a license tax measured by the number of trucks making deliveries into the city.[40] Although the court found the quantum of business activity sufficient to justify the imposition of a tax, the tax was invalidated because it was arbitrary and discriminatory.[41] The court declared that, since the taxable event was conducting business within the city, a tax measured by the number of vehicles entering the city bore no reasonable relationship to the amount of goods delivered into the city. A trucker might deliver in one vehicle as much as another delivers in ten, yet the former is liable for only one-tenth of the tax imposed on the latter.[42] Because the measure of the tax was not entirely based on the taxable event, the ordinance was struck down as arbitrary.

Another court elaborated on this reasonable relationship test in a case involving a San Francisco ordinance which imposed an occupational tax only on nonresident employees.[43] After calculating that nonresident employees constituted nearly twenty percent of its daytime population, San Francisco imposed a tax that would cause nonresident employees to bear approximately twenty percent of the total cost of services furnished by the city.[44] The court invalidated the tax on equal protection grounds. It noted that the city may justifiably allocate certain costs but it may not impose a tax solely upon nonresidents while totally exempting residents engaged in the same activity.[45]

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[38] Arguably, applying the city's taxing power to the occupations of nonresidents could pave the way for imposition of such taxes on any and all activities of nonresidents within the city, *e.g.*, shopping, amusements, travel. This concern can be dispelled by noting that the activities to be taxed must both meet the occasional transaction test and be reasonably related to the measure of the tax. It is questionable whether occasional nonresidential activities such as attendance at special events or shopping at downtown malls would meet the first prong of the test. Such activities as shopping and entertainment are sufficiently spurious that a tax could not be imposed on all nonresidential activities within the city.

[39] City of Los Angeles v. Shell Oil Co., 4 Cal. 3d 108, 124, 480 P.2d 953, 963, 93 Cal. Rptr. 1, 11 (1971), *cert. denied*, 404 U.S. 831 (1971).

[40] Security Truck Line v. City of Monterey, 117 Cal. App. 2d 441, 256 P.2d 366 (1st Dist. 1953).

[41] *Id.* at 454, 256 P.2d at 375.

[42] *Id.* at 453, 256 P.2d at 374.

[43] County of Alameda v. City and County of San Francisco, 19 Cal. App. 750, 97 Cal. Rptr. 175 (1971).

[44] A payroll withholding tax was imposed on all nonresident employees in the amount of one percent of gross earnings. *Id.* at 752, 97 Cal. Rptr. at 176.

[45] *Id.* at 756, 97 Cal. Rptr. at 178. The court also found the tax ordinance to be in violation of equal protection guarantees.

With regard to the allocation formula, the court stated that it was unreasonable to require nonresident employees to pay nearly twenty percent of the total city services simply because they comprise twenty percent of the daytime population. It pointed out that nonresidents do not use city services on a twenty-four hour basis. If the taxable event was the use of the city services by nonresident employees, the equitable apportionment of service consumption should be based on the time spent in the city and not on percentage of nonresident daytime population.[46] The court implied that a tax on nonresidents may not be invalid if it is based on the quantum of contact within the city.

The major infirmity, however, of San Francisco's occupational tax was that it was levied on nonresidents only. While properly noting that the taxing measure was unreasonable, the court's discussion concerning what would constitute a proper taxing measure failed to adequately focus on the taxable event. The activity that is being taxed is the privilege of engaging in an occupation in the city, the justification being that the city provides services to employees while they are engaged in their occupation. Since what is taxed is occupation, it should make little difference where one's non-working time is spent. Therefore, an occupational tax would only be valid if imposed on residents and nonresidents alike,[47] since full-time employees in the same occupation receive similar levels of service while at work, irrespective of whether they are residents or nonresidents. Since the taxable event, the privilege of engaging in an occupation, is the same for both categories of employees, the measure of their respective tax burden should be the same.

The issue of apportionment, therefore, properly arises only with regard to part-time employees. In this instance, the time employees spend in the city does have a direct bearing on the taxable event—services provided while employed within the city. If the taxable event reflects services provided during employment, then service consumption is a function of time employed; therefore, part-time employment requires apportionment. While exact apportionment is unnecessary, a reasonable relationship must exist.[48] For example, a

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[46] *Id.*

[47] In Weekes v. City of Oakland, 64 Cal. App. 3d 907, 134 Cal. Rptr. 858 (1st Dist. 1976), the court upheld an occupational tax equally applied to residents and nonresidents. The court noted that though residents may receive other municipal service while not working, the tax does not discriminate against nonresidents in the absence of a showing that such residents are not otherwise taxed for those services. *Id.* at 941, 134 Cal. Rptr. at 879.

[48] The equal protection due taxpayers under the Fourteenth Amendment does not require exacting equality of taxation. Travellers' Insurance Co. v. Connecticut, 185 U.S. 364, 372 (1902). Cities may impose occupational taxes in different classes provided the tax bears a reasonable relationship to the taxable event. *See*

tax based on a percentage of gross earning receipts[49] from employment in the city would appear to have a built-in apportionment factor. Such a measure, in the form of payroll withholding,[50] has the advantage of taxing only that portion of gross earning receipts derived from employment in the city. A flat tax rate can also meet the reasonable relationship test as long as it incorporates an apportioning factor. For example, a flat fee in the amount of ten dollars per month for full-time employees would have to be reduced accordingly for part-time employees.

In summary, when a regular course of activity is conducted within the city, the courts have recognized the municipality's broad discretion in imposing an occupational tax. The major consideration in imposing such a tax is to insure that the measure of the tax is reasonably related to the taxable event. This is particularly important when the tax is imposed on part-time employees. In such instances, the city must apportion the tax to reflect the part-time nature of the occupation, the taxable event.

## II. CONSTITUTIONAL LIMITATIONS ON THE POWER TO TAX

As the preceding discussion demonstrates, section 16000 of the Business and Professions Code and section 37101 of the Government Code empower a charter city to impose an occupation tax. This grant of authority, however, is complicated by two other statutory provisions. Section 17041.5 of the Revenue and Taxation Code prohibits the levying of an income tax by municipalities,[51] while section 50026 of the Government Code prevents the discriminatory practice of imposing an occupational tax on nonresidents only.[52] A con-

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Fox Bakersfield Theater Corp. v. City of Bakersfield, 36 Cal. 2d 136, 142, 222 P.2d 879, 883-84 (1950).

[49] For a discussion of this term, *see* text accompanying notes 53-63 *infra*.

[50] For administrative purposes, the most convenient manner of occupational tax collection is employer withholding. In this sense, the employer is a conduit to the city's tax collection. Employee self-reporting presents problems of earmarking earnings derived from employment in the city, as well as reporting and collection difficulties. For a further discussion of tax administration, *see* SIGAFOOS, *supra* note 10, at 32-67.

[51] CAL. REV. & TAX. CODE § 17041.5 (West 1970). The statute provides in part:

> Notwithstanding any statute, ordinance, regulation, rule or decision to the contrary, no city . . . whether charter or not, shall levy or collect or cause to be levied or collected any tax upon the income, or any part thereof, of any person, resident or nonresident.
>
> This section shall not be construed so as to prohibit the levy or collection of any otherwise authorized license tax upon a business measured by or according to gross receipts.

[52] CAL. GOV'T CODE § 50026 (West Supp. 1977). The statutue provides in part:

> The legislative body of any local agency, chartered or general law, which is otherwise authorized by law or charter to impose any tax on

sidered analysis of these statutes, within the context of constitutional constraints, is necessary to harmonize their impact on the charter city's authority to impose an occupational tax on nonresident employees.

### A. *The Income Tax Pitfall*

Section 17041.5 of the Revenue and Taxation Code, on its face, proscribes the levying of a municipal income tax. This prohibition, however, is not necessarily fatal to a municipal occupational tax measured by gross earning receipts. In the main, income tax laws apply only to taxes on net income and not taxes on gross receipts.[53] The courts have yet to resolve the question of whether section 17041.5 applies to all taxes measured by both gross receipts and net income. They have on numerous occasions upheld taxes measured by gross receipts and distinguished them from income taxes. In one case a flat-fee gross receipt tax was imposed on persons engaged in various trades, occupations and professions.[54] Dismissing the contention that the ordinance was an invalid income tax, the court stated: "A long line of decisions rendered in this state has sustained the validity of gross receipts taxes and furthermore a gross receipt occupation tax is not an income tax."[55] The later enactment of section 17041.5 did not alter the soundness of the court's dictum in that decision.

There are two reasons why one may conclude that section 17041.5 does not apply to occupational taxes measured by gross receipts. First, the Personal Income Taxation Part of the Revenue and Taxation Code, which includes section 17041.5, defines taxable income for purposes of this section as (1) "gross income minus deductions allowed by this part,"[56] and (2) "adjusted gross income."[57] A taxpayer's gross earning receipts include all income from earnings less expenses incurred in realizing those earnings. That is, for purposes of

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> the privilege of earning a livelihood by an employee . . . shall not impose any such tax, fee or charge on the earnings of any employee when such employee is not a resident of the taxing jurisdiction, unless exactly the same tax, fee or charge at the same rate, with the same credits and deductions, is imposed on the earnings of all residents of the taxing jurisdiction who are employed therein.
>
> This section shall not be construed as authorizing any tax prohibited by Section 17041.5 of the Revenue and Taxation Code or any other provision of law, nor shall it be construed so as to prohibit the levy or collection of any otherwise authorized tax upon a business measured by or according to gross receipts.

[53] *See generally* 71 AM. JUR. 2D *State and Local Taxation* § 447 (1973).

[54] In Franklin v. Peterson, 87 Cal. App. 727, 729, 197 P.2d 788, 789 (2d Dist. 1948), the flat-fee tax was in the sum of twelve dollars per year for the first $12,000 of gross receipts and one dollar per year for each additional $1,000.

[55] *Id.* at 733, 197 P.2d at 792 (dictum).

[56] CAL. REV. & TAX. CODE § 17073 (West 1970).

[57] CAL. REV. & TAX. CODE § 17072 (West Supp. 1976).

personal income taxation, gross income from earnings becomes taxable only after it has been adjusted by legitimate deductions. The earnings which are subject to personal income taxation are in effect net earnings, as opposed to gross earnings.

The fact that the taxable personal income definition of the Revenue and Taxation Code provides for deductions from gross income raises the inference that the legislature intended to limit the taxing provisions of the code to net income. Thus, section 17041.5's proscription of the imposition of income taxes by municipalities should be read as a limitation on net income taxation, not taxation on gross income. That section 17041.5 should be so construed is supported by administrative construction. California Franchise Tax Board regulations specify that the state's Personal Income Tax Law, of which section 17041.5 is a part, is a tax upon net income.[58]

Section 17041.5 expressly gives support to this construction by noting a distinction between a tax upon income and a tax upon gross receipts. The applicable provision reads: "This section shall not be construed so as to prohibit the levy or collection of any otherwise authorized license tax upon a business measured by or according to gross receipts."[59] One court has declared the language of section 17041.5 to mean that an occupational tax measured by the gross earning receipts from employment will not bring the tax within the prohibition of section 17041.5.[60] The court noted that a tax on the privilege of engaging in employment, measured by gross receipts, is not an attempt to tax income, but instead complementary to a business license tax.[61]

Furthermore, section 17041.5 was enacted in light of the common law distinction between income and gross receipt taxes. In the absence of express statutory language negating such distinctive treatment, it is unlikely that the legislature intended to be at variance with the common law recognition that a gross receipt tax is not an income tax.

Whether an occupational tax measured by gross earning receipts is an income tax may well be mooted by Government Code section 50026.[62] On its face, section 50026 proscribes any tax on the privilege of earning a livelihood, measured by employee earnings, levied exclusively on nonresidents. Section 17041.5, which was in existence for five years when section 50026 was enacted, purports to prohibit all municipal income taxes. If an occupational tax measured by gross

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[58] 18 CAL. AD. CODE ch. 3, sub ch. 2.5 Preface (1964).

[59] CAL. REV. & TAX. CODE § 17041.5 (West 1970).

[60] Weekes v. City of Oakland, 64 Cal. App. 3d 907, 937, 134 Cal. Rptr. 858, 876 (1st Dist. 1971).

[61] *Id.*

[62] CAL. GOV'T CODE § 50026 (West 1974), set forth in note 52 *supra.*

earnings receipts fell within the prohibition of section 17041.5, then passage of section 50026 would have been superfluous. Section 50026 demonstrates the legislature's recognition that a tax on gross earnings is more characteristic of an occupational tax than an income tax. Thus, section 17041.5 does not preclude an occupational tax measured by gross earning receipts.

A municipality seeking to impose an occupational tax must nevertheless draft its ordinance with some care to avoid an adverse construction by the courts. Drafters who wish to avoid the income tax pitfall must emphasize that it is the employment in the city which is the incident being taxed, not the income accrued therefrom. The earnings obtained through employment only constitutes the method of measurement of the tax.

### *B. Problems of State Preemption*

California constitutional provisions bear directly on the scope of a municipality's taxing powers. Generally, all municipalities may make and enforce all laws concerning local matters so long as they are not directly in conflict with state laws.[63] Additionally, a charter city may make and enforce all laws respecting "municipal affairs."[64] In determining whether a municipality has the constitutional authority to impose an occupational tax, courts must determine whether such taxing authority is a municipal affair.[65] Once a particular matter is deemed to be a municipal affair, local legislation is controlling,

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[63] CAL. CONST. art. XI, § 7, provides that: "A county or city may make and enforce within its limits all local, police, sanitary, and other ordinances and regulations not in conflict with general laws." It should be noted that this provision is applicable to all municipalities, whether chartered or not.

[64] CAL. CONST. art. XI, § 5(a) states in part that charter cities ". . . may make and enforce all ordinances and regulations in respect to municipal affairs, subject only to restrictions and limitations provided in their several charters and in respect to all other matters they shall be subject to general laws." While a general distinction must be made between the taxing powers of general law and charter cities, their power to levy occupational taxes is similar although the source of their authority differs. Charter cities have authority to make and enforce laws concerning municipal affairs. License taxation for revenue purposes has been held to be a municipal affair, *Ex parte* Braun, 141 Cal. 204, 213, 74 P. 780, 783-84 (1903). General law cities, however, must look to state statutory provisions to obtain the authority to impose occupational taxes. Section 37101 of the Government Code and Section 16000 of the Business & Professions Code provides such authority. Thus, while charter cities receive their grant of authority with respect to occupational taxes primarily from the state Constitution, general law cities receive their authority from the state legislature. *See* notes 16-17 *supra* for a discussion of the distinction between charter and general law cities.

[65] The municipal affairs doctrine generally refers to a charter city's constitutional grant of power that is protected from state legislative interference. A comprehensive discussion of this doctrine may be found in Sato, *Municipal Affairs in California*, 60 CAL. L. REV. 1055 (1972) [hereinafter cited as Sato, *Municipal Affairs*]; *see also* Comment, *The Traffic Congestion Bottleneck: City Police Power, Municipal Affairs and Tax Solutions*, this volume.

subject only to limitation by city charter and constitutional safeguards.[66] Conversely, if a particular matter is defined as a statewide concern, it is subject to the preemptive power of the state and thus is beyond municipal control.[67]

The legislature has the authority to designate a particular subject matter as a statewide concern, but its *de facto* determination is not dispositive of the issue. While the courts will give great weight to legislative intent, the final decision of whether a matter is a municipal affair or a statewide concern rests exclusively with the judiciary.[68] This prevailing exercise of judicial authority no doubt stems from a recognition that municipal power could be rendered completely nugatory if the legislature could simply declare a matter to be of statewide concern.

In determining what is a municipal affair, the courts have applied a three-part test. In the case of *In re Hubbard*,[69] the California Supreme Court held that a particular field is preempted when any of the following conditions exists: (1) the subject matter has been so fully covered by state law as to indicate that it is exclusively a matter of state concern; (2) the subject matter has been partially covered by general law so as to indicate that there is a paramount state concern that will not tolerate additional local action; or (3) the subject matter has been partially covered by state law, and the burden of local law on the transient citizens of the state outweighs the possible benefit to the municipality.[70]

Under this formulation, judicial analyses of whether a local matter is preempted by state law has produced discordant results,[71] with the lack of consistency stemming in part from the state supreme court's own flexible application of the *Hubbard* test.[72] Under *Hubbard*, the

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[66] *See* West Coast Advertising v. City and County of San Francisco, 14 Cal. 2d 516, 522, 95 P.2d 138, 142 (1939); *In re* Helm, 143 Cal. 553, 555, 77 P. 453, 454 (1904).

[67] *See* Pacific Tel. & Tel. Co. v. City and County of San Francisco, 51 Cal. 2d 766, 768, 336 P.2d 514, 516 (1959); Pipoly v. Benson, 20 Cal. 2d 366, 369-70, 125 P.2d 482, 484 (1942).

[68] In Bishop v. City of San Jose, 1 Cal. 3d 56, 62-63, 460 P.2d 137, 141, 81 Cal. Rptr. 465, 469 (1969), the court stated that the legislature is empowered neither to determine what constitutes a municipal affair nor to transform it into a statewide concern.

[69] 62 Cal. 2d 119, 396 P.2d 809, 41 Cal. Rptr. 393 (1964).

[70] *Id.* at 128, 396 P.2d at 815, 41 Cal. Rptr. at 399.

[71] For a discussion of the inherent confusion reflected in the divergent decisions reached by California courts on the preemptive issue, *see, e.g.*, Comment, *The California Preemption Doctrines: Expanding the Regulatory Power of Local Government*, 8 U.S.F. L. REV. 728, 730-32 (1974); and Sato, *Municipal Affairs*, *supra* note 65, at 1069-75.

[72] Realizing the dangers of a rigid rule, the court stated that changed conditions may transform what was once a matter of local concern into a matter of state concern. Bishop v. City of San Jose, 1 Cal. 3d 56, 63, 460 P.2d 137, 141, 81 Cal. Rptr. 465, 469 (1969).

relevant question in determining if the state has preempted local government's ability to levy an occupational tax on employees is whether the matter is of such paramount state concern that local taxation is impermissible. This question incorporates the first two parts of the *Hubbard* test. The third part of the test concerning the transient state citizen involves the mobility of citizens to seek employment, unencumbered by unnecessary barriers.

Section 50026 of the Government Code expressly states that an occupational tax is a matter of statewide interest and concern.[73] The legislature expressed its interest in the occupational tax in the context of the tax's possible restriction on the "rights of citizens to move freely about the state in search of employment."[74] The statute provides that no tax shall be imposed on nonresidents unless the same tax is imposed on residents.[75] This qualification impliedly approves occupational taxes and casts doubt on the proposition that the state has abrogated all local authority with respect to such taxes. If the legislature had intended a blanket prohibition on local occupational taxes, it could clearly have stated so. On the contrary, the legislature recognized that the state's interest in protecting its citizens' freedom of mobility could be given full effect as long as a local occupational tax is borne equally by residents and nonresidents.

Indeed, there is some doubt as to whether the state can preempt this area at all. One of the few cases which has challenged the validity of section 50026 concerned a San Francisco commuter tax that was imposed on nonresidents only.[76] While the court recognized that the precise tax at issue in the case was governed by section 50026, it did not base its holding on section 50026. Instead, the court chose the historically disfavored course of finding that the tax, as applied to nonresidents, was constitutionally deficient because it denied nonresidents equal protection under the law.[77] The court demonstrated

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[73] CAL. GOV'T CODE § 50026 (West Supp. 1977), set forth in note 52 *supra*.

[74] Ch. 559, § 3, 1968 Cal. Stat. 1014, adding CAL. GOV'T CODE § 50026 states that:

> The Legislature finds and declares that the right of citizens of California to move freely about the state in search of employment is a matter of statewide interest and concern. Any unnecessary barriers which impede the mobility of citizens of this state or limit their choice of employment are contrary to state policy. An occupation tax on employees measured by income which was not borne equally by residents and nonresidents of a taxing jurisdiction would be such a barrier.

[75] CAL. GOV'T CODE § 50026 (West Supp. 1977), set forth in note 52 *supra*.

[76] County of Alameda v. City and County of San Francisco, 19 Cal. App. 3d 750, 757, 97 Cal. Rptr. 175, 179 (1st Dist. 1971).

[77] *Id.* That the court chose to invalidate the tax because of its constitutional infirmity gives weight to the argument that the statute does not apply to charter cities. As a general rule, the constitutionality of an ordinance will not be considered where other grounds are available for the disposition of a case. *See* Estate of Johnson, 139 Cal. 532, 534, 73 P. 424, 425 (1903); *In re* Henry G.,

the limitation of section 50026 by implying that while the legislature may have intended to prohibit general law cities from enacting taxing ordinances like that imposed by San Francisco, it is questionable whether the legislature could prohibit or limit a charter city's inherent power of municipal taxation.[78] Arguably, since the court was unwilling to declare a charter city's taxing power preempted when its exercise was in direct violation of section 50026, it is unlikely to prohibit an occupational tax that conforms to the statute.

An issue raised by courts,[79] in considering whether an occupational tax is a matter of state-wide concern, is that the nonresidential occupational tax might produce retaliatory economic measures by neighboring cities; therefore, it is in the state's interest to prevent each city from creating an independent economic enclave.[80] Although this fear may be legitimate in the abstract, the experiences of numerous other states which impose similar taxes fail to support such a hypothesis. While there may be some retaliatory levies against a central city's imposition of an occupational tax, such opposition inevitably ceases once the citizenry and policymakers recognize the underlying reasons for the imposition of an occupational tax.[81] Those reasons include the fact that many central cities are experiencing severe fiscal crises that seriously affect their ability to continue to provide the quality of life which make cities a desirable place to work and live. In an effort to continue to provide an environment that is conducive to economic and social growth, nonresidents who

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28 Cal. App. 276, 278-79, 104 Cal. Rptr. 585, 586-87 (2d Dist. 1972); *accord*, Ashwander v. Valley Authority, 297 U.S. 288, 347 (1935).

[78] 19 Cal. App. at 757, 97 Cal. Rptr. at 179. This is not the first time the court has questioned the legislature's power to limit the authority of charter cities. In Ector v. City of Torrance, 10 Cal. 3d 129, 514 P.2d 433, 109 Cal. Rptr. 849 (1973), *cert. denied*, 415 U.S. 935 (1974), the court upheld a charter city's power to impose a residency requirement on municipal employees in violation of a state statute prohibiting such a requirement. The court found that charter cities have constitutionally established plenary power to prescribe residency requirements for municipal employees that may not be preempted by the state legislature. *Id.* at 132-33, 514 P.2d at 434-35, 109 Cal. Rptr. at 850-51. In City of Pasadena v. Charleville, 215 Cal. 384, 10 P.2d 745 (1932), involving a preemptive issue, the court found that the state legislature could not require a charter city to pay prevailing wages on municipal improvement contracts.

[79] *E.g.*, City of Los Angeles v. Shell Oil Co., 4 Cal. 3d 108, 119, 93 Cal. Rptr. 1, 7-8, 480 P.2d 953, 959-60 (1971), *cert. denied*, 404 U.S. 831 (1971); County of Alameda v. City and County of San Francisco, 19 Cal. App. 3d 750, 757, 97 Cal. Rptr. 175, 179 (1st Dist. 1971).

[80] One commentator suggests that an occupational tax will operate as a protective tariff thereby discriminating against goods and services from outside the city. This will result in retaliatory taxing measures being adopted by affected cities. This concern, however, may be alleviated by the use of an apportioned tax linked to the quantum of business conducted within the jurisdiction and by tax credits where an activity is exposed to double taxation. Sato, *Municipal Occupation Tax*, *supra* note 16, at 818.

[81] *See* SIGAFOOS, *supra* note 10, at 36-37.

reap benefits of the city's environment should be contributing to its continued existence. This policy should not be rejected summarily by speculative arguments of intercity economic warfare. Surely the economic effect that the financial collapse of a major central city would have on the surrounding communities would be greater than the imposition of occupational taxes by adjoining cities. State preemption should not be imposed as an economic straight jacket on the fiscal integrity of California central cities.

### C. *Local Authority to Levy an Income Tax*[82]

As discussed earlier, it is likely that an occupational tax measured by gross earnings receipts would not be characterized as an income tax by the courts.[83] Accepting, arguendo, that such a designation would fail and the tax is held to be an income tax, the state may lack the authority to preempt local income taxation in light of specific constitutional grants of power.

The California Supreme Court has recognized that the power to raise revenue through taxation is a municipal affair granted to charter cities by the California Constitution. In the leading case of *Ex parte Braun*,[84] the court stated that the power of charter cities to raise revenue for municipal purposes by taxation does not find its source in any grant from the legislature, but has been directly granted to them through constitutional provisions.[85] The courts have not decided if this constitutionally-granted taxing power includes the authority to levy a local income tax.[86]

The power to impose an income tax is derived from section 26 of article XIII of the California Constitution.[87] Section 26 is the only provision found in the state Constitution concerning income taxation. It implicitly authorizes California government to levy an income tax. However, section 26 does not expressly state which unit

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[82] Although an exhaustive analysis of this issue is beyond the scope of this article, the point is raised because no California decision has yet applied the state income tax preemptive doctrine to a municipal ordinance levying an occupational tax for revenue purposes only. For a more comprehensive treatment of the charter city's income taxing power, *see, e.g.*, Januta, *The Municipal Revenue Crisis: California Problems and Possibilities*, 56 CAL. L. REV. 1525 (1968) and Comment, *The Municipal Income Tax and State Preemption in California*, 11 SANTA CLARA LAW. 343 (1971).

[83] For the discussion of this proposition, *see* text and accompanying notes 51-62 *supra*.

[84] 141 Cal. 204, 74 P. 780 (1903).

[85] *Id.* at 211-12, 74 P. at 183.

[86] In Weekes v. City of Oakland, 64 Cal. App. 3d 907, 935, 134 Cal. Rptr. 858, 875 (1st Dist. 1976), the court had an opportunity to probe the question but chose to conclude that Oakland's occupational tax was more like a business license tax than an income tax.

[87] The section reads as follows: "Taxes on or measured by income may be imposed on persons, corporations, or other entities as prescribed by law."

of government may impose such a tax. It is debatable whether section 26 was intended to grant the power to levy income taxes to all governmental units in the state, including local governmental units, or whether it was intended only to apply to the state legislature.[88] The framers of the section could have expressly restricted the power to levy an income tax to the state legislature if that was their intent. There are numerous instances in article XIII where the state legislature is specifically identified and authorized to levy particular taxes.[89] Since section 26 does not expressly identify the state legislature, it can reasonably be inferred that other governmental units may also impose an income tax.

Section 33 of article XIII supplies further guidance for the exercise of the power to levy an income tax by declaring that the state legislature "shall pass all laws necessary to carry out the provision of this article." On its face, it would appear that section 33 gives the state legislature exclusive control over the power to levy an income tax. Yet such a reading of section 33 creates an anomalous result because article XIII contains a wide range of revenue and taxing matters, including taxing provisions which historically have been the primary domain of local government. For example, section 1 provides for the taxation of real property, while section 2 authorizes the taxation of personal property, areas in which municipalities have traditionally exercised taxing authority. If section 33 were given its literal reading, cities would have no authority to pass laws to carry out the provisions of section 1 and 2. Since section 33 of article XIII should not be interpreted to mean that charter cities cannot enact property tax ordinances, it should be concluded that section 33 does not give the state exclusive authority with respect to all other taxes enumerated in article XIII.[90]

A more plausible reading of the enforcement provision of section 33 is that the state Constitution vests charter cities with concurrent taxing authority by virtue of section 26, subject to the restrictions of the city's charter. Therefore, the legislative power under section 33 must be read in light of the constitutional grants given to charter

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[88] Many of the commentators conclude that the state legislature does not have exclusive income-taxing power. *See, e.g.*, Januta, *supra* note 82, at 1540-43; Comment, *supra* note 82, at 350-53; and Sato, *Municipal Affairs, supra* note 65, at 1098-105.

[89] *See, e.g.*, CAL. CONST. art. XIII, § 7 (exemption of certain realty of low value); § 15 (local disaster tax relief); § 20 (maximum local property tax rates and bonding limitations); § 21 (levy of school district tax); § 22 (limitations on property tax amount); and § 27 (taxation of banks and corporations).

[90] The proposition that express language is required to grant the legislature exclusive taxing power in an area is supported by case law. *See, e.g.*, Ainsworth v. Bryant 34 Cal. 2d 465, 472-73, 211 P.2d 564, 568 (1949); Territory of Alaska v. American Can Co., 246 F.2d 493, 489-499 (9th Cir. 1957).

cities,[91] which encompass the power to make and enforce all laws with respect to municipal affairs, including the power to tax for revenue purposes.[92] If the state legislature could preempt the constitutional taxing power vested in local government by simply passing a statute prohibiting such taxing authority, all constitutional powers of charter cities could be invalidated by legislative mandate. Such a proposition is untenable, since the constitutional provisions pertaining to charter cities expressly provide that their power is beyond the authority of the legislature to withdraw or modify.[93] Thus, it would appear that nothing in section 33 precludes a charter city from levying an occupational tax on gross earning receipts, even in the event that such a tax is labeled an income tax.

### *D. The Constitutional Right to Travel*

A final constitutional consideration is that the right to travel freely within the country is a privilege of national citizenship protected from state and local interference.[94] Arguably, nonresidents may challenge an occupational tax as an unlawful restriction on their right to travel because the imposition of such a tax deters them from seeking employment in the taxing city.

Generally, where a state law discriminates against nonresidents of the state and discourages their interstate movement, such a law burdens the fundamental right to travel and is unconstitutional unless the state can show that the classification furthers a compelling state interest in the least restrictive means possible.[95] While strict scrutiny is required in cases involving *interstate* travel, the state's burden is less onerous in restrictions on *intrastate* travel. In the leading California case, *Ector v. City of Torrence*,[96] involving a residency requirement for municipal employees, the court stated that there is no constitutional right to commute between one's home and place of em-

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[91] *See* constitutional provisions cited notes 63-64 *supra*.

[92] *Ex parte* Braun, 141 Cal. 204, 209-10, 74 P. 780, 783 (1903).

[93] CAL. CONST. art. XI § 8 (1879); Redwood Theaters, Inc. v. City of Modesto, 86 Cal. App. 2d 907, 911, 196 P.2d 119, 122 (1948).

[94] In United States v. Guest, 383 U.S. 745, 758 (1966), the court noted that:

> [The] right [to travel] finds no explicit mention in the Constitution. The reason, it has been suggested, is that a right so elementary was conceived from the beginning to be a necessary concomitant of the stronger Union the Constitution created. In any event, freedom to travel throughout the United States has long been recognized as a basic right under the Constitution.

[95] The leading case in this area is Shapiro v. Thompson, 394 U.S. 618, 634 (1969), in which a one-year residency requirement for welfare assistance was struck down on the grounds that such a requirement unduly inhibited the freedom of migration. *Accord*, Dunn v. Blumstein, 405 U.S. 330 (1972).

[96] 10 Cal. 3d 129, 514 P.2d 433, 109 Cal. Rptr. 849, (1973), *cert. denied* 415 U.S. 935 (1974). For a further discussion of the *Ector* decision, *see* Note, *Residency Requirement for Municipal Employees*, 62 CAL. L. REV. 434 (1974).

ployment.[97] The *Ector* court found the restriction on intrastate travel to be rationally related to several legitimate state purposes. These included the promotion of ethnic balance in the community, the reduction of unemployment, the improvement of the quality of employee job performance, the reduction of absenteeism among employees, and the general economic benefits that flow from local expenditure of employees' salaries.[98] The *Ector* decision demonstrated that intrastate mobility is not a fundamental right protected by either state or federal Constitution so as to preclude local legislation from reasonably restricting it. On the contrary, the court expressly reaffirmed the power vested in cities to restrict the freedom of intrastate travel when there is a rational basis for doing so.

The goal of insuring effective delivery of city services and maintaining fiscal integrity are as basic to city management as that of reducing unemployment, promoting ethnic balance, or reducing the absenteeism of city employees. It can hardly be disputed that the occupational tax is a rational means of promoting legitimate local goals. Certainly the reasons cited for imposing an occupational tax on nonresidents[99] are at least as legitimate as those enumerated by the *Ector* court. Therefore, an occupational tax would not fall prey to a constitutional challenge based on the right to travel.

## III. CONCLUSION

Today, central cities face economic crises that threaten their fiscal solvency. Their tax base is dwindling as the demands for services are increasing. The occupational tax provides a means of raising additional revenue to meet this urban crisis. The tax provides a means of support for vital city services that not only maintain the quality of urban life, but also provide an economic environment that enables nonresidents to secure and maintain a livelihood.

Through the exercise of its taxing power, a charter city may levy an occupational tax for the privilege of employment within the city. As a result of expansive statutory interpretation, such a tax may be imposed on virtually all employees within the municipality's geographical limits. To insure, however, that an ordinance imposing such a tax conforms to constitutional and statutory standards, certain safeguards must be incorporated.

An occupational tax should be measured by the gross earning receipts of the employee and administered in the form of payroll with-

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[97] *Id.* at 135, 514 P.2d at 436, 109 Cal. Rptr. at 852. *Accord,* Wardwell v. Board of Educ. of City School Dist., 529 F.2d 625, 627 (6th Cir. 1976), holds that the right to intrastate travel is not afforded federal constitutional protection and that the applicable test for cases involving intrastate travel restrictions is the "rational basis" standard.

[98] 10 Cal. 3d at 135, 514 P.2d at 436, 109 Cal. Rptr. at 852.

[99] *See* text accompanying notes 1-10 *supra.*

holding. The danger that such a tax would be construed as an income tax may be overcome by virtue of its application to gross earnings only. Moreover, charter cities may possess income taxing powers which would make such a tax valid even if it were held to be an income tax. State preemptive powers do not render an employee occupational tax nugatory. The state's interest in insuring its citizens equal protection under the law and freedom of mobility can be given full effect if the tax is applied to residents and nonresidents alike, and if the tax is apportioned when applied to part-time employees. Furthermore, the tax does not burden a federal constitutional right to travel, since intrastate travel is not a fundamental right protected by the Constitution.

Finally, the increased burden that nonresident employees place on the central city necessitates that it look beyond its boundaries for revenue. It is consistent with fundamental fairness that those who benefit from services should in fact pay for those services. An occupational tax is a realistic means of taxing nonresidents for the services they receive and provides a viable alternative for central cities to overcome their fiscal dilemma.

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