

TO CLARIFY STATE AUTHORITY TO TAX COMPENSATION  
PAID TO CERTAIN EMPLOYEES

JULY 25, 1997.—Committed to the Committee of the Whole House on the State of  
the Union and ordered to be printed

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Mr. HYDE, from the Committee on the Judiciary,  
submitted the following

R E P O R T

[To accompany H.R. 1953]

[Including cost estimate of the Congressional Budget Office]

The Committee on the Judiciary, to whom was referred the bill (H.R. 1953) to clarify State authority to tax compensation paid to certain employees, having considered the same, report favorably thereon without amendment and recommend that the bill do pass.

PURPOSE AND SUMMARY

H.R. 1953 provides that the income of certain employees at specific federal facilities located astride three state boundaries is to be taxed by the State or political subdivision thereof of which the employee is a resident. The bill addresses unique situations in which residents of one state travel onto a federal facility for their employment which, while still within that federal facility, is technically across a border into another state. The bill applies to: employees at Fort Campbell, Kentucky, located astride Kentucky and Tennessee; and federal employees at federal hydroelectric facilities along the Columbia River between Washington and Oregon, as well as a federal hydroelectric facility along the Missouri River between South Dakota and Nebraska.

BACKGROUND AND NEED FOR THE LEGISLATION

The Committee recognizes that the right of States to tax economic activities within their borders should be granted great deference and that Congress should intervene only in unusual circumstances such as those that were found to exist in the three areas addressed by H.R. 1953.

State taxation of income derived from a federal governmental unit has been accepted by the courts only in relatively recent times. Initially, Chief Justice John Marshall had found in the power to tax “the power to destroy”<sup>1</sup> and courts for more than a century afterwards held that the federal government and its properties, functions and instrumentalities enjoyed an implied immunity under the Constitution from state taxation. In *Graves v. New York ex rel. O’Keefe*,<sup>2</sup> however, the Supreme Court ceased to recognize this implied immunity from taxation by the states of personal income merely because the source was the federal government, although it did not rule on the question of whether Congress could expressly exempt such income from state taxation. With respect to the related question of state taxation of nonresidents generally, the Supreme Court had earlier upheld imposition of such a tax in *Shaffer v. Carter*,<sup>3</sup> although that decision obviously did not apply to federal employees who were at the time immune from state taxation.

Notwithstanding *Graves*, however, the Supreme Court has upheld the power of Congress to grant express tax immunity to its employees<sup>4</sup> and contractors<sup>5</sup> when it determines such immunity is necessary to carry out an enumerated constitutional power. Over the years, several express exemptions have been enacted. The Soldiers’ and Sailors’ Civil Relief Act of 1940<sup>6</sup> provides that a member of the military does not lose his residence or domicile in any State solely by reason of his absence therefrom pursuant to military orders, nor is he deemed to have acquired a residence or domicile in any State to which he happens to be assigned to duty merely because of his presence in that State and absence from his original state of residence. The Act furthermore provides that the military compensation of such individual is immune from state nonresident taxation.<sup>7</sup>

In 1977, Congress enacted an exemption for its own members similar to that for military personnel.<sup>8</sup> That law provides that no state, or political subdivision thereof, in which a member of Congress maintains an abode for purposes of attending sessions of Congress may, for purposes of any income tax, treat such a member as a resident or domiciliary of such State or treat any compensation paid by the United States to such a member as income for services performed within or from sources within such State.<sup>9</sup>

Congress, moreover, has created express exemptions for non-Federal employees. In 1990, Congress enacted as a part of the Amtrak Reauthorization and Improvement Act<sup>10</sup> an exemption for certain

<sup>1</sup>*McCulloch v. the State of Maryland*, 17 U.S. 316 (1819).

<sup>2</sup>*Graves v. New York ex rel. O’Keefe*, 306 U.S. 466 (1939).

<sup>3</sup>*Shaffer v. Carter*, 252 U.S. 37 (1920).

<sup>4</sup>*Dameron v. Broadhead, Manager of Revenue & Ex-Officio Treasurer of the City & County of Denver*, 345 U.S. 322 (1953).

<sup>5</sup>*Carson, Commissioner of Finance & Taxation v. Roane-Anderson Co.*, 342 U.S. 232 (1952).

<sup>6</sup>50 U.S.C. app. § 590 et seq.

<sup>7</sup>This exemption was upheld by the Supreme Court in *Dameron v. Broadhead*, supra note 4.

<sup>8</sup>4 U.S.C. §113.

<sup>9</sup>The provision was upheld in *U.S. v. Maryland*, 488 F. Supp. 347 (D. Md., 1988), affirmed 636 F. 2d 73, which concluded that Congress had determined that taxing members of Congress in the states they represent as well as the state in which they reside while serving in Washington, D.C. was a burden on the fulfillment of a Federal function. The court noted that Congress had not exempted its members from all state taxation, but rather had merely determined which state could tax their income.

<sup>10</sup>Pub. L. No. 101-322.

interstate transportation workers who perform regularly assigned duties in more than one state. Under that Act, such workers are subject to income tax only in the state of their residence.<sup>11</sup>

During the 104th Congress, Public Law 104-95 limited states in taxing the pension income of their expatriate nonresidents. The rationale for that law was in part that the nonresident no longer had a contact with his state of former residence sufficient to justify such taxation and that the record-keeping required to determine what deferred income was attributable to which state of former residence was onerous and impractical.

H.R. 1953 applies to unique geographical areas owned by the federal government sitting astride states with differing taxation schemes (one state with an income tax, the other without one). Because of the isolated nature and geographical idiosyncrasies of the federal facilities involved, a small number of workers enter the facility from their home state but, because these facilities are bisected by state boundaries, their work takes them over the state line and brings them under the taxing authority of the neighboring state. As a result, these workers must pay income taxes to that neighboring state even though they never actually use its roads or other services, nor are they entitled to avail themselves of benefits from that state on the same basis as residents.<sup>12</sup> Unlike most states, the two neighboring states lack reciprocal tax agreements that would credit residents for income taxed in the neighboring state. Perhaps because so few people are affected, the states in these cases have not moved to address these workers' problem.<sup>13</sup>

In addressing the question presented by this situation, the Committee concluded that this legislation is justified by the combination of highly unusual geography, the inability of the states to work out an equitable reciprocity agreement, and the fact that these workers can be said to have "worked" in the neighboring state only in the narrowest and most technical sense. The Committee believes H.R. 1953 meets the elevated threshold which has been set by the Congress for preempting state taxing authority.

H.R. 1953 applies to "federal" employees at the federal hydroelectric facilities because workers at these facilities are employed by the United States Army Corps of Engineers. With respect to Fort Campbell, the bill applies to "employee[s]" because many of those working at that federal facility are civilians not employed by, but rather contracted to, the Federal government. These contract employees perform similar services and, thus are similarly situated, as the federal employees with whom they work.

As noted, the Committee does not intend that its action in these unusual circumstances be taken as a precedent for other areas that might arise in a dispute between various states, as it is primarily the duty of these states to develop among themselves rational pro-

<sup>11</sup> See, 49 U.S.C. §§11504 (a)-(c).

<sup>12</sup> State Taxation of Employees at Certain Federal Facilities: Hearing on H.R. 865 and H.R. 874 Before the Subcomm. on Commercial and Administrative Law of the House Comm. on the Judiciary, 105th Cong., 1st Sess. (1997) (statement of Edwin Wilson, an employee at Fort Campbell).

<sup>13</sup> The Committee notes with approval the passage by the Oregon legislature, after some delay, of S.B. 998 addressing the situation of Washington residents working at federal hydroelectric facilities on the Columbia River. The legislation awaits signature by the Governor.

cedures to insure that their respective citizenry are treated equitably.

#### HEARINGS

The Committee's Subcommittee on Commercial and Administrative Law held a hearing on April 17, 1997 on two related bills, H.R. 865 and H.R. 874. The first panel of witnesses was composed of congressional members representing the States of Tennessee and two constituents, including: Rep. Ed Bryant, Sen. Fred Thompson, Mr. Worth Lovett and Mr. Edwin Wilson both of Clarksville, Tennessee. The second panel of witnesses was composed of congressional members from the State of Washington and their constituents, including: Rep. Doc Hastings, Rep. Linda Smith, Mr. Dwight Campbell of Goldendale, Washington, and Mr. Roger Hays of Kennewick, Washington. The third panel of witnesses was composed of a tax consultant, a union representative, a representative of state tax administrators and an expert on state taxation, including: Ms. Joy Wilen, of Vancouver, Washington; Mr. James Cunningham, President, The National Federation of Federal Employees; Mr. James C. Smith, Professor, The University of Georgia School of Law, Athens, Georgia and Mr. Harley T. Duncan, Executive Director, The Federation of Tax Administrators.

#### COMMITTEE CONSIDERATION

On June 19, 1997, the Subcommittee on Commercial and Administrative Law met in open session and ordered reported the bill H.R. 1953, by a voice vote, a quorum being present. On July 16, 1997, the Committee met in open session and ordered reported favorably the bill H.R. 1953 without amendment by a voice vote, a quorum being present.

#### VOTE OF THE COMMITTEE

There were no recorded votes.

#### COMMITTEE OVERSIGHT FINDINGS

In compliance with clause 2(1)(3)(A) of rule XI of the Rules of the House of Representatives, the Committee reports that the findings and recommendations of the Committee, based on oversight activities under clause 2(b)(1) of rule X of the Rules of the House of Representatives, are incorporated in the descriptive portions of this report.

#### COMMITTEE ON GOVERNMENT REFORM AND OVERSIGHT FINDINGS

No findings or recommendations of the Committee on Government Reform and Oversight were received as referred to in clause 2(1)(3)(D) of rule XI of the Rules of the House of Representatives.

#### NEW BUDGET AUTHORITY AND TAX EXPENDITURES

Clause 2(1)(3)(B) of House Rule XI is inapplicable because this legislation does not provide new budgetary authority or increased tax expenditures.

## CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

In compliance with clause 2(1)(3)(C) of rule XI of the Rules of the House of Representatives, the Committee sets forth, with respect to the bill, H.R. 1953, the following estimate and comparison prepared by the Director of the Congressional Budget Office under section 403 of the Congressional Budget Act of 1974:

U.S. CONGRESS,  
CONGRESSIONAL BUDGET OFFICE,  
*Washington, DC, July 24, 1997.*

Hon. HENRY J. HYDE,  
*Chairman, Committee on the Judiciary,  
House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 1953, a bill to clarify state authority to tax compensation paid to certain employees.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contacts are Mark Grabowicz (for federal costs) and Leo Lex (for the state and local impact).

Sincerely,

JUNE E. O'NEILL, *Director.*

Enclosure.

*H.R. 1953—A bill to clarify state authority to tax compensation paid to certain employees*

CBO estimates that enacting this legislation would have no impact on the federal budget. Because the bill would not affect direct spending or receipts, pay-as-you-go procedures would not apply. H.R. 1953 would impose an intergovernmental mandate because it would limit the ability of certain states to collect income taxes from some individuals working in those states. CBO estimates that the costs of this mandate would total less than \$5 million annually and thus would not exceed the threshold established in the Unfunded Mandates Reform Act of 1995 (UMRA). H.R. 1953 contains no new private-sector mandates as defined in UMRA.

H.R. 1953 would allow states to tax incomes of federal employees working at certain federal facilities only if those employees are residents of the state. This legislation would preclude three states from collecting taxes from employees who work in those states but live in another. This limitation on taxing authority would be an intergovernmental mandate as defined in UMRA. About 2,350 employees at three federal facilities would be affected by the bill, and the relevant state income tax rates range from 2 percent to 9 percent. Assuming an average annual salary of \$30,000, CBO estimates that the costs of this mandate would be less than \$5 million annually.

The CBO staff contacts for this estimate are Mark Grabowicz (for federal costs), who can be reached at 226-2860, and Leo Lex (for the state and local impact), who can be reached at 225-3220. This estimate was approved by Robert A. Sunshine, Deputy Assistant Director for Budget Analysis.

## CONSTITUTIONAL AUTHORITY STATEMENT

Pursuant to rule XI, clause 2(1)(4) of the Rules of the House of Representatives, the Committee finds the authority for this legislation in Article I, section 8 of the Constitution.

## SECTION-BY-SECTION ANALYSIS

## SECTION 1. LIMITATION ON STATE AUTHORITY TO TAX COMPENSATION PAID TO INDIVIDUALS PERFORMING SERVICES AT FORT CAMPBELL, KENTUCKY

Subsection (a) amends Title 4, United States Code, adding a new section 115 which provides that pay and compensation paid to an individual for personal services at Fort Campbell, Kentucky shall be taxed by the State or any political subdivision thereof of which that individual is a resident.

Subsection (b) contains a conforming amendment to the table of sections for Chapter 4 of Title 4, United States Code.

Subsection (c) provides that amendments made by this section shall apply to pay and compensation paid after the date of enactment.

## SEC. 2. CLARIFICATION OF STATE AUTHORITY TO TAX COMPENSATION PAID TO CERTAIN FEDERAL EMPLOYEES

Subsection (a)(1) contains a technical amendment to Section 111 of Title 4, United States Code.

Subsection (a)(2) amends Section 111 of Title 4, United States Code (which consents generally to state taxation of federal employees) by adding at the end a new subsection (b): which provides that pay or compensation paid by the United States for personal services as an employee of the United States at a hydroelectric facility owned by the United States on the Columbia River, portions of which are within the states of Oregon and Washington, shall be subject to taxation by the State or political subdivision thereof of which such employee is a resident; and a new subsection (c): which provides that pay or compensation paid by the United States for personal services as an employee of the United States at a hydroelectric facility owned by the United States on the Missouri River, portions of which are in the states of South Dakota and Nebraska, shall be subject to taxation by the State or any political subdivision thereof of which such employee is a resident.

Subsection (b) provides that amendments made by subsection (a) shall apply to pay and compensation paid after the date of enactment.

## AGENCY VIEWS

No agency views were received on H.R. 1953.

## CHANGES IN EXISTING LAW MADE BY THE BILL, AS REPORTED

In compliance with clause 3 of rule XIII of the Rules of the House of Representatives, changes in existing law made by the bill, as reported, are shown as follows (new matter is printed in italic and existing law in which no change is proposed is shown in roman):

**TITLE 4, UNITED STATES CODE**

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**CHAPTER 4—THE STATES**

Sec.

101. Oath by members of legislatures and officers.

\* \* \* \* \*

115. *Limitation on State authority to tax compensation paid to individuals performing services at Fort Campbell, Kentucky.*

\* \* \* \* \*

**§ 111. Same; taxation affecting Federal employees; income tax**

(a) *GENERAL RULE.*—The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States, a territory or possession or political subdivision thereof, the government of the District of Columbia, or an agency or instrumentality of one or more of the foregoing, by a duly constituted taxing authority having jurisdiction, if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation.

(b) *TREATMENT OF CERTAIN FEDERAL EMPLOYEES EMPLOYED AT FEDERAL HYDROELECTRIC FACILITIES LOCATED ON THE COLUMBIA RIVER.*—Pay or compensation paid by the United States for personal services as an employee of the United States at a hydroelectric facility—

- (1) which is owned by the United States,
- (2) which is located on the Columbia River, and
- (3) portions of which are within the States of Oregon and Washington,

shall be subject to taxation by the State or any political subdivision thereof of which such employee is a resident.

(c) *TREATMENT OF CERTAIN FEDERAL EMPLOYEES EMPLOYED AT FEDERAL HYDROELECTRIC FACILITIES LOCATED ON THE MISSOURI RIVER.*—Pay or compensation paid by the United States for personal services as an employee of the United States at a hydroelectric facility—

- (1) which is owned by the United States,
- (2) which is located on the Missouri River, and
- (3) portions of which are within the States of South Dakota and Nebraska,

shall be subject to taxation by the State or any political subdivision thereof of which such employee is a resident.

\* \* \* \* \*

**§ 115. Limitation on State authority to tax compensation paid to individuals performing services at Fort Campbell, Kentucky**

*Pay and compensation paid to an individual for personal services at Fort Campbell, Kentucky, shall be subject to taxation by the State*

*or any political subdivision thereof of which such employee is a resident.*

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