A state imposes a tax on the "income" of each of its residents. As defined in the taxing statute, "income" includes the fair rental value of the use of any automobile provided by the taxpayer's employer for the taxpayer's personal use.

The federal government supplies automobiles to some of its employees who are residents in the state so that they may perform their jobs properly. A federal government employee supplied with an automobile for this purpose may also use it for the employee's own personal business.

Assume there is no federal legislation on this subject.

May the state collect this tax on the fair rental value of the personal use of the automobiles furnished by the federal government to these employees?

A. No, because such a tax would be a tax on the United States.

B. No, because such a tax would be a tax upon activities performed on behalf of the United States, since the automobiles are primarily used by these federal employees in the discharge of their official duties.

C. Yes, because an exemption from such state taxes for federal employees would be a denial to others of the equal protection of the laws.

D. Yes, because the tax is imposed on the employees rather than on the United States, and the tax does not discriminate against persons who are employed by the United States.

Explanation:

Federal immunity from state & local taxes/regulations

Tax/regulation	**Definition**	**Permissibility**
Direct	Applies to federal government—including its agencies & instrumentalities	*Immune* unless: • Congress consents to tax/regulation
Indirect	Applies to affiliates—including persons/entities employed by or doing business with federal government	*Not immune* unless: • Congress grants immunity *or* • tax/regulation discriminates against or substantially interferes with federal duties

Under the Article VI **supremacy clause**, states are prohibited from taxing the federal government—including its agencies and instrumentalities—without congressional consent. But **states can tax** the **federal government's affiliates**—including federal employees (as seen here)—**unless**:

- **Congress has granted** the affiliate **immunity**
- the **tax discriminates** against the federal government or its affiliates *or*
- the **tax substantially interferes** with the affiliate's ability to accomplish its **federal purpose or duties**.

Here, the state seeks to collect an income tax on the value of the personal use of employer-provided automobiles from federal employees (not the U.S. government) **(Choice A)**. Congress did not grant these employees immunity, and the tax is nondiscriminatory since it applies to automobiles provided by *any* employer. Additionally, the tax does not substantially interfere with the employees' federal duties since it only applies to their personal use of the automobiles. Therefore, the state may collect this tax from the federal employees.

(Choice B) Although the automobiles may primarily be used by these federal employees in the discharge of their *official* duties, the tax only applies to *personal* use of the automobiles. Therefore, it is not a tax upon activities performed on behalf of the United States.

(Choice C) Under the equal protection clause, state actions that do not substantially impact a fundamental right or intentionally discriminate against a protected class (as seen here) are subject to mere rational basis scrutiny. State action almost always satisfies this standard, so a tax exemption for federal employees would likely be sustained under this clause.

Educational objective:

States can tax the affiliates of the federal government unless (1) Congress has granted the affiliate immunity, (2) the tax is discriminatory, or (3) the tax substantially interferes with the affiliate's federal purpose or duties.

References

- Graves v. New York, 306 U.S. 466, 486–87 (1939) (holding that a state income tax imposed on federal employees is not an unconstitutional burden).