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Madeline Tewes Lee

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NOTE

AD VALOREM TAXATION—COMPOUNDING THE PROBLEM IS NO SOLUTION: *HANLEY V. KUSPER*

Under the constitution of 1870, all personal property in Illinois was subject to taxation by valuation.¹ In actuality, however, the property was assessed by varying standards throughout the state, and the tax was collected primarily outside Cook County.² Recognizing the unfairness of the tax, the General Assembly proposed a constitutional amendment, article IX-A, to prohibit the taxation *as to individuals*.³ Following approval by the voters, the article was incorporated into the constitution of 1970 as part of a general plan to abolish all ad valorem personal property taxation by 1979.⁴ Extensive litigation ensued to determine the constitutionality of article IX-A and to designate which property remained subject to tax. The first case, *Lake Shore Auto Parts Co. v. Korzen*,⁵ culminated in a per curiam decision that corporations, partner-

1. ILL. CONST. art. IX (1870).

2. SIXTH ILLINOIS CONSTITUTIONAL CONVENTION, 3 RECORD OF PROCEEDINGS 2039 (1970) [hereinafter cited as PROCEEDINGS].

3. As originally introduced, Senate Joint Resolution No. 30 would have completely abolished the ad valorem system of personal property taxation. S. JOUR., 76th Ill. Gen. Assembly 1038 (April 29, 1969). The phrase "as to individuals" was added prior to the adoption of the resolution. *Id.* at 1407 (May 15, 1969). In this form the legislature approved the resolution and voted to submit it to the electorate. *Id.* at 3476 (June 30, 1969). As adopted, the constitutional provision states that "[n]otwithstanding any other provision of this Constitution, the taxation of personal property by valuation is prohibited as to individuals." ILL. CONST. art. IX-A, §1 (1870).

4. ILL. CONST. art. IX, §5(b)-(c). The new constitution stated that "[a]ny ad valorem personal property tax abolished on or before the effective date of this constitution shall not be reinstated." ILL. CONST. art. IX, §5(b). The effective date of Article IX-A was prior to the effective date of the constitution. For a comprehensive discussion of these provisions, see Kamin, *Constitutional Abolition of Ad Valorem Personal Property Taxes: A Looking-Glass Book*, 60 ILL. B.J. 432 (1972). See text accompanying notes 76-79 *infra*.

5. 49 Ill.2d 137, 273 N.E.2d 592 (1971), *rev'd sub nom.*, *Lehnhausen v. Lake Shore Auto Parts*, 410 U.S. 356, *on remand*, 54 Ill.2d 237, 296 N.E.2d 342 (per curiam), *cert. denied*, 414 U.S. 1039 (1973). *Lake Shore Auto Parts*, a corporation, brought suit against the County Clerk of Cook County, the county assessor, the members of the board of appeals, and the Director of the Illinois Department of Local Government Affairs. The company alleged that it represented itself and all members of a class composed of corporations and "non-individuals" subject to personal property tax. The plaintiffs asserted that the fourteenth amendment to the United States Constitution had been violated in that they were denied the equal protection of the laws. Declaratory relief and an injunction were sought and granted by the trial court. 49 Ill.2d 137, 141, 273 N.E.2d 592, 594 (1971). Eugene Maynard, "a natural person, citizen and taxpayer of the state of Illinois," filed and

ships, joint ventures, professional associations, and professional service corporations were subject to taxation. In the dicta of that opinion, the Illinois Supreme Court concluded that trustees and other fiduciaries were not exempted from taxation.

This ruling was recently modified in *Hanley v. Kusper*.⁶ In *Hanley*, the court ruled that property held in an involuntary fiduciary relationship, in which the natural person who owns the property is prevented by law from dealing with it as a natural person, is constitutionally exempt from the personal property tax. The three basic events which create these involuntary fiduciary relationships are the designation of an administrator or executor to settle a decedent's estate, the appointment of a conservator to protect the property of an incompetent, and the establishment of a guardianship to manage the property of a minor. Since these three exceptions constitute only a small portion of fiduciary relationships, most property held in trust remains subject to ad valorem taxation.

received leave to file an original action in the Supreme Court of Illinois on behalf of himself and one high school and three grade school districts which were afraid of lost revenue if the amendment were upheld. The action was filed against those defendants mentioned in the first case. The stated purpose in bringing the action was to represent those who owned non-business property to ensure that the issues would be fully litigated. *Id.* at 142, 273 N.E.2d at 594-95. A complaint was filed for declaratory judgement by Clemens Shapiro, a natural person who owned personal property in his own name, none of which was used for business purposes; Jerome Hartman, a natural person who was a sole proprietor; Guy S. Ross and Eugene Ross, who owned a partnership; and M. Weil and Sons, a corporation. The suit was dismissed as to all plaintiffs except Shapiro and his class. The trial court issued an order that article IX-A

is free of the ambiguity and uncertainty of intentment charged by the plaintiffs, and . . . its intentment is clearly declared to prohibit the taxation of personal property by valuation exclusively as to natural persons, where that property is used, by them, for the personal enjoyment of themselves and their families.

Id. at 144, 273 N.E.2d at 596. All three cases were consolidated on appeal where the Illinois Supreme Court concluded that the "meaning of article IX-A is that *ad valorem* taxation of personal property owned by a natural person or by two or more natural persons as joint tenants or tenants in common is prohibited." *Id.* at 148, 273 N.E.2d at 597. The court then held that such a classification, based solely on the ownership of property, is a violation of the equal protection clause. Justice Davis, dissenting, addressed the ownership issue and concluded that there was sufficient difference between a business owned by a natural person and a corporation to find that the classification was not an invidious discrimination. *Id.* at 162, 273 N.E.2d at 605. Two years later, the United States Supreme Court granted *certiorari* and reversed, noting that for equal protection purposes great discretion is allowed the state to tax corporations and individuals on different bases. *Lehnhausen v. Lake Shore Auto Parts Co.*, 410 U.S. 356 (1973). On remand, the Illinois Supreme Court issued its *per curiam* decision. *Lake Shore Auto Parts Co. v. Korzen*, 54 Ill.2d 237, 296 N.E.2d 342 *cert. denied*, 414 U.S. 1039 (1973).

6. 61 Ill.2d 452, 337 N.E.2d 1 (1975).

In making its decision, the *Hanley* court was faced with two options: it could classify personal property held in trust for the benefit of a natural person as property of an individual, or it could consider that property as the possession of a non-individual. Because the court chose the second option, personal property held for the benefit of a natural person remains taxable unless it is held in an involuntary fiduciary relationship.

In so ruling, the *Hanley* court expressly ignored a 1974 Illinois statute⁷ which exempted from taxation all personal property held for the exclusive benefit of a natural person. This legislation had been presented to the court solely for the purpose of demonstrating that the General Assembly had intended to abolish taxation of trust property when it drafted article IX-A.⁸ The court disagreed with this interpretation of the intended effect of the amendment. Consequently, the statute now is ineffective to the extent it exempts personal property held in voluntary fiduciary relationships from ad valorem taxation.

This Note will demonstrate that the court erred in its interpretation of article IX-A and mistakenly decided that trust property held voluntarily for the benefit of natural persons is taxable. Further, some ramifications of the decision, which may include serious injury to the utilization of the trust in Illinois and consequent harm to the trust industry, will be examined.

THE COURT'S DECISION: A CRITICAL ANALYSIS OF THE REASONING PROCESS

In interpreting a constitutional provision, a court is influenced primarily⁹ by the voters' understanding,¹⁰ the framers' intent,¹¹ legislative construction,¹² and stare decisis.¹³ In most instances, a thorough exami-

7. ILL. REV. STAT. ch. 120, §500.21(b) (1975).

8. Complaint for Plaintiff at 5, *Continental Ill. Bank and Trust Co. v. Kusper*, Docket No. 74L14739 (Cir. Ct. Cook Cty. Ill., filed Sept. 11, 1974).

9. Federal and state constitutional constraints, opinions of the attorneys general, and policy considerations may also have considerable impact. See notes 66-70 and accompanying text *infra*.

10. See *Wolfson v. Avery*, 6 Ill.2d 78, 88, 126 N.E.2d 701, 707 (1955); *People v. Stevenson*, 281 Ill. 17, 25, 117 N.E. 747, 750 (1917); *Burke v. Snively*, 208 Ill. 328, 344, 70 N.E. 327, 331 (1904); *City of Beardstown v. City of Virginia*, 76 Ill. 34, 41 (1875). The term voters' understanding is used throughout this Note to indicate that meaning which the voter attached to the language of the provision in deciding whether or not to vote to enact the amendment. See text accompanying notes 10-25 *infra*.

11. See *Wolfson v. Avery*, 6 Ill.2d 78, 88-89, 126 N.E.2d 701, 710 (1955); *People ex rel. McDavid v. Barrett*, 370 Ill. 478, 480, 19 N.E.2d 356, 358 (1939).

12. See *People v. Kelly*, 347 Ill. 221, 231, 179 N.E. 898, 902 (1932); *Hubbard v. Dunne*, 276 Ill. 598, 615, 115 N.E. 210, 216 (1917); *Nye v. Foreman*, 215 Ill. 285, 288, 74 N.E. 140, 141 (1905).

13. See *Maki v. Frelk*, 40 Ill.2d 193, 196-97, 239 N.E.2d 445, 447 (1968); *Heimgaertner v. Benjamin Elec. Mfg. Co.*, 6 Ill.2d 152, 167, 128 N.E.2d 691, 699 (1955).

nation of one or all of these interpretive factors would lead to a correct understanding of the constitutional provision. Unfortunately, the *Hanley* court did not use these tools correctly in interpreting the constitution. A proper use of these analytical factors would have led to the conclusion that ad valorem taxation of trust property held for the exclusive benefit of one or more natural persons was abolished by article IX-A.

Voters' Understanding

The Illinois Supreme Court has stated repeatedly that the primary object of inquiry in construing the language of a constitutional provision is the understanding of the voters who adopted the amendment.¹⁴ Unfortunately, no accurate means exist to discover the voters' subjective understanding.¹⁵ Therefore, examining the explanatory materials available to the voters at the time of the referendum is the best method of objectively determining their understanding.¹⁶ In this instance, those materials were the official explanation of the amendment and the arguments favoring and opposing adoption, copies of which were mailed to every registered voter.¹⁷

Previous judicial emphasis on the importance of the voters' understanding¹⁸ indicates that the *Hanley* court should have scrutinized all the available material to determine accurately the electorate's understanding. The court in *Hanley*, however, examined only the Explanation. The Explanation stated:

[T]he amendment would abolish the personal property tax by valuation levied against individuals. It would not affect the same tax levied

14. See cases cited note 10 *supra*.

15. No official record exists of the construction that a single voter gave to the wording in deciding whether to reject or to ratify the provision.

16. *Wolfson v. Avery*, 6 Ill.2d 78, 88-9, 126 N.E.2d 701, 707-08 (1955).

17. Senate Joint Resolution No. 43 provided that five members of each house would be appointed to prepare a brief explanation of the amendment, a brief argument in favor of the amendment, and the form in which the amendment would appear on the ballot; likewise, five members of each house were to prepare a brief argument against the amendment. S. JOUR., 76th Ill. Gen. Assembly 3479 (June 30, 1969). In actuality, only four members of the Senate and three members of the House participated in the preparation of the Majority Argument; three members of each house assisted in the formulation of the Minority Argument. *Id.* at 3535 (June 30, 1969). This resolution was passed under the authority of ILL. REV. STAT. ch. 7½, §§1-12 (1975). That act requires that the General Assembly prepare a brief explanation, a brief argument, and the form in which the amendment appears on the ballot. The Minority Argument is optional, but if prepared, the Secretary of State is required to include it in the pamphlet which is sent to the voters. *Id.* at §2.

18. See cases cited note 10 *supra*.

against corporations and other entities not considered in law to be individuals.¹⁹

Because the Explanation contained no specific reference to the taxability of property held by a fiduciary, it should be read with the Majority and the Minority Arguments as a single integrated document, each part contributing meaning to the whole.²⁰ The Minority Argument is particularly important because it contains the only mention of trusts in the entire publication. The Argument explains:

[T]hat which is owned by or held in a fiduciary capacity for the benefit of natural persons is exempted from taxes; that which is owned by corporations, etc., is subject to taxes.²¹

With this simple statement, the Minority Argument clearly established that the taxation of trust property had been abolished. Hence, as the voters sequentially scanned the material, they could have relied on the Minority Argument to resolve any confusion created by reading the Explanation and to provide a basis for their understanding of the proposed amendment.

The *Hanley* court refused to give any weight to the Minority Argument for two reasons. First, the court feared that any reliance upon the Minority Argument would allow the substitution of the minority's intention for the voters' purpose.²² This attempt to shield the electorate from any forced allegiance to a partisan viewpoint expressed by the minority to discourage adoption of the amendment is wise and commendable. However, the court failed to distinguish between those statements which were an accepted legislative interpretation of the amendment's meaning

19. S. JOUR., 76th Ill. Gen. Assembly 4203 (May 7, 1970). The Illinois Supreme Court based its original interpretation of the amendment upon this explanation in *Lake Shore Auto Parts v. Korzen*, 49 Ill.2d 137, 273 N.E.2d 592 (1971).

20. In construing a document, any single portion is meaningful only in its context.

As a constitution is dependent upon adoption by the people, the language used will be understood in the sense most obvious to the common understanding. The language and words of a constitution, unless they be technical words and phrases, will be given effect according to their usual and ordinary signification, and courts will not disregard the plain and ordinary meaning of the words used to search for some other conjectural intention.

People v. Stevenson, 281 Ill. 17, 26, 117 N.E. 747, 750 (1917). Presumably the same philosophy would apply to the materials sent to the voters, and they would be given their common understanding: one document with each section contributing meaning to the whole.

21. S. JOUR., 76th Ill. Gen. Assembly 4203 (May 7, 1970).

22. 61 Ill.2d at 460, 337 N.E.2d at 5.

and those which were included by the minority to persuade the electorate to reject the amendment. The statement in the Minority Argument regarding the taxation of trust property was adopted by the General Assembly as a statement of interpretation; the court incorrectly excluded it as a statement of persuasion. Additionally, some members of the electorate may have been motivated to vote for the amendment solely because personal property held for the benefit of a natural person would be exempt. The court frustrated the purpose of those voters by ignoring their understanding of the amendment.

The court's second reason for not relying on the Minority Argument was that it had never done so previously.²³ Very few proposed constitutional revisions have been adopted,²⁴ and the inclusion of a minority argument is optional. Therefore, no court had ever been confronted with the opportunity to consider such an argument. Unfortunately, the court in *Hanley* created a precedent of declining to review any minority argument. By rejecting an important portion of the explanatory materials sent to the electorate, it failed to inquire fully into the voters' understanding. Thus, the judicial respect traditionally accorded to the electorate's wishes²⁵ was not granted.

Framers' Intent

Four statements made by the legislature must be analyzed to discover the framers' intent: the Majority Argument, the Minority Argument, the Explanation, and Senate Joint Resolution No. 67.²⁶

The Majority Argument revealed that the General Assembly proposed article IX-A in order to remove an unjust and unfair personal property

23. *Id.* California also provides that a publication consisting of the amendment, an explanation, and arguments for or against the amendment be mailed to the electorate. Quoting *Helping Hand Home for Children v. San Diego*, 26 Cal.App.2d 452, 456, 79 P.2d 778, 781 (4th Dist. 1938), a California court noted in construing a constitutional provision that "the courts may properly resort to the records of debate in legislative bodies or constitutional conventions or to the arguments made to the electors in the submission of propositions for adoption, in order to ascertain which of the alternatives and admissible meanings should be ascribed to the language used." *Baumbaugh v. San Diego County*, 44 Cal.App.2d 898, 901-02, 113 P.2d 218, 220 (1941).

24. Only 15 of 36 proposed amendments to the constitution of 1870 were passed by the electorate. Of the 15 amendments which have been adopted, only 8 have been approved since 1908. STATE OF ILLINOIS, CONSTITUTION OF THE STATE OF ILLINOIS AND UNITED STATES, 9-11 (1970).

25. See note 10 *supra*.

26. Senate Joint Resolution No. 67 was adopted after the preparation of the Explanation and Arguments to indicate the legislature's intended meaning of the phrase "as to individuals." S. JOUR., 76th Ill. Gen. Assembly 4405 (May 19, 1970).

taxation system of individuals.²⁷ The majority did not directly address the issue of taxation of property held by fiduciaries. It should be noted, however, that each argument which was advanced in support of the amendment appears to apply equally to personal property held in trust for individuals.²⁸ Therefore, it is reasonable to conclude that, in eliminating the tax on property held by the persons themselves, the framers also intended to eliminate the tax on property held for those persons in trust.

While the vagueness of the Majority Argument invites conjecture as to the framers' intent, the clear language of the Minority Argument leaves no doubt that their purpose was to exempt trust property from taxation.²⁹ No indication exists that the minority was attempting to offer an interpretation which contradicted the majority. Furthermore, there is no reason to believe that the General Assembly would have adopted the minority's statement unless it was an accurate description of the intended effect of the amendment. In fact, as originally written the Minority Argument stated that trust property remained subject to taxation;³⁰ the argument was not adopted by the entire assembly until it was changed to exclude trust property from taxation.³¹ Nevertheless, the court apparently ignored the importance of the fact that the General Assembly adopted the Majority and Minority Arguments and the Explanation, as a single report,³² to inform the electorate of the amendment's meaning.

27. S. JOUR., 76th Ill. Gen. Assembly 4204 (May 7, 1970).

28. First, the legislature dealt with uneven administration as a problem caused by an unwillingness of the counties to adopt a uniform assessment process. Because the legislature is herein stating a difficulty inherent in all ad valorem systems of taxation, the analysis does not indicate necessarily an intent to exclude natural person beneficiaries from exempt status. The second reason given for the abolition of the tax is that in modern times material wealth is primarily owned in the form of intangible assets and is neither assessed nor taxed easily. The third reason stated to eliminate the tax is that it encourages tax evasion and cheating. In all probability some property held in trust by a corporate fiduciary may be reported more honestly than if it were owned outright by a natural person. However, even this factor does not fully distinguish the natural person from the natural person beneficiary because it is likely that some trustees who share a relationship of close friendship or kinship with the beneficiary may continue to cheat. Therefore, an examination of the three reasons given by the framers indicates that their purpose would not have been thwarted by construing article IX-A to abolish personal taxation by valuation of property held in trust for the benefit of a natural person.

29. See text accompanying note 21 *supra*.

30. S. JOUR., 76th Ill. Gen. Assembly 3537 (June 30, 1969); H. JOUR., 76th Ill. Gen. Assembly 5427 (Oct. 23, 1969).

31. H. JOUR., 76th Ill. Gen. Assembly 6316 (May 6, 1970); S. JOUR., 76th Ill. Gen. Assembly 4205 (May 7, 1970).

32. *Id.*

In its interpretation of the framers' intent, the court in *Hanley* used the official Explanation³³ and a subsequently approved legislative statement, Senate Joint Resolution No. 67,³⁴ to determine which individuals and forms of ownership were covered by article IX-A. The court first dealt with the Explanation, which provided that the amendment would affect only individuals, as opposed to other entities not considered in law to be individuals.³⁵ The question was whether the trustee or the beneficiary is considered in law to be an individual. The court emphasized that, for assessment purposes, the property is listed by the trustee.³⁶ This procedure was sufficient to indicate to the court that the tax is "levied against" the trustee.³⁷ This argument would be more significant if all property listed by a representative were taxed; however, some property is listed by a representative but nevertheless is tax exempt.³⁸ The court also noted that the trustee has a lien against the property assessed for the value of the tax.³⁹ With no additional reasoning or statement of authority, the court concluded that "trustees are not considered in law to be individuals."⁴⁰

The court then focused on Senate Joint Resolution No. 67, which stated:

[B]y the use of the phrase "as to individuals" this General Assembly intended to mean a natural person, or two or more natural persons as joint tenants or tenants in common.⁴¹

To the court, the resolution indicated that property was not exempt unless it was owned by a natural person or two or more natural persons as joint tenants or tenants in common. The crucial interpretation of the resolution should have centered around the concept of ownership. The court, however, failed to examine fully the range of ownership concepts possibly intended by the resolution. Natural person beneficiaries equitably own trust property⁴² as tenants in common.⁴³ The language used in

33. 61 Ill.2d at 460, 337 N.E.2d at 5-6.

34. See note 26 and accompanying text *supra*.

35. See note 19 and accompanying text *supra*.

36. ILL. REV. STAT. ch. 120, §534 (1975).

37. 61 Ill.2d at 460, 337 N.E.2d at 6.

38. Property held for natural persons such as clients, minors, idiots, lunatics, and decedents is listed by the representative and is also exempt. ILL. REV. STAT. ch. 120, §534 (1975).

39. *Id.* §700.

40. 61 Ill.2d at 460, 337 N.E.2d at 6. Despite the fact that the court placed the phrase in quotations, it cited no authority for this proposition.

41. S. JOUR., 76th Ill. Gen. Assembly 4405 (May 19, 1970); H. JOUR., 76th Ill. Gen. Assembly 7145 (May 29, 1970).

42. See, e.g., *Krensky v. DeSwarte*, 335 Ill.App. 435, 442, 82 N.E.2d 168, 171 (1st Dist. 1948).

43. See, e.g., *Commercial Cas. Ins. Co. v. Pearce*, 320 Ill.App. 221, 226, 50 N.E.2d 434, 436 (2d Dist. 1943).

the resolution does not exclude the possibility that the type of ownership to which the General Assembly referred was equitable. Further, the general scheme of personal property taxation in existence at the time when the resolution was adopted provides some support for the premise that equitable ownership would suffice. For example, the Illinois Revenue Act refers to property in trust as "belonging" to the person for whom it is held.⁴⁴ In addition, exemptions have been granted to certain institutions which applied even when their property was held in trust.⁴⁵ Nevertheless, the court flatly stated that neither a trustee nor a beneficiary owns property as a natural person.⁴⁶ The court evidently defined ownership as possession of the entire combination of benefits and burdens associated with the property, as opposed to a fiduciary relationship in which neither the trustee nor the beneficiary is the exclusive and absolute owner.⁴⁷ In reaching this conclusion, the court should have considered whether the resolution actually required the combination of all the incidents of ownership in a natural person or persons, or whether the interests held by the beneficiary would suffice.

In an attempt to support a requirement of absolute ownership, the court compared a trust to a corporation, which clearly was not exempted from taxation by article IX-A.⁴⁸ The court noted that a trust, like a corporation, is a legal creation designed to enable a natural person to accomplish a result which could not be achieved if he continued to own his property as a natural person.⁴⁹ The court apparently was suggesting that the trust was subject to the tax because its owners enjoyed certain privileges. However, the court disregarded the fact that the owners' privileges and duties vary with the trust. Although a trust can be cre-

44. ILL. REV. STAT. ch. 120, §539 (1975). This argument was ignored by the court.

45. ILL. REV. STAT. ch. 120, §§500-523.3 (1975). Under a prior edition of the Illinois Revenue Act, the statute stated:

[P]roperty described in this section, to the extent here limited, shall be exempt from taxation—that is to say, first, all lands donated by the United States for school purposes, not sold or leased; all public school houses; all property of institutions of learning, including the real estate on which the institutions are located not leased by such institutions or otherwise used with a view to profit.

Montgomery v. Wyman, 130 Ill. 17, 21, 22 N.E. 845, 846 (1889). In construing this section, the court stated, "No matter where the legal title to the property may be vested, it is sufficient for the operation of the statute if the institution is the ultimate or beneficial owner. . . ." *Id.* at 22, 22 N.E. at 846.

46. 61 Ill.2d at 461, 337 N.E.2d at 6. Again, the court failed to cite any authority for a major premise.

47. See notes 42-43 and accompanying text *supra*.

48. Lake Shore Auto Parts v. Korzen, 49 Ill.2d 137, 273 N.E.2d 592 (1971).

49. 61 Ill.2d at 461, 337 N.E.2d at 6.

ated for any legal purpose,⁵⁰ many trusts pass only negligible powers or duties to the trustee.⁵¹ Such a trustee receives only the quantity of interest in the trust estate which the purpose of the trust requires.⁵² Moreover, courts have sometimes held that it is the character of the beneficiary and not the trustee which determines exemption from ad valorem taxation.⁵³ Finally, in exempting involuntary trusts, the court classified guardianships, conservatorships, custodianships, and decedent's estates as forms of ownership.⁵⁴ Apparently the *Hanley* court was not willing to examine the varied nature of trust ownership. Consequently, its conclusion lacks a sound analytic basis.

Legislative Construction

The General Assembly's construction of the amendment provides additional insight into the intended effect of the provision.⁵⁵ Although the court is under no obligation to defer to the legislature, it has done so previously when the language of a provision is unclear, noting that the legislature's interpretation has "almost the force of judicial exposition."⁵⁶ The General Assembly recently enacted a statute which exempted all property held in trust for the benefit of a natural person from ad valorem taxation.⁵⁷ In allowing this act to become law without his signature, the Governor stated that the statute was meaningful only

50. *Babcock v. Chicago Rys. Co.*, 325 Ill. 16, 155 N.E. 773 (1927).

51. *Farkas v. Williams*, 5 Ill.2d 417, 125 N.E.2d 600 (1955).

52. *Brandt v. Phipps*, 398 Ill. 296, 309, 75 N.E.2d 757, 763 (1947).

53. Where a constitutional or statutory provision bases a property tax on ownership, "[i]t is the situation or character of the beneficial owner, the holder of the equitable title or estate, and not that of the holder of the legal title, which determines the question of exemption" *Town of Cascade v. Cascade County*, 75 Mont. 304, 311, 243 P. 806, 808 (1926). See also *Montgomery v. Wyman*, 130 Ill. 17, 22, 22 N.E. 845, 846 (1889). But see G. BOGERT, *TRUSTS AND TRUSTEES* §§ 287, 602 (2d ed. 1960).

54. 61 Ill.2d at 463, 337 N.E.2d at 7.

55. An analysis of the discussion at the Illinois Constitutional Convention of 1970 offers alternative insight into the intention of the amendment. The importance to be attached to the delegates' understanding is similar to that which should be given legislative construction because both are after-the-fact investigations of the framers' intent by an elected representative body which is composed partially of members who were present when the resolution was adopted. A great deal of confusion existed at the convention as to whether the court would declare article IX-A unconstitutional on equal protection grounds following the anticipated adoption. 3 PROCEEDINGS 1909. Despite admitted uncertainty concerning the meaning of the phrase "as to individuals," *id.* at 1908, and the failure of Senate Joint Resolution No. 67 to clarify the term, *id.* at 2039, the convention failed to replace the amendment with a new provision. In deferring to the electorate's understanding, the delegates showed a greater respect for the voter than did the *Hanley* court.

56. *People v. Stevenson*, 281 Ill. 17, 30, 117 N.E. 747, 751 (1917).

57. ILL. REV. STAT. ch. 120, §500.21(b) (1975).

because it allowed the legislature to "express its disagreement with the Supreme Court's interpretation of article IX-A"⁵⁸ in *Lake Shore Auto Parts*.⁵⁹ The court, however, refused to consider the legislation, stating that it "contributes nothing of significance to a determination of the ambiguous phrase 'as to individuals'."⁶⁰ In this one sentence dismissal, the court failed to decide the constitutionality of the statute.⁶¹ Nevertheless, the *Hanley* opinion negates the legislation's effect on tax exemption.

Stare Decisis

In deciding *Hanley*, the court was confronted with its prior decision in *Lake Shore Auto Parts Co. v. Korzen*.⁶² However, the court placed more reliance on this precedent than is required by the doctrine of stare decisis. In *Lake Shore Auto Parts Co. v. Korzen*,⁶³ the Illinois Supreme Court decided that article IX-A violated the equal protection clause of the United States Constitution because it established a system of property taxation which differentiated between classes of ownership. The United States Supreme Court reversed this decision in *Lehnhausen v.*

58. Letter from Daniel Walker to members of the Illinois House of Representatives. H. JOUR., 78th Ill. Gen. Assembly 9044 (Nov. 7, 1974). The Governor noted that the bill would be unconstitutional under the 1970 constitution which requires that:

[O]n or before January 1, 1979, the General Assembly by law shall abolish all *ad valorem* personal property taxes and concurrently therewith and thereafter shall replace all revenue lost by units of local government and school districts as a result of the abolition of *ad valorem* personal property taxes subsequent to January 2, 1971. Such revenue shall be replaced by imposing statewide taxes, other than *ad valorem* taxes on real estate, solely on those classes relieved of the burden of paying *ad valorem* personal property taxes because of the abolition of such taxes subsequent to January 2, 1971.

ILL. CONST. art. IX, §5(c) (1970). In *Elk Grove Engineering Co. v. Korzen*, 55 Ill.2d 393, 304 N.E.2d 65 (1973), the court held two statutes unconstitutional because the General Assembly exempted certain property from *ad valorem* taxation, but failed to concurrently impose a replacement tax.

59. 54 Ill.2d 237, 296 N.E.2d 342 (1973).

60. 61 Ill.2d at 459, 337 N.E.2d at 5.

61. See note 58 *supra*. The statute may be considered to be either an abolition of personal property taxes or an exemption from the taxes. If it is considered an abolition, the general consensus is that it is unconstitutional under article IX, section 5(c). *Id.* If, however, the statute is construed to be an exemption, then it is not permissible under section 6 of the same article. That section states, "[t]he General Assembly by law may exempt from taxation only the property of the State, units of local government and school districts and property used exclusively for agricultural and horticultural societies, and for school, religious, cemetery and charitable purposes."

62. 49 Ill.2d 137, 273 N.E.2d 592 (1971).

63. *Id.*

Lake Shore Auto Parts Co.,⁶⁴ stating that where the only federal right involved is equal protection, the state is allowed to make classifications which produce reasonable systems of taxation. On remand, the Illinois Supreme Court announced its per curiam decision.⁶⁵

The plaintiffs in *Hanley* argued that the application of article IX-A to trusts violated the federal equal protection clause. The Illinois court dismissed this federal equal protection issue, citing *Lehnhausen v. Lake Shore Auto Parts Co.* In *Lehnhausen*, however, the court placed a great deal of importance on the differences between corporations and individuals. Certainly, the differences between corporations and individuals are much greater than the differences between voluntary and involuntary relationships or between individuals and beneficiaries. Moreover, the federal court specifically limited its decision to the factual controversy presented without addressing natural person beneficiaries. Hence, the United States Supreme Court's hesitation in rendering its decision and its willingness to limit its opinion leaves the equal protection question open for future resolution.

When confronted with its own per curiam decision in *Lake Shore Auto Parts Co.*, the *Hanley* court recognized that its prior opinion had not settled the issues under the doctrine of stare decisis.⁶⁶ In *Lake Shore Auto Parts Co.*, no natural person beneficiaries were before the court. Therefore, no binding precedent existed for the *Hanley* plaintiffs, and any undue deference to the earlier per curiam decision was improper. Nevertheless, the court seemed unwilling to make a fresh examination of the beneficiary question. It modified its previous position only when the beneficiaries seemed particularly vulnerable or where few tax planning devices were at work.⁶⁷ The tie to the earlier decision may have been the result of the United States Supreme Court reversal.⁶⁸ In addition, concern over the impact of lost revenues may have influenced the court. Whatever the motivation, the court's adherence to its earlier opinion played a major role in *Hanley*.

In summation, article IX-A was drafted by the General Assembly,

64. 410 U.S. 356 (1973).

65. See text accompanying note 5 *supra*.

66. Recognizing the importance of the issue being litigated, the court agreed to "examine once more" the materials and the arguments of the parties. However, the court's statement that "the basic contentions now advanced were before the court in the earlier cases, although perhaps without some embellishments and refinements now included," strongly hinted that a complete reexamination would not be conducted. 61 Ill.2d at 456, 337 N.E.2d at 4. Among the "embellishments" were representative parties and ILL. REV. STAT. ch. 120, §500.21(b) (1975).

67. 61 Ill.2d at 456, 337 N.E.2d at 4.

68. *Lehnhausen v. Lake Shore Auto Parts*, 410 U.S. 356 (1973).

considered by the Constitutional Convention, approved by the electorate, and reaffirmed by the General Assembly. In addition, the amendment was explained by a state's attorney⁶⁹ and the Illinois Attorney General.⁷⁰ The expressed intent of all of these interpretive sources supports the conclusion that article IX-A was enacted to prohibit the taxation by valuation of *all* personal property owned by individual beneficiaries. The court in *Hanley* chose only to modify *Lake Shore Auto Parts* and to exclude personal property held voluntarily in trust for natural persons from the article IX-A tax exemption.

THE IMPACT OF HANLEY v. KUSPER

Judicial Usurpation of the Legislative Power and Duty to Tax: A State of Confusion

The power to raise revenues is vested in the legislative arm of the State of Illinois.⁷¹ The disregard shown in *Hanley* for the understanding of the electorate and the intentions of the framers is a judicial usurpation of that legislative function. These actions will operate to deny the relief embodied in article IX-A: the abolition of an unsatisfactory⁷² and unworkable system of personal property taxation. As a result of this opinion, personal property taxation will remain difficult to administer.

69. While the Illinois Supreme Court, in dicta, has refused to find that the opinions of the Attorney General of Illinois and the state's attorney are binding upon the court, it has found them persuasive. *Rogers Park Post No. 108, American Legion v. Brenza*, 8 Ill.2d 286, 292, 134 N.E.2d 292, 296 (1956); *Alsen v. Stoner*, 114 Ill.App.2d 216, 222, 252 N.E.2d 488, 491 (2d Dist. 1969); *Strat-O-Seal Mfg. Co. v. Scott*, 72 Ill.App. 480, 485, 218 N.E.2d 227, 229 (4th Dist. 1966); *City of Champaign v. Hill*, 29 Ill.App.2d 429, 442, 173 N.E.2d 839, 846 (3d Dist. 1961). Pointing to the Majority and Minority Arguments, and the statutory authority for their publication, the State's Attorney of Cook County stated:

[t]he clear import of this legislative explanation of the proposed amendment is that personal property held in a fiduciary capacity for the benefit of natural persons shall not be subject to the personal property tax.

S.A. Legal Opinion No. 1340 of the Cook County State's Attorney, dated December 28, 1970.

70. The Illinois Attorney General reached a similar decision: "[S]ince the effect of the tax would be directly upon an individual beneficiary, such personal property would be exempt." Ill. Op. Att'y Gen. No. S-260 (Jan. 22, 1971). He restated his position in a later letter, stating:

Thus, not only is the property of sole proprietors . . . exempt from the tax, but also the personal property . . . of a trust in which the beneficiaries are individuals, since in each of these instances, the tax would fall on property owned by "a natural person or by two or more natural persons as joint tenants or tenants in common.

Letter from William J. Scott, Attorney General, to all county treasurers, March 2, 1973.

71. ILL. CONST. art. IX, §1 (1970).

72. See *People ex rel. Hamer v. Jones*, 39 Ill.2d 360, 372, 235 N.E.2d 589, 596 (1968).

The property of a trust is often composed of intangible assets. As noted by the legislature, "[i]ntangible assets are common, but not easily assessed and taxed."⁷³ Consequently, cheating and evasion will continue to be encouraged. The procedures for personal property tax assessment also will provide opportunities for evasion. The current system provides that the owner on April 1st of each year is liable for taxes for that year.⁷⁴ How will the court deal with a power given the trustee in the granting instrument to revoke the trust on March 31st so that the owner on April 1st is a natural person who is restored to beneficiary status on April 2nd?

In addition to problems created by schemes devised to avoid the tax, the court left some unanswered questions. A decedent's estate is exempted from taxation; a trust is not. Is testamentary trust property subject to taxation during the period from the time of death until the executor or administrator closes the estate? When trust property is held by a guardian for a minor, does the property become taxable at the moment majority is reached or on April 1st of that year? The court's decision failed to supply a basis for resolution of these kinds of problems. The description of exempt beneficiaries, those natural persons who are prevented by law from dealing with the property as a natural person, fails to adequately distinguish between exempt and non-exempt beneficiaries. For instance, the widow beneficiary of a testamentary trust receives benefits from a voluntary trust. However, the trust assets must pass through the decedent's estate, which is an involuntary fiduciary relationship. The *Hanley* decision does not indicate whether the widow in this situation is prevented by law from dealing with the property as a natural person. Therefore, it is not clear whether the property is taxed or exempt.

In addition to these unresolved questions, the court has placed the legislature in a rather compromising position by refusing to review the newly enacted tax exemption statute. Consequently, a totally ineffective and possibly unconstitutional⁷⁵ statute continues to appear in the Revenue Act, inevitably creating confusion. Further, costly additional litigation or a legislative repeal will be required to remove the statute, a task the court could have accomplished easily in *Hanley*. The *Hanley* court refused to recognize that personal property tax on voluntary trusts had been abolished by article IX-A. It will now be extremely difficult

73. S. JOUR., 77th Ill. Gen. Assembly 4204 (May 7, 1970).

74. ILL. REV. STAT. ch. 120, §508a (1975).

75. See note 61 *supra*. In addition, the statute may also offend the provision of the constitution which authorizes the legislature to exempt certain classes from taxation. ILL. CONST. art. IX, §6 (1970).

to rid Illinois of personal property taxation.⁷⁶ The 1970 constitution requires the General Assembly to abolish all ad valorem personal property taxes on or before January 1, 1979, and to replace all lost revenues by imposing statewide replacement taxes on those classes relieved of taxation.⁷⁷ The Illinois Supreme Court, in *Elk Grove Engineering Co. v. Korzen*,⁷⁸ held that this provision is not self-executing and requires legislation to put it into effect. Therefore, the General Assembly must abolish personal property tax by statute and concurrently pass legislation embodying a replacement tax.⁷⁹ Designing a replacement tax may create such a problem that the legislature will be unable to abolish personal property tax. Presumably, without the *Elk Grove Engineering* decision the tax would have become unconstitutional automatically on January 1, 1979. Then the replacement tax problem could have been resolved independently.

The problem of designing a replacement tax is further complicated because voluntary trusts definitely will require a replacement tax while involuntary trusts may not. In *Hanley v. Kusper* the court did not consider whether abolition of the tax on involuntary trusts related back to the effective date of article IX-A, January 1, 1971. A retroactive application was implied in the decision, but the issue was not addressed directly. If the abolition relates back, presumably no replacement taxes will be required for these classes of individuals. Consequently, if the General Assembly abolishes the tax on voluntary trusts it will have to design a replacement tax which reaches voluntary trusts and exempts involuntary trusts. This will be difficult because of the similarities between voluntary and involuntary trusts. Both are typically administered by investing the trust corpus into intangible assets and distributing or accumulating the proceeds for the support of the beneficiary.

The problem is complicated further because some investment properties have been exempted from personal property tax by statute. Therefore, one trustee may have invested in both exempt and non-exempt intangibles⁸⁰ in the process of administering the trust. If this is the case,

76. The reply brief for fiduciary-appellants suggested that the Illinois income tax, ILL. REV. STAT. ch. 120, §§1-101 *et seq.* (1975), was intended to replace revenues lost by the abolition of *ad valorem* taxation of personal property. See also *id.* at §§9-901(b), which requires the treasurer to transfer 1/12 of the receipts of the Illinois income tax to the local distributive fund on a monthly basis. It was also argued that the abolition of the *ad valorem* taxation of personal property was planned as a relief for those individuals who were newly burdened by the income tax. Reply Brief for Fiduciary-Appellants at 14-15, *Hanley v. Kusper*, 61 Ill.2d 452, 337 N.E.2d 1 (1975).

77. ILL. CONST. art. IX, §5(c) (1970).

78. 55 Ill.2d 393, 304 N.E.2d 65 (1973).

79. ILL. CONST. art. IX, §5(c) (1970).

80. ILL. REV. STAT. ch. 120, §§499 *et seq.* (1975).

it is not clear whether the replacement tax will fall on all the trust assets because the beneficiary is a member of a class which has been relieved of personal property tax. A more equitable solution would be to put the replacement tax only on the assets which had previously been non-exempt. However, if this procedure is employed the newly established system would resemble an ad valorem system of taxation because the amount of the tax would be based on the value of certain property. These kinds of problems will increase the likelihood that the General Assembly will be unable to enact a satisfactory statute to abolish personal property taxes on property held in trust for one or more natural person beneficiaries.

The General Assembly may be forced to submit another resolution to the electorate in order to abolish personal property tax. Constitutional amendments have fared poorly in Illinois,⁸¹ and the chances of passage are slim. Consequently, the judicial action taken in *Hanley* may have created a permanent defect in the legislature's intended scheme of taxation.

Impact on the Trust and the Trust Industry

Concern has been expressed that the *Hanley* decision will have a substantial negative effect on the trust industry. This presents a particular threat in Illinois communities adjacent to other states⁸² because of the ease of transferring trust administration. Economic loss may result not only from transfer of trusts to other jurisdictions, but also from a growing reluctance to establish trusts.⁸³ Settlers with the power reserved have revoked trusts in order to avoid the imposition of personal property taxation.⁸⁴ A loss of trust business may have a severe detrimental effect on the economy of Illinois in lost employment and income tax revenue; the Corporate Fiduciaries Association of Southern Illinois alone represented \$156,000,000 in trust assets as of December 31, 1973.⁸⁵

In addition to the deleterious effect on the trust industry as a business, this decision may have a significant destructive impact on the trustee-beneficiary relationship. Mr. Justice Goldenhersh, in his dissenting opinion in *Lake Shore Auto Parts*, pointed out that "courts and fiduciaries will now be confronted with the question of whether 'men of

81. See note 41 *supra*.

82. Affidavit of John J. Gainer, Brief for Corporate Fiduciaries Association of Southern Illinois as Amicus Curiae, *Hanley v. Kusper*, 61 Ill.2d 452, 337 N.E.2d 1 (1975).

83. Brief for Fiduciary-Appellants at 2, *Hanley v. Kusper*, 61 Ill.2d 452, 337 N.E.2d 1 (1975).

84. *Id.*

85. *Id.*

prudence, discretion and intelligence' may safely counsel or approve the use of a device which for so long has performed service of inestimable value.⁸⁶ The trustee-fiduciary has a high duty of care to his beneficiary; his ability to prudently invest the trust res may be impaired by juggling investments between exempt⁸⁷ and non-exempt intangibles to achieve the highest rate-of-return after collection of the tax. In addition, some trustees may feel a conflict between their legal obligation to honestly list trust property for assessment and the fiduciary obligation to the beneficiary. Finally, a trustee in charge of a trust for an income beneficiary of declining health may feel a severe conflict of interest in preserving the corpus. He may have to decide whether the beneficiary should be declared an incompetent⁸⁸ to preserve the value of the personal property tax for the remainderman. Hence, the value of the trust as a device to protect those who are unable to care for themselves may have been severely diminished.

CONCLUSION

The Illinois Supreme Court, in refusing to find that personal property taxes were abolished as to natural person beneficiaries, has usurped the legislative power to tax and may have damaged the trust industry in the State of Illinois. The decision was not supported by the voters' understanding, the framers' intent, legislative construction, stare decisis, or policy considerations. Unless a valid equal protection argument can be made at the federal level, the impact of *Hanley* may be irreparable because of the difficulty in designing replacement tax legislation or obtaining approval of another constitutional amendment.

Madeleine Tewes Lee

86. 54 Ill.2d at 240, 296 N.E.2d at 344 (1973).

87. ILL. REV. STAT. ch. 120, §§499 *et seq.* (1975).

88. ILL. REV. STAT. ch. 3, §113 (1975).