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JUDICIAL TYRANNY

and

YOUR INCOME TAX

by

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To Peggy Christensen, who
has kept the flame of freedom
burning, often when there
wasn't even a candle.

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INTRODUCTION

When people began to live in groups to take advantage of the mutual benefits such associations provide, they determined the use of “self-help” to protect their lives and property was not in their best interest, and they voluntarily instituted governments and laws. The philosophy behind government is that certain functions necessary for the protection of the life, liberty and property of the people can be best handled by a centralized organization (government) which is given sufficient power (lawful right to pass laws and to enforce them) to accomplish those functions. Numerous types of governments have emerged under this concept, such as democracy, socialism, fascism, nazism, communism, and one experimental form of government known as a “Federal Republic,” now commencing its third centennial. Some degree of power (force) is essential to the ability of any government to operate successfully; it is the manner in which a government obtains the power and how it uses that power that separates people who are free from those who are not.

The first government known to each of us is the government ordained under the Laws of Nature, the parental government under which we are born. We are thrust into this relationship without any say whatsoever, and the power exerted over us—which we are helpless to protest or abridge—is total and absolute. Our only protection from the abuse of this potentially deadly power is the divinely inspired parental instinct to protect and nourish (love) the newborn, which creates the environment for us to live and prosper. It can thus be clearly seen that this power does not originate with our parents; but is granted to them from Nature’s God, is made known to them through God’s will (instinct), is essential for life to exist, and is held in trust by our parents solely for our benefit and protection.

Nature’s God creates each of us equally and endows us with certain inalienable rights, chief of which are life, liberty and the pursuit of

happiness. The gift of equality, ironically, is one of inequality; we are each distinct and have different built-in potential than any other human being. God's gift to us is the capacity to develop and exert our own uniqueness in the world for the purpose of maintaining our life and liberty and being happy; our respective duty is to develop to our full potential, thereby giving the benefit of our uniqueness to the world. This input into the universe results in a division of labor, and creates the basic foundation of all economics. As we are basically a society oriented species, a sound economic basis is thus created, for it is also our nature to improve and modify our environment in order to improve the quality of our lives. By exchanging unique services or products with others for their unique services or products, trade flourishes, the quality of life improves, we acquire more wealth, prosperity and happiness, and society blossoms. Under the Laws of Nature, our prosperity is also an inalienable right.

It is a fundamental principle of our uniqueness that only we can know it fully among our peers. Our duty to God to achieve maximum development of our potential necessarily prevents other people from interfering with the development and free exercise of our potential. It also creates a corresponding duty on us to resist any attempt by others to destroy the freedom of our will with respect to our uniqueness. This concept is embodied within the single word "Liberty."

The presence of other members in the family, however, adds yet another aspect to the parental form of government; the rightful exercise of the power to place such restraints on our conduct so as to best conserve the right of each of us to the greatest amount of personal liberty, taking into account the coequal and coextensive rights of each of the other family members. This rightful exercise imposes the corresponding obligation to be so restrained for the benefit of the rights of all. In order for the power to restrain to be lawful, it must be exercised so as not to destroy the very liberty it attempts to protect. The power, delegated in trust and tempered by love, secures our liberty, as the governed, in the familial society.

There can be no escape from the conclusion that under the Laws of Nature, government and society were created to benefit us; we were not created to benefit government and society. The purpose of the family (society) is to preserve our lives and our liberty; the purpose of parental power (government) is to preserve the family (society). When a parent transcends the limitation on the exercise of his or her delegated power and invades the domain of individual freedom (gets drunk and beats the kids), the parent usurps an authority never vested in him or her, and violates the very rights the protection of which was the only purpose for which the power was delegated. When a government transcends its limitation, the usurpation of authority is known as tyranny.

As we mature we learn to infuse our unique mental, moral and physical endowments with objects existing in Nature's universe, and we are thus able to create unique ideas and objects. These creations contain elements of our very essence, and from the beginning of time such creations have been referred to as personal property. The only limitation upon us in this process of acquiring personal property through our labor is the coexistent and coequal right of every other person in society to the same process. The taking of our property, without our consent, is a badge of mastery over us indicative of slavery, for it is a taking of a cherished inalienable right, a right essential to our very ability to survive. When the taking is in the name of the government, either through direct confiscation or through indirect means, it is a violation of duty and a usurpation of power akin to the beating of a child by a drunken parent.¹ Self-defense of our life, liberty, property and happiness from the usurpation of power—revolution if you dare—is an inalienable right pursuant to the Laws of Nature, and the exercise of this right formed the basis of our Federal Republic:

We hold these truths to be self-evident, that all men are created equal, that they are endowed by their Creator with certain unalienable Rights, that among these are Life, Liberty and pursuit of Happiness. That to secure these rights, Governments are instituted

among Men, deriving their just powers from the consent of the governed. That whenever any Form of Government becomes destructive of these ends, it is the Right of the People to alter or to abolish it, and to institute new Government, laying its foundation on such principles and organizing its powers in such form, as to them shall seem most likely to effect their Safety and Happiness.²

With the signing of the Declaration of Independence, the subjects of the Monarch, King George, declared themselves to be a free and independent people. To the extent they, as a society (political body) were operating under governments already in existence within the territory claimed by the thirteen colonies, an additional result of the signing of the document was the emergence of thirteen sovereign nations. Both under the common law and/or the laws passed by these new nations, inhabitants who were born in the colonies became citizens thereof, and those who were not so born, could either choose allegiance to the King or allegiance to the new political body. If they chose allegiance to the new political body, they were also considered “citizens.” These thirteen colonies came to be known as “states,” and as a result of the Articles of Confederation, came to be known in the community of nations as the United States of America. The Articles of Confederation soon proved to be ineffectual, and were replaced with the Constitution of the United States of America.

The Constitution created a form of government which expressly recognized the people (us) as sovereign, and limited the power of the federal government to that expressly delegated to it in the Constitution. The Constitution also limited the locations where the federal government could exercise its power.³ This concept is known as federal territorial and/or exclusive legislative jurisdiction. The principle is that while Mr. Jones may have parental power over his children, he cannot exercise that power over Mr. Smith’s children in Mr. Smith’s house; Mr. Smith’s house is outside the territorial jurisdiction of Mr. Jones’ parental power. Any attempt by

Mr. Jones to exercise his power over Mr. Smith's children in Mr. Smith's house is illegal, null and void. Of course the power may nevertheless be exerted, albeit illegally, and various legal remedies exist to return the status quo and to compensate for any injury sustained.

The power of the new federal government to tax was a power expressly delegated to the Legislative Branch of the federal government in Article I, Section 8, Clause 1 of the Constitution. This power to tax has been held by the United States Supreme Court to be all inclusive, subject to only two requirements: direct taxes must be apportioned per Article I, Section 2, Clause 3 and Article I, Section 9, Clause 4, and indirect taxes must be uniform, per Article I, Section 8, Clause 1.

Commencing with the earliest tax laws enacted by Congress, great debates have revolved around the issue of whether the enacted tax was a direct tax or an indirect tax. This is an important legal issue, for if Congress does not provide for apportionment of the tax and the tax is declared by the judiciary to be a direct tax, then a whole class of intended "taxpayers" would not be "taxpayers" as a result of the unconstitutionality of the tax for lack of apportionment. A law that is contrary to the Constitution, of course, is no law at all.⁴

The first income taxes legislated by Congress were enacted during the Civil War era. The constitutionality of those acts was not challenged in court. The next income tax was enacted in 1894 during a time of peace, and its constitutionality was challenged in the Supreme Court. The majority opinion of the Court declared the income tax to be a direct tax with no provisions for apportionment, and struck it down as unconstitutional. This court decision is known as the "Pollock" decision [*Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429, *aff. reh.*, 158 U.S. 601 (1895)]. The decision of the Supreme Court was by no means unanimous; a strong dissent was raised by a minority of Supreme Court justices that the tax was an indirect tax that did not require apportionment. One of these "dissenting" justices was Associate Justice White.

The *Pollock* opinion told Congress that if it did not like the result reached by the Court, the Constitution could be amended to change the result.⁵ In 1909, Congress took steps to amend the Constitution by proposing the Sixteenth Amendment in the following form:

Sixteenth Amendment:

The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.

This Amendment was certified as ratified⁶ in 1913, and Congress passed an income tax act which was virtually identical to the one held unconstitutional in *Pollock*. This law was also challenged as unconstitutional, and ultimately went to the Supreme Court where Justice White was now sitting as the Chief Justice. The resulting decision, known as the “*Brushaber*” decision [*Brushaber v. Union Pacific Railroad Co.*, 240 U.S. 1 (1916)], was written by Chief Justice White himself, and not surprisingly, the tax was classified as an indirect tax.⁷

The income tax was of such a nature that its presence was generally unknown to the majority of the people from its inception until World War II. At that time, Congress, claiming the need for additional revenue, passed the Victory Tax Act, an unapportioned direct tax on the personal property of United States citizens residing at home. The Victory Tax, which was collected with the income tax, was collected through withholding from wages. This started the erroneous association of the term “wages” with the term “income.” In law, especially at the time of the proffer of the Sixteenth Amendment by Congress, the terms were not synonymous. Income for purposes of federal income taxation has been defined by the Supreme Court as “the **gain** derived from capital, from labor or from both combined, provided it include **profit** gained through a sale or conversion of capital assets.” Labor, the contract to exchange labor for wages or other compensation,

and the wages or other compensation itself, have all been declared by the United States Supreme Court to constitute sacred, inviolable, personal property. The Sixteenth Amendment only addressed “income,” and was thus limited to the gain derived from labor or capital; neither the Sixteenth Amendment nor the federal personal income tax law provides any authority for the taxation of labor or the property for which the labor may be exchanged, most frequently wages, absent apportionment.

As a result of the *Brushaber* decision, numerous courts have held that wages constitute income and a tax on wages does not have to be apportioned. There is no question but that the *Brushaber* decision, holding the income tax to be an indirect tax, is in irreconcilable conflict with the decision of the Supreme Court in *Pollock* holding that the income tax is a direct tax.

In Chapter I of this book I have provided an analysis of prior federal income tax legislation. A study of this legislation is fundamental to an understanding of today’s Internal Revenue Code and exactly who and what is taxed under the law.

In Chapter II of this book I have provided an in-depth analysis of the *Pollock* and *Brushaber* decisions provided for the purpose of establishing the true purpose behind the Sixteenth Amendment and the exact power given to Congress by it.

In Chapter III of this book I have provided a statutory analysis of the Internal Revenue Code as it applies to the personal income tax, and an explanation of what is and, more importantly, what is not income.

In Chapters IV through XI of this book I have provided an in depth, case-by-case analysis of each and every federal court case that holds wages constitute income, in an effort to show the ignorance or intentional, treasonous actions of our federal judiciary in subverting our Constitution and the laws enacted by Congress. The simple fact is that no decision of the Supreme Court of the United States has

specifically held that wages constitute income, and as a matter of law, they do not.

With over a hundred cases purportedly holding that wages constitute income, at first impression one might believe that I disagree with the law. I do not. I do believe, however, that the law, for political and financial motives, has been subverted. I have attempted in this book, by providing a history of the income tax and an analysis of the Internal Revenue Code, to establish exactly what the law is, and to show how it has been undermined by our federal judiciary.

In Appendix A, I have provided a partial transcript from a federal criminal trial in the United States District Court for the District of Alaska, in the case of the *United States v. Carl Beery*, case No. A87-43CR. The transcript contains my cross-examination of I.R.S. Revenue Agent Knutson. The subject matter of the cross-examination was Mr. Beery's liability for the income tax and whether wages constitute income. The transcript fully discloses the Court's hostility to this line of questioning, but more importantly, points out the failure of the Internal Revenue Service to calculate "gain" in determining income.

In Appendix B, I have provided a partial transcript from another federal criminal trial in the United States District Court for the Southern District of Indiana, Evansville Division, in the case of the *United States v. James I. Hall*, case No. EV 87-20 CR. The transcript contains my cross-examination of I.R.S. Special Agent Shaffner. My cross-examination established through Ms. Shaffner, who was qualified as an expert witness, that no statute in the Internal Revenue Code made Mr. Hall liable for the income tax. Although not contained in the portion of the transcript reproduced in Appendix B, Federal District Court Judge Gene E. Brooks threatened to hit me with his gavel when I attempted to repeat Ms. Shaffner's testimony to the jury, and instructed the jury, contrary to the evidence and the law, that Mr. Hall was a taxpayer liable for the tax.

It was not my intention in writing this book to advise people not to pay income taxes. In fact, in the conclusion, I caution against taking steps that will most certainly subject you to tremendous governmental abuse. On the other hand, the truth is the truth, and armed with the truth, and fueled with the desire to maintain the cherished, divinely inspired principles of freedom and liberty, the people of the United States of America, by joining together and raising their voices in protest, can once again restore our country to a government of laws as opposed to a government of men. With this thought in mind, I have written this book for your consideration.

ENDNOTES

1. “It is none the less robbery, because it is done under the forms of law, and is called taxation” *Loan Association v. Topeka*, 87 U.S. 655, 664 (1879).
2. Declaration of Independence.
3. United States Constitution, Article I, Section 8, Clause 17.
4. “The particular phraseology of the Constitution of the United States confirms and strengthens the principle, supposed to be essential to all written constitutions, that a law repugnant to the constitution is void, and that courts, as well as other departments, are bound by that instrument.” *Marbury v. Madison*, 5 U.S. 137, 180 (1803).
5. *Pollock v. Farmers’ Loan & Trust*, 158 U.S. 601, 634- 635 (1895).
6. Bill Benson, *The Law That Never Was—The Fraud of the 16th Amendment and Personal Income Tax*, (Constitutional Research Assoc., Box 550, South Holland, IL 60473, 1985). Mr. Benson documents with certified state archive documents from each state then in the Union that the Sixteenth Amendment was never properly ratified as part of the United States Constitution. Mr. Benson also documents with certified U.S. archive documents that the non-ratification was specifically noted by the Solicitor General in his written report to the Secretary of State, Philander Knox, who nonetheless certified the Sixteenth Amendment as having been properly ratified. While several of the federal courts have been made aware of this fraud, they have refused to remedy the fraud by classifying the ratification process a “political question” non-reviewable by the Courts.
7. Even today the debate continues as some of the Federal Courts of Appeal take the position that the income tax is a direct tax

and some take the position that the income tax is an indirect tax. Compare, *Ficalora v. C.I.R.*, 751 F.2d 85 (2nd Cir. 1984) [holding the income tax is an indirect excise tax] with *Lonsdale v. C.I.R.*, 661 F.2d 71 (5th Cir. 1981) [holding the income tax is a direct tax].

CHAPTER I

PRIOR FEDERAL INCOME TAX LEGISLATION

Before the adoption of the U.S. Constitution, the original thirteen States were leagued together under the Articles of Confederation, the Congress of which had no power of taxation. The States, under the Articles of Confederation, possessed all powers of taxation and had surrendered none to the Articles' Congress, the revenue of which was derived solely through requisitions for money made by that Congress on the States. This system proved itself to be highly inefficient.

When the Philadelphia Constitutional Convention met in 1787, it was quickly determined that Congress should have a power of taxation, one which was not broad and general but one somewhat restrictive. At that time, the States imposed two types of taxes, those which were direct in their operation, and those which were indirect. The great question in reference to taxation before the Constitutional Convention was whether power would be given to Congress to impose only one or both types of taxes, and it was eventually decided to give Congress authority to impose both of these classes of taxes, under certain restrictions. The States felt that Congress should rely primarily upon indirect taxes for its revenue and that they would reserve for themselves direct taxes for their revenue. To insure this scheme, Congress was permitted to impose indirect taxes, known as duties, imposts and excises, by the rule of uniformity, a rule which Congress could easily meet. But, to protect the revenue of the States, Congress was required to impose all direct taxes by the regulation of apportionment, a very rigorous standard.

The agreement of the Convention manifests itself in the body of the Constitution. In Article I, Section 8, Clause 1, a power of taxation is granted to Congress in this manner:

Article I, Section 8, Clause 1:

The Congress shall have power to lay and collect taxes, duties, imposts and excise ...; but all duties, imposts and excises shall be uniform throughout the United States.

This clause clearly shows the rule of uniformity for indirect taxes. The regulation of apportionment for direct taxes is found in the Constitution at Article I, Section 2, Clause 3 and Article I, Section 9, Clause 4:

Article I, Section 2, Clause 3:

Representatives and direct taxes shall be apportioned among the several states.

Article I, Section 9, Clause 4:

No capitation, or other direct, tax shall be laid, unless in proportion to the census or enumeration herein before directed to be taken.

Few direct tax acts were intentionally imposed by Congress; one was laid in 1798,⁸ two were laid during the War of 1812 in 1813⁹ and 1815,¹⁰ and several were laid during and immediately following the Civil War.¹¹ To further finance the Civil War, Congress passed three income tax acts. The constitutionality of these acts was never challenged in court, no doubt because they were wartime measures. The next income tax was not passed by Congress until 1894, and was passed in a time of peace. The constitutionality of this tax was challenged in court; in the case of *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429, 15 S.Ct. 673, *aff. reh.*, 158 U.S. 601, 15 S.Ct. 912 (1895), the United States Supreme Court struck down the entire tax because the tax was found to be a direct, but unapportioned, tax. A review of these former taxes is important to obtain a clear understanding of the income taxes imposed by law today.

In 1861, Congress adopted an act which imposed both a direct tax and an income tax.¹² This income tax act was repealed the following year and replaced by another in “An Act to provide Internal Revenue to support the Government and to pay Interest on the Public Debt,” approved July 1, 1862, 12 Stat. 432, ch. 119. Section 86 of this Act, 12 Stat. 472, imposed a salary tax upon people in the employment or service of the United States. Section 90 of this Act, 12 Stat. 473, imposed an “income duty” as follows:

That there shall be levied, collected and paid annually, upon the annual gains, profits or income of every person residing in the United States ... a duty of three per centum ... ; and upon the annual gains, profits, or income ... by any citizen of the United States residing abroad ... there shall be levied, collected and paid a duty of five per centum.

These Acts taxed the salary of people working for the United States government, every “person” residing in the United States, and “citizens” of the United States residing abroad. This Act was replaced by another Act in 1864, 13 Stat. 223, ch. 173, which was amended in 1865 by an Act at 13 Stat. 469, ch. 78, and amended again in 1866 by an Act at 14 Stat. 137, ch. 184. This 1864 Act, as amended through the 1866 Act, read as follows:

Sec. 116. And be it further enacted, That there shall be levied, collected, and paid annually upon the annual gains, profits and income of every person residing in the United States, or of any citizen of the United States residing abroad ... a duty of five per centum ... And a like tax shall be levied, collected, and paid annually upon the gains, profits, and income of every business, trade or profession carried on in the United States by persons residing without the United States not citizens thereof.

This Act, as amended, taxed every “person” residing in the United States, United States “citizens” residing abroad, nonresident non-citizens on income derived from business, trades or professions carried on in the United States, and in Sec. 123, the salary of people employed by the United States government.

The 1894 income tax act, “An Act to reduce taxation, to provide revenue for the Government, and for other purposes,” approved August 27, 1894, 28 Stat. 509, ch. 349, at Section 27 [28 Stat. 553] read as follows:

That ... there shall be assessed, levied, collected, and paid annually upon the gains, profits, and income received in the preceding calendar year by every citizen of the United States, whether residing at home or abroad, and every person residing therein ... a tax of two per centum ... and a like tax shall be levied, collected and paid annually upon the gains, profits, and income from all property owned and of every business, trade, or profession carried on in the United States by persons residing without the United States.

This Act taxed every United States “citizen” whether residing at home or abroad, every “person” residing in the United States, and non-residents on income derived from business, trades or professions carried on in the United States.

It becomes clear that a distinction was made between the terms “citizens” and “persons” in these early income tax acts. The Act of 1894 specifically taxed “citizens of the United States” residing at home [in the United States] or abroad and persons” residing in the United States; there could be no reason for the statute to separately mention citizens and persons if they were in fact the same. The fact is, they are different. A “person” “residing in the United States” “who is not a citizen” would be either a resident alien (in the United States on a visa) or a resident National (an immigrant).

Mr. Pollock, identified by the Supreme Court as “a citizen of the State of Massachusetts,”¹³ was a shareholder of a corporation. He sought an injunction against the corporation from paying the corporate income tax¹⁴ on the grounds that as to the tax on the real estate held and owned by the corporation, the tax was a direct tax by virtue of it being imposed upon the rents, issues, and profits of the real estate, that the tax was a direct tax as to personal property held by the corporation, and the taxes not being apportioned, the tax was unconstitutional. Similar claims were made with respect to the taxes imposed upon Mr. Pollock’s income, and income derived from the stocks and bonds of the States of the United States which he held. The *Pollock* decisions held that a tax on the whole income of property was a direct tax in the constitutional sense. In speaking of the purpose of the *Pollock* Court in defining what a “direct tax” was, the Supreme Court said in *Brushaber*:

Concluding that the classification of direct was adopted for the purpose of rendering it impossible to burden by taxation accumulations of property, real or personal, except subject to the regulation of apportionment, it was held the duty existed to fix what was a direct tax in the constitutional sense so as to accomplish this purpose contemplated by the Constitution.” (157 U.S. 581.)

Brushaber, 240 U.S. at 15.

The *Pollock* Court, in its first decision, defined “direct taxes” as follows:

Ordinarily, all taxes paid primarily by persons who can shift the burden upon someone else, or who are under no legal compulsion to pay them, are considered indirect taxes; but a tax upon property holders in respect of their estates, whether real or personal, **or of the income yielded by such**

estates, and the payment of which cannot be avoided, are direct taxes. [Emphasis added.]

Pollock, 157 U.S. at 558.

This definition, however, was applied only in consideration of the validity of the tax on the income from real estate and income from invested personal property, as the issue before the Supreme Court in the first *Pollock* decision was quite limited. The decision of the Court rendered after rehearing, however, was more extensive:

We are now permitted to broaden the field of inquiry, and to determine to which of the two great classes a tax upon a person's **entire income**, whether derived from rents, or products, or otherwise, of real estate, or from bonds, stocks, or other forms of personal property, belongs; and **we are unable to conclude that the enforced subtraction from the yield of all the owner's real or personal property, in the manner prescribed, is so different from a tax upon the property itself, that it is not direct, but an indirect tax, in the meaning of the Constitution.** [Emphasis added.]

Pollock, 158 U.S. at 618.

The *Pollock* Court found there was no substantial difference between a tax on property, which was a direct tax, and a tax on the income derived from the property. The *Pollock* Court overturned the income tax act of 1894 by concluding that income taxes were direct taxes, direct taxes were required by the Constitution to be apportioned; the tax Congress imposed at 28 Stat. 509, c. 349, Section 27, p. 553, was not apportioned, and hence contrary to Article I, Section 2, Clause 3, and Article I, Section 9, Clause 4, of the United States Constitution. That statute read:

Sec. 27. That from and after the first day of January, eighteen hundred and ninety-five, and until the first day of January, nineteen hundred, there shall be assessed, levied, collected, and paid annually upon the gains, profits, and income received in the preceding calendar year by every citizen of the United States, whether residing at home or abroad, and every person residing therein, whether said gains, profits, or income be derived from any kind of property rents, interest, dividends, or salaries, or from any profession, trade, employment, or vocation carried on in the United States or elsewhere, or from any other source whatever, a tax of two per centum on the amount so derived over and above four thousand dollars, and a like tax shall be levied, collected, and paid annually upon the gains, profits, and income from all property owned and of every business, trade, or profession carried on in the United States. And the tax herein provided for shall be assessed, by the Commissioner of Internal Revenue and collected, and paid upon the gains, profits and income for the year ending the thirty-first day of December next preceding the time for levying, collecting, and paying said Tax.”

In rendering this decision, the *Pollock* Court also stated that:

We do not mean to say that an act laying by apportionment a direct tax on all real estate and personal property, or the income thereof, might not also lay excise taxes on business, privileges, employments, and vocations. **But this is not such an act; and the scheme must be considered as a whole.**¹⁵ [Emphasis added.]

Pollock, 158 U.S. at 637.

The *Pollock* Court clearly found that a tax on the entire income of a United States citizen was a direct tax that required apportionment to withstand constitutional validity.

To overcome the opinion of the *Pollock* Court that an income tax was a direct tax which must be apportioned, Congress proposed the Sixteenth Amendment.

After the adoption of the Sixteenth Amendment in 1913, Congress passed an income tax act; see “An Act to reduce tariff duties and to provide revenue for the Government, and for other purposes,” approved October 3, 1913, 38 Stat. 114, ch. 16. Section II of this act, 38 Stat. 166, imposed the following tax:

A. Subdivision 1. That there shall be levied, assessed, collected and paid annually upon the entire net income arising or accruing from all sources in the preceding calendar year to every citizen of the United States, whether residing at home or abroad, and to every person residing in the United States, though not a citizen thereof, a tax of 1 per centum ... and a like tax shall be assessed, levied, collected, and paid annually upon the entire net income from all property owned and of every business, trade, or profession carried on in the United States by persons residing elsewhere.

The Act also taxed the income from corporations at the rate of 1 per centum, and it was the tax on the corporations¹⁶ that was challenged as unconstitutional in *Brushaber*.

Suit was instituted by Mr. Brushaber who was a stockholder of Union Pacific Railroad. The Supreme Court in *Brushaber* was of the opinion that the *Pollock* Court was wrong in classifying income taxes as direct taxes, and ruled as erroneous Mr. Brushaber’s contention that the Sixteenth Amendment authorized only a particular character of direct tax without apportionment. The Court stated:

Indeed in the light of the history which we have given and of the decision in the *Pollock* case and the ground upon which the ruling in that case was based, there is no escape from the conclusion that the Amendment was drawn for the purpose of doing away for the future with the principle upon which the *Pollock* case was decided, that is, of determining whether a tax on income was direct not by a consideration of the burden placed on the taxed income upon which it directly operated, but by taking into view the burden which resulted on the property from which the income was derived, since in express terms the Amendment provides that income taxes, from whatever source the income may be derived, shall not be subject to the regulation of apportionment. From this in substance it indisputably arises, first, that all the contentions which we have previously noticed concerning the assumed limitations to be implied from the language of the Amendment as to the nature and character of the income taxes which it authorizes find no support in the text and are in irreconcilable conflict with the very purpose which the Amendment was adopted to accomplish. Second, that the contention that the Amendment treats a tax on income as a direct tax although it is relieved from apportionment and is necessarily therefore not subject to the rule of uniformity as such rule only applies to taxes which are not direct, thus destroying the two great classifications which have been recognized and enforced from the beginning, is also wholly without foundation since the command of the Amendment that all income taxes shall not be subject to apportionment by a consideration of the sources from which the taxed income may be derived forbids the application to such taxes of the rule applied in the *Pollock* case by which alone such taxes were removed

from the great class of excises, duties and imposts subject to the rule of uniformity and were placed under the other or direct class.

Brushaber, 240 U.S. at 18-19.

This position was reiterated in the opinion in *Stanton v. Baltic Mining Co.*, 240 U.S. 103 (1916), which was also written by Justice White at the same time he wrote the opinion in the *Brushaber* case:

[T]he Sixteenth Amendment conferred no new power of taxation but simply prohibited the previous complete and plenary power of income taxation possessed by Congress from the beginning from being taken out of the category of indirect taxation to which it inherently belonged.

Stanton, 240 U.S. at 112.

The *Brushaber* case also stated:

Moreover in addition the conclusion reached in the *Pollock* case did not in any degree involve holding that income taxes generically and necessarily came within the class of direct taxes on property, but on the contrary recognized the fact that taxation on income was in its nature an excise entitled to be enforced as such unless and until it was concluded that to enforce it would amount to accomplishing the result which the requirement as to apportionment of direct taxation was adopted to prevent, in which case the duty would arise to disregard form and consider substance alone and hence subject the tax to the regulation as to apportionment which otherwise as an excise would not apply to it. Nothing could serve to make this clearer than to recall that in the *Pollock* case in so far as the law taxed incomes from other classes of

property than real estate and invested personal property, that is, income from “professions, trades, employments, or vocations” (158 U.S. 637), its validity was recognized; indeed it was expressly declared that no dispute was made upon that subject and attention was called to the fact that taxes on such income had been sustained as excise taxes in the past. *Id.*, p. 635.

Brushaber, 240 U.S. at 16-17.

Justice White’s opinion in *Brushaber* upheld the constitutional validity of the 1913 Act, and without expressly overruling the *Pollock* decision, held, contrary to *Pollock*, that the income tax was an indirect tax. The conflict between the *Pollock* Court and the *Brushaber* Court is the subject of the next chapter and is fully addressed therein.

The *Brushaber* Court was thus of the opinion that in order for the tax imposed by Congress to withstand constitutional scrutiny, the tax could not be administered as a direct tax within the States;¹⁷ such a tax would continue to require apportionment even under the Sixteenth Amendment.¹⁸

On September 8, 1916, Congress adopted another federal income tax.¹⁹ The income tax in this act was imposed by Section l(a), which read as follows:

That there shall be levied, assessed, collected, and paid annually upon the entire net income received in the preceding calendar year from all sources by every individual, a citizen or resident of the United States, a tax of two per centum upon such income

The 1916 Act, in Section 24, 39 Stat. 776, repealed the 1913 income tax act. On October 3, 1917, Congress passed an Act which amended the 1916 income tax act primarily by increasing the graduated rates of the additional tax.²⁰

On February 24, 1919, the Revenue Act of 1918 was adopted by Congress.²¹ This Act was different from both the 1913 and 1916 Acts in that it imposed a “lieu” tax, or a tax merely in substitution of one previously imposed. This is demonstrated by the plain language of Section 210, 40 Stat. 1062, which read as follows:

That, in lieu of the taxes imposed by subdivision (a) of Section 1 of the Revenue Act of 1916 and by Section 1 of the Revenue Act of 1917, there shall be levied, collected and paid for each taxable year upon the net income of every individual a normal tax at the following rates

The Revenue Act of 1918 did contain provisions to repeal prior acts. In Section 1400 of this Act, the income tax title of the 1916 revenue act was repealed, subject to certain limitations. At Section 1400 (b), 40 Stat. 1150, the last sentence in this Section read as follows:

In the case of any tax imposed by any part of an Act herein repealed, if there is a tax imposed by this Act in lieu thereof, the provision imposing such tax shall remain in force until the corresponding tax under this Act takes effect under the provisions of this Act.

There can be but one construction given to this provision which can sustain the tax. If the entire income tax provisions in the 1916 Act were entirely repealed, then no tax under the 1916 Act would be imposed, and thus nothing would be imposed by the 1918 Act, the tax being simply “in lieu of” the 1916 tax. To sustain the tax itself, Section 210 of the 1916 Act must have continued in effect, only amended or modified by the 1918 Act.

The Revenue Act of 1921 was adopted by Congress on November 23, 1921.²² This Act closely followed the Revenue Act of 1918 in that it also imposed a “lieu” tax. In Section 210 of this Act, 42 Stat. 233, the section imposing the tax read as follows:

That, in lieu of the tax imposed by Section 210 of the Revenue Act of 1918, there shall be levied, collected, and paid for each taxable year upon the net income of every individual a normal tax

Thus, the 1921 Act was in lieu of the 1918 tax, which was in lieu of the 1916 tax. Like the similar repeal provision in the 1918 Act, the 1921 act had a Section 1400 which repealed the 1918 income tax act conditioned as follows at 42 Stat. 321:

In the case of any tax imposed by any part of the Revenue Act of 1918 repealed by this Act, if there is a tax imposed by this Act in lieu thereof, the provision imposing such tax shall remain in force until the corresponding tax under this Act takes effect under the provisions of this Act.

The Revenue Act of 1924 was adopted by Congress on June 2, 1924.²³ Like its predecessors, this Act imposed a tax in Section 210, 43 Stat. 264, which read as follows:

In lieu of the tax imposed by Section 210 of the Revenue Act of 1921, there shall be levied, collected, and paid for each taxable year upon the net income of every individual (except as provided in subdivision (b) of this Section) a normal tax

Thus, this Act imposed a tax in lieu of the 1921 tax, which was in lieu of the 1918 tax, which was in lieu of the 1916 tax. Like the prior acts, the repeal provisions in Section 1100, 43 Stat. 352, repealed the 1921 income tax provisions subject to this condition:

In the case of any tax imposed by any part of the Revenue Act of 1921 repealed by this Act, if there is a tax imposed by this Act in lieu thereof, the provision imposing such tax shall remain in force until the

corresponding tax under this Act takes effect under the provisions of this Act.

Some two years later, Congress enacted the Revenue Act of 1926.²⁴ Section 210 of this Act read almost identically with former acts imposing the tax:

In lieu of the tax imposed by Section 210 of the Revenue Act of 1924, there shall be levied, collected and paid for each taxable year upon the net income of every individual (except as provided in subdivision (b) of this section) a normal tax ...

Thus, this Act imposed a tax in lieu of the 1924 tax, which was in lieu of the 1921 tax, which was in lieu of the 1918 tax, which was in lieu of the 1916 tax. The repeal provisions in this Act were found in Section 1200, 44 Stat. 125, which repealed the 1924 income tax act, subject to this limitation:

In the case of any tax imposed by any part of the Revenue Act of 1924 repealed by this Act, if there is a tax imposed by this Act in lieu thereof, the provision imposing such tax shall remain in force until the corresponding tax under this Act takes effect under the provisions of this Act.

Again, two years later, Congress enacted another act called the Revenue Act of 1928.²⁵ By this time, Congress had been enacting similar legislation for about fifteen years, and it obviously chose to change the format of the income tax acts as an attempt at improvement. The format of this Act was decidedly different from the previous acts, and this format was ultimately used for the 1939 Internal Revenue Code. In this new style, the tax became imposed under Section 11:

Normal Tax on Individuals. There shall be levied, collected, and paid for each taxable year upon the net income of every individual a normal tax

It must be noted that, whereas previously the “in lieu of” feature of the tax appeared directly in the section imposing the tax, this Section 11 made no reference to the same, although the act itself did. Congress took the “in lieu of” feature out of the section imposing the tax and placed it in Section 63 of the Act:

Taxes in Lieu of Taxes Under 1926 Act. The taxes imposed by this title shall be in lieu of the corresponding taxes imposed by Title II of the Revenue Act of 1926, in accordance with the following table:

Taxes under this Title		Taxes under 1926 Act
Secs. 11 and 211	in lieu of	sec. 210
Sec. 12	in lieu of	sec. 211

Thus, this Act imposed an income tax in lieu of the 1926 tax, which was in lieu of the 1924 tax, which was in lieu of the 1921 tax, which was in lieu of the 1918 tax, which was in lieu of the 1916 tax.

The repeal provision in this Act was somewhat different from the previous ones in that there was no section which specifically defined what was repealed. Instead, Section 714 of this Act, 45 Stat. 882, stated:

The parts of the Revenue Act of 1926 which are repealed by this Act shall remain in force for the assessment and collection of all taxes imposed thereby, and for the assessment, imposition, and collection of all interest, penalties, or forfeitures which have accrued or may accrue in relation to any such taxes.

Due to the fact that this Act made the 1926 Act temporary and of no effect for tax years 1928 and afterward, the repeal provision meant little.

Congress did not enact after 1928 another major tax law for four years; on June 6, 1932, it did enact, however, the Revenue Act of 1932.²⁶ This Act was patterned upon its predecessor, the 1928 Act, and it thus had a Section 11 which imposed the tax, and a Section 63 providing the “in lieu of” feature:

Sec. 11. Normal Tax on Individuals. There shall be levied, collected, and paid for each taxable year upon the entire net income of every individual a normal tax ...

Sec. 63. Taxes In Lieu of Taxes Under 1928 Act. The taxes imposed by this title shall be in lieu of the corresponding taxes imposed by the sections of the Revenue Act of 1928 bearing the same numbers.

Since this Act was applicable for tax years 1932 and those subsequent, the prior acts were thus made temporary, and there was no need for repeal provisions, which this Act did not contain.

Two years later, Congress enacted the Revenue Act of 1934.²⁷ Like the 1928 and 1932 Acts, this Act contained a Section 11 and a Section 63 which read as follows:

Sec. 11. Normal Tax on Individuals. There shall be levied, collected, and paid for each taxable year upon the net income of every individual a normal tax

Sec. 63. Taxes In Lieu of Taxes Under 1932 Act. The taxes imposed by this title shall be in lieu of the corresponding taxes imposed by the Revenue Act of 1932.

Since this Act was applicable for tax years after December 31, 1933, the 1932 Act was thus made temporary and this Act contained no repeal provisions.

The next major income tax act of Congress was the Revenue Act of 1936.²⁸ Here, Congress continued the same scheme first established in 1928, with Sections 11 and 63:

Sec. 11. Normal Tax on Individuals. There shall be levied, collected, and paid for each taxable year upon the net income of every individual a normal tax

Sec. 63. Taxes In Lieu of Taxes Under 1934 Act. The taxes imposed by this title and Title IA shall be in lieu of the taxes imposed by Titles I and IA of the Revenue Act of 1934, as amended.

This Act made the 1934 Act, as amended in 1935, temporary, and thus there were no repeal provisions.

Finally, on May 28, 1938, Congress enacted the Revenue Act of 1938.²⁹ This Act followed the format of the similar income tax Acts adopted in 1928, 1932, 1934, and 1936, and this Act established most of the format of the 1939 Internal Revenue Code. Here again, there was a Section 11 and a Section 63 which read as follows:

Sec. 11. Normal Tax on Individuals. There shall be levied, collected, and paid for each taxable year upon the net income of every individual a normal tax

Sec. 63. Taxes In Lieu of Taxes Under 1936 Act. The taxes imposed by this title and Title IA shall be in lieu of the taxes imposed by Titles I and IA of the Revenue Act of 1936, as amended.

Since this Act became effective for years after December 31, 1937, the 1936 Act became temporary and this Act contained no repeal provisions.

On December 31, 1938, there was in existence a federal income tax which was imposed by the Revenue Act of 1938. But this Act simply imposed a tax which was in lieu of the 1936 tax, which was in lieu of the 1934 tax, which was in lieu of the 1932 tax, which was in lieu of the 1928 tax, which was in lieu of the 1926 tax, which was in lieu of the 1924 tax, which was in lieu of the 1921 tax, which was in lieu of the 1918 tax, which was in lieu of the 1916 tax.

At the same time, many other taxes were scattered throughout various Congressional tax acts, and there appeared to Congress a need to consolidate these laws all into one book or act. Hence the effort to enact the 1939 Internal Revenue Code.

On February 10, 1939, the 1939 Internal Revenue Code was approved and became a law.³⁰ In essence, those various internal revenue laws then valid, existing and in force on January 2, 1939, were placed into this one Act which created the Code. Section 4 of the enacting clause of this Code provided that any prior law codified in this act was thereby repealed; but, Section 4 did not operate to repeal any law not so codified. Most of the income tax provisions in the 1939 Code were from the 1938 Revenue Act, and Section 11 of the 1938 Act became Section 11 in the 1939 Code. But, while Sections 1 through 62 of the 1938 Act were placed into the Code, Section 63, which provided for the lieu tax feature, was not incorporated into that Code, and therefore was not repealed. Thus, the 1939 Code was nothing more than an incorporation of the 1938 Act into its provisions, and the unrepealed Section 63 in the 1938 Act operated to make the 1939 Code's income tax laws an act which was in lieu of the 1936 tax.

The unrepealed Section 63 in the 1938 Act operated to make that Code nothing more than a substitute for the 1938 Act. And of course, the 1954 Internal Revenue Code simply replaced the 1939

Internal Revenue Code. Today, the 1986 Code is merely a replacement or substitute for the 1954 Code.

ENDNOTES

8. Act of July 14, 1798, 1 Stat. 597, ch. 75.
9. Act of Aug. 2, 1813, 3 Stat. 63, ch. 37.
10. Act of Jan. 9, 1815, 3 Stat. 164, ch. 21.
11. Act of August 6, 1861; Act of July 1, 1862; Act of March 3, 1863; Act of June 30, 1864; Act of March 3, 1865; Act of March 10, 1866; Act of July 13, 1866, Act of March 2, 1867; and Act of July 14, 1870.
12. See Act of Aug. 5, 1861, 12 Stat. 292, 309, ch. 45.
13. *Pollock*, 157 U.S. at 674.
14. A tax of two percent was imposed upon the net profits of corporations, companies or associations in the 1894 act at Section 32.
15. So, too, the income tax contained in Subtitle A is not such an act; one need only compare the wording of Section 27 of the 1894 Act with the wording of Section 61 (a) of the 1954 Act to ascertain that the tax imposed in Subtitle A is not an excise tax on business, trades or professions.
16. *Brushaber*, 240 U.S. at 9.
17. Attorney General W. M. Evarts concluded as follows in 1871: “We are of the opinion that a tax on the gross income of an individual is embraced by the words “capitation, or other direct tax,” in the Constitution, and should be assessed and collected on the principle of apportionment and not of uniformity, and that the several sections of the Internal Revenue act imposing such tax are therefore unconstitutional. We are further of opinion that no decision of the Supreme Court of the United

States precludes this view or discourages the expectation that it will receive the sanction of the court. On the contrary, there are dicta and suggestions in the only decisions bearing upon the subject which tend to confirm the opinion we have expressed.” 13 Internal Revenue Record 76.

18. Relying upon this proposition, Attorney Lowell Becraft of Huntsville, Alabama, has made a powerful territorial/legislative jurisdictional argument that under the Supreme Court’s holding in *Brushaber*, the income tax cannot be imposed anywhere except within those limited areas within the states in which the Federal government has exclusive legislative authority under Article I, Section 8, Clause 17, of the United States Constitution, such as on military bases, national forests, etc., and within United States territories, such as Puerto Rico, etc. Indeed, Treasury Department delegation orders and the language of Treasury Regulation 26 C.F.R. Section 1.1-l(c) fully supports Mr. Becraft’s scholarly analysis. Thus, whether one relies upon the Supreme Court’s opinion in *Pollock* or its opinion in *Brushaber*, a tax upon a States citizen’s wages (personal property) falls without constitutional authority.
19. See “An Act To Increase The Revenue, And For Other Purposes,” 39 Stat. 756, ch. 463.
20. See “An Act To Provide Revenue To Defray War Expenses, And For Other Purposes”, 40 Stat. 300, ch. 63.
21. See “An Act To Provide Revenue, And For Other Purposes”, 40 Stat. 1057, ch. 18.
22. See “An Act To Reduce And Equalize Taxation, To Provide Revenue, And For Other Purposes,” 42 Stat. 227, ch. 136.
23. See “An Act To Reduce And Equalize Taxation, To Provide Revenue, And For Other Purposes,” 43 Stat. 253, ch. 234.

24. See “An Act To Reduce And Equalize Taxation, To Provide Revenue, And For Other Purposes,” 44 Stat. 9, ch. 27.
25. See “An Act To Reduce And Equalize Taxation, Provide Revenue, And For Other Purposes,” 45 Stat. 791, ch. 852.
26. See “An Act To Provide Revenue, Equalize Taxation, And For Other Purposes,” 47 Stat. 169, ch. 209.
27. See “An Act To Provide Revenue, Equalize Taxation, And For Other Purposes,” 48 Stat. 680, ch. 227.
28. See “An Act To Provide Revenue, Equalize Taxation, And For Other Purposes,” 49 Stat. 1648, ch. 690.
29. See “An Act To Provide Revenue, Equalize Taxation, And For Other Purposes,” 52 Stat. 447, ch. 289.
30. See 53 Stat., part 1.

CHAPTER II

DIRECT OR INDIRECT TAX

The distinction between direct and indirect taxation is fundamental to the federal government's constitutional power to lay and collect taxes from the citizens of the several states which comprise the United States of America. However, some 200 years after the ratification of the United States Constitution, it remains unsettled whether the federal income tax is a direct or an indirect tax.

The *Pollock* case is the leading decision from the United States Supreme Court which supports the proposition that the federal income tax is a direct tax. The *Brushaber* case is the leading decision from the Supreme Court which supports the proposition that the federal income tax is an indirect tax.

By virtue of the legislative history regarding the proffer of the Sixteenth Amendment, it cannot be denied that Congress intended to tax incomes. The question thus becomes, is the income tax a direct tax that is relieved from the requirement of apportionment by ratification of the Sixteenth Amendment or did the Amendment serve to define a tax on income as an indirect, excise tax? This analysis answers that question.

In 1894, Congress passed an income tax, and its constitutional validity was challenged. In *Pollock*, the United States Supreme Court held the income tax, as enacted and administered, was an unapportioned direct tax, and struck it down as repugnant to Article I, Section 2, Clause 3, and Article I, Section 9, Clause 4, of the Constitution.

In 1909, during a special session of Congress called by President Taft, the Sixteenth Amendment was proposed and sent to the States for ratification; it was certified as ratified in 1913.

Congress then enacted the Tariff Act of October 3, 1913, which contained income tax provisions, and those provisions were challenged as unconstitutional. In *Brushaber*, the United States Supreme Court upheld the income tax provisions as constitutional. In the process, however, it held the income tax to be an indirect tax by virtue of the operation of the Sixteenth Amendment.

The *Pollock* Court used the following language in defining a direct tax:

Ordinarily, all taxes paid primarily by persons who can shift the burden upon someone else, or who are under no legal compulsion to pay them, are considered indirect taxes; but a tax upon property holders in respect of their estates, whether real or personal, **or of the income yielded by such estates**, and the payment of which cannot be avoided, are direct taxes. [Emphasis added.]

Pollock, 157 U.S. at 558.

On rehearing, however, the Supreme Court enlarged the definition of a direct tax:

We are now permitted to broaden the field of inquiry, and to determine to which of the two great classes a tax upon a person's entire income, whether derived from rents, or products, or otherwise, of real estate, or from bonds, stocks, or other forms of personal property, belongs; and **we are unable to conclude that the enforced subtraction from the yield of all the owner's real or personal property, in the manner prescribed, is so different from a tax upon the property itself, that it is not direct, but an indirect tax, in the meaning of the Constitution.** [Emphasis added.]

Pollock, 158 U.S. at 618.

In direct contravention to the *Pollock* opinion that income taxes are direct within the meaning of the Constitution, the *Brushaber* Court said:

(T)he conclusion reached in the *Pollock* case did not in any degree involve holding that income taxes generically and necessarily came within the class of direct taxes on property

Brushaber, 240 U.S. at 16-17.

It is interesting to note that this alleged conclusion of the *Pollock* Court is not in quotes, nor is there a page reference to the *Pollock* decision. The absence of such a page reference is because the *Pollock* Court never stated such a conclusion.

The *Brushaber* Court was of the opinion that Mr. Brushaber was raising the issue that the Sixteenth Amendment provided for a power to tax not previously in existence:

We are of the opinion, however, that the confusion is not inherent, but rather arises from the conclusion that the Sixteenth Amendment provides for a hitherto unknown power of taxation, that is, a power to levy an income tax which although direct should not be subject to the regulation of apportionment applicable to all other direct taxes.

Brushaber, 240 U.S. at 10-11.

The Court then listed the several contentions made by Mr. Brushaber, and said:

But it clearly results that the proposition and the contentions under it, if acceded to, would cause one provision of the Constitution to destroy another; that

is, they would result in bringing the provisions of the Amendment exempting a direct tax from apportionment into irreconcilable conflict with the general requirement that all direct taxes be apportioned. Moreover, the tax authorized by the Amendment, being direct, would not come under the rule of uniformity applicable under the Constitution to other than direct taxes, and thus it would come ' to pass that the result of the Amendment would be to authorize a particular direct tax not subject either to apportionment or to the rule of geographical uniformity, thus giving power to impose a different tax in one State or States than was levied in another State or States.

Brushaber, 240 U.S. at 11-12.

The Court was, however, aware of the fact that the requirement as to apportionment of a direct tax was regulatory:

In fact the two great subdivisions embracing the complete and perfect delegation of the power to tax and the two correlated limitations as to such power were thus aptly stated by Mr. Chief Justice Fuller in *Pollock v. Farmers' Loan & Trust Company*, *supra*, at page 557: "In the matter of taxation, the Constitution recognizes the two great classes of direct and indirect taxation, and lays down two rules by which their imposition must be governed, namely: The rule of apportionment as to direct taxes, and the rule of uniformity as to duties, imposts and excises." It is to be observed, however, as long ago pointed out in *Veazie Bank v. Fenno*, 8 Wall 533, 541, that the requirement of apportionment as to one of the great classes and of uniformity as to the other class were not so much a limitation upon the complete and all embracing authority to tax, **but in their essence**

were simply regulations concerning the mode in which the plenary power was to be exerted.
[Emphasis added.]

Brushaber, 240 U.S. at 13.

Recognizing that the two requirements were but regulations prescribed in the Constitution, nothing prevented Congress from amending the Constitution to change one or both of the regulations. In fact, this is exactly what the *Pollock* Court specifically suggested as the proper course for Congress to take if it did not like the result of the *Pollock* decision:

In these cases our province is to determine whether this income tax on the revenue from property does or does not belong to the class of direct taxes. If it does, it is, being unapportioned, in violation of the Constitution, and we must so declare.

Differences have often occurred in this court—differences exist now—but there has never been a time in its history when there has been a difference of opinion as to its duty to announce its deliberate conclusions unaffected by considerations not pertaining to the case in hand.

If it be true that the Constitution should have been so framed that a tax of this kind [a direct income tax] could be laid [without apportionment], the instrument defines the way for its amendment. [Emphasis added.]

Pollock, 158 U.S. at 634-635.

At pages 14 and 15 of its opinion, the *Brushaber* Court discussed the case of *Hylton v. United States*, 2 U.S. 171 (1796), wherein the Supreme Court found that the carriage tax was valid because it was

an excise tax. The two *Pollock* decisions discussed this case in great detail. Some interesting and extremely important points are relevant:

It will be perceived that each of the justices, while suggesting doubt whether anything but a capitation or a land tax was a direct tax within the meaning of the constitution, distinctly avoided expressing an opinion upon that question or laying down a comprehensive definition, but confined his opinion to the case before the court.

The general line of observation was obviously influenced by Mr. Hamilton's brief for the government, in which he said: "The following are presumed to be the only direct taxes: Capitation or poll taxes, taxes on lands and buildings, general assessments, whether on the whole property of individuals, or on their whole real or personal estate. All else must, of necessity, be considered as indirect taxes." 7 Hamilton's Works (Lodge's Ed.) 332.

Mr. Hamilton also argued: "If the meaning of the word "excise" is to be sought in a British statute, it will be found to include the duty on carriages, which is there considered as an "excise". * * * An argument results from this, though not perhaps a conclusive one, yet, where so important a distinction in the constitution is to be realized, it is fair to seek the meaning of terms in the statutory language of that country from which our jurisprudence is derived." 7 Hamilton's Works (Lodge's Ed.) 333.

If the question had related to an income tax, the reference would have been fatal, as such taxes have been always classed by the law of Great Britain as direct taxes.

Pollock, 157 U.S. at 571-572.

After discussing the direct tax acts of Congress (Act of July 9, 1798; Act of July 14, 1798; Act of July 22, 1813; Act of August 2, 1813; Act of January 9, 1815) attributable to the War of 1812, and the direct tax acts of Congress (Act of August 6, 1861; Act of July 1, 1862; Act of March 3, 1863; Act of June 30, 1864; Act of March 3, 1865; Act of March 10, 1866; Act of July 13, 1866, Act of March 2, 1867; Act of July 14, 1870) attributable to the Civil War, the Court said:

The differences between the latter acts and that of August 15, 1894, call for no remark of this connection. These acts grew out of the war of the Rebellion, and were, to use the language of Mr. Justice Miller, “part of the system of taxing incomes, earnings, and profits adopted during the late war, and abandoned as soon after that war was ended as it could be done safely.” *Railroad Co. v. Collector*, 100 U.S. 595, 598.

Pollock, 157 U.S. at 573.

The Court then went on to say:

From the foregoing it is apparent (1) that the distinction between the direct and indirect taxation was well understood by the framers of the constitution and those who adopted it; (2) that, under the state systems of taxation, all taxes on real estate or personal property or the rents or income thereof were regarded as direct taxes; (3) that the rules of apportionment and of uniformity were adopted in view of that distinction and those systems; (4) that whether the tax on carriages was direct or indirect was disputed, but the tax was sustained as a tax on the use and as an excise; (5) that the original expectation was that the power of direct taxation would be exercised only in extraordinary exigencies; and down to August 15,

1894, this expectation has been realized. The act of that date was passed in a time of profound peace, and if we assume that no special exigency called for unusual legislation, and that resort to this mode of taxation is to become an ordinary and usual means of supply, that fact furnishes an additional reason for circumspection and care in disposing of the case.

Pollock, 157 U.S. at 573-574.

On rehearing, the *Pollock* Court had this to say regarding *Hylton*:

In this connection it may be useful, though at the risk of repetition, to refer to the views of Hamilton and Madison as thrown into relief in the pages of the *Federalist*, and in respect of the enactment of the carriage tax act, and again to briefly consider the *Hylton* case, 3 Dall. 171, so much dwelt on in argument.

The Act of June 5, 1794, c. 45, 1 Stat. 373, laying duties upon carriages for the conveyance of persons, was enacted in a time of threatened war.

The bill passed the House on the twenty-ninth of May, apparently after a very short debate. Mr. Madison and Mr. Ames are the only speakers on that day reported in the *Annals*. "Mr. Madison objected to this tax on carriages as an unconstitutional tax; and, as an unconstitutional measure, he would vote against it." Mr. Ames said: "It was not to be wondered at if he, coming from so different a part of the country, should have a different idea of this tax from the gentleman who spoke last. In Massachusetts, this tax had been long known; and there it was called an excise. It was difficult to define whether a tax is direct or not. He

had satisfied himself that this was not so.” Annals, 3d Cong. 730.

On the first of June, 1794, Mr. Madison wrote to Mr. Jefferson: “The carriage tax, which only struck at the Constitution, has passed the House of Representatives.” 3 Madison’s Writings, 18. The bill then went to the Senate, where, on the third day of June, it “was considered and adopted,” Annals, 3d Cong. 119, and on the following day it received the signature of President Washington...

It appears then that Mr. Madison regarded the carriage tax bill as unconstitutional, and accordingly gave his vote against it, although it was to a large extent, if not altogether, a war measure.

Where did Mr. Hamilton stand? At that time he was Secretary of the Treasury, and it may therefore be assumed, without proof, that he favored the legislation. But upon what ground? He must, of course, have come to the conclusion that it was not a direct tax. Did he agree with Fisher Ames, his personal and political friend, that the tax was an excise? The evidence is overwhelming that he did.

In the thirtieth number of the Federalist, after depicting the helpless and hopeless condition of the country growing out of the inability of the confederation to obtain from the States the moneys assigned to its expenses, he says: “The more intelligent adversaries of the new Constitution admit the force of this reasoning; but they qualify their admission, by a distinction between what they call **internal** and **external** taxation. The former they would reserve to the state governments; the latter, which they explain into commercial imposts, or rather

duties on imported articles, they declare themselves willing to concede to the Federal Head.” In the thirty-sixth number, while still adopting the division of his opponents, he says: “The taxes intended to be comprised under the general denomination of internal taxes, may be subdivided into those of the **direct** and those of the **indirect** kind. ... As to the latter, **by which must be understood duties and excises on articles of consumption**, one is at a loss to conceive, what can be the nature of the difficulties apprehended.” Thus we find Mr. Hamilton, while writing to induce the adoption of the Constitution, first, dividing the power of taxation into **external** and **internal**, putting into the former the power of imposing duties on imported articles and into the latter all remaining powers; and, **second** dividing the latter into **direct** and **indirect**, putting into the latter, duties and excises on articles of consumption. “

It seems to us to inevitably follow that in Mr. Hamilton’s judgment at that time all internal taxes, except duties and excises on articles of consumption, fell into the category of direct taxes.

Did he, in supporting the carriage tax bill, change his views in this respect? His argument in the *Hylton* case in support of the law enables us to answer this question. It was not reported by Dallas, but was published in 1851 by his son in the edition of all Hamilton’s writings except the Federalist. After saying that we shall seek in vain for any legal meaning of the respective terms “direct and indirect taxes,” and after forcibly stating the impossibility of collecting the tax if it is to be considered a direct tax, he says, doubtfully: “The following are presumed to be the only direct taxes. Capitation or poll taxes. Taxes on lands and buildings. General assessments, whether on the whole

property of individuals, or on their whole real or personal estate; all else must of necessity be considered as indirect taxes.” **“Duties, imposts and excises** appear to be contradistinguished from **taxes.**” “If the meaning of the word **excise** is to be sought in the British statutes, it will be found to include the duty on carriages, which is there considered as an **excise.**” “Where so important a distinction in the Constitution is to be realized, it is fair to seek the meaning of terms in the statutory language of that country from which our jurisprudence is derived.” 7 Hamilton’s Works, 848. Mr. Hamilton therefore clearly supported the law which Mr. Madison opposed, for the same reason that his friend Fisher Ames did, because it was an excise, and as such was specifically comprehended by the Constitution. Any loose expressions in definition of the word “direct,” so far as conflicting with his well-considered views in the Federalist, must be regarded as the liberty which the advocate usually thinks himself entitled to take with his subject.³¹ He gives, however, it appears to us, a definition which covers the question before us. A tax upon one’s whole income is a tax upon the annual receipts from his whole property, and as such falls within the same class as a tax upon that property, and is a direct tax, in the meaning of the Constitution. And Mr. Hamilton in his report on the public credit, in referring to contracts with citizens of a foreign country, said: “This principle, which seems critically correct, would exempt as well the income as the capital of the property. It protects the use, as effectually as the thing. What, in fact, is property, but a fiction, without the beneficial use of it? In many cases, indeed, the **income or annuity** is the property itself.” 3 Hamilton’s Works, 34.

We think there is nothing in the *Hylton* case in conflict with the foregoing. The case is badly reported. [Emphasis in original.]

Pollock, 158 U.S. at 623-626.

Commencing on page 15, the *Brushaber* Court discussed the tax acts passed from 1861 and continuing through the Civil War period, and erroneously stated that these were excise taxes. As quoted above, the *Pollock* Court considered these taxes in detail, found there was no substantial difference between these taxes and the income tax of 1894, held that because an income tax was now attempted to be levied in times of profound peace the issue had to be examined carefully, and held the tax to be an unapportioned direct tax and therefore unconstitutional.

The *Brushaber* Court then stated that the act of 1894 was assumed³² to come within the classification of excises, duties and imposts which were subject to the rule of uniformity but not to the rule of apportionment; that the constitutional validity of the law was challenged as levying a tax that was direct in the constitutional sense, and the *Pollock* Court was obliged to determine whether the tax was direct or indirect. The *Brushaber* Court stated:

Coming to consider the validity of the tax from this point of view, **while not questioning at all that in common understanding IT WAS DIRECT merely on income and only indirect on property**, it was held that considering the substance of things, it was direct on property in the constitutional sense since to burden an income by a tax was from the point of substance to burden the property from which the income was derived and thus accomplished the very thing which the provision as to apportionment of direct taxes was adopted to prevent. [Emphasis added.]

Brushaber, 240 U.S. at 16.

This quote shows that the *Brushaber* Court completely ignored the reasoning behind *Pollock*. *Pollock* held that there was no distinction between a tax on property and a tax on the income yielded therefrom; the tax on property was a direct tax, and the tax on income was a direct tax. The question of “source” was raised by the parties to the *Pollock* case in their legal briefs, and disposed of by the Court as follows:

But if, as contended, the interest when received has become merely money in the recipient’s pocket, and taxable as such without reference to the source from which it came, the question is immaterial whether it could have been originally taxed at all or not. This was admitted by the Attorney General with characteristic candor; and it follows that, if the revenue derived from municipal bonds cannot be taxed because the source cannot be, the same rule applies to revenue from any other source not subject to the tax; and the lack of power to levy any but an apportioned tax on real and personal property equally exists as to the revenue therefrom.

Admitting that this act taxes the income of property irrespective of its source still we cannot doubt that such a tax is necessarily a direct tax in the meaning of the Constitution.

In England, we do not understand that an income tax has ever been regarded as other than a direct tax. In Dowell’s *History of Taxation and Taxes in England*, admitted to be the leading authority, the evolution of taxation in that country is given, and an income tax is invariably classified as a direct tax. 3 Dowell, (1884), 103, 126. The author refers to the grant of a fifteenth and tenth and a graduated income tax in 1435, and to

many subsequent comparatively ancient statutes as income tax laws. 1 Dowell, 121. It is objected that the taxes imposed by these acts were not, scientifically speaking, income taxes at all, and that although there was a partial income tax in 1758, there was no general income tax until Pitt's of 1799. Nevertheless, the income taxes levied by these modern acts, Pitt's, Addington's, Petty's, Peel's and by existing laws, are all classified as direct taxes; and, so far as the income tax we are considering is concerned, that view is concurred in by the cyclopaedists, the lexicographers, and the political economists, and generally by the classification of European governments wherever an income tax obtains. [Emphasis added.]

Pollock, 158 U.S. at 630-631.

In addition, Justice White accidentally admitted the falsity of his position that an income tax is an excise when he said that the income tax of 1894 was indirect on property, but "direct on income," thereby admitting an income tax is a direct tax.

The *Brushaber* Court continued:

As this conclusion but enforced a regulation as to the mode of exercising power under particular circumstances, it did not in any way dispute the all embracing taxing authority possessed by Congress, including necessarily therein the power to impose income taxes if only they conformed to the constitutional regulations which were applicable to them.

Brushaber, 240 U.S. at 16.

Here the *Brushaber* Court recognized that income taxes must be apportioned, a result that requires the conclusion that income taxes are direct taxes.

The *Brushaber* Court then made another erroneous finding about what the *Pollock* Court held:

Moreover in addition the conclusion reached in the *Pollock* case did not in any degree involve holding that income taxes generically and necessarily came within the class of direct taxes on property but on the contrary recognized the fact that taxation on income was in its nature an excise entitled to be enforced as such unless and until it was concluded that to enforce it would amount to accomplishing the result which the requirement as to apportionment of direct taxation was adopted to prevent, in which case the duty would arise to disregard form and consider substance alone and hence subject the tax to the regulation as to apportionment which otherwise as an excise would not apply to it. Nothing could serve to make this clearer than to recall that in the *Pollock* case in so far as the law taxed income from other classes of property than real estate and invested personal property, that is, income from “professions, trades, employments, or vocations” (158 U.S. 637), its validity was recognized; indeed it was expressly declared that no dispute was made upon that subject and attention was called to the fact that taxes on such income had been sustained as excise taxes in the past. *Id.*, p. 635

Brushaber, 240 U.S., at 16-17.

This statement by the *Brushaber* Court attributed to the *Pollock* Court is false. What the *Pollock* Court actually stated at page 635 was:

We have considered the act only in respect of the tax on income derived from real estate, and from invested personal property, and have not commented on so much of it as bears on gains or profits from business, privileges, or employments, in view of the instances in which taxation on business, privileges, or employments has assumed the guise³³ of an excise tax and been sustained as such. [Emphasis added.]

Pollock, 158 U.S. at 635.

The *Pollock* Court was acutely aware that the facts before it did not allow the Court to decide the issue of whether the statute, as it applied to the taxation of income from professions, trades, employments or vocations was constitutional,³⁴ and avoided making a finding. But the Court had to consider whether it should declare the entire law unconstitutional or leave those sections not in issue in the case to stand:

[I]t is evident that the income from realty formed a vital part of the scheme for taxation embodied therein. If that be stricken out, and also the income from all invested personal property, bonds, stocks, investments of all kinds, it is obvious that by far the largest part of the anticipated revenue would be eliminated, and this would leave the burden of the tax to be borne by professions, trades, employments, or vocations; and in that way what was intended as a tax on capital would remain in substance as a tax on occupations and labors. We cannot believe that such was the intention of Congress. We do not mean to say that an act laying by apportionment a direct tax on all real estate and personal property, or the income thereof, might not also lay excise taxes on business, privileges, employments, and vocations. **But this is not such an act;** and the scheme must be considered as a whole. [Emphasis added.]

Pollock, 158 U.S. at 636-637.

This quote raises an interesting point. No more tax would be collected from those engaged in business, vocations, occupations or employments than if the other provisions were not struck down in that the amount of revenue that could be collected from business, privileges, employments and vocations was specifically set by the statute. The government would only collect less revenue. Thus the *Pollock* Court must have had an ulterior motive in making its statement, and I submit it did not want to see occupations and labor burdened with a tax disguised as an excise when it knew full well that such taxes were direct, and would be levied without apportionment. The *Pollock* Court was precluded from coming right out and saying the statute imposing such taxes was unconstitutional because the case did not involve that issue, so it said instead that such taxes had been sustained in the past having **assumed the guise** of an excise tax, and ruled the entire law unconstitutional, thus prohibiting the levying and collection of the tax on business, privileges, employments and vocations due to its inherent unconstitutionality. I submit the language “assumed the guise” of an excise tax does not support the conclusion attributable to it by *Brushaber* that a tax on the income derived from business, trades and professions is to be legally classified as an excise tax.

The *Brushaber* Court, after quoting the Sixteenth Amendment, stated:

It is clear on the face of this text that it does not purport to confer power to levy income taxes in a generic sense—an authority already possessed and never questioned—or to limit and distinguish between one kind of income taxes and another, but that the whole purpose of the Amendment was **to relieve all income taxes** when imposed from apportionment from a consideration of the source whence the income was derived. [Emphasis added.]

Brushaber, 240 U.S. at 17-18.

The *Brushaber* Court stated that the Sixteenth Amendment required all income to be treated alike without any distinction to be made between one kind of income tax and another. The *Brushaber* Court recognized income taxes as direct taxes, but held that if the source is not considered, which it could no longer be because of the Sixteenth Amendment, then the income tax would once again be considered an indirect tax which would not have to be apportioned. The Court continued:

Indeed, in the light of the history which we have given and of the decision in the *Pollock* case and the ground upon which the ruling in that case was based, there is no escape from the conclusion that the Amendment was drawn for the purpose of doing away for the future with the principle upon which the *Pollock* case was decided, that is, of determining whether a tax on income was direct not by a consideration of a burden placed on the taxed income upon which it directly operated, but by taking into view of the burden which resulted on the property from which the income was derived, since in express terms the Amendment provides that income taxes, from whatever source the income may be derived, shall not be subject to the regulation of apportionment.

Brushaber, 240 U.S. at 18.

This sentence needs careful analysis. It states the purpose of the Amendment was to do away with a principle allegedly laid down in the *Pollock* decision by Chief Justice Fuller in determining if the tax on income was a direct tax, thereby precluding the resort to that principle in the future. The next part of the sentence identifies the principle in two parts:

1. **NOT CONSIDERING** the burden placed on the taxed income, but;
2. **CONSIDERING** the burden which resulted on the property from which the income was derived.

In other words, the purpose of the amendment was to direct the Supreme and lower courts to only consider the burden on the income itself in determining if a subsequent income tax act imposed a direct or an indirect tax. Having determined this to be the purpose of the Sixteenth Amendment, the Court reached its ultimate conclusion that the income tax is not a direct tax which is relieved from the requirement of apportionment:

From this in substance it indisputably arises ... that the contention that the Amendment treats a tax on income as a direct tax although it is relieved from apportionment and is necessarily therefore not subject to the rule of uniformity as such rule only applies to taxes which are not direct, thus destroying the two great classifications which have been recognized and enforced from the beginning, is also wholly without foundation since the command of the Amendment that all income taxes shall not be subject to apportionment by a consideration of the sources from which the taxed income may be derived, forbids the application to such taxes on the rule applied in the *Pollock* case by which alone such taxes were removed from the great class of excises, duties and imposts subject to the rule of uniformity and were placed under the other or direct class.

Brushaber, 240 U.S. at 18-19.

Thus the *Brushaber* Court thought that in holding income taxes to be direct taxes, the *Pollock* Court used the principle of “considering the source from which the taxed income was derived” as the key in

its analysis, and that by removing this key, the income tax would be classified as an indirect tax. However, in using the language pattern “not by... but by...,” it suggested that the determination be made by considering the burden imposed on the income, and that is exactly the principle upon which the *Pollock* case was determined. The *Pollock* Court did not resort to a consideration of the source to reach its conclusion, but found that from the earliest enactment of income taxes in England and other European Countries, and in enactments imposing state income taxes prior to the adoption of the Constitution, such taxes were always deemed to be direct taxes. *Pollock* also relied upon the definition of direct taxes given by Hamilton in the *Federalist Papers*, the fact that incomes are personal property of general distribution, the candid admission of the Attorney General, and the views of cyclopaedists, lexicographers, and political economists. In stating that it was unable to conclude that the enforced subtraction from the yield of all the owner’s real or personal property, in the manner prescribed, was not any different than a tax on real or personal property, the *Pollock* Court was merely stating that any tax on real or personal property, including income, was considered by the framers of the Constitution to be a direct tax and subject to the rule of apportionment.

The *Brushaber* Court then reiterated the reason for its opinion:

We say this because it is to be observed that although from the date of the *Hylton* case because of statements made in the opinions in that case it had come to be accepted that direct taxes in the constitutional sense were confined to taxes levied directly on real estate because of its ownership, the Amendment contains nothing repudiating or challenging the ruling in the *Pollock* case that the word direct had a broader significance since it embraced also taxes levied directly on personal property because of its ownership, and therefore the Amendment at least impliedly makes such wider

significance a part of the Constitution—a condition which clearly demonstrates that the purpose was not to change the existing interpretation except to the extent necessary to accomplish the result intended, that is, the prevention of the resort to the sources from which a taxed income was derived in order to cause a direct tax on the income to be a direct tax on the source itself and thereby to take an income tax out of the class of excises, duties and imposts and place it in the class of direct taxes.

Brushaber, 240 U.S. at 19.

The *Brushaber* Court first stated that the Sixteenth Amendment impliedly recognized the broader classification of direct taxes propounded in *Pollock*, which classification encompassed **all personal and real property**. The *Brushaber* Court next stated the purpose of the Sixteenth Amendment was limited to changing existing interpretations [a clear reference to *Pollock*] to the extent necessary to accomplish the result necessary, and identified what it believed the intended result was to be:

[T]he prevention of the resort to the sources from which a taxed income was derived in order to cause a **direct tax on the income** to be a direct tax on the source itself and thereby to take an income tax out of the class of excises, duties and imposts and place it in the class of direct taxes. [Emphasis added.]

Brushaber, id.

After stating the income tax is a direct tax, how could Justice White contend it belonged in the class of excises, duties and imposts? Only by claiming the purpose of the Sixteenth Amendment was to change an admittedly direct tax into an indirect tax. He tells us this can be done because the only way it became a direct tax in the first place was by the *Pollock* Court's consideration of the source. However,

the *Pollock* Court never once said that an income tax was anything but a direct tax, clearly showing that the *Pollock* Court did not take the income tax out of the class of indirect taxes as claimed by the *Brushaber* Court. According to *Pollock*, income taxes had always been considered to be direct taxes in their own right because they operated directly on the ownership of personal property [including income], a result reached when considering the burden on the income itself. Since the *Pollock* Court used the correct principle, the position expressed by the *Brushaber* Court as to the purpose of the Amendment is clearly incorrect.

The absurd result of the *Brushaber* Court's reasoning as to the application of the alleged *Pollock* principle is shown as follows: 1) the *Brushaber* Court stated the tax is direct on income but indirect on the source, 2) by considering the burden on the income, the burden on the source is changed from indirect to direct, 3) this process somehow "causes" the direct tax on income to become an indirect tax. (*Brushaber*, 240 U.S. at 19.)

Now compare what the Supreme Court in *Eisner v. Macomber*, 252 U.S. 189 (1920), stated was the intended result of the Sixteenth Amendment:

The Sixteenth Amendment must be construed in connection with the taxing clauses of the original Constitution and the effect attributed to them before the Amendment was adopted. In *Pollock v. Farmers' Loan and Trust Co.*, 158 U.S. 601, under the Act of August 27, 1894, c. 349, Section 27, 28 Stat. 509, 553, it was held that taxes upon rents and profits of real property were in effect direct taxes upon the property from which such income arose,³⁵ imposed by reason of ownership; and that Congress could not impose such taxes without apportioning them among the States according to population, as required by Art. I, section 2, cl. 3, and section 9, cl. 4, of the original Constitution.

Afterwards, and evidently in recognition of the limitation upon the taxing power of Congress thus determined, the Sixteenth Amendment was adopted, **in words lucidly expressing the object to be accomplished: “The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.”** As repeatedly held, this did not extend the taxing power to new subjects, but merely removed the necessity which otherwise might exist for an apportionment among the States of taxes laid on income. [Citing *Brushaber*, 240 U.S. at 17-19, and other cases.]

A proper regard for its genesis, as well as its very clear language, requires also that this Amendment shall not be extended by loose construction, so as to repeal or modify, except as applied to income, those provisions of the Constitution that require an apportionment according to population for direct taxes upon property, real and personal. This limitation still has an appropriate and important function, and is not to be over ridden by Congress or disregarded by the courts.

In order, therefore, that the clauses cited from Article I of the Constitution may have proper force and effect, save only as modified by the Amendment, and that the latter also may have proper effect, it becomes essential to distinguish between what is and what is not “income” as the term is there used; and to apply the distinction, as cases arise, according to truth and substance, without regard to form. Congress cannot by any definition it may adopt conclude the matter, since it cannot by legislation alter the Constitution,

from which alone it derives its power to legislate, and within whose limitations alone that power can be lawfully exercised. [Emphasis added.]

Eisner, 252 U.S. at 205-206.

It is legally significant to note that in stating the purpose of the Sixteenth Amendment the *Eisner* Court found no necessity to add additional words, but the *Brushaber* Court did, in clear contravention to established legal principles:

The words of the Constitution are to be taken in their obvious sense, and to have a reasonable construction. In *Gibbons v. Ogden*, Mr. Chief Justice Marshall, with his usual felicity, said: "As men, whose intentions require no concealment, generally employ the words which most directly and aptly express the ideas they intend to convey, the enlightened patriots who framed our Constitution, and the people who adopted it must be understood to have employed words in their natural sense, and to have intended what they have said." 9 Wheat. 1, 188.

Pollock, 158 U.S. at 619.

I submit that the *Brushaber* Court had to use extra words in stating the purpose of the Sixteenth Amendment because *Brushaber* misstates the intent of Congress in proposing the Sixteenth Amendment. To support the *Brushaber* decision, it would have to be shown that Congress wanted to overturn the *Pollock* decision that income taxes are direct taxes. This follows because it is clear that the *Brushaber* Court believed the Sixteenth Amendment prevented income taxes from being classed as direct taxes by reference to the source, thereby placing them in the only other possible class, indirect taxes. Yet the *Brushaber* Court proves the invalidity of its decision when it stated in its opinion that Congress obviously did not challenge or repudiate the holding of the *Pollock*

Court that a tax on real and personal property, imposed by reason of its ownership, was a direct tax in the constitutional sense. The Sixteenth Amendment was not proposed in the form: Income taxes are indirect taxes and do not require apportionment! It was proposed that Congress shall have the power to lay and collect taxes on incomes without apportionment. If income taxes were not direct taxes, why did the Sixteenth Amendment remove the need to apportion them, when even *Brushaber* recognized that indirect taxes do not have to be apportioned? I submit the *Brushaber* decision fails to recognize that *Pollock* did consider the burden imposed on the income itself, and reached the conclusion that income taxes were direct taxes in the constitutional sense.

No other case in the history of income taxation went into such depth on the issue of what is and is not a direct tax as did *Pollock*. This issue was extensively researched and briefed by the parties involved in the case and by the Supreme Court. Justice White, being unable to refute this fact of law neither overruled the *Pollock* holding nor disputed it; instead Justice White held that the purpose of the Sixteenth Amendment was to prevent the use of the “*Pollock* principle.” It is my opinion that Justice White’s indirect attempt to overturn *Pollock* is wholly unpersuasive; he clearly failed to state a historical, factual or legal basis for his conclusion that a tax on income is an indirect, excise tax.

It is clear that Mr. Brushaber and his attorneys correctly stated the proposition to the Supreme Court that the Sixteenth Amendment relieved the income tax, which was a direct tax, from the requirement of apportionment, and that the *Brushaber* Court failed miserably in attempting to refute Mr. Brushaber’s legal position.

A tax imposed on all of a person’s annual gross receipts is a direct tax on personal property that must be apportioned. A tax imposed on the “income” derived from those gross receipts is also a direct tax on property, but as a result of the Sixteenth Amendment, Congress no longer has to enact legislation calling for the apportionment of a tax on that income. As stated in *Eisner*, the

issue does indeed become, “What is and what is not income?” That question is answered in the next chapter.

ENDNOTES

31. It appears that Mr. Hamilton was a forerunner of today's typical politician, saying one thing to be elected and doing the complete opposite once in office.
32. Who made this assumption is not stated in the *Brushaber* opinion.
33. The word "guise" is defined in Webster's Third New International Dictionary as: "A superficial seeming: an artful or simulated appearance (as of propriety or worth)<that such misconduct should take the guise of religious ritual is shameful> <tricked the widow in the guise of a friend of her late husband>"
34. See, *Pollock*, 157 U.S. at 687, quoting from the case of *Cohens v. Virginia*, 6 Wheat. 264, 399: "It is a maxim not to be disregarded that general expressions, in every opinion, are to be taken in connection with the case in which those expressions are used. If they go beyond the case, they may be respected, but ought not to control the judgment in a subsequent suit when the very point is presented for decision. The reason of the maxim is obvious. The question actually before the court is investigated with care, and considered in its full extent. Other principles which may serve to illustrate it are considered in their relation to the case decided, but their possible bearing on all other cases is seldom completely investigated."
35. This is not what *Pollock* held, but unlike *Brushaber* which held the income tax was an excise tax, *Eisner* correctly found the purpose of the Sixteenth Amendment was to remove the requirement for apportionment from the income tax, which *Pollock* did hold was direct in the constitutional sense.

CHAPTER III

INCOME AND THE INTERNAL REVENUE CODE

Any analysis of the federal tax laws requires a basic understanding of the arrangement of the Internal Revenue Code. Although not yet officially codified within the United States Code due to “inconsistent, redundant and obsolete provisions,”³⁶ the Internal Revenue Code of 1986, as amended, is nonetheless often referred to as “Title 26” of the United States Code. The “title” is broken down into subtitles, which are further broken down into chapters, subchapters, parts, subparts and sections. Sections can be further divided into lettered paragraphs, sub-paragraphs, sub-subparagraphs and sub-sub-subparagraphs. The primary Subtitles are:

- Subtitle A - Income Taxes
- Subtitle B - Estate and Gift Taxes
- Subtitle C - Employment Taxes and Collection of
Income Tax at Source
- Subtitle D - Miscellaneous Excise Taxes
- Subtitle E - Alcohol, Tobacco and Certain Other
Excise Taxes
- Subtitle F - Procedure and Administration
- Subtitle G - The Joint Committee on Taxation
- Subtitle H - Financing of Presidential Election
Campaign

The Internal Revenue Code (1988 edition) defines the term “taxpayer” as used in Title 26 as follows:

The term “taxpayer” means any person subject to any internal revenue tax.

26 U.S.C. Section 7701(a)(14).

The term “internal revenue tax” is not defined in the Internal Revenue Code, but I submit the Internal Revenue Code contains the only federal “internal revenue taxes.” Thus if one is subject to any particular tax imposed in the Internal Revenue Code, one is a taxpayer. A person may be a taxpayer with respect to more than one tax at a time, but may not therefore necessarily be a taxpayer with respect to a different tax. Whether or not one is a taxpayer is a mixed question of law and fact.

In the case of *Long v. Rasmussen*, 281 F. 236 (1922), the collector of Internal Revenue assessed certain excise taxes against Mr. Wise, and sought to collect the tax through seizure of certain property. Mr. Long brought a suit against the collector to prevent the sale of the property—claiming ownership of it—and to recover its possession. The collector argued that the anti-injunction statute, Section 3224 of the Internal Revenue Code, prevented Mr. Long from suing to challenge the collection of the tax. In refusing to dismiss the suit under the provisions of the anti-injunction statute, the Court held that as to the taxes assessed against Mr. Wise, Mr. Long was not the taxpayer of that tax, and therefore, Section 3224 did not apply to him:

The instant suit is not to restrain assessment or collection of taxes of Wise, but is to enjoin trespass upon property of plaintiff, and against whom no assessment has been made, and of whom no collection is sought. Note, too, the taxes are not assessed against the property. This presents a widely different case than wherein the person assessed, or whose property

is assessed, seeks to restrain assessment or collection on the theory that he or it is exempt from taxation, or that for any reason the tax is illegal.

The distinction between persons and things within the scope of the revenue laws and those without them is vital. See *DeLima v. Bidwell*, 182 U.S. 176, 179, 21 Sup.Ct. 743, 45 L.Ed 1041. To the former only does section 3224 apply (see cases cited in *Violette v. Walsh*, (D.C.) 272 Fed. 1016), and the well-understood exigencies of government and its revenues and their collection do not serve to extend it to the latter. It is a shield for official action, not a sword for private aggression.

Long v. Rasmussen, 281 F. at 238.

First National Bank of Emlenton, Pa. v. United States, 161 F.Supp. 844 (1958), also discusses this issue in *dicta*,³⁷ the suit having been dismissed because the United States was named as a party as opposed to the District Director. The purchaser of certain tools obtained a loan from the First National Bank, and as security for the loan gave the bank a chattel mortgage on the tools. The I.R.S. issued a lien for non-payment of employment taxes under Subtitle C of the Internal Revenue Code, and then seized the tools. The bank brought suit claiming an ownership interest in the tools as a result of its chattel mortgage. While the case was dismissed for lack of jurisdiction, the Court nonetheless discussed whether the bank was a nontaxpayer as to the tax assessed against the purchaser of the tools, and found that it was.

Stuart v. Chinese Chamber of Commerce of Phoenix, 168 F.2d 709 (1948), is similar to the above cases. Mr. Thet was arrested for narcotics violations and a search uncovered \$32,000 in a safe. The money was taken by the Narcotics Bureau and then it was seized by the I.R.S. for payment of Thet's tax liability. Suit was brought by the Chinese Chamber of Commerce alleging the \$32,000 was theirs,

and that Thet was just holding the money for them in his safe. The Court found that the Chinese Chamber of Commerce was not a taxpayer in the strict sense of the word; *i.e.*, they had no obligation as to Thet's taxes, which were the only taxes in question. The Court ordered the money to be returned to the Chinese Chamber of Commerce, and denied a motion by the I.R.S. for dismissal on the grounds the Chinese Chamber of Commerce did not follow the steps outlined in the Internal Revenue Code to recover their property. The Court specifically found that Section 3772 was not applicable to nontaxpayer third parties to the tax.

The *Economy Plumbing & Heating Co., Inc. v. U.S.* case, [470 F.2d 585 (1972)], was limited to the issue of whether or not the plaintiffs were entitled to interest (*Economy*, 470 F.2d at 587), and the comments about nontaxpayers are *dicta*. As a nontaxpayer Economy Plumbing & Heating would not receive interest on the money illegally seized by the I.R.S., so it was their attempt to be declared taxpayers. The Court stated:

We agree with the defendant that the plaintiffs are not taxpayers in this case with respect to these funds within the meaning of the revenue laws. Lieb was the taxpayer and it is not a party to this action. While it is true that there was a misapplication of plaintiffs' funds to the payment of Lieb's taxes, this wrongful act did not result in plaintiffs becoming taxpayers to the extent of misapplied funds. Neither was there any over payment of plaintiffs' taxes.

Economy, 470 F.2d at 588.

These cases lead to the conclusion that whether or not one is a taxpayer is dependent upon the particular tax in question. The Internal Revenue Service specifically recognizes that not everyone must file a federal income tax return. On page 4 of the instruction booklet for preparing the 1989 Form 1040, under the heading "Who

Must File,” the I.R.S. tells us: “Use Chart A below to see if you must file a return.”

Congress has enacted two laws, the Privacy Act, 5 U.S.C. Section 552a(e)(3), and the Paperwork Reduction Act, 44 U.S.C. Section 3504(c)(3)(C), which directs the government to advise you if you are required to file a federal income tax return.

The Privacy Act states that an agency [the Internal Revenue Service is such an agency]³⁸ requesting information from a citizen must:

(3) inform each individual whom it asks to supply information, on the form which it uses to collect the information or on a separate form that can be retained by the individual—

- (A) the authority which authorizes the solicitation of the information and whether disclosure of such information is mandatory or voluntary;
- (B) the principal purpose or purposes for which the information is intended to be used;
- (C) the routine uses which may be made of the information, as published pursuant to paragraph (4)(D) of this subsection; and
- (D) the effects on him, if any, of not providing all or any part of the requested information ...

The Paperwork Reduction Act states that the Director of the Office of Management and Budget must include with his information request:

[A] statement to inform the person receiving the request why the information is being collected, how it is to be used, and whether responses to the request are voluntary, required to obtain a benefit, or mandatory ...

The Privacy Act and Paperwork Reduction Act statements which the Internal Revenue Service currently uses with respect to the federal income tax state:

Our legal right to ask for information is Internal Revenue Code Sections 6001, 6011, 6012(a) and their regulations. They say that you must file a return or statement with us for any tax you are liable for. Your response is mandatory under these sections.

Sections 6001 and 6011 are set forth for your information:

Section 6001:

Every person liable for any tax imposed by this title, or for the collection thereof, shall keep such records, render such statements, make such returns, and comply with such rules and regulations as the Secretary may from time to time prescribe. Whenever in the judgment of the Secretary it is necessary, he may require any person, by notice served upon such person or by regulations, to make such returns, render such statements, or keep such records as the Secretary deems sufficient to show whether or not such person is liable for tax under this title. The only records which an employer shall be required to keep under this section in connection with charged tips shall be

charge receipts, records necessary to comply with Section 6053(c) and copies of statements furnished by employees under Section 6053(a).

Section 6011:

(a) General Rule. When required by regulations prescribed by the Secretary any person made liable for any tax imposed by this title, or for the collection thereof, shall make a return or statement according to the forms and regulations prescribed by the Secretary. Every person required to make a return or statement shall include therein the information required by such forms or regulations.

* * *

(f) Income, estate, and gift taxes. For requirement that returns of income, estate, and gift taxes be made whether or not there is tax liability, see subparts B and C.

As to Sections 6001 and 6011 it is important at this point to make the observation that in several places in the Internal Revenue Code Congress was quite specific in identifying those made liable for a tax and the fact that a return was required. For example, in Subtitle E pertaining to alcohol, tobacco and other excise taxes are found these provisions:

Section 5005:

(a) The distiller or importer of distilled spirits shall be liable for the taxes imposed thereon by section 5001(a)(1).

Section 5061:

(a) The taxes on distilled spirits, wines, and beer **shall be collected on the basis of a return.**

Section 5703:

(a)(l) The manufacturer or importer of tobacco products and cigarette papers and tubes **shall be liable** for the taxes imposed therein by section 5701.

(b)(l) ... Such taxes shall be paid on the basis of return.

In Subtitle D, pertaining to miscellaneous excise taxes, we find

Section 4374:

The tax imposed by this chapter **shall be paid**, on the **basis of a return**, by any person who makes, signs, issues, or sells any of the documents and instruments subject to the tax, or for whose use or benefit the same are made, signed, issued, or sold.

There is, however, no section in Subtitle A pertaining to **Income Taxes** stating that one is **liable** for the income tax,³⁹ that one is **required** to make a return or that one must pay the income tax, nor are there any cross references to any of the provisions in Subtitle F where Sections 6001 or 6011 are found. The only exception to this is found in Section 1461 which pertains to the withholding of taxes on nonresident aliens. Under the legal doctrine “*expressio unius est exclusio alterius*,”⁴⁰ it appears that Congress could have, but specifically chose not to create an automatic, statutory liability for Subtitle A Income Taxes.

Liability for income taxes is established through an administrative action known as an assessment:

The statute prescribes the rule of taxation. Some machinery must be provided for applying the rule to the facts in each taxpayer's case, in order to ascertain the amount due. The chosen instrumentality for the purpose is an administrative agency whose action is called an assessment. The assessment may be a valuation of property subject to taxation which valuation is to be multiplied by the statutory rate to ascertain the amount of tax. Or it may include the calculation and fix the amount of tax payable, and assessments of federal estate and income taxes are of this type.

Bull v. United States, 295 U.S. 247, 259
(1935).

The assessment procedure for taxes shown on returns is contained in Sections 6201, 6203 and 6303 of the Internal Revenue Code:

Section 6201:

(a)(1) The Secretary is authorized and required to make the inquiries, determinations, and assessments of all taxes (including interest, additional amounts, additions to the tax and assessable penalties) imposed by this title, or accruing under any former internal revenue law, which have not been duly paid by stamp at the time and in the manner provided by law. Such authority shall extend to and include the following: The Secretary shall assess all taxes determined by the taxpayer or by the Secretary as to which returns or lists are made under this title.

Section 6203:

The assessment shall be made by recording the liability of the taxpayer in the office of the Secretary in

accordance with rules or regulations prescribed by the Secretary. Upon request of the taxpayer, the Secretary shall furnish the taxpayer a copy of the record of the assessment.

Section 6303:

Where it is not otherwise provided by this title, the Secretary shall, as soon as practicable, and within 60 days, after the making of an assessment of a tax pursuant to Section 6203, give notice to each person liable for the unpaid tax, stating the amount and demanding payment thereof.

Sections 6001 and 6011 clearly apply to those taxpayers specifically made liable by statutes such as Sections 5005, 5061, 5703 and 4374, or to those who have been assessed. With respect to the personal federal income tax, and absent an assessment having been made, only the withholding agents described in Section 1441 fall within the requirement to file returns under Sections 6001 and 6011.

Section 6011(f) makes reference to subparts B and C.⁴¹ Subpart C involves estate and gift taxes.⁴² Subpart B involves federal income taxes and consists of Sections 6012 through 6017A.⁴³ Section 6013 pertains to the election to file a joint return if married; Section 6014 pertains to the election to have the government compute the tax; Section 6017A requires those required to file returns to provide information with respect to residence. Only Sections 6012 and 6017 are relevant to the determination of a statutory requirement to file; they are discussed below.

Section 6012(a):

(a) General rule. Returns with respect to income taxes under subtitle A shall be made by the following:

(1)(A) Every individual⁴⁴ having for the taxable year gross income which equals or exceeds the exemption amount or more, ...⁴⁵

Section 6017:

Every individual (other than a nonresident alien individual) having net earnings from self-employment of \$400 or more for the taxable year shall make a return with respect to the self-employment tax imposed by chapter 2.

The self-employment tax mentioned in Section 6017 is the “Tax on Self-Employment Income” as contained in Chapter 2 of Subtitle A, Sections 1401 through 1403. The definition of the term “net earnings from self-employment” is found at Section 1402(a) which states in pertinent part:

Section 1402:

(a) The term “net earnings from self-employment” means the gross income derived by an individual from any trade or business carried on by such individual, ...

Both Sections 6012 and 6017 require the understanding of the term “gross income.” It is defined in the Internal Revenue Code:

Section 61:

Except as otherwise provided in this subtitle, gross income means all income from whatever source derived, including (but not limited to) the following items:

- (1) Compensation for services, including fees, commissions, fringe benefits, and similar items;

- (2) Gross income derived from business;
- (3) Gains derived from dealings in property;
- (4) Interest;
- (5) Rents;
- (6) Royalties;
- (7) Dividends;
- (8) Alimony and separate maintenance payments;
- (9) Annuities;
- (10) Income from life insurance and endowment contracts;
- (11) Pensions;
- (12) Income from discharge of indebtedness;
- (13) Distributive share of partnership gross income;
- (14) Income in respect of a decedent; and
- (15) Income from an interest in an estate or trust.

Congress is unable to define the word “income” due to its inclusion in the Sixteenth Amendment,⁴⁶ and Congress acknowledges that the word “income” as contained in the Internal Revenue Code is to have

the meaning attributable to it in the Sixteenth Amendment.⁴⁷ While Section 61 states that “**gross**” **income** means “**all**” **income**, Congress did not define the term “**income**” in the Internal Revenue Code.⁴⁸

As was pointed out in Chapter II, the decision of the United States Supreme Court in *Brushaber* is in irreconcilable conflict with the decisions of the United States Supreme Court in *Pollock* and *Eisner*. The *Brushaber* Court took the position that the purpose of the Sixteenth Amendment was to cause the income tax to be considered an indirect, excise tax, while the *Eisner* Court took the position that the purpose of the Sixteenth Amendment was to amend the United States Constitution to relieve the direct income tax from the requirement of apportionment. As a result of these conflicting Supreme Court opinions there is a conflict between the United States Courts of Appeal; the Second Circuit takes the position that the income tax is an excise tax and the remaining circuits take the position that the income tax is a direct tax.

“Income Taxes” are contained in Subtitle A of the Internal Revenue Code. Excise taxes are contained in Subtitles D and E of the Internal Revenue Code, with excise taxes on “employers” being contained in Subtitle C. One could conclude, therefore, that Congress chose not to impose in Subtitle A an [indirect] excise tax on business, professions or vocations, but instead chose to impose an income tax on all income regardless of the source of the income, just as it had imposed under the 1894 Act. The conflict between the Circuit Courts of Appeal together with the irreconcilable conflict between the *Pollock*, *Brushaber* and *Eisner* cases will have to be determined by the United States Supreme Court in an appropriate case.

There is no question but that the taxes imposed by Subtitle A are not apportioned, so if the Sixteenth Amendment has not been properly ratified,⁴⁹ the taxes imposed by Subtitle A are not constitutional under the *Pollock* decisions. One would not be a taxpayer as to the income tax if the Sixteenth Amendment was never ratified.

Assuming, for further analysis, that the Sixteenth Amendment has been properly ratified, for purposes of Section 6012 of the Internal Revenue Code, one would be required to file a personal federal income tax return (Form 1040) only if one were an “individual”⁵⁰ as that term is used in Section 6012(a)(1), and one had more than the threshold amount of “gross income.”

Inasmuch as the term “income” is not defined in the Internal Revenue Code but is used in Section 61 (a), one must resort to the intent of Congress in enacting Section 61 in order to determine the meaning of the term “gross income.” The intent of Congress is set forth in both the Senate and House Reports which accompanied the Internal Revenue Code of 1954⁵¹ as follows:

Section 61 (a) provides that gross income includes “all income from whatever source derived.” This definition is based upon the 16th Amendment and the word “income” is used in its constitutional sense.

House Report No. 1337; Senate Report No. 1622; *U.S. Code Cong, and Admin. News*, 83rd Congress, 2nd Session, pages 4155 and 4802 respectively, 1954.

The United States Supreme Court has provided us with the constitutional definition of income based upon the Sixteenth Amendment:

Income may be defined as the gain derived from capital, from labor or from both combined, provided it include profit gained through a sale or conversion of capital assets.

Stratton’s Indep. v. Howbert, 231 U.S. 399 (1913); *Doyle v. Mitchell*, 247 U.S. 179 (1920); *So. Pacific v. Lowe*, 247 U.S. 330 (1918); *Eisner v. Macomber*, 252

U.S. 189 (1920); *Merchant's Loan v. Smietanka*, 255 U.S. 509 (1921).

and in order for wages, salaries, compensation for services, etc. received for labor to constitute income, there must be a gain derived from that labor. The procedure to determine whether there is or is not a gain also has its foundation in decisions of the United States Supreme Court:

It has been well said that, "The property which every man has in his own labor, as it is the original foundation of all other property, so it is the most sacred and inviolable."

Butchers' Union Co. v. Crescent City Co., 111 U.S. 746, 757 (1883) (concurring opinion of Justice Fields).

Not only does one's labor constitute property, but the employment contract also constitutes property:

The principle is fundamental and vital. Included in the right of personal liberty and the right of private property—partaking of the nature of each—is the right to make contracts for the acquisition of property. Chief among such contracts is that of personal employment, by which labor and other services are exchanged for money or other forms of property.

Coppage v. Kansas, 236 U.S. 1, 14 (1914).

Thus a contract for labor is a contract for the sale of property:

In our opinion that section, in the particular mentioned, is an invasion of the personal liberty, as well as of the right of property, guaranteed by that

Amendment (Fifth Amendment). Such liberty and right embraces the right to make contracts for the purchase of the labor of others and equally the right to make contracts for the sale of one's own labor; ...

Adair v. United States, 208 U.S. 161, 172 (1908).

Internal Revenue Code Sections 1001, 1011 and 1012, and their regulations, 26 C.F.R. Sections 1.1001-1(a) 1.1011-1 and 1.1012-1(a), provide the method for determining the gain derived from the sale of property:

Section 1001(a):

The gain from the sale or other disposition of property shall be the excess of the amount realized therefrom over the adjusted basis provided in section 1011 for determining gain, ...

Section 1001(b):

The amount realized from the sale or other disposition of property shall be the sum of any money received plus the fair market value of the property (other than money) received.

Section 1011:

The adjusted basis for determining the gain or loss from the sale or other disposition of property, whenever acquired, shall be the basis (determined under section 1012...), adjusted as provided in section 1016.

Section 1012:

The basis of property shall be the cost of such property ...

The cost of property purchased under contract is its fair market value as evidenced by the contract itself, provided neither the buyer nor seller were acting under compulsion in entering into the contract, and both were fully aware of all of the facts regarding the contract. *Terrance Development Co. v. C.I.R.*⁵² 345 F.2d 933 (1965); *Bankers Trust Co. v. U.S.*, 518 F.2d 1210 (1975); *Bar L Ranch, Inc. v. Phinney*, 426 F.2d 995 (1970); *Jack Daniel Distillery v. U.S.*, 379 F.2d 569 (1967); *In re Williams' Estate*, 256 F.2d 217 (1958). In other words, if an employer and employee agree that the employee will exchange one hour of his time in return for a certain amount of money, the cost, or basis under Section 1012, of the employee's labor is the pay agreed upon. By the same token, if an attorney, doctor or other independent contractor agrees to perform a certain service for an agreed upon amount of compensation, the value of the service to be performed is the amount agreed upon as payment for the service.

In the case of the sale of labor, none of the provisions of Section 1016 are applicable, and the adjusted basis of the labor under Section 1011 is the amount paid. Therefore, when the employer pays the employee the amount agreed upon, or the professional is paid for his or her services, there is no excess amount realized over the adjusted basis, and there is no gain under Section 1001. There being no gain, there is no "income" in the constitutional sense, and no "gross income" under Section 61 (a).

If one has no gain, one would not have sufficient "gross income" to require the filing of a federal personal income tax return under Section 6012. Likewise, without gain, there can be no "self-employment income," and one who is self-employed would not be required to file a federal personal income tax return under Section 6017.

If one has no income, one would also not be subject to many of the provisions of Subtitle C dealing with employment taxes, nor would one be required to file a Form W-4:

a) The Federal Insurance Contributions Act (FICA) tax contained in Subtitle C, Subchapter A of Chapter 21 at Section 3101 is imposed on the “individual’s” income; if there is no income, there can be no tax.

b) The corresponding FICA tax on employers contained in Subtitle C, Subchapter B of Chapter 21 at Section 3111 is clearly identified as a separate excise tax on employers.

c) The Railroad Retirement Tax on employees contained in Subtitle C, Subchapter A of Chapter 22 at Section 3201 is also a tax on the employee’s income; with no income there is no tax.

d) The corresponding Railroad Retirement Tax on employers contained in Subtitle C, Subchapter C of Chapter 22 at Section 3221 is a separate excise tax on employers.

e) The Federal Unemployment Tax contained in Subtitle C, Chapter 23 at Section 3301 is another excise tax on employers.

f) The Railroad Unemployment Repayment Tax contained in Subtitle C, Chapter 23A at Section 3321 is also a separate excise tax on employers.

g) The provisions for withholding of wages at the source under Chapter 24 of Subtitle C is also an income tax, but the amount of tax withheld is computed upon the amount of wages received.⁵³ Section 3402(m) makes it clear that if one anticipates a lower year-end income tax liability, one is entitled to additional withholding allowances. Each withholding allowance serves the function of lowering the amount of wages upon which the withholding is computed. And if one had no income tax liability for the preceding year and expects to have no income tax liability for

the current year, Section 3402(n) authorizes filing a W-4 claiming exempt.⁵⁴

The history of the federal income tax, decisions of the United States Supreme Court, and the Internal Revenue Code itself, all lead to the conclusion that wages do not constitute income. Notwithstanding the legal correctness of this proposition, many Federal Courts of Appeal have ruled that wages do constitute income. The next several chapters analyze these cases in detail, and, in my opinion, conclusively establish the erroneous and unconstitutional nature of those cases.

ENDNOTES

36. Preface to United States Code, 1982 edition, p. xv, contained in volume 26 U.S.C.A. Sections 1-100 (May 1988 supplement).
37. “Opinions of a judge which do not embody the resolution or determination of the court. Expressions in court’s opinion which go beyond the facts before court and therefore are individual views of author of opinion and not binding in subsequent cases.” *Black’s Law Dictionary*, p. 408 (5th Ed. 1988).
38. See 5 U.S.C. Section 551.
39. See Appendix B in which this was confirmed by the testimony of an I.R.S. expert witness during a criminal trial.
40. “The express mention of one thing means the implied exclusion of another.”
41. 26 U.S.C., Subtitle F, Chapter 61, Part II, Subparts B and C.
42. This subpart will not be analyzed in that estate and gift taxes have nothing to do with the federal income tax.
43. Sections 6015 and 6016 have been repealed.
44. Section 6012 also applies to corporations [6012(a)(2)J], estates [6012(a)(3)], trusts [6012(a)(4)], political organizations [6012(a)(6)] and homeowners’ associations [6012(a)(7)].
45. Section 6151(a) of the Internal Revenue Code provides that if a tax return is required, the amount of taxes shown on the return, if any, should be paid with the return when it is filed, and irrespective of any assessment, notice or demand.
46. *Eisner v. Macomber*, 252 U.S. 189, 206 (1920), [“In order, therefore, that the clauses cited from Article I of the

Constitution may have proper force and effect save only as modified by the Amendment, and that the latter also may have proper effect, it becomes essential to distinguish between what is and what is not “income,” as the term is there used; and to apply the distinction, as cases arise, according to truth and substance, without regard to form. Congress cannot by legislation alter the Constitution, from which alone it derives its power to legislate, and within whose limitations alone that power can be lawfully exercised.”].

47. 50 Cong. Rec., 63rd Cong., 1st Session, p. 3844.
48. The term “ordinary income” is defined in Section 64 as the gain from the sale or exchange of property.
49. See note 6.
50. The term “individual” which is used not only in Section 6012(a)(1) but also in Section 1 as the subject upon whose income the tax is imposed, is not defined in the Internal Revenue Code. It is, however, defined in the treasury regulations accompanying Section 1. The regulations make a distinction between “citizens” and “residents” of the United States, and define a “citizen” as every person born or naturalized in the United States **and** subject to its jurisdiction [see 26 C.F.R. Section 1.1-1(a)-(c)]. An extremely strong argument can be made that the federal income tax as passed by Congress and as implemented by the Treasury Department was only meant to apply to individuals within the “territorial or exclusive legislative jurisdiction of the United States,” as those individuals would be subject to the “jurisdiction of the United States.” These exclusive areas, per Article I, Section 8, Clause 17, of the United States Constitution, are Washington, D.C., federal enclaves and United States possessions and territories. Outside of these exclusive areas, state law controls, not federal law. Thus a State citizen, residing in a State, would not meet the two part test for being an “individual” upon whose income the tax is imposed in

Section 1 of the Internal Revenue Code, and would not have the “status” of a “taxpayer.” It is the official policy of the I.R.S. [Policy P-(11)-23] to issue, upon written request, rulings and determination letters regarding status for tax purposes prior to the filing of a return. On August 29, 1988, I requested such a “status determination” from the I.R.S. on behalf of one of my clients. The I.R.S. responded that the argument was “frivolous.”

51. No change was made in the 1986 Tax Reform Act, PL 99-514, with respect to the intent of Congress. See 2 U.S. Code, Cong. and Admin. News, 99th Congress, 2nd Session, 1986.
52. “C.I.R.” is the abbreviation for Commissioner of Internal Revenue.
53. This may account for the common misconception of today’s citizens that the terms “wages” and “income” have the same meaning.
54. Of course, one who does not have the status of a taxpayer would not be subject to Subtitle C taxes at all, and would have no requirement of filing a Form W-4. Thus one must determine if he is a taxpayer, and if so, the amount of his anticipated income tax liability. The filing of a Form W-4 could be considered as an admission of status as a taxpayer of the Subtitle A income tax, in which case one would probably be subject to additional income taxes under Subtitle C and subject to wage withholding. The I.R.S. imposes severe penalties for filing documents the contents of which are disagreeable to them, such as admitting status as a taxpayer and then claiming exempt. I suggest consultation with a competent professional any time you are asked to fill out any government form associated with your employment.

CHAPTER IV

THE LAW AND THE COURTS

1910-1919

A court decision is one or more judges' interpretation of the law written by Congress. The theory behind "case law" is that once a specific issue or statute has been litigated and decided upon, it should be considered finally settled unless in error. Thus litigants in an action often cite in their arguments prior case law in which the issue was previously determined. This concept is known as *stare decisis*. If there is no case law previously determining the issue, then the litigants look for cases that tend to support their position, and analogize those cases to the specific issue to be decided in order to persuade the Court that their position is legally correct. A court decision will usually state a principle of law and cite to prior cases which it has relied upon in deciding in favor of one litigant over the other.

In my analysis of the case law which holds that wages constitute income, I have analyzed not only those cases regarding that specific issue, but every case cited in the Court's written decision. I have arranged all of these cases by date in an attempt to provide an historical analysis of the subject.

Stratton's Independence, Ltd. v. Howbert, 231 U.S. 399 (1913):

Stratton's Independence, Ltd., was a British corporation carrying on mining operations in the State of Colorado upon mining lands owned by itself. Suit was brought by the corporation to recover taxes paid under protest. The issue presented in the trial court was whether the value of the ore in place that was extracted from the

mining property was properly allowable as depreciation in estimating the amount of net income of the corporation which was subject to taxation under the Corporation Tax Act of August 5, 1909.⁵⁵ Three questions were certified by the Court of Appeals to the United States Supreme Court:

I. Does Section 38⁵⁶ of the Act of Congress, entitled “An Act to provide revenue, equalize duties, and encourage the industries of the United States, and for other purposes,” approved August 5, 1909 (36 Stat., p. 11), apply to mining corporations?

II. Are the proceeds of ores mined by a corporation from its own premises income within the meaning of the aforementioned Act of Congress?

III. If the proceeds from ore sales are to be treated as income, is such a corporation entitled to deduct the value of such ore in place and before it is mined as depreciation within the meaning of Section 38 of said Act of Congress?

As pertinent to the issue of what is and is not income, the corporation argued that the proceeds of its mining operation resulted only from the conversion of the capital represented by real estate into capital represented by cash; the corporation thus argued that it had no income but a mere change in the form of its capital assets, and hence argued that it was not actually engaged in business as that term was used in the 1909 Act.

The Supreme Court distinguished between the mere selling of the land with the ore not extracted, calling this a conversion of capital from one form to another, and the selling of the ore which had been extracted from the land through a mining operation,⁵⁷ and called this engaging in business for a profit:

The very process of mining is, in a sense, equivalent in its results to a manufacturing process. And, however the operation shall be described, the transaction is

indubitably “business” within the fair meaning of the act of 1909; and the gains derived from it are property and strictly the income from that business; for “income” may be defined as the gain derived from capital, from labor, or from both combined, and here we have combined operations of capital and labor.

Stratton’s, 231 U.S. at 414-415.

The Court went on to say:

As to the alleged inequality of operation between mining corporations and others, it is of course true that the revenues derived from the working of mines result to some extent in the exhaustion of the capital. But the same is true of the earnings of the human brain and hand when unaided by capital, yet such earnings are commonly dealt with in legislation as income.

Stratton’s, id.

It is too bad that the Supreme Court failed to specifically identify the legislation to which it was referring. To the extent the Court is referring to the prior income tax acts passed by Congress, it must be remembered that these first acts each included a separate provision for the taxation of the salary of persons employed by the United States Government; others were taxed in these acts upon the profit and gain derived from business, vocations and professions, an altogether different tax than a direct tax on a civilian’s salary. Also, at the time of the passage of the 1909 Corporation Excise Tax Act, no income tax act was in effect, so the gratuitous comments about earnings from the human brain were not made with respect to any then existing income tax legislation.⁵⁸

Also, in discussing income, the Court distinguished between the type of income by which the corporation excise tax was measured

and the type of income that can be taxed under the Sixteenth Amendment:

As to what should be deemed “income” within the meaning of Section 38, it of course need not be such an income as would have been taxable as such, for at that time (the Sixteenth Amendment not having been as yet ratified), income was not taxable as such by Congress without apportionment according to population, and this tax was not so apportioned. Evidently Congress adopted the income as the measure of the tax to be imposed with respect to the doing of business in corporate form because it desired that the excise should be imposed, approximately at least, with regard to the amount of benefit presumably derived by such corporations from the current operations of the Government. In *Flint v. Stone Tracy Co.*, 220 U.S. 107, 165, it was held that Congress in exercising the right to tax a legitimate subject of taxation as a franchise or privilege, was not debarred by the Constitution from measuring the taxation by the total income, although derived in part from property which, considered by itself, was not taxable. It was reasonable that Congress should fix upon gross income, without distinction as to source, as a convenient and sufficiently accurate index of the importance of the business transacted. And from this point of view, it makes little difference that the income may arise from a business that theoretically or practically involves a wasting of capital.

Strattons, 231 U.S. at 416-417.

Finally, the Court recognized that the wasting of capital assets had to somehow figure into the computation of income:

Congress no doubt contemplated that such corporations, amongst others, were doing business with a wasting capital, and for such wastage they made due provision in declaring that from the gross income there should be deducted (*inter alia*) “all losses actually sustained within the year,” including “a reasonable allowance for depreciation of property, if any,” etc.

Stratton's, 231 U.S. at 417-418.

The Supreme Court, based upon this analysis, answered the first two questions certified to it in the affirmative, and then turned its attention to the third question.

The *Stratton's* case had come to the Supreme Court upon an agreed statement of facts, one of which was that the gross proceeds of the sale of the ores during the year were diminished by the moneys expended in extracting, mining, and marketing the ores, and the precise difference was taken to be the “value of the ores when in place in the mine.” The Supreme Court concluded that the definition of the “value of the ore in place” was intentionally adopted to exclude all allowance of profit upon the process of mining, and to attribute the entire profit upon the mining operations to the mine itself. Thus, the amount of profit, if any, would be reduced to zero through depreciating the value of the mine dollar for dollar. Of course, the Court concluded that this would serve to exempt mining companies from the corporate excise tax, and the Court, earlier in its opinion, had specifically decided that Congress had intended to tax them.

Accordingly, the Court had to answer the third question certified to it in the negative. The Court then declared that it was powerless to change the definition of “value of the ore in place” which definition was included within the third question certified for answering, and therefore the Court was precluded from adjudicating exactly how much depreciation should be deducted from the gross receipts to

compensate for the wasting of the capital asset—the original value of the ore [and to continue the analogy of the Court, the earnings of the human brain] in place.

The *Stratton's Independence, Ltd.*, decision thus stands for the proposition that “income” for purposes of measuring an excise tax is different than the “income” that can be taxed under the Sixteenth Amendment; gives us a broad definition of “income,” and for the decision of the case, adjudicates that the definition of “net income” in the Corporate Excise Tax Act of 1909 is gross receipts [called gross income by the Court] less the actual expenses of producing the gross receipts [this would result in determining the profit or gain except for the consideration of the wasting capital] less some unsettled amount as depreciation for the reduction of capital⁵⁹ [thus determining net income], such depreciation not to exceed the total amount of the gross receipts less the actual expenses of producing the gross receipts, where the ore is sold for many times more than its original cost/market value.

One can easily conclude from this that if the property is sold at a cost which approximates its intrinsic value, then a deduction of that amount from the gross receipts [or as called by the Court, from the gross income] is required prior to the calculation of the amount of the tax. Applying this same principle to wages, they would not constitute income.

Stanton v. Baltic Mining Co., 240 U.S. 103 (1916):

A stockholder of the Baltic Mining Company instituted a lawsuit to enjoin the corporation and its officers from voluntarily paying the tax assessed against it under the Income Tax Section of the 1913 Tariff Act, c. 16, Section 2, 28 Stat. 166, 181 applying to corporations. This particular statute contained a provision allowing the mining company to deduct, as a depreciation for the depletion of its ore deposits, up to 5% of the gross value at the mine of the output during the year. Mr. Stanton contended that “the 5 per cent deduction permitted by the statute was inadequate to allow for the

depletion of the ore body and therefore the law to a large extent taxed not the mere profit arising from the operation of the mine, but taxed as income the yearly product which represented to a large extent the yearly depletion or exhaustion of the ore body from which during the year ore was taken.” *Stanton*, 240 U.S. at 109-110.

This argument was phrased by the Supreme Court that Mr. Stanton was contending the statute under which the corporation was being taxed deprived the stockholders of equal protection and due process “[b]ecause [among other reasons] by reason of the differences in the allowances which the statute permitted, the tax levied was virtually a net income tax on other corporations and individuals and a gross income tax on mining corporations.”⁶⁰ *Stanton*, 240 U.S. at 111. The Court referred back to its opinion in the *Brushaber* case for the resolution of this issue.

A review of the *Brushaber* decision, however, shows that the specific issue raised in the *Stanton* case was not raised in the *Brushaber* case, although Mr. Brushaber did claim that several other aspects of the taxing act were violative of the due process clause. The Court disposed of these issues as follows:

So far as the due process clause of the Fifth Amendment is relied upon, it suffices to say that there is no basis for such reliance since it is equally well settled that such clause is not a limitation upon the taxing power conferred upon Congress by the Constitution; in other words, that the Constitution does not conflict with itself by conferring upon the one hand a taxing power and taking the same power away on the other by the limitations of the due process clause.

Brushaber, 240 U.S. at 25.

The *Brushaber* opinion cites the following cases to support this proposition: *Treat v. White*, 181 U.S. 264 (1901); *Patton v. Brady*,

184 U.S. 608 (1902); *McCray v. United States*, 195 U.S. 27 (1904); *Flint v. Stone Tracy Company*, 220 U.S. 107 (1911); and *Billings v. United States*, 232 U.S. 261 (1914).

Inasmuch as the history of the United States Constitution discloses that the first ten amendments were added after the original Constitution had been ratified, and because the people demanded that the protection enunciated in the Bill of Rights be set forth, it is absurd for the Court to take the position that the people did not intend the government to impose and collect taxes (provisions for which were contained in the original Constitution) in accordance with due process. A review of the cases cited by the Court in *Brushaber* clearly shows the unconstitutional position of the Court:

Treat v. White:

Section 25 of Schedule "A" of the War Revenue Act of June 13, 1898, 30 Stat. 448, provided for a stamp tax of two cents on each hundred dollars of face value on the sale, agreement to sell, memoranda of sale, delivery or transfer of shares or certificates of stock. Mr. White was a stock broker who sold "calls" for 30,200 shares of stock, upon which calls a tax was imposed and paid under protest. The issue decided by the Court was whether or not a "call" was an "agreement to sell" under the statute; Mr. White's argument was that if Congress intended the tax to apply to "calls," it would have specified the same in the statute. The Court discussed the several rules of statutory construction which Mr. White believed were controlling, decided against applying them, and then stated:

The power of Congress in this direction is unlimited. It does not come within the province of this court to consider why agreements to sell shall be subject to stamp duty and agreements to buy not. It is enough that Congress in this legislation has imposed a stamp duty upon the one and not upon the other.

In conclusion, we may say that the language of the statute seems to us clear. It imposes a stamp duty on agreements to sell. "Calls" are agreements to sell. We see nothing in the surroundings which justifies us in limiting the power of Congress or denying to its language its ordinary meaning.

Treat, 181 U.S. at 269.

No due process challenge was made to the fact that Congress chose to tax agreements to sell ("calls") and did not choose to tax agreements to buy ("puts"), nor was any other constitutional challenge made to the validity of this tax. Thus any reliance upon this case for the proposition that Congress can violate the Bill of Rights at will in legislating taxes is wholly without foundation.

Patton v. Brady:

In May of 1898, Mr. Patton purchased over 100,000 pounds of tobacco on the open market and paid all the taxes which to that point in time were due. In June of 1898 Congress passed a taxing act which imposed an additional tax on the tobacco. Mr. Patton refused to pay the tax, was threatened by seizure by the Collector, and paid the tax under protest. Mr. Patton contended the act passed by Congress was repugnant to the Constitution. The Court stated that Mr. Patton's right of recovery rested upon the unconstitutionality of the act, *Patton*, 184 U.S. at 611, and found:

It is true other counsel in their brief have advanced a very elaborate and ingenious argument to show that this is a direct tax upon property which must be apportioned according to population within the rule laid down in the *Income Tax Cases*, but, as we have seen, it is not a tax upon property as such but upon certain kinds of property, having reference to their origin and their intended use. It may be, as Dr. Johnson said, "a hateful tax levied upon

commodities”; an opinion evidently shared by Blackstone, who says, after mentioning a number of articles that had been added to the list of those excised, “a list which no friend to his country would wish to see further increased.” But these are simply considerations of policy and to be determined by the legislative branch, and not of power, to be determined by the judiciary. We conclude, therefore, that the tax which is levied by this act is an excise, properly so called, and we proceed to consider the further propositions presented by counsel.

Patton, 184 U.S. at 618-619.

Thus far, the Court is stating that Congress has the power to determine the articles, the consumption, or manufacture of which will be subject to an excise tax; the Court does not state that Congress can ignore the provisions of the Fifth Amendment in imposing the tax.

Mr. Patton next challenged the right of Congress to pass a tax which levied an excise tax on articles which had once before been subjected to an excise tax. This issue was disposed of by the Court under the doctrine that Congress passed the legislation under wartime exigencies and it was not the Court’s function to interpose its policy opinions over the policy opinions of the Legislature. But in direct opposition to the position elaborated in the *Brushaber* opinion [that the due process clause of the Constitution does not apply to taxation], quoting Mr. Justice Cooley in his work on Taxation at page 34, the *Patton* Court stated:

But so long as the legislation is not colorable merely, but is confined to the enactment of what is in its nature strictly a tax law, and so long as none of the constitutional rights of the citizen are violated in the directions prescribed for enforcing the tax, the legislation is of supreme authority.⁶¹

Patton, 184 U.S. at 621.

It was also contended by Mr. Patton that the power granted to Congress to impose excises was an arbitrary, unrestrained power. The Court responded:

[B]ut the Constitution, art. 1, sec. 8, provides that “all duties, imposts and excises shall be uniform throughout the United States.” The exercise of the power is, therefore, limited by the rule of uniformity. The framers of the Constitution, the people who adopted it, thought that limitation sufficient, and courts may not add thereto.

Patton, 184 U.S. at 622.

Here *Patton* clearly states the Court cannot change the Constitution by expanding on specific limitations which are contained in it. In the *Brushaber* quote above, the Court contends it has authority to remove the limitations of due process in the imposition and collection of federal taxes. No court has the power to destroy the Constitution or any part thereof.

McCray v. United States:

Mr. McCray, a licensed retail dealer in oleomargarine, bought fifty pounds of oleomargarine which was yellow colored because of the use of yellow coloring in butter, and butter was an included ingredient of the oleomargarine. Congress had imposed an excise tax on oleomargarine manufactured to look like butter at a higher rate than the excise tax imposed on oleomargarine manufactured not to look like butter. The government sought to collect from Mr. McCray the excise tax at the higher rate because of the yellow appearance of the oleomargarine he had purchased for resale under his license. Mr. McCray objected, alleging that despite the fact that the oleomargarine he had purchased looked like butter, it was not manufactured to look like butter by the introduction of artificial

coloring during the manufacturing of the oleomargarine. Therefore, he argued that the higher rate did not apply to the oleomargarine he had purchased, and having paid the excise tax at the lower rate, he argued that he had fully complied with the law. *McCray*, 195 U.S. at 27-28.

Mr. McCray also argued that if the proper construction of the law required him to pay the higher tax, then the law was repugnant to the Constitution because; 1) requiring the payment of the higher rate of tax would drive the price of oleomargarine up to the point where it could no longer compete with butter, and would thus destroy the oleomargarine industry, and deprive him of his property without due process of law; 2) the levy of such a burden (of the higher tax) was beyond the constitutional power of Congress; 3) the act was an unwarranted interference by Congress with the police powers reserved to the several States and to the people of the United States by the Tenth Amendment; 4) the act was unconstitutional because the statute left the determination of what constituted artificial coloration of oleomargarine with an executive officer thereby investing him with judicial authority;⁶² and 5) the tax discriminated against oleomargarine in favor of butter, which would result in a government-caused destruction of the oleomargarine industry in favor of the butter industry, violating fundamental principles of equality and justice which are inherent in the Constitution of the United States. *McCray*, 195 U.S. at 29-30.

This case was decided by Mr. Justice White⁶³ who first summarized the statutes in question. The first section defined butter as including or not including “additional coloring matter.” The second section defined oleomargarine as including that manufactured partially from butter. Mr. Justice White then recognized that the law had been amended in 1902,⁶⁴ and that the title of the act was:

An act to make oleomargarine and other imitation dairy products subject to the laws of any State or Territory or the District of Columbia in which they are

transported, and to change the tax on oleomargarine
...

McCray, 195 U.S. at 44.

The first section of the amended act provided that immediately upon importation into a State, Washington D.C., or a Territory, the product was to be subject to their respective laws as if produced within the jurisdiction itself, and this was so regardless of the oleomargarine having been introduced into the jurisdiction in its original packages.⁶⁵ The third section amended section eight of the original act, and provided that “[w]hen oleomargarine is free from artificial coloration that causes it to look like butter of any shade of yellow, said tax shall be one-fourth of one cent per pound.” The tax on colored oleomargarine was ten cents per pound under the amended act. *McCray*, 195 U.S. at 44-45.

The Court first found that Congress clearly intended to tax oleomargarine that was colored to look like butter at a higher rate, that Mr. McCray admitted the product was oleomargarine which contained a coloring to make the product yellow like butter, and therefore concluded the product fell within the statute. The Court was not impressed with the argument that the yellow coloring was used to make the butter look like butter⁶⁶ and was not used to make the oleomargarine look like butter. *McCray*, 195 U.S. at 47-50.

The Court next determined the issue of whether Congress exerted a power not granted to it in the Constitution when it passed this tax on oleomargarine. The Court concluded that the tax was a valid excise tax, and found invalid the following more detailed arguments raised by Mr. McCray:

(a) That the purpose of the tax was not to raise revenue, but to suppress the manufacture of the taxed article.

(b) That the power to regulate oleomargarine belonged in the States and not with the federal government.

(c) That the tax was so high [thereby suppressing the oleomargarine industry] that it was not a legitimate tax authorized by law.

(d) That the tax was discriminatory [on artificially colored oleomargarine] and thus acted to suppress the industry.

(e) That the tax was repugnant to the Fifth Amendment because the amount of the tax was so out of proportion to the value of the property taxed as to destroy that property, and thus amounted to a taking thereof without due process of law; and that the tax was repugnant to the Tenth Amendment because the necessary operation and effect of the acts would be to cause the destruction of the oleomargarine industry and thus exert a power not delegated to Congress, but reserved to the several States.⁶⁷

(f) That notwithstanding that the congressional power to tax was unlimited except as otherwise expressed in the Constitution, the tax was so onerous and so unjust as to be confiscatory, and therefore it amounted to a violation of those fundamental rights which was the duty of every free government to protect. *McCray*, 195 U.S. at 50-53.

The Court contended that all of the propositions raised by Mr. McCray rested only on inferences and deductions as to the motives and purposes of Congress, and disposed of the case by looking into the constitutional power of the Court to inquire into the purposes or motives of Congress in considering the power of that body to enact the laws in question. *McCray*, 195 U.S. at 53. Mr. McCray asked the Court to examine whether the tax fell within or without the mandates of constitutional limitations, and the Court decided to address the issue of whether or not Congress can impose an excise tax, two entirely different issues.

Mr. Justice White also had this to say:

Whilst, as a result of our written constitution, it is axiomatic that the judicial department of the government is charged with the solemn duty of enforcing the Constitution, and therefore in cases properly presented, of determining whether a given manifestation of authority has exceeded the power conferred by that instrument, no instance is afforded from the foundation of the government where an act, which was within a power conferred, was declared to be repugnant to the Constitution, because it appeared to the judicial mind that the particular exertion of constitutional power was either unwise or unjust. To announce such a principle would amount to declaring that in our constitutional system the judiciary was not only charged with the duty of upholding the Constitution but also with the responsibility of correcting every possible abuse arising from the exercise by the other departments of their conceded authority. So to hold would be to overthrow the entire distinction between the legislative, judicial and executive departments of the government, upon which our system is founded, and would be a mere act of judicial usurpation. [Emphasis added.]

McCray, 195 U.S. at 53-54.

With this thought in mind, Justice White, relying upon other cases for authority, further stated:

As quite recently pointed out by this court in *Knowlton v. Moore*, 178 U.S. 41, 60, the often quoted statement of Chief Justice Marshall in *McCulloch v. Maryland*, that the power to tax is the power to destroy, affords no support whatever to the proposition that where there is a lawful power to impose a tax its imposition may be treated as without

the power because of the destructive effect of the exertion of the authority.

McCray, 195 U.S. at 56.

Justice White was very adept at quoting the Constitution and subverting it at the same time. The very purpose of our system of government was to prevent abuse, the idea being if one department became abusive, the other two would prevent the abuse from harming the people:

To what expedient, then, shall we finally resort, for maintaining in practice the necessary partition of power among the several departments as laid down in the Constitution. The only answer that can be given is that as all these exterior provisions are found to be inadequate the defect must be supplied, by so contriving the interior structure of the government as that its several constituent parts may, by their mutual relations, be the means of keeping each other in their proper places.

* * *

But the great security against a gradual concentration of the several powers in the same department consists in giving to those who administer each department the necessary constitutional means and **personal motives** to resist encroachments of the others. The provision for defense must in this, as in all other cases, be made commensurate to the danger of the attack. Ambition must be made to counteract ambition. The interest of the man must be connected with the constitutional rights of the place. It may be a reflection on human nature that such devices should be necessary to control the **abuses of government**.

But what is government itself but the greatest of all reflections on human nature? [Emphasis added.]

James Madison, *The Federalist Papers*,
No. 51.

When the Constitution was proposed to the American people as the foundation of a form of government designed to 1) promote the maximum liberty for the people and 2) provide the maximum protection from government encroachment, Founding Father James Madison stated it was a mandated duty for members of one branch of government to examine the motives of those in the other branches of government and to stop abuses of government when found. Just a little over one hundred years later, Supreme Court Justice White declared it to be a mandated duty for members of the other branches of government not to stop abuse, especially when the abuse is founded under the guise of lawful constitutional authority.

All of the cases cited by Justice White support the position that the other branches of government cannot interfere with a legitimate exercise of the taxing power by Congress. With that principle there is no argument. However, when the taxation becomes destructive, as Justice White readily admits it can, then the power exerted by Congress is not legitimate. The power to tax under the Constitution doesn't change, but the exercise of the power can be either lawful or not. And when the power is exercised unlawfully, the other two branches of government are obligated to stop the abuse.

Justice White concluded here in the opinion that neither the motive nor the purpose of Congress in enacting the oleomargarine statutes could be inquired into,⁶⁸ and then proceeded to analyze whether Congress had exceeded its powers within the framework of its totally unfettered power. In this context, Justice White easily found that Congress had not exceeded its powers:

1. Undoubtedly, in determining whether a particular act is within a granted power, its scope and effect are to be considered. Applying this rule to the acts assailed, it is self-evident that on their face they levy an excise tax. That being their necessary scope and operation, it follows that the acts are within the grant of power. The argument to the contrary rests on the proposition that, although the tax be within the power, as enforcing it will destroy or restrict the manufacture of artificially colored oleomargarine, therefore the power to levy the tax did not obtain. This, however, is but to say that the question of power depends, not upon the authority conferred by the Constitution, but upon what may be the consequence arising from the exercise of the lawful authority.⁶⁹

McCray, 195 U.S. at 59.

The other contentions of Mr. McCray were also swiftly disposed of, leaving only the last argument that: “the taxing laws are void, because they violate those fundamental rights which it is the duty of every free government to safeguard, and which, therefore, should be held to be embraced by implied though none the less potential guaranties, or in any event to be within the protection of the due process clause of the Fifth Amendment.” *McCray*, 195 U.S. at 62-63. Justice White believed this principle did not apply in Mr. McCray’s case. Justice White reasoned that the Supreme Court had found oleomargarine could be mistaken for butter and hence the opportunity for deception existed. Thus, the Court had found that a State could, under its police powers, completely prohibit the manufacture of oleomargarine within its jurisdiction, and specifically found that such state legislation did not violate “the due process clause of the Fourteenth Amendment.” The conclusion of the Court was that Congress could impose a federal tax that is destructive of the manufacture of oleomargarine⁷⁰ [*McCray, id.*], a position contrary to the very principle that the Constitution is the Supreme Law of the Land and must be adhered to by the courts in

determining if a law passed by Congress is in conflict with its express provisions:

The question whether an act, repugnant to the constitution, can become the law of the land, is a question deeply interesting to the United States; but happily, not of an intricacy proportioned to its interest. It seems only necessary to recognize certain principles, supposed to have been long and well established, to decide it.

That the people have an original right to establish, for their future government, such principles, as, in their opinion, shall most conduce to their own happiness is the basis on which the whole American fabric has been erected. The exercise of this original right is a very great exertion; nor can it, nor ought it, to be frequently repeated. The principles, therefore, so established, are deemed fundamental. And as the authority from which they proceed is supreme, and can seldom act, they are designed to be permanent.

The original and supreme will organized the government, and assigns to different departments their respective powers. It may either stop here, or establish certain limits not to be transcended by those departments.

The government of the United States is of the latter description. The powers of the legislature are defined and limited, and that those limits may not be mistaken, or forgotten, the constitution is written. To what purpose are powers limited, and to what purpose is that limitation committed to writing, if these limits may, at any time, be passed by those intended to be restrained? The distinction between a government with limited and unlimited powers is abolished, if

those limits do not confine the persons on whom they are imposed, and if acts prohibited and acts allowed, are of equal obligation. It is a proposition too plain to be contested, that the constitution controls any legislative act repugnant to it; or, that the legislature may alter the constitution by an ordinary act.

Between these alternatives there is no middle ground. The constitution is either a superior paramount law, unchangeable by ordinary means, or it is on a level with ordinary legislative acts, and, like other acts, is alterable when the legislature shall please to alter it.

If the former part of the alternative be true, then a legislative act contrary to the constitution is not law; if the latter part be true, then written constitutions are absurd attempts, on the part of the people, to limit a power in its own nature illimitable.

Certainly all those who have framed written constitutions contemplate them as forming the fundamental and paramount law of the nation, and, consequently, the theory of every such government must be, that an act of the legislature, repugnant to the constitution, is void.

This theory is essentially attached to a written constitution, and, is consequently, to be considered, by this court, as one of the fundamental principles of our society. It is not therefore to be lost sight of in the further consideration of this subject.

If an act of the legislature, repugnant to the constitution, is void, does it, notwithstanding its invalidity, bind the courts, and oblige them to give it effect? Or, in other words, though it be not law, does it constitute a rule as operative as if it was a law? This

would be to overthrow in fact what was established in theory, and would seem, at first view, an absurdity too gross to be insisted on. It shall, however, receive a more attentive consideration.

It is emphatically the province and duty of the judicial department to say what the law is. Those who apply the rule to particular cases, must of necessity expound and interpret that rule. If two laws conflict with each other, the courts must decide on the operation of each.

So if a law be in opposition to the constitution; if both the law and constitution apply to a particular case, so that the court must either decide the case conformably to the law, disregarding the constitution, or conformably to the constitution, disregarding the law, the court must determine which of these conflicting rules governs the case. This is of the very essence of judicial duty.

If, then, the courts are to regard the constitution, and the constitution is superior to any ordinary act of the legislature, the constitution, and not such ordinary act, must govern the case to which they both apply.

Those, then, who controvert the principle that the constitution is to be considered, in court, as a paramount law, are reduced to the necessity of maintaining that courts must close their eyes on the constitution, and see only the law.

This doctrine would subvert the very foundation of all written constitutions. It would declare that an act which, according to the principles and theory of our government, is entirely void, is yet, in practice, completely obligatory. It would declare that if the

legislature shall do what is expressly forbidden, such act, notwithstanding the express prohibition, is in reality effectual. It would be given to the legislature a practical and real omnipotence, with the same breath which professes to restrict their powers within narrow limits. It is prescribing limits, and declaring that those limits may be passed at pleasure.

That it thus reduced to nothing what we have deemed the greatest improvement on political institutions, a written constitution, would of itself be sufficient, in America, where written constitutions have been viewed with so much reverence, for rejecting the construction. But the peculiar expressions of the constitution of the United States furnish additional arguments in favour of its rejection.

The judicial power of the United States is extended to all cases arising under the constitution.

Could it be the intention of those who gave this power, to say that in using it the constitution should not be looked into? That a case arising under the constitution should be decided without examining the instrument under which it arises?

This is too extravagant to be maintained.

In some cases, then, the constitution must be looked into by the judges. And if they can open it at all, what part of it are they forbidden to read or to obey?

There are many other parts of the constitution which serve to illustrate this subject.

It is declared that “no tax or duty shall be laid on articles exported from any states.” Suppose a duty on

the export of cotton, of tobacco, or of flour, and a suit instituted to recover it. Ought judgment to be rendered in such a case? Ought the judges to close their eyes on the constitution and see only the law?

The constitution declares “that no bill of attainder or ex post facto law shall be passed.”

If, however, such a bill should be passed, and a person would be prosecuted under it, must the court condemn to death those victims whom the constitution endeavors to preserve?

“No person,” says the constitution, “shall be convicted of treason unless on the testimony of two witnesses to the same overt act, or on confession in open court.”

Here the language of the constitution is addressed especially to the courts. It prescribes, directly for them, a rule of evidence not to be departed from. If the legislature should change that rule, and declare one witness, or a confession out of court, sufficient for conviction, must the constitutional principle yield to the legislative act?

From these, and many other selections which might be made, it is apparent, that the framers of the constitution contemplated that instrument as a rule for the government of courts, as well as of the legislature.

Why otherwise does it direct the judges to take an oath to support it? This oath certainly applies in an especial manner, to their conduct, in their official character. How immoral to impose it on them, if they were to be used as the instruments, and the knowing instruments, for violating what they swear to support!

The oath of office, too, imposed by the legislature, is completely demonstrative of the legislative opinion on this subject. It is in these words: "I do solemnly swear that I will administer justice without respect to persons, and do equal right to the poor and to the rich; and that I will faithfully and impartially discharge all the duties incumbent on me as _____, according to the best of my abilities and understanding agreeably to the constitution and laws of the United States."

Why does a judge swear to discharge his duties agreeably to the constitution of the United States, if that constitution forms no rule for his government? If it is closed upon him, and cannot be inspected by him?

If such be the real state of things, this is worse than solemn mockery. To prescribe, or to take this oath, becomes equally a crime.

It is also not entirely unworthy of observation, that in declaring what shall be the supreme law of the land, the constitution itself is first mentioned, and not the laws of the United States generally, but those only which shall be made in pursuance of the constitution, have that rank.

Thus, the particular phraseology of the constitution of the United States confirms and strengthens the principle, supposed to be essential to all written constitutions, that a law repugnant to the constitution is void; and that courts, as well as other departments, are bound by that instrument.

Marbury v. Madison, 5 U.S. 137, 176-180 (1803).

Flint v. Stone Tracy Company:

On August 5, 1909, Congress approved "The Corporation Tax" law, 36 Stat. c. 6, 11. Section 38 of the act provided:

That every corporation, joint stock company or association organized for profit and having a capital stock represented by shares, and every insurance company now or hereafter organized under the laws of the United States or of any State or Territory of the United States or under the acts of Congress applicable to Alaska or the District of Columbia, or now or hereafter organized under the laws of any foreign country and engaged in business in any State or Territory of the United States or in Alaska or in the District of Columbia, shall be subject to pay annually a special excise tax with respect to the carrying on or doing business by such corporation, joint stock company or association or insurance company equivalent to one per centum upon the entire net income over and above five thousand dollars received by it from all sources during such year, exclusive of amounts received by it as dividends upon stock of other corporations, joint stock companies or associations or insurance companies subject to the tax hereby imposed; or if organized under the laws of any foreign country, upon the amount of net income over and above five thousand dollars received by it from business transacted and capital invested within the United States and its Territories, Alaska and the District of Columbia, during such year, exclusive of amounts so received by it as dividends upon stock of other corporations, joint stock companies or associations or insurance companies subject to the tax hereby imposed.

Flint, 220 U.S. at 143-144.

Several companies brought suit to have Section 38 declared unconstitutional on several grounds, and the *Flint* case was a consolidation of those various suits. One of those grounds was that the act was void as lacking in due process of law. *Flint*, 220 U.S. at 167. The Court disposed of this issue by referencing what it had said as to the power of Congress to lay the excise tax in question.

The Supreme Court first analyzed Section 38 and stated that it was the intent of Congress to impose a special excise tax with respect to the carrying on or doing business by corporations, joint stock companies or associations, or insurance companies; that the tax was not imposed upon the franchises of the corporation irrespective of their use in business, nor upon the property of the corporation, but upon the doing of corporate or insurance business and with respect to the carrying on thereof, in a sum equivalent to one per centum upon the entire net income over and above \$5,000 received from all sources during the year. *Flint*, 220 U.S. at 145-146.

In other words, the tax is imposed upon the doing of business of the character described, and the measure of the tax is to be the income, with the deduction stated, received not only from property used in business, but from every source.

Flint, 220 U.S. at 146. The Court stated that:

This interpretation of the act, as resting upon the doing of business, is sustained by the reasoning in *Spreckles Sugar Refining Co. v. McClain*, 192 U.S. 397, in which a special tax measured by the gross receipts of the business of refining oil and sugar was sustained as an excise in respect to the carrying on or doing of such business.

Flint, 220 U.S. at 147.

Another allegation of those seeking a declaration that Section 38 was unconstitutional was so far as the tax was measured by the income of bonds non-taxable under Federal statutes, and of municipal and state bonds beyond the Federal power of taxation, and so far as the tax was measured by the income from real and personal estates, Section 38 must fall under the holding of *Pollock*. *Flint, id.* In disposing of this contention, the Court stated:

The act now under consideration does not impose direct taxation upon property solely because of its ownership, but the tax is within the class which Congress is authorized to lay and collect under Art. I, section 8, cl. 1, of the Constitution, and described generally as taxes, duties, imposts and excises, upon which the limitation is that they shall be uniform throughout the United States.

Within the category of indirect taxation, as we shall have further occasion to show, is embraced a tax upon business done in a corporate capacity, which is the subject-matter of the tax imposed in the act under consideration. The *Pollock* case construed the tax there levied as direct, because it was imposed upon property simply because of its ownership. In the present case the tax is not payable unless there be a carrying on or doing of business in the designated capacity, and this is made the occasion for the tax, measured by the standard prescribed. The difference between the acts is not merely nominal, but rests upon substantial differences between the mere ownership of property and the actual doing of business in a certain way.

Flint, 220 U.S. at 150.

The Court next cited to *Thomas v. United States*, 192 U.S. 363, regarding the terms “duties, imposts and excises,” and said:

We think that they were used comprehensively to cover customs and excise duties imposed on importation, consumption, manufacture and sale of certain commodities, privileges, particular business transactions, vocations, occupations and the like.

Duties and imposts are terms commonly applied to levies made by governments on the importation or exportation of commodities. Excises are “taxes laid upon the manufacture, sale or consumption of commodities within the country, upon licenses to pursue certain occupations, and upon corporate privileges.” Cooley, *Const. Lim.*, 7th ed., 680.

The tax under consideration, as we have construed the statute, may be described as an excise upon the particular privilege of doing business in a corporate capacity, *i.e.*, with the advantages which arise from corporate or quasi-corporate organization; or, when applied to insurance companies, for doing the business of such companies. As was said in the *Thomas* case, 192 U.S. 363 *supra*, the requirement to pay such taxes involves the exercise of privileges, and the element of absolute and unavoidable demand is lacking. If business is not done in the manner described in the statute, no tax is payable.

Flint, 220 U.S. at 151-152.

Another contention made by some of the insurance companies was that they had large investments in municipal bonds and other non-taxable securities, and in real estate and personal property not used in the business, and therefore the selection of the measure of the income from all sources is void, because it reaches property which is not the subject of taxation. The insurance companies relied upon the *Pollock* decision. *Flint*, 220 U.S. at 162. The Court stated:

But this argument confuses the measure of the tax upon the privilege, with direct taxation of the estate or thing taxed. In the *Pollock* case, as we have seen, the tax was held unconstitutional, because it was in effect a direct tax on the property solely because of its ownership.

* * *

There is nothing in these cases contrary, as we shall have occasion to see, to the former rulings of this court which hold that where a tax is lawfully imposed upon the exercise of privileges within the taxing power of the State or Nation, the measure of such tax may be the income from the property of the corporation, although a part of such income is derived from property in itself non-taxable. The distinction lies between the attempt to tax the property as such and to measure a legitimate tax upon the privileges involved in the use of such property.

* * *

It is therefore well settled by the decisions of this court that when the sovereign authority has exercised the right to tax a legitimate subject of taxation as an exercise of a franchise or privilege, it is no objection that the measure of taxation is found in the income produced in part from property which of itself considered is non-taxable. Applying that doctrine to this case, the measure of taxation being the income of the corporation from all sources, as that is but the measure of a privilege tax within the lawful authority of Congress to impose, it is no valid objection that this measure includes, in part at least, property which as such could not be directly taxed.

Flint, 220 U.S. at 162-165.

With respect to due process, the Court further stated:

It is urged that this power can be so exercised by Congress as to practically destroy the right of the States to create corporations, and for that reason it ought not to be sustained, and reference is made to the declaration of Chief Justice Marshall in *McCulloch v. Maryland* that the power to tax involves the power to destroy. This argument has not been infrequently addressed to this court with respect to the exercise of the powers of Congress. Of such contention this court said in *Knowlton v. Moore, supra*:

This principle is pertinent only when there is no power to tax a particular subject, and has no relation to a case where such right exists. In other words, the power to destroy which may be the consequence of taxation is a reason why the right to tax should be conditioned to subjects which may be lawfully embraced therein, even although it happens that in some particular instance no great harm may be caused by the exercise of the taxing authority as to a subject which is beyond its scope. But this reasoning has no application to a lawful tax, for if it had there would be an end of all taxation; that is to say, if a lawful tax can be defeated because the power which is manifested by its imposition may when further exercised be destructive, it would follow that every lawful tax would become unlawful, and therefore no taxation whatever could be levied.

In *Veazie Bank v. Fenno*, 8 Wall. 533, *supra*, speaking for the court, the Chief Justice said:

It is insisted, however, that the tax in the case before us is excessive, and so excessive as to indicate a purpose on the part of Congress to destroy the franchise of the bank, and is, therefore, beyond the constitutional power of Congress.

The first answer to this is that the judicial cannot prescribe to the legislative department of the government limitations upon the exercise of its acknowledged powers. The power to tax may be exercised oppressively upon persons, but the responsibility of the legislature is not to the courts, but to the people by whom its members are elected. So if a particular tax bears heavily upon a corporation, or a class of corporations, it cannot, for that reason only, be pronounced contrary to the Constitution.

Flint, 220 U.S. at 168-169.

The *Flint* Court next cited to the *McCray* case which was analyzed hereinabove. In deciding the due process question in the *Flint* case, there can be little question but that the justices departed from the principle enunciated in *Marbury v. Madison*.

Billings v. United States:

Section 37 of the Tariff Act of August 5, 1909, c.6, 36 Stat. 11, 112, levied a tonnage tax of seven dollars per gross ton upon the use of every foreign-built yacht, not used for trade, owned or chartered for more than six months by any citizen or citizens of the United States.

Section 37 went into effect on August 6, 1909, and the collector of the port of New York made a demand upon Mr. Billings, as the owner of a foreign-built yacht weighing 1,091.71 tons, for payment of \$7,644.00. Mr. Billings failed to pay the tax, the United States brought suit and Mr. Billings raised three defenses:

1) That the vessel was not enrolled, registered, or documented as a vessel of the United States and enjoyed no privileges from the United States. Also that the yacht had only been used outside of the waters and territorial limits or jurisdiction of the United States;

2) That the tax imposed by the statute was intended by Congress to be “an annual tax, that it should be prospective and operate only upon the future use of any such foreign-built yacht, and that said annual tax had not yet accrued and could not be duly levied and collected prior to the first day of September in the year 1910.”; and

3) After averring that there were within the United States many pleasure yachts not foreign-built which were virtually identical to Mr. Billings’ yacht, charged that the law imposing the burden sought to be enforced was void because repugnant to the due process clause of the Fifth Amendment. *Billings*, 232 U.S. at 278.

The lower court found the sum claimed was due by Mr. Billings as an excise or duty upon the use of his yacht and that the act imposing the tax was not repugnant to the Constitution, but found the government was not entitled to recover interest.

In order “to avoid if it may be the necessity of determining the constitutional question” (*Billings*, 232 U.S. at 279), the Court assumed the Tariff Act in question was adopted by Congress in the light of the ruling in *Pollock v. Farmers Loan & Trust Company*, stated it was certain that Congress intended Section 37 to be an excise tax, and stated that this was not seriously disputed in argument, with the controversy turning first upon the period when the tax provided for was to take effect and the nature and character of the use which was taxed. *Billings*, 232 U.S. at 279. The Court also stated the two issues were so interwoven that they would be considered and disposed of together.

The Court found that the word “annually” was used not for the purpose of postponing the time of payment, but rather as provision

for continuity, and found the tax could be imposed in September of 1909. The Court next addressed the issue of upon what the tax was assessed.

The Court stated the issue of upon what the tax was assessed was clearly addressed in the statute:

[T]he recurrence of the tax is annual and depends upon two elements, ownership or charter rights, as specified in the act, and the use for any time during the year. It is to be observed that the provision deals with ownership and distinguishes between ownership and use, since it bases the tax not upon the former but upon the latter.

Billings, 232 U.S. at 280.

The Court, in sophisticated double-talk, then attempted to point out that even though ownership necessarily entails and contemplates “use,” as used in the statute, some other type of “use” was intended than the mere privilege of using which the owner enjoys:

Let it be conceded that the ownership of property includes the right to use, plainly we think, as use and ownership are distinguished one from the other in the provision, the word “use” as there employed means more than the mere privilege of using which the owner enjoys, and relates to its primary signification, as defined by Webster; “The act of employing anything or of applying it to one’s service; the state of being so employed or applied.” If the use which arises from the fact of ownership without more was what the statute proposed, then it is inconceivable why the difference between use and ownership was marked in the provision and made the basis of the tax which it imposed. While this construction in this case leads to the same conclusion as does that which the court

below affixed to the statute, that is, that it taxed the privilege of use, or, in other words the potentiality of using involved in ownership, inherently there is this fundamental difference between the interpretation we give and that which the lower court adopted, since the privilege of use is purely passive (or subjective), a right which necessarily pertains to ownership and must exist where there is ownership, as one may not obtain ownership without acquiring the privileges of use which ownership gives. The other, on the contrary, that is, use in the statutory sense, although it arises from ownership, is active (objective), that is, it is the outward and distinct exercise of a right which ownership confers but which would not necessarily be exerted by the mere fact of ownership. The contention that inequality must be the result of making the tax depend upon mere use without reference to the extent of its duration, addresses itself not to the question of power, and is therefore beyond the scope of judicial cognizance.

Billings, 232 U.S. at 281.

The author of this opinion is none other than Justice White! On page 279 the Justice tells us he is going to do his best to avoid answering the constitutional questions. To do this, first he assumes Congress knows the distinction between a direct tax and an indirect tax,⁷¹ and then without examining the nature and effect of the tax in operation, found it to be an excise tax. And to conclusively establish that the tax was an excise, Justice White merely distinguished the “use” derived from ownership from the “use” derived from ownership, the former being “passive (or subjective)” and the latter being “active (objective).”

With respect to the due process issue of inequality of operation between citizens who own American-made yachts and citizens who own foreign-made yachts, Justice White disposed of it by stating,

without quoting any authority for the proposition, that the issue was “beyond the scope of judicial cognizance, and besides, the “excise” tax is levied uniformly among all of those it taxes, and thus is not violative of Article I, Section 8, Clause 1 nor the due process clause of the Fifth Amendment.” *Billings*, 232 U.S. at 282-284.

Finding the tax to be valid in all respects, Justice White ruled that the government was entitled to interest even though there was no provision for the collection of interest applicable to Section 37 taxes in the Tariff Act in question.

The above analysis of *Treat*, *Patton*, *McCray*, *Flint* and *Billings* shows that those cases cannot support the proposition of Justice White as stated in the *Brushaber* case that the due process provisions of the United States Constitution have no applicability to the levying and collection of federal taxes. And, notwithstanding Justice White’s closing his eyes to the Constitution, the *Stanton* case cannot be cited as authority for the proposition that wages constitute income.

Edwards v. Keith, 231 F. 110 (2nd Cir. 1916):

Mr. Edwards was an insurance salesman who received commissions when he first sold an insurance policy, and again whenever the policy was renewed. Mr. Edwards paid his income tax under protest and sued the collector, Mr. Keith, for its recovery. Mr. Keith filed a demurrer to the complaint which the lower court sustained and the Court then dismissed the case on its merits. This appeal followed on the single question of:

[W]hether or not the commissions payable to complainant under the contracts with the Assurance Society annexed to the complaint, upon renewal premiums paid on policies obtained through the instrumentality of appellant prior to March 1, 1913, but which commissions were not actually paid to and received by complainant until after March 1, 1913, and

between that date and December 31, 1913, constitute a part of the “entire net income” of complainant “arising or accruing from all sources” between those dates.

Edwards, 231 F. at 111.

The issue presented to the Court was not whether the commissions constituted income; that question was not raised by the parties. The Court was asked to consider the commissions as income, and determine in what year they were to be taxed:

[B]ut the question seems to us a very simple one and one absolutely determined by the provision in all the contracts that “commissions shall accrue only as the premiums are paid in cash.”

Edwards, 231 F. at 112.

One can only speculate as to how this Court would rule if the question as to what is and is not income were presented to it, for the Court stated in the last lines of the opinion:

[T]he statute and the statute alone determines what is income to be taxed. It taxes only income “derived” from many different specified sources; one does not “derive income” by rendering services and charging for them.

Edwards, 231 F. at 113.

Doyle v. Mitchell Brothers Co., 247 U.S. 179 (1918):

Mr. Doyle, the Collector of Internal Revenue, assessed additional taxes against Mitchell Brothers Company under the Corporation Excise Tax Act of August 5, 1909, c. 6, 36 Stat. 11, 112, Section 38. Mitchell Brothers paid the tax under protest and sued for its recovery. It won in both the District Court and Court of Appeals. *Doyle*, 247 U.S. at 180.

Mitchell Brothers was a lumber manufacturing corporation. In 1903 it purchased land with timber on it for \$20.00 per acre. In 1908 the land was valued at \$40.00 per acre. When the corporation filed returns under the 1909 tax act, it deducted from gross receipts the market value of the land from which trees were cut at the \$40.00 per acre value. The I.R.S. thought the land should have been valued at \$20.00, and sought the difference. *Doyle*, 247 U.S. at 181-182. As stated by the Court:

[T]he question is whether this difference (made the basis of the additional taxes) was income for the years in which it was converted into money, within the meaning of the act.

Doyle, 247 U.S. at 182.

The Court stated the position of the Collector as follows:

Starting from this point, the learned Solicitor General has submitted an elaborate argument in behalf of the Government, based in part upon theoretical definitions of "capital," "income," "profits," etc., and in part upon expressions quoted from our opinions in *Flint v. Stone Tracy Co.*, 220 U.S. 107, 147, and *Anderson v. Forty-two Broadway Co.*, 239 U.S., 69, 72, with the object of showing that a conversion of capital into money always produces income, and that for the purposes of the present case the words "gross income" are equivalent to "gross receipts"; the insistence being that the entire proceeds of a conversion of capital assets should be treated as gross income, and that by deducting the mere cost of such assets we arrive at net income.

Doyle, 247 U.S. at 183-184.

While the only issue before the Court was whether the \$20 or \$40 valuation should be used, based upon the government's argument, the Court felt compelled to respond:

Yet it is plain, we think, that by the true intent and meaning of the act the entire proceeds of a mere conversion of capital assets were not to be treated as income.

Whatever difficulty there may be about a precise and scientific definition of "income," it imports, as used here, something entirely distinct from principal or capital either as a subject of taxation or as a measure of the tax; conveying rather the idea of gain or increase arising from corporate activities. As was said in *Stratton's Independence v. Howbert*, 231 U.S. 399, 415: "Income may be defined as the gain derived from capital, from labor, or from both combined."

Understanding the term in this natural and obvious sense, it cannot be said that a conversion of capital assets invariably produces income. If sold at less than cost, it produces rather loss or outgo. Nevertheless, in many if not in most cases there results a gain that properly may be accounted as a part of the "gross income" received "from all sources"; and by applying to this the authorized deductions we arrive at "net income." In order to determine whether there has been gain or loss, and the amount of the gain, if any, we must withdraw from the gross proceeds an amount sufficient to restore the capital value that existed at the commencement of the period under consideration.

Doyle, 247 U.S. at 184-185.

The Court determined that the \$40 per acre was the correct amount to restore the capital value of the land for the cutting of the timber, and sustained the judgment of the Court of Appeals. Applying the same principle to labor, and deducting the cost of the labor from the wages received in exchange therefore, wages would not constitute income.

ENDNOTES

55. “As has been repeatedly remarked, the Corporation Tax Act of 1909 was not intended to be and is not in any proper sense an income tax law. This court had decided in the *Pollock* case that the income tax law of 1894 amounted in effect to a direct tax upon property, and was invalid because not apportioned according to population as prescribed by the Constitution. The act of 1909 avoided this difficulty by imposing not an income tax, but an excise tax upon the conduct of business in a corporate capacity, measuring, however, the amount of tax by the income of the corporation, with certain qualifications prescribed by the Act itself.” *Stratton’s*, 231 U.S. at 414.
56. Sec. 38 imposed a tax on every corporation, joint stock company or association, organized for profit and having a capital stock represented by shares, and every insurance company, organized under the laws of the United States or of any State or Territory of the United States, or organized under the laws of any foreign country and engaged in business in any State or Territory of the United States or in Alaska or in the District of Columbia.
57. “[E]mploying capital and labor in transmuting a part of the realty into personalty, and putting it into marketable form.” *Stratton’s*, 231 U.S. at 415.
58. There was no income tax between the years 1895 when *Pollock* held the Act of 1894 unconstitutional, and 1913, when Congress enacted an income tax law after the alleged ratification of the Sixteenth Amendment.
59. “It was of course contemplated that the income might be derived from the employment of property in business, and that this property might become more or less exhausted in the process; and because of this, a reasonable allowance was to be made for depreciation of it, if any. But plainly, we think, the valuation of

the property and the amount of the depreciation were to be determined not upon the basis of latent and occult intrinsic values, but upon considerations that affect market value and have their influence upon men of affairs charged with the management of the business and accounting of corporations that are organized for profit and are engaged in business for purposes of profit.” *Stratton’s*, 231 U.S. at p. 421.

60. It is interesting to note that the gross receipts of the corporation was called gross income by the Court. In *Doyle v. Mitchell*, 247 U.S. 179 (1918), the Supreme Court specifically held that the government’s contention that gross receipts were the same as gross income was erroneous (see p. 128).
61. The clear distinction between this quote upholding the fundamental principles of a federal republic and the *Brushaber* quote declaring that citizens have no constitutionally protected rights is indicative of our government today.
62. This argument was not contained in the “assignment of errors,” and was thus not considered by the Supreme Court. *McCray*, 195 U.S. at 46.
63. Thus Mr. Justice White cites himself in the *Brushaber* decision for his legal authority to excise the Fifth Amendment from the Constitution with respect to income taxation.
64. 32 Stat. 193.
65. It is clear that Congress here specifically ceded jurisdiction to the States and the governments of Washington D.C. and of the United States Territories to tax and otherwise regulate the oleomargarine industry within their respective jurisdictions.
66. Mr. McCray advised the Court that depending upon the season of the year, the color of natural butter went from pale yellow to

dark yellow, and that consumers preferred the darker yellow color.

67. The argument was worded such that it appears it is being argued that under the Tenth Amendment, the States have the power to destroy an industry. An interpretation of the Tenth Amendment as a grant from the people to the States to destroy industries defies reality.
68. Thereby eliminating from consideration whether the motive of Congress in enacting the legislation was merely the return of a political favor to the dairy lobby. If it was, then any legislation passed would be null and void as contrary to constitutional principles, and the Court would be without jurisdiction due to the lack of a statute imposing the tax.
69. Justice White again refused to recognize that the lawfulness of the authority ceases when the power becomes abusive. This includes not only the abuse arising at the time of enacting the statute, but each and every time an American is injured by the abuse. The injury resulting from an unlawful exertion of power includes having one's due process violated. It is clear, then, that Justice White used the *McCray* case to lay the foundation for the policy he announced in *Brushaber*, the complete eradication of the Fifth Amendment from proceedings involving taxation.
70. See note 68. This may explain why Congress gave concurrent jurisdiction to the States to tax oleomargarine when it amended the 1886 Act. Rather than challenging this nebulous quantum leap of jurisdiction, Justice White treacherously used it to avoid the one fundamental limitation on the exercise of governmental power over the American people—the lack of jurisdiction of the federal government in the States. The very fact that Justice White recognized the principle in light of a complaint of injury resulting from the violation of that principle shows that his destruction of the separation of powers doctrine was deliberate.

71. A highly suspect assumption in light of the fact the Supreme Court in *Pollock* had less than ten years before struck down a tax that Congress thought to be an indirect excise tax, but was in actuality a direct tax.

CHAPTER V

THE LAW AND THE COURTS

1920-1929

Eisner v. Macomber, 252 U.S. 189 (1920):

Justice Pitney, the author of the Court's majority opinion, stated that the question presented in the case was "whether, by virtue of the Sixteenth Amendment, Congress had the power to tax, as income of the stockholder and without apportionment, a stock dividend made lawful and in good faith against profits accumulated by the corporation since March 1, 1913." *Eisner*, 252 U.S. at 199.

Justice Pitney stated the statute in question was the Revenue Act of September 8, 1916, c. 463, 39 Stat. 756 *et seq.*, Sec. 2(a), which statute provided that the net income of a taxable person⁷² shall include, among other things, dividends. The statute also defined a dividend as any distribution made by a corporation out of its earnings or profits accrued since March 1, 1913, and payable to its shareholders, whether in cash or in stock of the corporation, said stock to be considered income to the amount of its cash value. *Eisner*, 252 U.S. at 199-200.

The facts were that on January 1, 1916, the Standard Oil Company of California had approximately \$50,000,000 worth of \$100 par value shares of stock outstanding. It also had surplus and undivided profits invested into the corporation worth approximately \$45,000,000, of which about \$20,000,000 had been earned prior to March 1, 1913. In January, 1916, in order to readjust the capitalization, it was decided to issue additional shares sufficient to constitute a stock dividend of fifty per cent of the outstanding stock,

and to transfer from surplus account to capital stock account an amount equivalent to such issue. *Eisner*, 252 U.S. at 200.

Ms. Macomber had been the owner of 2,200 shares of the old stock, and received certificates for 1,100 additional shares, of which 18.07 percent, or 198.77 shares, par value \$19,877, were treated as representing surplus earned between March 1, 1913, and January 1, 1916. *Eisner*, 252 U.S. at 200-201.

Ms. Macomber paid, under protest, a tax under Section 2(a) of the 1916 Act on the \$19,877, filed an administrative appeal, and then brought suit against the Collector to recover the tax. She contended that the 1916 tax act was in violation of Article I, Section 2, Clause 3, and Article I, Section 9, Clause 4, requiring direct taxes to be apportioned according to population, and that the stock dividend was not income within the meaning of the Sixteenth Amendment. *Eisner*, 252 U.S. at 201.

The Defendant, Mr. Eisner, filed a general demurrer to the complaint which was overruled, and he did not file any pleadings thereafter. Judgment was issued in favor of Ms. Macomber, and the case came to the United States Supreme Court on a writ of error. *Eisner, id.* In a split decision, the Court held that neither under the Sixteenth Amendment nor otherwise did Congress have power to tax without apportionment a true stock dividend made lawfully and in good faith, or the accumulated profits behind it, as income of the stockholder. The Court held the Revenue Act of 1916 contrary to Article I, Section 2, Clause 3, and Article I, Section 9, Clause 4, with respect to the tax imposed on such true stock dividends. *Eisner*, 252 U.S. at 219.

The Court relied upon the decision in *Towne v. Eisner*, 245 U.S. 418 (1918), where the question was whether a stock dividend made in 1914 against surplus earned prior to January 1, 1913, was taxable against the stockholder under the Act of October 3, 1913, c. 16, 38 Stat. 114, 166, which provided that net income should include “dividends,” and also “gains or profits and income derived from any

source whatever.” In *Towne* the Supreme Court relied upon the definition of a stock dividend given in *Gibbons v. Mahon*, 136 U.S. 549 (1890), to find that a stock dividend made against surplus did not constitute income as that word was used in the October 3, 1913, tax act. *Eisner*, 252 U.S. at 252. This was so because “[a] stock dividend takes nothing from the property of the corporation, and adds nothing to the interest of the shareholders. Its property is not diminished, and their interests are not increased... . The proportional interest of each shareholder remains the same. The only change is in the evidence which represents that interest, the new shares and the original shares together representing the same proportional interest that the original shares represented before the issue of the new ones.” *Gibbons*, 136 U.S. at 559-560. The Court went on to distinguish between the types of dividends represented by this issuance of stock, and the types of dividends represented by a distribution in specie of a portion of the assets of the corporation. *Eisner*, 252 U.S. at 204.

The Court, however, was not content to rely upon the mere holding that the stock dividend did not constitute income because Congress had stated that a “stock dividend shall be considered income, to the amount of its cash value.” *Eisner*, 252 U.S. at 205. The Court then went into an analysis of the Sixteenth Amendment, defined the very “income” which is discussed in the Sixteenth Amendment, discussed the nature of corporations and stock, and held that a stock dividend did not constitute income under the Sixteenth Amendment. With respect to the definition of “income,” the Court stated:

The Sixteenth Amendment must be construed in connection with the taxing clauses of the original Constitution and the effect attributed to them before the Amendment was adopted. In *Pollock v. Farmers’ Loan and Trust Co.*, 158 U.S. 601, under the Act of August 27, 1894, c. 349, section 27, 28 Stat. 509, 553, it was held that taxes upon rents and profits of real property were in effect direct taxes upon the property

from which such income arose, imposed by reason of ownership; and that Congress could not impose such taxes without apportioning them among the States according to population, as required by Art. I, section 2, cl.3, and section 9, cl.4, of the original Constitution.

Afterwards, and evidently in recognition of the limitation upon the taxing power of Congress thus determined, the Sixteenth Amendment was adopted, in words lucidly expressing the object to be accomplished: "The Congress shall have power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration." As repeatedly held, this did not extend the taxing power to new subjects, but merely removed the necessity which otherwise might exist for an apportionment among the States of taxes laid on income. [Citing *Brushaber*, 240 U.S. at 17-19, and other cases.]

A proper regard for its genesis, as well as its very clear language, requires also that this Amendment shall not be extended by loose construction, so as to repeal or modify, except as applied to income, those provisions of the Constitution that require an apportionment according to population for direct taxes upon property, real and personal.⁷³ This limitation still has an appropriate and important function, and is not to be overridden by Congress or disregarded by the courts.

In order, therefore, that the clauses cited from Article I of the Constitution may have proper force and effect, save only as modified by the Amendment, and that the latter also may have proper effect, it becomes essential to distinguish between what is and what is not

“income” as the term is there used; and to apply the distinction, as cases arise, according to truth and substance, without regard to form. Congress cannot by any definition it may adopt conclude the matter, since it cannot by legislation alter the Constitution, from which alone it derives its power to legislate, and within whose limitations alone that power can be lawfully exercised.

The fundamental relation of “capital” to “income” has been much discussed by economists, the former being likened to the tree or the land, the latter to the fruit or the crop; the former depicted as a reservoir supplied from springs, the latter as the outlet stream, to be measured by its flow during a period of time. For the present purpose we require only a clear definition of the term “income,” as used in common speech, in order to determine its meaning in the Amendment; and, having formed also a correct judgment as to the nature of a stock dividend, we shall find it easy to decide the matter at issue.

After examining dictionaries in common use (Bouv. L.D.; Standard Dict.; Webster’s Internat. Dict.; Century Dict.), we find little to add to the succinct definition adopted in two cases arising under the Corporation Tax Act of 1909 (*Stratton’s Independence v. Howbert*, 231 U.S. 399, 415; *Doyle v. Mitchell Bros. Co.*, 247 U.S. 179, 185)—“Income may be defined as the gain derived from capital, from labor, or from both combined,” provided it be understood to include profit gained through a sale or conversion of capital assets, to which it was applied in the *Doyle* case (pp. 183, 185).

Brief as it is, it indicates the characteristic and distinguishing attribute of income essential for a

correct solution of the present controversy. The Government, although basing its argument upon the definition as quoted, placed chief emphasis upon the word “gain,” which was extended to include a variety of meanings; while the significance of the next three words was either overlooked or misconceived. **“Derived — from — capital;” — “the gain — derived — from — capital;”** etc. Here we have the essential matter: **not a gain accruing to capital, not a growth or increment** of value in the investment; **but** again, **a profit**, something of exchangeable value proceeding from the property, **severed from the capital** however invested or employed, and **coming in, being “derived,” that is, received, or drawn by** the recipient (the taxpayer) for his **separate** use, benefit and disposal;—that is income derived from property. Nothing else answers the description.

The same fundamental conception is clearly set forth in the Sixteenth Amendment—**“incomes, from whatever source derived”**—the essential thought being expressed with a conciseness and lucidity entirely in harmony with the form and style of the Constitution. [Emphasis added.]

Eisner, 252 U.S. at 205-206.

After defining the word income, the Court made it very clear that the Sixteenth “Amendment applies to income only.” *Eisner*, 252 U.S. at 219.

Merchants’ Loan & Trust Co. v. Smietanka, 255 U.S. 509 (1921):

Merchants’ Loan & Trust Co. was the trustee under the will of Arthur Ryerson who died in 1912. Under the trust, the net income of

the property was to be paid to his widow during her life and used for the benefit of the children after her death until the age of twenty-five, at which age each child would receive his or her share of the trust fund. Under the terms of the trust the trustee could decide what “net income” was, except that stock dividends and accretions of selling values were not to be considered income. *Smietanka*, 255 U.S. at 514-515.

In 1917 Ryerson’s widow and four children were alive. *Smietanka*, 255 U.S. at 515.

Among other assets, the trust received 9,522 shares of capital stock of Joseph T. Ryerson & Son, a corporation. On March 1, 1913, the stock was valued at \$561,798. On February 2, 1917, the stock was sold for \$1,280,996.64. The Commissioner of Internal Revenue treated the difference as income for the year 1917, and assessed a tax under the Income Tax Act of Congress approved September 8, 1916, c. 463, 39 Stat. 756, as amended by the Act approved October 3, 1917, c. 63, 40 Stat. 300. The tax was paid under protest and an action was filed in the Federal District Court to recover its payment. *Smietanka*, 255 U.S. at 514-515.

In the lower court, the Collector, Mr. Smietanka, filed a demurrer to the complaint which was sustained. The case then came to the Supreme Court under a writ of error, in which the trustee contended that the sum charged as “income” represented appreciation in the value of the capital assets of the estate which was not “income” within the meaning of the Sixteenth Amendment and therefore could not, constitutionally, be taxed without apportionment. *Smietanka, id.*

The Court first addressed the language of the statute and found that the trustee was a taxable person, and if the sum charged as “income” was indeed income within the meaning of the Sixteenth Amendment, it was taxable under the statute. Whether or not the over \$700,000 gain was such income, the Court felt, was a question of definition, the answer to which could be found in recent

decisions of the Court itself. *Smietanka*, 255 U.S. at 516-517. The Court stated that while the Corporation Excise Tax Act of August 5, 1909 was not an income tax law, a definition of the word “income” was essential in its early administration, and an early case defined the word as “the gain derived from capital, from labor, or from both combined,” and cited to *Stratton’s Independence v. Howbert*, 231 U.S. 399, 415. The Court then referenced its “latest income tax decision,” *Eisner*, and gave the latest definition of the word income: “Income may be defined as the gain derived from capital, from labor, or from both combined, provided it be understood to include profit gained through a sale or conversion of capital assets.” *Smietanka*, 255 U.S. at 517-518.

The Court then reviewed two cases under the Corporation Excise Tax Act wherein it was held that the profit made on the sale of stock of another corporation was income to the selling corporation under the above definition, and thought it was obvious that these two decisions in principle ruled the case under consideration if the word “income” had the same meaning in the Income Tax Act of 1913 that it had in the Corporation Excise Tax Act of 1909. It then cited to *Southern Pacific Co. v. Lowe*, 247 U.S. 330, 335 (1918), where it was assumed for the purposes of decision in that case that there was no difference. The Court then unequivocally stated:

There can be no doubt that the word must be given the same meaning and content in the Income Tax Acts of 1916 and 1917 that it had in the Act of 1913. When to this we add that in *Eisner v. Macomber*, *supra*, a case arising under the same Income Tax Act of 1916 which is here involved, the definition of “income” which was applied was adopted from *Stratton’s Independence v. Howbert*, *supra*, arising under the Corporation Excise Tax Act of 1909, with the addition that it should include “profit gained through a sale or conversion of capital assets,” there would seem to be no room to doubt that the word must be given the same meaning in all of the Income Tax Acts of

Congress that was given to it in the Corporation Excise Tax Act and that what that meaning is has now become definitely settled by decisions of this court.

In determining the definition of the word "income" thus arrived at, this court has consistently refused to enter into the refinements of lexicographers or economists and has approved, in the definitions quoted, what it believed to be the commonly understood meaning of the term which must have been in the minds of the people when they adopted the Sixteenth Amendment to the Constitution. *Doyle v. Mitchell Brothers Co.*, 247 U.S. 179, 185; *Eisner v. Macomber*, 252 U.S. 189, 206-207. Notwithstanding the full argument heard in this case and in the series of cases now under consideration we continue entirely satisfied with that definition, and, since the fund here taxed was the amount realized from the sale of the stock in 1917, less the capital investment as determined by the trustee as of March 1, 1913, it is palpable that it was a "gain or profit" "produced by" or "derived from" that investment, and that it "proceeded," and was "severed" or rendered severable, from, by the sale for cash, and thereby became that "realized gain" which has been repeatedly declared to be taxable income within the meaning of the constitutional amendment and the acts of Congress. *Doyle v. Mitchell Brothers Co.*, and *Eisner v. Macomber*, *supra*.

Smietanka, 255 U.S. at 519-520.

Finding that the amount received on the sale of the stock over the basis, the gain or profit, fell within the definition of the word "income" as used in the Sixteenth Amendment, the Court affirmed the

decision of the lower court. *Smietanka*, 255 U.S. at 519.

ENDNOTES

72. Section 2(a) was contained in Part I [pertaining to the income tax on “individuals”] of Title I [pertaining to the Income Tax].
73. This is the exact argument which was raised by Mr. Brushaber [*Brushaber*, 240 U.S. at 11] and rejected by the *Brushaber* Court [240 U.S. at 12]. There is an irreconcilable conflict between the *Brushaber* case, which holds the income tax is an indirect tax not requiring apportionment, and the *Eisner* case, which holds the income tax is a direct tax relieved from apportionment.

CHAPTER VI

THE LAW AND THE COURTS

1930-1939

Lucas v. Earl, 281 U.S. 111 (1930):

In 1901 Mr. Earl entered into a contract with his wife in which it was agreed that any property either of them then had or might later acquire, including salaries or fees, would be held in joint tenancy with each other.⁷⁴ Thereafter, Mr. Earl filed an income tax return in which he claimed one-half of his salary as gross income. Mr. Lucas, the Commissioner of Internal Revenue, caused a tax to be imposed upon the whole of Mr. Earl's salary, and the Board of Tax Appeals sustained this action. The Circuit Court of Appeals, however, reversed, and the case came to the Supreme Court by a writ of certiorari. *Lucas*, 281 U.S. at 113-114.

The Supreme Court cited Section 213(a) of the Revenue Act of 1918 approved February 24, 1919, c. 18, 40 Stat. 1065, which, it stated, imposed a tax upon the net income of every individual including "income derived from salaries, wages, or compensation for personal service ... of whatever kind and in whatever form paid." *Lucas*, 281 U.S. at 114.

The Court next stated that Mr. Lucas made a very strong argument that by virtue of the contract with his wife, the salary and fees became the joint property of himself and his wife immediately upon receipt. To escape this effect under California law which should be controlling, the Court said that the case was to be determined upon the import and reasonable construction of the taxing act. *Lucas*, 281 U.S. at 114-115. The Court then said that:

There is no doubt that the statute could tax salaries to those who earned them and provide that the tax could not be escaped by anticipatory arrangements and contracts however skillfully devised to prevent the salary when paid from vesting even for a second in the man who earned it.

Lucas, id.

The Court then, without any legal reasoning, stated that what Congress could have done, but did not do, was the “import” of the statute Congress did pass and reversed the Court of Appeals.

It is of critical significance to note that unlike Ms. Macomber who challenged the constitutionality of the tax on the stock dividend notwithstanding the clear language of the statute imposing the tax on that stock dividend, Mr. Lucas failed to object to the tax being imposed directly on his salary and fees as opposed to being imposed on the “income derived from [his] salaries, wages, or compensation for personal service ... of whatever kind and in whatever form paid.” The issue of whether or not salaries, wages or compensation for personal service constitutes income taxable under the Sixteenth Amendment was not litigated nor discussed by the Court, and the *Lucas* case is not authority for that proposition.⁷⁵

Bass v. Hawley, 62 F.2d 721 (5th Cir. 1933):

Mr. Bass, the Collector of Internal Revenue, appealed a judgment against him and in favor of Mr. Hawley who sought a recovery of an income tax he paid in 1925. The question was whether \$16,250 received by Hawley was a gift or additional compensation for services. *Bass*, 62 F.2d at 721-722.

Mr. Hawley had for twenty-two years worked for the El Paso & Southwestern Railroad Company. During a corporate buy-out of the stock of that company, in order to “recognize the long and faithful service of the officers and employees,” the directors authorized the

payment of “additional compensation.” Mr. Hawley received the \$16,250, and based upon certain lower court cases, argued that since the payments were “over and above the wages and salaries due” and there was no obligation on the part of the railroad to pay the additional money, that the money was a gift. *Bass*, 62 F.2d at 722.

The Court cited to cases holding to the contrary,⁷⁶ and then stated that “whether a payment in a given case shall be deemed taxable compensation or a gift exempt from tax depends on the intention of the parties and particularly that of the payer, to be determined from the attending facts and circumstances.” *Bass*, 62 F.2d at 722-723.

In order to distinguish a gift from taxable income, the Court correctly cited to the holding in *Eisner* that “[i]ncome that may be taxed includes gain derived from labor.” *Bass*, 62 F.2d at 723. The Court went on to say:

One who in the peace and under the protection of the United States gainfully exercises his faculties of mind or body may be called on to share the gain with the public treasury. Section 213 of the Revenue Act of 1926 (26 USCA Section 954) here applicable includes in gross income to be taxed “gains, profits and income derived from salaries, wages, or compensation for personal service * * * of whatever kind and in whatever form paid.”

Bass, 62 F.2d at 723.

The Court cites no authority for its first sentence quoted above, so the reader is left to guess at what is meant. It appears the Court is saying that working in a situation where the government provides certain safeguards is a privilege and the tax is an excise on that privilege.⁷⁷ That would explain the reference to “receiving the protection of the United States,” but would exclude workers not receiving such protection; that is, the privilege of working under

this protection would only exist where the United States has lawful authority to give such protection, and that is in Washington D.C., the United States territories and other federal enclaves.⁷⁸ The Court went on to say:

It [the statute] excludes property acquired by “gift, bequest, devise or inheritance.” The intent is that all receipts in whatever form that come because of labor and service, whether payment could be compelled or not, shall be taxed as arising from labor.

Bass, 62 F.2d at 723.

The *Bass* Court, in choosing the language quoted above, appears to be stating that a conversion of labor into money always produces income. In *Doyle*, the government contended that a conversion of “capital” into money always produces income, and the Supreme Court held this was not necessarily so; it had to be determined based upon the facts, after deducting from gross receipts an amount sufficient to restore the capital value, whether there was a gain or loss (see p. 128). Since “income” is defined as “the gain derived from capital, from labor, or from both combined,” then by merely substituting the word “labor” for the word “capital” in the *Doyle* case one can easily see that the *Bass* Court’s wording, if taken literally, would be contrary to the theory of law as expressed by the United States Supreme Court.

In that the \$16,250 was over and above the employment contract price Mr. Hawley was charging the railroad for his services, the bonus payment was indeed a “profit or gain derived from his labor,” and as “income,” was taxable under the Sixteenth Amendment. Thus the *Bass* Court reached the proper conclusion in the case before it, obviously had a correct understanding of the applicable law, and it would appear clear that it did not intend to hold that an unapportioned direct tax on labor was authorized under the Sixteenth Amendment.

ENDNOTES

74. A joint tenant holds an undivided interest in the whole property subject to an identical interest of each of the other joint tenants. The Court recognized the validity of the contract under California community property laws, *Lucas*, 281 U.S. at 114, thus again confirming that salaries and fees constitute property.
75. It is the policy of the Supreme Court of the United States not to address an opinion upon an issue not before it unless its determination is necessarily involved in the adjudication of the case. *Sullivan v. Iron Silver Mining Co.*, 109 U.S. 550, 553 (1883).
76. On page 722 the Court admits that the Board of Tax Appeals and the Court of Claims had reached opposite conclusions as to the taxability of this type of payment.
77. The *Brushaber* Court found the tax to be an indirect excise tax, while *Pollock* and *Eisner* found the income tax to be a direct tax.
78. See United States Constitution, Article I, Section 8, Clause 17.

CHAPTER VII

THE LAW AND THE COURTS

1940-1949

Ward v. C.I.R., 159 F.2d 502 (2nd Cir. 1947):

Ward is another case in which “additional compensation” was litigated. On a tax return filed in 1941, the Commissioner determined a deficiency and issued a notice therefor. Mr. Ward petitioned the Tax Court, lost the case, and filed an appeal. *Ward*, 159 F.2d at 502.

Mr. Ward was the president of Fairchild Engine and Airplane Corporation. In 1941 a deferred refund annuity policy was purchased and delivered to Mr. Ward as additional compensation for services. Prior to purchasing the annuity, an attorney advised Fairchild that if the annuity was non-assignable, Mr. Ward would not be taxed until he started to receive payments under it. In other words, the value of the annuity given to Mr. Ward as additional compensation would not constitute income. *Ward*, 159 F.2d at 503-504.

Unfortunately, the annuity policy was not made nonassignable until 1945 when the parties learned the Commissioner claimed the value of the annuity policy was taxable as again derived from compensation for services. At that time it was “reformed” to conform to the original arrangement anticipated at the time of the purchase of the annuity policy. *Ward*, 159 F.2d at 503-504. The Court clearly defined the issue of the case to be one of law as follows:

On these facts the decisive issue presented on review is one of law. It is whether the policy which was not in 1941 in terms restricted as to assignability was nevertheless non-assignable by the taxpayer from the date of delivery because his employer had an enforceable interest in it which would have enabled Fairchild to prevent any attempt by the taxpayer to “realize” its assignable value in the taxable year of the policy’s receipt by him.⁷⁹

Ward, 159 F.2d at 504.

The Court pointed out that Mr. Ward had made no agreement to continue to work for Fairchild after receipt of the policy, and that the terms of his employment contract were unaffected by the terms of the annuity policy. *Ward, id.*

The Court concluded that since the annuity policy was assignable, Mr. Ward could do with it as he liked, and the value of the policy was taxable to Mr. Ward when he received it. *Ward, id.*

This case in essence confirms that a receipt of something worth value over and above payment as compensation for services as set forth in an employment contract is a gain derived from compensation for services, and is taxable as income. Whether or not the compensation for services can be taxed or only the gain derived from the compensation for services can be taxed was not in issue and was not litigated.

ENDNOTES

79. With Fairchild as the owner of an assignable policy, it could have asked Ward to return it and the policy could have been given to someone else. Because of this option, Fairchild still had an interest in the policy which precluded Ward from “realizing” the policy for his own separate use.

CHAPTER VIII

THE LAW AND THE COURTS

1950-1959

C.I.R. v. Glenshaw Glass Co., 348 U.S. 426 (1955):

The issue involved in the *Glenshaw Glass* case was whether money received as exemplary damages for fraud or as the punitive two-thirds portion of a treble-damage antitrust recovery had to be reported by a taxpayer as gross income under Section 22(a) of the Internal Revenue Code of 1939. *Glenshaw Glass*, 348 U.S. at 427. The Glenshaw Glass Company did not raise any constitutional objections to the imposition of a tax on punitive damages, so the question before the Supreme Court was one of statutory construction: Did the punitive damages that the Glenshaw Glass Company received after suing the Hartford-Empire Company fall within the definition of gross income as defined in Section 22(a)? *Glenshaw Glass*, 348 U.S. at 426.

The Court quoted Section 22(a), and emphasized the following bold-faced words: “Gross income includes ... gains or profits and income⁸⁰ derived from any source whatever ... The Court stated that this language was used by Congress to exert “the full measure of its taxing power,” and stated that the Court had given a liberal construction to this broad phraseology in recognition of the intention of Congress to tax all gains except those specifically exempted. The Court found that the punitive damage payments were noncompensatory in nature, they constituted an undeniable accession to wealth, clearly realized, and were such that the taxpayer had complete dominion over them. Finding such payments to thus constitute a “gain,” the Court held that the gain

fell within the provisions of Section 22(a) above bold-faced. *Glenshaw Glass, id.*

The *Glenshaw Glass* case does not stand for the proposition that wages constitute income—the case did not involve wages; the case stands for the direct proposition that punitive damages constitute a gain which falls within the definition of gross income, and for the indirect proposition that Congress intended to tax all receipts constitutionally taxable. With respect to the Sixteenth Amendment, those taxable receipts are those which represent a profit or a gain, not an equal exchange.

ENDNOTES

80. It is interesting to note that under the Internal Revenue Code of 1939, the definition of gross income used the words “gains or profits and income.” When the 1954 Internal Revenue Code was enacted, the words “gains or profits” were omitted from the definition of gross income as being unnecessary.

CHAPTER IX

THE LAW AND THE COURTS

1960-1969

Penn Mutual Indemnity Company v. C.I.R., 277 F.2d 16 (3rd Cir. 1960):

This case involved an insurance company which had filled out a Form 1120M reporting an income tax due of \$12,566.76. Attached to the form was a letter from an attorney advising the I.R.S. that the company was taking the position that the imposition of an income tax against it was invalid and unconstitutional. *Penn Mutual*, 277 F.2d at 17. The tax was imposed by Section 207(a)(2) of the Internal Revenue Code of 1939, and the relevant portion of that section was one which imposed a one percent tax upon the taxpayer's "gross amount of income from interest, dividends, rents, and net premiums," minus dividends to policyholders and tax-exempt interest; "net premiums" were defined as the total premiums written or received less return premiums. *Penn Mutual*, 277 F.2d at 18.

Penn Mutual, for the year in question, did not make a profit. In fact, it had underwriting losses of \$206,198.12 in excess of its "gross amount of income from interest, dividends, rents, and net premiums." It argued, therefore, that there being no profit or gain, there could be no "income tax" due. Accordingly, it did not pay the tax shown as due on the Form 1120M. *Penn Mutual*, 277 F.2d at 17-19.

In support of this argument *Penn Mutual* contended that since the tax-imposing provisions relied on [Section 207(a)(2)] occurred in the middle of an income tax statute and were labeled by Congress as

“income tax” provisions, the sole test of their validity was whether the provisions of the statute taxed “income” within the meaning of the Sixteenth Amendment.

With respect to this argument the Court stated:

We think petitioner’s argument imposes tighter restrictions on the federal taxing power than a century and a half of court decisions warrant.

Perm Mutual, 277 F.2d at 19.

The Court did not identify the “court decisions” it contended allowed for an income tax on something other than income. Instead, the Court first stated that the taxing power of Congress granted by Article I of the Constitution was exhaustive and embraced every conceivable power of taxation subject only to the requirement of apportionment for direct taxes, uniformity for indirect taxes and the prohibition of placing export duties on articles exported from the States, citing *Brushaber* and the United States Constitution as authority for these statements. The Court then stated that it did not take a constitutional amendment to allow Congress to impose an income tax citing to *Pollock*, and then stated that the Sixteenth Amendment removed the requirement for apportionment of the income tax, citing to the Sixteenth Amendment. Finally, the Court stated that the requirement for apportionment was pretty well strictly limited to taxes on real and personal property and capitation taxes, citing to *Hylton v. United States*, 3 U.S. 171 (1796); *Springer v. United States*, 102 U.S. 586 (1880); and *Pollock. Penn Mutual*, 277 F.2d at 19.

All of these contentions are correct, but do not add up to the proposition that Congress can tax as income something that is not a profit or gain. The United States Supreme Court made it abundantly clear in *Smietanka*, 255 U.S. at 519-520, that the word “income” was to have the same meaning in all of the income tax acts passed by Congress as it had in the Act of 1909. As previously set forth

hereinabove (see p. 144), that definition of income is a profit or gain.

The failure of the Court in *Penn Mutual* to abide by the Supreme Court's decisions defining income renders its decision fatally defective as contrary to established law. In any event, the case did not involve wages and hence, does not stand for the proposition that wages constitute income.

C.I.R. v. Daehler, 281 F.2d 823 (5th Cir. 1960):

The issue before the Court in *Daehler* was whether a real estate salesman's commission on the sale of a house that the salesman bought for himself constituted taxable income under Section 22(a) of the Internal Revenue Code of 1939. *Daehler, id.* Mr. Daehler made an offer to purchase certain real estate for himself. After the sale was consummated, the brokers for the seller and the buyer (the real estate broker for whom Mr. Daehler worked) split a ten percent commission, and Mr. Daehler's employer paid Mr. Daehler his proportionate share which he did not include in his tax return as income. The Tax Court held that since Mr. Daehler bought the house for himself, he was not acting as a salesman, and the amount that he received was a reduction in the purchase price as opposed to a commission. *Daehler*, 281 F.2d at 824.

The Court of Appeals reversed holding that the amount Mr. Daehler received from his employer was compensation for the actions he performed growing out of the employer-employee relationship, and that compensation for such services is taxable income⁸¹ of whatever kind and in whatever form it is received. *Daehler*, 281 F.2d at 824-825.

Mr. Daehler did not contest whether such commissions constituted income from the perspective of gain or profit, and the case did not involve the issue of whether wages constitute income. The issue not being raised in the case, *Daehler* does not constitute precedent for the issue of whether wages constitute income.

C.I.R. v. Mendel, 351 F.2d 580 (4th Cir. 1965):

Dr. Mendel was a physician who, at the request of his employer, moved from Newark, New Jersey, to Richmond, Virginia. He had been employed in New Jersey for four years prior to the move. He incurred moving expenses in the amount of \$558.99 for which he was reimbursed \$316.00 by his employer. Dr. Mendel “deducted” the difference from his gross income, and the deduction was not allowed by the Commissioner. The issue was taken to the Tax Court where it was held the deduction was permissible under Rev. Ruling 54-429, 1954-2 Cum.Bull. 53. *Mendel*, 351 F.2d at 581-582.

The Court of Appeals held that the Tax Court had proceeded upon an erroneous basis. The Tax Court had interpreted the Revenue Ruling as meaning that reasonable expenses incurred in relocating were business expenses, and could be deducted from total gross income. The Court of Appeals felt Revenue Ruling 54-429 did not stand for the proposition that moving expenses were a business expense, but stood for the proposition that reimbursed moving expenses did not constitute gross income. Under this analysis, the \$361.00 would not be taxed as gross income, but no deduction would be allowed for the difference between the amount reimbursed and the total cost of the move. *Mendel*, 351 F.2d at 582.

As the basis for its ruling, the Court of Appeals first cited to the theory expressed in *United States v. Woodall*, 255 F.2d 370 (10th Cir. 1958), that:

[A]ny economic or financial benefit conferred on an employee as compensation is gross income, and that there may be deducted from gross income only those expenditures expressly made deductible by statute. Ordinarily, reimbursement for moving expense to an existing employee would constitute gross income under the comprehensive definition in Section 61 (a) of the Revenue Code of 1954 that, “* * * gross income means all income from whatever source derived,

including (but not limited to) * * * Compensation for services, including fees, commissions, and similar items * * *.”

Mendel, 351 F.2d at 582

and then indicated its belief that:

Rev.Ruling 54-429, *supra*, sought to alleviate the rigors of the application of the statutory definition of gross income to reimbursement for moving expenses to an existing employee. An examination of the ruling discloses that its rationale is that reimbursement for moving expenses does not constitute gross income, not, as the Tax Court determined, that expenses of relocation are per se deductions for the employee.

Mendel, 351 F.2d at 582.

That Section 61 (a) does not include compensation for services in gross income, only the profit or gain derived from compensation for services has been established above. Thus Revenue Ruling 54-429 was not for the purpose of alleviating the rigors of the application of the statutory definition of gross income as contended by the Court, but for the purpose of bringing the administration of the law into conformity with the statutory definition. This is the only possible conclusion based not only upon the law, but from the long-standing Constitutional principle that the I.R.S. cannot change legislation by revenue rulings.⁸²

United States v. Rochelle, 384 F.2d 748 (5th Cir. 1967):

Mr. Addison was a promoter. He and his associates obtained “loans” to finance various enterprises from people based upon the assurance that the loaners would get their money back together with a part interest in the enterprise which would produce a profit. No such enterprises existed, and an involuntary petition in

bankruptcy was filed by the creditors who had loaned the money. The I.R.S. asserted that the money loaned constituted income, and filed a claim against the bankruptcy estate for income taxes. *Rochelle*, 384 F.2d at 749-750. The issue before the Court was stated as follows:

When an individual secures money from many third parties by false representations, and when such funds constitute his sole source of support for several years, do these sums constitute taxable income, under section 61 of the Internal Revenue Code, notwithstanding the fact that the transactions are in the form of loans.

Rochelle, 384 F.2d at 751.

The Court stated:

The proper labeling for tax purposes of various kinds of ill-gotten gains has long been a vexing question for the federal courts. In dealing with it, we keep in mind the admonition that in enacting what is now section 61 of the tax code, Congress meant “to use the full measure of its taxing power” under the Sixteenth Amendment. *Helvering v. Clifford*, 309 U.S. 331, 334. The Supreme Court, after many years of hesitation, has now firmly concluded that the economic benefit accruing to the taxpayer is the controlling factor in determining whether a gain is “income.” *Rutkin v. United States*, 343 U.S. 130 [1952]; *Commissioner v. Glenshaw Glass Co.*, 248 U.S. 426; *James v. United States*, 366 U.S. 213. A loan does not in itself constitute income to the borrower, because whatever temporary economic benefit he derives from the use of the funds is offset by the corresponding obligation to repay them. See, *James v. United States*, 266 U.S. at 219. Where the loans are obtained by fraud, and

where it is apparent that the recipient recognizes no obligation to repay, the transaction becomes a “wrongful appropriation” [and comes] within the broad sweep of “gross income.” [Emphasis in original.]

Rochelle, 384 F.2d at 751.

The “economic benefit” mentioned in *Glenshaw Glass* was the punitive damages awarded to the Glenshaw Glass Company, which the Court concluded were a “gain” (see p. 159). The issue before the Supreme Court in *Rutkin*, was whether money obtained by extortion is income taxable to the extortioner under Section 22(a) of the Internal Revenue Code. *Rutkin*, 343 U.S. at 131. The Supreme Court found that extorted funds do constitute a gain and are includible within the statutory definition of gross income. *Rutkin*, 343 U.S. at 137. The issue before the Supreme Court in *James* was whether embezzled funds were to be included in the gross income of the embezzler in the year in which the funds were misappropriated under Section 22(a) of the 1939 Internal Revenue Code and Section 61(a) of the 1954 Internal Revenue Code. *James*, 266 U.S. at 213-214. The Supreme Court, relying upon *Rutkin*, found that embezzled funds were a gain, and hence taxable. *James*, 266 U.S. at 218-219.

These cases may be cited for the proposition that unlawful gains are as taxable as lawful gains, but in that none of them addressed the issue as to whether wages constitute income, *Rochelle* does not constitute legal precedent for that issue.

Marks v. United States, 391 F.2d 210 (9th Cir. 1968):

Mr. Marks was convicted of federal income tax evasion for the year 1961; his tax return showed no taxable income while the government contended the return should have shown a taxable income. Mr. Marks contended that four specific items were not gross income but rather loans. The Court recognized that the

defendant presented evidence that showed on its face that the four transactions were loans, but also found that the jury had evidence in front of it to conclude the transactions were not loans. The government contended that the amounts received were either compensation for services or money obtained by Marks under false pretenses. *Marks*, 391 F.2d at 210-211.

With respect to the government's contentions, the Court stated that: "[e]ither is taxable" and footnoted to 26 U.S.C. Section 61 and *Rochelle*. *Marks*, 391 F.2d at 211. It has already been shown that compensation for services does not constitute gross income under Section 61; rather, the profit or gain derived from compensation for services constitutes gross income under Section 61. And as shown above, the *Rochelle* case did not involve the issue of whether wages constitute income. Thus, the *Marks* case does not support the conclusion that wages constitute income.

***Wilson v. United States*, 412 F.2d 694 (1st Cir. 1969):**

Mr. Wilson, a police officer, ate one meal per day, during his work period, in a restaurant away from home. He was reimbursed the cost of these meals by his employer. Mr. Wilson contended these amounts were excluded from gross income by virtue of Section 119 which excluded from gross income the value of any meals furnished by an employee by the employer for the convenience of the employer if the meals are furnished on the business premises of the employer. *Wilson*, 412 F.2d at 695.

The entire case turned around the wording of Section 119 and the legislative intent of Congress in enacting it. However, the Court made one statement, wholly unsupported by any citation to case law or statute, that:

We start with the proposition that all remuneration received for services is gross income unless it falls within a specific exclusion.

Wilson, 412 F.2d at 695.

This is the exact contention that the Supreme Court found untenable in *Doyle*, 247 U.S. at 183-184 (see p. 128). Remuneration for services can only constitute gross income if there is a profit or gain derived from that remuneration. The *Wilson* case stands for the principle that reimbursement for meals off the premises of the employer is not deductible as a business expense, not for the principle that remuneration for services constitutes income. The *dicta* of the *Wilson* Court is not supported by case law and is contrary to the *Doyle* decision by the United States Supreme Court. The *Wilson* case does not support the proposition that wages constitute income.

ENDNOTES

81. The use of the term “taxable income” by the Court of Appeals was technically incorrect. Taxable income is adjusted gross income less certain statutory deductions, and adjusted gross income is gross income less certain statutory deductions.
82. See *Morrill v. Jones*, 106 U.S. 466, 467 (1882); *U.S. v. 200 Barrels of Whiskey*, 95 U.S. 571, 576 (1887).

CHAPTER X

THE LAW AND THE COURTS

1970-1979

United States v. Silkman, 543 F.2d 1218 (8th Cir. 1976):

Mr. Silkman, representing himself, appealed an order of the District Court directing his compliance with an I.R.S. summons seeking certain records with respect to the 1973 and 1974 tax years. One of his contentions in seeking not to comply with the summons was that he was not an individual required to pay taxes because he was engaged in the common law occupations of farming and ranching. In rejecting this contention, the Court stated:

Finally, we find no merit in the taxpayer's contention that he is not an individual required to pay taxes because he is engaged in the common law occupations of farming and ranching. The Sixteenth Amendment broadly grants Congress the power to collect an income tax regardless of the source of the taxpayer's income.

Silkman, 543 F.2d at 1220.

The basis for Mr. Silkman's legal argument, if he made any, was not set forth in the opinion, nor did the Court cite to any case law or give any hint as to the basis of the Court's legal analysis of Mr. Silkman's argument. In any event, the case does not stand for the proposition that wages constitute income, as "wages" are not even mentioned in the case. As to the Court's statement that the Sixteenth Amendment broadly grants Congress the power to collect an income tax regardless of the source of the taxpayer's income,

there is no argument. A tax on one's labor, however, as has been shown herein, is not a tax on income!

Reading v. C.I.R., 70 T.C. 730 (1978):

Mr. Reading, representing himself and his wife in Tax Court, argued that Congress, by denying deductions for personal, living, and family expenses in the computation of taxable income, had exceeded its authority under the Sixteenth Amendment to the Constitution to lay and collect taxes on "incomes." Citing the definition of income in *Eisner*, he argued that the "gain" from labor could not be determined until their "cost of doing labor," *i.e.*, their expenditures at issue, had been subtracted from the amount received from the sale of labor. He attempted to support this contention by making an analogy between the "living expenses" of one who depends upon the sale of his services for his livelihood with the "cost of goods sold" concept in certain business contexts. *Reading*, 70 T.C. at 732. The Court stated:

Nevertheless, accepting the conclusion that some kind of "gain" must be realized for there to be income, the flaw in petitioners' analogy of what they call the "cost of doing labor" to the "cost of goods sold" concept—essentially its failure to acknowledge the difference between people and property—may be shown. The "cost of goods sold" concept embraces expenditures necessary to acquire, construct or extract a physical product which is to be sold; the seller can have no gain until he recovers the economic investment that he has made directly in the actual item sold. [Citations.] Labor, on the other hand, is, in the current context, behavior performed by human beings in exchange for compensation. One's living expenses simply cannot be his "cost" directly in the very item sold, *i.e.*, his labor, no matter how much money he spends to satisfy his human needs and those of his family. Of course we recognize the necessity for

expenditures for such items as food, shelter, clothing, and proper health maintenance. They provide both the mental and physical nourishment essential to maintain the body at a level of effectiveness that will permit its labor to be productive. We do not even deny that a certain similarity exists between the “cost of doing labor” and the “cost of goods sold” concept. But the sale of one’s labor is not the same creature as the sale of property, and whether the distinction comports with petitioners’ philosophical rationalization for their argument, it is recognized for Federal income tax purposes. See *Hahn v. Commissioner*, 30 T.C. 195 (1958), *affd. per curiam* 271 F.2d 739 (5th Cir. 1959). One’s gain, ergo his “income,” from the sale of his labor is the entire amount received therefor without any reduction for what he spends to satisfy his human needs. [Emphasis in original.]

Reading, 70 T.C. at 733-734.

In *Hahn*, the sole issue before the Tax Court was whether Mr. Hahn could claim his parents as dependents in 1952. *Hahn*, 30 T.C. at 195. Mr. Hahn claimed a \$600 deduction for each of his parents on his income tax return, having paid more than half of their support during the year. The deduction was only permissible if each of his parent’s gross income was under \$600. The I.R.S. reviewed his parents tax return, where at Schedule C, it was shown that the senior Mr. Hahn was a blacksmith, and that he had deducted a certain amount for costs of goods sold. The I.R.S. contended that inasmuch as the senior Mr. Hahn was a blacksmith he had no merchandise to sell; therefore, the expenses would not be deducted from gross receipts in computing gross income, but would be deducted from gross income in the computation of adjusted gross income. The I.R.S. disallowed the deductions as “cost of goods sold, such that each of the parents had more than \$600 of gross income under the Texas community property laws. *Hahn*, 30 T.C. at 197. The Tax Court found that the senior Mr. Hahn was not engaged in

manufacturing but in providing services, and agreed with the I.R.S. that the expenses were deductible as business expenses from gross income.

The *Hahn* case did not involve the issue of whether wages constitute income. While the Court did distinguish between those expenses which are deducted from gross receipts to obtain gross income when manufacturing is involved from those business expenses deducted from gross income to arrive at adjusted gross income, the conclusion of the *Reading* Court that everything that comes in to a wage earner constitutes income does not necessarily follow. This conclusion was rejected by the Supreme Court in *Doyle* (see p. 128).

The *Reading* Court then quoted from the Supreme Court as follows:

For income tax purposes Congress has seen fit to regard an individual as having two personalities: "one is [as] a seeker after profit who can deduct the expenses incurred in that search; the other is [as] a creature satisfying his needs as a human and those of his family but who cannot deduct such consumption and related expenditures."

United States v. Gilmore, 372 U.S. 39,
44 (1963).

In *Gilmore*, the question before the Court involved the deductibility for federal income tax purposes of that part of the husband's legal expense incurred in such proceedings as was attributable to his successful resistance of his wife's claims to certain of his assets asserted by her to be community property under California law. *Gilmore*, 372 U.S. at 40.

The bulk of Mr. Gilmore's property consisted of controlling stock interests in three corporations, each of which was a franchised General Motors automobile dealer. Mr. Gilmore was president and

principal managing officer of the three corporations. His overriding concern in the divorce litigation was the protection of those assets against the claims of his wife because he believed that if he lost controlling interest by transferring one-half of the shares to his wife, he might lose his corporate position which was the main source of his livelihood. *Gilmore*, 372 U.S. at 41-42.

Mr. Gilmore won the divorce action. He claimed his legal fees as a deduction on his income tax return as an expense “incurred ... for the ... conservation ... of property held for the production of income” under Section 23(a)(2) of the 1939 Internal Revenue Code. *Gilmore*, 372 U.S. at 43. The government contended that the test under Section 23(a)(2) as to whether the expenses were personal or for the conservation of income-producing property turned not upon the **consequences** of Mr. Gilmore’s failure to defeat his wife’s community property claims, but upon the **origin** and **nature** of the claims themselves. The government contended that the expense of defeating his wife’s claim against the stock must be deemed nondeductible “personal” or “family” expense under Section 24(a)(1) of the Code, not deductible expense under Section 23(a)(2) of the Code. *Gilmore*, 372 U.S. at 43-44.

It was in this context that the *Gilmore* Court made the statement quoted by the *Reading* Court. In resolving the issue against Mr. Gilmore, the Supreme Court stated:

A basic restriction upon the availability of a Section 23(a)(1) deduction is that the expense item involved must be one that has a business origin. That restriction not only inheres in the language of Section 23(a)(1) itself, confining such deductions to “expenses ... incurred ... in carrying on any trade or business,” but also follows from Section 24(a)(1), expressly rendering nondeductible “in any case ... [p]ersonal, living, or family expenses.”

Gilmore, 372 U.S. at 46.

The Court also said:

[T]he characterization, as “business” or “personal,” of the litigation costs of resisting a claim depends on whether or not the claim **arises in connection with** the taxpayer’s profit-seeking activities. It does not depend on the **consequences** that might result to a taxpayer’s income-producing property from a failure to defeat the claim, ... [Emphasis in original.]

Gilmore, 372 U.S. at 48.

The *Gilmore* case did not adjudicate the issue of whether or not wages constitute income.

Mr. Reading attempted to deduct personal expenses from his gross receipts to arrive at his gross income, and the decision of the *Reading* Court was that such deductions from gross receipts were not permissible. The issue of whether wages constitute income was not before the Court, and its unsupported statement that gross receipts is the same as income was *dicta*. The *Reading* Court also stated that the sale of one’s labor is not the same creature as the sale of property. It is interesting to note that in the case of *Adkins v. Children’s Hospital*, 261 U.S. 525 (1922), involving the constitutionality of a law providing for the fixing of minimum wages for women and children in the District of Columbia, the Supreme Court stated, although not in discussing income taxes:

In principle, there can be no difference between the case of selling labor and the case of selling goods.

Adkins, 261 U.S. at 558.

Perhaps as to the deductibility of personal expenses being on the same footing as the deductibility of cost of goods sold, the Court is correct. But the Supreme Court has specifically stated that the sale of one’s labor constitutes personal property (see p. 85). And while

personal expenses may not be deductible from gross income, the Internal Revenue Code specifically provides that only the amount received in excess of the fair market value of personal property upon its sale constitutes gain. (See 26 U.S.C. Sections 1001 *et seq.*) And even the *Reading* Court recognized that only gain constitutes income.

United States v. Russell, 585 F.2d 368 (8th Cir. 1978):

Mr. Russell, representing himself, appealed his conviction on two counts of failing to file federal income tax returns. As part of his appeal, he challenged the constitutionality of the entire tax law; the Court used the following language in stating Mr. Russell's contention:

In addition, Russell's constitutional challenge of the entire tax law, *i.e.*, earnings from the exercise of his "common law right to work" cannot be taxed under the Sixteenth Amendment, also fails, because "[t]he Sixteenth Amendment broadly grants Congress the power to collect an income tax regardless of the source of the taxpayer's income." *United States v. Silkman, supra*, 543 F.2d at 1220.

Russell, 585 F.2d at 370.

The *Russell* case relies entirely upon the *Silkman* case, which as shown immediately above, does not stand for the legal proposition that wages constitute income. Both *Russell* and *Silkman*, to the extent they warrant consideration as binding opinions, only stand for the proposition that income can be taxed even if the income is derived from certain occupations that were recognized in the common law. The cases do not stand for the proposition that the source of the income can be taxed.

Adams v. United States, 585 F.2d 1060 (Ct. Cls. 1978):

The Adams case involved a tax refund suit in which the issue was whether the fair rental value of a Japanese residence furnished to Mr. Adams by his employer was excludable from Mr. Adams' gross income. *Adams*, 585 F.2d at 1061. Mr. Adams was the president of a corporation located in Japan, which corporation was wholly owned by his employer, Mobil Oil Corporation. In order to maintain prestige in the Japanese business community, Mobil thought it important that Mr. Adams live in an appropriate house. Therefore, the corporation of which Mr. Adams was the president purchased a house in Japan and required that Mr. Adams live in it. The house was also designed so that it could accommodate the business activities of Mr. Adams, and he frequently conducted business there. The policy of Mobil, in order to attract qualified employees for foreign service and to maintain an equitable relationship between its domestic and American foreign-based employees, was to calculate a "U.S. Housing Element" for each American foreign-based employee, and to subtract that amount from the employee's salary. If Mobil provided housing to the employee, the employee would include in his gross income for federal tax purposes the U.S. Housing Element amount. *Adams*, 585 F.2d at 1062.

Mr. Adams included in his gross income for federal tax purposes, as the value of the housing furnished him by his employer, the U.S. Housing Element amounts which had been subtracted from his gross salary, totaling \$4,439 for 1970 and \$4,824 for 1971. However, because the cost of housing in Tokyo those years was considerably higher than that in the United States, the fair rental value of the residence furnished to Mr. Adams, it was agreed between the parties, was \$20,000 in 1970 and \$20,599.09 in 1971. The I.R.S., after auditing Mr. Adams for 1970 and 1971, increased his gross income by the difference in the amounts between the U.S. Housing Element and the fair market value of the house, and assessed an additional \$914.24 plus interest. Mr. Adams paid the tax and sought a refund. *Adams*, 585 F.2d at 1062-1063.

Mr. Adams did not contest whether the difference between the U.S. Housing Element and the fair market value of the residence constituted income to him, but contended that since the house was furnished to him by his employer for the convenience of the employer, the amount was specifically excluded from gross income under Section 119 of the Internal Revenue Code of 1954, and the Court of Claims agreed. *Adams*, 585 F.2d at 1063.

While the Court of Claims cited Section 61(a)(1) of the Internal Revenue Code and Section 1.61-2(d)(1) of the Treasury Regulation for the proposition that “[i]f services are paid for other than in money, the fair market value of the property or services taken in payment must be included in income,” the statement of the Court was *dicta*. The issue as to whether wages constitute income was not before the Court; and because that issue was not litigated, the *Adams* case is not binding precedent for the contention that wages constitute income.

CHAPTER XI

THE LAW AND THE COURTS

1980-1989

United States v. Francisco, 614 F.2d 617 (1980):

Mr. Francisco was charged with three counts of failure to file income tax returns and was convicted. On appeal, his first contention was that the government failed to prove the receipt of gross income sufficient to require the filing of a return under Section 6012.⁸³ The Court found this argument to be without merit in that Mr. Francisco had stipulated to receiving “gross compensation on sales” for each year in question, which figures were calculated by subtracting the cost of goods sold from total sales. Citing *United States v. Ballard*, 535 F.2d 400, 404-405 (8th Cir. 1976), the Court stated that gross income for merchants is the amount representing gross receipts less the cost of goods sold. *Francisco*, 614 F.2d at 618.

Mr. Francisco also raised a constitutional challenge to his conviction based upon two theories: 1) the income tax was an indirect tax; and (2) income received in exchange for labor or services was not income within the meaning of the Sixteenth Amendment. *Francisco*, 614 F.2d at 619. As to the first argument, the Court stated:

The cases cited by Francisco clearly establish that the income tax is a direct tax, thus refuting the argument based upon his first theory. See, *Brushaber v. Union Pacific Railroad Co.*, 240 U.S. 1, 19 (1916) (the purpose of the Sixteenth Amendment was to take the

income tax “out of the class of excises, duties and imposts and place it in the class of direct taxes.”)

Francisco, 614 F.2d at 619.

The Court, unfortunately, did not elucidate in its opinion what theory Mr. Francisco raised. However, the Court’s statement as to the purpose of the Sixteenth Amendment is exactly the opposite of what the *Brushaber* Court stated was the purpose of the Sixteenth Amendment:

Second, that the contention that the Amendment treats a tax on income as a direct tax although it is relieved from apportionment and is necessarily therefore not subject to the rule of uniformity as such rule only applies to taxes which are not direct, thus destroying the two great classifications which have been recognized and enforced from the beginning, is also wholly without foundation since the command of the Amendment that all income taxes shall not be subject to apportionment by a consideration of the sources from which the taxed income may be derived, forbids the application to such taxes of the rule applied in the *Pollock* case by which alone **such taxes were removed from the great class of excises, duties and imposts subject to the rule of uniformity and were placed under the other or direct class.** [Emphasis added.]

Brushaber, 240 U.S. at 18-19.

It is thus beyond peradventure that the *Francisco* case can carry any credibility whatsoever when the Court of Appeals so completely disregarded the holding of the United States Supreme Court in the *Brushaber* case.

The Court of Appeals next held that Mr. Francisco's argument based upon his challenge that income received from labor or services was not income that was taxable under the Sixteenth Amendment was inappropriate because Mr. Francisco stipulated to receiving "gross compensation on sales." The Court also stated that Mr. Francisco's argument was invalid because Congress intended to tax income from whatever source derived. *Francisco*, 614 F.2d at 619. The Court of Appeals was correct in its assertion that Congress did intend to tax income from whatever source derived, including labor or personal services, but that is not the same as saying money received in exchange for labor or services is income. To constitute income, there must be a profit or gain.

Hayward v. Day, 619 F.2d 717 (8th Cir. 1980):

Mr. Hayward was convicted by a jury of four counts of failure to file income tax returns. The Eighth Circuit Court of Appeals affirmed that conviction in an unpublished opinion. Thereafter, and representing himself, he sought post-conviction relief through a petition under 28 U.S.C. Section 2255. That petition was dismissed without a hearing, and he filed this appeal from that denial. Mr. Hayward represented himself. *Hayward*, 619 F.2d at 717.

On appeal, he contended that an income tax on wages was illegal as a direct tax on the source of income. The Court of Appeals, citing *Brushaber* and *Francisco*, held the appeal to be frivolous because:

Congress clearly intended to tax income regardless of the Source.

Hayward, 619 F.2d at 717.

Mr. Hayward, in contending that an income tax on wages was illegal as a direct tax on the source of income, never contested the fact that Congress did clearly intend to tax income regardless of the source. But that does not automatically change gross receipts into gross income, as recognized by the Supreme Court in *Doyle* (see p.

128). The *Hayward* case cannot constitute legal precedent for the conclusion that “wages” are income because not only did the Court not address that issue, but it relied upon the flawed opinion rendered by the *Francisco* Court.

Broughton v. United States, 632 F.2d 707 (8th Cir. 1980):

Michael A. Broughton filed a lawsuit in Federal District Court seeking a refund of income taxes paid in 1976 and 1977. The basis of his claim for refund in the District Court was identical to the single issue he raised on appeal:

He is not a person required to pay taxes because the wages he received as compensation for services in 1976 and 1977 are not subject to tax, and taxing those wages would be unconstitutional as a direct tax that is not apportioned among the states.

Broughton, 632 F.2d at 707.

The District Court had granted the government’s motion to dismiss Mr. Broughton’s complaint such that no trial on the merits would take place, and Mr. Broughton filed an appeal to challenge the validity of the dismissal of his complaint. In upholding the District Court’s dismissal, the Court of Appeals, citing *Brushaber*, stated that the Sixteenth Amendment authorizes the imposition of an income tax without apportionment among the States. *Broughton*, *id.* As pointed out in detail above, *Brushaber* stated the income tax was an excise tax that did not require apportionment. However, *Eisner* stated the Sixteenth Amendment authorized the imposition of an income tax without apportionment among the States; the statement of the *Broughton* Court, although wrongly cited, is correct.

The Court then went on to say:

Income includes wages or compensation received for services performed, and taxpayer's contention is frivolous and totally devoid of merit.

Broughton, 632 F.2d at 707.

To support this conclusion, the Court cited to *Hayward* and to *Francisco*. As has been demonstrated above at pages 185 and 183 respectively, those cases do not constitute valid legal authority for the proposition that wages or compensation for services constitute income. Section 61(a)(1) of the Internal Revenue Code clearly includes the income [profit or gain] "derived from" compensation for services in "gross income," but equally as clearly, does not discuss wages or include compensation for services itself in gross income. Having relied entirely on unsupported case law as binding legal precedent, the *Broughton* opinion cannot constitute legal precedent.

United States v. Buras, 633 F.2d 1356 (9th Cir. 1980):

Mr. Buras was convicted on four counts of willful failure to file income tax returns under 26 U.S.C. Section 7203. For eight years preceding 1974, he filed income tax returns in which he listed his wages as income. During this period of time he also had income taxes withheld from his wages. After concluding that he was not obligated under the tax laws to report his wages as income, Mr. Buras did not file tax returns for the years 1974 through 1978, and filed withholding exemption certificates (Form W-4E) such that no taxes would be withheld from his wages. *Buras*, 633 F.2d at 1358.

Prior to trial, Mr. Buras filed a pretrial motion asking for a judicial hearing to determine whether wages were income. The motion was denied. Mr. Buras then stipulated that during the period in question he had earned wages in excess of the amount of gross income which would obligate an individual to file a return, and further stipulated that he did not file any returns. *Buras, id.*

The Court considered these stipulations to be an admission of proof that two out of the three elements of the offense of failure to file⁸⁴ were conceded:

Thus, the only disputed element under I.R.C. Section 7203 was whether Buras' failure to file was willful.

Buras, id.

On appeal Mr. Buras argued, among other things, that it was error for the Court to instruct the jury that wages constitute income. Representing himself, he argued that only gain or profit can constitute income. He also argued that the income tax was an excise tax, and as a wage earner, he was not engaged in any privileged activity, such as employment by a government agency, subject to an excise tax. Mr. Buras also argued that Treasury Regulation Section 1.61-2(a)(1), which includes wages within the definition of income, was invalid for being inconsistent with the constitutional definition of income. *Buras*, 633 F.2d at 1361. As stated by the Court:

According to Buras, income must be derived from some source. Wages cannot be taxed because the wage earner enjoys no gain from that source. Since the wage earner exchanges his labor and personal time for its equivalent in money, he derives no gain and therefore cannot be taxed.

Appellant's argument is refuted by one of the cases he cites. In *Stratton's Independence, Ltd. v. Howbert*, 231 U.S. 399, 415, 34 S.Ct. 136, 140, 58 L.Ed. 285 (1913), the Court did define income as gain derived from labor. The Court went on to explain, however, that "the earnings of the human brain and hand when unaided by capital" are commonly treated as income. *Id.*

Buras, 633 F.2d at 1361.

Stratton's Independence was fully briefed herein. As pointed out at page 95, the Supreme Court did not say that earnings from the human brain and hand when unaided by capital are commonly treated as income, but stated that such earnings are commonly dealt with in legislation as income. The only federal legislation treating such earnings as income was legislation for the taxation of the salary of persons employed by the United States government, the exact privilege mentioned by Mr. Buras.⁸⁵

The *Stratton's Independence* case was sent to the United States Supreme Court on three specific issues which had been certified to it, none of which involved the issue of whether wages constitute income (see p. 93), and thus the case cannot be cited as controlling for that principle.⁸⁶

The Court of Appeals also stated:

As for Buras' argument that he may not be taxed because he is a wage earner, the Sixteenth Amendment is broad enough to grant Congress the power to collect an income tax regardless of the source of the taxpayer's income.

Buras, 633 F.2d at 1361.

There is no quarrel with this legal position. Congress can tax income regardless of the source. Wages, however, are not income, so they are not reached by the Sixteenth Amendment. Having relied on a prior Supreme Court case to support its position, which case did not even address the issue, the Court of Appeal's decision in *Buras* lacks legal credibility.

United States v. Romero, 640 F.2d 1014 (9th Cir. 1981):

Mr. Romero, representing himself, was convicted on five counts of willful failure to file income tax returns. Among other issues on appeal, Mr. Romero alleged bias and error on the part of the trial

judge based upon the judge's comments and instructions concerning the legal meaning of the terms "income" and "person" in 26 U.S.C. Sections 61 and 7203. *Romero*, 640 F.2d at 1016. Neither the basis of Mr. Romero's argument nor the trial court's instructions are set forth in the Court of Appeal's opinion, thus legal analysis of the case is impossible and it has no precedential value. The Court of Appeals stated:

Romero's proclaimed belief that he was not a "person" and that the wages he earned as a carpenter were not "income" is fatuous as well as obviously incorrect.

Romero, 640 F.2d at 1016.

To support this contention, the Court of Appeals cited to *Lucas v. Earl*, 281 U.S. at 114-115, and to *Roberts v. C.I.R.*, 176 F.2d 221, 225 (9th Cir. 1949). The *Lucas* case was analyzed previously, and as set forth at page 149, the issue of whether wages constitute income was not litigated in that case. In *Roberts*, the question before the Court was whether tips received by a taxicab driver constituted income. In deciding that tips did constitute income, the Court first went to the definition of income contained in Section 22 of the Internal Revenue Code of 1939, and found that Congress included in gross income gains, profits, and income derived from salaries, wages or compensation for personal service. The Court next went to Treasury Regulation 111 which included tips within the term "compensation for services." The Court, ignoring the use of the words "derived from,"⁸⁷ determined tips, being compensation for services, were income:

The essential question for determination is whether tips are income. The Regulation just cited declares them such.

Roberts, 176 F.2d at 223.

The Regulation does nothing more than include tips within the term “compensation for services.” According to the Supreme Court and the intent of Congress, there is no income unless there is a profit or gain derived from those tips. Whether or not Mr. Roberts profited from his tips was not litigated, however, because he argued that tips were a gift that fell without the income tax provisions of the law. The *Roberts* case also stated on page 225 that “[a]ny monies which come to the taxpayer as the fruits of his labor are ‘income.’” It must be pointed out that no case authority is cited for this conclusion.

The *Romero* Court next went on to say that:

Compensation for labor or services, paid in the form of wages or salary, has been universally held by the courts of this republic to be income, subject to the income tax laws currently applicable.

Romero, 640 F.2d at 1016.

This gratuitous statement on the part of the Ninth Circuit ignores the fact that the issue has never been directly ruled upon by the Supreme Court. As pointed out herein, those lower courts that have ruled on the matter have ignored the express language of the applicable statutes and/or the intent of Congress, or have cited to cases for propositions that are not supported by an analysis of those cases. Certainly the *Romero* case does not even attempt to give a legal analysis of the issue, but merely cites to other cases. As shown, those cases do not stand for the proposition that wages constitute income.

Amon v. United States, 514 F.Supp. 1293 (D.C. Col., 1981):

Mr. Amon paid federal personal income tax for the years 1977, 1978 and 1979, and then sought to recover those taxes. As grounds for the recovery, Mr. Amon, representing himself, raised the following three legal arguments: (1) that the compensation for services which

constituted his wages could not be subject to income taxation by the Internal Revenue Service because wages only represented an even exchange for labor, and consequently there was no gain or profit which was taxable income, (2) that with regard to the first assertion, the Sixteenth Amendment of the Constitution of the United States was not intended as a direct tax on compensation for labor, and therefore, the Internal Revenue Service collected taxes in contravention of the Constitution of the United States and (3) that the taxes he paid were, in reality, illegally imposed excise taxes because he did not occupy a status which would ordinarily incur tax liability. According to the Court's opinion, Mr. Amon equated an excise tax with an income tax. *Amon*, 514 F.Supp. at 1294.

The government argued that (1) the Internal Revenue Service had the constitutional and statutory power to tax Mr. Amon's gross income which was derived from compensation for services and (2) that Mr. Amon was properly taxed. *Amon*, *id.*

The Court pointed out that the government's brief addressed "the issue of whether Amon's income, as derived from compensation for services, and constituting wages, was properly taxable as income tax," while Mr. Amon addressed "only the issue of whether he was the proper subject for the imposition of an excise tax, which he asserted the government was collecting from his income derived from his wages." *Amon*, *id.*

In addressing Mr. Amon's contention that his compensation for services was only an even exchange for his labor which did not constitute a gain or profit from his labor,⁸⁸ the Court first quoted from *United States v. Safety Car Heating & Lighting Co.*, 297 U.S. 88, 99 (1936), as follows:

Income within the meaning of the Sixteenth Amendment is the fruit that is born of capital, not the potency of fruition. With few exceptions, if any, it is income as the word is known in the common speech

of men •*. * * when it is that, it may be taxed, though it was in the making long before.

Amon, 514 F.Supp. at 1295.

This is a correct statement of the law to the extent it addresses capital. In the *Safety Car* case, the issue was the taxability of the “profit” derived from a patent:

There is no denial that profits owing to a patentee by the infringer of a patent are income within the meaning of the statute, unless withdrawn from that category by the date of the infringement.

Safety Car, 297 U.S. at 93.

The case nowhere indicates that wages constitute a profit derived from labor.

The Court next cited to *Glenshaw Glass*, indicating that exemplary damages for fraud fell within the definition of Section 22, the predecessor to the present day Section 61 of 26 U.S.C. As already analyzed, exemplary damages constitute a profit or gain, and hence are to be included within gross income. Again, however, there is no reference to wages constituting a profit or gain in the *Glenshaw Glass* case. The Court then cited to *Helvering v. Clifford*, 309 U.S. 331 (1940), for the proposition that Congress has the power to impose an income tax on gross income. That is a true statement of the law. The *Clifford* case, however, involved the situation of a husband who declared himself trustee of certain securities he owned, the net income therefrom to be held for the exclusive benefit of the wife. The income was distributed to the wife, but the I.R.S., contending that the income was taxable to the husband, issued a deficiency notice. The issue before the Supreme Court was:

[W]hether the grantor after the trust has been established may still be treated, under this statutory

scheme [referencing Section 22 defining gross income], as the owner of the corpus.

Clifford, 309 U.S. at 334.

Again, no mention whatsoever that wages constitute income.

The Court went on to cite *C.I.R. v. Jacobson*, 336 U.S. 28 (1949), stating that in that case, the Supreme Court reiterated the purpose of the income tax laws as follows:

The income taxed is described in sweeping terms and should be broadly construed in accordance with an obvious purpose to tax income comprehensively.

Amon, 514 F.Supp. at 1295.

Once again, the Supreme Court correctly states the law, and once again the *Amon* Court cited to a case that has nothing whatsoever to do with whether or not wages constitute income. According to the Supreme Court:

This decision applies the federal income tax to gains derived by a debtor from his purchase of his own obligations at a discount and his consequent control over their discharge. It presents the specific question whether a solvent natural person, in straitened financial circumstances, must include in his gross income for federal income tax purposes the difference between (1) the face amount of his personal indebtedness as the maker of secured bonds, originally issued by him at face value for cash, and (2) a lesser amount paid by him for their purchase.

Jacobson, 336 U.S. at 29-30.

The issue of whether or not wages constitute income was clearly not addressed in the *Jacobson* case.

The Court then cited to *United States v. Swallow*, 511 F.2d 514 (10th Cir. 1975), as follows:

[T]he Tenth Circuit Court of Appeals commented on the comprehensive nature of taxation on compensation for services stating “[w]hen earnings are acquired, lawfully or unlawfully, without consensual recognition of an obligation to repay or restriction on their disposition, there is income.”

Amon, 514 F.Supp. at 1295.

A review of the *Swallow* case, however, shows that the Tenth Circuit was not speaking about compensation for services, but was speaking about loans:

The principal government theory of a substantial tax deficiency argued to the jury was that the loans were not good faith loans to Swallow, and that there was no effort, nor any evidence to indicate any intent by Swallow, to repay the loans. The trial court instructed on this theory. When earnings are acquired, lawfully or unlawfully, without consensual recognition of an obligation to repay or restriction on their disposition, there is income. *James v. United States*, 366 U.S. 213, 219-220, 81 S.Ct. 1052, 6 L.Ed.2d 246. And this principle applies to loans obtained in bad faith and without an intent to repay them, as well as to money illegally obtained by embezzlement as in the *James* case.

Swallow, 511 F.2d at 519.

The *Swallow* case nowhere discusses compensation for services and certainly did not involve the issue of wages.

That the Court was ignorant of federal tax law is clear from the following quote:

The current statutory guidelines for income tax assessment are Sections 61 and 63 of the Internal Revenue Code.

Amon, 514 F.Supp. at 1296.

Section 61 of the Internal Revenue Code, found in Subtitle A, merely defines “gross income,” and Section 63 defines “taxable income.” The statutory guidelines regarding income tax assessments are found in Subtitle F at Sections 6201, 6203 and 6303.

At page 1296 the Court then quoted from Section 61, and ignoring the words—income derived from—erroneously equated compensation for services with income. To support this erroneous equation, the Court cited to *Robertson v. United States*, 343 U.S. 711, 713-714 (1952). The *Robertson* case, however, involved the issue of whether a cash prize received by the winner of a contest in musical composition constituted gross income under Section 22 of the Internal Revenue Code. Once again, the Court cited to a case in which there was no mention whatsoever regarding wages constituting income.

The Court next cited to *C.I.R. v. Smith*, 324 U.S. 177 (1945), contending that the Supreme Court held that property which was transferred to an employee was compensation for services even though the transfer took the form of an exchange. In the *Smith* case, Mr. Smith’s employer gave to him, as compensation for his services, an option to purchase from the employer certain shares of stock of another corporation at a price not less than the then current market value of the stock. Two tax years later, when the market value of the stock was greater than the option price, Mr. Smith exercised the option. The question before the Supreme Court for decision was whether the difference between the market value and the option

price of the stock was compensation for personal services of the employee, taxable as income in the years when he received the stock, under Section 22(a) of the Internal Revenue Code. *Smith*, 324 U.S. at 177-178.

The Supreme Court found factually that the stock option was “in consideration of services rendered,” and that the stock option had no value at the time it was given to Mr. Smith. The Court thus concluded that at the time of the exercise of the option, the difference between the market value and the option price of the stock, which was zero, constituted profit that was derived from the compensation for services. This reasoning was in full accord with the applicable statute and regulations; and after quoting them, the Supreme Court was led to say:

Section 22(a) of the Revenue Act is broad enough to include in taxable income any economic or financial benefit conferred on the employee as compensation, whatever the form or mode by which it is effected. See *Old Colony Trust Co. v. Commissioner*, 279 U.S. 716, 729. The regulation specifically includes in income, property “transferred ... by an employer to an employee, for an amount substantially less than its fair market value,” even though the transfer takes the form of a sale or exchange, to the extent that the employee receives compensation.

Smith, 324 U.S. at 181.

If applied to wages, however, the analysis of the Supreme Court in *Smith* would not result in taxable income because the property transferred by the employer to the employee would be equal to the fair market value of the employee’s labor, not substantially less than the fair market value as the stock was under the facts of the *Smith* case. This is borne out by the last paragraph of the *Smith* decision:

The Tax Court thus found that the option was given to respondent as compensation for services, and implicitly that the compensation referred to was the excess in value of the shares of stock over the option price whenever the option was exercised. From these facts it concluded that the compensation was taxable as such by the provisions of the applicable Revenue Acts and regulations. We find no basis for disturbing its findings, and we conclude it correctly applied the law to the facts found.

Smith, 324 U.S. at 182.

The Supreme Court, as well as the Tax Court, recognized there was an **excess** over the basis of the stock, and that this excess constituted a **profit** (income) derived from compensation for services. As a profit, “the compensation was taxable as such by the provisions of the applicable Revenue Acts and regulations.” It logically and legally follows that compensation for services that does not constitute income (a profit or gain) is not taxable under the provisions of the applicable Revenue Acts and regulations. Thus the *Smith* case, cited by the *Amon* Court for the proposition that wages constitute income, actually supported the opposite proposition, that wages do not constitute income unless the employee receives an amount over and above the fair market value of his labor.

The *Amon* Court next cited to *Wilson*, 412 F.2d at 695, for the proposition that “all remuneration received for services is gross income unless it falls within a specific exclusion.” The *Wilson* case, as shown above at page 170, involved the interpretation of the terms “business premises” and “in kind” with regard to the question of the alleged non-taxability under Section 119 of the 1954 Internal Revenue Code, as income, of the reimbursement by the state employer to a state police officer while on duty, of the cost of a meal in a restaurant.

Mr. Wilson never contended the reimbursement was not income, he merely contended the amount received was specifically excludable from gross income by statute.

The Court also cited to *Neville v. Brodrick*, 235 F.2d 263 (10th Cir. 1956), contending that “the Tenth Circuit recognized that compensation for services rendered or to be rendered is taxable.” *Amon*, 514 F.Supp. at 1296. In *Neville*, the two issues before the Court were: 1) whether stock given to an employee and his family represented gifts or additional compensation for services rendered; and 2) what was the fair market value of the stock. After discussion of Section 22(a) defining “gross income” as including “gains, profits, and income derived from ... compensation for personal service” and Section 22(b)(3) exempting from taxation the value of property received as a gift, the Court said:

While sometimes difficult of application, the statute draws a clear distinction between compensation for services rendered or to be rendered and gifts, the former being taxable and the latter exempt.⁸⁹

Neville, 235 F.2d at 265.

After citing these non-supporting cases, the *Amon* Court concluded that:

Notwithstanding the fact that Amon asserts he did not receive any gain from his labor, and that the compensation for services was only a mere exchange, in view of the above authorities, his position is untenable. Compensation for services is taxable income and the government properly taxed Amon’s income for the years in question.

Amon, 514 F.Supp. at 1296.

In view of the above authorities, it is clear that a profit or gain derived from compensation for services is taxable income, but that the government improperly taxed Mr. Amon's gross receipts as opposed to his taxable income.

Lonsdale v. C.I.R., 661 F.2d 71 (5th Cir. 1981):

Mr. Lonsdale, representing himself, appealed from an adverse determination of the United States Tax Court. In its written opinion, the Court of Appeals openly admitted that the arguments of Mr. Lonsdale were extremely broad, consisted of interwoven legal and theological arguments, and that the Court's decision was not based upon any consideration of the underlying facts. *Lonsdale*, 661 F.2d at 72.

The Court believed the argument of Mr. Lonsdale to be that the United States Constitution forbids taxation of compensation received for personal services because: 1) the exchange of services for money is a zero-sum transaction, the value of the wages being exactly that of the labor exchanged for them and hence containing no element of profit; and 2) that under *Pollock v. Farmers Loan & Trust*, 157 U.S. 429 (1895), the income tax is a direct tax that must be apportioned among the several states. *Lonsdale*, 661 F.2d at 72.

As to the first of Mr. Lonsdale's arguments, the Court stated:

The Constitution grants Congress power to tax "incomes, from whatever source derived" U.S. Const, amend. XVI. Exercising this power, Congress has defined income as including compensation for services. 26 U.S.C. Section 61(a)(1). Broadly speaking, that definition covers all "accessions to wealth." See *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 431 (1955). This definition is clearly within the power to tax "incomes" granted by the sixteenth amendment.

Lonsdale, 661 F.2d at 72.

The fallacy of the Court's reasoning is immediately apparent in that at Section 61(a)(1) Congress did not define "income," but merely defined "gross income." Congress clearly defined "gross income" as including "income derived from compensation for services," but that is not the same thing as defining "income." The *Lonsdale* Court actually ignored the legislative history accompanying the passage of Section 61 of the 1954 Internal Revenue Code which specifically states:

Section 61 (a) provides that gross income includes "all income from whatever source derived." This definition is based upon the 16th Amendment and the word "income" is used in its constitutional sense.

House Report No. 1337; Senate Report No. 1622; *U.S. Code Cong. and Admin. News*, 83rd Congress, 2nd Session, pages 4155 and 4802 respectively, 1954.

The United States Supreme Court has provided us with the constitutional definition of income based upon the Sixteenth Amendment:

Income may be defined as the gain derived from capital, from labor or from both combined, provided it include profit gained through a sale or conversion of capital assets.

Stratton's Indep. v. Howbert, 231 U.S. 399 (1913); *Doyle v. Mitchell*, 247 U.S. 179 (1920); *So. Pacific v. Lowe*, 247 U.S. 330 (1918); *Eisner v. Macomber*, 252 U.S. 189 (1920); *Merchant's Loan v. Smietanka*, 255 U.S. 509 (1921).

The Congressional legislative history, together with the Supreme Court cases defining "income" and the analysis by the Supreme

Court in the *Glenshaw Glass* case, all show that the Court in *Lonsdale* was in error for not looking to the facts to ascertain if Mr. Lonsdale had a profit derived from his compensation for services.

The *Lonsdale* Court responded to Mr. Lonsdale's second argument by correctly stating that the Sixteenth Amendment did remove the requirement of apportionment from the direct income tax. *Lonsdale, id.* Thus if the "income" derived from "compensation for services" is taxed, the tax need not be apportioned. However, if the tax is applied directly to "compensation for services," it must still be apportioned pursuant to Article I, Section 2, Clause 3, and Article I, Section 9, Clause 4, of the United States Constitution. The failure of the Court to distinguish between "income derived from compensation for services" and "compensation for services" renders the Court's opinion unreliable as precedent for the proposition that wages constitute income.

Rice, T.C. Memo 1982-129, para. 82,129 P-H Memo TC (1982):

Mr. Rice, representing himself in Tax Court, argued that Congress intended to tax wages as compensation for services in Section 61(a)(1) of the Internal Revenue Code, but claimed that the statute was an unconstitutional attempt to tax, without apportionment, something which was not income within the meaning of the Sixteenth Amendment. He argued that wages were not income because they were not "gain derived from capital, from labor, or from both combined." Instead, Mr. Rice contended that wages arose from an equal exchange of labor or services for property, a transaction in which no gain was derived. *Rice, id.*

The Tax Court first stated:

The Supreme Court early established the principle that the word "income," as it is used in the Sixteenth Amendment, is to be construed according to its common, everyday meaning. In *Lynch v. Hornby*, 247

U.S. 339, 344 (1918), the Court stated, “* * * Congress was at liberty under the [Sixteenth] Amendment to tax as income, without apportionment, everything that became income, in the ordinary sense of the word * * *.” Under this principle, the ordinary, and perhaps most common, meaning of “income” has been wages. Thus, when a coal company argued before the Supreme Court that the proceeds from its sale of ore, which it had dug from its properties, were the return of depleted capital, not income, the Court dismissed the argument, observing “the same is true of the earnings of the human brain and hand when unaided by capital, yet such earnings are commonly dealt with in legislation as income.” *Stratton’s Independence v. Howbert*, *supra* note 6, at 415. This quote illustrates that whether or not wages can be characterized as the product of an exchange, they are still income within the Constitutional embrace.

Rice, id.

In *Lynch v. Hornby*, the specific issue before the Court was whether that portion of a stock dividend representing the conversion of property into money constituted net income under the Income Tax Act of 1913. *Lynch v. Hornby*, 247 U.S. at 341-342. The case did not involve wages. With respect to the quote that “Congress was at liberty under the Sixteenth Amendment to tax as income, without apportionment, everything that became income, in the ordinary sense of the word,” it was shown at page 144 in the *Smietanka* case that the term “income” pertained to what was in the minds of the people at the time of their ratification of the Sixteenth Amendment. (See also the legislative history regarding the enactment of Section 61 of the Internal Revenue Code of 1954 at page 84.) The Supreme Court has held that the term income was meant to be a profit or gain derived from labor, not the equal amount received in exchange for labor.

The quote attributed to the Supreme Court in *Stratton's Independence* has been shown at page 95 not to have been made with respect to any then existing income tax legislation. In addition, none of the three issues before the Court in *Stratton's Independence* involved wages, and the statement of the Court was *dicta*. It was also shown in the *Stratton's Independence* analysis that the Court recognized the principle of gain by stating that the wasting of capital assets had to somehow figure into the computation of income in order to arrive at the gain derived from the mining process and the sale of the ore (see p. 96).

The *Rice* Court next stated:

Mr. Rice misconstrues the oft-cited phrase that income is "gain derived from capital, from labor, or from both combined" to mean that wages are not income. Wages are "derived" from labor or services in the sense that they cannot be gained without such labor. Although the wages received by Mr. Rice may represent no more than the time-value of his work, they are nonetheless the fruit of his labor, and therefore represent gain derived from labor which may be taxed as income.

Rice, id.

Here the Court recognized the concept of basis; *i.e.*, that the wages Mr. Rice received might represent no more than the value of his labor. The Court then stated:

Even if we were to agree with Mr. Rice's contention that wages are, in effect, an exchange of equal value for value, he would still be taxable upon the wages he and Mrs. Rice received in 1978. The general doctrine that receipts representing a return of capital are not taxed does not apply when a taxpayer has a zero basis in the property he exchanged for the receipts. See

Wilson v. Commissioner, 27 T.C. 976 (1957), *affd. per curiam* 255 F.2d 702 [1 AFTR2d 1851] (5th Cir. 1958); *Bryan v. Commissioner*, 16 T.C. 972 (1951); *Rains v. Commissioner*, 38 B.T.A. 1189 (1938). Mr. Rice did not establish that he had a basis in the services he rendered to Matanuska, nor did he establish that Mrs. Rice had a basis in the services she rendered to Alaska Teamsters. Thus, each had taxable gain upon receipt of wages from their respective companies. Section 1001.

Rice, id.

In *Wilson v. Commissioner*, the issue before the Court was whether the cancellation of a debt should be considered a long-term capital gain or ordinary dividend income. Whether wages constitute income, or the value of one's labor established by the employment contract constitutes the basis of that labor, was not an issue before the Court.

In the *Bryan* case, the Court stated the issue before it as follows:

The issue to be decided is whether certain shares of stock, which were sold by the petitioner in 1944, were a gift to petitioner or whether they had been received by him for adequate consideration. If they were not a gift, a further issue is presented with respect to the basis of the stock for computing gain or loss thereon.

Bryan, 16 T.C. at 972.

This case also did not address the issue as to the basis of one's labor, but clearly recognized the concept that determination of basis is an essential part of the computation of gain.

In the *Rains* case the Court stated the issue before it as follows:

The issues are, first, whether respondent erred in determining that an option granted to petitioner's husband in 1929, to purchase stock of the Columbia Steel Corporation, was community property of petitioner and her husband, and in including in her gross income for the taxable year one-half of the income realized in respect of the option; and, second, whether petitioner realized gain or loss in the exchange, in the taxable year, of certain of her separate property for an interest in the option.

Rains, 38 B.T.A. at 1190.

As in *Wilson* and *Bryan*, this case did not involve the issue as to the basis of one's labor.

In ruling adversely to Mr. Rice, the Tax Court relied upon case law that did not address the specific issues before it, and failed to acknowledge the Supreme Court's holding that labor and the employment contract to sell one's labor constitutes personal property. The Court specifically recognized the issue raised by the Rices that the wages they received were in direct exchange for the time-value of their labor, but then chose, contrary to law, not to recognize the fair market value of the labor as the basis of that labor. Having ignored the law directly on point, the *Rice* case is erroneous, and cannot constitute legal authority for the proposition that wages constitute income.

United States v. Lawson, 670 F.2d 923 (10th Cir. 1982):

Mr. Lawson appealed his convictions for failing to file federal income tax returns and for supplying a false and fraudulent withholding certificate to his employer. One of the grounds raised on appeal was whether the trial court committed error in denying a pretrial motion to dismiss the case because his wages were not income within the meaning of the Internal Revenue Code and the Constitution. *Lawson*, 670 F.2d at 925.

With respect to the contention that Mr. Lawson's wages were not income within the meaning of the Internal Revenue Code, the Court cited Section 61(a)(1) as follows:

“[G]ross income means all income from whatever source derived, including (but not limited to) the following items: (1) Compensation for services, including fees, commissions, and similar items “

Lawson, id.

The Court then stated:

We must broadly interpret the definition to include all gains not specifically exempted. *Commissioner v. Kowalski*, 434 U.S. 77, 82-3 (1977).

Lawson, 670 F.2d at 925.

Thus, while recognizing that the definition of gross income applies to “gains,” including gains derived from compensation for services, it failed to apply the law as stated to the case before it:

Notwithstanding Lawson's belief that his wages are not gains or profits but merely what he has received in an equal exchange for his services, the Internal Revenue Code clearly included compensation of this nature within reportable gross income.

Lawson, id.

The Court failed to cite any case authority for this statement.

With respect to the contention that Mr. Lawson's wages were not income within the meaning of the Constitution, the Court did not set forth Mr. Lawson's contentions in the opinion, and disposed of the issue by stating:

Lawson's constitutional argument is specious. See *United States v. Russell*, 585 F.2d 368, 370 (8th Cir. 1978); *Kasey v. Commissioner*, 457 F.2d 369, 370 (9th Cir. 1972), *cert. denied*, 409 U.S. 869 (1972); *Porth v. Brodrick*, 214 F.2d 925, 926 (10th Cir. 1954).

Lawson, 670 F.2d at 925.

The *Russell* case has been previously analyzed herein at page 179. The *Kasey* case was an appeal from a decision of the Tax Court which upheld the Commissioner's denial of certain deductions claimed by the Kaseys for various litigation-related expenses. *Kasey*, 457 F.2d at 370. The case did not involve the issue of whether wages constitute income. The constitutional argument raised by the Kaseys as to the constitutional validity of the tax was dealt with by the Court in one sentence:

In arguing that the only proper tax would be something like a sales tax, the taxpayers seem to have overlooked the Sixteenth Amendment to the Constitution, which gives Congress "power to lay and collect taxes on incomes."

Kasey, 457 F.2d at 370.

The *Porth* case was an action brought by Mr. Porth to recover the sum of \$135 which he alleged was erroneously and illegally paid on his declaration of estimated income tax for the year 1951. The trial court dismissed the action upon the government's motion on the grounds that Porth's petition failed to state a claim upon which relief could be granted, and thereafter, Mr. Porth appealed. *Porth*, 214 F.2d at 925.

Mr. Porth raised two contentions: first, that the Sixteenth Amendment was unconstitutional because the taxpayer was placed in a position of involuntary servitude contrary to the Thirteenth Amendment; and second, that the Federal Tax legislation enacted

after the ratification of the Sixteenth Amendment had given rise to such a mass of ambiguous, contradictory, inequitable and unjust rules, regulations and methods of procedure, that he was compelled to assume unreasonable duties, obligations and burdens in order to make a just accounting of his income and pay the tax thereon. In disposing of the case, the Court stated:

The allegations of the petition are very broad and it is difficult, if not impossible, to determine therefrom just what the complaint is except that there exists a strong dislike for the taxing procedure. Apparently the taxpayer, while recognizing the taxing power of the United States, attacks both the legality of the Sixteenth Amendment and the constitutionality of the Federal tax laws, rules and regulations enacted pursuant thereto. It is admitted that a federal income tax may be levied under the Sixteenth Amendment and no law, rule or regulation is referred to which impinges upon or destroys any right guaranteed the taxpayer by the Constitution. The claim is clearly unsubstantial and without merit.

Porth, 214 F.2d at 926.

The *Kasey* and *Porth* cases cited by the Lawson Court in response to Mr. Lawson's unspecified challenge to the constitutionality of a tax upon his wages do not address the issue of whether or not wages constitute income. The *Russell* case cannot stand for the proposition that wages constitute income for the reasons previously set forth.

Funk v. Commissioner, 687 F.2d 264 (8th Cir. 1982):

Mr. Funk, representing himself, appealed from a decision entered by the United States Tax Court and argued, among other things, that the wages received by him in 1976 and 1977 were not subject to

federal income tax. Mr. Funk argued that compensation for labor was not constitutionally subject to the federal income tax, that an individual's labor was capital in which he possessed a property right, that an individual had the right to exchange that property for other property, *i.e.*, money, and that such a transaction was an equal exchange which did not give rise to any profit. *Funk*, 687 F.2d at 265.

The *Funk* Court stated it rejected Mr. Funk's Sixteenth Amendment claim because the constitutionality of the Sixteenth Amendment had been upheld by the Supreme Court in *Brushaber*, and also cited to *Eisner v. Macomber*. *Funk*, 687 F.2d at 265.

The Court then stated that there was no constitutional impediment to levying an income tax on compensation for a taxpayer's labors, and cited to two Tax Court decisions as authority for its statement: *Hanson v. Commissioner*, para. 80,197 T.C.M. (P-H) at 900 (1980)⁹⁰ and *Brooks v. Commissioner*, para. 80,206 T.C.M. (P-H) at 940 (1980).⁹¹

In Tax Court, Mr. Hanson, who was representing himself, argued that wages derived from a God-given, inalienable right to work were not constitutionally subject to the federal income tax, that a wage, salary, fee, first-time commission, or compensation for any kind of labor was not a gain, and that a tax on compensation for labor was a direct tax required to be apportioned under the Constitution. He also argued that wages and other compensation for labor were not a gain from capital or labor, because the gain from labor contemplated by the Supreme Court referred to gain derived by labor contractors who contracted to provide the services of employees. *Hanson*, at 900.

The Tax Court stated in its opinion that Mr. Hanson's arguments were without merit, because soon after the promulgation of the Sixteenth Amendment to the Constitution, numerous challenges to the income tax laws were raised on constitutional grounds. Citing to *Brushaber* and to *Tyee Realty Co. v. Anderson*, 240 U.S. 115 (1916),

the Tax Court stated that in the face of these challenges, the Supreme Court upheld the income tax law enacted in 1913, which law levied taxes on salaries and wages received by individuals as well as on other income items of both corporations and individuals. *Hanson*, at 900.

Neither of the cases cited by the Tax Court, however, involved a challenge to the constitutionality of a tax on wages, so that issue was not decided by the Supreme Court.⁹² Mr. Brushaber, as a stockholder of the Union Pacific Railroad Company, sought to enjoin the corporation from complying with the Income Tax provisions of the 1913 tax act pertaining to corporations. *Brushaber*, 240 U.S. at 9. The *Tyee Realty* case involved two cases, the *Tyee Realty* case involving a corporation and the *Thome v. Anderson* case involving an individual. *Tyee Realty* was decided less than a month after *Brushaber*; and the decision was written by Justice White, the author of the *Brushaber* decision, who stated:

Every contention relied upon for reversal in the two cases is embraced within the following propositions: (a) that the tax imposed by the statute was not sanctioned by the Sixteenth Amendment because the statute exceeded the exceptional and limited power of direct income taxation for the first time conferred upon Congress by that Amendment and, being outside of the Amendment and governed solely therefore by the general taxing authority conferred upon Congress by the Constitution, the tax was void as an attempt to levy a direct tax without apportionment under the rule established by *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429; 158 U.S. 601. (b) That the statute is moreover repugnant to the Constitution because of the provision therein contained for its retroactive operation for a designated time and because of the illegal discriminations and inequalities which it creates, including the provision for a progressive tax on the income of individuals⁹³ and the method

provided in the statute for computing the taxable income of corporations.

But we need not now enter into an original consideration of the merits of these contentions because each and all of them were considered and adversely disposed of in *Brushaber v. Union Pacific R.R.*, ante, p.1. That case, therefore, is here absolutely controlling and decisive. It follows that for the reasons stated in the opinion in the *Brushaber* case the judgments in these cases must be and they are affirmed.

Tyee Realty, 240 U.S. at 117-118.

While both cases stand for the proposition that the Sixteenth Amendment is constitutional and that as a result of the amendment a tax levied on an individual's income need not be apportioned, neither *Brushaber* nor *Tyee Realty* addressed the issue as to whether wages constitute income. It must be remembered here that the statute defining gross income does not itself violate the Constitution. The interpretation of that statute by the lower courts to the extent the interpretation allows the I.R.S. to collect a tax on something other than "income" is what violates the Constitution. All of the Supreme Court cases that have defined what is meant by the word "income" have correctly stated that it must be a profit or a gain derived from labor.

The *Hanson* Court then cited to *Autenrieth v. Cullen*, 418 F.2d 586 (9th Cir. 1969). In *Autenrieth*, one hundred and twenty-four plaintiffs sought refunds of a percentage of the federal income taxes paid by each of them on the grounds that the Viet Nam War was illegal, each was a conscientious objector to the war, and each had a First Amendment religious right not to pay for the war, claiming a constitutional exemption from paying the percentage of the tax necessary to finance the war. The lower court dismissed the complaints on the grounds that they did not state a valid claim for

relief. *Autenrieth*, 418 F.2d at 587-588. On appeal, the Ninth Circuit stated:

[W]e hold that nothing in the Constitution prohibits the Congress from levying a tax upon all persons, regardless of religion, for support of the general government. The fact that some persons may object, on religious grounds, to some of the things that the government does is not a basis upon which they can claim a constitutional right not to pay a part of the tax.

Autenrieth, 418 F.2d at 588.

Notwithstanding the fact that the issue as to whether wages constitute income was not a part of the *Autenrieth* case, the *Hanson* Court said:

It is clear from the facts in *Autenrieth v. Cullen, supra*, that the income being taxed was the salaries and wages of the taxpayers in that case. We therefore hold that there is no constitutional impediment against levying an income tax on compensation for petitioner's labor.

Hanson, at 900.

One can only presume that the author of the *Hanson* opinion, Administrative Law Judge Fay, chose to ignore the legal principle of *stare decisis* and the holdings of the Supreme Court in *Cohens v. Virginia*, 6 Wheat 264, 399 (1821); *Carroll v. Lessee*, 16 How. 275, 287 (1853); *Louisville R.R. Co. v. Letson*, 2 How 497 (1844); *Ex Parte Christy*, 3 How. 292 (1845); and *Woodruff v. Parham*, 8 Wall 123 (1868). These cases make it clear that the doctrine of *stare decisis* is a salutary one and to be adhered to on all proper occasions, but it only arises in respect of decisions directly upon the point in issue. In that the *Autenrieth* case did not directly involve

the issue of whether wages constitute income, the *Autenrieth* case cannot, legally, stand for the proposition asserted by Judge Fay.

The *Hanson* Court then set forth the definition of “gross income” contained in Section 61 (a) and said:

This broad definition of income has been uniformly held by the courts to include amounts received by an individual for personal services. Contrary to petitioner’s contention, payment for personal services has in a number of cases been referred to as “gain.”

Hanson, at 900.

The Court, however, failed to cite to any of those alleged cases.

The *Hanson* Court then stated that Mr. Hanson’s second contention was that a tax on wages was a direct tax and could not be levied without apportionment. *Hanson, id.* The Court’s treatment of this contention was based upon its unsupported analysis of Mr. Hanson’s first contention, and the Court failed to address the precise issue raised by Mr. Hanson:

However, even without considering whether the tax is a direct tax, petitioner’s argument must fail with our determination that “income” subject to tax does include petitioner’s wages. It is clear under the terms of the 16th Amendment that no apportionment of the tax is required.

Hanson, at 900-901.

Mr. Brooks also represented himself in Tax Court. He filed Forms 1040 which contained only his name, address, the amount of federal income tax withheld by his employers, and his signature. To the remainder of the information asked for on the forms, he claimed Fifth Amendment protection. In Tax Court, Mr. Brooks

argued that property is not federally taxable; an individual's labor is personal property; an individual has the right to exchange his property (*i.e.*, labor) for other property (money); and concluded that his wages could not constitutionally be taxable since he received money in exchange for something of equal value, *i.e.*, his labor— "property." Mr. Brooks called his argument "The Basis Theory." *Brooks*, at 940.

The Tax Court, citing to *Brushaber* and *Tyee Realty*, stated:

It cannot be doubted after all these years since the ratification of the Sixteenth Amendment that any receipt of wages in exchange for services rendered is taxable income.

Brooks, at 940.

The Tax Court next quoted the correct definition of income from *Eisner*, and then, citing to *Glenshaw Glass* stated:

There is also no doubt that sec. 61 encompasses all realized accessions to wealth. We reject as frivolous the argument that sec. 61(a)(1) does not withstand constitutional scrutiny.

Brooks, *id.*

The *Glenshaw Glass* case, it should be remembered (see p. 159), involved the issue of whether punitive damages constituted an element of "gross income." These damages, which are over and above the amount of damages necessary to replace that which was lost, were truly an "accession to wealth." Wages, on the other hand, are payments for the selling of one's labor which the Supreme Court has held is property.⁹⁴ One only realizes an accession to wealth upon the sale of property if one receives in excess of the fair market value of that property. 26 U.S.C. Sections 64 and 1001 *et seq.*

In ruling adversely to Mr. Brooks, the Tax Court misapplied *Glenshaw Glass*, and ignored three rulings of the United States Supreme Court and several provisions of the Internal Revenue Code.

The *Funk* Court next stated that Mr. Funk's argument that wages received for services were not taxable as income was frivolous, citing to *Broughton*, *Hayward* and *Francisco*. As analyzed herein at pages 186, 185 and 183 respectively, none of those cases are valid legal precedent for the proposition that wages constitute income.

Jones v. United States, 551 F.Supp. 578 (N.D.N.Y. 1982):

Mr. and Mrs. Jones, representing themselves, commenced an action to recover income taxes that they had paid for the years 1977 through 1980. The government moved to dismiss the action on the grounds that it failed to state a valid claim. The Joneses argued that compensation for services or wages was not income within the meaning of the Internal Revenue Code because: 1) wages had not specifically been designated as income in the Internal Revenue Code; and 2) the taxation of wages violated the prohibition against direct taxation without apportionment among the several States. *Jones*, 551 F.Supp. at 579.

In dismissing the case, the trial court cited to *Glenshaw Glass*; *Russell*; *Silkman*; *Lawson*; *Buras*; *Broughton*; *United States v. Moore*, 627 F.2d 830 (7th Cir, 1980); *Francisco*; *United States v. Edelson*, 604 F.2d 232 (3rd Cir. 1979); *United States v. Daly*, 481 F.2d 28 (8th Cir. 1973); and *United States v. Porth*, 426 F.2d 519 (10th Cir. 1970) as its authority enabling it to dispose of the Jones' claim that wages do not constitute income. *Glenshaw Glass* (see p. 159), *Russell* (see p. 179), *Silkman* (see p. 173), *Lawson* (see p. 206), *Buras* (see p. 187), *Broughton* (see p. 186) and *Francisco* (see p. 183) have been analyzed hereinabove and shown to be legally insufficient to sustain the proposition that wages do constitute income.

The issues raised in *Daly* were: 1) whether Defendant's filing of returns containing no information relating to income or expenses was sufficient to comply with the Section 7203 requirement that he "make a return"; 2) whether the Fifth Amendment excuses defendant from answering all questions on the return relating to income and expenses; 3) whether a subpoena directed against the I.R.S. was erroneously quashed; 4) whether the District Court erroneously refused to instruct the jury on the definition of a dollar; and 5) whether defendant's criminal prosecution was illegal because it should have been preceded by some form of administrative action. *Daly*, 481 F.2d at 29.

The issues addressed in *Edelson* were: 1) the validity of his claim of privilege under the Fifth Amendment on his tax returns; 2) the correctness of his interpretation of "constitutional dollars"; and 3) whether he was entitled to have the question of his subjective "good faith" exercise of the Fifth Amendment privilege put to the jury. *Edelson*, 604 F.2d at 233-234.

The issues raised in *Moore* were: 1) whether the District Court allowed the introduction of irrelevant and prejudicial evidence; 2) whether the District Court judge participated excessively in the trial, particularly in questioning the defendant while he was testifying; 3) whether the jury instructions adequately informed the jury of the defendant's good faith defense; and 4) whether the District Court usurped the jury's function in deciding the issue of whether or not a return had been filed. *Moore*, 627 F.2d at 832.

The issues raised in *Porth* were: 1) whether his prosecution was barred by the statute of limitations; 2) whether there was a fatal variance between the allegations of the indictment and the proof on counts I and II of the indictment; 3) whether the return he did file constituted a valid return under the Fifth Amendment; and 4) whether he should be granted a new trial because of alleged bias and prejudice of one of the jurors. *Porth*, 426 F.2d at 521-523.

Neither *Daly*, *Edelson*, *Moore* nor *Porth* involved the issue of whether wages constitute income.

Donovan v. Maisel, 559 F.Supp. 171 (D.Del. 1982):

Five plaintiffs, each representing himself, filed substantially identical complaints, each seeking an injunction against the I.R.S. to prevent it from enforcing levies against the plaintiffs' wages for alleged past due income taxes. The issue before the Court was whether or not the government was entitled to a dismissal of the suit under the anti-injunction statute, 26 U.S.C. Section 7421 (a), which prohibits lawsuits for the purpose of restraining the assessment or collection of any tax. *Donovan*, 559 F.Supp. at 172-173.

The Court recognized that there was an exception to the anti-injunction statute where the government had made no disclosure as to whether the assessment had a basis in fact, citing to *Commissioner v. Shapiro*, 424 U.S. 614 (1976). The Court held that *Shapiro* was not applicable in the plaintiffs' case because the facts in the case showed that the plaintiffs were earning income and that the I.R.S. was not required to accept the taxpayers' unsubstantiated allegations that they were exempt from taxes on their wages. *Donovan*, 559 F.Supp. at 174.

The *Donovan* Court did not address whether wages constitute income, but merely held that the plaintiffs failed to provide evidence that they were exempt from income on their wages. The plaintiffs' argument on this issue was not set forth in the opinion and was not addressed by the Court. Therefore, the case cannot, and does not, stand for the proposition that wages constitute income.

Knighen v. C.I.R., 702 F.2d 59 (5th Cir. 1983):

Mr. Knighen, representing himself, appealed from the Tax Court's grant of summary judgment in favor of the I.R.S. The Court of

Appeals stated it was difficult to determine precisely what points Mr. Knighten was attempting to raise on appeal, *Knighten*, 702 F.2d at 60, and further stated:

The Tax Court understood one of Knighten's arguments to be that his wages were not income. On appeal, he avers that the Tax Court misunderstood the issue: the argument was that only "gain" is taxable, and the Commissioner's deficiency assessment did not accurately reflect Knighten's "gain." The problem with this argument is that the burden of proving any inaccuracy in the Commissioner's assessment was on Knighten. [Citations.] Knighten has not even attempted to carry that burden: he has failed to allege any fact or legal theory that would tend to show that the computation was incorrect. His unsupported claim of error was not enough to withstand a motion for summary judgment.

Knighten, id.

The *Knighten* Court did not rule that wages do not constitute income, and hence the case cannot be cited for the proposition that they do.

Lively v. Commissioner, 705 F.2d 1017 (8th Cir. 1983):

In 1977, Mr. & Mrs. Lively filed a Form 1040 together with Wage and Tax Statements showing the receipt of a little more than \$30,000 in wages. Rather than putting this amount on their Form 1040, it was put on a Schedule C⁹⁵ as a "receipt," from which was subtracted approximately \$23,000 for personal expenses, said calculations being made on a separate sheet of attached paper. The difference, \$7,918, was shown on the Schedule C as "net profit," and tax was paid on that amount. The Commissioner sent a notice of deficiency disallowing the "deductions" for personal expenses, and the Tax Court upheld the Commissioner. On appeal from that

decision, the Livelys claimed error because they did not claim the amount subtracted from wages as deductions, and further argued that the income tax was unconstitutional because it was a direct tax which was not apportioned, that there was no law imposing an income tax on them for 1977, that 26 U.S.C. Sections 3101, 3102 and 3402 were unconstitutional, that income could not be defined or measured, and that an individual's "gross receipts" could not be taxed. *Lively*, 705 F.2d at 1018.

The Court of Appeals stated that the Lively's arguments were without merit and that the appeal was frivolous, but failed to either set forth the details of the Lively's arguments or to respond to them. No case law was cited by the Court of Appeals, rendering the *Lively* case valueless as legal precedent for the issue of whether wages constitute income.

United States v. Stillhammer, 706 F.2d 1072 (10th Cir. 1983):

Mr. and Mrs. Stillhammer were each convicted on four counts of failure to file income tax returns and one count of filing a false withholding exemption certificate, Form W-4. Their tax returns, other than containing their names, address and social security numbers, contained no other information; they had claimed Fifth Amendment protection as to the other requested information on the Forms 1040. Their Forms W-4 claimed they had no tax liability. *Stillhammer*, 706 F.2d at 1073-1074.

On appeal, among other issues, the Stillhammers argued that the income tax statutes could not be construed to apply to them because Congress intended the Sixteenth Amendment to authorize taxation of the income of business enterprises only. *Stillhammer*, 706 F.2d at 1077.

The Court first stated that such a limited purpose of taxing only such business organizations was not apparent from the language of the Sixteenth Amendment. The Court noted that following the

ratification of the Sixteenth Amendment, the Supreme Court observed that the Amendment granted no new power to Congress, but merely freed it to exercise the taxing power granted in Article I, Section 8 to tax income without the restriction of apportionment, citing to *Brushaber*, 240 U.S. at 17-19. *Stillhammer*, 706 F.2d at 1077.

The Court next observed that prior to the ratification of the Sixteenth Amendment, an income tax act had been held partially invalid because of the Article I conditions of apportionment for direct taxes, and the finding by the *Pollock* Court that the tax was a direct tax as applied to income, such as rents, derived from real property.⁹⁶ *Stillhammer*, 706 F.2d at 1077. The Court then stated:

It is unnecessary to delve into the difficult question of the distinction between direct and indirect taxes because even a cursory study of these early cases teaches that the power of Congress to impose an income tax on salaries and wages has never been seriously doubted. In *Pollock* the Court stated:

[T]he power of Congress to tax is a very extensive power. It is given in the Constitution, with only one exception and only two qualifications. Congress cannot tax exports, and it must impose direct taxes by the rule of apportionment, and indirect taxes by the rule of uniformity. Thus limited, and thus only, it reaches every subject, and may be exercised at discretion.

157 U.S. at 557, 15 S.Ct. at 680 (quoting *The License Tax Cases*, 72 U.S. (5 Wall.) 462, 471, 18 L Ed. 497 (1866)). Thus, prior to ratification of the Sixteenth Amendment Congress could tax the earnings of individuals. The Amendment was passed to overrule

Pollock (see *Brushaber*, 240 U.S. at 18, 36 S.Ct. at 241-242) and to remove the apportionment limitation with respect to the laying and collection of taxes on income.

Stillhammer, 706 F.2d at 1077.

There is no question but that Congress could tax the “earnings” of individuals prior to the adoption of the Sixteenth Amendment; the tax merely needed to be apportioned. And there is no question but that after the adoption of the Sixteenth Amendment, “income of an individual” could be taxed without apportionment. But unless “earnings” of the individual constitute “income,” the “earnings” of an individual must still be taxed by apportionment, because the Sixteenth Amendment only applies to “income.” Thus the question becomes whether “earnings” constitute “income.” It is clear from the above quote that the *Stillhammer* Court equated “earnings” with “income,” but it is equally as clear that only the profit or gain **derived from** those “earnings” (labor) constitute “income.” The *Stillhammer* Court quoted the definition of income contained in *Eisner* and *Doyle* in its written opinion (*Stillhammer*, 706 F.2d at 1077-1078), but then ignored the precise prohibition contained in *Doyle* of equating “gross receipts” with “gross income.”⁹⁷

The precise holding of the *Stillhammer* Court was:

We feel it is clearly implicit in these decisions that Congress has the power to tax the income of individuals.

Stillhammer, 706 F.2d at 1078.

That is a correct statement of the law. However, to the extent the case purports to hold that wages constitute income, the case is at odds with various decisions of the United States Supreme Court, and is therefore legally defective.

United States v. Venator, 568 F.Supp. 832 (N.D.N.Y. 1983):

Mr. Venator was charged with five counts of failing to file income tax returns for the years 1976, 1977, 1978, 1979 and 1980. He filed pretrial motions, among others, to dismiss the charges against him on constitutional grounds. *Venator*, 568 F.Supp. at 833. He argued that compensation for services or “wages” was not income and that the current income tax on wages was contrary to the Sixteenth Amendment. *Venator*, 568 F.Supp. at 835. The District Court relied entirely on the *Jones* case in denying the motion to dismiss. *Jones* was fully analyzed herein at page 216 and shown to be unreliable precedent.

Rowlee v. Commissioner, 80 T.C. 1111 (1983):

Mr. Rowlee, for the years 1977, 1978 and 1979, filed Forms W-4 with his employers in which he claimed he was exempt from income taxation, and did not file income tax returns for those years. The I.R.S. issued letters of deficiency to Mr. Rowlee, and representing himself, he petitioned the United States Tax Court claiming he was not required to file any federal income tax returns because he was a “natural unfranchised individual and freeman”; that the Sixteenth Amendment only permitted a tax on income rather than on the source of income; that the tax laws set forth in the Internal Revenue Code were unconstitutional because they taxed the source rather than the income; that gain was a prerequisite to income; and that he had received no gain or profit because his labor was capital and the compensation received for his services was equal to the value of his labor. *Rowlee*, 80 T.C. at 1111-1113.

In ruling against Mr. Rowlee, the Court stated that:

In *Pollock v. Farmers’ Loan & Trust Co.*, 158 U.S. 601 (1985), the U.S. Supreme Court held unconstitutional a tax on incomes derived from property. It conceded at that same time, however, that taxes on income from

“professions, trades, employments or vocations” were valid. The entire statute was voided on the ground that Congress did not intend to permit the entire “burden of the tax to be borne by professions, trades, employments, or vocations.” 158 U.S. at 637.

Rowlee, 80 T.C. at 1119.

This first part of this statement is patently false; the *Pollock* Court actually said:

We do not mean to say that an act laying by apportionment a direct tax on all real estate and personal property, or the income thereof, might not also lay excise taxes on business, privileges, employments, and vocations. But this is not such an act; and the scheme must be considered as a whole.

Pollock, 158 U.S. at 637; (see pp. 27, 224).

Thus the *Pollock* Court clearly distinguished between an income tax on business, privileges, employments, and vocations and an excise tax on business, privileges, employments, and vocations.

The *Rowlee* Court next commented that the Sixteenth Amendment had been adopted in 1913, and that the *Brushaber* Court held the income tax law to be Constitutional. The *Rowlee* Court stated:

The propriety of taxing incomes from professions, trades, employments, or vocations was reaffirmed, the [*Brushaber*] Court stating that in the *Pollock* case “its validity was recognized; indeed, it was expressly declared that no dispute was made upon that subject and attention was called to the fact that taxes on such income had been sustained as excise taxes in the past.” 240 U.S. at 17.

Rowlee, 80 T.C. at 1119.

It was previously pointed out at page 58 that the *Pollock* Court, understanding the principle that the Supreme Court could only address issues actually before it, did not specifically address the issue of whether or not an income tax on business, privileges, employments, and vocations would be constitutional absent apportionment. The *Pollock* Court did state, however, that Section 27 of the 1984 Tax Act did not impose an excise tax on business, privileges, employments or vocations, and that previous courts had sustained a tax on business, privileges, employments and vocations under the “guise”⁹⁸ that such taxes were excise taxes. Thus *Pollock* does not stand for the principle that an income tax on business, privileges, employments or vocations is constitutional in the absence of apportionment, and *Brushaber* only holds that such taxes are excise taxes. It has been pointed out at page 83 that Congress did not impose an excise tax on business, privileges, employments or vocations in Subtitle A of the Internal Revenue Code, but imposed an income tax in Subtitle A.

The *Rowlee* Court next cited to *Eisner* stating the issue before that Court was the taxability of stock dividends, and that in *dicta* the Court referred to income as “gain derived from capital, from labor, or from both combined.” *Rowlee*, 80 T.C. at 1119. Since the definition of income was essential to the determination as to whether stock dividends constituted income under the law, it is not clear that *Eisner*’s definition of income was merely *dicta*.

The *Rowlee* Court next discussed Section 61 (a) of the Internal Revenue Code of 1954, and stated:

Petitioner has admitted that he exchanged his labor for the amounts paid to him by his employers during the taxable year. He argues that taxation of the amounts paid to him in exchange for his labor is a tax on the “source” of income and not on the income itself. This “taxation on source” argument is spurious;

the tax is imposed on the money he receives for his services, not on the performance of those services... . Finally, petitioner claims that he did not have any taxable income or “gain” because the value of his labor was the same as (or more than) the payment he received for it.

Rowlee, 80 T.C. at 1119-1120.

The *Rowlee* Court ignored the fact that in Section 61 (a) Congress defined gross income as the gain derived from compensation for services. To support its position, the *Rowlee* Court relied upon *Reading* (p. 174), *Lonsdale* (p. 200), *Buras* (p. 187) and *Rice* (p. 202). Those cases have been previously shown not to be legal precedent for the contention that wages constitute income. Contrary to the statement in *Rowlee* that the tax is imposed on the money received for services, that tax is imposed at Section 1 of the Internal Revenue Code upon taxable income. Taxable income is the profit or gain derived from compensation for services less the deductions authorized by Sections 62 and 63 of the Internal Revenue Code. In ruling against Mr. Rowlee, the Tax Court ignored the applicable decisions of the United States Supreme Court, the legislative history of the enactment of Section 61, and the law with respect to “basis” set forth in Section 1001 *et seq.* of the Internal Revenue Code. Therefore, *Rowlee* is not credible authority for the proposition that wages constitute income.

United States v. Richards, 723 F.2d 646 (8th Cir. 1983):

Mr. Richards was convicted of failing to file income tax returns for the years 1979, 1980 and 1981, and representing himself, appealed those convictions. *Richards*, 723 F.2d at 647. Among other issues, he contended that wages and salaries were not income within the meaning of the Sixteenth Amendment, and therefore he had no duty to file income tax returns. *Richards*, 723 F.2d at 648. The Court stated:

Although the sixteenth amendment, giving Congress the power to tax income, does not define “income,” the courts have interpreted the term in its every day usage to mean gain derived from capital, from labor, or from both combined. See *United States v. Safety Car Heating & Lighting Co.*, 297 U.S. 88, 89, 56 S.Ct. 353, 358, 80 L.Ed. 500 (1936); *Helvering v. Edison Bros. Stores, Inc.*, 133 F.2d 575, 579 (8th Cir. 1943), *cert. denied*, 319 U.S. 752, 63 S.Ct. 1166, 87 L.Ed. 1706 (1943). Clearly wages and salaries fall within this definition and are therefore constitutionally taxable.

Richards, 723 F.2d at 648.

As pointed out at page 193, the issue before the Court in the *Safety Car Heating & Lighting Co.* case was the taxability of the “profit” derived from a patent, and not whether wages constitute income. In *Edison Bros. Stores*, according to that Court:

The questions presented on these petitions to review a decision of the United States Board of Tax Appeals are whether the taxpayer realized taxable income in either or in both of the years 1935 and 1937 from sales to its employees of shares of its capital stock, previously acquired for that purpose, and whether, where the taxpayer discharged a debt owing to its general counsel for services rendered, by transfer to him of shares of its capital stock, it was entitled to deduct as a business expense the cost of the stock to the taxpayer at the time of its acquisition, or the fair market value of the stock at the time of its transfer to the general counsel, the gain to the taxpayer in the transaction not having been reported as income.

Edison Bros. Stores, 133 F.2d at 577.

It is clear that neither of these cases concerned the issue of whether wages constitute income. It is equally clear that the *Richards* Court ignored the holding of the Supreme Court in *Eisner* (see p. 137) regarding the words “gain derived from labor” in holding that wages and salaries fall within the definition of income. The *Richards* case being contrary to the applicable decisions of the Supreme Court, it does not constitute legal precedent for the contention that wages constitute income.

Parker v. Commissioner, 724 F.2d 469 (5th Cir. 1984):

Mr. Parker filed an income tax return for 1977 in which he failed to provide financial data, but instead claimed Fifth Amendment protection. This case was an appeal from an adverse determination of the United States Tax Court. *Parker*, 724 F.2d at 470.

On appeal, representing himself, Mr. Parker maintained that “the I.R.S. and the government in general, including the judiciary, mistakenly interpret the Sixteenth Amendment as allowing a direct tax on property (wages, salaries, commissions, etc.) without apportionment. *Parker*, 724 F.2d at 471.

The Court of Appeals cited to *Lonsdale* for the proposition that the Sixteenth Amendment was enacted for the express purpose of providing for a direct income tax, and then cited to *Brushaber* for the proposition that the Sixteenth Amendment provided the needed constitutional basis for the imposition of a direct, non-apportioned tax. *Parker*, 724 F.2d at 471.

Mr. Parker cited to *Flint* in support of his contention that the income tax was an excise tax applicable only against special privileges, such as the privilege of conducting a business, and was not assessable against income in general. The Court correctly pointed out that *Flint* did not address the personal income tax, but rather addressed the Corporate Excise Tax Act of 1909, and *Flint* was pre-Sixteenth Amendment. *Parker*, 724 F.2d at 471-472. ⁹⁹ Relying upon *Lonsdale*, the Court did not bother to address the

issue of whether or not wages constitute income. The *Lonsdale* case has been shown above (see p. 200) to be insufficient precedent for the determination of that issue.

Pascoe v. I.R.S., 580 F.Supp. 649 (E.D.Mich.S.D. 1984):

Mr. Pascoe, representing himself, had filed a Form W-4 claiming he was exempt from taxation. The I.R.S. notified his employer to withhold the income tax from his wages, and Mr. Pascoe sought to stop the withholding by filing a court action seeking a preliminary injunction. *Pascoe*, 580 F.Supp. at 650-651. One of the grounds asserted by Mr. Pascoe was that the wages that he received from his employer did not constitute “income” as that term was used in Section 61 of the Internal Revenue Code. *Pascoe*, 580 F.Supp. at 652. The District Court stated:

Although Section 61 does not by its terms define income, the courts have repeatedly stated that the term is broad enough to include as compensation any economic or financial benefit from any source, conferred in any form on any employee, see e.g. *Ritter v. United States*, 393 F.2d 823 (Ct.Cls. 1968), *cert. denied* 393 U.S. 844, 89 S.Ct. 127, 21 L.Ed.2d 115 (1968). Such a broad definition of “income” certainly would encompass the primary and perhaps only source of compensation that plaintiff receives from his employer, his wages.

Pascoe, 580 F.Supp. at 652.

In the *Ritter* case, Mr. Ritter filed an action to recover federal income taxes and interest thereon attributable to certain payments made to him by his employer in 1958. The issue before the Court was whether those payments, which were occasioned by a transfer of Mr. Ritter’s place of employment . for the convenience of his employer, constituted ordinary income to Mr. Ritter and, if so, whether Mr. Ritter could deduct as expenses the items for which

payments were made. *Ritter*, 393 F.2d at 824. More specifically, Mr. Ritter claimed that the reimbursements from his employer were not income as defined by Section 61 of the Internal Revenue Code. *Ritter*, 393 F.2d at 826.

In ruling against Mr. Ritter, the Court, citing to *Glenshaw Glass*, stated:

The Supreme Court has consistently given the term “gross income” as defined by the Revenue Code a broad construction in order “to tax all gains except those specifically exempted.” [Emphasis added.]

Ritter, 393 F.2d at 827.

The Court next cited to several cases in which the Supreme Court held that payments to an employee from an employer constituted income. The Court first cited to *C.I.R. v. Smith*. That case was analyzed herein at page 196, where it was shown that what was taxed in that case was the gain recognized when a stock option, which had no market value at the time of the option, was exercised, at which time the stock had a positive market value.

The Court next cited to *C.I.R. v. LoBue*, 351 U.S. 243 (1956), another stock option case. In *LoBue*, as a result of the exercise of the stock option, Mr. LoBue obtained \$9,930 worth of stock for \$1,700, realizing a gain in the amount of \$8,230, which Mr. LoBue did not report on his tax return. The issue in Tax Court was whether the stock option constituted additional compensation for personal services, in which case the gain would be taxable, or whether the options were intended to provide Mr. LoBue with “a proprietary interest in the business, in which case the gain would not constitute gross income. *LoBue*, 351 U.S. at 245.

Mr. LoBue won in both Tax Court and in the Court of Appeals, and the Supreme Court granted certiorari to consider whether those tribunals had given Section 22(a) of the 1939 Internal Revenue

Code too narrow an interpretation. The Court held that in enacting Section 22(a) Congress intended to “tax all gains except those specifically exempted,” citing to *Glenshaw Glass*. The Supreme Court next held that unless the stock option was a gift, it was taxable. Finally, the Supreme Court stated that there was not the slightest indication of the kind of detached and disinterested generosity which might evidence a gift, finding from the Tax Court record that the stock option plan was designed to achieve more profitable operations by providing the employees “with an incentive to promote the growth of the company by permitting them to participate in its success.” *LoBue*, 351 U.S. at 246. The Court also said:

When assets are transferred by an employer to an employee to secure better services they are plainly compensation. It makes no difference that the compensation is paid in stock rather than in money. Section 22(a) taxes income derived from compensation “in whatever form paid.”¹⁰⁰ And in another stock option case we said that Section 22(a) “is broad enough to include in taxable income any economic or financial benefit conferred on the employee as compensation, whatever the form or mode by which it is effected.” *Commissioner v. Smith*, 324 U.S. 188, 188. *LoBue* received a very substantial economic and financial benefit from his employer prompted by the employer’s desire to get better work from him. This is “compensation for personal service” within the meaning of Section 22(a).

LoBue, 351 U.S. at 247.

In both the *Smith* case and the *LoBue* case, only the difference between the option price and the market value of the stock at the time the option was exercised was subject to inclusion within “gross income.” Thus what was included was the **gain** derived from compensation for services.

Wages are clearly paid as compensation for services, but only the gain derived therefrom is includible within the statutory definition of gross income. This was confirmed by the Supreme Court in *LoBue* as follows:

It is true that our taxing system has ordinarily treated an arm's length purchase of property even at a bargain price as giving rise to no taxable gain in the year of purchase. See *Palmer v. Commissioner*, 302 U.S. 63, 69. But that is not to say that when a transfer which is in reality compensation is given the form of a purchase the Government cannot tax the **gain** under Section 22(a). [Emphasis added.]

LoBue, 351 U.S. at 248.

In ruling against Mr. Ritter, and after citing the Supreme Court cases of *Glenshaw Glass*, *Smith* and *LoBue*, the Court, relying upon a Court of Appeals case, *United States v. Woodall*, 255 F.2d 370 (10th Cir. 1958), stated:

Economic gain does not necessarily require profit in its usual sense.

Ritter, 393 F.2d at 832.

This statement is contrary to the precise holdings of *Glenshaw Glass*, *Smith* and *LoBue* based upon the facts in those cases wherein a profit was indeed realized by each of the taxpayers.

The *Woodall* case involved the issues of 1) whether an amount received by an employee as reimbursement for the costs of relocating himself and his family at the place of his new employment was gross income for income tax purposes; and 2) whether such costs were deductible business expenses. *Woodall*, 255 F.2d at 371. In ruling in favor of the government, the Court

basically relied upon *Glenshaw Glass, Smith and LoBue. Woodall*, 255 F.2d at 372.

Since the *Ritter* Court failed to adhere to the law as set forth by the Supreme Court, and since the issue before the *Woodall* and *Ritter* Courts were not whether wages constitute income, the *Pascoe* case is not legal precedent for the proposition that wages do constitute income.

Simanonok v. C.I.R., 731 F.2d 743 (11th Cir. 1984):

Mr. Simanonok filed suit in Tax Court seeking a redetermination of his tax liability, claiming, among other things, that he had not received income because his paychecks were received in exchange for his costs and disbursements of labor. The Tax Court ruled in favor of the Commissioner's determination of tax, and Mr. Simanonok, representing himself, appealed. *Simanonok*, 731 F.2d at 744.

Mr. Simanonok's legal arguments raised on the appeal were not set forth in the Court's opinion. Without citing any case law or other authority, the Court stated:

The tax court correctly determined that Simanonok's contentions are completely without merit; we therefore affirm the tax court's decision as to these issues.

Simanonok, id.

Having failed to set forth the Court's reasoning or any legal authority therefor, the case is of no value as legal precedent.

Lovell v. United States, 579 F.Supp. 1047 (W.D.Wis. 1984):

Mr. and Mrs. Lovell filed Forms 1040 in which they claimed no income from wages, salaries or tips. During a deposition taken in the case, Mr. Lovell stated that he did not receive any wages, but

instead received compensation in equal exchange for his labor or a commodity. *Lovell*, 579 F.Supp. at 1047-1048. While the nature of the lawsuit brought by the Lovells, representing themselves, was not stated in the opinion, it was apparently a suit for refund of income taxes withheld by their employers through withholding.

In ruling against the Lovells, the Court stated, citing *Kowalski* and *Glenshaw Glass* that:

It is well settled, and beyond dispute, that compensation for labor or service is taxable income, and no deduction is allowed for the value of labor expended.

Lovell, 579 F.Supp. at 1048.

As previously set forth at pages 202 and 153 respectively, *Kowalski* and *Glenshaw Glass* stand for the proposition that gain constitutes income, not that wages constitute income.

United States v. Koliboski, 732 F.2d 1328 (7th Cir. 1984):

Mr. Koliboski was convicted of two counts of willful failure to file income tax returns for the years 1980 and 1981, and filing four false W-4 statements in 1980, 1981 and 1982. On Appeal, Mr. Koliboski, representing himself, raised several issues, none of which involved the issue of whether wages constitute income. *Koliboski, id.* Notwithstanding this fact, the Court stated in a footnote:

Although not raised in his brief on appeal, the defendant's entire case at trial rested on his claim that he in good faith believed that wages are not income for taxation purposes. Whatever his mental state, he, of course, was wrong, as all of us already are aware. Nonetheless, the defendant still insists that no case holds that wages are income. Let us now put that to rest: WAGES ARE INCOME. Any reading of tax cases

by would-be tax protesters now should preclude a claim of good-faith belief that wages—or salaries—are not taxable. [Emphasis in original.]

Koliboski, 732 F.2d at 1329, n.l.

The Court cites no case law to support this gratuitous statement, and provides no analysis for consideration. The statement constitutes pure *dicta*, and thus the case cannot constitute legal precedent for the proposition stated.

Karpowycz v. United States, 586 F.Supp. 48 (N.D.I11.E.D. 1984):

Mr. Karpowycz was assessed a \$500 penalty for filing a frivolous income tax return and, representing himself, brought suit for a refund. *Karpowycz*, 586 F.Supp. at 49-50. He argued that a substantial portion of his wages earned while employed by Sun Electric Corporation was non-taxable, since he earned the wages while he was a “nominee-agent” for Professional and Technical Services, a purported trust created by an entity known as American Dynamics Corporation. He claimed that by virtue of owning a property interest in his own labor, he could convey his “personal services property assets” to the trust in accordance with a personal service contract executed between himself and the trust. *Karpowycz*, 586 F.Supp. at 51.

The trial court, in granting the government’s motion for summary judgment, relied upon the principle that income must be taxed to the one who earns it, and pointed out that Mr. Karpowycz had failed to show the existence of a contract or other agreement between the trust and his employer, and did not claim that the trust had the right to direct or control his activities as an engineer. *Karpowycz*, *id.*

It does not appear from the Court's opinion that Mr. Karpowycz claimed that wages do not constitute income. Nonetheless, the Court stated:

It is well settled that gross income includes compensation for services. 26 U.S.C. Section 61. In addition, the Supreme Court has held that compensation for labor or services paid in the form of wages or salaries is income taxable under federal income tax laws. See *e.g.*, *Commissioner v. Kowalski*, 434 U.S. 77 (1977).

Karpowycz, 586 F.Supp. at 51.

In *Kowalski*, the issue before the Supreme Court was whether cash payments to state police troopers, designated as meal allowances, were included in the definition of gross income under Section 61 (a) of the Internal Revenue Code of 1954, and, if so, were otherwise excludable under Section 119 of the Code. *Kowalski*, 434 U.S. at 78. Contrary to the above quote from *Karpowycz*, the issue of whether compensation for labor or services paid in the form of wages or salaries constituted income taxable under federal income tax laws was not addressed by the *Kowalski* Court.

The Supreme Court stated:

The starting point in the determination of the scope of "gross income" is the cardinal principle that Congress in creating the income tax intended "to use the full measure of its taxing power." *Helvering v. Clifford*,¹⁰¹ 309 U.S. 331, 334 (1940); *accord*, *Helvering v. Midland Mutual Life Ins. Co.*,¹⁰² 300 U.S. 216, 223 (1937); *Douglas v. Willcuts*, 296 U.S. 1, 9 (1935); *Irwin v. Gavit*,¹⁰³ 268 U.S. 161, 166 (1925). In applying this principle to the construction of Section 22(a) of the Internal Revenue Code of 1939 this Court stated that "Congress applied no limitations as to the

source of taxable receipts, nor restrictive labels as to their nature [, but intended] to tax all gains except those specifically exempted.” *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 429-430 (1955), citing *Commissioner v. Jacobson*,¹⁰⁴ 336 U.S. 28, 49 (1949) and *Helvering v. Stockholms Enskilda Bank*,¹⁰⁵ 293 U.S. 84, 87-91 (1934). Although Congress simplified the definition of gross income in Section 61 of the 1954 Code, it did not intend thereby to narrow the scope of that concept. See *Commissioner v. Glenshaw Glass Co.*, *supra*, at 432, and n.11; H.R. Rep.No. 1337, 83rd Cong., 2d Sess., A18 (1954); S. Rep.No. 1622, 83rd Cong., 2d Sess., 168 (1954). In the absence of a specific exemption, therefore, respondent’s meal-allowance payments are income within the meaning of Section 61 since, like the payments involved in *Glenshaw Glass Co.*, the payments are “undeniabl[y] accessions to wealth, clearly realized, and over which the [respondent has] complete dominion.” *Commissioner v. Glenshaw Glass Co.*, *supra* at 431. See also *Commissioner v. LoBue*, 351 U.S. 243, 247 (1956); *Van Rosen v. Commissioner*, 17 T.C. 834, 838 (1951).

Kowalski, 434 U.S. at 82-83.

Commissioner v. LoBue, analyzed herein at page 230, involved a stock option case, and involved the taxation of a gain. The *Van Rosen* case involved the question of whether the receipt by Mr. Van Rosen of cash payments by his employer in lieu of subsistence and quarters was to be included in his gross income. *Van Rosen*, 17 T.C. at 834. Mr. Van Rosen did not challenge whether money or other consideration, to the extent of the value thereof received by an employee as consideration for the services rendered by him, was income taxable to the employee. *Van Rosen*, 17 T.C. at 836. The Tax Court, despite quoting Section 22(a) of the Internal Revenue Code

of 1939 which included in gross income “gains, profits and income derived from salaries”, stated:

We find it difficult to conclude that, for the purpose of reporting income and paying the tax thereon, this petitioner should be regarded in a light more favorable, tax-wise, than any other civilian employee whose employment is such as to permit him to live at home while performing the duties of his employment. In both instances, there is de facto receipt under the employment contract of x dollars, whether the consideration be denominated salary only, or salary and allowances, or base pay plus an allowance of subsistence and quarters, which dollars the employee, in each instance, has as his own and without any restriction on their use or expenditure.

Van Rosen, id.

Under Section 22(a) of the 1939 Internal Revenue Code it was not the receipt of dollars that was includible in gross income, it was the receipt of a profit, gain and income derived from labor (employment) that was includible in gross income.

Thus contrary to the erroneous assertion in *Karpowycz* that the Supreme Court has held that compensation for labor or services paid in the form of wages or salaries is income taxable under federal income tax laws, the Supreme Court in *Kowalski* specifically held that a **gain** from any source constitutes income includible in gross income. The Supreme Court even referenced the case of *Jones v. United States*, 60 Ct. Cls. 552 (1925) and stated:

The Court of Claims, in addition, rejected the argument that money paid in commutation of quarters [provided to military officers] was income on the ground that it was not “gain derived ... from labor”

within the meaning of *Eisner v. Macomber*, 252 U.S. 189 (1920)

Kowalski, 434 U.S. at 87.

The *Karpowycz* Court's contentions that wages constitute income is not supported by the authorities cited, and is thus erroneous as a matter of law.

Gattuso v. Pecorella, 733 F.2d 709 (9th Cir. 1984):

Mr. Gattuso, representing himself, filed an action in District Court to abate the finding of the I.R.S. that he and his wife owed taxes for the years 1980, 1981 and 1982. He claimed that their wages were not income within the meaning of the Internal Revenue Code. *Gattuso*, 733 F.2d at 709. The Ninth Circuit asserted that this claim was frivolous citing to *Romero*, *Buras* and *Funk*. Those cases have been shown herein at pages 184, 181 and 205 respectively to be deficient precedent for the proposition that wages do constitute income.

United States v. Burton, 737 F.2d 439 (5th Cir. 1984):

Mr. Burton appealed his convictions for failing to file income tax returns and for filing false withholding allowance certificates. His contentions on appeal were: 1) that the District Court effectively withheld the essential element of willfulness from the jury by instructing them that his alleged good faith belief that wages were not taxable income was not a defense; 2) that the district judge should have allowed a defense expert to testify concerning the legal uncertainty over whether wages are income; and 3) that it was error for the judge to appoint a jury foreman. The Court found in favor of Mr. Burton's first argument and reversed his conviction. *Burton*, 737 F.2d at 440.

The Court, citing to *Lonsdale*, stated:

Beyond dispute, wages are income.

Burton, 737 U.S. at 441.

As shown above at page 200, the *Lonsdale* Court ignored the precise holdings of the Supreme Court which defined “income,” failed to ascertain if Mr. Lonsdale had a profit derived from his compensation for services, and failed to distinguish between “income derived from compensation for services” and “compensation for services.” Thus the contention in *Burton* that wages constitute income, to the extent it relies wholly on the erroneous holding of the *Lonsdale* case, is equally erroneous.

Granzow v. C.I.R., 739 F.2d 265 (7th Cir. 1984):¹⁰⁶

Mr. Granzow appealed an adverse determination of the United States Tax Court which rejected his contention that wages do not constitute income. The Seventh Circuit Court of Appeals stated that:

It is well settled that wages received by taxpayers constitute gross income within the meaning of section 61(a) of the Internal Revenue Code ... and that such gross income is subject to taxation.

Granzow, 739 F.2d at 267.

In support of this proposition, the Court cited to the following cases which have been previously analyzed herein: *Koliboski* (see p. 234), *Lonsdale* (see p. 200), *Knighten* (see p. 218), *Reading* (see p. 174), *Hayward* (see p. 185), *Broughton* (see p. 186), *Funk* (see p. 209), *Lively* (see p. 219), *Buras* (see p. 187) and *Romero* (see p. 189). Having relied entirely on cases that do not support the proposition, the *Granzow* case does not provide precedent for the proposition that wages constitute income.

Davis v. United States Government, 742 F.2d 171 (5th Cir. 1984):

Mr. and Mrs. Davis filed a Form 1040 for the year 1982 in which they reported no income from “wages, salaries, [or] tips,” nor any other “gross income,” even though four Forms W-2 from their employers in 1982 attached to their return indicated they had received in excess of \$60,000 in wages or other compensation for that year. Instead, they claimed a business loss of \$3,551 by deducting from their gross receipts the “cost of labor” which equaled the amount shown on their Forms W-2, and other deductions for “materials and supplies,” “car and truck expenses” and “laundry and cleaning.” *Davis*, 742 F.2d at 172.

The I.R.S. assessed a “frivolous return” penalty of \$500. The Davises paid fifteen percent of the penalty, and after their claim for refund was denied by the I.R.S., filed a suit for refund, additionally seeking a refund for taxes paid by them from 1979 through 1982 and \$50,000,000 in damages for mental and physical suffering. The lower court dismissed the complaint, and representing themselves, Mr. and Mrs. Davis filed an appeal, contending: 1) the income tax is an excise tax applicable only against special privileges and not assessable against income in general; and 2) an individual receives no taxable gain from the exchange of labor for money because the wages received are offset by an equal amount of “costs of labor.”

As to the first contention, the Court merely quoted from *Parker*, 724 F.2d at 471 as follows:

At this late date, it seems incredible that we would again be required to hold that the Constitution, as amended, empowers the Congress to levy an income tax against any source of income, without the need ... to classify it as an excise tax applicable to specific categories of activities.

Davis, 742 F.2d at 172.

As to the second contention, the Court stated:

We held this contention meritless in *Lonsdale v. C.I.P.*, 661 F.2d 71, 72 (5th Cir. 1981).

Davis, 742 F.2d at 172.

Having relied entirely upon *Parker* and *Lonsdale*, which as shown above at pages 228 and 200 respectively were decided contrary to the applicable decisions of the United States Supreme Court, *Davis* cannot support the legal proposition that wages constitute income.

Crain v. C.I.R., 737 F.2d 1417 (5th Cir. 1984):

Mr. Crain, representing himself, appealed the dismissal of his Tax Court petition in which he, according to the Court, defied the jurisdiction of the Internal Revenue Service to levy taxes on his income. *Crain*, 737 F.2d at 1417. The Court failed to set forth Mr. Crain's arguments and cited no case law in its opinion. Accordingly, the case cannot constitute legal precedent for the contention that wages constitute income.

Hansen v. United States, 744 F.2d 658 (8th Cir. 1984):

In *Hansen*, nineteen people brought an appeal from the dismissal by the lower court of their action against the United States. The nineteen people did not report their wages on their respective income tax returns. After the I.R.S. obtained Tax Court judgments against them, it started to seize their property, and the nineteen sought to enjoin the I.R.S. from these seizures. The nineteen argued on appeal that wages were not income under the Sixteenth Amendment. *Hansen*, 744 F.2d at 659.

The Court of Appeals relied upon *Richards* in holding against the nineteen on their argument that wages did not constitute income, and relied upon *Rowlee* in holding against the nineteen on their

argument that labor was a property right given in exchange for wages, therefore no gain was recognized. *Hansen*, 744 F.2d at 660. As shown on pages 223 and 219 respectively, neither *Richards* nor *Rowlee* is valid legal precedent for the positions for which they were relied upon by the *Hansen* Court.

Cameron v. I.R.S., 593 F.Supp. 1540 (N.D.Ind. Fort Wayne Div. 1984):

In an action in District Court for an injunction against the Internal Revenue Service, Mr. Cameron, representing himself, raised, among other issues, that wages did not fall under the statutory provisions for income because they were part of an equal exchange of wages for services rendered, and thus had no element of profit or gain. *Cameron*, 593 F.Supp. at 1544. Mr. Cameron cited to several Supreme Court cases,¹⁰⁷ which the Court classified as “old,” for the proposition that income means profit or gain. The Court stated:

However, none of these decisions were intended to be definitive definitions of the concept; all deal with specific questions under specific statutory provisions. The Supreme Court rejected an argument, based on *Eisner*, that the Code’s definition of income is limited to gain in *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426 (1955). The Court specifically stated that the “income as gain” definition of *Eisner* “was not meant to provide a touchstone to all future gross income questions.” *Id.* at 431.

Cameron, 593 F.Supp. at 1552.

As to the statement by the *Cameron* Court that none of these decisions were intended to be definitive definitions of the concept, said statement is contrary to the express holding of the Supreme Court’s opinion in *Smietanka* that:

[T]here would seem to be no room to doubt that the word must be given the same meaning in all of the Income Tax Acts of Congress that was given to it in the Corporation Excise Tax Act and that that meaning is has now become definitely settled by decisions of this court.

Smietanka, 255 U.S. at 519 (see p. 144).

As to the statement by the *Cameron* Court that the definition of income as set forth in *Eisner* was not meant to provide a touchstone to all future gross income questions, that sentence was taken out of context. The complete quote was:

Such decisions demonstrate that we cannot but ascribe content to the catchall provision of Section 22(a), “gains or profits and income derived from any source whatever.” The importance of that phrase has been too frequently recognized since its first appearance in the Revenue Act of 1913 to say now that it adds nothing to the meaning of “gross income.”

Nor can we accept respondents’ contention that a narrower reading of Section 22(a) is required by the Court’s characterization of income in *Eisner v. Macomber*, 252 U.S. 189, 207, as “the gain derived from capital, from labor, or from both combined.” The Court was there endeavoring to determine whether the distribution of a corporate stock dividend constituted a realized gain to the shareholder, or changed “only the form, not the essence,” of his capital investment. *Id.*, at 210. It was held that the taxpayer had “received nothing out of the company’s assets for his separate use and benefit.” *Id.*, at 211. The distribution, therefore, was held not a taxable event. In that context—distinguishing gain from capital—the definition served a useful purpose. But it was not

meant to provide a touchstone to all future gross income questions. [Citations omitted.]

Here we have instances of undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion.

Glenshaw Glass, 348 U.S. at 430-431.

The *Court* in *Glenshaw Glass* was merely distinguishing that income may be derived from any source, not only from labor or capital, and did not hold that income was something other than a gain. The Sixteenth Amendment authorized an unapportioned tax on income “from whatever source derived,” and the language of Section 22(a) of the Internal Revenue Code of 1939 and of Section 61(a) of the Internal Revenue Code of 1954 shows Congress’ intent to tax income “from whatever source derived.”

Remembering that the issue in *Glenshaw Glass* was the taxability of punitive damages, the holding in *Glenshaw Glass* that punitive damages falls within the definition of statutory gross income is in full accord with that part of the definition of gross income as stated in *Eisner* and the other “old” cases cited by Mr. Cameron that “income” must be a “profit or gain.”

The *Cameron* Court next stated that:

More recently the Court rejected the assumption that the current statutory definition of income (in 26 U.S.C. Section 61) incorporated the income as gain definition of *Eisner*, See *Commissioner v. Kowalski*, 434 U.S. 77, 94 (1977).

Cameron, 593 F.Supp. at 1552.

In *Kowalski*, the Supreme Court said:

Jones also rests on *Eisner v. Macomber*, 252 U.S. 189 (1920), but Congress had no reason to read *Eisner's* definition of income into Section 61 and, indeed, any assumption that Congress did is squarely at odds with *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426 (1955).

Kowalski, 434 U.S. at 94.

As shown immediately above, the Supreme Court in *Glenshaw Glass* was merely indicating that income could be derived from sources other than from labor or from capital. In addition, the legislative history of the enactment of Section 61 clearly discloses that the word “income” was to have the same meaning as it had in the Sixteenth Amendment, which has never been interpreted by the Supreme Court to include anything other than a profit or gain (see p. 84). Also, the Supreme Court in *Kowalski* explicitly stated, citing *Glenshaw Glass* as its authority, that:

Congress applied no limitations as to the source of taxable receipts, nor restrictive labels as to their nature [, but intended] to tax all **gains except those specifically exempted.**” [Emphasis added.]

Kowalski, 434 U.S. at 82-83.

Certainly, then, the language of the Supreme Court in *Kowalski* at page 94 referred only to the source element of the definition of *Eisner*, and not to the profit or gain element of the *Eisner* definition.

The Cameron Court next cited to *Koliboski*, *Granzow*, *Knighten* and *Romero* and stated:

It is therefore unmistakably clear that plaintiff is wrong in concluding that his wages are not taxable income. The initial assumption behind the argument

(that income is gain or profit) is incorrect because it is not exclusive.

Cameron, 593 F.Supp. at 1552.

The case law of the United States Supreme Court, including *Glenshaw Glass* and *Kowalski*, makes it clear that the gain or profit part of the definition of income is exclusive; only the sources from which the income may be derived definition of *Eisner* is not exclusive.

Having ignored Supreme Court decisions on point, the *Cameron* case cannot stand as legal authority for the proposition that wages constitute income.

Hallowell v. C.I.R., 744 F.2d 406 (5th Cir. 1984):

In appealing an adverse determination of the United States Tax Court against them, Mr. and Mrs. Hallowell, representing themselves, argued that the Sixteenth Amendment did not contemplate wages to be includible in the definition of income. *Hallowell*, 744 F.2d at 408. The Court disposed of this issue in a footnote, stating:

We perceive no need to refute these arguments with somber reasoning and copious citation of precedent; to do so might suggest that these arguments have some colorable merit.

Hallowell, 744 F.2d at 408, n.2.

Having failed to address the issue, the case does not constitute legal precedent.

Snyder v. I.R.S., 596 F.Supp. 240 (N.D.Ind. Fort Wayne Div. 1984):

Mr. Snyder, representing himself, attempted to sue the I.R.S. and one of its agents. He claimed that his wages did not constitute income. *Snyder*, 596 F.Supp. at 243. The case was before the same judge, Judge Lee, who decided the *Cameron* case. In disposing of Mr. Snyder's claim, Judge Lee's opinion was almost word for word identical to his opinion in *Cameron*. For that reason, reference is made to the *Cameron* analysis hereinabove at page 243.

Perkins v. C.I.R., 746 F.2d 1187 (6th Cir. 1984):

Mr. Perkins, representing himself, appealed from an adverse decision of the United States Tax Court. He argued that wages paid for his labor were non-taxable receipts and that the Sixteenth Amendment did not permit an imposition of tax on wages. *Perkins*, 746 F.2d at 1188.

The Court stated, citing to *Brushaber*, *Glenshaw Glass* and *Funk*:

First, gross income means all income from whatever source derived including compensation for services. Second, 26 U.S.C. 61 (a) is in full accordance with Congressional authority under the Sixteenth Amendment to the Constitution to impose taxes on income without apportionment among the states.

Perkins, 746 F.2d at 1188.

Neither *Brushaber* nor *Glenshaw Glass* involved the issue as to whether wages constitute income. *Funk* has been shown above at page 209 to be unreliable precedent. There is no question but that Section 61 (a) is in full accordance with Congressional authority under the Sixteenth Amendment, but the statute defines gross income as income derived from compensation for services. The interpretation of that statute to allow an unapportioned tax directly

on compensation for services violates the Sixteenth Amendment, as only a tax on the income derived from that compensation is embraced within its terms.

Hill v. United States, 599 F.Supp. 118 (M.D.Tenn. Nashville Div. 1984):

Mr. Hill, representing himself, filed an action for a judicial review of a penalty assessment imposed against him by the I.R.S. for filing a frivolous income tax return. His argument was that wages did not constitute income. *Hill*, 599 F.Supp. at 119-120.

Quoting from the unsupported footnote in *Koliboski* (see p. 234), the Court stated:

[I]f anything in our tax law is clear, it is that:
 “ * * * WAGES ARE INCOME. * * * ”

Hill, 599 F.Supp. at 120.

The Court next stated that:

The Supreme Court of the United States upheld in 1926 the application of the federal income tax to “ * * * items of income [which] were received by the taxpayers as compensation for their services as consulting engineers * * * ,” *Metcalf & Eddy v. Mitchell*, 269 U.S. 514, 519 (1926), and no Court of the land has ever held or suggested that the Congress could not tax constitutionally wages as income.

Hill, 599 F.Supp. at 120-121.

In *Metcalf & Eddy* it was not contended that wages do not constitute income. *Metcalf & Eddy* were consulting engineers who, either individually or as co-partners, were professionally employed to advise States or subdivisions of States with reference to proposed water supply and sewage disposal systems. During 1917 the fees

received by them for these services were paid over to the firm and became, according to the Court, a part of its gross income. In seeking a refund of the taxes paid by the partnership, they contended they were exempt from the tax by a provision of the War Revenue Act of 1917 (Act of October 3, 1917, c. 63, Section 209, 40 Stat. 300, 307),¹⁰⁸ and that Congress had no power under the Constitution to tax the income in question. *Metcalf & Eddy*, 269 U.S. at 518. As to the first question, the Court stated:

The War Revenue Act provided for the assessment of a tax on net income; but Section 201(a) (40 Stat. at 303) contains a provision for exemption from the tax as follows:

“This title shall apply to all trades or businesses of whatever description, whether continuously carried on or not, except—

“(a) In the case of officers and employees under the United States, or any State, Territory, or the District of Columbia, or any local subdivision thereof, the compensation or fees received by them as such officers or employees.”

Metcalf & Eddy, 269 U.S. at 519.

In resolving this question against *Metcalf & Eddy*, the Court found that they had failed to sustain their burden of establishing that they were officers of a State or a subdivision of a State within the exception of Section 201 (a), and that the facts stated in their bill of exceptions did not establish that they were employees, but rather established they were independent contractors. *Metcalf & Eddy*, 269 U.S. at 520.

The second issue before the Court was the power of Congress to impose a tax on the instrumentalities of a State government.

Messrs. Metcalf and Eddy never raised the issue of whether wages constitute income, and this issue was not before the United States Supreme Court in the case.

The *Hill* Court's gratuitous comment that no court of the land has ever held or suggested that Congress could not tax constitutionally wages as income is extremely disingenuous. By the same token, The *Hill* Court certainly did not cite to any Supreme Court cases in which the highest court of the land, when presented with the issue, has stated that Congress could tax wages as income. As has been repeatedly shown herein, those lower court cases in which it has been stated that wages constitute income either have ignored the Supreme Court's statement that income must be a profit or gain, have ignored the existence of the words "income derived from any source whatsoever" in both Sections 22(a) and 61 (a) of the Internal Revenue Codes of 1939 and 1954 respectively, have ignored the legislative history accompanying the passage of Section 61 (a) by Congress, or have ignored the Supreme Court's holdings that one's labor is personal property and the corresponding provisions of the Internal Revenue Code, Sections 64 and 1001, *et seq.*, providing the law with respect to how to compute gain on the sale of personal property.

The *Hill* Court next cited to *Perkins* (see p. 248), *Romero* (see p. 189), *Davis* (see p. 241), *Funk* (see p. 209), *Moore* (see p. 216), *Lawson* (see p. 206), *Lonsdale* (see p. 200), *Buras* (see p. 187), *Broughton* (see p. 186), *Hayward* (see p. 185), *Francisco* (see p. 183), *Adams* (see p. 180), *Russell* (see p. 179), *Wilson* (see p. 170), *Marks* (see p. 169), *Daehler* (see p. 165), *Lucas v. Earl* (see p. 149) and *Stratton's Independence* (see p. 93) for the proposition that wages constitute income. All of these cases has been analyzed herein and shown not to be valid legal precedent for that proposition.

Ficalora v. C.I.R., 751 F.2d 85 (2nd Cir. 1984):

Mr. Ficalora appealed a determination of the Tax Court regarding his tax liability for the year 1980. He argued in Tax Court, among other issues, that wages do not constitute income. *Ficalora*, 751 F.2d at 86.

The Court first addressed Mr. Ficalora's contention that neither the United States Congress nor the United States Tax Court possessed the constitutional authority to impose on him an income tax for the year 1980. Mr. Ficalora, relying on *Pollock*, argued on appeal that an income tax was a "direct" tax, and that Congress lacked the constitutional authority to impose such a tax in the absence of apportionment. *Ficalora*, 751 F.2d at 87. The Court stated:

In making his argument that Congress lacks constitutional authority to impose a tax on wages without apportionment among the States, the appellant has chosen to ignore the precise holding of the Court in *Pollock*, as well as the development of constitutional law in this area over the last ninety years. While ruling that a tax upon income from real and personal property is invalid in the absence of apportionment, the Supreme Court explicitly stated that taxes on income from one's employment are not direct taxes and are not subject to the necessity of apportionment. *Pollock v. Farmers's Loan and Trust Co.*, 158 U.S. at 635.

Ficalora, 751 F.2d at 87.

It has previously been shown at pages 50 and 219 in connection with the analysis of the *Rowlee* case that the *Pollock* Court did not hold that taxes on income from one's employment are not direct taxes.

The *Ficalora* Court continued:

Finally, in the case of *New York ex rel. Cohn v. Graves*, 300 U.S. 308, 57 S.Ct. 466, 81 L.Ed. 666 (1937), the Supreme Court in effect overruled *Pollock*, and in so doing rendered the Sixteenth Amendment unnecessary, when it sustained New York's income tax on income derived from real property in New Jersey. *Id.* at 314-15, 57 S.Ct. at 468-469. Hence, there is no question but that Congress has the constitutional authority to impose an income tax upon the appellant.

Ficalora, 751 F.2d at 87.

In *New York ex rel Cohn v. Graves*, the issue before the Court was stated as follows:

This case presents the question whether a state may constitutionally tax a resident upon income received from rents of land located without the state and from interest on bonds physically without the state and secured by mortgages upon lands similarly situated.

New York ex rel Cohn, 300 U.S. at 310.

It thus becomes immediately clear that the case involved the State of New York's income tax, and not the federal income tax. The Supreme Court also stated:

We accordingly limit our review to the question considered and decided by the state court, whether there is anything in the Fourteenth Amendment which precludes the State of New York from taxing the income merely because it is derived from sources, which, to the extent indicated, are located outside the State.

New York ex rel Cohn, 300 U.S. at 312.

This statement makes it abundantly clear that the Supreme Court did not even address the Sixteenth Amendment in its opinion. And finally, with respect to the alleged overruling of *Pollock*, what the Supreme Court actually stated was:

Nothing which was said or decided in *Pollock v. Farmers Loan & Trust Co.*, 157 U.S. 429, calls for a different conclusion. There the question for decision was whether a federal tax on income derived from rents of land is a direct tax requiring apportionment under Art. I, Section 2, Cl. 3 of the Constitution. In holding that the tax was “direct,” the Court did not rest its decision upon the ground that the tax was a tax on the land, or that it was subject to every limitation which the Constitution imposes on property taxes. It determined only that for purposes of apportionment there were similarities in the operation of the two kinds of tax which made it appropriate to classify both as direct, and within the constitutional command.

New York ex rel Cohn, 300 U.S. at 315.

Rather than overruling *Pollock*, the Supreme Court in effect reaffirmed the *Pollock* decision. No Court, including the *Brushaber* Court, has ever taken the position that the Sixteenth Amendment is unnecessary to allow an unapportioned tax on income!

With respect to Mr. Ficalora’s contention that the term “income,” as used in the taxing statutes, has no defined meaning and is unconstitutionally vague and indefinite, the Court stated:

As discussed above, Section 61 of the Code defines gross income as “all income from whatever source derived.” Even if we were to assume, *arguendo*, that this phrase is somehow vague or indefinite, Section 61 of the Code specifically cites “compensation for

services ...” as a concrete example of what is meant by the term income. The wages which the appellant received for his services rendered to New York Telephone in taxable year 1980, fall squarely within the definition of income contained in Section 61(a)(1) of the Code. The appellant’s argument that the term “income,” as used in the Code, is unconstitutionally vague and indefinite, is totally without merit.

Ficalora, 751 F.2d at 88.

It has been previously set forth that Section 61 defines gross income as the profit or gain derived from, among other sources, “compensation for services,” and that a tax on the actual “compensation for services” is a direct tax that does in fact, under the law, require apportionment. The *Ficalora* decision, especially to the extent it states that *Pollock* was overruled and the Sixteenth Amendment is not necessary to empower the Congress to pass legislation imposing a tax upon income without apportionment, is a disgrace to the American people.

The case does not constitute valid legal precedent for the contention that wages constitute income.

Schiff v. Commissioner, 751 F.2d 116 (2nd Cir. 1984):

Mr. Irwin Schiff appealed from an order of the United States Tax Court which dismissed his petition for redetermination of income tax deficiencies for the years 1974 and 1975. Among other issues, Mr. Schiff argued that a tax on wage income is unconstitutional. *Schiff*, 751 F.2d at 116-117.

The Court ruled against Mr. Schiff without addressing any of his arguments and without citing any case law. Accordingly, the case has no legal precedent for the proposition that wages constitute income.

Lovell v. United States, 755 F.2d 517 (7th Cir. 1984):

Mr. & Mrs. Lovell, representing themselves, were assessed a \$500 frivolous return penalty by the I.R.S. The lower court granted summary judgment in favor of the United States, and the Lovells appealed. *Lovell*, 755 F.2d at 518-519. They first argued that they were exempt from federal taxation because they were “natural individuals” who have not “requested, obtained or exercised any privilege from an agency of government.” *Lovell*, 755 F.2d at 519.

With respect to this argument the Court stated:

This is not a basis for an exemption from federal income taxes. See *Holker v. United States*. All individuals, natural or unnatural, must pay federal income tax on their wages, regardless of whether they received any “privileges” from the government.

Lovell, 755 F.2d at 519.

No case law is cited here by the Court for the proposition that wages are subject to the federal income tax.

The Lovells next argued that the Constitution prohibits imposition of a direct tax without apportionment. The Court stated the Lovells were wrong citing to the Sixteenth Amendment. *Lovell, id.*

The Lovells next argued that money received in compensation for labor is not taxable. The Court cited to *Davis, Simanonok* and *Koliboski*, stating that these Courts had rejected the same arguments as raised by the Lovells. Those cases have been analyzed herein at pages 241, 233 and 234 respectively and shown not to be legal precedent for the proposition that money received in compensation for labor constitutes income. Only gain received in compensation for labor constitutes income.

Knies v. Richardson, 600 F.Supp. 763 (E.D.Wis. 1985):

Mr. and Mrs. Knies, representing themselves, filed suit against numerous State officials in connection with assessment of state income taxes against them. One of the issues they raised was whether the Wisconsin Department of Revenue unconstitutionally considered their wages as income. *Knies*, 600 F.Supp. at 764. The Court stated:

Wages are properly considered taxable under both state and federal law. *Kile v. C.I.R.*, 739 F.2d 265 (7th Cir. 1984); 21 [sic] U.S.C. Section 61(a);

Knies, 600 F.Supp. at 765.

As shown above at page 240, The *Kile/Granzow* Court relied entirely upon case law which lacks legal validity for the proposition that wages constitute income.

United States v. Latham, 754 F.2d 747 (7th Cir. 1985):

On appeal from conviction on two counts of failing to file income tax returns and four counts of filing false withholding allowance certificates, *Latham*, 754 F.2d at 749, among other issues, Mr. Latham contended that the District Court improperly refused his requested jury instruction defining “income” as distinct from “gross income.”

The Seventh Circuit stated:

As we stated in *Koliboski*, a claim of this nature is without merit. *Id.* at 1329 n. 1. Latham’s wages *were* and are income; thus, his proposed jury instruction was a misstatement of the law and the district court properly refused to adopt the same in the instructions. [Emphasis in original.]

Latham, 754 F.2d at 750.

Having relied entirely upon *Koliboski*, the *Latham* decision does not constitute legal precedent for the proposition that wages are income.

Peth V. Breitzmann, 611 F.Supp. 50 (E.D.Wis. 1985):

Mr. Peth, representing himself, filed a civil rights lawsuit under the provisions of 42 U.S.C. Section 1983 against several I.R.S. employees alleging the defendants conspired to deprive him of his property without due process of law. Among other arguments, Mr. Peth alleged that he was not a person liable to pay taxes under 26 U.S.C. Section 6001 because the tax imposed by Title 26 was not apportioned, and further alleged that he had earned no income because he received a paycheck for his labor equal to the fair market value of his labor, hence there was no taxable gain. *Peth*, 611 F.Supp. at 52-53.

The Court ruled against Mr. Peth as to both of his arguments; the first by citing to *Brushaber*, and the second by citing to *Granzow*. As discussed at page 240, the *Granzow* case does not support the proposition that wages constitute income.

Harris v. United States, 758 F.2d 456 (9th Cir. 1985):

Mr. Harris, representing himself, moved to quash I.R.S. administrative summonses on various grounds, one of which was that wages do not constitute income. He appealed the denial of his motion by the District Court. *Harris*, 758 F.2d at 457.

The Court cited to *Gattuso* (see p. 239), *Romero* (see p. 189) and *Buras* (see p. 187) to dispose of this issue. Those cases have been shown to not support the lower court's contention that wages do constitute income.

United States v. Overton, 617 F.Supp. 5 (W.D.Mich. 1985):

Mr. Overton was charged in an indictment with failure to file income tax returns and with income tax evasion. Representing himself, he moved to dismiss the indictment on several grounds, one of which was that he had incurred no gain from his labor which may properly be accounted as income. *Overton*, 617 F.Supp. at 6.

The Court denied Mr. Overton's motion citing to *Burton, Richards, Stillhammer, Lovell*, 579 F.Supp., *Koliboski* and *Glenshaw Glass*. As previously shown at pages 237, 223, 216, 231, 231 and 153 respectively, those cases do not support the Court's conclusion that wages constitute income.

Olson v. United States, 760 F.2d 1003 (9th Cir. 1985):

Mr. Olson filed an unsigned Form 1040 for 1982 on which he listed his wages as zero and cautioned that it was not a return. Attached to the Form 1040 was a W-2 Form showing payment of wages, on which he wrote "incorrect." He also attached a Schedule C profit or loss statement in which he offset the wages he received by a greater amount of "cost of labor" and other deductions incurred in earning his wages. He also attached a letter stating he had studied the tax laws and determined that he owed no taxes because he had not obtained any privilege from a governmental agency. He stated he filed the Form 1040 only to obtain a refund and not with the intent to file a return. *Olson*, 760 F.2d at 1004.

The I.R.S. attempted to have Mr. Olson sign the return, which he refused to do. Thereafter, the I.R.S. assessed a \$500 frivolous return penalty under Section 6702 of Title 26. Mr. Olson paid the required fifteen percent of the penalty and then filed a claim for refund. When the I.R.S. denied the claim for refund, he brought suit to recover the fifteen percent and to have the \$500 penalty abated. The District Court dismissed the suit, and Mr. Olson, representing himself, appealed. *Olson*, 760 F.2d at 1004-1005.

With respect to Mr. Olson's attempt to deduct his wages as the "cost of labor," the Court stated that the Court had repeatedly rejected the argument that wages were not income, citing to *Gattuso*, *Romero* and *Buras*. Those cases, analyzed at pages 239, 189 and 187 respectively, have been shown not to constitute legal precedent for the proposition that wages do constitute income.

Stelly v. C.I.R., 761 F.2d 1113 (5th Cir. 1985):

Upon receipt of a notice of deficiency from the I.R.S., the Stellys petitioned the United States Tax Court. The Tax Court dismissed their petition, and representing themselves, they appealed to the Fifth Circuit Court of Appeals. On appeal they argued that the Sixteenth Amendment only authorized taxes on "gain," not income,¹⁰⁹ asserting that compensation for labor was not gain because it was an even exchange. *Stelly*, 761 F.2d at 1114-1115.

In ruling that the income tax on wages was constitutional, the Court cited to numerous cases, all of which have been previously analyzed. See *Glenshaw Glass* (p. 159), *Eisner* (p. 137), *Brushaber* (see Chapters I and II), *Perkins* (p. 248), *Granzow* (p. 240), *Crain* (p. 242), *Funk* (p. 209), *Lonsdale* (p. 200), *Romero* (p. 189), *Broughton* (p. 186), *Francisco* (p. 183), *Russell* (p. 179) and *Porth* (p. 208). In addition, the Court cited to *Acker v. C.I.R.*, 258 F.2d 568 (6th Cir. 1958). That case challenged the constitutionality of the Internal Revenue Code on the grounds that:

(1) the rates are so high as to make the levy not a tax but a confiscation of property contrary to the Fifth Amendment to the Constitution, (2) the progressive rates are unconstitutional, and (3) the "income tax law considered as a whole in its excessive rates and arbitrary provisions is openly subversive of the fundamental philosophy of the Constitution of the United States and repugnant to its continued existence."

Acker, 258 F.2d at 574.

As none of these cases support the proposition that wages constitute income, so too, the *Stelly* case is not legal precedent for that proposition.

Hyslep v. United States, 765 F.2d 1083 (11th Cir. 1985):

Mr. Hyslep filed a 1982 Form 1040 on which he listed wages, and deducted, as an adjustment to income, the full amount of the wages received, claiming that he was a “source-exchanger,” and that therefore his wages were “non-taxable.” The I.R.S. assessed a \$500 frivolous return penalty, and Mr. Hyslep, representing himself, brought a civil suit to recover the penalty.

In ruling against Mr. Hyslep, the Court stated that Congress had defined income as including compensation for services in Section 61(a)(1), citing to *Lonsdale* and to *Simanonok*. As stated above, in Section 61(a)(1) Congress defined gross income as the gain derived from compensation for services, and neither the *Lonsdale* case (see p. 200) nor the *Simanonok* case (see p. 233) supports the legal proposition that wages constitute income.

Wheeler v. United States, 768 F.2d 1333 (D.C. Cir. 1985):

The *Wheeler* case was a consolidated case brought by Mr. and Mrs. Wheeler and Mr. and Mrs. McLaughlin who appealed an adverse decision of the Court of Claims for a refund of income taxes. Mr. Wheeler and Mr. McLaughlin were employees of the South Bend Tribune Corporation who entered into a college educational benefit plan agreement with Educo, Inc., which provided funds for the college expenses of the children of certain key employees. South Bend made the arrangement “for the purposes of retaining such present employees, of attracting future employees, and generally to increase employee loyalty to Employer.” Under the plan, annual payments were made to the children toward their college education. *Wheeler*, 768 F.2d at 1334.

The payments to the children were not included within the Wheeler's or the McLaughlin's respective tax returns, and the I.R.S. issued notices of deficiencies. The deficiencies were paid, and a suit for refund was filed. The Court of Claims dismissed the suit, and this appeal was brought. The Court of Appeals held that despite the fact that the payments were made to the children, the payments constituted income earned by the parents. *Wheeler*, 768 F.2d at 1334-1335. The Court stated:

Section 61 (a) of the Internal Revenue Code of 1954 defines gross income to include "compensation for services." This covers any economic or financial benefit conferred in any form on the employee unless it is specifically exempted by another section of the Code.

Wheeler, 768 F.2d at 1335.

As pointed out numerous times, Section 61(a) defines gross income as income derived from compensation for services. In any event, the case did not involve wages, and the case does not constitute legal precedent for the principle that wages are income.

***Biermann v. C.I.R.*, 769 F.2d 707 (11th Cir. 1985):**

Mr. Biermann, representing himself, appealed an adverse decision of the United States Tax Court. He argued, among other issues, that the monies he received should not be considered income because the Internal Revenue Code does not define "income," and that his wages were not income. *Biermann*, 769 F.2d at 708.

The Court ruled against Mr. Biermann on these issues without providing any legal analysis or citing to any case law. Accordingly, the *Biermann* case does not constitute legal precedent for the proposition that wages constitute income.

Connor v. C.I.R., 770 F.2d 17 (2nd Cir. 1985):

Mr. Connor appealed an adverse determination of the United States Tax Court, and representing himself, argued among other issues, that wages were not income but an exchange of property. He argued that since money was property and labor was property, his work for wages was a non-taxable exchange of property. Mr. Connor also argued that because wages were property, a tax on them was a property tax that had to be apportioned. *Connor*, 770 F.2d at 20.

The Court of Appeals ruled against these argument citing to *Schiff*, which, as shown at page 255, totally failed to provide any legal analysis of those issues. Neither *Schiff* nor *Connor* qualifies as legal precedent for the contention that wages constitute income.

Cameron v. I.R.S., 773 F.2d 126 (7th Cir. 1985):

Mr. Cameron, representing himself in both the District Court and the Court of Appeals, brought an action against the Internal Revenue Service seeking injunctive relief and damages for alleged bad faith of the I.R.S. in handling his case. Among other issues, he argued that wages were compensation for services rendered and hence not profits in the sense of windfalls. *Cameron*, 773 F.2d at 127.

As to this argument the Court stated:

This is true; wages—most wages anyway—are compensation, rather than windfalls; but the income tax is a tax on income in general, not just on windfall income.

Cameron, id.

Wages are compensation for services rendered, but the general tax on income taxes the gain derived from compensation for services, not the compensation nor the wages themselves, as has been

repeatedly shown. The Court did not cite any case law or other authority on this issue in its opinion, and therefore, *Cameron* does not suffice as legal authority for the proposition that wages constitute income.

Carter v. C.I.R., 784 F.2d 1006 (9th Cir. 1986):

Mr. and Mrs. Carter did not file income tax returns for the years 1980 and 1981. The I.R.S. issued notices of deficiency, and the Carters petitioned the United States Tax Court. Their petition was dismissed and they appealed. Mrs. Carter did not sign the notice of appeal, and her appeal was dismissed for lack of jurisdiction. *Carter*, 784 F.2d at 1007-1008. Mr. Carter, representing himself, argued that proceeds received for personal services could not be given a “zero-basis for the purpose of the assessment of taxation.” *Carter*, 784 F.2d at 1009.

The Ninth Circuit held that this argument was but a variation of the “wages are not income theme,” and ruled against Mr. Carter citing to *Olson*, *Gattuso* and *Romero*. *Carter*, *id.* As shown herein, neither *Olson* (see p. 259), *Gattuso* (see p. 239) nor *Romero* (see p. 189) constitutes valid legal precedent that wages constitute income. The *Carter* case totally failed to address the issue of the existence of Sections 1001 *et seq.* in attributing a zero-basis to labor, which the United States Supreme Court has held to constitute property.

Motes v. United States, 785 F.2d 928 (11th Cir. 1986):

Mr. Motes and several others sued for a refund of income taxes under the Tucker Act, 28 U.S.C. Section 1346, raising, among other issues, that their wages were not income subject to tax, that a tax on wages was a tax on their property (labor), and that they should be allowed to exclude from the amount of the wages they received the cost of maintaining their well-being. *Motes*, *id.*

The Court of Appeals rejected these arguments, without legal analysis, citing to *U.S. v. Goetz*, 746 F.2d 705 (11th Cir. 1984);

Simanonok, U.S. v. Vance, 730 F.2d 736, 738 (11th Cir. 1984); and *Melton v. Kurtz*, 575 F.2d at 547 (5th Cir. 1978). *Simanonok* has been shown at page 233 not to provide legal authority that wages constitute income.

In the *Goetz* case, two defendants were convicted of failing to file income tax returns. Both defendants had filed tax returns in which, rather than reporting an amount of income on the return, they claimed protection under the Fifth Amendment. *Goetz*, 746 F.2d at 707. The trial court instructed the jury that returns without financial information upon them were not returns and therefore the returns filed by the two defendants were not returns as a matter of law. *Goetz*, 746 F.2d at 708. In addition, the trial court refused to allow the defendants the opportunity to present to the jury the defense that they had claimed Fifth Amendment protection in good faith. *Goetz*, 746 F.2d at 710. The Court of Appeals held that the trial court committed error with respect to these two issues, and reversed the convictions. No issue as to whether wages constitute income was present in the *Goetz* case, and therefore the case does not support the contention that wages constitute income.

In the *Vance* case, Mr. Vance was convicted of failing to file income tax returns for the years 1977, 1978 and 1979, and appealed. On appeal he contended that the District Court committed error in refusing to conduct a pretrial *in camera* hearing on his claim of Fifth Amendment privilege, in improperly admitting certain evidence, and in improperly instructing the jury, and that his conviction should be reversed because he was the subject of selective or vindictive prosecution. *Vance*, 730 F.2d at 737. Only the second of these issues involved income, and that indirectly.

The Court stated:

Vance next contends that the district judge improperly admitted evidence showing that Vance earned a substantial amount of income for the years in question and thus was required to file tax returns.

Vance contends that this evidence was inadmissible under Rule 404 of the Federal Rules of Evidence. The evidence was clearly admissible in this case. First, the evidence was relevant to show that Vance had a duty to file tax returns for the years in question; thus, the evidence cannot be characterized as evidence of bad character or bad acts to prove that Vance acted “in conformity therewith on a particular occasion.” Fed.R.Evid. 404. In addition, the evidence was clearly admissible to show that Vance, because he had incurred a substantial tax liability, had a motive to file the inadequate returns and did not act in good faith under *Booher*, 641 F.2d at 220. See *Fed.R.Evid. 404(b)*.

Vance, 730 F.2d at 738.

The *Vance* case did not address what the specific evidence of income was, and did not involve the issue of whether wages constitute income. Accordingly, it is not precedent for the contention that wages do constitute income.

The *Melton* case was a civil lawsuit against numerous employees of the Internal Revenue Service in which Mr. Melton sought a declaration that certain federal tax statutes were unconstitutional and an injunction to prevent the Commissioner from assessing and collecting taxes from him. *Melton*, 575 F.2d at 548. The contentions raised by Mr. Melton were that: (1) the graduated or progressive income tax is unconstitutional because it denies taxpayers equal protection, *Melton, id.*; (2) the statutes establishing the Tax Court of the United States are unconstitutional, *Melton, id.*; and (3) he need not fill in the blanks on his federal income tax return because to do so would violate his Fifth Amendment rights, *Mel ton*, 575 F.2d at 549.

The *Melton* case, like *Goetz* and *Vance*, did not address the issue of whether or not wages constitute income.

Coleman v. C.I.R., 791 F.2d 68 (7th Cir. 1986):

The *Coleman* case was a consolidation of two appeals, one brought by Mr. Coleman, and one brought by Mr. Holder. Mr. Coleman petitioned the United States Tax Court and argued that wages do not constitute income. *Coleman*, 791 F.2d at 70. Mr. Holder was charged a \$500 frivolous return penalty, paid fifteen percent, and brought suit in District Court for a refund of the payment, also arguing that wages were not taxable. *Coleman, id.*

In ruling against Mr. Coleman and Mr. Holder as to these arguments, the Court cited to *United States v. Thomas*, 788 F.2d 1250 (7th Cir. 1986); *Lovell*, 755 F.2d; *Granzow*; *Koliboski*; and *Brushaber*. *Lovell* (see p. 256), *Granzow* (see p. 240), *Koliboski* (p. 234) and *Brushaber* (see Chapters I and II) have been shown not to legally support the contention that wages constitute income.

The *Thomas* case was an appeal from a conviction for failure to file returns and filing false withholding allowance certificates. The only issue with respect to wages not constituting income came about as follows:

Thomas testified before the grand jury that returned the superseding indictment. He presented his explanations for not paying taxes, including his belief that wages are not income and an assertion that “all individual income tax revenues are gone before one nickel is spent on the services which taxpayers expect from their government.” In response to questions asked by the prosecutor, Thomas conceded that he had received technical training paid for by the Navy, payment funded by taxes. Thomas maintains that the indictment should be dismissed because of these questions, which he says are improper; because the prosecutor failed to present the grand jury with exculpatory evidence (other than Thomas’s own testimony); and because the prosecutor advised the

grand jurors that Thomas's legal theories are incorrect.

Thomas, 788 F.2d at 1254.

The Court did not adjudicate the question of whether wages constitute income, and therefore the *Thomas* case does not provide legal precedent for that proposition.

Stubbs v. C.I.R., 797 F.2d 936 (11th Cir. 1986):

Mr. Stubbs, representing himself, appealed an adverse determination of the United States Tax Court. One of the issues Mr. Stubbs raised was the contention that wages do not constitute income. *Stubbs*, 797 F.2d at 938.

The Court of Appeals ruled against Mr. Stubbs on this issue citing to *Biermann*. As discussed above at page 262, the *Biermann* case is not legal precedent for the contention that wages do constitute income.

Colson v. United States, 67 B.R. 30 (1986):

Mr. Colson, representing himself, filed a petition to have his taxes discharged in bankruptcy. He filed an adversary complaint in which he argued, among other things, that wages do not constitute income. *Colson*, 67 B.R. at 32. The Court rejected this argument citing to *Stubbs*, which, as shown immediately above, does not support the contention that wages do constitute income.

Casper v. C.I.R., 805 F.2d 902 (10th Cir. 1986):

Mr. Casper, representing himself, appealed an adverse determination of the United States Tax Court in which he argued that wages do not constitute income. *Casper*, 805 F.2d at 904-905.

The Tenth Circuit sustained the Tax Court's determination that wages do constitute income citing to *Lawson, Rowlee, Connor*,

Lovell, 755 F.2d., *Perkins*, *Simanonok*, *Funk*, *Lonsdale*, *Romero*, *Wilson*, *Mendel*, *Woodall* and *Stelly*. Those cases have been shown at pages 206, 223, 263, 256, 248, 233, 209, 200, 189, 170, 166, 166 and 260 respectively not to be legal precedent for the contention that wages do constitute income.

Grimes v. C.I.R., 806 F.2d 1451 (9th Cir. 1986):

Mr. Grimes, representing himself, appealed the dismissal of his Tax Court petition. Mr. Grimes acknowledged the receipt of wages, which he referred to as “gross receipts,” but argued that he was constitutionally entitled to an exemption for expenditures to provide his family with the “American Standard of good living.” He contended that, applying this purported exemption, he owed no taxes as his “gross receipts” were “entirely consumed” in providing for his family. *Grimes*, 806 F.2d at 1452-1453.

The Court stated:

There can be no doubt that the tax on income is constitutional and that, for the purpose of the Sixteenth Amendment, income includes “gain derived from capital, from labor, or from both combined.” *Eisner v. Macomber*, 252 U.S. 189, 207 (1920). Sections 1 and 61 of the Internal Revenue Code impose a tax on income, and wages are income. See *Gattuso v. Pecorella*, 733 F.2d 709, 710 (9th Cir. 1984).

Grimes, 806 F.2d at 1453.

The *Grimes* Court correctly set forth that Section 61 of the Internal Revenue Code is constitutional and correctly defined income as a “gain derived from labor.” Section 61 does not, however, impose a tax; the tax is imposed in Section 1 on “taxable income.” The *Gattuso* case, (see p. 239) does not legally support the contention

that wages constitute income. Here again, an appellate court has ignored the very definition it cited.

McLaughlin v. C.I.R., 832 F.2d 986 (7th Cir. 1987):

Mr. McLaughlin appealed an adverse determination of the United States Tax Court. On appeal, and representing himself, he posed three arguments: (1) that his liability for federal income tax was contractual in nature and he had rescinded that contract; (2) that his religious scruples prevented him from “entering into contracts with the inhabitants of the land”; and (3) that he received no benefits from the state and therefore owed nothing to the state. *McLaughlin*, 832 F.2d at 987.

Mr. McLaughlin did not argue that wages do not constitute income; nonetheless, the Court stated:

Furthermore, case law in this circuit is well-settled that individuals must pay federal income tax on their wages regardless of whether they avail themselves of governmental benefits or privileges.

McLaughlin, id.

The Court cited to *Coleman* (see p. 267) and to *Lovell* (see p. 256) to support this contention. Those cases have been shown above not to constitute legal precedent for the contention that wages constitute income.

Wilcox v. C.I.R., 848 F.2d 1007 (9th Cir. 1988):

Mr. Wilcox, representing himself, appealed an adverse determination of the United States Tax Court. Among other issues, he contended that wages do not constitute income. *Wilcox*, 848 F.2d at 1008.

The Ninth Circuit stated that “wages are income” and cited to *Carter* as legal authority for its statement. The *Carter* case has been

shown above at page 264 to have not addressed the issue presented before the Court with respect to the proper method of determining gain/income. Having relied upon case law that does not constitute valid legal authority for the proposition that wages do constitute income, the *Carter* case is also not valid legal authority for that proposition.

ENDNOTES

83. 26 U.S.C. Section 6012 imposes a filing requirement on “individuals” who receive more than a certain amount of “gross income” per tax year.
84. The three elements of willful failure to file a tax return under Section 7203 are: (1) the defendant had a legal duty to file a tax return; (2) he failed to do so; and (3) he acted willfully. *United States v. Foster*, 789 F.2d 457, 460 (7th Cir. 1986).
85. See, “An Act to provide Internal Revenue to support the Government and to pay Interest on the Public Debt,” approved July 1, 1862, 12 Stat. 432, Ch. 119, Section 86 at 12 Stat. 472.
86. See *Cohens v. Virginia*, 6 Wheat. 264, 399; and *Pollock v. Farmer’s Loan & Trust Co.*, 157 U.S. at 574, for the principle that a case cannot be cited as controlling on a legal issue unless the legal issues in both cases are the same.
87. The Court also ignored the holding of the Supreme Court in *Eisner* that the three words—**income derived from**—must be given meaning in determining what is, and what is not, income (see p. 141).
88. The Court having stated that Mr. Amon did not brief this issue, it is unclear exactly what was or was not briefed.
89. The Court found that the stock constituted a gift and was not taxable. Thus, the mere presence of the employer-employee relationship does not mean that all things of value which pass between them constitute income.
90. The case actually commences on page 899, not on page 900.
91. The case actually commences on page 939, not on page 940.

92. See note 75.
93. It is interesting to note that a progressive tax upon individuals is the second plank of the *Communist Manifesto*.
94. *Butchers' Union Co. v. Crescent City Co.*, 111 U.S. 746,757 (concurring opinion of Justice Fields) (1883); *Coppage v. Kansas*, 236 U.S. 1, 14 (1914); *Adair v. United States*, 208 U.S. 161, 172 (1908).
95. A Schedule C is used to report Profit or (Loss) from Business or Profession (Sole Proprietorship).
96. This statement by the Court was only partially correct. On rehearing, the Supreme Court in *Pollock* determined a tax on income from all of an owner's real or personal property was a direct tax within the meaning of the Constitution. *Pollock*, 158 U.S. at 618.
97. See p. 130.
98. See the definition of "guise" at note 34.
99. It is interesting to note that the Court of Appeals read *Brushaber* as removing the requirement of apportionment from the "direct" income tax when *Brushaber* stated the purpose of the Sixteenth Amendment was to do away with the *Pollock* rule which caused the indirect income tax from being classified as a direct tax by considering the source of the income. Mr. Parker apparently correctly read *Brushaber*, and relied upon *Flint* for its definition of an excise tax to show that he was not engaged in any activity taxable as an excise.
100. The Supreme Court took some liberality with this sentence in that Section 22(a) merely defined "gross income"; it did not impose the tax in that section.

101. The issue before the Court in *Clifford* was whether the grantor, after a trust had been established, may still be treated under Section 22 as the owner of the corpus (see p. 193).
102. The issue before the Court in the *Midland Mutual* case was whether an amount of accrued interest was to be considered as gross income where a life insurance company, at a foreclosure sale, bid the principal of its mortgage loan plus accrued interest and took over the property in satisfaction of the whole debt without payment and repayment of any cash. *Midland Mutual*, 300 U.S. at 220.
103. The issue before the Court in the *Irwin* case was whether sums received by a beneficiary under a will which created a trust were taxable to the beneficiary. *Irwin*, 268 U.S. at 166.
104. The issue before the Court in *Jacobson* was whether the federal income tax applied to gains derived by a debtor from his purchase of his own obligations at a discount and his consequent control over their discharge (see p. 194).
105. The issue before the Court in the *Stockholms Enskilda Bank* case was whether interest paid upon the amount of a tax return to a foreign corporation fell within the classification of “interest on bonds, notes, or other interest-bearing obligations of residents, corporate or otherwise.” *Stockholms Enskilda Bank*, 293 U.S. at 86.
106. This case was consolidated with two others, *Basic Bible Church of America v. C.I.R.* and *Kile v. C.I.R.*
107. Goodrich, Smietanka, Eisner and Stratton’s Independence.
108. This was a wartime taxing act imposing, in Title I, a “normal” tax, and in Title II, in which section 201 (a) was located, a “war excess profits tax.”

109. Income is in fact gain, hence the Stellys were in error in setting forth their legal position.

CONCLUSION

The Sixteenth Amendment to the United States Constitution, proposed by Congress in response to the *Pollock* decision, authorized an unapportioned direct tax on income. Income has been defined by the United States Supreme Court to be a profit or gain derived from various sources, such as labor and capital. A tax directly on the source is a direct tax, and must still be apportioned. A tax on the income derived from the source need not be apportioned. Labor, the labor contract, and the right to sell labor have all been held by the Supreme Court to constitute property. The procedure to determine if there is a gain derived from the sale of this property has been set forth by Congress. Gain is derived only if one receives over and above the fair market value of the cost of the property. These basic principles are simple to state and simple to apply. They also lead to one inescapable conclusion:

WAGES DO NOT CONSTITUTE INCOME

I want to emphasize that I do not purport to state that the income tax law is itself unconstitutional. Thus if one has legal status as a “taxpayer” and has the threshold amount of “gross income,” that “individual” would have a legal obligation to file a return and to pay the taxes, if any, shown on the return. However, filing requires the use of a form prescribed by the Secretary of the Treasury. That form is the Form 1040. Since the Internal Revenue Service administers the tax as a gross receipts tax as opposed to an income tax, one cannot fill out the form in a manner that both complies with the law and complies with the Internal Revenue Service’s administrative policy. A Form 1040 filled out and filed based on the concept that wages do not constitute income would most certainly be classified as a frivolous return by an Internal Revenue Service employee, and the filer would be classified as an “illegal tax protester.” Such an administrative classification, made without affording one an administrative hearing or judicial review, is inherently illegal as a

denial of due process of law. Of course, long ago, Chief Justice White held that Americans have no due process rights with respect to taxation.

In addition, once a return is classified as frivolous, it is deemed by the Internal Revenue Service not to be a return, it is not assigned a document locator number, and the now non-return is sent to the Criminal Investigation Division for analysis of recommendation for criminal prosecution for the violation of one or more of the following statutes: Sections 7201, 7203, 7206 or 7207. (See Trial Transcript, pages 59-60, *U.S. v. Burkhardt*, 3-82-Criminal-38, United States District Court, District of Minnesota, Third Division, July 19, 1982.)

This is a classic example of when a valid claim under the Fifth Amendment right not to be a witness against one's self should be made if one does not want to waive that right. The Supreme Court in *Garner v. United States*, 424 U.S. 648 (1976), stated:

The information revealed in the preparation and filing of an income tax return is, for Fifth Amendment analysis, the testimony of a "witness" as that term is used herein.

Garner, supra at 662-663.

The Supreme Court case of *Sullivan v. United States*, 274 U.S. 259 (1927), stated that if one wanted to raise an objection to a particular question when filling out a personal income tax return, one had to raise the objection on the return, but could not refuse to file any return at all.

The Internal Revenue Service, however, takes the position that returns claiming Fifth Amendment objections are also frivolous, with the same results as outlined above. Thus under current United States Government procedure, the exercise of Fifth Amendment rights leads to criminal prosecution. Additionally, any return filed

with the Internal Revenue Service can be used against the filer under the Internal Revenue Code itself, Section 6103(i). This atrocious result was achieved by Federal Judges such as the dishonorable Learned Hand, who while disobeying his oath of office to uphold the Constitution of the United States, declared:

Logically, indeed, he (the taxpayer) is boxed in a paradox for he must prove the criminatory character of what it is his privilege to suppress just because it is criminatory. **The only practicable solution is to be content with the door's being set a little ajar, AND WHILE AT TIMES THIS NO DOUBT PARTIALLY DESTROYS THE PRIVILEGE, ... nothing better is available.** [Emphasis added.]

United States v. Weisman, 111 F.2d 260,
262 (1947).

The only practicable solution for Judge Hand was to declare the requirement of filing an income tax return to be unconstitutional as repugnant to the Fifth Amendment. This result is mandated by *Marbury v. Madison*, 5 U.S. 137, 180 (1803) and the only result conceivable under law if the United States Constitution is indeed the Supreme Law of the Land. However, and despite the fact that in the landmark case of *Miranda v. Arizona*, 384 U.S. 436, the Supreme Court stated:

The Fifth Amendment provision that the individual cannot be compelled to be a witness against himself cannot be abridged.

(and)

Where rights secured by the Constitution are involved, there can be no rule-making or legislation which would abrogate them.

Miranda, supra.

the federal courts refuse to comply with law as evidenced by the decisions analyzed in the preceding chapters.

The *Sullivan* Court recognized that some conditions might exist requiring the “extreme and extravagant” position that the Fifth Amendment allows one otherwise required to file a return to file no return at all. Inasmuch as the federal government openly admits by statute that returns can be used against the person in any civil or criminal matter, and inasmuch as claiming Fifth Amendment protection on a tax return leads to criminal prosecution, it is my opinion that the conditions mentioned in *Sullivan* now clearly exist, and the nonfiling of returns is justified as protected under the Fifth Amendment.

You must be cautioned that not filing a return with the Internal Revenue Service could result in the imposition of civil penalties and/or the recommendation for criminal prosecution. This illegal conduct on the part of our Executive Department of government is yet but another in a long line of abuses, similar to those which resulted in the Declaration of Independence. It is nonetheless my contention that provisions contained in the United States Constitution, together with decisions of the United States Supreme Court, fully support the legal conclusion that wages do not constitute income as shown in previous chapters, and reinforce the position that the Internal Revenue Service is violating the law in its administration of the personal federal income tax, with the full consent of our federal judiciary.

I have endeavored in this book to set forth the true law with respect to the federal personal income tax. What any American chooses to do with that knowledge is a matter of choice.

APPENDIX A

UNITED STATES DISTRICT COURT

DISTRICT OF ALASKA

U.S.A.)	Case No. A87-43CR
)	
Plaintiff,)	Anchorage, Alaska
)	Thursday, February 4, 1988
vs.)	9:00 a.m.
)	
CARL BEERY,)	
)	
Defendant.)	
<hr/>		

VOLUME III
 TRANSCRIPT OF TRIAL
 BEFORE THE HONORABLE H. RUSSEL HOLLAND
 JUDGE, UNITED STATES DISTRICT COURT, and a jury

APPEARANCES:

For the Plaintiff:

NEIL EVANS, Esq.
 MARK DAVIS, Esq.
 701 C Street, Box 9
 Anchorage, Alaska 99513
 (907) 271-5071

For the Defendant:

JEFFREY DICKSTEIN, Esq.
 P.O. Box 7306
 Missoula, Montana 59807

CROSS EXAMINATION OF
SPECIAL AGENT KNUTSON

BY MR. DICKSTEIN:

Q Sir, you indicated that it was your function to examine tax returns?

A That's correct.

Q And where are the tax returns for Mr. Beery?

A To my knowledge, none were filed.

Q You didn't examine tax returns in this case, did you?

A I received the information from the special agent.

Q And you didn't examine tax returns in this case, did you?

A No.

Q Isn't it true that the Code of Federal Regulations limits you to the examination of tax returns?

MR. EVANS: Objection—

THE COURT: Sustained.

MR. EVANS:—foundation.

May I see what you're handing the witness, please?

MR. DICKSTEIN: It's Exhibit T, you have a copy.

(Defendant Exhibit T was thereupon marked for identification.)

BY MR. DICKSTEIN:

Q Sir, do you recognize Defendant's Exhibit T?

MR. EVANS: Objection, Your Honor. He's handed what appears to be a portion of—

MR. DICKSTEIN: Treasury regulations which describe this man's job function.

THE COURT: Is that the only purpose of this exhibit?

MR. DICKSTEIN: No, its purpose is to show that this man violated numerous rights in the computation of this tax, that this isn't the correct tax determination because Mr. Beery was afforded none of his due process rights in this determination, which is coming in as a final—

THE COURT: Just a moment, sir. I've allowed this witness to testify as an expert witness to a tax computation. You may cross-examine him on that tax computation.

MR. DICKSTEIN: I am, sir, the illegality of the tax computation under the regulations that describes this man's conduct and the due process rights that are supposed to be afforded to Mr. Beery.

MR. EVANS: Your Honor, if we're going to have argument regarding the law—

THE COURT: Well, we aren't going to have any more argument.

MR. DICKSTEIN: I will request the Court to take judicial notice of the Code of Federal Regulations put out by the Treasury Department, 26 C.F.R. Section 601.105.

THE COURT: For purposes of jury instructions, I may very well take a look at that.

MR. DICKSTEIN: No, for purposes of cross—

THE COURT: For purposes—

MR. DICKSTEIN:—examination of this witness as to his testimony, Judge.

THE COURT: For the purpose of cross-examining this witness, I do not see any relevancy of this document and it—

MR. DICKSTEIN: Well, let me develop the relevancy, Judge.

THE COURT: Go ahead, if you can.

BY MR. DICKSTEIN:

Q Are you familiar with these regulations, sir?

A Yes.

Q These are the regulations that govern the examination of returns, are they not?

A All right. Now —

THE COURT: Now, stop right there, Mr. Dickstein. This witness isn't here for the purpose of examining a tax return and you will not inquire any further into this subject.

MR. DICKSTEIN: The lack of a tax return is a prerequisite to the prosecution of Mr. Beery, sir. The secretary is required under Section 6020(b)(1) to prepare the return—

THE COURT: Stop.

MR. DICKSTEIN:—and that return—

THE COURT: Stop.

MR. DICKSTEIN: - goes to him.

THE COURT: Stop. No more argument in front of the jury on this point. I've ruled. Ask another question.

MR. DICKSTEIN: Then, can we have a sidebar so I can argue to Your Honor?

THE COURT: You may argue to me on this legal aspect later, when we've set up the jury instructions.

MR. DICKSTEIN: Then it's too late because I can't cross-examine him under the law, Judge.

THE COURT: You may cross-examine on anything that he was asked on direct examination.

MR. DICKSTEIN: This is what he was asked. He computed the liability. I want to see if he afforded Mr. Beery due process. Under *Mendoza-Lopez*, we're entitled to go into that at the time of trial.

THE COURT: Mr. Dickstein, enough of this argument. Ask another question, if you've got one.

BY MR. DICKSTEIN:

Q Well, I've got one question. Sir, where in the Internal Revenue Code, and will you please show us where it says Mr. Beery is a taxpayer?

MR. EVANS: Objection.

THE COURT: Sustained.

BY MR. DICKSTEIN:

Q Are you aware of any such section in the code which identifies Mr. Beery as a taxpayer?

MR. EVANS: Objection.

THE COURT: Sustained.

BY MR. DICKSTEIN:

Q Sir, you made the assumption, did you not, that wages constitute income?

MR. EVANS: Objection.

THE COURT: I'll allow that question.

THE WITNESS: Okay, Yes,

BY MR. DICKSTEIN:

Q And where in the Internal Revenue Code, if anywhere, does it establish that wages are income?

MR. EVANS: Same objection.

THE COURT: Sustained. I will be instructing on that subject.

MR. DICKSTEIN: We know, Judge.

BY MR. DICKSTEIN:

Q In making your computations you use the word here “statutory gross income,” do you not?

A Yes.

Q All right. You also use the word “adjusted gross income,” do you not?

A Correct.

Q And you also use the word “taxable income,” do you not?

A Correct.

Q Now, the words “gross, adjusted and taxable” are all adjectives defining the word income, aren’t they, they’re different types of income?

A That’s correct.

Q And isn’t it true, sir, that the word “income” is not defined anywhere in the Internal Revenue Code?

MR. EVANS: Objection.

THE COURT: Sustained.

BY MR. DICKSTEIN:

Q Do you know whether the word “income” is defined in the code?

THE COURT: Whether he knows or not doesn’t matter, counsel. You don’t need to answer that question.

MR. DICKSTEIN: No, and we don’t need a trial either, Judge. May we have a two- or three-minute recess so I can cool down, please?

THE COURT: Yes, we’ll be in recess for five minute, ladies and gentlemen.

MR. DICKSTEIN: Thank you, Judge.

(Brief recess.)

(Jury in at 11:32 a.m. Call to order of the Court.)

THE COURT: Mr. Dickstein?

MR. DICKSTEIN: All right, sir.

BY MR. DICKSTEIN:

Q Now, on the form you use the term “statutory gross income,” is that correct?

A That’s correct.

Q And that's statutory gross income under the Internal Revenue Code?

A That's correct.

Q In fact, all of your computations were based upon your interpretation of the Internal Revenue Code, is that correct.

A That's correct.

MR. DICKSTEIN: Your Honor, at this time I move for the admission of the Internal Revenue Code of 1981 into evidence.

THE COURT: No, sir.

MR. DICKSTEIN: All right. I move for the admission of Section 61, which is the statutory definition of gross income.

THE COURT: I will instruct on it if it's appropriate.

MR. DICKSTEIN: I move for the admission of Section 63, which defines taxable income.

THE COURT: Mr. Dickstein, if this litany needs to go on, I will consider all of your requests for instructions at the appropriate time, which will be a little later.

MR. DICKSTEIN: Yes, sir. I believe for the record I have to at least offer these things into evidence so they can be reviewed at a later time.

THE COURT: No, sir, you do not have to do it at this time. You were to file your proposed instructions earlier, which I believe you did, and we will settle up instructions and take your exceptions to them on the record before the instructions are read to the jury and that's where you preserve your right to appeal on the question of jury instructions.

MR. DICKSTEIN: I'm not referring to jury instructions. I am referring to exhibits that go to the jury Judge.

THE COURT: And what you are requesting me now will not put in exhibit form to the jury. If they are used, they will be used in instructions.

MR. DICKSTEIN: All right. Are you specifically instructing me not to list the exhibits that I would like to have admitted into evidence at this point in time?

THE COURT: No, sir. I am instructing you not to request me to take judicial notice of any further statutory provision at this time.

Do you have further cross-examination for this witness?

MR. DICKSTEIN: Yes, sir, I do.

BY MR. DICKSTEIN:

Q Sir, you indicated that the special agent gave you a bunch of exhibits and told you to compute income—or compute the taxable income?

MR. EVANS: Objection, I think he's mischaracterizing the testimony. Perhaps he could ask him where he got the figures from.

THE COURT: Would you rephrase the question, please?

MR. DICKSTEIN: Yes.

BY MR. DICKSTEIN:

Q From where did you get the figures to use in your computations?

A I received them from the special agent.

Q All right. Now, did you conduct an audit in computing these—this alleged tax due and owing?

A I did not do an audit.

Q You just took those figures for face value?

A With the exception of reconciling them. Like the W-2 income, I verified that those amounts were correct.

Q And how did you verify that those were the correct amounts?

A I saw copies of the W-2s.

Q All right. Now, sir, what section, if any, did you rely upon in determining which tax tables—did you apply tax tables to this?

A Which one are you referring to—well, basically, I applied tax tables only to 1983 because of the—the amount that was taxable, the tax tables weren't—the taxable income was more than the tax tables for 1981, or 1980, 1981 and 1982.

Q All right. You had to rely on something, though, to figure out the tax, right?

A The tax rate schedules, yes.

Q And that's contained in Section 1 of the code?

A That's correct.

Q And that imposes a tax on individuals, does it not?

A Yes.

Q And have you ever done any research into what the word “individual” means?

MR. EVANS: Objection as to relevancy.

MR. DICKSTEIN: The relevance is whether or not Mr. Beery is an individual as defined in the Internal Revenue Code. We submit he’s not, Judge.

MR. EVANS: We’ve already heard testimony from Ms. Vest that as far as the IRS is concerned an individual is somebody with a social security number that is kept in a record at the service center in Ogden, Utah.

THE COURT: I’ll sustain the objection.

MR. DICKSTEIN: And my objection, Judge, is we’ve heard from the IRS but we’re not getting the other side of the story out. We can prove Mr. Beery is not a taxpayer if you’ll let us do that, Judge.

THE COURT: The objection—

MR. DICKSTEIN: I’m asking for that right.

THE COURT: The objection has been sustained.

MR. DICKSTEIN: I understand that.

BY MR. DICKSTEIN:

Q Sir, please turn to page 95—I'm sorry, Exhibit 95. Now, under this figure of interest income that you have—

A Yes.

Q —in computing this were you aware that half of the payments that this represents was to the original purchaser or the original owner of the property?

A No, I was not.

Q That would have been something that would have been brought to your attention had an audit been conducted, wouldn't it?

A Very possibly.

Q And if Mr. Beery had knowledge that this was your contention, he could have come in and told you otherwise, couldn't he?

A That is correct.

Q That's what an audit process is about, isn't it?

A Right.

Q And he's had no opportunity to do that in this case, has he?

MR. EVANS: Objection.

THE COURT: Overruled.

THE WITNESS: Are you speaking to me, at my personal attempts to contact him, or are you speaking from what I understand the service tried to contact him?

BY MR. DICKSTEIN:

Q No, I'm talking about—well, let's do both. Did you try to personally contact him?

A No.

Q You were instructed not to, weren't you?

A No.

Q Then, why didn't you?

A The attempts, from my understanding, numerous attempts were made and nobody was able to contact him.

Q Oh? And from where did you get this understanding, sir?

A Just in discussions.

Q With whom?

A The special agent.

Q And when did the special agent tell you that she had attempted to contact Mr. Beery?

MR. EVANS: This is getting beyond the scope of direct. It has nothing to do with his computation of the taxes. He's testified he was given figures by the special agent.

THE COURT: Sustained.

BY MR. DICKSTEIN:

Q What are capital gains?

A Capital gains is normally sale of capital assets which have been held more than, it used to be six months and then 12 months and—

Q What's—

A If they're sold at a gain, they get preferential tax treatment.

Q In fact, gain is what income is, isn't it? If you sold it at a loss, you wouldn't tax it, would you?

A No.

Q And if was a mere equal exchange of property it wouldn't be taxed either, would it?

A If it's a qualified exchange, no.

Q Okay. If I gave Mr. Evans a book worth \$10 and he gave me a book worth \$10, there wouldn't be a taxable—that wouldn't be a taxable event, would it?

MR. EVANS: First of all, that would never happen. Second of all, this is irrelevant.

THE COURT: Sustained on your relevancy side.

MR. EVANS: Thank you.

MR. DICKSTEIN: Here, let me give you this, Mr. Evans.

BY MR. DICKSTEIN:

Q Sir, in computing a gain, don't you have to know what the value of the property was originally?

A That's correct.

Q And that's known as basis, isn't it?

A That's correct.

Q And how is basis determined?

A Basis would be your cost, plus any improvements, plus the purchase costs, less—if it's depreciable property, then it would be less any depreciation claimed while you held the property.

Q All right. Cost is basically what's known as fair market value, isn't it?

A Cost and fair market value can differ.

Q In what way?

A Well, if you got a bargain purchase, maybe fair market value would exceed cost. Cost is cost.

Q Don't you often determine fair market value by virtue of the contract which the property was purchased for?

MR. EVANS: Does this relate—I don't think this relates to the computation of his figures.

MR. DICKSTEIN: It goes to the computation of capital gains, Judge.

THE COURT: Well, if you would clarify something for me, Mr. Dickstein, through a question. I don't see where fair market value comes into the computation. If it does—

MR. DICKSTEIN: I'm trying—

THE COURT:—then there may be some relevancy to what you're asking.

MR. DICKSTEIN: I'm trying to ascertain what basis this gentleman gave to the property to determine the amount of the capital gain.

THE COURT: Fine, you may ask him that.

THE WITNESS: Okay, basically, I received the numbers, like I stated before, and it's my understanding that Mr. Beery bought these two lots for \$32,000, and we assigned or it was—this was done initially, I guess, by the other, the prior agent, they assigned a \$16,000 cost to each lot.

BY MR. DICKSTEIN:

Q All right. Now, those figures came off the sales contracts, didn't they?

A That's my understanding, they would.

Q And that's what's known as an arm's-length transaction between the buyer and the seller?

A Correct.

Q Okay. And then you computed how much more than what the cost was when it was sold, is that correct?

A Well, to that \$16,000, Mr. Beery put in a sewer system which had been capitalized and was depreciated. On lot—on one of the lots he placed—he purchased a trailer house that was—depreciation was allowed on, it was a five-year life, with a salvage of 2200, and it was

down to 2200 in the year of—before it was sold. So, that was the basis of the trailer. But the land cost remained 16,000.

Q Now, these procedures for determining gain are actually set forth in the Internal Revenue Code, aren't they?

A That's correct.

Q And you followed those procedures, didn't you?

A That's right.

Q Okay. Now, will you tell the jury what the cost of Mr. Beery's labor was and what basis you assigned to that?

MR. EVANS: Objection. We're not talking about the computations.

THE COURT: The question was the cost of Mr. Beery's labor?

MR. DICKSTEIN: The basis of his labor for the purposes of determining gain, which is what the income tax is all about.

THE COURT: You may answer the question if you understand it.

THE WITNESS: Well, the way I understand it, personal services would not increase my basis unless I reported income from it. For example, on charitable contributions, I can get a deduction for my out-of-pocket costs for the charity, but if I go down and work as a cement worker or a carpenter and the value of my services are 20 bucks an hour, I don't get a deduction for my time. The only way I would is if the charitable organization paid me the 20 bucks and I picked it up in income, then I've got—and then I said “Here's your money back,” but then I've got income, it's offsetting and there's no tax effect.

BY MR. DICKSTEIN:

Q That's right, because you've got the value of the labor—

A I'd have—

Q —in direct exchange for what you were paid and there's no profit or gain there, is there, it's an equal exchange?

A Well, there wouldn't be an equal exchange unless I gave my pay back to the charitable organization.

Q So, the value of your time is zero?

A So, the value turns out, for basis purposes, it would be zero.

Q And do you get paid a salary for what you do?

A Pardon?

Q Do you get paid a salary?

A I don't know what you're directing it at now, maybe—I think—

A Of my labor, okay.

MR. EVANS: This is irrelevant.

THE COURT: Sustained.

MR. DICKSTEIN: No, it's extremely relevant, Judge, because we're misconstruing the provisions of the code that deal with the amount of gain from property, and the Supreme Court has defined labor as property.

THE COURT: Not for purposes of this case, sir.

MR. DICKSTEIN: For any purpose, Judge.

THE COURT: No, not for purposes of this case.

MR. DICKSTEIN: Well -

THE COURT: You may ask another question.

BY MR. DICKSTEIN:

Q Sir, in your direct examination you used the term "sources of income," did you not?

A That's correct.

Q And what's the difference between a source of income and income?

A Well, in sources of income, I refer to wages, interest income, there are different types of income. So, a source would be just a generic term covering all sources and like interest income is interest income and capital gains income would be capital gains income.

Q Well, the source of interest income would be money sitting in the bank, wouldn't it?

A Well—

Q For example—

A —in this case, it's a contract. So, it's not really money sitting in the bank, it's payments being made.

Q And the tax isn't imposed on the source, is it, it's imposed on the income derived from the source?

A The one receiving the money, right, the beneficiary of the money is taxed.

Q The income from the source, right?

A Right.

Q That in fact is what Section 61 talks about, right, gross income from whatever source derived?

A That's correct.

Q Right. And that's the profit or gain derived from the source, isn't it?

A Correct.

Q And the source of his wages was his labor, wasn't it?

A His labor produced the source. The way I would interpret it, the source would be his employer who paid him the money, that is where the money came from and he exchanged his services for money.

Q Exactly. Thank you, sir.

APPENDIX B

IN THE UNITED STATES DISTRICT COURT

SOUTHERN DISTRICT OF INDIANA

EVANSVILLE DIVISION

UNITED STATES OF AMERICA,)

PLAINTIFF,)

v.)

No. EV 87-20 CR

JAMES I. HALL,)

DEFENDANT.)

CROSS EXAMINATION OF SPECIAL AGENT SHAFFNER

PARTIAL TRANSCRIPT OF PROCEEDINGS

The following proceedings took place during a Jury Trial in the above entitled cause on Thursday, April 21, 1988 in Evansville, Indiana, before the Honorable Gene E. Brooks.

APPEARANCES:

For the Government:

Mr. Larry Mackey
Mr. Robert Barnes
Assistant U.S. Attorneys
U.S. Courthouse - Room 500
Indianapolis, Indiana 46204

For the Defendant:

Mr. Jeffrey A. Dickstein
Post Office Box 7306
Missoula, Montana 59807

PATRICIA A. SHAFFNER

being first duly sworn testified as follows:

CROSS EXAMINATION BY MR. DICKSTEIN:

Q Mrs. Shaffner, you have a Bachelor's and a Master's Degree in Language?

A Yes, sir.

Q Is it safe to assume then that you are fairly knowledgeable about grammatical patterns and the placement of words?

A Yes, sir.

Q Would it be fair to say that the meaning of specific words are important for understanding sentences?

A Yes, sir.

Q And that some words may have different meanings?

A I'm sorry - I am not sure that I understand.

Q Isn't it true that a word might have a different meaning depending upon how it is used in a sentence?

A That would be true.

Q Now, you indicated that you have a 4.0 grade point average—

A —Yes, sir.

Q For your CPA Courses?

A Yes, sir.

Q What was your grade point average for your Bachelor's courses?

A 3.7.

Q All right. And your GPA for your Master's courses?

A 3.9.

Q So, you did fairly well in school?

A Yes, sir.

Q Now, you indicated in your Unit One training that you were taught how to interpret the Code and Regulations. Is that correct?

A That's correct.

Q Tell the Jury what it means to interpret a code section?

A Sometimes it is difficult to understand exactly what the Code means by the words that are used in a particular section. Therefore, we are instructed as to how to research that to the final point of understanding it. For example, if something in the Code needs to be explained by going to the Treasury Regulations, and it is really interpreted in terms of the facts that were presented here and how the Code would apply—to those particular facts.

Q Now, you might not only go to the regulations for an interpretation, but you might also have to go to decisions of the United States Supreme Court. Isn't that true?

A That would be true when we are trying to determine how the code would apply to a particular set of facts.

Q Or even to a particular person?

A It would be the facts that we would be trying to apply to the code, not to the person.

Q You make no interpretation then as to who is or who isn't a taxpayer? Is that what you are telling this Jury?

A We make that determination but I guess I considered that we made that determination on the facts and circumstances surrounding that person - not just based upon who that person is. I guess that I misunderstood you.

Q All right. That is known as “status”, isn’t it, to determine whether a person is or isn’t a taxpayer.

A I guess you could say that.

Q You have the regulations there, do you not?

A Yes, sir, I do.

Q Will you look at 26 C.F.R. 602.101, please?

A Would you say that again, please?

Q I’m sorry - It’s 601.201.

THE COURT: 601.201?

MR. DICKSTEIN: Yes, sir, I’ll apologize in advance this time.

A 601.201 - I don’t have that cite.

MR. DICKSTEIN: May I approach the witness, Your Honor?

THE COURT: Yes.

Q (By Mr. Dickstein) I would like to hand you what has been marked as Defendant's Exhibit "AX". Do you recognize that as a regulation of the Treasury Department?

A No, sir, I don't.

Q You have never seen this?

A No, sir, I haven't.

Q So, there are numerous regulations that you haven't seen. Is that correct?

A If this is a Treasury Regulation—I have not seen it. Obviously, there would be regulations that I have not seen.

Q You have seen Regulation 601.105, haven't you?

A No, sir, I haven't.

Q Now, you were in the Audit Division for a while?

A Yes, sir, the Examination Division.

Q And you are not familiar with the regulations dealing with the examination of the returns?

A Sir, according to the regulations that I have in front of me, anything under 601. would have to do with bank affiliates.

Q With what?

A Bank affiliates.

Q I would like to hand you what has been marked as Defendant's Exhibit "B", Mrs. Shaffner. I would ask you to take a look at that please?

MR. DICKSTEIN: Let the record reflect that Defendant Exhibit "B", is Treasury Regulation 26 C.F.R. 601.105.

Q (By Mr. Dickstein) Mrs. Shaffner, would you please read the title of that?

A Yes—"Examination of returns and claims for refund, credit, or abatement; determination of correct tax liability."

Q Now, you examine returns, don't you?

A Yes, sir.

Q And you determine correct liability?

A Correct.

Q And you have never seen your own departmental regulation for those purposes?

A I have seen the regulations, but apparently, we may have a numbering system different—I am sure that I have seen the regulations, but not by this particular number.

Q Find them in your own regulations, if you can, please? To the best of my knowledge, they are 26 C.F.R. - 601.

A I want to explain that our regulations—the way that we have them printed, the first number in it is based upon the code section to which it relates, and 601. code section refers to a special deduction for bank affiliates.

Q In fact, the first number of parts are contained in the code of Federal Regulations, aren't they? For example, the regulations dealing with the Internal Revenue Codes - with Section 1 of the Internal Revenue Codes in Part One of the Code, Federal Regulations. That is why it is 1.1-1, pertaining to Section 1 of the Code?

THE COURT: Now, wait a minute, I think we are talking about two sets of books. She has a book, called “Federal Regulations”, and you are talking about C.F.R. You are talking

about a different set of books. She has one set of books, and you have another one.

MR. DICKSTEIN: They are different titles, Judge, but Treasury Regulations are contained in the Code of Federal Regulations.

THE COURT: How about the numbering system?

MR. DICKSTEIN: The numbering system should be the same in terms of regulations.

THE COURT: They should be, but apparently, they are not.

Q (By Mr. Dickstein) Now, you talked about the code sections, for example, like the regulations for Section 3401.

A Yes, sir.

Q That is preceded by a number 31, isn't it?—That is 31.3401?

A Yes, sir, it would be.

Q And regulations like Section 1 of the Internal Revenue Code is 1.1 something, isn't it?

A Yes, sir, that would be correct.

Q Doesn't the One (1.) mean a part of the regulations—that's the part number?

A Yes, sir.

Q And 601. is part 601. of the Code of Federal Regulations?

A It is still a different number system, sir, and that is why I am having difficulty in finding your cite. That is not the same number that we are accustomed to research.

Q You have looked at your regulations for examination of returns and determinations of correct tax liability. Is that your testimony?

A Yes, sir.

Q Did you turn to pages right after that to get the next regulation, called "Rulings and Determination Letters?"

A Yes, I see it on yours, but I am at a loss finding it because your system is very different. I'm sorry, but I am accustomed to researching these particular regulations or the regulations of the C.P.A., and not under C.F.R.

Q The Code of Federal Regulations is the official Treasury Regulations, aren't they?

A Yes, sir.

Q They are the ones that have been codified?

A Yes, sir, that's correct.

Q All right, then you are not using the official volume?

A I am using the regulations but I am using them in a form that is more easily accessible for me, because that is important to my job.

Q All right. But it is not the official volume, is it?

A If what you are saying is correct, that would be correct, yes.

Q Would you examine 601.105 which I have handed you, Defendant's Exhibit "B". Despite the difference in numbering, will you see if those aren't, in fact, the regulations that pertain to your job in auditing returns and determining correct liability?

A Without reading all of them, sir, they would appear to be so.

Q All right. Do you deny that it is the policy of the Internal Revenue Service to answer inquiries of individuals as to their status for tax purposes and as to the tax affects of their acts or transactions?

A I'm sorry. Will you repeat that question?

Q Yes. Do you deny that it is the practice of the Internal Revenue Service to answer inquiries of individuals as to their status for tax purposes and as to the tax affects of their acts or transactions?

MR. MACKEY: Objection, Judge, as to relevancy.

THE COURT: What is the relevancy?

MR. DICKSTEIN: The relevancy, Judge, is the fact that this client was not given any opportunity to explain his tax determination or status as a taxpayer and the I.R.S. has not made such a determination, despite the fact that it is their policy.

THE COURT: Objection is sustained.

MR. DICKSTEIN: Judge, I would ask the Court to take Judicial notice of Defendant's Exhibit AX, please?

THE COURT: Judicial notice of it?

MR. DICKSTEIN: Judicial notice, yes, sir, of the Code of Federal Regulations, 26 C.F.R. Section 601.201.

MR. MACKEY: The same objection that was made yesterday, Your Honor, regarding portions of the regulations.

MR. DICKSTEIN: Could I have a ruling, please?

THE COURT: You have already got it.

MR. DICKSTEIN: The Court is refusing to take judicial notice of 26 C.F.R. 601.201?

THE COURT: I don't know of any reason to take judicial notice of it.

MR. DICKSTEIN: The decision under United States vs. Mendoza- Lopez.

THE COURT: I just don't think it has any relevancy in this case.

MR. DICKSTEIN: All right.

Q (By Mr. Dickstein) Now, you testified—well, let's go back a little bit. You also told the Jury that in Unit One, you learned how to interpret regulations. Is that correct?

A Yes, sir, that's correct.

Q So, sometimes you have to go to the regulations to determine the meaning of a Statute?

A That is correct.

Q Sometimes you have to go somewhere else to learn how to interpret a regulation?

A As it applies to a particular set of facts, yes, sir.

Q Now, when was the first time that you read the regulation 1.1-1, which you testified to yesterday?

A That probably would have been in 1979, when I first came on board. That's the best that I can remember, about 1979.

Q Would you look at that section again, please?

THE COURT: What section?

MR. DICKSTEIN: 26 C.F.R. 1.1-1.

A Yes, sir.

Q Now, under sub-paragraph C, does it tell who a citizen is?

A Yes, sir, it does.

Q There are two parts to that, isn't there?

A I don't see that it is separated distinctly into two parts.

Q It's "born or naturalized in the United States?"

A I understand what you are saying - yes, sir.

Q All right.

A And “subject to its jurisdiction.”

Q And with a Master’s in Language, you know that the word, “and,” means that it has to be both of those things, don’t you?

A That would be correct, sir.

Q Tell the Jury exactly what you studied with respect to the language, “subject to its jurisdiction?”

A “Subject to its jurisdiction,” the best that we were able to determine would be that means that you would be—

Q —Ma’am, please tell the Jury what you studied with respect to that?

THE COURT: Do you mean what book, or what are you talking about?

MR. DICKSTEIN: That is what I am trying to find out from the witness, Judge.

A No, sir, we do not go to another book for this, because the terms are commonly used terms as far as being subject to jurisdiction. The basic understanding is that you would be subject to the laws of our country, and that would be to be a citizen.

Q It is called Legislative Jurisdiction, isn't it? Subject to the law?

A That would be correct.

Q So, we are talking about Legislative Jurisdiction, aren't we?

A That would be a correct assumption.

Q Now, tell the Jury what facts makes Mr. Hall subject to the Legislative Jurisdiction of the United States, please?

MR. MACKEY: Objection, Judge. Matters of jurisdiction are personal subject matters and—

MR. DICKSTEIN:—This was opened up by direct examination when the witness testified from Section 1.1-1, as to the determination as to who is or isn't an individual upon whom the tax is imposed. I have a right to cross examine her on that, Your Honor. The government opened it up.

MR. MACKEY: Judge, the examination on direct examination explained the fundamental starting point for her determination of taxes. Section 1, she—

THE COURT:—The Court has already ruled on this. Objection is sustained.

MR. DICKSTEIN: Judge, you aren't going to let us cross examine on this?

THE COURT: No.

Q (By Mr. Dickstein) Ma'am, the taxes imposed on an individual is in Section 1?

A Yes, sir.

Q And you have to determine who an individual is, don't you?

A Sir—

Q —If you are not an individual, the tax is not imposed on you, is it?

A Sir, I make the distinction as to whether a person is an individual, corporation, partnership, a trust or an estate.

Q Please turn to Section 7701 (a) of the Internal Revenue Code.

A Yes, sir.

Q I believe it is (a)(14)—Definition of a Person?

A (a)(14) is the definition of a taxpayer.

Q Definition of a person is (a)(1)?

A Yes, sir.

Q What is the definition of a person?

A The term, person, shall be construed to mean and include an individual, a trust, an estate, partnership, association, company or corporation.

Q All right, so an individual might be a person or an individual is a person, is that correct?

A That's correct.

Q But a person may not be an individual for purposes of the code. Is that correct?

A That's correct, for purposes of the code.

Q A person might be a corporation?

A That is correct.

Q And all throughout the code, they distinguish between an individual and persons, don't they?

A To the best of my recollection, sir, yes, they do.

Q Yesterday, you read Section 6001, did you not?

A Yes, sir.

Q And then you read Section 6012—well, you didn't read it, you said that it means any person with a gross income?

A Yes, sir.

Q But the fact is, it says any individual, doesn't it? It doesn't say person? If you don't know, please look it up.

A Sir, I will look it up because I know that you are making a distinction between those terms. 6012 has the heading, "Persons Required to Make Returns of Any Kind."

Q What does the language of the actual statute say though?

A The language of the statute does refer to every individual having for the taxable year a gross income of some kind.

Q And, when you studied the tax laws they told you, did they not, that the headings of the codes were meaningless for the purposes of interpretation purposes?

A No, sir, they did not make that statement.

Q The captions—that is right in the Internal Revenue Code itself, isn't it?

A I don't know that, sir.

Q You haven't read the entire code, have you?

A No, sir, I have not read the entire code and I testified to that yesterday.

Q Okay. So, there is some distinction between individuals and persons in the Internal Revenue Code? Is that correct?

A That's correct.

Q Now, will you please tell the Jury exactly what steps you took to make the determination that Mr. Hall is an individual as defined in Section 1.1 of the Code—the regulations?

A Sir, the steps that I took were that I looked at Mr. Hall sitting in the courtroom—he is not a corporation. He is not a partnership. I had the choice of is he a corporation, a partnership, a trust estate and he is an individual. He is not any of the other entities.

Q Ma'am, Section 1.1-1 of the Regulations defines an individual, does it not?

A As a citizen, yes, sir.

Q And, also subject to the jurisdiction of the United States?

A Yes.

Q And, you have presumed that Mr. Hall is subject to the jurisdiction of the United States, haven't you?

A That would be correct.

Q You did not make an independent factual determination as to whether or not Mr. Hall was subject to the jurisdiction of the United States?

A That would be correct.

Q And, we are talking about legislative jurisdiction, are we not?

A That was your term and I agreed to it, yes, sir.

Q Was there some other term that you know of?

A No, sir, not at this point.

MR. DICKSTEIN: Judge, at this time I am going to ask the Court to take judicial notice of what has been marked as Defendant's Exhibit "AZ". It is a report of the Inter-Departmental Committee for the study of jurisdiction over federal areas within the states. Part I being the facts and Committee recommendations; Part II being a text of the law on legislative jurisdiction of the United

States - these are government documents presented by the United States government printing office in Washington in 1956.

THE COURT: I don't know what it is. Can you explain it in three sentences—what it is?

MR. DICKSTEIN: Yes, sir, I can. This is the document from the report of the United States government which specifically defines the limited area of federal jurisdiction—legislative jurisdiction over Washington, D.C., federal enclaves, and territories.

THE COURT: And, after I take judicial notice what do you want me to do?

MR. DICKSTEIN: The next thing that I want the Court to take judicial notice of is Chapter I of Volume 4-21-1-1 of the statutes of Indiana which indicates those areas where federal legislative jurisdiction is conceded to the United States for purposes of determining that no such jurisdiction has been ceded over those areas where Mr. Hall lives and, therefore he is a—lives in a foreign country as that term is used with respect to foreign jurisdiction, that is being subject to another government. We will get into that

because that term is also defined in the Code of Federal Regulations which we will get into in a moment, and the statutes for the State of Indiana, Defendant's Exhibit "BA". And, I would make an offer of proof at this time that Mr. Hall is outside the legislative jurisdiction of the United States and therefore he is not an individual as defined in the Code. There is no section of the Internal Revenue Code which imposes a liability on Mr. Hall.

MR. MACKEY: The question as to whether this Court has jurisdiction over Mr. Hall as an individual in the subject matter of this criminal prosecution has been ruled on.

MR. DICKSTEIN: We are not denying that this Court has judicial jurisdiction. We are claiming that Mr. Hall is a nontaxpayer because of legislative jurisdiction.

THE COURT: What do you want me to do, just take judicial notice of it?

MR. DICKSTEIN: At this point in time, yes, sir.

THE COURT: All right. I will take judicial notice of it.

MR. DICKSTEIN: And, I want to move now that they be introduced into evidence.

MR. MACKEY: Objection, Your Honor, as to relevancy.

THE COURT: You are asking me to admit something and take time out and read it for about three hours?

MR. DICKSTEIN: No, sir. The Court has taken judicial notice of it. I am asking the Court to admit it into evidence so that it can go to the Jury for their determination as to whether or not Mr. Hall is the individual upon whom the tax is imposed.

THE COURT: What is the government's response?

MR. MACKEY: The Court can take judicial notice of any statute and question whether those statutes apply and are relevant.

THE COURT: He wants them admitted into evidence.

MR. MACKEY: I would object to their admission.

THE COURT: On what grounds?

MR. MACKEY: On the grounds that they are irrelevant.

MR. DICKSTEIN: Whether or not Mr. Hall is a taxpayer, Your Honor, is most definitely relevant to this case.

MR. MACKEY: The question of jurisdiction, Your Honor, which has been represented by his counsel of this subject matter is not a question for the Jury. It is a question for the Court to rule upon. We would object to this going to the Jury as being irrelevant.

MR. DICKSTEIN: Not based upon the testimony of the witness, Your Honor.

THE COURT: Let's take a recess. Take the Jury out.

THE CLERK: Please rise. Court is in short recess.

(COURT IN RECESS)

(THE FOLLOWING PROCEEDINGS TOOK PLACE OUTSIDE THE PRESENCE OF THE JURY):

THE COURT: What is your argument, that the Court has no jurisdiction—that the Court has no jurisdiction?

MR. DICKSTEIN: No, sir, absolutely not.

THE COURT: Do you want me to dismiss the case or what?

MR. DICKSTEIN: I want the issue—we have already asked the Court to dismiss the case and the Court has refused. I am asking that this go to the Jury.

THE COURT: Be submitted to the Jury for a question about the fact for them to decide?

MR. DICKSTEIN; Absolutely—is Mr. Hall or is he not an individual upon whom the tax is imposed in Section I, which is what—

THE COURT:—Wouldn't that be one of the things that the Seventh Circuit said you couldn't do?

MR. DICKSTEIN: No, sir.

THE COURT: What does it say? Is this one of those tired old arguments again?

MR. DICKSTEIN: No, sir, it is a brand new argument.

THE COURT: Brand new?

MR. DICKSTEIN: Absolutely.

THE COURT: Brand new where?

MR. DICKSTEIN: Brand new right here. There is no case law on point, Judge.

THE COURT: I have had it a half dozen times myself.

MR. DICKSTEIN: And probably never presented in this format or supported by testimony of the witness or the documents that we are asking the Court to take judicial notice of. We are not contending the 16th Amendment wasn't properly ratified. We are not contending whether or not wages are not income. We are not contending whether the tax laws are unconstitutional. We are not contending the filing of an income tax return violates the privilege against self incrimination and we are not raising the issue of whether federal notes constitute cash or income. The Court specifically says as to issues of jurisdiction those would be preserved for the trial according to the Court's own order. That is exactly what we are doing within the Court's order.

MR. MACKEY: Judge, jurisdiction is a question of law. Citizenship is a question of fact. That is what Mrs. Shaffner testified to yesterday. The two combined, no doubt, can be before the Court to hear this case or the prosecution to prosecute, but the separation has to remain. The question of law is for the Court and the question

of fact is for the Jury. There has been submitted to this Jury meaningless, confusing, and very irrelevant information—

MR. DICKSTEIN:—It is a frivolous argument, Judge. He called us frivolous and he is saying whether or not Mr. Hall is a taxpayer according to regulations is meaningless and that is frivolous, Judge. He is saying Section 1.1-1 in the Code of Regulations is frivolous and that it is meaningless. That is frivolous, and since we have been branded as the tax protestors and we have been branded as frivolous, I think that I am entitled to a little chuckle. By the way, Your Honor, my paralegal has brought an anti-sanction, anti-contempt tool with him. So, I am trying to stay real calm and cool so that he doesn't use this over my mouth.

THE COURT: What is it—tape?

MR. DICKSTEIN: Yes, sir. Sir, we are not talking about judicial subject matter jurisdiction in this case, Your Honor. We are talking about whether or not Mr. Hall is a taxpayer. Everybody in this Courtroom presumes that he is—even Your Honor, because of

your experience in filing returns, which we contend violates the separation of powers In Article III of the Constitution. However,—

THE COURT: Are you asking me if I should try it?

MR. DICKSTEIN: No, sir, because you are a taxpayer subject to jurisdiction of the Executive Branch. Originally, the Supreme Court ruled that Federal Judges were exempt from taxation in order to maintain judicial separation of powers.

THE COURT: Have you ever heard of the rule of necessity?

MR. DICKSTEIN: Yes, sir, what does that have to do with it?

THE COURT: Sometimes you may decide to do it, even though you may have some conflict in some way.

MR. DICKSTEIN: No, sir.

THE COURT: You have never heard of that rule before, have you?

MR. DICKSTEIN: Yes, sir, I have heard of that. I don't believe that it is applicable. If you will give me a moment, I will try and explain it.

THE COURT: How have you heard about the rule?

MR. DICKSTEIN: I have read it, Judge. I have gone to law school. But this is not a matter of a rule of necessity. Originally, Federal Judges were exempt from taxation and the Supreme Court stated that was necessary in order to maintain the separation of powers, so Judges could be fairly impartial and not subject to the Internal Revenue Code.

THE COURT: Just give me the essential facts, Mr. Dickstein.

MR. DICKSTEIN: The essential facts are that the witness testified that the taxes imposed upon Mr. Hall, pursuant to Section 1 of the Internal Revenue Code, as an individual. The term, “individual” is defined in Section 1.1 of the regulations as a person born or naturalized in the United States and subject to its jurisdiction. That means legislative jurisdiction. Legislative jurisdiction is confined to Washington, D.C., Federal enclaves, et cetera. Those are areas within a State and according to Indiana law, where there has been accession to the United States, and a plat filed by the United States. That has not taken place here. This gets right into the—Well, I am not going to get into that. The Court says that’s

frivolous, although in this context, I believe that it is non-frivolous. We are not raising the issue, Your Honor, that Congress cannot tax Mr. Hall. We are raising the issue that they have not done so in this particular case.

THE COURT: Why?

MR. DICKSTEIN: Why—because the taxes are imposed in Washington D.C., Federal enclaves, and territories. The government has failed to prove that Mr. Hall was within a Federal enclave or Washington, D.C. The evidence is that he was born in the State of Indiana. There is a difference in the terms of sovereignty between the government of Indiana and the government of the United States. Congress and the United States has jurisdiction in limited areas pursuant to Article I, Section 8, Clause 17, of the United States Constitution. There is a procedure for the United States to obtain jurisdiction over areas in Indiana, as set forth in Indiana Statutes. They have not yet done so. The government can't prove that they have. Mr. Hall is not a taxpayer.

THE COURT: We will take a short recess.

THE CLERK: Court stands in recess.

(THE FOLLOWING PROCEEDINGS TOOK PLACE AFTER A SHORT RECESS, OUT OF THE PRESENCE OF THE JURY):

THE COURT: Show that the Defendant requested that Defendant's Exhibits BA and AZ be submitted to the Jury and the Court denies the same for the reason it is not a question of fact. It is a question of law. It is not factual in nature and the Court recognizes that there may be situations where, "subject to the jurisdiction of the United States." It may be a question of fact concerning whether or not someone is a citizen at the time, certain fact situations could arise, giving rise to that dispute, which would be a question for the Jury. But in this particular instance, it is a question of law and therefore, it is not proper to be submitted to the Jury. Anything else, gentlemen, before the Jury returns?

MR. MACKEY: No, sir.

MR. DICKSTEIN: No, sir.

THE COURT: Bring in the Jury.

(DEFENDANT EXHIBITS BC AND AZ NOT ADMITTED)

(THE FOLLOWING PROCEEDINGS TOOK PLACE BACK IN FRONT OF JURY):

THE COURT: So, the Jury understands, when you were in Court prior to this time, Defendant had submitted two exhibits in evidence which I have now denied their submission in evidence. You may continue.

MR. DICKSTEIN: Your Honor, at this time, I would like to submit Defendant's Exhibit BC, which is a 1988 map of Indiana. This particular map shows those areas of the United States within the State of Indiana. I would request the Court to take judicial notice of the fact that Tell City and Rockport is outside of any designated areas of the United States within the State of Indiana.

MR. MACKEY: I have no objection to the map, Judge. I do have an objection as to his statement of law concerning conclusions about whether it is portions of Indiana or the whole State of Indiana.

THE COURT: All right. I will take judicial notice of the statement but I don't know about the map. That is a question of law about the statement of the portions of Indiana.

MR. DICKSTEIN: I understand. I submit that this map accurately portrays those areas that conceded to the United States—jurisdiction was conceded to the United States.

THE COURT: Is that the purpose for your putting it in evidence?

MR. DICKSTEIN: That's the purpose and the Court's judicial notice that Tell City and Rockport falls without those areas.

THE COURT: If that is the purpose, I will deny it.

MR. DICKSTEIN: All right, sir, as long as it is marked and goes up to the Court of Appeals. We will take exception to the ruling, sir.

THE COURT: Have the witness take the stand.

(MS. SHAFFNER IS BACK ON THE WITNESS STAND):

CROSS EXAMINATION OF MRS. SHAFFNER CONTINUING BY MR. DICKSTEIN:

Q Now, you testified before that in the examination audit process that you notified the taxpayer? Do you recall that testimony?

A Yes, I do.

Q Did you notify Mr. Hall?

A I was referring to the fact that I would notify a taxpayer that I was conducting an examination.

THE COURT: Did you notify Mr. Hall?

A I did not.

Q (By Mr. Dickstein) But you did conduct an examination?

A No, sir, I did not conduct an examination. Under Civil, I cannot conduct an examination.

Q But you determined it was a tax liability?

A Yes, sir.

Q You are out of the examination division, aren't you?

A Yes, sir, I am.

Q Did you notify Mr. Hall of his rights to appeal to your determination of tax liability?

A No, sir, I didn't.

Q All right. Did you conduct your examination off his substitute return?

A I did not conduct an examination for civil purposes.

Q Did you make your determination of the correct tax liability off a substitute return?

A No, sir.

Q And, what do you contend is an examination then as opposed to what you did in this case?

A An examination is a civil process whereby I notify the taxpayer that the return they had filed is under examination by me in which I go back to their original books and records to prove what is on the return.

Q Can you show me any authority, either in the Internal Revenue Code or the Regulations that you have on the book, which gives you the authority to make a determination of tax liability from other than a tax return?

A Not at this time.

Q The fact is Section 601.105 that you referred to, states that you should make your determination off the return, doesn't it?

A Are those what you have presented to me?

Q Yes. Those are the Regulations that pertain to your job and examination?

A Let me see.

(WITNESS LOOKING AT REGULATIONS)

A (By Witness) Do you have the exact cite?

Q (By Mr. Dickstein) It is your job. More importantly, you don't know what your authority is to do what you did?

A I know that my authority is to do my job, but as far as to do it from a tax return or not from a tax return, no, I don't know that at this time.

Q Would you take a moment to review the Regulations that I have handed you and see if there is any authority in there for doing it other than from on a tax return?

(WITNESS LOOKING AT REGULATIONS)

A (By Witness) I have not come to that part. I have seen the part where we are authorized to examine any books, papers, records, or memorandum bearing upon that as required to be included in federal tax returns and to take testimony relative thereto.

Q (By Mr. Dickstein) Ma'am, would you accept my representation that there is no authority set forth in that Regulation?

A I hesitate to do so, but if you could give me the exact cite, then I could—

Q —It is not there, ma'am. I can't give you a cite for something that is not there.

A It goes on and says that the examiner will check the entire return filed by the taxpayer and will examine all books, papers, records, and memorandums dealing with matters required to be included in the return.

Q In Section 6020(b)(1) of the Code, it indicates that if a taxpayer doesn't file a return and one is required the Secretary shall file a return. Isn't that correct?

A I believe that is what it states.

Q And, the Secretary didn't bother to file a return in this case, did he?

MR. MACKEY: Objection, Your Honor. This matter came up numerous times yesterday. There have been previous rulings and it is irrelevant.

MR. DICKSTEIN: This is under a new subject, Judge.

THE COURT: What is the new subject?

MR. DICKSTEIN: The subject is this lady's authority to make a determination of tax liability.

MR. MACKEY: Your Honor, I didn't ask this lady any questions about a substitute return and it goes beyond the scope of direct examination.

MR. DICKSTEIN: No, but he did ask her lots of questions about tax liability and her determination thereof. She is the lady that supposedly made the determination. That is why she is on the stand.

THE COURT: I will overrule the objection. You may answer the question.

A (By Witness) Would you repeat the question, please?

Q (By Mr. Dickstein) Yes. The Secretary didn't file or make a return in this action, did he?

A That is correct.

Q And, the word, shall, appears there, doesn't it, - the Secretary shall make a return?

A Yes, sir.

Q And, we heard—you were sitting here when you heard Ms. Elizabeth Jew—testify that Status Code 06 says that no return is required?

A It doesn't say that. It says an acceptable reason for non-filing.

Q For non-filing—right. One of those acceptable reasons might be that the person isn't a taxpayer. Isn't that correct?

A I don't know that to be a fact.

Q Nontaxpayers don't file tax returns do they, ma'am?

A The two terms would seem to coincide, yes, sir.

Q Yes, now as far as the computer is concerned, you folks had a W-4 and a W-2. Is that correct?

A Yes, sir.

Q And, so the Internal Revenue Service would naturally assume that somebody who submitted those was a taxpayer, wouldn't they?

A That would be a reasonable assumption.

Q And, then they might go out and ask where a tax return is from the person they presumed to be a taxpayer. Isn't that correct?

A Yes, sir.

Q But, if a person was a nontaxpayer no return would be required—yes or no?

A That term nontaxpayer is—

Q —Something that you have never considered, have you? You file your tax returns, don't you?

A Yes, of course.

Q Of course, and you don't know what the term, subject to the jurisdiction of the United States means either, do you?

A I know my understanding of it.

Q Right—the official IRS understanding?

A I wouldn't go so far as to call it the official IRS understanding. It is my understanding of it based upon my experience.

Q Which isn't based on a study of the law around that section, is it—or under that term?

A Do you mean the law outside of the Code?

Q Yes, ma'am.

A No.

Q The law which might explain that?

A That would be correct.

Q Certainly not based upon the Interdepartmental Committee of Federal Legislative Jurisdiction within the states?

A Certainly not.

Q Certainly not. Ma'am, you heard testimony that Mr. Hall had picked up a certificate and claimed that he was a minister?

A Yes, sir.

Q And, you are familiar with Sections 1402 of the Code dealing with the exemptions for ministers?

A Yes, sir.

Q Did Mr. Hall ever claim that he was a minister for purposes of exception from that Code?

A No, sir, not to my knowledge.

Q In fact, Mr. Hall never claimed any exemptions from federal taxation based upon being a minister, has he?

A Based upon what has been presented here, sir, I don't have any evidence that he did at this time.

Q There are things such as the vow of poverty that could be filed to take advantage of Section 1402?

A Yes, sir.

Q There is no vow of poverty in this case, is there?

A There has been none presented, sir.

Q And, there had been no application for exemption as a charitable organization under 501 (c) of the Code either, has there?

A There has been none presented here, sir.

Q And, you don't know of any either, do you?

A No.

Q All right, ma'am. You testified to Section 6011 during your direct examination?

A Yes, sir.

Q And, would you turn to that section, please?

A All right.

Q By the way, 6011 is in Subtitle F of the Code, isn't it?

A That's correct.

Q And, you were qualified as an expert under Subtitle A and Subtitle C of the Code?

A I can show you exactly which Subtitles I was qualified under, sir.

Q Income taxes under Subtitle A?

A Yes, sir.

Q And, employment taxes under Subtitle C?

A Yes, sir.

Q And, do you claim the same knowledge, training, skill, and expertise with respect to Subtitle F as you do with respect to Subtitle A and Subtitle C?

A It would be similar but I have not made reference to it as often as I have to Subtitle A.

Q Now, Section 6001 deals with any person made liable for any tax under this title?

A Sir, are you referring to 6001?

Q Yes, 6001.

A Yes, sir.

Q Requiring him to keep books and records?

A Yes, sir.

Q And, the statute specifically uses the term, made liable, doesn't it?

A Every person liable.

Q It doesn't say who is made liable, does it?

A No, sir, not in this section.

Q How about Section 6011?

A No, sir, at that point it doesn't either.

Q How is liability determined then? How is a person made liable?

A By the tax imposed by Section I.

Q Would you please look at Section 1461 of the Code.

A All right.

Q Would you read that language to the Jury, please?

A Do you want the title on that or not, sir?

Q Sure.

A Liability for Withheld Tax—every person required to deduct and withhold any tax under this chapter is hereby made liable for such tax and hereby indemnified against the claims and demands of any person for the amount of any payments made in accordance with the provisions of this chapter.

Q So, the statute specifically says that the person is made liable. Is that right?

A Yes, sir.

Q Now, would you find the same section which says that Mr. Hall is made liable under Subtitle A of the Internal Revenue Code?

A Sir, that would begin in Section 1, but then you need to refer to the regulations thereunder to find that he would be liable.

Q Ma'am, there is no statute—no law that says Mr. Hall is made liable as there is for the person in Section 1461, is there?

A That's correct, sir. There is nothing within the Code itself.

Q Regulations are binding only on the Internal Revenue Service, aren't they?

A Binding, yes, sir, only on the Internal Revenue Service.

Q So, a regulation can't, as a matter of law, make somebody liable for a tax, can it?

A Not as a matter of law, sir.

Q There has to be a statute?

A That would be correct.

Q And, there is no statute in Subtitle A which makes Mr. Hall liable, is there?

A I have never seen one.

Q There is another way that a person can be made liable, isn't there—that is by an assessment?

A Yes, sir.

Q And, the Secretary—or the IRS make assessments, don't they?

A Yes, they do.

Q And, under Section 6201, they make assessments from the returns of the taxpayer or of the Secretary, isn't that correct? Why don't you take a look at 6201, please?

(WITNESS LOOKING AT DOCUMENT)

A (By Witness) Yes, sir.

Q (By Mr. Dickstein) So, if a taxpayer files a return or the secretary files a return under Section 6020(b) then those taxes can be assessed. Isn't that right?

A Yes, sir.

Q And, the assessment process is contained in Section 6203, isn't it?

A Yes, sir.

Q Would you read that to the Jury, please?

A "Section 6203. Method of Assessment. The assessment shall be made by recording the liability of the taxpayer in the office of the Secretary. Upon request of the taxpayer, the Secretary shall furnish the taxpayer a copy of the record of the assessment."

Q Ma'am, where is the record of assessment for Mr. Hall?

A To my knowledge, no assessment has been made at this time.

Q That's right. So, there is no statute imposing liability and there is no assessment imposing liability, is there?

A That's correct.

MR. DICKSTEIN: Thank you, ma'am. That's all that I have.

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