Liberty Tree

Vol. 23, No. 8 — August 2021

Upsetting the Apple Cart?

How the Pollock case changed *everything* without really changing *anything*

By Dick Greb

In my series of articles examining the 1796 decision in *Hylton v. United States* (3 U.S. 171), I showed how a relative handful of Federalists were able to effectively amend the Constitution by means of collusion, rather than through the only *legal* method laid out in Article 5 of that document. The result of their coup was to forever alter the *de jure* meaning of the term "direct taxes," as it is used in the Constitution. Never again would the economic incidence of a tax be the deciding factor on whether or not a tax was direct. Instead, the black-robed liberty thieves on the Supreme Court simply declared that there were only two direct taxes: taxes on land and slaves; and capitation taxes (so called "head taxes"). All other taxes must therefore, *by default*, be "indirect taxes."

The importance of this change can hardly be overstated. As you know, the Constitution establishes different rules for the application of direct and indirect taxes. Direct taxes must be apportioned among the states, which links their economic impact on each state to the same proportion as that state's voting strength in enacting the tax. Since representation and direct taxes are both directly tied to the population according to the decennial census,[1] the greater the number of votes a state can bring to bear on the enactment of a direct tax, the greater share of the burden of the tax it will likewise have to bear. This prevents more populous states from using their superior numbers of votes to burden the less populous states with onerous taxes.

Indirect taxes, on the other hand, merely have to be uniform throughout the states.[2] The Supremes have construed this required *uniformity* to be strictly geographical, thereby allowing all manner of disparity in the application of indirect taxes to different individuals, as long as the disparities aren't a function of the state in which one lives. Since the economic impact of these indirect taxes aren't proportional to the voting strength used in enacting them, there is great potential for abuse by the more populous states. In fact, one of the factors in the secession of the southern states in the Lincoln era, was the financial burdens being laid upon the south while the benefits accrued to the interests of the northern states.[3]

Thus, with respect to the two great classes of taxes, direct taxes are safer from abuse. However, that safety comes at a price, and unfortunately for we the people, that price is borne by the government. The problem comes from the uniformity (or lack thereof) of the distribution of the potential objects of direct taxation. Objects with a relatively even distribution among the states could equitably be taxed directly, since the incidence of the tax would likely be more evenly distributed within the state as well. An easy example would be a tax on dinnerware — plates, bowls,

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1. "Representatives and direct taxes shall be apportioned among the several States which may be included within this Union, according to their respective Numbers, which shall be determined by adding to the whole Number of free Persons, including those bound to Service for a Term of Years, and excluding Indians not taxed, three-fifths of all other Persons." Article 1, Section 2, Clause 3.
2. "The Congress shall Power To lay and collect Taxes, Duties, Imposts and Excises, to pay the Debts and Provide for the common Defence and general Welfare of the United States, but all Duties, Imposts and Excises shall be uniform throughout the United States." Article 1, Section 8, Clause 1.
3. "The people of the Southern States, whose almost exclusive occupation was agriculture, early perceived a tendency in the Northern States to render the common government subservient to their own purposes *by imposing burdens on commerce as a protection to their manufacturing and shipping interests*. ... By degrees, as the Northern States gained preponderance in the National Congress, self-interest taught their people to yield ready assent to any plausible advocacy of their right as a majority to govern the minority without control." Jefferson Davis' "Message to the Confederate Congress" of April 29, 1861, as it appears in: *Great Issues in American History: From the Revolution to the Civil War, 1765–1865*, Richard Hofstadter, ed. (1958).

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etc. There would hardly be anyone who didn't own some dinnerware, and therefore the effect of the tax would closely mirror population. An object like a yacht, on the other hand, would not have such even distribution, either among the states or within a state. Thus, a tax on yachts would greatly affect some individuals and some states more than others, and this lack of universal ownership would make yachts a poor object for a direct tax.

So, we see that the price to the government of the economic incidence view of direct taxes — that is, whether the tax falls immediately and directly on the tax-payer, or whether, through the tax-payer, it ultimately falls on the consumer — is that it removes a great many potential objects of taxation from the government's clutches, due to the resulting inequity and injustice that taxing unequally distributed objects would engender. But if you get rid of that economic incidence view, as the Supremes did in *Hylton*, then it brings all those unevenly distributed objects into the grasp of the taxing power. Seen in this light, it is no wonder that the usurpers wasted little time in their subversion of the constitutional meaning of *direct taxes*. But it is we the people who pay for this subversion, not only because it brings such a numberless mass of objects within the purview of taxes, but also because it undermines the protection against the more populous states using their superior voting strength to shift the tax burden for the federal government onto the less populous states, which have less representation, and therefore weaker voting power.

The final installment of the *Hylton* series[4] tracked the legacy of that seditious decision through almost 70 years of Supreme Court challenges to various taxes, including the income tax enacted during the War Between the States. In each case, the court claimed the tax was *indirect*, and every time they based their erroneous determinations on the dicta[5] of those Federalist judges in *Hylton*. So, by the time we get to the *Pollock* case[6] — challenging the income tax enacted in 1894 — there is a full century of bad precedence built upon the faulty foundation of the *Hylton* decision. Indeed, to my knowledge, *every* tax considered by the Supremes in that time was held to be *indirect*, every one tracking back to that same seditious decision.

With this history in view, challenging the new income tax as direct must have seemed like a fool's errand. But Charles Pollock took a little different approach to the problem, and in so doing, achieved a record that I believe stands to this very day — the only Supreme Court decision to ever invalidate a tax, laid by Congress as an indirect tax, because it was held to actually be direct! The immediate impact of that decision was Americans were relieved from the oppression of a tax on their income for almost twenty years. But, of course, ultimately it precipitated Congress to propose the 16th Amendment, which — once it had been *declared* ratified by the requisite number of states[7] — was used to justify imposing another income tax in 1913. And, like Pollock's record, that income tax also continues to stand to this very day.

Breaking with tradition?

In the *Pollock* decision, the Supremes seemingly departed from their earlier unbroken string of precedent whereby every tax — except those on land and on the 'head' (capitations) — was, constitutionally speaking, deemed to be indirect. They invalidated the 1894 income tax on the grounds that it was, *in its effect*, direct, and being unapportioned, thereby unconstitutional. If you strip away all of the reasoning of the court, you are left with just the naked proposition that the income tax was unconstitutional. Naturally, that proposition makes the *Pollock* case a real favorite among the 'tax honesty' crowd. In fact, it is often used as a foundational stepping stone (along with the later *Brushaber* case[8]) in promoting the position that the imposition of income taxes on citizens is still likewise unconstitutional. Indeed, it is for that reason this case is of any real importance to us now.

However, in my view, the *Pollock* decision is in large part misunderstood in the tax movement, or at the very least, misconstrued. The case is so intertwined with the *Hylton* decision that without a prior comprehension of that earlier case, it would be nearly impossible to come to a proper understanding of the latter. That combination — the general lack of comprehension of *Hylton*, and my recognition of its importance in *Pollock* — was what prompted me to write the 10-part series on *Hylton* for the *Liberty Tree*. And with that now out of the way, I will pick up the thread with this current series (of an as-yet-unknown number of parts), in the hopes of promoting a proper understanding of *Pollock*.

Actually, there are two separate decisions in the *Pollock* case,[9] because the judges were evenly divided on three questions presented in the first hearing. So, a rehearing was requested, and granted, to decide those

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4. See "Coup in the courts — part 10" in the February 2019 issue of *Liberty Tree*.
5. *Dicta* is nothing more than the personal opinion (as opposed to the judicial opinion) of a judge. For more on this issue, review the section called "The trouble with dicta" in part 3 of the *Hylton* series in the June 2018 issue of *Liberty Tree*.
6. *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429 (1895).
7. Bill Benson and M. J. "Red" Beckman extensively documented the myriad issues affecting the validity of the ratification process in their 1985 book, *The Law That Never Was*.
8. *Brushaber v. Union Pacific Railroad Co.*, 240 U.S. 1 (1916).
9. First hearing was decided on April 8, 1895 (157 US 429); rehearing was decided on May 20, 1895 (158 US 601).

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outstanding issues. The initial hearing invalidated only portions of the new income tax laws, leaving all the rest undisturbed. It was only in the rehearing that the entirety of the income tax provisions of the much larger tax act was invalidated as being unconstitutional. And only then because to remove just those portions determined to be invalid would shift the balance of the tax burden of what remained. The judges said such imbalance, never intended by the legislature, could not be implemented by mere judicial fiat, and so they threw out the entire scheme.

> According to the census, the true valuation of real and personal property in the United States in 1890 was $65,037,091,197, of which real estate with improvements thereon made up $39,544,544,333. ... [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 a tax on occupations and labor.*** We cannot believe that such was the intention of Congress. ... [T]he scheme must be considered as a whole. ***Being invalid as to the greater part***, and falling, as the tax would, if any part were held valid, in a direction which could not have been contemplated except in connection with the taxation considered as an entirety, ***we are constrained to conclude that [the income tax provisions]*** of the Act, [of] August 28, 1894, ***are wholly inoperative and void.*** *Pollock v. Farmers' Loan & Trust Co.*, 158 U.S. 601, 636 (1895).

Nothing new

Notice the portions of the income tax act that the court did ***not*** invalidate: that which would "be borne by professions, trades, employments, or vocations" — that is, the "tax on occupations and labor." The reason given for not striking down those portions was the prior precedents of those cases which, in turn, relied upon the faulty reasoning of *Hylton*.

> 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 guise of an excise tax and been sustained as such***. *Ibid.*

Chief Justice Fuller, who penned the majority opinions in both *Pollock* cases, did not elaborate on the prior instances to which he adverts here, although he had previously discussed the *Springer* case,[10] which challenged the first round of income taxes laid during Lincoln's war against the southern states.

> That was an action of ejectment, brought on a tax deed issued to the United States on sale of defendant's real estate for income taxes. The defendant contended that the deed was void, because the tax was a direct tax, not levied in accordance with the constitution. ***Unless the tax were wholly invalid, the defense failed.*** ... The original record discloses that the income was not derived in any degree from real estate, but was in part professional as attorney at law, and the rest interest on United States bonds. It would seem probable that the court did not feel called upon to advert to the distinction between the latter and the former source of income, ***as the validity of the tax as to either would sustain the action***.
>
> The opinion thus concludes: '***Our conclusions are that direct taxes, within the meaning of the constitution, are only capitation taxes, as expressed in that instrument, and taxes on real estate***; and that the tax of which the plaintiff in error complains is within the category of an excise or duty.'
>
> While this language is broad enough to cover the interest as well as the professional earnings, ***the case would have been more significant as a precedent if the distinction had been brought out in the report and commented on in arriving at judgment, for a tax on professional receipts might be treated as an excise or duty, and therefore indirect, when a tax on the income of personalty might be held to be direct***.
>
> Be this as it may, ***it is conceded in all these cases, from that of Hylton to that of Springer, that taxes on land are direct taxes, and in none of them is it determined that taxes on rents or income derived from***

10. *Springer v. United States*, 102 U.S. 586 (1880).

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land are not taxes on land. *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429, 578 (1895).

Justice Fuller stresses that last point because that is the main issue relied on by Pollock to challenge the tax, and it forms the very narrow distinction on which the first *Pollock* decision differs from all its predecessors. Reliance on that distinction allowed the court to upset the apple cart — that is, strike down the tax — without actually having to overturn any of the previous decisions. Since none of those earlier cases had "determined that taxes on rents or income derived from land are not taxes on land," then this case didn't need to expand the definition of direct taxes as established by the dicta in *Hyton*. It merely acknowledged that taxing the proceeds of land was just another form of a tax on land, and was therefore direct.

> [I]t is admitted that a tax on real estate is a direct tax. ***Unless, therefore, a tax upon rents or income issuing out of lands is intrinsically so different from a tax on the land itself that it belongs to a wholly different class of taxes, such taxes must be regarded as falling within the same category as a tax on real estate*** eo nomine ["under that name"]. The name of the tax is unimportant. The real question is, is there any basis upon which to rest the contention that real estate belongs to one of the two great classes of taxes, and the rent or income which is the incident of its ownership belongs to the other? We are unable to perceive any ground for the alleged distinction. *Ibid.,* at 580.

Therefore, according to the majority of the court:

> We are of opinion that the law in question, so far as it levies a tax on the rents or income of real estate, is in violation of the constitution, and is invalid. *Ibid.,* at 583.

Bonds … municipal bonds

In addition to the issue of income from real estate, Pollock also challenged the taxability of the income from interest on municipal bonds, of which Farmers' Loan & Trust owned $2 million worth, and for which it received about $60,000 per year in interest. The court said:

> As the states cannot tax the powers, the operations, or the property of the United States, nor the means which they employ to carry their powers into execution, so it has been held that the United States have no power under the constitution to tax either the instrumentalities or the property of a state.
>
> A municipal corporation is the representative of the state, and one of the instrumentalities of the state government. ***It was long ago determined that the property and revenues of municipal corporations are not subjects of federal taxation.*** *Ibid.,* at 584.
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> ***[W]e think the same want of power to tax the property or revenues of the states or their instrumentalities exists in relation to a tax on the income from their securities, and for the same reason***; and that reason is given by Chief Justice Marshall, in *Weston v. City Council*, where he said: 'The right to tax the contract to any extent, when made, must operate upon the power to borrow before it is exercised, and have a sensible influence on the contract. The extent of this influence depends on the will of a distinct government. To any extent, however inconsiderable, it is a burthen on the operations of government. It may be carried to an extent which shall arrest them entirely.' … Applying this language to these municipal securities, ***it is obvious that taxation on the interest therefrom would operate on the power to borrow before it is exercised, and would have a sensible influence on the contract, and that the tax in question is a tax on the power of the states and their instrumentalities to borrow money***, and consequently repugnant to the constitution. *Ibid.,* at 586.

The bottom line is that if the federal government could tax the interest on the bonds issued by a state or any of its instrumentalities, then the states would be forced to pay a higher rate of interest to potential investors in order to make it worth their investment. And by so doing, the feds could ultimately prevent a state from being able to borrow money at all, effectively putting it out of business. Of course, the opposite is also the case. States are likewise prohibited from taxing the feds' 'business.'

The distinction between these two issues is one of taxability. While income from real estate might be taxed directly — that is, through the means of apportionment, the income from state and municipal bonds are exempt from any kind of federal taxation, both direct and indirect.

Coming attractions

In the coming installments, we'll be digging some more into Fuller's majority opinions — in both the initial hearing and the rehearing, as well as Justice Field's very interesting separate opinion. We'll also be taking a little side trip to look at the *Springer* decision, so we can see how it affected the present case. And of course, our study wouldn't be complete without a discussion of the *dissenting* opinions; two from the initial hearing, and four — count 'em, FOUR — from the rehearing. So stay tuned!