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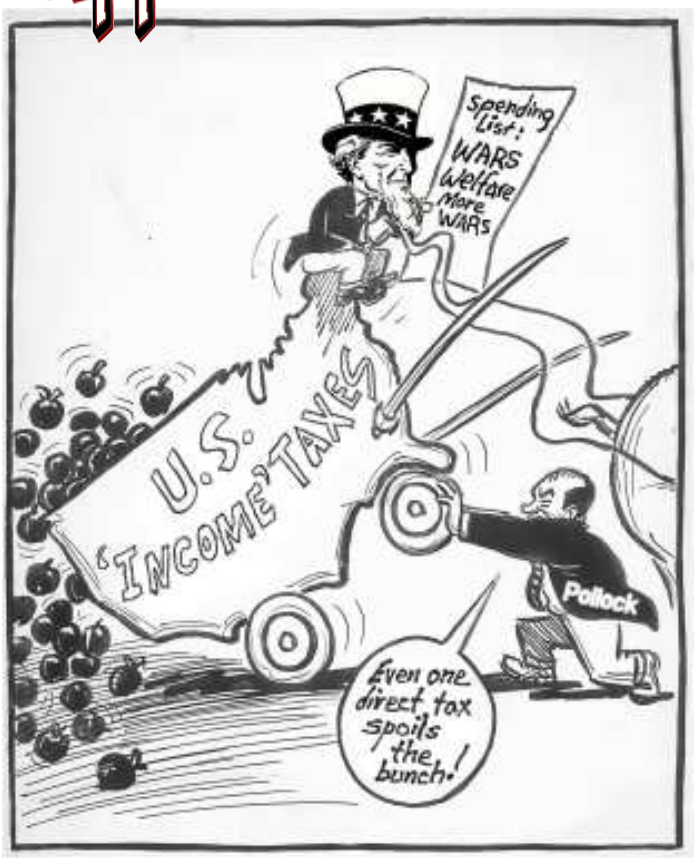
Upsetting the Apple Cart?

The Pollock Case, Part III

By Dick Greb



In this current series, we've been looking into the 1895 Supreme Court case, *Pollock v. Farmers' Loan & Trust Company*. That case, challenging the income tax enacted in 1894,[1] was actually comprised of two separate decisions: the initial hearing was decided on April 8, 1895; the rehearing was decided on May 20, 1895.[2] In the last installment, our attention was primarily on Chief Justice Fuller's majority opinion in the rehearing, which was made necessary by the justices being evenly divided in the original hearing on the question of whether a tax on the *income from personal property* was or was not direct. Ultimately, the majority decided — just as they had for *income from real property* in the first hearing — that such income could only be taxed by the direct method.

Since the taxes on these two sources of income comprised a major part of the total amount of income taxes to be collected by the act, the court determined that eliminating them while leaving the remainder intact would impermissibly "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."[3] For this reason, the entire income tax scheme was struck down as unconstitutional, for trying to tax indirectly that which could only be reached directly — that is, by means of apportionment.

Notably, the court explicitly declined to decide on the classification of a tax on what is commonly known as 'earned income':

> *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.[4]

Notice here that Fuller admits that the court DID NOT CONSIDER the tax as applied to employments, so there was no actual decision that that portion of the tax was in fact constitutional! And although Fuller offers as an excuse for the court's failure that such a tax "has assumed the guise of an excise tax" by earlier case decisions, it's hard to believe that such guise would have been upheld in the face of a direct challenge. However, the Pollock case did not present a direct challenge on that aspect of the tax, and neither did the case which was 'bundled' with it for the hearings, *Hyde v. Continental Trust Co.*[5]

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1. "An Act to Reduce Taxation, to Provide Revenue for the Government, and for other purposes," enacted on August 27, 1894. 28 Stat. at L. 509, 553.
2. The original hearing (hereinafter "1st") is reported at 157 U.S. 429; and the rehearing (hereinafter "2nd") is reported at 158 US 601.
3. 2nd, at 637.
4. 2nd, at 635.
5. 157 U.S. 654 (1895).

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Both of these cases were suits in equity brought by stockholders against corporations.

The mystery of Moore

But there also appears to have been a third case bundled with the *Pollock* hearings at some point, too. And that case (as far as I can determine) was instituted by John G. Moore against the Commissioner of Internal Revenue at that time, Joseph S. Miller. I say it *appears* it was bundled in with *Pollock* because one reporting of the case — the Lawyer's Edition of the Supreme Court Reports[6] — contains the oral argument made by Mr. George F. Edmunds, an attorney for Moore, who is described as being a broker. However, this case remains a bit of a mystery. Other than the aforementioned oral argument (which is said to be on behalf of "appellant, John G. Moore, in [Docket] No. 915"), there is only one mention of the case — in the arguments presented by Attorney General Richard Olney, on behalf of the United States — which is cited as "*Moore v. Miller*, N. Y. L. J. Feb. 1, 1895." This reference looks to be an article in the February 1, 1895 issue of the *New York Law Journal* which discussed the case — probably while it was still in the lower courts.

In the case proper though, there is nothing whatsoever that addresses Mr. Moore. His name doesn't show up in the caption of the case report with Pollock and Hyde (whose docket numbers are 893 and 894, respectively). His issues never seem to be addressed by the court. But what may be the oddest thing about the case is that, searching Supreme Court case records, that case doesn't seem to exist. At least, not under "Docket No. 915." And yet, I did find a case report for one that matches in every respect I can check, except the docket number. The citation for that case (which has the docket number 531) is 163 U.S. 696, and wasn't finished until October 30, 1895 — more than five months after the Pollock decision. Here's the entirety of the body of the case report:

> Appeal from the court of appeals of the District of Columbia.
> George F. Edmunds, Samuel Shellabarger, and J. M. Wilson, for appellant.
> The Attorney General and Asst. Atty. Gen. Whitney, for appellee.
> No opinion. ***Dismissed, with costs, on motion of Mr. Samuel Shellabarger, for the appellant***.

Notice that Moore's case was dismissed as a result of a motion to dismiss filed by his own attorney. The names of Moore's three lawyers as well as the Assistant Attorney General all match the information given in the *Pollock* case, which certainly makes it look like the same case, but so far, I've been unable to verify it for sure.

Now, as engaging as this mysteriousness is as a sideline, I mention the case because Moore's attorney brought some interesting arguments forward. As already mentioned, Moore was a broker, and was challenging the income tax as it was being pressed upon him, as an individual, while Pollock and Hyde were challenging the tax as it applied to corporations. Therefore, Moore's inclusion in the case should have opened the door for a specific decision on the direct or indirect nature of the tax against his earnings. However, as mentioned above, the court explicitly did NOT consider that question.

Challenging the Anti-Injunction Act

One of the arguments presented by Edmunds dealt with the anti-injunction act, which was originally enacted on March 2, 1867, by way of §10 of "An Act to amend existing Laws relating to Internal Revenue, and for other Purposes."[7] At the time of Pollock, it was §3224 of the Revised Statutes, and stated simply, "No suit for the purpose of restraining the assessment or collection of any tax shall be maintained in any court." This prohibition, although amended several times, still exists as §7421(a) of the Internal Revenue Code. This ban was considered by the government to foreclose the opportunity for all three of these cases to go forward, and so each had to address the issue. Moore was the most direct. His argument — which was never mentioned in any of the court's opinions — was that Congress had no power to enact such a prohibition.

> [I]f [the Act of Congress of 1867] means, as it probably was intended to mean, to apply to questions of *merely the amount of the assessment or of the classification, of irregularities, and of all the technicalities, of all the multifarious detail of affairs*, it would have been in one point of view consistent with public interest. But if it meant, as I assume it now to mean, a prohibition, as on its face it professes to be, against every citizen to whom a man falsely pretending to be a collector or assessor of taxes comes without any real act of Congress behind him, and by the sheer arbitrary force of an executive branch of the government, to invade his office and his books, and decide whether he has reported truthfully or not, as a final judge, and finally to seize his property, then ***I say it is a declaration that Congress had no***

6. The citation for that version is 39 L.Ed. 759, (hereinafter "L.Ed 1st") and Moore's oral argument starts on page 781.
7. Chap. 169, 14 Stat. at L. 471, 475.

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> ***power to make; and if it had been decided a thousand times by the courts that it was a power that Congress had a right to exercise, I should again feel it to be a duty to ask your honors to reconsider the question and come back again to exercise the true and bounden duty of the judiciary under a constitutional government, to defend and protect private rights against the tyranny of usurped power.*** … If Congress can say that the citizen shall not sue to restrain, cannot it say that he shall not sue for damages, when the Constitution says both belong to the judicial power?[8]

Pollock and Hyde, however, due to their circumstances, took a more 'evasive' maneuver. They took advantage of the stockholder/corporation dynamic to establish the lack of any other remedy to the ills they would suffer if the injunction didn't issue. Their arguments rested on the harm done to their financial interests in the corporations as a result of the payment of what they considered to be unlawful taxes. That is, the capital of the corporations, of which as shareholders they owned a portion, would be diminished by the sums so paid. The majority of the court agreed with them:

> The jurisdiction of a court of equity to prevent any threatened breach of trust in the misapplication or diversion of the funds of a corporation by illegal payments out of its capital or profits has been frequently sustained.
>
> As in *Dodge v. Woolsey*, this bill proceeds on the ground that the defendants would be guilty of such breach of trust or duty in voluntarily making returns for the imposition of, and paying, an unconstitutional tax; and also on allegations of threatened multiplicity of suits and irreparable injury.[9]

Justice White, on the other hand, was very much opposed to letting the cases be heard. In fact, he spent more than four pages of his dissent dealing with this issue:

> The [decisions of this court] have established the rule that the proper course, in a case of illegal taxation, is to *pay the tax under protest or with notice of suit, and then bring an action* against the officer who collected it. The statute law of the United States, in express terms, gives a party who has paid a tax under protest the right to sue for its recovery. Rev. St. §3226.
>
> The act of 1867 forbids the maintenance of any suit 'for the purpose of restraining the assessment or collection of any tax.' The provisions of this act are now found in Rev. St. §3224.
>
> The complainant is seeking to do the very thing which, according to the statute and the decisions above referred to, may not be done. If the corporator cannot have the collection of the tax enjoined, it seems obvious that he cannot have the corporation enjoined from paying it, and thus do by indirection what he cannot do directly.[10]

8. L.Ed 1st, at 782.
9. 1st, at 553.
10. 1st, at 610.
11. Rev. St. §3226.

The idea underlying Pollock's claim to the right to initiate the suit was that he had no remedy for the damage that would accrue to him due to the corporation's actions. White's description of the process for filing suit, rather than refuting that idea, actually shows it to be true. While the payer of the tax may be able to file suit to recover taxes paid under protest, Farmers' Loan & Trust Co. had already said it would not do so. Pollock had formally petitioned the board of directors with his request that it "refuse to pay said income tax, and to contest the constitutionality of said act," but they refused his request. And since Pollock himself wasn't the taxpayer, he had no individual right to file for the return of the tax paid by the corporation.

Justice delayed is justice denied

The whole process points out the validity of Edmund's argument shown above. Such post-payment suits as regards only the particular details of the tax amount or process may be functional, but in the case of a challenge to the constitutionality of the enactment itself, it is, in the interests of justice, unworkable. One major reason is that no suits are allowed "until appeal shall have been duly made to the Commissioner of [the] Internal Revenue, … and a decision of the Commissioner has been had therein."[11] But the Commissioner, as an executive branch official, cannot declare a statute uncon-

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stitutional. And so, the end result of an appeal in such cases must always be to uphold the tax (or to do nothing, whereby the suit can proceed after six months). Thus, the primary result of this process is simply to postpone any judicial decision on the constitutionality of a tax.

Attorney General Richard Olney, in his arguments at the rehearing gives a good example of how that timing affects the overall picture:

> Though of minor consequence, it is certainly relevant to point out that, if the new exposition of the Constitution referred to is to prevail, the United States has under previous income tax laws collected vast sums of money which on every principle of justice it ought to refund, and which it must be assumed that Congress will deem itself bound to make provision for refunding by appropriate legislation.[12]

Of course, Olney wasn't arguing against the Anti-injunction Act. Rather, he was referring to the effect of an unfavorable ruling in the *Pollock* rehearing on the sums collected during the War of Northern Aggression. In other words, if the court were to find that income taxes in general were direct, then it would be unjust for the government to keep all the money it previously collected by means of an indirect income tax. Yet, despite Olney's assertion, and even though the Supremes did indeed declare them to be direct taxes, Congress apparently did NOT deem itself bound to return the taxes it had collected on the income from real or personal property — or at least, they were willing to live with the injustice of keeping their ill-gotten gains.

Since the 1894 income tax was to become due and payable beginning on July 1, 1895,[13] Pollock's timely suit resulted in a favorable decision months before the public would be adversely affected by the unconstitutional provisions. But if the decision had been delayed because of the restrictions imposed by the Anti-injunction Act, millions of people might have already been damaged, and forced to jump through hoops to get back what should never have been demanded of them in the first place.[14] Such would have been the case if Frank Brushaber had prevailed in his challenge of the 1913 income tax. Even though it was originally filed in the District Court on March 13, 1914, his suit wasn't decided by the Supreme Court until January 24, 1916. Thus, two years of taxes and returns had already been collected.

Justice Edward Douglass White (1845-1921) was a Louisiana lawyer who fought on the side of the Confederacy, and eventually became a U.S. Senator. He was appointed to the Supreme Court in 1894, and remained there until he died in 1921. In addition to flip-flopping concerning the Anti-Injunction Act, he is known for joining the majority in the notorious *Plessy v. Ferguson* decision, and for writing the opinion in *Arver v. United States*, 245 U.S. 366 (1918), also known as the *Selective Draft Law Cases*, upholding the Selective Service Act of 1917. He held that a military draft did not violate the Thirteenth Amendment's prohibition of involuntary servitude, nor the First Amendment's protection of freedom of conscience.

Now, that's not to say it was the fault of the Anti-injunction Act for that two-year time lapse, because Brushaber used the same approach as Pollock and Hyde to get around that. It's interesting that White, who as an Associate Justice in the *Pollock* case argued so rigorously against allowing that case to proceed, accepted jurisdiction of the *Brushaber* case — as Chief Justice, having succeeded Fuller in the post — without a squawk:

> To put out of the way a question of jurisdiction we at once say that in view of these averments and **the ruling in *Pollock v. Farmers' Loan & T. Co.*, sustaining the right of a stockholder to sue to restrain a corporation under proper averments from voluntarily paying a tax charged to be unconstitutional** on the ground that to permit such a suit **did not violate the prohibitions of § 3224, Revised Statutes, against enjoining the enforcement of taxes**, we are of opinion that the contention here made that there was no jurisdiction of the cause, since to entertain it would violate the provisions of the Revised Statutes referred to, is without merit.[15]

Now, perhaps Justice White just felt so strongly about precedent that he simply acquiesced to the majority's decision in *Pollock* regarding jurisdiction. Or, could it be that he left his objections from that earlier case by the wayside specifically so that as Chief Justice, he could use the case as a platform to solidify his views on the 16th Amendment for the public at large? We'll not likely ever find the answer to that question, but that won't stop us from looking some more into White's dissents in the *Pollock* case in future installments. Stay tuned!

12. The citation for this version of the rehearing is 39 L.Ed. 1108 (hereinafter "L.Ed 2nd"), and this quote is on page 1110.
13. 28 Stat. at L. 509, 555; § 30.
14. The same principle applies to the various rules used by the Supreme Court to avoid ruling on constitutional questions. See my series "Steering Clear of the Constitution" in the Nov. 2008, Jan. 2009, and Mar. 2009 *Liberty Tree* for more on this issue.
15. *Brushaber v. Union Pacific Railroad Co.*, 240 U.S. 1, 9 (1916). .