

from

Was Grandpa Really a Moron?
Critical Inquiries for a New American Century

by

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**A Brief Introduction To The Fascinating Truth About The
Income Tax**



PART ONE

The purpose of this brief study is to introduce a couple of key facts that must be known by anyone hoping for a clear understanding of the legal character of the United States federal income tax (and the state and local impositions of the same tax). We're going to start by:

- 1. Examining the meaning of the Constitutional term "capitation" (a tax effectively falling on revenue generally-- that is, a tax on "what comes in", either in its entirety, or on any part, of otherwise undistinguished revenue); and*
- 2. Establishing that the income tax is, and always has been, an exercise-of-privilege-based "piece of the action" excise tax on distinguished activity, rather than a capitation, and that "income" as meant in the context of the tax refers only to that distinguished activity (the amount of which is measured by the dollar value it produces).*

The Meaning of "Capitation"

There is a persistent misunderstanding in America about the meaning of one of the key terms in our own federal Constitution. That term is "capitation", and it is the sole specifically-listed type of direct tax in the Constitution.

It's a funny thing that this term should be so poorly understood, and has seen little effort in the past to discern its meaning. Under the utterly explicit and still-controlling prescription of the Constitution, anything which qualifies as a capitation is subject to the rule of apportionment (by which the total to be collected with each imposition of the tax is divided among the states in proportion to their shares of the national population, and is then collected and remitted by the state governments). The reciprocal of this, of course, is that in order for the income tax we know and love (or any other tax, for that matter) to be administered WITHOUT apportionment, and yet still be valid, it CANNOT be a capitation. Before we discuss what the tax IS then, let's have a close look at what it CANNOT be...

"CAPITATION, A poll tax; an imposition which is yearly laid on each person according to his estate and ability.

2. The Constitution of the United States provides that "no capitation, or other direct tax, shall be laid, unless in proportion to the census, or enumeration, therein before directed to be taken." Art. 1, s. 9, n. 4. See 3 Dall. 171; 5 Wheat 317. Bouvier's Law Dictionary, 6th Ed. (1856). (Emphasis added.)

In a way, this simple definition from what was, in its time, the Congressional law dictionary of record more-or-less tells us all that we need to know. A capitation is an annual imposition on each person measured by his estate and ability. Some may split hairs on the meaning of "estate", but "ability" pretty clearly refers to ability to pay, and that pretty clearly means "revenue". On the other hand, the reference to a "poll

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tax" leads to some confusion as well, especially when more modern references are relied upon.

For instance, the entire definition of "capitation" offered by Black's Law Dictionary (fifth edition) is as follows:

***Capitation tax.** A poll tax (q.v.). A tax or imposition upon the person. It is a very ancient kind of tribute, and answers to what the Latins called "tributum", by which taxes on persons are distinguished from taxes on merchandise, called "vectigalia".*

Not very illuminating.

Turning to the definition of "poll tax" in the same collection, we find:

***Poll-tax.** A capitation tax; a tax of a specific sum levied upon each person within the jurisdiction of the taxing power and within a certain class (as, all males of a certain age, etc.) without reference to his property or lack of it.*

Poll taxes as a prerequisite to voting in federal elections are prohibited by the 24th Amendment and as to state elections such were held to be unconstitutional in Harper v. Virginia Bd. of Elections, 383 U.S. 663, 86 S. Ct. 1079, 16 L.Ed2d 169."

If one makes no further study of this subject, and relies on Black's definitions, one would conclude that a "capitation" is just a "poll tax" (that is, a "head tax"), and might even confuse it with a "voting tax"-- that is, a tax taken at the polling place before the right to vote can be exercised.

However, Black's definitions are woefully incomplete and misleading. A capitation is NOT simply a "poll tax", and a "poll tax" is not a "voting tax" (as is self-evident when the Constitution's "apportionment" clause is considered, since apportionment can't apply to a "voting tax", and is superfluous in regard to "head tax"). Nonetheless, since most have never made a study of this subject, sloppy presentations in prominent

sources such as Black's have muddied the subject enough to make "capitation" a cognitive 'hiccup' term. Far too many who encounter the term, even while poring over the language of our fundamental law, simply skim past with no registration of its meaning or import.

So, just to clear up (or forestall) such confusion, let's examine the relevant observations of a couple of fellows who were inarguably in a position to know what they were talking about. We'll start with Alexander Hamilton, one of the chief authors of the Constitution itself, who discussed direct and indirect taxes in the first tax case argued before the United States Supreme Court, observing that:

"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."

In addition to his inclusion of general assessments on personal estates as being in the class of direct taxes, note also that Hamilton does NOT characterize "poll tax" as just an alternative name for "capitation"; more important still, as will become clearer in a moment, he specifically declares "poll taxes" to also be among the direct taxes subject to the apportionment rule.

Now let's turn to the singular expert on this subject, and the one whose work guided the framers in their use of terms in the taxing clauses, Adam Smith, author of 'The Wealth Of Nations', perhaps the most important work ever written about economics and taxation:

"The taxes which, it is intended, should fall indifferently upon every different species of revenue, are capitation taxes,"... "Capitation taxes, if it is attempted to proportion them to the fortune or revenue of each contributor, become altogether arbitrary. The state of a man's fortune varies from day to day, and without an inquisition more intolerable than any tax, and renewed

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at least once every year, can only be guessed at. "...Capitation taxes, so far as they are levied upon the lower ranks of people, are direct taxes upon the wages of labour, and are attended with all the inconveniences of such taxes. ..." In the capitation which has been levied in France without any interruption since the beginning of the present century, the highest orders of people are rated according to their rank by an invariable tariff; the lower orders of people, according to what is supposed to be their fortune, by an assessment which varies from year to year." (Bear in mind that Smith is using the common word 'wages', not the custom-defined legal term of the same spelling found in the modern revenue laws.)

Smith goes on to discuss the version of capitations imposed under the name of "poll taxes", as well, observing that in the first poll tax, for instance, many were taxed according to their supposed fortune, being *"assessed at three shillings in the pound of their supposed income"*.

Clearly, a general, indiscriminate tax on income read as "all that comes in", or on "every species of revenue", qualifies as either a "capitation" or a "poll tax" (or both) as each term is properly understood. Consequently, we know that any such tax must, under the provisions of the Constitution, be administered exclusively by the rule of apportionment.

I'll close this introductory discussion of "capitations" with the acknowledgment by the United States Supreme Court, in the case of *Pollock v. Farmer's Loan & Trust*, 157 U.S. 429 (1895), that the understanding of the term that I have presented here is precisely the one which informed the Framers of the Constitution when choosing the wording "capitations and other direct taxes" in laying down the rule of apportionment. Declaring the meaning of the phrase "capitations and other direct taxes" in its ruling in the case, the court resorts to the authority of Albert Gallatin, Pennsylvania state congressman, United States Representative and Senator, United States

Minister to England and France, respectively, and the longest serving Secretary of the Treasury in American history, and says:

"...Albert Gallatin, in his Sketch of the Finances of the United States, published in November, 1796, said: 'The most generally received opinion, however, is that, by direct taxes in the constitution, those are meant which are raised on the capital or revenue of the people;...'

...

"He then quotes from Smith's Wealth of Nations, and continues: 'The remarkable coincidence of the clause of the constitution with this passage in using the word 'capitation' as a generic expression, including the different species of direct taxes-- an acceptance of the word peculiar, it is believed, to Dr. Smith-- leaves little doubt that the framers of the one had the other in view at the time, and that they, as well as he, by direct taxes, meant those paid directly from the falling immediately on the revenue;...'"

The Origin of the Tax; Its Character as an Excise; and the Meaning of "Income"

"The name by which the tax is described in the statute is, of course, immaterial. Its character must be determined by its incidents..." Dawson v. Kentucky Distillers & Warehouse Co., 255 U.S. 288 (1921)

The Lincoln administration was aware of all that we have just discussed when, in 1862, it instituted the income tax we've since come to know so poorly, but loathe so well. The Lincoln administration knew the Constitution prohibits capitations and other direct taxes unless apportioned; it knew a tax that actually touched upon the "all species of revenue" which constitute the broad class of receipts known as "income" in the common usage of that word WOULD be a capitation, and had under various names always been recognized and designated as a direct tax throughout history; and it also knew that apportioned direct taxes were really only suited to one-time debt-retirements and had traditionally been used exclusively for

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that purpose.

One-time debt-retirement was not what the Lincoln administration needed or wanted. Lincoln was looking to finance an ongoing war effort, and he needed the kind of tax that, once instituted, keeps on giving and giving without the inconveniences of repeated legislation and voting. In short, he wanted an excise, and that's what he imposed-- an excise on certain activities, measured by (and typically paid out of) the revenue they produced.

"...in Springer v. U. S., 102 U.S. 586 (1880), it was held that [the] tax upon gains, profits, and income was an excise or duty, and not a direct tax, within the meaning of the constitution, and that its imposition was not, therefore, unconstitutional." United States Supreme Court, Pollock v. Farmer's Loan & Trust, 158 U.S. 601, (1895);

"...taxation on income was in its nature an excise entitled to be enforced as such,"

United States Supreme Court, Brushaber v. Union Pacific R. Co., 240 U.S. 1 (1916), quoting and reiterating language used in its ruling in Pollock v. Farmer's Loan and Trust.

*"I hereby certify that the following is a true and faithful statement of the gains, profits, or income of _____, of the _____ of _____, in the county of _____, and State of _____, whether derived from any kind of property, rents, interest, dividends, salary, or from any profession, trade, employment, or vocation, or from any other source whatever, from the 1st day of January to the 31st day of December, 1862, both days inclusive, and subject to an income tax **under the excise laws** of the United States."*

(from the first income tax return form, emphasis added).

As legislative draftsman for the United States Treasury Department F. Morse Hubbard put it in no uncertain terms while

testifying before Congress in 1943:

"The income tax... ...is an excise tax with respect to certain activities and privileges which is measured by reference to the income [earnings] which they produce."

House Congressional Record, March 27, 1943, page 2580

* * *

Perhaps because the tax can easily be mistaken for a tax on the revenue itself (due to the fact that the amount of activity being taxed is measured by the dollars produced, and the amount of tax-due is determined by applying the rate of tax to that amount of dollars), the name "income tax" recommended itself to Congress; nonetheless, the tax is not, for reasons we have observed, any kind of general tax on income read as "all that comes in". Instead, it is a tax on only a specialized subset of the larger class of income, consisting exclusively of revenues attributable to the voluntary, profitable use of federal privilege, property or powers-- that is, revenues in which the federal government has a direct ownership interest, and to which it can therefore exercise a direct claim as a matter of right.

(As an aside, it is worth noting that within the realm of federal privilege, and within the context of the tax, though, "income" COULD be described as effectively meaning "all that comes in", and sometimes is so described by courts and government agencies. This is because every activity involving the use of federal privilege, property or prerogative measurable by dollars (or dollar-value) produced qualifies as the "income" subject to the tax:

"(a) GENERAL DEFINITION. 'Gross income' includes gains, profits, and income derived from salaries, wages, or compensation for personal service . . . of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or

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dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. . . .” (emphasis added)
Commissioner v. Glenshaw Glass Co., 348 U.S. 426 (1955)

So, to the extent that one operates within the federal universe (so to speak), “income” DOES mean “all that comes in”, and may be described that way within the appropriate context. But this doesn’t extend the reach of the tax to activities outside of that universe. Thus, even within that universe and context, the more accurate and complete definition of the term “income” is “all that comes in here”.)

The language of the original income tax enactment is helpful in illuminating the true character of the tax and the “income” to which it applies:

*‘An Act to provide Internal Revenue to support the Government and to pay interest on the Public Debt’
Sec. 86. And be it further enacted, That on and after the first day of August, eighteen hundred and sixty-two, there shall be levied, collected, and paid on all salaries of officers, or payments to persons in the civil, military, naval, or other employment or service of the United States, including senators and representatives and delegates in Congress, when exceeding the rate of six hundred dollars per annum, a duty of three per centum on the excess above the said six hundred dollars; and it shall be the duty of all paymasters, and all disbursing officers, under the government of the United States, or in the employ thereof, when making any payments to officers and persons as aforesaid, or upon settling and adjusting the accounts of such officers and persons, to deduct and withhold the aforesaid duty of three per centum, and shall, at the same time, make a certificate stating the name of the officer or person from whom*

such deduction was made, and the amount thereof, which shall be transmitted to the office of the Commissioner of Internal Revenue, and entered as part of the internal duties;... (“Income” derived from less formalized federally-connected activities, such as investment in, or contracts with, federal entities is also taxed under other provisions in the act.)

It is because the tax confines itself solely to revenue-generating federal activities as listed in part in this section of law that it is NOT a capitation-- that is, a tax on revenue generally. This limited scope also prevents the “income” tax from amounting to a tax burdening the exercise of individual rights, by the way-- a transgression which by itself would drop the tax squarely into the category of “direct” even without regard to the capitation issue. As the Supreme Court observes in the case of Knowlton v. Moore, 178 U.S. 41 (1900), quoting the long-standing official French tax law definition as being illustrative of the distinctions drawn in the U. S. Constitution:

“Direct taxes bear immediately upon persons, upon the possession and enjoyments of rights;”

Many other rulings make the same, utterly fundamental point, which is self-evident, in any case. To tax undistinguished revenue simply as an exercise of power is to tax a person's exercise of the fundamental individual right to work or trade.

“The right to follow any of the common occupations of life is an inalienable right...

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. The patrimony of the poor man lies in the strength and dexterity of his own hands, and to hinder his employing this strength and dexterity in what manner he thinks proper, without injury to his neighbor, is a plain violation of this most sacred property.’” United States Supreme Court, *Butcher's Union Co. v. Crescent City Co.*, 111 U.S. 746 (1883);

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"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"
United States Supreme Court, *Coppage v. Kansas*, 236 U.S. 1 (1915).

On the other hand, to tax revenue proceeding from the voluntary, profitable exercise of the government's own property or powers (whether directly or by proxy through investment) is to impose an indirect tax having nothing to do with the taxpayer's rights. Instead, such a tax merely involves an ownership-related claim to a piece of the privileged "action".

"PRIVILEGE: A particular benefit or advantage enjoyed by a person, company, or class beyond the common advantages of others citizens. An exceptional or extraordinary power of exemption. A particular right, advantage, exemption, power, franchise, or immunity held by a person or class, not generally possessed by others." Black's Law Dictionary, 6th Edition.

...the requirement to pay [excise] taxes involves the exercise of privilege." United States Supreme Court, *Flint vs. Stone Tracy Co.* 220 U.S. 107 (1911);

"The terms 'excise tax' and 'privilege tax' are synonymous. The two are often used interchangeably." *American Airways v. Wallace*, 57 F.2d 877, 880 (Dist. Ct., M.D. Tenn., 1937)

"The 'Government' is an abstraction, and its possession of property largely constructive. Actual possession and custody of Government property nearly always are in someone who is not himself the Government but acts in its behalf and for its purposes. He may be an officer, an agent, or a contractor. His personal advantages from the relationship by way of salary, profit, or beneficial personal use of the property may be taxed..." United

States Supreme Court, United States v. County of Allegheny, 322 US 174 (1944)

Its confinement to activities distinguished by privilege-dependence is what keeps the "income" tax from crossing the line into being both a capitation and a burden on the exercise of natural rights.

For the sake of clearing away possible cognitive stumbling blocks it is necessary to point out that while the realm in which the tax operates is limited, within that realm the tax is quite comprehensive. As was noted previously, within the federal universe, EVERY gainful activity qualifies as "income"-producing, because every such activity is "privileged" in the relevant sense. While working for the Post Office might not seem like the exercise of a "privilege" as we are accustomed to think of that word (as opposed to, say, the privilege involved in profiting from investment in a railroad running on federally-granted or -subsidized land, or owning or investing in a national bank or other federal instrumentality), in a legal sense it very much is. ANYTHING one does that requires the permission of another is the exercise of a privilege, and can properly be subject to conditions such as taxes.

In fact, legally speaking, even something as mundane as being allowed to borrow my lawnmower for use in your landscaping business is a privilege-- something to which you have no inherent right and which I can withhold from you-- or tax-- at my pleasure. Opening and operating "Joe's Delivery Service" is a matter of right, and anyone can do it without anyone else's permission. Working for the United States Post Office, on the other hand, can only be done with the permission of the United States. By confining itself exclusively to receipts proceeding from such voluntarily-engaged-in, but federal-privilege-dependent activities-- whether those of a federal worker, investor, office-holder or cash-grant beneficiary-- the "income tax" as practiced in America does not cross the line

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from an indirect tax to what would otherwise inescapably be a direct tax, and one which would require the mechanism of apportionment in its administration.

It is true that the external appearance of many of these activities is indistinguishable from those conducted as matters of private right. A doctor working for the federal government practices medicine in the same manner as a doctor in private enterprise does. A plumber in the civil service uses the same tools and skills as the one that comes to your home. An investor buying stock in a national bank or railroad, or other federal corporation or instrumentality, places those orders with his broker at the same time that he buys stock in Sears, and his dividend check may even combine the profits from all of these investments.

However, the superficial similarity of private and privileged activities masks a fundamental difference between them, which is that those in the subset to which the tax applies are made possible only due to the existence, and with the cooperation, of the federal government. In a very real and explicit sense, the aptly-named "income" tax in this country is, in fact, a "FEDERAL income tax". A detailed, accurate and comprehensive study of the income tax law-- such as that presented exclusively in 'Cracking the Code- The Fascinating Truth About Taxation In America' (CtC)-- makes clear that this distinction is thoroughly embedded in that law. In no respect whatsoever does the federal income tax purport to be anything but the limited, specialized tax that it must be, or to touch upon any revenue not distinguished as noted here-- decades of diligent efforts to obscure that fact in the public mind notwithstanding.

For instance, a close examination of the current statutory structure defining "wages"-- a term central to the measurement and reporting of "income"-taxable activities by paid-performers-of-services-- illustrates that the tax remains scrupulously adherent to its proper Constitutional limits. The

term confines itself to remuneration paid to:

"...an officer, employee, or elected official of the United States, a State, or any political subdivision thereof, or the District of Columbia, or any agency or instrumentality of any one or more of the foregoing."*

*"State", as used in this statute, has its own custom definition in the law.

This definition also explicitly covers remuneration paid for service as officers of federal corporations, and implicitly covers other federal workers/office holders not listed, by virtue of the "includes" mechanism discussed briefly below and in detail in CtC. (NOTE: The language presented above is from the general "wage withholding" section of the internal revenue laws. The more narrowly focused FICA "income" surtaxes are also measured and reported using the term "wages", but deploy a somewhat more elaborate structure to define the term, which is also discussed in detail in CtC.) Similarly, the statutory definition of the conduct of a "trade or business", the receipts from which are to be reported and taxed as "income", is:

"...the performance of the functions of a public office."

By virtue of the statutory rule of construction concerning "includes"-- another custom legal term deployed in the definitions of both of "wages" and "trade or business", these terms are amenable to a narrowly limited potential expansion to cover other things of the same class (legal character) as those already listed, but nothing else.

"Includes" and "including" are deployed in a number of key statutes by which the "income" tax is laid, and the terms have been a source of confusion in some quarters, even within the legal profession. Thus, they merit an extended discussion.

Normally, "includes" and "including" are flatly restrictive. As United States Supreme Court Chief Justice John Marshall derisively observed when presented with a strained argument to the contrary in an 1808 case:

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"It [is argued that] the word "including" means "moreover", or "as well as"; but if this was the meaning of the legislature, it was a very embarrassing mode of expressing the idea." United States v. The Schooner Betsey and Charlotte, 8 U.S. 443 (1808).

Marshall goes on to declare that the proposition that "moreover" or "as well as" is, in fact, what is meant by the legislative use of "including" (or, by extension, "includes") is nonsense. The court re-iterates this rule a century later:

"The [state supreme] court also considered that the word 'including' was used as a word of enlargement, the learned court being of the opinion that such was its ordinary sense. With this we cannot concur." Montello Salt Co. v. Utah, 221 U.S. 452 (1911)

In federal tax law, though, "includes" and "including" are permitted a little bit of latitude, being controlled by the following rule:

"Includes and including: The terms "includes" and "including" when used in a definition contained in this title shall not be deemed to exclude other things otherwise within the meaning of the term defined." Rev. Act of 1938 §901(b) (Codified at 26 USC 7701(c).)

The Department of the Treasury has helpfully clarified the meaning of this provision with the following regulatory language:

"The terms "includes and including" do not exclude things not enumerated which are in the same general class;" 27 CFR 26.11 and 27 CFR 72.11

The United States Supreme Court has been even more helpful:

"[T]he verb "includes" imports a general class, some of whose particular instances are those specified in the definition. This view finds support in § 2(b) of the Act, which reads: "The terms 'includes' and 'including,' when used in a definition contained in this title, shall not be deemed to exclude other things otherwise within the

meaning of the term defined.” Helvering v Morgan’s, Inc, 293 U.S. 121, 126 fn. 1 (1934)

The court refers to and re-iterates this observation in Federal Land Bank of St. Paul v. Bismarck Lumber Co. 314 U.S. 95, 62 S.Ct. 1 U.S. (1941):

“[I]ncluding... ...connotes simply an illustrative application of the general principle.”

(That is, the enumerated items in a definition in which “including” is deployed “illustrate”-- identify, and thus establish-- the contours of the class which the defined term represents-- the “general principle” of its application). In Massachusetts v. EPA, 549 U.S. 497 (2007), the court re-iterates this doctrine concerning the meaning of “includes” and “including” in a dissent on other grounds authored by Justice Scalia and joined by Chief Justice Roberts and Justices Thomas and Alito:

“The word “including” can indeed indicate that what follows will be an “illustrative” sampling of the general category that precedes the word. Federal Land Bank of St. Paul v. Bismarck Lumber Co., 314 U.S. 95, 100 (1941).” (Internal quote marks in the original.)

The reference to the Federal Land Bank ruling, which itself drew on the Helvering v. Morgan ruling, makes clear that the circumstances under which the 2007 court recognizes that the use of “including (or “includes”) indicates that what follows is an illustrative sampling of a general category being defined is when their use is under the influence of the language of 26 USC 7701(c).

The principle involved in the “includes” mechanism is largely that described by the Supreme Court in Gustafson v. Alloyd Co. (93-404), 513 US 561 (1995):

“...a word is known by the company it keeps (the doctrine of noscitur a sociis). This rule we rely upon to avoid ascribing to one word a meaning so broad that it

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is inconsistent with its accompanying words, thus giving "unintended breadth to the Acts of Congress."

The 1st Circuit Court of Appeals puts it this way in *Brigham v. United States*, 160 F.3d 759 (1st Cir. 1998):

*"[T]he terms 'includes' and 'including' . . . shall not be deemed to exclude other things otherwise within the meaning of the term defined." 26 U.S.C. § 7701(c). In light of this we apply the principle that a list of terms should be construed to include by implication those additional terms of like kind and class as the expressly included terms. *fn2: This follows from the canon noscitur a sociis, "a word is known by the company it keeps." Neal v. Clark, 95 U.S. 704, 708-09 (1878)."*

The principle is clarified by these additional, related rulings:

"When a statute includes an explicit definition, we must follow that definition, even if it varies from that term's ordinary meaning." Stenberg v. Carhart, 530 U.S. 914 (2000)

"It is axiomatic that the statutory definition of the term excludes unstated meanings of that term." Meese v. Keene, 481 U.S. 465 (1987)

"Of course, statutory definitions of terms used therein prevail over colloquial meanings. Fox v. Standard Oil Co., 294 U.S. 87, 95, 55 S.Ct. 333, 336." Western Union Telegraph Co. v. Lenroot, 323 U.S. 490 (1945)

These rulings reflect the fact that when a word becomes a statutorily-defined "term", its original meaning is entirely stripped away and replaced with the new meaning described. This is why, for instance, the definition of "employee" at which we looked earlier explicitly lists "federal employees". Despite being identically spelled and pronounced, the statutorily-defined-term doesn't mean "anyone who works for a boss", or whatever dictionary definition you might find for the common word 'employee'; nor does it mean 'employee' as commonly-

defined plus the additional listed persons or types (by virtue of which federal employees would have been encompassed without being listed). When the former understanding and usage is intended, no statutory definition is provided; and when the latter construction is intended qualifying phrases such as, "includes, but is not limited to..." and "including, but not limited to..." are deployed, as can be found in dozens of places within the body of federal tax law.

If a definition IS provided, and "includes" is used without additional qualifying language (as in the definition of "employee" discussed above) the term only means what the enumerated list describes-- in this case, persons working for the federal government or its subordinate entities, under a variety of different labels and in a variety of different capacities. Thanks to the limited-expansion rule provided at 7701(c), the meaning of the defined-term "employee" can be considered to cover others not listed who also work for the federal government or its subordinate entities (and who are thus within the class established by the existing list), but no one else. These rules and statutory practices play an important role in preventing the "income" tax from functioning as a de facto capitation or other direct tax.

PART TWO

OK, now we've seen that the income tax is, always has been, and can only be, an exercise-of-privilege-based "piece of the action" excise tax on distinguished activity, rather than a capitation, and that "income" as meant in the context of the tax refers only to that distinguished activity (the amount of which is measured by the dollar value it produces).

Now we'll look at what the 16th Amendment was all about, and discover that, rather than instituting, or authorizing the "income" tax, the amendment concerned nothing more than

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closing a loophole opened by a late-nineteenth-century Supreme Court ruling that briefly impeded the application of the tax to a particular kind of "income", which is distinguished from the larger subclass of distinguished, revenue-measured taxable activity by virtue of its connection to personal property.

"The whole body of internal revenue law in effect on January 2, 1939... ..has its ultimate origin in 164 separate enactments of Congress. The earliest of these was approved July 1, 1862; the latest, June 16, 1938."

-Preamble to the 1939 Internal Revenue Code

It is clear that were the distinct, limited meaning of the "income" subject to the "income tax" to be eroded away, and the tax come to be applied to "all that comes in", it would be, and would have to be recognized as, a capitation or other direct tax. The United States Supreme Court explicitly declares in its 1916 ruling in *Brushaber v. Union Pacific R. Co.*, 240 U.S. 1 (while specifically considering the limited meaning and effect of the 16th Amendment) that should the tax ever come to exceed its proper boundaries,

"the duty would arise to disregard form [that is, any pretense by which it is made to appear that the tax is being confined to its proper limits when it is not, such as by creatively construing the meaning of "income", or the use of any pretense, scheme or construction by which non-specialized revenue or activities are made to appear otherwise so as to be subjected to the tax] and consider substance alone [that is, what the tax is actually falling upon as a practical reality], and hence subject the tax to the regulation as to apportionment which otherwise as an excise would not apply to it."

But, of course, the law behind the tax never has exceeded those boundaries. This is why the very tax which is administered today, on the same activities as it is administered today-- without apportionment, and without any pretense of relief of the apportionment rule, such as is inaccurately ascribed

to the 16th Amendment-- could be laid and administered for decades BEFORE that amendment, and yet be upheld by the United States Supreme Court.

For example, in *Gray v. Darlington*, 82 U.S. 63 (1872), the court had occasion to rule on a "capital gains" application of the tax, citing the following language from the 1867 statute,

"There shall be levied, collected, and paid annually upon the gains, profits, and income of every person, . . . whether derived from any kind of property, rents, interest, dividends, or salaries, or from any profession, trade, employment, or vocation, . . . or from any other source whatever, . . . a tax of five per centum on the amount so derived over \$ 1000 . . . And the tax herein provided for shall be assessed, collected, and paid upon the gains, profits, and income for the year ending the 31st of December next preceding the time for levying, collecting, and paying said tax."

The court finds no issue with the tax generally, but merely holds that,

"The rule adopted by the officers of the revenue in the present case would justify them in treating as gains of one year the increase in the value of property extending through any number of years, through even the entire century. The actual advance in value of property over its cost may, in fact, reach its height years before its sale; the value of the property may, in truth, be less at the time of the sale than at any previous period in ten years, yet, if the amount received exceed the actual cost of the property, the excess is to be treated, according to their views, as gains of the owner for the year in which the sale takes place. We are satisfied that no such result was intended by the statute."

Again, in *Springer v. U. S.*, 102 U.S. 586 (1880), a test case of which the Supreme Court declares that:

"The central and controlling question in this case is whether the tax which was levied on the income, gains, and profits of the plaintiff in error, as set forth in the record, and by pretended virtue of the acts of Congress

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and parts of acts therein mentioned [the act of June 30, 1864, as amended by the act of March 3, 1865-- the relevant language of which duplicated that quoted above in the Gray case], is a direct tax;”

and that:

“The plaintiff in error advises us by his elaborate brief ‘that on the trial of the case below the proceedings were merely formal,’ and that ‘no arguments or briefs were submitted, and only such proceedings were had as were necessary to prepare the case for the Supreme Court’”;

the court ultimately concludes (as summarized in a later case) that,

“[The] tax upon gains, profits, and income [is] an excise or duty, and not a direct tax, within the meaning of the constitution, and that its imposition [is] not, therefore, unconstitutional.” United States Supreme Court, Pollock v. Farmer's Loan & Trust, 158 U.S. 601, 1895.

In the Pollock ruling itself, the most exhaustive judicial consideration of the federal taxing power undertaken in American history (and another ruling preceding the 16th Amendment), the Supreme Court observes first that when used in the generic sense of “all that comes in”, a tax on income is inherently a direct tax:

“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.”

and,

“At the time the constitution was framed and adopted, under the systems of direct taxation of many of the states, taxes were laid on incomes from professions, business, or employments...”

The court then proceeds to distinguish the tax laid by the federal income tax statutes as being only on a special class of receipts amenable to taxation by excise (that is, the class we have been referring to as "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.**" (Emphasis added)*

(Remember, as noted in the Brushaber decision, a tax does not qualify as an excise because the government chooses to call it one [form], but because its character-- both as to object and application-- is, in every particular, such a tax [substance].) The court goes on to point out that this excise on "income" is, in fact, what is taxed as such under the federal income tax structure:

*"If [the portion of the 1894 Revenue Act laying the tax on income from real estate] 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. 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 [because the real estate and personal property exactions were not, in fact, laid by apportionment in the act], and the scheme must be considered as a whole." (Emphasis added)*

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The continued strict and scrupulous adherence of the "income" tax to the same proper and necessary boundaries by which it has been confined since its inception in 1862 is why the Supreme Court is able to repeatedly declare over the years SINCE the 16th Amendment that the amendment did not create a new tax:

"The provisions of the Sixteenth Amendment conferred no new power of taxation..." Stanton v. Baltic Mining Co., 240 U.S. 103 (1916);

did not extend the tax to anything it had not embraced before:

"The Sixteenth Amendment, although referred to in argument, has no real bearing and may be put out of view. As pointed out in recent decisions, it does not extend the taxing power to new or excepted subjects..." Peck v. Lowe, 247 U.S. 165 (1918);

did not create authority for some hybrid tax which could fall upon any traditional or inherent object of a direct tax (such as a general income tax) but which was now simply not subject to the rule of apportionment:

"We are of opinion, however, that the confusion is not inherent, but rather arises from the conclusion that the 16th 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. And the far-reaching effect of this erroneous assumption will be made clear by generalizing the many contentions advanced in argument to support it..." Brushaber v. Union Pacific R. Co., 240 U.S. 1 (1916);

and cannot be otherwise construed, since to do so would cause:

"...one provision of the Constitution [to] destroy another; that is, [it] would result in bringing the provisions of the Amendment [supposedly] exempting a direct tax from apportionment into irreconcilable conflict with the general requirement that all direct taxes be apportioned." Id;

and yet continue to find the unapportioned "income" tax Constitutional. The tax didn't need any of these changes in order to be Constitutional, because it didn't become anything it hadn't previously been upon the advent of the 16th Amendment. It still is not, and cannot be, a tax on undistinguished, unspecialized activities (or the revenue produced thereby).

This point bears repeating, due to the pervasiveness of tax-agency-cultivated misunderstanding about the 16th Amendment: All these observations by the Supreme Court are simultaneously true and in harmony with each other **because the limited nature of the tax has never changed**, the 16th Amendment notwithstanding; in fact, these observations CAN ONLY be simultaneously true and in harmony with each other because the limited nature of the tax has never changed:

"[T]he settled doctrine is that the Sixteenth Amendment confers no power upon Congress to define and tax as income without apportionment something which theretofore could not have been properly regarded as income." Taft v. Bowers, 278 US 470, 481 (1929) (Emphasis added.)

In 1988, in *South Carolina v. Baker*, 485 U.S. 505, the Supreme Court revisits the subject and observes that,

"The legislative history merely shows... ...that the sole purpose of the Sixteenth Amendment was to remove the apportionment requirement for whichever incomes were otherwise taxable." (Emphasis added.)

The court is (again) recognizing that the 16th Amendment operates only on those "incomes" which already were, and always have been, inherently taxable under the "income" excise, and which had been so taxable-- without apportionment-- BEFORE the 16th amendment, until the application of the tax in certain cases was briefly thwarted by the Pollock loophole in 1895. Howard M. Zaritsky, Legislative Attorney of the American

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Law Division of the Library of Congress, helpfully summarizes all of this in his 1979 Report NO. 80-19A entitled "Some Constitutional Questions Regarding The Federal Income Tax Laws":

"The Supreme Court, in a decision written by Chief Justice White, first noted that the Sixteenth Amendment did not authorize any new type of tax, nor did it repeal or revoke the tax clauses of Article I of the Constitution, quoted above. Direct taxes were, notwithstanding the advent of the Sixteenth Amendment, still subject to the rule of apportionment..."

So, what exactly DID the 16th Amendment do? It simply closed a "loophole" introduced into the administration of the federal income tax by the Supreme Court in its ruling regarding the taxation of "income" from invested personal property in the case of *Pollock v. Farmer's Loan & Trust* discussed above.

The *Pollock* ruling held that the application of the tax to the proceeds of investments and real estate leases functioned as a property tax rather than a federal income tax. The reasoning was that to tax such gains-- even when the investments and leases were in, or to, federal entities, as was involved in the case-- is to effectively tax the stock and land itself. Since both are personal property, such a tax was really a property tax and not, in this respect, an excise which could be applied without apportionment. With this ruling the court struck down ten sections of the recently reactivated federal income tax, which had been dormant since its last two-year implementation had expired in 1873.

The effect of this reasoning was to relieve the Robber-Baron class, which was heavily invested in money-making federal instrumentalities such as national banks and railroads and had numerous sweet-heart deals leasing property to the

feds, from the burden of the tax. This didn't sit well with the growing and reactionary populist movement, which had little patience with the idea that a cadre of coupon-clipping fat cats-- widely, and accurately, perceived as pulling Washington's strings and benefiting handsomely thereby-- should escape the tax, while revenue tariffs, by which even the poorest Americans were affected, stood relatively high in order to make up the loss.

The populists demanded an amendment to the Constitution to close the loophole, and eventually succeeded with the 16th Amendment, which declares that what is otherwise inherently taxable under the federal income tax cannot be shielded therefrom by a resort to the source of the revenue involved. Treasury Department legislative draftsman F. Morse Hubbard usefully summarizes this sole and exclusive effect of the amendment in his 1943 testimony:

"[T]he amendment made it possible to bring investment income within the scope of the general income-tax law, but did not change the character of the tax. It is still fundamentally an excise or duty with respect to the privilege of carrying on any activity or owning any property which produces income." (that is, "income otherwise taxable", as the Supreme Court reminds us some four-and-a-half decades later in the *South Carolina v. Baker* decision...)

Remember, as soon as Lincoln's 1862 act was passed, "income" acquired a fixed, limited and specialized definition for purposes of federal tax law (without which it would have been ruled unconstitutional for lack of apportionment in several cases arising before *Pollock*). Thus:

- The 1894 act that *Pollock* challenged only sought to tax "income" so defined.
- The Supreme Court ruling in that case only addressed the application of the tax to "income" so defined.
- The 16th Amendment only removed the apportionment

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requirement to “income” so defined-- and only that part of it comprising gains from invested personal property and real estate, because it was only that form of “income” that the Pollock court had concluded couldn't be taxed other than by apportionment. All other forms of “income” have always been able to be taxed without apportionment, because of the particular legal character of the receipts which qualify for the tax and which were (and are) the only variety which the tax attempts to reach.

That is why the court can say that direct taxes remain subject to the rule of apportionment even after the amendment; that the provisions of the amendment conferred no new power of taxation; that the amendment does not extend the taxing power to new or excepted subjects; that the sole purpose of the amendment was to remove the apportionment requirement for whichever “incomes” were otherwise taxable; and that the “income” tax remains Constitutional even though capitations still require apportionment.

(A few lower courts have made confusing-- or confused-- declarations over the years to the effect that the 16th Amendment authorized a direct tax without apportionment. What they mean is that in the context of the Pollock court's reasoning, the amendment removed the apportionment requirement from what is really a property-- and therefore inherently direct-- tax, because that's what the Pollock court saw the tax on dividends to be.

However, since the “property tax” involved only applies to gains which otherwise qualify as “income” by virtue of their federal connections, such declarations are misleading when offered without context. Property which is taxable “directly” under the new protocol is not just any property, but only that producing benefits from a voluntarily-undertaken federal linkage. That's why we don't all get federal property-tax bills every year. In reality, the 16th Amendment resulted in an

unapportioned "direct" tax only on receipts which are within the class of those IN-directly taxed.)

PART THREE

We're going to conclude this introduction to the truth about the income tax with a look at how general American understanding of all of the foregoing was lost over the course of the twentieth century, but also at how the means of individually correcting misapplications of the "income" tax are inherent within the very structure of the tax itself..

So how did all of this slip away from the American consciousness? Slowly, for one thing. At no time prior to 1942, eight decades after the federal income tax was first introduced, did more than 8% of American households ever file federal income tax returns in any given year. In most of those years, the percentage was far lower than even that small figure. As recently as 1936, only 3.9% of the entire American population filed returns, according to the Treasury Department's Division of Tax Research (Division Staff Memo: "Collection at Source of the Individual Normal Income Tax", 9 January, 1941).

Nonetheless, by 1943, thanks to the distractions of a world war, the exhortations of Donald Duck™ (see www.losthorizons.com/NewSpiritExcerpt.wmv and ask yourself: how many MANDATORY obligations must be sold to the public by cartoon animals?), and the adoption of a vague and confusingly-worded temporary measure called "The Victory Tax", the percentage of households sending in payments declared to be of "income" taxes rose to 38. That same year, the Treasury Department introduced its masterwork: 'The Current Tax Payment Act of 1943', by which the practice of withholding tax deposits from "wages", which had been a feature of the very first federal income tax acts but had been abandoned early in the 20th Century, was re-introduced. The

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new version was a rare work of lawyerly art, and contributed enormously to the ongoing erosion of general understanding of the nature of the tax-- already well advanced at that point, thanks to the extended passage of time since the initial adoption of the vast bulk of the relevant law. In short, the understanding of the limits of the federal income tax also slipped away from American consciousness organically.

We have suffered heavily for our carelessness ever since, to the tune of trillions of dollars of wealth improperly extracted from us over the years. The fact that the tax is limited as it is, and doesn't actually apply to most receipts, doesn't mean that it does not, or cannot, affect most Americans. In fact, there is an elaborate bureaucratic and legal structure in place which inadvertently leads to the application of the tax outside its proper scope, by encouraging everyone making payments to others to substantively allege that the payments were connected with the conduct of a taxable activity, whether this is actually true or not.

By way of this structure, most UN-taxable receipts become presumptively taxable in the eyes of the law, and the recipients become presumptively required to file a tax return and pay a resulting tax. Of course, false presumptions can be corrected, and in this case, a quirky idiosyncrasy of the relevant law provides that the means by which an inaccurate presumptive transformation of untaxable receipts into taxable receipts is corrected itself involves the filing of a tax return.

Although this appears strange-- even contradictory-- at first glance, it really is not. Every legal action involves an allegation and an answer. The only way to prove that there is nothing to be answered for is by the making of the answer-- however much that dynamic has the character of a "Catch-22". There is simply no other way for the law to work, since to make no rebuttal in the face of an allegation is to admit to what is alleged, by default. So, Congress, recognizing the need, has specified that the making of the same type of tax return used to

acknowledge the receipt of "income" when, and to the degree that, allegations to that effect are true is also the formal means of rebutting such allegations when they are not:

"And be it further enacted,...that any party, in his or her own behalf,...shall be permitted to declare, under oath or affirmation, the form and manner of which shall be prescribed by the Commissioner of Internal Revenue,... ...the amount of his or her annual income,... liable to be assessed,... and the same so declared shall be received as the sum upon which duties are to be assessed and collected." Section 93 of The Revenue Act of 1862.

Knowing how these allegations are made, the details of the related provisions and specifications made by Congress, and the underlying principles of law involved in properly answering them requires a careful and thorough reading of 'Cracking the Code- The Fascinating Truth About Taxation In America'. However, a general sense of these things, and of the manner in which the exploitive and obnoxious structure needing to be proactively addressed each year by most Americans came to be, can be had by reading the little parable in the following chapter.