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LET'S BE FRANK

The *Brushaber* Decision, Part V

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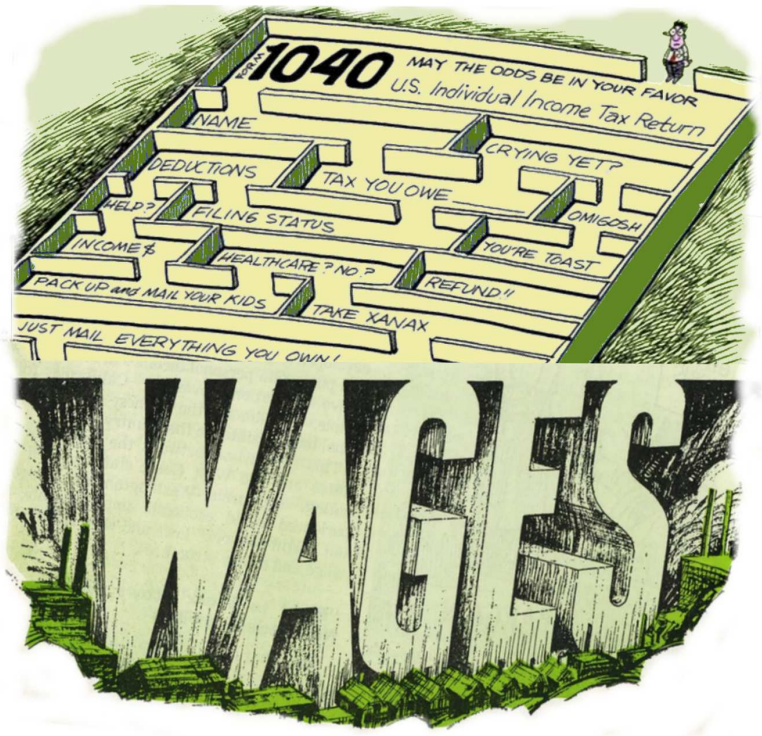

WAGES V. INCOME

On this series, we've been breaking down the majority opinion, written by Chief Justice Edward White, in the 1916 Supreme Court case *Brushaber v. Union Pacific Railroad Company*.[1] In the last installment we ended with White explaining that: "the whole purpose of the [16th] Amendment was to relieve all income taxes when imposed from apportionment *from a consideration of the source whence the income was derived*.[2] It was just such a consideration of the source of income — in particular, income derived from real and personal property — that provided the justification for then-Chief Justice Fuller to declare the income tax enacted in 1894[3] to be unconstitutional in the pair of 1895 Supreme Court cases titled *Pollock v. Farmers' Loan & Trust Company*.[4]

Ironically perhaps, White and I agree that Fuller's 'consideration of the source' was a "mistaken theory" (as he called it in *Stanton v. Baltic Mining Co.*),[5] although for slightly different reasons. I recognize that ***income is nothing more nor less than a species of personal property***, thereby making any tax on income direct, thus making it unnecessary — a mistake if you will — to consider the source. White, on the other hand, although he acknowledged time after time that the tax was ***directly on income***, still irrationally held that it was not a tax ***on property***, thereby claiming it to be an indirect tax. As such, he also believed it was a mistake to consider the source of the income, particularly when it resulted in making apportionment necessary.

Maintaining limitations

We'll pick up with White's often verbose *Brushaber* opinion as he continues to expound on the 16th Amendment:

> Indeed, from another point of view, the Amendment demonstrates that no such purpose [that is, treating a tax on income as a direct tax although it is relieved from apportionment] was intended, and on the contrary shows that *it was drawn with the object of maintaining the limitations of the Constitution and harmonizing their operation*. We say this because it is to be observed that although from the date of the Hylton Case, because of statements made in the opinions in that case, it had come to be accepted that direct taxes in the constitutional sense were confined to taxes levied directly on real estate

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1. 240 U.S. 1 (1916).
2. *Brushaber*, at 17.
3. "An Act to Reduce Taxation, to Provide Revenue for the Government, and for other purposes," enacted August 27, 1894. (28 Stat. at L. 509, 553.)
4. The original hearing (hereinafter "1st") is reported at 157 U.S. 429; and the rehearing (hereinafter "2nd") is reported at 158 US 601.
5. 240 U.S. 103, 113 (1916)

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> because of its ownership, *the Amendment contains nothing repudiating or challenging the ruling in the Pollock Case that the word 'direct' had a broader significance, since it embraced also taxes levied directly on personal property because of its ownership, and therefore the Amendment at least impliedly makes such wider significance a part of the Constitution*,—a condition which clearly demonstrates that the purpose was not to change the existing interpretation except to the extent necessary to accomplish the result intended; that is, the prevention of the resort to the sources from which a taxed income was derived in order to cause *a direct tax on the income to be a direct tax on the source itself*, and thereby to take an income tax out of the class of excises, duties, and imposts, and place it in the class of direct taxes.[6]

So, here White identifies the two-fold purpose of the amendment: first, to *maintain the limitations* of the Constitution; and second, to *harmonize* their operation. What high-minded purposes! Well, we know that one important limitation established in the Constitution is the requirement of apportionment for all direct taxes, and the inherent constraint that introduces on the range of *suitable* objects for such taxes. The more evenly an object is distributed throughout the states, the more suitable it becomes as a taxable object; and conversely, unevenly distributed objects are less suitable.[7] Keep in mind that this limitation doesn't affect the range of *possible* objects, it affects only the *suitability* of any object within that range.

Unfortunately, it's readily apparent that White isn't waxing eloquent about that limitation. Rather, he means the limitation on the need for apportionment, as effected by contracting the range of *possible* directly taxable objects, and placing them instead into the category of possible *indirect* taxes, which was accomplished by means of the Federalist coup in the *Hylton* case. In response to that proposition, I give you once again Justice Fuller's admonition about such a ploy from the *Pollock* decision:

> If, by calling a tax indirect when it is essentially direct, the rule of protection could be frittered away, one of the great landmarks defining the boundary between the nation and the states of which it is composed would have disappeared, and with it one of the bulwarks of private rights and private property.[8]

But of course, that was the whole point of the exercise, to fritter away one of the bulwarks of private rights and private property!

Harmonious tyranny and the broader significance

When it comes to harmonizing the operations of the limitations, White seems to have meant the harmony that comes from making apportionment unnecessary. No direct tax had been laid since Lincoln's war of aggression against the Confederate States of America anyway, and now, with income taxes securely under their belt — or should I say thumb — apportionment officially became a thing of the past. Remember that apportionment tied tax burdens to voting strength. Whatever percentage of the total votes a state had in the House of Representatives — from which, according to Article 1, §7 of the Constitution, "[a]ll Bills for raising Revenue shall originate" — that same percentage would be the share of the total direct tax which that state's citizens would have to pony up.[9] So, it's a real boon to the populous states to get rid of direct taxation, thereby freeing them from the constraints of apportionment. This allows them to shift the burdens of their impositions onto less populous states that can't muster the voting strength to prevent passage of such bills. But imagine how popular the income tax would be if the Supremes had correctly held it to be direct, thus requiring 33 percent of the total (pursuant to the 2020 census) to come from the citizens of just four states — California, Texas, Florida and New York!

Due to this move away from direct taxes, White's comment about the alleged broader significance of the word "direct" in the Constitution is an illusion at best. Whether "direct" taxes include only taxes imposed on real property, or also includes those imposed on personal property, makes little differerence when direct taxes — and therefore apportionment — are simply avoided altogether. And that avoidance was ultimately accomplished by simply "calling a tax indirect when it is essentially direct."

And yet, the 16th Amendment does indeed introduce a broader significance to the Constitution, just not in the way White asserted. Rather, that significance is because of the fact that the amendment uses the term "income" within it, and therefore, the definition of that term cannot be altered by any act of Congress. The Supreme Court spelled this out clearly in *Eisner v. Macomber*, 252 U.S. 189, 206 (1920):

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6. *Brushaber,* at 19.
7. For more on this subject, see my *Hylton* series, https://tinyurl.com/mryrd2kv.
8. *Pollock* 1st, at 583.
9. For more on the mechanics of apportionment, particularly with respect to the fact that the state's *citizens* were chargeable for the tax, and not the states themselves, see my article "Apportionment" in the August 2011 *Liberty Tree* .

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> In order, therefore, that the clauses cited from article 1 of the Constitution may have proper force and effect, save only as modified by the amendment, and that the latter also may have proper effect, *it becomes essential to distinguish between what is and what is not 'income,' as the term is there used*, and to apply the distinction, as cases arise, according to truth and substance, without regard to form. *Congress cannot by any definition it may adopt conclude the matter, since it cannot by legislation alter the Constitution, from which alone it derives its power to legislate, and within whose limitations alone that power can be lawfully exercised.*
>
> ... After examining dictionaries in common use, we find little to add to the succinct definition adopted in two cases arising under the Corporation Tax Act of 1909 (Stratton's Independence v. Howbert; Doyle v. Mitchell Bros. Co.), '*Income may be defined as the gain derived from capital, from labor, or from both combined*,' provided it be understood to include profit gained through a sale or conversion of capital assets, to which it was applied in the Doyle Case.

So, the definition of 'income' as that term is used in the 16th Amendment is set in stone, and it comes down to *profit* or *gain*. And remember, *profit* is calculated by subtracting from one's *receipts* the total *expenditures* in producing those receipts .

Receipts vs. profits

Now, there are some in the Tax Honesty movement who don't seem to understand this inability of Congress to define 'income,' and claim that makes the definition of 'gross income' in the tax code — "[G]ross income means all income from whatever source derived ..."[10] — vague or circular. But, plugging in the definition from the court, *gross income means all profit from whatever source derived*. Not all *receipts*, but only all *profit*. So, the calculation of profits — that is, *receipts minus expenses* — must occur in order to arrive at *gross income*; and only then can any deductions, credits, etc., be accounted for to arrive at *taxable income*. The bottom line is that the provisions of the tax code don't come into play until after that original determination of profit is complete.

On this point, the Internal Revenue Service prefers to ignore the necessity of that initial calculation, and consistently presses the wrongful notion that *receipts* and *income* mean the same thing. By means of that mischaracterization, the only subtractions from receipts then are the legislatively created deductions and allowances, rather than the actual expenses incurred in producing the receipts. This is especially true when it comes to wages and salaries.

The late Tommy Cryer — attorney and founder of Truth Attack — regularly argued about the incorrectness of the IRS' insistence that ones entire wages was income. As part of his defense against tax evasion charges, he submitted the following:

> The wage issue is exactly the same. Not only does one personally earning a wage, salary or fees incurring [sic] *costs for tools, work clothes and other expenses, he is depleting his working life* along with a goodly portion of his life itself, *a finite*, albeit of unknown duration, *capital asset*, his "most sacred and inviolable" asset .[11]

The IRS, on the other hand, simply asserts that one has no 'cost basis' in their labor. That, they say, means that the entire amount of your wages is not just receipts, but it is also gain (or gross income). However, the IRS' use of the term cost basis is problematic as a support for their position. According to *Black's Law Dictionary, 5th Ed.* (1979), the term has a more restrictive meaning than might be assumed:

> ***Cost basis.*** In accounting, the value placed on an asset in a financial statement in terms of its cost; *used in determining capital gains or losses*.

Black's 8th Ed. (2004) expands on the definition a bit, but the relationship to capital gains or losses remains:

> **basis.** ... 2. **Tax.** The value assigned to a taxpayer's investment in property and used primarily for computing gain or loss from a transfer of the property. When the assigned value represents the cost of acquiring the property, it is also called cost basis. ...
> ***adjusted cost basis***. Basis resulting from the

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10. IRC § 61(a).
11. Memorandum in support of Motion to Dismiss Charges in *United States v. Tommy K. Cryer,* No. 06-50164-01(Western District of Louisiana, Shreveport Division), p. 104.

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original cost of an item plus capital additions minus depreciation deductions.[12]

You can see that, according to these definitions, cost basis is basically the price one pays to acquire a *capital asset*, while the *adjusted cost basis* is that price plus all costs incurred in maintaining the asset until the time of its sale. So when the IRS says that you have no "cost basis" in your labor, all they're really saying is that your paid nothing for it. However, even if it were true that you have no cost basis in the labor itself, that's not the end of the story, because there are plenty of other costs you incur in producing the receipts represented by your wages. Besides the few Tommy mentioned above, another obvious example would be transportation costs. Certainly, you must travel to your job, and that cost comes off receipts before gain can be realized. I would submit that there are many other costs involved in getting that paycheck. Could you produce your labor without proper food or rest? Without clothes? Without proper sanitation? Then the costs of all those items must also be subtracted from your receipts to find your profit. I'm sure you get the idea.

Wages vs. Income

Taking all this into consideration then, it can be seen that *wages*, in and of themselves, are **not** *income*. This, of course, has been a common refrain among the tax movement for many years. And yet, very few people seem to recognize that the reasoning above is in truth the determining factor for that position. Instead, most contrive distinctions for wages (and more generally, citizens) that purportedly remove them from the scheme of income taxes.[13] Indeed, to my mind, this contributes in great part to the factious nature of the movement. Every distinction engenders a faction which promotes it (most often to the exclusion of all others), thus dividing the movement into many small groups, often working at cross purposes to each other, rather than a single coherent group, combining effort and resources. Is it any wonder the movement has made so little progress in nearly a half-century?

Getting back to the point, while wages are not income, that doesn't make them irrelevant in determining one's income. This is because they are a possible *source* of income. That is, one may indeed generate a profit from the wages he receives. All it would take is for him to receive more in wages than it costs him to produce them. Again, the excess of receipts over related expenses is profit, plain and simple.

As one example, consider a corporation executive. He may receive millions in salary, but he must live somewhere, travel to work, eat, maintain his health, etc. That he may choose to be extravagant in each of these necessities — that is, live in a mansion, or drive a limousine — doesn't change the fact that they represent his *actual* expenses, and should properly be accounted for in determining the amount of profit derived from his salary. Keep in mind, however, that only the expenses incident to producing the salary are subtracted from the receipts, but no others. Chances are, this guy would probably have quite a bit of profit left over at the end of his calculations.

On the other hand, consider a single mother working a low-paying job. After paying her housing, transportation, food, utilities, day-care (can't take your kid to work every day, after all) and other necessary expenses (for producing the wages), she could conceivably have nothing left over. That is, no profit; no income at all. So, while her wages would still constitute a *source* of income for her, she would realize no income from that source.

We'll pick this thread back up in the next installment, so stay tuned.

WHAT CAN SAVE-A-PATRIOT DO?

Members and others who hear about the Fellowship ask us: What can Save-A-Patriot DO for me? **And the answer is — more than you might imagine.**

In fact, Save A Patriot Fellowship stands ready to assist with any state or local taxing problems, citations, tickets, licensing issues — any area where state or local government bureaucrats are interfering with patriots' freedoms or misapplying the law, and where legal research could help clarify the situation. SAPF is also willing to assist with federal matters other than IRS income tax issues, and can help with Freedom of Information Act requests and Privacy Act Requests for information (even from the IRS disclosure office).

Finally, SAPF has years of experience with IRS policies and procedures, and can help you *understand* the methods of the IRS. So please call with your questions and problems. We *are here* to help save patriots.

12. Internal citations omitted throughout.
13. For more on one of these — the idea that contracting for your labor is a fundamental right — see "Taxing your rights: the power to destroy" in the April 2011 issue of *Liberty Tree*.