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The Constitutional Significance of Trusts and Estates Fiduciary Accounting Rules: Additional Support for the Taxpayers' Position in *Moore v. United States*

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The Constitutional Significance of Trusts and Estates Fiduciary Accounting Rules: Additional Support for the Taxpayers' Position in *Moore v. United States*

Jeffrey N. Schwartz*

This article includes and expands upon the analysis of the brief amicus curiae filed by the author and Sixteenth Amendment Insights, LLC in Moore v. United States *(U.S. S. Ct. Docket No. 22-800) on September 6, 2023. The analysis presented supports the views of those who believe that, absent some realization event, Congress may not impose a federal individual "indirect" income tax on an individual taxpayer's unrealized gains in respect of property held for personal use or investment purposes, and that the corresponding non-recognition of unrealized gains in respect of property owned at death is a necessary element of federal income tax law required to ensure compliance with applicable constitutional limitations on congressional taxing authority.*

Introduction

On August 30, 2023, Charles and Kathleen Moore filed their brief on the merits in *Moore v. United States*[1] challenging the constitutionality of certain provisions

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[1] U.S. S. Ct. Docket No. 22-800.

of federal tax law enacted as part of the Tax Cuts and Jobs Act of 2017 (the "Mandatory Repatriation Tax Provisions") on the basis that these provisions are or include an improperly apportioned federal direct tax on unrealized gains.

The Moores' arguments in support of their position effectively begin with an explanation of how,

> [f]rom the very beginning, th[e Supreme] Court's precedents have understood that the Sixteenth Amendment's exemption from Article I's apportionment [among the States by population] requirement [applicable to all federal "direct taxes"] is limited to taxes on a taxpayer's *realized* gains. That principle, first established by the Court's 1920 landmark decision in *Eisner v. Macomber* [252 U.S. 189 (1920)], has been consistently applied through the decades and to the modern era.[2]

On September 6, 2023, Sixteenth Amendment Insights, LLC, and Jeffrey N. Schwartz, the author of this article and the founder of Sixteenth Amendment Insights, LLC, filed a brief *amicus curiae* in support of the Moores (the "Brief Amicus Curiae")[3] explaining, in part, the importance of the Supreme Court's pre-*Macomber* decision in *Brushaber v. Union Pacific Railroad Co.*,[4] validating the constitutionality of the first post-Sixteenth Amendment federal tax on the incomes of individuals, in the Revenue Act of 1913, as a properly apportioned federal *indirect* tax in its entirety, and how:

1. The Sixteenth Amendment does not technically "exempt" any federal tax from any of the provisions of Article I of the Constitution;

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[2] Brief for Petitioners, *Moore v. United States*, at 17, available at https://www.supremecourt.gov/DocketPDF/22/22-800/278464/20230830102536217_22-800%20Brief%20for%20Petitioners.pdf.

[3] The Brief Amicus Curiae is available at https://www.supremecourt.gov/DocketPDF/22/22-800/278911/20230906121314854_22-800%20Amicus%20BOM%20Sixteenth%20Amendment%20Insights.pdf. Copies of both the Brief Amicus Curiae and a redacted version of the SALT deduction refund claim mentioned therein (that was filed by the author of this article and his wife with the IRS in September 2022, and granted, in full, in March 2023) can also be downloaded from a website maintained by Sixteenth Amendment Insights, LLC at www.directtaxrefund.org (the "Website"). The Website also includes, among other materials, links to materials reflecting the extraordinary public and private service of Charles Evans Hughes and additional information relating to the formation and anticipated recognition of The Charles Evans Hughes Society, Inc, as a 501(c)(3) tax-exempt organization. Among his many accomplishments, Hughes played important roles in the ratification and interpretation of the Sixteenth Amendment during his service as: Governor of New York during early debates over ratification; an Associate Justice of the United States Supreme Court who participated in the Court's 1916 validation of the first post-Sixteenth Amendment federal tax on the incomes of individuals, enacted in 1913; an attorney in private practice after his having resigned from the Court to run for President; and the subsequently appointed 11th Chief Justice of the United States, serving from 1930 to 1941. See infra notes 47, 51 & 53.

[4] 240 U.S. 1 (1916).

2. The Sixteenth Amendment instead functions to overturn the result of the second decision in *Pollock v. Farmers' Loan & Trust Co.*[5] ("*Pollock II*"), by modifying relevant jurisprudence so that a post-Sixteenth Amendment federal tax on a properly measured amount of "incomes" must be categorized *in its entirety* as a tax other than a federal direct tax for Article I purposes (that is, as a federal "indirect tax"), irrespective of the sources from which any one or more of the incomes being subjected to federal tax are derived;
3. The Mandatory Repatriation Tax Provisions value relevant unrealized accessions to the wealth of non-controlling, minority shareholders without the application of related valuation discounts,[6] and therefore in an amount in excess of the value over which those shareholders could have exercised complete dominion if, for example, they had sold or otherwise disposed of the entirety of their relevant non-controlling, minority interests;[7] and
4. The Mandatory Repatriation Tax Provisions therefore include an unconstitutional, improperly apportioned federal direct tax on the wealth and/or accessions to the wealth of individuals in excess of

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[5] 158 U.S. 601 (1895). The first decision ("*Pollock I*") is found at 157 U.S. 429 (1895).

[6] See Internal Revenue Manual 4.48.4.2.3(6) (09-22-2020), available at https://www.irs.gov/irm/part4/irm_04-048-004:

> As appropriate for the assignment, and if not considered in the process of determining and weighing the indications of value provided by other procedures, the appraiser should separately consider the following factors in reaching a final conclusion of value:
>
> a. Marketability, or lack thereof, considering the nature of the business, business ownership interest or security, the effect of relevant contractual and legal restrictions, and the condition of the markets.
> b. Ability of the appraised interest to control the operation, sale, or liquidation of the relevant business.
> c. Other levels of value considerations (consistent with the standard of value in IRM 4.48.4.2.2 (1) list item g) such as the impact of strategic or synergistic contributions to value.
> d. Such other factors which, in the opinion of the appraiser, are appropriate for consideration.

[7] The text of the Brief Amicus Curiae not reproduced below cites to pages 41–42 and 51–52 of the Moores' brief on the merits to support the observation that "attributing or imputing income earned by an entity or organization that is a partnership, trust or S corporation for [f]ederal tax purposes to its partners, beneficiaries or shareholders, as applicable, is in no way the equivalent of an imputation or attribution of income involving individuals (meaning human beings) who own interests in a company that is not otherwise a "flow-through" entity or organization for [f]ederal tax purposes." and does directly address the attribution of "corporate incomes" to the shareholders of "controlled foreign corporations" such as the controlled foreign corporation at issue in the *Moore* case. Brief Amicus Curiae at 27. Although a limited number of observations relating to the federal income taxation of shareholders of controlled foreign corporations are contained in infra notes 16, 21 & 78–79, a full analysis of related matters is beyond the scope of this article.

> a proper measurement of the amount or value of their "incomes" within the meaning of the Sixteenth Amendment ("Sixteenth Amendment Incomes").[8]

On October 16, 2023, the United States filed its brief on the merits (the "Government's Brief on the Merits") in response to the Moores' arguments.[9] That brief does not directly respond to the analysis of the Brief Amicus Curiae and, among other matters, includes a selective quotation from Chief Justice Roberts's 2012 opinion in *National Federation of Independent Business v. Sebelius* ("*NFIB*")[10] to support a proposition that is at odds with the analysis of the Brief Amicus Curiae and the plain meaning of the actual text of that opinion.[11]

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[8] See Brief Amicus Curiae at 8–28. A numeric example is included in a footnote to this section of the Brief Amicus Curiae but is not reproduced in the discussion, in "Analysis from Argument Section of Brief Amicus Curiae," later in this article. See Brief Amicus Curiae at 26–27 n.35:

> [F]or example, if a corporation in which a shareholder has a 13% minority interest [(corresponding to the Moores' 13% interest in KisanKraft)] earns $100 of after-tax net income, the Internal Revenue Service generally would not expect the value of that minority interest to increase by a full $13 (13% of $100 of net income), but would instead expect the value of that interest to increase by some lesser amount after taking into consideration factors supporting related valuation discounts, e.g., by $10.40, and not $13, if relevant factors supported a 20% valuation discount ($13 x (100%-20%) = $10.40). Correspondingly, if that 13% minority shareholder acquired its interest for $5 and sold that interest immediately after the corporation earned $100 of after-tax net income, but experienced no other changes in value, it is very unlikely that the minority interest could be reasonably valued at an amount equal to $5 + $13, as contrasted to some lesser amount taking into account appropriate, including arms-length negotiated, valuation discounts (e.g., possibly $5 + $10.40 if a corresponding 20% valuation discount was appropriate under the relevant facts and circumstances).

[9] All of the briefs that have been filed in the Supreme Court in the *Moore* case are available at http//www.supremecourt.gov/search.aspx?filename=/docket/docketfiles/html/public/22-800.html.

[10] 567 U.S. 519 (2012).

[11] Compare Government's Brief on the Merits at 4 ("In 1913, *Pollock 'was overturned* by the Sixteenth Amendment,' *NFIB*, 567 U.S. at 571.") (emphasis added), with *NFIB*, 567 U.S. at 570–71 (emphasis added).

> [I]n 1895, we [the Supreme Court] expanded our interpretation [of direct taxes] to include taxes on personal property and income from personal property, in the course of striking down aspects of the federal income tax. *Pollock v. Farmers' Loan & Trust Co.*, 158 U.S. 601, 618 (1895). *That result was overturned* by the Sixteenth Amendment, although we continued to consider taxes on personal property to be direct taxes. *See Eisner v. Macomber*, 252 U.S. 189, 218-219 (1920).

As explained later in this article, overturning the result of *Pollock II* is significantly different from overturning the entirety of *Pollock II*, including because the analysis of *Pollock II* also incorporates certain of the analysis of *Pollock I* and, as discussed below, was further clarified by

This article includes the analysis of the Brief Amicus Curiae, with certain related additions, and then expands on that analysis to examine the further constitutional question of whether Congress may ever impose a federal indirect income tax on a *properly measured* amount of an individual taxpayer's unrealized gains in respect of property held by that individual for personal use or investment purposes (the "More General Gain Realization Question"). The analysis presented beyond that included in the Brief Amicus Curiae focuses, in large part, on two of the cases cited in *Cottage Savings v. Commissioner*,[12] and additional trusts and estates fiduciary accounting rules alluded to in a footnote to the Brief Amicus Curiae.[13] The expanded analysis supports and complements related analysis advanced by the Moores in their brief on the merits[14] and by others who have submitted briefs *amicus curiae* in support of the Moores analyzing the More General Gain Realization Questions.[15]

The ultimate conclusions of this expanded analysis support the views of those who believe that:

1. Absent some realization event, Congress is constitutionally prohibited from imposing a federal tax in the form of an *indirect* tax (that is, one apportioned by the application of a geographically uniform

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subsequent decisions of the Court issued prior to the adoption of the congressional resolution that was ultimately ratified as the Sixteenth Amendment. Correspondingly, the government's reliance on *Collector v. Hubbard*, 79 U.S. 1 (1871), to support certain of its income attribution arguments may be misplaced for the very reason that *Hubbard* is a pre-*Pollock* decision that may no longer be relevant as a consequence of its having, for the reasons explained later in this article, been overturned by analysis of *Pollock I* and *Pollock II* that was then further clarified by other pre-Sixteenth Amendment decisions and implicitly incorporated into the Constitution as a result of the ratification of the Sixteenth Amendment. The Government's Brief on the Merits also employs related misconceptions of the Sixteenth Amendment as a standalone grant of taxing authority to defend its own arguments. Compare Government's Brief on the Merits at 33 ("In arguing that the Sixteenth Amendment's *grant* of power somehow stripped Congress of a preexisting authority recognized in *Hubbard*, petitioners stake their case on dictum in *Macomber* implying that shareholders must receive monetary distributions of corporate earnings before being taxed on them.") (emphasis in original), with the analysis presented later on in this article under "Meaning and Function of the Sixteenth Amendment."

[12] 499 U.S. 554 (1991).

[13] See Brief Amicus Curiae at 21 n.28. That footnote is reproduced with the addition of a citation to a biography of Charles Evans Hughes and other limited modifications in infra note 51.

[14] This article was submitted for publication prior to the Moores' having filed their reply brief to the Government's Brief on the Merits.

[15] See, e.g., Brief Amici Curiae of The Manhattan Institute for Policy Research and Professors Erik M. Jensen and James W. Ely in Support of Petitioners, *Moore v. United States* (Sept. 2023) available at https://www.supremecourt.gov/DocketPDF/22/22-800/279005/20230906154449246_22-800.tsac.Manhattan.pdf.

rate of tax to a geographically uniform measurement of the matters or things being subjected to federal tax) on the unrealized gains of individuals in respect of property held by them for personal use or investment purposes (or at least in respect of that category of property acquired by the holder prior to the date of enactment of any such tax);[16] and

2. The non-recognition of gain at death associated with the so-called "step-up in basis" in respect of property includible in a decedent's gross estate[17] cannot be properly characterized as a "loophole" and is instead a necessary element of federal income tax law required to ensure compliance with otherwise applicable constitutional limitations on congressional taxing authority.[18]

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[16] See infra note 29 & accompanying text. IRC § 1256 is an example of a federal income tax "mark-to-market" provision that, as applied to individuals not engaged in any active trade or business, might be defended as being a proper indirect tax because it was enacted in 1981 on a relatively non-retroactive basis and with respect to a relatively narrow category of property such that a taxpayer can avoid its application by investing in property not subject to the section. See Economic Recovery Tax Act of 1981, P.L. 97-34, § 508(a), 95 Stat. 172, 333 (reflecting enactment on August 13, 1981, with respect to property such as "regulated futures contracts" acquired after June 23, 1981). See Erik M. Jensen, "The Apportionment of 'Direct Taxes': Are Consumption Taxes Constitutional?" 97 Colum. L. Rev. 2334, 2393–97 (1997) (describing the nature of "indirect taxes" as ones that can be avoided). Correspondingly, while the analysis of the Brief Amicus Curiae could potentially raise broader issues with respect to federal income taxation of minority shareholders of existing "controlled foreign corporations" that are beyond the scope of this article, the federal government might be able to argue in that context that, unlike the Moores (who already owned their equity interests at the enactment of the Tax Cuts and Jobs Act of 2017), individual shareholders who have acquired their interests in controlled foreign corporations *after* the enactment of other relevant federal tax rules have "voluntarily" subjected themselves to those rules as a result of their voluntary, post-enactment decision to invest in the relatively narrow category of property made subject to those rules (i.e., by making a post-enactment investment in a "controlled foreign corporation") in a manner sufficient (when combined with prior tax reporting and any applicable duties of consistency) to negate their ability to claim current income tax refunds in respect of open tax years or on a going-forward basis.

[17] The federal income tax basis of property includible in a decedent's gross estate for federal estate tax purposes is not technically "stepped up" at death, but is instead adjusted to its corresponding fair market value at the date of the decedent's death, which may be higher or lower than the owner's federal income tax basis in the property immediately prior to death, subject to special rules that may apply if certain federal estate tax elections are made, including one which, if it would reduce the federal estate taxes otherwise payable and is made by the executor, generally adjusts the federal income tax basis of each asset to its value on the earlier of the disposition of that asset or six months after the decedent's death. See IRC §§ 1014(a), 2032. Under IRC § 1014(c), there is also no basis increase in respect of property constituting a right to receive "income in respect of a decedent" within the meaning of IRC § 691.

[18] The author respectfully notes how related mischaracterizations may, depending on one's personal views, be useful for political purposes, but can also hinder the development of alternative mechanisms for constructively addressing underlying policy concerns, and lead to confusion and misunderstandings that may contribute to the erosion of public confidence in our political system, including as to matters that may relate to the Constitution, the Supreme Court, and developments in related jurisprudence.

The underlying analysis, however, should not be understood as implying that Congress cannot: (1) treat a lifetime gift or other affirmative act taken in respect of appreciated securities or other property as a "realization event" for federal income tax purposes; (2) impose a federal inheritance tax in the form of a federal indirect tax that effectively treats the receipt of a gift or bequest as additional gross income of the recipient in the year of receipt; or (3) impose an additional or higher rate of federal transfer tax in the form of an indirect tax on the value of transferred property in excess of the transferor's federal income tax basis therein at the time of transfer (for example, a higher rate of federal estate tax on the value of property transferred by reason of death representing long-term capital gain that remained unrealized at death not already constituting "income in respect of a decedent" within the meaning of Section 691).[19]

The underlying analysis also should not be understood as calling into question any provision of federal tax law applicable to the income taxation of corporations at the corporate level. This is the case because federal corporate income taxes (for example, taxes imposed on one or more or all of the gross accessions to the wealth of a corporation derived from any source whatever) are characterized for constitutional purposes as the equivalent of a franchise tax imposed on the corporation in respect of one or more of the privileges of conducting activities in corporate form (such as limitations on the liability of officers, directors, and shareholders), and therefore are not subject to categorization as taxes that may be imposed by Congress only in the form of direct taxes (that is, only in the form of taxes that are apportioned among the states by population).[20]

A discussion of whether, absent a further amendment to the Constitution, Congress has the authority to enact a federal tax in the form of an indirect tax on the incomes of individuals including unrealized gains (or to

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[19] Unless otherwise indicated, section references in this article are to the Internal Revenue Code of 1986, as amended (the "IRC").

[20] Explained with a slightly different focus, the federal corporate income tax is properly categorized in its entirety as an "indirect" tax because it is a tax imposed on the affirmative choice of individuals—actual human beings who are sometimes referred to as "natural" persons as contrasted to "juridical" or "corporate" persons—to conduct their activities in the form of an "association treated as a corporation for federal tax purposes" instead of conducting related business or holding company activities directly themselves in some non-corporate form such as a general or limited partnership. This treatment and understanding regarding federal corporate income taxes, in general, is not only consistent with the Supreme Court's analysis in *Pollock II,* but was confirmed by the Supreme Court in its post *Pollock II* decision in *Flint v. Stone Tracy Co.*, 220 U.S. 107 (1911), issued after the passage, but prior to the ratification, of the Sixteenth Amendment. This treatment was also confirmed as continuing to apply after the ratification of the Sixteenth Amendment in the Court's unanimous decision in *Stanton v. Baltic Mining Co.*, 240 U.S. 103 (1916), issued subsequent, but effectively as a companion case, to its also unanimous, earlier decision in *Brushaber*. See infra note 34, and infra notes 41–44 and accompanying text.

eliminate non-recognition of gain at death) in respect of securities or other property acquired by an individual taxpayer after the date of enactment also is beyond the scope of this article.[21]

The analysis presented begins with relevant constitutional background, includes the analysis of the "arguments" section of the Brief Amicus Curiae, and expands on that analysis with, among other additions, a discussion of the relevance of certain fiduciary accounting rules and an expanded discussion of certain of the cases cited in *Cottage Savings* (which is itself among the cases cited in the Brief Amicus Curiae).

Constitutional Background

Article I of the Constitution contains a series of tax clauses that together comprise a federal tax categorization and apportionment system under which: (1) all federal taxes other than federal "direct taxes" must comply with a "uniformity requirement" contained in Article I, section 8; and (2) all federal capitations and other direct taxes must instead be apportioned in the same manner as representation in the House of Representatives—that is, among the several states by population, based on a periodic census or enumeration. The category comprised of all federal taxes other than direct taxes is often

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[21] A full discussion of the possible implications of the analysis presented with respect to the federal income taxation of shareholders of "controlled foreign corporations," such as the controlled foreign corporation at issue in the *Moore* case, is similarly beyond the scope of this article. Nevertheless, it may be helpful to keep in mind in the context of any such analysis that the categorization of an organization as a trust for federal income tax purposes continues to be subject to a multi-factor categorization test developed prior to the adoption by the Treasury of the current check-the-box regulations. See Howard M. Zaritsky, Norman Lane & Robert Danforth, *Federal Income Taxation of Estates and Trusts* ¶ 1.07[3] (3d ed. 2001); Robert C. Lawrence III & Dina Kapur Sanna, "Trust Classification Times Four," 49 U. Miami Inst. on Est. Plan. ¶ 1501.2 (2004); Von E. Sanborn, "U.S. Tax Classification of Trusts: When Is a Trust Not a Trust?" 31(4) Est. Plan. 440 (Sept. 2004). Trusts categorized as "simple" or "complex" trusts for federal income tax purposes are also sometimes referred to as "quasi-passthrough" vehicles for such purposes because the federal income tax imposed on the trust's taxable income (including capital gains) is imposed *either* at the trust level (on taxable income deemed to have been retained at the trust level) *or* at the beneficiary level (on a "passthrough" basis in respect of current taxable income or, in certain circumstances, in the form of a "throwback tax" on previously accumulated taxable income). Under these circumstances, it may be difficult to conceptualize an actual juridical entity (as contrasted to a common law trust) that is also to be categorized as a corporation, and not a trust or partnership, under the rules in effect prior to the adoption of the current check-the-box regulations, as anything other than a "corporation" for constitutional purposes. To some extent, the Mandatory Repatriation Tax Provisions also might be conceptualized as an attempt to impose a "throwback tax" equivalent in the corporate context without any associated actual distribution of trust/corporate property to the relevant beneficiaries/shareholders and therefore a tax that is significantly different than either the "corresponding current tax year" attribution under the "normal" non-Mandatory Repatriation Tax Provisions applicable in respect of controlled foreign corporations or the "throwback rules" applicable in respect of foreign trusts.

referred to as "indirect taxes,"[22] although that term does not appear in either Article I or the Sixteenth Amendment.[23]

A federal tax properly categorized as a direct tax for Article I purposes is, by definition, not subject to the Article I uniformity requirement because that requirement is applicable only to federal indirect taxes. Correspondingly, if a federal tax imposed on a particular matter or thing otherwise properly categorized as a federal direct tax (for example, a "capitation tax") was ever to be "exempted" from the requirement that it be apportioned among the states by population without, at the same time, also being made subject to some other rule of apportionment, Congress would be free to impose that federal direct tax on the subject of taxation free of the uniformity requirement (because, as mentioned above, that requirement is applicable *only* to indirect taxes), and therefore be able to impose that federal direct tax with whatever geographically discriminatory rate of federal tax Congress might desire. For example, Congress could impose different rates of federal tax on taxpayers possessing or doing the same matter or thing being subjected to federal tax, or that employed different measurements of the same relevant subject of taxation, based solely on where in the United States the relevant taxpayer, or matter or

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[22] See *Brushaber*, 240 U.S. at 12–13 (explaining as part of its analysis validating the constitutionality of the first post-Sixteenth Amendment federal tax on incomes):

> the authority conferred upon Congress by § 8 of Article I [of the Constitution] "to lay and collect taxes, duties, imposts and excises" is exhaustive and embraces every conceivable power of taxation has never been questioned, or, if it has, has been so often authoritatively declared as to render it necessary only to state the doctrine. And it has also never been questioned from the foundation, without stopping presently to determine under which of the separate headings the power was properly to be classed, that there was authority given, as the part was included in the whole, to lay and collect income taxes. Again it has never moreover been questioned that the conceded complete and all-embracing taxing power was subject, so far as they were respectively applicable, to limitations [applicable to indirect taxes] resulting from the requirements of Art. I, § 8, cl. 1, that "all duties, imposts and excises shall be uniform throughout the United States," and to the limitations of Art. I, § 2, cl. 3, that "direct taxes shall be apportioned among the several States" and of Art. I, § 9, cl. 4, that "no capitation, or other direct, tax shall be laid, unless in proportion to the census or enumeration hereinbefore directed to be taken." In fact the two great subdivisions embracing the complete and perfect delegation of the power to tax and the two correlated limitations as to such power were thus aptly stated by Mr. Chief Justice Fuller in *Pollock* . . ., at page 557: "In the matter of taxation, the Constitution recognizes the two great classes of direct and indirect taxes, and lays down two rules by which their imposition must be governed, namely: The rule of apportionment as to direct taxes, and the rule of uniformity as to [indirect taxes such as] duties, imposts and excises."

[23] Id.; see also U.S. Const. amend. XVI ("The Congress shall have power to lay and collect taxes on incomes, from whatever source derived [for example, on a proper measurement of accessions to wealth derived from the continued ownership of property, real or personal, irrespective of its use or disposition], without apportionment among the several States, and without regard to any census or enumeration."). Earlier drafts of what became the Sixteenth Amendment are mentioned in infra note 43.

thing being subjected to federal *direct* taxation, was located. That would be in addition to the very specific, and geographically discriminatory, rate of tax that, by definition, results as a matter of mathematics from the requirement that all federal direct taxes be apportioned among the states by population.[24]

This observation is among those contained in the Supreme Court's unanimous opinion in *Brushaber* validating the first post-Sixteenth Amendment federal tax on the incomes of individuals as a properly apportioned federal indirect tax in its entirety.[25] As explained in corresponding sections of the Brief Amicus Curiae included below, the analysis of *Brushaber* is, in turn, key to a full understanding of the meaning and function of the Sixteenth Amendment, and of the reasoning and analysis of *Macomber*.

In this context, a number of scholars and commentators have argued in favor of a narrow reading of the requirement that all federal direct taxes be apportioned in the same manner as representation in the House of Representatives (and, correspondingly, would likely argue in favor of a narrow "realization requirement"[26]) because the original, underlying population counting

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[24] See Mark E. Berg, "The Proposed Federal Wealth Tax Would Be Unconstitutional," 37(3) Daily Tax Rep. 2 (Bloomberg Tax, Feb. 2, 2019), available at https://www.fcingoldalpert.com/siteFiles/26925/Wealth-Tax-2-26-19.pdf (containing the following example and observations related to the consequences of categorizing a national wealth tax as a direct tax):

> State A has a population of 5 million with aggregate household wealth of $100 billion, so that its wealth per capita is $20,000. State B has a population of 1 million with aggregate household wealth of $10 billion, so that its wealth per capita is $10,000. Because the population of State A is 5 times the population of State B, a tax that is apportioned as between State A and State B would be required to generate 5 times as much revenue from State A than from State B. A federal wealth tax imposed at a uniform 2 percent tax rate would not be apportioned as between State A and State B because total collections of the tax in State A (2% of $100 billion = $2 billion) would be 10 times, rather than 5 times, total collections of the tax in State B (2% of $10 billion = $200 million).
>
> In order for the wealth tax to be apportioned as between State A and State B, the tax rate in State A would have to reflect the difference in wealth per capita in the two states by being set at one-half the tax rate in State B. Thus, for example, if the tax were imposed at a rate of 1 percent in State A and 2 percent in State B, total collections of the tax in State A (1 percent of $100 billion = $1 billion) would be 5 times total collections of the tax in State B (2 percent of $10 billion = $200 million) and the wealth tax would be apportioned as between State A and State B.
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> Indeed, it is precisely this counterintuitive, regressive, and politically infeasible aspect of the apportionment requirement—an apportioned tax must be imposed at a proportionately higher rate in states having less per capita of the item being taxed—that has caused many scholars (and some early judges) to look askance at the Direct Tax Clauses by narrowly defining the term direct tax.

[25] See infra notes 41–44 and accompanying text.

[26] See Brief of Amici Curiae Professors Bruce Ackerman, Joseph Fishkin & William E. Forbath in Support of Respondent, *Moore v. United States*, available at https://www.supremecourt.gov/DocketPDF/22/22-800/285682/20231020135857418_Amicus%20Curiae%20Brief%20of%20Ackerman%20Fishkin%20Forbath.pdf (urging the Court to affirm the lower

methodology employed for apportionment purposes was forged in a compromise over slavery.[27]

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court's decision in favor of the government on the basis of an explanation of the original understanding of the Sixteenth Amendment including a citation to *"Replies to Hughes—Root on Income Tax Amendment*, N.Y. Daily Tribune, March 1, 1910, at 4" and references to Justice Harlan's dissent in *Pollock II,* but not including mention of: (1) *Brushaber*; (2) Governor Hughes's January 5, 1910, Special Message to the New York State Legislature opposing ratification of the Sixteenth Amendment; (3) how the Sixteenth Amendment addresses only taxes on "incomes," while Justice Harlan's dissent in *Pollock II* refers to Congress's power to "impose a duty or tax upon personal property, or upon income arising either from rents of real estate or from personal property, including invested personal property, bonds, stocks" as reflected in the text of Justice Harlan's dissent quoted infra note 34; and (4) how Merlo J. Pusey described related matters in his Pulitzer Prize winning biography *Charles Evans Hughes* (1951), cited with related excerpts in infra notes 47 & 51. Of note, as mentioned in the preface, "Charles Evans Hughes himself contributed more to [the related volume] than any other individual." Pusey, supra, at vii.

[27] See, e.g., Joseph R. Fishkin & William E. Forbath, "Congress Has Broad Power to Tax," appearing as part of the debate on the Sixteenth Amendment presented by the National Constitution Center, available at https://constitutioncenter.org/interactive-constitution/interpretation/amendment-xvi/interps/139:

> Why read the "direct"/"indirect" distinction narrowly? The simplest and best reason is that this bit of constitutional text is part of a 1789 compromise over slavery that Americans later decisively rejected, on the battlefields of the Civil War. As Bruce Ackerman explains . . ., the original point of the apportionment rules for "direct" taxes was this: if the Southern states were going to get extra representatives and presidential votes because of their (completely disenfranchised) slaves, then those states should also pay extra taxes. The ratio would be the same: three-fifths. The constitutional debates make this clear. You can also see it in the text of the Constitution itself. The same sentence in Article I, Section 2, Clause 3 apportions both "Representatives and direct Taxes"—all according to "the whole number of free Persons . . . and three fifths of all other persons" (slaves) in each state.
>
> So to summarize: For a century after 1789, the Court read the limitation on direct taxes very narrowly. In the middle of that period, we eliminated slavery, and with it the point of the original apportionment compromise. Nonetheless, in *Pollock*, five justices made the ill-advised decision to revive and expand the "direct" tax apportionment rule in an effort (in the view of some) to hobble the modern progressive state. This failed. Through the Sixteenth Amendment, the People reversed the Court. After a few feints the other way in the 1920s, such as *Eisner v. Macomber*, the Supreme Court has come to accept that after the Sixteenth Amendment, the federal government is no longer hobbled by any far-reaching "direct" tax rule. That is how it ought to stay.
>
> Still, in constitutional politics, old ideas—even bad ideas—have a way of coming back around again. We agree with Professor Jensen that we may not yet have seen the last of claims arguing, *Pollock*-style, that the direct apportionment clause blocks the federal government from enacting some future tax.

See also Mitchel M. Gans, "Progressive Taxation and a Conservative Supreme Court: Reading the Tea Leaves," 283 ACTEC L.J. 283 (Spring/Summer 2022) (containing a thoughtful analysis, despite the absence of any mention of *Brushaber*, and describing the Article I direct tax apportionment by population requirement in its introduction as "[a]n obscure constitutional provision, forged at the founding in a compromise over slavery," with related citations to Bruce Ackerman, "Taxation and the Constitution," 99 Colum. L. Rev. 1 (1999), and Calvin H. Johnson, "Fixing the Constitutional Absurdity of the Apportionment of Direct Tax." 21 Const. Comment. 295, 297–98 (2004)).

The drafting and passage of the resolution that became the Sixteenth Amendment, however, represents a conscious, post-Civil War determination by Congress to retain the Article I tax categorization and apportionment system, including its rule requiring that all federal capitation and other "direct taxes" be apportioned in the same manner as representation in the House of Representatives. That congressional decision, made as part of the drafting and ultimate passage by Congress in 1909 of the congressional resolution that would ultimately be ratified as the Sixteenth Amendment to the Constitution in 1913, happened more than 30 years after the original, and highly problematic, constitutional compromise over population counting was corrected, at least as a technical matter, by the ratification of the Thirteenth and Fourteenth Amendments in 1865 and 1868, respectively.

This background is helpful in evaluating both the strength of the analysis contained in the Brief Amicus Curiae and that contained in the balance of this article.

Analysis From Argument Section of the Brief Amicus Curiae

Direct and Indirect Taxes and Related Tax Apportionment Rules in General. Under Article I of the Constitution (1) all federal "Capitation[s]" and "other direct" taxes must be apportioned in the same manner as representation in the House of Representatives (that is, among the several states based upon relative populations as determined by a periodic census or enumeration)[28] and (2) all federal taxes other than direct taxes (often referred to as "indirect taxes" although that term does not appear in the Constitution itself) must be apportioned by the application of geographically uniform rates of federal *indirect* taxation to geographically uniform measurements of the relevant matter or thing being subjected to federal indirect taxation (for example, properly measured Sixteenth Amendment Incomes).[29]

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[28] See U.S. Const., art. I, § 2, cl. 3; § 9, cl. 4.

[29] Although federal indirect taxes are sometimes referred to as being "unapportioned" because they do not have to meet the special rule of apportionment requiring all federal direct taxes to be apportioned among the states by population, the only tax that is truly "unapportioned" is a tax that raises no revenue or, perhaps, a tax on a matter or thing located in a single jurisdiction that raises all of its revenue from a single taxpayer. If a tax raises revenue from multiple taxpayers or is imposed on a matter or thing located, held, generated, or otherwise properly sourced in multiple jurisdictions, the aggregate revenue collected by that tax must, as a matter of mathematics, (1) be paid by one taxpayer relative to another, or from one jurisdiction relative to another, in proportion to something, and (2) therefore also be apportioned "by" something. A federal indirect tax is apportioned by the application of geographically uniform rates to geographically uniform measurements of the matter or thing being subjected to federal tax. See U.S. Const. art. I, § 8, cl. 1; *Knowlton v. Moore*, 178 U.S. at 106–07.

***Pollock I, Pollock II,* and Other Jurisprudence in Effect at the Passage and Ratification of the Sixteenth Amendment.** In *Pollock II,* the Supreme Court reconsidered certain of its analysis in the first *Pollock* decision ("*Pollock I*") relating to a federal tax on incomes from any source whatever that Congress believed to be a properly apportioned federal indirect tax.[30] The Court struck down the relevant statutory provisions in their entirety based upon an analysis that they included an improperly apportioned federal direct tax on the incomes of individuals derived from their continued ownership of property, real or personal, held for personal use or investment purposes, and the fact that relevant statutory provisions had been enacted as a whole.[31]

Pollock I includes an analysis explaining why "direct" taxation includes both (1) "property taxes" on real estate held by individuals for personal use or

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> [T]hose who opposed the ratification of the Constitution clearly understood that the uniformity clause as to taxation imported but a geographical uniformity, and made that fact a distinct ground of complaint. Thus in the report made to the legislature of Maryland by Luther Martin, attorney general of the State, detailing and commenting upon the proceedings of the convention of 1787, of which convention Mr. Martin was a delegate, in the course of comments upon the tax clause of the Constitution Mr. Martin said [1 Elliott Debates at 369]:
>
> > Though there is a provision that all duties, imposts and excises shall be uniform—*that is, to be laid to the same amount* [i.e., to the same rate and measurement] *on the same articles in each State*—yet this will not prevent Congress from having it in their power to cause them to fall very unequally and much heavier on some States than on others, because these duties may be laid on articles but little or not at all used in some other States, and of absolute necessity for the use and consumption in others; in which case, the first would pay little or no part of the revenue arising therefrom, while the whole or nearly the whole of it would be paid by the last, to wit, the States which use and consume the articles on which imposts and excises are laid.

See also U.S. v. Ptasynski, 462 U.S. 74, 84–85 (1983) ("Where Congress defines the subject of a[n indirect] tax in nongeographic terms [and imposes a uniform rate of tax on a uniform measurement of that subject], the Uniformity Clause is satisfied. . . . But where Congress does choose to frame a tax in geographic terms, [the federal courts] will examine the classification closely to see if there is actual geographic discrimination.").

[30] See Act of Aug. 27, 1894, ch. 349, § 27, 28 Stat. 509, 553 (emphases added):

> [F]rom and after the first day of January, eighteen hundred and ninety-five . . . *there shall be assessed, levied, collected, and paid annually upon the gains, profits, and [other] income received in the preceding calendar year* by every citizen of the United States . . . and every person residing therein, whether said gains, profits, or income be derived from any kind of property, rents, interest, dividends, or salaries, or from any profession, trade, employment, or vocation carried on in the United States or elsewhere, *or from any* other *source whatever,* a tax of two percentum on the amount so derived over and above four thousand dollars, and a like tax shall be levied, collected, and paid annually upon the gains, profits, and income from all property owned and of every business, trade, or profession carried on in the United States by persons residing without the United States.

[31] See infra note 34.

investment purposes (as contrasted to "corporate franchise taxes" that might include the value of real estate held by a corporation as part of the relevant tax base[32]) and (2) taxes on the accessions to the wealth of individuals derived from the continued ownership of real estate held for personal use or investment purposes (for example, on rents derived from renting a personal residence while temporarily living at another location as contrasted to profits derived from being engaged in the rental of real estate as an active trade or business).[33]

Pollock II then expands upon the jurisprudence of *Pollock I* by categorizing federal taxes on an individual's ownership of real estate *and/or personal property* held for personal use or investment purposes (for example, a federal "intangibles tax" on stocks and bonds held for personal investment purposes) as a direct tax and, correspondingly, also includes in the direct tax category taxes on accessions to wealth derived from the continued ownership of real estate *and/or personal property* held for personal use or investment purposes (for example, taxes on cash dividends derived from owning common stock held as a personal investment as contrasted to profits derived from trading in that same stock as a broker-dealer).[34]

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[32] See cases cited in supra note 20 and reference to taxes on privileges in infra note 34.

[33] See infra note 34.

[34] See *Pollock II*, 158 U.S. at 635, 637:

> We have considered the act only in respect of the tax on income derived from real estate, and from invested personal property, [from continued ownership thereof only] 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. . . .
>
> We do not mean to say that an act laying by apportionment a direct tax on all real estate or personal property, or the income thereof, might not also lay [indirect taxes such as] excise taxes on business, privileges, employments, and vocations. . . .
>
> Our conclusions may, therefore, be summed up as follows:
>
> *First*. We adhere to the opinion already announced [in *Pollock I*], that, taxes on real estate being indisputably direct taxes, taxes on the rents or income of real estate are equally direct taxes.
>
> *Second*. We are of opinion that taxes on personal property, or on the income of personal property, are likewise direct taxes.
>
> *Third*. The tax imposed by sections twenty-seven to thirty-seven, inclusive, of the act of 1894, so far as it falls on the income of real estate and of personal property, being a direct tax within the meaning of the Constitution, and, therefore, unconstitutional and void because not apportioned according to representation, all those sections, constituting one entire scheme of [income] taxation, are necessarily invalid.

See also id. at 672 (Harlan, J., dissenting):

> When, therefore, this court adjudges, as it does now adjudge, that Congress cannot impose a duty or tax upon personal property [which post-*Knowlton* constraint is not addressed by the Sixteenth Amendment], or upon income arising either from rents of real estate or from personal property, including invested personal property, bonds, stocks, and investments of all kinds, except by apportioning the sum to be so

Although subsequent pre-Sixteenth Amendment decisions of the Supreme Court did not expand *Pollock I* and *Pollock II* beyond income and wealth taxes,[35] they also did not permit Congress to impose indirect taxes on the wealth of individuals or on accessions to that wealth derived from the mere continued ownership of property.[36]

Meaning and Function of the Sixteenth Amendment. As explained in portions of Chief Justice Roberts's 2012 opinion in *National Federation of Independent Business v. Sebelius* ("*NFIB*"),[37] representing the views of a majority of the Court, the Sixteenth Amendment was adopted to overturn the result of *Pollock II*.[38]

Read in isolation, the Sixteenth Amendment can be easily misunderstood as a standalone authorization for Congress to lay and collect taxes on "incomes, from whatever source derived."[39] This is clearly not the case, however, including because the actual grant of congressional authority to lay and collect taxes on incomes, from whatever source derived, is contained in provisions of Article I that predate the adoption and ratification of the Sixteenth Amendment.[40]

The function of the Sixteenth Amendment is analyzed in the Court's unanimous opinion in *Brushaber* validating the first post-Sixteenth Amendment federal tax on the incomes of individuals (the Revenue Act of 1913) as

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raised among the States according to population, it *practically* decides that, *without an amendment of the Constitution*—two-thirds of both Houses of Congress and three-fourths of the States concurring—such property and incomes can never be made to contribute to the support of the national government.

[35] See, e.g., *Knowlton v. Moore*, 178 U.S. at 106–07 (explaining in the context of categorizing an inheritance tax as an indirect tax during the period in which the Sixteenth Amendment was drafted that "the public contribution which death duties exact is predicated on the passing of property as the result of death, as distinct from a [direct] tax on property disassociated from its transmission or receipt by will or as the result of intestacy"). See also Fernandez v. Wiener, 326 U.S. 340, 362 (1945) ("A tax imposed upon the exercise of some of the numerous rights of property is clearly distinguishable from a direct tax, which falls upon the owner merely because he is owner, regardless of his use or disposition of the property.").

[36] While Senator Brown's first draft of the resolution that ultimately became the Sixteenth Amendment referred to taxes on both incomes and inheritances, his second draft introduced after *Knowlton* referred only to income taxes. See infra note 43.

[37] 567 U.S. 519 (2012).

[38] See id. at 570–71 ("In 1895, we expanded our interpretation to include taxes on personal property and income from personal property, in the course of striking down aspects of the federal income tax. [*Pollock II*, 158 U.S. at 618.] That result was overturned by the Sixteenth Amendment, although we continued to consider taxes on personal property to be direct taxes. See *Eisner v. Macomber*, 252 U.S. 189, 218–219 (1920).").

[39] See U.S. Const. amend. XVI ("The Congress shall have the power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.").

[40] See U.S. Const., art. I, § 8, cl. 1.

a properly apportioned federal indirect tax.[41] As explained in *Brushaber*, the Sixteenth Amendment overturns the result of *Pollock II* by:

1. Leaving in place the pre-existing Article I tax categorization and apportionment system;
2. Eliminating the very last (and only the very last), incremental element of relevant jurisprudence that led the Court in *Pollock II* to categorize a tax on a properly measured amount of Sixteenth Amendment Incomes as one including one or more direct taxes—that is, a consideration of the fact that the incomes being subjected to federal tax included incomes derived by individuals from the continued ownership of property, real and personal;[42] and

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[41] The Court in *Brushaber* specifically rejected the notion that the Sixteenth Amendment created some new, third category of federal taxation, or permits a federal direct tax to be imposed other than with an apportionment among the states by population. See *Brushaber*, 240 U.S. at 11–12:

> [T]he confusion is not inherent, but rather arises from the [erroneous] conclusion that the Sixteenth Amendment provides for a hitherto unknown power of taxation, that is, a power to levy an income tax which, although direct, should not be subject to the regulation of apportionment applicable to all other direct taxes. . . .
>
> But it clearly results that the proposition and the contentions under it, if acceded to, would cause one provision of the Constitution to destroy another; that is, they would result in bringing the provisions of the Amendment exempting a direct tax from apportionment into irreconcilable conflict with the general requirement that all direct taxes be apportioned. Moreover, the tax authorized by the Amendment, being direct, would not come under the rule of uniformity applicable under the Constitution to other than direct taxes, and thus it would come to pass that the result of the Amendment would be to authorize a particular direct tax not subject either to apportionment or to the rule of geographical uniformity, thus giving power to impose a different tax in one State or States than was levied in another State or States. This result, instead of simplifying the situation and making clear the limitations on the taxing power, which obviously the Amendment must have been intended to accomplish, would create radical and destructive changes in our constitutional system and multiply confusion.

[42] See *Brushaber*, 240 U.S. at 18–19:

> [T]he command of the Amendment that all income taxes shall not be subject to apportionment by a consideration of the sources from which the taxed income may be derived, forbids the application to such taxes of the rule applied in the *Pollock Case* by which alone such taxes were removed from the great class of excises, duties and imposts subject to the rule of uniformity and were placed under the other or direct class. This must be unless it can be said that although the Constitution as a result of the Amendment in express terms excludes the criterion of source of income, that criterion yet remains for the purpose of destroying the classifications of the Constitution by taking an excise out of the class to which it belongs and transferring it to a class in which it cannot be placed consistently with the requirements of the Constitution. Indeed, from another point of view, the Amendment demonstrates that no such purpose 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.

3. Thereby causing a post-Sixteenth Amendment federal tax on a properly measured amount of Sixteenth Amendment Incomes to be categorized in its entirety as a federal indirect tax, irrespective of the sources of the income being subjected to federal indirect taxation.[43]

Brushaber further explains how the use of this particular mechanism to overturn the result of *Pollock II*—a narrowly tailored and limited modification to otherwise applicable jurisprudence—also implicitly incorporated the

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[43] See supra note 41 and additional legislative history explained in the Brief Amicus Curiae at 4 n. 4 ("[T]he difficulties, and risks of misinterpretation, associated with the manner in which the Sixteenth Amendment functions to overturn the result of an earlier decision of this Court while, at the same time, preserving as much of related jurisprudence as possible, are highlighted by relevant legislative history involving Senator Norris Brown of Nebraska."):

> Brown proposed the following language [prior to the Supreme Court's decision in *Knowlton v. Moore*, 178 U.S. 41 (1900), categorizing an inheritance tax as an indirect tax]: "The Congress shall have power to lay and collect taxes on incomes and inheritances." . . .
>
> However meritorious a constitutional amendment might have been in the abstract, Senator Isidor Rayner of Maryland quickly pointed out that Brown's language was useless. Congress already had the power to tax incomes and inheritances, he noted. The problem, at least with an income tax, was that the Court had said such a tax must be apportioned [among the States by population]: "[I]f this amendment . . . were to go through, it would not affect the [direct-tax clauses] and there would still have to be an apportionment [by population]." Rayner was obviously right, and this Brown proposal went nowhere.

Erik M. Jensen, "The Taxing Power, the Sixteenth Amendment, and the Meaning of 'Incomes,'" 33 Ariz. St. L. J. 1057, 1115 (2001) (citations omitted].

Senator Brown proposed a second draft amendment that expressly authorized Congress to lay and collect direct taxes on incomes without apportionment in the manner required of all direct taxes; Senator Brown's second draft was subsequently modified before passage; and further modifications were made by a Finance Committee chaired by Nelson Aldrich of Rhode Island, who is often characterized as an anti-tax villain. See id. at 1116–18. Of note, if Senator Brown's second draft had been adopted, it would have authorized Congress to impose federal taxes falling within the category of "direct taxes on incomes" free of both the special rule of apportionment applicable to direct taxes and the uniformity requirement contained in U.S. Const. art. I, § 8, cl. 1, because the uniformity requirement applies only to indirect taxes, and thereby would have caused the very "radical and destructive changes in our constitutional system" identified by the Court in *Brushaber*, supra note 4, as part of its rejection of related contentions and its validation of the first post-Sixteenth Amendment federal tax on the incomes of individuals as a properly uniform indirect tax in its entirety.

See also Brief of Amicus Curiae Tax Professors Donald B. Tobin & Ellen P. Apprill in Support of Respondent in Moore v. United States, at 27–29 (containing related history and citations, some of which do not reflect a misunderstanding of the function of the Sixteenth Amendment, such as the helpful citation to Edwin R.A. Seligman, "The Income-Tax Amendment," 25 Pol. Sci. Q. 193, 198 (1910) ('To say 'from whatever source derived' is simply another way of saying 'irrespective of source,' or a shorter way of saying 'from all sources alike, whether the source be one that previously made apportionment necessary or not.')"), available at https://www.supremecourt.gov/DocketPDF/22/22-800/285724/20231020160543752_44293%20pdf%20Tobin.pdf.

unmodified jurisprudence, as it existed immediately prior to the adoption and ratification of the Sixteenth Amendment, into the Constitution itself as the basis upon which to analyze whether a post-Sixteenth Amendment federal tax on the ownership of property (for example, a so-called "national wealth tax"), or on a measurement of the accessions to the wealth of an individual in excess of a properly measured amount of Sixteenth Amendment Incomes, is to be categorized as either "direct" or "indirect" for Article I purposes.[44] This secondary function and purpose of the Sixteenth Amendment—preservation of as much of the Article I direct versus indirect tax categorization and apportionment system and related jurisprudence as possible—is the generally "underappreciated" or "unknown" purpose of the amendment that is the counterpart of the "known purpose" of the Sixteenth Amendment referred to by Justice Holmes in his separate dissent in *Macomber*.[45] From Justice Holmes's emphasis on the "known purpose" of the amendment, one can also deduce that the views of the majority of the Court in *Macomber* must

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[44] See *Brushaber*, 240 U.S. at 19 (emphasis added):

> [T]he 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 [under relevant jurisprudence, including *Pollock I*, *Pollock II*, and *Knowlton*] 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 [on the basis of the source of properly measured income] to take an income tax out of the class of excises, duties and imposts, and place it in the class of direct taxes.

The result is that a tax on a properly measured amount of one or more Sixteenth Amendment Incomes remains an indirect tax, irrespective of the sources from which those properly measured incomes are derived, but a tax on an improperly measured amount of those incomes, or on the ownership property, is still subject to potential categorization as direct tax. See also supra note 34 (containing Justice Harlan's description of *Pollock II* that identifies concerns not addressed by the Sixteenth Amendment, such as limitations on Congress's authority to tax ownership of personal property).

[45] See *Macomber*, 252 U.S. at 219–20 (Holmes, J. dissenting):

> I think that *Towne v. Eisner*, 245 U. S. 418, was right in its reasoning and result and that on sound principles the stock dividend was not income. But it was clearly intimated in that case that the construction of the statute then before the Court might be different from that of the Constitution. 245 U. S. 425. I think that the word "incomes" in the Sixteenth Amendment should be read in "a sense most obvious to the common understanding at the time of its adoption." *Bishop v. State*, 149 Indiana, 223, 230; *State v. Butler*, 70 Florida, 102, 133. For it was for public adoption that it was proposed. *McCulloch v. Maryland*, 4 Wheat. 316, 407. The known purpose of this Amendment was to get rid of nice questions as to what might be direct taxes, and I cannot doubt that most people not lawyers would suppose when they voted for it that they put a question like the present to rest. I am of opinion that the Amendment justifies the tax. See *Tax Commissioner v. Putnam*, 227 Massachusetts, 522, 532, 533.

have correspondingly been influenced, at least in part, by the corresponding "less appreciated" or even "unknown to the general public" purpose.

Although not mentioned in the Brief Amicus Curiae, the related disagreement between Justice Holmes and the majority of the Court in *Macomber* can also, for the reasons explained below, be understood as a disagreement as to the weight to be given legal meanings in interpreting the language of the Sixteenth Amendment, taking into account the particular function of the amendment explained in *Brushaber* and any legislative history relating thereto that might have already been known or brought to the attention of the Court, and with the majority giving additional weight to legal meanings in the trusts and estates fiduciary accounting context explained below.[46]

The analysis of the unanimous Court in *Brushaber* (that included Justice Holmes[47]) is ultimately the basis for why, as noted by Chief Justice

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[46] See Dep't of Labor v. Greenwich Collieries, 512 U.S. 267, 275 (1994) (emphasizing in a statutory construction context "the meaning generally accepted in the legal community at the time" of adoption).

[47] The unanimous opinion in *Brushaber* was written by Chief Justice White, joined by Justices McKenna, Holmes, Day, Hughes, Devanter, and Pitney, and with Justice McReynolds having taken no part in the consideration or decision of the case. As an Associate Justice, Chief Justice White had dissented in *Pollock I* and *Pollock II* and subsequently wrote the opinion of the Court in *Knowlton*. Associate Justice White's opinion in *Knowlton* was joined by Chief Justice Fuller (the author of the majority decision in *Pollock II*) and Associate Justices Harlan, Gray, Brewer, Brown, Shiras, and McKenna, but with Justice Brewer dissenting from so much of the opinion as held that a progressive rate of tax could be imposed as part of a federal indirect tax (and in other respects concurring), a further dissent written by Justice Harlan and joined by Justice McKenna relating to a matter of statutory construction (and in other respects concurring) and Justice Peckham having taken no part in the decision. Because Justice Hughes joined in the unanimous opinion in *Brushaber*, it is also reasonable to conclude that the logic of *Brushaber* reflects the reasoning that convinced him during the early debates over the ratification of the Sixteenth Amendment, when he was serving as Governor of New York, to drop his opposition to ratification. This historical fact is also relevant to a proper understanding of matters addressed in the SALT Deduction Refund Claim. See Jensen, supra note 43, at 1122 (citations omitted):

> The ratification fight was often intense, but the Amendment was ratified quickly, in less than four years. . . . There were bumps along the way, most significantly opposition from New York Governor Charles Evans Hughes. . . . Opponents of the Amendment latched onto the Hughes argument, which delayed ratification in a few states, but Hughes received assurances that the Amendment was intended to remove apportionment only for income taxes already within congressional power, not to extend taxing power to new categories of income. Thereafter, ratification went surprisingly fast.

Although not mentioned in the Brief Amicus Curiae, Pusey's Pulitzer Prize winning biography of Charles Evans Hughes also includes related information. See Pusey, supra note 26, at 253–54 (explaining how, during the early debates over ratification, Hughes was concerned about the possibility that interpretations other than those advocated by Senator Root might prevail but that "[w]hen the scope of the amendment was tested in the Supreme Court, Justice White chose the Root interpretation and Hughes, then an Associate Justice, agreed. In his Chief Justiceship he treated the issue as closed by White's opinion . . . .").

Roberts in *NFIB*,[48] the Supreme Court continued, even after ratification of the Sixteenth Amendment, to apply relevant pre-Sixteenth Amendment jurisprudence to categorize a tax on personal property as a direct tax.[49]

Macomber addresses a constitutional issue relating to the federal income taxation of stock dividends that had previously been addressed as a matter of statutory interpretation in the Supreme Court's decision in *Towne v. Eisner*.[50] In *Towne*, a unanimous Court held the stock dividend at issue in that case *not* to be "net income" within the meaning of the Revenue Act of 1913. The majority in *Macomber* were of the view that the same type of stock dividend that had been determined not to be "net income" for statutory purposes in *Towne*, but that was expressly made subject to federal income tax under the second post-Sixteenth Amendment federal tax on the incomes of individuals, should also not be considered "income" within the meaning of the Sixteenth Amendment.[51]

The connection between *Brushaber* and *Macomber*, and the continued relevance of pre-Sixteenth Amendment jurisprudence, is implicit in additional analysis appearing on the page in *Macomber* immediately preceding the pages cited by Chief Justice Roberts in *NFIB*.[52] This connection is also reflected in the analysis of later cases.[53] The Supreme Court has also previously rejected requests to reconsider *Macomber*.[54]

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[48] Citing to pages 218–19 of *Macomber*.

[49] See supra note 38.

[50] 245 U.S. 418 (1918).

[51] The analysis in *Towne* and *Macomber* focuses, in part, on trusts and estates fiduciary accounting rules; and there are additional fiduciary accounting rules for when gains and losses are to be "realized" for those purposes as well. The syllabi of *Towne* and *Macomber* also reflect former Associate Justice, and future Chief Justice, Hughes as having participated in each case as an attorney for the ultimately successful taxpayers. See *Towne*, 245 U.S. at 419; *Macomber*, 252 U.S. at 194. Hughes's participation in *Towne* is also noted in Pusey, supra note 26, at 374 ("Although he had sat on the Supreme Bench for six years, Hughes argued his first case before that court on December 12, 1917 [citing to *Towne v. Eisner*, 245 U.S. 418].").

[52] See supra note 38; *Macomber*, 252 U.S. at 217:

> That Congress has power to tax shareholders upon their property interests in the stock of corporations is beyond question [because Congress may in all events lay and collect taxes on that subject in the form of a federal "direct tax"], and that such interests might be valued [for purposes of measuring the matter or thing being subjected to federal tax] in view of the condition of the company, including its accumulated and undivided profits, is equally clear. But that this would be taxation of property because of ownership [and not, for example, on actively doing something with property], and hence would require apportionment [as a "direct tax"] under the provisions of the Constitution, is settled beyond peradventure by previous decisions of this court [that include *Brushaber*, *Knowlton*, *Pollock II*, and *Pollock I*].

[53] See, e.g., Helvering v. Indep. Life Ins. Co., 292 U.S. 371, 378–79 (1934) ("If the statute lays taxes on the part of the building occupied by the owner or upon the rental value of that space, it cannot be sustained, for that would be to lay a direct tax requiring apportionment.") (citing, *inter alia*, *Pollock I*, *Pollock II*, *Macomber*, and *Brushaber*).

[54] See Helvering v. Griffiths, 318 U.S. 371, 374-75 (1943), (declining to reconsider *Macomber* by deciding the issue in that case as a matter of statutory interpretation).

Accordingly, if a federal tax on one or more "incomes" of individuals includes a tax on their wealth, or on a measurement of the accessions to their wealth in excess of a proper measurement of Sixteenth Amendment Incomes (for example, a tax on the particular type of non-cash dividend at issue in *Macomber*), then the tax on that wealth or excess income must be analyzed under the jurisprudence that existed immediately prior to passage and ratification of the Sixteenth Amendment to determine whether that tax is, or is not, properly apportioned in its entirety. Under this pre-Sixteenth Amendment jurisprudence (as it continued to be applied after ratification to subjects of taxation other than "incomes" within the meaning of the amendment), a federal tax on an individual's mere continued ownership of wealth (as contrasted to a use or disposition of that wealth), or on a realized or unrealized accession to that wealth derived from the continued ownership of property, is to be categorized as a direct tax that, like capitations and all other direct taxes, must be apportioned in the same manner as representation in the House of Representatives (that is, among the states based on relative populations).

The Moores Were Subjected to a Tax That Is or Includes an Unconstitutional, Improperly Apportioned Federal Direct Tax. *Commissioner v. Glenshaw Glass Co.*,[55] decided in 1955, is often viewed as the beginning of a "modern era" of income tax jurisprudence, separate and distinct from the one including *Macomber*.[56] The reasoning of *Glenshaw Glass* begins with an observation that the punitive damages awards at issue in that case are "undeniable accessions to wealth, clearly realized, and over which the taxpayers ha[d] complete dominion," which ultimately leads to an expansion of earlier, and more limited, descriptions of Sixteenth Amendment Incomes (including the one in *Macomber*) as a result of the Supreme Court holding those accessions to wealth, as so described, to be "income" both within the meaning of relevant statutory provisions and within the meaning of the Sixteenth Amendment.[57]

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[55] 348 U.S. 426 (1955).

[56] See Nathel v. Comm'r, 615 F3d 83, 88-89 (2d Cir. 2010):

> *Macomber's* limited definition of income [for constitutional purposes] was expanded [as a matter of statutory interpretation] in *United States v. Kirby Lumber Co.*, 284 U.S. 1 (1931) (finding that discharge of indebtedness caused the corporation taxpayer to realize an 'accession to income' and was taxable under the Code). Subsequently, in *Commissioner v. Glenshaw Glass Co.*, . . . the Supreme Court adopted a broad definition of income [for both statutory and constitutional purposes] as "instances of undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion." . . . The Court distinguished the narrow definition of income in *Macomber*, but in doing so, it was careful to maintain the distinction between capital and income.

[57] *Glenshaw Glass*, 345 U.S. at 431.

Cottage Savings Ass'n v. Commissioner,[58] decided in 1991, indicated that the realization element highlighted in *Glenshaw Glass* may not be constitutionally required, and instead may have been relevant only as a matter of statutory interpretation.[59] Nothing in *Cottage Savings* questions the constitutional relevance of the balance of the description of Sixteenth Amendment Incomes in *Glenshaw Glass*, thereby supporting the further conclusion that, even if Sixteenth Amendment Incomes may in certain instances include *unrealized* accessions to wealth, a proper measurement of those incomes cannot include unrealized accessions over which a taxpayer is unable to exercise "complete dominion."

In this context, one of the practical functions of an individual income tax realization requirement is to ensure a proper measurement of the amount or value of an individual taxpayer's gross incomes/accessions to wealth for a relevant measurement period. This is the case because the occurrence of a "realization event" provides an opportunity to properly measure the amount or value of a taxpayer's relevant gross "realized accession to wealth," thereby ensuring that an otherwise properly apportioned federal indirect tax (for example, one generally imposing a properly uniform rate on a proper measurement of the undeniable accessions to wealth over which the taxpayer is able to exercise complete dominion) does not in fact include either:

1. An unconstitutional, improperly apportioned federal direct tax on that individual's continued ownership of wealth held for personal use or investment purposes (as contrasted to the tax being in its entirety a tax on accessions to that wealth); or
2. An unconstitutional, improperly apportioned federal direct tax on some amount or value of that individual's accessions to wealth in excess of a properly measured amount of Sixteenth Amendment Incomes as the result of some form of mismeasurement or other matter.[60]

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[58] 499 U.S. 554 (1991).

[59] See id. at 559 (1991) (quoting Helvering v. Horst, 311 U.S. 112, 116 (1940) ("the concept of realization is 'founded on administrative convenience'").

[60] See Winkler v. U.S., 230 F2d 766 (1st Cir. 1956) (finding it unconstitutional for Congress to subject a bookmaker's profits on bets on horse racing without providing a deduction against the winnings from a single horse race for at least all of the losses incurred by the bookmaker from losing bets on the same race and possibly unconstitutional not to allow the bookmaker to calculate his income for the entire period of taxation netting his aggregate winnings against aggregate losses for the period covered). As explained in the Brief Amicus Curiae, in the case of the Moores, relevant provisions of federal tax law appear to have overstated the value of the unrealized accessions to their wealth over which they could have exercised

Relevance of Fiduciary Accounting Rules

As mentioned above, *Macomber* addressed a constitutional issue involving the federal income taxation of stock dividends that had previously been addressed as a matter of statutory interpretation in the Court's earlier decision in *Towne*. In *Towne*, where the only written opinion was that of Associate Justice Oliver Wendell Holmes, a unanimous Court including Associate Justice Louis D. Brandeis held that the stock dividend at issue in that case was not "net income" within the meaning of the Revenue Act of 1913.

The majority in *Macomber* were of the view that the same type of stock dividend that had been determined not to be "net income" for statutory purposes in *Towne,* but that was expressly made subject to federal tax under a new provision enacted as part of the second post-Sixteenth Amendment federal tax on the incomes of individuals, also should not be considered "income" within the meaning of the Sixteenth Amendment.

In reaching its conclusions and describing Sixteenth Amendment Incomes relatively narrowly, the majority explained, in part, that:

> [t]he essential and controlling fact is that the stockholder has received nothing out of the company's assets for his separate use and benefit; on the contrary, every dollar of his original investment, together with whatever accretions and accumulations have resulted from employment of his money and that of the other stockholders in the business of the company, still remains the property of the company, and subject to business risks which may result in wiping out the entire investment. Having regard to the very truth of the matter, to substance and not to form, he has received

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complete dominion. This is the case because of: (1) the nature of the Moores' equity interest (i.e., their being minority equity owners of a company whose owners did not, or could not, voluntarily elect to be subjected to federal income tax on a "flow-through" basis as a partnership or under the special flow-through type rules applicable to shareholders of so-called S corporations); (2) the apparent inability of the Moores, as the federal tax equivalent of minority shareholders in a corporation, to exercise any meaningful control over the relevant company's dividend policy; and (3) the failure to apply any lack of marketability, lack of control, or other minority ownership type valuation discount typically applied by the Internal Revenue Service in other valuation measurement contexts. See Brief Amicus Curiae at 25–27. The Brief Amicus Curiae also notes how the relevant fact pattern at issue in *Moore* is significantly different from, for example: (i) situations in which Congress has made a reasonable effort to impute to individual taxpayers a reasonable measurement of "unrealized" interest income in the form of an amortization of "original issue discount" within the meaning of IRC § 1272 or as interest income deemed to have been received in respect of a "below-market rate loan" under IRC § 7872; and (ii) the fact pattern that would arise if Congress were to attempt to tax some properly measured amount of unrealized appreciation in respect of property held for personal investment purposes that, if the relevant property had been sold or otherwise voluntarily disposed of, would have generated an equivalent amount of realized gains for federal individual income tax purposes). Id. at note 7.

> nothing that answers the definition of income within the meaning of the Sixteenth Amendment.[61]

Also of note, for the reasons explained below, is that, although Justice Brandeis had joined in Justices Holmes's opinion for the Court in *Towne*, they wrote separate dissents in *Macomber*. From the language of Justice Holmes's dissenting opinion in *Macomber*, the significance of Justices Holmes and Brandeis having written separate opinions in dissent in *Macomber* appears to relate primarily to differing views with respect to the earlier analysis in *Towne* regarding the allocation of stock dividends between trust accounting "income" and "principal/capital" for general trusts and estates fiduciary accounting purposes. Only a relatively few years earlier, in 1912, the New York Court of Appeals (New York's highest court) had stated that "no more perplexing problem had come before that tribunal than that of the proper apportionment between capital and income

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[61] *Macomber*, 252 U.S. at 211. This holding in *Macomber* is limited to a very narrow category of stock dividends but has never been overruled. See *Helvering v. Griffiths*, 318 U.S. at 374–75, denying the Government's request to reconsider *Macomber* by deciding the issue in that case as a matter of statutory interpretation and noting additional history:

> Although *Eisner v. Macomber* dealt only with a dividend of common stock to common stockholders, it was at once accepted as the basis for a broader exemption. The Treasury ruled that receipt of dividend stock generally was not income, and Congress provided in § 201(d) of the Revenue Act of 1921 that "A stock dividend shall not be subject to tax . . . ." Treasury Regulations under this statute and subsequent reenactments construed it as covering all dividends paid in stock of the distributing corporation.
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> There the matter stood for nearly fifteen years, although in the meantime this Court pointed out in reorganization cases that a distinction existed between the type of stock dividend before it in *Eisner v. Macomber* and one which gave the stockholder a different stock, or different proportionate interests, than before. *United States v. Phellis*, 257 U.S. 156 (1921); *Rockefeller v. United States*, 257 U.S. 176 (1921); *Cullinan v. Walker*, 262 U.S. 134 (1923); *Weiss v. Stearn*, 265 U.S. 242 (1924); *Marr v. United States*, 268 U.S. 536 (1925).
>
> Inaction did not mean, however, that persons who received stock dividends were escaping all support of the revenues. Taxation was only postponed, as is taxation of many securities taken in corporate reorganizations, until sale or other realization has occurred. . . . On March 30, 1936, this Court granted certiorari in *Koshland v. Helvering*, 298 U. S. 441, in which the taxpayer . . . argued that her dividend, notwithstanding *Eisner v. Macomber*, to which she gave a narrow reading, was constitutionally taxable as income at the time received. The Court held unanimously and squarely that the dividend in question did constitute income within the Sixteenth Amendment, and in effect limited *Eisner v. Macomber* to the kind of dividend there dealt with. But it did not overrule that decision or question its authority as to dividends such as we have in this case. With two Justices dissenting it struck down the apportionment regulations [at issue in *Koshland*] as being beyond statutory authorization.

of extraordinary dividends where the trust estate contains corporate stock and its creator has not expressed his wishes."[62]

In this context, it is important to note how the specific type of non-cash dividend at issue in *Macomber* was a stock dividend paid to all shareholders of a corporation in the form of common stock of the same class and in the same corporation previously held by those shareholders. For general trusts and estates fiduciary accounting purposes, depending on the relevant jurisdiction, some portion or all of the stock dividend might have been distributable to a "life-tenant/income beneficiary" instead of being allocable in its entirety to "principal/capital."[63] If the dividend at issue in *Macomber* had in fact been payable to the trustee of a trust required to allocate the entirety of that dividend to trust principal, none of the dividend would have been distributable to a "life tenant/income beneficiary" and, under these circumstances, the trustee's receipt of the stock dividend also would not have changed the aggregate "inventory" value of the holding (consisting of both the original stock and the dividend in the form of additional stock) for trust accounting purposes, including for reporting gain or loss in accounting schedules submitted in judicial accounting proceedings for purposes of enabling beneficiaries to identify sales or dispositions that might merit closer attention and

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[62] See, e.g., 5 *Warren's Heaton on Surrogate's Court Practice* § 69.08(5)(a):

> [U]ntil a 1926 amendment to former [New York] Personal Property Law Section 17-a was enacted, it was difficult to determine how to distribute stock dividends declared during the administration of the estate. Former Section 17-a as amended in 1926 provided that in the absence of an expression of contrary intent, all stock dividends were to be allocated to principal. Prior to the enactment of the 1926 amendment to former Section 17-a, the most significant decision was *In re Osborne* [103 NE 723 (N.Y 1912).] In this case, the court enunciated a very complex rule of apportionment in which extraordinary dividends not required for "preserving the integrity of the trust fund" would be distributable to income. If the stock distribution were capitalized entirely from capital surplus, it would be principal. If capitalized entirely from earned surplus, it would be payable to the income beneficiary. If capitalized from both capital and earned surplus, the dividend would be apportioned. Following the *Osborne* decision, a lack of clarity and precision continued with respect to the apportionment of stock dividends between income and principal. There were conflicting decisions, and no general rule could be stated applicable to all cases, but rather each case was required to be decided on its own facts. In fact, the Court of Appeals stated that no more perplexing problem had come before that tribunal than that of the proper apportionment between capital and income of extraordinary dividends where the trust estate contains corporate stock and its creator has not expressed his wishes.

[63] See the excerpts from Justice Brandeis's opinion in dissent in *Macomber* included as part of infra note 71.

which are sometimes referred to as a beginning "responsibility" value with respect to an investment.[64]

More complicated fiduciary accounting adjustments are required in the event of a partial, or full, allocation of a stock dividend to trust accounting "income" and its subsequent distribution to the income beneficiary/life tenant as part of the "net income" that may be required to be distributed to those beneficiaries.[65] Those complications may include matters related to the computation of trustee commissions.[66]

It is also important to note how, to this day, "gain" from the sale or disposition of property is almost always allocable, in the first instance, to trust accounting principal/capital,[67] while increases in value attributable to original issue discount (that is effectively treated as imputed "unrealized"

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[64] See Form JA-4 Trust Accounting with Instructions of the New York Surrogate's Court Procedure Act (explaining information to be included in specifically enumerated schedules required to be submitted in connection the judicial settlement of a trustee's account of proceedings that include, among others, Schedule A (principal received), Schedule A-1 (realized increases), and Schedule B (realized decreases), and explaining with respect to Schedule A, in part, that the schedule "must contain an itemized statement of all the moneys and other personal property [generally reported at "inventory" value] constituting principal for which each accounting party is charged"). It is also potentially noteworthy from an income tax realization perspective that under the historical "Massachusetts" rule, subsequently known more generally as the "prudent man" rule, and then as the "prudent person" rule, that predated the current, generally applicable "prudent investor" standard, a trustee was also effectively charged with responsibility on an asset-by-asset inventory value basis as a result of the relevant test for prudence also being applied on an investment-by-investment basis as contrasted to the portfolio as a whole. See Austin Wakeman Scott, Mark L. Ascher & William Franklin Fratcher, *Scott and Ascher on Trusts* § 19.1 (2022 Cum. Supp. 2006-2021).

[65] See infra note 71.

[66] See, e.g., New York Surrogates Court Procedure Act (NYSCPA) § 2309, which, in the case of statutory commissions of trustees in respect of non-wholly charitable trusts established after August 31, 1956, provides for a trustee's receipt of both "annual" commissions determined based on the value of principal (but not income) with respect to an annual rest date used for commission base value measurement purposes, and additional "paying" commissions in respect of payments and distributions of principal, but not of income. In this context, it is also the case that, under current New York law, the party that wishes to depart from the use of inventory values in connection with computation of the statutorily prescribed rates of annual commissions has the related burden of proof, whether the person seeking to depart from the use of inventory values is a trustee seeking to support the trustee's receipt of additional compensation, or a beneficiary seeking a reduction in fees previously taken. See language at the end of NYSCPA § 2309(1) (permitting the use of actual values in lieu of the "presumptive" (i.e., "inventory") value, but with "[t]he burden of proving that the actual value of any principal asset . . . differs from its presumptive value is upon the trustee . . . or other person claiming the difference").

[67] See, e.g., New York Uniform Principal and Income Act § 11-A-4.4(2).

income for federal income tax purposes) may, in the first instance, be properly allocated to trust accounting "income."[68]

This fiduciary accounting treatment is relevant because, as indicated above, fiduciary accounting treatment was, in fact, a factor taken into consideration by the Court in both *Towne* and *Macomber*. As mentioned earlier, the only written opinion in *Towne* is the one authored by Justice Holmes, joined by all of the other justices but with Justice McKenna joining only in the result. As part of that opinion in *Towne*, Justice Holmes wrote:

> Notwithstanding the thoughtful discussion that the case received below we cannot doubt that the dividend was capital as well for the purposes of the Income Tax Law as for distribution between tenant for life and remainderman [under trusts and estates fiduciary accounting principles]. What was said by this court upon the latter question is equally true for the former. "A stock dividend really takes nothing from the property of the corporation, and adds nothing to the interests of the shareholders. Its property is not diminished, and their interests are not increased. . . . The proportional interest of each shareholder remains the same. The only change is in the evidence which represents that interest, the new shares and the original shares together representing the same proportional interest that the original shares represented before the issue of the new ones." . . . In short, the corporation is no poorer and the stockholder is no richer than they were before.[69]

Nevertheless, Justice Holmes was among the justices writing in dissent to Justice Pitney's majority opinion for the Court in *Macomber,* explaining that "[t]he *known purpose of this Amendment* was to get rid of nice questions as to what

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[68] 6 New York Civil Practice: EPTL ¶ 11-A-4.6[1]:

> With obligations owed to the trust that were acquired at a discount and without a stated rate of interest (e.g., short-term obligations such as U.S. Treasury Bills, long-term obligations such as U.S. Savings Bonds, zero-coupon bonds, and discount bonds), the incremental increase in value at maturity is deemed income. [Citation to: EPTL 11-A-4.6(b). See, e.g., In re Small, . . . 862 NYS2d 815 (Sur. Ct. Onondaga County 2008), *aff'd as modified*, . . . 886 NYS2d 529 (4th Dep't 2009) (finding as proper, trustee's annual distribution of accreted income from zero-coupon bonds to income beneficiary).] Unrealized incremental increases in income from such obligations may be distributed out of principal, but the principal is to be reimbursed when the income is realized. In deciding whether and to what extent to exercise the power to adjust between principal and income granted by EPTL 11-2.3(b)(5), a relevant factor for the trustee to consider is the effect on the portfolio as a whole of having a portion of the assets invested in bonds that do not pay interest currently.

[69] *Towne*, 245 U.S. at 426 (citing Gibbons v. Mahon, 136 U.S. 549, 559, 560 (1890), and *Logan County v. U.S.*, 169 U.S. 255, 261 (1898), and quoted in *Macomber,* 252 U.S. at 202–03).

might be direct taxes, and I cannot doubt that most people not lawyers would suppose when they voted for it that they put a question like the present to rest."[70]

In *Macomber*, Justice Brandeis also wrote in dissent separately from Justice Holmes, possibly because, upon reconsideration of relevant fiduciary accounting matters, he was less certain than Justice Holmes that the Supreme Court's earlier analysis in *Towne* (as to which he had previously been in agreement) was correct.[71]

Moreover, in addition to the fact that Justices Holmes, White, McKenna, Day, Devanter, and Pitney were members of the Court in both *Macomber* and *Brushaber*,[72] the above reference in Justice Holmes's dissenting opinion in *Macomber* to the "known purpose of this Amendment" can be understood as a further indication of how, as discussed above, (1) the justices who decided *Macomber* were very much aware of what might be described as the "not generally known but still analyzed and explained in *Brushaber*" purpose of the Sixteenth Amendment to preserve the bulk of the *Pollock II* analysis; and (2) that "not generally known purpose" must have influenced the willingness of the majority in *Macomber* to consider fiduciary accounting treatment as part of both (a) their analysis of the meaning of "income" for constitutional purposes (and not only for statutory interpretation purposes); and (b) their formulation of a relatively narrow description of incomes for purposes of the future application of what they might have viewed as a very narrowly tailored Sixteenth Amendment that should, correspondingly, be read narrowly, particularly in light of Justice Holmes's stated preference in dissent in favor of interpreting constitutional amendments in keeping with, at least in the case

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[70] *Macomber*, 252 U.S. at 220 (emphasis added). See supra note 45 (setting out the full Holmes opinion).

[71] See *Macomber*, 252 U.S. at 234–35 (including an explanation appearing in Brandeis's opinion in dissent of three different fiduciary accounting rules potentially applicable to the allocation of dividends between "income" and "principal/capital"):

> [t]he so-called English rule . . . that a dividend representing profits, whether in cash, stock or other property, belongs to the life-tenant if it was a regular or ordinary dividend, and belongs to the remainderman if it was an extraordinary dividend[;] . . . [t]he so-called Massachusetts rule . . . that a dividend representing profits, whether regular, ordinary or extraordinary, if in cash belongs to the life-tenant, and if in stock belongs to the remainderman[; and] . . . [t]he so-called Pennsylvania rule. . . that where a stock dividend is paid, the court shall inquire into the circumstances under which the fund had been earned and accumulated out of which the dividend, whether a regular, an ordinary or an extraordinary one, was paid. If it finds that the stock dividend was paid out of profits earned since the decedent's death, the stock dividend belongs to the life-tenant; if the court finds that the stock dividend was paid from capital or from profits earned before the decedent's death, the stock dividend belongs to the remainderman.

[72] Justice McReynolds was also a member of both Courts but did not participate in the decision or consideration of the case in *Brushaber*.

of stock dividends, the "most obvious . . . common understanding at the time of its adoption" of "most people not lawyers."

It is also noteworthy, particularly in the context of the matters discussed earlier, that none of the four dissenting justices in *Macomber* appears from the two opinions in dissent to have been in disagreement with the statement in Justice Pitney's opinion (reflecting the views of the other five justices) explaining how the fact

> [t]hat Congress has power to tax shareholders upon their property interests in the stock of corporations is beyond question [because that may in all events be done in the form of a *direct* tax]; and that such interests might be valued in view of the condition of the company, including its accumulated and undivided profits, is equally clear. But that this [as contrasted to, in the view of the minority, the taxation of the receipt of additional shares in form of a stock dividend] would be taxation of property because of ownership, and hence would require apportionment [as a direct tax] under the provisions of the Constitution, is settled beyond peradventure by previous decisions of this court [that include *Brushaber, Knowlton and Pollock II*].[73]

Instead, their disagreement with the majority appears to have related only to whether the particular type of stock dividend at issue in *Macomber* was, or was not, "income" within the meaning of the Sixteenth Amendment, as contrasted to the consequences and related analysis to be applied if a federal tax on incomes, from whatever source derived, includes a tax on accessions to wealth in excess of a properly measured amount of Sixteenth Amendment Incomes.

Additional *Cottage Savings* Analysis

Although not mentioned the Brief Amicus Curiae, the difference between an actual exercise of dominion and control over accrued "income" and mere "unrealized gain" is itself highlighted by an analysis of *Cottage Savings* and the cases cited therein. For example, the earlier decision of the Supreme Court cited in *Cottage Savings* to support an understanding of realization as having been "founded on administrative convenience" involved an individual's realization of accrued interest income via an actual use or disposition of accrued and unpaid interest by reason of an assignment of that accrued income by gift.[74] Correspondingly, no basis adjustment is available at death in respect

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[73] *Macomber*, 252 U.S. at 217.

[74] See *Cottage Savings*, 499 U.S. at 559 (quoting Helvering v. Horst, 311 U.S. 112, 116 (1940)).

of accrued but unpaid interest income constituting "income in respect of a decedent" within the meaning of Section 691.

As indicated by *Macomber* and explained below, however, realization of gain in respect of appreciated property in the absence of some voluntary use or disposition of the appreciated property by the owner[75] requires a material change in the aggregate ownership rights associated with the ownership of that property. *Cottage Savings* itself explains how, "In a series of early decisions involving the tax effects of property exchanges, this Court made clear that a taxpayer realizes taxable income only if the properties exchanged are 'materially' or 'essentially' different."[76]

The first of the relevant cases cited in *Cottage Savings* is *United States v. Phellis*,[77] decided in 1921. In ruling on the taxability, pursuant to a corporate reorganization, of the receipt of, among other things, stock of a new corporation in exchange for stock of an old corporation, the majority in *Phellis* rejected both like-kind exchange treatment and a broader interpretation of *Macomber* advanced by the dissent. The opinion for the Court is written with a focus on relevant statutory language, but may also be understood as reflecting a trusts and estates fiduciary accounting understanding of what constitutes "income derived from property" for Sixteenth Amendment purposes and explains:

> The act under which the tax now in question was imposed (Act of October 3, 1913, c. 16, 38 Stat. 114, 166, 167) declares that income shall include, among other things, gains derived "from interest, rent, dividends, securities, or the transaction of any lawful business carried on for gain or profit, or gains or profits and income derived from any source whatever." Disregarding the slight looseness of construction, we interpret "gains profits, and income derived *from* . . . dividends," etc., as meaning not that everything in the form of a dividend must be treated as income, but that income derived in the way of dividends shall be taxed. Hence, the inquiry must be whether the shares of stock in the new company received by claimant as a dividend by reason of his ownership of stock in the old company constituted *(to apply the tests laid down in Eisner v. Macomber, 252 U. S. 189, 252 U. S. 207), a gain derived from capital, not a gain accruing to capital,*

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[75] The constructive sale rules under IRC § 1259 may be understood as involving a voluntary, constructive use of the appreciated position as a hedge against the newly acquired, offsetting position. Correspondingly, unrealized gain in respect of property owned by a decedent at death generally is not treated as an item of income in respect of a decedent within the meaning of IRC § 691 unless, during lifetime, the decedent took sufficient steps to be able to be treated as if the decedent had disposed of the property prior to, and not as a result of, death.

[76] *Cottage Savings*, 499 U.S. at 561–62 (citing U.S, v Phellis, 257 U. S. 156, 173 (1921); Weiss v. Stearn, 265 U. S. 242, 253–54 (1924); Marr v. U.S., 268 U.S. 536, 540–42 (1925); *Macomber*, 252 U. S. at 207–12.)

[77] 257 U.S. 156 (1921).

> *nor a growth or increment of value in the investment,* but a gain, a profit, something of exchangeable value proceeding from the property, severed from the capital however invested, and coming in, that is, received or drawn by the claimant for his separate use, benefit, and disposal.[78]

As explained above, if a federal tax on an individual taxpayer's "unrealized gains" (meaning a mere "gain accruing to capital" or "growth or increment in value of an investment") is to be properly understood as something other than a tax on "income *derived* from property" for Sixteenth Amendment purposes and instead a tax on something that continues to be property itself, that tax is, for the reasons previously explained in this article, a federal *direct* tax.[79]

The analysis of the next case cited in *Cottage Savings*, *Weiss v. Stearn*, is even more clearly intended to apply for both statutory interpretation and constitutional law purposes, as contrasted to having been intended to leave the constitutional issue undecided and thereby permit the adoption of different meanings of "income" for statutory and Sixteenth Amendment purposes along the lines suggested by Justices Holmes and Brandeis in their dissenting opinions in *Macomber*. Notably, Justices Holmes and Brandeis also dissented

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[78] Id. at 168–69 (emphasis added). Additional analysis of *Phellis* may also be helpful in understanding related conceptualizations and understandings of the nature of the "income" that can be "derived" from stock ownership. See id. at 171–72 (explaining in a manner applicable to both the stock dividend at issue in *Phellis* and to other types, including cash, of dividends):

> Where, as in this case, the dividend constitutes a distribution of profits accumulated during an extended period and bears a large proportion to the par value of the stock, if an investor happened to buy stock shortly before the dividend, paying a price enhanced by an estimate of the capital plus the surplus of the company, and after distribution of the surplus, with corresponding reduction in the intrinsic and market value of the shares, he was called upon to pay a tax upon the dividend received, it might look in his case like a tax upon his capital. But it is only apparently so. In buying at a price that reflected the accumulated profits, he, of course, acquired as a part of the valuable rights purchased the prospect of a dividend from the accumulations—bought "dividend on," as the phrase goes—and necessarily took subject to the burden of the income tax proper to be assessed against him by reason of the dividend if and when made. He simply stepped into the shoes, in this as in other respects, of the stockholder whose shares he acquired, and presumably the prospect of a dividend influenced the price paid and was discounted by the prospect of an income tax to be paid thereon. In short, the question whether a dividend made out of company profits constitutes income of the stockholder is not affected by antecedent transfers of the stock from hand to hand.

[79] Focusing on what types of income are "derived" from stock ownership may also be helpful in drawing conceptual distinctions for shareholder attribution purposes between (1) attributing *income of a corporation* to its relevant shareholders and (2) attributing *the activities of a corporation* to its relevant shareholders so that a share of the income *derived* from those current operations can be attributed to relevant shareholders on a periodic, current basis in respect of their deemed direct participation for that tax period in the deemed joint enterprise that generated their respective shares of related profits or other income derived from those activities.

from the opinion of the majority of the Court, written by Justice McReynolds, in *Weiss v. Stearn.*[80]

A proper analysis of these cases, taking into account the meaning and function of the Sixteenth Amendment, makes it difficult to conclude that "realization" of gain is a matter of "administrative convenience" only and not also a matter of constitutional significance.

Conclusions to Be Drawn

In light of (1) the fiduciary accounting treatment described above (under which "gains" from the disposition of property are, in the first instance, clearly to be allocated to principal/capital (and not "income") and also are

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[80] See *Weiss v. Stearn*, 265 U. S. at 253–54 (emphasis added):

> *Eisner v. Macomber*, 252 U. S. 189, gave great consideration to the nature of income and stock dividends. It pointed out that, within the meaning of the Sixteenth Amendment, income from capital is gain severed therefrom and received by the taxpayer for his separate use; that the interest of the stockholder is a capital one, and stock certificates but evidence of it; that, for purposes of taxation, where a stock dividend is declared, the essential and controlling fact is that the recipient receives nothing out of the company's assets for his separate use and benefit. The conclusion was that, "having regard to the very truth of the matter, to substance and not to form, he has received nothing that answers the definition of income within the meaning of the Sixteenth Amendment."
>
> Applying the general principles of *Eisner v. Macomber*, it seems clear that, if the National Acme Manufacturing Company had increased its capital stock to $25,000,000, and then declared a stock dividend of 400 percent, the stockholders would have received no gain—their proportionate interest would have remained the same as before. If, upon the transfer of its entire property and business for the purpose of reorganization and future conduct, the old corporation had actually received the entire issue of new stock and had then distributed this pro rata among its stockholders, their ultimate rights in the enterprise would have continued substantially as before—the capital assets would have remained unimpaired, and nothing would have gone therefrom to any stockholder for his separate benefit. The value of his holdings would not have changed, and he would have retained the same essential rights in respect of the assets.
>
> We cannot conclude that mere change for purposes of reorganization in the technical ownership of an enterprise, under circumstances like those here disclosed, followed by issuance of new certificates, constitutes gain separated from the original capital interest. Something more is necessary—something which gives the stockholder a thing really different from what he theretofore had. *Towne v. Eisner*, 245 U. S. 418; *Southern Pacific Co. v. Lowe*, 247 U. S. 330; *Gulf Oil Corp. v. Lewellyn*, 248 U. S. 71. The sale of part of the new stock and distribution of the proceeds did not affect the nature of the unsold portion; when distributed, this did not in truth represent any gain.
>
> Considering the entire arrangement, we think it amounted to a financial reorganization under which each old stockholder retained half of his interest and disposed of the remainder. Questions of taxation must be determined by viewing what was actually done, rather than the declared purpose of the participants, and *when applying the provisions of the Sixteenth Amendment and income laws enacted thereunder* we must regard matters of substance, and not mere form.

generally not "realized" for those purposes until an actual sale, exchange, or other disposition of the relevant property); (2) the analysis of *Brushaber,* as applied in *Macomber*, explaining the function and dual purposes of the Sixteenth Amendment (that is, to both narrowly overturn the result of *Pollock II* and also preserve the balance of relevant jurisprudence and the Article I direct vs. indirect tax categorization and apportionment system); (3) the fact that a federal tax must tax something more than the mere continued ownership of property for that tax to be properly categorized as a federal indirect tax;[81] (4) the analysis of certain of the cases cited in *Cottage Savings;* and (5) the fact that subjecting unrealized gains to federal income tax could, in many instances, force a taxpayer to sell the appreciated property in order to raise funds to pay the related federal tax,[82] it is unlikely that the Supreme Court would today hold a properly uniform federal indirect individual income tax imposed on an individual taxpayer's income including properly measured unrealized gains in respect of property held for personal use or investment

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[81] See, e.g., Fernandez v. Wiener, 326 U.S. 340, 362 (1945) ("A tax imposed upon the exercise of some of the numerous rights of property is clearly distinguishable from a direct tax, which falls upon the owner merely because he is owner, regardless of his use or disposition of the property."). The analysis of *Fernandez* and earlier cases cited therein is the constitutional basis for the imposition of a federal indirect tax on the value of trust property in connection with the "taxable termination" that occurs for federal generation-skipping transfer (GST) tax purposes when property is held in trust for multiple generations and the last beneficiary in the generation closest to the original creator of the trust dies (e.g., the "transfer" tax that is imposed when an individual creates a single trust for the benefit of multiple children, grandchildren, and more remote descendants and the last member of the child generation dies, even if the property itself is not distributed from the trust and the trust, instead, simply continues to be administered in accordance with the same terms and conditions that were in effect prior to the death of the last surviving child generation beneficiary). Notably, while the issuance of the stock dividend at issue in *Macomber* did result in a change in the property via the issuance and receipt of additional shares held by the owner, the relevant change is significantly different from the one that occurs with respect to a GST tax taxable termination because the issuance of the particular type of stock dividend at issue in *Macomber* did not involve any meaningful economic or ownership change with respect to the relevant property interest as a whole, which property interest continued to represent the same percentage ownership interest in the same class of common stock of the corporation as to which no legal or beneficial interest or right had lapsed or otherwise been transferred to a new legal or beneficial owner.

[82] See Erik M. Jensen, "Wealth Taxes Can't Satisfy Constitutional Requirements," Daily Tax Rep. (Bloomberg Tax, July 27, 2021), available at https://news.bloombergtax.com/daily-tax-report/wealth-taxes-cant-satisfy-constitutional-requirements ("The proposals [including one applicable to unrealized appreciation found in many trusts] would 'deem' such appreciation to have been realized, even though no sale has occurred. Worse yet, the tax would be imposed on asset appreciation in trusts that were created decades ago, when no one could have imagined these proposals. Left unsaid is how trusts are expected to pay the tax without liquidity from an actual sale."); Brief of Amicus Curiae L.E. Simmons in Support of Respondent, *Moore v. United States*, at 11–14 (Oct. 2023), available at https://www.supremecourt.gov/DocketPDF/22/22-800/284757/20231011163919945_22-800_Amicus%20Brief.pdf (containing text of section entitled "An Income Tax on Unrealized Capital Gains that Compels the Sale Of Property to Pay the Tax Could Implicate the 'Public Use' Component of the Takings Clause").

purposes acquired prior to the date of enactment to be properly apportioned in its entirety.

Correspondingly, non-recognition of unrealized gains at death cannot be properly characterized as a "loophole," but is instead a necessary element of federal income tax law required to ensure compliance with otherwise applicable constitutional limitations on congressional taxing authority.

As noted earlier, however, the underlying analysis presented should not be understood as implying that Congress cannot: (1) treat a lifetime gift or other affirmative act taken in respect of securities or other property as a "realization event" for federal income tax purposes; (2) impose a federal inheritance tax in the form of a federal indirect tax that effectively treats the receipt of a gift or bequest as additional gross income of the recipient in the year of receipt; or (3) impose an additional or higher rate of federal transfer tax in the form of a federal indirect tax on the value of transferred property in excess of the transferor's federal income tax basis therein at the time of transfer (for example, a higher rate of federal estate tax on the value of property transferred by reason of death representing long-term capital gains that remained unrealized at death not already constituting "income in respect of a decedent" within the meaning of Section 691).

Similarly, the underlying analysis presented should not be understood as calling into question any provision of federal tax law applicable to the income taxation of corporations at the corporate level because federal corporate income taxes (federal taxes imposed on one or more or all of the realized or unrealized incomes of corporations derived from any source whatever) are subject to proper recharacterization for relevant constitutional purposes as the equivalent of a franchise tax imposed in respect of the privilege of conducting activities in corporate form.

A discussion of whether, absent a further amendment to the Constitution, Congress has the authority to enact a federal tax in the form of an indirect tax on incomes including unrealized gains (or to eliminate non-recognition of gain at death or, in the case of a foreign corporation, to attribute accumulated "profits" to current U.S. shareholders without the distributions corresponding to those that would trigger trust "throwback" taxation[83]) in respect of securities or other property acquired after the date of enactment is beyond the scope of this article.

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[83] See the discussion of certain trust and controlled foreign corporation matters in supra notes 16, 21 & 78–79.

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