Barry Law Review

Volume 12
Issue 1 *Spring 2009*

Article 2

2009

"Taxnapping": How Murphy v. IRS Used Direct Taxation to Steal the Tax Reform Debate

Jason A. Derr

"TAXNAPPING": HOW *MURPHY V. IRS* USED DIRECT TAXATION TO STEAL THE TAX REFORM DEBATE

Jason A. Derr[*]

ABSTRACT

Suppose someone asks you, "You know, I'm fed up with the tax policy of the United States, what can I do to change it?" Although some may respond with ideas of protest, one of the most common responses will likely be, "Call your Congressperson." However, after the D.C. Circuit's decision in *Murphy v. IRS*, a new response is offered. If you want to change tax policy, "call *the judge's chambers*."

In *Murphy v. IRS*, decided in 2007, the D.C. Circuit considered whether the taxation of emotional injury damages violated the "direct tax clauses" of the United States Constitution. The direct clauses are a mysterious pair of clauses that were never defined in the Constitution, made even more complex by early Supreme Court case law, and have since been ignored by the Court for over 70 years. It was 1934 when the Supreme Court last addressed the issue of direct taxation, and since that date, there is still no clear answer to the question, "What is a 'direct tax?'"

Murphy's direct tax analysis was a complicated mess of precedent. The court's application of stare decisis is internally inconsistent. Additionally, the court's analysis contradicts Supreme Court case law and some of the major originalist interpretations of the direct tax clauses.

By confusing the law on direct taxation, the D.C. Circuit has put fundamental income tax reform in jeopardy. Any shift from the current federal income tax to a "flat tax" or a "FairTax" may raise the constitutional issue of whether such a tax is a "direct tax." Since *Murphy* leaves the law open-ended, anyone who objects to such tax reform can use the federal courts to stop Congress from reforming the income tax. When a judicial decision steals the tax policy debate away from the legislature, they have committed "taxnapping," a term defined for the first time in this Note. In short, "taxnapping" is wrong, and this Note shows how to define it and how the Supreme Court can stop it.

* Member, Maryland State Bar; Attorney, Board of Governors of the Federal Reserve System, Office of Inspector General, Washington, D.C.; J.D., Catholic University of America, Columbus School of Law; B.A., King's College, Wilkes-Barre, PA. The author's views and opinions expressed in this Note are in no way endorsed by, or affiliated with, the United States Government or the Board of Governors of the Federal Reserve System. The content of this Note is solely the viewpoint of the author. The author wishes to thank Professor A.G. Harmon, J.D., Ph.D. for his expert guidance and insight during the conception, revision, and completion of this Note, as well as Professor Norman Stein for his assistance in the initial stages of working through the *Murphy* case and its direct taxation implications. In addition, the author wishes to thank his fiancée, Suzanne, for her constant love and endless support.

I. INTRODUCTION

"Taxnapping" can be understood to occur when the judiciary steals tax policy debate away from the legislature.[1] There are three prerequisites for taxnapping to occur: (1) a tax case must be before the court; (2) the court's decision must have the potential to alter tax policy; and (3) the court's opinion must leave the tax law ambiguous. When these three elements combine, there is taxnapping because the courthouse doors swing open for tax policy protestors to reroute their policy arguments through the judiciary instead of through the legislature. An unclear judicial decision that has the potential to change tax policy will create an incentive for those in opposition to file lawsuits in hopes of exploiting the law to alter tax policy. Therefore, whenever a court fails to clarify the tax law in an area that has a significant chance of altering tax policy, the court has taxnapped, thereby making it possible for tax policy protestors to change tax policy in the courtroom instead of at the voting booth.

Taxnapping leads to inappropriate and undemocratic results. With taxnapping exposing the judiciary to competing tax policy arguments, courts are placed in the position of favoring one side's argument and thereby rendering a decision that underhandedly creates tax policy. But courts are inappropriate policymaking fora because they lack the necessary resources.[2] Without the legislature's ability to hold hearings and consult with experts, courts cannot obtain the best possible information on which to base sound policy decisions.[3] In addition, courts are not adequately staffed to evaluate the effectiveness of their policy decisions.[4] Policymaking in the judiciary is also undemocratic because it allows judges—always a minority—to render a decision that makes public policy without the approval of the majority.[5]

1. The term "taxnapping" is a term of art used for the first time by this author. Also, please note that throughout this paper, "taxnapping" is discussed in its federal manifestation because the noted case of *Murphy v. Internal Revenue Service* (*Murphy I*), 493 F.3d 170 (D.C. Cir. 2007), which created the idea for the term, only relates to federal tax law. However, there is no reason why the term "taxnapping" cannot also refer to state court decisions on state tax law.

2. *See* Missouri v. Jenkins, 495 U.S. 33, 69 (1990) (Kennedy, J., concurring) (stating that the judiciary lacks the ability to hold hearings and must "grope ahead with only the assistance of the parties, or perhaps random *amici curiae*") (emphasis in original); G. ALAN TARR, JUDICIAL PROCESS AND JUDICIAL POLICYMAKING 299 (4th ed. 2006) (summarizing "well-known" judicial policymaking critic, Donald Horowitz, as asserting that "courts are less likely than other institutions to obtain relevant information and use it effectively" because, for example, courts decide cases based on "legal considerations rather than on the desirability of a policy or the likely consequences of alternative approaches to a problem").

3. *See* Hon. Malcolm Richard Wilkey, *Judicial Activism, Congressional Abdication, and the Need for Constitutional Reform*, 8 HARV. J.L. & PUB. POL'Y 503, 511 (1985) (describing that courts have "no facilities for holding public hearings to gather expert information and facts on which important policy decisions should be based").

4. *Id.* at 512.

5. *See id.* at 504 (describing the process of judges making policy as containing a "fundamentally anti-majoritarian element"). It is also important to note that taxnapping in the main case of *Murphy v. Internal Revenue Service* is especially undemocratic. In some contexts, judicial policymaking, although never absolutely favored, can occasionally be acceptable. *See* TARR, *supra* note 2, at 299 (describing how judicial policymaking is not necessarily always undemocratic, such as when the court engages in "statutory policymaking and judicial oversight of administrative agencies" and the judges are "presumably giving effect to, rather than overriding, the will of the legislature"). However, "constitutional policymaking," which is what occurs in *Murphy v. Internal Revenue Service*, is inappropriate because it often pits the elected legislature directly against the unelected judiciary. *Id.*

It is difficult to imagine a greater ambiguity in tax law than the constitutional mystery of direct taxation. The term "direct tax" derives from two provisions in the United States Constitution that limit Congress's power to tax.[6] Although the Constitution grants Congress the broad power "[t]o lay and collect [t]axes,"[7] this authority is limited by the two direct tax clauses found in Article I, Section 2[8] and Article I, Section 9.[9] Read together, these clauses restrain Congress from imposing a "direct" tax unless the tax is "apportioned,"[10] meaning that the tax would have to be structured so that each state pays the tax in proportion to its population.[11]

The mystery of the direct tax clauses exists because the term "direct tax" was never defined in the text of the Constitution.[12] In fact, when Rufus King asked the assembly for a "precise meaning of direct taxation" at the Constitutional Convention of 1787, no one answered him.[13] Modern legal scholars continue to argue over the meaning of the term, citing to sources such as the dictionary of 1787,[14] the Federalist Papers,[15] and even the economic theories of the French Physiocrats.[16] In addition, scholars such as Yale Professor Bruce Ackerman point out that the direct tax clauses originated as part of a "political compromise" over slavery.[17] Ackerman argues that the apportionment requirement of direct taxation was placed into the Constitution so that slave states, if they wanted their slaves to count toward representation in the House, would have to pay taxes in proportion to their popula-

6. U.S. CONST. art. I, § 2, cl. 3; U.S. CONST. art. I, § 9, cl. 4.

7. U.S. CONST. art. I, § 8, cl. 1.

8. *See* U.S. CONST. art. I, § 2, cl. 3 (providing that "direct [t]axes shall be apportioned among the several States . . . according to their respective [n]umbers . . . .").

9. *See* U.S. CONST. art. I, § 9, cl. 4 (providing that "[n]o [c]apitation, or other direct, [t]ax shall be laid, unless in [p]roportion to the Census or Enumeration herein before directed to be taken").

10. *See* U.S. CONST. art. I, § 2, cl. 3 (limiting Congress's power to tax by providing that "direct [t]axes shall be apportioned among the several States . . . according to their respective [n]umbers . . . ."); U.S. CONST. art. I, § 9, cl. 4 (limiting Congress's power to levy a "[c]apitation, or other direct, [t]ax" unless such tax is "in [p]roportion to the Census or Enumeration herein before directed to be taken").

11. *See* Bruce Ackerman, *Taxation and the Constitution*, 99 COLUM. L. REV. 1, 2 (1999) (describing how direct taxes would require any flat tax rate to "vary . . . on a state-by-state basis with the aim of assuring that each one contributed a sum proportional to its population"). Professor Ackerman also comments on the regressive nature of the apportionment requirement. Ackerman states, "[Apportionment] means that the citizens of a poor state such as Alabama—whose per capita levels of income and consumption are relatively low—would have to pay a higher flat tax than citizens of a rich state such as Oregon." *Id.*

12. *See* U.S. CONST. art. I, § 2, cl. 3 (stating that "direct [t]axes shall be apportioned among the several States . . . according to their respective [n]umbers . . . ." without any further definition of the term "direct [t]axes"); U.S. CONST. art. I, § 9, cl. 4 (providing that "[c]apitation, or other direct, [t]ax" must be "in [p]roportion to the Census or Enumeration herein before directed to be taken" without providing any indication as to the meaning of the phrase "or other direct" tax).

13. 2 RECORDS OF THE FEDERAL CONVENTION OF 1787 350 (Max Farrand ed., Yale Univ. Press 1911) (1787).

14. *See* Calvin H. Johnson, *Fixing the Constitutional Absurdity of the Apportionment of Direct Tax*, 21 CONST. COMMENT. 295, 314 (2004) (stating, under the subsection "The 1787 Dictionary Meaning of 'Direct Tax,'" that the dictionary definition of "direct tax" would have listed it as "a synonym for apportioned tax").

15. *See* Erik M. Jensen, *The Apportionment of "Direct Taxes": Are Consumption Taxes Constitutional?*, 97 COLUM. L. REV. 2334, 2395 (1997) (defining direct taxation by extrapolating from Alexander Hamilton's definition of indirect taxes in The Federalist No. 36).

16. *See* Ackerman, *supra* note 11, at 16–17 (stating that the idea of distinguishing direct taxation from other taxes, such as indirect taxation, was first introduced by John Locke and then "more systematically developed in the course of the eighteenth century by the school of French Physiocrats led by Francois Quesnay and Baron Turgot").

17. *Id.* at 4.

tion.[18] However, Professor Erik M. Jensen argues that a focus on slavery alone is inappropriate because the direct tax clauses were also meant to limit the new federal government's power to enact "sectionally directed" taxes on the states.[19]

It should come as no surprise that arguments over the meaning of the direct tax clauses quickly came before the United States Supreme Court. Beginning in 1787, with the case of *Hylton v. United States*, and continuing on for nearly a century, the Supreme Court defined direct taxation so narrowly that the term was essentially read out of the Constitution.[20] In case after case, no taxes imposed by Congress were struck down due to the Court's constricted reading of the direct tax clauses.[21] But in 1895, nearly one hundred years of precedent changed when the Supreme Court decided *Pollock v. Farmer's Loan & Trust Co.* and struck down the entire federal income tax for violating the direct tax clauses.[22] Despite this fact, immediately after *Pollock*, the Court quickly changed its mind and began eroding its rationale for the *Pollock* decision and upholding many federal taxes as constitutional.[23]

As the Court was beginning to move away from the *Pollock* rationale,[24] a major event occurred: the adoption of the Sixteenth Amendment to the Constitution.[25] Proposed by President Taft as an effort to allow Congress to impose a broad in-

18. *Id.*

19. Erik M. Jensen, *Interpreting the Sixteenth Amendment (By Way of the Direct-Tax Clauses)*, 21 CONST. COMMENT. 355, 377 (2004).

20. *See* Hylton v. United States, 3 U.S. (3 Dall.) 171, 181 (1796) (stating that the Constitution's use of the term "direct taxes" refers to only such taxes "*as could be apportioned*") (emphasis in original); Pacific Ins. Co. v. Soule, 74 U.S. (7 Wall.) 433, 446 (1869) (applying the *Hylton* rule that direct taxes are only those that can be apportioned and holding that a tax on the income of an insurance company was not a direct tax); Veazie Bank v. Fenno, 75 U.S. (8 Wall.) 533, 546 (1869) (stating, in accordance with the narrow definition of direct tax described in *Hylton*, that the only direct taxes requiring apportionment are "capitation taxes," "taxes on land," and "perhaps taxes on personal property by general valuation and assessment of the various descriptions possessed with the several States"); Scholey v. Rew, 90 U.S. (23 Wall.) 331, 346–47 (1874) (holding that a real estate tax for succession during the Civil War was only an excise tax and not a direct tax because it was a tax on the transfer of property); Springer v. United States, 102 U.S. 586, 602 (1880) (citing *Hylton* and holding that the Civil War income was not a direct tax because direct taxes are only capitation taxes and taxes on land).

21. *See Hylton*, 3 U.S. (3 Dall.) at 181 (upholding a carriage tax); *Pacific Ins. Co.*, 74 U.S. (7 Wall.) at 446 (upholding a tax on the income of insurance companies); *Veazie Bank*, 75 U.S. (8 Wall.) at 546 (upholding a ten percent tax on the insurance of bank notes); *Scholey*, 90 U.S. (23 Wall.) at 346–47 (upholding a real estate tax for succession during the Civil War); *Springer*, 102 U.S. at 602 (upholding an income tax imposed to fund the Civil War).

22. *See* Pollock v. Farmers' Loan & Trust Co. (*Pollock I*), 157 U.S. 429, 583 (1895) (holding that the portions of the post-Civil War income tax that imposed taxes on "rents" or "income of real estate" violated the direct tax clauses); Pollock v. Farmers' Loan & Trust Co. (*Pollock II*), 158 U.S. 601, 637 (1895) (holding that taxes on "personal property" and on "the income of real property" are direct taxes and striking down the entire income tax of 1894 as unconstitutional because it constitutes "one entire scheme of taxation").

23. *See, e.g.*, Gregory L. Germain, *Taxing Emotional Injury Recoveries: A Critical Analysis of* Murphy v. Internal Revenue Service, 60 ARK. L. REV. 185, 230–40 (describing how the Supreme Court began a "retreat" from the *Pollock* cases by allowing taxes on the exchange of property to be upheld despite the fact that *Pollock*'s rationale was based on the idea that it was not exchange that mattered but whether "the source of item subject to tax was property").

24. *See, e.g.*, *id.* at 231–35 (discussing how the next two cases after *Pollock*, *Knowlton v. Moore* and *Thomas v. United States*, moved away from Pollock's focus on whether the source of the tax was property and instead the Court became more concerned with whether the tax was placed on a transaction).

25. *See id.* at 237–38 (showing the importance of the passage of the Sixteenth Amendment in 1913 by stating that it prevented the Supreme Court from creating a "fully developed . . . distinction between direct and indirect taxation").

come tax,[26] the Sixteenth Amendment created an exception that allowed income taxes to be imposed even if they were direct taxes and violated the apportionment requirement.[27] The passage of the Sixteenth Amendment restrained the Court from developing a clear definition of direct taxation.[28] All direct taxes on "income" were now protected from the apportionment rules.[29]

However, the direct tax clauses and their apportionment requirement were not wiped out entirely by the passage of the Sixteenth Amendment.[30] The clauses still retain their full effect on taxes that are not "income" taxes.[31] Since 1934, the Supreme Court has not heard a case on the meaning of the direct tax clauses.[32] The Court's long silence has left many questions unanswered, including what, if any, precendential weight should be given to the Court's two major direct tax cases of *Hylton* and *Pollock*.

In 2007, *Murphy v. Internal Revenue Service*, decided by the United States Court of Appeals for the District of Columbia Circuit, the Court chose to unearth the nearly forgotten direct tax clauses.[33] *Murphy*'s treatment of direct taxation is a disaster and a patent case of taxnapping. The court devotes an entire section of its opinion to arguments over the meaning of the direct tax clauses, citing to the Federalist Papers, various legal scholars, and the decisions of both *Hylton* and *Pollock*.[34] In doing so, the court lays out a convoluted description of the law that comes nowhere near a clear rule.[35] Moreover, the court contradicts its own view of the case law by citing some cases for support while suggesting that those cases may not be good law in a footnote.[36] What *Murphy* amounts to is an outline of the open loopholes in the definition of direct taxation—loopholes that can be used by tax policy protestors when they do not get their way in Congress.

Murphy's practical impact is that the decision places fundamental income tax reform in jeopardy of being held up inappropriately and undemocratically by the judiciary.[37] In the past few decades, many scholars have proposed a wide range of

26. *Id.* at 237.

27. *See* U.S. CONST. amend. XVI (stating, "The Congress shall have 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").

28. *See* Germain, *supra* note 23, at 237–38 (stating that the court "never fully developed the distinction between direct and indirect taxation because Congress passed and the states adopted the Sixteenth Amendment to the United States Constitution in 1913").

29. *Id.*

30. *Id.* at 240.

31. *See* U.S. CONST. amend. XVI (providing that only "taxes on incomes" may be imposed without apportionment).

32. ERIK M. JENSEN, *DIRECT TAXES IN* THE HERITAGE GUIDE TO THE CONSTITUTION 159, 160 (David F. Forte & Matthew Spalding eds., 2005).

33. Murphy v. Internal Revenue Service (*Murphy I*), 493 F.3d 170, 180–86 (D.C. Cir. 2007).

34. *Id.*

35. *See, e.g., id.* at 181–85 (outlining the arguments presented by Murphy on direct taxation and the arguments presented by the government on direct taxation—many of which are based on the Federalist Papers and originalism—and then rejecting the theories of both sides in order to move to an excise tax analysis).

36. *See id.* at 181 n.** (citing case law to support that there are three taxes that are "definitely known" to be direct taxes but also questioning in a footnote whether caselaw relied on in creating this list of three taxes is good law).

37. *See supra* notes 2–5 and accompanying text.

policy proposals for fundamental reform of the federal income tax system.[38] Responding to various inefficiencies in the current federal income tax,[39] no less than five different tax reform systems have been proposed.[40] The major reform proposals include: (1) a national retail sales tax,[41] (2) a value-added tax,[42] (3) a flat tax,[43] (4) a "USA," or "unlimited savings allowance," tax,[44] and (5) a "FairTax."[45] Understanding the pros and cons of each reform proposal can be daunting, and there are seemingly endless arguments and counterarguments on each side.[46] Many of these tax proposals will shift the tax base from "income," which is exempt from the direct tax clauses,[47] to "consumption,"[48] which is not so clearly exempt from the direct tax clauses.[49] If any of these reform proposals were to become federal law, *Murphy*'s failure to create a clear rule on direct taxation allows those who oppose tax reform to run to the courts and use the ambiguous law of direct taxation to push aside the will of the majority.

This Note argues that *Murphy v. Internal Revenue Service* is a problematic case of taxnapping that threatens to reroute the public debate over fundamental income tax reform. In Part II, this Note begins by providing a brief snapshot of the complex policy debate over fundamental income tax reform. Part III outlines the scope of Congress's power to tax and the ways in which this power is limited by the direct tax clauses. Part IV focuses on the direct tax clauses and describes the confusion over the original meaning by summarizing the many different originalist interpretations. Part V shows how the case law of the United States Supreme Court has only amplified the confusion over the meaning of the direct tax clauses. Part VI

38. *See generally* MICHAEL J. BOSKIN, FRONTIERS OF TAX REFORM (Michael J. Boskin ed., 1996) (compiling essays on all income tax reform proposals, including the flat tax, retail sales tax, value-added tax, USA tax, and hybrid consumption tax).

39. *See, e.g.*, J. Scott Moody, Wendy P. Warcholik & Scott A. Hodge, *The Rising Cost of Complying with the Federal Income Tax*, 138 TAX FOUNDATION 1, 1 (2005) (predicting that in 2005 "individuals, businesses, and non-profits will spend an estimated 6 billion hours complying with the federal income tax code," which amounts to a compliance cost of roughly $265.1 billion).

40. *See* HENRY J. AARON & WILLIAM G. GALE, INTRODUCTION TO ECONOMIC EFFECTS OF FUNDAMENTAL TAX REFORM 1, 6–14 (Henry J. Aaron & William G. Gale eds., 1996) (outlining briefly the various pros and cons of each major income tax reform proposal).

41. *Id.* at 6.

42. *Id.* at 7.

43. *Id.* at 12; Robert E. Hall & Alvin Rabushka, *The Flat Tax: A Simple, Progressive Consumption Tax*, *in* FRONTIERS OF TAX REFORM 27–53 (Michael J. Boskin ed., 1996).

44. AARON & GALE, *supra* note 40, at 12–13; Murray Weidenbaum, *The Nunn-Domenici USA Tax: Analysis and Comparisons*, *in* FRONTIERS OF TAX REFORM 54–69 (Michael J. Boskin ed., 1996).

45. NEAL BOORTZ & JOHN LINDER, THE FAIRTAX BOOK: SAYING GOODBYE TO THE INCOME TAX AND THE IRS (2005); NEAL BOORTZ & JOHN LINDER, FAIRTAX: THE TRUTH, ANSWERING THE CRITICS (2008).

46. *See* AARON & GALE, *supra* note 40, at 6–14 (outlining briefly the pros and cons of each major proposal in the fundamental tax reform debate).

47. *See* U.S. CONST. amend. XVI (exempting "taxes on incomes" from the apportionment requirement).

48. *See* Jensen, *supra* note 15, at 2402–09 (describing the retail sales tax, value-added tax, flat tax, and USA tax as "consumption taxes"); Lester B. Snyder & Mariane Gallegos, *Redefining the Role of the Federal Income Tax: Taking the Tax Law "Private" Through the Flat Tax and Other Consumption Taxes*, 13 AM. J. TAX. POL'Y 1, 8–18 (1996) (describing the flat tax, USA tax, and value-added tax as all "consumption" taxes).

49. *Compare* Jensen, *supra* note 15, at 2407 (arguing that the flat tax and the USA tax are "direct" taxes and that they will have to be apportioned), *with* Lawrence Zelenak, *Radical Tax Reform, the Constitution, and the Conscientious Legislator*, 99 COLUM. L. REV. 833, 837–45, 855 (1999) (critiquing Jensen's argument that the flat tax and USA are "direct" taxes and concluding that some of Jensen's distinctions "make no sense (or are even perverse) . . . .").

analyzes the case of *Murphy v. Internal Revenue Service* and describes how the court's decision, like the many cases before it, leaves the law on direct taxation incredibly unclear. In conclusion, Part VII argues that *Murphy*'s treatment of direct taxation is a clear case of taxnapping and describes how the Supreme Court can solve *Murphy*'s taxnapping deficiency and make sure tax policy decisions stay out of the judiciary.

II. FEDERAL TAX REFORM: FROM THE DRUNKEN PAST TO THE CONSUMPTION PRESENT

Tax reform in the United States dates as far back as the Whiskey Rebellion of 1794. The Whiskey Rebellion began on July 16, 1794, when roughly fifty western Pennsylvania men protested the collection of a tax on all "domestically distilled spirits."[50] When John Neville, the local tax collector, refused to resign his post or hand over his collection records, the shooting began, leaving one man dead.[51] The next day, the mob grew to between 400 and 800 individuals who began setting homes and barns on fire throughout the region.[52] After the masses grew to include 7,000 Pennsylvanians and a multitude of others from western Maryland, President George Washington gathered 12,950 militiamen to finally crush the insurrection.[53]

Although gunfire and arson are no longer the chosen methods of today's tax protestors, the United States still retains its distaste for taxation. In the past several decades, the tax reform movement in the United States has focused narrowly on one particular method of taxation: the federal income tax.[54] Criticisms abound concerning the current federal income tax system.[55] For example, in 2005, a report issued by the Tax Foundation estimated the cost of complying with the current federal income tax at $265.1 billion.[56] In response to these and other deficiencies, no less than five major tax reform systems have been proposed.[57] As described previously, the major reform proposals include (1) a national retail sales tax,[58] (2) a value-added tax,[59] (3) a flat tax,[60] (4) a "USA," or "unlimited savings allowance," tax,[61] and (5) a "FairTax."[62]

50. THOMAS P. SLAUGHTER, THE WHISKEY REBELLION: FRONTIER EPILOGUE TO THE AMERICAN REVOLUTION 3 (1986).

51. *Id.*

52. *Id.*

53. *Id.*

54. *See* AARON & GALE, *supra* note 40, at 1 (stating that proposals for fundamental tax reform, such as proposals to "alter or replace the current personal and corporation income taxes," came "barely a decade after President Reagan signed the Tax Reform Act of 1986").

55. *See, e.g.*, Moody, Warcholik & Hodge, *supra* note 39, at 138 (predicting that in 2005 "individuals, businesses, and non-profits will spend an estimated 6 billion hours complying with the federal income tax code," which amounts to a compliance cost of roughly $265.1 billion).

56. *Id.*

57. *See* AARON & GALE, *supra* note 40, at 6–14 (summarizing many of the major income tax reform proposals).

58. *Id.* at 6.

59. *Id.* at 7.

60. *Id.* at 12; Hall & Rabushka, *supra* note 43, at 27–53.

61. AARON & GALE, *supra* note 40, at 12–13; Weidenbaum, *supra* note 44, at 54–69.

Each income tax reform system has its supporters and its opponents. The arguments in favor of each system are as numerous as the criticisms. Those in favor of these various systems argue that their reforms will lead to simplicity, efficiency, and fairness. For example, supporters of the national retail sales tax and the flat tax submit that their systems are simple because each will eliminate the current graduated tax rates in favor of a single, fixed tax rate on consumption.[63] The reforms outlined in the flat tax, USA tax, and FairTax are claimed to be more economically efficient than our current federal income tax because each system creates savings incentives that can be used for future investment.[64] Finally, proponents of the flat tax and FairTax argue that these systems are fair because each reform proposal protects low-income taxpayers from a disproportionately high, flat tax rate on their consumption of basic needs.[65]

Opponents, on the other hand, counter that these tax reform proposals raise serious administrability and fairness issues. The retail sales tax is criticized as unworkable because many services are not easily taxable, such as financial services.[66] The USA tax, which does not tax any money that is saved, presents transitional problems because it creates incentives for individuals to hide assets in the transition phase until they can later be placed into tax-free savings accounts.[67] Both the retail sales tax and the value-added tax are discounted because, by taxing retail sales, the systems place heavy tax burdens on low-income taxpayers.[68] And the flat tax system and the FairTax system, which both protect low-income taxpayers with exemptions, can nevertheless be criticized as unfair because each plan reduces the tax

62. BOORTZ & LINDER, THE FAIRTAX BOOK, *supra* note 45; BOORTZ & LINDER, THE TRUTH, *supra* note 45.

63. *See* Stephen Moore, *The Economic and Civil Liberties Case for a National Sales Tax*, *in* FRONTIERS OF TAX REFORM 115, 117 (Michael J. Boskin ed., 1996) (describing how the national sales tax is simple because it "exempts all savings and investments," eliminates "the double taxation problem," and is "a single flat rate"); Hall & Rabushka, *supra* note 43, at 53 (stating that the flat tax "would bring a drastic simplification of the tax system" because, in part, "[i]t imposes an across-the-board consumption tax at the low rate of 19 percent").

64. *See* Hall & Rabushka, *supra* note 43, at 36–37 (describing how under the flat tax system "[s]aving is untaxed" and, since "[e]very act of investment in the economy ultimately traces back to an act of saving," the flat tax will provide investment incentives); Weidenbaum, *supra* note 44, at 59 (outlining how, "under a consumption-based tax," such as the USA Tax, "both saving and long-term investment are encouraged at the expense of current consumption"); BOORTZ & LINDER, THE FAIRTAX BOOK, *supra* note 45, at 108 (claiming, "Virtually every economic study on the FairTax proposal concludes that people from one end of the economic spectrum to the other—from the poor to the very rich—will either start a savings and investment plan or increase the one they already have").

65. *See* Hall & Rabushka, *supra* note 43, at 53 (claiming, "The flat tax is progressive—it exempts the poor from paying any tax and imposes a tax that is a rising share of income for other taxpayers"); BOORTZ & LINDER, THE FAIRTAX BOOK, *supra* note 45, at 108 (describing how the FairTax plan protects low-income taxpayers by providing a "prebate," which is a "monthly check covering taxes on all basic household necessities").

66. *See* AARON & GALE, *supra* note 40, at 7 (criticizing the national retail sales tax because of its "serious and possibly insuperable administrative problems," such as the difficulty in taxing "banking services").

67. *See id.* at 13 (stating that the USA Tax raises "administrative problems" because "taxpayers would have powerful incentives to conceal old wealth, perhaps by moving it offshore, and to bring it back after the new tax comes into effect, thereby qualifying for the unlimited savings allowance").

68. *See id.* at 12 (stating, "[T]he value-added tax, like the retail sales tax, imposes disproportionate burdens on low-income households").

rates of high-income taxpayers and shifts the tax burden onto all remaining taxpayers.[69]

The debate over how to best reform the federal income tax raises fundamental questions about the value system behind the principal source of federal government revenue. Proponents of reform argue that revenue should be raised efficiently.[70] Opponents argue that revenue should be raised fairly.[71] There is no easy answer to the debate, and any attempt to formulate an answer is no doubt beyond the scope of this Note. Rather, the purpose of this Note is to clearly outline the appropriate role for the judiciary in the tax policy process.

III. CONGRESS'S POWER TO TAX AND ITS "DIRECT" LIMITATIONS

While considering the debate on fundamental tax reform, it is easy to believe that a reform-minded Congress can choose which tax system it prefers, turn the system into legislation, present it to the President, and wait for the simplicity, efficiency, and fairness to materialize. However, before Congress can make such a decision, it must overcome the restrictions of the two "direct tax clauses" of the U.S. Constitution.[72]

The two direct tax clauses appear in Article I of the Constitution, and their function is to limit Congress's otherwise plenary power of taxation.[73] Article I, Section 8, Clause 1 grants Congress the broad authority "[t]o lay and collect Taxes, Duties, Imposts, and Excises, to pay the Debts and provide for the common Defence and general Welfare of the United States."[74] However, Congress's power to tax is limited in the two direct tax clauses that appear at Article I, Section 2[75] and Article I, Section 9.[76] Article I, Section 2 states the requirement that "direct Taxes shall be apportioned among the several States . . . according to their respective Numbers . . . ."[77] Article I, Section 9 provides that "No Capitation, or other direct, Tax shall be laid, unless in Proportion to the Census or Enumeration herein before directed to be taken."[78]

69. *See e.g.*, BOORTZ & LINDER, THE TRUTH, *supra* note 45, at 176–79 (discussing the criticism that with the reduction of higher tax rates for higher-income taxpayers, it will be "the middle class" that "foot[s] the bill").

70. *See supra* note 63 and accompanying text.

71. *See supra* notes 67–68 and accompanying text.

72. U.S. CONST. art. I, § 2, cl. 3; U.S. CONST. art. I, § 9, cl. 4.

73. It is important to note that Congress's power to tax is also limited by the "uniformity" rule found at the end of Article I, Section 8, Clause 1. U.S. CONST. art. I, § 8, cl. 1; Jensen, *supra* note 15, at 2339–40. This Clause provides that "all Duties, Imposts and Excises shall be uniform throughout the United States. U.S. CONST. art. I, § 8, cl. 1. As Professor Erik Jensen describes, "The uniformity rule has been held to require only geographical uniformity: the standards that apply in one state must apply in all other states as well." Jensen, *supra* note 15, at 2340. Jensen provides the following example of the limitation imposed by the uniformity clause: "Congress may not tax a particular transaction in New York at a ten percent rate and an otherwise identical transaction in Delaware at a fifteen percent rate." *Id.* The limitations imposed on Congress' taxing authority by the uniformity rule is not discussed further because the issue is not raised in the case of *Murphy v. Internal Revenue Service*; thus, the uniformity rule is beyond the scope of the Note.

74. U.S. CONST. art. I, § 8, cl. 1.

75. U.S. CONST. art. I, § 2, cl. 3.

76. U.S. CONST. art. I, § 9, cl. 4.

77. U.S. CONST. art. I, § 2, cl. 3.

78. U.S. CONST. art. I, § 9, cl. 4.

After reviewing the precise language of both direct tax clauses, the limitation they impose is clear: if Congress wants to impose a direct tax, it must be apportioned. Professor Bruce Ackerman has described what apportionment would look like if a reform system such as the flat tax system was implemented in the United States. According to Ackerman, "The Constitution would then require Congress to vary the flat tax rate on a state-by-state basis with the aim of assuring that each one contributed a sum proportional to its population."[79] An unfortunate consequence of the apportionment rule is that in certain instances, such as Ackerman's flat tax example, the rule requires citizens of states with lower levels of per capita income to pay higher tax rates than citizens from states with much higher levels of income.[80]

IV. THE MYSTERIOUS ORIGINAL MEANING OF THE "DIRECT TAX" CLAUSES

The mystery of the direct tax clauses exists because the term "direct tax" was never defined. As Professor Jensen writes, "The debates of the founding generation are hardly crystal clear, and the substantial body of case law is often hopeless."[81] However, the lack of a clear definition has not stopped legal scholars from pouring through various notebooks[82] and dictionaries[83] of the founding era in order to arrive at their own "original" understanding of the direct tax clauses.[84] To date, there are five different originalist interpretations of the direct tax clauses, each deriving from a unique source or a unique method.[85] Reading these various interpretations, which nearly all contradict one another, is the first step toward understanding how the confused decision of *Murphy v. Internal Revenue Service* occurred.

Modern scholars use one of two approaches for describing the original understanding of the direct tax clauses, with some using both methods. The first method is to define the direct tax clauses by precisely defining the words "direct tax." The second method is to define the direct tax clauses by considering how the language of the clauses made it into the United States Constitution in the first place.

79. Ackerman, *supra* note 11, at 2.

80. *See id.* (stating that apportionment "means that citizens of a poor state such as Alabama—whose per capita levels of income and consumption are relatively low—would have to pay a higher flat tax than citizens of a rich state such as Oregon"). Professor Calvin Johnson has also written about the unfortunate consequences of the apportionment rule. According to Johnson, "Apportionment by population preys upon poor states, requiring tax rates to be highest where the tax base is thinnest. Apportionment by state can force an entire state's quota to fall upon a few taxpayers, perhaps upon a single innocent taxpayer." Johnson, *supra* note 14, at 296.

81. Jensen, *supra* note 15, at 2336.

82. *See, e.g.,* Ackerman, *supra* note 11, at 17–18 (citing to Alexander Hamilton's written notes from his role as attorney in the case of *Hylton v. United States* in order to argue that the French Physiocrat economists were "the source of the Founders' belief in the existence of a distinct category of 'direct' taxation").

83. *See, e.g.,* Johnson, *supra* note 14, at 314–19 (looking to the dictionary of 1787 to find the "original" meaning of "direct tax").

84. *See*, Ackerman, *supra* note 11, at 6–20 (discussing the French Physiocrats' definition of direct taxation under the heading "Original Understandings"); Johnson, *supra* note 14, at 299–316 (providing the 1787 dictionary definition of "direct tax" under the heading "The Original Meaning of the Apportionment Requirement").

85. *See infra* Part IVA-B.

A. Originalist Approach One: Defining the Clauses by Defining "Direct Tax"

1. "Land and Head" Definition: Looking to John Locke and the French Physiocrats

Looking to the origin of the term "direct tax," Yale Professor Bruce Ackerman argues that the idea of "distinguish[ing] rigorously between 'direct' taxation and other forms" came from John Locke and the French Physiocrats.[86] According to Ackerman, it was John Locke who "first introduced" this idea, "which was later 'systematically developed' by the French Physiocrats."[87] The French Physiocrats were an eighteenth century school of economic thought that believed the only route to wealth was through agriculture.[88] Thus, the Physiocrats stated that a tax on land, which would strike precisely at agriculture, was a direct tax.[89] Later, one of the leaders of the French Physiocrats, Baron Turgot, included a head, or capitation, tax under the term "direct tax."[90]

Although Ackerman states that it was not the "original point" of the direct tax clauses "to codify the best economic thought on the subject,"[91] he nevertheless points out that the Founding Fathers had the Physiocrats on their mind. First, Alexander Hamilton credited the Physiocrats as "the source of the Founders' belief in . . . 'direct' taxation."[92] Second, Ackerman argues that John Marshall "reflect[ed] Physiocratic ideas" when he stated to the Virginia Convention "that direct taxes were 'well understood' to include taxes on 'land, slaves, stock,' and 'a few other articles of domestic property.'"[93]

2. "Avoidance" Definition: Reading Thomas Cooley and Extrapolating from the Federalist Papers

Professor Erik M. Jensen defines "direct tax" by looking to the nineteenth century tax scholar, Thomas Cooley, and also by extrapolating from passages of The Federalist Papers written by Alexander Hamilton. Jensen states that "the heart of the historical understanding" of direct taxation can be understood by an avoidance definition: "direct taxes are imposed differently than indirect taxes, and they cannot

86. Ackerman, *supra* note 11, at 16–17. It is very important to note that Professor Ackerman does not believe that the French Physiocrats' understanding of direct tax was the "original point" of the direct tax clauses. *Id.* at 19. Instead, Ackerman states, "The original understanding of these clauses was political, not economic." *Id.* Ackerman's "political" definition of the direct tax clauses concerns the slavery compromise definition of the clauses and is discussed in section IV.B.1 of this Note.

87. *Id.* at 16–17.

88. *Id.* Professor Ackerman adds that the Physiocrats were "the only reputable economists of the time who were attempting to construct the distinction between direct and indirect taxation into a central pillar of enlightened political economy." *Id.* at 17.

89. *Id.* at 17.

90. *Id.*

91. *Id.* at 19.

92. *Id.* at 17–18.

93. *Id.* at 18.

be *avoided* as easily."[94] Jensen summarizes how this avoidance works as follows: "[A]n indirect tax is one which the ultimate consumer can generally decide whether to pay by deciding whether to acquire the taxed product."[95] Jensen argues that Thomas Cooley's writings from 1876 support his avoidance theory because Cooley understood direct taxes to be taxes on one's "property, person, business, income, etc," and indirect taxes to be those "levied on . . . commodities before they reach the consumer, and are paid by those upon whom they ultimately fall."[96] In addition, Jensen finds support by extrapolating from Alexander Hamilton's writings in The Federalist No. 21. Hamilton wrote that "all duties upon articles of consumption" can be "compared to a fluid, which will in time find its level with the means of paying for them."[97] Jensen argues that this passage shows Hamilton understood taxes on consumer goods to include an avoidability feature because such taxes will force consumers to "adjust their behavior to the cost of such products."[98]

3. "Apportioned Taxes" Definition: Reading the Dictionary of 1787

Professor Calvin Johnson defines "direct tax" as it was in the dictionary of 1787. According to Johnson, a 1787 dictionary would define "direct tax" as a synonym for "apportioned tax."[99] He further states that this definition is an outgrowth of the process of apportionment itself;[100] whenever the term "direct tax" was used, it was used to refer to "those taxes [that] were typically apportioned."[101] Thus, under the late-eighteenth-century dictionary definition of "direct taxation," Article I, Section 2 of the Constitution should circularly read, "Representative and *apportionable taxes* shall be *apportioned* among the several States."[102]

B. Originalist Approach Two: Defining the Clauses by Why They Appear in the United States Constitution

1. The Clauses Represent a Slavery Compromise

Although Professors Ackerman and Johnson define the direct tax clauses by respectively looking to the French Physiocrats and the dictionary of 1787, they both argue that the primary origin of the clauses was a slavery compromise.[103] As Ack-

94. Jensen, *supra* note 15, at 2393 (emphasis added).
95. *Id.* at 2395.
96. *Id.* at 2393.
97. *Id.* at 2395 (quoting THE FEDERALIST No. 21 (Alexander Hamilton)).
98. *Id.*
99. Johnson, *supra* note 14, at 314.
100. *Id.*
101. *Id.*
102. *See* Jensen, *supra* note 15, at 2354 (discussing, within the context of *Hylton v. United States*, the circular nature of the idea that "only those [taxes] that can be practically apportioned" are direct taxes).
103. *See* Ackerman, *supra* note 11, at 19 (referring to the slavery compromise origin of the clauses and stating that "the original understanding of [the direct tax] clauses was political" because the language was "aimed at avoiding the disastrous dissolution of the Founding dream of a 'more perfect Union'"); Johnson, *supra* note 14, at 297 (stating, "Apportionment was brought into the Constitution, in the midst of a debate about determining representation in Congress, so as to discourage the South from acquiring more slaves").

erman and Johnson describe, the direct tax clauses were created out of the debate over how to count slaves for the purpose of representation in Congress.[104] It was Pennsylvania delegate, Gouverneur Morris, who first proposed the language that would later become the direct tax clause of Article I, Section 2.[105] Because the South was determined to have its slaves count towards representation, Morris, who opposed the representation of slaves, moved to have all taxation imposed in proportion to representation.[106] The idea, of course, was that if the South wanted to have additional representation for their slaves, then they would be concomitantly.[107] Although Southerners realized the inherent fairness of this compromise,[108] some, such as George Mason and James Wilson, thought that taxation based on relative populations would raise administrability problems.[109] In response, Morris suggested that only "direct taxation" should be proportional to population.[110] Morris's correction has been described as a "miracle cure" because it benefited the North by not giving away the issue of representation for slaves without consequence, and it benefited the South by limiting the breadth of taxes that must be apportioned.[111]

2. The Clauses Prevent "Sectionally Directed Taxation"

Professor Erik Jensen counters the interpretation that slavery was the single motivating factor behind the direct tax clauses. Jensen writes, "Part—but only part—of the concern was slavery."[112] According to Jensen, an additional "reason[] for [the] existence" of the direct tax clauses, and the corresponding apportionment

104. *See* Ackerman, *supra* note 11, at 7–8 (describing how the direct tax clauses were "introduced into the constitutional text" based on the debate between the large and small states for how slaves should be counted for representation); Johnson, *supra* note 14, at 306 (stating, "The tax on slaves served to bridge the stalemate . . . over how to count slaves for purposes of representation").

105. *See* Ackerman, *supra* note 11, at 9 (stating that it was Gouverneur Morris who "took the first constructive step" toward connecting taxation to representation).

106. *Id.* at 8–9 (describing that Morris, in the beginning of July 1787, stated, "[T]he people of Penn. will never agree to a representation of Negroes," and then discussing that on Thursday, July 12, Morris "moved that 'taxation shall be in proportion to Representation'").

107. *See id.* at 9 (discussing Morris's logic as being, "If the South insisted upon extra representation for its slaves, why not require it to pay a price at tax time?").

108. *See id.* (discussing Morris's motion to make taxation proportional to representation and stating, "Even Southerners who were insisting on full representation for their blacks conceded the justice of this principle, which resonated deeply in revolutionary ideology").

109. *See* Johnson, *supra* note 14, at 307 (stating that George Mason of Virginia was opposed to apportionment because it "would drive Congress to requisitions" and that James Wilson was against apportionment because "he could not understand how apportionment could be performed unless restricted to direct taxation").

110. Ackerman, *supra* note 11, at 10.

111. *Id.* Professor Ackerman also recounts the history of the second direct tax clause that appears in Article I, Section 9. According to Ackerman, the language of "[n]o Capitation, or other direct, [t]ax . . ." was entered "at the last minute" in a "mop-up session" on September 14. *Id.* at 13. The language was added by George Read of Delaware. *Id.* At the time of the Constitutional Convention, some states, such as Delaware, had outstanding debts to the central government arising out of the old requisition system. *Id.* Ackerman argues that George Read of Delaware added in the language of "direct" tax in order to limit the ways in which the new Congress could come back after Delaware to pay its past requisition debts. *Id.* Ackerman's point in discussing this history is to show that that the direct tax clause at Article I, Section 9 was about protection of Delaware and not, as Ackerman puts it, "some grand principle of taxation." *Id.*

112. Jensen, *supra* note 19, at 372.

rule, was to prevent "sectionally directed taxation."[113] The apportionment rule prevents direct taxes from disproportionately falling on one area of the country.[114] For example, without the apportionment rule, a direct tax "on the ownership of sleighs" would fall predominantly on the North.[115] However, by adding the apportionment rule, the North cannot become a victim to this "sectionally concentrated tax" because the remaining states would also bear a proportion of the tax burden.[116] To support his claim that such sectional taxation was a part of the original understanding, Jensen writes, "Given the founders' fears of national taxing power, it's hard to imagine that the Constitution would have included no limitations on direct taxation even if slavery had not existed."[117]

V. THE SUPREME COURT'S INTRICATE JURISPRUDENCE ON DIRECT TAXATION

While constitutional scholars continue searching for the original meaning of the direct tax clauses, beginning in 1796, the Supreme Court has attempted to form its own definition of the direct tax clauses.[118] In the first 100 years of case law, the Court gave a very narrow interpretation to the direct tax clauses.[119] However, the rationale for this narrow interpretation was never clarified.[120] Some Justices expressed a view of direct taxation that was similar to Professor Johnson's 1787 dictionary approach, that direct taxes are only those that can be easily apportioned.[121] Other Justices sought to limit the application of the apportionment rule because of its connection to slavery.[122]

After decades of narrow interpretations for various reasons, the Court made an about-face and gave the clauses an extremely expansive reading in the 1895 case of *Pollock v. Farmer's Loan & Trust Co.*[123] However, beginning with the first case

113. *Id.* at 377.

114. *See* Jensen, *supra* note 15, at 2341 (stating, "The apportionment rule . . . ties a state's share of the total direct-tax liability to its share of the nation's population, measured using the currently applicable census rules").

115. *See* Jensen, *supra* note 19, at 372–73 (providing an example of "sectionally directed taxation" by using a tax imposed "on the ownership of sleighs" and writing, "Although rates may be the same throughout the country . . . only the North will bear the burden of the tax—unless the tax is direct").

116. *See id.* (describing how, due to apportionment, a direct tax on sleighs "must also fall on states with a sleigh deficit—with the liability of any state dependent on its fraction of the national population, not the concentration of sleighs in that state").

117. *Id.* at 377.

118. *See* Jensen, *supra* note 15, at 2351 (stating that *Hylton v. United States*, decided in 1796, was when "the Supreme Court first considered the meaning of 'direct taxes'").

119. *See* Germain, *supra* note 23, at 217–25 (surveying the first 100 years of case law interpreting the direct tax clauses and concluding that "[t]he early courts had thus interpreted the direct taxing clause[s] very narrowly").

120. *See id.* at 217–21 (discussing the various opinions in *Hylton v. United States* and stating that it is "difficult to glean a clear rule" from the case).

121. *See, e.g.*, Hylton v. United States, 3 U.S. (3 Dall.) 171, 174 (1796) (Chase, J.) (stating, "The Constitution evidently contemplated no taxes as direct taxes, but only such as Congress could lay in proportion to the census").

122. *See, e.g.*, *Hylton*, 3 U.S. (3 Dall.) at 177–78 (Paterson, J.) (discussing the direct tax clauses' connection to slavery and concluding, "The rule of apportionment . . . is radically wrong; it cannot be supported by any solid reasoning. . . . The rule, therefore, ought not to be extended by construction.").

123. *See* Pollock v. Farmers' Loan & Trust Co. (*Pollock II*), 158 U.S. 601, 637 (1895) (expanding the Court's interpretation of the direct tax clauses to include taxes on all income from real and personal property); Ackerman, *supra* note 11, at 28 (discussing the case of *Pollock v. Farmers' Loan & Trust Co.* under the heading

after *Pollock*, the Court never again expressed such a broad reading of the clauses.[124] Eventually, the Court called the *Pollock* decision "mistaken,"[125] but the Court never formally overruled the opinion.[126] As the case law got more confusing and the states ratified the Sixteenth Amendment (which made way for the current federal income tax), the Court became increasingly silent.[127] Eventually, the Court stopped discussing direct taxation in 1934.[128] The following section of this Note outlines a broad overview of the Supreme Court's direct tax jurisprudence.

A. The *Hylton* Century: The Supreme Court Narrowly Interprets the Direct Tax Clauses

The first major case to address the meaning of the direct tax clauses was *Hylton v. United States*, decided by the United States Supreme Court in 1796. On June 5, 1794, Congress imposed a tax on passenger carriages.[129] The carriage tax was part of Alexander Hamilton's plan to increase federal revenue by levying "luxury" taxes.[130] When Daniel Hylton was fined for failing to pay the carriage tax on his 125 carriages, he filed suit claiming that the carriage tax was unconstitutional because it was an un-apportioned "direct tax."[131] The procedural history of the case is unclear;[132] however, the Supreme Court heard the case during the February Term of 1796.[133]

The *Hylton* decision does not have an "Opinion of the Court" because the older Supreme Court cases were written seriatim, with each member of the Court expressing his opinion in turn.[134] Ultimately, the Court determined that the carriage tax was not a direct tax, and thus apportionment was not required; however, each Justice provided his own rationale for the decision. Therefore, *Hylton* stands as a case with a very clear outcome, but with an extremely unclear rationale.

"The Court Reverses Itself" and stating that *Pollock* was "one of the Court's greatest breaches with the principle of stare decisis").

124. *See* Germain, *supra* note 23, at 230–39 (discussing various post-*Pollock* cases to show how the Court immediately effected a "retreat").

125. Stanton v. Baltic Mining Co., 240 U.S. 103, 112–113 (1916).

126. *See* Germain, *supra* note 23, at 242 (stating that "*Pollock* . . . was not overruled in *Stanton*" due to the fact that the Sixteenth Amendment undercut *Pollock*'s primary rationale).

127. *See id.* at 237–38 (explaining, "The courts never fully developed the distinction between the direct and indirect taxation because Congress passed and the states adopted the Sixteenth Amendment to the United States Constitution in 1913").

128. Jensen, *supra* note 32, at 160.

129. Hylton v. United States, 3 U.S. (3 Dall.) 171, 171 (1796).

130. Ackerman, *supra* note 11, at 20. Hamilton's "luxury" taxes were strongly opposed by Jefferson and Madison. *Id.* Professor Ackerman writes that Jefferson and Madison believed that Hamilton's sin tax was just another example of "the Federalists' nationalizing pretensions." *Id.* According to Professor Erik Jensen, *Hylton* was a "test case crafted out of whole cloth" so that a Court dominated by Federalists can increase the power of the national government. Jensen, *supra* note 15, at 2351.

131. *Hylton*, 3 U.S. (3 Dall.) at 171–72.

132. Germain, *supra* note 23, at 218.

133. *Hylton*, 3 U.S. (3 Dall.) at 171.

134. Jensen, *supra* note 15, at 2352.

Only three of five Justices wrote substantive opinions in the case: Justices Samuel Chase, William Paterson, and James Iredell.[135] Taken collectively, the Justices put forth three different interpretations of the direct tax clauses. Justices Chase and Iredell expressed the first interpretation.[136] Both Justices believed that direct taxes were only those taxes easily capable of apportionment.[137] Writing first, Justice Chase stated, "The Constitution evidently contemplated no taxes as direct taxes, but only such as Congress could lay in proportion to the census."[138] Justice Iredell, writing later in the decision, wholeheartedly agreed with Justice Chase, writing that is was "evident that the Constitution contemplated [no taxes] as direct but such as could be apportioned."[139] Essentially, this narrow interpretation of clauses reads the text out of the Constitution. As Professor Jensen has stated, "[i]f apportionment is to be applied only when it makes no difference, what's the point of the Direct-Tax Clauses?"[140]

The second interpretation of the clauses, expressed in the *Hylton* decision, was that there are only two forms of direct taxation: capitation taxes and taxes on land.[141] The primary proponent of this view was Justice Chase.[142] After previously stating that direct taxes are only those capable of apportionment, Justice Chase ended his legal reasoning with some of his personal opinion, stating, "I am inclined to think, but of this I do not give a judicial opinion, that the direct taxes contemplated by the Constitution are only two, to wit, a capitation, or poll tax, . . . and a tax on [land]."[143] The bulk of this view was seconded by Justice Paterson's belief that the "principal" forms of taxation that the framers intended be apportioned were "a capitation tax and a tax on land."[144] However, Justice Paterson specifically qualified his agreement with Justice Chase by writing that capitation taxes and land taxes, in his opinion, were not "the only" forms of direct taxation.[145]

Justice Paterson alone expressed the third and final reading of the direct tax clauses. Justice Paterson stated that the apportionment rule, as contained in the direct tax clauses, should be curtailed because of the rule's relationship with slavery.[146] He wrote that the clauses were merely "a work of compromise" intended to protect the Southern states from having their land and slaves taxed arbitrarily by the other states in the Union.[147] In Justice Paterson's words, if it were not for the

135. *See* Germain, *supra* note 23, at 218 (stating that only three Justices "issued substantive separate opinions").

136. *See* Jensen, *supra* note 15, at 2352–2354 (stating that Justice Chase's and Justice Iredell's opinions are examples of "Proposition I" that can be gleaned from *Hylton*, which is that "direct taxes are only those that can be practicably apportioned").

137. *Id.*; *Hylton*, 3 U.S. (3 Dall.) at 174, 181.

138. *Hylton*, 3 U.S. (3 Dall.) at 174.

139. *Id.* at 181.

140. Jensen, *supra* note 19, at 379.

141. *Hylton*, 3 U.S. (3 Dall.) at 175.

142. *See* Germain, *supra* note 23, at 219 (discussing Justice Chase's view that there are only two kinds of direct taxes: a capitation tax and a tax on land).

143. *Hylton*, 3 U.S. (3 Dall.) at 175.

144. *Id.* at 177 (Paterson, J.).

145. *Id.*

146. *Id.* at 177–78.

147. *Id.*

apportionment rule, "[t]he Southern States . . . would have been wholly at the mercy of the other States."[148] In concluding his discussion on the tainted history of the apportionment rule, Justice Paterson stated, "The rule, therefore, ought not to be extended by construction."[149]

Despite its three-part interpretation of the direct tax clauses, *Hylton* clearly shows that a majority of the Court believed that the direct tax clauses should be read narrowly. Over the course of the next 100 years, the Court would continue to follow the *Hylton* decision and restrict its interpretation of the clauses, thereby allowing the federal government a large amount of freedom in how it chose to raise revenue.[150] The two *Hylton* interpretations that remained over the next century were: (1) direct taxes are only those that can be easily apportioned, and (2) direct taxes only come in two forms, capitation taxes and taxes on land.[151] Of the many cases that followed these two interpretations, the best examples are *Pacific Insurance Co. v. Soule* and *Springer v. United States*.

In 1868, *Pacific Insurance Co. v. Soule* affirmed the *Hylton* rationale that direct taxes are only those taxes that can be practically apportioned.[152] The plaintiff in *Pacific Insurance Co.* challenged the constitutionality of the first federal income tax.[153] In part, Pacific Insurance's lawsuit claimed that it was entitled to recover taxes on its business income because such taxes were unconstitutional direct taxes.[154] In its holding, the Court refused to find that the tax on Pacific Insurance's business income was direct because it could not be fairly apportioned.[155] Writing for the Court, Justice Swayne explained how apportionment would not be appropriate in this case:

> The [results of apportionment] are very obvious. Where such corporations are numerous and rich, it might be light; where none exist, it could not be collected; where they are few and poor, it would

148. *Id.* at 177.

149. *Id.* at 178.

150. *See* Pac. Ins. Co. v. Soule, 74 U.S. (7 Wall.) 433, 446 (1868) (applying the *Hylton* rule that direct taxes are only those that can be apportioned and holding that a tax on the income of an insurance company was not a direct tax); Veazie Bank v. Fenno, 75 U.S. (8 Wall.) 533, 546 (1869) (stating, in accordance with the narrow definition of direct tax described in *Hylton*, that the only direct taxes requiring apportionment are "capitation taxes," "taxes on land," and "perhaps taxes on personal property by general valuation and assessment of the various descriptions possessed with the several States"); Scholey v. Rew, 90 U.S. (23 Wall.) 331, 346–47 (1875) (holding that a real estate tax for succession during the Civil War was only an excise tax and not a direct tax because it was a tax on the transfer of property); Springer v. United States, 102 U.S. 586, 601–02 (1880) (citing *Hylton* and holding that the Civil War income was not a direct tax because direct taxes are only capitation taxes and taxes on land).

151. *See* Germain, *supra* note 23, at 221–25 (discussing the next 100 years of cases after *Hylton v. United States* and showing that *Hylton*'s rule that direct taxes are only those capable of apportionment continued to be used, as well as the rule that direct taxes only come in two forms: capitation and land taxes). Professor Germain also describes that the first 100 years of cases after *Hylton* showed that maybe "general lists of personal property would be subject to apportionment." However, because this conclusion is not one of *Hylton*'s three main opinions, the author has omitted this suggestion from the textual discussion.

152. Pac. Ins. Co., 74 U.S. (7 Wall.) at 446.

153. *Id.* at 436, 440–42; Germain, *supra* note 23, at 221–22.

154. *Pac. Ins. Co.*, 74 U.S. (7 Wall.) at 440–41, 443.

155. *Id.* at 446; Germain, *supra* note 23, at 222.

> fall upon them with such weight as to involve annihilation. It cannot be supposed that the framers of the Constitution intended that any tax should be apportioned, the collection of which on that principle would be attended with such results.[156]

However, *Hylton*'s "capability of apportionment" rationale was not the only view followed during the *Hylton* century. In 1880, *Springer v. United States* followed *Hylton*'s interpretation that there are only two types of direct taxes, capitation taxes and taxes on land.[157] In *Springer*, the plaintiff, William M. Springer, refused to pay a tax assessment of $4,799.80 on $50,798.00 of income because the tax was direct and must be apportioned.[158] The Court rejected Springer's claim in a single sentence of analysis.[159] After stating that "direct taxes, within the meaning of the Constitution, are only capitation taxes . . . and taxes on real estate,"[160] the Court found that the tax on Springer's income was not direct precisely because it did not fit into either of the two categories of capitation or land.[161] Ultimately, the Court ruled that the tax was an "excise or duty."[162]

B. The *Pollock* Case Stops the *Hylton* Century in its Tracks

The *Hylton* century of narrow interpretation came to an abrupt end in 1895 when the Supreme Court issued two opinions in the case of *Pollock v. Farmers' Loan & Trust Co.*[163] Professor Ackerman, a critic of the *Pollock* cases, has stated that *Pollock* "blew [the direct tax] clauses up to unprecedented proportions."[164] The *Pollock* cases arose as a challenge to Congress's enactment of an income tax in 1894.[165] The model for the 1894 income tax was the statute from *Springer v. United States*, which the Court upheld in that decision.[166] Charles Pollock was a shareholder in Farmers' Loan & Trust Company.[167] In order to prevent the company from complying with the federal income tax of 1894, Pollock sued Farmer's Loan & Trust Co., claiming, among other things, that all taxes on income from the business's "real and personal property" were direct taxes and must be apportioned.[168]

Although *Pollock* was two separate cases, the Court's decision can be collapsed into one holding. After digging deeply into the historical understanding of

156. *Pac. Ins. Co.*, 74 U.S. (7 Wall.) at 446.
157. Springer v. United States, 102 U.S. 586 (1880).
158. *Id.* at 587–89.
159. *Id.* at 602.
160. *Id.*
161. *Id.*
162. *Id.*
163. Pollock v. Farmers' Loan & Trust Co. (*Pollock I*), 157 U.S. 429 (1895); Pollock v. Farmers' Loan & Trust Co. (*Pollock II*), 158 U.S. 601 (1895). The Court issued two rulings on the *Pollock* case, *Pollock I* on April 8, 1895, *Pollock I*, 157 U.S. at 429, and *Pollock II* on May 20, 1895. *Pollock II*, 158 U.S. at 601.
164. Ackerman, *supra* note 11, at 28.
165. *Id.*; Germain, *supra* note 23, at 225.
166. Ackerman, *supra* note 11, at 28.
167. *Pollock I*, 157 U.S. at 430.
168. *Id.* at 430–33; Germain, *supra* note 23, at 225.

direct and indirect taxation,[169] the Court broadly held that a tax on all income from both real and personal property was a direct tax that required apportionment.[170] The Court's expansive decision was largely based on what Professor Ackerman has called a "tracing principle."[171] In order to hold that income from real and personal property was a direct tax, the Court had to show why a tax on income *from* property was the same as a tax *on the property* itself.[172] Chief Justice Fuller, writing for the Court, believed there was no difference, and stated as follows:

> The real question is, is there any basis upon which to rest the contention that real estate belongs to one of the two great classes of taxes, and the rent or income which is the incident of its ownership belongs to the other? We are unable to perceive any ground for the alleged distinction.[173]

Thus, as Professor Jensen has stated, under *Pollock*, "a tax on the income from property was deemed to be equivalent to a tax on the property itself."[174] In the end, *Pollock* resulted in the Court striking down the entire 1894 federal income tax as unconstitutional.[175]

C. Was *Pollock* a Mistake? The Supreme Court Quickly Sounds Retreat

The *Pollock* decision unleashed major political backlash primarily because the case greatly limited the taxing power of the federal government.[176] As a result, the Court immediately stepped back from a broad reading of the direct tax clauses.[177] The case of *Knowlton v. Moore* exemplifies how the Court performed its retreat.[178] In *Knowlton*, the issue was whether an un-apportioned inheritance tax was constitu-

169. *Pollock I*, 157 U.S. at 555–84.

170. *Pollock II*, 158 U.S. at 637.

171. Ackerman, *supra* note 11, at 29.

172. *See* Ackerman, supra note 11, at 29 (stating that in order "[t]o leap over" various "conceptual obstacle[s]" and find that income from real and personal property was a direct tax, the Court had to create a "tracing principle").

173. *Pollock I*, 157 U.S. at 581.

174. Jensen, *supra* note 15, at 2343.

175. *See Pollock II*, 158 U.S. at 637 (holding that
the tax imposed by sections 27 to 37, 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 taxation, are necessarily invalid).

176. *See, e.g.*, Ackerman, *supra* note 11, at 31 n.119 (citing ARTHUR SCHLESINGER, JR., HISTORY OF AMERICAN PRESIDENTIAL ELECTIONS 1828–29 (1971)) (describing how the Democratic Party Platform of 1896 struck out against *Pollock* and called for Congress "to use all the Constitutional power which remains after the decision, or which may come from its reversal by the court as it may hereafter be constituted, so that the burdens of taxation may be equally and impartially laid, to the end that wealth may bear its due proportion of the expense of the Government").

177. *See* Ackerman, *supra* note 11, at 31 (stating, "[A]t this stage, it is enough to say that political opposition to Pollock was so intense that the Court soon began to retreat from its aggressive course"); Germain, *supra* note 23, at 230 (writing, "[T]he negative political reaction to the . . . decision . . . led the Court quickly to retreat").

178. Knowlton v. Moore, 178 U.S. 41 (1900).

tional.[179] Considering *Pollock*'s tracing rule, it would seem that this tax, which applied to a decedent's property, would be a direct tax.[180] However, the Court upheld the tax as a "duty or excise."[181]

The Court's about-face in *Knowlton* was based on two different rationales. First, the Court moved entirely away from the tracing rule in *Pollock* to a new understanding of direct taxation based on "exchange."[182] The Court stated, "Direct taxes bear immediately upon persons, upon the possession and enjoyments of rights; indirect taxes are levied upon the happening of an event or an exchange."[183] Professor Germain points out that the Court's shift to a focus on an "event or exchange" is "very different" from the *Pollock* rationale because the *Pollock* decision focused "on whether the source of the item subject to tax was property."[184] Second, the Court refused to adopt the economic argument that the inheritance tax was direct because it could not be "shifted."[185] The Court rejected this interpretation by pointing out that the *Pollock* decision was not based on shift-ability but on the Court's belief that there is no difference between taxes on income from property and a tax on the actual property.[186]

D. From Retreat to Surrender? The Citizens and the Court (Almost) Reject *Pollock*

As the Court was continuing to move away from a broad reading of the direct tax clauses, two major events dramatically altered the legal landscape of direct taxation: the ratification of the Sixteenth Amendment and the Supreme Court's decision in *Stanton v. Baltic Mining Co.*[187] Although neither event can be appropriately called the coup de grace of *Pollock*,[188] each of these events significantly called into question the precedential weight of the case.

Initiated out of anger over the *Pollock* decision,[189] the Sixteenth Amendment made the issue of direct taxation moot, so long as Congress taxed "incomes."[190] Upset over the *Pollock* decision, Congress was determined to challenge the Su-

179. Germain, *supra* note 23, at 230.

180. *See* Ackerman, *supra* note 11, at 31–32 (discussing *Knowlton* and stating, "[A]t first glance, this levy seemed much more 'direct' than the income tax condemned by Pollock. After all, it directly hit the property itself . . . .").

181. *Knowlton*, 178 U.S. at 83.

182. *See* Germain, *supra* note 23, at 231 (describing how *Knowlton*'s theory of "exchange" was "very different from the theory underlying *Pollock*").

183. *Knowlton*, 178 U.S. at 47.

184. Germain, *supra* note 23, at 231.

185. *Knowlton*, 178 U.S. at 81–82.

186. *Id.*

187. U.S. CONST. amend. XVI; Stanton v. Baltic Mining Co., 240 U.S. 103 (1916).

188. *See* Germain, *supra* note 23, at 242 (stating, "*Pollock II* was not overruled in *Stanton*, but only because *Pollock II*'s 'mistaken' source theory had been rendered moot by the adoption of the Sixteenth Amendment").

189. *See, e.g.*, Germain, *supra* note 23, at 237 (stating that President Taft's proposal to enact the Sixteenth Amendment was a compromise proposal that counterbalanced the "strong support in Congress for enacting a new broad-based income tax with which to challenge *Pollock II* head-on").

190. *See* U.S. CONST. amend. XVI (providing that "Congress shall have power to lay and collect taxes on incomes . . . without apportionment among the several States, and without regard to any census or enumeration").

preme Court's ruling with a major piece of income tax legislation.[191] However, President Taft offered a solution: Why not avoid the necessity of another Court ruling and just amend the Constitution?[192] The outgrowth of President Taft's compromise was the Sixteenth Amendment.[193] The language of the Amendment permits Congress to tax "incomes" without apportionment.[194] Thus, after the Amendment's enactment in 1913, Congress could freely tax incomes without ever having to worry if such taxes were direct or indirect. Professor Johnson comments that the Sixteenth Amendment was a reversal of *Pollock* by "the nation as a whole,"[195] and, according to Professor Ackerman, the Amendment was *Pollock*'s final repudiation.[196]

However, the Sixteenth Amendment did not entirely remove the need for a direct taxation doctrine. Since the language of the Amendment only exempts "income" taxes from apportionment, the direct tax clauses still retain their effect for any tax base beyond income.[197] In the absence of another constitutional amendment, only Supreme Court case law can truly wipe out the rule of apportionment. It did not take the Court long to try.

Just three years after the ratification of the Sixteenth Amendment, in the case of *Stanton v. Baltic Mining Co.*, the Supreme Court issued its clearest statement rejecting the underlying rationale of *Pollock*.[198] In *Stanton*, the 1913 income tax was challenged as imposing a tax on the property of the Baltic Mining Company.[199] The plaintiff argued that since the tax fell on property and not "income," it was a direct tax and had to be apportioned.[200] The court held that the Sixteenth Amendment applied and thus the tax was constitutional.[201] However, the Court took the opportunity to attack the "tracing principle" of *Pollock*.[202] Writing for the Court, Chief Justice White stated that *Pollock* was based on a "mistaken theory" because its analysis "tested the tax not by what it was" and focused instead on "the origin or source of the income taxed."[203]

191. *See* Germain, *supra* note 23, at 237 (writing, "Beginning in 1909 there was strong support in Congress for enacting a new broad-based income tax with which to challenge *Pollock II* head-on").

192. *See id.* (stating that President Taft proposed the Sixteenth Amendment as a "compromise" that would allow Congress to tax incomes without having to challenge the *Pollock II* decision).

193. Germain, *supra* note 23, at 237.

194. U.S. CONST. amend. XVI ("The Congress shall have 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").

195. Johnson, *supra* note 14, at 298.

196. Ackerman, *supra* note 11, at 5.

197. U.S. CONST. amend. XVI.

198. Stanton v. Baltic Mining Co., 240 U.S. 103, 112–113 (1916).

199. *Id.* at 107–09.

200. *Id.* at 109.

201. *Id.* at 112–14.

202. *See id.* at 112–13 (stating that a theory that determines whether a tax is direct based on "the origin or source of the income taxed" is a "mistaken theory"); Ackerman, *supra* note 11, at 29 (discussing *Pollock*'s rationale of looking to the source of the tax as being based on a "tracing principle"); Germain, *supra* note 23, at 242 (providing that *Stanton*'s use of the phrase "mistaken theory" was a "direct assault" on *Pollock*'s underlying rationale).

203. *Stanton*, 240 U.S. at 112–113.

VI. *MURPHY V. INTERNAL REVENUE SERVICE*: UNEARTHING THE FORGOTTEN DIRECT TAX CLAUSES

Stanton's rejection of the *Pollock* rationale did not overrule the case;[204] however, it was the Court's most direct undercutting of *Pollock*'s precedential value. The Court's patent rejection of the "tracing principle" raises the question of whether *Hylton v. United States* should be revived as the better view. Unfortunately, it was 1934 when the Court last addressed the direct tax clauses.[205] Despite such confusion over the precedent and over seventy years of silence from the Supreme Court, the D.C. Circuit decided to apply a direct tax analysis in the 2007 case of *Murphy v. Internal Revenue Service*.[206]

A. Facts of the Case

The case of *Murphy v. Internal Revenue Service* began in 1994 when Marrita Murphy (then Marrita Leveille) filed a complaint with the Department of Labor alleging that her employer, the New York Air National Guard (NYANG), had, in her words, "blacklisted" her in violation of certain whistleblower protection statutes.[207] Murphy claimed that NYANG had given her unfavorable references to future employers as a form of retaliation because Murphy alerted state authorities of environmental hazards on one of NYANG's airbases.[208] The Secretary of Labor "remanded the case to an Administrative Law Judge (ALJ) 'for findings on compensatory damages'" after concluding that Murphy's employer retaliated against her.[209]

At her hearing before the ALJ, Murphy claimed that she suffered from "mental and physical injuries as a result of the NYANG's blacklisting her."[210] Murphy presented evidence that showed NYANG's discriminatory and retaliatory conduct, which caused her to experience "'somatic' and 'emotional' injuries," as well as "physical" injuries such as teeth grinding, anxiety attacks, dizziness, and shortness of breath.[211] The ALJ awarded $45,000 for emotional distress and $25,000 for reputational injuries.[212] In 1999, the Administrative Review Board of the Department of Labor upheld the ALJ's award.[213]

The event that gave rise to Murphy's case against the Internal Revenue Service (IRS) arose in 2000 when Murphy filed her income tax return.[214] In her 2000 filing, Murphy strictly obeyed Section 61 of the Internal Revenue Code (IRC) and included her $70,000 damages from her case against NYANG as part of her "gross

204. *See* Germain, *supra* note 23, at 242 (stating that "*Pollock* . . . was not overruled in *Stanton* . . . .").
205. Jensen, *supra* note 32, at 160.
206. Murphy v. Internal Revenue Service (*Murphy I*), 493 F.3d 170, 180–86 (D.C. Cir. 2007).
207. *Id.* at 171–72.
208. *Id.* at 172.
209. *Id.*
210. *Id.*
211. *Id.*
212. *Id.*
213. *Id.*
214. *Murphy I*, 493 F.3d at 172.

income."[215] However, Murphy later filed for a refund of the taxable portion of her $70,000 under Section 104(a)(2) of the IRC.[216] Section 104(a)(2) provides that "gross income does not include . . . damages . . . received . . . on account of personal physical injuries or sickness."[217] The IRS rejected Murphy's refund claim on the grounds that her damages were not "physical" damages that resulted from either "physical injuries" or "physical sickness."[218] Murphy's disagreement with the IRS led her to file suit in district court.[219]

Murphy's complaint stated that she was entitled to a refund of the $20,665, which was the amount of income tax she paid on her $70,000 award, because her damages against NYANG were for "physical personal injuries."[220] Alternatively, Murphy argued that any tax on the $70,000 award was unconstitutional because "the award was not 'income' within the meaning of the Sixteenth Amendment."[221] The district court disagreed with both of Murphy's arguments and eventually granted summary judgment for both the IRS and the government.[222] Murphy consequently appealed to the United States Court of Appeals for the District of Columbia Circuit.[223]

B. The Initial D.C. Circuit Holding

The D.C. Circuit held that Murphy was not entitled to an exemption under Section 104(a)(2) of the IRC because her damages award was for "mental pain and anguish" and "professional reputation" rather than "physical injury."[224] The court stated that the Board's award "left no room for doubt about the grounds for her award" because the Board specifically stated that the award was only "for mental pain and anguish" and "for injury to professional reputation."[225] Based on these explicit statements, the court held that Murphy's damages were not the sort of "physical" injuries that are exempt from gross income under Section 104(a)(2).[226]

However, despite its ruling on Section 104(a)(2), the D.C. Circuit held that taxation of Murphy's award was unconstitutional under the Sixteenth Amendment.[227] The court's Sixteenth Amendment analysis was laden with citations and discussion relating to Supreme Court precedent on the definition of income, legislative history on the drafting and adoption of the Sixteenth Amendment, and even the work of Nobel Prize winning economist Gary S. Becker.[228] The court con-

215. *Id.*
216. *Id.*
217. I.R.C. § 104(a)(2) (2006); *Murphy I*, 493 F.3d at 172.
218. *Murphy I*, 493 F.3d at 172.
219. *Id.*
220. *Id.*
221. *Id.*
222. *Id.* at 172–73
223. *Id.* at 173.
224. Murphy v. Internal Revenue Service (*Murphy II*), 460 F.3d 79, 84 (D.C. Cir. 2006), *vacated*, 493 F.3d 170 (D.C. Cir. 2007).
225. *Id.*
226. *Id.*
227. *Id.* at 92.
228. *Id.* at 84–92.

cluded its extensive analysis by writing, "In sum every indication is that damages received solely in compensation for a personal injury are not income within the meaning of that term in the Sixteenth Amendment."[229] The government sought en banc review of the case and argued, for the first time, the following: "[E]ven if Murphy's award is not income, there is no constitutional impediment to taxing it because a tax on the award is not a *direct tax* . . . ." The D.C. Circuit vacated its judgment and decided to rehear the case anew.[230]

C. The Second, and Final, D.C. Circuit Holding

On rehearing, the D.C. Circuit ruled against Murphy on three separate grounds. The court held that (1) Murphy's award was still not based on "personal physical injuries" under Section 104(a)(2) of the IRC, (2) Murphy's award was properly taxable as "gross income" under Section 61 of the IRC, and (3) the tax placed on Murphy's award was constitutional as an excise tax and not a direct tax.[231] The court's third holding was reached after a full analysis of whether a tax on Murphy's award was a "direct tax" under the U.S. Constitution.[232] An analysis of the court's third holding on "direct tax" will be the focus of the remainder of this Note.

D. A Critical Analysis of *Murphy's* Direct Tax Analysis

The court uses a three-step analysis to reach *Murphy*'s excise tax holding: (1) the court attempts to clearly define "direct tax," (2) the court outlines Murphy's arguments on the definition of direct tax and rejects them all, and (3) the court outlines the government's arguments on the definition of direct taxation and rejects them all.[233] Only when the court has discarded all the parties' arguments on direct taxation does it move to an entirely new analysis—an excise tax analysis.[234] The court's approach is unclear, contradictory, and entirely unhelpful.

1. The Court's Confusing Definition of Direct Tax

From the start, the court's opinion is perplexing. The court begins by laying out what is "definitely known" about direct taxes.[235] The court states, "Only three taxes are *definitely known* to be direct (1) a capitation, (2) a tax upon real property,

229. *Id.* at 92.

230. Murphy v. Internal Revenue Service (*Murphy I*), 493 F.3d 170, 173 (D.C. Cir. 2007) (emphasis added). Why did the court vacate the decision? The court supports its decision as follows: "In view of the importance of the [direct tax] issue thus belatedly raised, the panel sua sponte vacated its judgment and reheard the case." *Id.* However, it is worth noting that the court's decision came under heavy criticism. *See, e.g.*, Germain, *supra* note 23, at 187, 187 n.4 (stating that the *Murphy* decision "caused an uproar in the tax community" and citing various news articles and tax professor blogs that criticized the court's decision).

231. *Murphy I*, 493 F.3d at 186.

232. *See id* at 180–86 (analyzing the facts of the case under the heading "The Congress's Power to Tax" and applying a direct tax analysis).

233. *Id.*

234. *See id.* at 181–85 (addressing both side's direct tax arguments in turn before applying an excise tax analysis).

235. *Id.* at 181.

and (3) a tax upon personal property."[236] As support for this concise listing of the "known" direct taxes, the court cites, among other cases, *Pollock v. Farmers' Loan & Trust Co.*[237] However, in a footnote, the court completely erodes its own citation.[238] Despite the fact that *Murphy*'s text states a personal property tax is a "definitely known" direct tax, the court's footnote provides, "Whether that portion of *Pollock* remains good law is unclear."[239] Thus, in the D.C. Circuit's view of direct taxation, the "definitively known" still remains unknown.

2. Murphy's Arguments: The Court Rejects Originalism with Precedent

In the second part of its analysis, the court applies stare decisis to strike down a major originalist interpretation of the direct tax clauses. After its confusing list of the "definitely known" direct taxes, the court addresses each party's view on the meaning of direct taxation.[240] The court analyzes Murphy's position first.[241] Murphy argued that direct taxation is determined based on the "incidence of the tax"—if the tax cannot be avoided, such as a business passing a tax on to a consumer via higher priced goods, then it is a direct tax.[242] Citing to Alexander Hamilton,[243] Albert Gallatin,[244] and Professor Jensen[245] (who also argues that tax incidence was the original understanding of direct tax),[246] Murphy states that her definition "was the distinction drawn when the Constitution was ratified."[247]

The court entirely ignores Murphy's originalist perspective and brings down the hammer of stare decisis.[248] First, the court rejects Murphy's tax incidence definition because it conflicts with the court's prior cases on excise taxation.[249] The court writes that many excise taxes, such as the estate tax, cannot be shifted to someone else, but yet the court has never held any of these taxes were direct taxes.[250] Second, the court rejects Murphy's incidence argument because the prior case of *Knowlton v. United States* expressly rejected the idea that tax incidence was the core defining factor of direct taxation.[251] The court wrote that *Knowlton*, a post-*Pollock* case decided in 1900, rejected the idea that "ability to shift" was "the hallmark of a direct tax."[252]

236. *Id.* (citations omitted and emphasis added).
237. *Id.*
238. *See id.* at 181 n.** (stating, "*Pollock* . . . held that a tax upon the income of real or personal property is a direct tax. Whether that portion of *Pollock* remains good law is unclear") (citations omitted).
239. *Id.*
240. *Id.* at 181–84.
241. *Id.* at 181–82.
242. *Id.* at 181.
243. Id. at 182.
244. *Id.*
245. *Id.*
246. *See supra* notes 94–98 and accompanying text.
247. *Murphy I*, 493 F.3d at 181.
248. *See id.* at 184 (addressing Murphy's direct taxation arguments while failing to address her originalism arguments and only applying stare decisis).
249. *Id.*
250. *Id.*
251. *Id.*
252. *Id.*; Knowlton v. Moore, 178 U.S. 41, 81–82 (1900).

3. The Government's Arguments: The Court Rejects Originalism and Distorts Precedent

Finally, in the last prong of its analysis, the court discusses the government's arguments on the meaning of direct taxation.[253] One would assume that, after entirely rejecting Murphy's view of direct taxation, the court would instead adopt the government's view. However, the court again uses stare decisis to strike down another originalist interpretation of direct taxation.[254] The government argued that direct taxes were originally understood as the "only 'taxes that are capable of apportionment . . . specifically, capitation taxes and taxes on land.'"[255] The government asserts that the intent of the Constitution was to give Congress unlimited taxing power because the Continental Congress lacked the ability to raise revenue under the preexisting Articles of Confederation.[256] Therefore, according to the government, "the Framers could not have intended to give Congress plenary taxing power, on the one hand, and then so limit that power by requiring apportionment for a broad category of taxes, on the other."[257]

In order to support its originalist interpretation of the clauses, the government cites to *Hylton v. United States*.[258] *Hylton* held, in part, that direct taxes are only those that can be reasonably apportioned.[259] The government argued that this holding supports its originalist interpretation because (1) *Hylton* is directly on point with the government's interpretation, and (2) *Hylton* was rendered almost contemporaneously with the ratification of the Constitution.[260]

Just as it did to Murphy, the court rejected every argument put forward by the government, and instead moved on to an excise tax analysis.[261] The court cast aside all of the government's arguments with a confusing application of stare decisis. First, the court rejected the government's originalism argument that direct taxes are "only those capable of satisfying the constraint of apportionment" because, "[i]n the abstract, such a constraint is no constraint at all."[262] This conclusion by the court is problematic for two reasons: (1) the court uses common sense to fully reject one of the major holdings of the *Hylton* case, and (2) the court supported its conclusion by citing to *Pollock*—the very case that the court stated was questionable law a mere three pages earlier.[263]

253. *Murphy I*, 493 F.3d at 182–84.
254. *See id.* (outlining the government's originalist interpretation of direct taxation based on the work of Professor Calvin H. Johnson but analyzing the government's arguments by applying stare decisis and failing to address the originalist interpretation).
255. *Murphy I*, 493 F.3d at 182.
256. *Id.* at 182–83.
257. *Id.* at 183.
258. *Id.*
259. Hylton v. United States, 3 U.S. (3 Dall.) 171, 174 (1796).
260. *Murphy I*, 493 F.3d at 183.
261. *See id.* at 184 (failing to address the government's originalism argument and choosing instead to apply stare decisis, and then moving on to consider the tax under an excise analysis).
262. *Murphy I*, 493 F.3d at 184.
263. *See id.* (citing *Pollock* to reject the government's position).

Second, the court refused to accept the government's interpretation of direct taxation because it conflicted with the long-held view that land taxes are direct taxes.[264] The court pointed out that a land tax is "widely understood to be a direct tax."[265] In addition, the court stated that it would be difficult to apportion a tax on land throughout the United States because it would require "imposing significantly non-uniform rates."[266] Thus, the court concluded that the government's definition of "direct tax" as a tax "capable of satisfying apportionment" was erroneous because a well-known direct tax, such as a land tax, would be extremely difficult to apportion.[267]

The court's analysis here, once again, contorts Supreme Court precedent. *Hylton* directly holds that which *Murphy* rejects. Justice Chase's opinion in *Hylton*, as described above, stated the precise conclusion that *Murphy* finds so illogical.[268] Specifically, Justice Chase wrote that direct taxes are only those that can "reasonably" be apportioned.[269] However, just a few paragraphs later, he also stated, "the direct taxes contemplated by the Constitution, are only two, to wit, a capitation . . . and a *tax on LAND*."[270] Therefore, *Murphy*'s rejection of the government's position directly contradicts the opinion of Justice Chase. Moreover, *Murphy*'s support for rejecting the government's argument is a citation to the *Hylton* case itself—but it is a citation to Justice Paterson's opinion.[271] Thus, following in its continual pattern of mangling stare decisis, not only does *Murphy* reject two of the main conclusions of *Hylton*, but it cites a separate member of the *Hylton* Court to support doing so.

VII. *MURPHY* HAS TAXNAPPED AND IT MUST BE STOPPED

A. *Murphy's* Taxnapping

The *Murphy* decision is "taxnapping" in its purest form. The court's direct tax analysis meets all three of the taxnapping prerequisites. As outlined above, the three prerequisites for taxnapping are: (1) a tax case must be before the court, (2) the court's decision must have the potential to alter tax policy, and (3) the court's opinion must leave the tax law ambiguous.

First, and most obviously, *Murphy*'s application of a direct tax analysis means that *Murphy* is a tax case.[272] Second, the decision does have the potential to impact tax policy. Despite the passage of the Sixteenth Amendment, the direct tax clauses

264. *Id.* at 184.
265. *Id.*
266. *Id.*
267. *Id.*
268. *See* Hylton v. United States, 3 U.S. (3 Dall.) 171, 174 (1796) (Chase, J.) (stating, "The rule of apportionment is only to be adopted in such cases where it can reasonably apply").
269. *Hylton*, 3 U.S. (3 Dall.) at 174.
270. *Id.* at 175 (emphasis added).
271. *See* Murphy v. Internal Revenue Service (*Murphy I*), 493 F.3d 170, 184 (D.C. Cir. 2007) (citing *Hylton*, 3 U.S. (3 Dall.) at 175–81 (Paterson, J., concurring) (rejecting the government's position).
272. *See id.* at 180–84 (applying a direct tax analysis).

still restrain Congress's power to tax if such taxes are not based on "income."[273] Nearly all of the current proposals to reform the federal income tax are "consumption" taxes and not "income" taxes,[274] arguably making the Sixteenth Amendment inapplicable.[275] There are three main types of consumption taxes and each major reform proposal fits into each category. The three forms of consumption taxes are: (1) an "expenditure tax" imposed on "total consumption expenditures,"[276] which includes the flat tax, Fair Tax, and the USA tax;[277] (2) a "sales tax" imposed on "sales of goods and services;"[278] and (3) a "value-added tax" imposed on "the difference between a firm's sales and its purchases."[279] If any of these major "consumption" taxes became law, then the meaning of the direct tax clauses would become extremely important. In fact, although some disagree,[280] Professor Erik Jensen has argued that the flat tax and the USA tax are unconstitutional direct taxes because "[t]he tax liability falls directly on individuals."[281]

Finally, *Murphy*'s direct tax analysis meets the third element of taxnapping because it leaves the case law on direct taxation ambiguous. At the conclusion of *Murphy*'s bewildering direct tax analysis, it is difficult to determine if anything—or everything—remains of the case law interpreting the direct tax clauses.[282] *Murphy* rejects two of the three major opinions in *Hylton v. United States*,[283] leaving only Justice Paterson's interpretation intact.[284] In addition, *Murphy* questions whether *Pollock v. Farmers' Loan & Trust Co.* remains good law while simulta-

273. *See* U.S. CONST. amend. XVI (providing that "Congress shall have power to lay and collect taxes on incomes . . . without apportionment among the several States, and without regard to any census or enumeration"); Germain, *supra* note 23, at 240 (stating, "The Sixteenth Amendment did not, however, eliminate the apportionment requirement entirely. The apportionment requirement remains for direct taxes that are not income taxes . . . .").

274. *See* Jensen, *supra* note 15, at 2402–09 (describing the retail sales tax, value-added tax, flat tax, and USA tax as "consumption taxes"); Snyder & Gallegos, *supra* note 48, at 8–18 (describing the flat tax, USA tax, and value-added tax as all "consumption" taxes).

275. *See generally* Jensen, *supra* note 19 (discussing how the Sixteenth Amendment's "taxes on incomes" provision should be interpreted).

276. JOSEPH A. PECHMAN, FEDERAL TAX POLICY 183 (4th ed. 1983).

277. *See* Jensen, *supra* note 15, at 2403 (describing how the flat tax and USA tax are levied against expenditures because both taxes "would effectively remove savings from the tax base" and "tax only consumption"); NEAL BOORTZ & JOHN LINDER, THE FAIRTAX BOOK: SAYING GOODBYE TO THE INCOME TAX AND THE IRS 75 (2005) (stating that the FairTax would be a "single-rate personal consumption tax"). Please note that it is also possible to classify the FairTax as a hybrid consumption-sales tax because it is defined as not just "single-rate personal consumption tax," but also a "simple sales tax" on goods and services. NEAL BOORTZ & JOHN LINDER, THE FAIRTAX BOOK: SAYING GOODBYE TO THE INCOME TAX AND THE IRS 75 (2005)

278. PECHMAN, *supra* note 276, at 183.

279. *Id.*

280. *See generally* Johnson, *supra* note 14 (disagreeing with Professor Jensen's conclusion that some of the major consumption tax reforms are unconstitutional direct taxes).

281. Jensen, *supra* note 15, at 2407.

282. *See supra* notes 234–70 and accompanying text.

283. *See* Murphy v. Internal Revenue Service (*Murphy I*), 493 F.3d 170, 184 (rejecting the argument that direct taxes are "only those capable of satisfying the constraint of apportionment"); Hylton v. United States, 3 U.S. (3 Dall.) 171, 174, 181 (showing that two of the three Justices that wrote substantive opinions, Justice Chase and Justice Iredell, believed that direct taxes were only those capable of being apportioned).

284. Justice Paterson's opinion outlined two interpretations of the direct tax clauses. First, Justice Paterson wrote that direct taxes come in at least two forms, capitation taxes and land taxes. *Hylton*, 3 U.S. (3 Dall.) at 176–77. Second, Justice Paterson stated that the direct tax clauses should not be "extended by construction" because the clauses arose out of a slavery compromise. *Id.* at 178.

neously citing the case for support.[285] *Murphy* leaves a little something for everyone. Attorneys may cite to *Murphy*'s rejection of nearly every *Hylton* opinion to show that *Pollock*'s broad reading of the clauses is the better rule. However, advocates of *Hylton*'s narrow reading of the clauses can use *Murphy*'s footnote to show that *Pollock* may no longer be good law.

With all three taxnapping prerequisites met, *Murphy* makes it possible for the judiciary to decide the future of tax reform. The fact that scholars continue to debate whether a flat tax or USA tax is an unconstitutional direct tax shows that there is room for argument in future litigation.[286] The policy debate over tax reform is complex and multifaceted.[287] To decide which plan is best, it will take much more than a mere consideration of legal rules.[288] Therefore, the proper forum for choosing a tax reform plan is the legislature and not the judiciary.[289] As long as *Murphy*'s direct tax analysis remains good law, the D.C. Circuit will become the nation's top home-field advantage for tax reform protestors. All who object to tax reform based on a consumption tax model may use *Murphy*'s confusing analysis to their favor; in particular, they can suggest that the court's rejection of *Hylton* means that the expansive *Pollock* interpretation is best.[290]

B. A "Supreme" Corrective

The United States Supreme Court must repair *Murphy*'s taxnapping. Although the *Murphy* court botched its application of stare decisis, the court can be forgiven for failing to glean a clear rule from over 200 years of bewildering precedent. The Supreme Court's case law on the direct tax clauses has allowed the narrow reading of *Hylton*, the broad reading of *Pollock*, and *Stanton*'s rejection of *Pollock*'s rationale to exist simultaneously.[291] By granting certiorari in *Murphy*, the Court can finally clarify the case law and prevent taxnapping.[292] There are two ways that the Court can do this, and they can be used alternatively: (1) the Court can eliminate the effect of the clauses by adopting *Hylton* as the preferred interpretation, or (2) the Court can give effect to the clauses but set out a clear rule based on originalism.

285. *Murphy I*, 493 F.3d at 181; *see supra* notes 234–38 and accompanying text.

286. *Compare* Jensen, *supra* note 15, at 2407–08 (arguing that the flat tax and the USA tax are "direct" taxes and that they will have to be apportioned), *with* Zelenak, *supra* note 49, at 837–45, 855 (critiquing Jensen's argument that the flat tax and USA are "direct" taxes and concluding that some of Jensen's distinctions "make no sense (or are even perverse) . . . .").

287. AARON & GALE, *supra* note 40, at 8–11 (providing a four-page chart of the characteristics of each major tax reform proposal).

288. *See id.* at 6–14 (outlining and critiquing the various tax reform proposals based on criteria such as fairness to lower-income taxpayers and overall economic efficiency).

289. *See* TARR, *supra* note 2, at 299 (summarizing "well-known" judicial policymaking critic, Donald Horowitz, as asserting that courts are poor policymakers because courts decide cases based on "legal considerations rather than on the desirability of a policy or the likely consequences of alternative approaches to a problem").

290. *See supra* note 283 and accompanying text.

291. *See supra* notes 118–202 and accompanying text.

292. Petition for Writ of Certiorari, Murphy v. Internal Revenue Service (*Murphy I*), 493 F.3d 170 (D.C. Cir. 2007) (No. 07-802); Brief for the Respondents in Opposition, Murphy v. Internal Revenue Service (*Murphy I*), 493 F.3d 170 (D.C. Cir. 2007) (No. 07-802). The government just filed its "Brief for the Respondents in Opposition" in March 2008. *See* Brief for the Respondents in Opposition, Murphy v. Internal Revenue Service (*Murphy I*), 493 F.3d 170 (D.C. Cir. 2007) (No. 07-802) (stating that the brief was filed in "March 2008").

First, the Supreme Court can thwart *Murphy*'s taxnapping by choosing *Hylton*'s narrow reading as the best interpretation of the direct tax clauses. To do this, the Court should expressly adopt Justice Chase's view in *Hylton* that direct taxes are only those that can be reasonably apportioned.[293] Under this reading, the direct tax clauses would be read out of the Constitution. For example, Article I, Section 2 would read, "Representatives and reasonably apportionable taxes shall be apportioned."[294] This circular reading would end the limiting effect of the clauses, and also ensure the end of taxnapping, because it would not be possible for Congress to pass a "reasonably apportionable" tax that cannot be apportioned.[295]

Although some may object to this reading as violating the rule against surplusage,[296] the Court can support its determination with the original understanding of "direct tax" from the dictionary of 1787. Under the 1787 dictionary, direct taxes were a synonym for "apportioned taxes."[297] Therefore, although the Court may be diminishing the effect of the clauses, the validation lies in originalism.[298] It should be noted that there is another method the Court may use in order to give no effect to the clauses: the court may refuse to apply the clauses because they were rooted in slavery.[299] However, this approach is inappropriate because various parts of the Constitution arose from slavery compromises.[300] Applying the slavery reading to the direct tax clauses would set a problematic precedent for other constitutional provisions.[301]

Second, the Court can prevent *Murphy*'s taxnapping by using originalism to set a clear rule on direct taxation. A clear constitutional rule will preclude taxnapping by ensuring that courts are hearing constitutional law arguments instead of veiled

293. *See* Hylton v. United States, 3 U.S. (3 Dall.) 171, 174 (1796) (Chase, J.) (stating, "The rule of apportionment is only to be adopted in such cases where it can reasonably apply").

294. *See* Jensen, *supra* note 15, at 2354 (discussing, within the context of *Hylton v. United States*, the circular nature of the idea that "only those [taxes] that can be practically apportioned" are direct taxes).

295. A happy consequence of this approach is that the rule of apportionment would forever be prevented from operating and creating inequitable results.

296. *See* Jensen, *supra* note 19, at 366 (stating that any interpretation of the direct tax clauses should give effect to the clauses "in [their] most robust form" and "[i]f your method of interpretation leads you to conclude that a provision is nonsensical . . . the appropriate response is to reconsider the method . . . .").

297. *See* Johnson, *supra* note 14, at 314 (stating, under the heading "The 1787 Dictionary Meaning of 'Direct Tax,'" that a "well-constructed dictionary at the time of the Constitution" would define "direct tax" as "a synonym for apportioned tax").

298. The dictionary of 1787 is a particularly useful tool for applying originalism. Justice Scalia has stated, "What I look for in the Constitution is precisely what I look for in a statute: the original meaning of the text, not what the original draftsmen intended." Antonin Scalia, *Common-Law Courts in a Civil-Law System: The Role of United States Federal Courts in Interpreting the Constitution and Laws*, *in* A MATTER OF INTERPRETATION: FEDERAL COURTS AND THE LAW 3, 38 (1997). Since a dictionary is based on the common usage of various words at the time it was written, the dictionary of 1787 serves as a solid basis for the Court to ground its adoption of the *Hylton* reading of the direct tax clauses. *See* Johnson, *supra* note 14, at 314 (stating, "Dictionaries were constructed in 1787, as they are now, through a broad sampling of word usage").

299. *See* Hylton v. United States, 3 U.S. (3 Dall) 171, 177–78 (Paterson, J.) (stating that the direct tax clauses "ought not to be extended by construction" due to their connection to slavery).

300. *See* Jensen, *supra* note 19, at 376 (stating that eliminating the effect of the direct tax clauses simply because they are connected with slavery "would expose the Constitution to a seemingly endless series of challenges" because, as Jensen writes, "Where do we stop if we start unraveling the compromises that had some arguable connection with slavery?").

301. *Id.*

public policy.[302] The best originalist interpretation for the Court to adopt is Professor Jensen's avoidance definition, which provides that direct taxes are those that cannot be avoided by the taxpayer.[303] For example, a national sales tax is *indirect* because a taxpayer can refuse to purchase the good or service, and a land tax is *direct* because it is levied on the property the taxpayer currently owns.[304] By adopting this rule and giving effect to the clauses, the Court will not violate the rule against surplusage. Moreover, since the avoidance definition is based on originalism, it may eliminate the confusion over whether *Hylton* or *Pollock* is the better rule.

VIII. CONCLUSION

The D.C. Circuit's direct tax analysis in *Murphy* was a mistake.[305] The court's convoluted analysis creates problems that extend far beyond the taxation of an award for emotional damages.[306] *Murphy* may allow the judiciary to determine the direction of fundamental tax reform—an act first defined in this article as "taxnapping." As the United States contemplates various proposals to reform the federal income tax, *Murphy* stands as an open door to all those in opposition. In order to make sure the legislature determines tax policy, the meaning of direct taxation must be clarified. The United States Supreme Court has been silent on the issue for over 70 years.[307] The inappropriate and undemocratic effects of taxnapping must spur the Court into action. By granting certiorari in *Murphy*, and finally clarifying the meaning of direct taxation, the Court can make certain that tax policy remains in the hands of the legislature.

302. Taxnapping is prevented by a clear rule because the third prerequisite for taxnapping cannot be met. For there to be a risk that tax policy protestors will run to the courts, the law must be susceptible to arguments that favor both sides of the debate. An unambiguous rule makes this extremely difficult.

303. *See supra* notes 94–98 and accompanying text.

304. *Id.*

305. *See supra* notes 232–270 and accompanying text.

306. *See supra* notes 271–89 and accompanying text.

307. Jensen, *supra* note 32, at 160.