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SOME CONSTITUTIONAL ASPECTS OF THE EXCESS PROFITS TAX

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SO FAR AS REVENUE YIELD WAS CONCERNED, A SUFFICIENTLY HIGH FLAT TAX UPON BUSINESS OR CORPORATE INCOMES WOULD HAVE BEEN AS EFFECTIVE AS THE NEW TAX, AND WOULD HAVE BEEN EASIER TO COMPUTE AND TO ADMINISTER. A HIGH FLAT TAX WOULD, HOWEVER, HAVE BORNE WITH UNDUE HARDSHIP ON THE ENTERPRISE HAVING AN INCOME WHICH WAS BUT A LOW RETURN UPON THE INVESTMENT. AND IT WOULD NOT HAVE REACHED THE LIMIT OF WHAT WAS CONCEIVED TO BE THE TAX-PAYING ABILITY OF THE ENTERPRISE ENJOYING, PERHAPS THROUGH WAR CONDITIONS, A VERY HIGH RETURN UPON ITS INVESTMENT. THE EXCESS PROFITS TAX WAS, THEREFORE, FRAMED SO AS TO EXEMPT A MODERATE RETURN UPON CAPITAL, AND TO INCREASE ACCORDING TO THE RICHNESS OF THE RETURN UPON THE CAPITAL.

THE AMOUNT OF NET INCOME IS, OF COURSE, THE TRUE INCREASE IN ASSETS FROM EARNINGS OR PROFITS DURING A CERTAIN PERIOD OF TIME. THE RICHNESS OF AN INCOME PRODUCED BY THE AID OF CAPITAL IS MEASURED BY THE RELATION OF THE INCOME TO THE CAPITAL. CAPITAL IS NO FIXED AND CERTAIN THING: ESPECIALLY IN THE CASE OF CORPORATIONS, SEVERAL DIFFERENT BASES OF RECKONING MIGHT HAVE BEEN CHosen. ONE BASIS IS THE STOCK, OR STOCK, BONDS AND OTHER SECURITIES ISSUED; ANOTHER IS THE VALUE OF THE PROPERTY CURRENTLY EMPLOYED IN THE BUSINESS. A THIRD ARTIFICIAL BASIS SOMETIMES SUGGESTED IS AN ESTIMATED NORMAL RATIO OF INVESTMENT TO GROSS INCOME IN A PARTICULAR INDUSTRY. THE BASIS ACTUALLY SELECTED FOR

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the 1917 act, and adhered to, after consideration, in the Act of 1918 (more particularly discussed in this article), is that of the cash or equivalent of cash put into the business for stock or left in the business through the accumulation of income. This statutory "invested capital" is subject to certain qualifications, such as that where good will and trade-marks and the like (and under the 1918 act, patents) were paid in for stock, the value so contributed may not be allowed beyond a sum exceeding a certain percentage of the par value of the stock, and the qualification that the earnings of the current taxable year cannot be included. Capital secured by borrowing may not be included but the interest upon the obligations is deductible as an expense in determining the net income.

The cash-paid-in-basis for reckoning capital was by no means the most generous basis which might have been chosen. It is probable, however, that had Congress adopted a more liberal basis it would have counteracted the beneficial effect by making the rates of tax higher, for the tax was worked out so as to yield a definitely estimated amount of revenue.\(^4\) The distinctive feature of the excess profits tax is not so much its amount, but the novel distribution of the tax between different taxpayers. The method adopted in the statute operates to produce for enterprises similarly circumstanced in every respect, except that of cash or cash value paid or left in against stock, tax burdens which are materially different. Thus, if corporation A and corporation B are both engaged in the same line of business, each employing property of the same value and producing the same net return, the tax of A may be higher than that of B if: (a) a substantial part of the capital of A was procured through the issue of bonds while all the capital of B was procured through stock; or (b) A acquired its property some time before B, when the cost of such property was materially less than the cost prevailing when B made its acquisition; or (c) A manages to carry on its business on materially less capital than B, which may have capital invested in some property not returning much income. These instances may be multiplied.

By the so-called relief sections a special method of assessment is provided for particularly difficult cases. These cases are those in which there is lack of adequate data for determining invested capital, or in which upon application the commissioner of internal revenue finds that owing to abnormal conditions affecting the capital or income the tax if assessed under the primary provisions of the act, would be grossly disproportionate to that upon "representative" corporations engaged in like business. In such cases the tax is to be an amount

\(^4\)Report of Senate Committee on Finance No. 617 (December, 1919) 1-4—showing that the 1918 Revenue Act as reported was framed as closely as possible to yield $6,000,000,000, and that of this amount the war excess profits tax was expected to yield $2,400,000,000 and the income tax $2,207,000,000.
which bears the same ratio to the net income of the taxpayer as that of representative corporations bears to their net income. The relief section of the 1917 act was less full in its terms than that of the 1918 act but was found to warrant substantially the same relief as that provided for in the later act.

Outstanding legal questions as to this new use of invested capital as a tax factor are: (1) whether a method of assessment involving unlike taxes upon taxpayers similarly circumstanced, except as to statutory invested capital; and (2) whether a method of relief for hard cases resting upon no certain rule and involving the exercise of discretion by administrative officers, are constitutional. Other questions as to the acts might be discussed, but these are perhaps the principal ones. The decided cases appear to disclose little probability that the statute will be upset on either ground. The remedy for the inequalities of the law is legislative, rather than judicial.

The only provision which might operate to limit the power of Congress in prescribing a method of apportionment like that involved is the Fifth Amendment to the Constitution. Although there is as yet no decision to that effect, the “due process” requirement there imposed must be held applicable to the taxing power, and would render invalid a basis of tax operating to produce purely arbitrary discrimination in the amounts assessed upon different taxpayers.

The power of Congress to levy taxes, without action by the states, is “the one great power upon which the whole national fabric is based” and it has been jealously guarded by the courts. Important aspects of it are set forth in the often quoted statement of Chief Justice Chase:

*Another such question is whether the special war excess profits tax could be made, as it was by the Revenue Act of 1918, to apply solely to corporations. The decisions appear to indicate that this separate classification of corporations is proper. See elaborate note in 60 L. R. A. 33-60; also Flint v. Stone Tracy Co. (1911) 220 U. S. 107, 31 Sup. Ct. 342; Coitler v. Louisville & N. R. R. (1905) 196 U. S. 599, 25 Sup. Ct. 342; Western Union Tel. Co. v. Indiana (1897) 165 U. S. 304, 17 Sup. Ct. 345. A further question is whether the act of 1918 is objectionable in that it was not passed until after the close of the year on the basis of which the tax was assessed. The decisions indicate that no constitutional limitation is violated by using as the standard of the tax, income for a period elapsed at the time of the passage of the act. Brushaber v. Union Pacific Ry. (1916) 240 U. S. 1, 36 Sup. Ct. 235; Stockdale v. Insurance Co. (1873, U. S.) 20 Wall. 323, 331: “The right of Congress to have imposed this tax by a new statute, although the measure of it was governed by the income of the past year, cannot be doubted; much less can it be doubted that it could impose such a tax on the income of the current year, though part of that year had elapsed when the statute was passed.” As to the treatment of personal service “corporations,” cf. Collector v. Hubbard (1870, U. S.) 12 Wall. 1.

*“No person shall . . . . be deprived of life, liberty or property, without due process of law; nor shall private property be taken for public use without just compensation.” U. S. Constitution, Art. V.
"It is true that the power of Congress to tax is a very extensive power. It is given in the Constitution, with only one exception and only two qualifications. Congress cannot tax exports, and it must impose direct taxes by the rule of apportionment, and indirect taxes by the rule of uniformity. Thus limited, and thus only, it reaches every subject, and may be exercised at discretion."

Congress may select at discretion the subjects of taxation: It may tax the privilege of manufacturing in some lines and not in others; it may tax the use of foreign-built yachts and not that of domestic yachts; it may, through stamps or otherwise, tax some commercial transactions and not others. It exercises a concurrent power to tax with that of the states, and may tax the exercise of rights and privileges created by the states. There is no limit as to the amount of tax which may be imposed—the tax may indeed be destructive. Congress has very wide discretion as to the manner of tax: it may tax a privilege according to the special capacity of the taxpayer to exercise it, rather than according to the extent of its actual exercise by him.

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7 License Tax Cases (1866, U. S.) 5 Wall. 462, 471. "The Congress shall have Power To 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; but all Duties, Imposts and Excises shall be uniform throughout the United States." U. S. Constitution, Art. 1, sec. 8.


12 McCray v. United States (1904) 195 U. S. 27, 24 Sup. Ct. 767—Oleomargarine act imposing a tax of one-fourth of one per cent. on oleomargarine not artificially colored any shade of yellow, and a tax of ten cents a pound on oleomargarine so colored, sustained; the court holding that it is not its province to go into the motives or purposes of Congress in passing the act. "As quite recently pointed out by this court in Knowlton v. Moore, 178 U. S. 41, 60, the oft-enquoted statement of Chief Justice Marshall in McCulloch v. Maryland, that the power to tax is the power to destroy, affords no support whatever to the proposition that where there is a lawful power to impose a tax its imposition may be treated as without the power because of the destructive effect of the exertion of the authority." Ibid., 56. Veazie Bank v. Fenno (1869, U. S.) 5 Wall. 533: prohibitive tax on state bank notes sustained. Pacific Insurance Company v. Soule (1868, U. S.) 7 Wall. 433.

13 United States v. Singer (1872, U. S.) 15 Wall. 111, sustaining liquor manufacturing tax based on manufacturing capacity of the distillery; Anderson v. The Forty-Two Broadway Co. (1915) 239 U. S. 60, 36 Sup. Ct. 17, sustaining provision of 1909 Corporation Excise Tax law limiting amount of interest which could be deducted in computing income subject to tax; Stanton
ing inheritances it may provide that the rate of tax shall increase with the amount of the inheritance; and in taxing incomes it may also prescribe progressive rates.

A few taxes sought to be imposed have been held to be invalid because in violation of the express limitations of the Constitution. Thus burdens upon exports, although light and fairly remote, have not been sanctioned, although no objection was found to the application of a general income tax to income from exportation. No tax has been invalidated because of lack of uniformity, as that requirement as to indirect taxes has been held to mean only that the tax must operate with geographical uniformity throughout the United States, and not with “intrinsic uniformity” with reference to the incidence of the tax upon different taxpayers. The only tax invalidated as being a direct tax, not apportioned between the states according to population, was, until March 8, 1920, the 1894 income tax, in the Pollock case. The holding in this case that a tax upon the income from real estate was in the nature of a direct tax, was met by the Sixteenth Amendment, authorizing Congress “to tax incomes from whatever source derived, without apportionment.” This Amendment, as the Supreme Court has shown, is not the source of the power of Congress to tax incomes. It merely removes a disability in taxing a certain kind of income. One implied exception to the power to


\footnote{**Knowlton v. Moore**, supra.}

\footnote{**Brushaber v. Union Pacific Ry.**, supra.}


\footnote{**Peck & Co. v. Lowe** (1918) 247 U. S. 165, 38 Sup. Ct. 432.}

\footnote{**Knowlton v. Moore**, supra. The provision in sec. 8 of Art. 1 of the Constitution that “all Duties, Imposts and Excises shall be uniform throughout the United States” was urged in objection to the graduated inheritance tax, but it was held that the uniformity required was merely a geographical uniformity. \textit{Flint v. Stone Tracy Co.}, supra.}

\footnote{**Pollock v. Farmers’ Loan & Trust Co.** (1895) 157 U. S. 429, 15 Sup. Ct. 673; (1895) 158 U. S. 601, 15 Sup. Ct. 706.}

\footnote{“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.” U. S. Constitution, Art. XVI.}

\footnote{**Peck & Co. v. Lowe** (1918) 247 U. S. 165, 172, 38 Sup. Ct. 432, (1918) 27 \textit{Yale Law Journal}, 1096. “The Sixteenth Amendment, although referred to in argument, has no real bearing and may be put out of view. As pointed out in recent decisions, it does not extend the taxing power to new or excepted subjects, but merely removes all occasion, which otherwise might exist, for
tax has also become established. Fearing the ultimate destructive consequences of the power to tax, the Court has held that Congress may not tax the instrumentalities of the states, as it was the intent of the Constitution to preserve the states. 22

So vigorous has been the Court in its support of federal taxing power that all the attacks upon taxing statutes under the Fifth Amendment, upon the ground of their unequal operation, have so far failed, 23 and the Court has sometimes declared that the taxing power is not limited by the due process provision. Such is the implication of the dictum of Chief Justice Chase. And in the McCray case in which the Court strongly sustained the tax obviously designed through discriminating burdens to stamp out the sale of artificially colored oleomargarine, the Court said:

"Whilst undoubtedly both the Fifth and Tenth Amendments qualify, in so far as they are applicable, all the provisions of the Constitution, nothing in those amendments operates to take away the grant of power to tax conferred by the Constitution upon Congress. 24

" . . . no instance is afforded from the foundation of the government where an act, which was within a power conferred, was declared to be repugnant to the Constitution, because it appeared to the judicial mind that the particular exertion of constitutional power was either unwise or unjust. 25

In the foreign-built yacht tax case, the Court strikingly declared:

" . . . the authority to tax which is given in express terms is not limited or restricted by the subsequent provisions of the Constitution or of the amendments thereto, especially the due process clause . . . (To hold otherwise) would result in rendering the Constitution unconstitutional." 26

an apportionment among the States of taxes laid on income, whether it be derived from one source or another. Brushaber v. Union Pacific R. R. Co. 240 U. S. 1, 17-19; Stanton v. Baltic Mining Co. 240 U. S. 103, 112-113." In Eisner v. Macomber (March 8, 1920) U. S. Sup. Ct. Oct. Term, 1919, No. 318, a divided Court held that the provision of the 1916 act treating stock dividends as income was invalid on the ground that they are capital and could be taxed to the recipient only by a direct tax according to population. This relates to the definition of income—not to the basis of apportioning a tax upon income.


23 In Flint v. Stone Tracy Co., supra, the tax cases up to date of the decision are collected in notes at the foot of pages 159 and 160. Cases since the Stone Tracy decision, sustaining federal taxing acts against the claims of want of due process are: Brushaber v. Union Pacific Co., supra; Stanton v. Baltic Mining Co., supra; Dodge v. Osborne (1916) 240 U. S. 118, 36 Sup. Ct. 275; Lynch v. Hornby, supra.

24 McCray v. United States, supra, 61. 25 Ibid., 54.

It has commonly been urged by counsel as to any new and unusual tax, particularly when it could be shown that it did not operate uniformly as to all taxpayers, that it was void under the amendment as resulting in deprivation of property without due process. Yet as lately as in the Brushaber decision, sustaining the 1913 income tax, Chief Justice White said:

"So far as the due process clause of the Fifth Amendment is relied upon, it suffices to say that there is no basis for such reliance since it is equally well settled that such clause is not a limitation upon the taxing power conferred upon Congress by the Constitution; in other words, that the Constitution does not conflict with itself by conferring upon the one hand a taxing power and taking the same power away on the other by the limitations of the due process clause."

It can hardly be doubted, however, that upon this point the pronouncement of the Court is more drastic than will be its ultimate decision. Even in the McCray case, the Court was not satisfied to rely upon the bald proposition as to the non-application of the amendment to the taxing power, but proceeded to maintain that the classification made under the oleomargarine statute was not a palpably unreasonable one. In the Billings case also, there was a defence by the Court of the classification made by Congress, and in the Brushaber case, following the passage above quoted, we have a qualification characteristic of the Chief Justice:

"This doctrine would have no application in a case where although there was a seeming exercise of the taxing power, the act complained of was so arbitrary as to constrain to the conclusion that it was not the exertion of taxation but a confiscation of property."

Without doubt the Chief Justice would in such terms denounce a statute which purported, in the language of the classic moot case, to tax red haired men at one rate and black haired men at a lower rate. Other judges might be less ready to rest a decision upon the ground that what was denominated by Congress as a taxing act, was not such in fact. They would be likely to base their rejection of the use of the hair test in taxation upon the simple propositions that it lacked that modicum of justice required under any conception of due process.

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27 See cases referred to in note 23, supra.
28 Brushaber v. Union Pacific Ry., supra, 24.
29 McCray v. United States, supra, 63. "Moreover, concede for the sake of argument only, that even although a particular exertion of power by Congress was not restrained by any express limitation of the Constitution, if by the perverted exercise of such power so great an abuse was manifested as to destroy fundamental rights which no free government could consistently violate, that it would be the duty of the judiciary to hold such acts to be void upon the assumption that the Constitution by necessary implication forbade them" and argument pp. 63-64. Italics are those of the present writer.
30 Brushaber v. Union Pacific Ry., supra.
31 In the leading case of Loan Association v. Topeka (1873, U. S.) 20 Wall. 655, 650. the court in holding that a statute purporting to authorize taxation
The proposition that to hold that the amendment limits the taxing power would be "to render the constitution unconstitutional" is the opposite of the truth. The amendment, if it has any application at all, can apply only to powers. An act beyond the power of the acting government agency is no act at all; regardless of the due process clause or any other limitation, it would fail because of the want of power. The Court has unhesitatingly decided that the due process limitation applies to other powers of the government, for example, the power to regulate interstate commerce and the power to regulate the post. The power to tax, vital as it is, stands upon no higher basis; it must be subject to the same general restraint against the exercise of governmental power in a manner purely arbitrary. The due process limitation conflicts with the grant of power to tax only in the same sense that the brakes upon a locomotive conflict with the driving wheels.

It by no means follows that the Court's judgment as to what is arbitrary and discriminatory may be substituted for the judgment of Congress. This is shown by the very wide discretion which the Court has already recognized in Congress as to the form of taxing statutes. In the Pollock case, so able a judge as Mr. Justice Field believed that the comparatively slight graduations of the income tax then before the Court, and the exemptions granted from it made the tax so arbitrarily unequal as to render the tax invalid. In the more recent
cases, the exemptions from the tax and the far more marked gradua-
tion of the rates did not win the adverse vote of a single judge.44
The latitude accorded to the legislative body is even more strongly
shown by the decisions of the courts with reference to the state taxing
acts sought to be invalidated under the equal protection or due process
clauses of the Fourteenth Amendment—provisions closely similar in
their scope to the federal restrictions of the Fifth Amendment. In
sustaining a state statute, under which bonds were taxed at their face
value instead of at their actual value, the Court declared that “clear
and hostile discriminations against particular persons and classes,
especially such as are of an unusual character, unknown to the practice
of our governments,” might be obnoxious under the Fourteenth
Amendment, but with reference to the wide discretion of the legislature
in the exercise of the state taxing power, said:

“It may impose different specific taxes upon different trades and pro-
fessions, and may vary the rates of excise upon various products; it
may tax real estate and personal property in a different manner; it
may tax visible property only, and not tax securities for payment of
money; it may allow deductions for indebtedness, or not allow them.”55

In the leading case sustaining a classification of a graduated state
inheritance tax law, the Court said as to the rule of equality:

“The rule prescribes no rigid equality and permits to the discretion
and wisdom of the State a wide latitude.”56

In this case, Mr. Justice Brewer in dissenting, maintained that the
classification of inheritances was purely arbitrary because based upon
wealth and was intentionally made unequal. This dissent left no
imprint upon the subsequent course of decisions.57

In the latest case upon this point, the Court declared:

“In making classification, which has been uniformly held to be
within the power of the state, inequalities necessarily arise for some
classes are reached, and others omitted, but this has never been held
to render such statutes unconstitutional. . . . In order to invalidate

and fundamental nature and character of a tax is that of a contribution to
the support of the government, levied upon the principle of equal and uniform
apportionment among the persons taxed, and any other exaction does not
come within the legal definition of a tax” (p. 599).

44 See note 15, supra; Flint v. Stone Tracy Co., supra.
45 Bell’s Gap Railroad Co. v. Pennsylvania (1890) 134 U. S. 232, 237, 10
Sup. Ct. 533.
46 Magoun v. Illinois Trust and Savings Bank (1898) 170 U. S. 283, 293, 18
Sup. Ct. 594.
47 Campbell v. California (1906) 200 U. S. 87, 26 Sup. Ct. 182; Beers v. Glynn
this tax it must be held that the difference in the manner of assessing the transmission of property by testators or intestates, as between resident and non-resident decedents, is so wholly arbitrary and unreasonable as to be beyond the legitimate authority of the state."

In the decisions as to state statutes, we have, however, at least two instances in which the manner chosen for the levy of tax was so arbitrary as to be held invalid. In the latest of these decisions, invalidating a palpably unreasonable manner of assessing on the abutters the cost of paving, Mr. Justice Holmes said:

"The differences were not based upon any consideration of difference in the benefits conferred but were established mechanically in obedience to the criteria that the charter directed to be applied. The defendants' case is not an incidental result of a rule that as a whole and on the average may be expected to work well, but as an ordinance that is a farrago of irrational irregularities throughout."

Notwithstanding the recognized latitude which Congress enjoys in choosing methods of tax, the Court will undoubtedly hold that Congress like a state legislature, may not take property under a "farrago of irrational irregularities."

There are those who would unhesitatingly characterize the invested capital provisions as any sort of a "farrago." This charge might be entitled to weight in Congress but is not likely to be sustained to the satisfaction of the judicial mind.

Congress sought through the invested capital concept to set a standard by which a moderate return could be protected from excessive levy, and the rate increased accordingly to the ability of the taxpayer to respond. The problem here involved was practical rather than legal. "Taxation is eminently practical," as the Court has remarked, and the validity of a tax law is not to be decided "with reference to those theoretical and abstract ideas whose correctness is the subject of dispute and contradiction among those who are experts in the science of political economy." As to a method of taxation, like any "classification," the question is whether there is any reasonable ground for it or whether it is simply arbitrary. The decided cases show that the presumption that each act of Congress is valid, is applied with special readiness to revenue acts and that the Court, even without the persua-

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8 Maxwell v. Bugbee (1919) 40 Sup. Ct. 2. Upon the specific point decided in this case—that the amount of inheritance tax upon property of a non-resident decedent within the state may be compared by first determining what the tax would be if the entire estate were within the State and then taking such portion of this amount as the property within the State bears to the total estate—four of the Justices dissenting. See (1920) 29 YALE LAW JOURNAL, 464.


sive effect of the imperative need for war revenue, would not be likely to declare invalid a taxing act framed with anything like reasonable regard to its just incidence.

In seeking to overthrow under the Fifth Amendment a basis adopted by Congress for that purpose, it is by no means sufficient to show that under it some taxpayers pay not only more but at a higher rate than others. That broad objection is disposed of by the cases sustaining the graduated inheritance taxes and more directly by the decisions sustaining the graduated income tax. What must be shown is that the basis for applying the higher rate to one taxpayer rather than another is entirely without logical foundation.

That the amount of capital paid into an enterprise for stock, together with the earnings or profits voluntarily left in by the stockholders, has some bearing upon the question of what return is to be exempted from special tax and how progressive rates may be applied, cannot be denied. We are not dealing here with any question of a taking of property either directly or through the unreasonable reduction of the return upon it. When that question is involved, as in the eminent domain or rate cases, the capital basis to be adopted is the fair value of the property at the time of the taking, and in determining that question many elements aside from the cost of the investment must be taken into account. But no property and no rate of return is protected from the levy of tax; taking cases have no bearing upon the validity of a tax law. Nor are we considering a question of determining capital for the purpose of ascertaining income. In computing the profit from the sale of property, a taxpayer is entitled to deduct the fair value of his property, at least at the date when the taxing law became operative. The question here, however, is not one of income determination but the very different question of a basis for distributing tax against income. The cash which the stockholders paid or left in to be employed in the business furnishes at least one basis for measuring the richness of the income from the business and the idea of making the rate of tax increase according to the richness of the income is the plan of the progressive rates for individual incomes which the court has already approved. Unlike individual incomes, corporate incomes cannot be justly rated merely according to their amount, but only according to their relation to some measure of capital.

Even though the cash paid in is a relevant factor in rating corporate incomes, its use for this purpose might be regarded as arbitrary if there is available some other basis which is equally practicable and manifestly more just. No such other basis has as yet been worked out.

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*a* See note 15, supra.


Few would venture to claim this merit for the simple basis of the par value of stock or other securities issued. Stock all too frequently represents aspirations rather than assets. It has been widely urged that property secured through borrowing, particularly long term borrowing, should have been included in invested capital. It is difficult, however, to say that Congress had to ignore the possibility which would thus have been opened up of artificially increasing capital, and that there is no reasonable ground for distinguishing between funds furnished by stockholders and those furnished by debt holders, particularly when the interest on the debt is made deductible as an expense. If the value of the property employed in the business had been made the measure, appraisals and interminable investigation would have been needed in the case of every assessment as the rate cases have abundantly shown. Great administrative difficulty would also have been involved by a provision that invested capital should in all cases be some fixed percentage of gross to net income, the percentage to be determined for each particular industry. If it be urged that Congress should not have adopted any one definite basis for determining invested capital, but should have provided that all possible bases should have been taken into account, the Court would doubtless take the view that in order to make the statute workable, it was necessary to prescribe some single and fairly definite standard.

If the basis adopted has relation to the issue, if it is not one which must be rejected by most fair minds in favor of some other practicable basis, the fact that the basis does result in discrimination as between taxpayers is not sufficient for its invalidation. Such injustice as it causes is likely to be regarded as incidental rather than as fundamental. By as early an authority as Plato, it was remarked,

"When there is an income-tax, the just man will pay more and the unjust less on the same amount of income."44

It has always been recognized that equality in the distribution of tax burdens could not be obtained. In considering the graduated inheritance tax, the Court said:

"The rule of equality permits many practical inequalities. . . . In a classification for governmental purposes there cannot be an exact exclusion or inclusion of persons and things."45

In sustaining the corporation excise tax of 1909, Chief Justice Fuller remarked:

"The tax must be measured by some standard, and none can be chosen which will operate with absolute justice and equality upon all corporations."46

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44 Plato's Republic (Jowetts' 3d ed. 1888) 21.
Of the state taxing power, the Court recently said:

"Absolute equality is impracticable in taxation and is not required by the equal protection clause and inequalities that result not from hostile discrimination, but occasionally and incidentally in the application of a system that is not arbitrary in its classification, are not sufficient to defeat the tax."47

War tax burdens are heavy, and the inequalities inherent in all plans of taxation are bound to be accentuated in war tax measures. In fields other than taxation the Court has been inclined to recognize the power of the legislature to meet new social conditions by measures which lessen the sphere of individual liberty as conceived in an earlier day.48 In a similar way the latitude permitted to Congress in taxation is likely to be extended under the pressure of new conditions at the further expense of equality in the treatment of individual taxpayers. The Bench which sustained the Selective Draft Law is not likely to have very serious difficulty with the discrimination involved in the revenue measures which backed up the draft.

Under the relief sections, the taxpayer entitled to relief because of some abnormal condition, is to have his tax determined not according to his invested capital, but so as to "bear the same ratio to the net income of the taxpayer as the average tax of representative corporations bear to their net income." The constitutional objection to this remedial provision would be not that the statute is too rigid, but that it is too flexible; that as to cases falling within the relief clause, Congress has not legislated, but has delegated its power to administrative officers. Against any delegation might be urged the declaration of Hamilton, quoted by Mr. Justice Field in his dissent in the Pollock case:

"The genius of liberty reprobates every thing arbitrary or discretionary in taxation. It exacts that every man, by a definite and general rule, should know what proportion of his property the State demands."49

47 Maxwell v. Bugbee, supra.
49 (1895) 157 U. S. 439, 596, 16 Sup. Ct. 673. See also opinion per Matthews, J., in Yick Wo v. Hopkins (1886) 118 U. S. 356, 369, 6 Sup. Ct. 1064. "When we consider the nature and theory of our institutions of government, the principles upon which they are supposed to rest, and review the history of their development, we are constrained to conclude that they do not mean to leave room for the play and action of purely personal and arbitrary power."
There is in the statute a difficult but reasonably clear rule for all but abnormal cases, but a taxpayer believing himself entitled to relief because of exceptionally harsh operation of the primary provisions of the act cannot by any specific provision in the statute determine whether he is so entitled or what relief would be. The leaving of these questions to be determined without a mathematical formula and in the first instance by the commissioner of internal revenue, does not appear however to involve any unconstitutional delegation of the power of Congress.

The power to tax is conferred by the Constitution upon Congress, and no other agency. In any polity of English origin, this power belongs historically to the Legislature. The contest between Parliament and the Crown over the power of taxation ended in defeat for the executive. It was not likely that the men of the colonies, who rested their right of revolution so largely upon the wrong of taxation without representation, would vest the taxing power elsewhere than in the most numerous and direct representatives of the people. Yet the power with reference to taxation which was conferred upon Congress was legislative power. Congress is not called upon to exercise any function with reference to it which is not a legislative function.

Even in England where there was no doctrine as to the necessary separation of powers, the power exercised over taxation exercised by Parliament was general rather than specific. Any idea that a tax had to be so levied that the individual could determine the amount which he was called upon to pay by a simple mathematical process is possibly a result of a misunderstanding of Coke's Second Institute.

"The values of merchandise for which the subsidy of poundage is paid do appear in a book of rates in print, whereby the merchant knows what he has to pay." Coke's Second Institute, *76.

This simply means that there was a published rate of ad valorem taxes. Parliament preserved the right to say what percentage of property should be taken for revenue, but the value at which property should be assessed, and the settlement of disputes arising from claims that the rate levied was excessive for the property, were always executive and judicial functions.

Unlike some of the state constitutions, the federal Constitution contains no prohibition of the delegation of power from one branch to another. It is clear, of course, that for want of authority no such delegation would be sustained, notwithstanding the absence of a pro-

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47 Coke's Second Institute, *76.
48 Magna Charta, ch. 38; Case of Ship-Money (1637) 3 How. St. Tr. 825; 1 Thayer, Cases on Constitutional Law (1893) 17.
But so long as it can be said that all that is left by Congress to administrative officers is the determination of how a taxing provision applies to a particular state of facts, no delegation is involved.

The distinction between delegation of power and mere provision for practical administration is well shown by the cases as to state taxing acts. A state legislature may not delegate the power to tax except to elected representatives of the people, granted by it jurisdiction in a certain subdivision of the state. The legislature may, however, give to administrative officers tax functions involving the exercise of much discretion. The making of the customary valuations of real or personal property of course involves discretion, but such authority has been exercised by administrative officers from the beginning. A statute giving a board of equalization the power to determine the fair cash value of the capital stock of a railway, over and upon its tangible property, does not involve any delegation even though there is involved the establishment by the board of rules and principles for determining intangible values. Assessors may determine what lands are "specialy benefited" by an improvement and assess them accordingly. But a statute giving a state board power to increase the tax rates prescribed by the legislature in order to meet deficiencies in collection of taxes is bad.

This general line of distinction has been many times affirmed by the Supreme Court in passing upon Acts of Congress. Thus under the

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88 See clear statement of Miller, J., speaking for the Court in Kilbourn v. Thompson (1880) 103 U. S. 168. Chief Justice Marshall in Wayman v. Southard (1825, U. S.) 10 Wheat 1, 42, in considering the authority of courts to rules, declared: "It will not be contended, that Congress can delegate to the Courts, or to any other tribunals, powers which are strictly and exclusively legislative. But Congress may certainly delegate to others, powers which the legislature may rightfully exercise itself. . . . The line has not been exactly drawn which separates those important subjects, which must be entirely regulated by the legislature itself, from those of less interest, in which a general provision may be made, and power to those who are to act under such general provision, to fill up the details." Pallelly v. Commissioners (1907) 16 N. D. 25, 111 N. W. 615; Bradley v. Richmond (1913) 227 U. S. 477, 33 Sup. Ct. 318; State ex rel. Howe v. Des Moines (1897) 103 Iowa, 76, 72 N. W. 639; State v. Sickles (1832) 24 N. J. Law 125.


90 Houghton v. Austin (1874) 47 Cali. 646.

91 Miller v. Mayor of New York (1888) 109 U. S. 385, 3 Sup. Ct. 228. Congress may delegate to the Secretary of War the function of determining whether a bridge constitutes an obstruction of navigation. Union Bridge Co. v. United States (1907) 204 U. S. 364, 27 Sup. Ct. 357. St. Louis etc. Ry. v. Taylor (1907) 210 U. S. 281, 28 Sup. Ct. 616, sustaining a statute by which it was left to the American Railway Association to determine what should be
Tariff Acts, the fixing of standards according to which different articles are rated—a matter essential for the determination of the levy—is properly left to the Secretary of the Treasury.9 A striking decision is that sustaining a statute which left to the President power to determine when certain tariff schedules should go into effect as against a foreign country because of the imposition by it of duties against the United States which he might deem to be reciprocally unequal or unreasonable in application to exports from the United States.60 Recognizing the increasing variety of the subject-matter upon which statutes operate, and the increasing complexity of the result sought to be achieved by statutes, the courts have gone much farther than under the simpler conditions of an earlier period in supporting the extensive use by the legislative arm of the more flexible executive instrumentality.61

the height for the draw bars of railway cars, and to the Interstate Commerce Commission to enforce this standard; Intermountain Rate Cases (1914) 234 U. S. 476, 34 Sup. Ct. 985, sustaining the statute giving power to the Interstate Commerce Commission to fix railroad rates conforming to the general requirements set forth in the act; Prentis v. Atlantic Coast Line (1908) 211 U. S. 210, 29 Sup. Ct. 67, contra, overruled. Gilligan v. City of Covington, December 8, 1919, advance opinions page 80. See also Pound, Justice According to Law (1914) 14 Col. L. Rev. 15; also an excellent discussion by Professor Green Separation of Governmental Powers (1920) 29 Yale Law Journal, 369.


10 Field v. Clark (1892) 143 U. S. 649, 12 Sup. Ct. 495.

11 United States v. Grimaud (1911) 220 U. S. 506, 31 Sup. Ct. 480. These two decisions in the same case strikingly indicate the present tendency of the Court. The case came up on demurrers to an indictment for grazing sheep on a Government forest reserve without a permit as required by rules prescribed by the Secretary of Agriculture. The statute charged this officer with the protection of these reserves, authorized him to make rules and regulations to that end and provided that violation of the regulations should be punishable. In the first decision, the Court affirmed a decision of the District Court sustaining the demurrers on the ground that the rules violated rested upon an attempted delegation of power of Congress. On a petition for rehearing, the new case was reargued before a bench containing three new Justices (Hughes, Van Devanter and Lamar, vice Fuller, Brewer and Moody), and in the second decision, the District Court was overruled. Lamar, J., expressing the unanimous opinion of the Court, said:

"In the nature of things it was impracticable for Congress to provide general regulations for these various and varying details of management. Each reservation had its peculiar and special features; and in authorizing the Secretary of Agriculture to meet these local conditions Congress was merely conferring administrative functions upon an agent and not delegating to him legislative power." For a state decision see Moers v. Reading (1853) 21 Pa., 188, 202.

"Half the statutes on our books are in the alternative, depending on the discretion of some person or persons to whom is confided the duty of determining whether the proper occasion exists for executing them. But it cannot be said that the exercise of such a discretion is the making of the law."
EXCESS PROFITS TAX

For a long time a large discretion to deal with special cases has been lodged in administrative officers, under federal taxing acts; thus the commissioner of internal revenue has long exercised the power to determine whether any tax has been illegally assessed, and more particularly the commissioner and the Secretary of the Treasury have exercised the power to compromise taxes assessed. While there has been some difference of opinion among the United States Attorneys General as to whether, under this power, a compromise could be made on other than fiscal considerations, the prevailing view appears to be that in making a compromise, discretion may be exercised on any grounds that seem relevant. Administration of the relief provisions in question involves less broad exercises of discretion than the compromise power. Under these sections there is a fairly definite guide as to the result to be obtained—the tax on the particular corporation having abnormal capital or income is to be adjusted as closely as possible to the tax upon corporations found to be similar in essential respects other than the abnormality. Clearly also this is a little more discretionary than the fixing of the standard for products under tariff acts or the making of valuations under all taxing acts.

An answer to the objection that the relief clause confers upon the Commissioner arbitrary power is that his action is not final. His

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9 U. S. Rev. St. sec. 3229. "The Commissioner of Internal Revenue, with the advice and consent of the Secretary of the Treasury, may compromise any civil or criminal case arising under the internal-revenue laws instead of commencing suit thereon; and, with the advice and consent of the said Secretary and the recommendation of the Attorney General, he may compromise any such case after a suit thereon has been commenced."

"In 17 Opinions, Attorney General (1881) 213, 216 Attorney General MacVeagh ruled that in considering any compromise under sec. 3229, or sec. 3469, the Secretary of the Treasury while "not at liberty to act from motives merely of compassion and charity" was at liberty "to consider not only pecuniary interests of the Treasury, but also general considerations of justice and equity and of public policy." To the same effect see an opinion of Attorney General Bonaparte, 26 Opinions, Attorney General (1907) 282, as to compromise of claims against solvent tax-payers arising out of violations of the oleomargarine statute; also 29 Opinions, Attorney General (1911) 217, opinion of Solicitor General Lehman, approved by Attorney General Wickersham. And sustaining compromise on general grounds of penalties established under internal revenue laws, see recent opinion of Attorney General Palmer, Corporation Trust Company, Income Tax Service (1920) par. 1929 ff. But see opinion Attorney General Devens, 16 Opinions, Attorney General (1879) 248, to the effect that there may not be compromised "a tax lawfully assessed upon and due from a solvent person or corporation"; and as to restriction of the power of compromise under sec. 3469, see (1879) 16 ibid., 259, 617; (1894) 21 ibid., 50; (1895) ibid., 204; (1900) 23 ibid., 18; (1902) ibid., 631; (1904) 27 ibid., 241; (1911) 29 ibid., 149.
assessments are in every case subject to judicial review. A taxpayer may be compelled to pay any tax assessed under the relief or any other provision, but he has the remedy of suing in the courts of the United States to recover back the amount believed to have been illegally assessed, after refusal or failure of the Commissioner to refund it upon application. Prompt collection of the revenue is essential and a provision for preliminary administrative determination as to the application of the revenue law to the case of each taxpayer is reasonable, and does not subject the taxpayer to discretionary power. The rule to be followed by the Commissioner in making relief assessments under the ruling section is fully as definite as many rules worked out by the courts for their own guidance.

There are many objections to the plan of the excess profits tax. To place the heaviest rate of tax, especially in times of peace, upon the most successful concerns is to penalize efficiency. The effort to shift this heavy but somewhat uncertain tax is a factor in the increase of prices; and may have resulted in a greater increase than would have been caused by a simpler and more uniform tax. This method of tax requires the exercise of inquisitorial powers, involves much delay and uncertainty and consumes effort of taxpayers which might otherwise be productively employed. Theoretically at least none of these considerations has any bearing upon the constitutional validity of the tax. If the courts cannot be convinced that the plan adopted by Congress involves discrimination that is merely wanton they cannot stay its operation. There is little likelihood that the court will conclude that the discrimination involved in the excess profits tax is hostile or arbitrary. It is to Congress rather than to the courts that the taxpayer must look for a fairer and wiser distribution of the revenue burden.

*U. S. Rev. St. sec. 3226.*