The Constitutionality of a Federal Net Wealth Tax:

A Socioeconomic Analysis of a Strategy Aimed at Ending the Under-taxation of Land

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ABSTRACT. Consideration of a Federal *Net Wealth Tax* would help settle the question of the scope and limits of the *taxing powers* of the *United States Government.* The confusion attending this, which has prevented the federal government from taxing *land* and kept *state taxation* of land too low to be an efficient allocator of this *resource,* can be clarified. The *Constitution's* Article I, Section VIII, gave the federal government power to levy taxes, duties, imports and excises, as "indirect" taxes, requiring only that the duties, imposts and excises be "uniform throughout the United States." The 16th Amendment authorized a "direct" tax on "incomes, from whatever source derived." The intent of the Founding Fathers—almost all large landholders—was to prevent the new federal government from using land as a *tax base.* But the distinction between the types of taxes lacks economic meaning. By making the base of a new tax the net wealth of taxpayers, *Congress* could obtain a *Supreme Court* test to end the confusion. If the Court, following precedent, required that land be excluded from the tax base, this would assure land as a tax base to the states and permit them to tax it in a way to end speculative withholding of tracts and sites and to bring about orderly development according to current need.

ALTHOUGH DIFFERENCES of opinion exist as to the seriousness of the problem, there is a general consensus that consideration of a federal Net Wealth Tax—a tax on wealth less debt—would, at the very least, bring to center stage the constitutional limitations on the taxation powers of the federal government. The declaration that the federal estate tax was legal does not provide the precedent that seems obvious. The estate tax, because a single payment is involved, was placed by the court under the excise tax mantle.[1]

There has been, from the very beginning of the United States, considerable confusion as to the taxation powers of the federal government. Much of this difficulty was erased by the 16th Amendment in 1913. However, court

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American Journal of Economics and Sociology, Vol. 43, No. 4 (October, 1984).

decisions and legal writings since the amendment's adoption have demonstrated that it is not as broad as Justice Holmes and others had thought.[2]

I

Tax Provisions of the Constitution

THE FEDERAL CONSTITUTION includes clauses that extend taxation powers to the federal government and clauses that limit the federal government's taxation powers. Our interest is directed primarily toward Article I, Sections VIII and IX plus Amendment XVI (1913). The 16th Amendment is often praised because of its apparent simplicity and directness. It says:

> 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.

This amendment was enacted as an answer to Section IX of Article I. It goes like this:

> No capitation or other direct tax shall be laid, unless in proportion to the census or enumeration hereinbefore directed be taken.

It was thought at the time the 16th Amendment was adopted that the concept of direct taxes had both a definite and well considered legal and economic meaning. The settled meaning was that in combination with Article I, Section VIII, Clause 1, which reads:

> The Congress shall have power to lay and collect taxes, duties, imports and excises, to pay the debts and provide for the common defense and general welfare of the United States; but all duties, imports and excises shall be uniform throughout the United States; . . .

The Congress has "exhaustive" power of taxation which "embraces every conceivable power of taxation" and every possible subject of taxation. Article I, Section VIII, Clause 1, included all taxes that might be considered indirect and the 16th Amendment all taxes that might be considered as direct.[3]

The problem in identifying in practice where the taxation powers of Congress may be exercised arises because of a fundamental error of the constitutional provisions. The error was in believing that indirect and direct as referring to taxes had a real legal or economic meaning.

II

Legality of Net Wealth Tax

THE BASIC DEFINITIONAL ACTION to follow in making net wealth a legal taxable base for use by the federal government is to accept the concept that the right and ability to operate in the U.S. can be measured by the market value of the assets possessed. Here, we have wealth being substituted for income as the measure of the value of the privilege.

The above reasoning permits the conclusion that the value of a privilege may be measured by the capital value of the associated assets, as well as by some legislatively determined definitions of net income or profits. This being true, a subject consisting of the income derived from federal related benefits could be made liable to pay taxes based on the net worth of property. The measure becomes the net wealth. It is assumed in this analysis that net wealth, or rights to income are as readily used as a tax base as is income under the 16th Amendment.

A constitutional unapportioned net wealth tax would be establishable on about the same grounds as the 1909 Corporate Profits tax, that is, upon the receipt of certain benefits. For example, a tax could be established on the receipt of federal legal, military, and police protection of all kinds. The measure of such a tax could be the value of the property and assets receiving this protection, that is, the value or wealth of the individual or institution protected net of all debts.

The concept of separating the measure from the subject, the base, of a tax has a long tradition in Supreme Court decisions. For example, the first Chief Justice, John Marshall, pointed out that if the subject of a tax were constitutional, then it would make little difference, ordinarily, what the measure might be.[5] More recently, the Court pointed out that the 1909 Corporate Profits tax was not an income tax, but rather an excise on the benefits of operating a business in the corporate form, and was only measured by corporate income.[6] To make this distinction clear, the court went on to say that since "the subject of the tax (was) within the power of Congress, measure of it is largely a matter for its discretion."

The information we have on what the writers of the federal Constitution had in mind when they included the clauses restricting the levy of direct taxes, is very limited. However, interpreters of the notes and analyses of the debates of the members of the convention writing the Constitution do develop a consensus in this area.

Briefly stated, this view is that without doubt the taxation of land was the levy of a direct tax. The aim of the prohibition of federal levy of direct taxes was to make land, a much more basic source of power and wealth, then than now, available without dilution or restriction for use as a tax by the states. This action giving states control over the taxation of land was envisaged as another spoke guaranteeing the fiscal and therefore political independence of the states.

Another aspect of the restriction of the taxing power of the federal government was the desire of our founding fathers to protect the economic independence of a strong class of yeomen. The accomplishment of this aim would be enhanced by restricting the central government's power over the

taxation of land. Taking away the federal government's power to levy direct taxes was seen to mean taking away its power to tax land. This strengthened the likelihood of a strong and independent yeomen group.[7]

The same action also acted to guarantee that the substantial landowners making up the constitutional convention would not have to fight the strong federal government they were establishing to assure protection of their land holdings from high federal taxes. Limiting federal taxation of land, through prohibition of direct taxes avoided using the words "land would be tax free."[8]

III

Conclusion

THE SEPARATE EVALUATION of a tax's measure and subject is a well established method used by the Supreme Court in judging the constitutionality of a tax. As regards the constitutionality of an unapportioned net wealth tax, the relative question gets down to whether a constitutionally acceptable subject can be measured by the net wealth of the taxpayer. In the past, the Court has allowed the measure of a tax to reach out to property that otherwise could not be taxed without apportionment, but the extent of the property measured by these taxes has always been limited in scope in some way.

The trend of Supreme Court decisions in the area of basic government management has apparently been toward greater liberty of action. Therefore, one can with considerable confidence conclude that a federal Net Wealth Tax would be declared constitutional. Chances would more than likely be enhanced if land were excluded from the definition of net wealth to be subject to taxation.[9] This approach would also increase the political support a net wealth tax would enjoy, for the taxation of net wealth as land would be prohibited to the federal government and completely assured to the states. The aim of the founding fathers would be realized.[10]

Notes

1. *Barritt v. Tomlinson,* 129F Suppl. 642 (OC., SD, FLA., 1955).
2. *Eisner v. Macomber,* 252 U.S. 206 (1920).
3. *Brushaber v. Union Pacific Railroad Co.,* 240 U.S. 1, 12 (1916) and *Veazie Bank v. Fenno,* 75 U.S. 541 (1869).
4. *Ray Consolidated Copper Co. v. United States,* (268 U.S. 373, 376, 1925).
5. *Brown v. the State of Maryland,* (12 Wheat 419 (1827)).
6. *Flint v. Stone Tracy Co.,* (220 US 107 (1911)).
7. *Hylton v. The United States,* 3 U.S. 171ff. (1796).
8. Cp. Charles A. Beard, *An Economic Interpretation of the Constitution of the United States* (1913) (New York: The Free Press, 1965), pp. 19–24, and 253*ff.*
9. *Flint v. Stone Tracy Co., loc. cit.*
10. Justice Peterson, in *Hylton v. the United States, loc. cit.*