THE POWER OF CONGRESS TO IMPOSE EXCISE TAXES RETROACTIVELY*

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Very recently the United States Supreme Court held the processing taxes under the National Agricultural Adjustment Act unconstitutional. The Secretary of Agriculture, in public addresses, denounced the action of the Supreme Court in ordering the refund of the amounts which were paid into the Federal District courts, pending the final determination of preliminary injunctions issued by such courts, and he and those who sponsored that illegal statute now urge upon Congress that it impose a similar processing tax retroactively to replace and take up the former illegal exaction.

At this time, an analysis of the power of Congress in this respect is in the national interest. ". . . the power to destroy which may be the consequence of taxation is a reason why the right to tax should be confined to subjects which may be lawfully embraced therein, even although it happens that in some particular instance no great harm may be caused by the exercise of the taxing authority as to a subject which is beyond its scope." (*Knowlton v. Moore,* 178 U. S. 41)

Excise taxes have always been borne with resentment and occasionally in history have been a contributing cause of rebellion and of the downfall of governments. Samuel Johnson defined an excise as "A hateful tax levied upon commodities and adjudged not by the common judges of property, but by wretches hired by those to whom this excise is paid."

Blackstone says (Jones Ed. Sec. 441):

> ". . . But, at the same time, the rigor and arbitrary proceedings of excise laws seem hardly compatible with the temper of a free nation. For the frauds that might be committed in this branch of the revenue, unless a strict watch is kept, make it necessary, wherever it is established, to give the officers a power of entering and searching the houses of such as deal in excisable commodities, at any hour of the day, and in many cases, of the night likewise. And the proceedings in case of transgressions are so summary and sudden,

* For a previous article supporting another view of the problem see Ralph R. Neuhoff, "Retrospective Tax Laws," 21 St. L. L. Rev. 1.

> that a man may be convicted in two days' time in the penalty of many thousand pounds by two commissioners or justices of the peace; to the total exclusion of the trial by jury, and disregard of the common law. . . . Its original establishment was in 1643, and its progress was gradual; being at first laid upon those persons and commodities where it was supposed the hardship would be least perceivable, viz., the makers and venders of beer, ale, cider and perry, and the royalists at Oxford soon followed the example of their brethren at Westminster by imposing a similar duty; both sides protesting that it should be continued no longer than to the end of the war, and then be utterly abolished. But the parliament at Westminster soon after imposed it on flesh, wine, tobacco, sugar, and such a multitude of other commodities, that it might fairly be denominated general: in pursuance of the plain laid down by Mr. Pymme (who seems to have been the father of the excise) in his letter to Sir John Hotham; signifying, 'that they had proceeded in the excise to many particulars, and intended to go on further; but that it would be necessary to use the people to it by little and little.' . . . But, from its first original to the present time, its very name has been odious to the people of England. (then following a list of excises, he says) "A list, which no friend to his country would wish to see further increased."

With a change of time and place, Blackstone's statement is the history of the excise in the United States: It was first imposed upon the manufacture of whiskey and was the cause of the "Whiskey Insurrection" in 1794. It was then contended that there are certain natural rights which no government confers and upon which no government can impose a condition. In many later cases, it has been urged that the United States may excise only privileges which it grants and can withhold, for instance, that the privilege of inheritance being granted by the states cannot be taxed by the United States. Neither limitation has been sustained (*Knowlton v. Moore,* supra). As Pymme proposed, it was introduced "little by little" until, as appears from the list hereafter written, it has become almost general.

The power of Congress to impose taxes is conferred by Section 8, Article 1 of the Constitution:

> "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."

"No tax has yet been found which is not either a direct tax or included under the words, duties, imposts and excises." (*Pollock v. Farmers' Loan & Trust Co.*, 157 U. S. 557). Section 9, Article 1 of the Constitution requires that capitation and other direct taxes imposed by Congress shall be proportioned to the census. Because of this limitation, no taxes, conceded to be direct, have been imposed since the first years of the nation. All internal revenue taxes now imposed by Congress are, or purport to be, excise taxes.

Johnson and Blackstone limited the excise to commodities at the points of consumption or retail sale. As has happened with most terms describing governmental functions, the meaning of the word "excise" has been broadened by practise and the mounting complexity of social relations.

It is defined in *Flint v. Stone Tracy & Co.*, 220 U. S. 106 (quoting Cooley Constitutional Limitations) as follows:

> "Excises are 'taxes laid upon the manufacture, sale, or consumption of commodities within the country, upon licenses to pursue certain occupations, and upon corporate privileges.'"

In *Thomas v. United States*, 192 U. S. 363, the Court said:

> "There is no occasion to attempt to confine the words, 'duties, imposts, and excises' to the limits of precise definition. We think that they were used comprehensively to cover customs and excise duties imposed on importation, consumption, manufacture, and sale of certain commodities, privileges, particular business transactions, vocations, occupations, and the like."

In *United States v. Philadelphia*, 262 Fed. 188, it is said that "it is a charge for the privilege of following an occupation, or trade, or carrying on a business."

In *Patton v. Brady*, 184 U. S. 608, the court, quoting part of the argument said:

> "Taking these three sources of information and combining them, it would seem that the leading idea of excise is that it is a tax, laid without rule or principle, upon consumable articles, upon the process of their manufacture and upon licenses to sell them."

At the present time, the national government excises, among other things, sales of real estate, the issuance or transfer of

stocks or bonds, the sale or manufacture of brewers' wort, grape juice and grape syrup, crude petroleum, fuel oil, lubricating oil, gas, coal and coke, tires and tubes, toilet preparation, fur articles, jewelry, automobiles, radios, mechanical refrigerators, sporting goods, firearms and cartridges, cameras, matches, chewing gum, playing cards, electricity, products of tobacco, liquor, wines, beer, lease of safety deposit vault, the use of telegraph, telephone, radio or cable for messages, transportation of oil by pipe lines, the use of a corporate franchise, admissions to places of amusement, dues and assessments paid to a social club, sales on an exchange, passage tickets to points out of the United States, transfers of interests in silver, the making of a gift, the transfer of property at death, and the receipt of income, a list, which in the words of Blackstone, "no friend to his country would wish to see further increased." Before the Supreme Court's decision, the processing of most food materials and of cotton was also excised.

An excise is a condition or toll imposed upon the exercise of a privilege. The nature of an excise shows that, in theory at least, it is voluntarily assumed by the taxpayer. The tax becomes due only when the privilege is exercised. One is not compelled to exercise the privilege.

In *South Carolina v. United States,* 39 Ct. of Claims, 257-286, affirmed 199 U. S. 437, the Court said:

> "A tax is obligatory; from it there is no escape. An excise is voluntary; the purchaser who would pay it cannot be compelled to purchase."

In *Thomas v. United States,* supra, the Court said:

> "The stamp duty is contingent on the happening of the of sale, and the element of absolute and unavoidable demand is lacking."

In *New York Trust Company v. Eisner,* 256 U. S. 1. c. 349, concerning the estate tax upon the passage of property at death, it is said:

> "It is argued that when the tax is on the privilege of receiving, the tax is indirect because it may be avoided; whereas here the tax is inevitable, and therefore direct. But that matter also is disposed of by Knowlton v. Moore, not by an attempt to make some scientific distinction, which would be at least difficult, but on an interpretation of language by

its traditional use,—on the practical and historical ground that this kind of tax always has been regarded as the antithesis of a direct tax,—'has ever been treated as a duty or excise, because of the particular occasion which gives rise to its levy.' "

The transmission of property at death is ruled to be a privilege. (*Nichols v. Coolidge*, 274 U. S. 537). One does not need to be possessed of any property. If one dies possessed of property and passes it to his heirs or by his will, he has exercised a privilege and voluntarily subjected the property which he leaves —his estate—to excise.

Under the definition of an excise—a condition or toll imposed upon the exercise of a privilege—it is plain that it cannot be imposed after the privilege is exercised. After the privilege has been exercised, there is nothing left to excise. Thus, in *Forbes Boat Line v. Board of Commissioners*, 258 U. S. 338, where the legislature of Florida undertook in 1919 to impose a toll upon the plaintiff for passage through the locks of a canal in 1917, the Court said:

"If we apply that principle this statute is invalid. For if the legislature of Florida had attempted to make the plaintiff pay in 1919 for passages through the lock of a canal that took place before 1917, without any promise of reward, there is nothing in the case as it stands to indicate that it could have done so any more effectively than it could have made a man pay a baker for a gratuitous deposit of rolls."

The principle is not as clear cut as the foregoing statement indicates, nor is it recognized without contradiction. The Constitution imposes no plain limitation upon the power of Congress in this respect. In *Frew v. Bowers*, 12 F. (2d) l. c. 630, this question is considered and Justice Hand, in his concurring opinion, said:

"If it were necessary that an excise should be imposed upon the activity or privilege which determines the tax, I should at once agree that it could not operate upon one exercised or enjoyed before the law was passed. There would be no subject-matter to tax. But I cannot see that it need be so imposed, and cases like Billings v. U. S. 232 U. S. 261, U. S. v. Bennett, 232 U. S. 299, Flint v. Stone Tracy Co., 220 U. S. 107, and Brushaber v. Union Pac. R. R. Co., 240 U. S. 1, seem to me to establish the contrary. I can find no

> helpful definition of excise, but there seems no reason why it should not be imposed upon individuals personally, merely because of some activity in which they have engaged or privilege which they have enjoyed. These will serve to define the class to be taxed, and the tax need not necessarily be direct, for that is purely a historical and conventional question. Knowlton v. Moore, 178 U. S. 41, 20 S. Ct. 747, 44 L. Ed. 969."

As appears from a later quotation from Justice Hand's concurring opinion in Frew v. Bowers, the court held the statute unconstitutional, if applicable, as far as it was retroactive, and the quoted statement was merely argumentative.

Mr. Justice Brandeis in *Untermeyer v. Anderson,* 276 U. S. 440, in his dissenting opinion, stated:

> "The need of the government for revenue has hitherto been deemed a sufficient justification for making a tax measure retroactive whenever the imposition seemed consonant with justice and the conditions were not such as would ordinarily involve hardship."

An examination of the authorities cited in the quotation above from *Frew v. Bowers,* and in the dissenting opinion of Justice Brandeis, discloses that the taxes approved in thoses cases, if retroactive at all, were so only to a limited extent.

In *Billings v. U. S.* cited in *Frew v. Bowers,* the act of August 5, 1909, imposed a tax on the first day of September of each year upon the use of every foreign-built yacht now or hereafter owned or chartered for more than six months by a citizen of the United States. The court held "that the six months clause is concerned not with the period when the tax imposed shall be levied and collected, but addresses itself to the subject-matter upon which the tax is placed; in other words, it qualifies the word 'charter,' and therefore only indicates when the use of a chartered vessel shall become subject to the duty imposed." So far as the tax applied to the use between the date of the passage of the act and the first day of the following September, it was certainly not retroactive in any sense. The Court said: "Again let it be conceded that the causing the tax for the annual period to become due in September, 1909, is to give it in some respects a retroactive effect, such concession does not cause the act to be beyond the power of Congress under the Constitution to adopt."

United States v. Bennett, also cited, construed the same statute. In *Flint v. Stone Tracy Co.,* the court sustained the act, passed August 5, 1909, imposing a tax upon the doing of business in a corporate capacity measured by the income of the calendar year 1909. In a proper sense, it was not retroactive at all, because it applied only to corporations doing business on the date of or after the passage of the act. In *Stockdale v. The Ins. Company,* 20 Wall. 323, cited by Justice Brandeis, the Court held that an income tax was constitutional which was not retroactive beyond the beginning of the year of the passage of the act. The same ruling was made in *Brushaber v. Union Pacific R. R. Co.,* 240 U. S. 1. The income of a year is taxed as a unit and if the whole unit is not passed when the tax is imposed, the imposition of the tax is, in a sense, not retroactive at all.

In a general way these cases disclose the limits of retroactivity in taxation which the courts have sustained. Justice Brandeis also cites the fact that the Revenue Act of 1918 was not passed until February, 1919 and no one contested the validity of this Act. A similar fact is the sole authority for the ruling of the court in the case of *Stockdale v. Insurance Company,* supra, which is the prime citation in every decided case and in every obiter statement in various opinions of the courts that Congress may impose retroactive excise taxes. The Act, passed in 1864, which no one contested, was passed in the period of war and the national war hysteria uniformly denounces every act opposed to the successful prosecution of the national effort. If any person has been willing to begin a contest in those critical periods, without doubt the question would have been deemed unpatriotic. Reason always surrenders to desire, and the courts participate in intense national feelings.

But, as is clearly pointed out by Justice Brandeis in his dissenting opinion in the case of *Burnet v. Coronado Oil & Gas Company,* 285 U. S. 393, even *stare decisis* is not as final upon constitutional questions as upon other law principles. He says: "This is strikingly true under the due process clause when the question is whether a statute is unreasonable, arbitrary or capricious." If, upon the application of the constitution, the reasoned opinions of the Supreme Court are not controlling, then, in reason, mere public inaction should not be even persuasive. The

present writer does not believe that any authority, except obiter, supports the conclusions of Justice Brandeis and Justice Hand in the quotations above written.

The limitation of the power of Congress to impose retroactive excise taxes results from the Fifth Amendment. The recognition by the courts that a tax could violate the 5th Amendment was slow in developing. Thus, in *Frew v. Bowers*, supra, decided in 1926, the court was unable to find any authority directly ruling that a tax could violate the 5th Amendment. It said:

> "But it is answered that this result goes only to the equal assessment of the tax and must rest upon the Fifth Amendment, which does not apply to federal taxation. I quite agree that the Supreme Court has in many cases implied or said as much (Citations). If the rule is to be taken unconditionally, taxpayers may be selected by lot and assessments may vary with the price of wheat. Perhaps it would have been necessary to go so far, had it not been for the opinions in Brushaber v. Union Pacific, 240 U. S. 1, and Barclay & Co. v. Edwards, 267 U. S. 442, 450, and the strong intimations in Lewellyn v. Frick, 268 U. S. 238, 251, 252. But these make it clear that the power is not utterly absolute. A tax may be so 'arbitrary and capricious,' its 'inequality' so 'gross and patent,' that it will not stand, and as I can think of no other pertinent constitutional limitation, but the Fifth Amendment, it seems to me that the rule is not as stark as the defendant argues. If there be any limit whatever, I own I cannot, except in fancy, think of a case more plainly beyond it than this."

The cases cited in the last quotation, by way of concession in in the opinion, stated only that Congress may not confiscate property under the guise of taxation or exercise general legislative powers not within the powers conferred upon it and the court in 1926 did not find any authority freely supporting its ruling that the Fifth Amendment imposed a limitation upon a conceded tax.

The proposition, that a tax under a duly enacted statute, may not be due process of law, developed more or less in step with the attempted use of the taxing power to accomplish social reforms. The Court, until recent years, was not required to rule a tax imposed by Congress violative of the Fifth Amendment, because no tax imposed by Congress gave occasion for such

ruling. In recent years a number of federal taxes have been held confiscatory. In many of such cases, retroactivity was the sole taint.

Thus, in *Blodgett v. Holden,* 275 U. S. 142, the Court said:

> "It seems wholly unreasonable that one who, in entire good faith and without the slightest premonition of such consequence, made absolute disposition of his property by gifts should thereafter be required to pay a charge for so doing."

This is in reference to a gift tax imposed by the act of June 2, 1924 and made retroactive to the beginning of the year.

In *Untermeyer v. Anderson,* supra, it was held that the fact that the gift was made while the Revenue Act of 1924 was in the last stages of progress through Congress, did not "relieve the legislation of the arbitrary character." The Court said:

> "The taxpayer may justly demand to know when and how he becomes liable for taxes—he cannot foresee and ought not to be required to guess the outcome of pending measures. The future of every bill while before Congress is necessarily uncertain. The will of the lawmakers is not definitely expressed until final action thereon has been taken."

In both of the last cited cases, the gift tax imposed by the Act of June 2, 1924 was held invalid so far as it attempted to impose a tax upon gifts made prior to the passage of the Act. *Lewellyn v. Frick,* 268 U. S. 238, ruled that the Revenue Act of 1918 (including for estate tax, insurance under policies taken out by a decedent upon his own life) does not apply to policies the right to the proceeds of which had vested in the beneficiaries before the passage of the statute. This was a construction of that particular statute. But in *Industrial Trust Company v. United States,* 80. L. Ed. 208, decided December 9, 1935, the Court held that if any of the retroactive provisions of the Revenue Act of 1926 apply to such a policy "the provision is open to grave doubt as to its constitutionality."

In *Nichols v. Coolidge,* 274 U. S. 531, the Court said:

> "Under the mere guise of reaching something within its powers Congress may not lay a charge upon what is beyond them. . . . Section 402 (c) of the statute, insofar as it requires that there shall be included in the gross estate the value of property transferred by a decedent prior to its

passage merely because the conveyance was intended to take effect in possession or enjoyment at or after death, is arbitrary, capricious and amounts to confiscation."

In *Helvering v. Helmholz,* 80 L. Ed. 5, the decedent, with others, had created a trust which they could terminate by joint action. Under the act subsequently passed providing for the inclusion of trusts which the grantor may revoke, either alone or in conjunction with any other person, it was sought to include in the gross estate of decedent, the value of the property transferred upon this trust. The court said:

"Another and more serious objection to the application of Sec. 302 (d) in the present instance is its retroactive operation. The transfer was complete at the time of the creation of the trust. There remained no interest in the grantor. She reserved no power in herself alone to revoke, to alter or to amend. Under the revenue act then in force the transfer was not taxable as intended to take effect in possession or in enjoyment at her death. If Sec. 302 (d) of the Act of 1926 could fairly be considered as intended to apply in the instant case its operation would violate the Fifth Amendment. Nichols v. Coolidge, 274 U. S. 531."

On the other hand, as to a similar trust *created after the passage of the act,* the court ruled in *Helvering v. City Bank Farmers Trust Company,* 80 L. ed. 1:

"A legislative declaration that a status of the taxpayer's creation shall, in the application of the tax, be deemed the equivalent of another status falling normally within the scope of the taxing power, if reasonably requisite to prevent evasion, does not take property without due process; . . . ."

In the case of *White v. Poor,* 80 L. ed. 8, the court ruled:

"An estate tax law cannot, consistently with due process, be so applied as to tax property in which decedent transferred, prior to its enactment, his entire interest without reservation of power to revoke, alter, or amend."

One must draw a narrow line to discover the controlling distinction. In the writer's opinion, it is this:

The question does not depend upon hardship or fairness in the particular case. Taxation must be confined to lawful subjects "even although in some particular instance no great harm may be done." The fairness or justice of the statute is determined

by the legislature. The courts can consider only the constitutional power of the legislature to enact the statute.

Where any part of the right which is excised, as for instance the receipt of income for the year, has not been finally exercised when the taxing act is passed, the tax is not necessarily arbitrary and capricious so that the court, approaching the question with that delicacy which one branch of the government should entertain toward the acts of a coordinate branch, can disregard it under the Constitution. Congress may write such rules effective thereafter as are appropriate and necessary for prevention of evasion of taxes. It may, if reasonably appropriate to that purpose, fix the taxable status, after the passage of the statute, of any acts or arrangements which a citizen may thereafter do or establish.

If completely retroactive excise taxes were permissible in any case, the courts could enforce no limitations except those written in the statute, which might impose the tax, say upon income received twenty years before, long after it was spent or had become capital, or upon estates of persons who were dead ten years.

The legislature does not ask the consent of the citizen for the imposition of taxes. They are "in invitum." If the legislature imposes them validly, the citizen is compelled to pay them. There must be some reason why the particular citizen is selected for the payment of tax. The legislature cannot select persons by name, that is, particular individuals, and impose a tax upon them. This would be confiscation.

An excise tax, upon the exercise of a privilege, it is said, is laid without rule or principle. But the occasion for the incidence of the tax being the exercise of a privilege or right, it can be imposed only on one who enjoys and exercises such privilege or right. A tax upon the exercise of a privilege is similar to a penalty for a violation of the law. The penalty can be imposed only upon the guilty.

No one contradicts that a law is tyrannical which imposes a penalty upon an act which, when the act was done, one was at liberty to do without any liability. Such a law is prohibited under the constitution as ex post facto. Identically the same logic condemns the imposition of a civil liability—a tax—for the exercise of a privilege after the privilege has been exercised.

A tax which is imposed upon a man for something he has already done and which possibly he would not have done if he had been forewarned, is pure caprice. An excise is hateful in itself, because it conditions rights which men consider belong to them naturally. (*Beals v. State,* 139 Wis. l. c. 555.) Even the Government cannot reverse the order of events in times of their happening. After an act is done, it is not possible to impose a condition upon the doing of the act. The imposition in that event is not a condition for doing the thing, but a penalty for having done it.

Due process of law requires "a pre-existing rule of conduct, not an act of the legislature framed to take away the very rights whose destruction is complained of" (*Wynehamer v. People,* 13 N. Y. 378). In principle, an excise tax is imposed upon the exercise of a privilege. The past enjoyment of a privilege affords nothing for present tax. There is not presently anything to tax merely because at some former time one did an act he then could do without tax. To tax one because in the past he did an act, or enjoyed a privilege, is without reason. The occasion of selection for tax—an act already done—is necessarily arbitrary and capricious—pure tyranny—like advising a man for the first time that he must account for his past meal.