

U.S. Department of Justice
Assistant United States Attorney
Donna Ford
Federal Building, Room 7211
300 North Los Angeles Street
Los Angeles, CA 90012

October 10, 2004

RE: ED CV 04-00075 RT (Mcx).

Dear Ms. Ford,

This is our request for a conference pursuant to Local Rule 37-1, (F.R.Civ.P. 37). We were in hopes that this request would not be necessary in light of our letter to you dated May 18, 2004, and your agreement under paragraph (g-h) of the Scheduling Conference Report to provide the requested information. Again, we must have misunderstood the process.

Rule 37-1 requires us to identify the “issues and or discovery request in dispute”. This is difficult for us, because we have never had the opportunity to discuss the issues, or any other aspect of our suit, with you or anyone else in the Treasury or Justice Departments. The answers you did provide, in response to our complaint and request for refund, were of no help to us in addressing our questions. Where are the answers to our concerns, or court cases in which our allegations are addressed and disposed of? For you to deny everything, without providing any documentation refuting our position, leads us to believe you have no real answers. In which case, it seems to us that ignoring the problem will not make the problem go away, so, perhaps it is time for us to initiate a discussion of those issues

In our letter to you, dated May 18, 2004, we requested copies of the W-4 withholding certificate and instructions issued in 1942, the first year common law, labor for hire, employees became “taxpayers”. [FN-1] In that year, common law, labor for hire, employees were required to pay the “victory tax” and the “optional tax rate” on gross income, through the “withholding” provisions imposed under Part II of Subchapter D. [FN-2]

According to the Congressional Record, Committee Reports, and other historical documents, the Victory Tax was to be a form of “enforced savings,” that is, a compulsory loan to the Federal Government to offset the cost of borrowing the money necessary to continue the war effort. The intended benefit was to curb inflation caused by increased federal spending, by removing a portion of the consumer’s spending power. [FN-3]

Part I, of Subchapter D, imposed a 5% tax upon what Congress defined as “victory tax net income,” that is, gross income less business expenses allowed by section 23 (a) (1) and (2) and the “specific exemption” allowed by section 452. Or, in the case of the *taxpayer* filing under the provision of the “optional tax rates,” allowed by section 400, “victory tax net-income” meant “gross income,” i.e., wages. [FN-4]

The “withholding tax,” as it is commonly referred to, originates from Part II—Collection of Tax at Source on Wages”, and is specifically directed at the employer, not the employee. The employee was only required to furnish the properly signed W-4, it was up to the employer to “withhold, collect, and pay” the tax to the Treasury. [FN-5] As such, it was the W-4 certificate which directed the employer to withhold from the employee’s paycheck the proper amount of tax applicable to the employee’s “wages,” which were “includible in the gross income” of the employee. [FN-6]

The Revenue Act of 1942, itself, was based upon **commercial net-income**, not “wages”, gross income, or annual receipts [FN-7]. In order to implement the “Victory Tax,” Congress redefined “net-income” for purposes of Subchapter D. [FN-8] Note the combination of the two measurements of “income,” as this presents the basis for the legal issues we are raising. [FN-9]

Why did Congress choose the phrase “victory tax **net-income**,” then include gross income wages within that definition? Why did Congress call “withholding at the source” a tax, when, in fact, they implemented a collection method for the “optional tax rates”, allowed by Chapter 1 of the Code? [FN-10] The answer, from what we have determined, begins with the Revenue Acts of 1940 and 1941. Those Revenue Acts made changes to section 51 of the 1940 Code and added Supplement T to the 1941 Code, but did not change the power or authority of the Statute in relation to the subject matter upon which the tax operated. [FN-11]

Section 11, of the 1942 Revenue Act, is titled “Normal Tax on Individuals,” it reads:

“There shall be levied, collected, and paid for each taxable year upon the **net-income** of every individual a normal tax of 6 per centum of the amount of the **net-income** in excess of the credits against **net income** provided in section 25. (For alternative tax, if **gross** income from certain sources is \$3,000 or less, see section 400)”

Supplement T, of that year, is the “Optional Tax Rates” imposed by section 400, it reads:

“*In lieu of the tax imposed under sections 11 and 12*, an individual who makes his return on the cash basis **may elect**, for each taxable year, to pay the tax shown in the following table if his gross income for such taxable year is \$3,000 or less and consists wholly of one or more of the following: salary, wages, compensation for personal services, dividends, interest, or annuities:”

Supplement T does not impose a tax upon anyone, it provides an optional way of computing the tax imposed by Section 11 upon net-income. If the citizen was not subject to the **commercial net-income** provisions of Chapter 1, they could not arbitrarily be made “liable” for the **optional tax rates** imposed by section 400.

Treasury Regulations 103, 111, and 118 all start with the same proclamation setting forth the power and authority conveyed by the Title 26 Statute, it reads: “Scope of Regulations”

“These regulations deal with the taxes upon **net income** imposed by chapter 1 of the Internal Revenue Code,”

That is all the power Congress claimed to take from the 16th Amendment. [FN-12] If it was not **net-income**, there was no power or authority given by the Statute to levy a tax of any kind upon it. The “Victory Tax” was no different, therefore, Congress used the phrase “victory tax net-income” in order to limit the scope of the tax, in compliance with the power and authority taken by **chapter 1** of the implementing Statute. In order for Congress to levy their tax upon “gross” income they would be required, by Constitutional principles, to re-write the entire Law. Congress has, so far, refused to do that. Therefore, the interpretation of the Law must be kept within the power and authority taken by the Statute written in 1913. [FN-13]

In that light, follow the wording of the Legislation enacted between 1940 and 1944. Did Congress specifically make the common law, labor for hire, employee’s “wages”, net-income for purposes of the Statute? Or, did Congress provide a collection method for the **commercial net-income taxes** imposed by **chapter 1** of the Code; from which the employee’s gross annual “wages,” as their sole means of yearly support, were exempt?

Section 450 imposed the “Victory Tax,” it reads:

“There shall be levied, collected, and paid for each taxable year beginning after December 31, 1942, a victory tax of 5 per centum *upon the victory tax net income* of every individual (other than a nonresident alien subject to the tax imposed by section 211 (a))

This concept of **net-income** was a total departure from the concept of the “income tax,” as imposed under all of the previous Revenue Acts passed by Congress. Case in point: The Congressional Record of October 9, 1942, page 7987 and the remarks of Senator George, the Chairman of the Senate Finance Committee.

“If we are going to depart during this war, as an emergency matter, from the concept which has run through our tax system, that is to say, imposing a tax on net income, there would seem to me to be little or no purpose to the pending proposal if no one would be reached who was not subject to the net-income tax provisions of the bill as passed by the House and as reported to the Senate. In other words, if it would not bring in additional taxpayers; if it would not reach the vast number of income producers who will not pay taxes on net income, there would be little reason in departing from the net income system and going to the gross-income system in collecting a tax.”

Note the change in the meaning of the term “net income,” in relation to the “new taxpayers” brought in by the withholding provisions of Section 465. Prior to Subchapter

D, the income tax was levied only upon the net-income or profits derived from commercial and financial transactions. This, by definition, included the “compensation for personal services” rendered by the individual during the course of their business activity. From this **commercial net-income**, Congress allowed a credit against **net-income** for the personal exemption and other specified personal expenses allowed by section 25, before determining the amount of excise tax payable. Thus the reason for excluding “personal living and family expenses” from the computation of **commercial net income**, and then providing an allowance for those expenses afterwards.

Subchapter D, however, changed that relationship. The “Victory Tax” paid under Supplement T, when filed by the millions of new “taxpayers” brought in by the withholding provisions, was, in effect, a tax levied upon and measured by gross income, not **commercial net-income**. Read the definition of “victory tax **net income**”. In reality, if the interpretation is kept within the proper scope of the Statute, there is nothing wrong with that definition in relation to **commercial net income**. However, by tying the filing of the “victory tax” return to the simplified 1040A form, Congress changed the relationship between **commercial net income** and the gross income wages of millions of common law, labor for hire, employees.

The simplified tax return required the use of the “option tax rate” schedule allowed by section 400, i.e., Supplement T. Supplement T provided an “*optional*” way of computing **commercial net income** by allowing an arbitrarily determined amount of “expenses” from gross income. Congress then allowed the “specific exemption” of \$624 to a single person, or up to \$1248 for married persons if both were working, from this “victory tax net income,” before determining the amount of tax owed.

In other words, The Victory Tax, through the use of Supplement T, changed the concept of “income” taxation from that of an excise tax upon commercial and financial gains and profits, to a direct tax imposed upon the annual receipts of the household. [FN-14]

In this regard, the basic question that must be answered by the court is whether or not Congress has the Constitutional authority to implement a program of “enforced savings,” or “compulsory loans,” for any purpose? If they do, the terminology Congress used in 1942 is meaningless, in that they would have the power, through Article 1, Section 8, to take the money anyway. If they do not, can Congress arbitrarily change the definition of **commercial net-income**, in relation to the scope of the Statute, in order to levy a tax upon the gross annual “wages” of the common law, labor for hire, employee?

Or, were the common law, labor for hire, employees given the option to not participate in the “Victory Tax” program, thereby avoiding the filing of a tax return and becoming a “taxpayer”? If they were not given that choice, does the law comply with the due process requirements of the 5th Amendment? [FN-15] This can only be determined by reviewing the instructions that accompanied the 1942 certificate.

Next, we requested a copy of the 1943 W-4 withholding certificate and instructions, because Congress repealed the 1942 legislation and re-implemented the same

requirements, with specific changes to the definition of “wages”. They also change the name from “Collection of Tax at Source on Wages” to “Collection of Income Tax at Source on Wages”. They relocated the withholding provisions out of Chapter 1 and into Chapter 9, without requiring a new withholding certificate to be filed, and provided for the refunding of “taxes” paid by “honest mistake” as to liability. [FN-16]

Why were these changes made if the exercise of the taxing power was valid under the Statute imposing a tax upon commercial net income? If all “wages” were, in fact, considered to be “net-income,” what did Congress mean, in the 1942 withholding provision, by “wages” that are “includible in gross income” (Sec. 466 (a))? Unless, of course, **gross income wages** are “exempt under the law from the tax imposed by Chapter 1 of the code,” as implied in all three of the 1943 Committee Reports.

The income tax is imposed by the operation of the Statute, that is, the legislation passed by Congress, not by the wording of the 16th Amendment. Just because something might be “income,” in the accepted common speech usage of that word, it does not follow that Congress imposed a tax upon it. [FN-17] Congress specifically identified, in 1913, the type of “income” they chose to tax, and until Congress chooses to change that specific type of “income,” it remains as the sole basis for the tax imposed by the Statute [FN-18].

However, Congress knew that a loophole existed in the Statute. That the sole-proprietor or independent contractor could pay themselves “wages” and avoid the “income tax” altogether. How did Congress close that loophole, and at the same time keep the income tax a valid excise upon “gains and profits,” in accordance with court’s definition of “income” under the 16th Amendment?

Answer: Congress, in 1943, re-defined “wages” under section 1622 (a), in relation to the withholding provisions, by removing the reference in section 466 (a) to “that such wages are includible in gross income.” However, they did not change section 465 (b) (1621 (a)) to remove the reference to “IF paid as compensation for services”. [FN-19] Who’s “services” were they talking about, under the commercial net income provision of the Statute in existence at the time? Do all employees “provide services,” for which they receive commercial net income in exchange? Or do most employees provide labor, in order for their employers to “provide services” to the public for profit? [FN-20]

Under Supplement T, “Compensation for personal services” related to the money the individual paid to themselves out of the gross receipts of the commercial or financial activity they were engaged in. Such compensation, in effect, being a portion of the yearly net-income derived from the commercial activity, not the gross income or annual receipts produced by that activity. Salaries, on the other hand, usually represented a substantial amount of compensation, generally allowing the individual the opportunity to invest in profit making ventures, from which they became liable for the tax imposed upon **commercial net income**. The term “wages” was a wild card, in that it could mean any of the above, or, it could mean the gross annual receipts of the common law, labor for hire, employee.

IF there was not some sort of a legal problem with withholding on everyone's "wages," it would seem there would have been no need for the "clarifying amendment" discussed in all three Committee Reports attached to The Current Tax Payment Act of 1943.

The common law, labor for hire, employee provides labor to his employer in exchange for annual receipts, such receipts are called "wages". The employer, on the other hand, "provides services" to those who patronize his business in exchange for annual receipts, from which he pays himself compensation for the personal services rendered (wages). Unless the common law, labor for hire, employee is, in fact, a sole-proprietor or independent contractor paying themselves "compensation" out of their yearly "wages," how are their annual receipts converted to **commercial net-income** in compliance with the Statute's power and authority? It can not be done arbitrarily, by allowing an amount from wages, as accomplished through the use of Supplement T.

What method did Congress provide for distinguishing between the two types of "wages"? So that the "income" tax was properly collected from those who owed the "excise" tax levied upon **commercial net income**, and not from those who were "exempt" from the excise tax imposed by Chapter 1? The "withholding" provisions did not create a new "tax," they simply implemented a collection method for the "excise tax" upon commercial net income imposed by Chapter 1 of the 1939 I.R.C.

This was the reason for our request for determination of status under Subtitle A of the current Tax Code. Are we, as common law, labor for hire, employees, working for County government, in fact, sole-proprietors or independent contractors in compliance with 26 USC 7701 (a) (1) and Section 6001, 6011 and 6012? [FN-21] If so, give us the specific court case, or cases, in which the Supreme Court has made that determination. If not, where is the authority, other than that based upon the filing of a W-4 certificate, to classify us as taxpayers?

The third item we asked for was the 1944 "Revised" withholding certificate and the accompanying instructions. Why? Because Congress required everyone, whether or not they had a current valid withholding certificate on file or not, to re-file the new certificate. [FN-22] What purpose did that serve? Was it done in an effort to allow the common law, labor for hire, employee the opportunity to refute, or acknowledge, the "liability" for the tax imposed by Chapter 1? If so, how did the Treasury Department word that certificate so that both the employee and the employer knew whether or not they were required to withhold from the paycheck?

In 1944 the "Victory Tax" was repealed, meaning there was no longer a "gross income" basis for the collection of the enforced savings "tax". Without the "gross income" basis, how was Congress going to continue collecting a "**commercial net-income tax**" from the common law, labor for hire, employee's gross annual receipts (wages)?

Answer. They created the "new concept" of adjusted gross income, under the "**commercial net income**" provisions of the existing Statute. [FN-23] This "new

concept,” by the way, confused everyone, even the judges administering the tax laws [FN-24]. Remove Section 62 from the Internal Revenue Code and nothing changes, at least, as far as the computation of the amount of tax liability. Why? Because the current Law is in pari-materia with all the previous Revenue Acts imposing the excise tax liability upon the basis of “net-income”. [FN-25]

What would change, is the removal of the common law, labor for hire, employee’s gross annual wages from line 7 of the 1040 tax return; as the sole reason for incurring the tax liability imposed upon line 22. [FN-26] This is not saying that IF the “individual” has other **net**-income to report, their wages would still be exempt. It is saying that BECAUSE they have other **net**-income to report, their wages are includible on line 7 in the report of gross **net** income, i.e., line 22 of the 1040 tax return. The balance between the two types of “income” is reliant upon the adequacy of the personal exemption allowance in relation to the actual cost of living and maintaining a household [FN-27].

The questions we presented are directly related to 26 USC 3402 (n), “*Employees incurring no income tax liability*” and the fact that Congress provided for, under Section 3770 (c), “*honest mistakes*” as to the liability for the **excise** tax imposed upon commercial net income.

When did these provisions enter the withholding requirements implemented under the Internal Revenue Code? Was it before, during, or after 1943? We believe they did not exist before the Revised Certificate of 1944, after most employees had been paying the “Victory” tax. If Subsection (n) entered the Code after 1943, and the employee had been paying the tax in question, they could not qualify as “exempt” under the current wording of that section, unless they filed for a refund of the previous years tax on the basis of “honest mistake”. [FN-28] It is doubtful that many, or any for that matter, common law, labor for hire, employees understood the nature and purpose of the Federal Income Tax during the war years. Why should they? Their government needed the money to fight the war and they were proud to contribute. Only the 1944 Revised instructions and certificate can answer these questions.

It has always been understood that Congress had the authority to “exclude” items or amounts of income from the operation of the excise tax upon “income”. This is simply a virtue of having the power to tax and has nothing to do with “liability”. [FN-29] However, it is just as well understood that Congress does not have the power to include items or amounts of income within the operation of the excise tax which are specifically “exempted” by the wording of the Statute or in compliance with the 16th Amendment requirements. [FN-30]

It seems to us that the purpose of Section 3402 (n) was to provide a method of communication as to actual liability for the tax imposed by Chapter 1. IF the employee had other forms of net-income upon which the tax operated, they could provide for the required amount of tax through withholding on their “wages,” rather than having to set aside an amount in a savings account. If they did not have any “income” falling within the requirements of Chapter 1, they could report their wages as “exempt” and thereby

avoid the withholding from their paycheck and the filing for a refund of taxes paid in error.

We are, therefore, requesting that the Department of Justice furnish to us copies of the 1942, 1943, and 1944 “revised” W-4 certificate and instructions. We also request a complete copy of the Senate Finance Subcommittee Hearings of August 19-22, 1942, as entered into the Congressional Record of October 9, 1942, page 7992, by Senator Danaher. What was Senator Clark talking about when he said:

“Of course, you withhold not only from taxpayers but non-taxpayers.”

What point was Congressman Jenkins making by his statement on page 3979, of the May 3, 1944 Record, when he stated:

“Not only our experts and the Treasury experts, but other experts outside say that if we do that we are going to relieve from taxation 11 or 12 million people who are now paying taxes and who are making no strenuous objections to it.”

Who were those 11 or 12 million people, and why would they be relieved from paying the tax by combining all three tax bases into one?

Respectfully Submitted,

John Gary Given

Michele Louise Given

FOOTNOTES

[FN-1]: Graphs 1,2, and 3 attached to and made part of our suit for refund. Congressional Record of May 3, 1944, page 3979, statement of Congressman Jenkins in reference to the 1942 “Victory Tax”: “Up to that time many people escaped taxation, not willfully, maliciously, and illegally, but the tax structure was such that they were not brought within the purview of the law.”

[FN-2]: 56 Statutes at Large, Chapter 619, October 21, 1942, page 884, Section 172. Temporary Income Tax on Individuals:

“There shall be levied, collected, and paid for each taxable year beginning after December 31, 1942, a victory tax of 5 per-centum upon the victory tax net income of every individual (other than a nonresident alien subject to the tax imposed by section 211 (a)).”

[FN-3]: Congressional Record of 1942, H.R. 7378; House Report No. 2333, July 14, 1942; Senate Report No. 1631, October 2, 1942; Conference Report No. 2586, October 19, 1942

[FN-4]: 56 Statutes at Large, Chapter. 619, pg. 884, Section 172, Temporary Income Tax on Individuals, Section 451. Victory Tax Net Income:

“(a) Definition—The term ‘victory tax net income’ in the case of any taxable year means (except as provided in subsection (c)) the gross income for such year (not including gain from the sale or exchange of capital assets as defined in section 117, or interest allowed as a credit against net income under section 25 (a) (1) and (2), or amounts received as compensation for injury or sickness which are included in gross income by reason of the exception contained in section 22(b) (5)) minus the sum of the following deductions: (1) Expenses allowed by section 23 (a) (1) and (2); (2) Interest; (3) Taxes; (4) Losses; (5) Bad debts; (6) Depreciation; (7) Depletion; (8) Pension Trusts; (9) Net operating loss; (10) Amortization; (11) Alimony; (12) Special Deductions; (13) Estates and Trusts

(b) Items Not Deductible—The deductions allowable by subsection (a) shall be subject to the limitations contained in section 24 and Supplement J and, in the case of nonresident aliens subject to the victory tax, shall be subject to the limitations contained in Supplement H.

(c) Supplement T Taxpayers—If for any taxable year a taxpayer makes his return and pays the tax under Supplement T, the term ‘victory tax net income’ means gross income for such year.”

[FN-5]: 56 Statutes at Large, Chapter 619, pg. 887, Part II—Collection of Tax at Source on Wages, Sec. 466 (a). Requirement of Withholding:

“(a) Requirement of Withholding.—There shall be withheld, collected, and paid upon all wages of every person, to the extent that such wages are includible in gross income, a tax

equal to 5 per centum of the excess of each payment of such wages over the withholding deduction allowable under this part.”

[FN-6] Federal Register of March 31, 1943, Volume 8, page 3901, Treasury Decision 5249, section 19.466-1 (b): Wages Includible In Gross Income

“Under the provisions of section 466, wages are subject to withholding only if and to the extent includible in gross income. The term “includible in gross income” as it relates to wages from which the tax is required to be deducted and withheld refers only to the taxability of the income. Thus, if an item of wages constitutes gross income under provisions of section 22, it is includible in gross income within the meaning of this section and is subject to withholding.”

[FN-7]: Federal Register of Wednesday, November 3, 1943, Volume 8, page 14882, Treasury Regulation 111, subsection 29.21-1 Meaning of Net Income:

“29.21-1 Meaning of Net Income.—The tax imposed by chapter 1 is upon income. Neither income exempted by statute or fundamental law, nor expenses incurred in connection therewith, other than interest, enter into the computation of net income as defined in section 21. (a) Income (in the broad sense), meaning all wealth which flows in to the taxpayer other than a mere return of capital. It includes the forms of income specifically described as gains and profits, ... (b) Gross income, meaning income (in the broad sense) less income which is by statutory provision or otherwise exempt from the tax imposed by chapter 1. (c) Net income, meaning gross income less statutory deductions, the statutory deductions are in general, though not exclusively, expenditures, other than capital expenditures, connected with the production of income. (d) Net income less credits. The normal taxes and surtaxes imposed on individuals and on corporations are computed upon net income less certain credits. Although taxable net income is a statutory conception, it follows, subject to certain modification as to exemptions and as to deductions for partial losses in some cases, the lines of commercial net income. Subject to these modifications statutory net income is commercial net income. This appears from the fact that ordinarily it is to be computed in accordance with the method of accounting regularly employed in keeping the books of the taxpayer.”

[FN-8]: Senate Report 1631, H.R. 7378, October 2, 1942, page 6, II Victory Tax and pages 162-165 Section 174. Temporary Income Tax on Individuals. 56 Statutes at Large, Chapter 619, page 892, Part III—Expiration Date and Definitions, Section 475 (a):

“NET INCOME—When used in this **title**, where not otherwise distinctly expressed or manifestly incompatible with the intent thereof, the term “net income” shall be construed to mean “victory tax net income” for the purposes of this **subchapter**.

[FN-9] *Lukhard v. Reed*, 481 U.S. 368, 374 (1987):

“This argument begins from the premise that since personal injury awards are purely compensatory, they do not result in any gain to their recipients. And since both general and legal sources define “income” as involving gain, see, e. g., Webster’s Third New

International Dictionary 1143 (1976) (“a gain or recurrent benefit that is usually measured in money...”); 42 C. J. S., Income, p. 531 (1944) (“in common speech ‘income’ generally is understood as gain or profit...” (footnote omitted); *Eisner v. Macomber*, 252 U.S. 189, 207 (1920) (“Income may be defined as the gain derived from capital, from labor, or from both combined, provided it be understood to include profit gains through a sale or conversion of capital assets...” (quoting *Stratton’s Independence, Ltd. V. Howbert*, 231 U.S. 399, 415 (1913); *Doyle v. Mitchell Brother’s Co.*, 247 U.S. 179, 185 (1918))), respondents conclude that personal injury awards cannot fairly be characterized as income. ... More importantly, however, as Lukhard and the Secretary point out, general and legal sources also commonly define “income” to mean “any money that comes in,” without regard to any related expenses incurred and without any requirement that the transactions producing the money result in a net gain. See, e. g., *Oxford English Dictionary* 162 (1933) (“That which comes in ... (considered in reference to its amount, and commonly expressed in money); ... receipts ...”)

[FN-10]: Congressional Record of May 4, 1944, remarks of Congressman Cooper, page 4014: “The withholding is not a tax. It is just a method of collecting the tax that the taxpayer owes, whether you collected it by withholding or any other method.”
Baral v. United States, District of Columbia No. 98-1667, February 22, 2000.

[FN-11]: 54 Statutes at Large, Chapter 419, page 519, June 25, 1940, H.R. 10039, Section 7 Returns of Income Tax; Congressional Record H.R. 10039; House Report No. 2491, June 10, 1940; Senate Report No.1856, June 15, 1940; Conference Report No.2697, June 21, 1940; 55 Statutes at Large, Chapter 412, H.R. 5417, page 689, September 20, 1941, Section 102. Optional Tax on Individual with Certain Gross Income of \$3,000 or Less; House Report No. 1040, July 24, 1941; Senate Report No. 673 Parts 1-4, September 2, 1941; Conference Report No. 1203, September 15, 1941, Congressional Record H.R. 5417. [The Act of 1940 changed the filing requirement under section 51 from a basis of net-income to a basis of gross income. The Act of 1941 introduced Supplement T as an optional way of computing and paying the net income tax imposed under sections 11 and 12 of chapter 1]

[FN-12]: Congressional Record of August 28, 1913, H.R. 3321, page 3844, statement of Senator Cummins: “when it is declared in the first lines of this bill that a tax is levied upon the entire net income of all the citizens of this country, we have exercised all the power we have.”

Treasury Regulation 45, Article 21 (1918); Treasury Regulation 103 (1939), Sections 19.1-1 and 19.21-1; Treasury Regulation 111 (1942), Sections 29.1-1 and 29.21-1; Treasury Regulation 118 (1953), Sections 39.1-1 and 39.21-1

[FN-13] *Heiner v. Donnan*, 285 U.S. 312, 329 (1932):

“that a constitutional prohibition cannot be transgressed indirectly by the creation of a statutory presumption any more than it can be by direct enactment. The power to create presumptions is not a means of escape from constitutional restrictions.”

[FN-14]: Congressional Record of October 20, 1942, page 8468, the remarks of Congressman Doughton, Chairman of the House Ways and Means Committee: “The Victory Tax will greatly increase the number of persons who will pay a direct tax to the Government—a direct contribution to the war effort.”

[FN-15]: *United States v. Romano*, 382 U.S. 136 (1965), *Tot v. U.S.*, 319 U.S. 463 (1943):

“The test to be applied to the kind of statutory inference involved in this criminal case is not in dispute. In *Tot v. United States*, 319 U.S. 463, the Court, relying on a line of cases dating from 1910, reaffirmed the limits which the Fifth and Fourteenth Amendments placed “upon the power of Congress or that of the state legislature to make the proof of one fact or group of facts evidence of the existence of the ultimate fact on which guilt is predicated.” *Id.*, at 467. Such legislative determination would not be sustained if there was “no rational connection between the fact proved and the ultimate fact presumed, if the inference of the one from the proof of the other is arbitrary because of lack of connection between the two in common experience...[W]here the inference is so strained as not to have a reasonable relation to the circumstances of life as we know them, it is not competent for the legislature to create it as a rule governing the procedure of the court.”

[FN-16]: Congressional Record of 1943, H.R. 2570 The Current Tax Payment Act of 1943; House Report No. 401, April 30, 1943; Senate Report No. 221, May 10, 1943, page 34 “Rule where no tax liability”; Conference Report No. 510, May 28, 1943, page 48.

[FN-17]: *Eisner v. Macomber*, 252 U.S. 189, 206: As repeatedly held, this did not extend the taxing power to new subjects, but merely removed the necessity which otherwise might exist for an apportionment among the States of taxes laid on income.”

[FN-18]: Treasury Regulation 118, Subsection 39.22 (a) –1 (a): “In general, income is the gain derived from capital, from labor, or from both combined”

[FN-19] Federal Register of March 31, 1943, Volume 8, page 15211, Treasury Decision 5249, section 19.465-2 Wages:

(a) In general, the term “wages” means all remuneration for services performed by an employee for his employer unless specifically excepted under section 465 (b) or section 466 (g).

The name by which the remuneration for services is designated is immaterial. Thus, salaries, fees, bonuses, commissions on sales or on insurance premiums, pensions, and retired pay are wages within the meaning of the statute **IF paid as compensation for services** performed by the employee for his employer.”

Section 466 (g): Included and excluded “wages”. If the remuneration paid by the employer to an employee for services performed during one-half or more of any pay-roll period constitutes wages, all remuneration paid by such employer to such employee for such period shall be deemed to be wages; but if the remuneration paid by the employer to employee for services performed during more than one-half of any such pay-roll period

does not constitute wages, then none of the remuneration paid by the employer to such employee for such period shall be deemed to be wages.”

Section 1622, “Income Tax Collected at Source (57 Stat. Ch. 120 (1943) pg. 128)
“(a) Requirement of Withholding—Every employer making the payment of wages shall deduct and withhold upon the wages a tax equal to the greater of the following:”

See Treasury Regulations 115, published September 7, 1973, Volume 8, page 12262, Part 404—Collection of Income Tax at Source on Wages; and Regulation 116, published December 14, 1944, Volume 9, page 14573, Part 405—Collection of Income Tax at Source on Wages.

[FN-20]: Taxing the Exercise of Natural Rights by John M. Maguire, Harvard Legal Essays 1934. Cited by the Supreme Court in *Steward Machine Co v. Davis* 301 U.S. 548, 580.

Senate Report 221, H.R. 2570, page 17; Federal Register, November 3, 1943, Treasury Regulation 111, page 15211, subsection 29.465-2; 26 CFR 31.3401(a)-1(a)(2) (1996)

[FN-21]: 26CFR301.7701-2. Business entities; definition (a)....

“A business entity with only one owner is classified as a corporation or is disregarded; if the entity is disregarded, its activities are treated in the same manner as a sole-proprietorship, branch, or division of the owner.”

[FN-22]: 58 Statutes at Large, Chapter 210, May 29, 1944, page 254 (e) New Withholding Exemption Certificates To Be Furnished (1) Old Certificates Made Ineffective (2) Requirement of Furnishing New Certificate

[FN-23]: 58 Statutes at Large, Chapter 210, Section 8, Adjusted Gross Income; Congressional Record H.R.4646; House Report No. 1365, April 24, 1944, page 3, page 22 Section 8; Senate Report No. 885, May 16, 1944, page 3, page 20 section 5, page 24 section 8

[FN-24]: 14-TC-943, May 26, 1950, *Chapman v. C.I.R.*:

“The tax as shown opposite a taxpayer’s “adjusted gross income” in the tax table contained in section 400 of Supplement T of the Internal Revenue Code is a tax computed on the taxpayer’s “**net**-income,” arrived at by allowing deductions substantially equal to 10 per cent of the taxpayer’s gross income, his personal exemption, and credits for dependents.”

See also, *United States v. Gilmore*, 372 U.S. 39, 42 (1963):

“For income tax purposes Congress has seen fit to regard an individual as having two personalities; “one is [as] a seeker after profit who can deduct the expenses incurred in that search; the other is [as] a creature satisfying his needs as a human and those of his family but who cannot deduct such consumption and related expenses.”

And, *Noland v. C.I.R.*, 269 F2d 108, 111 [2-3] (1959):

“We start with the assumption that every person who works for compensation is engaged in the business of earning his pay, ...”

[FN-25]: Congressional Record of 1954, H.R. 8300, The Internal Revenue Code of 1954; House Report No. 1337, March 9, 1954, Detailed Discussion of the Technical Provisions of the Bill, pages A-9 Section 1. Tax Imposed, A18 to A20 Subchapter B—Computation of Taxable Income, sections 61, 62, and 63; Senate Report No. 1622, June 18, 1954, Detailed Discussions, pages 159 and 168 to 170; section 63. Taxable Income Defined:

“This change in the term ‘net-income’ as used in section 21 of the 1939 Code to ‘taxable income’ creates a new concept. It eliminates terms such as ‘normal tax net income,’ ‘surtax net income,’ in the case of individuals, and ‘adjusted net income,’ ‘normal tax net income,’ and ‘corporate surtax net income,’ in the case of corporations and ‘net income’ for both individuals and corporations. The change in language clarifies the tax base. It eliminates the necessity for credits against net income and exemptions which become deductions in arriving at ‘taxable income’ for both corporations and individuals.”

[FN-26]: Study of the Overall State of the Federal Tax System and Recommendations for Simplification, Pursuant to Section 8022 (3) (B) of the Internal Revenue Code of 1986. Volume II, Part III: Recommendations of the Staff of the Joint Committee on Taxation to Simplify the Federal Tax System. Section II, Individual Income Tax, A (6) Above the line deductions and itemized deductions.

“A taxpayer’s adjusted gross income is determined by subtracting certain deductions from gross income. These deductions are commonly referred to as “above the line” deductions and are allowed to all taxpayers, including those who do not itemize deductions. A taxpayer calculates taxable income by subtracting either the standard deduction or allowable itemized deductions from adjusted gross income. In general, taxpayers choose to itemize their deductions if the total amount if itemized deductions exceeds the standard deduction. ...”

Present law does not reflect a coherent theory for treating some deductions as above the line and some deductions as itemized deductions. Although above the line deductions are frequently thought of as deductions related to the production of income and itemized deductions are frequently thought of as reflecting ability to pay or encouraging certain behavior, not all deductions can be accounted for under these principles. For example, the above the line deduction for contributions to medical savings accounts is not related to the production of income. Rather, the deduction is intended as an incentive to encourage taxpayers to alter the way in which they purchase medical care in an effort to help reduce overall medical costs. Similarly, not all expenses that are related to the production of income are above the line deductions. For example, employee business expenses are allowable only as an itemized deduction (subject to the two-percent floor on itemized deductions).”

See also; *Alexander v. Internal Revenue Service*, First Circuit No. 95-1451 (1995), and *Ware v. United States*, Sixth Circuit 94-1293 (1995 FED App. 0308P (6th Cir.))

[FN-27]: <http://waysandmeans.house.gov/legacy.asp?file=legacy/fullcomm\107cong\2-13-01\record\given.htm> Letter to Allison Giles, Staff Director, Committee on Ways and Means, February 6, 2001

[FN-28]: 26 CFR 31.3402 (n)-1 Employee incurring no income tax liability
“Notwithstanding any other provision of the subpart, an employer shall not deduct and withhold any tax under chapter 24 upon the payment of wages made to an employee after April 30, 1970, if there is in effect with respect to the payment a withholding exemption certificate furnished to the employer by the employee which contains statements that—
(a) The employee incurred no liability for income tax imposed under subtitle A of the Code for his preceding taxable year; and
(b) The employee anticipates that he will incur no liability for income taxes imposed by Subtitle A for his current taxable year.

[FN-29] *Pittsburgh v. Alco Parking Corp.*, 417 U.S. 369 (1974)
“The fact that a tax is so excessive as to render a business unprofitable or even threaten its existence furnishes no ground for holding the tax unconstitutional.”

[FN-30] *South Carolina v. Baker*, 485 U.S. 505, 516 (1988):
“The United States cannot convert an unconstitutional tax into a constitutional one simply by making the tax conditional. Whether Congress could have imposed the condition by direct regulation is irrelevant; Congress cannot employ unconstitutional means to reach a constitutional end