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WHAT A HISTORY OF TAX WITHHOLDING TELLS US ABOUT THE RELATIONSHIP BETWEEN STATUTES AND CONSTITUTIONAL LAW

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ABSTRACT—In this Article, I explain what a seemingly obscure statute, the Current Tax Payment Act of 1943, can tell us about the relationship between statutes and constitutional law. I use William Eskridge and John Ferejohn's notion of a "superstatute" as a lens through which to view this relationship. A "superstatute," in Eskridge and Ferejohn's conception, is a statute that has small "c" constitutional emanations, emanations that both affect interpretations of the large "C" Constitution and are entrenched against subsequent legislative change. To better understand the precise contours of the notion of a superstatute, I look at the Current Tax Payment Act of 1943, which instituted the system of federal tax withholding for wage income. I describe the history of federal income tax withholding leading up to the passage of that Act, explaining in turn how that history sheds light on the underlying notion of a superstatute.

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INTRODUCTION: ENTRENCHMENT, STATUTES, AND SUPERSTATUTES

Entrenchment. It's the holy grail of constitutional theory. How exactly does a "constitution" entrench values, policies, or what have you, such that a democratically elected majority is—or, ought to be—precluded from promulgating a currently desired policy preference? In the modern American context, that question is of course often asked by framing the problem as the countermajoritarian difficulty—when can an unelected judiciary override an elected legislature? We might reformulate the problem in slightly less institutionally oriented terms and think of it—as Chief Justice Marshall first articulated it and many Americans remain wont to do—as a question of when the words of a Constitution, ratified by a group of Americans in 1787–1788 and amended twenty-something times since then (in accordance with procedures for amendment ratified at that same initial "moment" in 1787–1788), conflict with the words of a statute and must thus necessarily override that statute.[1] Of course, things have always been more complicated, even in Chief Justice Marshall's day, but it can still be said that a single, focused written document that purports to entrench—at a single moment—a "higher" law remains one of the United States' most lasting contributions to legal and political theory.[2] The magic of that entrenchment is of course the source of endless fascination and is why some of our greatest legal minds have spent their careers grappling with this fundamental question: when should judges use the Constitution to entrench a legal principle so as to make it more difficult for legislation to

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[1] *See* Marbury v. Madison, 5 U.S. (1 Cranch) 137, 177–78 (1803) ("It is emphatically the province and duty of the judicial department to say what the law is. Those who apply the rule to particular cases, must of necessity expound and interpret that rule. If two laws conflict with each other, the courts must decide on the operation of each. . . . If then the courts are to regard the constitution; and the constitution is superior to any ordinary act of the legislature; the constitution, and not such ordinary act, must govern the case to which they both apply.").

[2] *See* JACK RAKOVE, REVOLUTIONARIES: A NEW HISTORY OF THE INVENTION OF AMERICA 159 (2010) (noting that the American Revolution's "most lasting legacy . . . was the great innovation that treated a constitution not as a working description of a government but as a single authoritative document, written at a known moment of historical time, under rules that made it legally superior to all the other acts that the government it created would subsequently adopt").

change law? Or, more descriptively, what factors entrench the Constitution—that is, why do judges decide to invalidate laws as unconstitutional?

William Eskridge and John Ferejohn's recent book *A Republic of Statutes* is a refreshing twist on this theme: they completely reframe the question of entrenchment. No longer is entrenchment simply an unelected judiciary overriding an elected legislature or executive. Instead, entrenchment becomes a more complex phenomenon, whereby statutes—the product of legislatures themselves—can in turn act to bind future legislatures. Simplistic American constitutional theory cannot abide such complexity. Under the basic later-in-time rule, a statute can always be repealed by a subsequent legislature. The principle dates to Roman times and is found clearly in Blackstone: "Acts of parliament derogatory from the power of subsequent parliaments bind not."[3] Only "the Constitution" can entrench; only the Constitution itself can prevent a legislature from making change. Statutes cannot entrench because they cannot be made unrepealable. This relationship between past statutes and the present legislature is not inevitable, though it often seems to be so. Just ask Britain. Until recently, its "Constitution" included a series of statutes, and notwithstanding the basic premise of parliamentary sovereignty, these statutes were viewed as sacrosanct, if not entrenched.[4]

A fundamental part of what Eskridge and Ferejohn have done is to reframe what a statute is and can be. And, like all brilliant ideas, this reframing changes the way you see a statute and does so in a way that simply cannot be undone. As Eskridge and Ferejohn put it on the very first page of their book, "Our framework . . . reveals how [statutes, executive orders, congressional–executive agreements, and agency rules] have become entrenched, indeed to the point of molding the Constitution itself."[5] The book is nearly 600 pages long and contains nine chapters, each on a completely different area of law, from rights-based statutory schemes, such as the Pregnancy Discrimination Act of 1978 and Voting Rights Act, to aspects of market regulation, such as the Sherman Act, to structural aspects of the economy, such as the Federal Reserve Act of 1913. Yet, the book has nary a mention of tax law. This is not, I suspect, because they think there are no entrenched tax laws, but instead because they had already written so much. In this Article, I want to look at one, almost invisible, part of tax law

[3] 1 WILLIAM BLACKSTONE, COMMENTARIES *90. For a debate on whether the legislature can bind a future legislature, see Eric A. Posner & Adrian Vermeule, *Legislative Entrenchment: A Reappraisal*, 111 YALE L.J. 1665 (2002), arguing yes, and John C. Roberts & Erwin Chemerinsky, *Entrenchment of Ordinary Legislation: A Reply to Professors Posner and Vermeule*, 91 CALIF. L. REV. 1773, 1777 (2003), arguing no.

[4] *See* ERIC BARENDT, AN INTRODUCTION TO CONSTITUTIONAL LAW 26–34 (1998).

[5] WILLIAM N. ESKRIDGE JR. & JOHN FEREJOHN, A REPUBLIC OF STATUTES: THE NEW AMERICAN CONSTITUTION 1 (2010).

and ask whether it has been "entrenched" in Eskridge and Ferejohn's meaning.

Let me start with Eskridge and Ferejohn's definition of "entrenchment":

> We use the term "entrenched" to refer to norms and practices that are accepted not just because of their Weberian authority to command but also because of the force of a Weberian constellation of interests, namely, *a popular consensus that the norm or practice is a good thing to believe or do*.[6]

Their emphasis is on the ways in which both formal law and social norms "entrench." They describe the "process of deep entrenchment" as having three features: (1) public deliberation; (2) several institutions involved in that deliberation, both cooperating and protecting their own authority; and (3) deliberation that occurs "over a long period of time" and "does not stick . . . until former opponents agree that the norm is a good one" (or at least acceptable).[7] They then dub a statute that is entrenched through this sort of public deliberation a "superstatute."

Though Ferejohn had previously been a Professor of Social Science (at CalTech) and Political Science (at Stanford),[8] Eskridge and Ferejohn probably do not mean their theory to be grounded in social science. The book interweaves the descriptive and the normative too easily and does not really provide a testable hypothesis. This is not a criticism per se: they are law professors after all. Moreover, their goal is to complicate the standard account of how both constitutional and statutory law operate at the level of actual legislatures and courts. Still, their formulation raises questions about how closely their definition matches their own conclusions. In particular, are all laws that satisfy Eskridge and Ferejohn's three features entrenched, while those that fail to satisfy the three features not entrenched? Or, are these "features" just characteristics that entrenched statutes sometimes share? If the former, we have the beginnings of a testable hypothesis. If the latter, we merely have a way to begin thinking about how we might construct a testable hypothesis.

Moreover, if we take Eskridge and Ferejohn's "three features" of entrenchment seriously, I think we also want to know how closely their definition matches one's intuitive sense of what the concept entails: "entrenched" as something that is "establish[ed] so firmly that change is difficult."[9] For, as Adrian Vermeule has noted, Eskridge and Ferejohn's conception of entrenchment differs from the way in which the term is usually used in constitutional scholarship—something that a current

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6 *Id.* at 13 (emphasis added).

7 *Id.* at 7.

8 *John A. Ferejohn: Biography*, N.Y.U. SCH. L., https://its.law.nyu.edu/facultyprofiles/profile.cfm?section=bio&personID=19914 (last visited May 18, 2014).

9 CONCISE OXFORD ENGLISH DICTIONARY LUXURY EDITION 477 (12th ed. 2011).

majoritarian institution is prohibited from changing. As Vermeule puts it, "The acid test of entrenchment occurs when a statute survives *despite* the opposition of a current majority or supermajority."[10] After all, if Eskridge and Ferejohn's references to social norms are to be understood properly, their principal point is that the current majority does not want—or seek—to change the laws they describe as being entrenched.

If we compare what on the surface is the way in which entrenchment is defined, we see Eskridge and Ferejohn's theory and Vermeule's theory seemingly at two ends of a pole: For Vermeule, entrenchment is a de jure concept—in what circumstances is a majority that seeks change precluded as a matter of law from being able to do so? For Eskridge and Ferejohn, in contrast, entrenchment appears to be primarily a de facto concept. Once a statute becomes a superstatute, it has, according to Eskridge and Ferejohn, become part of the majority's preference set, and for that reason, has become entrenched. Vermeule's critique is trenchant though—in what sense is a statute entrenched if the majority does not *want* to change it?

Vermeule suggests ways out of the dilemma. One way is to note that a statute can sometimes engender coordination benefits, benefits that might outweigh the cost even for those who initially opposed the statute. Such a statute might thus be "entrenched" notwithstanding the opposition of a current majority. Vermeule's second suggestion, though, is of a very different ilk. Noting that "political preferences are partially endogenous," Vermeule points out that "[s]ometimes the passage of the statute . . . itself shapes" subsequent political preferences, and he acknowledges that this may be what Eskridge and Ferejohn mean with their emphasis on public deliberation.[11]

This is not only right, but also at the core of what I suspect Eskridge and Ferejohn mean with their title, *A Republic of Statutes*. The crux of Eskridge and Ferejohn's agenda is neither statutory nor constitutional law, but rather values. The core of much constitutional jurisprudence and scholarship—even among those who categorically reject a "Herculean" approach to constitutional law[12]—is in fact values. By bringing statutes into the debate about the polity's values, Eskridge and Ferejohn are attempting not simply to fiddle along the edges with the concept of entrenchment, but instead to raise our awareness that statutes can sometimes be at the core of our republic—perhaps even more so than the large "C" Constitution—because they shape values.

Thought of in those terms, Vermeule may be right about "the acid test" for entrenchment but wrong when he says that "Eskridge[] and

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10 *See* Adrian Vermeule, *Superstatutes*, NEW REPUBLIC (Oct. 26, 2010), http://www.tnr.com/book/review/superstatutes (reviewing ESKRIDGE & FEREJOHN, *supra* note 5) (emphasis added).

11 *Id.*

12 RONALD DWORKIN, LAW'S EMPIRE 239 (1986) (positing an "imaginary judge of superhuman intellectual power and patience," known as "Hercules," as the model for judging).

Ferejohn's treatment of the statutory constitution is so capacious, the boundaries of their enterprise so ill-defined, that it threatens to swallow up all of ordinary politics."[13]

If the core of Eskridge and Ferejohn's book is values, not just statutes, then the crucial point is the dialectical relationship between law and the majority's views. Vermeule clearly recognizes this last point, but seems to miss Eskridge and Ferejohn's insistence on the role of values in shaping that dialectical relationship. Perhaps I am reading too much into Eskridge and Ferejohn's account here, but the mere framing of each chapter's title not around a particular statute but around a value—"[e]quality," "[d]emocra[cy]," "the [m]arket," "the [f]amily," "[n]ational [s]ecurity"[14]—suggests that what matters to Eskridge and Ferejohn when they focus on entrenchment is not so much the entrenchment of the statute qua statute but instead the entrenchment of the values the statutes embody.

I. WAR, TAXES, AND THE WITHHOLDING SUPERSTATUTE

Eskridge and Ferejohn tell us their list of superstatutes is "nonexhaustive,"[15] but Vermeule's challenge is to articulate the category with sufficient precision that legal theorists can analyze whether a statute is a superstatute—or at least recognize one intuitively.[16] My claim in this Article includes four components: (1) a normative value is the core attribute in Eskridge and Ferejohn's conception of a superstatute; (2) to understand whether a statute is a superstatute, we have to understand the relationship between law and societal values as dialectical; and (3) societal institutions play an important role in shaping that dialectical relationship and hence whether a statute is "super"; but (4) a value embedded into a judicial interpretation of the large "C" Constitution is a crucial component of this understanding. But even this, Vermeule could rightly reply, is unhelpful with the onerous task of determining the contours of the category.

So, let me try a few examples. Daryl Levinson gives the mortgage tax deduction as an example of a politically entrenched policy,[17] but intuition tells us this is not what Eskridge and Ferejohn have in mind. I suspect the answer may, at least in part, be that the entrenchment of the mortgage interest tax deduction is premised on self-interest, not a transcendent societal value. We can see this in part by the fact that Eskridge and Ferejohn's chapter headings are designed to evoke values that can be characterized as important for "We (Us?) the People." Their references to

13 Vermeule, *supra* note 10.

14 ESKRIDGE & FEREJOHN, *supra* note 5, at v–vi.

15 *Id.* at 16.

16 *See* Vermeule, *supra* note 10.

17 Daryl J. Levinson, *Parchment and Politics: The Positive Puzzle of Constitutional Commitment*, 124 HARV. L. REV. 657, 687 (2011).

concepts such as "The Constitution of the Market and State Legitimacy" and "The Safety Net Constitution" are all attempts to frame certain statutes around broader normative values.[18] Now one could perhaps quibble about the mortgage tax deduction too. After all, who doesn't remember the "Ownership Society" principle celebrated during the presidency of George W. Bush?[19] Certainly we could easily tie the mortgage tax deduction to home ownership as a value. That, after all, remains the ostensible public policy rationale (independent, of course, of the self-interest of the millions of its beneficiaries). And, of course, the way in which it stifles mobility, which itself might be another core American value, is at least one piece of the case against it. So, values are found in the mortgage tax deduction too.

Still, the answer has to be that the statute providing for the mortgage tax deduction is not a superstatute, and the answer must lie in the way in which the value structure—again, the core of Eskridge and Ferejohn's understanding—intersects with the entrenchment process. Entrenchment here does not depend on an ideological shift that the statute either sparks or further perpetuates. Entrenchment does not depend on an underlying normative view permeating American society that exalts home ownership over mobility. Rather, it is self-interest that acts as the vehicle through which entrenchment occurs. If self-interest is driving the entrenchment, then this cannot be a superstatute.

So let me tweak Levinson's example a little, making the question tougher for Eskridge and Ferejohn. Is the Current Tax Payment Act of 1943 a superstatute? If you have never heard of the statute, don't worry. Perhaps that alone should be enough to weigh heavily, if not dispositively, against it being thought of as a superstatute. Having said that, there is a case to be made that for the vast majority of Americans, the Current Tax Payment Act of 1943 transformed their relationship with the federal government so dramatically that the statute is entrenched in the way Eskridge and Ferejohn mean. Yet, at the same time, it lacks some of the features of deep entrenchment they describe.

As I said, if you have never heard of the Current Tax Payment Act of 1943—and I am confident that Eskridge and Ferejohn, as steeped in our "republic of statutes" as they are, probably haven't either—that's okay. You have, I am sure, heard of what it did: create a system of mandatory federal tax withholding at the source of wage income.[20] The Current Tax Payment Act of 1943 established tax withholding from wage income in such a way that it is now embedded deeply into the fabric of American society. Although tax withholding was a feature of both the short-lived Civil War income tax and the first post-Sixteenth Amendment income tax

[18] ESKRIDGE & FEREJOHN, *supra* note 5, at v–vi.

[19] *See, e.g.*, STEPHEN MOORE, BULLISH ON BUSH: HOW GEORGE W. BUSH'S OWNERSHIP SOCIETY WILL MAKE AMERICA STRONGER 3–11 (2004).

[20] *See infra* Part 38.

in 1913, it was World War II, the Current Tax Payment Act, and a legislative compromise that put the country on the path to a system that now shapes the relationship between the federal government and the vast majority of the American population. Indeed, if we are looking to "constitutional" principles, we might say the Current Tax Payment Act "constitutes" that relationship. But, as Vermeule reminds us, entrenched policies do not necessarily make constitutional law.[21] As we will see, tax withholding is very different from the mortgage tax deduction, which seems almost trivially easy to reject as being either entrenched or in the category of "constitutional" law. By looking at tax withholding instead, I think we will begin to see a kernel of Eskridge and Ferejohn's insight in a slightly new—and, I hope, clearer—light.

Imagine a politician—let us call her Novera Groquest—whose sole goal is to reduce federal government revenues, *actual* government revenues, not the amount the law was written to take in. Where might our putative tax cutter look? She might think about state tax collection and note that the tax with perhaps one of the lowest collection rates is the "use tax"—the sales tax equivalent for purchases made out of state via phone, catalog, and the Internet, purchases for which tax is not collected at the source of the sale. So, for example, Amazon.com currently collects state sales tax in only a handful of states (though the list is growing), but residents of all other states with sales taxes are generally required to pay a use tax for online purchases from Amazon, in an amount equivalent to the state sales tax, directly to the state's department of revenue when filing state income tax forms at the end of the year.[22] Not surprisingly, compliance with this legally binding requirement is modest to say the least. Realizing this, Ms. Groquest might think to herself that rather than aim at the standard techniques of tax cutters—lowering rates, increasing exemptions and deductions, etc.—the best thing she could do is to eliminate tax collection at the source. And, of course, we know that one of the principal sources of federal revenue is the income tax.[23] Ms. Groquest might think that the best way to reduce *actual* revenues would be to eliminate tax collection at the source of income—i.e., employer tax withholding.

What does this have to do with constitutional law, entrenchment, or the "republic of statutes"? It suggests, I contend, that there are entrenched statutes, maybe superstatutes, and, if one stretches, even small "c"

[21] Vermeule, *supra* note 10.

[22] *See* BLACK'S LAW DICTIONARY 1597 (9th ed. 2009) (defining "use tax" as a "tax imposed on the use of certain goods that are bought outside the taxing authority's jurisdiction" and "designed to discourage the purchase of products that are not subject to the sales tax"); *see generally* 2 WALTER HELLERSTEIN ET AL., STATE TAXATION § 16.01 (3d ed. 2013).

[23] HISTORICAL TABLES, BUDGET OF THE UNITED STATES GOVERNMENT, FISCAL YEAR 2014, at 35 tbl.2.2 (2013), http://www.whitehouse.gov/sites/default/files/omb/budget/fy2014/assets/hist.pdf.

constitutional law to be found in the oddest places, embedded deep within societal institutions, often governmental institutions. In the case of income tax withholding, I am referring of course to the Internal Revenue Service (IRS) and its relationship not only to the nation's taxpaying wage earners but also to the country's employers. In particular, in this Article, I want to explore the question of whether we could call the statutory provisions that established income tax withholding a "superstatute" or entrenched or in some sense constitutional.

If we look at our current federal tax system, recent reformers have proposed numerous different types of changes—from a blanket reduction in rates combined with elimination of deductions and exemptions, to a flat tax, to a consumption tax, to filing on postcard-sized forms—but virtually no prominent reformer has proposed repealing income tax withholding.[24] The fact that almost no one wants to change this fundamental feature of the tax system suggests that it is entrenched in a de facto sense. But, income tax withholding at source is entrenched in another sense too. If one sought to argue that tax withholding is an unconstitutional taking under the Fifth Amendment or outside Congress's Sixteenth Amendment power to "collect taxes on incomes,"[25] because it is a "harbinger of state socialism"[26] or a violation of basic liberty principles for requiring employees to "disclose to employers information [about] their prospective income,"[27] that sort of constitutional claim would have very little chance of success, even though these were arguments against the constitutionality of withholding in the post-Sixteenth Amendment era. Perhaps we now see tax withholding at the source of income as embedded into the federal government's Sixteenth Amendment power. It was not, however, always so—and, in the following sections of this Article, I will show how the history of federal income tax withholding in the United States led us to the point at which federal tax withholding became entrenched.

In doing so, I would like to explore more broadly the question of whether it is possible to see a deeply entrenched policy—one that is entrenched not just because it has created an interest group, not just because it is in some trivial sense favored by a majority of Americans, and not just because it provides a coordination benefit, but primarily because of a complex array of social, institutional, and indeed cultural factors—as

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[24] *See, e.g.*, H. COMM. ON WAYS & MEANS, 113TH CONG., DISCUSSION DRAFT OF THE TAX REFORM ACT OF 2014 (2014), http://waysandmeans.house.gov/UploadedFiles/Statutory_Text_Tax_Reform_Act_of_2014_Discussion_Draft__022614.pdf (major tax reform proposal drastically reshaping federal tax law, but making no changes to withholding of taxes on wage income). *But see* Freedom and Fairness Restoration Act of 1994, H.R. 4585, 103d Cong. § 103; NEAL BOORTZ & JOHN LINDER, THE FAIRTAX BOOK: SAYING GOODBYE TO THE INCOME TAX AND THE IRS 19–30 (2005); Dick Armey, *Review Merits of Flat Tax*, WALL ST. J., June 16, 1994, at A16.

[25] U.S. CONST. amend. XVI.

[26] RANDOLPH E. PAUL, TAXATION IN THE UNITED STATES 308 (1954) (quoting Rep. Jenkins).

[27] *Id.* (citing Rep. Carlson).

small "c" constitutional when its actual large "C" constitutional emanations are so weak.

A complex array of factors has shaped people's expectations about the income tax and the meaning of the federal power embedded in the Sixteenth Amendment. Perhaps it is fair to characterize our conception of tax withholding's entrenchment as being based on the force of social norms, but that strikes me as wrong. Tax withholding is not entrenched in the way that the Civil Rights Act of 1964 is. It is true that a wave of anti-tax sentiment could lead to the end of withholding, though that might be less plausible than ending the mortgage tax deduction.[28] But, on the other hand, it strikes me as more plausible that a court could strike down aspects of the Civil Rights Act on constitutional grounds[29] than it could similarly strike down tax withholding. Neither is impossible of course, but the former is more plausible in part because it is entrenched *only*—or at least primarily—through the means of social norms, whereas tax withholding's entrenchment is embedded in an institutional context—here, the IRS. We might see this as what economist Charlotte Twight refers to (quite derisively) as "entrenchment of the machinery of government."[30]

II. A HISTORY OF U.S. INCOME TAX WITHHOLDING

The United States has had income tax withholding at source, in fits and starts, since the Civil War, but withholding's crucial moment of entrenchment took place with the Current Tax Payment Act of 1943. Before explaining this history and its connection to Eskridge and Ferejohn's conception of a superstatute, let us begin with a brief explanation of a few crucial phrases. To start, the terms "tariffs" and "customs duties" refer to taxes imposed on imports or exports. Simple economics suggests, of course, that they lead to higher prices for purchasers of the dutied products, but that fact naturally remains—in the ordinary course—hidden from the consumer. Tariffs can be contrasted with the broad category of "internal taxes" (or, as we are now familiar, the term "internal revenue"), which refers to any type of tax other than those

[28] *Cf.* H. COMM. ON WAYS & MEANS, 113TH CONG., DISCUSSION DRAFT OF THE TAX REFORM ACT OF 2014 § 1402 (2014), http://waysandmeans.house.gov/UploadedFiles/Statutory_Text_Tax_Reform_Act_of_2014_Discussion_Draft__022614.pdf (proposing reductions in maximum deduction for home mortgage interest).

[29] *See, e.g.*, Ricci v. DeStefano, 557 U.S. 557, 594 (2009) (Scalia, J., concurring) (noting that the Court may soon have to confront the question of "[w]hether, or to what extent, . . . the disparate-impact provisions of Title VII of the Civil Rights Act of 1964 [are] consistent with the Constitution's guarantee of equal protection").

[30] CHARLOTTE A. TWIGHT, DEPENDENT ON D.C.: THE RISE OF FEDERAL CONTROL OVER THE LIVES OF ORDINARY AMERICANS 127 (2002).

imposed on a nation's imports or exports.[31] Excise and sales taxes are internal taxes, but like tariffs, are imposed on transactions.[32] The term "direct tax" has acquired a distinctive meaning and become a term of art in U.S. constitutional jurisprudence.[33] Although the details of that debate are not relevant at the moment, I will use the phrase primarily as meaning a tax imposed directly on a person or property. Head (or "capitation") taxes and property (both real and personal) taxes are direct taxes. Of course, the question of whether an income tax—whether one imposed on the *income* from property (rent, dividends, interest, etc.) or labor (salary, wages, etc.)—is a "direct tax" (in the sense the Constitution uses the term) was contested in the nineteenth century.[34] For now though, I will limit the conception of direct tax so as to exclude income taxes. The phrase "income tax withholding" refers to a process by which taxes are withheld from income at source. Unsurprisingly, governments generally find that tax withholding increases compliance with laws imposing tax liability on income.[35] Income tax withholding thus makes income taxes bear a resemblance to other means of collecting taxes such as excise or sales taxes and tariffs. The phrase "current tax payment," in contrast, refers simply to a system whereby taxes are paid "currently"—in other words, at the time the relevant transaction occurs. For income tax, the phrase would thus refer to tax payment at the point at which the income is earned. Though intertwined in our modern minds with tax withholding, the concept of current tax

[31] *See* BLACK'S LAW DICTIONARY, *supra* note 22, at 1593 (defining "tariff" as "duties imposed by a government on imported or exported goods"); *id.* at 890 (defining "internal revenue" as "[g]overnmental revenue derived from domestic taxes rather than from customs or import duties").

[32] In modern parlance, the term "sales taxes" usually refers to taxes charged as a percentage of the value of the goods—ad valorem, as they say—whereas excise taxes are imposed on a unit of measure. So, broad state sales taxes—e.g., 5.5% of the value of the goods sold—are sales taxes, while taxes on cigarettes or gasoline are excise (because they are imposed on a per-pack or per-gallon basis). *See id.* at 1597 (defining "sales tax" as a "tax imposed on the sale of goods and services, usu[ally] measured as a percentage of their price"); *id.* at 646 (defining "excise tax" to include a "tax imposed on the manufacture, sale, or use of goods"); *see, e.g.*, I.R.C. § 4611(a), (c) (2012) (imposing excise tax on crude oil and petroleum products on per-barrel basis); *id.* § 5001(a)(1) (imposing excise tax on alcohol on a per-gallon basis).

[33] For a sampling of the literature on this question, see Charlotte Crane, Reclaiming the Meaning of "Direct Tax" 2 n.3 (Feb. 15, 2010) (unpublished manuscript), *available at* http://ssrn.com/abstract=1553230.

[34] *See* Pollock v. Farmers' Loan & Trust Co., 157 U.S. 429, *vacated on reh'g*, 158 U.S. 601 (1895); Springer v. United States, 102 U.S. 586 (1881).

[35] Indeed, in 1803, when Great Britain first introduced "stoppage-at-source," as withholding was known, this was precisely the rationale. Self-reporting of income "was found to depend to[o] much on the imperfection of human nature. It became unequal in the execution, and thereby defeated its own principle." AN EXPOSITION OF THE ACT FOR A CONTRIBUTION ON PROPERTY, PROFESSIONS, TRADES, AND OFFICES; IN WHICH THE PRINCIPLES AND PROVISIONS OF THE ACT ARE FULLY CONSIDERED, WITH A VIEW TO FACILITATE ITS EXECUTION, BOTH WITH RESPECT TO PERSONS CHARGEABLE, AS PERSONS LIABLE, TO THE TAX BY WAY OF DEDUCTION, AND THE OFFICERS CHOSEN TO CARRY IT INTO EFFECT 3 (London, I. Gold 1803).

payment does not inherently require withholding. One could imagine taxes being due upon receipt of the income, with the burden of paying the tax being placed on the earner, not the employer. Moreover, withholding does not necessarily imply taxes being paid "currently." For example, an assessment on the previous year's taxes could be made (let us say, by January 15th of the following year), and the tax due from that previous year could then be withheld from a worker's salary at that point, either in a lump sum if the amount is small enough or in installments. To be sure, neither of these approaches is how our income tax system works, but, as we will see, we could have set the system up in this way.[36] The fact that we intertwined tax withholding with the idea of "current payment" was part of what allowed income tax withholding to become so integrated into our income tax system.

As I explain in more detail below, one of my themes here will be to extract from Eskridge and Ferejohn's *A Republic of Statutes* the notion of administrative constitutionalism. Tax withholding is intimately connected with tax collection—it enables and facilitates tax collection. If we see tax collection as the linchpin of taxation itself, we can see that the administrative apparatus of tax collection (and perhaps even tax assessment) can be thought of in Eskridge and Ferejohn's terms as part of America's "working constitution."[37] Going further, let me suggest that the creation of an institutional structure for income tax collection—of which tax withholding is one important component—can arguably be seen as "interpreting" the Sixteenth Amendment. Inquiring whether that is enough to render the Current Tax Payment Act a superstatute with small "c" constitutional emanations—one that is entrenched in a meaningful way—will, I hope, help us better understand what entrenchment means.

In the following subsections, I look at the history of income tax withholding up to (and including) the 1943 Current Tax Payment Act. Obviously, income tax withholding requires an income tax, and understanding the way in which withholding became part of the income tax in 1943 requires some understanding of the income tax itself prior to that point. Sections A, B, and D discuss that history and explain that income tax withholding was by no means a completely new phenomenon in 1943. But, the story of income tax withholding is not complete without understanding the development of the administrative mechanism that enabled withholding. To understand that requires understanding the development of the administrative processes for the collection of Social Security taxes, for as I explain in section C, it was the fact that by 1943 withholding of Social Security taxes was an existing facet of the relationship between wage

[36] This is how withholding worked in England and Australia during the early 1940s. *See* George E. Lent, *Collection of the Personal Income Tax at the Source*, 50 J. POL. ECON. 719, 720–21 (1942).

[37] ESKRIDGE & FEREJOHN, *supra* note 5, at 9.

earners and the federal taxing authorities that made withholding administratively possible.

A. Civil War

The nation's first federal income taxes, adopted during the Civil War, included withholding as part of the tax collection machinery. As I explain in more detail, the approach to withholding in the various Civil War income tax laws depended on several salient facts: (1) treatment of withholding as a tax that was distinct from (although very similar to) the income tax; and (2) inequities between the withholding tax and the income tax, inequities that were due to the need for administrative convenience.

Although President Madison's Secretary of the Treasury Alexander Dallas had proposed a federal income tax during the War of 1812,[38] it was not until the Civil War that the United States first enacted such a tax. It should not be surprising that it was war—and a bitter and expensive one at that—that led to a federal tax innovation.[39] It was, after all, a dramatic increase in federal expenditures and the concomitant need for money that forced Congress to look for new sources of revenue. From the end of the War of 1812 until the Civil War, the federal government had received virtually all of its revenue from two sources: customs duties and public land sales.[40] There were no federal income taxes, direct taxes, or excise taxes—in short, no *internal* taxes of any kind.[41]

The war necessitated a dramatic shift in federal tax policy. Although the details of this shift are not necessary here, I want to focus on the introduction of taxes that were subject to what we would now call "withholding." The first income tax was adopted during a special session of Congress during the summer of 1861.[42] Secretary of the Treasury Salmon Chase proposed a series of new taxes, including $20 million "by direct taxes or internal duties or excises, or both."[43] Because the Constitution

[38] EDWIN R.A. SELIGMAN, THE INCOME TAX: A STUDY OF THE HISTORY, THEORY, AND PRACTICE OF INCOME TAXATION AT HOME AND ABROAD 430 (The Lawbook Exchange, Ltd. 2d ed., rev. & enl. with a new chapter 2004) (1911).

[39] *See generally* STEVEN A. BANK ET AL., WAR AND TAXES, at xii (2008) (noting that "[w]ar has been the most important catalyst for long-term, structural change in the nation's fiscal system"). The sentence in the text might need an emphasis on the word "federal." Some states had income taxes prior to the Civil War (some of which originated with colonial-era "faculty taxes"), as had both England and Prussia. *See* SELIGMAN, *supra* note 38, at 57–166, 223–42, 367–406. Robert Stanley minimizes the innovative nature of the Civil War income tax. *See* ROBERT STANLEY, DIMENSIONS OF LAW IN THE SERVICE OF ORDER: ORIGINS OF THE FEDERAL INCOME TAX, 1861–1913, at 38 (1993). Whether he is correct or not in his characterization is not crucial to me here because my focus is on federal policy.

[40] HARRY EDWIN SMITH, THE UNITED STATES FEDERAL INTERNAL TAX HISTORY FROM 1861 TO 1871, at 1 (1914).

[41] *Id.* at 1, 24; *see also* Act of Dec. 23, 1817, 3 Stat. 401 (repealing internal taxes).

[42] SMITH, *supra* note 40, at 45–48.

[43] SELIGMAN, *supra* note 38, at 431.

required that direct taxes be apportioned to the states according to their population,[44] there was intense opposition to the direct taxes from those in the agricultural West and South.[45] The unfairness of imposing a tax that would effectively place equal burdens on every single person in the country led to outcries when the bulk of the nation's wealth was in the Northeast.[46] Although Chase's proposal was vague as to exactly what form of direct tax to impose, the most common type of direct tax was a tax on real property, and the assumption was that this is what he meant.[47] If so, however, that would only make the unfairness more pronounced: a real property tax would completely exempt much of the wealth in the Northeast, because it took the form of stocks and bonds.[48] The compromise that resulted was to reduce the revenues derived from the direct tax and to adopt the first federal income tax in U.S. history.[49] This 1861 Revenue Act imposed an income tax with a 3% rate and an $800 annual exemption.[50] It covered income earned during calendar year 1861 and required payment of the tax prior to June 30, 1862.[51]

Though the 1861 Revenue Act formally went into effect immediately upon passage, the income tax portion of it was never enforced. One problem was the simple practical question of how to enforce it. An income tax was new and would require administrative machinery for collection; it would require, to start with, the hiring of new federal officials to assess and

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[44] *See* U.S. CONST. art. I, § 9, cl. 4.

[45] HEATHER COX RICHARDSON, THE GREATEST NATION OF THE EARTH: REPUBLICAN ECONOMIC POLICIES DURING THE CIVIL WAR 112 (1997); *see also* SELIGMAN, *supra* note 38, at 431 ("[T]he chief objections to the scheme consisted in the fact that it was confined to real estate, and . . . the constitutional method of levying the tax by apportionment would result in crass inequality, bearing with especial rigor upon the western states."). Of course, because most of the southern states had seceded by this point, the South's opposition was less important. Still, the special session of Congress that met during the summer of 1861 included some representatives and senators from southern states. *See* KENNETH C. MARTIS, THE HISTORICAL ATLAS OF UNITED STATES CONGRESSIONAL DISTRICTS, 1789–1983, at 95 (1982). The "sectional effects" of an income tax remained a crucial issue even in 1913 with the passage of the first post-Sixteenth Amendment income tax. *See, e.g.*, HAROLD B. HINTON, CORDELL HULL: A BIOGRAPHY 140 (1942); Cordell Hull, *Some Features of the New Income Tax Law*, *in* N.Y. STATE BAR ASS'N, PROCEEDINGS OF THE THIRTY-SEVENTH ANNUAL MEETING 121, 142 (1914).

[46] Joseph A. Hill, *The Civil War Income Tax*, 8 Q.J. ECON. 416, 418 (1894). This dividing line, including intense opposition to the income tax in the Northeast, was also a feature of the 1894 debates around the income tax that was eventually struck down in *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429, *vacated on reh'g*, 158 U.S. 601 (1895). *See* KOSSUTH KENT KENNAN, INCOME TAXATION: METHODS AND RESULTS IN VARIOUS COUNTRIES 258 (1910); SELIGMAN, *supra* note 38, at 499–508, 520–21.

[47] *See* Hill, *supra* note 46, at 418.

[48] *See* SELIGMAN, *supra* note 38, at 431–32.

[49] *See* Act of Aug. 5, 1861, §§ 49–51, 12 Stat. 292, 309–11 [hereinafter 1861 Revenue Act].

[50] *Id.* § 49, 12 Stat. at 309. $800 in 1861 was the equivalent of approximately $20,000 in 2013. *See* Morgan Friedman, THE INFLATION CALCULATOR, http://www.westegg.com/inflation (last visited May 18, 2014).

[51] *See* 1861 Revenue Act, §§ 49, 51, 12 Stat. at 309–10.

collect the tax. Although the law authorized the President and Secretary of the Treasury to create such an administrative system,[52] doing so would have been a significant task. In contrast, direct taxes—because of the constitutional requirement that they be apportioned based on state populations—could be collected directly (if you'll pardon the pun) from the state governments themselves. That way, the states could collect the tax any way they so chose, using their preexisting tax collection processes.[53] The laws imposing direct taxes during the War of 1812 had similarly permitted states to pay their apportionment in a lump sum directly to the U.S. Treasury,[54] and that is certainly how Secretary Chase envisioned collection of the direct tax.

Given this approach to collecting the direct tax, it was the income tax alone that would have required a new federal administrative system. Given Chase's skepticism that the new income tax would yield any significant revenues at all, he took no steps to enforce it.[55] In any event, Congress was scheduled to return for its regular session in December 1861—before any income tax payments were due—and both Chase and Congress recognized full well that Congress would likely have to revisit tax issues then.[56] Sure enough, by the end of 1861, events in the war made the summer predictions about needs for revenue seem woefully inadequate.

So in 1862, Congress passed a second tax law, the 1862 Revenue Act.[57] Again, the law included a wide variety of both tariffs and internal taxes and again, a crucial question involved the imposition of a direct tax. Once again, the divisions were drawn primarily on regional lines, and once again, the resulting law was a compromise between advocates of a direct tax on real property, one that would be apportioned on the basis of population, and an income tax, which would not be so apportioned. This time, though, the resulting compromise strongly favored advocates of the income tax. The direct tax "was suspended for two years," by which time "[i]t had been driven from the field by its rival, the income tax."[58]

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52 *See id.* §§ 9, 12, 12 Stat. at 296–97.

53 *See id.* § 53, 12 Stat. at 311–12; SMITH, *supra* note 40, at 46.

54 *See* Act of Jan. 9, 1815, § 40, 3 Stat. 164, 179; Act of Aug. 2, 1813, § 7, 3 Stat. 53, 71; SMITH, *supra* note 40, at 25.

55 Hill, *supra* note 46, at 420. In late 1861, prior to any collection of the 1861 Act's income tax, Chase wrote, "Considering . . . how large a proportion of incomes, after the deductions sanctioned by law, will fall within the exemption limit of $800 a year; and considering also what numerous questions will certainly perplex its assessment and collection, [the Secretary] respectfully submits to the consideration of Congress whether the probable revenue affords a sufficient reason for putting in operation, at great cost, the machinery of the act, with a view . . . to the collection of the income tax alone." U.S. DEP'T OF THE TREASURY, REPORT OF THE SECRETARY OF THE TREASURY ON THE STATE OF THE FINANCES FOR THE YEAR ENDING JUNE 30, 1861, at 15 (1861).

56 Hill, *supra* note 46, at 420.

57 Act of July 1, 1862, ch. 119, 12 Stat. 432 [hereinafter 1862 Revenue Act].

58 Hill, *supra* note 46, at 422.

Due to the need for greater revenue and the fact that the direct tax was suspended, the 1862 Act increased the income tax. The exemption was reduced to $600 and a new graduated tax—albeit, one that was only modestly progressive—was introduced. The basic rate remained at 3%, but for income over $10,000 (the equivalent of approximately $222,000 today), the rate was 5%.[59] The bill was signed into law on July 1, 1862, and among its provisions was a repeal of the income tax in the 1861 Revenue Act.[60]

This first form of what we would today call an income tax actually consisted of several different taxes, and it is here that the nation's tentative steps into withholding began. The 1862 Revenue Act contained several different titles covering what we would today view as income. The first was entitled "Railroad Bonds,"[61] and despite its name, it covered both the interest from railroad company bonds and the dividends from railroad company stock. The tax was imposed directly on the company itself,[62] not on the recipient of interest or dividends, and it consisted of a 3% tax on the interest and dividends paid by the company. The law then "authorized *and required*" the company to "deduct and withhold from all payments made . . . the said duty or sum of three per centum."[63] In other words, though the tax was strictly speaking imposed on the railroad company, the company was required to pass the tax through to its bond- and stockholders. The next title of the Act was called "Banks, Trust Companies, Savings Institutions, and Insurance Companies," and it imposed a similar 3% tax, though just on the dividends paid by such companies, again with a requirement that the companies deduct the amount from dividend payments.[64] These taxes were widely viewed as taxes on the individual, not the company.[65]

The next title in the 1862 Act was called "Salaries and Pay of Officers and Persons in the Service of the United States, and Passports."[66] This portion of the law imposed on "all salaries" of those working for the federal government, "when exceeding the rate of six hundred dollars per annum, a

[59] *Id.* For a more precise and detailed explanation, see *infra* text accompanying notes 61 to 72. To give a sense of the impact of the $600 exemption, it is worth noting how few people paid the income tax. Although figures were not kept prior to 1866, the highest percentage of the population that ever paid the tax was 1.3%. *See* STANLEY, *supra* note 39, at 40.

[60] 1862 Revenue Act, § 89, 12 Stat. at 473.

[61] *Id.* § 81, 12 Stat. at 469.

[62] Or, strictly speaking, on "any person or persons owning or possessing, or having the care or management of any railroad company or railroad corporation." *Id.*

[63] *Id.* § 81, 12 Stat. at 469–70 (emphasis added).

[64] *Id.* § 82, 12 Stat. at 470.

[65] *See* Hill, *supra* note 46, at 427.

[66] § 87, 12 Stat. at 472. Passports? Yes, the same title imposed a $3 fee for every passport issued. *Id.* Clearly, the legislative classification process has always been an inexact science.

duty of three per centum on the excess above the said six hundred dollars"—in essence, a 3% marginal tax rate on amounts over $600.[67]

The next title was called "Advertisements," and it imposed on publishing companies a 3% tax "on the gross receipts for all advertisements."[68] This of course is an ad valorem sales tax, not an income tax, and the 1862 Revenue Act also contained other ad valorem sales taxes, including on manufactured goods, in earlier titles. Though these are not income taxes, bear with me for a moment. The importance of these ad valorem sales taxes will become relevant in a moment.

Finally there was the title named "Income Duty." It imposed a tax "upon the annual gains, profits, or income of every person residing in the United States, whether derived from any kind of property, rents, interest, dividends, salaries, or from any profession, trade, employment, or vocation . . . or from any other source whatever, except as hereinafter mentioned."[69] The rate was 3% on amounts over $600 if the person's income was between $600 and $10,000 and 5% on amounts over $600 if income was above $10,000.[70] The law then provided that this "income duty" would not be levied on interest and dividends from railroad companies, dividends from banks, trust companies, etc., and salaries from the U.S. government. But, it did something more. It also excluded all "gains, profits, or income . . . derived from advertisements, or any articles manufactured, upon which specific, stamp or ad valorem duties shall have been directly assessed or paid."[71]

With this detail, we can see a few things about the nation's first assessed income tax. First, it included withholding. Second, withholding was limited to dividends from a select set of companies, bond interest from one type of company, and federal government salaries. Third, the legislation drafters created a withholding system by treating what we would today call "income" as *not* being income. Indeed, income on which withholding was not imposed was treated the same as gross receipts from

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[67] *Id.* § 86, 12 Stat. at 472.

[68] *Id.* § 88, 12 Stat. at 472.

[69] *Id.* § 90, 12 Stat. at 473.

[70] *Id.* Yes, you read that right. Congress clearly hadn't thought through the concept of the marginal tax rate. Someone with $9999 in income would pay $281.97 and someone with $10,000 in income would pay $470, amounting to a whopping 18,803% marginal rate for the ten thousandth dollar of income.

[71] *Id.* § 91, 12 Stat. at 474. Notice that this badly worded provision might have been read to exclude from income virtually all business profits, most of which were derived from some type of "article[] manufactured." One early twentieth-century scholar contended that no one took advantage of this, *see* SELIGMAN, *supra* note 38, at 438, but no one really could have, because the words "or any articles manufactured" were repealed a year later, *see* Act of Mar. 3, 1863, § 1, 12 Stat. 713, 718 (amending the 1862 Revenue Act), before any income tax payments were due. *See* 1862 Revenue Act, § 92, 12 Stat. at 474 (stating that the first "duties on incomes herein imposed" were not due until June 30, 1863).

publishers' advertising revenue. Both were excluded from the actual "income duty" in exactly the same way.[72]

This approach obviously made drafting the withholding provisions easier, but it also led to what we can easily identify as inequities. First, the interest and dividend withholding lacked a $600 exemption. Many "widows and orphans," whose sole income came from bond interest, had 3% deducted from *all* their income.[73] The flip side, of course, is that Mr. Moneybags, the financier whose income from railroad or financial institutions' stock dividends or railroad bond interest exceeded $10,000, would, according to the statute, still pay only the 3% rate.[74] The reason for these inequities, though, is probably obvious: administrative convenience. To pay the tax, the companies subject to it simply calculated a lump-sum 3% of their total interest or dividend payment. They thus had no need to keep track of the tax payments of individual stock- and bondholders, because as I noted above, the tax was strictly speaking on the company paying the interest or dividend, not on the holders of the securities.[75]

Withholding from the salaries of U.S. government officials had a similar inequity vis-à-vis the "income duty," but it was of much less practical effect. Although salary withholding did require federal paymasters

[72] These statutory classifications also mattered to the internal workings of the new administrative structure. The Commissioner of Internal Revenue's first report, covering the year ending June 30, 1863 (published at the end of 1863), accounted for the "revenue received from tax on salaries" (i.e., tax revenue from government salaries) in a completely separate table from all other revenues. *See* REPORT OF THE COMMISSIONER OF INTERNAL REVENUE ON THE OPERATIONS OF THE INTERNAL REVENUE SYSTEM FOR THE YEAR ENDING JUNE 30, 1863, at 231 tbl.C (1864). Likewise, receipts from "[d]ividends, interest, and premiums from banks, railroads, insurance companies &c., sections 81, 82, 84" were kept distinct from the tax receipts from "Income, section 90." *See id.* at 208–27. Indeed, the Commissioner distinguished receipts from each of the different types of companies subject to the taxes on dividend and interest. *See id.* at 204; *cf. id.* at 183–84 (providing a breakdown of revenue derived from "incomes" as a distinct category). The 1864 Report is similar—indeed, the 1864 Report created a new table especially for "[c]ollections from banks, insurance, railroad, canal and turnpike companies." *See* REPORT ON THE COMMISSIONER OF INTERNAL REVENUE ON THE OPERATIONS OF THE INTERNAL REVENUE SYSTEM FOR THE YEAR ENDING JUNE 30, 1864, at 260–71 tbl.B (1865); *see also id.* at 248–49 ("Incomes"); *id.* at 273–74 tbl.C ("Salaries").

[73] *See* Hill, *supra* note 46, at 428.

[74] This particular inequity was caught by the Commissioner of Internal Revenue who issued regulations requiring assessors to impose an additional 2% tax on anyone with an income of over $10,000 who deducted from their tax return the dividend or interest income for which the company had already paid taxes. *See* SMITH, *supra* note 40, at 55. We can see that right from the beginning of the income tax, tax administrators sought to address inequities, including those caused by differential withholding rules that were specifically written into the statute.

[75] *See id.*; Hill, *supra* note 46, at 427. One recent commentator has suggested that this disparity could have been either an oversight or the result of legislative compromise, *see* Scott A. Taylor, *Corporate Integration in the Federal Income Tax: Lessons from the Past and a Proposal for the Future*, 10 VA. TAX REV. 237, 264 (1990), but another has countered that "more likely it was a result of the administrative difficulties of imposing a graduated tax at the business level," STEVEN A. BANK, FROM SWORD TO SHIELD: THE TRANSFORMATION OF THE CORPORATE INCOME TAX, 1861 TO PRESENT 21 (2010).

to keep track of individual payments and to exempt the first $600 of annual income, it did not require a 5% rate for those making more than $10,000. Since few federal officials made that sum of money, though, this hardly mattered.[76]

A further inequity arose from an amendment to the law that went into effect before any "income duty" payments were due. The amendment provided that a person subject to the "income duty" could deduct "the amount actually paid . . . for the rent of the dwelling-house or estate on which he resides."[77] The salaries of soldiers and other federal employees, however, had no deduction for rent.[78]

Another inequity between the official "income duty" and these other taxes that we would today also see as taxes on "income" was the initial dates of coverage. The law went into effect on July 1, 1862, and the withholding provisions kicked in immediately after passage of the law. The "Railroad Bonds" and "Banks, Trust Companies, Savings Institutions, and Insurance Companies" provisions required the payment of the tax on any interest or dividends paid after July 1, 1862;[79] and the withholding from U.S. government officials salaries began on August 1, 1862.[80] In contrast, the "income duty," which was not due until June 30, 1863,[81] applied to income for the entire calendar year starting from January 1, 1862.[82]

One final inequity that was not explicitly written into the law but was of great importance was the significant differences in tax evasion potential. Employees of the U.S. government simply could not avoid the tax—it was taken out before they even received their pay—whereas all other employees could.[83] Similarly, railroad company bondholders could not avoid the tax on their interest, whereas all other creditors could. And, finally, the shareholders of stock of railroad companies, banks, trusts, etc. were likewise effectively subject to the tax before receiving their payments and were thus unable to avoid it.

In short, income tax withholding began with Congress defining the sums subject to withholding as not being "income"—and doing so in ways

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[76] *See* SMITH, *supra* note 40, at 54; Hill, *supra* note 46, at 427.

[77] Act of Mar. 3, 1863, § 11, 12 Stat. 713, 723 (amending the 1862 Revenue Act); *see also* SMITH, *supra* note 40, at 56 (discussing the amendment).

[78] *See* Joseph L. Bopeley, *Pay-as-You-Go, Civil War Style*, 21 TAXES 376, 376–77 (1943).

[79] 1862 Revenue Act, § 81, 12 Stat. at 469; *id.* § 82, 12 Stat. at 470.

[80] *Id.* § 86, 12 Stat. at 472.

[81] *Id.* § 92, 12 Stat. at 474.

[82] *Id.* § 91, 12 Stat. at 474 ("[T]he duty . . . shall be assessed and collected upon the income for the year ending the thirty-first day of December next preceding the time for levying and collecting said duty, that is to say, on the first day of May, eighteen hundred and sixty-three . . . .").

[83] Although it is probably impossible to determine with any precision how much evasion of the Civil War-era income tax took place, one early twentieth-century scholar has estimated "that not more than one-tenth of the actual taxable income of the country was reached." KENNAN, *supra* note 46, at 256.

that created some obvious inequities—in large part to facilitate the administrative process of tax collection.

The next major revenue statute of the war, the 1864 Revenue Act, continued the same basic approach, although it did increase rates. The $600 exemption remained, but the lowest rate was raised from 3% to 5%; a second rate—7.5%—for amounts between $5000 and $10,000 was created; and the top rate, for incomes over $10,000, was increased to 10%.[84] The approach to withholding, however, remained the same. Five percent was to be withheld from dividends and bond interest from certain types of companies, and again the tax was imposed on the company, not the stock- and bondholders.[85] One key distinction with the 1862 Revenue Act, however, was that companies were no longer *required* to deduct the tax from the payments to the individual owners of the securities.[86] The approach to U.S. government salaries was the same as the 1862 Act: for amounts above $600, a 5% tax was withheld.[87] These amounts were then all excluded from the income subject to tax in exactly the same way as in the 1862 Revenue Act.[88] All the basic inequities that I described with the 1862 Act remained,[89] though of course things would have improved dramatically for bondholders of company debt if the company paid the bond interest tax without deducting it from the interest payment.[90] The 1864 Revenue Act, did, however, rearrange the statutory structure so that all these provisions were in a single title with the heading "Income."[91]

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84 Act of June 30, 1864, § 116, 13 Stat. 223, 281 [hereinafter 1864 Revenue Act]. The language of the Act did solve the problem of the outrageous marginal rate for the ten thousandth dollar in the 1862 Revenue Act, *see supra* note 70, by making all the rates marginal rates.

85 1864 Revenue Act, § 120, 13 Stat. at 283–84. The range of companies subject to the payment of the tax on bond interest was expanded to include "canal, turnpike, canal navigation, [and] slackwater compan[ies]," *id.* § 122, 13 Stat. at 284, but the approach was identical.

86 Recall that the 1862 Revenue Act "authorized and required" the withholding. *See supra* text accompanying note 63. In contrast, the 1864 Revenue Act provided that the companies were simply "authorized to deduct and withhold from all payments . . . the said duty of five per centum." § 120, 13 Stat. at 284. Apparently, according to one nineteenth-century commentator, the tax on at least bond interest effectively amounted to a tax on the corporation, because "as a matter of fact [the corporations] generally assumed the tax themselves without withholding it from the bondholder." Edwin R.A. Seligman, *The Income Tax*, 9 POL. SCI. Q. 610, 629 (1894).

87 1864 Revenue Act, § 123, 13 Stat. at 285.

88 *See id.* § 117, 13 Stat. at 281.

89 *See supra* text accompanying notes 73–83.

90 *See supra* note 86 and accompanying text. The Commissioner of Internal Revenue issued regulations providing that "[t]axes paid by corporations cannot be allowed as deductions from the income of a stockholder." GEORGE S. BOUTWELL, A MANUAL OF THE DIRECT AND EXCISE TAX SYSTEM OF THE UNITED STATES; INCLUDING THE FORMS AND REGULATIONS ESTABLISHED BY THE COMMISSIONER OF INTERNAL REVENUE, THE DECISIONS AND RULINGS OF THE COMMISSIONER, TOGETHER WITH EXTRACTS FROM THE CORRESPONDENCE OF THE OFFICE 153 (Boston, Little, Brown & Co. 4th ed. 1864), *cited in* BANK, *supra* note 75, at 20.

91 *See* 1864 Revenue Act, 13 Stat. at 281. Once again, as with the 1861 Revenue Act, the income tax provisions of the law never went into effect because Congress repealed the law on March 3, 1865,

While the 1864 Revenue Act was winding its way through Congress, Secretary of the Treasury Chase lobbied for an additional income tax to meet increased revenue needs.[92] So Congress passed a joint resolution imposing a special one-time income tax on all 1863 income (again, with a $600 exemption), to be collected by October 1, 1864. This resolution explicitly stated that government salaries and interest income and dividends subject to withholding would be subject to the special tax.[93] This created somewhat of a conundrum, particularly for assessing and collecting the special tax from soldiers in the field. The district assessor from the soldier's locality generally had little contact with those in the military because the assessor understood that the soldier's salary was subject to withholding. By the time the war had ended, the vast majority of the one-time special-tax assessments against those in the army and navy had not been paid. Eventually, though, Congress cancelled the special-tax liabilities for all officers and soldiers who had been honorably discharged.[94]

When the war ended in April 1865, there were calls to reduce internal taxes. Although there was an enormous public debt still to be repaid, tax receipts in 1865–1866 came in much higher than expected. So Congress passed a tax-reduction bill.[95] Despite reducing internal taxes in general, this first postwar tax law made only minor changes to the income tax. But it did make one important change to the salary withholding process: it provided that federal paymasters were to withhold taxes for salaries over $5000 at the same marginal rate—10%—as the rate imposed on other income.[96]

In essence, this provision required the rates in the salary withholding provision to match those in the "income duty." This was obviously a way to end the inequity between "salaries" and other income that I described earlier.[97] Given the wartime inflation and the introduction of the

prior to the due date for tax payments. The 1865 Revenue Act changed the rates so that the 10% marginal rate kicked in at $5000, rather than $10,000, but because the withholding provisions only imposed a 5% rate in any case, the 1865 Revenue Act left the 1864 withholding provisions intact. *See* Act of Mar. 3, 1865, 13 Stat. 469, 479 (amending the 1864 Revenue Act).

92 *See* SMITH, *supra* note 40, at 64.

93 *See* H.R.J. Res. 77, 38th Cong. (1864).

94 *See* Bopeley, *supra* note 78, at 377.

95 *See* Act of July 13, 1866, 14 Stat. 98 (including in its title "[a]n Act to reduce Internal Taxation").

96 *See id.* § 9, 14 Stat. at 139. When initially passed, every income tax was assumed by most congressmen to be a temporary measure that would end when the revenue needs associated with the war were over. After all, as I noted at the beginning of this section, most of Congress—indeed, most of the country—saw internal taxes as unnecessary for the ordinary peacetime operations of the federal government. Sunset provisions were often written directly into the law. So, for example, the 1867 amendments to the 1864 Revenue Act specifically provided that the law's income tax would expire in 1870 (covering income through the end of 1869). *See* Act of Mar. 2, 1867, § 13, 14 Stat. 471, 480 [hereinafter 1867 Revenue Act]. The law failed, however, to set an end date for the withholding taxes on salaries, dividends, and bond interest.

97 *See supra* text accompanying note 76.

"greenbacks" in 1863, the number of federal government employees benefitting from the rate disparity on salaries over $5000 had increased.

This provision, however, effectively lasted less than a year, as the following Congress eliminated the graduated rate structure altogether, raising the exemption to $1000 and setting a single tax rate of 5% for all income above the $1000 exemption;[98] this rate structure was applied equally to all governmental salaries.[99] In 1870, Congress vigorously debated whether to continue the income tax, and once again, compromise was the order of the day. The income tax—and withholding—was given a two-year reprieve, although the exemption was raised to $2000 and the rate reduced to 2.5%.[100] In 1872, the income tax then expired on its own terms without much congressional support for its continuance.[101] Those taxes subject to withholding (the government salary tax and the tax on dividends and bond interest) also expired.[102]

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[98] *See* 1867 Revenue Act, § 13, 14 Stat. at 477–78.

[99] *See id.* § 13, 14 Stat. at 480. The 1864 Revenue Act's income tax provisions were similarly set to sunset in 1870. *See* 1864 Revenue Act, § 119, 13 Stat. 223, 283. Again, however, there was no sunset clause for the federal employees' salary tax. *See* 1867 Revenue Act, § 13, 14 Stat. at 480; *see also* 1864 Revenue Act, § 123, 13 Stat. at 285.

[100] *See* Act of July 14, 1870, ch. 225, §§ 6, 8, 11, 16 Stat. 256, 257–59 [hereinafter 1870 Revenue Act].

[101] STANLEY, *supra* note 39, at 55–56.

[102] The 1870 Revenue Act imposed an interesting twist on those taxes subject to withholding. Recall that the 1862 Revenue Act imposed withholding taxes beginning in July 1862 but that incomes not subject to withholding were subject to the income tax for all of 1862. *See supra* text accompanying notes 79–82. In a fit of extraordinarily inconsistent drafting, Congress both recognized this fact and didn't. In one section of the 1870 Revenue Act, Congress set a deadline of August 1, 1870, for the withholding of tax imposed by the 1867 amendments to the 1864 Revenue Act—that is, 5% on income over $1000. *See* 1870 Revenue Act, § 17, 16 Stat. at 261. Yet, in drafting the provisions of the law going forward, Congress ignored this fact altogether. The regular income tax covered the calendar years 1870 and 1871, in effect expiring for income earned after December 31, 1871. The withholding taxes, however, also ended the same day. This expiration date applied at least to the interest and dividend withholding. *See id.* § 15, 16 Stat. at 260. Unfortunately, I have been unable to find in the 1870 statute any indication that the withholding tax for U.S. government salaries was continued after August 1, 1870. Indeed, one provision in the law implies a difference of treatment between U.S. government salaries on the one hand and interest and dividend income on the other. When delineating what income is to be included in a person's assessment, the statute states, "there shall be included all income . . . including any amount received as salary or pay for services in the civil, military, naval, or other service of the United States, or as senator, representative or delegate in Congress; except that portion thereof from which, under authority of acts of Congress previous hereto, a tax of five per centum shall have been withheld." *Id.* § 7, 16 Stat. at 257–58. This language clearly refers only to withholding under the pre-1870 Revenue Act regime, implying that this is the only salary income subject to withholding. In contrast, two lines later in the same section of the statute, also excluded from income is "the amount received from any corporations whose officers, as authorized by law, withhold and pay as taxes a per centum of the dividends made, and of interest or coupons paid by such corporations," language that includes withholding more broadly, not just limited to the pre-1870 Revenue Act regime. *See id.* § 7, 16 Stat. at 258. The law seems, therefore, to assume that Congress wanted to exclude all dividend/interest income *and* all salaries subject to withholding from the amount of income subject to the income tax proper. Yet, two turn-of-the-century scholars both indicate that salary withholding and dividend/interest

Despite this, the withholding provision of the Civil War-era income tax provided the government with an efficient and relatively easily enforced mechanism of taxing "income."

Before I turn to the story of the twentieth-century income tax, let me add a quick word about the income tax provisions of the Revenue Act of 1894. These provisions were effectively invalidated in 1895 in *Pollock v. Farmers' Loan & Trust Co.*,[103] and so never went into effect. Though the income tax provisions in the law largely mirrored the basic outlines of the Civil War income tax, withholding in the new law would have differed somewhat. The law did require withholding of federal government salaries in much the same manner as the Civil War income tax.[104] There, however, the similarities ended. First, there was no withholding of the tax on bond income. Second, the law no longer provided a specific tax on corporate dividends at all. Instead, the law introduced the first tax on net corporate profits.[105] Since dividends came from those profits, the theory was that those dividends had effectively already been taxed. Thus, the 1894 law did not provide any tax on the recipient of the dividends on precisely the grounds argued by those who oppose the taxation of dividends today: the

withholding applied throughout 1871 (though neither applied between August 1 and December 31, 1870). *See* SMITH, *supra* note 40, at 86; Hill, *supra* note 46, at 443–44. A third early twentieth-century scholar seems to agree, although what could simply be a misprint raises some ambiguity about the issue. Edwin Seligman writes, "The result of this whole situation was that the old five per cent tax on dividends and salaries continued until August 1, 1870, and that the new tax, at a rate of two and one-half per cent, was levied only during the year 1871, with an interregnum from August 1 to December 31, 1870. With the close of 1870 the tax on salaries and dividends ceased, while the rest of the income tax was still assessed in 1872, although only on the income of 1871." SELIGMAN, *supra* note 38, at 465–66. Seligman also clearly refers to the August-through-December-1870 period as an "interregnum" and explicitly states that the 2.5% tax "was levied . . . during the year 1871." *Id.* at 466. Yet, at the same time, he says, "With the close of *1870* the tax on salaries and dividends ceased." *Id.* (emphasis added). If he meant 1871, then he would be in complete agreement with Hill and Smith. Finally, the most recent work specifically addressing the Civil War-era income tax, a 1954 doctoral dissertation, likewise asserts that the withheld salary tax was treated the same as the withheld dividends/interest tax. *See* 2 HAROLD Q. LANGENDERFER, THE FEDERAL INCOME TAX, 1861–1872, at 664 (1980) ("[T]he tax on salaries, interest, and dividends was five per cent from January to August, 1870, and two and a half per cent during 1871."). Moreover, the report of the Commissioner of Internal Revenue indicates a significant amount of money collected from U.S. government salary withholding between July 1, 1871, and June 30, 1872. *See* ANNUAL REPORT OF THE COMMISSIONER OF INTERNAL REVENUE ON THE OPERATIONS OF THE INTERNAL REVENUE SYSTEM FOR THE YEAR 1872, at VI (1872).

[103] 157 U.S. 429, *vacated on reh'g*, 158 U.S. 601 (1895); *see generally* 8 OWEN M. FISS, HISTORY OF THE SUPREME COURT OF THE UNITED STATES: TROUBLED BEGINNINGS OF THE MODERN STATE, 1888–1910, at 75–100 (1993) (discussing the decision in *Pollock* to invalidate the 1894 income tax provisions).

[104] *See* Act of Aug. 27, 1894, ch. 349, § 33, 28 Stat. 509, 557 [hereinafter 1894 Revenue Act]. The exemption was $4000, and the law provided for a single, marginal rate of 2% on income above the exemption.

[105] *See id.* § 28, 28 Stat. at 554.

argument against double taxation.[106] The law did provide that corporations were required to report the name, address, and salary of each employee who was paid more than $4000.[107] These salaries, however, were simply part of the expenses from which profits were calculated, and there was certainly no withholding on behalf of the employee in the manner provided for federal employees.

B. Wilson Era

In 1913, with the election of Woodrow Wilson and the ratification of the Sixteenth Amendment, Congress again brought an individual income tax back into its revenue arsenal.[108] The 1913 tax law weaved withholding deeply into the fabric of the income tax in ways far more extensive than had the Civil War income tax. Reaching across the Atlantic to learn from English income tax administration,[109] the 1913 law started with a presumption that *all* income would be subject to withholding at source. It did so in ways that might seem counterintuitive to twenty-first-century Americans, even those accustomed to our deeply entrenched system of withholding. Under the law, all payers (or "debtors," the term the Treasury regulations used for those who withheld and paid income tax on behalf of another) of any kind—employers, stock and bond issuers, other debtors such as mortgagers, as well as renters—were required to withhold income taxes. The goal was of course primarily "to secure the maximum revenue and to prevent evasion by the dishonest taxpayer."[110] As we will see, however, the system failed to prevent evasion, and the United States' experiment with a fully integrated withholding system ended a mere four years later.

The reintroduction of an income tax in 1913 was found in Section II of the Underwood–Simmons Tariff Act and served as part of the offset for a

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106 *See, e.g.*, CHARLES E. MCLURE, JR., MUST CORPORATE INCOME BE TAXED TWICE? A REPORT OF A CONFERENCE SPONSORED BY THE FUND FOR PUBLIC POLICY RESEARCH AND THE BROOKINGS INSTITUTION (1979).

107 *See* 1894 Revenue Act, § 35, 28 Stat. at 559. The basic idea, though, was that the tax on corporate income was simply the Civil War dividends tax in a new guise. After all, in the mid-nineteenth century, corporations generally distributed most of their earnings as dividends. BANK, *supra* note 75, at 21. So the extension from a dividends tax to a corporate income tax was natural because a corporate income tax was largely viewed as simply a tax on both dividends and undistributed profits. *Id.* at 49. So, the concept of "withholding" of the stockholder's income tax at source had taken a small step toward the creation of a new and distinct concept: the corporate income tax. Although there was a clear sense that taxing the income of an individual owner of shares at the corporate level was primarily grounded on the increased likelihood of collecting the tax, the idea that a corporate income tax was simply a "withholding" of the shareholders' income eventually gave way. *See generally id.* at 40–55.

108 In 1909, Congress passed an "excise tax" on corporate income. This was an attempt to skirt the Supreme Court's invalidation of the income tax in *Pollock* rather than to attack it head on, and the Court upheld it in 1911. *See* Flint v. Stone Tracy Co., 220 U.S. 107 (1911).

109 *See* H.R. REP. NO. 63-5, at 38 (1913); *see infra* text accompanying note 132.

110 *See* SIDNEY RATNER, TAXATION AND DEMOCRACY IN AMERICA 336 (1967).

broad reduction in tariffs.[111] The basic thrust of the law was to create a 1% tax on all income above $3000[112] with an increasing "surtax" for incomes above $20,000.[113] The rate was obviously low by today's standards. Indeed, even with the "surtax," rates were low in comparison to other countries.[114] Since $3000 in 1913 was, with inflation, the equivalent of more than $70,000 today, the exemption meant that only 2% of the population even paid the income tax at all.[115]

The fact that the law affected but a sliver of the population was by design. But, the design was not simply aimed at "soaking the rich."[116] Rather, drafters of the law knew that they were creating something new and consciously chose to start (relatively) small. As one scholar put it at the time, "[I]t is important to view the new income tax, not as an ideal or perfected system, but as the first step in the introduction of a vast and more or less complex system."[117] They recognized that the law would be

111 *Id.* at 324–25.

112 Act of Oct. 3, 1913, ch. 16, §§ II.A, II.C, 38 Stat. 114, 166, 168 [hereinafter 1913 Revenue Act]. Heads of households were entitled to a $4000 exemption, but this did not affect the withholding provisions. *Id.* § II.C, 38 Stat. at 168.

113 *See* RATNER, *supra* note 110, at 334. The 1% "normal tax" rate covered income up to $20,000. *Id.* The so-called "surtax" provided for an additional marginal tax of the following:

RATES OF SURTAX	AMOUNT OF INCOME
1%	$20,000–$50,000
2%	$50,000–$75,000
3%	$75,000–$100,000
4%	$100,000–$250,000
5%	$250,000–$500,000
6%	$500,000 and above

ROY G. BLAKEY & GLADYS C. BLAKEY, THE FEDERAL INCOME TAX 96 (1940).

114 *See* Roy G. Blakey, *The New Income Tax*, 4 AM. ECON. REV. 25, 34 (1914) (noting that these rates were lower than "most countries, as, for example, in England, Prussia, Austria, and Italy").

115 JOHN F. WITTE, THE POLITICS AND DEVELOPMENT OF THE FEDERAL INCOME TAX 78 (1985) ("[L]ess than 2 percent of the labor force filed returns in the years 1913–1915."); *see* Sheldon D. Pollack, *Origins of the Modern Income Tax, 1894–1913*, 66 TAX LAW. 295, 326 (2013).

116 The law may well have been a compromise on this point. *Compare, e.g.*, HINTON, *supra* note 45, at 143 (Hull's "income tax . . . was not intended to redistribute the nation's wealth"), *with* Blakey, *supra* note 114, at 37 ("Without doubt, the desire to level incomes, and the willingness of politicians to cater to the prejudices of the masses have had some part in the demand for the income tax.").

117 Blakey, *supra* note 114, at 38; *see also* 50 CONG. REC. 508 (1913) ("[L]ike any new tax law, it will be necessary for the people to become acquainted with the proposed law . . . ."); HINTON, *supra* note 45, at 141 ("[T]he [income] tax would apply to relatively few persons at first, enabling both the public and the tax collectors to become accustomed to its workings gradually."); Hull, *supra* note 45, at 131 ("[I]t was not deemed wise in the beginning to enact [an income tax] law of almost universal application, because, like all new laws, it must first be understood by the people and become adjusted to the intricate business conditions of the country before its administration could be expected to prove entirely convenient and satisfactory.").

administratively burdensome and that withholding was a key part of what made it so.

Initially drafted by Cordell Hull, then a Democratic member of the House Committee on Ways and Means,[118] the income tax sections included withholding provisions covering three categories of income: (1) corporate bond income; (2) foreign bond income and foreign corporate dividends; and (3) a catch-all category covering any "interest, rent, salaries, wages, premiums, annuities, compensation, remuneration, emoluments, or other fixed or determinable annual gains, profits, and income,"[119] with the exception of corporate dividends (which were not taxed because corporate income was already taxed). Withholding on the first two categories was required irrespective of amount (much like the Civil War bond interest and dividends tax) whereas withholding was required on the third category only if the amount received by a person exceeded $3000 in a taxable year, the amount of the exemption (similar in approach to the salary withholding for government employees during the Civil War).[120] It is worth noting that in contrast to the Civil War-era "income duty," there was no attempt to designate the taxes subject to withholding as somehow legally distinct from the income tax (i.e., a "salary tax" or a "dividend tax"), and thus no attempt to define "income" so as to exclude earnings that were otherwise subject to the withholding tax. Earnings subject to withholding were now very much "income."

Although there was a mild progressivity in income tax rates,[121] the basic rate—the so-called "normal tax"—was 1%, and this was the withholding rate irrespective of the recipient's income.[122] Moreover, this was an actual effective rate, not a marginal rate, even for the third category, which required withholding only if the sum paid by the withholding agent exceeded $3000. So, for bond interest, since there was no $3000 exemption, the 1% withholding rate amounted to both a 1% effective and a 1% marginal rate. Someone with $1500 of annual bond interest from a corporation would have had 1% (in this case, $15) withheld from the payments, and someone with $4000 in bond interest would likewise have had 1% (in this case, $40) withheld from the payments. On the other hand, an employee with an annual salary of $3000 or less would have had nothing withheld, while an employee with, say, an annual income of $4000 would have $40 withheld. As a practical matter, one scholar described the

[118] RATNER, *supra* note 110, at 325.

[119] 1913 Revenue Act, § II.E, 38 Stat. 114, 170.

[120] *Id.* § II.E, 38 Stat. at 170–71. Owners of securities subject to withholding under the first two categories could get the exemption by filing a certificate with the withholding agent. *See id.* Recipients could deduct the "tax withheld from the total tax due on their net incomes." *See* THE AMERICAN WAY IN TAXATION: INTERNAL REVENUE, 1862–1963, at 118 (Lillian Doris ed., 1963).

[121] *See supra* note 113.

[122] § II.A, 38 Stat. at 166.

system as follows: if an employee got paid, for example, $300 per month for a total of $3600 per year, he would have nothing withheld for the first ten months of the year. Then, in the eleventh month, the annual pay he received from his employer (i.e., this particular withholding agent) would hit $3300, thus exceeding the $3000 exemption. At that point, the employer would be required to withhold $33 (i.e., 1% on the total $3300, not just 1% on the $300 earned that month). Then in the twelfth month, the employer would withhold $3 (i.e., 1% of the $300 earned that month) for a total tax withheld of $36.[123]

Now, the $3000 exemption was significant, and as I said, in the first few years, the number of individuals directly affected was small.[124] Moreover, the withholding arithmetic was easy. Only the "normal tax" of 1% had to be withheld even if the amount of income exceeded $20,000, the point at which the graduated "surtax" kicked in.[125] But, for those who had to withhold, the hassles were enormous. Looking at the third category of income subject to withholding that I described above, notice that it includes not only "salaries" and "wages," but also, for example, "rents" and "interest" on loans.

Moreover, in contrast to the Civil War withholding provisions for corporations paying bond interest and dividends—which simply required a lump-sum payment—the 1913 law required the withholding agent to keep track of the individuals for whom the tax was being withheld. So, for example, bond owners were required to file a certificate with the issuer of the bond listing the owner's name and address; the bond issuer would then have to provide these certificates to the tax authorities. If the bond owner failed to do this, the bond issuer would be required to file a separate certificate attesting to that fact.[126] The certificate would include not only the bond owner's name and address, but also an indication of whether the bond owner was claiming the tax exemption and/or any of the law's deductions.[127] Notice, then, that the bond issuer needed to keep track of the certificate to determine whether the tax was to be withheld from the bond payment. Notice also that the claim of exemption was something that the bond owner could change each time payment was due and so these certificates would have to be filed each time there was a bond payment. Bond payments were usually semiannual, but remember that this was an era when bond interest was paid not electronically as today but upon

[123] *See* HENRY CAMPBELL BLACK, A TREATISE ON THE LAW OF INCOME TAXATION UNDER FEDERAL AND STATE LAWS § 361, at 557–58 (2d ed. 1915).

[124] *See supra* text accompanying note 115.

[125] The theory was that no single one of the taxpayer's "debtors" could know the taxpayer's total income. *See* Blakey, *supra* note 114, at 32.

[126] *See* BLACK, *supra* note 123, §§ 79–83, at 49–51.

[127] Strictly speaking, it was even worse, for there were separate "forms" that needed to be filed depending on whether an exemption or deductions or neither were being claimed. *See* BLACK, *supra* note 123, § 370, at 566–67; *id.* app. at 713–15.

presentation of a coupon, which entitled the bearer to payment irrespective of who the coupon bearer was. So this meant more paper shuffling for the bond issuer. It also led to delays in the payment of interest.[128] Moreover, the bond owner could present his coupon at any time after the payment date, so the administrative hassle was a constant feature of life as a bond issuer, not just a semiannual event. Moreover, if an agent of the bond owner presented the coupon, the bond issuer would have to "be satisfied as to the identity and responsibility of the agent, calling upon him for evidence of his authority, if necessary, and when so satisfied, . . . writ[ing] or stamp[ing] a statement to that effect on the face of the certificate."[129] One goal of these detailed certificates was to ensure that the taxpayer who was entitled to the exemption in fact got it. At the same time, though, these certificates obviously helped the tax authorities audit if necessary, since they eventually got the certificates.[130]

I give such detail not to bore the reader with the minutiae of a century-old law that was repealed in 1917, but rather to give a taste of the way in which the law introduced administrative burdens—primarily, though not exclusively, on corporations—burdens that were dramatically greater than those imposed during the 1860s and the likes of which no one in the United States had ever seen before. This is of course just one example of the onus placed on withholding agents. There were separate regulations for dealers in foreign stocks and bonds, renters or mortgagors of real property, and others.[131] Key is that these detailed regulations were, on the one hand, no doubt necessary to implement a full-fledged withholding system and yet, on the other hand, completely new and foreign to the relationship between the government and "debtors" in the American context. I say "foreign" in large part because the principle of withholding in its broad form (i.e., covering virtually every "payer" of any kind) was borrowed from the English, who had had such a system since 1799.[132] So, not only did the principle have the backing of the top tax policy theorists of the day,[133] but it had been tried and had worked. The approach had worked, however, in part *because* it had been around for so long. The federal income tax of 1913 attempted to install the system without fully laying the groundwork

[128] *See* Mortimer L. Schiff, *Some Aspects of the Income Tax*, 58 ANNALS AM. ACAD. POL. & SOC. SCI. 15, 25 (1915).

[129] BLACK, *supra* note 123, § 356, at 551; *id.* § 116, at 73–74.

[130] Incredibly enough, the law even made the withholding agent "personally liable" for the tax owed by the person to whom he was indebted. *See* 1913 Revenue Act, § II.E, 38 Stat. at 170; Blakey, *supra* note 114, at 32. Because of this, the corporation would have to make a copy for its files—and this is an era of mimeographs and spirit machines, long before photocopying. *See* Schiff, *supra* note 128, at 22. Nor was there any reimbursement for the administrative costs incurred by businesses, costs that one contemporary estimated at between 10% and 20% of the taxes collected. *See id.* at 24.

[131] *See* BLACK, *supra* note 123, §§ 363–364, at 560–63; *id.* § 361, at 556–60.

[132] SELIGMAN, *supra* note 38, at 78.

[133] *See, e.g.*, *id.* at 661–62.

necessary to ensure that such a complicated system, one demanding the compliance of large numbers of entities that had to expend significant resources, could work.[134]

The fact that the law attempted to bring withholding into this brand new income tax system so abruptly had its costs. Initial estimates were that the withholding provisions would yield two-thirds of income tax revenue,[135] but in 1916, less than 5% came from withholding.[136]

So, by the time Congress next seriously addressed tax issues in 1916, there was a groundswell of opposition to withholding.[137] Indeed, even Secretary of the Treasury William McAdoo advocated "do[ing] away with the withholding of the income tax at the source, and in place thereof . . . requir[ing] information at the source." McAdoo concluded "that it will mean the collection of a larger amount of revenue and eliminate a great deal of criticism which has been directed against the law."[138] Although Congress left withholding in place in the 1916 Revenue Act,[139] it completely revamped the system the following year. Eliminating withholding for virtually all income,[140] the War Revenue Act of 1917 instituted a system of "information at source" in its stead.[141] In effect, those "debtors" that had been required to withhold under the 1913 Revenue Act now merely had to report to the tax authorities the names of the recipients or employees along with the amounts paid to them. This change was made along with an increase in rates. More important for my purposes, the

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[134] *Cf.* Schiff, *supra* note 128, at 20 (articulating some distinctions between England and the United States). It is worth noting that the successful Wisconsin income tax of 1911, which served as the model for the Revenue Act of 1913, had a system requiring payers to provide information to the tax authorities but did not require withholding. *See* Ajay K. Mehrotra, *Forging Fiscal Reform: Constitutional Change, Public Policy, and the Creation of Administrative Capacity in Wisconsin, 1880–1920*, 20 J. POL'Y HIST. 94, 106–07 (2008).

[135] *See* H.R. REP. No. 63-5, at 38 (1913).

[136] THE AMERICAN WAY IN TAXATION, *supra* note 120, at 119; *see also* BLAKEY & BLAKEY, *supra* note 113, at 143 (estimating it as "less than one-fourth").

[137] *See* BLAKEY & BLAKEY, *supra* note 113, at 143; Roy G. Blakey, *The New Revenue Act*, 6 AM. ECON. REV. 837, 842 (1916) ("Perhaps no feature of the income tax law has caused more unfavorable criticism than the stoppage-at-the-source provision, which throws much of the burden of collecting the government's revenues upon banks, trust companies, corporations, and other agents."); *see also* Schiff, *supra* note 128, at 20–27 (describing many problems with the withholding system).

[138] U.S. TREASURY DEP'T, ANNUAL REPORT OF THE SECRETARY OF THE TREASURY ON THE STATE OF FINANCES FOR THE FISCAL YEAR ENDED JUNE 30, 1915, at 19 (1916); *see also* W. Elliot Brownlee, *Wilson and Financing the Modern State: The Revenue Act of 1916*, 129 PROC. AM. PHIL. SOC'Y 173, 197 (1985) (noting that Schiff and McAdoo "enthusiastically endorsed information at the source").

[139] Act of Sept. 8, 1916, ch. 463, sec. 8(d), 39 Stat. 756, 762.

[140] Act of Oct. 3, 1917, ch. 63, § 1204(2), 40 Stat. 300, 332 [hereinafter 1917 War Revenue Act] (repealing section 8(d) of the 1916 Revenue Act). The exemptions were "for nonresident aliens and income from tax-free covenant bonds." THE AMERICAN WAY IN TAXATION, *supra* note 120, at 119; *see* 1917 War Revenue Act, § 1205(1), 40 Stat. at 332–33.

[141] 1917 War Revenue Act, § 1211, 40 Stat. at 336–37.

individual exemption was reduced to $1000,[142] and the new reporting requirement was triggered whenever annual payments of $800 were made.[143] So, the number of individual recipients—in particular, employees—about whom information was furnished was significantly greater than the number for whom withholding had occurred under the 1913 Revenue Act. Nonetheless, the burden of providing information was a welcome relief for everyone involved. In the end the extensive withholding system of the 1913 Revenue Act was perhaps just a bit too much too fast. The next time withholding would come to the federal income tax, that mistake would not be made again.

Before I turn to the New Deal and World War II, it is worth pointing out what a look at the law of withholding has shown us up until now: nothing. Or, more precisely, by 1917, the country had had three attempts to experiment with withholding, but there can be no argument that withholding was entrenched or that the statutes embodying withholding were superstatutes or had any constitutional emanations of any kind. We can see this in numerous ways, but of course the easiest is that none of them lasted. Moreover, there was no claim that eliminating withholding raised constitutional problems. Indeed, in 1895, withholding suffered, along with the income tax itself, by being found *un*constitutional. In both 1872 and 1917, Congress repealed withholding. Of course, in both 1872 and 1895, withholding itself was not at issue—withholding was simply necessary collateral damage from the fact that the income tax itself had ended. But, this is why it is the Revenue Act of 1917 that so clearly tells us that withholding was not entrenched in any sense of that word: an income tax without any withholding was not only possible, it had now become law. In 1913, one certainly could have thought of withholding as an integral component of a system of taxing income—at least with respect to certain types of income. After all, the federal government had never had an income tax without withholding. But no one viewed it that way. Though tax theorists of the day clearly viewed withholding as a crucial component of a well-functioning income tax system,[144] the administrative practice effectively failed, whether because of actual government administrative failures or interest group politics. The reasons are not crucial. What is crucial is that starting in 1917, the federal government abandoned withholding—in all its forms, including those that had worked with success during the Civil War—as a component of its system of income tax administration, and no one even remotely thought this was a constitutional problem (whether large or small "c").

[142] $2000 for head of households. *Id.* § 1–2, 40 Stat. at 300–01.

[143] *Id.* § 1211, 40 Stat. at 337.

[144] *See* SELIGMAN, *supra* note 38, at 661–62.

C. Social Security Withholding

The next step in understanding the ways in which withholding became embedded into the federal income tax takes us to the Social Security Act of 1935. Despite the fact that the "contributions" made under the Social Security Act are not ordinarily viewed as part of the income tax, the introduction of social security was key to income tax withholding because it demonstrated that withholding was administratively possible—for both the government and employers. This laid the groundwork for the full-scale adoption of withholding enacted during World War II.

President Roosevelt signed the Social Security Act on August 14, 1935. It was an omnibus statute encompassing unemployment insurance; old-age, survivors, and disability insurance; and old-age and dependent children assistance.[145] Of interest to me are the provisions covering old-age insurance, what we colloquially refer to today as "social security." The old-age insurance system was—and remains—thought of as a comprehensive, mandatory social insurance program into which both employees and employers contribute and out of which those employees who reach a certain age can then collect. Both workers and their employers are viewed as paying "contributions," not taxes, and are viewed as having "accounts" from which they are paid out "benefits." Having employees and taxpayers view it in these terms was important from the beginning and remains a cornerstone of the popular conception and popularity of the social security "program" today.[146]

As a legal matter, however, the old-age insurance system consisted of two distinct features: taxes and benefits. Or, more precisely, (1) "taxes with respect to employment," which consisted of an "excise" tax on employers and an "income" tax on employees, each of which were a percentage of the employees' wages;[147] and (2) a system of "federal old-age benefits," which were loosely tied to those of the individual's wages that were subject to the tax.[148] One important reason the system was set up in this manner rather than as a straightforward "social insurance" program with "compulsory[]

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[145] Social Security Act, 49 Stat. 620 (1935).

[146] *See, e.g.*, Susannah Camic Tahk, *Making Impossible Tax Reform Possible*, 81 FORDHAM L. REV. 2683, 2713–16 (2013). Roosevelt was apparently quoted years later as saying, "We put those payroll contributions there so as to give the contributors a legal, moral, and political right to collect their pensions . . . . With those taxes in there, no damn politician can ever scrap my social security program." ARTHUR M. SCHLESINGER, JR., THE AGE OF ROOSEVELT: THE COMING OF THE NEW DEAL 308–09 (1958).

[147] *See* Social Security Act, §§ 801, 804, 49 Stat. at 636–37.

[148] *See id.* §§ 201–202, 49 Stat. at 622–23. This remains the basic structure of the system today. *See, e.g.*, Allison Christians, *National Report USA*, *in* DOUBLE TAXATION CONVENTIONS AND SOCIAL SECURITY CONVENTIONS 683, 685–90 (Michael Lang ed., 2006).

contributory . . . annuities"[149] was to reduce the likelihood of the law being struck down by the Supreme Court.[150] The structuring of the old-age insurance system as a tax, however, led to a bifurcation in the administration of the system, between the taxing provisions of the law and the benefits provisions.

Title II of the Social Security Act created the benefits, and Title VIII imposed the taxes. The taxes, then as now, were imposed on both the employer and the employee, initially 1% each and slated to rise incrementally over time. Congress deferred the date that the old-age insurance system would go into effect until January 1, 1937, a full sixteen months after adoption of the law.[151] Moreover, though the taxes (i.e., the "contributions") were set to begin in 1937, the monthly benefits were deferred even longer, until January 1, 1942.[152] Key to me here is that then—as now—the statute required that the tax on employees "be collected by the employer of the taxpayer, by deducting the amount of the tax from the wages as and when paid."[153] In essence, the law required the employer not only to pay its own portion of the tax, but also to withhold and pay the employee's portion as well.

The bifurcation also applied to the administrative agencies tasked with establishing and managing the system. The Act created a new independent agency, the Social Security Board, which was in charge of benefits (Title II).[154] In contrast, the Bureau of Internal Revenue, still part of the Department of the Treasury, was given control of the taxes (Title VIII).[155]

Now the administrative headaches of establishing the old-age insurance system were obviously tremendous, and I need not belabor the difficulties the Social Security Board's Bureau of Old-Age Insurance (or Bureau of Old-Age *Benefits*, as it was originally called[156]) had in creating and maintaining a central index system, along with millions of individual

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149 NAT'L CONFERENCE ON SOC. WELFARE, THE REPORT OF THE COMMITTEE ON ECONOMIC SECURITY OF 1935 AND OTHER BASIC DOCUMENTS RELATING TO THE DEVELOPMENT OF THE SOCIAL SECURITY ACT 49–54 (50th anniversary ed. 1985).

150 *See* JERRY R. CATES, INSURING INEQUALITY: ADMINISTRATIVE LEADERSHIP IN SOCIAL SECURITY, 1935–54, at 31 (1983). The Court did eventually uphold the old-age provisions of the Act. *See* Helvering v. Davis, 301 U.S. 619 (1937).

151 Social Security Act, Title VIII (Taxes with Respect to Employment), §§ 801–811, 49 Stat. at 636–39.

152 *Id.* § 202(a), 49 Stat. at 623. If an individual hit 65 or died prior to January 1, 1942, the government would provide the 65-year-old (or, in the case of death, his estate) a lump-sum payment, equal to 3.5% of his post-December 31, 1936 wages. *Id.* §§ 203(a), 204(a), 49 Stat. at 623–24. The 1939 Amendments to the Social Security Act accelerated the start of payments to January 1940. Social Security Act Amendments of 1939, Pub. L. No. 76-379, ch. 666, sec. 201, § 201, 53 Stat. 1360, 1362.

153 Social Security Act, § 802(a), 49 Stat. at 636.

154 *Id.* §§ 701–704, 49 Stat. at 635–36.

155 *Id.* § 807(a), 49 Stat. at 637.

156 ARTHUR J. ALTMEYER, THE FORMATIVE YEARS OF SOCIAL SECURITY 86 (1966).

employee "accounts."[157] In the days before electronic computers, the accounting challenge posed by the program was massive, and it is no wonder the Bureau's accounting operation was referred to as "the largest bookkeeping job in the world."[158] By the middle of 1940, the Bureau had processed more than 312 million "wage items"—in essence, line items in an employer report listing the employee along with the amount of money withheld—"plac[ing them] on punch cards and then post[ing them] mechanically to the individual employee's account."[159]

Almost as incredible an administrative task had to be performed on the taxing side of the bifurcated old-age insurance system. For that, the Bureau of Internal Revenue had to create a new system of withholding, payment, and itemization for the approximately 3.5 million employers who were to begin making "contributions" on behalf of their more than 30 million employees.[160] This system had to be created effectively out of whole cloth because employers were previously not required to pay any taxes on behalf of employees. Since 1917, they had of course been providing "information at source" to the tax authorities—that is, they had been required to provide the government with information about the earnings of all high-income employees.[161] Employees subject to income tax were then required to file their own annual returns and to pay all owed taxes directly themselves.[162] Moreover, the number of employees subject to the ordinary income tax was in any event quite small.[163] With the advent of the old-age insurance provisions of the Social Security Act, in contrast, withholding would now be required, and for virtually all employees. There were a few exceptions, such as agricultural and domestic workers,[164] but there was no income threshold beneath which withholding would not be required. So, for employers, the administrative burden was far greater than that imposed by the 1913 withholding, the system that led to an outcry and eventually to repeal in 1917.[165]

Moreover, there was going to have to be a massive coordination effort between the Bureau of Internal Revenue and the Social Security Board's

[157] By June 30, 1937, six months after the system went into operation, the Social Security system's central index contained more than 30 million names. *See id.* at 71. In contrast, only 3.4 million individuals paid personal income tax in 1937. *See* BLAKEY & BLAKEY, *supra* note 113, at 593 tbl.41.

[158] ALTMEYER, *supra* note 156, at 87.

[159] *Id.* at 86–87.

[160] *Id.* at 71; CHARLES MCKINLEY & ROBERT W. FRASE, LAUNCHING SOCIAL SECURITY: A CAPTURE-AND-RECORD ACCOUNT, 1935–1937, at 309 (1970).

[161] *See supra* text accompanying note 141.

[162] 1917 War Revenue Act, § 3, 40 Stat. 300, 301.

[163] *See* Carolyn C. Jones, *Class Tax to Mass Tax: The Role of Propaganda in the Expansion of the Income Tax During World War II*, 37 BUFF. L. REV. 685, 695 (1988–1989) (noting that in 1933, only 2.6% of the population was subject to income tax).

[164] *See* Social Security Act, §§ 210(b), 811(b), 49 Stat. 620, 625, 639 (1935).

[165] *See supra* Part II.B.

Bureau of Old-Age Insurance. The details of this effort are, again, not crucial, but suffice it to say that 1936 and 1937 involved coordination challenges unlike any the Bureau of Internal Revenue had dealt with since Congress created the first Commissioner of Internal Revenue in 1862.

The system set up by the tax authorities worked as follows: starting on January 1, 1937, every employer was required to file quarterly tax and information "returns" with the tax collector for the district of its principal place of business.[166] The returns would provide the employer's "identification number" and a list of all employees along with their "account numbers" (i.e., today's Social Security number), both of which had just been created in a flurry of activity in the last two months of 1936.[167] The forms required calculating and then itemizing the tax for each employee (both the employer's "excise" tax and the employee's "income" tax), after which the return had to be "executed." This meant verifying and signing the form—for corporations, by "the president, vice president, or other principal officer"—under oath before "any officer duly authorized to administer oaths."[168] When submitting the returns, the employer would of course also have to pay both taxes.

As I noted, this was new and quite obviously a major hassle and expense for employers. So, as we think about how this system eventually became deeply entrenched, it is worth noting a few key points.

First, employer opinion was solicited early on and was taken into account. This is despite the fact that many businesses were categorically opposed to the Social Security Act itself and were spearheading constitutional challenges to its various parts.[169] One example showing how government officials incorporated employer concerns should suffice. The statute gave the Commissioner of Internal Revenue discretion to collect the taxes "either by making and filing returns, or by stamps, coupons, tickets, books, or other reasonable devices or methods necessary or helpful in securing . . . proper identification of the taxpayer."[170] There were two principal methods considered: a "stamp" approach and a system of filing returns. When the Committee on Economic Security had been drafting Roosevelt's ideas for social security in 1934–1935, the academics advising the Committee looked to other advanced industrial societies with social security programs, Britain in particular, and explicitly recommended a "stamp tax system."[171]

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[166] Treas. Reg. §§ 401.402, 401.409 (1938). The tax returns were monthly during 1937, the first year of operation. *Id.* § 401.401.

[167] MCKINLEY & FRASE, *supra* note 160, at 364–74.

[168] Treas. Reg. § 401.407.

[169] ESKRIDGE & FEREJOHN, *supra* note 5, at 184.

[170] Social Security Act, § 807(b), 49 Stat. 620, 637 (1935).

[171] MCKINLEY & FRASE, *supra* note 160, at 313–15; *see also* Lent, *supra* note 36, at 721 (describing Australia's use of a similar system for its normal income tax).

A stamp plan would work something like this: the employer would purchase stamps in an amount equal to the amount of tax it was going to withhold. These could either be physical adhesive stamps or use some form of metering like metered mail. Employers could purchase the stamps either at post offices or more likely directly from Social Security or Internal Revenue offices. The employer would then provide the stamps to the employee who would keep them in a passbook. The passbook would thus keep track of the employee's "contributions." When the book became full of stamps, the employee would turn it into the Internal Revenue office in exchange for some kind of a receipt. Many within the Social Security Board—influential Board member Arthur Altmeyer in particular—strongly favored the stamp-book approach.[172] The thought was that this would be the simplest system for small employers and for those whose employees changed frequently (e.g., longshoremen and migrant workers).[173] Most importantly, in keeping with Roosevelt's view that employees should feel they have a "legal, moral, and, political right to collect their pensions,"[174] Altmeyer wanted employees to have proof that their employer had actually made contributions on their behalf.[175]

The big problem with the stamp-book method, however, was that it required the employer to stamp the employee's book each and every pay period. For small employers, this was not a huge deal and perhaps even preferable to filing regular—say, quarterly—returns with the Bureau of Internal Revenue. For large employers, in contrast, it would mean that they "would have to handle thousands of stamp books every pay period, which would be a very large burden upon them, particularly in view of the fact that the Bureau of Internal Revenue is very reluctant to require employers to buy or to rent any particular type of mechanical equipment."[176] Although Pitney–Bowes, which made the "mechanical equipment" that could perform this task, was strongly in favor of the stamp-tax approach,[177] those in the Treasury anticipated the complaints such a system would lead to. So, the Treasury chose a system of filed returns.[178]

Moreover, the government adopted the return system not just because it found the stamp-tax system unacceptable. It also sought to build on the pre-existing relationship between employers and the tax authorities. Recall that since 1917 employers had been required to provide "information-at-

[172] MCKINLEY & FRASE, *supra* note 160, at 314.

[173] *Id.*

[174] SCHLESINGER, *supra* note 146, at 308.

[175] MCKINLEY & FRASE, *supra* note 160, at 314.

[176] *Id.* at 316 (quoting Frank Mires, U.S. Treasury Department coordinator with the Social Security Board).

[177] *Id.* at 314.

[178] *See* Treas. Reg. § 401, subpart D (1938); Employees' Tax and the Employers' Tax Under Title VIII of the Social Security Act, 1 Fed. Reg. 1764, 1771–73 (Nov. 11, 1936).

source." The system of returns and payment for the new "old-age insurance" taxes would be similar in nature and, as one Treasury official put it, "it would be a simple matter to coordinate these two activities so that little more would be required of the employer than he already does."[179] Whether "little more would be required of the employer" was an accurate assessment of the burden or not—after all, the number of employees covered by Social Security far exceeded those subject to the income tax—at least the idea was to build on what employers were already doing with respect to their employees' taxes. So, incredibly enough, the 1917 abandonment of stoppage at source in favor of information at source actually laid the groundwork for the choice of administrative method when withholding was next introduced into the law. One certainly cannot say the stamp-tax approach would have otherwise been adopted or that it necessarily would have been less successful had it been adopted, but there is a nice sense in which the edifice of withholding in 1936–1937 was built on the ashes of its destruction in 1917.

In addition to the ways in which government officials specifically took employer concerns into account, the resulting entrenchment of withholding was also deeply intertwined with the political context of social security. The battles surrounding social security made withholding a relatively minor issue. While this was to some extent true of the 1913 income tax as well, the complaints about the administrative burdens of withholding in the teens transcended opposition to the income tax itself, while simultaneously feeding that opposition. Through 1916 and 1917, complaints about withholding continued after the Supreme Court upheld both the income tax and withholding itself.[180] In contrast, once the Supreme Court upheld both the unemployment insurance[181] and the old-age insurance provisions[182] on the same day in May 1937, withholding was no longer an issue. Indeed, since the requirement to withhold the employees' share of the new Title VIII tax was paired with the tax on employers, there was little additional administrative hassle associated with withholding the employees' share. So, once the Court upheld the entire scheme of both Title II (old-age benefits) and Title VIII (income and excise taxes), it was no longer worthwhile for employers to complain about withholding per se. After all, getting rid of withholding alone would not reduce the burden of having to comply with—and pay—the employers' excise tax. In contrast, the 1917 repeal of withholding shifted the burden of paying the employees' income tax entirely onto the employees themselves.

179 MCKINLEY & FRASE, *supra* note 160, at 317 (quoting Frank Mires, U.S. Treasury Department coordinator with the Social Security Board).

180 *See* Brushaber v. Union Pac. R.R., 240 U.S. 1 (1916) (upholding income tax against several constitutional challenges); *id.* at 21–22, 24 (upholding collection at source).

181 Steward Mach. Co. v. Davis, 301 U.S. 548, 578–98 (1937).

182 Helvering v. Davis, 301 U.S. 619, 640–45 (1937).

In sum, the Social Security Act's tax on employees' wage income brought withholding back to American law and did so in the context of a huge number of employers and employees. The law effectively forced employers to create managerial processes to deal with this new tax. With its $2500 exemption,[183] the normal income tax remained the province of a small minority of relatively wealthy wage earners. Those taxpayers still paid their taxes once annually, and employers' only responsibility was to provide the tax authorities with information, not cash. But the new system occasioned by the Social Security Act made it crystal clear that a withholding system was workable—for everyone: employees, employers, and the government alike. Withholding was now a part of the fabric of the American internal revenue collection process.

Before the Second World War, withholding of income tax at source—at least in the context of wage income—came in fits and starts, but with the Social Security Act, one can see the beginnings of what Eskridge and Ferejohn refer to as "administrative constitutionalism."[184] The law directed that employee contributions to social security be withheld, and the Bureau of Internal Revenue promulgated regulations that put teeth into the statute's withholding requirement. When the statute was then upheld by the Supreme Court in May 1937, administrative structures were in place to entrench withholding.

At this point, though, the beginnings of this entrenchment were premised almost entirely on a simple economic concept: the expenditure of start-up costs. By 1941, the system of withholding employee contributions to social security obviously could have been abolished—at least in literal terms—either by repealing the Social Security Act altogether or by shifting the burden of payment to the employee. The former was theoretically possible (though, of course, not with Roosevelt still as President!), but that sort of "repealing" would of course have been unconnected to withholding per se. The latter, on the other hand, was equally implausible, but for a different reason. Both the government and employers had invested the bulk of the resources, in terms of both money and managerial know-how, in setting the system up. The marginal cost of continuing with such a system was relatively low, and the disruption costs of change were unknown and, in any event, likely to be larger. This is entrenchment of a sort, akin to the co-ordination principle that Vermeule alludes to (e.g., we all drive on the right side of the road),[185] but this hardly seems the stuff of constitutionalism or superstatutes. As we turn to the next chapter in the withholding saga,

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183 BLAKEY & BLAKEY, *supra* note 113, at 512.

184 *See, e.g.*, ESKRIDGE & FEREJOHN, *supra* note 5, at 29; *cf.* Gillian E. Metzger, *Ordinary Administrative Law as Constitutional Common Law*, 110 COLUM. L. REV. 479, 497 (2010) (using the phrase "administrative constitutionalism" in the context of arguing that ordinary administrative law can at times be viewed as constitutional common law).

185 *See* Vermeule, *supra* note 10; *supra* text accompanying notes 10–11.

however, we will see a deeper entrenchment. Notice, moreover, that I still have not mentioned my putative superstatute. In this sense, the beginnings of entrenchment are, in contrast to Eskridge and Ferejohn's model, occurring *before* the statute even gets passed.

D. World War II

World War II changed everything, and income tax policy was no exception. From a "class tax" to a "mass tax," the income tax "changed its morning coat for overalls."[186] In 1940, there were seven million federal income taxpayers in the country; by 1945, that number had ballooned to 42 million.[187] As Professor Carolyn Jones has described it, "A tax intended at least symbolically to soak-the-rich during the Depression became a feature of everyday life for most Americans. It was an incredible transformation."[188] One key to this transformation was the government's increased need for wartime revenue. A second factor was conscious government policy aimed at suppressing inflation,[189] which war often causes.[190] Like the Civil War, World War II brought the country phenomenal changes in tax policy. The difference, though, was that this time the changes survived the enemy's surrender.

Income tax withholding was a fundamental part of this transformation in tax policy. It permitted both the increase in tax rates and the reduction of exemption levels that led to the enormous increase in the number of Americans being subject to the income tax. This in turn facilitated the massive growth in government occasioned by the war and eased the process by which the "mass tax" aspect of the income tax survived the end of the war.[191]

Tax policymakers recognized the importance of tax withholding as a tool in converting the income tax into a mass tax. Prior to World War II, income taxpayers paid federal tax in one chunk on March 15th of the year after the earning of the income.[192] Taxpayers also had the option of paying

186 Jones, *supra* note 163, at 685–86; *id.* at 695 (quoting PAUL, *supra* note 26, at 318).

187 *Id.* at 686.

188 *Id.* at 699.

189 PAUL, *supra* note 26, at 281, 294; Lent, *supra* note 36, at 735. Not surprisingly, the need for wartime revenues, rather than inflation fighting, turned out to be the more successful approach to convincing the public that the mass income tax was a positive development. *See* Carolyn C. Jones, *Mass-Based Income Taxation: Creating a Taxpaying Culture, 1940–1952*, *in* FUNDING THE MODERN AMERICAN STATE, 1941–1995: THE RISE AND FALL OF THE ERA OF EASY FINANCE 107, 114–15 (W. Elliot Brownlee ed., 1996).

190 *See* BANK, *supra* note 39, at 168–70; ROBERT HIGGS, CRISIS AND LEVIATHAN: CRITICAL EPISODES IN THE GROWTH OF AMERICAN GOVERNMENT 204–11 (1987).

191 *See* TWIGHT, *supra* note 30, at 96 ("Withholding is the paramount administrative mechanism that since 1943 has enabled the federal government to collect, without significant protest, sufficient private resources to fund a vastly expanded welfare state.").

192 *See* I.R.C. § 56(a) (1940).

in four quarterly installments, starting on that same day.[193] In either case, the approach required a level of liquidity that many people would find difficult. So, for example, in 1940, an unmarried individual with a weekly income of, say, $200 and no investment income would have had an annual tax bill of $316.[194] It is not difficult to see how this would require some cash flow planning for that March 15th bill. When the income tax was only affecting the top 2.6% of the population,[195] the government expected individuals to have the wherewithal to plan around this problem. Once the income tax was to affect nearly 70% of the population,[196] however, this simply was not possible.

In 1942, Beardsley Ruml made a variation of this cash flow problem famous. Ruml, the Chairman of the New York Federal Reserve Bank, was simultaneously working for R.H. Macy's & Co. at the time, and his example was meant to make the time-lag problem of income tax payments more vivid.[197] He described a successful executive who retires and is given a pension. In Ruml's telling, the executive can never afford his income tax bill because in the first year of retirement, he needs not only the pension but also a top-up of enough additional money to pay the taxes from his previous year's (higher) salary. Then, in the second year after retiring, he still needs more than his pension because he has to pay taxes on the previous year's pension *plus* taxes on the previous year's top-up to pay the income tax from the year before that. The process continues indefinitely.

Ruml's solution was current tax payment. Tax would be due as the income was earned, so that no one could have a mismatch between income and tax liability. Importantly—and, a point to which I will return—the actual "Ruml plan" would have resulted in a complete forgiveness of one year's taxes in the transition to "current tax payment." Taxpayers would just start paying "on this year instead of on last year."[198] Moreover, Ruml's proposal included little about withholding. The presumption was that taxpayers would still pay just as they always had, directly to the Treasury. The problem Ruml worried about was a cash flow or planning problem, not a tax collection problem; it was a problem from the perspective of the tax*payer*, not the tax *collector*.[199]

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[193] *See id.* § 56(b).

[194] His annual income would be 52 × $200 = $10,400. He would be entitled to a $2500 exemption. This would yield taxable income of $7900, and the tax rate was a flat 4%. *See* BLAKEY & BLAKEY, *supra* note 113, at 512.

[195] This was the percentage of the population subject to the income tax in 1933. *See* Jones, *supra* note 163, at 695.

[196] In 1943, the figure was 68.9%. *Id.*

[197] PAUL, *supra* note 26, at 328–29.

[198] *Id.* at 329 (quoting Ruml).

[199] *See* Beardsley Ruml, *Ruml's Own Story*, 21 TAXES 160 (1943).

At the same time, Treasury officials—in particular, Randolph Paul, Treasury's General Counsel and a key player on tax policy issues—realized that the transformation of the income tax into a mass tax had dramatic implications for collections. Among their worries was the problem of tax compliance. Their solution was to bring withholding back to the income tax.[200] So, in November 1941, Treasury Secretary Henry Morgenthau presented to Congress a proposal for collection at source.[201] The idea built on one initially proposed by Albert G. Hart, an economics professor at Iowa State.[202] At first, nothing came of it. Incredibly enough, the Commissioner of Internal Revenue, Guy Helvering, opposed the plan on the grounds that he viewed it as administratively unworkable.[203] Despite Helvering's opposition, though, Morgenthau pushed the idea to Congress in 1942, and the House passed a revenue bill that included a comprehensive set of withholding provisions, applying to dividends and bond interest income, as well as wages.[204] The Senate rejected the House's withholding provisions, but simultaneously passed a bill that included a supplemental tax known as the Victory Tax. The Victory Tax was a flat 5% tax imposed only on salaries and wages for all income above a $624 annual exemption; the tax was expected to last through the end of the war.[205] With this extraordinarily low exemption, the Victory Tax hit nearly every wage earner, and to accomplish this dramatic increase in the tax rolls, the Victory Tax was to be collected through withholding at source.[206] The House agreed to the Senate's version, and with that, the Revenue Act of 1942 re-introduced withholding to the "income tax," albeit for only one portion of the income tax, the Victory Tax.

"With a foot in the door," the Treasury sought to expand withholding to the rest of the income tax.[207] This, however, would have to wait until the following year, and would make its way into law only after colliding with the Ruml plan.

Key, though, was that step by step, withholding was becoming an administrative feature of tax collection. By 1943, income tax withholding

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200 PAUL, *supra* note 26, at 330; JOSEPH J. THORNDIKE, THEIR FAIR SHARE: TAXING THE RICH IN THE AGE OF FDR 252–53 (2013).

201 *See* JOHN MORTON BLUM, FROM THE MORGENTHAU DIARIES: YEARS OF URGENCY 1938–1941, at 316–18 (1964).

202 *Revenue Revision of 1941: Hearings on H.R. 5417 Before the H. Comm. on Ways & Means*, 77th Cong. 330–48 (1941).

203 PAUL, *supra* note 26, at 330–31; THORNDIKE, *supra* note 200, at 254.

204 Revenue Act of 1942, H.R. 7378, 77th Cong. § 153 (1942); H.R. REP. NO. 77-2333, at 125–35 (1942).

205 Revenue Act of 1942, Pub. L. No. 77-753, § 172, 56 Stat. 798, 884–94.

206 *Id.* § 172, 56 Stat. at 888–91; S. REP. NO. 77-1631, at 6–28, 162–74 (1942).

207 Dennis J. Ventry, Jr. & Joseph J. Thorndike, *The Plan that Slogans Built: The Revenue Act of 1943*, TAX ANALYSTS (Sept. 1, 1997), http://www.taxhistory.org/thp/readings.nsf/ArtWeb/671F701C110A19D985256E430079173D?OpenDocument.

was integrated into two different types of income taxes—Social Security taxes and the Victory Tax—both of which applied to the vast majority of employees. The administrative machinery for withholding as a collection method had now been established. Randolph Paul, Henry Morgenthau, and others all understood that the operation of a system of withholding was now workable in a way that it had not been back in 1913.[208] Employers were now used to it, and though there might be opposition, administrative costs and inconvenience would no longer have the salience they had had thirty years earlier.

The central opposition to withholding—besides the Bureau of Internal Revenue's—centered around the transition to current payment: if the system were to switch from payment in the year following the tax liability to current payment, there would be a year (the transition year) during which individuals would have to pay two years' worth of taxes, the past year's and the current year's. Many, including Ruml, described such a state of affairs as akin to "double" taxation. They sought a complete forgiveness of a full year's taxes.[209] Under this way of thinking, shifting to current payment while forgiving the previous year's tax liability in full would continue to provide a consistent uninterrupted flow of tax revenues to the Treasury: "[A]s far as the Treasury and income were concerned, things would move along just the same as time moves on under daylight saving . . . ."[210] Indeed, as an economic matter, there is a good argument that switching to current payment would *increase* the Treasury's revenues, even holding rates and exemptions constant and even with complete forgiveness of the previous year's taxes. If national income increases from one year to the next, the Treasury's revenues would similarly increase.[211]

As economist Charlotte Twight points out, a second potential issue with a switch to current payment involves the time value of money.[212] Requiring taxpayers to pay taxes a year earlier—even if the nominal dollar-value liability is the same—actually constitutes a tax increase. A hundred dollars today is worth more than a hundred dollars a year from now, particularly in an era such as World War II when inflation and nominal interest rates were so high. Knowing the economic sophistication of those advocating the switch to current payment, Twight accuses Treasury officials at the time of "important misrepresentations" because they insisted that withholding did not increase anyone's taxes.[213] This may well have

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208 *See* TWIGHT, *supra* note 30, at 117–18.

209 *Id.* at 109; *Withholding Tax: Hearing on Data Relative to Withholding Provisions of the 1942 Revenue Act Before a Subcomm. of the S. Comm. on Fin.*, 77th Cong. 5 (1942).

210 PAUL, *supra* note 26, at 329 (quoting Ruml).

211 *See Individual Income Tax: Hearings on a Proposal to Place Income Tax of Individuals on a Pay-as-You-Go Basis Before the H. Comm. on Ways & Means*, 78th Cong. 17–18 (1943); TWIGHT, *supra* note 30, at 112–13; PAUL, *supra* note 26, at 335 (citing Ruml).

212 TWIGHT, *supra* note 30, at 105–08.

213 *Id.* at 106.

been the case with respect to the Treasury's plan for withholding, which involved "current payment" and no forgiveness. Indeed, public support for withholding may well have been dependent on the idea of forgiveness.[214] But, recall that withholding can theoretically occur after the liability is incurred, much like, say, the way garnishment of wages for child support works today.[215] Moreover, if an entire year's liability was to be forgiven—as in the initial Ruml plan—the only time-value-of-money problem in the switch to current payment would be for those whose incomes increase, and the problem would only apply to the tax-liability difference between the current and the previous year.

Of course, the Ruml plan, with Ruml's allusion to a "daylight savings" switch, had its own problems, chief among them the perception (and most likely, reality) that forgiveness would lead to a huge boon to the richest Americans in the midst of what was supposed to be a moment of wartime sacrifice. As 1942 wore on and 1943 began, the public conception of withholding became intertwined not only with current payment, but also forgiveness. In the public's mind, the Ruml plan became the face of withholding, and many taxpayers began to think that they would not be required to pay their 1942 taxes (or at least the first quarterly payment) on March 15, 1943, as the law provided. Congressional leaders reminded the country that the law on the books still required that March 15th payment.[216] At the same time, Treasury officials, Democrats in Congress, and the President were all categorically opposed to forgiveness. As Roosevelt put it, "I cannot acquiesce in the elimination of a whole year's tax burden on the upper-income groups during a war period when I must call for an increase in taxes and savings from the mass of our people."[217]

In sum, 1943 saw government officials strongly advocating a new system of current-payment withholding while facing numerous obstacles. Notice, however, that except for Helvering's opposition based on administrative complexity, none of these were problems with withholding per se, but were rather features of "current payment" and in particular, problems only with the transition. This is important, as it meant that opposition was not focused on what turned out to be the most important and lasting change the law was to make: the switch to employer withholding of employees' income tax.

[214] *See id.* at 109–10.

[215] At the time, both England and Australia had tax systems that provided for withholding, but only of tax liability already incurred. So, for example, in Australia, deductions for the tax year ending June 30, 1940, would begin on January 1, 1941. *See* Lent, *supra* note 36, at 720–21.

[216] PAUL, *supra* note 26, at 332; THORNDIKE, *supra* note 200, at 255.

[217] BANK, *supra* note 39, at 101 (quoting W. ELLIOT BROWNLEE, FEDERAL TAXATION IN AMERICA: A SHORT HISTORY 114 (2d ed. 2004)); *see also id.* (Treasury officials noting that forgiveness "would bestow the greatest benefit on those best able to pay and the smallest benefit on those least able to pay").

Given these complexities and objections, the resulting law was not surprisingly a compromise. Roosevelt signed the Current Tax Payment Act of 1943 on June 9th. The law provided for withholding of all income taxes and provided that taxes were to be paid based on current income.[218] The law cancelled 75% of one year of an individual's taxes, based on the lower of the taxpayer's 1942 or 1943 tax liability.[219] To ease the cash flow problem, the unforgiven amount was due in two installments, on March 15, 1944, and March 15, 1945.[220] Importantly, amidst the many compromises that had to be made to get the bill passed, withholding remained a centerpiece of the legislation and garnered little opposition in Congress.[221] Although many Democrats in Congress fumed about the windfall given to the wealthy, the trade-off was probably a small price to pay for what may well have been one of the most transformative changes in the history of the federal tax system. As Professor Jones has put it, the Act "revolutionized the income tax" in large part by helping to "creat[e] a taxpaying culture."[222] By doing this, the Current Tax Payment Act's reintroduction of withholding into the American income tax system helped to "ensure[] the status of the income tax as a major and massive revenue source."[223]

At this point, let me make a disclaimer. I do not intend to argue about whether withholding is a good or bad thing as a normative matter. Others, such as Professor Twight, have indicted withholding as a tool of oppression.[224] To decide whether tax withholding is good or bad, though, one must take a position, whether explicitly or implicitly, on the question of whether the federal government takes in the right amount of revenue, and in the right way. This in turn implicitly assumes a position on the appropriateness of the size of federal spending—indeed, of the federal government itself. Advocates of lower taxes such as Twight have clear views that the federal government is too large, making it easy to reject withholding.[225] Similarly, when Secretary of the Treasury Morgenthau and General Counsel Randolph Paul pushed for withholding, they too had clear

[218] Current Tax Payment Act of 1943, Pub. L. No. 78-68, ch. 120, sec. 2(a), §§ 1621–1622, 57 Stat. 126, 126–35.

[219] *Id.* sec. 6(a)–(c), 57 Stat. at 145–46.

[220] *Id.* sec. 6(e), 57 Stat. at 147–48.

[221] TWIGHT, *supra* note 30, at 114.

[222] Jones, *supra* note 189, at 130, 147.

[223] *Id.* at 130. As with withholding in 1913, there was an attempt to challenge the constitutionality of the withholding provisions in the Current Tax Payment Act of 1943. An employer, Vivien Kellems, refused to withhold and baited the government to indict her. Though the government seized her assets and she sued to recover, she was unable to challenge the statute's constitutionality in court. *See* VIVIEN KELLEMS, TOIL, TAXES, AND TROUBLE (1952); TWIGHT, *supra* note 30, at 120–21.

[224] *See* TWIGHT, *supra* note 30, at 96 ("Withholding . . . is a velvet-gloved . . . manipulation."); *see also id.* ("[T]ax withholding has raised the cost to citizens of perceiving and resisting bloated expropriations of their earnings . . . .").

[225] *See id.*; *see also* Armey, *supra* note 24 ("Our government is too big, and it spends, taxes and regulates too much.").

views on the size of the federal government, though of course they believed the collective good justified the increase in revenues facilitated by withholding. Whatever one's views of the appropriate size of the federal government, however, there is little question that withholding facilitates—indeed, enables—government growth in ways that both proponents and opponents of a large federal government recognize. Whether Twight is correct that federal taxation involved "bloated expropriations of [the public's] earnings,"[226] there is little question that she is correct that returning to the pre-1943 system of having individuals pay their tax liabilities in one chunk would "focus the taxpayer's mind on the cost of government,"[227] most likely increasing opposition to federal income taxes. Moreover, there is little question that the mechanism by which this occurs involves both the "installment" nature of the payments (smaller payments made more often) as well as the less transparent nature of taxation that withholding permits.

It is also most probably the case, as Professor Jones has argued, that the fact that withholding arose in the context of both war and a concerted government propaganda campaign about paying taxes in general helped maintain withholding.[228] Now one might also question whether it is appropriate to use the pejorative term "propaganda" to describe the public relations campaign to induce people to pay taxes. One might instead simply call it an effort to prevent law breaking on the part of a massive number of new taxpayers. In any event, the simple descriptive point is clear, and it applies both as a historical fact about the introduction of withholding into the modern federal income tax system and as a contemporary statement about the likely psychological impact of withholding on current taxpayers: withholding has enabled, and continues to enable, a much larger federal government than we would have without it. How much larger is anyone's guess, but it would be hard to dispute "larger."

This larger federal government is one sense in which the Current Tax Payment Act of 1943 can be thought of as a superstatute. A second, related sense is the way it fundamentally structures the relationship between the individual and the federal government. By placing the employer in a position of providing money directly to the federal government on behalf of the taxpayer, withholding helps mediate that relationship. This, of course, is why April 15th takes on such importance in taxpayers' minds. Withholding makes income tax filing the focus of the taxpayer's relationship with the government by shielding the taxpayer from the relationship during the rest of the year.

[226] TWIGHT, *supra* note 30, at 96.

[227] *Id.* at 97.

[228] Jones, *supra* note 163.

CONCLUSION

Is the Current Tax Payment Act of 1943 a superstatute? If we ignore the courts altogether, we have some reasons to think so. First, it structures the relationship between individuals and the state in a fundamental way; it constitutes, so to speak, that relationship. Second, it is entrenched in a de facto sense. That entrenchment plays itself out in the way policy advocates on all sides of the political spectrum have largely treated withholding of taxes on wage liability as an assumed part of the tax policy landscape. Third, the fact that the law is entrenched is both a historical consequence of what Eskridge and Ferejohn refer to as "administrative constitutionalism" and a spur to an even more complex administrative structure that effectively provided a positive feedback loop to entrench the law further. In that sense, it fits perfectly into the concept of a superstatute.

It is probably not entrenched, however, in at least one of the ways Eskridge and Ferejohn implicitly view superstatutes. The statute has not really embedded a value or norm into the public consciousness. Withholding is not, in Eskridge and Ferejohn's words, a norm or practice that is accepted "because of the force of a Weberian constellation of interests, namely, a popular consensus that the norm or practice is a good thing to believe or do."[229] It is simply part of the underlying fabric of tax collection and enforcement. While tax wonks might view it as a "good thing to . . . do" (or not), the public is simply not conscious of it (despite being quite conscious of taxes as a general matter). The law might thus be viewed as akin to a coordination benefit like driving on the right side of the road.

Thought of through this lens, perhaps even opponents of the policy effects that withholding of wage income entails (e.g., better enforcement of tax liability for wage income; possibly comparatively better tax evasion potential for income from nonwage sources) are willing to accept withholding because eliminating it would cause enough other negative effects. Yet, that doesn't seem quite right either. As I noted in Part I, eliminating withholding would be an extremely good policy for anyone who advocates a reduction in actual federal tax revenues.

Finally, there is one other very important way in which the Current Tax Payment Act of 1943 cannot even remotely be viewed as a superstatute. It has had virtually no effect on judicial interpretations of the large "C" Constitution. We might say that authority for the federal government to collect income taxes via withholding is now embedded into the Sixteenth Amendment. Beyond that somewhat minor constitutional holding, however, it is difficult to imagine what else the extensive history of withholding has done to the large "C" Constitution or judicial interpretations of it.

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229 *See* ESKRIDGE & FEREJOHN, *supra* note 5, at 13.

In the end, then, what the history of federal tax withholding tells us is that there may well be entrenched statutes littered throughout the law, statutes that evoke no value of any kind and yet are fundamental to the operation of the government. Whether one views such statutes as "super" enough may well be just a function of how important public values or norms are to the definition of a superstatute.