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# WHY A WEALTH TAX IS DEFINITELY CONSTITUTIONAL

*By John R. Brooks & David Gamage\**

*(Draft of January 9, 2020)*

Wealth tax reform proposals are playing a major role in the 2020 presidential campaign. In particular, two leading Democratic primary candidates—Elizabeth Warren and Bernie Sanders—have proposed wealth tax reforms as central components of their campaign platforms. These candidates claim their wealth tax reforms would raise substantial revenues from the super rich, to fund proposed new spending programs for the middle class. However, some opponents of these wealth tax reform proposals have claimed that a wealth tax would be unconstitutional.<sup>1</sup> Other prominent critics have argued that wealth tax reforms are probably unconstitutional, so that, after review by the courts, the “likeliest outcome is that a wealth tax will raise exactly zero dollars.”<sup>2</sup>

These claims are wrong. More precisely, these claims are wrong because wealth tax legislation can be drafted to comply with the strictest interpretation of the Constitution, while still being fair and administrable. As we will explain in this essay, properly drafted, wealth tax reform legislation is definitely constitutional and thus capable of raising substantial revenues to fund new spending programs for the middle class.

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<sup>1</sup> E.g., <https://thefederalist.com/2019/08/08/heres-elizabeth-warrens-wealth-tax-completely-unconstitutional/>; <https://www.washingtonexaminer.com/opinion/memo-to-democrats-a-wealth-tax-is-unconstitutional/>; <https://usatoday.com/story/opinion/2019/11/15/elizabeth-warren-bernie-sanders-wealth-tax-plan-unconstitutional-irs-column/2577982001/>.

<sup>2</sup> <https://www.nytimes.com/2019/11/07/opinion/wealth-tax-constitution.html>

Without a doubt, there are constitutional uncertainties surrounding some wealth tax reform proposals, which is why even some progressive scholars and activists argue that reforms should focus on shoring up the income tax instead. These arguments tend to overlook the similar constitutional uncertainties surrounding competing reform proposals like mark-to-market and progressive consumption taxation.<sup>3</sup> Nevertheless, it is a step too far to claim that any of these reform proposals would be unconstitutional (at least without qualifications about poor legislative drafting). Quite the contrary, so long as the legislation enacting any of these options for reform is drafted with sufficient care, all of these reform options can fit squarely within the strictest readings of the Constitution.<sup>4</sup>

This essay summarizes some of the analysis that we are in the process of developing in much greater depth in a work in progress, and that we plan to ultimately publish in a law review format. Because we worry that misunderstandings about the constitutionality of wealth tax reform proposals are currently muddying public debates, we are making this short summary of our analysis available now so as to correct the record.

The Constitution specifies two paths for assessing a new federal tax. As

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<sup>3</sup> If the 16<sup>th</sup> Amendment is to be interpreted narrowly, then either or both of mark-to-market reform proposals and cash-flow progressive consumption tax reform proposals could be held to be direct taxes that would need to follow the apportionment path in order to be constitutionally valid, which raises essentially the same issues as with our discussion of a new federal wealth tax in the body of this essay. Indeed, a least one notable scholar has recently argued that both mark-to-market reforms and cash-flow progressive consumption tax reforms should be held to the same standards as wealth tax reforms (Erik Jensen). If the Supreme Court is inclined to interpret the 16<sup>th</sup> Amendment narrowly, to exclude wealth tax reforms, we thus think it likely that the Supreme Court would also be inclined to exclude mark-to-market reforms and possibly also cash-flow progressive consumption tax reforms.

With respect to mark-to-market reforms in particular, part of the question is whether existing Supreme Court precedent interpreting the 16<sup>th</sup> Amendment requires something like realization in order to distinguish income from wealth. *Macomber*; *Glenshaw Glass*. While the Internal Revenue Code already uses accrual taxation in narrow circumstances (OID, 475), comprehensive mark-to-market could potentially raise new and different issues. To be clear, we do not agree with this view. But a Supreme Court that would strike down a wealth tax very well could agree.

<sup>4</sup> By this, we mean that there is no reasonable reading of the Constitution that could support striking down a properly drafted version of these reforms. We cannot completely guarantee that the Supreme Court might not go rogue and disingenuously rule against the plain text of the Constitution and prior precedents; but we think it exceedingly unlikely that the Supreme Court would go rogue to that extent, and a Supreme Court inclined to go rogue to that extent might potentially strike down any piece of legislation no matter how sound its constitutionality (including, *inter alia*, alternative income tax reforms).

we will explain, a wealth tax reform can be drafted so as follow either of these paths, and then fallback clauses can be drafted to cope with the uncertainty about which of these paths the Supreme Court might rule a wealth tax must follow in order to be constitutional. In that way, the legislation can be constitutional regardless of which path the Supreme Court demands.

The first path applies to “[indirect] taxes,”<sup>5</sup> “duties, imposts, and excises,”<sup>6</sup> and “income taxes.”<sup>7</sup> This path requires that the federal tax be *uniform*. That is, the federal tax rates must be the same in every state. All current federal taxes follow this path, which we will call the “uniformity path.”

The second path applies to “direct taxes.”<sup>8</sup> This path requires that the federal tax be *apportioned*, rather than that it be uniform. That is, the federal tax must raise the same revenue per capita from every state. Because some states have wealthier populations, this path would require that federal wealth tax rates be set lower in wealthier states and higher in less-wealthy states. We will call this path the “apportionment path.”

Constitutional and tax scholars disagree about which of these paths should apply to a new federal wealth tax.<sup>9</sup> Many have made strong arguments that a comprehensive wealth tax is not a “direct tax,” and therefore should be uniform, rather than apportioned. Our view is that, even if a comprehensive wealth tax would have been a “direct tax” at the founding, the 16<sup>th</sup> Amendment should be interpreted broadly to encompass wealth tax reforms—as well as encompassing mark-to-market reforms, progressive consumption tax reforms, and other reform proposals designed to assess tax based on comprehensive measurements of ability to pay.<sup>10</sup> In essence, this is because the lines between what is “income” and what is “wealth” (and, for that matter, what is “consumption”) are fluid and contingent, and it is likely impossible to give Congress the tools it needs to tax income without also thereby giving it the tools to tax wealth or other measures of ability to pay. In contrast, the doctrines and interpretive tools that courts would use to prohibit wealth taxation would end up also severely

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<sup>5</sup> U.S. CONST. art. I., § 8, cl. 1.

<sup>6</sup> U.S. CONST. art. I., § 8, cl. 1.

<sup>7</sup> 16<sup>th</sup> Amendment

<sup>8</sup> U.S. CONST. art. I., § 2, cl. 3.

<sup>9</sup> E.g., Bruce Ackerman, Calvin Johnson, Dawn Johnsen, Walter Dellinger, Joseph Dodge, Erik Jensen, etc.

<sup>10</sup> Our view builds on prior work by Ari Glogower, among others.

undermining income taxation. Under this view, the Supreme Court's necessary deference to Congress in applying the 16<sup>th</sup> Amendment to the federal income tax also authorizes a uniform federal wealth tax.

However, we cannot predict with any confidence whether the Supreme Court would agree with our views on this question.<sup>11</sup> The jurisprudence on direct taxes—nearly all of which occurred in the 19<sup>th</sup> century—is admittedly confusing and sometimes contradictory. And the history and interpretation of the 16<sup>th</sup> Amendment is also disputed, with some scholars saying it was clearly intended to overrule *Pollock*, and others disagreeing. The Supreme Court has simply not provided sufficient indication in the past as to how it would rule on the question of whether a new federal wealth tax would need to be designed in accordance with the uniformity path or the apportionment path.<sup>12</sup> This is why there are constitutional uncertainties surrounding wealth tax reforms, and why we propose that a new federal wealth tax should be designed first to follow the uniformity path (in accordance with our view as to how the Supreme Court should rule), but then with fallback clauses specifying as a backup option how the new federal wealth tax would be redesigned to follow the apportionment path in case the Supreme Court were to rule that this is the required route.

Designing a federal wealth tax to follow the uniformity path is the easier route, apart from constitutionality concerns. All existing federal taxes were designed in accordance with the uniformity path, and this is thus the path that Congress, scholars, and the public are the most familiar with. All that is required to design a federal wealth tax in accordance with the uniformity path is for the wealth tax to assess the same tax rates in every state and geographic region, just like we do for the federal income tax.

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<sup>11</sup> Consider that Bruce Ackerman, a leading advocate of the position that a wealth tax should be constitutional under the uniformity path, recently concluded an essay written to refute arguments by Daniel Hemel and Rebecca Kysar as to why a wealth tax would “very likely” need to instead be designed to follow the apportionment path, with “Nobody can say how [the Supreme Court will rule as to a new federal wealth tax. . . .] Sorry, but my crystal ball clouds over at this point.”; <https://prospect.org/justice/why-are-liberal-democrats-leading-the-constitutional-campa/>

<sup>12</sup> In addition to our view that the 16<sup>th</sup> Amendment should be interpreted broadly to encompass wealth tax reforms, a number of other scholars have argued on different, but related, grounds for why a new federal wealth tax should be constitutional if designed in accordance with the uniformity path. See, e.g., Ackerman, Johnson, Johnsen & Dellinger. But other scholars have disputed these conclusions, arguing that a new federal wealth tax would only be constitutional if designed in accordance with the apportionment path, *see*, e.g., Dodge, Jensen. Importantly, there are no scholarly arguments concluding that a federal wealth tax would be unconstitutional under both paths; rather, the debate has been entirely about which path a new federal wealth tax would need to follow.

Yet it is also possible to design a federal wealth tax in accordance with the apportionment path. Although this route would be somewhat more complicated than following the uniformity path, these extra complexities are relatively minor and readily manageable as compared to other issues involved in designing a major new federal tax reform.<sup>13</sup>

Consider that, between 1798 and 1861, Congress five times levied direct taxes designed to follow the apportionment path.<sup>14</sup> These direct taxes were not comprehensive wealth taxes, but instead were taxes on specified forms of wealth, such as real estate (and slaves). The first four of these direct taxes worked reasonably well. But the fifth—the Direct Tax of 1861—created numerous problems. The reason was the Civil War.

Scholars disagree about why the founders wrote the apportionment requirement for direct taxes into the Constitution. One view is that this was all about protecting slavery from being taxed more than other forms of wealth. (The scholars who take this view generally conclude that a federal wealth tax should be authorized under the uniformity path, as the 13<sup>th</sup> Amendment has mooted the issues related to taxing slavery.) But other scholars argue that the apportionment requirement was meant to serve a broader state sovereignty purpose—beyond just protecting slavery—and thus conclude that a federal wealth tax could only be authorized following the apportionment path. Perhaps the leading advocate of this view argues that the goal behind the apportionment requirement for direct taxes was for state governments to be able to act as a buffer between state residents and direct federal taxes by tying direct tax liabilities to representation.

Regardless of the founders' intentions, this institutional arrangement of allowing state governments to act as a buffer between taxpayers and the federal government's direct taxing power proved rather problematic at a time when some state governments were in open revolt. Consequently, although the Direct Tax of 1861 was largely successful in raising revenues from the Union states, questions of what to do about taxpayers in the Confederate states created lingering controversy.<sup>15</sup> As a result, this historical

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<sup>13</sup> For some early thoughts by one of us on some of the other, relatively less minor, issues involved in designing a new federal wealth tax, see David Gamage, *Five Key Research Findings on Wealth Taxation for the Super Rich*, available at SSRN: <https://ssrn.com/abstract=3427827>.

<sup>14</sup> For discussion, see, e.g., Charles F. Dunbar, *The Direct Tax of 1861*, 3 QUARTERLY J. OF ECON. 436 (1889); John Joseph Wallis, *A History of the Property Tax in America*.

<sup>15</sup> For elaboration, see Joseph J. Thondike, *Tax History: Federal Wealth Taxes Have a*

episode “effectively discredited” direct taxes, and Congress has not seriously considered levying a direct tax since 1861.<sup>16</sup>

However, modern tools of tax administration and fiscal federalism would make it much easier to levy an apportioned direct tax today. Before we explain why, we should acknowledge that our contributions on this topic build on prior work by John Plecnik, who has previously argued for one possible approach for designing a federal wealth tax in a manner that he argues would satisfy the apportionment requirement.<sup>17</sup>

Plecnik’s approach would involve the federal government levying a uniform federal-level wealth tax—with the same federal tax rates in every state—but with the federal government then immediately refunding to the taxpayers the amount needed to have the total revenue collected satisfy the apportionment requirement. State governments would then be allowed or encouraged to enact “pick-up” taxes, which would essentially confiscate the amounts of these refunds. If state governments fully used this power, the end result for taxpayers would be the same as paying a single-rate wealth tax, but with that total tax revenue split between state and federal tax rates.<sup>18</sup>

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*Long and Uneasy History*, 165 TAX NOTES FEDERAL 1264 (NOV. 25, 2019).

<sup>16</sup> Dunbar, at 461.

<sup>17</sup> John T. Plecnik, *The New Flat Tax: A Modest Proposal For A Constitutionally Apportioned Wealth Tax*, 41 HASTINGS CONST. L.Q. 483 (2014).

<sup>18</sup> To elaborate the brief explanation in the text above, Plecnik’s approach would begin by levying a single, national federal wealth tax rate in each state. Then, Plecnik’s approach would have the federal government keep only a portion of the wealth tax revenues raised from each state, an amount calculated by multiplying each state’s population by the per-capita wealth tax revenues raised in the state with the smallest per-capita wealth tax base. The rest would be refunded to the taxpayers, in proportion to their tax payments. Thus, all of the revenues raised in the state with the smallest per-capita wealth tax base would remain with the federal government, whereas much of the revenues raised in states with larger per-capita wealth tax bases would be refunded to taxpayers.

Plecnik then proposes allowing or encouraging states to claim those refunds through a state-level “pick-up” tax, similar to the pre-EGTRRA credit for state estate taxes under I.R.C. § 2011. If states exercised that ability fully, then taxpayers would be in the same circumstances as if the federal government had just kept all the initial tax payments.

Plecnik argues that the end result would be a uniform combined wealth tax rate – that is, the same combined rate levied in every state – but with states differing in how much of the revenue from that combined rate tax goes to the the federal government (as opposed to the state government). As Plecnik explains, “[t]his approach is not only horizontally equitable as between taxpayers in different states, but it complies with the letter and spirit of the Apportionment Clause. It complies with the letter of the law, because each state pays no more than its apportioned share to the federal government. In addition, this approach complies with the spirit of the law because no state is enriched at another’s expense. . . . Thus, there is no realistic concern that federal and state “pick up” wealth taxes would be collapsed as one through the substance-over-form or step transaction doctrines. There is

Although we applaud Plecnik's thinking on this issue and, indeed, we build on his contributions in this essay, we ultimately think that Plecnik's proposals are not the best way to design an apportioned federal wealth tax. One issue with Plecnik's approach is that it would raise only limited revenues for the federal government, because much of the revenues raised by the combined state- and federal-level wealth tax rates would go to state governments.

Thus, Plecnik's approach could perhaps work reasonably well if the primary goal of a new federal wealth tax were to address distributional concerns or to help fund state government spending programs, rather than raising substantial new federal revenues.<sup>19</sup> But, even then, his approach depends on state governments choosing to enact a pick-up tax to fully collect the federal refunds. Plecnik claims state governments would do so in order to seize a source of free revenue (and if not, that the federal government could use some sticks and carrots to encourage them to do so). But the politics are still questionable—that revenue is hardly “free.” Wealthy taxpayers in poor states exert disproportionate power, and it is quite likely that they would strongly resist a perceived state-level wealth tax on top of a federal tax if it resulted in them paying a greater share of their wealth in total taxes compared to the wealth in neighboring states.

For this reason, we prefer a somewhat different approach for designing a new federal wealth tax to follow the apportionment path. Our approach would begin with Congress first legislating the desired nationwide annual revenue targets for the new tax.<sup>20</sup> The apportionment requirement would then result in different state-specific federal wealth tax rates, with these state-specific federal rates being set lower in wealthier states and higher in

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nothing unconstitutional or untoward about a state leveling direct taxes without apportionment; the states have done so throughout history and they continue to do so through various property taxes.” Plecnik at 514-15.

<sup>19</sup> Indeed, David Hasen has praised Plecnik's proposals for this reason. David Hasen, *Accretion-Based Progressive Wealth Taxation*, 20 FLA. TAX REV. 277, 304-05 (2017).

<sup>20</sup> For any given estimate of the nationwide wealth tax base, the desired nationwide annual revenue targets are mechanically equivalent to the desired nationwide average tax rates (which is presumably what Congress would specify for a uniform federal wealth tax). That is, a nationwide revenue target could be calculated by multiplying the desired nationwide average federal tax rates by the CBO's estimate of the nationwide wealth tax base for each year. In this manner, the tax rates specified for a uniform federal wealth tax could be converted into revenue targets for an apportioned federal wealth tax that could operate as a fallback option in case the Supreme Court strikes down the uniform federal wealth tax.



less-wealthy states.<sup>21</sup> In other words, in contrast to Plecnik's proposal, the enacted federal wealth tax would be apportioned in the first instance, with non-uniform rates across the states.<sup>22</sup>

We think that the best approach for implementing the apportionment requirement – so as to set lower state-specific federal tax rates in wealthier states and higher state-specific federal tax rates in less-wealthy states – would be to follow a variation on the methods used by the Direct Tax Act of 1813.<sup>23</sup> The 1813 Act had the Committee of Ways and Means set county-specific tax rates for every county in each state; however, for a modern implementation of this approach, it would probably be better to delegate the task of setting the annual tax rates to the Treasury Department or the IRS<sup>24</sup>

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<sup>21</sup> As an intermediate step, the nationwide annual revenue targets could be divided into separate revenue quotas for each state, with the revenue quotas apportioned on a per-capita basis. State-specific wealth tax rates could then be calculated based on the estimates of the rates needed to meet each state's revenue quota.

<sup>22</sup> An alternative approach that would also be viable would be to begin with uniform federal-level wealth tax rates, and then have the Treasury Department calculate partial rebates to be provided to taxpayers in wealthier states so as to satisfy the apportionment requirement. However, unless the uniform federal-level wealth tax rates were set equal to the rates needed in the least wealthy state (such that taxpayers in every other state would receive partial rebates) this approach would raise less revenue for the federal government. We thus think it is somewhat simpler and more straightforward to begin with different, state-specific federal tax rates, as we explain above.

<sup>23</sup> See Dunbar, at 441-44.

<sup>24</sup> So long as the delegation instructions are clear and sufficiently precise, there should not be any non-delegation doctrine issues involved in delegating the setting of state-specific federal tax rates to Treasury or the IRS. Indeed, Congress already delegates to the IRS the task of annually adjusting federal income tax brackets to account for inflation, for example. Delegating the task of annually setting the state-specific federal wealth tax rates in accordance with the apportionment requirement could work similarly.

That said, a concern arises (and we thank Daniel Hemel for bringing this concern to our attention) that it is at least theoretically possible that some less-wealthy states might lack a sufficient tax base of wealthy taxpayers subject to the federal wealth tax for the state-specific federal tax rates in these states to be set high enough to satisfy the apportionment requirement. To address this concern, we recommend that the enacting legislation specify a maximum cap on the state-specific federal wealth tax rates (say 10%). If these maximum rates would not suffice to raise sufficient funds in any less-wealthy state to satisfy the apportionment requirement, then we recommend that the enacting legislation further specify a back-up residual tax that would go into effect in those states, similar to the approach used in the Direct Tax Act of 1798. (The 1798 Act levied uniform federal tax rates on houses and slaves, along with a residual tax on land within each state, with the amount of the residual tax owed within each state calculated separately "as a residual after the amount of tax derived from the first two categories was subtracted" so as to satisfy the overall apportionment requirement for direct taxes. Judith Green Watson, *A Discovery: 1798 Federal Direct Tax Records for Connecticut*, available at <https://www.archives.gov/publications/prologue/2007/spring/tax-lists.html>. See also Davis

and to only set state-specific tax rates rather than county-specific tax rates.<sup>25</sup> In any case, the apportionment requirement would be satisfied by setting different, state-specific federal wealth tax rates in each state, with these rates being set lower in wealthier states and higher in less-wealthy states.<sup>26</sup>

On its own, this might seem inequitable. But consider that, for the existing U.S. income tax, combined federal- and state-level rates already differ amongst the states. For instance, the highest capital gains tax rate is currently 13.3 percentage points higher in California than in Florida.

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R. Dewey, *Financial History of the United States* at 109-110).

There are several potential ways to design this residual tax, and we will explore them in our longer work. As illustration, one possibility is for the base of this residual tax to be all property within each applicable state that is subject to that state's property tax laws and that is valued above a specified threshold by that state's property tax system. For instance, the threshold could be set at \$1M, so that all property valued at over \$1M would be subject to the residual tax, but with the residual tax rate applying only to the valuation amounts in excess of that \$1M threshold. The state-specific rate of this residual tax would be set at whatever level is needed to raise the additional revenues required to satisfy the apportionment requirement for each applicable state, to the extent that this is needed after capping the state-specific federal wealth tax rates. If desired, the enacting legislation could also offer state governments the option of raising these residual funds from some other method, similar to the options provided to state governments under the Direct Tax Acts of 1813 through 1816; *see* Thorndike.

This approach for designing the residual tax has appeal because every state already has a property tax, and so no new valuation rules or other base-definition rules would be needed for a federal residual tax designed to piggyback on existing state property tax systems. By contrast, other possible approaches for designing a residual federal direct tax would be more complicated, because there are no existing federal direct taxes to piggyback on and no other existing state level direct taxes with sufficiently broad bases that are levied in every state.

<sup>25</sup> Indeed, the Direct Tax Act of 1815 abandoned the 1813 Act's approach of apportioning at the county level, and instead apportioned at the state level, like we recommend. Dewey at 141 ("These taxes were apportioned among the States on the census of 1810, and the first act [the 1813 Act] went so far as to apportion to each county in the several States the amount it should pay, thereby creating great inequities. To avoid this evil the second act [the 1815 Act] did not attempt to apportion the quotas among the counties . . . . In view of the infrequent attempts throughout our history to levy a direct tax, it is suggestive to note that the several assessments made upon the States were met with a fair degree of exactitude and promptness. If there was an unequal incidence, there was little grumbling, thus showing the distinct advance from the disastrous policy of requisitions under the Confederacy.")

<sup>26</sup> It is worth noting that one possible advantage of both Plecnik's proposal and the alternative we discuss in note 23, *supra*, is that it would be somewhat simpler administratively to assure proper apportionment, because the rebates would be based on the amount of revenue actually raised, rather than an ex ante estimate of the wealth tax base in each state. However, seeing at the Direct Tax Acts of 1813 and 1815 calculated the state-specific tax rates needed for apportionment based on ex ante estimates of the wealth tax base, we do not view this as a substantial obstacle.

Because all existing federal taxes follow the uniformity path, federal-level tax rates are currently set the same in every state, with state-level piggyback taxes then making the combined tax rates unequal. Yet, in our federal system, what ultimately matters to taxpayers isn't the rate levied by just one level of government, but rather the overall combined state-and-federal-level rate. Therefore, we can make our apportioned wealth tax fair—that is, sufficiently uniform—by combining it with state-level credits or rebates facilitated by federal block grants provided to state governments through a fiscal equalization program.

Congress could implement this through two steps. First, Congress could streamline state governments' ability to levy piggyback taxes, credits, or rebates for the new wealth tax. (This is already being done with the existing income tax, which is why state-level income taxes use relatively simple forms based on information from the federal-level returns.) Thus, the less-wealthy states could just allow a credit against their own taxes for any "excess" wealth tax paid to the federal government, thus leaving taxpayers with uniform overall rates.

Second, Congress could implement a fiscal equalization system to ensure that the governments of less-wealthy states have sufficient funds to rebate the combined wealth tax rates down to the nationwide average levels, to the extent that these state governments opt to do so. To achieve this, the enacting legislation could specify that the state-specific tax rates set for the wealthiest state be set equal to the rates Congress would have desired for a uniform federal wealth tax, so that the state-specific rates would then be set higher in every state other than the wealthiest.<sup>27</sup> Then, Congress would take the "extra" revenue raised from each state (except the wealthiest) and send it back to each state's government as a block grant. This would give every state's government the extra revenues needed to fund state tax credits, thereby reducing the *combined* federal- and state-level wealth tax rates down to the level specified for the wealthiest state—the level that Congress would have desired for a uniform federal wealth tax.

Whereas Plecnik's proposal arguably satisfies the apportionment requirement, our approach clearly satisfies the apportionment requirement and should thus reduce the constitutional risk to nil (at least assuming the

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<sup>27</sup> This need not be done as part of the legislation enacting the wealth tax. Congress could alternatively wait to see how the Supreme Court rules and only legislate a fiscal equalization system if the Supreme Court ultimately holds that the wealth tax needs to be apportioned, with the fiscal equalization system then being enacted through subsequent legislation following such a Supreme Court decision.

legislation is well drafted).<sup>28</sup> This is because, under our approach, the federal wealth tax would be apportioned in the first instance, rather than only after combining it with refunds. Because our proposed fiscal equalization program would then channel excess revenues to state governments, rather than to taxpayers, the Apportionment Clause would not be implicated. Then, our approach would ask state governments to credit or rebate the extra federal funds received to the states' taxpayers, rather than asking that state governments affirmatively levy what might be considered new taxes. Thus, the wealthy taxpayers that might attempt to block the new state-level pick-up taxes under Plecnik's proposal should instead be the strongest supporters of using the revenues that state governments would receive from the federal government under our proposal to fund state-level credits or rebates. At the same time, because it is ultimately up to each state's government whether to credit, it would be virtually impossible for a court to combine all the possibilities when testing for apportionment.

Our proposed fiscal equalization step may sound complicated at first. But consider that fiscal equalization systems of this sort already exist in Canada, Australia, and other federal nations, and have been proposed for the United States.<sup>29</sup> Moreover, existing federal grants to state governments, such as through Medicaid and Title I of the Elementary and Secondary Education Act, already operate as a form of fiscal equalization, and "General Revenue Sharing" under the State and Local Fiscal Assistance Act of 1972 made unrestricted grants directly to states and municipalities based in part on income and need, prior to its repeal under President Reagan.<sup>30</sup> It would thus be relatively straightforward for Congress to implement a new

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<sup>28</sup> Because the fiscal equalization funds would be granted to the governments of the less-wealthy states, rather than the taxpayers within those states, leaving it up to the discretion of each state's government whether and to what extent to rebate those funds to the taxpayers within each state, we think it exceedingly unlikely that the Supreme Court would rule that our proposed approach would not satisfy the apportionment requirement. That said, we are not completely confident that there is no plausible reading of the Constitution that might support the Supreme Court ruling that our proposed fiscal equalization program might violate the apportionment clause when combined with apportioned federal wealth tax rates. To address this possibility, enacting legislation could also include severance instructions that would drop out the fiscal equalization system, while retaining the rest of the wealth tax, were the Supreme Court to so rule. To address the inequities that such a ruling could cause (in the exceedingly unlikely event of the Court ruling in this manner), Congress could then subsequently implement an independent fiscal equalization system (of the sort we have proposed) in new legislation following such a Supreme Court decision.

<sup>29</sup> See Kirk J. Stark, Rich States, Poor States: Assessing the Design and Effect of a U.S. Fiscal Equalization Regime, 63 TAX L. REV. 957 (2010).

<sup>30</sup> <http://www.jct.gov/s-1-73.pdf>

fiscal equalization system as part of enacting an apportioned federal wealth tax. This would provide less-wealthy state governments the funds needed to rebate their residents' wealth tax burdens down to the desired nationwide average levels.

Ultimately, it would be up to each state's government to decide how much of a rebate to offer to the state's taxpayers, or even whether to instead levy an additional state-level piggyback tax. Thus, just as wealthy Californians currently face higher overall capital gains tax rates as compared to wealthy Floridians, different state governments might make different choices with respect to a new apportioned wealth tax, resulting in the wealthy residents of some states having higher tax burdens than others. But this is a natural consequence of the constitutional structure of our fiscal federation, wherein the federal government has limited powers to infringe on state governments' fiscal domains.<sup>31</sup> The precise nature of how the federal government must act in deference to state government's fiscal discretion is somewhat different for apportioned taxes than for uniform taxes—which results in the need for a fiscal equalization system to achieve equity for an apportioned federal wealth tax and not for a uniform federal wealth tax. But the broader picture remains the same: the Constitution protects state governments' fiscal discretion from undue infringement by the federal government's taxing powers.<sup>32</sup> Accordingly, our proposal is consistent not only with the text of the Constitution, but also with the balancing of federal and state fiscal interests that the Apportionment Clause represents.

We have thus explained how Congress could legislate a federal wealth tax that would definitely survive scrutiny under either the uniformity or the apportionment path. But, then, what to do about the fact that we do not yet know how the Supreme Court would rule as to which of these paths a new federal wealth tax would need to follow?

The solution here is fallback clauses. Both the structure of the Constitution and prior Supreme Court precedent are absolutely clear that Congress can write instructions for what is to happen if portions of legislation are held unconstitutional. The only challenges are that Congress must write such instructions unambiguously and the fallback options must

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<sup>31</sup> See David Gamage and Darien Shanske, *The Federal Government's Power to Restrict State Taxation*, 81 STATE TAX NOTES 547 (2016).

<sup>32</sup> *Id.*; see also David Gamage and Darien Shanske, *Tax Cannibalization and Fiscal Federalism in the United States*, 111 NORTHWESTERN UNIVERSITY LAW REVIEW 295, 353-69 (2017).

themselves be constitutional.<sup>33</sup> For a new federal wealth tax, this means that Congress should write instructions clearly specifying that if the wealth tax is held to be unconstitutional under the uniformity path then a modified version of the wealth tax designed in accordance with the apportionment path should then go into effect.

Drafting these instructions into legislation would involve some additional challenges beyond what we can explain here. But the overall task is very manageable in the context of designing a major new tax reform. The bottom line is that carefully drafted federal wealth tax legislation would be definitely – without any doubt – constitutional.

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<sup>33</sup> See, e.g., *Bowsher v. Synar*, 478 U.S. 714, 735-36; Tom Campbell, *Severability of Statutes*, 62 HASTINGS L.J. 1495 (2011); Michael C. Dorf, *Fallback Law*, 107 COLUM. L. REV. 303 (2007).