No. 22-800

IN THE

Supreme Court of the United States

CHARLES G. MOORE and KATHLEEN F. MOORE,

Petitioners,

v.

UNITED STATES OF AMERICA,

Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit

BRIEF FOR PETITIONERS

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QUESTION PRESENTED

Whether the Sixteenth Amendment authorizes Congress to tax unrealized sums without apportionment among the states.

PARTIES TO THE PROCEEDING AND RULE 29.6 STATEMENT

Petitioners Charles and Kathleen Moore were plaintiffs in the district court proceedings and appellants in the court of appeals proceedings.

Respondent United States of America was the defendant in the district court proceedings and appellee in the court of appeals proceedings.

Because no petitioner is a corporation, a corporate disclosure statement is not required under Supreme Court Rule 29.6.

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INTRODUCTION

The Sixteenth Amendment empowers Congress "to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States." The Constitution originally required apportionment of all "direct taxes," which the Court in *Pollock v. Farmers' Loan & Trust Co.*, 158 U.S. 601, 637 (1895), held to include taxes on "the income of real estate, and of personal property," such as rents and dividends. The Amendment's framers drafted its text to overrule that holding while retaining the apportionment requirement for other direct taxes, including taxes on property. That is why its reach is limited to "taxes on *incomes*." Then, as now, income was understood to refer to gains realized by a taxpayer through payment, exchange, or the like, not mere increase in the value of property. Appreciation in the value of a home or other asset is not income—at least, not until it is sold and the gain is realized. Realization is not only what distinguishes income from property in general, but what makes income income.

That was the holding of the Court's Sixteenth Amendment landmark, *Eisner v. Macomber*, 252 U.S. 189 (1920). The "characteristic and distinguishing attribute of income" is that "a gain, a profit, something of exchangeable value" is "*received* or *drawn* by the recipient (the taxpayer) for his *separate* use, benefit and disposal." *Id.* at 207 (emphases in original). "Nothing else answers the description." *Id.* Accordingly, mere "enrichment through increase in value of capital investment is not income in any proper meaning of the term." *Id.* at 214–15. The Court has never retreated from *Macomber*'s core holding on realization; to the contrary, its precedent from that era to the modern day consistently observes the necessity of realization to income. Congress, too, has accepted that understanding, structuring federal income taxes to turn on taxpayer realization.

With one recent exception. Enacted to offset the cost of a 2017 corporate tax reform, the Mandatory Repatriation Tax was designed to achieve a one-time windfall in tax revenue from earnings that had been accumulated by foreign corporations with U.S. owners over the preceding three decades. Rather than encourage those corporations to make distributions with a favorable tax rate, as Congress had previously done, the MRT simply deems their accumulated earnings to be the "income" of whoever happened to own the requisite number of shares on an arbitrary date in 2017. Unlike with other income-attribution schemes, MRT liability does not turn on constructive realization of income by those being taxed; instead, it turns on ownership of a specified asset at a specified time. It is a tax on property, not income in any sense of the word. Petitioners Charles and Kathleen Moore were hit with MRT liability because they are minority shareholders in a foreign corporation that reinvested its earnings to grow its business, without distributing a penny to them—and it may well never. Yet the MRT tagged them with $132,512 in 2017 "income" and taxed them on it.

Because it was undisputed that the Moores had realized nothing, to uphold their tax liability the Ninth Circuit was compelled to hold that "realization of income is not a constitutional requirement" for an income tax under the Sixteenth Amendment. Pet.App.12. That radical notion stands in conflict with the Amendment's original meaning, this Court's longstanding precedent, and a century of constitutional practice. Worse, it renders the Constitution's apportionment requirement a dead letter, opening the door to unapportioned taxation of anything that Congress might deem a person's "income," from property to growth in retirement investments to uncertain or even fictional gains. The Constitution's Framers were wary of direct taxation because they knew it could be used to work "partiality or oppression" against disfavored persons and places. The Federalist No. 36 (Hamilton). Their solution was to align this dangerous mode of taxation with representation, ensuring that its burdens would be shared broadly, not imposed according to political power or caprice. The Sixteenth Amendment's framers retained that vital protection, being no less wary than their predecessors of federal taxation of property.

The Ninth Circuit's decision upends the careful balance of power and accountability that the Framers struck and the Sixteenth Amendment preserved, solely to uphold a novelty of a tax enacted without any consideration of its constitutional validity. That decision should be reversed.

OPINIONS BELOW

The Ninth Circuit's opinion is reported at 36 F.4th 930 and reproduced at Pet.App.1. The opinion of the District Court for the Western District of Washington is unpublished and reproduced at Pet.App.21.

JURISDICTION

The judgment of the court of appeals was entered on June 7, 2022. Pet.App.1. A timely petition for rehearing was denied on November 22, 2022. Pet.App.35. The petition for certiorari was timely filed on February 21, 2023. This Court has jurisdiction under 28 U.S.C. § 1254(1).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The Sixteenth Amendment to the U.S. Constitution provides:

> Congress shall have the power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several States, and without regard to any census or enumeration.

The Constitution's Apportionment Clause and Direct Tax Clause, U.S. Const., art. I, § 2, cl. 3; *id.* § 9, cl. 4, and relevant portions of the Tax Code are reproduced at Pet.App.57 *et seq*.

STATEMENT OF THE CASE

A. Legal and Historical Background

1. "There is no such thing in the theory of our national government as unlimited power of taxation." *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429, 599 (1895) (Field, J., concurring) (quotation marks omitted). It is true that "[t]he experience with the breakdown of taxation" under the Articles of Confederation "drove the Constitutional Revolution of 1787." Roger H. Brown, Redeeming the Republic: Federalists, Taxation, and the Origins of the Constitution 3 (1993). The Articles had deprived the national government of taxing power, leaving it to rely on requisitions to the states, which were often ignored, to disastrous effect. Erik M. Jensen, The Apportionment of "Direct Taxes": Are Consumption Taxes Constitutional?, 97 Colum. L. Rev. 2334, 2380–81 (1997). The Framers of the Constitution therefore resolved to make the new federal government financially self-sufficient. *Id.* At the same time, "those patriotic men well knew that the unrestrained and unregulated power of taxation had been, in all the experience of the world, the chief instrument of oppression and tyranny." Arthur Graves, Inherent Improprieties in the Income Tax Amendment, 19 Yale L.J. 505, 513 (1910) (quotation marks omitted).

The Framers' generation understood that danger to inhere especially in direct taxation. Indirect taxes like excises and duties can be avoided by refraining from the activity being taxed and thereby "contain in their own nature a security against excess." The Federalist

No. 21 (Hamilton). By contrast, the power to levy direct taxes on things like property and income by its nature places "no limits to the discretion of the government," *id.*, particularly at the national level. Some among the Framers thought Congress "could not be trusted with such a power. It might ruin the Country. It might be exercised partially, raising one and depressing another part of it." 2 Records of the Federal Convention of 1787, p. 307 (M. Farrand ed. 1911) (E. Gerry) (hereinafter Farrand). Indeed, the Constitution's opponents decried direct taxation as a "*dangerous* and *oppressive* power." Jensen (1997), *supra*, at 2399 (quoting Luther Martin, Information to the General Assembly of the State of Maryland (1788)); *see also* 9 Documentary History of the Ratification of the Constitution 962 (Merrill Jensen ed. 1976) (P. Henry) (warning of "oppression" and "ruin" and that Virginians will be "most shamefully robbed").

Even those advocating for a strong national government understood that an unbridled power of direct taxation threatened their goal. As Gouverneur Morris explained at the Philadelphia Convention: "For a long time the people of America will not have money to pay direct taxes. Seize and sell their effects and you push them into revolts." 2 Farrand 307. In the political climate of the era, featuring widespread tax resistance and even revolts, all appreciated the "political sensitivity over direct taxes," Brown, *supra*, at 36–37, and the threat that it posed to acceptance of the new Constitution, *e.g.*, 2 Farrand 359 (L. Martin) ("The power of direct taxation is most likely to be criticized by the public.").

The needed check on the power of direct taxation came in the rule of apportionment set forth in Article I's Apportionment and Direct Tax Clauses—"one of the few matters deemed by the framers of the constitution so important as to be twice mentioned." David J. Brewer, The Income Tax Cases and Some Comments Thereon 5 (1898). As Alexander Hamilton explained, apportionment according to "an actual census or enumeration of the people…shuts the door to partiality or oppression." Federalist No. 36 (Hamilton). By mandating apportionment in that fashion, and thereby tying direct taxation to representation in the House of Representatives, "[t]he abuse of this power of taxation seems to have been provided against with guarded circumspection." *Id.*; *see also* 3 Farrand 365 (explaining that apportionment's purpose was to deny Congress "power to gratify one part of the Union by oppressing another").

As a matter of both principle and politics, apportionment was a masterstroke, overcoming the Antifederalists' central argument that the new national government would oppress the states and their people through direct taxation. Jensen (1997), *supra*, at 2396; James W. Ely, Jr., 'One of the Safeguards of the Constitution:' The Direct Tax Clauses Revisited, 12 Brigham-Kanner Prop. Rts. J. 6 (Vanderbilt L. Rsch. Working Paper, No. 23-02, Feb. 2, 2023). Without apportionment's safeguard against that abuse, "the

Constitution never would have been ratified." Graves, *supra*, at 516.

2. The Sixteenth Amendment was adopted to overrule this Court's decision in *Pollock*, which held the Constitution to require apportionment of taxes on income derived from real and personal property. *See Brushaber v. Union Pac. R.R. Co.*, 240 U.S. 1, 18 (1916). Political and popular support for a federal income tax grew during the decade following *Pollock*. Erik M. Jensen, The Taxing Power, the Sixteenth Amendment, and the Meaning of "Incomes," 33 Ariz. St. L.J. 1057, 1107–08 (2001). The policy was endorsed by President Theodore Roosevelt and then, with some reluctance, by his successor William Howard Taft. *Id.* at 1008.

By the summer of 1909, Congress was sharply divided over whether to pursue an amendment or simply legislate in the face of *Pollock*. *Id.* at 1111. The day after President Taft came out in favor of the amendment route, 44 Cong. Rec. 3344–45 (June 16, 1909), Sen. Norris Brown of Nebraska proposed the following language: "The Congress shall have the power to lay and collect direct taxes on incomes without apportionment among the several States according to population." S.J. Res. 39, 61st Cong., 44 Cong. Rec. 3377 (June 17, 1909). The text was revised into its current form shortly thereafter. S.J. Res. 40, 61st Cong., 44 Cong. Rec. 3900 (June 28, 1909). After the Finance Committee discharged its resolution, the full Senate voted down an alternative, proposed by Sen.

Anselm McLaurin of Mississippi, to strike the Constitution's references to direct taxes. 44 Cong. Rec. 4120 (July 5, 1909). The Senate proceeded to pass the resolution on July 5, 44 Cong. Rec. 4121, and the House followed suit on July 12, 44 Cong. Rec. 4440.

The Amendment was adopted upon the ratification of the thirty-sixth state in February 1913. 37 Stat. 1785 (1913).

3. The Mandatory Repatriation Tax was enacted as part of the Tax Cuts and Jobs Act of 2017, 131 Stat. 2054 (2017) (TCJA). It targets U.S. shareholders who own 10 percent or more (by value or voting power) of foreign corporations that are primarily owned or controlled by U.S. persons. 26 U.S.C. § 965; *see also id.* § 957 (defining subject corporations). Prior to the MRT, these shareholders were usually taxed when the foreign corporation distributed its earnings. Pet.App.6. The MRT, however, simply deems the corporations' retained earnings going back to 1986 to be the 2017 income of their U.S. shareholders in proportion to their ownership stakes on a prescribed date in 2017.[1] 26 U.S.C. § 965(a). The shareholders are then taxed on that deemed "income"—which, by definition,

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[1] Treasury regulations provide that the relevant date of ownership is "the last day" of the corporation's applicable tax year. 26 C.F.R. § 1.965-1(f)(30)(i). Because the tax applies in "the last taxable year of [the] corporation which begins before January 1, 2018," 26 U.S.C. § 965(a), some shareholders were subject to MRT liability in 2018 instead of 2017. For ease of discussion, and because most corporations use the calendar year as their tax year, this brief refers to 2017.

has not been distributed to them—at a rate based on how the corporation held the retained earnings in 2017: 15.5 percent for earnings held in cash or cash equivalents and 8 percent otherwise. *Id.* § 965(a), (c); *see also id.* § 951(a).[2]

The MRT taxes shareholders irrespective of whether they owned shares at the time the corporation made the earnings on which they're being taxed and irrespective of whether they have the power to force the corporation to make a distribution. All that matters is that a given shareholder owned the requisite number of shares on the prescribed date in 2017. *Id.* §§ 965(a), 951(a).

The principal legislative purpose of this one-time tax was to partially fund the TCJA's shifting of U.S. corporate taxation from a worldwide system toward a territorial one—that is, one where U.S. corporations are taxed only on their domestic-source income.[3] To accomplish this shift, the statute prospectively relieved U.S. corporations from paying taxes on most distributions received from foreign corporations, including subsidiaries. 26 U.S.C. § 245A. That change was limited to corporate taxpayers, *id.*; individual

[2] The effective tax rates for individuals are (at a minimum) 17.54 percent and 9.05 percent, respectively. Mark Berg & Fred Feingold, The Deemed Repatriation Tax—A Bridge Too Far?, 158 Tax Notes 1345, 1349 (2018).

[3] *See generally* Jim Tankersley et al., Republican Plan Delivers Permanent Corporate Tax Cut, N.Y. Times (Nov. 2, 2017), *available at* https://nyti.ms/2iV3TJI.

taxpayers remain liable for income tax on distributions they receive, *id.* § 61(a)(7).

B. Factual and Procedural Background

1. Charles and Kathleen Moore are a retired couple residing in Washington State, where Charles worked in software development. Pet.App.70. In the early 2000s, Charles's friend and former coworker, Ravindra "Ravi" Kumar Agrawal, had the idea of starting a business to supply farmers in India's most impoverished regions with basic tools and equipment that were readily available in the United States, but not in India. Pet.App.70. The Moores were moved by Ravi's vision of empowering India's rural farmers to improve their livelihoods. Pet.App.71. They contributed $40,000 to help Ravi found KisanKraft Machine Tools Private Limited, an Indian corporation. Pet.App.71. In exchange, they received about 13 percent of KisanKraft's common shares. Pet.App.74

KisanKraft's rapid growth confirmed that Ravi had identified a genuine need. It was profitable almost from the start, and its revenues increased every year since its founding. CA9.ER.38. True to Ravi's original business plan, KisanKraft reinvested all its earnings to grow the business, which has expanded to serve farmers across India. Pet.App.71, 73; CA9.ER.37–38. By 2017, it employed over 350 representatives in 14 regional offices serving 2,500 local dealers. CA9.ER.38.

The Moores received regular updates from Ravi on KisanKraft's activities, as well as annual financial statements. Pet.App.72. Charles visited India several times and was impressed with the difference that KisanKraft was making in the lives of India's rural poor. Pet.App.72. The Moores never received any distributions, dividends, or other payments from KisanKraft. Pet.App.73. And as minority shareholders without any role in KisanKraft's management, they had no ability to force the company to issue a dividend. Pet.App.73. For the Moores, it was payment enough that they were able to support KisanKraft's "noble purpose…to improve the lives of small and marginal farmers in India" and see the good that it was doing. Pet.App.71.

In 2018, the Moores discovered that they were liable for taxes on KisanKraft's reinvested earnings going back to 2006 under the MRT. Pet.App.74. Ultimately, the Moores had to declare an additional $132,512 as taxable 2017 income and pay an additional $14,729 in tax. Pet.App.74–75.

2. The Moores filed this action to obtain a refund of the additional tax they paid to satisfy the MRT. Pet.App.78. They alleged that the MRT is an unapportioned direct tax in violation of the Constitution's apportionment requirements, U.S. Const., art. I, § 2, cl. 3; *id.* § 9, cl. 4, because it taxes them on ownership of personal property (their KisanKraft shares), not on income they had realized. Pet.App.83–84. Before the district court and the court of appeals, the Government did not dispute that the Moores realized nothing from their investment in KisanKraft; instead, it argued that realization of income by the taxpayer is unnecessary for a tax to be exempt from apportionment under the Sixteenth Amendment. It was also undisputed that the MRT is not apportioned among the states according to population.

The district court granted the Government's motion to dismiss and denied the Moores' cross-motion for summary judgment. Pet.App.21–22. It acknowledged that this Court's cases like *Macomber* adopted a "realization framework" for Sixteenth Amendment "income," Pet.App.26, but concluded that "*Macomber*'s realization standard" had been undercut by lower-court decisions addressing constructive realization of income and was therefore not controlling, Pet.App.26–28. Without further analysis, it declared the MRT "a tax on income." Pet.App.28.

The Ninth Circuit affirmed, holding the MRT to be a tax on income authorized by the Sixteenth Amendment. Pet.App.13. Like the district court, the panel did not explain how KisanKraft's reinvested earnings became the Moores' income. Instead, it declared that "realization of income is not a constitutional requirement" for Congress to avail itself of the Sixteenth Amendment's exemption from apportionment for "taxes on incomes." Pet.App.12. It therefore followed that "there is no constitutional prohibition against Congress attributing a corporation's income pro-rata to its shareholders." Pet.App.13.

SUMMARY OF ARGUMENT

The Sixteenth Amendment carves out a narrow exception to Article I's apportionment clauses for "taxes on incomes." This Court's precedents correctly understand that exception to be limited to taxes on gains *realized* by the taxpayer. The Ninth Circuit's contrary holding not only defies those precedents, it sweeps away *the* essential restraint on Congress's taxing power, opening the door to unapportioned taxes on property (as in this case) and anything else Congress might deem to be a given taxpayer's "income."

I. This Court has consistently held that "income" within the meaning of the Sixteenth Amendment turns on realization. Just a few years after the Amendment's adoption, the Court held in *Macomber* that the "characteristic and distinguishing attribute of income" is that "a gain, a profit, something of exchangeable value" is "*received* or *drawn* by the recipient (the taxpayer) for his *separate* use, benefit and disposal." *Macomber*, 252 U.S. at 207 (emphases in original). Mere "enrichment through increase in value of capital investment is not income in any proper meaning of the term." *Id.* at 214–15. Since that time and through to the modern era, the Court has reiterated and applied that principle in numerous cases.

Macomber's holding on realization was correct, and there is no conceivable justification to depart from *stare decisis* at this late date. The principle that income requires realization is compelled by the original meaning of the Sixteenth Amendment, as evidenced by an enormous body of ratification-era sources addressing the nature of income. That understanding is also the only one to comport with constitutional structure: without a realization requirement, Article I's apportionment requirement, which the Amendment's framers generally preserved, would be a dead letter. It is also supported by consistent congressional practice since the Amendment's ratification—at least prior to the tax at issue here.

II. The Ninth Circuit's reasoning does not withstand scrutiny. This Court has never overruled *Macomber*'s holding that income requires realization. And the MRT plainly is not a tax on income under *Macomber*: it taxes ownership of specified property on a specific date in 2017, not realized gains. The Ninth Circuit's failure to follow directly applicable controlling precedent is inexcusable.

The Ninth Circuit's fear that following *Macomber* would "call into question the constitutionality of many other tax provisions" is unfounded. Pet.App.16. The income tax provisions cited by the Ninth Circuit all involve actual or constructive realization of income. Unlike those provisions, the MRT is an outright tax on property because of ownership. And unlike with taxpayers subject to those provisions, it is undisputed that petitioners realized *nothing* from their ownership of shares in KisanKraft.

ARGUMENT

I. Sixteenth Amendment "Incomes" Require Realization by the Taxpayer

The Sixteenth Amendment created a limited exception for "taxes on incomes" from the requirement that direct taxes be apportioned among the states according to population. The Court's precedents from the decades prior to the Amendment's adoption through to the current era consistently hold that income turns on realization by the taxpayer. That was the common understanding of the word "income" at the time of the Amendment's conception, drafting, and ratification, as evidenced by court decisions, dictionaries, legal authorities, and more. Then, as now, the people understood income to be that which comes in, or is realized, not mere appreciation in value in the absence of realization. To redefine the term by divorcing income from realization would fundamentally transform Congress's taxing power, authorizing it to levy all manner of unapportioned taxes—on property, on paper or imaginary gains, even effectively on heads—that have always been understood to be direct taxes requiring apportionment. "Unrealized income" is an oxymoron, not a legitimate object of Congress's Sixteenth Amendment power.

A. The Court's Sixteenth Amendment Precedents Uniformly Require Taxpayer Realization

From the very beginning, this Court's precedents have understood that the Sixteenth Amendment's exemption from Article I's apportionment requirement is limited to taxes on a taxpayer's *realized* gains. That principle, first established by the Court's 1920 landmark decision in *Eisner v. Macomber*, has been consistently applied through the decades and to the modern era. "Notwithstanding the consistent evolution in the personnel and ideology of the Supreme Court, the basic realization concept has remained remarkably stable since the *Macomber* decision." Henry Ordower, Revisiting Realization: Accretion Taxation, the Constitution, *Macomber*, and Mark to Market, 13 Va. Tax Rev. 1, 29 (1993). The Ninth Circuit's position that *Macomber* and its progeny stated no "universal" rule requiring realization for gains to be taxable as income, Pet.App.15, is flat-out wrong.

1. *Macomber* itself contradicts that position. It holds that the "characteristic and distinguishing attribute of income" is that "a gain, a profit, something of exchangeable value" is "*received* or *drawn* by the recipient (the taxpayer) for his *separate* use, benefit and disposal." 252 U.S. at 207 (emphases in original). That "fundamental conception is clearly set forth in the Sixteenth Amendment—'incomes, *from* whatever *source derived*'"—with the "conciseness and lucidity" typical of constitutional text. *Id.* at 207–08. Accordingly, mere "enrichment through increase in value of capital investment is not income in any proper meaning of the term." *Id.* at 214–15.

On that basis, the Court ruled that a stock dividend, issued to shareholders to account for the corporation's accumulated earnings but without altering their respective ownership stakes, was not subject to taxation under the Sixteenth Amendment. The "essential and controlling fact is that the stockholder has received nothing out of the company's assets for his separate use and benefit." *Id.* at 211. It was not enough that, as the Government argued, the dividend "measure[s] the extent to which the gains accumulated by the corporation have made [shareholders] the richer." *Id.* at 214. That is because a shareholder "has no individual share in accumulated profits, nor in any particular part of the assets of the corporation." *Id.* at 219. Accordingly, taxing a shareholder on the corporation's profits would be "taxation of property because of ownership, and hence would require apportionment." *Id.* at 217. Only upon distribution "does the stockholder realize a profit or gain which becomes his separate property, and thus derive income from the capital that he or his predecessor has invested." *Id.* at 209.

2. While *Macomber* was the first decision to specifically confront the question of realization, its seeds were sown in two of the Court's earliest Sixteenth Amendment cases. The first, *Brushaber*, analyzed the Amendment's purpose and scope to reject the idiosyncratic argument that its exception from the apportionment requirement reached only a tax on all income from all sources. 240 U.S. at 11. The Amendment's "whole purpose," the Court concluded, "was to relieve all income taxes…from a consideration of the source whence the income was derived," as confirmed by the fact that it "contains nothing repudiat[ing] or challenging" *Pollock*'s holding that "taxes levied directly on personal property because of its ownership" must be apportioned. *Id.* at 18–19. What *Brushaber* understood to distinguish those two categories—taxes on income versus taxes on property—is that income is "derived" from a "source" like property. *Id.* at 19; *compare Macomber*, 252 U.S. at 207 (glossing "income" as "'the *gain-derived-from-capital*'").

The second, *Lynch v. Hornby*, 247 U.S. 339 (1918), directly presages *Macomber*'s realization holding by recognizing that corporate earnings become shareholder income only upon realization by the shareholder through a distribution. Having paid income tax on a distribution of earnings accrued prior to the Sixteenth Amendment's ratification, a shareholder sought a refund, arguing the unapportioned tax was unconstitutional. *Id.* at 340–41. The Court disagreed, reasoning that Congress "was at liberty…to tax as income, without apportionment, everything that became income…after the adoption of the amendment." *Id.* at 344. That included dividends paid to a shareholder after adoption, because they became "a part of his income when they came to hand," not when the corporation made the earnings it distributed. *Id.*

Macomber's realization holding was the logical consequence of *Brushaber* and *Lynch* and is inseparable from the Court's basic understanding of the Sixteenth Amendment's scope and purpose.

3. *Macomber* does not stand alone in recognizing realization as the *sine qua non* of Sixteenth Amendment "incomes." While the Court has applied that principle in many contexts, it has come up most often in cases involving, as in *Macomber* and this case, shareholders in corporations carrying retained earnings. The constitutional question in each of those cases was whether a share dividend or other distribution caused the shareholder to realize some portion of the retained earnings as income taxable without apportionment.

For example, *United States v. Phellis* recited *Macomber*'s realization test and found it satisfied when a corporate reorganization—essentially, a spin-off—resulted in a distribution of shares in a new corporation, incorporated in a different state, to shareholders in the old one. 257 U.S. 156, 168–70 (1921). Because the shareholders "received assets of exchangeable and actual value…and drawn by them severally for their individual and separate use and benefit," they had realized "individual income in the proper sense," taxable without apportionment. *Id.* at 170; *see also Rockefeller v. United States*, 257 U.S. 176, 183–84 (1921) (same reasoning, where shareholder received "actual exchangeable assets…for his separate use in partial realization of his former indivisible and contingent interest in the corporate surplus"); *Cullinan v. Walker*, 262 U.S. 134, 138 (1923) (same reasoning, where shareholder "realized his gain" upon distribution of "securities in [] three new corporations"); *Marr v. United States*, 268 U.S. 536, 540 (1925) (same reasoning, where shareholder received "securities with essentially different characteristics in an essentially different corporation"); *cf. Koshland v. Helvering*, 298 U.S. 441 (1936) (holding that untaxed stock dividend was income under *Macomber* and therefore not capital, such that cost basis of original shares was not apportioned to new shares); *Helvering v. Gowran*, 302 U.S. 238 (1937) (same).

By contrast, *Weiss v. Stearn* applied the "principles of *Eisner v. Macomber*" to hold that shareholders had not realized any gain through distribution of shares in a materially identical successor corporation. 265 U.S. 242, 253 (1924). The fact that a shareholder "retained the same essential rights in respect of the assets" meant that "nothing would have gone therefrom to [him] for his separate benefit." *Id.* Accordingly, the share distribution resulted in no gain taxable as Sixteenth Amendment income. *Id.* at 254; *see also Miles v. Safe Deposit & Trust Co. of Baltimore*, 259 U.S. 247, 253–54 (1922) (holding that distributions to existing shareholders of subscription rights in new stock offering were not income under *Macomber*, but that their sale resulted in realization of income); *cf. McDonald v. Maxwell*, 274 U.S. 91, 98 (1927) (applying *Macomber* to hold that stock dividends were not income that increased the value of an estate).

The line of Sixteenth Amendment corporate-distribution cases came to an end when Congress clarified the tax treatment of stock dividends. *See* § I.C, *infra*.

Initially it excluded all stock dividends from taxation. *See Koshland*, 298 U.S. at 444 & n.6. Later it narrowed the exclusion to encompass only distributions that do "not constitute income to the shareholder within the meaning of the sixteenth amendment to the Constitution." *Helvering v. Griffiths*, 318 U.S. 371, 383 (1943). While the Court's subsequent decisions were decided on statutory grounds, they continued to apply *Macomber*'s constitutional line of realization. *See id.* at 394–95, 402 ("*Eisner v. Macomber* fixed the meaning" of "the Constitution" as embraced by dividend-tax provision, which thereby "defer[s] taxation…until realization."); *Helvering v. Sprouse*, 318 U.S. 604, 607 (1943) (applying realization test to two stock dividends and holding one untaxable because "the distribution brought about no change whatever in [the shareholder's] interest").

In sum, the Court's "corporate distribution cases subsequent to *Macomber* adhere firmly to that decision," all "work[ing] from the constitutional limitation on taxability—the constitutional realization requirement." Ordower (1993), *supra*, at 35.

4. The Court's early Sixteenth Amendment cases applied *Macomber*'s realization holding in a variety of other circumstances. *Taft v. Bowers*, 278 U.S. 470, 481–82 (1929), relied on it in holding that the recipient of a gift of stock could, upon sale, be taxed on its appreciation prior to the donation because, "when through sale or conversion the increase was separated therefrom, it became income." Citing *Macomber*, *United States v. Safety Car Heating & Lighting Co.*, 297 U.S. 88, 99 (1936), held essentially the same as to an award of profits that had been earned by a patent infringer prior to the Sixteenth Amendment's ratification, reasoning that realization is when a gain "may be taxed, though it was in the making long before." Similarly, *MacLaughlin v. Alliance Ins. Co. of Philadelphia*, 286 U.S. 244, 249 (1932), held that the Revenue Act of 1928 lawfully taxed appreciation prior to its enactment that was realized thereafter because it was "a gain from capital investment which, when realized, by conversion into money or other property…has consistently been regarded as income within the meaning of the Sixteenth Amendment and taxable as such in the period when realized." *Helvering v. Bruun*, 309 U.S. 461, 469 (1940), likewise restated and applied *Macomber*'s central holding that Sixteenth Amendment "income" requires "realization of gain" through the "exchange of property, payment of the taxpayer's indebtedness, relief from a liability, or other profit realized from the completion of a transaction"—in that instance, receipt of a tenant-erected building upon forfeiture of a lease.

Finally, three cases extended the logic of *Macomber*'s realization holding to assignments of income. *Helvering v. Horst* involved a taxpayer who had directed that interest on bonds he owned be paid to a family member. 311 U.S. 112, 114 (1940). Applying "the rule that income is not taxable until realized," the Court reasoned that the "power to procure the payment of income to another is the enjoyment and hence the realization of the income by him who exercises it." *Id.* at 116, 118; *accord Helvering v. Eubank*, 311 U.S. 122 (1940); *see also Corliss v. Bowers*, 281 U.S. 376, 378 (1930) ("The income that is subject to a man's unfettered command and that he is free to enjoy at his own opinion may be taxed to him as his income, whether he sees fit to enjoy it or not."). Significantly, these cases identified realization to have occurred not when the right to payment accrued or upon assignment of that right, but only when payment was made to the assignee. *See Horst*, 311 U.S. at 118; *Eubank*, 311 U.S. at 127; *Corliss*, 281 U.S. at 378.

5. *Macomber*'s insistence on realization has carried through to the modern era, beginning with *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426 (1955), which held punitive damages awards to be taxable income. The decision observes that *Macomber*'s language defining income as "'the gain derived *from capital, from labor, or from both combined*'" was "not meant to provide a touchstone to all future gross income questions" where income might arise from other kinds of sources. *Id.* at 430–31 (emphasis added). But it did not question *Macomber*'s core holding on realization; to the contrary, it reasons that punitive damages are taxable as income because they are "undeniable accessions to wealth, *clearly realized*, and over which the taxpayers have *complete dominion*." *Id.* at 431 (emphases added).[4]

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[4] Although *Glenshaw Glass* and the decisions following it are statutory cases, the Court understood itself to be interpreting

The Court subsequently recited and applied *Glenshaw Glass*'s formulation of the realization rule in a series of decisions. The first were *James v. United States*, 366 U.S. 213, 219 (1961) (holding that embezzled funds are taxable income); *see also id.* at 251–52 (Whittaker, J., concurring in part and dissenting in part) (disputing that embezzler realizes stolen funds as income), and *Commissioner v. Kowalski*, 434 U.S. 77, 83 (1977) (holding that meal-allowance payments are taxable income because they are "'accessions to wealth, clearly realized'").[5]

Those were followed by *Commissioner v. Indianapolis Power & Light Co.*, which ruled that refundable customer deposits held by a utility were not taxable income because the utility never obtained "complete dominion" over them and therefore were merely "advance payment[s]" that had not yet been "realized" by the utility. 493 U.S. 203, 208–09 (1990). The Court concluded by echoing *Macomber*'s central holding on realization from 70 years before: "[A] taxpayer does not realize taxable income from every event that improves his economic condition." *Id.* at 214; *compare*

the Sixteenth Amendment because the statutory definition of "gross income" at issue is "based upon the 16th Amendment and the word 'income' is used in its constitutional sense." 348 U.S. at 432 n.11 (quotation marks omitted); *see also* BIO.9 (acknowledging as much).

[5] Similarly, *Ivan Allen Co. v. United States*, 422 U.S. 617, 627, 634 (1975), found no violation of *Macomber*'s "'realization of income' concept" because the challenged "accumulated earnings tax" was laid only on "current taxable income" and "not on unrealized appreciation of [the taxpayer's] securities."

Macomber, 252 U.S. at 214–15 ("[E]nrichment through increase in value of capital investment is not income in any proper meaning of the term.").

* * *

The Court's Sixteenth Amendment precedents recognize, with perfect clarity and consistency, that only those gains realized by taxpayers are "incomes" taxable as such without apportionment. Even if the Amendment's text was unclear in some respect, *but see* § I.B, *infra*, the Court's "regular course of practice" across many decades long ago sufficed to "liquidate & settle the meaning" of that term and the Amendment's scope. *Chiafalo v. Washington*, 140 S. Ct. 2316, 2326 (2020) (quoting Letter from J. Madison to S. Roane (Sept. 2, 1819), in 8 Writings of James Madison 450 (G. Hunt ed. 1908)); *see also* Federalist No. 37 (Madison).

B. That Line Is Compelled by Constitutional Text and Structure

The need for "incomes" to be realized to be taxed without apportionment, as recognized by the Court's precedents, follows inexorably from the constitutional text and structure. There is no conceivable basis for the Court to abandon *stare decisis* and reverse course at this late date.

1. Begin with the text. The Sixteenth Amendment's exemption from apportionment is limited to "taxes on incomes, from whatever source derived." As *Macomber* astutely observed, that text plainly contemplates that "incomes" must be realized: a gain is not income unless and until it has been "derived" by the taxpayer from some "source." 252 U.S. at 207–08. *Pollock*, the Amendment's target, likewise distinguished between a "source" like property and "income" "derived" from that source. *E.g.*, 158 U.S. at 618, 629. The Amendment sensibly employs the same language to make the same distinction.

That "income" refers to the receipt of an economic gain was well understood at the time of the Sixteenth Amendment's drafting and ratification. "The word 'income'…has a settled legal meaning" and was "uniformly construed" by "courts…to include only the receipt of actual cash as opposed to contemplated revenue due but unpaid." *Maryland Cas. Co. v. United States*, 52 Ct. Cl. 201, 209 (Ct. Cl. 1917).

Pre-ratification precedent confirms as much. The Court's 1872 decision in *Gray v. Darlington*—frequently cited in treatises over the subsequent three decades—had no trouble recognizing that "[m]ere advance in value in no sense constitutes…income" but "constitutes and can be treated merely as increase in capital." 82 U.S. 63, 66 (1872). Income, *Gray* understood, was limited to "such gains or profits as may be realized." *Id.* at 65; *see also Mut. Ben. Life Ins. Co. v. Herold*, 198 F. 199, 214–15 (D.N.J. 1912) ("[I]ncome…means what has actually been received, and not that which, although due, has not been received, but its payment for some reason deferred or postponed."); *United States v. Schillinger*, 27 F. Cas. 973, 973 (C.C.S.D.N.Y. 1876) ("[I]ncome must be taken to mean money, and not the expectation of receiving it, or the right to receive it, at a future time."); Americans for Tax Reform Cert. Amicus Br. at 11–12 (surveying state-court decisions).

Case law of the era applied that understanding specifically to questions of shareholder income. *E.g.*, *Gibbons v. Mahon*, 136 U.S. 549, 558 (1890) (explaining that a corporation's accumulated earnings are, to shareholders, "capital, and not income"); *Minot v. Paine*, 99 Mass. 101, 111 (1868) ("The money in the hands of the directors may be income to the corporation; but it is not so to a stockholder till a dividend is made.").

Decisions immediately following ratification of the Amendment are to the same effect, defining income as "the gain *derived* from capital, from labor, or from both combined." *Stratton's Indep., Ltd. v. Howbert*, 231 U.S. 399, 415 (1913) (emphasis added); *see also Connecticut Gen. Life Ins. Co. v. Eaton*, 218 F. 188, 205 (D. Conn. 1914) (applying *Stratton's Independence*'s definition of "income" and holding that taxpayer received no income on items listed as assets "until the same were paid or realized"); *Doyle v. Mitchell Bros. Co.*, 247 U.S. 179, 185 (1918) (applying *Stratton's Independence*'s definition to hold that an investment's initial "capital value" was not taxable as income). That specific definition governed for decades. *See Comm'r v. Culbertson*, 337 U.S. 733, 740 (1949); *Glenshaw Glass*, 348 U.S. at 430.

Ratification-era dictionary definitions also recognized that realization is inherent to income. The 1913 edition of *Webster's* defined "income" as "that gain which *proceeds from* labor, business, property, or capital of any kind…revenue; receipts; salary." *Webster's Revised Unabridged Dictionary* (1913) (emphasis added); *see also Webster's American Dictionary of the English Language* (1889) ("That gain which proceeds from labor, business, or property of any kind."). Likewise, the *Century Dictionary and Cyclopedia* (1901) defined "income" as "[t]hat which *comes in to a person* as payment for labor or services rendered in some office, or as gain from lands, business, the investment of capital, etc." (emphasis added). *See also* Robert Hunter & Charles Morris, *Universal Dictionary of the English Language* (1898) ("That gain which a person derives from his labor, business, profession, or property of any kind."); Joseph Worcester, *Dictionary of the English Language* (1875) ("Gain derived from any business or property.").

Contemporaneous legal authorities identically understood income to turn on realization. The 1910 edition of *Black's Law Dictionary* defined income to include "that which *comes in* or is *received from* any business or investment of capital." *Black's Law Dictionary* 612 (2d ed. 1910) (emphases added). It further defined "income tax" as "[a] tax on the yearly profits arising from property, professions, trades, and offices." *Id. Black's* author also published a treatise on income tax shortly after the Sixteenth Amendment's ratification. Henry Campbell Black, A Treatise on the Law of Income Taxation Under Federal and State Laws (1913). The very first page begins, "An income tax is distinguished from other forms of taxation" in that it is "levied…upon the acquisitions of the taxpayer arising from" trade and business. *Id.* at 1. Black's treatise proceeds to define "income" as "that gain *which proceeds* from labor, business, or capital of any kind." *Id.* at 73 (emphasis added). Realization, it explains, is essential: when, for example, the owner of an appreciated security "sells, then the sum gained may be constitute a part of his income, but it cannot be so described while he continues to hold the security." *Id.* at 77. Indeed, it would have been "shocking to the common sense of business men to call that 'income' of the year which has not been received or 'come in.'" *Id.* at 110.

Black's understanding followed that of Thomas Cooley, among the nation's most renowned jurists and legal scholars. His influential 1876 tax-law treatise defined income as "that which comes in and is received from any business or investment of capital." Thomas Cooley, Law of Taxation 160 n.1 (1876). Cooley's treatise also aired a common objection to income taxation turning on that understanding: that it is "unequal" because those holding property "for the rise in value escape it altogether—at least until they sell, though their actual increase in wealth may be great and sure." *Id.* at 20.

And Edwin Seligman, the "dominant academic voice" in favor of the Sixteenth Amendment and federal income tax and participant in the public debate over the Amendment's ratification,[6] recognized the necessity of realization in his influential book, The Income Tax (1911). Income, he stated, "is that which *comes in* to an individual above all necessary expenses of acquisition, and which is *available for his own consumption*." *Id.* at 19 (emphases added); *see also* Edwin Seligman, Are Stock Dividends Income?, 9 Am. Econ. Rev. 517, 519 (1919) ("If it is not realized, there is no income."). Seligman's research grounds that understanding in history. It traced the emergence of state-level income taxes in the Nineteenth Century, finding that they differed from the property-focused "faculty taxes" that they replaced in looking instead to what "the person…receive[d]." Edwin Seligman, The Income Tax in the American Colonies and States, 10 Political Sci. Quarterly 221, 246 (1895).

Legal commentators understood the realization principle to apply specifically to the income of corporate shareholders. Explained one treatise of the era, corporate earnings "are not income of the stockholder until the corporation has set them apart as dividend." Edwin Howes, The American Law Relating To Income and Principal 17 (1905); *see also* The Federal Corporation Tax, 70 Cent. L.J. 91, 91 (1910) ("[I]ncome does not vest in the shareholders, until it is formally set apart by the declaration of a dividend.").

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[6] Ajay K. Mehrotra, Edwin R.A. Seligman and the Beginnings of the U.S. Income Tax, 109 Tax Notes 933, 946–48 (2005).

The same understanding of income as requiring realization prevailed upon ratification of the Amendment in 1913 and institution of the federal income tax. Notably, the first Congress to legislate under the Amendment rejected proposed statutory language that, due to poor drafting, could be read to permit taxing shareholders on corporations' "gains and profits…when they are not divided and distributed." 44 Cong. Rec. 3774 (Aug. 26, 1913). Sen. Elihu Root, who had advocated for the Amendment, objected that undistributed earnings "can not by any possibility, in accordance with our existing law, be regarded as income of the stockholder until the directors of the corporation have declared a dividend on it." *Id.* Sen. William Borah, a leading proponent of the income tax, agreed: "until the directors declare a dividend it is not the property of the stockholders, and it could not be their income." *Id.* A colleague observed that "nobody ever disputed that legal proposition." *Id.* To address the "very serious constitutional question" posed by taxing shareholders on corporate earnings they had not realized, the provision was ultimately limited to cases of "fraudulent" abuse of the corporate form to avoid taxation. 50 Cong. Rec. 4379–80 (Sept. 6, 1913).

Following enactment of the income tax, the Treasury Department likewise recognized that income was limited to sums realized by the taxpayer. It instructed tax collectors, "Returnable and taxable income is that actually realized during the year." Robert H. Montgomery, Income Tax Procedure 20 (1917) (reprinting

Letter to Collectors, Aug. 14, 1914). Mere "appreciation in the value of assets" was "held not to be income" until it "has been converted into cash or its equivalent, that is, has been realized…." *Id.* at 19–20.

By all indications, that was also the unanimous view of the tax bar. *See* Thomas Gold Frost, A Treatise on the Federal Income Tax Law 7, 15 (1913) (explaining that "the new Federal Income Tax is in no sense a tax upon property" and defining income as "that which comes in or is received"); Robert H. Montgomery, Income Tax Procedure 198 (1919) (stating that the federal government has no "right to tax any transaction unless there is an actual realization of income"); Godfrey Nelson, Income Tax Law and Accounting 19, 36 (1918) (defining taxable income as "gains, profits, salaries and wages received" and explaining that an "increase in the book value of assets" is not "taxable as income"); Charles E. Clark, *Eisner v. Macomber* and Some Income Tax Problems, 29 Yale L.J. 735, 738 (1920) ("[M]ere general appreciation in value of capital should not be deemed income so long as it is unrealized to the owner….").

In holding that Sixteenth Amendment "incomes" require realization, *Macomber* followed "the commonly understood meaning of the term which must have been in the minds of the people when they adopted the Sixteenth Amendment to the Constitution." *Merchants' Loan & Trust Co. v. Smietanka*, 255 U.S. 509, 519 (1921).

2. That understanding is the only one that comports with constitutional structure. Rather than eliminate Article I's requirement that direct taxes be apportioned, the Sixteenth Amendment carved out an exception limited to "taxes on incomes." Permitting Congress to define and tax as "income" sums that a taxpayer has not realized would effectively render Article I's apportionment requirement a dead letter.

The Sixteenth Amendment was designed to overrule *Pollock*'s holding that taxes on the income derived from property required apportionment. In proposing what became the Sixteenth Amendment, Congress considered and voted down the broader approach of striking the direct-tax clauses altogether. *See* Jensen (2001), *supra*, at 1116; Seligman, The Income Tax, at 594–95. The Amendment's principal author explained, "*my purpose is to confine it to income taxes alone*." Jensen (2001), *supra*, at 1116 (quoting 44 Cong. Rec. 3377 (June 17, 1909)). As adopted, the Amendment's text exempts only "taxes on incomes" from apportionment, without otherwise addressing the application of Article I's Apportionment and Direct Tax Clauses, U.S. Const., art. I, § 2, cl. 3; *id.* § 9, cl. 4.

The consequence of that decision was to *retain* the plenary requirement that direct taxes be apportioned among the states, subject to an exception only for "taxes on incomes." *See Brushaber*, 240 U.S. at 18–19. As the Court has understood from the beginning, the Sixteenth Amendment does not relieve Congress of its obligation to apportion other direct taxes, such as those "levied directly on personal property because of its ownership." *Id.* at 19; *see also Nat'l Fed'n of Indep. Bus. v. Sebelius*, 567 U.S. 519, 571 (2012) (explaining that the Court has "continued to consider taxes on personal property to be direct taxes" requiring apportionment). For that reason, the Court has repeatedly warned that the Amendment must "not be extended by loose construction, so as to repeal or modify…those provisions of the Constitution that require an apportionment." *Macomber*, 252 U.S. at 206; *see also Burk-Waggoner Oil Ass'n v. Hopkins,* 269 U.S. 110, 114 (1925) ("Congress cannot make a thing income which is not so in fact."); *Taft*, 278 U.S. at 481 (similar).

That is the precise consequence of dispensing with the constitutional requirement of realization by the taxpayer. Absent that requirement, nothing prevents Congress from levying an unapportioned tax on anything that it might deem to be a taxpayer's income. That includes property, whether based on value, appreciation in value, or rental value. *Contra Pollock*, 158 U.S. at 637; *Ivan Allen*, 422 U.S. at 633–34; *Helvering v. Indep. Life Ins. Co.*, 292 U.S. 371, 379 (1934). It includes, as in this case, taxing shareholders on the long-ago-retained earnings of corporations in which they've invested—no matter that the pro-rata earnings may exceed any appreciation in the value of their shares. *Contra Macomber*, 252 U.S. at 214–15; *Weiss*, 265 U.S. at 253–54. It includes, again as in this case, contingent or uncertain gains that the taxpayer may never realize. *Contra Safety Car Heating & Lighting*, 297 U.S. at 99; *Indianapolis Power &*

Light, 493 U.S. at 214. It includes gains realized not by the taxpayer but by other persons. *Contra Comm'r v. Banks*, 543 U.S. 426, 433–35 (2005). It may well include the pro-rata value of government spending that benefits all Americans. *Contra* U.S. Const., art. I, § 9, cl. 4 (requiring apportionment of any "capitation"). In short, "without a realization requirement, it is hard to see what's left of the constitutional apportionment requirement." Pet.App.39–40 (Bumatay, J., dissenting).

Ultimately, realization is what makes income income, what distinguishes income from property in general, and what connects income to particular taxpayers so that it is permissible to tax *them* on it. To divorce income from realization is to abandon any limiting principle and thereby override the mandate of Article I's Apportionment and Direct Tax Clauses.

* * *

The Court's precedents beginning with *Macomber* correctly interpret the Sixteenth Amendment according to its original meaning as exempting only those gains realized by taxpayers from Article I's apportionment requirement. Given the textual, structural, and historical evidence compelling that interpretation, there is no basis for the Court to depart from the doctrine of *stare decisis* and demolish the legal foundation of its many income tax precedents. Far from being "egregiously wrong," *Dobbs v. Jackson Women's Health Org.*, 142 S. Ct. 2228, 2265 (2022), *Macomber*'s core holding on realization was entirely right.

C. Congress Has Observed that Line in Practice

From the aftermath of *Macomber* until enactment of the MRT, Congress consistently observed the need for realization of taxable income. Congress's respect for that principle is reflected in major income-tax provisions subject to sustained discussion and debate—unlike the MRT, the constitutional status of which went unconsidered. Today, no different than in the 1920s, the object of the federal income tax is the taxpayer's realized gains. *See* 26 U.S.C. § 61(a) (defining "gross income" as "income from whatever source derived" and enumerating included categories of realized gains like "compensation for services," "rents," and "dividends"). This "[l]ong settled and established practice is a consideration of great weight" in interpreting the Sixteenth Amendment. *NLRB v. Noel Canning*, 573 U.S. 513, 524 (2014) (quoting *The Pocket Veto Case*, 279 U.S. 655, 689 (1929)).

Four years after *Macomber* held that a taxpayer derives income from property upon realization, "Congress effectively crystallized [that] requirement in the Revenue Act of 1924." Jeffrey Kwall, When Should Asset Appreciation Be Taxed?: The Case for a Disposition Standard of Realization, 86 Ind. L.J. 77, 86 (2011). It provided that a "gain" on property is taxed upon "sale or other disposition" based on the "the excess of the amount realized therefrom over the basis." Revenue Act of 1924, ch. 234, § 202(a), 43 Stat. 253, 255. It then defined the "amount realized" as "the sum of any money *received* plus the fair market value of the property…*received*." *Id.* § 202(c) (emphases added). By contrast, the initial income-tax statutes had simply referred to "gains…derived from…sales[] or dealings in property" or "growing out of the ownership or use of or interest in real or personal property," Revenue Act of 1913, ch. 16, § II(B), 38 Stat. 114, 167–68, "without any guidance as to when and how such gain was measured," Kwall, *supra*, at 86 n.48. By clarifying that gain in property becomes income only upon its sale or exchange and that the resulting income gain is measured by the amount realized, "Congress established a realization framework." *Id.* at 86. That framework remains in place to this day, generally governing taxation of gains in property. *See* 26 U.S.C. § 1001(a), (b).

That central provision is not the only major component of the income tax where Congress embraced *Macomber's* interpretation of the Sixteenth Amendment. As especially relevant here, *Macomber* led Congress to revamp its treatment of corporations' retained earnings. "[E]very Revenue Act since the adoption of the Sixteenth Amendment in 1913 has imposed a tax upon unnecessary accumulations of corporate earnings effected for the purpose of insulating shareholders" from personal income-tax liability. *Ivan Allen*, 422 U.S. at 624–25. This tax was initially imposed on shareholders, but following *Macomber* the "incidence of the tax was shifted…to the corporation itself…due to doubts as to the validity of taxing income which the [shareholders] had never received." *Id.* at 625 n.8 (quotation marks omitted). Subsequent versions of the tax were likewise "drafted to avoid the limitations set upon Congressional power by *Eisner v. Macomber*," notwithstanding the desire of some in Congress to target shareholders and recurring concerns that limiting the tax to corporations rendered it less than "fully effective." *Griffiths*, 318 U.S. at 386–87; *see also id.* at 376–77 & nn.10–12 (discussing congressional debates over the Revenue Act of 1936). To this day, the tax is levied only on corporations that unnecessarily withhold earnings from distribution, not the shareholders who may benefit without realizing anything. 26 U.S.C. § 531.

Congress's tax treatment of stock dividends followed precisely the same course. Prior to *Macomber*, the law provided that a "stock dividend shall be considered income, to the amount of its cash value." Revenue Act of 1916, ch. 463, § 10, 39 Stat. 757. As described above, the year after the decision Congress exempted all stock dividends from taxation, and ultimately limited taxation of stock dividends to that permitted under *Macomber*. *See* § I.A.3, *supra*; *Koshland*, 298 U.S. at 444 (discussing statutory and legislative history); *Griffiths*, 318 U.S. at 376–77, 380–81, 384–87, 389–93 (recounting congressional debate on the constitutional issue). That too remains the law today. 26 U.S.C. § 305.

What unites these provisions is that they all concern income taxes that Congress, appreciating the limits on its Sixteenth Amendment power, reconfigured to observe the line of taxpayer realization. Not only have those changes stuck for a century, but Congress has also refrained all that time from redefining the Tax Code's central "gain or loss" provision to include unrealized appreciation in property—despite decades of proposals and pressure to do so. *See, e.g.*, Edward Roehner & Sheila Roehner, Realization: Administrative Convenience or Constitutional Requirement, 8 Tax L. Rev. 173, 173 & n.5 (1953). While the Government has identified various tax provisions that it contends—incorrectly, *see* § II.C, *infra*—are inconsistent with a realization requirement, the core object of the federal income tax was and remains taxpayers' realized gains.

II. The Ninth Circuit's Counterarguments Fail

The Ninth Circuit's decision brushed aside the Court's precedents recognizing and applying the realization requirement and gave no consideration to constitutional text, structure, and history. Instead, it reasoned that other precedents contradicted the principle that income turns on taxpayer realization, that the tax at issue is not one on property, and that a ruling in favor of the Moores would call into question longstanding tax provisions. None of these rationalizations withstands scrutiny.

A. The Court Has Not Overruled *Macomber*'s Realization Holding

No decision of this Court has retreated from *Macomber*'s core holding that Sixteenth Amendment "incomes" must be realized to be taxed as such without apportionment. Nonetheless, the Ninth Circuit declared, in plain defiance of controlling precedent, that "realization of income is not a constitutional requirement" under the Sixteenth Amendment. Pet.App.12. The Government, in opposing certiorari, did not go quite so far, contending only that a handful of later decisions—essentially the same ones cited by the Ninth Circuit, Pet.App.12–13—"severely limited [*Macomber*'s] relevance as a constitutional precedent." BIO.13. Even that more restrained contention is unsupportable.

The Ninth Circuit centered its discussion of the issue on *Heiner v. Mellon*, 304 U.S. 271 (1938), which it took to hold that "[w]hether the taxpayer has realized income does not determine whether a tax is constitutional," Pet.App.12. But *Mellon* was a purely statutory case, deciding no constitutional issue directly or by implication—which explains why the Government did not rely on it before the Ninth Circuit or in opposing certiorari. The portion cited by the decision below holds only that, under the Revenue Act of 1918, partners may be taxed on their "proportionate share of the net income of the partnership," notwithstanding "that it may not be currently distributable…by agreement of the parties or by operation of [state] law." 304 U.S. at 281. That holding follows from the principle that, unlike shareholders in a corporation, partners *personally* "own[] the property" of the partnership, *Goesele v. Bimeler*, 55 U.S. 589, 591 (1852), such that its income is by definition their income. *See also Merchants' Nat'l Bank of Cincinnati v. Wehrmann*, 202

U.S. 295, 300 (1906) (explaining that, unlike a partnership, a "corporation is legally distinct from its members"). That state law or contractual arrangements may restrict partners' *use* of their partnership income does not alter the fact that they realized it. *Mellon* is entirely consistent with *Macomber* and casts no doubt on its realization holding.

Nor do the other cases cited by the Ninth Circuit. *Bruun* explicitly accepted that "realization of gain" is necessary for Sixteenth Amendment "income," 309 U.S. at 469, and found realized gain in a landlord's receipt of a tenant-constructed building upon forfeiture of a land lease—a straightforward application of the long-established principle that receipt of property, no less than receipt of cash, is a realized gain taxable as income, *id.* at 469 n.9.[7] Like *Bruun*, *Horst* addresses what counts as realization, holding that exercise of the "power to procure the payment of income to another is the enjoyment and hence the realization of the income by him who exercises it." 311 U.S. at 118. Far from questioning the need for realization, *Horst* recites and applies the "rule that income is not taxable until realized" and underscores the point by holding that an assignor of income is not subject to tax until the assigned income is realized by the assignee.

[7] Confirming as much, the Court reached the opposite result, on statutory grounds, where a lessee's improvements to property remained in the lessee's possession, reasoning that, although "the improvements increased the value of the building, that enhancement is not realized income of [the] lessor." *M.E. Blatt Co. v. United States*, 305 U.S. 267, 279 (1938) (citing *Macomber*, 252 U.S. at 207).

Id. at 116, 120. Finally, *Griffiths*—another stock-dividend case—was decided solely on statutory grounds (in the taxpayer's favor) and expressly refused the Government's request to overrule *Macomber*. 318 U.S. at 404.

None of these decisions purports to reconsider or even limit *Macomber*'s realization holding. Any claim that they did so implicitly would be incorrect, both on the merits and based on the Court's subsequent reassertion of the need for realization in *Glenshaw Glass* and later cases. *See* § I.A.5, *supra*; *see also* Roehner & Roehner, *supra*, at 174 ("[T]he Supreme Court has in no post-*Eisner v. Macomber* case indicated the slightest relaxation in the rule that realization is necessary before there can be taxable income."). As the leading scholar in this field put it, "Of course *Macomber* is still good law!" Erik M. Jensen, *Murphy v. Internal Revenue Service*, the Meaning of "Income," and Sky-Is-Falling Tax Commentary, 60 Case W. Res. L. Rev. 751, 850 n.222 (2010).

Even if subsequent decisions had refined *Macomber*'s rule in some fashion, that still would not justify the decision below. After all, *Macomber* specifically rejected the attribution of a corporation's retained earnings to its shareholders as their "income" where they had, in fact, realized nothing, and this case identically involves the attribution of corporate earnings to shareholders who realized nothing from their investment. In refusing to follow the precedent of this Court with "direct application" to the case before it, the Ninth Circuit "clearly erred." *Mallory v.*

Norfolk S. Ry. Co., 143 S. Ct. 2028, 2038 (2023) (quotation marks omitted).

B. The MRT Taxes Ownership of Property, Not Realization of Income

The Ninth Circuit's conclusion that the MRT is not a tax on property cannot be squared with the operation of the statute. *See* Pet.App.13. To describe the MRT is to understand that it taxes shareholders on ownership of property, not income.

The sole event that triggers MRT liability is ownership of specified property on a specific date in 2017. The statute defines something called a "deferred foreign income corporation," based on whether the corporation "has accumulated post-1986 deferred foreign income," which is in turn defined as accumulated earnings going back to 1986 that have not yet been taxed. 26 U.S.C. § 965(d)(1)–(2). The statute's operative provision then deems those earnings to be the 2017 "income" of U.S. persons who happened to own at least 10 percent of its shares in 2017. *Id.* § 965(a), (d)(1). In this way, the MRT imposes liability on shareholders based on their 2017 ownership of shares in a corporation carrying accumulated earnings.

The MRT takes no account of whether the shareholders it targets have realized anything. In that respect, it differs from other provisions of Subpart F, a statutory scheme dating to the 1960s that taxes controlling U.S. shareholders of "controlled foreign corporations" on narrow categories of corporate income. *See*

§ II.C, *infra* (discussing Subpart F). Unlike those provisions, MRT liability does not turn on any event of constructive realization of income by shareholders, such as the corporation's receipt of investment earnings while subject to the shareholders' control. Instead, all that matters is ownership, divorced from realization of income: the MRT tags a shareholder with taxable "income" even if he or she purchased the shares in 2017, long after the corporation earned the sums being taxed; conversely, a taxpayer who owned shares in the same corporation for years as it retained earnings but sold before the trigger date in 2017 has no liability under the MRT. Whether a taxpayer is subject to the MRT turns on ownership of an asset at a particular time, not the taxpayer's realization of income.

That conclusion is reinforced by two additional features of the MRT. First, the MRT by definition taxes corporate earnings that Congress never had any basis to tax through Subpart F, its comprehensive income-attribution regime for "controlled foreign corporations." Subpart F regards U.S. shareholders as constructively realizing certain narrow categories of income earned by foreign corporations that they control. That reticulated scheme singles out specific categories of "movable income" that could have been earned directly by controlling U.S. shareholders, rather than shifted to a foreign corporation they control. *See* 26 U.S.C. §§ 952–54; *see also* § II.C, *infra*. But income outside of those categories was taxed only upon an actual or *de facto* distribution to U.S. shareholders. Pet.App.6.

This was not an inadvertent omission from Subpart F. It reflects the lack of any factual basis to regard ordinary, non-movable corporate earnings as shareholder income. *See* Sean P. McElroy, The Mandatory Repatriation Tax Is Unconstitutional, 36 Yale J. Reg. Bull. 69, 80–81 (2018); Mark Berg & Fred Feingold, The Deemed Repatriation Tax—A Bridge Too Far?, 158 Tax Notes 1345, 1355–56 (2018). Subpart F carefully observed that limitation for 55 years; the MRT demolishes it, going back 30 years, without so much as a legislative finding justifying that change or even an acknowledgement of the reversal in the legislative history.[8]

Second, the MRT contains its own unique rate structure based on the status of the property being taxed, not any circumstance of the shareholders it taxes. The retained earnings that the MRT deems to be shareholders' "income" are taxed at a 15.5-percent rate for earnings held by the corporation in cash or cash equivalents and at an 8-percent rate for other assets. 26 U.S.C. § 965(c). This property-based rate

[8] Notably, Congress observed that line when it last sought to address accumulated active business income held overseas. Rather than deem those earnings shareholder "income," it encouraged repatriation by enacting a "tax holiday" during which they could be voluntarily distributed to domestic shareholders at a favorable rate. *See* 26 U.S.C. § 965(a) (2017).

structure confirms that the MRT's object is ownership of property.

The MRT is not a tax on income but "is levied solely because the U.S. shareholder is the owner of an asset that, as of an arbitrary date, has accumulated foreign earnings." McElroy, *supra*, at 82 (footnote omitted). That is "taxation of property because of ownership, and hence would require apportionment." *Macomber*, 252 U.S. at 217.

C. Other Income Taxes Rest on Theories of Taxpayer Realization

To support its constitutional holding, the Ninth Circuit reasoned that a decision in favor of the Moores "would also call into question the constitutionality of many other tax provisions that have long been on the books." Pet.App.16. Picking up on that thread, the Government has cited a handful of income taxes that it says "share common features with the MRT." BIO.11. Putting aside the mistaken assumption that Congress may gain constitutional ground through adverse possession, *see Noel Canning*, 573 U.S. at 593 (Scalia, J., concurring in the judgment), no income tax provision cited to date shares the MRT's defect of taxing property because of ownership. Instead, each rests on a theory of constructive realization of income by those being taxed.

"This Court has recognized that 'income' may be realized by a variety of indirect means." *Diedrich v. Comm'r*, 457 U.S. 191, 195 (1982). That principle includes the doctrine of constructive realization, which "treats as taxable income which is unqualifiedly subject to the demand of a taxpayer…, whether or not such income has actually been received in cash." *Ross v. Comm'r*, 169 F.2d 483, 490 (1st Cir. 1948). It "has been incorporated in the Treasury Regulations from the beginning," *id.*, and also in precedent. The Court's 1930 decision in *Corliss*, for example, explained that income "taxation is not so much concerned with the refinements of title as it is with actual command over…the actual benefit for which the tax is paid," and offered this example: "If a man directed his bank to pay over income as received to a servant or friend, until further orders, no one would doubt that he could be taxed upon the amounts so paid." 281 U.S. at 378.

Indeed, one of the Court's very first cases under the Sixteenth Amendment, *Southern Pacific Co. v. Lowe*, applied the doctrine to hold that a corporate parent had realized income earned by a subsidiary prior to the Amendment's adoption, even though it was distributed to the parent thereafter. 247 U.S. 330, 338 (1918). The parent's "complete ownership and right of control" of the subsidiary rendered the formal payment of the distribution nothing more than "a paper transaction" of no tax significance. *Id. Macomber* likewise acknowledges application of the constructive realization doctrine to corporate shareholders, recognizing that the law may "look through the form of the corporation and determine the question of the stockholder's right, in order to ascertain whether he has received income taxable by Congress without apportionment." 252 U.S. at 213.

Congress relied on the constructive realization doctrine in enacting Subpart F. Its provisions (apart from the MRT) address circumstances where Congress determined that domestic taxpayers have, while exercising ownership and control of income-producing assets, "interpose[d] [] a foreign corporate framework between themselves and [the] income." *Whitlock's Estate v. Comm'r*, 59 T.C. 490, 507 (1972), *aff'd in part, rev'd in part*, 494 F.2d 1297 (10th Cir. 1974). Accordingly, it treats certain narrow categories of income earned by these "controlled foreign corporations" as the income of their controlling U.S. shareholders. *See generally* IRS, LB&I International Practice Service Concept Unit, Subpart F Overview, at 3 (2014).[9] That includes "investment income such as dividends, interest, rents and royalties"; income from "from the purchase or sale of personal property involving a related person"; and income "from the performance of services by or on behalf of a related person." *Id.* at 4. While the precise categories of income subject to Subpart F have been refined over time, they are all things Congress regarded as "movable income" that could have been earned directly by domestic controlling shareholders, and thereby taxed as their income, if they had not shifted it to a corporation in "a low- or no-tax country." *Id.*; *see also* Henry Ordower, Abandoning Realization and the Transition Tax: Toward a Comprehensive Tax Base, 67 Buff. L. Rev. 1371, 1390 (2019).

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[9] *Available at* https://www.irs.gov/pub/int_practice_units/DPL-CUV_2_01.PDF.

Subpart F's proponents principally justified its constitutionality based on constructive realization. Congress relied on an analysis provided by the Treasury Department's general counsel, which concluded that this Court "would find that within existing precedents the taxes under the proposed bill would be imposed upon income constructively received" by shareholders. *Hearings Before House Committee on Ways and Means on the Tax Recommendations of the President Contained in His Message Transmitted to the Congress*, 87th Cong., 1st Sess., at 314 (1961). Citing decisions like *Horst*, it observed that "the courts have accepted constructive receipt…where the owner could demand the income but did not do so and, therefore, failed to receive it through his own choice." *Id.* at 315. It accordingly reasoned that "Congress has the power under the 16th amendment" to tax controlling U.S. shareholders on corporate earnings "on the ground that it may find that such income is constructively received by the U.S. shareholder" and that *Macomber*'s realization holding therefore posed no "constitutional obstacle to the proposed legislation." *Id.* at 316.

While this Court has not addressed the constitutionality of Subpart F, its provisions predating the MRT all target specific *events*—like a foreign corporation's earning of investment income while being controlled by a small number of domestic shareholders—

that Congress found resulted in constructive realization of income by controlling shareholders.[10] The Court has historically deferred to that sort of legislative determination, so long as it is rational and does not transgress constitutional limitation. *See Haynes v. United States*, 390 U.S. 85, 98 (1968); *Barclay & Co. v. Edwards*, 267 U.S. 442, 450 (1925). By contrast, the MRT simply attributes a foreign corporation's retained earnings going back thirty years to whoever owned its shares in 2017, irrespective of any event by which they might have realized anything. The MRT's invalidity as an unapportioned tax on property therefore does not cast doubt on the facial constitutionality of Subpart F's other provisions.

The same is true of the other tax provisions cited by the Government. Partners are taxed on a general partnership income, 26 U.S.C. §§ 701–02, because it is *their* income, partnerships having no existence separate from their partners, *see* § II.A, *supra* (discussing *Mellon*); Black, *Treatise*, *supra*, at 145. Similarly, the owners of an "S corporation" unanimously elect to be taxed on the business's income, 26 U.S.C. § 1362(a)(2), thereby conceding that its income is theirs, *Garlin v. Murphy*, 42 A.D.2d 30, 32 (N.Y. App.

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[10] Its application has been upheld by lower courts on that basis. *See, e.g.*, *Whitlock's Estate*, 59 T.C. at 507 (1972) (finding that corporations' "earnings and profits were as much petitioners' income as if petitioners had received such earnings and profits themselves"), *aff'd in part, rev'd in part*, 494 F.2d 1297 (10th Cir. 1974); *Garlock Inc. v. Comm'r*, 58 T.C. 423, 438 (1972) (finding "constructive receipt of income" by taxpayer), *aff'd*, 489 F.2d 197, 200 (2d Cir. 1973); *Dougherty v. Comm'r*, 60 T.C. 917, 930 (1973).

Div. 3d 1973), *aff'd*, 34 N.Y.2d 921 (1974). And the "exit tax" on persons renouncing citizenship permits liability to be deferred "until the due date of the return for the taxable year in which such property is disposed of," 26 U.S.C. § 877A(b)(1)—that is, when the taxpayer actually realizes the income being taxed.[11]

The "mark-to-market" tax on regulated futures contracts, 26 U.S.C. § 1256, was justified by Congress and upheld against challenge based on the fact that those contracts are settled daily and give the taxpayer "the right to withdraw cash from…his futures trading account on a daily basis"—amounting to constructive or even actual realization of gain, much as a bank depositor realizes interest even if it is not withdrawn. *Murphy v. United States*, 992 F.2d 929, 930–31 (9th Cir. 1993); *see also* S. Rep. No. 97-144, at 156–57 (1981), *reprinted in* 1981 U.S.C.C.A.N. 105, 255–56 (relying on "doctrine of constructive receipt" because traders "receive[] profits as a matter of right…in cash daily").

Finally, the similar mark-to-market taxes on securities held by securities dealers not for investment but as inventory, 26 U.S.C. § 475(a), and on "segregated assets" held by life insurance companies, *id.* § 817A(b), are not necessarily "taxes on incomes" at

[11] While no court has decided the question since this tax was adopted in 2008, the exit tax might be justified as an excise on the act of renouncing citizenship and removing property from U.S. taxing jurisdiction. *Cf. Bromley v. McCaughn*, 280 U.S. 124, 136–37 (1929).

all. *See Flint v. Stone Tracy Co.*, 220 U.S. 107, 150 (1911) (holding that taxes on "the actual doing of business in a certain way" are excises, even if "measured" by income).[12] That aside, Congress had at least some basis to find that securities dealers (who continually hold out inventory securities for sale at market price) and life insurers (who maintain segregated assets "valued at market for annual statement purposes" that are subject to liquidation and payment at market value at any time, *see* 26 U.S.C. § 817A(d)) continually realize gains on the assets in question through their specific business activities.

Ultimately, this case does not call on the Court to mark the constitutional limits of the constructive realization doctrine, because it is undisputed that the Moores realized nothing in any fashion. Pet.7. Even if application of one or another of the cited income taxes might overstep the constitutional line in some hypothetical case, they are facially valid because they kept that line in sight. The MRT does not.

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[12] To be clear, that rationale would not support the MRT, because it is "imposed upon property simply because of its ownership," not the "carrying on or doing of business in [any] designated capacity." *Id.* at 150.

CONCLUSION

The judgment below should be reversed.

Respectfully submitted,

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