Book Review. Selected Studies in Federal Taxation, 2nd ed. by Randolph E. Paul

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to be taken by cautious practitioners prior to judicial settlement of proce-
dural uncertainties. As evidence of the practical worth of the book there
may be cited the discussion of non-resident motorist statutes under Rule 4
on Process, of pleading jurisdiction and of the amount in controversy under
Rule 8 on Pleading, of contribution among tort-feasors under Rule 14 on
Third-Party Practice, and of the federal assignment statute under Rule 17
on Parties. For those unfamiliar with pre-trial procedure there is included
a form of a pre-trial order of court in the analysis of Rule 16. The mechan-
ical make-up of the work, and aid in expeditious use, is explained in the
preface. The thirteen page schedule of time covering all the rules should
prove of value to the practitioner and judge. And the probable effect of
the doctrine of Erie Railroad Co. v. Tompkins on some of the new federal
rules is pointed out.

The third volume contains a supplementary discussion, of one hundred
and thirty-three pages, of original and removal jurisdiction of district courts,
of venue and of appellate jurisdiction. This volume also includes fifty-six
forms, twenty-seven of which were prepared by the Advisory Committee,
with annotations and cross-references to the text.

As expected, the investigations of the authors, one as Chief of the Re-
search Staff of the Reporter to the Supreme Court Advisory Committee and
the other as a member of that staff, have aided in the production of more
than a mere practice manual. For those not engaged in the federal practice
a study of the work should prove profitable as it presents readable essays,
rather than disjointed annotations, on liberal and modernized procedure.
And for those who have studied with care the eighty-six brief and simple
rules and the Advisory Committee's Notes, the three volumes may be used
as a reference work. It cannot therefore be said of this work what Thomas
Jefferson said of Blackstone's Commentaries that "it is nothing more than
an elegant digest of what they will then have acquired from the real foun-
tains of the law."

Julian S. Waterman,†

SELECTED STUDIES IN FEDERAL TAXATION (SECOND SERIES). By Ran-
$5.00.

This book, like its predecessor of the same name, consists of a number
of articles on entirely separate questions, though all relate to federal income,
gift, or estate tax problems. In this book, there are seven such articles,
having no particular connection with each other except as already stated;
but each discusses a problem where, in the opinion of the author, the present
situation is uncertain or unsatisfactory. It should be noted that the author
had the assistance of Mr. Philip Zimet in two of these articles, and that the
last one is stated as having been written solely by Mrs. Paul.

The preface to the book appears to accept the "realist" legal philoso-
phy, almost to the extent advocated by Jerome Frank; but the articles them-
selves show little influence of such ideas. The preface is also rather remark-
able in the author's confessing astonishment that there is so little uniformity
in the various state tax systems; an astonishment which it would seem that

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the slightest research would have removed long ago. But perhaps this is meant as an argument that federal tax matters should be less complex.

The first article relates to the effect on federal taxation of local rules of property. It is obvious that such effect as local rules have is to discourage equality, uniformity, and simplicity; though it is freely conceded that any considerable simplicity in federal tax matters can not be attained. Many reasons for this are given, though the author perhaps neglects the importance of the many remedial provisions intended to remove some of the major hardships of a less complicated law.

A number of statutory provisions in the federal laws are noted where there is an explicit refusal to follow the state property rules. One of the worst examples of this was in the apparently moribund Undistributed Profits Tax, where corporations were penalized for failure to make dividends which were illegal or even criminal under the law of the state. On the other hand, there are a number of express provisions subjecting particular features of the problem to the rules of the state laws.

The worst problem, at least from the standpoint of statutory interpretation and administration, is whether subjection to state rules should be implied, or the contrary. The author objects to a construction in favor of implied subjection to state rules if it is possible to avoid it. As horrible examples of the lack of uniformity which such unnecessary subjection to state laws gives, he cites the situation as to trusts for alimony, depletion, community property, and state rules as to the vesting or contingency of interest. Some of these difficulties cannot perhaps be avoided. It is certain that the precise state terminology is unimportant; but, on the other hand, it seems impossible for the Federal Government to tax one on income from property which, according to the law of the state which governs, he does not own. As might be expected, there is more uniformity in collecting than in imposing taxes, as here the state rules have little or no effect. The author feels that the recent decision of *Erie Railroad Co. v. Tompkins* does not evidence any intention by the Supreme Court to magnify the importance of state laws; but it is difficult to see how it can have any other effect.

The next article relates to federal tax compromises. The author criticizes, with much justice, the rulings prohibiting the Treasury Department from compromising taxes where liability or collectibility is not in question. This is done informally anyway. The problem is linked up with that as to the validity of non-retroactive regulations which interpret the statute; such regulations when merely procedural are unquestionably valid. It is demonstrated that Congress intended to give the Treasury this broader power, but it is admitted that its validity can be attacked under the doctrine that legislative power cannot be delegated. While the author seems disposed to think that this rule has been entirely done away with—a contention which is distinctly questionable—yet his argument that this is not an undue delegation and will be sustained, seems probably correct. He seems to show some tendency to confuse retroactive and double taxation, which are not the same thing; but it must be conceded that retroactive taxation frequently leads to double taxation. He believes that Congress should delegate to the Treasury full power to compromise tax cases, even where the legality and collectibility of the tax is in question, if it is considered that this will avoid undue hardship to the taxpayer; and the reviewer is inclined to agree. There seems to be little danger that the Treasury would treat this power as an invitation to throw away government revenue.

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1. 304 U. S. 64 (1938).
Next comes a discussion of *res judicata* in federal taxation. Much of this article does not deal with tax law at all, but with the principles of *res judicata* in general. The tax problem is posited by *Tait v. Western Maryland Ry. Company,*\(^2\) which held that a court decision as to income tax in one year was binding upon the taxpayer and the government as to the same questions and the same tax in subsequent years. The decision has been severely criticised, but the author seems inclined to admit that it may be correct. His contention that *res judicata* is necessary in tax matters in order to enforce the Statute of Limitations seems questionable; but here, as elsewhere, the doctrine is necessary to protect the courts and perhaps, to some extent, other taxpayers. The author does criticise vigorously and justly the distinction which the Supreme Court has made as to *res judicata* in suits against a collector, as distinguished from suits against the Commissioner of the United States. This is a purely procedural distinction, and a judgment in one sort of action should be as binding as in the other. It would seem that it is time to abolish suits against collectors, anyway.

The author says that *res judicata* “should be employed to save unnecessary litigation, but not to perpetuate error.” Quite so; but how is this to be done? Here he is fairly specific, but certainly radical. He suggests following the *Tait* case generally, but with a statutory provision that a judgment should not be binding in subsequent years if it is seriously detrimental to uniformity between taxpayers. This is certainly handing the Treasury Department a good deal of discretion, which many judges would undoubtedly regard as quite inadmissible; but there is something to be said for it.

The fourth article relates to the definition of “earnings and profits” for the purpose of corporate distributions. The problem arises, because it is only a distribution by a corporation from earnings and profits that constitutes a taxable dividend.

In its solution, state corporation laws as to dividends are not necessarily conclusive. It is clear that earnings and profits may include non-taxable earnings—even earnings that could not be constitutionally taxed by the United States—and may be diminished by undeductible expenses. In addition there is, or may be, a difference as to the base for determining taxable profit, and the base for earnings and profits; but as to this, the authorities are not clear. Whether a distribution in kind by a corporation constitutes earnings and profits depends on the unsettled question whether the corporation realizes gain thereby. But the most serious problems are dividends paid out of unrealized appreciation, and corporate gain or loss on reorganizations or similar transactions, which are not closed because of special statutory provisions. As to the first, the author expresses the opinion that they should not be taxed; if they are, it would seem logical that unrealized losses should be deducted from earnings and profits. It seems to be not only logical but sound policy to correlate taxable dividends and the effect on earnings and profits. As to gain or loss on reorganizations or similar transactions, the same argument applies; and it is the opinion of the author that the statute also prescribes this result. The Treasury itself seems to be in accordance with the view of the author, but at least some of the decisions of the Board of Tax Appeals take the view that such a gain or loss does affect earnings and profits even though the Statute prescribes that it does not give rise to taxable profit or deductible loss. The desirability of a final court decision on this point is both indicated and stated.

Next comes the question of “step transactions”. The problem is stated as one of “separating or segregating transactions”; that is, whether two or

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2. 289 U. S. 620 (1933).
more transactions which have some connection in fact should be treated separately for tax purposes, or as a unit. The problem is a difficult one, and many of the suggested solutions do not help. For instance, the author demonstrates that the familiar segregation of “form” and “substance”, however realistic it sounds, is actually a purely metaphysical test. He also shows that resort to the so-called “intention of the parties” is also non-productive, but this can be better discussed in connection with the next article.

The parol evidence rule—if there is any such thing—is obviously not applicable, since the government is a party to all tax controversies. However, various writings made as part of the same transaction are generally construed together. But this is not always so; for instance, a single instrument may create more than one trust. The author demonstrates that the courts—whatever they say—are in fact influenced in this problem by an apparent motive of tax avoidance, and they seek to defeat it: a tendency which he somewhat doubtfully approves. The courts also consider the ultimate result as important, but it cannot be decisive; otherwise, step transactions would always be treated together. Apparently the most important and most often used test is that of interdependency. It is said that this test should be somewhat “refined”, but the precise nature of the suggested refinement is not clear. Even this test is not always used, and perhaps should not be. The author concludes somewhat discouragingly but, certainly sensibly: “The problem is, in a sense, insoluble; but at least it should be so stated as not to intensify the difficulties or enmesh the courts in a tangle of conflicting and meaningless generalities.”

The next article deals with motive and intent in federal tax law. The author distinguishes “immediate” and “ulterior” intent, but ulterior intent seems indistinguishable from motive. Roughly, and to use the reviewer’s own expression (for which the author is not responsible), intent seems to be the mental side of what one does; motive is why he does it.

The author says that psychology has taught us much about the mind of man, but seems to admit that it has not taught us any way to find out mental processes other than through the words and deeds of the person involved. In tax matters, motive is usually more important than intent; this is unfortunate, because it is much harder to ascertain. The author casts much scorn upon the frequent judicial delvings into “legislative intent”, saying that this is pure fiction. More specifically, he criticises the tendency to lay considerable stress upon administrative rulings promulgated before the statute is re-enacted. He says that most of the members of the legislative body know nothing about these rulings. This may be granted, but those who are actually concerned in drafting the legislation usually do, as is evidenced by the frequent passage of legislation doing away with some particular administrative ruling. The author also believes that the power to tax is much broader than the power to raise revenue; that it is regulatory and may even be confiscatory. It is submitted that this is unsound. The author properly condemns the idea that the power to tax is the power to destroy; but if the power to tax includes unlimited power to regulate, it is in fact the power to destroy. In this connection, the author expresses the opinion that judges are too timid in legislating. This is, perhaps, generally true, but one can hardly blame them for being a little more timid in filling in tax legislation than would ordinarily be the case.

The chief problem, however, is the effect of the motive or intent of the taxpayers themselves. Here it is conceded that if any importance is to be given, there must be a pragmatic test. But it is demonstrated that the taxpayer’s motive is often made material by the very terms of the tax statute.
For instance, he cites the recent change of the burden of proof with respect to "incorporated pocket-books", though it may be added that he has some doubt as to the effectiveness of this change. Then we have the problem of transfers to foreign corporations for the apparent purpose of avoiding the federal tax; here the Government usually wins. Another important example is gifts in contemplation of death, for Federal Estate Tax purposes. Here it is suggested that the presumption be put in terms of the age of the donor at the time of the gift rather than, as at present, on the date of death.

Even more troublesome are situations where taxpayers' motives are important even though the statute does not say so expressly. One important example is the often-criticised case of *Gregory v. Helvering*, holding that an ostensible corporate reorganization was not free from tax where it had no business purpose. The decision seems probably sound. Though it does bring in intent and motive, these are susceptible of a reasonably objective test. It is admitted that the case has not, as was predicted, resulted in a flood of litigation. It is pointed out that the provision in the Gift Tax Law making a purported sale for inadequate consideration constitute a taxable gift, has been construed by the Bureau as applying only when a donative intent is shown. This is clearly commendable, since otherwise everyone who made a bad bargain would be additionally penalized by having to pay a gift tax. And, more generally, the motives of the taxpayer (especially to avoid taxes) have some evidentiary importance with respect to the facts themselves.

The author's conclusion that the courts are justified in giving some weight to intent and motive seems well taken. He shows that an attempt to block all methods of tax evasion by specific provisions in the statute would give rise to hopeless complexity, and is really impossible anyway, since Congress cannot permanently out-guess taxpayers' counsel. The only possible solution is a consideration of intent and motive, which seems worthwhile even though it does make the law less certain.

The last article relates to the tax status of will contestants. This is the most strictly legalistic article in the book, at least so far as tax law is concerned. The problem involves both estate and income taxes, but is more important in connection with the latter. It arises only in case of a contest, or at least a threatened contest, of a will, which dispute is settled by compromise. The basic problem is whether the contestant who is thus bought off receives taxable income. The constitutionality of imposing an income tax in this situation is unsettled, but the opinion is expressed that it will probably be upheld. Furthermore, there can be no doubt that it is included by the terms of the statute, unless explicitly exempted. The only possible statutory exemption is property acquired by "inheritance". It is clear that a person named in a prior will who is paid for not contesting a subsequent will does not receive such payment by inheritance. But in the more usual situation where only one will is involved, it is more arguable. There is considerable disagreement among the states as to whether such a payment is subject to an inheritance tax; and the author is of the opinion that such disputes should, in the interest of uniformity, be disregarded for federal tax purposes. It is argued that legalistically the situation has all the elements of a contract. The right to contest the will is acquired by inheritance; but it, of course, has no exchangeable value. From this it would follow that the payment constitutes taxable income. But the author immediately rejects his own legalistic argument by contending that the problem should be treated from the realistic business point of view. From this standpoint, it

is a non-taxable exchange. The right to contest, while not itself exchange-
able, is actually as valuable to the owner as what he can get for it—namely, the amount paid to him for withdrawing his contest. This seems abundantly sensible. He adds that if the courts decide otherwise, and subject such amounts to tax, they should be explicitly exempted in the statute, so as to encourage compromises. Possibly this suggestion might be criticised as tending to increase the number of contests of wills; but in such contests the tax problem is rarely the vital one.

The book includes a table of secondary authorities, and a table of cases. It also has an adequate index. The general make-up is excellent, the extensive footnotes being in a very readable type. One rather irritating habit is that of placing many of the footnotes where it is necessary to read further in the text in order to understand the note itself. But this, at worst, is annoying rather than really serious.

The problems are certainly well-selected; all of them are of considerable importance and great difficulty. Under each problem there is a full collection of the authorities, and an extremely valuable discussion of them. The conclusions are sometimes—though not often—open to question, but are invariably stimulating and helpful. The book cannot, therefore, fail to be interesting and valuable to anyone concerned with federal tax problems.

Robert C. Brown.†


The present volume is a revised edition of the first edition of this book which appeared in 1934. Such developments as the Securities Legislation of 1933 and 1934, the Public Utility Act of 1935 and a number of other important statutory developments, both state and federal, necessitated the new edition. There have been added four new chapters dealing with the control of security issues, the economics of the corporation, the momentous and practically important chain-store problem, and the present status of antitrust laws.

Part One deals with non-corporate forms of business organizations. Herein are discussed in a simple and lucid manner the single proprietorship, the partnership, the joint stock company, and the Massachusetts trust.

Part Two deals with the corporation and discusses, both from the business and social viewpoints, its history and nature, the corporate charter and by-laws, capital stock and shares of stock, control of corporate security issues, directors, the investment trust (including its practices), and the economics of the corporation.

Part Three deals with industrial combination. Chapter XIV in this part is particularly helpful, for it discusses the various types of modern industrial combination and the respective advantages and disadvantages of large size business.

Part Four deals with methods of combination. Herein are discussed so-called "gentlemen's agreements", price and profits pools, the "trust", and the community of interest problem. There are also chapters dealing with the consolidated company, the leased company, and the holding company. The two concluding chapters take up trade associations and the so-called cooperatives.

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