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CRIMINAL LAW CASE NOTES AND COMMENTS

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THE FEDERAL GAMBLING TAX AND THE CONSTITUTION

Professional gambling is a multi-billion dollar business in the United States.[1] This naked fact serves only as an introduction to the enormity of the social evil of commercialized gambling. The recent revelations of the Senate Crime Investigating Committee[2] forcefully dramatized the urgent need for corrective action in order to solve this socio-political problem. In the Revenue Act of 1951, Congress, recognizing the necessity of controlling organized crime, enacted two new tax laws on gambling.[3]

The first law imposes a ten per cent excise tax on all wagers on sports events or other contests placed with a person engaged in the business of accepting wagers or in a wagering pool or lottery conducted for profit.[4] The second law is a special $50.00 per year occupational stamp tax on a person liable for the tax on wagers or a person who receives wagers in behalf of any person so liable.[5] Under the law, every person liable for the special tax must register with the Collector of the district and give certain information including (1) his name and place of residence, (2) each place of business where his gambling activity is carried on, and the names and places of residence of persons engaged in receiving wagers for him or on his behalf, and (3) the name and place of residence of each person for whom he is receiving wagers.[6]

The required information is made available for public inspection in the Collector's Office.[7] Furthermore, the statute specifically provides that the payment of the tax shall not exempt any person from criminal penalties for violations of federal or state laws prohibiting such gambling activities.[8] To insure compliance, there is a fine of $1,000 to $5,000 for failure to pay either the wagering or registration tax.[9] In addition there is a fine for willful violations up to the amount of $10,000 and imprisonment up to five years.[10]

It is fairly apparent that the purpose of these taxes is to discourage gambling and to facilitate the enforcement of state criminal laws against gambling.[11] Thus, the act places professional gamblers in a dilemma. If

1. H. R. REP. No. 586, 82d Cong., 1st Sess. 55 (1951); SEN. REP. No. 781, 82d Cong., 1st Sess. 113 (1951). See Comment, *Federal Regulation of Gambling*, 60 YALE L. J., 1396, (1951).
2. *I.e.*, the Kefauver Committee. See generally *Hearings before a Special Committee to Investigate Crime in Interstate Commerce*, 81st Cong., 2d Sess. and 82d Cong., 1st Sess. (1951-52); Kefauver, CRIME IN AMERICA (1951).
3. Act of October 20, 1951, 26 U. S. C. § 3285 et seq. (Supp. 1952).
4. INT. REV. CODE § 3285.
5. *Id.* § 3290.
6. *Id.* § 3291.
7. *Id.* §§ 3292, 3275.
8. *Id.* § 3297.
9. *Id.* § 3294(a).
10. *Id.* § 3295(c).
11. The Congressional committees defended the tax as a revenue producing measure. H. R. REP. No. 586, 82d Cong., 1st Sess. 54-55 (1951); SEN. REP. No. 781, 82d Cong., 1st

they register and provide the information required by the act, they may be subject to prosecution as violators of state anti-gambling laws. On the other hand, if they refuse to register, the sanctions of the wagering statute become operative. It is not surprising to find, therefore, that the constitutionality of the occupational stamp tax has been immediately contested in the federal courts.

Although the wagering tax was challenged on several grounds,[12] the primary objection raised is that the legislation constituted an encroachment by the federal government upon the police powers reserved to the states by the Tenth Amendment to the Federal Constitution. In *United States v. Kahriger*,[13] defendant was charged with failure to pay the $50.00 occupational tax and to register with the Collector of his district. The Pennsylvania District Court, in granting defendant's motion to dismiss, held that, because the information required by the registration provisions was "peculiarly applicable to the applicant from the standpoint of law enforcement and vice control," the wagering tax invaded the "sanctuary of state control," and therefore was not a tax but a penalty.[14] The Supreme Court is entertaining an appeal in the *Kahriger* case.[15] In three subsequent federal district court cases,[16] however, the validity of the gambling tax has been sustained. Before discussing these cases, it might be instructive to examine briefly former Congressional exercises of the taxing power for regulatory purposes.

In the past the objection has been frequently urged in attacking other taxing statutes that the Congress, under the pretext of its taxing power, seeks to invade the reserved powers of the states by regulating matters which the federal government might not otherwise control.[17] This is not to say that the taxing power may not be used for regulatory purposes. There can be no doubt of the power of the national government to employ its taxing power for nonrevenue purposes when to do so will assist it in carrying out one of its delegated powers. An example of such a use of power

Sess. 112-113 (1951). Annual revenue from the tax was estimated at $400,000,000. *Ibid.* However, according to the New York Times, collections for the first four months of this fiscal year totaled less than one per cent of the estimated figure (*i.e.*, $4,000,000). N. Y. Times, Nov. 25, 1952, p. 22, col. 6.

12. In Combs v. Snyder, 101 F. Supp. 531 (D.C. 1951), the district court, in denying plaintiff's motion for an injunction to restrain enforcement of the gambling tax, recognized the constitutional questions involved, but felt it "unnecessary to discuss" them because "it is within the discretion of a court of equity to deny its aid to one who does not come into court with clean hands." *Id.* at 531-532. The Supreme Court affirmed *per curiam.* 342 U.S. 939 (1951).

United States v. Forrester, 105 F. Supp. 136 (N. D. Ga. 1952) raised the constitutional question of the privilege against self-incrimination. Taxpayers claimed that the informational requirements of the federal wagering tax necessitated disclosure of incriminating facts with the collector, which contravened the Fifth Amendment: "No person . . . shall be compelled in any criminal case to be a witness against himself . . ." U.S. CONST. AMEND. V, § 1. Citing United States v. Murdock, 284 U.S. 141 (1931), the district court stated the settled rule that the constitutional privilege does not accord protection to a person where the information might be used against him in some form of criminal proceedings brought by a state or another country. The privilege only protects a person against prosecution under federal laws.

13. 105 F. Supp. 322 (E.D. Pa. 1952).

14. *Id.* at 323.

15. 21 U. S. L. WEEK 3087 (U.S., Oct. 14, 1952); argued Dec. 16-17, 1952, 21 U. S. L. WEEK 3178 (U.S., 1952).

16. United States v. Robinson, 107 F. Supp. 38 (E.D. Mich. 1952); United States v. Smith, 106 F. Supp. 9 (S.D. Cal. 1952); United States v. Nadler, 105 F. Supp. 918 (N.D. Cal. 1952).

17. Cases are collected and briefly discussed in Notes, 95 L. Ed. 50 (1951); 81 L. Ed. 776 (1936). See also Rottschaefer, AMERICAN CONSTITUTIONAL LAW, 175-181 (1939).

to tax is *Veazie Bank v. Fenno.*[18] That case involved a federal tax of ten per cent on the amount of state bank notes in order to protect the notes of the newly established national banks from competition. The Supreme Court upheld the tax on the theory that Congress was merely doing in an indirect manner what it could do directly under its currency power. Similarly, the Supreme Court later sustained the protective tariff on the ground that it is a valid regulation of foreign commerce.[19]

It should be carefully noted, however, that an entirely different situation exists where the federal government uses the taxing power for the ulterior purpose of regulating matters wholly outside the scope of any delegated federal power. In 1902 Congress levied a prohibitive tax of ten cents per pound on colored oleomargarine.[20] Clearly, the purpose of the tax was to eliminate oleomargarine as a competitor for the butter market. However, in upholding the validity of the oleomargarine tax in *McCray v. United States,*[21] Mr. Justice White developed the so-called doctrine of "objective constitutionality." Briefly stated, the test is that a taxing measure is valid if "on its face" it does not disclose other than a revenue purpose. The judiciary shall not consider it a part of its function to explore the motives which may have led Congress to enact the tax law. In other words, the Court confines itself to the express language of the revenue act, and pretends to be ignorant of what everyone knows about the purposes of the law. Such a test was an open invitation to Congress to use the taxing power as a means of exercising a general national police power.[22]

The invitation was readily accepted by the proponents of a federal child labor act. After the disappointing experience of *Hammer v. Dagenhart*.[23] another basis was sought upon which to justify a new federal child labor law. Naturally enough they turned to the taxing clause with some assurance after the *McCray* decision. In *Bailey v. Drexel Furniture Co.,*[24] however, the Court in an eight to one decision held unconstitutional a federal tax of ten per cent of the net profits of certain designated industries employing children below specified ages. The Court, finding it difficult to void the tax under the "objective constitutionality" formula, devised another test—the so-called "penalty" doctrine. Although Chief Justice Taft did not indicate exactly what characteristics are necessary to brand an act as "penal" rather than fiscal, he expressed a willingness to examine and evaluate other evidences present in the act besides superficial statements indicating the purposes to raise revenue. Nevertheless, the Court in the

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18. 75 U.S. 533 (1869).

19. Hampton & Co. v. United States, 276 U.S. 394 (1928). See Reuschlein and Spector, *Taxing and Spending: The Loaded Dice of a Federal Economy,* 23 CORNELL L. Q. 1, 5-11 (1937). The first issue of this volume of the Cornell Law Quarterly contains a symposium on regulatory taxes. It is a useful source of reference.

20. The tax was repealed in 1950, 64 STAT. 20.

21. 195 U.S. 27 (1904). For an incisive analysis of the *McCray* and other cases in this area, consult the articles by Professor Cushman. *Social and Economic Control Through Federal Taxation,* 18 MINN. L. REV. 759 (1934); *The National Police Power under the Taxing Clause of the Constitution,* 4 MINN. L. REV. 247 (1920). *Cf.* Bergman, *The Federal Power to Tax and to Spend,* 31 MINN. L. REV. 328 (1947); Grant, *Commerce, Production, and the Fiscal Powers of Congress,* 45 YALE L. J. 751 (1936).

22. Cushman, *Social and Economic Control Through Federal Taxation,* 18 MINN. L. REV. 759, 776 (1934).

23. 247 U.S. 251 (1918). (First child labor law unconstitutional under the commerce clause).

24. 259 U.S. 20 (1922); Powell, *Child Labor, Congress and the Constitution,* 1 N. C. L. REV. 61 (1922).

Bailey opinion refused to overrule the inconsistent doctrine of "objective constitutionality" and the *McCray* case.

As Professor Cushman has so aptly pointed out,[25] the Oleomargarine Case and the Child Labor Tax Case provided the courts with two available judicial techniques for dealing with the validity of national police regulations under the taxing power. When a court wants to uphold a taxing measure, it may utilize the *McCray* doctrine and refuse to see or know anything about the tax which does not appear in the language of the act. On the other hand, if a court wants to invalidate a taxing statute, it may take judicial notice of the palpable legislative intention to regulate or destroy rather than raise money, and hold the act unconstitutional on the ground that it is not a tax but a penalty.[26]

In the cases subsequent to the Child Labor Tax Case, the Supreme Court readily employed the convenient alternative theories. Thus, in *United States v. Constantine,*[27] the Court in declaring void a special federal excise tax of $1,000 imposed annually on all persons conducting the liquor business in violation of state law talked in terms of the *Bailey* decision, and found the tax not a true tax but a penalty employed to enforce state law. But two years later, in *Sonzinsky v. United States,*[28] the Court upheld the National Firearms Act of 1934 which not only imposed an annual license tax of $200 on dealers in firearms, but also levied a tax of $200 on each transfer of a machine gun, sawed-off shot gun, and other noxious type firearms. Speaking for a unanimous court, Mr. Justice Stone declared that the act contained "no regulations other than the mere registration provisions, which are obviously supportable as in aid of a revenue purpose. *On its face* it is only a taxing measure . . ."[29] (Italics supplied). In its most recent decision on this subject, *United States v. Sanchez,*[30] the Supreme Court again reaffirmed the "on its face" doctrine in upholding a tax on marihuana which obviously had as its object the discouragement of the narcotic traffic.[31]

It is not at all surprising that in the present wagering tax cases the

25. Cushman, *supra* note 22, at 782.

26. See Cushman's comments on Magnano Co. v. Hamilton, 292 U.S. 40 (1934), which held a state excise tax on butter substitutes constitutional. *Constitutional Law in 1933-34,* 29 AM. POL. SCI. REV. 36, 51 (1935).

27. 296 U.S. 287 (1935). Mr. Justice Roberts wrote the majority opinion. For an elaboration of his views on the relationship between the taxing power and the states' police power, see Roberts, THE COURT AND THE CONSTITUTION (1951). In a dissenting opinion by Justice Cardozo, in which Justices Brandeis and Stone joined, the argument is made that the Court cannot assume that the "Congress is . . . punishing for a crime against another government." *Id.* at 298. The tax may be justified, according to the dissenters, one the theory that illegal dealers cannot complain of a higher tax if Congress felt that "a business carried on illegally and furtively is likely to yield larger profits than one transacted openly by law-abiding men" or that "the furtive character of the business would increase the difficulty and expense of the process of tax collection." *Id.* at 297.

28. 300 U.S. 506 (1937).

29. *Id.* at 513.

30. 340 U.S. 42 (1950). See Comment, 36 IOWA L. REV. 699 (1951).

31. Note the following language of Mr. Justice Clark: "It is beyond serious question that a tax does not cease to be valid merely because it regulates, discourages, or even definitely deters the activities taxed. Sonzinsky v. United States . . . The principle applies even though the revenue obtained is obviously negligible, Sonzinsky v. United States . . . or *the revenue purpose of the tax may be secondary,* Hampton & Co. v. United States. . . ." (Italics supplied) 340 U.S. 42, 44 (1950). The italicized portion of the above quotation is a questionable statement of the law. As previously pointed out, note 19 *supra,* the*Hampton* case was supportable on the constitutional power to regulate foreign commerce.

lower federal courts utilize both of the techniques developed by the Supreme Court. In the *Kahriger* decision,[32] Judge Welsh bases his arguments on the penalty doctrine to invalidate the tax. Turning his attention to the registration and informational provisions of the statute, he poses this question: "Is the purpose of the Act . . . to create revenue or to constitute a host of informers?"[33] Relying solely on *United States v. Constantine,* he finds the gambling tax void as an invasion of the police power of the states, because "the exaction is in no proper sense a tax but a penalty imposed in addition to any the state may decree for the violation of a state law."[34] But as demonstrated by the three subsequent cases supporting the wagering tax,[35] the analogy to the *Constantine* situation is a weak one. *Constantine* involved a federal tax of $1,000 on liquor dealers operating contrary to state laws. There was a regular federal excise of $25.00 on all liquor dealers; only those illegally dealing in intoxicants were subject to the $1,000 tax. Consequently, the tax was limited to those persons who were state law violators. In the gambling tax, however, there is no such discrimination. Commission of a crime is not a condition precedent to the payment of the tax. It applies irrespective of the legality of the gambling activity under state law.

The trio of decisions sustaining the wagering tax rely heavily on the *McCray-Sonzinsky-Sanchez* rationale. The district courts stress the fact that it is not their duty to search out the motives which impelled Congress to enact such a law. The language is familiar; the "on its face" doctrine is reiterated.[36] In the *Nadler* case,[37] the court notes that the registration and informational provisions of the statute are similar to those found in many other tax laws. On previous occasions the Supreme Court has declared that where the regulations have some reasonable relationship to the exercise of the taxing power, they are valid.[38] It may be argued that the information required here is necessary for the efficient collection of the taxes. It is well-known that professional gamblers operate in a surreptitious fashion. Therefore, the Government maintains that it is necessary to obtain names and the location of the gamblers' whereabouts in order to facilitate the collection of the ten per cent wagering tax.[39] However, even if this

32. United States v. Kahriger, 105 F. Supp. 322, 323 (E.D. Pa. 1952).
33. *Ibid.*
34. See note 27 *supra.*
35. Two of the cases distinguish the *Constantine* decision on the basis of the above analysis. United States v. Robinson, 107 F. Supp. 38, 40 (E.D. Mich. 1952); United States v. Nadler, 105 F. Supp. 918, 919 (N.D. Cal. 1952). However, Judge Yankwich considers the *Constantine* case overruled. United States v. Smith, 106 F. Supp. 9, 12 (S.D. Cal. 1952).
36. *E.g.,* note Judge Holtzoff's statement: "The Courts may not delve into the minds of the members of Congress. The judiciary is without power to scrutinize the motives and the purposes of the legislative branch of the government. If an Act of Congress professes on its face to levy a valid tax, it is immaterial that the Congress may have, in fact, sought to attain a different or additional objective." United States v. Robinson, 107 F. Supp. 38, 39-40 (E.D. Mich. 1952).
37. United States v. Nadler, 105 F. Supp. 918, 919 (N.D. Cal. 1952).
38. *E.g.,* in United States v. Doremus, 249 U.S. 86 (1919), the Supreme Court upheld the elaborate regulatory provisions of the Harrison Narcotics Act on the theory that they were designed to facilitate the enforcement of the tax. But there can be little doubt that the dominant purpose of the tax was to regulate an exclusively state matter. Cushman, *supra* note 22, at 771-773. For subsequent judicial history of the tax, see Linder v. United States, 268 U.S. 5 (1925); United States v. Daugherty, 269 U.S. 360 (1926); Nigro v. United States, 276 U. S. 322 (1928).
39. Brief for Appellant, pp. 13-26, United States v. Kahriger, 105 F. Supp. 322 (E.D. Pa. 1952).