

Income Tax Is Voluntary

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In this article, we will explore the evidence that indicates that the vast majority of Americans do not lawfully owe income taxes. Once you become convinced that you don't owe any income tax, the next question is how do you un-volunteer. So the article will also address techniques that may allow you to un-volunteer.

Authority to Tax

We will first discuss the authority of the federal government to tax Americans. The Constitution allows Congress the power to lay and collect two kinds of taxes: direct taxes and indirect taxes.

There are two authorities in the constitution delegating this power of direct taxation given to Congress.

"Representatives and direct taxes shall be apportioned among the states which may be included within this Union, according to their respective numbers..." [Article 1, Section 2, Clause 3]

"No capitation, or other direct tax, shall be laid, unless in proportion to the census or enumeration herein before directed to be taken." [Article 1, Section 9, Clause 4]

A direct tax is one levied directly on an individual (e.g. poll tax, capitation tax) or their property (e.g. property taxes). This means a direct tax is a property rights issue because Americans have inalienable rights to their person and their property. Your person or property cannot be federally taxed with a direct tax. This restriction does not apply to the states. So, states can impose a direct tax on your person or your property, i.e. property tax. Also note that the inalienable right of property also includes the income from that property. This means the federal government cannot directly tax the income from your person or your property.

The Constitution says direct taxes must be “apportioned among the states”. This means “*to distribute or allocate proportionally*” (Webster). It means the tax must be divided up equally among the states, based on their population. That is one of the reasons a census is taken every ten years. So, the power to lay a direct tax on the people and/or their property was not delegated to the federal government.

In practical terms, this means that the States become the collecting agency for direct taxes for the federal government. If Congress wants to raise 10 million dollars, it divides that amount proportionally among the states, based on their population. The states legislatures would then collect the necessary monies. The States would be required to assess and collect their portion of the direct taxes apportioned to it by Congress and to forward the revenues to the Department of the United States Treasury.

Notice that the State must assess the tax. Rendering an assessment of a direct tax is the function of the government, not the taxpayer. To require a citizen to self-assess a direct tax involuntarily (by filling out a Form 1040) is a violation of the 13th Amendment (prohibition against “involuntary servitude”). The Supreme Court has ruled that the “machinery” or “instrumentality” which ascertains the amount of tax due is the government “agency whose action is called an assessment.” For direct taxes, if there is no assessment made by the government, there is no liability to pay the tax. Anyone who files a tax return (Form 1040) is assessing himself. They are also declaring, under “penalty of perjury,” that the information provided on the tax return is true, complete and correct. So filling out a tax return and remitting payment of any amount of revenue is a voluntary act.

Although Congress has the power to levy direct taxes, it has not done so since the Civil War. Some people think the 16th Amendment removed the apportionment feature of direct taxes. This is not true. Even if direct taxes did not have to be apportioned, the tax must still be applied to the states, not to the individual people. This means that all federal taxes currently in effect are in the class of indirect taxes, including the “income tax”.

An indirect tax is one laid on taxable activities. Some activities are taxable and some are not. This kind of tax is usually passed on to consumers. The authority to levy an indirect tax is also found in the Constitution.

[“The Congress shall have power to lay and collect taxes, duties, imposts and excises to pay the debts and provide for the common defense and general welfare of the United States: But all duties, imposts and excises shall be uniform throughout the United States.”](#)
[Article 1 Section 8, Clause 1, emphasis added]

First note that indirect taxes must be uniform. This means that all subjects in a taxable category or class will be taxed at the same rate. If the tax on distilling alcohol is 5% of the net income, then all distilling of alcohol must be taxed at the same rate.

Next, notice that this section of Constitution lists three kinds of indirect taxes, including only: excise, duties on imports, or tariff.

[“Excise. ... Tax laid on manufacture, sale or consumption of commodities or upon license to pursue certain occupations or upon corporate privileges.”](#) [Black’s Law Dictionary, 5th Edition]

This includes, but is not limited to, taxes on products such as cigarettes and liquor. It would also include taxes on corporations.

“Duties on imports. This term signifies not merely a duty on the act of importation, but a duty on the thing imported.”[Black’s Law Dictionary, 5th Edition]

“Tariff. The list or schedule of articles on which a duty is imposed upon their importation into the United States, with the rates at which they are severally taxed.” [Black’s Law Dictionary, 5th Edition]

A tax on duties, imposts and excises is not on the person (capitation tax) engaged in an activity, and it is not on the income (property) received from an activity, but is on the activity itself. And this taxable activity is a ‘privilege’ that is granted and regulated by the government. The tax rate is imposed on that activity is determined by the income produced by that activity. The income is just a guideline for determining the amount of tax. The tax is not on the income!

The important distinction for an indirect tax is that it is a tax on an activity, it is on something you do. You can avoid the tax by not engaging in the activity. These three forms of taxation are referred to as “voluntary” or “privilege” taxes because the activity which is taxable is engaged in voluntarily and as a privilege granted by the government. It does not cover activities which are exercised by citizens as a natural, constitutionally secured right. The income itself is not taxed. It is the activity that produced the income that is taxed. And that activity is always a taxable privileged activity.

For example, a gasoline excise tax is not on the gasoline, it is on the sale of the gasoline. Gasoline is property, not an activity. Property can only be taxed with a direct tax. It is the ‘sale’ of the gasoline that is taxable, an activity. The amount of the indirect tax is usually passed on to the consumer as the tax is included in the price of the product.

An easy way to remember the distinction between direct and indirect taxes is to correlate them to inalienable rights and privileges. Inalienable rights, exercised by an individual, can only be taxed directly with a capitation (head) tax, or a direct tax apportioned among the states. A capitation tax is on your body, which is your personal property, and is imposed on the state where the people live, not on the people directly. Indirect taxes (duties, imposts and excises) are applied to privileges and they must be taxed uniformly. The tax is not on the people or the property, because these can only be taxed directly, through apportionment. Therefore, the tax is called indirect, because it is on a privileged activity (such as the manufacture of alcohol), but the tax is indirectly passed on to the people buying the alcohol. Any tax on a company activity is really passed on to the customers. That makes it an indirect tax.

If the Supreme Court had ruled that the income tax was a direct tax, it would be unconstitutional because it is not apportioned. However, the following case shows that the Supreme Court has ruled that it is an excise tax which makes it constitutional.

“The conclusion reached in the Pollock case ...recognized the fact that **taxation on income was**, in its nature, an excise, entitled to be enforced as such.” [Brushaber v. Union Pacific Railroad Co. 240 U.S. 1, 16-17 (1916)]

An excise tax is not on property, but is on privileges. Privileges granted by the government. Before you can be liable for an income tax, you must be exercising a government privilege that is producing income. The question to ask here is: When I receive income, am I receiving it in connection with the exercise of an inalienable right, or in connection with the exercise of a government privilege? What is the source of that

income, and is there a tax imposed on that source activity? The Internal Revenue Code (IRC), in section 61, lists items of income from taxable 'sources', whatever that source may be. If the items of income are received 'in connection with' the exercise of an inalienable right (the source), then that income can only be taxed with a direct tax with apportionment among the states. If the items of income are received 'in connection with' the exercise of an excise taxed activity, a privilege (the source), then that income can be taxed with an indirect excise tax on the privileged activity that produces the income.

Is your income received from the exercise of an inalienable right or from the exercise of a privilege? What is the source? To stack the deck in their favor, the federal government always presumes that your income was received from an excise taxed activity, unless and until you claim otherwise.

You may wonder how you can know if an activity is a government-granted privilege. The answer is simple. If a license or certificate is required by law in order to engage in the activity the activity is essentially a privilege which is subject to indirect tax. Said another way, the activity would be illegal without the license or certificate issued by the government.

With indirect taxes, the assessment of the amount to be paid is made by the individual who, with the government's permission, has engaged in the taxable activity which is the subject of the tax law.

A crucial question we must ask is 'labor', or the 'income from labor' (wages), considered property? Or is the receiving of income a taxable activity? Is converting labor to cash a privileged excise taxable activity, or is it an inalienable right? Is labor and cash both something you own? Or something you do? What about a tax on income received from your labor, when your occupation does not require a license? Is labor a privileged taxable activity? Or is labor an inalienable property right that can only be taxed with a direct tax? Again, to the Supreme Court.

"As in our intercourse with our fellow-men certain principles of morality are assumed to exist, without which society would be impossible, so certain inherent rights lie at the foundation of all action, and upon a recognition of them alone can free institutions be maintained. These inherent rights have never been more happily expressed than in the Declaration of Independence, that new evangel of liberty to the people: "We hold these truths to be self-evident" - that is so plain that their truth is recognized upon their mere statement - "that all men are endowed" - not by edicts of Emperors, or decrees of Parliament, or Acts of Congress, but "by their Creator with certain inalienable rights" -- that is, rights which cannot be bartered away, or given away, or taken away except in punishment of crime -- "and that among these are life, liberty and the pursuit of happiness, and to secure these" -- not grant them but secure them-- "governments are instituted among men, deriving their just powers from the consent of the governed. ...Among these inalienable rights, as proclaimed in that great document, is the right of men to pursue their happiness, by which is meant the right to pursue any lawful business or vocation, in any manner not inconsistent with the equal rights of others, which may increase their prosperity or develop their faculties, so as to give them their highest enjoyment. **The common business and callings of life, the ordinary trades and pursuits, which are innocuous in themselves, and have been followed in all communities from time immemorial, must, therefore, be free in this country to all alike upon the same conditions. The right to pursue them, without let or hindrance, except that which is applied to all persons of the same age, sex, and condition, is a distinguishing privilege of citizens of the United States, and an essential element of that freedom which they claim as**

their birthright. ... It has been well said that, "The property which every man has is his own labor, as it is the original foundation of all other property, so it is the most sacred and inviolable. The patrimony of the poor man lies in the strength and dexterity of his own hands, and to hinder his employing this strength and dexterity in what manner he thinks proper, without injury to his neighbor, is a plain violation of the most sacred property. [Butchers' Union Co. v. Crescent City Co. 111 U.S. 746 (1883), emphasis added]

"Included in the right of personal liberty and the right of private property - partaking of the nature of each - is the right to make contracts for the acquisition of property. Chief among such contracts is that of personal employment, by which labor and other services are exchanged for money or other forms of property." [Coppage v. Kansas 236 U.S. 1, at 14 (1915), emphasis added]

The Supreme Court has ruled that your labor is your most sacred property, and it is the basis of all other inalienable property rights. Can inalienable rights be taxed as privileges granted by the government? Not legally. Maybe Congress, when they passed the income tax laws, meant labor to be taxed? But, remember, Congress cannot legislate away parts of the Constitution. They can only pass laws that are in accordance with the Constitution, because the Constitution is where Congress gets its authority. If Congress could vote out the Constitution, you would have no rights.

Congress, the legislative body responsible for writing the tax code, understands that the income tax is really an excise tax.

"So the amendment (16th) made it possible to bring investment income within the scope of the general income-tax law, but did not change the character of the tax. It is still fundamentally an excise or duty with respect to the privilege of carrying on any activity or owning any property which produces income. The income tax is, therefore, not a tax on income as such. It is an excise tax with respect to certain activities and privileges which is measured by reference to the income they produce. The income is not the subject of the tax: it is the basis for determining the amount of tax." [Congressional Record - House March 27, 1943. pg 2580, emphasis added]

More recent evidence indicates that Congress understands that the income tax is really an excise tax.

"The Supreme Court, in a decision written by Chief Justice White, first noted that the Sixteenth Amendment did not authorize any new type of tax, nor did it repeal or revoke the tax clauses of Article I of the Constitution, quoted above. Direct taxes were, notwithstanding the advent of the Sixteenth Amendment, still subject to the rule of apportionment and indirect taxes were still the subject of the rule of uniformity. Rather, the Court found that the Sixteenth Amendment sought to restrain the Court from viewing an income tax as a direct tax because of its close effect on the underlying property." [From a report by The Congressional Research Service. Report No. 84-168A, 784 / 725 titled "Some Constitutional Questions Regarding the Federal Income Tax Laws", dated May 25, 1979, and updated Sept. 26, 1984, pg. 5, emphasis added]

So, since the income tax is an excise tax on privileged activities, how can it be mandatory unless you engage in privileged activities? According to the Supreme Court, it isn't mandatory!

"Our system of taxation is based upon voluntary compliance and self assessment, and not upon distraint [force]." [Flora v. U.S. 362 U.S. 145, at 176 (1960)]

So, the Supreme Court is saying that the income tax is voluntary and it is self-assessed. The IRS also knows that the income tax system is voluntary. On page 3 of the "1993

Instructions for Form 1040” there is a note from the commissioner of the IRS indicating that the income tax is voluntary. It says:

“Dear Taxpayer: Thank you for making this nation’s tax system the most effective system of voluntary compliance in the world.” [emphasis added]

How do you volunteer to participate in the income tax? We will see later that you volunteer partly by filling out a W-4 form with your employer. How do you assess yourself the tax? You fill out a Form 1040 and sign it under penalty of perjury that what you have reported is true.

The government lays various traps for people to convert an inalienable right into a privilege. Let’s take an example of running your own small business, sole proprietorship. A tax on the income from your personal inalienable right to work in your business would have to be a direct tax. But if you used that same business in a corporate activity, (a privilege) then the income would be taxable as an indirect excise tax on the privilege. Do you see why the government recommends incorporation for any business? It converts your inalienable right to a taxable privilege.

Some would argue that the 16th Amendment has given the Congress new taxing authority.

“The Congress shall have 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 constitutionality of the 16th Amendment was challenged in the case of Brushaber vs. Union Pacific R.R. Co., 240 US 1 (1916). The U.S. Supreme Court acknowledged the apparent conflict between Article 1, Section 2, Clause 3, of the Constitution, which required all direct taxes to be apportioned, and the 16th Amendment, which appeared to eliminate the apportionment requirement. The Court pointed out that the 16th Amendment did not repeal Article 1, Section 2, Clause 3, but noted that it was under a duty to uphold the 16th Amendment, if it could be interpreted in such a way so as to eliminate the conflict. The Court did hold the Amendment constitutional by interpreting it as applying only to “indirect taxes” or “excise taxes,” and not to “direct taxes.” This and other cases that followed stated that the 16th Amendment did not give Congress any new or additional taxing authority.

The IRS is aware of the distinction between direct and indirect taxes. They are also aware that a private citizen is not required to file a tax return. They have created a special form for those individual who, though not subject to the income tax, wish to voluntarily file. It is called “Form 1040 U.S. Individual Income Tax Return.” All money remitted in this manner, due to the voluntary nature of the requirements, lose their identify as a tax and are, in fact, a donation.

Income Tax and Regulations

Now we will look at the statutes which authorize the “income tax”. The statutes are found in Title 26 of the United States Code (USC) which may be found at <http://www.fourmilab.to/uscode/26usc/>. The regulations associated with the IRC can be found in Title 26 of the Code of Federal Regulations (CFR) which may be found at <http://www.access.gpo.gov/nara/cfr/index.html>. Title 26 of USC shows that the IRC is broken down into 9 subtitles, listed below:

Subtitle A – Income Taxes

Subtitle B – Estate and Gift Taxes

Subtitle C – Employment Taxes

Subtitle D – Miscellaneous Excise Taxes

Subtitle E – Alcohol, Tobacco, and Certain Other Excise Taxes

Subtitle F – Procedure and Administration

Subtitle G – The Joint Committee on Taxation

Subtitle H – Financing of Presidential Election Campaigns

Subtitle I – Trust Fund Code

Notice that Subtitle D and E cover various excise taxes. Remember that excise taxes are a form of indirect taxation that is authorized by the Constitution. These are legitimate taxes collected in a valid manner.

For our purposed study, we will be exploring Subtitles A which deal with “Income Taxes”, and C which deals with “Employment Taxes.” Traditionally, we think of both of these as being “income tax.” relate to what we refer to as “income tax”. If the income tax, is an excise tax on certain privileged activities, let’s look in Subtitle A to see the types of activities that are deemed privileged. To do this we’ll look in Chapter 1 (titled, “Normal Taxes and Surtaxes”) for a list of activities. Here we will list the subchapter headings that seem to designate privileged activities:

- Corporate Distributions and Adjustments
- Banking Institutions [includes banks, credit unions, savings & loans]
- Natural Resources [oil companies, mining companies, etc.]
- Estates, Trusts, Beneficiaries and Decedents
- Partners and Partnerships
- Insurance Companies
- Regulated Investment Companies and Real Estate Investment Trusts
- Disposition of Property
- Capital Gains and Losses
- S Corporations
- Cooperatives and Their Patrons

You will notice that these taxes apply to businesses and do not apply to most working Americans. Chapter 2 of Subtitle A deals with “Tax on Self-employment Income” and Chapter 3 deals with “Withholding of tax on Nonresident Aliens and Foreign Corporations.” Again, these do not apply to most Americans.

The first “income tax”, imposed at Subtitle A, is a tax on income removed from America by non-resident aliens (one who is neither a resident or a citizen of this country), or a tax on Americans removing income from foreign nations. The second “income tax” (called employment taxes in this subtitle C), is a tax on wages of federal, state and local government employees or corporate officers. This is the section that most employers believe authorizes them to withhold wages to employees pay. We will see that there is no authorization for this withholding in most cases.

Income subject to tax under Subtitle A is either: income derived from **U. S. sources** by nonresident aliens, or by certain American businesses. **Withholding** of income tax from payments of **items** of income under Subtitle A is limited to those who are **authorized** and

required to withhold, called “withholding agents”. Instructions for withholding agents are found in Publication 515, “Withholding of Taxes on Nonresident Aliens and Foreign Corporations.” Although there is a tax on foreign income received by Americans, the withholding provisions of Subtitle A do not apply to this income.

Publication 515 does not refer to **American** citizens, except to state that its rules **do not apply to them**. It says that if an individual furnishes a statement that he or she is a citizen or resident of the United States, not to withhold. It also says, “instead, get Publication 15, Circular E, Employer’s Guide to Withholding.” Note carefully that it does not refer to another publication that explains income tax withholding; it refers us to Employment tax withholding. This is a clear indication that income tax withholding is limited to nonresident aliens and businesses. The statute substantiates this position.

Circular E, which relates to Subtitle C [employment taxes] taxes not Subtitle A, says that employers are required to withhold “income, FICA, and FUTA taxes” from employees, file 941’s and 945’s, 1099’s, etc. It says that there are two classes of employers - Federal Government Employers, and State and Local Government Employers. Subtitle C has its own definition of “employee”:

“For purposes of this chapter [the chapter in the IRC dealing with employment taxes], the term ‘employee’ includes an officer, employee, or elected official of the United States, a State, or any political subdivision thereof, or the District of Columbia, or any agency or instrumentality of any one or more of the foregoing. The term ‘employee’ also includes an officer of a corporation.” [26 UCS § 3401(c), comment added]

Before fully analyzing this definition, let’s see what some of the words mean. The usage of the terms “United States” and “State” in the above definition is misleading. These terms are defined in the IRC as follows:

“When used in this title [mean the entire IRC], where not otherwise distinctly expressed or manifestly incompatible with the intent thereof - ... The term ‘United States’ when used in a geographical sense includes only the States and the District of Columbia.” [26 USC § 7701(a)(9), comments added]

“When used in this title [mean the entire IRC], where not otherwise distinctly expressed or manifestly incompatible with the intent thereof - ...The term “State” shall be construed to include the District of Columbia, where such construction is necessary to carry out provisions of this title.” [26 USC § 7701(a)(10), comment added]

So, at first blush the definition “employee” would seem to include only those who work for the federal government, state, county or local governments, or officers of a corporation. However, when we see the definition of “United States” and “State”, we see that these terms mean the District of Columbia. The definition for employee also includes the phrase “instrumentality”. This term cannot mean the *de jure* [meaning right, legitimate and lawful] States since they created the federal government and therefore cannot be an instrumentality of the entity they created. It is possible that the States have been federalized in some fashion. [See our article on the Buck act for more on this topic.] If it is referring to Federal States, then it would be possible for them to be instrumentalities. However, if they are instrumentalities, then they are *de facto* [one which must be accepted but for all practical purposes but is illegal or illegitimate] federal States and their jurisdiction is no greater than the federal government which includes only the District of Columbia [per 4 USC § 72]. So there is no federal jurisdiction to tax either

de jure or *de facto* States. So, it is evident from these definitions, that the IRS only has authority in the District of Columbia.

Since 26 USC § 3401 is located in subtitle C (employment taxes), Chapter 24 (collection of Income Tax at source on wages), it means that the definition for “employee” applies to employment taxes. Since Subtitle C defines “employee” in this way, it is obvious that the vast majority of Americans do not fit the definition and therefore they do not owe employment taxes.

If you are an American residing in America and are not receiving foreign income, you are not subject to Subtitle A income taxes. If you are not employed by a government agency or work in the District of Columbia or are an officer in a corporation, you are not an employee for purposes of Subtitle C Employment taxes. Thus, if you are not subject to “income tax” or “employment taxes,” it is your choice to stop volunteering to pay it.

The government has us all confused. **Income**, for purposes of Subtitle A, is taxable to Americans only if it comes from a foreign source, which does not affect most of us. Subtitle C “income” is wages or salaries paid to government officials or workers, which does not apply to most of us. If you are an American who is paying income tax, it is most likely the Subtitle C “employment tax”.

We will examine Subtitles A and C in much greater detail below.

Subtitle A Taxes

Much of Subtitle A deals with taxes on foreigners working in the U.S. or Americans working overseas. So it would be helpful to see how the IRC defines “foreign.”

“When used in this title [the entire IRC], where not otherwise distinctly expressed or manifestly incompatible with the intent thereof - ...The term ‘foreign’ when applied to a corporation or partnership means a corporation or partnership which is not domestic.” [26 USC § 7701(a)(5)]

But to understand what “domestic” means, we have to see how it is defined.

“When used in this title [the entire IRC], where not otherwise distinctly expressed or manifestly incompatible with the intent thereof - ...The term ‘domestic’ when applied to a corporation or partnership means created or organized in the United States or under the law of the United States or of any State unless, in the case of a partnership, the Secretary provides otherwise by regulations.” [26 USC § 7701(a)(4), comments added]

So, according to the above definitions “foreign” means outside the UNITED STATES. This cannot include the 50 States since the definition for the UNITED STATES excludes the States. The Supreme Court also has ruled that the 50 States are foreign to the UNITED STATES. But the federal government does not have any jurisdiction over the *de jure* States according to the U.S. Constitution Article 1, Section 8, clause 18. Therefore, the federal government does not have any direct taxing authority within the States.

Subtitle A deals with “income taxes.” But we shall see that certain income is excluded from the income tax. According to 26 CFR § 1.861-8T(d)(2)(ii)(A), income which is exempt is excluded from federal income taxes.



For purposes of this section, the term **exempt income** means any **income that is**, in whole or in part, **exempt, excluded, or eliminated for federal income tax** purposes. [emphasis added]

Then, 26 CFR § 1.861-8T(d)(2)(iii)(A through D) goes on to list income which is included in this tax. The list includes (A) the income of foreigners working in the UNITED STATE, (B) income of DISC and FSC [will be defined later], (C) the income of a possession corporation [defined later], and (D) foreign earned income as defined in 26 USC 911 which deals with UNITED STATES citizens living and working abroad. Logic dictates that all other income is excluded from Subtitle A income tax.

Certain American businesses, known as FSC (Foreign Sales Corporations) and DISC (Domestic International Sales Corporations), are taxed by the United States on their foreign income. The remainder of the Subtitle A income tax code applies to nonresident aliens (under one or more tax conventions), who are taxed on the income from the United States [District of Columbia] and it's Possessions. Certain foreign businesses operating in the District or the Possessions are taxed on their "domestic" income. This part of the income tax, codified at Subtitle A, has nothing to do with the 50 States or any of their citizens. From this point forward, we will demonstrate this in a step by step fashion. Pay careful attention as it can get confusing.

Here, directly from the regulations, is a brief description of how to determine **taxable income** under Subtitle A. In Subtitle A, Chapter 1, Subchapter N deals with "Tax[s] Based on Income From Sources Within or Without the United States." The following provisions apply in determining whether items of income, from sources within or without the United States, are taxable.

"Sections 861(b) and 863(a) state in general terms how to determine taxable income of a taxpayer from sources within the United States after gross income from sources within the United States has been determined." [26 CFR § 1.861-8(a)(1)]

Once "**gross income** from sources within the United States has been determined" we are instructed to refer to 861(b) and 863(a) for instructions on how to determine **taxable** income. According to IRC § 61, "Gross income means all income from whatever source derived." This definition is not all-inclusive, as one must determine "gross income" from "sources within or without" the United States before one can apply other provisions to determine **whether** it is taxable or not.

"Determination of taxable income. The taxpayer's taxable income from sources within or without the United States will be determined under the rules of Secs. 1.861-8 through 1.861-14T for determining taxable income from sources within the United States." [26 CFR § 1.863-1(c)]

So, 26 CFR 1.861-8 through 1.861-14T govern how taxable income is determined.

"...the term '**statutory grouping**' means the gross income from a specific source or activity which must first be determined in order to arrive at 'taxable income' from which specific **source or activity** under an operative section. (See paragraph (f)(1) of this section.)" [26 CFR § 1.861-8(a)(4)]

It appears that in order to determine whether income is taxable, we must analyze it in light of its **statutory grouping**. Statutory groupings include both specific **sources** of income **and** specific income-producing **activities**, under **operative sections** shown below, at 26 CFR § 1.861-8 (f)(1) which says in part "...the determination of taxable

income of the taxpayer from specific sources or activities and which gives rise to statutory groupings to which this section is applicable...”

The regulations continue to narrow down the process of determining taxable income. It is the sources or the activities which give rise to the statutory groupings, so income must be allocated to one or the other, whether source or activity, in order to be exposed to taxation. But, no matter what, it is the specific source or the specific activity that gives rise to the statutory grouping.

“The rules contained in this section apply in determining taxable income of the taxpayer from specific sources and activities under other sections of the Code, referred to in this section as operative sections. See paragraph (f)(1) of this section for a list and description of operative sections.” [26 CFR § 1.861-8(a)(1)]

This includes another reference to paragraph 26 CFR § 1.861-8 (f)(1) for the list of operative sections. The first sentence of the above citation says “the rules contained in this section (Section 1.861-8) apply in determining taxable income....” We must be getting close to a full understanding. We now know that we must first determine gross income from sources (or activities) and then apply the rules under 1.861-8 to determine whether our “gross income from sources” is subject to an income tax. These rules tell us that we must find the **operative sections** to make the final determination. Note that so far, we have not been told who taxpayers are.

26 CFR § 1.861-8 Computation of taxable income from sources within the United States and from other sources and activities. “The operative sections of the Code which require the determination of taxable income of the taxpayer from specific sources or activities and which gives rise to statutory groupings to which this section is applicable include the sections described below.” [26 CFR § 1.861-8 (f)(1)]

Here, the term “include” means “**includes only**.” The above sentence says “these are the only operative sections.” We need not look any further! This section has six subsections (i through vi). The first three (i through iii) state:

26 CFR § 1.861-8 (f)(1)(i)
Overall limitation to the foreign tax credit...{as provided in section 904(a)(2)}

26 CFR § 1.861-8 (f)(1)(ii)
[Reserved]

26 CFR § 1.861-8 (f)(1)(iii)
DISC and FSC taxable income... [Domestic International Sales Corporation and Foreign Sales Corporation] {Sections 925 and 994}

So, (i) has to do with the foreign tax credit, (ii) is reserved, and (iii) has to do with the foreign income of a DISC or FSC. So (iii) is the only one that might possibly describe an American business. These two business types are United States businesses deriving most of their profits from exporting goods. There are no other provisions that tax the income of American businesses or people. Since FSC and DISC are the only American businesses subject to the tax, and the tax is on foreign-source income and not domestic-sourced income, **American citizens are not subject to Subtitle A income tax**, unless we are nonresident aliens deriving income from “United States” sources. For purposed of clarity on this issue, it would not make any difference if an individual is a UNITED STATES

citizen or an American National (State Citizen) [See our article about State vs. Federal Citizen for more details on these two classes of citizens.]

The last three subsections (iv through vi) apply either to nonresident aliens or foreign corporations, whether operating “within the United States” (the District of Columbia) or “without the United States” (the possessions or foreign nations).

26 CFR § 1. 861-8 (f)(1)(iv)

Effectively connected taxable income. Nonresident alien individuals and foreign corporations engaged in trade or business [“trade or business” is defined in 26 USC 7701(a) included the performance of the function of a public office] within the United States...

26 CFR § 1. 861-8 (f)(1)(v)

Foreign base company income...

26 CFR § 1. 861-8 (f)(1)(vi)

Other operative sections. The rules provided in this section also apply in determining—

This last section deals with “other operative sections”. It has thirteen subsections (A through M) listed below:

26 CFR § 1. 861-8 (f)(1)(vi)(A)

The amount of foreign source items...[FSC & DISC]

26 CFR § 1. 861-8 (f)(1)(vi)(B)

The amount of foreign mineral income...[FSC & DISC]

26 CFR § 1. 861-8 (f)(1)(vi)(C)

[Reserved]

26 CFR § 1. 861-8 (f)(1)(vi)(D)

The amount of foreign oil and gas extraction income [FSC & DISC]

26 CFR § 1. 861-8 (f)(1)(vi)(E)

[deals with tax credit of a domestic corporation]

26 CFR § 1. 861-8 (f)(1)(vi)(F)

[deals with Puerto Rico tax credits]

26 CFR § 1. 861-8 (f)(1)(vi)(G)

[deals with Virgin Islands tax credits]

26 CFR § 1. 861-8 (f)(1)(vi)(H)

The income derived from Guam by an individual...

26 CFR § 1. 861-8 (f)(1)(vi)(I)

[deals with China Trade Act corporations]

26 CFR § 1. 861-8 (f)(1)(vi)(J)

[deals with foreign corporations]

26 CFR § 1. 861-8 (f)(1)(vi)(K)

[deals with insurance income of foreign corporations]

26 CFR § 1. 861-8 (f)(1)(vi)(L)

[deals with countries subject to international boycott]

26 CFR § 1. 861-8 (f)(1)(vi)(M)

[deals with the Merchant Marine Act of 1936]

The **operative sections**, 26 CFR § 1.861-8 (f)(1)(vi)(A through M) do not include businesses within the 50 states or income derived from sources within the 50 states.

Section 862 and its regulations apply to income derived from sources without the United States, and unless one had income from any of those sources, including the Possessions, that part does not apply. Therefore, Subtitle A does not apply unless one is a FSC or DISC receiving income from foreign sources or a nonresident alien or business deriving income from United States sources.

In summary, if you or your business are not a DISC or FSC, it appears that none of the above operative sections apply to **your** income. If you apply the above operative sections to your income, which one would you apply? Remember that the above are ALL the operative sections. Unless your business and your income are clearly described in Subchapter N, you had no income on which the United States can lay a claim for a Subtitle A income tax. Clearly, this statute does not apply to all Americans, or to all income. In fact, it would apply to very few Americans.

Subtitle C Taxes

The provisions that require withholding from employees are found only in Subtitle C, Employment Taxes. They are not imposed on foreign income, or on nonresident aliens, but on wages and salaries. The source of income or activity for Subtitle C is employment. Whether derived from “within or without” the United States is not a criterion for this Subtitle. Subtitle C requires employers to obtain W-4’s, deduct and withhold taxes from wages, file statements and transmittals, etc.

It should be clear that taxes on employment and taxes on business profits are two entirely different things. It is for this reason that they are discussed in different Subtitles and in different publications. Publication 15, “Employer’s Guide to Withholding”, describes procedures for employers to withhold taxes. It explains that “most employers” are required to withhold Social Security Taxes (FICA), Federal Unemployment Tax (FUTA) and “Income Tax”. Under General Instructions, it shows only two classes of employers-Federal Government Employers, and State and Local Government employers.

Subtitle C is divided into 5 Chapters:

- Chapter 21 is Social Security
- Chapter 22 is FUTA
- Chapter 23 is Railroad Retirement
- Chapter 24 is “Collection of Income Tax at Source on Wages”
- Chapter 25 is “General Provisions Relating to Employment Taxes and Collection of Income Taxes at Source”

The government has made it appear that the “income tax” paid by most businesses, and the tax withheld and collected from employees, is the income tax imposed by Subtitle A; they call it an income tax, but calling it an income tax does not make it one.

Most employers require their employees to furnish them with a W-4. Let’s examine a Form W-4 carefully. According to its instructions, Form W-4 is an authorization (providing that your earnings are, in fact, ‘wages’ as defined) to withhold federal income taxes, furnished by employees to employers. Under the instructions provided at the top of the front page, it says, “Purpose. Complete Form W-4 so your employer can withhold the

correct Federal Income tax from your pay.” In the Privacy Act Statement on the back of the form, it says the information required on the Form is required by Code Sections 3402 and 6109, and their regulations. Section 3402 is the section that imposes “employment tax” withholding and other requirements on employers. Bearing in mind that withholding agents withhold income taxes, and that employers withhold employment taxes, it becomes clear that not only are the two income taxes on different subjects, they are collected by different individuals, from different individuals, and for different reasons.

Since both the law and the W-4 say that employers are required to obtain a W-4 from employees and withhold taxes, the law must tell us also which employers these laws affect.

The IRC describes employers in section 3401 which says:

“For purposes of this chapter, the term ‘employer’ means the person for whom an individual performs or performed any service, of whatever nature, as the employee of such person...” [26 USC § 3401(d)]

This definition could include almost anyone. However, 3401(c) clearly defines employee in such a way that it is very clear who employers really are:

“For purposes of this chapter, the term ‘employee’ includes an officer, employee, or elected official of the United States [could read Washington D.C. per the definition of United States found at 26 USC § 7701(a)(9)], a State [could read Washington D.C. per the definition of State found at 26 USC § 7701(a)(10)], or any political subdivision thereof, or the District of Columbia, or any agency or instrumentality of any one or more of the foregoing. The term ‘employee’ also includes an officer of a corporation.” [26 USC § 3401(c), comments added in brackets]

The above [government] **employees** are the only Employees subject to the provisions of withholding of income tax at source on wages (Chapter 24).

For further clarification, let’s also look at part of the definition for “wages” which are taxable.

“For purposes of this chapter [relating to “Collection of Income Tax at Source of Wages” only], the term ‘wages’ means all remuneration (other than fees paid to a public official) for services performed by an employee for his employer, including the cash value of all remuneration (including benefits) paid in any medium other than cash; except that such term shall not include remuneration paid -” [26 USC § 3401(a), comments added]

It then goes on to list 21 separate items where wages are “not included”. Item 8 will be of importance to most Americans.

“for services for an employer (other than the United States or any agency thereof) - performed by a **citizen of the United States** if, at the time of the payment of such remuneration, it is reasonable to believe that such remuneration will be excluded from gross income under section 911;” [26 USC § 3401(a)(8)(A)(i), emphasis added]

At first blush it would appear that it would exclude the “wages” of most American citizens. But it says in order to qualify for this exclusion it has to adhere to the provisions of 26 USC § 911 which provides an exclusion for foreign earned income (American working and earning income in foreign jurisdictions). This is where the wages of most American would appear to get re-included. Since most Americans do not work for the government, it would appear that their wage are still not taxable.

Laws are precise. If they are not, they would be void for vagueness. The IRC is not **vague**. It's meaning is **obfuscated** (deliberately hidden from view). IRC § 3401(a) says the term “wages” means “all remuneration ... for services performed by an **employee** for his **employer**...” As we have already seen, you can't understand who an “employer” is until you understand who an “employee” is. Most Americans do not fall into the definition of employee. This being the case, why should employers collect taxes for the government when their employees don't qualify as IRC defined “Employees”?

There is a wonderful principle underlying all American lawmaking. Laws are meant and required to be understood by the average American. The common language is also the language of the law, and the rules of construction, syntax, and punctuation for the English language must be strictly adhered to when reducing laws to writing. When the lawmakers use a term differently than it is ordinarily understood, they must define the term as it is being used, **because** it means something different than its ordinary use would indicate. Thus, for purposes of Title 26, Internal Revenue, Congress has defined “employees” subject to “employment” taxes as government workers. For the rest of us, wages are not taxable.

When we read Subtitle C provisions relating to withholding, we find that the tax withheld is called or described vaguely as “a tax”:

SUBTITLE C EMPLOYMENT TAXES

Chapter 24 COLLECTION OF INCOME TAX AT SOURCE ON WAGES

SECTION 3402. INCOME TAX COLLECTED AT SOURCE

(a) REQUIREMENT OF WITHHOLDING

(1) IN GENERAL

Except as otherwise provided in this section, every employer making payment of wages [to government employees as defined in 26 UCS § 3401(c)] shall deduct and withhold upon such wages a tax determined in accordance with tables or computational procedures prescribed by the Secretary.

The sentence above could have said “the income tax imposed by Subtitle C, Section....” It does not. Instead, it says “a tax determined in accordance with tables ... prescribed by the Secretary.”

Below there will be several quotes from IRS Publication 515, “Withholding of Taxes from Nonresident Alien Individuals and Foreign Corporations”. It says that anyone who is required to withhold is a “withholding agent”.

“You are a withholding agent if you are a U.S. or foreign person that has control, receipt, custody, disposal, or payment of any item of income of a foreign person that is subject to withholding.”

It says that nonresident alien individuals and foreign corporations are subject to withholding.

“Generally, a foreign person is subject to U.S. tax on its U.S. source income. Most types of U.S. source income received by a foreign person are subject to U.S. tax of 30%. ... The tax is generally withheld (NRA withholding) from the payment made to the foreign person... Payments to all foreign persons, including nonresident alien individuals, foreign entities and governments, may be subject to NRA withholding.”

It says that if a payee furnishes a statement that he or she is a citizen or resident of the United States you do not have to withhold under these rules.

“Generally, you must withhold 30% from the gross amount paid to a foreign payee unless you can reliably associate the payment with valid documentation that establishes either of the following.

- The payee is a U.S. person.
- The payee is a foreign person that is the beneficial owner of the income and is entitled to a reduced rate of withholding.”

Until recently, it went on to say, “instead, get Publication 15, Circular E, Employer’s Guide to Withholding.”

Publication 515 does not refer us to any other publication for withholding taxes from items of income paid to citizens or residents. Publication 15 shows two classes of employers - Federal government employers, and State and Local government employers, matching precisely those who employ the “employees” defined at 3401(c). Publication 15 refers us to no other publication. Publication 15 also shows that employers are required to obtain W-4’s and furnish W-2’s to employees and 1099’s to independent contractors.

Now, it looks like the vast majority of American employers are withholding employment taxes, believing they are withholding income taxes. The only income taxes, required to be withheld on income, are on items paid to nonresident aliens. The only other “withholding” affects employment taxes for government employees. So every additional employer is voluntarily giving part of his employees’ pay to the government without any reason, except ignorance or fear, or a combination of both.

An additional evidence that most American’s do not owe employment taxes can be found in the function performed by the Office of Management and Budget (OMB). Congress has passed the Paperwork Reduction Act of 1980 [Pub. L. 104-13, Sec. 2, May 22, 1995, 109 Stat. 163, implemented as 44 USC § 3501] in order to suppress the ever-increasing burden of paperwork required by various government agencies. The act requires that every single request for information from the general public must bear a current OMB number. The act states:

“This bill ... requires all information request of the public to display a **control number**, an **expiration date**, and indicate **why the information is needed**, how it will be used, and **whether it is a voluntary or mandatory request**. Requests which do not reflect a current OMB control number or fail to state why not, are ‘**bootleg**’ requests and may be ignored by the public.” [emphasis added]

If you take a look at Form 1040, the only thing found is an OMB number, 1545-0074. The expiration date and the other information required by the Paperwork Reduction Act are missing. The CFR has a table at 26 CFR § 602.101, which lists all of the OMB numbers for IRS forms in compliance with the Paper Work Reduction Act. There are over ninety references to OMB 1545-0074 in the CFR relating to Subtitle A taxes. There are not references to Subtitle C taxes in the CFR for this OMB number. You can look at the relationship between 26 CFR and 26 USC in “Parallel Table of Authorities and Rules” [http://www.access.gpo.gov/nara/cfr/parallel/parallel_table.html]. Subtitle A only deals with income taxes for American working outside of the country, non-resident aliens working in American and certain types of corporations (FISC and DSC). Since it only relates to Subtitle A taxes then Form 1040 only relates to these taxes. It also means that Form 1040 does not apply to Subtitle C (employment taxes).

How You Volunteered

The last three sections have admittedly been rather complicated. But hopefully you could follow the logic. If so, you should have come to the conclusion that most Americans are not required to pay “withholding” taxes. If this is true, then there is an urgent question that must be asked. How did you volunteer to pay this tax? The answer can be found in IRC Section 3402.

(p) Voluntary withholding agreements

(3) Authority for other voluntary withholding

The Secretary is authorized by regulations to provide for withholding -
(A) from remuneration for services performed by an employee for the employee's employer which (without regard to this paragraph) does not constitute wages, and ...

This statute basically says that you can volunteer to have your employer withhold taxes from your wages. If we look in the Code of Federal Regulations (CFR) § 31.3402(p)-1, we find the document you use to volunteer for this tax. is a W-4 form.

Sec. 31.3402(p)-1 Voluntary withholding agreements.

(a) In general. An employee and his employer may enter into an agreement under section 3402(b) to provide for the withholding of income tax upon payments of amounts described in paragraph (b)(1) of Sec. 31.3401(a)-3 ...

(b) Form and duration of agreement. (1)(i) Except as provided in subdivision (ii) of this subparagraph, an employee who desires to enter into an agreement under section 3402(p) shall furnish his employer with Form W-4 (withholding exemption certificate) executed in accordance with the provisions of section 3402(f) and the regulations thereunder. The furnishing of such Form W-4 shall constitute a request for withholding.

So when you fill out a W-4 form, you volunteer to allow your employer to withhold taxes from your pay. The best way to avoid this problem is to not volunteer for it in the first place. Next time you start a new job, decline to fill out a W-4 form. There is no federal statute requiring you to do so. There is a federal statute requiring employers to ask for your SSN but there is not statute requiring you to provide an SSN. However, for a many people this would be frightening. They would be afraid that if they did not fill out a W-4 when taking a new job that the new employer would not allow them to work. While such an action would not be legal on behalf of the employer, it still is a risk that you would take. There have been Equal Employment Opportunity Commission suites have been won on this issue. The EEOC has ruled that an employer cannot refuse to hire an employee because they will not give their SSN.

Btu most people are already in a job where they have volunteered to pay withholding taxes by filling out a W-4. If this is your situation, you have two problems: how to get back the money the employer is withholding and how to stop the withholding. The next section will describe how to solve both of these problems.

How To Un-volunteer

If your employer is currently withholding “employment” taxes from you wages, the only way to get back the tax you paid is to file a tax return or an amended return. So, even though there does not appear to be a statute which requires most people to file, you may want or need to file in order to get a refund.

There is a little know and understood section of the IRC which can be used to get a refund. IRC § 1341 can be used for this purpose. The title of IRC Section 1341 is “Computation of tax where taxpayer restores substantial amount held under claim of right.” The relevant paragraphs of this section state:

(a) General rule

If-

- (1) an item was included in gross income for a prior taxable year (or years) because it appeared that the taxpayer had an unrestricted right to such item;*
- (2) a deduction is allowable for the taxable year because it was established after the close of such prior taxable year (or years) that the taxpayer did not have an unrestricted right to such item or to a portion of such item; and*
- (3) the amount of such deduction exceeds \$3,000,*
then the tax imposed by this chapter for the taxable year shall be the lesser of the following:

You can see that this is not the clearest language you have ever read and I’m sure you are wonder what this means. You are not alone. We have not found any tax preparers, CPAs or tax attorneys that know that it means either. In order to understand what it means, you would have to do extensive research into two areas: the common law and the history of the tax code. We’ve done this research in these areas and we’ll give you a brief overview of what we’ve found.

The key to understand the “claim of right” can be found in the common law. Great Britain, like the Roman Empire before it, has a dual legal system. The King and eventually Parliament controlled civil law. The civil courts included the equity and admiralty courts. These controlled cases where the government had an interest. The common law is the body of law that grew out of the people’s courts, the common law courts. These courts created law through a process of deciding cases which set a precedence which was upheld by later cases. The earliest explanation of this case law can be found in William Blackstone’s “Commentaries on the Laws of England.” A study of these commentaries reveals that there was not tax on compensation for labor due to a common law right that excluded compensation for personal labor from taxation. The taxes to run the government essentially came from commercial activity rather than from a tax on wages.

When the United States was founded and the Constitution was ratified by the 13 states, we essentially adopted the same dual legal system as existed in Great Britain. The individual’s common law right to his compensation for personal labor was carried over into our system of law.

The Constitution allows Congress the power to lay and collect two kinds of taxes: direct taxes and indirect taxes. A direct tax is one levied directly on anybody or anything. An

indirect tax is one laid on taxable activities, but only on those activities which are taxable and some activities are not taxable. Prior to 1913, there were a number of attempts to create a tax on the wages of an individual. The federal judiciary struck down all of these attempts because the Constitution granted no authority for such a tax.

When the first income tax statutes were passed, after the 16th Amendment was ratified, they were basically indirect excise taxes on profit from business activity. Few if any American's paid income tax in those days.

A dramatic change took place in the IRC took place in 1939 when the definition of income was changed to include "wages". This change was an attempt to convert an inalienable right, the right exchange your labor or money, into a taxable activity. However, chapter 1, §23 contains a remedy. In very clear language, this section says that compensation for personal services rendered is fully deductible. This means that people were able to take a deduction for all the wages they were paid. In 1954, Congress removed § 23 and moved the cure to §1341. However, the new language is very obscure. It talks about a "claim of right" and an "unrestricted right." But § 1341 still recognizes the right to compensation for labor without it being taxed.

This section can be applied to a tax return and in most cases you can get a complete refund. Using §1341, you can take a deduction on Schedule A (itemized deductions) for the entire amount of your wages. In most cases this reduces the taxable income to zero. No taxes due if there is no taxable income. So a complete refund can be requested.

Once you have a full a complete tax refund for your most recent tax year, you can stop future withholding by that employer. Take a copy of the tax return and the refund check with you to work. Then ask the payroll department to allow you to fill out a new W-4. Check the box that says "exempt". Read the back of the form and you will see the statutory requirements to prove that you are in fact exempt. Your latest tax return and refund check meet the requirement to prove you are exempt.

With no taxes being withheld, you will have to decide if there is any reason to continue to file a tax return. If you choose not to file a return, the IRS may send you a form letter asking you to file a return. You should be able to handle the problem by sending them a letter with an affidavit explaining how your only source of income was wages and that you are taking a "claim of right" based on IRC § 1341.