No. 02-1809

In The Supreme Court of the United States

J. ELLIOTT HIBBS, in his official capacity as Director of the Arizona Department of Revenue,

Petitioner,

v.

KATHLEEN M. WINN, Arizona taxpayer; DIANE WOLFTHAL, Arizona taxpayer; MAURICE WOLFTHAL, Arizona taxpayer; LYNN HOFFMAN, Arizona taxpayer,

Respondents.

On Writ Of Certiorari To The United States Court Of Appeals For The Ninth Circuit

PETITIONER'S REPLY ON THE MERITS

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ARGUMENT

I. The Plain Language of the Tax Injunction Act Prohibits This Challenge to Arizona's Tax Credit.

The Court can easily begin and end this case with the plain language of the Tax Injunction Act. By its express terms, the Act prohibits federal district courts from interfering not only with the "collection" of state taxes, but also with the "assessment" of such taxes. And the plain meaning of the word "assessment" refers to the process of calculating a taxpayer's ultimate tax liability – a process that includes the state tax credit at issue here. *See* Pet. Br. at 12-14.

Respondents have no plausible argument to explain why the term "assessment" in the Tax Injunction Act should not be given its ordinary meaning. Their best effort comes in the tentative suggestion that "[i]f the term 'assessment' is to be applied [here] in the same way as it is ordinarily applied to property taxes," then "'assessment' . . . would appear" to apply to only above-the-line calculations of taxable income. Resp. Br. at 15-16. But "assessment" as used in the Tax Injunction Act refers not to an assessment of property or income, but to an "assessment of . . . any tax." 28 U.S.C. § 1341. Further, Congress should be presumed to have used the term "assessment" in that Act the same way it uses the term in other federal statutes. As the Solicitor General details, "assessment" is used consistently in the Internal Revenue Code to mean the government's determination of a taxpayer's ultimate liability. U.S. Amicus Br. at 11-12. Respondents do not explain why Congress would have intended "assessment" to have a different meaning in the Tax Injunction Act than it has in other parts of the federal code, especially in the Internal Revenue Code.

Perhaps recognizing that "assessment" is only sensibly read to refer to the process of determining ultimate tax liability, Respondents now advance a new argument, one not adopted below: even if the Arizona tax credit is a component of an "assessment," nothing about their federal-court challenge "enjoin[s], suspend[s] or restrain[s]" that assessment. Resp. Br. at 16. That argument makes no sense. Respondents' own lawsuit requests that the district court "enjoin" the State from applying its tax credit in making "assessments" of state tax. Joint App. 15. If Respondents are successful, then they will have "enjoined" and "restrained" the State from making the "assessment . . . under State law." 28 U.S.C. § 1341; s*ee also Webster's New Int'l Dictionary* 2125 (2d ed. 1934) (giving one definition of "restrain" as "to hold back from acting, proceeding, or advancing, either by physical or moral force, or by any interposing obstacle" as well as other consistent definitions).[1]

Nor does *Jefferson County v. Acker* support Respondents' position that a suit to enjoin a tax credit does not restrain the State's assessment of taxes. 527 U.S. 423 (1999) (discussed in Resp. Br. at 15-16). *Jefferson County* involved a county's lawsuit to collect taxes from federal

[1] A taxpayer's involvement in the assessment of income tax does not eliminate the State's involvement in the assessment process. Although in most cases taxpayers initially determine their tax liability by filling out and filing their tax forms, the State assures compliance by checking the self-assessment. *See* Ariz. Rev. Stat. § 42-1108(A) ("the department [of revenue] may examine any return . . . to determine the correct amount of tax"). Moreover, Respondents request the district court to order Petitioner to disallow tax credits, which thus would require the State to examine each self-assessment.

judges that the county filed in state court and the judges removed to federal court. 527 U.S. at 423. In *Jefferson County*, the Court applied the plain language of the Tax Injunction Act and concluded that "a suit to collect a tax is surely not brought to restrain state action, and therefore does not fit the Act's description of suits barred from federal district court adjudication." *Id.* at 424. Here, in contrast, Respondents' lawsuit specifically requests the district court to enjoin state action – that is, to enjoin the State from applying its state tax credit law in making assessments of state tax.

In essence, Respondents' position is that the Tax Injunction Act applies only when a federal-court action, if successful, would deprive the state of tax revenue – that is, when a suit seeks to enjoin the *collection* of state taxes. Resp. Br. at 19-20. If Congress had wanted to enact that statute, it would have been easy enough; it could have deleted the words "assessment" and "levy" from the Tax Injunction Act. But that is not what Congress did, and Respondents cannot write the word "assessment" out of the Tax Injunction Act.[2]

Respondents cannot make sense of the statutory language in a manner that conforms to their position. According to Respondents, the term "assessment" refers only to above-the-line tax calculations, so that the statute

[2] Respondents wrongly argue that Petitioner attempts to rewrite the Tax Injunction Act in asserting that Congress intended the Act to prevent interference with state tax administration. Resp. Br. at 17. Congress's intent is demonstrated by its use of the words "assessment, levy and collection," which encompasses all three major parts of the state taxation system.

precludes challenges to tax *deductions*, but not to tax credits like the one at issue here. *See* Resp. Br. at 16. But a successful challenge to a tax deduction, like a challenge to a tax credit, may have the result of increasing state revenues – which under Respondents' theory should take it outside the scope of the Tax Injunction Act. And a litigant challenging a tax credit as underinclusive may seek expansion of the credit to other entities – or the court may award that relief – so that Respondents' own reading of the Act would allow federal courts to adjudicate a challenge that could deprive a State of tax revenue. In short, it is impossible to reconcile Respondents' policy arguments about when federal-court interference with state taxation should be prohibited with the actual language of the Tax Injunction Act. That language controls, and it is enough to dispose of this case.

II. The Tax Injunction Act's Legislative History Neither Overrides Nor Conflicts with Its Plain Language.

Respondents attempt to avoid the plain language of the Tax Injunction Act by arguing that its legislative history limits its scope to revenue-protection purposes and therefore does not apply to challenges to state tax credits. Resp. Br. 18-20. It is unnecessary to resort to legislative history because the language of the Act is clear and unambiguous. *See Davis v. Mich. Dep't of Treasury*, 489 U.S. 803, 808 n.3 (1989) (resort to legislative history unnecessary where statutory text is clear). Even if the Act's legislative history were relevant, it does not support Respondents' argument that Congress intended to limit its application to lawsuits that stop state revenue collection. While Congress sought, in part, to curtail efforts by out-of-state taxpayers to

avoid paying tax, this history does not limit the application of the Tax Injunction Act to that situation. *See Moskal v. United States,* 498 U.S. 103, 111 (1990) ("This Court has never required that every permissible application of a statute be expressly referred to in its legislative history.")

Further, Respondents ignore other aspects of the Act's legislative history that show that Congress was also concerned with federal-court challenges that interfered with the States' administration of the core sovereign function of taxation.[3] This Court has repeatedly noted this as an important congressional purpose behind the Tax Injunction Act. For example, in *Arkansas v. Farm Credit Services*, the Court stated:

> Enactment of the Tax Injunction Act of 1937 reflects a congressional concern to confine federal court intervention in state government, a concern prominent after the Court's ruling in *Ex parte Young*, 209 U.S. 123 (1908), that the Eleventh Amendment is not in all cases a bar to federal court interference with individual state officers alleged to have acted in violation of federal law.

520 U.S. 821, 826-27 (1997); *see also Nat'l Private Truck Council v. Okla. Tax Comm'n*, 515 U.S. 582, 590-91 (1995)

[3] There are two additional reasons behind the Tax Injunction Act that are discussed in *Aluminum Company v. Department of Treasury*, 522 F.2d 1120, 1124 (6th Cir. 1975). The first reason is a concern that the added expense of litigating in the federal courts might make it financially unsound for the State or a local taxing authority to contest a wealthy corporation's tax liability. The other reason is to relieve congestion in the federal courts by letting state courts settle state controversies. *Id.* (citing S.Rep. No. 1035, 75th Cong., 1st Sess. 102 (1937) and 81 *Cong. Rec.* 1416-17 (1937)).

("the Tax Injunction Act may be best understood as but a partial codification of the federal reluctance to interfere with state taxation"); *California v. Grace Brethren Church*, 457 U.S. 393, 410 n.22 (1982) ("Congress worried not so much about the form of relief available in the federal courts, as about divesting the federal courts of jurisdiction to interfere with state tax administration"); *Tully v. Griffin*, 429 U.S. 68, 73 (1976) (the Tax Injunction Act "has its roots in equity practice, in principles of federalism, and in recognition of the imperative need of a State to administer its own fiscal operations"); *Perez v. Ledesma*, 401 U.S. 82, 128 n.17 (1971) (Brennan, J., concurring in part and dissenting in part) (reasons for the Tax Injunction Act include that "federal constitutional issues are likely to turn on questions of state tax law, which, like issues of state regulatory law, are more properly heard in the state courts").

Respondents argue that the Court's language interpreting the Tax Injunction Act to prohibit interference with the state tax system is taken "out of context." Resp. Br. at 28. Although the Court's Tax Injunction Act cases have generally dealt with lawsuits that sought to interfere with the State's collection of taxes, the Court has never suggested that the plain language of the statute should be ignored in favor of a single purpose of the Act. To the contrary, the Court has held that the "statutory text 'is to be enforced according to its terms' and should be interpreted to advance 'its purpose' of 'confin[ing] federal-court intervention in state government.'" *Jefferson County*, 527 U.S. at 433 (quoting *Farm Credit Servs.*, 520 U.S. at 826-27).

The Tax Injunction Act's federalism purpose is the same purpose underlying the Johnson Act of 1934, 28 U.S.C. § 1342, which prohibits federal-court interference

with orders issued by state administrative agencies to public utilities. *See Grace Brethren*, 457 U.S. at 410 n.22. Respondents suggest that it is inappropriate to rely on the legislative history of the Johnson Act to explain the Tax Injunction Act. Resp. Br. at 17-18 n.10. But this Court itself has looked to the Johnson Act as a guide for interpreting the Tax Injunction Act – which is hardly surprising, given the fact that Congress itself expressly relied on the purpose underlying the Johnson Act when it enacted the Tax Injunction Act. *Grace Brethren*, 457 U.S. at 410 n.22; *Rosewell v. LaSalle Nat'l Bank*, 450 U.S. 503, 513-14 (1981) ("[a]s Senator Bone made clear, '[m]ost of the arguments which were used in support of the Johnson Act . . . apply in like manner' to the Tax Injunction Act") (quoting 81 *Cong. Rec.* 1416 (1937)). Thus, Congress's reliance on the congressional purpose for enacting the Johnson Act demonstrates that, in enacting the Tax Injunction Act, it was concerned with federal interference with a core sovereign function of state government as well as interference with the State's ability to collect revenue.

III. The Tax Injunction Act's Plain-Language Meaning Is Entirely Consistent with This Court's Precedent and with Many Lower Court Decisions.

Apparently recognizing the weakness of their textual and legislative history arguments, Respondents rely heavily on decisions of this Court adjudicating the merits of cases initiated in a federal district court that challenge constitutional state tax credits or deductions: *Committee for Public Education and Religious Liberty v. Nyquist*, 413 U.S. 756 (1973); *Mueller v. Allen,* 463 U.S. 388 (1983); and *Griffin v. Prince Edward County School Board*, 377 U.S.

218 (1964). Resp. Br. at 21-23. Respondents acknowledge, however, that the parties in these cases never raised the Tax Injunction Act and that the Court did not discuss the Act. It is well established that this Court does not consider itself bound by prior sub silentio holdings "when a subsequent case finally brings the jurisdictional issue" before it. *Fed. Election Comm'n v. NRA Political Victory Fund*, 513 U.S. 88, 97 (1994); *see also Will v. Mich. Dep't of State Police*, 491 U.S. 58, 63 n.4 (1989) (same); *United States v. L.A. Tucker Truck Lines, Inc.*, 344 U.S. 33, 38 (1952) (same). Moreover, the Tax Injunction Act allows federal jurisdiction if there is no plain, speedy or efficient remedy in the state courts. The Court may therefore presume that the parties' failure to raise the issue in *Nyquist, Mueller,* and *Griffin* was due to the inadequacy of the state court remedies. *See De Buono v. NYSA-ILA Med. and Clinical Servs. Fund*, 520 U.S. 806, 810 n.5 (1997) (Court presumed that lower court correctly determined that there was not an adequate state remedy and therefore no bar under the Tax Injunction Act given the State's "active participation in nearly four years of federal litigation with no complaint about federal jurisdiction"). Therefore, *Nyquist*, *Mueller*, and *Griffin* provide no assistance in determining whether the Tax Injunction Act applies to state tax credits.

Contrary to Respondents' assertion, the plain-language reading of the statute to cover challenges to tax credits is not a novel one; or one that breaks with a line of lower court authority. Many lower courts – including the district court below – have held that challenges that may result in "more" revenue for the State are barred by the Tax Injunction Act and principles of comity because such suits "restrain" or "enjoin" the "assessment" of tax. *ACLU v. Bridges*,

334 F.3d 416, 421-22 (5th Cir. 2003) (determining whether an individual or organization qualifies for an exemption is part of the "assessment" process and therefore a lawsuit seeking invalidation of the exemption is barred by the Tax Injunction Act); *Kraebel v. New York City Dep't of Hous. Pres. and Dev.*, 959 F.2d 395, 400 (2d Cir. 1992) (holding that the Tax Injunction Act barred taxpayer's constitutional challenge to a property tax exemption and abatement scheme); *Colonial Pipeline Co. v. Collins*, 921 F.2d 1237, 1242 (11th Cir. 1991) (rejecting the suggestion that a suit that could result in the increase in state tax collections was outside the scope of the Tax Injunction Act because the "requested relief, if granted, . . . would clearly conflict with the principle underlying the Tax Injunction Act that the federal courts should generally avoid interfering with the sensitive and peculiarly local concerns surrounding state taxation schemes"); *In re Gillis*, 836 F.2d 1001, 1005 (6th Cir. 1988) (although the court found it unnecessary to reach the Tax Injunction Act because the suit was barred by the principles of comity, it noted a suit that seeks to enhance state revenues may nonetheless fall within the Act's ban because "the Act is not, by its own language, limited to the collection of taxes"); *United States Brewers Ass'n, Inc. v. Perez*, 592 F.2d 1212, 1215 (1st Cir. 1979) ("[A]n order of a federal court requiring Commonwealth officials to collect taxes which its legislature has not seen fit to impose on its citizens strikes us as a particularly inappropriate involvement in a state's management of its fiscal operations.")

There are of course cases holding to the contrary – most notably, the decision of the Ninth Circuit below. That is presumably why this Court granted certiorari. But Respondents' suggestion that reversal of the Ninth Circuit

would run contrary to an "overwhelming body of authority and uniform practice" is without basis.[4]

IV. The Principles of Comity Bar Respondents' Federal-Court Lawsuit Challenging Arizona's Tax Credit.

Respondents attempt to narrow the principles of comity in the same way they do the Tax Injunction Act, insisting that those principles apply only when a tax law challenge "would stop a state from collecting revenue." Resp. Br. 40. But as with the Tax Injunction Act, principles of comity are far more expansive than Respondents would like. Respondents' argument ignores the crucial federalism

[4] Respondents also err in contending that judicial interpretations of the Anti-Injunction Act support the Ninth Circuit's interpretation of the Tax Injunction Act. Contrary to Respondent's suggestions, Resp. Br. 32-37, the principles supporting the Anti-Injunction Act are fully present in cases where the requested relief would *increase* federal tax collections. *See*, *e.g.*, *Louisiana v. McAdoo*, 234 U.S. 627, 632 (1914) (recognizing that action to compel a higher tariff would "disturb the whole revenue system of the government.") Moreover, most of the lower-court decisions that Respondents relied on were reversed on other grounds. *See* Resp. Br. 36 (acknowledging that two of the cases were reversed on appeal); *see also Wright v. Regan*, 656 F.2d 820 (D.C. Cir. 1981), *rev'd by Allen v. Wright*, 468 U.S. 737 (1984), on standing grounds. Finally, Respondents fail to recognize a crucial distinction between the Anti-Injunction Act and the Tax Injunction Act. In most cases brought by plaintiffs seeking to invalidate federal tax credits or exemptions conferred on other taxpayers, there is no other avenue of relief in federal court and the Anti-Injunction Act does not apply. *South Carolina v. Reagan*, 465 U.S. 367, 378 (1984) ("Congress did not intend the [Anti-Injunction] Act to apply to actions brought by aggrieved parties for whom it has not provided an alternative remedy.") By contrast, it is undisputed in this case that Respondents have an adequate remedy in state court.

underpinnings of the Court's comity decisions and the disruptive effect on state tax administration that is caused by challenges to state tax credits. In *Fair Assessment in Real Estate Association, Inc. v. McNary*, this Court noted that the principles of comity predate the Tax Injunction Act, and found that "the very maintenance of [a lawsuit] would intrude on the enforcement of the state [tax] scheme." 454 U.S. 100, 114 (1981). Thus, while revenue interference clearly falls under the scope of comity, the broader federalism purpose of that doctrine covers all matters that disrupt a state tax system, including challenges to state tax credits.

The common theme throughout this Court's decisions regarding comity is that state tax matters should be heard in state court *unless* those remedies are not "plain, adequate, and complete." *See Fair Assessment*, 454 U.S. at 116; *Great Lakes Dredge & Dock Co. v. Huffman*, 319 U.S. 293, 297 (1943); *Matthews v. Rodgers*, 284 U.S. 521, 525-26 (1932) ("the mere illegality or unconstitutionality of a state or municipal tax is not in itself a ground for equitable relief in the courts of the United States").[5] Consequently, the issue is not whether a state tax challenge will increase or decrease revenue to a State, as Respondents contend, but rather whether the state court system provides an adequate remedy for the challenger. There is no dispute that the Arizona courts clearly provide such a remedy. Resp. Br. 11

[5] In *Fair Assessment*, the Court noted that there is no significant difference between remedies that are "plain, adequate, and complete," as that phrase has been used in articulating the doctrine of equitable restraint based on notions of comity, and those that are "plain, speedy and efficient" as used in the Tax Injunction Act. *Id.* at 116 n.8.

n.7. Thus, the district court correctly dismissed the Respondents' suit under the principles of comity.

Respondents also wrongly argue that their lawsuit seeking a federal court order enjoining the state tax credit will not disrupt Arizona's tax administration. A federal-court ruling that is inconsistent with the Arizona Supreme Court's decision in *Kotterman v. Killian,* 972 P.2d 606 (Ariz.), *cert. denied*, 528 U.S. 921 (1999) and *cert. denied sub nom. Rhodes v. Killian*, 528 U.S. 810 (1999), would be highly disruptive. First, if Petitioner complies with a federal-court order enjoining him from allowing the tax credit for contributions to school tuition organizations (STOs) that contribute to religious schools, Arizona taxpayers who nevertheless contributed to such STOs could file a refund action in state court and that court must follow Arizona Supreme Court precedent. Second, Respondents are wrong that *Kotterman* did not include taxpayers who sought to use the tax credit as parties. Taxpayers who intended to take the Arizona private school tuition credit intervened in the *Kotterman* lawsuit. *See* Pet. for Writ of Cert. *Kotterman v. Killian*, 528 U.S. 921 (1999) (No. 98-1716). Therefore, allowing Respondents to pursue relief in federal court creates a very real possibility that the Arizona Department of Revenue will have to deal with inconsistent adjudications.

The relief that Respondents seek is also inherently disruptive because it could result in a court order prohibiting the State from allowing tax credits for contributions to STOs that give to religious schools, but permitting tax credits to STOs that give to non-religious schools. This relief would create new and onerous administrative burdens on the Arizona Department of Revenue to determine what type of schools the different student tuition

organizations support through their scholarship programs. This relief would also prevent the State from determining conclusively which taxpayers are eligible for the tax credit and which are not until this litigation and any appeals are ended. Respondents' assumption that a lawsuit interferes with the State's tax administration only if, in the end, the State loses revenue ignores the fact that any change in tax law affects tax administration.

Although Respondents acknowledge that the State may remedy an unconstitutional credit in a way that decreases revenues, they inexplicably claim that this does not implicate the revenue-protection purpose of the comity principle. Resp. Br. at 44-45. The parties to lawsuits challenging tax provisions cannot predict the final remedy that will be ordered by the court or adopted by the Legislature. *Cf*. *Bridges*, 334 F.3d at 421 (noting that "it is not necessarily true that declaring exemptions unconstitutional will result in the State collecting more taxes"). For example, the Arizona Legislature could, in response to a decision striking down the credit as it applies to religious schools, expand the credit by allowing student tuition organizations to distribute monies to public schools.

Because Respondents' lawsuit interferes with Arizona's assessment of state taxes and requests relief that is disruptive to Arizona's tax administration, the Court should affirm the district court's dismissal based on the principles of comity.

V. Congress and This Court Have Entrusted State Courts to Decide Federal Constitutional Issues.

The same theme permeates Respondents' brief and the briefs of their amici: regardless of the Tax Injunction Act language, the Court should construe it (as well as principles of comity) narrowly because otherwise States will be able to "effectuat[e] unconstitutional policies through tax credits," without any meaningful judicial check. Resp. Br. at 47. In their opinion, state courts cannot be trusted to correct federal constitutional violations, which will remain unremedied unless federal district court review is authorized. *See, e.g.,* Br. of Americans United for Separation of Church and State at 13-15. This argument blatantly ignores the very principles of federalism that are fundamental to the Tax Injunction Act and the principles of comity. *See Idaho v. Coeur d'Alene Tribe*, 521 U.S. 261, 275 (1997) ("A doctrine based on the inherent inadequacy of state forums would run counter to basic principles of federalism.").

By enacting the Tax Injunction Act, Congress has squarely rejected the notion that only federal district courts are capable of deciding federal constitutional issues. *See Rosewell*, 450 U.S. at 515 n.19 (noting that the Tax Injunction Act "embodied Congress' decision to transfer jurisdiction over a class of substantive federal claims from the federal district courts to the state courts, as long as state procedures were 'plain, speedy and efficient' and final review of the substantive claims could be obtained in this Court"); *Grace Brethren*, 457 U.S. at 416-17 ("Carving out a special exception for taxpayers raising First Amendment claims would undermine significantly Congress' primary purpose 'to limit drastically federal district

court jurisdiction to interfere with so important a local concern as the collection of taxes.' ") (quoting *Rosewell*, 450 U.S. at 522).

This Court has also repeatedly recognized that state courts have a constitutional obligation to uphold federal law and has expressed its confidence in their ability to do so. *Coeur d'Alene Tribe*, 521 U.S. at 275; *see also Grace Brethren*, 457 U.S. 417 n.37 (rejecting appellees' argument "to the extent that it assumes that the state courts will not protect their constitutional rights"); *Alden v. Maine*, 527 U.S. 706, 755 (1999) (Court is "unwilling to assume the States will refuse to honor the Constitution or obey the binding laws of the United States"); *Stone v. Powell*, 428 U.S. 465, 494 n.35 (1976) (same). Indeed, Arizona state judges and officers take an oath to uphold the federal constitution. Ariz. Const. art. VI, § 26 (judges); Ariz. Rev. Stat. § 38-231 (officers).

In addition, the Court has recognized that both the Tax Injunction Act and the principles of comity have safeguards that protect federal rights. *See Grace Brethren*, 457 U.S. at 415 n.31. Under the Tax Injunction Act, litigants are entitled to federal-court relief if the state court remedy is not "plain, speedy and efficient." And, under the principles of comity, litigants are entitled to seek relief in federal court if the state-court remedy is not "plain, adequate and complete." Here, Respondents have never contended that their remedy at state law was defective. Indeed, the Arizona Supreme Court took original jurisdiction in *Kotterman* to resolve the constitutional challenge to the tax credit at issue here and this Court denied review of that decision. Respondents' disagreement with the result in *Kotterman* is hardly a sufficient basis to avoid the Tax Injunction Act and principles of comity.

Finally, Respondents fail to address one of the most important safeguards in the Tax Injunction Act: this Court's review of federal issues arising out of state court proceedings. Again, there is no reason to presume that the sound judgment of state officials and review by state courts will not be sufficient to prevent the parade of horribles hypothesized by Respondents and their amici. But should that parade materialize, there is also no reason to assume that this Court will be unwilling or unable to protect federal constitutional rights. Respondents' concerns are entirely unwarranted and should not be the basis for overriding Congress's decision to prevent federal district court interference with the assessment of state taxes.

CONCLUSION

For the foregoing reasons, this Court should reverse the decision of the Court of Appeals for the Ninth Circuit and affirm the district court's dismissal of this matter.

Respectfully submitted,

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