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Nos. 09-987, 09-991

In The
Supreme Court of the United States

ARIZONA CHRISTIAN SCHOOL TUITION ORGANIZATION,

Petitioner,

v.

KATHLEEN M. WINN, et al.,

Respondents.

GALE GARRIOTT, in his official capacity as Director of the Arizona Department of Revenue,

Petitioner,

v.

KATHLEEN M. WINN, et al.,

Respondents.

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

RESPONDENTS' SUPPLEMENTAL BRIEF REGARDING A CHANGE IN STATE LAW

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RESPONDENTS' SUPPLEMENTAL BRIEF REGARDING A CHANGE IN STATE LAW

STATEMENT

This case involves an Establishment Clause challenge to the constitutionality of an Arizona statutory tuition-voucher program that was originally enacted by the Arizona Legislature in 1997. The district court dismissed respondents' (plaintiffs') complaint for failure to state a claim upon which relief could be granted. The court of appeals reversed the dismissal of the complaint and remanded the case to the district court in order to give respondents an opportunity to prove their allegations. Petitions for rehearing en banc were denied. Certiorari petitions were filed, and this Court granted review on May 24, 2010. No temporary or preliminary injunctive or other relief has been granted.

Respondents file this supplemental brief to bring to the Court's attention the fact that, after the decision below, extensive changes were made in the state legislation that is the subject of this case. The changes were made after the denial of rehearing in the court below, and after the filing of the petitions for certiorari and respondents' brief in opposition, but shortly before petitioners filed reply briefs at the petition stage. Those briefs made no mention of the new legislation, nor did the parties bring the new legislation to the Court's attention in the three weeks that elapsed between the filing of those briefs and the grant of certiorari. The Court thus granted certiorari

without knowledge that the governing state law had been substantially changed.

The legislative changes are contained in two separate bills, S.B. 1274 and H.B. 2664. They are reproduced at App. 1 – App. 17 of petitioner Garriott's brief on the merits. The bills were enacted on April 20 and 27, 2010, and signed into law by the Governor on April 27 and May 10. S.B. 1274 amends Arizona's existing tax-credit statute, codified as A.R.S. § 43-1089. S.B. 1274 became effective on July 27, 2010. H.B. 2664 adds a new chapter to Title 43 of the Arizona Revised Statutes, which deals with taxation. The new chapter imposes extensive new regulations on Arizona's school tuition organizations (STOs) – the organizations that award scholarships in the Arizona program. The new regulatory system will be enforced and administered by the Arizona Department of Revenue. H.B. 2664 will become effective on January 1, 2011. Respondents first learned of this new legislation when they received petitioners' briefs on the merits.

The new legislation is mentioned, but summarily dismissed as irrelevant, in footnotes in petitioners' merits briefs. See Pet. Garriott Br., p. 4, n. 2; Pet. Arizona Christian School Tuition Organization Br., p. 5, n. 4. See also Resp. Arizona School Choice Trust Supporting Petitioners Br., p. 3, n. 2. The new legislation, however, is not irrelevant. Petitioners have maintained, throughout this litigation, that Arizona's tax-credit program is a program of private charity that need not comply with the Establishment Clause.

Arizona's new legislation demonstrates conclusively that the program is not a program of private charity, but rather a governmental spending program that uses STOs as the state's surrogates to distribute government tax revenues for the government's educational purposes. The parties will no doubt disagree about the extent of the effect of the new legislation on the issues before the Court. The Court, however, should have been informed of the passage of the new legislation prior to granting the petitions for certiorari. This supplemental brief is filed to notify the Court of the change in Arizona legislation as promptly as possible after respondents became aware of it.

DISCUSSION

The new legislation responds to recommendations for comprehensive reform of the Arizona tax-credit program that were made to the Arizona Legislature by a legislative task force during the Legislature's 2010 session. The task force was formed in response to strong public concerns over misuse and corruption in the tax-credit program, which were revealed in lengthy investigative reports published by two major Phoenix newspapers during 2009. See Respondents' Brief in Opposition, pp. 9-12. The Department of Revenue's lack of sufficient resources and legal authority adequately to control the tax-credit program was emphasized in these articles.

The new legislation includes the following major provisions:

- **Requirement for STO Certification.** STOs will hereafter be required to apply for, and obtain, certification from the Department of Revenue in order to participate in the tax-credit program. To be certified, they must establish that their *sole* purpose is "to receive contributions from taxpayers for the purposes of income tax credits under section 43-1089," and that they "meet . . . the requirements imposed by this [new] chapter." The Department of Revenue is required to "[m]aintain a public registry of currently certified school tuition organizations," keep the registry up to date, and post the registry of certified STOs on its official web site. A.R.S. § 43-1602(A), (B), App. 9-App. 10. (All App. Cites are to the Appendix to Petitioner Garriott's Brief on the Merits.

- **When "Contributions" May Be Made to STOs.** The new legislation provides, for the first time, that taxpayers may make a "contribution" to an STO, and receive a 100%, dollar-for-dollar credit for that "contribution," when they file their tax return for the year for which they claim the credit. Taxpayers therefore no longer need to spend even a single penny of their own money to "contribute" to an STO. They simply pay their tax bill by paying part of their taxes due to the STO, and part to the Department of Revenue, at the same time. The taxpayer pays the same amount in taxes whether or

not the taxpayer "contributes" to an STO. The money "contributed" is not the taxpayer's money or the STO's money. It is the state's money. A.R.S. § 43-1089(C), App. 5.

• **Increase in the Dollar Amount of the Credit.** The amount taxpayers may take as a credit is newly linked to the consumer price index. The amount, however, may now never be reduced. A.R.S. § 43-1089(C), App. 5.

• **Regulation of STO Finances.** State law will now not only require STOs to award at least 90% of the tax revenues they receive as state-funded scholarships (the remainder of the tax revenues they receive are used to pay STO salaries and administrative costs, so that STO operations are funded entirely by the state), but will prohibit them from accumulating revenues in order to invest or reserve funds for future awards. To permit the Department of Revenue to monitor compliance with this new requirement, STOs will be required annually to report the number and amount of "contributions" they receive each year, and the number and amount of scholarships they award each year from those revenues. STOs must also report the number and amount of scholarships awarded according to the schools the students attend. In addition, STOs will be required annually to report the "names, job titles and annual salaries of the three [STO] employees who receive the highest annual salaries." A.R.S.

§ 43-1603(B)(1), App. 12; A.R.S. § 43-1604, App. 13-15.

• **Scholarship Award Standards.** Before the new legislation, STOs were free to use any standards they wished in selecting scholarship recipients. In the future, they will be required "to consider the financial need of applicants." They must annually report to the Department of Revenue (1) the "total dollar amount of educational scholarships and tuition grants awarded during the previous fiscal year to [s]tudents whose family income meets the economic eligibility requirements established under the [federal] national school lunch and child nutrition acts," and (2) the amount awarded to students whose family income falls between that amount and one hundred eighty-five percent of the federal school lunch amount. A.R.S. § 43-1603(D)(2), App. 13; A.R.S. § 43-1604(A)(7)(8), App. 14-15.

STOs will also be newly forbidden to "award, designate or reserve scholarships solely on the basis of donor recommendations"; nor may they permit taxpayers to "designate student beneficiaries as a condition of any contribution," or "facilitate, encourage or knowingly permit the exchange of beneficiary student designations." These had all been common STO practices prior to the legislative revision. A prescribed official "NOTICE" of the new restrictions must be included by the STO in any "printed materials soliciting donations, in applications for

scholarships and on [the STO's] website." A.R.S. § 43-1603(B)(3)(4), App. 12; A.R.S. § 43-1603(C), App. 12-13.

- **State Supervision and Enforcement.** These new rules are mandatory, not advisory. Compliance is to be closely monitored by the Department of Revenue, which "shall send written notice by certified mail to a school tuition organization if the department determines that the [STO] has engaged in" any prohibited activity or practice. An STO will have "ninety days to correct the violation." If the STO fails to comply within that period, the Department has power to withdraw the STO's certification and to require the STO to "offer to refund all donations received after the date of the notice of termination of certification." An STO may request an administrative hearing to review the Department's termination of its certification. If the termination of certification is sustained, that decision is subject to judicial review. A.R.S. § 43-1602(D), App. 11.

- **Audits of STO Operations.** Each STO must newly subject itself each year, at its expense, to an audit or financial review (depending upon the amount of contributions received by the STO that year). The audit or review is to be conducted by an independent licensed certified public accountant, who is required to "evaluate the organization's compliance with the fiscal requirements of this article." STOs must file signed copies of the annual audits filed with the Department of

Revenue within five days of their receipt. A.R.S. § 43-1605, App. 15-17.

The questions before the Court in this case are whether respondents' complaint states a cause of action under the Establishment Clause, and whether respondent taxpayers have standing to make that claim. Despite petitioners' and *amici*'s suggestions to the contrary, respondents' claim is not based on the contention that state voucher plans are not constitutionally permitted to pay for religious-school tuition, or that a state voucher plan is unconstitutional because a large majority of parents receiving the vouchers decide to use them at religious schools. Respondents' claim is based on their allegations that, in Arizona, most state scholarships are *awarded* to parents on the basis of religion, and that these scholarships *require* parents to send their children to religious schools. The court of appeals has held that these allegations state an Establishment Clause claim, and that taxpayers who are taxed to fund the scholarship program have standing to assert that claim.

No one, we believe, would contend that a state Department of Education, authorized by state law to award scholarships from state funds to students attending non-public schools, could constitutionally make scholarship awards that are based on the religion of student applicants, or make scholarship awards that require parents to send their children to a religious school in order to receive a scholarship. The core of respondents' case is that those

prohibitions apply to Arizona's STOs, as they would apply to the state, because those STOs do exactly what a state agency would do as part of an ordinary state-voucher plan – they award state funds, for a state purpose, pursuant to rules and procedures prescribed by the state.

The court of appeals has held that respondents' complaint states a claim that the Constitution's prohibitions on religiously based state scholarships apply to Arizona's STOs. The court based that holding on the relationship that exists between Arizona and its STOs, including the following: all of the funds that STOs award as scholarships are tax revenues (rather than private charitable contributions); the STOs award these wholly state-funded scholarships on the state's behalf, pursuant to a state statute, to serve the state's educational (rather than private charitable) purposes; STOs are the only organizations that perform this scholarship-granting function for the state; and this the only function that the STOs perform – they engage in no other charitable or non-charitable activity.

Petitioners, their *amici*, and the court of appeals judges who dissented from the denial of rehearing en banc below, disagree with the court of appeals' characterization of the relationship between Arizona and its STOs. They argue that STOs are private charitable organizations that are completely immune from Establishment Clause scrutiny. Arizona's new legislation obviously bears directly upon this core issue. By requiring STOs to be certified by the state in order

to award scholarships on the state's behalf, by giving the Department of Revenue authority to withdraw that certification, by requiring STOs to be established solely for the purpose of participating in the state's scholarship program, by subjecting STOs to extensive new state regulations of their finances and their reasons for awarding scholarships, and by clarifying that every penny of scholarship money that STOs award is tax revenue, not private charity, the new legislation strongly confirms the conclusion that the relationship between Arizona and its STOs may warrant Establishment Clause scrutiny of STO religious discrimination. Respondents will so argue in their brief on the merits, which will, of course, address the relationship between the state and its STOs under Arizona's new tax-credit system, rather than the less entangled relationship considered by the district court and the court of appeals.

Neither the court of appeals nor the district court has had an opportunity to assess the impact on this case of the changes that Arizona has made in its law, nor have respondents had the opportunity to amend their complaint to take account of those changes. Had the court been informed of these changes before acting on the petitions for certiorari, that information might have been relevant to the Court's decision whether initially to assess the impact of the changes itself, without the benefit of the consideration of that issue by the courts below, or whether to permit the case to be remanded to the district court, as the court

of appeals held, for proceedings that would address Arizona's current program.

CONCLUSION

The Court was not informed of significant changes in Arizona law that occurred prior to the decision to grant the petitions for certiorari. It may wish to consider remanding the case, which has never proceeded beyond the interlocutory stage, for further proceedings that would take account of the extensive statutory changes that have be made subsequent to the decision below.

Respectfully submitted,

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