No. 21-966

IN THE

Supreme Court of the United States

State of NEW YORK, State of CONNECTICUT,
State of MARYLAND, State of NEW JERSEY,
Petitioners,

v.

JANET YELLEN,
in her official capacity as Secretary of
the United States Department of Treasury, et al.,
Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

REPLY BRIEF FOR THE PETITIONERS

LETITIA JAMES
Attorney General
State of New York
BARBARA D. UNDERWOOD*
Solicitor General
ANISHA S. DASGUPTA
Deputy Solicitor General
ESTER MURDUKHAYEVA
Senior Assistant
Solicitor General

28 Liberty Street
New York, New York 10005
(212) 416-8020
barbara.underwood@ag.ny.gov
**Counsel of Record*

(*Additional counsel on signature pages.*)

TABLE OF CONTENTS

Page

Table of Authorities ii

Introduction 1

Argument 2

I. Certiorari Is Warranted to Resolve a Novel and Important Constitutional Question That Was Decided Incorrectly Below 2

II. Petitioners Have Standing and the Suit Is Not Barred by the Anti-Injunction Act 9

Conclusion 12

TABLE OF AUTHORITIES

Cases **Page(s)**

Department of Com. v. New York, 139 S. Ct. 2551 (2019) 2

Department of Homeland Sec. v. Regents of the Univ. of Cal., 140 S. Ct. 1891 (2020) 2

Dimond v. District of Columbia, 792 F.2d 179 (D.C. Cir. 1986) 11

Georgia v. Pennsylvania R. Co., 324 U.S. 439 (1945) 10

National Fed'n of Indep. Bus. v. Sebelius, 567 U.S. 519 (2012) 8,9

New Mexico v. Department of the Interior, 854 F.3d 1207 (10th Cir. 2017) 10

South Carolina v. Baker, 485 U.S. 505 (1988) 4

South Carolina v. Regan, 465 U.S. 367 (1984) 11

Steward Mach. Co. v. Davis, 301 U.S. 548 (1937) 8

Texas v. United States, 787 F.3d 733 (5th Cir. 2015) 10

Trump v. Hawaii, 138 S. Ct. 2392 (2018) 2

United States v. Texas, 579 U.S. 547 (2016) 2

Wyoming v. Oklahoma, 502 U.S. 437 (1992) 10

Laws & Rules

26 U.S.C.
§ 63(b) 5
§ 68(a) 6

Sup. Ct. R. 10(c) 2

Miscellaneous Authorities **Page(s)**

Alan D. Viard, *The Myth of the Limits on Itemized Deductions*, Am. Enter. Inst. (Jan. 9, 2013), https://www.aei.org/articles/the-myth-of-the-limits-on-itemized-deductions/ 6

Daniel Hemel, *Easy on the SALT: A Qualified Defense of the Deduction for State and Local Taxes* (Coase-Sandor Inst. for Law & Econ., No. 830, 2017), https://chicagounbound.uchicago.edu/cgi/viewcontent.cgi?article=2499&context=law_and_economics 6

Edwin R. A. Seligman, *The Income Tax: A Study of the History, Theory, and Practice of Income Taxation at Home and Abroad* (2d ed. 1914) 7

Jared Walczak, Tax Found., *Unpacking the State and Local Tax Toolkit: Sources of State and Local Tax Collections* (Fiscal Fact No. 550, 2017), https://files.taxfoundation.org/20170726152105/TaxFoundation-FF550.pdf 7

Kyle Pomerleau, *The Pease Limitation on Itemized Deductions Is Really a Surtax*, Tax Found. (Oct. 16, 2014), https://taxfoundation.org/pease-limitation-itemized-deductions-really-surtax/........................ 6

Tax Pol'y Ctr., *Briefing Book* (2020), https://www.taxpolicycenter.org/sites/default/files/briefing-book/tpc_briefing_book_2021.pdf 5

INTRODUCTION

Respondents do not contest the novelty or importance of the question presented here: whether Congress may interfere with the States' sovereign taxing authority by severely curtailing the longstanding deduction from federal taxable income for state and local taxes ("SALT"). Respondents' arguments against certiorari instead rest chiefly on an erroneous view of the applicable constitutional provisions and federalism principles. Respondents also rehash jurisdictional contentions that were squarely rejected below. None of these arguments is a reason to deny certiorari.

Contrary to Respondents' arguments, the long and unbroken lineage of the SALT deduction for property and income taxes reflects a constitutional mandate, not a policy choice. Respondents fail to address the extensive historical evidence supporting Petitioners' position. Instead, they point to distinguishable case law and materially different prior tax reforms. Likewise, Respondents improperly minimize the cap's impermissibly coercive effects and fail to address evidence showing that the purpose of the cap was to pressure politically disfavored States into changing their taxation and spending policies.

Respondents also incorrectly argue that jurisdictional barriers make this case a poor vehicle for review of the question presented. As the court of appeals correctly found, Petitioners asserted sufficient injury-in-fact based on the loss of a specific stream of tax revenue from the SALT deduction cap, namely tens of millions of dollars of real estate transfer taxes. Petitioners identified further bases for standing that the courts below did not address. The court of appeals also

correctly determined the Anti-Injunction Act ("AIA") does not bar this suit because Petitioners have no other mechanism to assert their constitutional claims and suits by individual taxpayers would not sufficiently vindicate the States' sovereign injuries.

ARGUMENT

I. Certiorari Is Warranted to Resolve a Novel and Important Constitutional Question That Was Decided Incorrectly Below.

1. This case presents a novel constitutional question that is of paramount importance to Petitioners. See Pet. 13-16. Respondents do not challenge the novelty or importance of this case. At most, Respondents note that the court of appeals' decision is the only appellate decision addressing the question presented. *See* Br. in Opp. ("Opp.") 19, 21. But this Court's rules do not require the existence of a circuit split to grant certiorari, Sup. Ct. R. 10(c), and this Court frequently reviews cases in the absence of circuit conflict where the decisions below raise novel and important questions of federal law, *see, e.g.*, *Department of Homeland Sec. v. Regents of the Univ. of Cal.*, 140 S. Ct. 1891 (2020); *Department of Com. v. New York*, 139 S. Ct. 2551 (2019); *Trump v. Hawaii*, 138 S. Ct. 2392 (2018); *United States v. Texas*, 579 U.S. 547 (2016).

Here too, the novelty and importance of the question presented warrant this Court's review. The question presented has never been litigated precisely because Congress has never before curtailed the SALT deduction with the purpose and effect of constraining the States' ability to make sovereign decisions regarding taxation and spending. And because the SALT deduction cap imposes harms on Petitioners every year that

it is in effect, the States should not be required to wait for a circuit split to ripen.

2. Respondents are equally incorrect in contending that the federal income taxing power is absolute and, therefore, that a SALT deduction in any form is a matter of congressional grace rather than a constitutional requirement. *See* Opp. 10-12.

a. Congress's taxing authority (as set forth in Article I, Section 8 and the Sixteenth Amendment) is cabined by the structural requirements of federalism, which prevent the federal government from directly interfering with the States' ability to generate revenue to sustain their operations. The long history of federal income taxation demonstrates that Congress and the States equally understood that a deduction for all or nearly all state and local property and income taxes was constitutionally required to preserve state sovereign taxing authority. See Pet. 4-8, 16-19.

The SALT deduction cap increases the cost of state taxes and therefore impairs the States' ability to maintain their current tax rates or increase them in the future to generate revenue for important public programs. Each of the Petitioner States has already felt compelled to enact legislative changes in response to the cap, a fact that underscores the cap's direct interference with the States' sovereign discretion. (*See* CA2 J.A. 16, 49-51, 57-58.)

Respondents mischaracterize Petitioners as advancing a broad principle of "no-overlapping-taxation." *See* Opp. 18. Congress and the States may, of course, tax the same moneys. What the Constitution prohibits Congress from doing is inflating the cost of state and local property and income taxes to a degree that impedes the States from levying those taxes, which

have historically represented a key portion of state revenues. The SALT deduction is not an "indirect federal subsidy" to the States (*id.* (emphasis and quotation marks omitted)) but a mechanism essential to the collection of federal income tax in a constitutional manner.

b. Contrary to Respondents' argument (*id.* at 11-12; *see also* Pet. App. 21a), this Court's decision in *South Carolina v. Baker*, 485 U.S. 505 (1988), does not foreclose Petitioners' challenge.

As Petitioners previously explained (Pet. 19), *Baker* involved a law of general applicability that eliminated the tax-exempt status of interest earned on all unregistered bonds, including but not limited to state-issued bonds, 485 U.S. at 510-11, 526-27. This Court made clear that "States have no constitutional entitlement to issue bonds paying lower interest rates *than other issuers*," *id.* at 525 (emphasis added), and noted that the challenged statute does not "discriminate against States," *id.* at 526. By contrast, the SALT deduction cap targets only state and local property and income taxes, which cannot be levied by other parties, and as described in more detail below (at 7-9), the cap was enacted with discriminatory intent and is accompanied by discriminatory effects. Finally, the tax law at issue in *Baker* had a "*de minimis*" effect on the States' ability to raise revenue, *see id.* at 529 (Rehnquist, C.J., concurring in judgment), unlike the SALT deduction cap which has a substantial effect on many States including Petitioners.

c. Respondents also overstate the significance of past tax modifications that had a minimal effect on the SALT deduction. *See* Opp. 13-15. None of these modifications affect state sovereignty in a manner that is comparable to the SALT deduction cap.

Respondents claim, for example, that the introduction of the standard deduction in 1944 eliminated the SALT deduction for taxpayers who do not itemize their deductions. *Id.* at 13. But the standard deduction effectively provides a deduction for SALT because taxpayers generally elect a standard deduction only if their total itemized deduction (including the deduction for SALT payments) is less than the value of the standard deduction. *See* 26 U.S.C. § 63(b). And because the standard deduction is elective, a taxpayer always has the option of itemizing and claiming the SALT deduction.

Respondents also exaggerate the extent to which the alternative minimum tax ("AMT") reduces the value of the SALT deduction to taxpayers. *See* Opp. 14. First, the number of taxpayers subject to the AMT is relatively small.[1] Second, for at least some taxpayers who pay the AMT, the removal of the full SALT deduction from the normal tax scheme could increase their ultimate tax liability even though the AMT does not itself allow a deduction for SALT.

Specifically, the AMT requires qualifying taxpayers (usually high-income earners) to calculate their liability under ordinary tax rules, which permit a deduction for SALT from taxable income, and also under the AMT rules, which do not allow a SALT deduction from taxable income. The taxpayer must then pay the higher amount of liability.[2] For some taxpayers (namely those paying a substantial amount of state and local property

---

[1] *See* Tax Pol'y Ctr., *Briefing Book* p. 204 (2020) (internet) (estimating that only three percent of taxpayers paid the AMT in 2017). (For authorities available on the internet, full URLs appear in the Table of Authorities. All URLs were last visited on March 23, 2022.)

[2] *See* Tax Pol'y Ctr., *Briefing Book*, *supra*, at p. 200.

and income taxes), the availability of a full SALT deduction reduces their taxable income and may result in a tax liability under ordinary rules that falls below the AMT amount, requiring those taxpayers to pay the AMT. In the absence of a full SALT deduction, those same taxpayers would have had higher taxable income and may therefore have a tax liability under ordinary rules that exceeds the AMT liability. For taxpayers in this position, the AMT owed in the first scenario could be lower than the ordinary tax liability owed in the second scenario.[3]

As Respondents acknowledge (*id.*), the so-called Pease Limitation (which is suspended through the 2025 tax year) applied only to taxpayers above certain adjusted gross income ("AGI") thresholds, *see* 26 U.S.C. § 68(a). For these taxpayers, the total of certain itemized deductions was reduced by three percent of the amount of AGI exceeding the threshold, up to eighty percent of the amount of all itemized deductions. *See id.* § 68(a)(1)-(2). Because the Pease Limitation was pegged to AGI, rather than the value of itemized deductions, tax experts recognized that it had no material effect on the marginal benefit of a deduction, including the SALT deduction.[4]

Finally, Respondents discuss at length the fact that Congress removed sales taxes from the SALT deduction

---

[3] For a mathematical illustration of this hypothetical, see Daniel Hemel, *Easy on the SALT: A Qualified Defense of the Deduction for State and Local Taxes* 6 & n.27 (Coase-Sandor Inst. for Law & Econ., No. 830, 2017) (internet).

[4] *See* Kyle Pomerleau, *The Pease Limitation on Itemized Deductions Is Really a Surtax*, Tax Found. (Oct. 16, 2014) (internet); Alan D. Viard, *The Myth of the Limits on Itemized Deductions*, Am. Enter. Inst. (Jan. 9, 2013) (internet).

in 1986, and only partially restored the availability of the deduction for sales taxes in 2004. Opp. 14-15. Unlike sales taxes, income and property taxes have a unique historical and legal pedigree because they have been imposed since before the formation of the union.[5] Although Respondents note that in 2014 some States derived more revenue from sales tax than from property or income tax (*id.* at 15), such recent developments cannot alter the special status historically given to state property and income taxes.[6]

In short, capping the SALT deduction for property and income taxes raises the cost of state taxes and erodes a structural protection that was put in place to protect the States' ability to generate revenue. In likening the cap to prior tax reforms, Respondents ignore constitutionally significant distinctions between materially different measures.

3. Similarly, Respondents erroneously disregard Congress's deliberate intent to target Petitioner States, and they inaccurately minimize the economically coercive effect of the SALT deduction cap.

The Tenth Amendment's prohibitions on coercion apply when the federal government impedes States

---

[5] *See* Edwin R. A. Seligman, *The Income Tax: A Study of the History, Theory, and Practice of Income Taxation at Home and Abroad* 388-406 (2d ed. 1914) (describing history of income and property taxes levied by the colonies and by the States prior to the Civil War). (*See also* CA2 J.A. 22-24.)

[6] In any event, even the source cited by Respondents demonstrates that property and income taxes represent between 66.9% and 72.4% of total tax revenues for Petitioner States. *See* Jared Walczak, Tax Found., *Unpacking the State and Local Tax Toolkit: Sources of State and Local Tax Collections* 3 (Fiscal Fact No. 550, 2017) (internet).

from pursuing their own policies by attaching crushing financial penalties to sovereign actions. *See National Fed'n of Indep. Bus. v. Sebelius* (*NFIB*), 567 U.S. 519, 576-78 (2012) (op. of Roberts, C.J.); *see also Steward Mach. Co. v. Davis*, 301 U.S. 548, 589-90 (1937). Respondents do not deny that contemporaneous statements from legislators and from officials tasked with enforcing the SALT deduction cap make Congress's goal abundantly clear: to compel Petitioners to reduce taxes and investments in schools, hospitals, and infrastructure or else face a significant financial penalty. See Pet. 20-21. Respondents do not address these statements at all, in essence conceding that Congress deliberately targeted Petitioners and similarly situated States when enacting the cap.

Instead, Respondents erroneously assert that the cap merely "alters the financial consequences of a variety of economic activities and choices" and does not impose coercive effects that would violate the Tenth Amendment. *See* Opp. 20-21. First, Respondents miss the mark in arguing that because the 2017 tax amendments containing the SALT deduction cap "decreased Americans' tax liability in the aggregate," Petitioners cannot be "impermissibly pressured by a drastic increase in their residents' federal tax obligations" (*id.* at 20). The effect of the omnibus 2017 legislation on the average national tax burden is irrelevant to whether the SALT deduction cap creates substantial additional tax burdens in the Petitioner States—which it concededly does. *See id.* (acknowledging that cap "may increase the federal tax liability of certain individuals who reside in the petitioner States").

Second, Respondents incorrectly contend that Petitioners cannot assert coercion based on "costs imposed on a State's residents." *See id.* No authority

suggests that Congress can overcome the Tenth Amendment's prohibition on coercion by imposing crushing penalties on a State's residents rather directly than on the state governments representing those residents—penalties that could be lessened by changes in state policy. Either form of penalty can constitute an impermissible effort to coerce a State to alter its sovereign taxation or public spending policies. *Cf. NFIB*, 567 U.S. at 578 (op. of Roberts, C.J.).

Finally, Respondents argue that the economic harms identified by Petitioners, including billions of dollars in increased tax burdens, decreases in billions of dollars in home equity values and in-state spending, tens of thousands of lost jobs, and decreases in hundreds of millions of dollars in real estate transfer taxes, are too minimal to establish coercion. *See* Opp. 20-21. As explained in the petition (at 21), this Court has never identified a constitutional minimum sufficient to establish coercion, and the aggregate penalties imposed by the SALT deduction cap constitute impermissible compulsion under the governing standard. *See NFIB*, 567 U.S. at 577 (op. of Roberts, C.J.).

II. Petitioners Have Standing and the Suit Is Not Barred by the Anti-Injunction Act.

The court of appeals' decision is a final judgment on the merits of Petitioners' claims, and therefore this petition is an ideal vehicle to resolve the important constitutional question presented. Respondents' assertions regarding purported defects in standing and justiciability rely on arguments that were squarely and properly rejected below. Pet. App. 8a-16a, 39a-50a.

1. Respondents acknowledge (Opp. 22) that States may assert standing based on "a direct injury in the

form of a loss of specific tax revenues" that are "demonstrably affected by" challenged legislation, *Wyoming v. Oklahoma*, 502 U.S. 437, 448, 450 (1992). Petitioners identified such an injury by pointing to "specific losses in tax revenue derived from property and real estate transfer taxes" which are caused by the depressive effect of the SALT deduction cap on home purchase rates. Pet. App. 10a.

Moreover, Petitioners established the causal connection through unrebutted declarations from tax and budgetary experts who explained that the predictable effect of the SALT deduction cap will be a decrease in home purchases in Petitioner States, which will directly produce a decline in real estate transfer tax revenues. The record evidence thus readily contravenes Respondents' contention that a decline in transfer tax revenues is "attenuated and speculative" or is merely "an incidental result" of the challenged conduct. *See* Opp. 22 (quotation marks omitted).

Petitioners also identified additional bases for standing that the courts below did not address, including injuries to state sovereignty stemming from the cap's coercive effects and from Congress's impermissible targeting of certain States for unequal treatment under the federal tax code. (*See* Pet. App. 41a.) These injuries are independently sufficient to establish Petitioners' standing. *See Georgia v. Pennsylvania R. Co.*, 324 U.S. 439, 451 (1945) (State had standing where the allegations, if true, "relegate[] [the plaintiff State] to an inferior economic position among her sister States"); *Texas v. United States*, 787 F.3d 733, 749 (5th Cir. 2015) ("[B]eing pressured to change state law constitutes an injury."); *New Mexico v. Department of the Interior*, 854 F.3d 1207, 1218 (10th Cir. 2017) (same).

2. Respondents' contention that the Anti-Injunction Act ("AIA") bars this action (Opp. 23-24) rests on an erroneous view of *South Carolina v. Regan*, in which this Court held that the AIA bars an injunctive suit "only in situations in which Congress had provided the aggrieved party with an alternative legal avenue by which to contest the legality of a particular tax," 465 U.S. 367, 373 (1984). As the court of appeals properly concluded, "the AIA was never intended to leave a party without *any* forum in which to assert its tax claims." Pet. App. 13a.

Respondents mischaracterize *Regan* as creating a "narrow, case-specific exception" that applies only where it is certain that individual taxpayers would have neither the incentive nor the ability to challenge a particular tax law. *See* Opp. 23. To the contrary, *Regan* squarely holds that the available alternate avenue must allow "an aggrieved party to litigate its claims *on its own behalf*." 465 U.S. at 381 (emphasis added). "Congress did not intend the [AIA] to apply where an aggrieved party would be required to depend on the mere possibility of persuading a third party to assert his claims." *Id.*

Accordingly, the existence of a pending taxpayer suit challenging the SALT deduction cap has no bearing on the applicability of the AIA, contrary to Respondents' arguments. *See* Opp. 23-24. Although private parties can raise federalism-based arguments in challenging legislation, private parties have different incentives and objectives from those of governmental entities that are "charged by law with representing the public interest of [their] citizens." *See Dimond v. District of Columbia*, 792 F.2d 179, 192 (D.C. Cir. 1986). The AIA does not compel Petitioners to delegate the defense of their distinct sovereign interests to private parties.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

LETITIA JAMES
Attorney General
State of New York
BARBARA D. UNDERWOOD*
Solicitor General
ANISHA S. DASGUPTA
Deputy Solicitor General
ESTER MURDUKHAYEVA
Senior Assistant
Solicitor General
barbara.underwood@ag.ny.gov

March 2022 * *Counsel of Record*

(*Counsel listing continues on next page.*)

WILLIAM TONG
Attorney General
State of Connecticut
CLARE KINDALL
Solicitor General
55 Elm Street
Hartford, CT 06106

BRIAN E. FROSH
Attorney General
State of Maryland
STEVEN M. SULLIVAN
Solicitor General
200 St. Paul Place
Baltimore, MD 21202

MATTHEW J. PLATKIN
Acting Attorney General
State of New Jersey
JEREMY FEIGENBAUM
State Solicitor
25 Market Street
Trenton, NJ 08625