PACIFIC LEGAL FOUNDATION

August 1, 2018

Ms. Molly C. Dwyer
Clerk of Court
United States Court of Appeals
For the Ninth Circuit
1010 Fifth Avenue
Seattle, WA 98104

Re: *Jerry and Kathy Armstrong & Association of Christian Schools International v. Gene Walborn*, Case No. 16-35422

Dear Ms. Dwyer:

This case is about whether the Montana Department of Revenue can deny privately funded scholarship assistance to students who want to attend private religious schools.

This Court has asked the parties to brief whether the Tax Injunction Act (TIA) bars the claims asserted by the Association of Christian Schools International (ACSI). No. 16-35422, Memorandum (July 19, 2018). The TIA does not strip the federal courts of jurisdiction over ACSI's claims because ACSI is not a taxpayer challenging its own tax liability, and its request for relief does not ask a federal court to restrain the levy, assessment, or collection of state taxes.

BACKGROUND

Montana's scholarship tax credit program allows Montana taxpayers to receive a modest tax credit if they donate to state-approved scholarship organizations. *See* Mont. Code Ann. § 15-30-3103. Those scholarship organizations are then tasked with distributing the scholarship funds to help students afford private-school tuition. *See* Mont. Code Ann. § 15-30-3104. The Montana Department of Revenue promulgated an administrative rule that forbids students from using those scholarship funds to attend religious schools. *See* Mont. Admin. R. 42.4.802.

Jerry and Kathy Armstrong and ACSI sued the Department in federal district court, claiming that the Department's rule violated the First and Fourteenth Amendments to the United States Constitution and Montana's Administrative Procedure Act. *See Armstrong v. Kadas*, Case No. 6-15-cv-114-SEH, First Amended Complaint (Feb. 12, 2016). The federal district court dismissed the case on abstention grounds due to parallel state litigation. *See id.*, Order (Apr. 20, 2016). On appeal, this Court upheld dismissal of the Armstrongs' claims on a separate ground—a jurisdictional bar imposed by the TIA. *Armstrong v. Kadas*, No. 16-

35422, Memorandum (July 19, 2018). The Court has retained jurisdiction to consider whether ACSI's constitutional claims are likewise barred by the TIA. *Id*. at 4 n.3.

ARGUMENT

The TIA does not apply to nontaxpayer claims that do not ask for relief that directly restrains taxation, even if the relief requested might have a negative impact on state tax administration. *Direct Marketing Ass'n v. Brohl*, 135 S. Ct. 1124, 1132-33 (2015) (The TIA did not apply to a suit brought by nontaxpayers that threatened to have an indirect but significant impact on state sales tax collection.). ACSI is not a Montana taxpayer asking a federal court to rule on an issue related to its own tax liability. Rather, ACSI's request for relief only relates to the allocation of privately donated scholarship funds for which donors can receive a tax credit. ACSI's claims would only affect how funds are distributed after they have already been donated to student scholarship organizations. The TIA therefore does not apply.

The TIA states, in relevant part, "The district courts shall not enjoin, suspend, or restrain the assessment, levy, or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State." 28 U.S.C. § 1341. The law has two objectives, both designed to protect state revenue:

(1) ensure equal treatment of out-of-state taxpayers seeking relief in federal court and resident taxpayers with access only to state court; and (2) prevent taxpayers, through resort to a federal injunction, from "withholding large sums" of tax revenue from the state and "thereby disrupting state government finances." *Hibbs v. Winn*, 542 U.S. 88, 104 (2004).

The Supreme Court has consistently maintained a narrow reading of the TIA that focuses on direct attempts by a taxpayer to prevent payment of a tax. The TIA concerns itself with three "discrete phases of the taxation process": assessment, levy, and collection. *Brohl*, 135 S. Ct. at 1129; 28 U.S.C. § 1341. In resolving any TIA issue, a court must determine whether the action that the plaintiff seeks to enjoin, suspend, or restrain is an act of "assessment, levy, or collection." *Brohl*, 135 S. Ct. at 1129. "Assessment" refers to the official calculation of tax owed. *Id*. at 1130. It is an "official action taken based on information already reported to the taxing authority." *Id*. "Levy" means, in its broadest sense, "an official government action imposing, determining the amount of, or securing payment on a tax." *Id*. And "collection" is the actual act of obtaining taxes owed. *Id*. Importantly, the TIA only

protects these specific phases of tax administration and does not extend "to all activities that may improve a State's ability to assess and collect taxes." *Id*. at 1131.

A federal court lacks jurisdiction over claims that seek to "enjoin, suspend, or restrain" one of the specific steps outlined above. 28 U.S.C. § 1341. Each of these verbs refers to "equitable remedies that restrict or stop official action." *Brohl*, 135 S. Ct. at 1132. The TIA only forbids an order from a federal court that directly interferes with "assessment, levy, or collection." *Id*. This narrow reading fits Congress's intent to target only direct interference with state finances through a court's equitable powers: "Congress trained its attention on taxpayers who sought to avoid paying their tax bill by pursuing a challenge route other than the one specified by the taxing authority." *Hibbs*, 542 U.S. at 104-05.

Two key principles distilled from the TIA's text apply to this dispute: (1) the TIA does not bar claims brought by third parties who do not challenge their own tax liability; and (2) the TIA does not bar claims that only incidentally inhibit state tax administration.

As to the first principle, the Supreme Court has declined to apply the TIA to claimants who do not contest their own state tax liability. The TIA does not bar

federal jurisdiction over claims brought by "outsiders to the tax expenditure . . . whose own tax liability [is] not a relevant factor." *Levin v. Commerce Energy, Inc.*, 560 U.S. 413 (2010). In *Hibbs v. Winn*, the Supreme Court held that federal courts enjoyed jurisdiction over a constitutional challenge to a state tax-credit program. *Hibbs*, 542 U.S. at 92. Specifically, an Arizona law offered a maximum $500 tax credit for donations to scholarship tuition organizations that then issued scholarships to private-school students from the donor funds. *Id*. at 95. Arizona taxpayers challenged the tax-credit program in federal court as a violation of the Establishment Clause. *Id*. at 94. The Court held that the TIA did not bar the claim. *Id*. at 92. The TIA simply had no bearing on a claim that "was essentially an attack on the allocation of state resources for allegedly unconstitutional purposes." *Levin*, 560 U.S. at 430 (describing *Hibbs*).

Second, the TIA does not apply to "every suit that would have a negative impact on States' revenues." *Brohl*, 135 S. Ct. at 1133. For example, in *Direct Marketing Association v. Brohl*, the Supreme Court addressed whether the TIA barred a lawsuit brought by online retailers who challenged a Colorado law that required the retailers to notify consumers of their responsibility to pay a sales tax on

their online purchases and provide a report regarding online sales to Colorado taxpayers. *Id*. at 1128. The Court recognized that enjoining the notice and reporting requirements would entail significant losses in sales-tax revenue to the state, but the Court nonetheless held that the TIA did not apply because the claim for relief would not "restrain" tax assessment, levy, or collection. *Id*. at 1133. The Court concluded: "a suit cannot be understood to 'restrain' the 'assessment, levy or collection' of a state tax if it merely inhibits those activities." *Id*.

ACSI's constitutional claims do not seek to enjoin, suspend, or restrain Montana's assessment, levy, or collection of state taxes. ACSI does not seek to avoid its own tax liability, and the amount it would pay in state taxes would be the same regardless of whether the Department's rule is enjoined or not. Rather, ACSI seeks to enjoin an agency rule regarding the allocation of privately donated scholarship funds after those funds have passed through the state taxation process. The Montana Department of Revenue's administrative rule states that religious schools are not among the qualified education providers whose students can receive scholarship funds. *See* Mont. Admin. R. 42.4.802. ACSI hopes to enjoin that rule so that students

attending religious schools can apply for and receive scholarship assistance, just like students attending private secular schools.

The Department's discriminatory rule does not fit within the discrete phases of tax administration that the TIA addresses—assessment, levy, or collection. The rule is not part of calculating taxes owed under the phase of "assessment." Certainly, determining whether a taxpayer is eligible for a scholarship tax credit is part of calculating and assessing tax liability. But ACSI's request for relief does not challenge that process. Rather, ACSI only seeks relief with respect to how private donations eligible for a tax credit are allocated. If ACSI was granted relief tomorrow, the Department of Revenue's ability to grant or withhold a tax credit and calculate tax liability would be the same as it is today.

Nor does ACSI's claim "restrain" the levy or collection process. Even if the record indicated that more taxpayers might opt for a tax credit if their donations could go to students at religious schools, such an impact on revenue through increased use of the tax credit is purely incidental and expressly allowed by the state legislature. As *Brohl* held, relief that merely inhibits a state's ability to collect revenue does not "restrain" state tax administration in the manner prohibited by the

TIA. *Brohl*, 135 S. Ct. at 1133. Here, any speculation regarding how many taxpayers might or might not opt for a tax credit in the absence of the Department's rule does not affect the TIA analysis, because ACSI does not seek to "restrain" collection. ACSI's request for relief would only affect how funds are distributed after they have been donated by taxpayers. Such relief would not restrain Montana in approving or denying the tax credits that donors can receive because ACSI's relief only relates to the donated funds' destination after the donation has occurred.

Just like the claimants in *Hibbs*, ACSI is not a taxpayer and does not seek to restrain state tax administration in any manner. *Hibbs*, 542 U.S. at 93 ("Plaintiff-respondents do not contest their own tax liability. Nor do they seek to impede Arizona's receipt of tax revenues. Their suit, we hold, is not the kind § 1341 proscribes."). Like in *Hibbs*, ACSI's claim for relief is "essentially an attack on the allocation of state resources for allegedly unconstitutional purposes." *Levin*, 560 U.S. at 430. Instead, ACSI attacks restrictions on how private scholarship donations are distributed after any scholarship donors have sought and received any tax credit.

CONCLUSION

ACSI is not a taxpayer seeking to avoid liability, and ACSI's claims do not seek to restrain Montana in assessing, levying, and collecting state taxes. ACSI only asks that scholarship organizations be allowed to distribute privately donated scholarship money among students attending both secular and religious schools. A court order enjoining the Department's discriminatory rule only affects the fate of funds that have already passed through the taxation process. The TIA therefore does not bar ACSI's claims.

Respectfully submitted,

JOSHUA P. THOMPSON
ETHAN W. BLEVINS
WENCONG FA

Pacific Legal Foundation

By s/ Ethan W. Blevins
ETHAN W. BLEVINS

Attorneys for Plaintiffs-Appellants

9th Circuit Case Number(s) 16-35422

NOTE: To secure your input, you should print the filled-in form to PDF (File > Print > *PDF Printer/Creator*).

****

CERTIFICATE OF SERVICE
When All Case Participants are Registered for the Appellate CM/ECF System

I hereby certify that I electronically filed the foregoing with the Clerk of the Court for the United States Court of Appeals for the Ninth Circuit by using the appellate CM/ECF system on (date) Aug 1, 2018 .

I certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the appellate CM/ECF system.

Signature (use "s/" format) s/ Ethan W. Blevins

****

CERTIFICATE OF SERVICE
When Not All Case Participants are Registered for the Appellate CM/ECF System

I hereby certify that I electronically filed the foregoing with the Clerk of the Court for the United States Court of Appeals for the Ninth Circuit by using the appellate CM/ECF system on (date) .

Participants in the case who are registered CM/ECF users will be served by the appellate CM/ECF system.

I further certify that some of the participants in the case are not registered CM/ECF users. I have mailed the foregoing document by First-Class Mail, postage prepaid, or have dispatched it to a third party commercial carrier for delivery within 3 calendar days to the following non-CM/ECF participants:

Signature (use "s/" format)