UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF TEXAS AMARILLO DIVISION

STATE OF TEXAS, STATE OF MISSISSIPPI, STATE OF LOUISIANA,

Plaintiffs,

v.

JANET YELLEN, in her official capacity as Secretary of the Treasury; RICHARD K. DELMAR, in his official capacity as acting inspector general of the Department of Treasury; UNITED STATES DEPARTMENT OF THE TREASURY; and the UNITED STATES OF AMERICA,

Defendants.

CIVIL ACTION NO: 2:21-cv-0079-Z

NEW CIVIL LIBERTIES ALLIANCE BRIEF *AMICUS CURIAE* IN SUPPORT OF PLAINTIFF STATES

MARGARET A. LITTLE, N.D. Tex. Bar No. 303494CT
SHENG LI
MARK CHENOWETH
NEW CIVIL LIBERTIES ALLIANCE
1225 19th St. NW, Suite 450
Washington, DC 20036
(202) 869-5210

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CORPORATE DISCLOSURE STATEMENT

New Civil Liberties Alliance is a nonprofit organization under the laws of the District of Columbia. It has no parent corporation, and no publicly held corporation owns 10 percent or more of its stock.

TABLE OF CONTENTS

CORPORATE DISCLOSURE STATEMENT i
TABLE OF CONTENTS ii
TABLE OF AUTHORITIES iii
STATEMENT OF INTEREST 1
INTRODUCTION 2
BACKGROUND 3
ARGUMENT 4
I. CONGRESS CANNOT PURCHASE STATES' SOVEREIGN POWER OF TAXATION 4
A. The Tax Cut Ban Commandeers State Officials 4
B. Federal Direction of State Policy Is a Structural Violation 4
C. Commandeering Infringes Americans' Right of Self-Government in the States 9
D. Courts Have a Duty to Follow the Law, Including the Constitution, and Cannot Leave the States to the "Political Safeguards of Federalism" 11
II. THE TAX CUT BAN'S AMBIGUITY GIVES RISE TO TWO DIFFERENT BUT INTERRELATED CONSTITUTIONAL DEFECTS 12
A. The Tax Cut Ban Is Irredeemably Ambiguous 12
B. ARPA Must Be Construed Using the Constitutional Clear Statement Rule 16
III. THE NONDELEGATION DOCTRINE PROHIBITS TREASURY FROM CLARIFYING THE TAX CUT BAN THROUGH REGULATION 18
CONCLUSION 23

TABLE OF AUTHORITIES

Cases

A.L.A. Schechter Poultry Corp. v. United States,
295 U.S. 495 (1935) 20

Arlington Cent. Sch. Dist. Bd. of Educ. v. Murphy,
548 U.S. 291 (2006) 15, 16

Bennett v. Kentucky Department of Education,
470 U.S. 656 (1985) 19

Bond v. United States,
564 U.S. 211 (2011) 11

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510 U.S. 332 (1994) 12

Dep't of Revenue of State of Wash. v. Ass'n of Wash. Stevedoring Cos.,
435 U.S. 734 (1978) 10

FCC v. Fox TV Stations, Inc.,
556 U.S. 502 (2009) 21

FDA v. Brown & Williamson,
529 U.S. 120 (2000) 22

Gibbons v. Ogden,
22 U.S. (9 Wheat.) 1 (1824) 12

Grayned v. City of Rockford,
408 U. S. 104 (1972) 20

Gregory v. Ashcroft,
501 U.S. 452 (1991) 16

Gundy v. United States,
139 S. Ct. 2116 (2019) 20

Heckler v. Chaney,
470 U.S. 821 (1985) 22

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448 U.S. 607 (1980) 20

Int'l Union v. OSHA,
938 F.2d 1310 (D.C. Cir. 1991) 20

Jones v. Rath Packing Co.,
430 U.S. 519 (1977) 16

Kentucky v. Yellen,
--- F. Supp. 3d ---, 2021 WL 4394249 (E.D. Ky. Sept. 24, 2021) 6, 9

Marbury v. Madison,
5 U.S. 137(1803) 12

McCollough v. Maryland,
17 U.S. 316 (1819) 7

Murphy v. NCAA,
138 S. Ct. 1461 (2018). 4, 7

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567 U.S. 519 (2012). ..... *passim*

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--- F. Supp. 3d ---, 2021 WL 1903908 (S.D. Ohio May 12, 2021) 18, 20

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--- F. Supp. 3d ---, 2021 WL 2712220 (S.D. Ohio July 1, 2021) ..... *passim*

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451 U.S. 1 (1981) 4, 16

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521 U.S. 898, 921 (1997). ..... *passim*

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329 U.S. 69 (1946) 10

School Dist. of City of Pontiac v. Secretary of U.S. Dep't of Educ.,
584 F.3d 253, 268 (6th Cir. 2009) 16

South Dakota v. Dole,
483 U.S. 203 (1987) 12, 15

Texas Educ. Agency v. United States Dep't of Educ.,
992 F.3d 350 (5th Cir. 2021) 19

Union Pac. R. Co. v. Peniston,
85 U.S. (18 Wall.) 5 (1873) 15, 17

United States v. Butler,
297 U.S. 1 (1936) 8

Va. Dep't of Educ. v. Riley,
106 F.3d 559 (1994) (en banc) (per curiam) 19, 21

Whitman v. Am. Trucking Assocs.,
531 U.S. 457 (2001) 19, 21

Younger v. Harris,
401 U.S. 37 (1971) 12

Statutes

18 U.S.C. § 287 9

42 U.S.C. § 802. ..... *Passim*

Rules

31 C.F.R. § 35.8 3

31 C.F.R. § 35.10 3

86 Fed. Reg. 26,786 (May 17, 2021) ..... *passim*

Constitutional Provisions

U.S. Const. amend. XVI 10

U.S. Const. Art. I, § 8 ..... 4, 10

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No. 1:21-cv-00181-DRC, Dkt #29 (Apr. 16, 2021) 15

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No. 2:21-cv-00514-SMB, Dkt. #1, ¶ 3 (Mar. 25, 2021),
available at https://tinyurl.com/rwp8jeks 14

Hearing on CARES Act Quarterly Report,
Sen. Banking, Hous. & Urb. Affairs Comm (Mar. 24, 2021) 14

Laura Davison,
Treasury Clears States to Cut Taxes—But Not With Stimulus,
BLOOMBERG (Mar. 18, 2021), *available at* https://tinyurl.com/2s5eb6fv 13

Letter from Janet L. Yellen to 21 State Attorneys General (Mar. 23, 2021),
available at https://tinyurl.com/tsn9t9a7 13

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A Last-Minute Add to Stimulus Bill Could Restrict State Tax Cuts,
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https://www.nytimes.com/2021/03/12/us/politics/biden-stimulus-state-tax-cuts.html. 14

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available at https://www.merriam-webster.com/dictionary/offset. 13

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PHILIP HAMBURGER,
PURCHASING SUBMISSION: CONDITIONS, POWER AND FREEDOM (2021) 11, 23

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1:21-cv-00181-DRC, Dkt. #30, *available at* https://tinyurl.com/2wwfjz3r 14

Toby Eckert,
Yellen: Treasury Faces 'Thorny Questions' About Restrictions On State Tax Cuts,
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What to Know About All Three Rounds of Coronavirus Stimulus Checks,
available at https://tinyurl.com/t9xj8mwv (Mar. 15, 2021) 18

White House,
Path Out of the Pandemic, *available at* https://www.whitehouse.gov/covidplan/ 15

STATEMENT OF INTEREST

The New Civil Liberties Alliance ("NCLA") is a nonpartisan, nonprofit civil-rights organization founded by Philip Hamburger to defend constitutional freedoms against unlawful exercises of administrative power and conditions imposed on spending as another means of legislating outside proper constitutional channels.[1] NCLA challenges constitutional defects in the modern American legal framework by bringing original litigation, defending Americans from unconstitutional actions, filing *amicus curiae* briefs, and petitioning for a redress of grievances in other ways. Although Americans still enjoy the shell of our Republic, a very different sort of government has developed within it—a type, in fact, that our Constitution was designed to prevent.

Congress's practice of imposing "conditions" on federal spending is particularly disturbing. Far too often, Congress attaches conditions on the receipt of federal funds, thereby defeating state constitutional guarantees. This case goes even further and constitutes a historically unprecedented usurpation of core power exclusively assigned to the States—the power to change or reduce the taxation of citizens. Worst of all, Congress has done so by ambiguous legislation and unconstitutional delegation to the U.S. Department of Treasury, which in turn published an Interim Rule that only compounds the constitutional injury. When Congress purports to tell States what laws their legislatures can—and cannot—pass, or what their tax policies must be, whether by law or agency regulation, it violates state sovereignty. This structural violation of the Constitution intrudes upon the States' core sovereignty to direct their own fiscal affairs and make choices about how to tax residents.

NCLA was founded to restore constitutional limits on administrative power and to protect

[1] No counsel for a party authored any part of this brief. And no one other than the amicus curiae, its members, or its counsel contributed money that was intended to finance the preparation or submission of this brief.

the civil liberties of all Americans—including their right as U.S. citizens to be governed only by federal legislation passed via constitutional channels and their right as self-governing state citizens to have the States alone set tax policy in their respective legislatures. As explained below, Congress's attempted usurpation of state legislative powers, which were reserved to the several States by the enumeration of congressional powers and the Tenth Amendment, violates several bedrock provisions of the U.S. Constitution that define and constrain federal lawmaking.

INTRODUCTION

The condition in the America Rescue Plan Act of 2021 ("ARPA" or "the Act") that States accepting ARPA funds not reduce their own taxes upends the structure of American constitutionalism. This consequence is true regardless of whether, as the States allege, they are, in essence, compelled to accept ARPA funding. Setting aside the coercive aspects of this scheme, the Constitution is a law—the supreme law. Being a law and, indeed, a law made by the people, its limits are not alterable by private, state, congressional or executive consent, but only by the consent of the people. Accordingly, the federal government cannot escape its constitutional bounds by getting, let alone purchasing, the consent of any lesser body, whether individuals, private institutions, or States. In *New York v. United States*, 505 U.S. 144, 182 (1992), the Supreme Court recognized that "[w]here Congress exceeds its authority relative to the states, … the departure from the constitutional plan cannot be ratified by the 'consent' of state officials." Looking at it through the lens of enumerated powers, the court concluded, "[s]tate officials … cannot consent to the enlargement of the powers of Congress beyond those enumerated in the Constitution." *Id.*

Whatever else the Constitution permits, state taxation must remain firmly in the hands of locally elected legislatures. Taxation can be a source of deep discontent, as our Founding proved, and it is not only unconstitutional but dangerous to centralize control over taxes in the hands of federal officials, whether members of Congress, the Executive Branch, or both branches. The state electorate

votes for *state* officials who will decide—and be accountable for—state fiscal policy. Congress's arrogation of power over state taxation and delegation of it to the Treasury Department breaks that social compact, disenfranchises the state electorate, and violates the U.S. Constitution as elucidated in *New York*.

BACKGROUND

The Act, enacted on March 11, 2021, offers approximately $195 billion to States and their residents to assist with economic recovery from the Covid-19 pandemic. 42 U.S.C. § 802(a). But there is a catch: ARPA prohibits States from using the funds "to either directly or indirectly offset a reduction in the net tax revenue of such State … resulting from a change in law, regulation, or administrative interpretation … that reduces any tax." *Id.* § 802(c)(2)(A). ARPA authorizes the U.S. Department of the Treasury ("Treasury") (a) to recoup funds that are used by the States as direct or indirect offsets and (b) to "issue such regulations as may be necessary or appropriate" to implement the Act (and thus define what direct and indirect offsets means in practice). *Id.* § 802(f). Treasury issued an Interim Rule on May 17, 2021, purporting to implement the Tax Cut Ban and invited comments regarding how the interim regulation may be revised in a future final rule. *Coronavirus State and Local Fiscal Recovery Funds*, 86 Fed. Reg. 26,786 (May 17, 2021) ("Interim Rule").

The Interim Rule provided a detailed four-step process (absent from ARPA itself) whereby a State is required to estimate, for each change in law, regulation, or guidance, the amount by which that change resulted in a reduction in tax revenue, as compared to 2019, and the amount of reduction that was offset directly or indirectly by ARPA funds. 86 Fed. Reg. at 26,807-09. *See* 31 C.F.R. § 35.8 (b)(1)-(4). The Interim Rule further authorizes Treasury to police each State's estimate and recoup any reduction in tax revenue that, in its judgment, has not been "paid for" using non-ARPA funds. 31 C.F.R. § 35.10. NCLA was among many commenters that objected to the Interim Rule, pointing out its constitutional and statutory defects. *See* Exhibit A. Treasury has not yet issued a final rule.

ARGUMENT

I. CONGRESS CANNOT PURCHASE STATES' SOVEREIGN POWER OF TAXATION

A. The Tax Cut Ban Commandeers State Officials

The anti-commandeering doctrine serves as "one of the Constitution's structural protections of liberty." *Printz v. United States*, 521 U.S. 898, 921 (1997). The Constitution "divides authority between federal and state governments for the protection of individuals." *New York*, 505 U.S. at 181. It does so by "confer[ring] on Congress not plenary legislative power but only certain enumerated powers. Therefore, all other legislative power is reserved for the States, as the Tenth Amendment confirms." *Murphy v. NCAA*, 138 S. Ct. 1461, 1476 (2018). No enumerated power in the Constitution confers authority upon Congress to pass statutes that direct, let alone micromanage, state tax policy. The Commerce Clause, by its very terms, does not, nor is ARPA either "necessary" or "proper" and thus authorized by the Sweeping Clause. U.S. Const., art. I, sec. 8, cl. 18. The Supreme Court has recognized that state tax powers are a sphere of authority the federal government cannot invade and hence invading that province cannot possibly be necessary and proper to the exercise of an enumerated power. *See infra* pp. 10-11, 14-16, 23.

B. Federal Direction of State Policy Is a Structural Violation

Courts have affirmed some Spending Clause conditions under a contract-based theory of state consent. *See Pennhurst State School and Hospital v. Halderman*, 451 U.S. 1, 17 (1981). But that legal fiction is strained because state consent is being purchased by funds taken from the State's own tax base, *i.e.*, federal taxation of its citizens and businesses. There is no parity between contracting parties if one of those parties, the federal government, always has one of its hands in the pockets of its counterparties, the States. "The Supreme Court has recognized that unfettered use of [spending] power, especially when coupled with Congress's power to tax, could quickly alter the balance of powers between the federal government and the States," *Ohio v. Yellen*, --- F. Supp. 3d ---, 2021 WL 2712220, at *11 (S.D. Ohio July 1, 2021) ("*Ohio II*").

Courts must therefore vigilantly police the boundaries of consent to ensure Spending Clause conditions do not violate the Constitution's structure. *Id.* Two important limitations are relevant. *First*, Congress may not coerce States into accepting a spending condition by offering a massive amount of funding (which is drawn from the States' own citizens and businesses). *Nat'l Fed'n of Indep. Bus. v. Sebelius*, 567 U.S. 519, 581, (2012) ("NFIB"). *Second*, the federal government may not use spending conditions to "direct the functioning of the state [government], and hence to compromise the structural framework of dual sovereignty." *Printz*, 521 U.S. at 932. As explained below, the Tax Cut Ban violates both limitations and thus unconstitutionally commandeers.

The Supreme Court explains that commandeering is especially dangerous because "where the federal government compels states to regulate, the accountability of both state and federal officials is diminished." *New York*, 505 U.S. at 168. Congress cannot direct States in their choices of how to govern; it cannot require them to carry out specific federal regulations; nor can it "require the States to govern according to Congress' instructions." *Id.* at 162, 178. The federal government simply lacks power to direct or command the States to adopt regulatory, spending, or other policies, whether by statute or administrative edict, and this "is true whether Congress directly commands a State to regulate or indirectly coerces a State to adopt a federal regulatory system as its own." *NFIB*, 567 U.S. at 578.

Financial inducement crosses over into unconstitutional commandeering if it is so large it amounts to "a gun to the head." *Id.* at 581. Here, the $195 billion in Americans' tax dollars dangled by ARPA in front of the States exceeds 23% of state governments' revenue nationwide,[2] a sum that eclipses the massive Medicaid funding held to be coercive in *NFIB*. In *NFIB*'s context of Medicaid

[2] See National Association of State Budget Offices, Fiscal Survey of the States, (Fall 2020), 58, 64 ("current total estimate" of state revenue nationwide in 2021 is $838.8 billion, hence $195 billion in ARPA funds amounts to 23.25%.).

expansion, the Supreme Court held that "[t]he threatened loss of over 10 percent of a State's overall budget … is economic dragooning that leaves the States with no real option but to acquiesce." *Id.* at 582. Given that *NFIB*'s 10% figure already exceeds the tolerable limits of the anti-coercion principle, there can be no doubt that the even greater amounts in ARPA, *see* Complaint, ¶¶ 115-119 (setting out that ARPA funding constitutes 20-29% of the Plaintiff States' budgets), goes beyond permissible encouragement and amounts to unconstitutional commandeering of state sovereignty. *Id.* The only federal court that has considered the Tax Cut Ban on coercion grounds agreed: Judge Van Tatenhove permanently enjoined the Tax Cut Ban as to Kentucky and Tennessee because he concluded the vast sum of ARPA funds being offered for pandemic assistance—"equal to roughly one-fifth of their general revenue for the preceding year"—transformed the Tax Cut Ban into an unconstitutional "'gun to the head' contract of adhesion." *Kentucky v. Yellen*, --- F. Supp. 3d ---, 2021 WL 4394249, at *4, 6 (E.D. Ky. Sept. 24, 2021) (quoting *NFIB*, 567 U.S. at 575).

The unprecedented need for assistance arising from the Covid-19 pandemic combined with the dramatic financial carrot of ARPA funds makes it impractical for the Plaintiff States to refuse the enormous funding levels to which they are entitled under ARPA. Only the federal government has the means to provide such funds because it can raise taxes across the entire nation and because it can deficit spend, unlike most state governments cabined by balanced-budget requirements.[3] So, States are in no political or practical position to turn down the funds taken, in part, from their own residents and redirected to alleviating the far-reaching and undeniable economic and public health effects of a once-in-a-century pandemic.

But it isn't just the size of the carrot that effectively demotes the States from independent sovereigns to mere federal foot soldiers—it is the price of surrender that also renders this scheme

[3] *See* Tax Policy Center, *What are State Balanced Budget Requirements and How Do They Work?*, *available at* https://tinyurl.com/z8u6tdne (2015).

unconstitutionally coercive. The Tax Cut Ban would force States to surrender taxation powers that lay at "the core of state sovereignty reserved by the Tenth Amendment." *New York*, 505, U.S. at 177. In *McCollough v. Maryland*, Chief Justice Marshall held that a State cannot tax a federal entity because "the power to tax involves the power to destroy." 17 U.S. 316, 431 (1819). Here, running in the other direction, the federal government insisting that States maintain their current level of taxation for a span of about three years, again makes the violation structural. The anti-commandeering doctrine asks, has the challenged action substantially altered the balance of power between federal and state government? If so, it is commandeering because "the Constitution divides authority between federal and state governments for the protection of individuals," and a "healthy balance of power between the States and the Federal Government [reduces] the risk of tyranny and abuse from either front." *Murphy*, 138 S. Ct. at 1477 (quoting *New York*, 505 U.S. at 180-81 (alteration in original)). As Judge Cole held in granting a permanent injunction to Ohio, 'this is not division for division's sake.' At its founding, the Framers insisted upon these state and federal checks and balances to protect and preserve individual liberty." *Ohio II*, 2021 WL 2712220, at *1.

In prior commandeering cases, federal intrusion had been limited to a particular area of state government decision-making—for example, *New York* concerned disposition of nuclear waste and *Printz* concerned gun control. The Tax Cut Ban, however, is not so limited because tax policy affects *every* aspect of state government. The Tax Cut Ban further seeks to control States' spending powers, since spending levels to support various state programs determine whether a State can pay for a reduction in tax revenue using non-ARPA funds. A State would effectively be required to consult Treasury's regulations and guidance for every policy decision or else run the risk of a future claw back of revenue. Any legal or regulatory change might negatively impact tax revenue and thus risk a later recoupment action by Treasury. Would raising the budget of a state environmental agency lead to fewer non-ARPA funds that could pay for any reduction in tax revenue? Even after consulting Treasury' rules, the answer may still elude the State, which must then rely on the mercy of its federal

masters. Without full control over its own tax and spending policy, the Constitution's guarantee of dual sovereignty would transform into a "Mother may I" relationship between the States and the federal government. In short, were the federal courts to agree that the political branches possessed the power to control state taxes, the federal courts would greenlight the destruction of federalism.

It makes no difference that the instrument of such destruction is a spending condition to which a State has agreed, as opposed to a direct federal mandate. Under the Tax Cut Ban, the federal government imposes high tax rates on residents and businesses of the 50 States and then offers each State a portion of those federal proceeds to purchase control over that State's tax and spending policies. Because a State's tax and spending powers are so integral to its continued sovereignty, the federal government's attempt to purchase such powers is tantamount to an attempt to purchase state sovereignty itself. But that is simply not permitted under the Constitution's dual-sovereign structure: irrespective of the amount of money being offered, a State can no more sell its sovereignty than an individual can contract him or herself into bondage.

The Supreme Court has long acknowledged the clear danger posed to federalism by the unfettered use of federal tax power, on one hand, and spending powers on the other. The line between legitimate spending power and abuses of the spending power is drawn best in *United States v. Butler*, 297 U.S. 1 (1936). Where Congress has no enumerated power to legislate, it "may not indirectly accomplish those ends by taxing and spending to purchase compliance." *Id.* at 74. If the taxing and spending powers are not so limited, they "would become the instrument for total subversion of the governmental powers reserved to the individual states." *Id.* at 75.

More recently, the Supreme Court has refined this analysis. It has held that Congress may use its Spending Clause powers "to grant federal funds to the States, and may condition such grants upon the States' taking certain actions that Congress could not require them to take." *NFIB*, 567 U.S at 581-82 (internal quotation marks omitted). But the Court also "recognized limits on Congress's power

under the Spending Clause to secure state compliance with federal objectives … Otherwise the two-government system established by the Framers would give way to a system that vests power in one central government, and individual liberty would suffer." *Id.* at 576. As such, spending conditions must not be imposed coercively, and "Spending Clause legislation [must] not undermine the status of the States as independent sovereigns in our federal system." *Id.* at 577.

If these limits are to mean anything at all, they must prohibit the Tax Cut Ban. Congress says to the States, here is an offer you can't refuse: we know you are over the barrel for funds to fight the pandemic and its economic consequences, so surrender your sovereignty, account to us for your legislation and stewarding of the public fisc, and if you are lucky and your legislation over the next several years passes muster with us, we won't throw your certifying public officials in jail.[4] It is hard to envision a more coercive scheme or one more injurious to state sovereignty.

C. Commandeering Infringes Americans' Right of Self-Government in the States

The Tax Cut Ban also offends the Constitution's requirement that "[t]he United States shall guarantee to every State in this Union a Republican Form of Government." U.S. Const. Art. IV, § 4, cl. 1. Whatever else this provision secures, it at least protects Americans from federal interference in their freedom of elective self-government in the States. Even an elected government is not "Republican" if it is deprived of the power to enact its own laws. Federal efforts that disrupt the fiscal powers essential to *all aspects* of such a government are surely anathema to the Constitution.

The Eastern District of Kentucky recently struck down ARPA's Tax Cut Ban on commandeering grounds, in part, based on the size of funds being offered. *See Kentucky*, 2021 WL 4394249, at *6. Federal purchasing of state taxing power, however, inflicts far greater injury on the design and operation of federalism than in the seminal commandeering cases (*Printz*/*New York*). Those

[4] Possible criminal consequences exist under ARPA because state officials signing the initial certification in 42 U.S.C. § 802(d)(1) could be subjected to criminal fraud penalties if federal officials disagree with the accuracy of the certification. *See* 18 U.S.C. § 287.

cases prohibited States from becoming federal underlings. Here, seizure of taxing powers would deprive States of their life's blood, the very source of their independence. The amount offered does not matter because the State's taxing power is priceless and inalienable under the Constitution.

No constitutional provision authorizes the federal government to eliminate the state power to cut taxes. Article I, Section 10, Clause 2 of the Constitution provides: "No state shall, without the consent of the Congress, lay any imposts or duties on imports or exports, except what may be absolutely necessary for executing its inspection laws." This is the sole express restriction on state taxing power in the Constitution and it is flatly inapplicable to defend the validity of a broadly interpreted Tax Cut Ban to bar any state tax reduction during the "covered period."

The Import-Export Clause even prescribes where any state inspection-related revenues must be deposited: "[T]he net produce of all duties and imposts, laid by any state on imports or exports, shall be for the use of the treasury of the United States; and all such laws shall be subject to the revision and control of the Congress." *Id.* This, along with the fact that the Constitution carefully defines in several provisions the extent of federal tax power, reveals that the Framers knew how to limit tax powers when they wanted to. *See* U.S. Const. Art. I, § 8, cl. 1; *id.* Art. I, § 9, cl. 1, 4, 5; amend. XVI. Constitutional silence thus dictates that Congress must respect state prerogatives to tax or relieve tax burdens as the States see fit, as long as they do not run afoul of other, broad-gauge constitutional restrictions (*e.g.*, by trenching upon the rights of due process or equal protection).

Further restrictions on state tax power cannot be read into the Constitution. *See Dep't of Revenue of State of Wash. v. Ass'n of Wash. Stevedoring Cos.*, 435 U.S. 734, 759-60 (1978) (the Import-Export Clause does not even bar all forms of state taxation on imports and exports but only those that qualify as "imposts" or "duties"); *Richfield Oil Corp v. State Corp. of Equalization*, 329 U.S. 69, 76 (1946) ("The fact of a single exception [to offset state inspection laws] suggests that no other qualification of the absolute prohibition was intended."). Under this constitutional brand of *expressio unius* reasoning, even if both

(a) the Tax Cut Ban were not ambiguous but clearly banned state tax reductions;[5] *and* (b) a State somehow opted to earmark any new ARPA monies it received to fund a reduction in a preexisting state tax, the State Tax Cut Ban would still be unconstitutional.

D. Courts Have a Duty to Follow the Law, Including the Constitution, and Cannot Leave the States to the "Political Safeguards of Federalism"

By vesting Congress with only limited federal powers, the Constitution simultaneously protected the States and individuals from federal incursions into the spheres of state sovereignty on the one hand and private rights on the other. But even while protecting state sovereignty, the Constitution indirectly secures individual rights as well, for what is called *federalism* is, at the most fundamental level, the freedom of individuals to enjoy localized self-government. In short, federalism is itself a matter of guaranteeing personal liberty. *See NFIB*, 567 U.S. at 536 ("[F]ederalism protects the liberty of the individual from arbitrary power.") (quoting *Bond v. United States*, 564 U.S. 211, 222 (2011)).

Judges have a duty to uphold these freedoms. The federal government increasingly dictates state policy, even on matters as far outside federal authority, and of inherently localized concern, such as state taxation, land use, and K-12 education. *See* PHILIP HAMBURGER, PURCHASING SUBMISSION: CONDITIONS, POWER AND FREEDOM, 139-41 (2021). Indeed, federal conditions have restructured internal state governance in line with federal administrative models. *See id.* at 41-45. So the notion that States can protect themselves politically is an illusion. *See id.* at 137-39. When States are denied constitutional protection in the courts, as the States of Missouri and Arizona were when courts denied

[5] But the Tax Cut Ban, in fact, is unclear and ambiguous and remains so after Treasury's Interim Rule. *See* Argument Sections II & III, *infra*.

them standing to protect the structural integrity of their fiscal powers,[6] individuals are profoundly affected.

Political power is not a substitute for law. The Constitution was adopted precisely to enable Americans and their institutions to rely on law in place of mere power or force. As put by Justice Marshall, it is "emphatically" the duty of the judges "to say what the law is." *Marbury v. Madison*, 5 U.S. 137, 177 (1803). Judges must not abdicate their constitutional duty to enforce the Constitution when States come into court. To do so is to abandon judicial duty, misunderstand the political process, lawlessly expand federal power, thereby demolishing federalism and the individual freedom it safeguards.

II. THE TAX CUT BAN'S AMBIGUITY GIVES RISE TO TWO DIFFERENT BUT INTERRELATED CONSTITUTIONAL DEFECTS

Two separate constitutional doctrines converge to establish that ARPA's significant ambiguities must be interpreted to invalidate the Tax Cut Ban. These bars to the Tax Cut Ban operate even if the federal government could, in essence, purchase state tax powers, though for the reasons explained above in Argument Section I, the federal government lacks such a power to circumvent "Our Federalism." *Younger v. Harris*, 401 U.S. 37, 44 (1971). For tax powers are "indispensable" to the very "existence" of the States. *Gibbons v. Ogden*, 22 U.S. (9 Wheat.) 1, 199 (1824). *See also Dep't of Revenue v. ACF Indus., Inc.*, 510 U.S. 332, 345 (1994) ("taxation authority [is] recognized as central to state sovereignty").

A. The Tax Cut Ban Is Irredeemably Ambiguous

"[I]f Congress desires to condition the States' receipt of federal funds, it must do so unambiguously." *South Dakota v. Dole*, 483 U.S. 203, 203 (1987). ARPA, however, does not define the

[6] *See Arizona v. Yellen*, 2021 WL 3089103 (D. Ariz. July 22, 2021); *Missouri v. Yellen*, 2021 WL 1889867. (E.D. Mo. May 11, 2021).

ambiguous and amorphous term "directly or indirectly" at all. The term is thus open to speculation, to post-distribution-of-funds rulemaking (as already exists in Treasury's Interim Rule), to recoupment demands by the Inspector General, or to other enforcement actions that could be brought against the States. *See, e.g., supra* n.4 (flagging the possibility of criminal penalties to discipline inaccurate certifications by state officials signing papers to take ARPA funds).

From one perspective, the key verb in the Tax Cut Ban is "offset." The most natural reading of the verb to "offset" requires an *explicit one-to-one matching* of state tax reductions during the "covered period" with the federal "funds provided under this section," and so would continue to allow state tax cuts that have nothing to do with receiving ARPA COVID-relief funds. *See* OXFORD ADVANCED AMERICAN DICTIONARY, defining "offset" as "*to use* one cost, payment, or situation to cancel or reduce the effect of another," *available at* https://www.oxfordlearnersdictionaries.com/us/definition/english/offset_1?q=offset (emphasis added); *see also* MERRIAM-WEBSTER DICTIONARY (defining the verb "offset" as "*to place over against something*" and "offset" in noun form as "something that serves to counterbalance or to compensate *for something else,*" *available at* https://www.merriam-webster.com/dictionary/offset (emphasis added)). Close in time to ARPA's passage, the Treasury Department interpreted the provision this way. *See* Laura Davison, *Treasury Clears States to Cut Taxes—But Not With Stimulus*, BLOOMBERG (Mar. 18, 2021), *available at* https://tinyurl.com/2s5eb6fv; Letter from Janet L. Yellen to 21 State Attorneys General (Mar. 23, 2021), *available at* https://tinyurl.com/tsn9t9a7 ("[T]he Act does not deny States the ability to cut taxes in any manner whatsoever. It simply provides that funding received under the Act may not be used to offset a reduction in net tax revenue resulting from certain changes in state law.") (cleaned up).

But from another perspective, the provision can also be read more broadly because it restricts state power "directly or indirectly" and thus could be intended to head off at the pass the inherent fungibility of money. This appears to have been swing-vote Senator Manchin's reason for supporting

the Tax Cut Ban. *See* Alan Rappeport, *A Last-Minute Add to Stimulus Bill Could Restrict State Tax Cuts*, N.Y. TIMES (Mar. 12, 2021), *available at* https://www.nytimes.com/2021/03/12/us/politics/biden-stimulus-state-tax-cuts.html. The open choice between these two interpretations thus represents just one fatal ambiguity under the *Dole* test currently applied by the Supreme Court to define proper Spending Clause restrictions on deals with States. And, as explained further in Argument Section II.B, *infra*, this ambiguity equally runs afoul of the constitutional clear-statement rule designed to protect state sovereignty.

Further, we *independently know* the conditions are dangerously ambiguous from the pre-suit communications between the States and Congress on the one hand and the Department of Treasury on the other. *See* Arizona Complaint in *Arizona v. Yellen*, No. 2:21-cv-00514-SMB, Dkt. #1, ¶ 3 (Mar. 25, 2021), *available at* https://tinyurl.com/rwp8jeks (Treasury: States remain "free to make policy decisions to cut taxes" so long as they do not "use the pandemic relief funds to pay for those tax cuts."). But when Secretary Yellen was pressed by Senators on what that statement means in a world where money is fungible and tax cuts are not paid for by invoice, she admitted that the issue is "thorny." Hearing on CARES Act Quarterly Report, Sen. Banking, Hous. & Urb. Affairs Comm (Mar. 24, 2021), *cited in* Rep. in Support of Mot. for a Prel. Inj, 2-3, in *Ohio v. Yellen*, 1:21-cv-00181-DRC, Dkt. #30, *available at* https://tinyurl.com/2wwfjz3r. In an exchange at that hearing between Secretary Yellen and Senator Crapo about the Act's bar on using the relief funds that would even "indirectly" cause a revenue decrease, given the "fungibility of money," the Secretary conceded that it is "hard … to answer" exactly how ARPA may "hamstr[i]ng" the States. Toby Eckert, *Yellen: Treasury Faces 'Thorny Questions' About Restrictions On State Tax Cuts*, Politico (Mar. 24, 2021), *available at* https://tinyurl.com/4vmrpajz.

Moreover, Secretary Yellen, speaking through the U.S. Justice Department, has now also gone on record in litigation several times, including when she resisted Ohio's challenge to the Tax Cut Ban.

See Br. in Opp. to Ohio's Mot. for Prel. Inj., in *Ohio v. Yellen*, No. 1:21-cv-00181-DRC, Dkt #29 (Apr. 16, 2021). The federal government strangely but repeatedly emphasized that States are free to cut any particular tax, as long as state tax levels as a whole do not go down: "Under the Act's plain terms, a State is free to impose taxes as it believes appropriate, with no effect on the amount of the federal grant, as long as the changes—taken together over the reporting period—do not result in a reduction to the State's net tax revenue." *Id.* at 17; *see also id.* at 2, 6. How generous of the federal government! State tax collection can be shifted around (*e.g.*, state personal income tax cuts can be offset by state sales tax increases), but during the period ARPA is in effect, net tax burdens must not be reduced.

What the federal government overlooks is that there is no constitutional basis at all that lets it stand in the way of state government downsizing, if that is the will of the State's voters. "*The extent to which* [*state tax power*] *shall be exercised*, the subjects upon which it shall be exercised, and the mode in which it shall be exercised, are all equally within the discretion of the legislatures to which the States commit the exercise of the power." *Union Pac. R. Co. v. Peniston*, 85 U.S. (18 Wall.) 5, 30 (1873) (emphasis added). And as *Peniston* concludes, "[t]here is nothing in the Constitution which contemplates or authorizes any direct abridgment of this power by National legislation." *Id.*

The Supreme Court insists that Congress must condition spending "unambiguously" so States may "exercise their choice knowingly, cognizant of the consequences of their participation." *Dole*, 483 U.S. at 207; *see also Arlington Cent. Sch. Dist. Bd. of Educ. v. Murphy*, 548 U.S. 291, 296 (2006) (requiring "clear notice" of conditions). The condition here is neither clear nor unambiguous and cannot be made so, given that state legislation will always affect fungible tax receipts in some way. Finalized Treasury regulations cannot cure the problem, and as shown in Argument Section III, *infra*, the existing Treasury Interim Rule has certainly not fixed the problem. This is especially true given that we are in a pandemic. States must adjust to a dizzying array of new federal policies in the pandemic era, coming online as they do on a daily or weekly basis. *See* White House, *Path Out of the Pandemic*, *available at*

https://www.whitehouse.gov/covidplan/ (last visited Oct. 4, 2021) (listing six major policy headings, each with their own multiple sub-links, ranging from "Vaccinating the Unvaccinated" to "Protecting Our Economic Recovery" to "Improving Care for those with COVID-19"). The States simply cannot afford to wait to make policy, fiscal, and tax policy adjustments until Treasury's regulatory regime fully comes to rest. *See also Ohio II*, 2021 WL 2712220, *8 ("[I]ssues regarding taxation are never completely removed from legislative consideration. With a two-year budget cycle and a balanced-budget requirement, planning, at least informal planning, regarding taxation and expenditures will start anew as a practical matter, almost immediately …."). "States cannot knowingly accept conditions of which they are 'unaware' or which they are '*unable to ascertain*.'" *School Dist. of City of Pontiac v. Secretary of U.S. Dep't of Educ.*, 584 F.3d 253, 268 (6th Cir. 2009) (emphasis added) (quoting *Arlington*, 548 U.S. at 296) (in turn quoting *Pennhurst*, 451 U.S. at 17)).

"The legitimacy of Congress's exercise of the spending power thus rests on whether the State voluntarily and knowingly accepts the terms of the contract. Respecting this limitation is critical to ensuring that Spending Clause legislation does not undermine the status of the States as independent sovereigns in our federal system." *NFIB*, 567 U.S. at 577 (internal quotation marks and citations omitted). The Tax Cut Ban thus flunks the ambiguity test because it offers up only a black box with contents that may not be fully illumined until years down the road.

B. ARPA Must Be Construed Using the Constitutional Clear Statement Rule

Gregory v. Ashcroft requires as a threshold matter that any infringements on state sovereignty be "plain to anyone reading the [statute]." 501 U.S. 452, 467 (1991). The rule is "an acknowledgment that the States retain substantial sovereign powers under our constitutional scheme, powers with which Congress does not readily interfere." *Id.* at 461. Specifically, the *Gregory* clear-statement rule "provides assurance that 'the federal-state balance' will not be disturbed unintentionally by Congress or unnecessarily by the courts." *Jones v. Rath Packing Co.*, 430 U.S. 519, 525 (1977) (citation omitted).

The Court in *Gregory*, faced with a situation where the historic state power to define the qualifications of its judges was threatened, thought the federal statute did not *just* sweep "beyond an area traditionally regulated by the States," instead classing "it [a]s a decision of *the most fundamental sort* for a sovereign entity," 501 U.S. at 460 (emphasis added). The state taxing power is even more fundamental because "the taxing power of a State is one of its attributes of sovereignty … [I]t exists independently of the Constitution of the United States, and underived from that instrument; and … it may be exercised to an unlimited extent upon all property, trades, business, and avocations … within the territorial boundaries of the State … ." *Peniston*, 85 U.S. at 29. Yet, no one can say whether ARPA prohibits any state "reduction in the net tax revenue" or can be read more modestly only to bar using ARPA monies, *specifically*, to "offset" such funds. What is beyond dispute, then, is that Congress did not speak clearly.

Because the Tax Cut Ban was open to interpretation by the Treasury Interim Rule (*see* Argument Section III, *infra*) and remains open to further interpretation by final Treasury rules, the States have no *ex ante* assurance of what they must do to comply with the Tax Cut Ban. A State may not know until months or even years after funds are already received and long spent that the federal government deems the State to have violated the Tax Cut Ban, or Treasury's interpretation of it. This circumstance also has a chilling effect—because to avoid the federal claw back penalty, a State will have to err in favor of *raising* revenues in order to avoid an inadvertent miscalculation that incurs federal wrath and could send certifying officials to federal prison. That is not only an unwarranted invasion of the independent sphere reserved to the States in which to exercise their tax powers, it is terrible policy in a pandemic where families are hurting, inflation is rising, and tax relief at the state level could help Americans respond to COVID's many challenges. The federal government knows this well. To much fanfare, it has touted its own "stimulus" tax cuts as helping citizens face the

challenges of COVID. *See, e.g., What to Know About All Three Rounds of Coronavirus Stimulus Checks*, *available at* https://tinyurl.com/t9xj8mwv (Mar. 15, 2021).

The Southern District of Ohio's Judge Cole best summarized the Tax Cut Ban's indeterminacy:

> In its previous Opinion, the Court observed that it could not ascertain what an indirect offset may (or may not) be. And the Court was not alone in that. At oral argument on the motion for preliminary injunction, the Secretary declined to take any position on that term either. Perhaps unsurprisingly, Ohio too expressed confusion regarding the contours of the phrase.

Ohio II, 2021 WL 2712220, at *14. In other words, neither (1) Judge Cole, nor (2) the Secretary of Treasury (speaking through the Justice Department at oral argument), nor (3) the State of Ohio could figure out what the Tax Cut Ban really means. The New Civil Liberties Alliance, standing as a friend of this Court and representing the perspective of the people, is similarly mystified, despite studying the provision itself on many occasions in connection with filing amicus briefs in several cases like this one. Or as Judge Cole originally wrote in May 2021: "Despite poring over this statutory language, the Court cannot fathom what it would mean to 'indirectly offset a reduction in the net tax revenue' of a State, by a 'change in law … that reduces any tax (by providing for a reduction in a rate, a rebate, a deduction, a credit, or otherwise).'" *Ohio v. Yellen*, --- F. Supp. 3d ---, 2021 WL 1903908, at *12 (S.D. Ohio May 12, 2021) ("*Ohio I*").

III. THE NONDELEGATION DOCTRINE PROHIBITS TREASURY FROM CLARIFYING THE TAX CUT BAN THROUGH REGULATION

Treasury conceded in a prior ARPA litigation that "the Tax Mandate may be ambiguous" as written. *Ohio* I, 2021 WL 1903908, at *13. It does again so in this case by contending that clarity is not needed after all—rather, Congress merely must put States on notice that "acceptance of federal funds obligates the State to comply with a condition," even if ambiguous, since "any particularized question can be addressed by agency regulations[.]" ECF No. 19 at 31 (emphasis added). According to Treasury,

Congress "expressly authorized Treasury 'to issue such regulations as may be necessary or appropriate to'" resolve the Tax Cut Ban's ambiguities. *Id.* at 32 (quoting 42 U.S.C. § 802(f)).

This view, however, would amount to an unconstitutional delegation of legislative and Spending Clause powers. "Article I, § 1, of the Constitution vests all legislative powers herein granted … in a Congress of the United States. This text permits no delegation of those powers." *Whitman v. Am. Trucking Assocs.*, 531 U.S. 457, 473 (2001) (cleaned up). Accordingly, the Fifth Circuit has held that it is Congress rather than an agency that must clearly articulate Spending Clause conditions. *Texas Educ. Agency v. United States Dep't of Educ.*, 992 F.3d 350, 361 (5th Cir. 2021) ("The needed clarity cannot be [agency] provided—it must come directly from the statute"). An agency may sometimes supply administrative details, but only if, as was the case in *Bennett v. Kentucky Department of Education*, 470 U.S. 656, 666 (1985), "[t]he requisite clarity … is provided by [the statute]" in the first place.[7] Here, the statute is hopelessly vague.

[7] Treasury's suggestion that that its Tax Cut Ban regulation should receive *Chevron* deference is misplaced. *See* ECF No. 19 at 35. The Supreme Court explicitly declined a federal agency request to defer to its interpretation of a spending condition in *Bennet*, 470 U.S. 656 ("We find it unnecessary here to adopt the Government's suggestion that the Secretary may rely on any reasonable interpretation of the requirements of Title I"). Such deference would eviscerate the contract-based legal fiction undergirding a Spending Clause condition: a State cannot "knowingly" agree to an ambiguous condition that an agency may later define through regulation. *See id*

That problem is especially acute here because Treasury's Interim Rule is explicitly subject to subsequent revision. A Spending Clause condition must be clear when offered to States. As the Fifth Circuit recently explained: "Relying on regulations to present the clear condition, … is an acknowledgment that Congress's condition was not unambiguous" when first offered. *Texas Educ. Agency*, 992 F.3d at 361. The Fourth Circuit has further elaborated that deference to an agency's interpretation of a spending condition is inappropriate where, as here, the statute has "implications for the balance of power between the Federal Government and the States." *Va. Dep't of Educ. v. Riley*, 106 F.3d 559 567 (4th Cir. 1997) (en banc) (per curiam).

Where Congress delegates regulatory power to an agency, it must supply "an intelligible principle to guide the deleg[at]ee's use of discretion." *Gundy v. United States*, 139 S. Ct. 2116, 2123 (2019). While the Supreme Court is split regarding the precise parameters of the intelligible-principle test, *see id.* ("'intelligible principle' was just another way to describe the traditional rule that Congress may leave the executive the responsibility to find facts and fill up details") (Gorsuch, J. dissenting), there can be no doubt the Tax Cut Ban fails. And, as noted above, the only federal court that has attempted to decipher the Tax Cut Ban's text was forced to throw up its hands and say: "the Court cannot fathom what it would mean to 'indirectly offset a reduction in the net tax revenue' of a State, by a 'change in law … that reduces any tax.'" *Ohio I*, 2021 WL 1903908, at *12 (quoting 42 U.S.C. § 802(c)(2)(A)). A second round of briefing only "confirm[ed] the Court's suspicion that the phrase is *unintelligible*." *Ohio II*, 2021 WL 2712220, at *14 (emphasis added).

Treasury's contention that ARPA authorizes it to "issue such regulations as may be necessary or appropriate" to implement the "unintelligible" Tax Cut Ban, ECF No. 19 at 32 (quoting 42 U.S.C. § 802(f)), is thus foreclosed as a "sweeping delegation of legislative power," *Indus. Union Dep't, AFL-CIO v. Am. Petroleum Inst.*, 448 U.S. 607, 646 (1980) (quoting *A.L.A. Schechter Poultry Corp. v. United States*, 295 U.S. 495, 539 (1935)). In *American Petroleum*, the Supreme Court rejected the Secretary of Labor's argument that the Occupational Safety and Health Act authorized him to promulgate regulations that were "reasonably necessary or appropriate to provide safe or healthful employment." *Id.* at 640-41 (quoting 29 U.S.C. 652(8)). As the D.C. Circuit in *International Union v. OSHA* explained, authorizing an agency to regulate in whatever manner it deems "necessary or appropriate" to achieve vague policy objectives, such as workplace health and safety, would "raise a serious nondelegation issue" and thus must be rejected. 938 F.2d 1310, 1317 (D.C. Cir. 1991); *See also Grayned v. City of Rockford*, 408 U. S. 104, 108–109 (1972) ("A vague law impermissibly delegates basic policy matters

… ."). Treasury's reliance on the same "necessary or appropriate" standard in 42 U.S.C. § 802(f) to regulate in furtherance of an equally vacuous anti-tax-cut objective likewise fails.

"If agencies were permitted unbridled discretion, their actions might violate important constitutional principles of separation of powers and checks and balances. To that end the Constitution requires that Congress' delegation of lawmaking power to an agency must be 'specific and detailed.'" *FCC v. Fox TV Stations, Inc.*, 556 U.S. 502, 536 (2009). The ambiguities in the Tax Cut Ban, however, are so vast that allowing Treasury to resolve them would essentially rewrite the statute to say: "the Secretary may recoup ARPA funding to the extent that the Secretary determines, *in her discretion*, that [a tax] rate reduction resulted in the State losing tax revenues, and the Secretary further determines, *in her discretion*, that those losses were offset with ARPA funding," whether directly or indirectly. *Ohio II*, 2021 WL 2712220, at *14 (emphases added). Because it is impossible to discern what indirectly offsetting a reduction in tax revenue with ARPA funds means, this grant of power would be devoid of any intelligible boundaries on Treasury's discretion, let alone "specific and detailed" ones. *Id.* Treasury cannot supply its own boundaries to cabin this unconstitutional discretion. "The idea that an agency can cure an unconstitutionally standardless delegation of power" is "internally contradictory." *American Trucking*, 531 U.S. 457, 473. This is because "[t]he very choice of which portion of the power to exercise—that is to say, the prescription of the standard that Congress had omitted—would itself be an exercise of the forbidden legislative authority." *Id.* Courts and States are unable to ascertain what the Tax Cut Ban requires. *Ohio II*, 2021 WL 2712220, at *14. Nor does Treasury have special insight into the Tax Cut Ban's unintelligible requirements—it has repeatedly admitted confusion on that count. *See, e.g.*, *supra* at Argument Section II.B. Hence,Treasury's attempt to "clarify" such requirements through regulation would amount to an impermissible enactment of its own agency-created Spending Clause condition, in clear breach of the Constitution's separation-of-powers safeguards.

Treasury's inability to resolve the Tax Cut Ban's ambiguities through regulation is reinforced by the "major questions" doctrine. Given the sums at stake and the federalism questions raised, the Tax Cut Ban presents questions of deep "economic and political significance," and if Congress intended for Treasury to answer such "major questions," it must say so clearly. *FDA v. Brown & Williamson*, 529 U.S. 120, 159 (2000). Any authority to infringe on state sovereignty, such as allowing Treasury to interpret the Tax Cut Ban, must also be made "plain to anyone reading the [statute]." *Gregory*, 501 U.S. at 467. Not only are such clear statements missing in this case (*see supra* at Argument Section II.B for more on this point), but ARPA expressly allowed States to certify adherence to the Tax Cut Ban in exchange for funds immediately upon the Act's effective date. "That is strong evidence that Congress considered the terms of the deal to be complete as of that date. At the very least, the timing here does not provide the necessary evidence that Congress meant to conscript agency drafters into completing its legislative efforts." *Ohio II*, 2021 WL 2712220, at *20.

Finally, instead of providing clarity, Treasury's Interim Rule deepens the Tax Cut Ban's vagueness and illustrates the need for clear statutory boundaries. The power Treasury gave itself in 31 C.F.R. § 35.10 to recoup state tax cuts that, in its judgment, have not been "paid for," *see* 86 Fed. Reg. at 26,808 and 26,810, offers the easiest way to see that the Interim Rule fails to purge ambiguity out of the ARPA deal being proposed to the States. Under that catch-all power, Treasury would be free to consider "all relevant facts and circumstances" in deciding whether to seek recoupment for unpaid-for tax cuts. *Id.* at 26,810. This arrogation of power cloaks Treasury's system behind a dark and mysterious curtain and is particularly insidious because executive enforcement choices are often unreviewable. *See Heckler v. Chaney*, 470 U.S. 821, 833 (1985). The unintelligible Tax Cut Ban, combined with the standardless discretion Treasury has conferred on itself no less to consider "all relevant facts," thus gives Treasury nearly unchecked and uncheckable power over how, when, and against which States it will choose to claw back billions in ARPA funds. The potential for abusive and arbitrary

enforcement is gigantic. Treasury's enforcement decisions are largely beyond review, and there is nowhere for a State to turn if that power is used for political or other illegitimate purposes—or even if that power is just executed incompetently. This policy reason alone requires Congress to provide clearer standards to ensure Treasury's oversight of the Tax Cut Ban is even-handed and not subject to abuse.

CONCLUSION

The Tax Cut Ban runs afoul of a host of constitutional provisions and legal doctrines. But ultimately, this case is not only about the legal issues of *Dole*, *NFIB*, clear statements, ambiguity, reasonable relationships, coercion, commandeering, or the rest that could be brought to bear on this breathtaking federal arrogation of power—though the very wealth of offended doctrines stands as sure proof that a critical underpinning of federalism and state sovereignty has been eviscerated.

Beyond these provisions and doctrines, what is really at stake is the kind of issue courts do not see every day: a fundamental threat to the very structure of American government. The Founders who first put state constitutions in place, followed by experiments in federal power like the Articles of Confederation that led to the United States Constitution as we know it, would recoil at the idea that Congress would use massive federal levies on state residents and businesses coupled with massive deficit spending to create an enormous pot of tax proceeds that could be used to purchase state submission to federal control.

Congress knows full well that it could never hope to defend legislation that explicitly shifted control of state budgets to the federal government. This attempted federal regulation of Americans' state fiscal decisions through conditions on federal largesse, rather than through law, is "an irregular pathway of government control" that displaces *both* the lawful exercise of state power over the States' own fiscs *and* Americans' right to vote for those who will lawfully make those decisions. *See* HAMBURGER, PURCHASING SUBMISSION at 11; *see also New York*, 505 U.S. at 169 ("Accountability is

thus diminished when, due to federal coercion, elected state officials cannot regulate in accordance with the views of the local electorate in matters not pre-empted by federal regulation.").

Respectfully submitted,

/s/ Margaret A. Little
Margaret A. Little, N.D. Tex. Bar No. 303494CT
Sheng Li
Mark Chenoweth
NEW CIVIL LIBERTIES ALLIANCE
1225 19th St. NW, Suite 450
Washington, DC 20036
(202) 869-5210
peggy.little@ncla.legal
Counsel for Amicus Curiae

October 4, 2021

CERTIFICATE OF COMPLIANCE

I certify that this brief complies with the typeface requirements of this court's orders in this case because this brief was prepared using Microsoft Word in 12-point Garamond, a proportionally spaced typeface in the body of the brief and 12-point typeface in the footnotes.

/s/Margaret A. Little

CERTIFICATE OF SERVICE

I hereby certify that on October 4, 2021, an electronic copy of the foregoing motion for leave to file a brief *amicus curiae* was filed with the Clerk of Court for the United States District Court for the Northern District of Texas using the CM/ECF filing system and that service upon counsel for the parties will be accomplished using the CM/ECF system.

/s/Margaret A. Little

New Civil Liberties Alliance

July 15, 2021

FILED VIA REGULATIONS.GOV

The Honorable Janet Yellen
Secretary of the Treasury
U.S. Department of the Treasury
1500 Pennsylvania Ave., NW
Washington DC, 20220

Re: Interim Final Rule, Coronavirus State and Local Fiscal Recovery Funds
Docket No. TREAS-DO-2021-0008-0002

Dear Secretary Yellen:

The New Civil Liberties Alliance (NCLA) submits the following comments in response to the Department of the Treasury's (Treasury) *Interim Final Rule—Coronavirus State and Local Fiscal Recovery Funds*, 31 CFR Part 35. NCLA sincerely appreciates this opportunity to comment and express its concerns about the Interim Final Rule (IFR).

I. INTERESTS OF NCLA

The New Civil Liberties Alliance is a nonpartisan, nonprofit civil rights organization founded to protect constitutional freedoms from violations by the administrative state. NCLA's original litigation, *amicus curiae* briefs, regulatory comments, and other means of advocacy strive to tame the unlawful power of federal agencies. NCLA defends civil liberties by invoking constitutional constraints to limit administrative power. Although Americans still enjoy a shell of their Republic, a very different sort of government has developed within it—a type, in fact, the Constitution's design sought to prevent.

Not only does the administrative state evade constitutional limits through administrative rulemaking, adjudication, and enforcement, but increasingly agencies coerce state and local actors by conditioning receipt of federal funds upon acquiescence to certain policies. Frequently, this coercion directly conflicts with the vesting of authority to set such policies elsewhere, as in this case where the right to set their own tax policies is reserved to the states. Such unconstitutional administrative actions violate more rights of more Americans than any other aspect of American law, which is why they are the focus of NCLA's efforts.

Where agencies are poised to act beyond their lawful powers, NCLA encourages them to curb the illegitimate exercise of such power by establishing meaningful limitations on administrative rulemaking, adjudication, and enforcement. The courts are not the only government bodies with the duty to attend to the law. Even more immediately, agencies and agency heads must examine whether their modes of rulemaking, adjudication, and enforcement comply with the Administrative Procedure Act (APA), laws of Congress, and the Constitution. The Department of the Treasury should do so here before more courts must act to set aside the unlawful IFR.

II. BACKGROUND

The American Rescue Plan Act of 2021 (ARPA), enacted on March 11, 2021, offers approximately $195 billion to states and their residents to assist with economic recovery from the Covid-19 pandemic. As a condition of acceptance, however, a state must agree not to use ARPA funds "to either directly or indirectly offset a reduction in the net tax revenue of such State … resulting from a change in law, regulation, or administrative interpretation … that reduces any tax." 42 U.S.C. § 802(c)(2)(A). ARPA authorizes the Treasury to recoup any violation of this condition, *id*. § 802(e), which is referred to hereinafter as the "Tax Cut Ban."

On May 17, 2021, Treasury published an interim final rule in the Federal Register that purports to interpret the Tax Cut Ban. 86 Fed. Reg. 26,786 (May 17, 2021) ("IFR"). The IFR sets out a four-step methodology to identify state tax cuts that Treasury might later try to recoup. Boiled to their essence, the four steps are:

> (1) Sum All State Tax Cuts Each Year: Each change in [state] law, regulation, or administrative interpretation is identified that could reduce net tax revenue and those reductions are then summed. "The sum of these values in the year for which the government is reporting is the amount it needs to 'pay for' with sources other than [ARPA] Funds …"
>
> (2) De Minimis Safe Harbor: If the total value of the tax reductions for the reported year fall below a 1% de minimis level, then that bucket of tax reductions does not need to be "paid for" and will not be recouped.
>
> (3) Comparison to Fiscal 2019 as Baseline Year: "If the recipient government's actual tax revenue is greater than the amount of tax revenue received by the recipient for the fiscal year ending 2019, adjusted annually for inflation," then the state will be deemed not to have reduced its net tax revenue.
>
> (4) Identification of Offsets: The state can then "identify any sources of funds that have been used to permissibly offset the total value of covered tax changes other than [ARPA] Funds."

86 Fed. Reg. at 26,807-09. *See* 31 C.F.R. § 35.8 (b)(1)-(4).

In practice, there is also an unstated fifth step: 31 C.F.R. § 35.10 allows Treasury to identify the amount of tax cuts that, in its judgment, have not been "paid for" using the above methodology. 86 Fed. Reg. at 26,808 & 26,810. The IFR states that Treasury would consider "all relevant facts and circumstances" it deems relevant, "including information regarding planned spending cuts and budgeting assumptions" to determine the amount to recoup, if any. *Id.* at 26,810.

A number of states have challenged the Tax Cut Ban in federal court. NCLA filed *amicus curiae* briefs in support of lawsuits in the Northern District of Alabama and the Southern District of Ohio. These briefs are appended to this comment to provide further reasons why ARPA's Tax Cut Ban and Treasury's IFR interpreting it are unlawful. Most recently, the Southern District of Ohio held the Tax Cut Ban is unconstitutional and permanently enjoined Treasury from enforcing it against Ohio. *Ohio v. Yellen*, 2021 WL 2712220, at *2 (S.D. Ohio July 1, 2021).

III. THE STATE TAX CUT BAN VIOLATES ARTICLE I, SECTION 8'S SPENDING CLAUSE

The Tax Cut Ban disregards numerous restrictions on Congress' Article I, Section 8 Spending Power. *See* U.S. Const. art. I § 8. Among other deficiencies, the Tax Cut Ban is unconstitutionally ambiguous, coercive, and not reasonably related to ARPA's purposes. While mutually reinforcing, each of these defects is sufficient to render the Tax Cut Ban unconstitutional.

First, as the Southern District of Ohio held, the Tax Cut Ban is unconstitutionally ambiguous. *Yellen*, 2021 WL 2712220, at *15. A Spending Clause condition must provide sufficient clarity to make states "cognizant of the consequences" of accepting the funds, or else it is unconstitutionally vague. *South Dakota v. Dole*, 483 U.S. 203, 210 (1987). Here, it is impossible for states to determine the exact nature of the consequences associated with accepting ARPA funds. The mandate that states may not "indirectly offset a reduction in net tax revenue" is incurably ambiguous. *State of Ohio v. Yellen*, 2021 WL 1903908, at *12 (S.D. Ohio May 12, 2021) ("Despite poring over this statutory language, the Court cannot fathom what it would mean to indirectly offset a reduction in net tax revenue of a State"). Given this ambiguity, states cannot possibly "understand their obligations" and act according to them. *See Sch. Dist. of City of Pontiac v. Sec'y of U.S. Dept. of Educ.*, 584 F.3d 253, 277 (6th Cir. 2009).

Treasury's IFR cannot cure the Tax Cut Ban's unconstitutional vagueness because the requisite clarity of a Spending Condition must be supplied by "Congress," not an administrative agency. *Pennhurst State Sch. & Hosp. v. Halderman*, 451 U.S. 1, 17, (1981) (requiring that "Congress speak with a clear voice"); *Bennett v. Kentucky Dep't of Educ.*, 470 U.S. 656, 663 (1985) ("Congress must express clearly its intent to impose conditions."); *Com. of Va., Dep't of Educ. v. Riley*, 106 F.3d 559, 567 (4th Cir. 1997) (en banc) (adopting panel-stage dissenting opinion's conclusion that only the statutory language enacted by Congress, rather than an agency's regulation, matters for Spending Clause clarity purposes). Even if Treasury could cure the ambiguity with the IFR—which it cannot—the IFR only further complicates how to determine whether an unlawful, indirect offset has occurred. In particular, the power Treasury conferred on itself to consider "all relevant facts and circumstances" to determine if a state tax cut has been "paid for" using ARPA funds renders Treasury's system a black box for the states trying to navigate it. 86 Fed. Reg. at 26,808 and 26,810. In making tax and spending decisions, states have no way of knowing *ex ante* what facts and circumstances Treasury will fixate on to determine whether a reduction in the net tax revenue was "indirectly" paid for using ARPA funds. In other words, Treasury knows an indirect offset when it sees one. While this "standard" may pass muster with unelected bureaucrats in Washington who desire *carte blanche* control over state tax policy, it fails to clarify states' obligations in connection with accepting ARPA funds since Treasury will consider "all relevant facts"—without clearly defining ahead of time what Treasury might find relevant. Instead of curing the original constitutional defect, Treasury's IFR has only exacerbated the ambiguity problem. The Constitution demands clearer standards for spending conditions than

either ARPA or the innovations the IFR works on the ARPA scheme provide. *South Dakota*, 483 U.S. at 210.

Second, the Tax Cut Ban is unconstitutionally coercive. While Congress may condition federal funding, it may not use those conditions to coerce a state into "adopting a federal regulatory system as its own." *NFIB v. Sebelius*, 567 U.S. 519, 578 (2012). A condition is coercive when states have "no choice" but to accept the conditioned funding. *Id.* Congress, via ARPA, unconstitutionally coerces the states into adopting its preferred taxation framework by conditioning funds states have "no real choice" but to accept. *See id.* at 587. COVID-19 wreaked unprecedented fiscal damage to states and their budgets, making it impossible for states to refuse the funds.[1] Now, upon receipt of those funds, states can stave off economic damage and even enjoy temporary surpluses. This is unsurprising, since available ARPA funds represent "5% to more than 20% of annual spending" in each state.[2] In *NFIB*, the Supreme Court held that "[t]he threatened loss of over 10 percent of a State's overall budget … is economic dragooning that leaves the States with no real option but to acquiesce." 567 U.S. 519. ARPA funds represent the same or even greater levels of economic coercion and thus also present states with two options: economic ruin, or else accept the funds but acquiesce to Washington's current preference for higher taxation. This is not a real choice or "mild encouragement"— "it is a gun to the head." *NFIB*, 567 U.S. at 581. As a result, the condition is clearly coercive and exceeds the limit of Congress' ability to condition funding.

Finally, the Tax Cut Ban bears no reasonable relation to ARPA's purpose. *South Dakota*, 483 U.S. at 207 (observing that conditions on federal funding may be "illegitimate if they are unrelated… to the interest in particular national projects…"). ARPA funds must be used for a range of pandemic-related purposes, including, *inter alia*, responding to "negative economic impacts" by providing "assistance to households, small businesses, and nonprofits, or aid to impacted industries, such as tourism, travel, and hospitality." 42 U.S.C. § 802(c)(1)(A). Tax relief is one of the most obvious and direct means of providing such assistance to targeted groups, one that ARPA itself uses extensively.[3]

ARPA attempts to monopolize the tool of tax cuts so that the political benefits of providing those cuts flow only to the federal government's legislative and executive branches. This aim is clear from the fact that the federal stimulus monies provided through ARPA have been so highly

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[1] *See* The World Bank, *Covid-19 to Plunge Global Economy into Worst Recession since World War II* (June 8, 2020), WorldBank.org. For example, prior to the availability of ARPA funding, states cumulatively faced $127 billion in budget shortfalls and lacked the reserves to address them. Congressional Research Service, *State and Local Fiscal Conditions and COVID-19* (Dec. 7, 2020) Crsreports.congress.gov. Given that states, subject to varying restrictions, must balance their budgets, these shortfalls would have resulted in devastating budget crises with disastrous impacts to states and their populations. Josh Goodman, *How States Can Use Federal Stimulus Money Effectively* (May 11, 2021), PewTrusts.org.

[2] Barb Rosewicz, *How Far American Rescue Plan Dollars Will Stretch Varies by State* (June 28 2021), PewTrusts.org.

[3] ARPA contains countless tax cuts, including, *inter alia*, tax-free stimulus checks of up to $1,400 per person; health care tax credits; expanded child tax credits; additional child-and-dependent care tax credits; expansion of the earned income tax credit; and tax relief for individuals whose student loans were discharged. *See* Sidney Kess, Joseph Buble, and James R. Grimaldi, Tax Changes for Individuals in the American Rescue Plan Act, CPA Journal, June 2021.

touted. *See, e.g.*, White House, https://www.whitehouse.gov/american-rescue-plan/ (first blue plus-sign on the President's ARPA Plan: "$1,400 per-person checks"). But this political rationale does not equate to a rational basis under Article I for denying state tax relief to American families and businesses, particularly in light of the need for federalism to protect state spheres of autonomy. For the mere existence of federal "tax cuts for COVID" makes clear that the federal government does not object *as a general matter* to providing COVID relief by reducing tax burdens (a neutral principle); it just wants to make sure that the valuable tool of providing COVID relief via the tax code is *uniquely unavailable to the states*. Additionally, in light of this problem, it is even more irrational for the IFR to *expand on* the limited scope of the Tax Mandate as framed in ARPA's text. Yet, Treasury does exactly that by trying in the IFR to confer on itself the ability to engage in a case-by-case assessment of whether each state in any given year has cut its taxes *too much*, exposing such states to recoupment actions whenever its officials see fit.

Prohibiting states from providing tax-relief assistance is not merely unrelated to ARPA's core purpose, it actively undermines it. This contradiction is all the more stark considering that Congress took no steps to prevent fungible ARPA monies from being used to *indirectly* offset spending on any other purpose. In fact, the only other express restriction Congress placed on the expenditure of ARPA monies by states is that they cannot directly fund pension liabilities. *Id.* Conspicuously, though, a restriction on *indirect* funding of pensions is not present. *Id.* This demonstrates that states can use ARPA funds to indirectly finance spending unrelated to ARPA's purposes, including funding pensions, but not apparently to provide tax-relief "assistance to households, small businesses, and nonprofits." Thus, instead of imposing reasonable restrictions necessary to effectuate ARPA's purpose, Congress made state tax cuts *verboten* out of an apparent disdain for lower state taxes. Because the Tax Cut Ban bears no reasonable relation to ARPA's ostensible purposes and for the reasons set forth above, the Tax Cut Ban violates the Spending Clause.

IV. ALLOWING TREASURY TO INTERPRET THE STATE TAX CUT BAN VIOLATES THE NON-DELEGATION DOCTRINE

The Tax Cut Ban is an unconstitutional delegation of Congress' Spending Power. *See Whitman v. Am. Trucking Assocs.*, 531 U.S. 457, 473 (2001) ("Article I, Section 1, of the Constitution vests all legislative Powers … in a Congress … This text permits no delegation of those powers."). Congress may only delegate legislative power if it provides an "intelligible principle" an agency must adhere to when exercising the delegated legislative power. *Gundy v. United States*, 139 S. Ct. 2116 (2019). Here, Congress provided no such principle. Even worse, by failing to define "net tax revenue," when a state experiences a "reduction" in revenue "resulting from a change in law, regulation, or administrative interpretation," or to specify how Treasury should determine whether a reduction was "directly or indirectly offset" by ARPA funds, Congress has passed a "vague law" that "impermissibly" delegates these "basic policy matters" to Treasury. *See Grayned v. City of Ruckford*, 408 U.S. 104, 108-09 (1972). Treasury cannot define these terms itself, as doing so requires Treasury to use Congress' legislative power without an intelligible principle to guide the exercise. *F.C.C. v. Fox Television Stations, Inc.*, 556 U.S. 502, 536 (2009) ("Congress must clearly delineate the general policy an agency is to achieve and must specify the boundaries of the delegated authority") (cleaned up).

Treasury cannot cure the unconstitutional delegation with the Interim Final Rule. "The idea that an agency can cure an unconstitutionally standardless delegation of power" is "internally

contradictory." *Whitman*, 531 U.S. at 473. This is because "[t]he very choice of which portion of the power to exercise—*i.e.*, the prescription of the standard that Congress omitted—would itself be an exercise of … legislative authority." *Id.* The ambiguity in the condition described above means Treasury cannot discern Congress' intent for how the condition ought to be interpreted. Treasury's attempt to cure this ambiguity with the Interim Final Rule required it to choose interpretations among multiple competing possibilities, based solely on its own policy preferences. This choice, however, itself represents an exercise of Spending Clause power that Congress may not lawfully delegate to Treasury. Thus, Treasury's attempt to cure ARPA's ambiguities runs afoul of the non-delegation doctrine.

Even if some "intelligible principle" could be extracted from the Tax Cut Ban's incurably vague text—despite no such principle existing—Treasury still would lack authority to issue the IFR. The Tax Cut Ban presents questions of deep "economic and political significance," and if Congress intended for Treasury to answer such "major questions," it must say so clearly. *FDA v. Brown & Williamson*, 529 U.S. 120, 159 (2000). Any authority to infringe on state sovereignty, such as allowing Treasury to interpret the Tax Cut Ban, must also be made "plain to anyone reading the [statute]." *Gregory v. Ashcroft*, 501 U.S. 452, 467 (1991). ARPA contains no such clear statement empowering Treasury to decide "major questions" or infringe upon state sovereignty. As such, Treasury has not been delegated authority to issue the IFR. *Yellen*, 2021 WL 2712220, at *20 ("[E]ven assuming that Congress can outsource to an agency the obligation to provide the answers needed to meet the Spending Clause clarity requirement, Congress made no such delegation in ARPA.").

V. THE INTERIM FINAL RULE VIOLATES THE ADMINISTRATIVE PROCEDURE ACT

Treasury's choice of 2019 as the base year to determine whether a tax or spending cut has taken place violates the Administrative Procedure Act's prohibition against arbitrary and capricious decision-making. 5 U.S.C. Section 706(2)(A). An agency decision is arbitrary and capricious when it lacks a "rational connection" between the "facts found and the choice made." *Encino Motorcars, LLC, v. Navarro*, 136 S. Ct. 2117, 2125 (2016); *see also Fox*, 556 U.S. at 537 (explaining that it is a "duty of agencies" under the APA to provide a "reasoned explanation" for their policy choices). Here, no rational basis exists for requiring states not to fall below their tax revenue levels for 2019. *See* 86 Fed. Reg. at 26,823. Consider two states, A and B, that each experience the same reduction in tax revenue from $20 billion in 2020 to $18 billion in 2021. State A's 2019 revenue was $17 billion while State B's revenue was $19 billion. While both states experienced identical tax revenue reductions, only State B would be deemed to have experienced a tax reduction.

The IFR attempts to reconcile this nonsensical result by explaining that 2019 "is the last full fiscal year prior to the COVID-19 public health emergency." 86 Fed. Reg. 26,808. But that is irrelevant in defining the statutory text of "reduction in the net tax revenue." The IFR also states that 2019 is "consistent" with "ARPA sections 602(c)(1)(C) and 603(c)(1)(C), which identify the 'most recent full fiscal year of the [State, territory, or Tribal government] prior to the emergency'; as the comparator for measuring revenue loss." But those two provisions concern the use of ARPA funds to address shortfalls in tax revenue attributable to the COVID-19 pandemic and are wholly irrelevant in determining whether a prohibited tax cut occurs. The most natural way to measure changes in tax revenue is a year-to-year comparison. That is precisely how Treasury reports its

own receipt of tax revenue. The IFR contains no rational explanation for departing from this commonsense method and instead adopting 2019 as a baseline year.

The IFR's use of 2019 as a baseline is even more irrational in the context of determining whether a state may pay for tax cuts with its own spending cuts, thus obviating the need for any "indirect or direct offset" using ARPA funds. Such spending cuts must, however, be measured "relative to total spending for the recipient's fiscal year ending in 2019, adjusted for inflation." 86 Fed. Reg. at 26,810. Consider a state that increased spending on small business assistance from $80 million in 2019 to $100 million in 2020 to provide additional relief during the COVID-19 pandemic. If it now cuts spending back to $80 million, it could not use the $20 million spending cut to pay for a tax reduction because, under the IFR, spending did not decrease relative to 2019 levels. The IFR contains no answer for such an absurd outcome. This omission violates one of Treasury's most basic responsibilities under the APA, and it demonstrates the arbitrary nature of many of Treasury's choices in the IFR.[4]

VI. THE TAX CUT BAN UNDERMINES FEDERALISM AND ENCOURAGES ARBITRARY ENFORCEMENT

The Tax Cut Ban blatantly disregards tenets of federalism inherent in our constitutional order. *See NFIB*, 567 U.S. at 522-23 ("The Constitution simply does not give Congress the authority to require states to regulate …" and doing so "runs counter to this Nation's system of federalism."). Here, Congress' attempt to hijack state tax policy is particularly egregious. A "strong … principle" exists "against federal interference with state taxation." *National Private Truck Council, Inc. v. Oklahoma Tax Com'n*, 515 U.S. 582, 589 (1995). Faced with the ambiguity of the state Tax Cut Ban, states might choose to forgo tax cuts to avoid being hit with a ruinous recoupment action from Treasury.[5] In effect, the coercive influence of the Tax Cut Ban means Congress, and not the states, controls state taxation. The United States' system of federalism exists in large part to ensure a diffusion of sovereign power and prevent consolidation of policymaking in an omnipotent, potentially tyrannical, leviathan. *See New York v. U.S.*, 505 U.S. 144, 166 (1992) (Congress may not "outright coerce" the states); *see generally* Federalist No. 46 (Madison) (States retain strong "means of opposition" to "unwarrantable measure[s] of the federal government."). A unified system of state tax policy overseen by unelected, unaccountable bureaucrats at Treasury represents a grave, new threat to individual liberty and should be rejected. *See McCulloch v. Maryland*, 17 U.S. 316, 431 (1819) ("The power to tax involves the power to destroy"). The United States' system of federalism demands better than bad-faith attempts to commandeer state tax policy by unaccountable bean counters and bureaucrats seeking to impose their proclivity for excessive taxation on the states.

A particularly insidious aspect of the Tax Cut Ban is that Treasury retains substantial discretion as to how it will enforce it. Because executive enforcement choices are given deference

[4] The one percent *de minimis* standard Treasury has imposed is subject to the same critique. *See* 86 Fed. Reg. 26,808, 31 C.F.R. Part 35. Treasury states the one percent level "reflects historical effects of state-level tax policy changes in state EITCs implemented to effect policy goals other than reducing net tax revenues." 86 Fed. Reg. 26,809. But nothing in the statutory text of the Tax Cut Ban limits its application to reductions of net tax revenue that are intended as policy goals. To the contrary, the rest of the IFR's Tax Cut Ban provisions makes clear that it is the actual or anticipated *effect* rather than *intent* that matters when measuring tax revenue reductions. *Id.* at 26,823.

[5] *See* Jared Walczak, *ARPA's Tax Cuts Limitation Is a Problem for More States Than You Think* (April 5, 2021), TaxFoundation.org.

and are often non-reviewable, little would stop Treasury from exercising more scrutiny over states which are perceived to hold views dissenting from Treasury's pro-tax dogma. *See Heckler v. Chaney*, 470 U.S. 821, 833 (1985) ("[A]gency decision[s] not to take enforcement action should be presumed immune from judicial review under the" APA). This is especially true where an action is "committed to agency discretion by law." *Casa De Maryland v. U.S. Department of Homeland Security*, 924 F.3d 684, 697 (4th Cir. 2019). Given the ambiguities in the Tax Cut Ban described above, Treasury retains substantial discretion over how, when, and against which states it will choose to claw back funding or otherwise enforce it. Treasury's ability to arbitrarily enforce the Tax Cut Ban is not hypothetical—executive agencies possess a track record of harassing political enemies[6] and disregarding civil liberties.[7] It is not hard to imagine a scenario where Treasury would choose to exercise more oversight of compliance with this powerful spending condition against states perceived to be politically opposed to the White House. This policy reason alone requires that Congress provide clearer enforcement standards to ensure Treasury's oversight of the Tax Cut Ban is even-handed and not abused. No one watches over Treasury's enforcement decisions, and there is nowhere for a state to turn if that power is used for political or other illegitimate purposes.

CONCLUSION

For the above reasons, and those stated in the attached briefs that NCLA hereby incorporates by reference, NCLA opposes the Interim Final Rule.

Very truly yours,

/s/ Sheng Li

Mark Chenoweth, General Counsel
Sheng Li, Litigation Counsel
Peggy Little, Senior Litigation Counsel
Christian Clase, Law Clerk
New Civil Liberties Alliance

sheng.li@ncla.legal

[6] The Internal Revenue Service employed "'heightened scrutiny and inordinate delays' and demanded unnecessary information as it reviewed applications for tax-exempt status" of conservative leaning non-profits during President Obama's administration. Peter Overby, *IRS Apologizes for Aggressive Scrutiny of Conservative Groups* (Oct. 27, 2017), NPR.org.

[7] *See generally*, Philip Hamburger, IS ADMINISTRATIVE LAW UNLAWFUL? (2014).