NATIONAL TAXPAYERS UNION FOUNDATION

Issue Brief

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Six Lawsuits Filed to Challenge ARPA Ban on State Tax Cuts

Introduction

The federal ban on states cutting their taxes through 2024 is now being fought in federal courts across the country. Six lawsuits are currently pending challenging the restriction inserted into the American Rescue Plan Act (ARPA) that prohibits states from using funds to "directly or indirectly offset a reduction in the net tax revenue...or delays the imposition of any tax or tax increase" through 2024.[1] With states left unclear what policies might trigger the provision (although some have moved ahead with tax cuts anyhow), NTUF requested that the Treasury Department provide guidance to clarify the matter.[2]

Key Facts:

- **The federal ban on states cutting taxes until 2024, enacted in March 2021 as part of the American Rescue Plan Act, is being challenged in six federal courts**
- **Challengers and NTUF are making a strong argument that the provision is an unconstitutional condition and improperly commandeers state governments**
- **Judges are moving quickly in considering the cases, and Congress is also considering four bills to repeal the provision**

[1] American Rescue Plan Act of 2021, Pub. L. 117-2, Subtitle M, Section 9901, codified at 42 U.S.C. § 602(c)(2)(A). *See also* Bishop-Henchman, Joe. "Provision Added to Stimulus Bill to Halt State Tax Cuts." NTUF (Mar. 10, 2021), https://www.ntu.org/foundation/detail/provision-added-to-stimulus-bill-to-halt-state-tax-cuts.

[2] *See* Letter from Joe Bishop-Henchman to Janet Yellen, Re: Request for Guidance on Treasury Department Interpretation of American Rescue Plan Act State Tax Cut Provision, and Request for Timeline; Bishop-Henchman, Joe. "NTU Requests Clarification on State Tax Provision in American Rescue Plan." NTUF (Apr. 7, 2021), https://www.ntu.org/foundation/detail/ntu-requests-clarification-on-state-tax-provision-in-american-rescue-plan. *See also* Hammel, Paul. "Nebraska lawmakers pass a series of tax cuts, including one on Social Security." Omaha World-Herald (May 20, 2021), https://omaha.com/news/state-and-regional/govt-and-politics/nebraska-lawmakers-pass-a-series-of-tax-cuts-including-one-on-social-security/article_96e4ed56-b976-11eb-b0d2-9b28c052f6b4.html; Micheli, Chris. "COVID Relief Act: Federal Tax Conformity Bill Finally Passes CA Legislature." California Globe (Apr. 26, 2021), https://californiaglobe.com/section-2/covid-relief-act-federal-tax-conformity-bill-finally-passes-ca-legislature/; Associated Press, "Arkansas governor plans special session on income tax cuts." (Apr. 22, 2021), https://apnews.com/article/arkansas-business-government-and-politics-ee314b2e0d70986fe8a7575ec035c8ed; Gruber-Miller, Stephen. "Iowa Legislature moves to cut taxes, shift mental health care funding to the state." Des Moines Register (May 17, 2021), https://www.desmoinesregister.com/story/news/politics/2021/05/17/iowa-senate-passes-bill-cut-income-inheritance-property-taxes-move-mental-health-funding-to-state/5127079001/; Phillips, Mark. "[Arizona] Legislature begins its work on 2021-22 state budget, including the largest

Unfortunately, the resulting guidance cleared up some areas but not others.[3]

NTUF is filing briefs in each of the cases, making two key points: (1) the provision is so vague and ambiguous that its enforcement will be arbitrary, giving no fair notice as to what conduct is not permitted, and (2) the term "indirectly" is an unconstitutionally intrusive condition on state governments because money is fungible and budget allocations are a post-hoc accounting exercise, which means that any state that accepts federal funds and cuts taxes can be said to have "indirectly" used funds for that purpose.

The cases touch on two main areas of constitutional law.

First is the area of unconstitutional conditions, or the extent to which the federal government can impose restrictions on the use of federal funds provided to states. Under current U.S. Supreme Court precedent, Congress can impose conditions on federal funds, but only if the condition is related to a federal interest in a national project or program, the condition is unambiguous, and the condition encourages rather than coerces states to act. In *South Dakota v. Dole* (1987), the Supreme Court upheld a congressional condition that required any state that refused to raise the drinking age from age 18 to age 21 to forfeit 5 percent of federal transportation funds.[4] In *NFIB v. Sebelius* (2012), the Supreme Court struck down a congressional condition that required any state that refused to expand Medicaid to forfeit all federal Medicaid funds because it amounted to "economic dragooning that leaves the States with no real option but to acquiesce."[5]

Second is the anti-commandeering doctrine, which holds that Congress may not issue direct orders to state governments without violating the Tenth Amendment and blurring the lines of federalist structure and political accountability. In *New York v. United States* (1992), the Supreme Court struck down a federal law that required states to take title to nuclear waste within their borders if the state declined to participate in a federal regulatory program.[6] In *Printz v. United States* (1997), the Supreme Court held that a federal law that required local officials to implement gun control measures amounted to drafting local officials into federal service beyond what the Constitution permits.[7] In *Murphy v. NCAA* (2018), the Supreme Court struck down a federal law that banned states from allowing sports betting as an unconstitutional direct order to state governments.[8]

Cases

***State of Ohio v. Secretary, Department of Treasury* (No. 1:21-cv-00181)**

Filed on March 17 in federal court in Ohio, the lawsuit argues that Ohio has little choice but to accept the federal aid and the condition that goes along with it, and that the condition is so ambiguous as to be an impermissible exercise of congressional power and a Tenth Amendment violation for commandeering the power to set tax policy away from state officials.

Briefs were filed (including NTUF's brief), and on May 12, the judge denied Ohio's motion for preliminary injunction. The judge explained that Ohio is likely to win its case on the merits, since the phrases "indirectly offset" and "net tax revenue" have no discernible meaning and Congress cannot constitutionally offer the

tax cut in history." ABC 15 (May 24, 2021), https://www.abc15.com/news/region-phoenix-metro/central-phoenix/legislature-begins-its-work-on-2021-22-state-budget-including-the-largest-tax-cut-in-history; Vaughan, Dawn Baumgartner. "Tax cuts, child deduction and business relief on the table under NC Republican tax plan." News & Observer (May 25, 2021), https://www.newsobserver.com/news/politics-government/article251651868.html; 11Alive, "[Georgia] Gov. Brian Kemp signs $140 million state income tax cut." (Mar. 22, 2021), https://www.11alive.com/article/news/local/georgia-gov-kemp-tax-cuts/85-7100ff74-8ea5-48f6-895f-18690fcb32fd; Forman, Carmen."Three years ago lawmakers raised taxes. Now tax cuts are coming." Oklahoman (May 23, 2021), https://www.oklahoman.com/story/news/2021/05/23/oklahoma-tax-cuts-kevin-stitts-gives-final-approval/5127607001/.

[3] Bishop-Henchman, Joe. "Treasury Explains What State Tax Cuts are OK Under ARPA Provision." NTUF (May 11, 2021), https://www.ntu.org/foundation/detail/treasury-explains-what-state-tax-cuts-are-ok-under-arpa-provision.

[4] *South Dakota v. Dole*, 483 U.S. 203 (1987).

[5] *National Federation of Independent Business v. Sebelius*, 567 U.S. 519, 582 (2012).

[6] *New York v. United States*, 505 U.S. 144 (1992).

[7] *Printz v. United States*, 521 U.S. 898 (1997).

[8] *Murphy v. National Collegiate Athletic Association*, 584 U.S. ----, 138 S. Ct. 1461 (2018).

states money on ambiguous terms. However, the judge added, only a permanent injunction rather than a preliminary injunction would be a remedy that would protect Ohio's interests. On May 19, Ohio filed for a permanent injunction, with briefing to be completed by June 11.

***State of Arizona v. Yellen* (No. 2:21-cv-00514)**

Filed on March 25 in federal court in Arizona, the lawsuit makes two claims. First, it argues that the ARPA spending condition is ambiguous (as illustrated by contradictory interpretations of what it means) that states have no clear notice of the condition being placed on the federal funds.[9] Second, the prohibition on "indirectly" using the federal funds for tax purposes amounts to prohibiting the states "from cutting taxes in essentially any manner" in violation of the Tenth Amendment, exceeding what Congress can permissibly condition, intruding on the powers left to the states, and commandeering the policy processes of the states. The federal government's reply brief disputed whether Arizona suffered any harm if it was not considering any tax reductions.

Briefs have been filed (including NTUF's brief), and a hearing will be held on June 22.

***State of Missouri v. Yellen* (No. 4:21-cv-00376)**

Filed on March 29 in federal court in Missouri, the lawsuit contends that the word "offset" in the statute limits its scope only to direct uses of ARPA funds and any broader reading means the statute is unconstitutionally vague, imposes conditions unrelated to federal interests, constitutes federal coercion of the states, and amounts to commandeering of state policy.

Briefs were filed (including NTUF's brief), and on May 11, the judge dismissed the case on standing and ripeness grounds. In short, the judge assumed what he was supposed to determine: because ARPA cannot harm states, he cannot determine whether ARPA harms states. The judge explained that Missouri will face no harm unless it uses federal funds to offset a tax cut, and such a condition is permissible. Further, Missouri "has not sustained or is immediately in danger of sustaining some direct injury," and therefore the case is premature. In past Supreme Court cases evaluating unconstitutional conditions, not even dissenting justices have suggested a lack of standing or ripeness to dismiss the action.[10]

On May 18, Missouri gave notice that it is appealing to the U.S. Court of Appeals for the Eighth Circuit. The initial brief will be due July 7.

***State of West Virginia, et al. v. U.S. Department of the Treasury* (No. 7:21-cv-00465)**

Filed on March 31 in federal court in Alabama, this lawsuit is brought jointly by 13 states[11] and makes two arguments. First, the size of the funds involved (in many cases, over 20 percent of state budgets) and

[9] *See* Bishop-Henchman, Joe. "Guidance Is Needed to Prevent ARP From Overriding State Fiscal Policy." NTU (Mar. 24, 2021), https://www.ntu.org/foundation/detail/guidance-is-needed-to-prevent-arp-from-overriding-state-fiscal-policy.

[10] Indeed, the dissenters in the Affordable Care Act case specifically rejected a standing-based argument as unsound. See *NFIB v. Sebelius*, 567 U.S. at 696-97 (Scalia, J., dissenting) (holding that declining to hear the case on standing grounds "would be particularly destructive of sound government [because i]t would take years, perhaps decades, for each of its provisions to be adjudicated separately—and for some of them (those simply expending federal funds) no one may have separate standing. The Federal Government, the States, and private parties ought to know at once whether the entire legislation fails."). *See also id*. at 589 (Ginsburg, J., concurring in part, concurring in the judgment in part, and dissenting in part) (rejecting the state challenge to the federal statute on grounds other than standing); *South Dakota v. Dole*, 483 U.S. 203, 212 (1987) (Brennan, J., dissenting) (dissenting on the ground that the 21st Amendment reserves to the states the power to set alcohol policy and that a condition on a federal grant abridges that right); *Id*. (O'Connor, J., dissenting) (dissenting on the ground that drinking age is not reasonably related to transportation policy); *New York v. United States*, 505 U.S. at 188 (White, J., concurring in part and dissenting in part) (disagreeing with the majority on the grounds that New York consented to the requirements); *Id*. at 310 (Stevens, J., concurring in part and dissenting in part) (disagreeing with the anti-commandeering doctrine); *South Carolina v. Baker*, 485 U.S. 505 (1988) (upholding a federal statute of taxing state bonds with no justice raising standing as an issue). But see *Massachusetts v. Mellon*, 262 U.S. 447, 485 (1923) (denying standing to Massachusetts but conceding "[w]e need not go so far as to say that a state may never intervene by suit to protect its citizens against any form of enforcement of unconstitutional acts of Congress; but we are clear that the right to do so does not arise here.").

[11] Alabama, Alaska, Arkansas, Florida, Iowa, Kansas, Montana, New Hampshire, Oklahoma, South Carolina, South Dakota, Utah, and West Virginia. On May 19, the Wisconsin Legislature filed a motion to join the lawsuit. The federal government is opposing the motion, arguing that only the Wisconsin Attorney General make such an action on behalf of a state.

the lack of relationship between pandemic relief and restricting state tax authority (while allowing cities and tribal governments to cut taxes using ARPA funds) together create an unprecedented level of federal coercion of state policy. Second, Congress is imposing a forced mandatory tax policy on states in violation of the anti-commandeering doctrine of the Tenth Amendment.

Briefs have been filed (including NTUF's brief), with the last submitted on May 14.

Commonwealth of Kentucky, et al. v. Yellen **(No. 3:21-cv-00017)**

Filed on April 6 by Kentucky and Tennessee in federal court in Kentucky, the lawsuit makes four claims. First, the provision is hopelessly ambiguous, providing no clear notice to the states on linking tax policy with revenue impacts because causation is complex. Second, the provision's unequal application (forbidding states from using ARPA funds to cut taxes but allowing cities to do so) means it is not reasonably related to ARPA's stated interests. Third, the size of the federal aid and potential loss of funds is inherently coercive, particularly since the aid comes in a time of financial distress. Fourth, the provision violates the anti-commandeering doctrine by having the federal government direct state tax policy.

Briefing is currently underway.

State of Texas, et al. v. Yellen **(No. 2:21-cv-00079)**

Filed on May 3 by the states of Texas, Mississippi, and Louisiana, the lawsuit makes four claims. First, a choice to states to decline billions of dollars or cede the authority to set tax policy is coercive. Second, the provision is unconstitutionally broad since there is no limiting principle on how attenuated an "indirect offset" can get, and because it is also underinclusive in not restricting cities or tribal governments, it is not sufficiently related to ARPA's stated interests. Third, while the provision does not give a direct order to the states, it has the same effect and therefore violates the anti-commandeering doctrine. Fourth, by targeting only those states who seek to cut taxes, it violates a principle of equal sovereignty found in the Tenth Amendment.

Briefing has not yet commenced in the case.

Conclusion

Four bills have been introduced in Congress to repeal the ARPA provision: S. 730, sponsored by Sen. Mike Braun (R-IN) and seventeen co-sponsors; S. 743, sponsored by Sen. Mike Crapo (R-ID) and ten co-sponsors; H.R. 2002, sponsored by Rep. Dan Bishop (R-NC) and 54 co-sponsors; and H.R. 2189, sponsored by Rep. Kevin Brady (R-TX) and 26 co-sponsors. Passage of any of these bills would moot the various lawsuits and clear up continuing confusion.

The ARPA cases have been filed in six federal courts within six different appeals court jurisdictions. The likely legal strategy behind this capitalizes on the fact that the U.S. Supreme Court is more likely to agree to hear a case if the issue involves a "circuit split," or differing conclusions from various appeals courts. So far the judges have been considering these cases in a relatively expedited manner, and with the Missouri judge ruling for the federal government and the Ohio judge likely to rule for the state soon, the case may reach the Supreme Court by fall.

The issuance of Treasury Department guidance in May 2021 clarifies some implementation questions but ultimately does not address the broader constitutional issue raised by the lawsuits: whether Congress can

pass such a provision in the first place. Judges weighing that question must also decide whether they are evaluating the provision as enacted (with language using undefined and contradictory terminology) or with the more generous interpretation issued by Treasury officials.

About the Author

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