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Supreme Court Ruling on Maryland's Double Income Tax Could Impact Other States and Localities.

The U.S. Supreme Court has ruled that Maryland's local tax on out-of-state income is unconstitutional and amounts to double taxation, a ruling that could impact more than a dozen other states with similar local taxes.

In a divided 5-4 ruling issued Monday, the justices' reasoning relied heavily on the question of tax fairness for Maryland residents, concluding that "Maryland's tax scheme is inherently discriminatory and operates as a tariff." (The U.S. Constitution prohibits tariffs between states.) The court ruled Maryland's local tax on out-of-state income violated the Interstate Commerce Clause, adding that such a "tariff is the quintessential evil" targeted by the so-called dormant Commerce Clause principle.

Chief Justice John Roberts, and Justices Anthony Kennedy, Stephen Breyer, Samuel Alito and Sonia Sotomayor joined the majority opinion. Justices Antonin Scalia, Clarence Thomas, Ruth Bader Ginsburg and Elena Kagan dissented in three separate opinions.

At issue was a dispute between Maryland residents Brian and Karen Wynne and the state controller over local taxes levied by Howard County, where the Wynnes live. As a partial owner of a national health-care corporation, Brian receives income in dozens of states. Maryland, like every state that taxes income, gives a state income tax credit to residents for income earned out-of-state. But it doesn't give any credit for local taxes owed. This essentially means that the Wynnes and other Maryland residents pay taxes on their out-of-state income to the state where they work and the locality where they live.

In the 28-page majority opinion by Alito, the court picked apart the arguments made by Maryland that the tax was fair because residents can purportedly respond to unfair taxes at the ballot box. Alito soundly rejected that argument: "the notion that the victims of such discrimination have a complete remedy at the polls is fanciful," he wrote. Especially, he added, because only a distinct minority of the state's residents likely earn income out of state and therefore hardly amount to enough of a quorum to effect change.

Maryland also argued that any ruling against the state would compromise the state's taxing power and be an extreme action to accommodate people who want to live in Maryland but work elsewhere. But the court called that notion a "red herring," and said that the overall point is that the state's tax burden is higher and therefore unfair to those who earn out-of-state income.

In his dissenting opinion, Scalia disagreed with the ruling based on his belief that courts have too broadly interpreted the Constitution's Commerce Clause. "The Clause says nothing about prohibiting state laws that burden commerce," Scalia wrote, and was joined in the dissent by Thomas in calling the negative Commerce Clause a "judicial fraud." (Thomas also wrote his own dissent, joined by Scalia.)

Ginsburg, joined in dissent by Scalia and Kagan, argued that Maryland was justified in applying the

local tax to the Wynnes' out-of-state income because the Wynnes were residents and used local services and therefore all their income should be taxed by that locality. On the issue of fairness, Ginsburg noted that the other states that taxed the Wynnes' income also elected not to give them a credit for their county taxes, and wrote that "More is given to the residents of a State than to those who reside elsewhere, therefore more may be demanded of them."

It's unclear so far to what extent this ruling will impact localities in other states. Maryland's comptroller estimates that the state's counties will now owe a combined \$200 million in tax refunds to taxpayers across the state. A total of 16 other states have localities that also levy local income taxes but some may already give local tax credits for income earned out-of-state. For those that don't, some localities may try to distinguish between their case and Maryland's. That is, that Maryland's local taxes are collected by the state, which is subject to the Interstate Commerce Clause, and then redistributed back to localities. By contrast, localities in other states collect their own income tax and therefore could argue the Interstate Commerce Clause doesn't apply to them.

"I think that's guaranteed to be an argument localities put forward," said Alan D. Viard, a resident scholar and tax policy expert at the American Enterprise Institute. "But collecting taxes at the state or city level, in my mind, there's no distinction. People are going to have to actually look at these laws in detail and see how it actually affects them."

For any localities that are affected by the decision, said the Tax Foundation's Joseph Henchman, the solution is relatively straightforward. Either start offering a credit on out-of-state income or repeal the local tax.

He added that the 5-4 split decision would likely be the closest one issued by the court this term. That's because taxes typically get a lot of deference from judges who don't want to appear as if they are interfering with the elected branches on tax policy. In fact, Henchman, an attorney and policy analyst, was one of the many people who was surprised the court took up the case at all after the Maryland Court of Appeals ruled in favor of the Wynnes.

"There's a lot of power on the state and local government side for tax policy," he said. "So it's really important that what protections there are for taxpayers be very well guarded. And that's argument I think Alito made yesterday."

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