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# SUMMARY OF *AMICUS CURIAE* BRIEF BY THE D.C. AFFAIRS SECTION IN BANNER, ET AL. V. U.S., BEFORE THE SUPREME COURT OF THE UNITED STATES

The D.C. Affairs Section intends to join many former Bar presidents in a brief as *amici curiae* in support of Petitioners' petition for writ of certiorari.[1] The brief is similar to the brief filed by the Section and former Bar presidents with the District Court, which was recognized by U.S. District Judge Ellen Segal Huvelle as compelling, and in the United States Court of Appeals for the District of Columbia Circuit, and other business organizations are considering joining as additional *amici*.[2]

Petitioners' lead counsel is former Bar president John W. Nields, Jr., and he is joined by Section steering committee member Walter Smith. The brief was prepared by Joseph Rieser, Jr. and Joseph Price of Arent Fox. Section steering committee member Jon S. Bouker is of counsel. The D.C. Affairs Section is concerned with issues relating to the laws and government of the District of Columbia, has a longstanding interest in a strong, economically viable home rule in the District, and has filed *amicus curiae* briefs on other issues relating to home rule. The brief focuses on the fundamental principle of law that a jurisdiction has the legal authority to tax income earned within its borders. Denying the District, alone among all U.S. jurisdictions, the benefit of taxing all income earned within its borders requires judicial scrutiny. Because the District is prohibited from taxing the income of non-residents, it must attempt to make up for this lost revenue by "over-taxing" D.C. residents in order to address what the General Accounting Office concluded was a "structural imbalance" in the District's fiscal system. The *amici curiae* support Petitioners' challenge to the Prohibition and urge the Supreme Court to grant a writ of certiorari.

The Section is seeking clearance to file the brief on March 6. The steering committee has consented to filing the brief. Co-Chairs James S. Bubar and Charlotte Brookins-Hudson are of counsel.

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[1] The views expressed represent only those of the individual past presidents and the D.C. Affairs Section of the D.C. Bar and not those of the D.C. Bar or of its Board of Governors.

[2] The Section anticipates that there may be some non-substantive changes and that the amici joining on the brief could change. The brief is largely the same as the brief filed in the District and Circuit courts, so the argument can be made that this really is a "subsequent" statement of a previously filed brief. Nonetheless, the Section is circulating the brief.

## INTEREST OF THE AMICI CURIAE[1]

Amici are the District of Columbia Affairs Section of the District of Columbia Bar (the "D.C. Affairs Section"), former presidents of the District of Columbia Bar (the "former Bar presidents"), the Federation of Citizens Associations of the District of Columbia, the Washington, D.C. Federation of Civic Associations, the Federal City Council, the Greater Washington Board of Trade, and the Washington, D.C. Chamber of Commerce.[2]

The D.C. Affairs Section is concerned with issues relating to the laws and government of the District of Columbia, including the operation of the District under home rule. Its membership includes both individuals who live in the District and individuals who live elsewhere. The Federation of Citizens Associations of the District of Columbia was founded in 1910 and has over forty-five member associations, most of which have several hundred members. The purposes of the Federation are to work for the strengthening of residential communities and neighborhoods and to further the interests of the people of the District. The D.C. Federation of Civic Associations was founded in 1921 and represents over forty citizens and member associations. It is dedicated to informing, supporting, and representing the

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[1] The parties have consented to the filing of this brief under Supreme Court Rule 37.2, and their letters of consent have been lodged with the Clerk of the Court. Pursuant to Supreme Court Rule 37.6, *amici* state that counsel for a party did not author this brief in whole or in part and that no one other than *amici*, their members, or their counsel made a monetary contribution to the preparation or submission of this brief.

[2] With respect to the D.C. Affairs Section and the former Bar presidents, the views expressed herein are those of such Section and individuals, respectively, and not those of the D.C. Bar or of its Board of Governors.

residents of the District and is a recognized voice for the District's general welfare.

Amici have a keen interest in the economic health and well-being of the District of Columbia. In the case of the amici D.C. Affairs Section and former Bar presidents, such interest arises because the District is where its members, or they, as the case may be, practice or have practiced their profession. In the case of the Federation of Citizens Associations of the District of Columbia, it is because the District is where the members of its member organizations live. In the case of the Federal City Council, it is because its mission is to work for the improvement of the Nation's Capital.

All amici are concerned that the continued federal ban found at D.C. Code § 1-206.02(a)(5) on the District government's ability to tax the income of those who work in the District but live elsewhere (the "Prohibition") seriously threatens the economic vitality of the District of Columbia. Amici further believe that the District is treated inconsistently and unfairly when compared to all other states and territories that choose to impose an income tax.[3]

Although the District has managed to reverse the financial insolvency that prompted Congress to create a financial control board a decade ago, an in-depth study by

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[3] Some of the individual amici live and work in the District. Others work in the District but live elsewhere. Still others, by virtue of retirement or relocation, neither work nor live in the District. Consequently, the elimination of the Prohibition will most likely affect them in their respective capacities as individual taxpayers differently. Despite those differences, the individual amici join in submitting this brief because they share a common interest in the continued vitality of the District.

Congress' own investigative arm, the Government Accountability Office ("GAO") (formerly known as the General Accounting Office), shows that this recent fiscal success is not sustainable. According to the GAO, this bleak outlook is the result of a "structural imbalance" in the District's ability to raise revenue to provide basic services, a key aspect of which is the Prohibition. *See District of Columbia: Structural Imbalance and Management Issues*, GAO 03-666 (May 2003) at 8-9 (hereinafter "GAO Report"). Amici are deeply concerned that, because of this structural imbalance, the District will once again become fiscally insolvent or will be unable to provide an adequate level of basic governmental services. Either would be detrimental to the District's economy and well-being.

Amici also are troubled by the Prohibition's unfairness. The federal government does not impose a similar ban on any other jurisdiction in the United States. Consequently, each of the forty-one states that imposes an income tax on individuals applies that tax to nonresidents who work in the state. Moreover, the Prohibition was enacted at the behest of the representatives of the several States, which enjoy voting rights in the Congress of the United States, while the District does not. Just as importantly, the Prohibition – both in its own right and because the resulting structural imbalance contributes to an environment of uncertainty, inadequate services and decaying infrastructure – unfairly discriminates against the District in its effort to attract and retain residents and employers and to promote economic opportunity for its citizens.

Amici believe that the District's economic future is jeopardized by the Prohibition. Therefore, amici urge the Court to grant the petition for a Writ of Certiorari and review

the judgment of the United States Court of Appeals for the District of Columbia Circuit in this case.

## SUMMARY OF ARGUMENT

In the proceedings below, Petitioners raised serious questions about the constitutionality of the Prohibition. The amici agree with Petitioners that this case presents important issues that this Court should consider. Amici also agree with Petitioners that, if the Writ is granted, this Court should hold, after hearing this case, that heightened scrutiny is required and that the Complaint should be reinstated so that such scrutiny may be applied.

The arguments advanced here underscore two points in Petitioners' Brief. One is that the Prohibition, and the discrimination effected thereby, is unique. The second is that the Prohibition seriously undermines and jeopardizes the future fiscal health of the District because of its severe detrimental effect on the District's finances and ability to provide basic services. For both of these reasons, and in light of the District's singular importance as the Seat of Government, this case is worthy of the Court's review.

## ARGUMENT

### I. THE PROHIBITION IS THE ONLY LAW OF ITS KIND IN THE UNITED STATES.

#### A. The Universal Rule of Taxation is That Income is Taxed at Its Source.

It is fundamental that a jurisdiction can tax income earned within its borders. *See Oklahoma Tax Comm'n v. Chickasaw Nation*, 515 U.S. 450, 463 n.11 (1995); *Shaffer v. Carter*, 252 U.S. 37, 52 (1920); Jerome R. Hellerstein & Walter Hellerstein, *State Taxation* ¶ 6.03 (3d ed. 1999)

("There are two fundamental, but alternative, predicates for state power to tax income: residence and source."). This fundamental rule is rooted in the principle that the cost of government should be paid for by those who benefit from it. *See Oklahoma Tax Comm'n*, 515 U.S. at 463; *Shaffer*, 252 U.S. at 52-53.

For a state's residents, the "[e]njoyment of the privileges of residence in the state and the attendant right to invoke the protection of its laws are inseparable from responsibility for sharing the costs of government." *Oklahoma Tax Comm'n*, 515 U.S. at 463 (quoting *New York ex rel. Cohn v. Graves*, 300 U.S. 308, 313 (1937)). For nonresidents, the "very fact that a citizen of one state has the right to hold property or carry on an occupation or business in another is a very reasonable ground for subjecting such nonresident . . . to the extent of his property held, or his occupation or business carried on therein, to a duty to pay taxes . . . ." *Shaffer*, 252 U.S. at 53. Indeed, taxing income according to source is such a bedrock concept that the leading commentators on state taxation have noted that, if for Constitutional reasons (such as to avoid double taxation under the Commerce Clause) a choice had to be made between taxing by residence or by source, taxing by source would in their view trump taxing by residence. *See* Hellerstein & Hellerstein, *State Taxation* ¶ 6.03.

This Court first recognized the right of a jurisdiction to tax the income of nonresidents in 1920 in *Shaffer v. Carter*. Noting that a government may "resort to all reasonable forms of taxation in order to defray . . . government expenses" and that income taxes are a favored method of distributing the burdens of government, the Court held that a nonresident who holds a job or operates a business in a state has an *obligation* to pay for the cost of that state's

government, from which the nonresident benefits. *Shaffer*, 252 U.S. at 50-53.

### B. The Rule is Followed by the United States and Every State that Imposes an Income Tax.

As noted above, it is fundamental that a jurisdiction can tax the income earned within its borders. Just as importantly – and what makes the Prohibition so astonishingly unique – both the United States and every state that imposes an income tax exercise this authority.

Thus, the United States taxes the income of nonresidents earned within its borders, although the Executive Branch (with the consent of the Senate) may choose to limit this in bilateral treaties entered into with other countries. *See* 26 U.S.C. §§ 871(a) and 871(b) (taxation of nonresident individuals on interest, dividends, royalties, etc. and on trade or business income, respectively, derived from within the U.S.) and 26 U.S.C. §§ 881(a) and 881(b) (same for foreign corporations). Indeed, United States income tax statutes have provided for such taxation of nonresidents since at least 1894. *See* Joseph Isenbergh, *U.S. Taxation of Foreign Persons and Foreign Income* ¶ 30.2 (2002 ed.).[4] U.S. tax law specifically provides that (with some exceptions adopted for reasons not relevant here) income derived by a nonresident from the performance of services within the United States is subject to its income tax. *See* 26 U.S.C. § 864(b)(1).

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[4] Prof. Isenbergh, like Professors Hellerstein, is a leading authority in his field, and his treatise, like theirs, was cited by this Court in *Chickasaw Nation*.

Similarly, every state that has an income tax takes the same approach. That is, each such state has exercised the authority that this Court in *Shaffer* affirmed it had and taxed the income earned by nonresidents within its borders. *See* St. Tax Guide (CCH) ¶ 200 *et seq*. (listing state statutes authorizing taxation of all income earned within the state).[5] Even Puerto Rico and the Virgin Islands do so. *See* P.R. Laws Ann. 13 § 8605 (1995); 33 V.I. Code Ann. § 541 (1986). None – not a single one – gives nonresidents a "free pass."[6]

Indeed, the taxation of nonresidents on the income they earn within a jurisdiction is such a fundamental principle of public finance that it extends not just to those who travel every day from their home in one jurisdiction to their place of business in another but also to those who may have been in the jurisdiction only briefly. And taxing authorities can be quite vigorous in assuring that the tax is

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[5] To avoid overtaxing residents who work in other states, states typically provide their residents with a credit for the income tax they paid the state where the income was earned, up to the amount of tax such residents would otherwise have owed to their home state on such income. Maryland and Virginia are no different in this regard, since each would allow a credit against its income tax for income taxes paid to the District. *See Roach v. Comptroller of the Treasury*, 610 A.2d 754 (Md. 1992); *Mathy v. Dep't of Taxation*, 483 S.E.2d 802 (Va. 1997). So, the proposed nonresident income tax payable to the District would be offset by a credit against the income tax due to a nonresident's home state. (*See* Pet'rs Br. 8).

[6] To be sure, some states choose to enter into a treaty (a "reciprocal agreement") with some neighboring states whereby each agrees not to tax the wages or salaries earned by residents of the other. *See* St. Tax Guide (CCH), Charts ¶ 700-600 (Jan. 2005). States may decide whether to enter into a reciprocal agreement and presumably do so when it does not harm them economically and is to their administrative or other benefit.

collected on income earned during such brief stays, at least if the amount is enough to warrant the effort.

This is true with respect to U.S. income taxation. *See, e.g., Ingram v. Bowers*, 47 F.2d 925 (S.D.N.Y. 1931), *aff'd*, 57 F.2d 65 (2d Cir. 1932) (involving the royalties which the famed Italian singer Enrico Caruso received for recording a few songs at the New Jersey studio of The Victor Company pursuant to a 1909 agreement, which were subject to U.S. tax as payments for services performed in the U.S. even though derived in part from foreign record sales). *See also Johansson v. United States*, 336 F.2d 809 (5th Cir. 1964) (U.S. income taxation of the Swedish heavyweight boxer Ingemar Johansson on the purses he received from his celebrated prize fights with Floyd Patterson). And it is equally true with respect to state taxation. For example, the Commonwealth of Virginia has imposed its income tax on Tennessee residents who work at a hospital that straddles the Tennessee/Virginia border. *See* Tenn. Op. Atty. Gen., No. 84-193 (Tenn. A.G. 1984).[7]

Congress has denied only the District, alone among all U.S. jurisdictions, the benefit of taxing all income earned

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[7] For other examples of the lengths to which states are willing to go to tax nonresidents, *see* Richard R. Hawkins, Terri Slay & Sally Wallace, *Play Here, Pay Here: An Analysis of the State Income Tax on Athletes*, 26 State Tax Notes (Nov. 25, 2002) (reporting on a survey the authors conducted of state income taxation of visiting professional athletes and indicating that each of the twenty-five states which completed the survey stated that they taxed the income such visiting athletes earned when playing the state's home team(s)). *See also Speno v. Gallman*, 35 N.Y.2d 256 (1974) (nonresident employee of a New York business required to pay New York income tax on portion of salary attributable to days he worked from his home in New Jersey where employee's business activities were for his convenience, rather than for the convenience of the employer).

within its borders. Congress has not denied itself, or any other jurisdiction except the District, the right to tax income earned within its borders. The Prohibition is truly one of a kind.

## II. THE PROHIBITION HAS A SEVERE DETRIMENTAL EFFECT ON THE DISTRICT'S FISCAL HEALTH.

Because of the Prohibition, the District must over-tax D.C. residents in order to provide merely a basic level of public services. GAO Report at 12. Furthermore, the District's finances are constrained by a substantial "structural imbalance" that ensures the District's expenditures will constantly outpace the city's ability to raise revenue. *Id.* at 4, 12.

This annual structural deficit is beyond the control of the District's elected officials and amounts to between $470 million and $1.1 billion each year. GAO Report at 8, 12. Even if the District were to cut expenditures further, conduct operations as efficiently as possible, and impose higher taxes on its citizenry, the structural imbalance would remain. *Id.* at 15. And leading Washington area business and civic groups have all recognized that this structural imbalance has impaired the District's ability to attract new residents and businesses, provide necessary services, and maintain infrastructure. *See* Testimonies of Fred Thompson, President, Federal City Council, Ted Trabue of the Greater Washington Board of Trade, and Stephen J. Trachenberg, Chairman of the Board, D.C. Chamber of Commerce before the Subcommittee on the District of Columbia of the Senate Committee on Appropriations, June 22, 2004. Moreover, the GAO report illustrates that a key factor driving the structural

imbalance is the Prohibition.[8] GAO Report at 43. Because of the Prohibition, the District is unable to tax two-thirds of the income earned in the city, which amounts to over $30 billion annually. Pet. App. 69a-70a.

The Prohibition has a particularly insidious effect on the District's efforts to promote economic opportunity for its residents and grow its way out of any fiscal imbalance. As do other jurisdictions, the District attempts, through property tax abatements and other incentives, to persuade employers to remain or locate in the District. Because of the Prohibition, however, it competes on a less-than-level playing field in these efforts. Since so many of those who work in the District live in Maryland or Virginia,[9] much of the increased job opportunities and enhanced tax revenues resulting from the District's efforts inures to the benefit of the neighboring states, leaving it with only modest left-overs, such as income tax from the small fraction of employees living in the District, some sales tax on the employees' meals and sundries, and (if the employer is not an exempt institution) some income tax from the business. In other words, although the District expends the resources, because of the Prohibition it is the neighboring states that reap much of the reward.

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[8] Other constraints include: (1) the District's inability to tax 42% of the real property in the city because that property is owned by the federal government, foreign governments or international institutions; and (2) the limitation resulting from the federally-imposed height restrictions on D.C. structures on the District's ability to tax high-density real property. GAO Report at 43.

[9] The 2000 Census indicates that more than 2 out of every 3 jobs in the District are filled by non-residents. U.S. Census Bureau, *County-to-County Worker Flow Files*, at http://www.census.gov/population/www/cen2000/commuting.html#DC.

Thus, because of the Prohibition, the District truly faces a catch-22 dilemma. Either it does nothing to attract and retain employers in the face of constant criticism to do more, or it does what it can even though much of the benefit will flow to its neighbors.[10] Accordingly, the suggestion in the Opinion of the Court of Appeals that the Prohibition may have been prompted by a concern that, otherwise, employers might decide to move out of the District rather than subject those of their employees who do not live in the District to the District's high tax rates (*see* Pet. App. 11a) is quite ironic and misperceives what is the cause and what is the effect: it is not that high rates caused the Prohibition; rather, as shown in the GAO Report and Petitioners' Brief, it is the Prohibition that has caused high rates.

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[10] Consider, for example, the debate over the last few years regarding the relocation of a Major League Baseball team to Washington, D.C. The mean baseball team payroll is approximately $69,000,000. USA Today, Inc., *USA Today Salaries Database*, at http://asp.usatoday.com/sports/baseball/salaries/totalpayroll.aspx?year=2005. Many states apportion a team member's income based on "duty days" and apply a rule that there are roughly 220 duty days in a baseball season. Thomas Heath & Albert Crenshaw, *In Professional Sports, States Often Claim Players*, *Wash. Post*, Feb. 24, 2003, at D1. In a 162-game season, there would be 81 games in the District. Assuming there are 85 duty days in the District for home team players and personnel, 81 duty days for visiting team players and personnel, and an average payroll for both the visiting and home teams, this would yield a tax base of approximately $52,063,000 ([81+85)/220] x $69,000,000). If the Prohibition did not apply and the District could tax this income, and if you applied an average tax rate on this income of 7% - for 2005, the District's highest marginal tax rate was 9% on taxable incomes over $30,000 – this would yield annual revenue of $3,644,000, which would produce $109,000,000 over 30 years. Whatever may be the merits of a new baseball stadium – on which amici intend no comment – the debate over those merits would likely have been much different if this revenue stream had been available to help underwrite the stadium's cost.

Removal of the Prohibition would permit a significant reduction in the structural imbalance and would place the District in the same position as other taxing jurisdictions that can tax income at its source. Nonresidents who work in the District benefit from public safety and public works-related services provided by the District. As an example, approximately eighty percent of all of the cars that benefit from the District's infrastructure are from Maryland and Virginia, yet the District cannot tax the income of car owners who work in the District to help pay for road maintenance. 148 Cong. Rec. E311 (daily ed. Mar. 11, 2002). As the Supreme Court noted in *Shaffer*, nonresidents who earn a living in a jurisdiction and benefit from governmental services in that jurisdiction have an obligation to contribute to the costs thereof. The Prohibition creates an unfair and discriminatory exception to this rule with respect to the District.

## CONCLUSION

The Prohibition constitutes a unique departure from the rule that is otherwise generally applied that income can and will be taxed at its source. Furthermore, as outlined in the GAO Report, the Prohibition jeopardizes the District's financial health. For these reasons, and for those stated in Petitioners' Brief, the amici urge the court to grant a Writ of Certiorari as requested by Petitioners.

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