Case No. 21-6108

UNITED STATES COURT OF APPEALS
FOR THE SIXTH CIRCUIT

COMMONWEALTH OF KENTUCKY, and

STATE OF TENNESSEE

Plaintiffs-Appellees

v.

JANET YELLEN,
in her official capacity as
Secretary of the Treasury, *et al.*

Defendants-Appellants

On Appeal from the United States District Court
for the Eastern District of Kentucky
Case No. 3:21-cv-00017

BRIEF FOR THE COMMONWEALTH OF KENTUCKY AND STATE OF TENNESSEE

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STATEMENT REGARDING ORAL ARGUMENT

The Appellee States request oral argument. While the States do not disagree that there are overlapping issues between this case and *Ohio v. Yellen*, No. 21-3787, the record here is significantly different and the issues are not identical. The Appellee States thus request oral argument regardless of panel assignment.

STATEMENT OF JURISDICTION

The district court had subject-matter jurisdiction under 28 U.S.C. § 1331 because the plaintiffs asserted claims arising under federal law. [Amend. Compl., R.23, PageID#148–55]. The district court granted the plaintiffs' motion for summary judgment and entered a final judgment on September 24, 2021. [Op. & Order, R.42, PageID#644; Judgment, R.43, PageID#645–46]. The defendants appealed that order on November 22, 2021. [Notice of Appeal, R.45, PageID#648–50]. This Court has jurisdiction under 28 U.S.C. § 1291 over final judgments from the United States District Court for the Eastern District of Kentucky.

STATEMENT OF ISSUES

The district court permanently enjoined enforcement of a federal statute that effectively prohibits the States from lowering their taxes or else lose billions of dollars in federal Covid-19 relief. The issues presented are:

1. Whether the States have Article III standing to challenge an ambiguous and coercive condition under the Spending Clause that invades their sovereign interest in controlling their own tax policies.

2. Whether the district court correctly held that Congress's offer of billions of dollars in financial aid during a once-in-a-century pandemic unconstitutionally coerces the States into giving up their sovereign authority over state tax policy.

3. Whether the district court's permanent injunction should be affirmed on the alternative ground that the prohibition restricting the States from using federal funds to "indirectly" offset revenue losses is unconstitutionally ambiguous.

4. Whether the district court's permanent injunction should be affirmed on the alternative ground that the prohibition restricting the States from using federal funds to "indirectly" offset revenue losses unconstitutionally intrudes on the traditional powers of the States reserved under the Tenth Amendment.

STATEMENT OF THE CASE

The American Rescue Plan Act provides the States with almost two hundred *billion* dollars to combat the effects of Covid-19. But it comes with a price. To accept the funds, the States must agree to an incomprehensible condition that effectively prohibits the States from lowering their taxes. This case is about whether that condition is constitutional.

The American Rescue Plan Act. President Biden signed the American Rescue Plan Act of 2021, Pub. L. No. 117-2, into law on March 11, 2021. This was Congress's sixth major relief effort since the pandemic began in early 2020. All told, the Rescue Plan cost taxpayers almost $2 trillion. And of that $2 trillion, Congress returned about $195 billion directly to the States (the District of Columbia included). 42 U.S.C. § 802(b)(3).

The States can spend their Rescue Plan funds on four broad categories of Covid-related expenses. *Id.* § 802(c)(1). First, the States can use the money to provide assistance to several groups and industries affected by the pandemic—households, small businesses, nonprofits, etc. *Id.* § 802(c)(1)(A). Second, the States can fund salary increases ("premium pay") for employees "that are performing . . . essential work." *Id.* § 802(c)(1)(B). Third, the States can use Rescue Plan funds to make up for any revenue losses caused by the pandemic. *Id.* § 802(c)(1)(C). And

fourth, the States can make "investments in water, sewer, or broadband infrastructure." *Id.* § 802(c)(1)(D). Although broad, these four categories define the universe in which the States can use Rescue Plan funds.

Kentucky and Tennessee expect to receive Rescue Plan funds equal to roughly *one-fifth* of each State's general-fund revenue from the prior fiscal year. That is a little more than $2.1 billion for Kentucky, [Amend. Compl., R.23, PageID#140 (¶ 26)], and about $3.725 billion for Tennessee, [Niknejad Decl., R.25-2, PageID#221 (¶ 5)].

These funds are critical for many States as they work toward rebuilding their economies. Kentucky spent some of its money before the funds even came in. It earmarked Rescue Plan funds to address its unemployment crisis, to invest in infrastructure improvements, and to mitigate other effects of Covid-19. *See* 2021 Ky. Acts. ch. 171, § 3; 2021 Ky. Acts ch. 194, §§ 11, 15, 16, 17; 2021 Ky. Acts ch. 195, § 1; 2021 Ky. Acts ch. 196, §§ 4, 6. That list includes repaying hundreds of millions of dollars in debt that Kentucky accumulated on extended unemployment services during the pandemic. 2021 Ky. Acts ch. 196, § 6. Each of these legislative initiatives falls into one of the four categories of permissible expenditures described in § 802(c)(1).

The Tax Mandate. It is not enough, however, that the States spend their Rescue Plan funds only on the items listed in § 802(c)(1). The Rescue Plan also requires that the States refrain from lowering their taxes during any of the years that they spend the federal money.

It accomplishes this through an opaque restriction on how the States "use" their funds—the Tax Mandate. Under § 802(c)(2)(A), the States are prohibited from using Rescue Plan funds to "directly or indirectly offset a reduction in [their] net tax revenue" caused by "a change in state law, regulation, or administrative interpretation." In other words, if the States change their tax laws in a way that lowers the tax burden on their citizens, the Rescue Plan prohibits the States from using federal funds to "indirectly" offset any revenue losses.

But the statute does not further define what it means to "indirectly" offset a loss in tax revenue. Nor does it identify the starting point from which the States must measure any reduction in their "net tax revenue." Those critical terms are left to the imagination, as the full provision states only the following:

> A State or territory shall not use the funds provided under this section or transferred pursuant to section 803(c)(4) of this title to either directly or indirectly offset a reduction in the net tax revenue of such State or territory resulting from a change in law, regulation, or administrative interpretation during the covered period that reduces any tax (by providing for a reduction in a rate, a rebate, a deduction, a credit, or otherwise) or delays the imposition of any tax or tax increase.

Id. § 802(c)(2)(A).

Because the statute does not define these key terms, it is impossible to explain how the Tax Mandate operates. Consider one example: A State spends Rescue Plan funds on healthcare infrastructure—a "use" squarely within the parameters of § 802(c)(1). But suppose that at the same time, the State reduces its budget for its department of corrections and provides a tax credit to individuals who suffered economic harm from the pandemic—both in amounts equal to what it spent on healthcare infrastructure. Because money is fungible, the Tax Mandate provides no way to discern whether the State "indirectly" offset the tax credits with the Rescue Plan funds or by cutting its budget for corrections. The answer could be either. Or neither, if the State made similar expenditures and budgetary changes elsewhere. It is simply impossible to know.

This problem led a group of States to seek guidance from Treasury soon after the Rescue Plan became law. But Treasury had no answer. Secretary Yellen had herself admitted that the fungibility of money raised "thorny questions" about

what the Tax Mandate means.[1] And when pressed by the States, Secretary Yellen failed to explain the scope of these terms.[2] [Letter, R.23-2, PageID#164–65].

The immediate effect on the States. The Tax Mandate created immediate budgeting issues for the States. Tennessee exemplifies the problem. The State has a long history of cutting taxes to spur economic growth. [Niknejad Decl., R.25-2, PageID#222 (¶ 6)]. In the last decade, Tennessee has enacted dozens of tax cuts, the fiscal impact of which likely exceeds "$800 million in budgeted revenue reductions." [*Id.*]. Those tax-relief efforts include reducing the sales tax rate on groceries, repealing the inheritance tax, and removing 15 categories of licensed professions from burdensome professional-privilege taxes. [*Id.* at PageID#222–23 (¶¶ 7–8)]. Tennessee has also considered other kinds of tax relief—such as a

[1] Treasury Secretary and Federal Reserve Chair Testimony on COVID-19 Economic Recovery at 58:20–59:03, *available at* https://www.c-span.org/video/?510059-1/treasury-secretary-federal-reserve-chair-testimony-covid-19-economic-recovery (Mar. 24, 2021).

[2] Treasury eventually published an Interim Final Rule related to the Tax Mandate. *See* Coronavirus State and Local Fiscal Recovery Funds, 86 Fed. Reg. 26,786 (May 17, 2021) (codified at 31 C.F.R. Part 35). It then followed that interim rule with a Final Rule. *See* Coronavirus State and Local Fiscal Recovery Funds, 87 Fed. Reg. 4,338 (Jan. 27, 2022). Treasury conceded below that any rulemaking cannot cure the constitutional deficiencies of the statute. [Mot., R.31, PageID#360 ("[A]gency regulations should have no bearing on the Spending Clause analysis.")].

complete phase out of the professional privilege tax—but the Covid-19 pandemic delayed action on those proposals. [*Id.* at PageID#223 (¶ 9)].

The Tax Mandate threatens to stall Tennessee's efforts even longer. Because the Tax Mandate's reach is both ambiguous and potentially sweeping, the risk of an enforcement action after spending Rescue Plan funds means the State must necessarily defer, slow, or reconsider some of its taxing decisions for several years. [*Id.* at PageID#225 (¶ 14)]. This effectively limits the State's ability to enact its preferred tax cuts that are necessary to ensure long-term economic growth, [*id.* (¶ 15)], even when those tax cuts have nothing to do with Covid-19 or how Tennessee otherwise spends its Rescue Plan funds.

On top of that, the Tax Mandate will cost States like Tennessee money. Tennessee does not ordinarily account for "forgone" revenue in its budgeting process—revenue the State does not receive because it delays implementing a scheduled tax or tax increase. [Eley Decl., R.25-3, PageID#229–30 (¶ 6)]. But under the Tax Mandate, it must do so. 42 U.S.C. § 802(c)(2)(A). That means Tennessee will have "to develop additional processes to identify and account for any bills that are scored as causing '[forgone]' revenue and to ensure that such bills are 'paid for' in the budgeting process by other sources of state revenue." [Eley Decl., R.25-3, PageID#230 (¶ 6)]. This requires "[reallocating] the time of existing

staff or [hiring] additional staff." [*Id.*]. Either way, complying with the Tax Mandate will cost Tennessee money.

Nor is that the only way it does so. Tennessee currently has no process in place for determining whether a specific source of funds pays for a specific expenditure. [*Id.* at PageID#231 (¶ 8)]. Instead, when Tennessee balances its budget, it compares only "total expenditures to total revenues." [*Id.*]. The State "does not typically connect expenditures to specific revenue" in the way the Tax Mandate contemplates. [*Id.*]. So Tennessee will have "to create new accounting processes that specifically track whether federal funds received under the Rescue Plan are being used to 'directly or indirectly offset' any state expenditures resulting from a reduction in tax revenue." [*Id.*]. That "will require at least one budget analyst and one revenue analyst to divert at least some of their work to that task"—again, costing Tennessee money. [*Id.* at PageID#232 (¶ 8)].

This lawsuit. Because they faced immediate harm, the Commonwealth of Kentucky and the State of Tennessee sued the defendants[3] to prevent them from enforcing the Tax Mandate. [Compl., R.1, PageID#1–25]. The States challenged

[3] The defendants are the Department of Treasury, Treasury Secretary Yellen, and the Treasury Department's Acting Inspector General, Richard K. Delmar. [Amend. Compl., R.23, PageID#130, 135–36 (¶¶ 15–17)].

the Tax Mandate on two fronts. First, the States argued that the Tax Mandate violates the Spending Clause, which prohibits Congress from imposing ambiguous or coercive conditions on federal funds. *See South Dakota v. Dole*, 483 U.S. 203, 207–10 (1987). The Tax Mandate is both. Second, the States argued that the Tax Mandate violates the anti-commandeering doctrine by using Congress's spending authority to co-opt an essential feature of State sovereignty—the power of a State to set its own tax policies.

After cross-motions on all the claims, the district court entered summary judgment in the States' favor. The court held that the Tax Mandate is unconstitutionally coercive. [Op. & Order, R.42, PageID#628, 632–39]. The court explained that "the federal government overstep[ped] its bounds" by "unduly influenc[ing] the States' power to set their own tax policies" in the midst of a once-in-a-century pandemic. [*Id.* at PageID#639]. Because "the spending power of the federal government does not go so far," [*id.* at PageID#628], the district court entered a permanent injunction prohibiting the defendants from enforcing § 802(c)(2)(A) against Kentucky or Tennessee, [*id.* at PageID#644]. The court declined to address the States' other claims—finding it unnecessary given the permanent injunction. [*Id.* at PageID#639–40].

Treasury then filed this appeal. [Notice of Appeal, R.45, PageID#648–50].

SUMMARY OF ARGUMENT

I. The States have Article III standing for three separate reasons.

First, the uncontroverted evidence below establishes that Tennessee will incur administrative costs to comply with the budgeting and accounting requirements of the Tax Mandate. Those costs are directly traceable to the Tax Mandate, which requires the States to account for expenditures and revenue losses that Tennessee is not capable of determining using its already-existing administrative processes.

Second, the Tax Mandate invades the sovereign interests and traditional prerogative of the States to set their own tax policies. While Congress tried to style the Tax Mandate as nothing more than a restriction on how the States spend federal dollars, the broad and ambiguous language effectively prohibits the States from lowering their taxes during the covered years.

Third, the States satisfy the ordinary requirements for pre-enforcement review. Both Kentucky and Tennessee have established an intent to lower the tax burden on some of their citizens, doing so is arguably prohibited by the Tax Mandate, and there is every reason to believe the Treasury Defendants will enforce the statute.

II. The Tax Mandate violates the Spending Clause for two reasons.

First, the Tax Mandate is unconstitutionally coercive. The sheer size of the federal aid in light of a once-in-a-century pandemic puts the States in an untenable position. The Treasury Defendants, for their part, do not even dispute that is coercive. Instead, they argue only that the Spending Clause's prohibition against coercive offers does not apply when Congress merely restricts how federal funds are used. But the Tax Mandate is not a restriction on the "use" of federal money. Its broad and ambiguous language effectively prohibits the States from lowering their taxes because every Rescue Plan expenditure could be deemed an indirect offset of a revenue reduction. The fact that Congress styled this sweeping prohibition as a "use" restriction is immaterial to the analysis. The Tax Mandate's *effect* is to do much more than simply require the States to spend their federal funds in a particular way.

Second, the Tax Mandate is also unconstitutionally ambiguous. Because money is fungible, the statute's restriction on "indirectly" offsetting revenue reductions is impossible to understand. Every expenditure of Rescue Plan funds could be deemed to "indirectly" offset a revenue loss. And that means the Treasury Defendants have virtually limitless discretion to decide whether a State has violated the Tax Mandate if it has lowered its revenue while also spending the federal funds. On top of that, the Tax Mandate is similarly opaque as to how the

States should measure revenue reductions. That is no small matter. The core premise of the Tax Mandate requires knowing whether changes in state law caused revenue losses—but the Tax Mandate provides no guidance as to the baseline from which to measure such a reduction, or how to account for the predictive (and unpredictable) nature of revenue adjustments. The Spending Clause requires Congress to provide the States with more clarity before subjecting them to such conditions.

III. The Tax Mandate violates the anti-commandeering principles embodied in the Tenth Amendment. The Constitution divides power between the States and the federal government, leaving to the States authority over certain core sovereign interests. The power to tax (or not to tax) is one of those interests. Congress cannot use its enumerated powers—including the Spending Clause—to direct the States to adopt the federal government's preferred policy choices on issues like taxation. Doing so blurs the lines of political accountability on an issue central to the structural divide of power embodied in our Constitution.

STANDARD OF REVIEW

This Court "give[s] fresh review to the district court's application of [the summary judgment] standard" as a matter of law. *Arrington-Bey v. City of Bedford Heights, Ohio*, 858 F.3d 988, 992 (6th Cir. 2017) (citation omitted). That means the Court must decide whether "there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law." Fed. R. Civ. P. 56(a).

ARGUMENT

I. The States have standing.

The Treasury Defendants argue that the States lack Article III standing. To establish standing, the States must show they will suffer (1) an injury in fact (2) that is traceable to the unlawful conduct and (3) is redressable by the court. *Kentucky v. Biden*, 23 F.4th 585, 601 (6th Cir. 2022). Though the Treasury Defendants never explain which of these elements is lacking, they appear to dispute that the Tax Mandate causes the States an injury in fact. They are wrong.

The States have Article III standing for three reasons. First, the Tax Mandate imposes pocketbook injuries in the form of administrative costs—a "paradigmatic" injury in fact. *Danvers Motor Co. v. Ford Motor Co.*, 432 F.3d 286, 291 (3d Cir. 2005) (Alito, J.). Second, the Tax Mandate invades the "sovereign interests and traditional prerogatives" that States have in setting their own tax policies without federal influence. *See Kentucky*, 23 F.4th at 602. Third, the States face the realistic probability that the federal government will enforce the Tax Mandate against them. Any one of these three theories of standing satisfies Article III.

A. The Tax Mandate imposes administrative costs.

The easiest answer to the standing question is that the Tax Mandate imposes pocketbook injuries. The record establishes that Tennessee will suffer economic losses (in the form of administrative costs) that are directly traceable to the Tax Mandate. So Tennessee has Article III standing to challenge the law's legality.[4] *See Dep't of Com. v. New York*, 139 S. Ct. 2551, 2565 (2019).

Economic harm is a "paradigmatic" injury in fact. *Danvers Motor*, 432 F.3d at 291. That is true for a State as it is for any other plaintiff. *See Dep't of Com.*, 139 S. Ct. at 2565. When a federal law will cause a State to lose money through "diversion of resources," the State has standing to challenge its constitutionality. *See id.* And "[f]or standing purposes, a loss of even a small amount of money is ordinarily an injury." *Czyewski v. Jevic Holding Corp.*, 137 S. Ct. 973, 983 (2017) (quotation marks omitted).

Tennessee's evidence on this issue is "uncontroverted." *See Online Merchs. Guild v. Cameron*, 995 F.3d 540, 548 (6th Cir. 2021). Tennessee does not currently have the administrative processes in place to comply with the Tax Mandate, and so it will have to spend additional resources to do so. For example, Tennessee's

[4] It is well-established that the standing of a single plaintiff creates Article III standing. *Rumsfeld v. Forum for Acad. & Inst. Rights, Inc.*, 547 U.S. 47, 52 n.2 (2006).

budgeting process does not calculate revenue losses when a new law delays implementing a tax or tax increase. [Eley Decl., R.25-3, PageID#229–30 (¶ 6)]. That means Tennessee has no way of identifying legislation that causes such a revenue loss—something that the Tax Mandate requires it to do. 42 U.S.C. § 802(c)(2)(A) (including within its scope revenue losses caused by "delays" in implementing taxes). So to comply, Tennessee must spend additional resources to develop new administrative processes. That pocketbook injury satisfies Article III. *See Dep't of Com.*, 139 S. Ct. at 2565; *Online Merchs. Guild*, 995 F.3d at 547–48.

And that is not all. Tennessee's budgeting process also has no mechanism to "connect expenditures to specific revenue sources" in the way that the Tax Mandate requires. [Eley Decl., PageID#231 (¶ 8)]. Instead, Tennessee balances its budget by simply comparing "total expenditures to total revenues." [*Id.*]. So Tennessee will have "to create new accounting processes that specifically track whether federal funds received under the Rescue Plan are being used to 'directly or indirectly offset' any state expenditures resulting from a reduction in tax revenue." [*Id.*]. Again, that costs Tennessee resources, [*id.* at PageID#232 (¶ 8)], which is an Article III injury, *Dep't of Com.*, 139 S. Ct. at 2565; *Online Merchs. Guild*, 995 F.3d at 547–48.

The Treasury Defendants make only two cursory responses. [Br. at 9–10]. They do not dispute that the kinds of costs Tennessee will incur are enough to establish standing in a Spending Clause case.[5] Rather, they argue that Tennessee's costs are traceable to a different part of the Rescue Plan—not the Tax Mandate. And they argue that Tennessee need not incur those costs anyway. Both arguments—which the Treasury Defendants spend only three sentences developing—simply ignore the evidence presented below.

First, they argue that the administrative costs are not traceable to the Tax Mandate because the States have an independent obligation to "keep track of their expenditures" and report them back to Treasury under § 802(d)(2). [Br. at 9]. But Tennessee's costs do not arise because of the reporting requirement. Rather, the Tax Mandate imposes costs on Tennessee because it requires Tennessee to track

[5] The district court below raised a question about whether the States have standing given that their injuries are allegedly self-inflicted because they arise only if the States "decid[e] to take the money." [Oral Arg. Tr., R.41, PageID#580]. The Treasury Defendants have not raised that argument here, and they declined to press it below as well. For good reason: That argument would render the constitutional limits on the Spending Clause illusory because no State could challenge an unlawful condition. Yet the point of the Supreme Court's Spending Clause precedent is that the States have a right to accept federal funds without being constrained by unconstitutional conditions that Congress attaches. *See Sch. Dist. of Pontiac v. Sec'y of U.S. Dep't of Educ.*, 584 F.3d 253, 278 (6th Cir. 2009) (en banc) (plurality op.); *id.* (Sutton, J., concurring).

and calculate changes in the State's revenue that Tennessee would not otherwise account for. Without the Tax Mandate, Tennessee is not required to calculate delayed revenue for its budgeting process, nor is it required to identify how specific revenue losses will be paid for by specific sources other than Rescue Plan funds. Those additional administrative tasks are independent of the reporting requirements in § 802(d)(2). They are directly traceable to the Tax Mandate.

Second, the Treasury Defendants argue that Tennessee will not suffer these administrative costs because the Treasury Department "has made clear . . . that States may rely on their existing budget projections in determining the anticipated revenue effects of changes to their tax laws." [Br. at 9 (citing 86 Fed. Reg. at 26,807)]. But the Treasury Defendants do not even try to explain how that statement makes sense. Tennessee's undisputed evidence establishes that it is *impossible* to determine the necessary revenue effects using its established budgeting processes. It is no answer to that evidence for the Treasury Defendants to wave their hands and claim otherwise.

Tennessee's expected administrative costs from the Tax Mandate are "uncontroverted." *See Online Merchs. Guild*, 995 F.3d at 548. That establishes Article III standing, *see Dep't of Com.*, 139 S. Ct. 2565, and the Court need not go further.

B. The Tax Mandate harms the States by intruding on their sovereign authority to set tax policy.

The States also have Article III standing because the Tax Mandate threatens to "invade[]" their "sovereign interests and traditional prerogatives." *Kentucky*, 23 F.4th at 602. That is an injury under Article III that this Court has recognized as recently as this year. *Id.*

The authority to set tax policy is a traditional prerogative of the States. In fact, the Supreme Court has held that such authority is "indispensable" to a State's existence. *Lane Cnty. v. Oregon*, 74 U.S. (7 Wall.) 71, 76 (1868). "It is an essential function of government," and "[t]here is nothing in the Constitution which contemplates or authorizes any direct abridgement of this power by national legislation." *Id.* at 76–77. That means the States have a traditional sovereign interest in passing tax laws that reflect their views of sound public policy without Congress's input.

The Tax Mandate invades this "traditional prerogative[]" of the States by narrowing the range of permissible tax policies the States may enact. *See Kentucky*, 23 F.4th at 602. That is, under ordinary circumstances, the States may craft whatever tax policies they desire. But the Tax Mandate imposes a constraint on that authority. Once the States accept Rescue Plan funds, they can no longer set taxes

based only on their own views of sound policy. Instead, the States must also consider whether their preferred tax policy violates the Tax Mandate. And so it limits the range of policy options available to the States—"invad[ing]" their "sovereign interests and traditional prerogatives." *Id.*

Look no further than Tennessee's evidence for proof of this problem. The Tax Mandate's opaque restriction on using Rescue Plan funds to "indirectly" offset revenue reductions means that Tennessee "must necessarily defer, slow, or reconsider some of its taxing decisions" in the coming years. [Niknejad Decl., R.25-2, PageID#225 (¶¶ 14–15)]. Although the State cannot predict with certainty the precise nature of the tax cuts its leaders will likely pursue, one thing is certain: Rather than making those decisions based on its leaders' view of sound policy, Tennessee must consider whether its desired policies will conflict with the federal Tax Mandate. [*Id.* at PageID#225–26 (¶¶ 14–17)]. As the Governor's Policy Director explained, the State's "deliberative process" regarding tax and spending decisions "will now need to be shaped around an analysis of the permissibility or impermissibility of any proposed change in tax policy under the Tax Mandate," rather than simply deciding what is best for Tennessee. [*Id.* at PageID#225 (¶ 15)]. On top of that, Tennessee's desire to continue its history of pro-growth tax cuts, [*id.* at PageID#222–24 (¶¶ 6–13)], combined with the Tax Mandate's ambiguous

and potentially sweeping scope, together create "a substantial risk" that the State will be forced to forgo or delay certain tax policies it would otherwise pursue immediately. *See Dep't of Com.*, 139 S. Ct. at 2565 (quoting *Susan B. Anthony List v. Driehaus*, 573 U.S. 149, 158 (2014)). This constraint on the traditional prerogative of the States is an Article III injury. *See Kentucky*, 23 F.4th at 602; *see also Alfred L. Snapp & Son, Inc. v. Puerto Rico, ex rel., Barez*, 458 U.S. 592, 601 (1982).

The Treasury Defendants counter that this injury is imagined because the Tax Mandate "does not prohibit a State from cutting taxes," but instead only restricts how the States use their federal funds. [Br. at 6 (quoting *Missouri v. Yellen*, 538 F. Supp. 3d 906, 912 (E.D. Mo. 2021), *appeal pending*, No. 21-2118 (8th Cir.))]. But that argument conflates the standing inquiry with the merits. *See Ariz. State Legislature v. Ariz. Indep. Redistricting Comm'n*, 576 U.S. 787, 800 (2015). The merits question in this case is whether the Tax Mandate unconstitutionally restricts the States' taxing authority. The Treasury Defendants, no surprise, argue that the law does no such thing. But even if the Court agrees with the Treasury Defendants' interpretation, it must be careful not to "confus[e] weakness on the merits with absence of Article III standing." *Id.* (quoting *Davis v. United States*, 565 U.S. 229, 249 n.10 (2011)). It is certainly "arguabl[e]" that the Tax Mandate's broad and incoherent restriction on "indirect[]" offsets effectively prohibits the States from

lowering their tax revenue during the covered years. *See Susan B. Anthony List*, 573 U.S. at 162–63. And if that is true (a merits question), no one doubts that the Tax Mandate "invades" the "sovereign interests and traditional prerogatives" of the states (the Article III question). *Kentucky*, 23 F.4th at 602.

The Treasury Defendants also argue that the States "did not show that they intend to take concrete actions that would contravene the [Tax Mandate]." [Br. at 7]. But that misstates the test for a case like this where the States allege that the federal law invades their "constitutionally guarded role." *See Ariz. State Legislature*, 576 U.S. at 800. The Supreme Court addressed this issue most recently in *Arizona State Legislature*. The Court held that the Arizona legislature had standing to challenge a law that intruded on its claimed constitutional authority over redistricting. *Id.* at 800–01. That was true regardless of whether the Arizona legislature in fact possessed the constitutional authority it claimed (a merits question) and regardless of whether it could identify "some specific legislative act that would have taken effect but for" the challenged law. *Id.* (quotation marks omitted). Invading the state legislature's asserted "constitutionally guarded role" over redistricting was an Article III injury by itself. *Id.* at 800; *see also id.* at 793.

A similar analysis applies here. To receive their Rescue Plan funds, Kentucky and Tennessee must surrender at least *some* of their preexisting authority to

set state tax policy free from federal constraints. Regardless of whether this Court agrees about the scope of their claimed authority over tax policy (a merits question), losing their "prerogative" to freely cut taxes as much as they wish injures the States. *See Arizona State Legislature*, 576 U.S. at 800. And that remains true even if the States do not identify "some specific" tax cut they would have enacted "but for" the Tax Mandate. *See id.* (quotation marks omitted). Under *Arizona State Legislature*, States "asserting institutional injury to their lawmaking authority" have standing. *Texas v. United States*, 809 F.3d 134, 154 (5th Cir. 2015).[6]

That this federal intrusion on State taxing authority takes the form of a funding condition does not change the analysis. In analogous funding contexts, recipients of government funds have standing to challenge allegedly unconstitutional conditions on the receipt of those funds regardless of whether the government has actually withheld or revoked the funds. *See, e.g.*, *Forum for Acad. & Institutional Rights, Inc. v. Rumsfeld*, 291 F. Supp. 2d 269, 286 (D.N.J. 2003), *rev'd and remanded*, 390 F.3d 219, 228 n.7 (3d Cir. 2004) (agreeing that the plaintiff had

[6] Moreover, Tennessee has shown that the Tax Mandate creates at least a substantial risk that the State will in fact forgo or delay enacting certain tax policies that it would otherwise pursue immediately. *See supra* at 7–9.

standing "for the reasons [the district court] provided"), *rev'd and remanded*, 547 U.S. 47, 52 n.2 (2006) (agreeing with lower courts that the plaintiff had standing).

The same reasoning applies in this Spending Clause context: forcing the States to choose between abandoning their constitutional taxing powers or risking the loss of federal funds "is a dilemma that it was the very purpose of the Declaratory Judgment Act to ameliorate." *Sch. Dist. of Pontiac v. Sec'y*, 584 F.3d 253 at (Sutton, J., concurring) (quoting *MedImmune, Inc. v. Genentech, Inc.*, 549 U.S. 118, 129 (2007)). Put differently, a State's "forced choice" between financial hardship and abandoning its preferred policies "is itself an injury" that satisfies Article III. *Texas*, 787 F.3d at 749.

C. The States face a realistic danger of injury from enforcement of the Tax Mandate.

The States also satisfy the traditional criteria for standing in a pre-enforcement suit to avoid an imminent injury. *See Susan B. Anthony List*, 573 U.S. at 159. An injury is imminent under Article III if (1) the plaintiff intends to "engage in a course of conduct arguably affected with a constitutional interest"; (2) the law at issue "arguably proscribe[s]" the plaintiff's intended conduct; and (3) there is a substantial threat of enforcement by the defendant. *Id.* at 159, 162–64. The States plainly satisfy all three elements.

First, both Kentucky and Tennessee have shown they intend to enact tax reforms that could reduce the net tax revenue of their respective States. [Mot., R.25, PageID#186–87]. Doing so amounts to conduct "arguably affected with a constitutional interest" because the States have a constitutional interest in enacting their preferred legislative priorities, particularly when those priorities involve setting tax policies.

Second, the Tax Mandate "arguably proscribe[s]" this conduct because the phrase "indirectly offset" is broad and ambiguous enough to encompass *any* expenditure that a State makes during the same year it reduces its revenue. *See supra* at 5–7; *infra* at 31–36, 38–40. But again, the point is not whether this Court agrees with the States about how the Tax Mandate operates—that is a merits question. The only issue for standing purposes is whether the States have a reasonable argument that the law forbids their intended conduct. *See Virginia v. Am. Booksellers Ass'n*, 484 U.S. 383, 392 (1988). So long as the States' position is arguable, the Court must assume their "interpretation of the statute is correct" for purposes of addressing standing. *Id.* And so the States easily satisfy the second prong of *Susan B. Anthony List*.

Third, there is a credible threat of enforcement against the States. "Most obviously," the federal government has a history of enforcing federal funding

conditions against the States. *See Susan B. Anthony List*, 573 U.S. at 164; *see, e.g.*, *Bennett v. Ky. Dep't of Educ.*, 470 U.S. 656, 658 (1985); *Bennett v. New Jersey*, 470 U.S. 632, 636 (1985); *Bell v. New Jersey*, 461 U.S. 773, 775–77 (1983); *Sch. Dist. of Pontiac*, 584 F.3d at 278 (Sutton, J., concurring); *Mass. ex rel. Exec. Off. of Health & Hum. Servs. v. Sebelius*, 701 F. Supp. 2d 182, 184 (D. Mass. 2010). True, Treasury has not yet enforced the Tax Mandate. But that is only because the law is brand new, the States are just beginning to receive their Rescue Plan funds, and—at least for Kentucky and Tennessee—the federal government has been enjoined from enforcing it for several months. Treasury "has not suggested that the newly enacted law will not be enforced, and [there is] no reason to assume otherwise." *Am. Booksellers Ass'n*, 484 U.S. at 393. To the contrary, Treasury has vigorously defended the law in litigation and has promulgated an extensive regulation detailing how it intends to enforce the law—including through recoupment proceedings. 87 Fed. Reg. 4,338–4,454 (Jan. 27, 2022). The prospect of future enforcement is far from "imaginary or wholly speculative." *Susan B. Anthony List*, 573 U.S. at 160 (citation omitted).

And so both Kentucky and Tennessee are entitled to pre-enforcement review. Kentucky has made recent efforts to provide tax relief for reasons unrelated to Covid-19, and so it faces the looming possibility that the Treasury Department

could seek recoupment. The State, for example, recently enacted a law that uses tax incentives to revitalize a predominantly minority area of Louisville hurt by decades of divestment. *See* 2021 Ky. Acts ch. 203. Kentucky has also begun the process of modernizing its tax code—a shift that could lead to temporary revenue reductions as Kentucky lowers its income tax and expands its sales tax. *See* House Bill 8 (2022 Regular Session), *available at* https://apps.legislature.ky.gov/record/22rs/hb8.html. Tennessee likewise has a history of reducing tax revenue to spur growth, but the threat of federal recoupment proceedings "immediately" disrupted that process and caused the State to "defer, slow, or reconsider some of its taxing decisions." [Niknejad Decl., R.25-2, PageID#225 (¶ 14)]. This uncertainty is exactly what pre-enforcement review is for. *See Sch. Dist. of Pontiac*, 584 F.3d at 278 (Sutton, J., concurring) ("Putting the school districts to the choice of abandoning their legal claim or risking sanctions is a dilemma that it was the very purpose of the Declaratory Judgment Act to ameliorate." (cleaned up)).

II. The Tax Mandate violates the Spending Clause.

Congress has broad power to impose conditions on federal funds. *Dole*, 483 U.S. at 207. But its "spending power is of course not unlimited." *Id.* Two restrictions matter here. First, Congress cannot use its virtually unlimited purse strings to coerce the States into accepting unwanted conditions. *Id.* at 211. Second,

Congress must state its conditions "unambiguously" so that the States can "ascertain" what the conditions are. *Arlington Cent. Sch. Dist. Bd. of Educ. v. Murphy*, 548 U.S. 291, 296 (2006) (citation omitted). The Tax Mandate runs afoul of both limitations.

A. The Tax Mandate is unconstitutionally coercive.

The district court correctly held that the Rescue Plan is an unconstitutional "coercive grant of federal money." [Op. & Order, R.42, PageID#628]. This Court should affirm.

1. Congress cannot use an offer of federal funds to coerce the States into adopting the federal government's preferred policies. *Dole*, 483 U.S. at 211. Conditions attached to spending grants must *encourage*, rather than *compel*, the States to comply. *Id.* at 211–12. And while the Supreme Court has not "fix[ed] a line" as to when "financial inducement offered by Congress" is "so coercive as to pass the point at which 'pressure turns into compulsion,'" it has given a few guideposts. *Nat'l Fed. of Indep. Bus. v. Sebelius*, 567 U.S. 519, 580, 585 (2012) ("*NFIB*") (op. of Roberts, C.J.) (quoting *Dole*, 483 U.S. at 211).

For example, the threat of withholding a small percentage of highway funding was not enough to coerce the States into adopting the federal government's preferred legal drinking age. *Dole*, 483 U.S. at 211–12. But a threat to withdraw

Medicaid funding equal to 10 percent of a State's total budget easily crossed the line. *NFIB*, 567 U.S. at 582, 585 (op. of Roberts, C.J.) ("It is enough for today that wherever that line may be, this statute is surely beyond it."). As the Chief Justice explained, an offer that significant is "much more than 'relatively mild encouragement'—it is a gun to the head." *Id.* at 581. No State could reasonably turn down funding when doing so meant the State must give up such a large portion of its budget. *Id.* at 582.

The "sheer size" of the Rescue Plan is similarly coercive. *Id.* at 683 (dissenting op.). For both Kentucky and Tennessee, the aid amounts to roughly one fifth of each State's general fund revenue from the fiscal year prior to the Rescue Plan.[7] That is magnitudes greater than the small percentage of highway funding in *Dole*, and looks much more like the coercive offer in *NFIB*.

Even if the dollar amount alone were not enough to make this offer coercive, the dire circumstances "surely" do. *See id.* at 585 (op. of Roberts, C.J.). The Rescue Plan funds are needed "to combat the health ramifications of the corona-

[7] *Compare* [Niknejad Decl., R.25-2, PageID#221–22 (¶ 5) (about $3.725 billion in Rescue Plan funds)], *with* Governor Bill Lee, State of Tennessee, *The Budget: Fiscal Year 2021-2022* A-62 (2021), *available at* https://perma.cc/3E79-BTKU (about $18.1 billion in estimated total state revenues for Fiscal Year 2020-2021).

virus," as "the pandemic has thrown many States and citizens into severe economic hardship." [Op. & Order, R.42, PageID#636]. That is why many "[s]tate and local officials have" called the Rescue Plan funds "a life preserver thrown to drowning government bodies." [*Id.* at PageID#637]. In such circumstances, "refusing to accede to the conditions set out in the [law] is not a realistic option." [*Id.* at PageID#635 (quoting *NFIB*, 567 U.S. at 681)].

Take Kentucky as an example. Kentucky spent nearly half of its Rescue Plan funds before it even knew how much the State would receive. It had no other choice. Kentucky needed to repay millions of dollars in debt it accumulated for extended unemployment benefits during the pandemic. *See* 2021 Ky. Acts ch. 196, § 6. The Rescue Plan offers extraordinary sums of money in a time of need, and the federal government knows that "refusing to accede to the conditions set out in the [law] is not a realistic option" for the States. *See NFIB*, 567 U.S. at 681 (dissenting op.).

2. The Treasury Defendants make only one argument in response. They do not contest that the "sheer size" of the offer is coercive, nor do they dispute that the once-in-a-century pandemic puts enormous pressure on the States to accept the money. Instead, the Treasury Defendants argue only that the coercion test does not apply when Congress imposes a condition on how the States *use* their

federal funds, rather than a condition that requires the States to implement a separate policy. [Br. at 13–15]. The Treasury Defendants may be right that the coercion restriction from *Dole* has less force when a condition attaches to how federal funds are used. But they are wrong in arguing that is what the Tax Mandate does.

A simple illustration shows why. Suppose a State spends $1 million in Rescue Plan funds for Covid-19 testing while raising the same amount of revenue as the year prior. The State might then do one of three things: It could add that $1 million to its existing healthcare budget (that is, spend $1 million more on healthcare than the prior year). The State also could keep its healthcare budget constant and use the extra $1 million in its budget to build a golf course. Or a State could keep its healthcare budget constant and use the extra $1 million to provide a tax credit for families that incurred additional childcare expenses during the pandemic. In all three examples, the State "used" the federal money the same way—it spent $1 million on Covid-19 testing.

But the Tax Mandate seems to only penalize the State in the last example, and it does so—not because of how the State "used" Rescue Plan funds—but because of how the State used *other money* from its own revenue. And the result is bizarre: The State can use its excess revenue to build a golf course, but it cannot use that same money to provide tax credits to individuals who suffered pandemic-

imposed hardships. So in what sense does the Tax Mandate have anything to do with how the States "use" their federal dollars? It doesn't. Instead, the statute does what it was obviously intended to do: It restricts the policymaking choices of States that wish to lower their taxes regardless of how they spend Rescue Plan funds.

The federal government tried the same maneuver in *NFIB*—with no success. There, Congress created an expanded Medicaid program that the States could technically opt out of. *NFIB*, 567 U.S. at 581 (Roberts, C.J. op.). But if they did, the federal government could withhold *all* of the States' Medicaid funding, not just the new funding offered as part of the expansion. *Id.* The government argued that because Medicaid is a single federal program, all Congress did was tell the States how to use their Medicaid dollars—a much less coercive act than leveraging spending to force the States to adopt new policies. *Id.* at 582–83. But the Supreme Court did not bite. Even though "Congress styled" the condition as simply a restriction on how Medicaid dollars must be spent, the reality was that Congress was leveraging a significant part of the States' budget to force the States into adopting *new* policies by expanding Medicaid. *See id.* ("The Medicaid expansion, however, accomplishes a shift in kind, not merely degree."). That Congress

styled the conditions as a mere restriction on how funds are used was "irrelevant" to the analysis. *Id.* at 582.

So too here. Even though Congress "styled" the Tax Mandate as a restriction on how the States use their Rescue Plan funds, it is nothing of the sort. Instead, Congress is wielding an offer of billions of dollars to coerce the States into adopting the preferred tax policies of the federal government.

Nor is the Tax Mandate saved by comparisons to the kinds of anti-supplanting conditions that the Supreme Court upheld in *Bennett v. Kentucky Department of Education*, 470 U.S. 656 (1985). In fact, that comparison only highlights how the Tax Mandate differs from a typical restriction on using federal funds. At issue in *Bennett* were federal funds aimed at increasing expenditures on "education programs for disadvantaged children." 470 U.S. at 659. To make sure that the federal funds were used to increase educational opportunities, rather than simply supplant state money that would have been allocated to the same purpose, Congress provided money on the condition that the States would maintain their current level of spending on their own programs for the same groups of children. *Id.* at 660. In other words, the law provided that the State could not use federal funds to replace State funds that would have otherwise been spent on education. That

makes sense. Without the condition, Congress could not ensure that the funds would *expand* education access—the purpose of the law.

More importantly, an anti-supplanting condition like that is an actual restriction on how the States use federal funds. A State accepting the money must spend it on a state program that maintains prior funding levels. That is plainly a restriction on how (or where) the funds are spent.

The Tax Mandate is not this kind of anti-supplanting condition. There is no requirement that the States spend Rescue Plan funds only in areas in which they maintain their pre-planned level of expenditures. Just return to the prior example to understand why. A State can use Rescue Plan funds to supplant its healthcare spending and then use its freed-up revenue to build a golf course. The Tax Mandate has nothing to say about that because it does not restrict how the States use their federal funds.

One more example drives this point home. Imagine, as discussed above, that a State simultaneously spends Rescue Plan funds on healthcare infrastructure while also providing tax credits to individuals of the same amount and reducing its budget for the department of corrections by the same amount. Did the State "use" Rescue Plan funds to indirectly offset the tax credits, or did it indirectly offset those tax credits by reducing its corrections budget? It is impossible to say.

Because money is fungible, either one could be said to have "indirectly" offset the tax reduction. And yet, the answer to that question—which decides whether the State violated the statute—has nothing to do with how the State *used* its federal funds because in either case, the State spent the money on healthcare infrastructure.

The Treasury Defendants' only response to the district court's coercion analysis is to insist that the rule does not apply because the Tax Mandate only restricts how States use their funds. While that "interpretation" of the statute may have "surface appeal," it "proves to be sleight of hand." *See Van Buren v. United States*, 141 S. Ct. 1648, 1655 (2021). The Court should reject it as such.

B. The Tax Mandate is unconstitutionally ambiguous.

Because the district court held that the Tax Mandate was coercive, it did not address whether the Tax Mandate is unconstitutionally ambiguous. [Op. & Order, R.42, PageID#639–40]. If the Court disagrees on the coercion issue, it should nevertheless affirm on this alternative ground. *See Sazerac Brands, LLC v. Peristyle, LLC*, 892 F.3d 853, 859 (6th Cir. 2018).

When Congress attaches conditions on spending, it must state those conditions "unambiguously." *Arlington*, 548 U.S. at 296 (citations omitted). The basic theory is this: "'Legislation enacted pursuant to the spending power is much in

the nature of a contract,' and therefore, to be bound by 'federally imposed conditions,' recipients of federal funds must accept them 'voluntarily and knowingly.'" *Id.* (quoting *Pennhurst State Sch. & Hosp. v. Halderman*, 451 U.S. 1, 17 (1981) (alterations adopted)). That means Congress must make it clear that conditions apply, *Pennhurst*, 451 U.S. at 17, and it must state those conditions with language that allows the States "to ascertain" what they are, *Arlington*, 548 U.S. at 296 (citations omitted).

What makes a condition "unambiguous"? To answer that question, the Court must consider whether the language would be clear "from the perspective of a state official who is engaged in the process of deciding whether the State should accept [the] funds and the obligations that accompany those funds." *Sch. Dist. of Pontiac*, 584 F.3d at 271 (plurality op.) (citing *Arlington*, 548 U.S. at 295). Ordinary principles of interpretation apply. The Court must "begin with the text" and "presume that a legislature says in a statute what it means and means in a statute what it says." *Arlington*, 548 U.S. at 296 (quoting *Conn. Nat. Bank v. Germain*, 503 U.S. 249, 253–54 (1992)). But if the text allows for more than one plausible interpretation, the spending condition is unconstitutionally ambiguous. *See Sch. Dist. of Pontiac*, 584 F.3d at 284–85 (Sutton, J., concurring).

The Tax Mandate suffers from two fatal ambiguities. It is unclear from the text and structure of the law, first, what it means to "indirectly offset" a loss in tax revenue, and second, how States should measure a "net reduction in tax revenue" in the first place. Resolving these questions is critical for knowing how the Tax Mandate operates. Yet on both counts, the Tax Mandate leaves the States guessing.

The indirect offset. The Tax Mandate prohibits States from using Rescue Plan funds to "directly or indirectly offset" a reduction in their net tax revenue. 42 U.S.C. § 802(c)(2)(A). The first part of that restriction is straightforward. A State would likely offset a tax cut *directly* if it lowered its revenue, made no changes to its budget, and then spent its Rescue Plan funds to pay for the tax cuts. But what does it mean for a State to "use" federal funds to "indirectly offset" a tax cut? The sweeping potential of that language leaves open too many possibilities to settle on an answer.

As explained above, it is plausible to read the Tax Mandate as prohibiting the States from enacting tax relief during the covered period *no matter what the States spend the money on*. That's because "[m]oney is fungible." *See Holder v. Humanitarian Law Project*, 561 U.S. 1, 37 (2010). A dollar spent here is always a dollar that cannot be spent somewhere else. And so an influx of additional cash into the

State's treasury will "necessarily free[] up other funds for other purposes," providing "[i]ndirect benefits" to virtually every part of a State's budget. *See Ark Encounter, LLC v. Parkinson*, 152 F. Supp. 3d 880, 904 (E.D. Ky. 2016). That means that *any* expenditure of Rescue Plan funds could be deemed to "indirectly" offset a reduction in revenue.

Yet maybe the Tax Mandate does not reach so broadly. One potential problem with that interpretation is that (as explained above) it renders the word "use" superfluous. The Tax Mandate provides that a State "*shall not use* the funds . . . to either directly or indirectly offset a reduction in the net tax revenue of such State." 42 U.S.C. § 802(c)(2)(A) (emphasis added). That language suggests it matters *how* a State spends its Rescue Plan funds, not just whether the State cuts taxes. So the fact that money is fungible—coupled with the word "indirectly"—turns the phrase "shall not use" into surplusage. *See City of Chicago v. Fulton*, 141 S. Ct. 585, 591 (2021) ("The canon against surplusage is strongest when an interpretation would render superfluous another part of the same statutory scheme." (quoting *Yates v. United States*, 574 U.S. 528, 543 (2015) (plurality op.))).

There is no reasonable way for the States to make sense of this. Go back to the example above in which a State—after providing tax credits to its citizens—both spends Rescue Plan funds and also lowers its budget for an unrelated agency.

The statute does not explain how the Treasury Defendants will determine whether a State indirectly offset its tax credits with Rescue Plan funds or with a budget reduction. It is, as one district court observed, "almost as though Congress had written the Tax Mandate" to give the Treasury Secretary limitless discretion in resolving this problem. *Ohio v. Yellen*, 547 F. Supp. 3d 713, 733–34 (S.D. Ohio 2021). That makes it impossible for "a state official who is engaged in the process of deciding whether the State should accept [the] funds" to "ascertain" the meaning of this condition. *See Arlington*, 548 U.S. at 296. It is therefore unconstitutionally ambiguous. *See id.*

The reduction in net tax revenue. Even if the phrase "indirectly offset" had a clear meaning, the phrase "reduction in the net tax revenue" does not. The problem has several layers but boils down to this: A State can only reduce its tax revenue relative to a baseline, but the Tax Mandate never says what that starting point is. And while there are multiple possibilities, picking one would require the States (or this Court) to simply guess.

One could imagine, for example, that the Tax Mandate prohibits the States from cutting taxes in any given year relative to the year prior. That makes sense. But there's reason to doubt that is what Congress intended. Elsewhere in the law, the States are permitted to use Rescue Plan funds to make up for losses in revenue

caused by the pandemic. *See* 42 U.S.C. § 802(c)(1)(C). That provision specifies that States are to judge their losses in revenue "relative to revenues collected in the most recent full fiscal year." *Id.* No similar provision exists in the Tax Mandate, suggesting that Congress might have had something different in mind. *See Pennhurst*, 451 U.S. at 17–18 ("[I]n those instances where Congress has intended the States to fund certain entitlements as a condition of receiving federal funds, it has proved capable of saying so explicitly.").

Treasury's regulation gives another possible answer. Under the rule, States must evaluate revenue losses relative to the last fiscal year that ended before the pandemic. 31 C.F.R. §§ 35.3, 35.8(b). That arguably makes some sense from a policy perspective. But what in the statute makes this interpretation unambiguously clear? The question under the Spending Clause is not whether an agency can come up with a reasonable interpretation of an ambiguous condition. The question is whether that interpretation is the clear, unambiguous meaning of the law Congress passed. *See Sch. Dist. of Pontiac*, 584 F.3d at 277 (plurality op.).

Nor is establishing the baseline the only issue. Suppose, for example, that in Year 1 after accepting Rescue Plan funds, the State increases its tax revenue by $10 million relative to its last pre-pandemic fiscal year, but then in Year 2 decreases its tax revenue by $5 million relative to that same year. The net effect is

an *increase* in $5 million, spread out over two years instead of one. Can Treasury nevertheless recoup $5 million from the State for having collected too little in Year 2? Because the Tax Mandate provides no clarity as to how States should understand what amounts to a "reduction" in tax revenue, Treasury can answer this question just about any way it chooses. And that, ultimately, is the problem. The issue is not whether it makes sense to adopt Treasury's preferred interpretation—it's whether the statute unambiguously compels it.

Making matters worse, the Tax Mandate says nothing about when the reduction in net tax revenue must occur for the State to "indirectly offset" it with Rescue Plan funds. The Tax Mandate covers any reduction in revenue caused by the State changing its law "during the covered period." 42 U.S.C. § 802(c)(2)(A). But it does not limit the *effect* of those changes—that is, the actual reduction in revenue—to the same period. So suppose that a State spends all of its Rescue Plan funds during the covered period and, in the last month of that covered period, eliminates its income tax for the next fiscal year. Could an enterprising Treasury Secretary view the State's decision as some kind of gamesmanship and initiate a recoupment action against the State for the revenue loss after the covered period ends? After all, Congress limited the period in which the Tax Mandate applies to changes in state law, but it did not similarly limit the period in which to measure

revenue reductions, leaving open the possibility of never-ending oversight for any tax policies enacted during the covered period. And while that might be good or bad policy, the fact is that the statue provides no clarity for the States to make a reasonably informed decision.

One final point: What should the States make of the fact that tax policies are often predictive, and those predictions might take time to play out? If a State enacts tax reform with the goal of keeping revenue neutral, will it be punished for making a bad prediction? Or what if the State's prediction is correct, but it takes several years to materialize? Can Treasury recoup funds from the State because one fiscal year saw a dip in revenue even though the next three years saw an increase?

Kentucky faces this problem right now. The General Assembly is considering substantial changes to modernize its tax code by reducing its income tax and expanding its sales tax. *See* House Bill 8 (2022 Regular Session), *available at* https://apps.legislature.ky.gov/record/22rs/hb8.html. In the long-term, Kentucky hopes that this change will not cause revenue losses. But such a major policy shift could have unexpected outcomes that the State may need to address in the coming years. And yet, it is impossible for Kentucky to know whether the Treasury Defendants can (or will) punish Kentucky for any unpredictable revenue

losses in the future that the federal government might trace back to Kentucky's tax reform.

This ambiguity only amplifies what is already a coercive intrusion into State sovereignty. By prohibiting the States from enacting tax policies that cause an ill-defined effect, Congress is freezing out the States from legislating in an area that is central to their historical and guaranteed sovereignty. *See Lane Cnty.*, 74 U.S. at 76–77. The federal government perhaps hopes that the States will simply idle along for the next four years (or perhaps longer) on tax reform for fear of losing billions of dollars in federal funding. That fear is itself the constitutional problem.[8] The States should not be made to guess about the meaning of a law on an issue of such central importance to their sovereignty so that they can receive billions of dollars in needed financial relief.

III. The Tax Mandate violates the Tenth Amendment.

The Court can also affirm the district court's judgment on the alternative ground that the Tax Mandate violates the anti-commandeering principles embodied in the Tenth Amendment. *See Sazerac Brands*, 892 F.3d at 859.

[8] The uncertainty here further shows why the States suffer an Article III injury to their sovereign interests right now. The States must legislate on tax issues in the shadow of a Tax Mandate that they cannot possibly know the meaning of.

The anti-commandeering doctrine is "the expression of a fundamental structural decision incorporated into the Constitution, *i.e.*, the decision to withhold from Congress the power to issue orders directly to the States." *Murphy v. Nat'l Collegiate Athletic Ass'n*, 138 S. Ct. 1461, 1475 (2018). The Tenth Amendment confirms this principle by expressly providing that "[t]he powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people." In its most basic form, the anti-commandeering doctrine prohibits Congress from "requir[ing] the States to govern according to Congress' instructions." *New York v. United States*, 505 U.S. 144, 162 (1992). The doctrine safeguards individual liberty and promotes political accountability by preventing Congress from using the States to implement its preferred (and possibly unpopular) policies. *Printz v. United States*, 521 U.S. 898, 920–25, 929–30 (1997).

Few powers of government are as central to sovereignty as the power to tax—or just as importantly, the power *not* to tax. *Lane Cnty.*, 74 U.S. at 76; *see also Dep't of Revenue v. ACF Indus., Inc.*, 510 U.S. 332, 345 (1994). The power to control the taxing policy of a State is nothing short of the "power to destroy." *M'Culloch v. Maryland*, 17 U.S. (4 Wheat.) 316, 327 (1819). That's why, for example, when James Madison sought to persuade the States that the Constitution would not

make the federal government too powerful, he used *tax collectors* as an example to contrast the relative strength of each government. *See* The Federalist No. 45 (J. Madison) ("Should it happen, however, that separate collectors of internal revenue should be appointed under the federal government, the influence of the whole number would not bear a comparison with that of the multitude of State officers in the opposite scale.").

There is no doubt that Congress is using the Tax Mandate to "blur[]" the lines of political accountability on an issue of supreme importance. *See Murphy*, 138 S. Ct. at 1477. Taxes touch on every part of political life. By prohibiting the States from offering tax relief to their citizens, Congress is handcuffing local governments and leaving them unable to respond to electoral pressures that drive a healthy democracy. Yet when a State's taxes are too high, it is the State—not Congress—that will face the voters. And *that* is a central problem the anti-commandeering doctrine exists to prevent. *See id.*

But the Tax Mandate compounds the problem even more. Congress has not only coerced the States into adopting higher tax policies than they might otherwise do, it has done so while *lowering* the federal tax burden. *See, e.g.*, American Rescue Plan Act of 2021, Pub. L. No. 117-2 § 9611 (temporarily increasing the

child tax credit and making it fully refundable); *id.* § 9631 (increasing the maximum tax credit for dependent care). So with one hand, Congress has extended favorable federal tax relief to its constituents (for which Congress can then take political credit). And with the other hand, Congress has prohibited the States from providing similar relief (for which Congress can deflect the blame). This unprecedented commandeering of State power is thus doubly problematic: it blurs political accountability for unpopular policy choices and leaves the federal government with the political spoils that the States might otherwise earn.

One final point: It must be the case that there are some features of State sovereignty that the federal government cannot intrude on, even when leveraging its Spending Clause power. The federal government, for example, cannot order a State to relocate its capitol as part of a bargain to admit that State into the union. *Coyle v. Smith*, 221 U.S. 559, 565–67 (1911). Surely the power to tax one's citizens—or not tax them—is of similar importance to state sovereignty. *See Lane Cnty.*, 74 U.S. at 76. Thus, whether Congress has couched the Tax Mandate as a spending condition or not, it amounts to unlawful commandeering in violation of the Tenth Amendment.

CONCLUSION

The Court should affirm the district court's judgment.

Respectfully submitted by,

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CERTIFICATE OF COMPLIANCE

As required by Federal Rule of Appellate Procedure 32(g) and 6th Cir. R. 32, I certify that this brief complies with the type-volume limitation in Fed. R. App. P. 32(a)(7)(B) because it contains 10,432 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(f) and 6th Cir. R. 32(b)(1).

This brief complies with the typeface requirements of Fed. R. App. P. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because it has been prepared in a proportionally spaced typeface, Garamond, in 15-point font using Microsoft Word.

s/ Brett R. Nolan

CERTIFICATE OF SERVICE

I certify that on March 10, 2022, I electronically filed this brief with the Clerk of the Court for the United States Court of Appeals for the Sixth Circuit using the CM/ECF system. I further certify that all participants in the case are registered CM/ECF users and that service will be accomplished by the CM/ECF system.

s/ Brett R. Nolan

ADDENDUM

Kentucky and Tennessee designate the following as relevant documents from the district court:

1. Complaint: R.1, PageID#1–25
    a. Letter to Secretary Yellen (Exhibit A), R.1-1, PageID#26–32
    b. Letter to the States (Exhibit B), R.1-1, PageID#33–34
2. Amended Complaint, R.23, PageID#130–56
    a. Letter to Secretary Yellen (Exhibit A), R.23-1, PageID#157–63
    B. Letter to the States (Exhibit B), R.23-2, PageID#164–65
3. Plaintiffs' Motion for Summary Judgment, R.25, PageID#171–218
    a. Kentucky Certification (Exhibit A), R.25-1, PageID#219
    b. Niknejad Decl. (Exhibit B), R.25-2, PageID#220–26
    c. Eley Decl. (Exhibit C), R.25-3, PageID#227–32
4. Defendants' Resp. & Mot. to Dismiss, R.31, PageID#321–65
5. Plaintiffs' Reply & Response, R.36, PageID#468–505
6. Defendants' Reply, R.38, PageID#544–74
7. Opinion & Order, R.42, PageID#628–44
8. Judgment, R.43, PageID#645–46
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