

Alert | State & Local Tax (SALT)



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Federal Challenges to State Taxes

Taxpayers are generally limited in their options for contesting state and local tax matters. The statutes imposing income, corporate, sales and property taxes prescribe the steps to be taken and the forum for challenging those taxes. The doctrine of 'exhaustion of administrative remedies' requires taxpayers to go through the administrative procedures before being able to go to court to adjudicate their protests. This year, the U.S. Court of Appeals for the Seventh Circuit opened the door to federal challenges to state taxes when a taxpayer is precluded from making constitutional claims under the state's tax adjudication process.

Under 28 USC § 1341, "[t]he district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State."

Enacted in 1948, 28 USC § 1341, the "Tax Injunction Act," is intended to preclude federal courts from interfering with state tax collections as long as the state provides a "plain, speedy and efficient" means for challenging the tax at issue. This prohibition has been upheld in instances where refunds without interest are delayed by two years (*Rosewell v. LaSalle Nat'l Bank*, 450 U.S. 503); where an allegation that the "the adjudicators in those bodies were too corrupt to be able to neutrally review charged issues" (*Capra v. Cook County Board of Review*, 733 F.3d 705, 715 (7th Cir. 2013); the argument that two-year delays in a taxpayer's Appeal Board proceedings made them insufficiently "speedy." *Heyde v. Pittenger*, 633 F.3d 512, 521 (7th Cir. 2011).

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Now, the U.S. Supreme Court has been asked to review a decision of the Seventh Circuit Court of Appeals that allowed a challenge to the Cook County property tax to be pursued in federal court. The Seventh Circuit found there was no plain, speedy and efficient way to make the taxpayer's claims in the Illinois state courts. *A.F. Moore & Associates, Inc. v. Pappas*, No. 19-1971 (7th Cir. 2020); petition for certiorari filed Sept. 4, 2020, captioned *Maria Pappas, Cook County Treasurer*, et al. v. A.F Moore & Associates, Inc., et al.

In *A.F. Moore*, the taxpayer claimed, and the defendant did not dispute, that provisions of the Illinois statute setting the procedures for contesting property tax assessments (35 ILCS 200/23-15) precluded the taxpayer from making claims under the equal protection clause of the U.S. Constitution. Judge Amy Coney Barrett wrote for the court; "[s]ince the defendants agree that the taxpayers cannot make their equal protection case in state court, the taxpayers have no 'remedy' at all for their claims—never mind a 'plain, speedy and efficient' one—and the Tax Injunction Act does not bar their federal suit."

Given *A.F. Moore*, questions now abound on whether statutes that provide for tax refunds without interest when the refunds are delayed for many years; laws that limit issues that may be raised in tax challenges; and the substantial delays in hearing and determining tax cases (property tax petitions in NYC take at least five years to be heard) could result in more cases being brought in federal courts.

Many administrative agencies that hear tax appeals cannot consider certain claims—including the New York State and New York City Tax Appeals Tribunals. These administrative tribunals cannot hear facial challenges to the constitutionality of state and city tax laws—they can only determine if the law was unconstitutionally applied. *Matter of Hazan*, Tax Appeals Tribunal, April 21, 1989, confirmed sub nom *Matter of David Hazan*, *Inc. v Tax Appeals Trib. of State of N.Y.*, 152 AD2d 765 [1989], affd 75 NY2d 989 [1990]; *Siemens Corporation f/k/a/ Siemens Capital Corporation*, TAT(E) 93-237 (GC), New York City Tax Appeals Tribunal (1999). Commencing an action for a declaratory judgment in state court may be available in some circumstances, but the question remains whether making taxpayers go through an administrative process to make arguments to adjudicators that cannot hear the entirety of their complaints provides a "plain, speedy and efficient" remedy. It may be plain, but it is neither speedy nor efficient. Taxpayers should carefully analyze the statutes providing for protesting tax assessments to ensure that all claims protecting their rights can be made. If there are arguments that are precluded or limited, there may be another forum available so that all claims can be properly heard and all of their rights protected.

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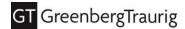
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