A Wynne for Taxpayers: Supreme Court Invalidates Components of Maryland's Income Tax Regime

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On May 18, 2015, the United States Supreme Court held that the component of Maryland's taxing scheme that provided a credit for taxes paid to other states against the state income tax, but not the county income tax, was unconstitutional [1]. This case reaffirms the Court's commitment to the dormant Commerce Clause and represents a significant step forward in clarifying state restrictions on taxing income earned without a particular state.

Maryland's Taxing Scheme
In Maryland, the income tax imposed on state residents includes both a state component and a county component. As in most states, a credit for taxes paid to other states is allowed against the Maryland income tax, but this credit is only allowed against the state portion of taxes paid, not the county portion [2]. The current case was brought by a Maryland couple challenging this dichotomy in the crediting scheme.

Facts
In this case, the taxpayers were a married couple residing in Maryland [3]. During the tax years at issue, the taxpayers held interests in an S-Corporation that did not have activity in Maryland, but which filed income tax returns in 39 other states [4]. The S-Corporation income then flowed through to the taxpayers' Maryland income tax return, as required for residents [5]. On their tax return, the taxpayers claimed a credit for taxes paid with respect to this income in other states against both the state and county portion of the tax [6]. On audit, Maryland denied the credit for the county portion of income and assessed a tax deficiency [7]. Over the course of the next several years, the taxpayers protested this decision which was affirmed at the Maryland Tax court, and then reversed at the Maryland Circuit Court. Finally, the circuit court's decision was upheld at the Maryland Court of Appeals, Maryland's highest court [8]. That is, the Maryland Court of Appeals held that the taxing regime was unconstitutional under the Commerce Clause [9]. The Comptroller appealed and the United States Supreme Court granted review.

The Supreme Court Provides Justice to the Wynnes
Writing for the majority, Justice Alito upheld the Maryland Court of Appeals and found that Maryland's taxing regime violated the dormant Commerce Clause [10]. In so doing, the Court first reiterated an important distinction between Due Process and Commerce Clause jurisprudence—namely that merely because a state has authority to impose a tax under the Due Process clause, it does not have the authority to impose a tax in violation of the Commerce Clause [11]. In its Commerce Clause analysis, the Court found that Maryland's taxing scheme violated the internal consistency test as enunciated in Complete Auto Transit v. Brady [12]. To illuminate this point, the Court noted that if all states enacted Maryland's taxing scheme, interstate commerce would bear a higher tax burden than intrastate commerce. This, under the Commerce Clause, cannot stand. On a related note, the Court also found that the dormant Commerce Clause would apply regardless of the type of tax (net income v. gross receipts) and on whom it was imposed (corporations v. individuals) [13]. Finally, the Court noted that it did not foreclose the possibility that there was a way to modify Maryland's taxing scheme to make it constitutionally permissible [14]. However, since such a revised scheme was not before the Court, they could make no decisions on what modifications might render the scheme constitutional [15].

Final Observations
This case represents a significant victory for the individual respondents in this case as well as all taxpayers who have income earned both within and without their domicile. This case makes clear that there are boundaries that states must respect in terms of imposing tax on their residents. Critically, for nonresidents increasingly tapped for taxes by remote states in an era of Congressional deadlock, this case provides much-needed confirmation of the Court's commitment to the dormant Commerce Clause doctrine. The Court also affirmed that a state's authority to impose tax consistent with Due Process does not permit taxation in violation of the Commerce Clause. This is good news because lower courts too frequently seem to be citing Due Process principles when deciding Commerce Clause cases. Finally, this case serves as a warning to other states that, even in light of significant budget shortfalls, taxation that is constitutionally impermissible will not be tolerated.

1. Comptroller of the *Treasury of Maryland v. Wynne et ux.*, 575 U.S. ____ (2015), at 1-2. Justice Alito wrote for the majority, including Justices Roberts, Kennedy, Breyer, and Sotomayor. Justice Scalia filed a dissenting opinion in which Justice Thomas partially joined, while Justice Thomas filed a dissenting opinion in which Justice Scalia partially joined. Justice Ginsburg filed a dissenting opinion in which Justices Kagan and Scalia joined.
2. Maryland also has a taxing regime that applies to nonresidents. That scheme consists of the state income imposed on all income sourced to Maryland and a "special nonresident tax" that is applied on income sourced to Maryland which is equal to the lowest county rate.
3. Comptroller of the *Treasury of Maryland v. Wynne et ux.,* 575 U.S. ____ (2015), at 1-2.
4. *Id.* at 3.
5. *Id.*
6. *Id*.
7. *Id.*
8. Comptroller of the *Treasury of Maryland v. Wynne et ux.,* 575 U.S. ____ (2015), at 3.
9. *Id.* at 3-4.
10. *See id.* at 5-31.
11. *Id*. at 13.
12. *Id.* at 21.
13. Comptroller of the *Treasury of Maryland v. Wynne et ux.*, 575 U.S. ____ (2015), at 7-8.
14. *Id.* at 25-26.
15. *Id.*