MICHAEL J. HOLZHEID, *et. al.*,	*	
	*	IN THE
Plaintiffs,		
	*	CIRCUIT COURT
v.		
	*	FOR
COMPTROLLER OF MARYLAND, *et al.*,		
	*	BALTIMORE CITY
Defendants.	*	Civil Action No. 24-C-15-005700

* * * * * * * * * * * *

REPLY MEMORANDUM IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS COMPLAINT

The exhaustion doctrine encompass two interrelated concepts: A plaintiff challenging agency action must obtain a final decision from the agency in question and must also complete the specific administrative appeals process established by the General Assembly before resorting to the Maryland courts. *See, e.g., Board of Pub. Works v. K. Hovnanian's Four Seasons at Kent Island, LLC*, 443 Md. 199, 222 (2015); *Renaissance Centro Columbia, LLC v. Broida*, 421 Md. 474, 484 (2011); *Maryland Comm'n on Human Relations v. Downey Commc'ns*, 110 Md. App. 493, 528 (1996). These well-established principles are interrelated because "it may be said fairly that" a plaintiff who has not exhausted his or her administrative remedies has not yet received a final decision from the agency. *Smith v. County Comm'rs of Kent Cnty.*, 418 Md. 692, 712 n.20 (2011). The dual requirements are also central tenets of Maryland law in that "share the common goal of preventing potentially unnecessary and premature disruption

by the courts of the activities of administrative agencies." *Downey Commc'ns*, 110 Md. App. at 528.

Here, the plaintiffs—and the putative class members they purport to represent—have failed to begin, much less complete, the exclusive administrative process for challenging final decisions by the Comptroller: an appeal to the Maryland Tax Court. *See* Md. Code Ann., Tax-Gen. §§ 3-103, 13-510. In light of the plaintiffs' failure to exhaust that administrative process, the plaintiffs' claims must be dismissed. Moreover, some of the plaintiffs—and many of the putative class members—apparently have not even obtained final decisions from the Comptroller on their refund claims because they have yet to receive the tax refunds that they challenge as being too low.[1] (Compl. ¶¶ 35, 46, 47, 55.)

Those plaintiffs who have yet to receive a refund decision are effectively asking this Court to process their tax returns for them, determine if they are eligible for a refund, determine the amount of the refund that is due, and then calculate the proper interest payment on that refund. But all of those tasks are for the Comptroller to perform in the first instance. After all, it might turn out that some of the plaintiffs are not even entitled to refunds or that the final amount of their refunds are less than they anticipated.

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[1] The complaint alleges that Michael Holzheid has yet to receive his refund (Compl. ¶ 46), and that Bruce Feinerman and Jeffrey and Arielle Grill have yet to receive their refunds for some of the tax years that they are challenging. (Compl. ¶¶ 35, 47.) Similarly, the putative class includes "all" taxpayers who timely filed a *Wynne*-related refund claim, which presumably includes both those who have and have not yet received refunds. (Comp. ¶ 55.)

Therefore, even assuming that exhaustion were not required, this Court must still dismiss the claims of those plaintiffs (including the putative class plaintiffs) who have not received a final decision from the Comptroller on their refund claims.[2]

ARGUMENT

I. THE PLAINTIFFS' DECLARATORY JUDGMENT CLAIMS MUST BE DISMISSED BECAUSE THE TAX COURT PROVIDES A SPECIAL REMEDY THAT MUST BE USED IN LIEU OF THE DECLARATORY JUDGMENT ACT.

The plaintiffs do not seem to dispute that when the General Assembly has provided a special form of remedy, plaintiffs must use that remedy in lieu of the Declaratory Judgment Act. *See* Md. Code Ann., Cts. & Jud. Proc. § 3-409. Nor do the plaintiffs dispute that an appeal to the Tax Court is such a special form of remedy. *See, e.g., Furnitureland S., Inc., v. Comptroller*, 364 Md. 126, 133 (2001); *White v. Prince George's Cnty.*, 282 Md. 641, 649 (1978); *Reiling v. Comptroller*, 201 Md. 384, 387-89 (1953). In fact, the plaintiffs implicitly acknowledge that a declaratory judgment action cannot lie when the Tax Court has power to resolve the challenges at issue; their argument is instead that the Tax Court lacks that power with respect to (1) constitutional challenges and (2) challenges to the interest on a tax refund as opposed to the refund itself. (*See* Pls.' Resp. at 9, 14.) The problem with this argument is that the Tax Court in fact has jurisdiction to resolve both types of challenges.

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[2] Plaintiffs spend a surprisingly large portion of their memorandum attempting to defend the merits of their constitutional claims under the Commerce Clause and the Fourteenth Amendment. Needless to say, the defendants disagree that the plaintiffs have meritorious claims, but the merits of their suit is not at issue in this motion to dismiss because the defendants moved to dismiss only on procedural grounds.

Under Maryland's statutory scheme, the Tax Court "has jurisdiction to hear appeals from the final decision" of any unit of State government authorized to make the final decision "about *any* tax issue," including "the determination of a claim for refund." Tax-Gen. § 3-103(a)(3) (emphasis added); *see also id.* § 13-510(a)(6) (providing that an aggrieved person may appeal the Comptroller's final decision on a refund claim). Although the plaintiffs seek to artificially divorce the interest on a tax refund from the underlying refund, the amount of the total refund, including the interest, is still—by definition—a "tax issue."

As the Court of Appeals has explicitly recognized, the Tax Court "ha[s] jurisdiction to consider [an] interest issue" because "the question of interest on the refund is part of the inquiry resulting from an appeal of the disallowance of the claim for [a] refund." *Comptroller v. Science Applications Int'l Corp.*, 405 Md. 185, 195 (2008).[3] This is true even when the interest payment is the only issue in dispute. *See Comptroller v. Fairchild Indus., Inc.*, 303 Md. 280, 282-83 (1985) (illustrating that the Tax Court will adjudicate a case involving only an interest-related issue). In other words, the amount of the interest on a tax refund is part and parcel of the refund claim, and the Tax Court has jurisdiction to consider challenges related to the interest payment.

[3] The plaintiffs argue that this case is distinguishable because it involved whether interest was due at all, not the amount of the interest. (Pls.' Resp. at 13.) While that may be true, it is not a material distinction. The amount of the interest is no less "part of the inquiry" into a refund claim than the entitlement to interest in the first place.

Similarly, the Tax Court also has jurisdiction to consider constitutional challenges to tax laws, including the plaintiffs' arguments here under the Commerce Clause and the Fourteenth Amendment. The Court of Appeals has specifically held that the Tax Court, like other administrative agencies in Maryland, is "fully competent to resolve issues of constitutionality and the validity of statutes or ordinances in adjudicatory administrative proceedings which are subject to judicial review." *Furnitureland S., Inc.*, 364 Md. at 137-38 (internal quotation omitted); *see also Goldstein v. Time-Out Family Amusement Ctrs., Inc.*, 301 Md. 583, 591 (1984) (finding "no merit" to plaintiff's argument that the Tax Court could not decide constitutional issues). Thus, taxpayers must first raise their constitutional arguments in that forum. *See, e.g., Furnitureland S., Inc*, 364 Md. at 137-38; *Goldstein*, 301 Md. at 591; *White*, 282 Md. at 265. Because the plaintiffs failed to use the special remedy available through the Tax Court for resolution of these issues, the plaintiffs' declaratory judgment claims must be dismissed.

II. THE PLAINTIFFS' ACTION UNDER SECTION 1983 MUST BE DISMISSED.

The plaintiffs broadly contend that a claim under 42 U.S.C. § 1983 can never be dismissed for failure to exhaust administrative remedies. (Pls.' Resp. at 9-10.) Although they are correct that exhaustion usually is not required for a § 1983 claim, *see Felder v. Casey*, 487 U.S. 131 (1988), they overlook the well-established exception to that rule when a plaintiff attacks the constitutionality of a state tax system. *See, e.g., Fair Assessment in Real Estate Ass'n, Inc. v. McNary*, 454 U.S. 100, 108-09, 116 (1981); *Bancroft Info. Grp., Inc. v. Comptroller*, 91 Md. App. 100, 113-14 (1992).

In *McNary*, the Supreme Court held that "principle[s] of comity" barred taxpayers "from asserting § 1983 actions against the validity of state tax systems in federal courts" without exhausting state administrative and judicial remedies. 454 U.S. at 116. The Court reasoned that permitting such claims in federal court without requiring exhaustion would impermissibly disrupt the States' tax systems and significantly interfere with the "fiscal operations of state governments" by damaging the state budget and reducing the state's revenue stream. *Id.* at 109, 113-14 (internal quotation omitted). Although the Court did not expressly require that plaintiffs also must exhaust administrative remedies before filing § 1983 actions in *state* court, there is "no basis for saying that exhaustion of administrative remedies will be required, as a matter of law in federal courts, but may not even be permitted, as a matter of sovereign choice, in state courts." *Nutbrown v. Munn*, 311 Or. 328, 340, 811 P.2d 131, 138 (1991) (emphasis omitted).

Accordingly, the Court of Special Appeals has held that states may "impose such a requirement" to exhaust administrative remedies in tax cases under § 1983 "without offending federal law."[4] *Bancroft Info. Grp.*, 91 Md. App. at 113-14 (relying on *Nutbrown* and dismissing a § 1983 claim challenging a State tax law for failure to exhaust administrative remedies); *see also Hogan v. Musolf*, 163 Wis.2d 1, 17-19, 471 N.W.2d 216, 222-23 (1991) (reaching the same conclusion under Wisconsin law); *Nutbrown*, 311 Or. at 340-42, 811 P.2d at 138-39 (reaching the same conclusion under

[4] The Court carved out a narrow exception to the exception for First Amendment challenges, but that rule does not apply here. *See Bancroft Info. Grp.*, 91 Md. App. at 108 n.5.

Oregon law). After all, "it would be no less disruptive of the state's internal economy and administrative tax procedures for a state court to act under § 1983 and suspend the usual tax collection and refund procedures of the state than it would be for a federal court to do so." *Hogan*, 163 Wis.2d at 18, 471 N.W.2d at 222; *see also Nutbrown*, 311 Or. at 341, 811 P.2d at 138-39 ("If Congress' purposes will not be defeated by [an exhaustion] requirement in federal court, we cannot conceive how those purposes would be any more thwarted by imposition of precisely the same kind of procedural requirement when the § 1983 action is brought in state court.").

The plaintiffs attempt to circumvent this rule by protesting that (1) they are not challenging the *collection* of taxes, merely the interest on a tax refund and (2) the Tax Court does not provide an adequate remedy because it does not allow for class actions. (Pls.' Resp. at 10-12.) Neither attempt is successful. First, the exhaustion requirement established by *McNary* and *Bancroft* is not limited to challenges based on allegedly unconstitutional tax collection. The principle instead applies with equal force to suits concerning "refund procedures," *Hogan*, 163 Wis.2d at 18, 471 N.W.2d at 222, and other legal attacks that threaten to "disrupt state tax administration" or "deplete state coffers" by reducing tax revenue, *Levin v. Commerce Energy, Inc.*, 560 U.S. 413, 417, 425 (2010). In fact, in *Levin*, the Supreme Court rejected the overly narrow view advanced by the plaintiffs here that the exhaustion requirement applies "only when plaintiffs have sought . . . to arrest or countermand state tax collection." *Id.* at 425, 430 (quoting *Hibbs v. Winn*, 542 U.S. 88, 107 n.9 (2004)).

A ruling in favor of the plaintiffs in this case would unquestionably disrupt Maryland's administration of its tax system. As explained above, the laws governing the interest on tax refunds are part and parcel of the laws governing tax refunds. *See, e.g.*, Md. Code Ann., Tax-Gen. §§ 13-603, 13-604. Moreover, a judicial determination that the Comptroller owes the plaintiffs additional interest would effectively entitle a staggering number of taxpayers to larger refund payments and thus "deplete state coffers," *Levin*, 560 U.S. 425, in the same way as a successful challenge to tax collection or refund procedures. Given that the practical result would be the same, there is no logical reason to draw an artificial distinction between constitutional attacks on the amount of a tax refund and on the amount of the interest payment on that tax refund. Either way, the plaintiffs' claim could throw "state tax administration into disarray" and cause significant "damage to the State's budget." *McNary*, 454 U.S. at 108 n.6 (quoting *Perez v. Ledesma*, 401 U.S. 82, 128 n.17 (Brennan, J., concurring in part and dissenting in part)). The plaintiffs are thus precluded from raising a §1983 claim in Maryland court without exhausting their administrative remedies.

Second, the fact that a class action is not available in Tax Court does not render Maryland's administrative procedure inadequate. A remedy is adequate under the federal Tax Injunction Act and the related comity doctrine so long as it meets "certain minimal *procedural* criteria" and provides a "full hearing and judicial determination" of all federal constitutional issues. *Rosewell v. LaSalle Nat'l Bank*, 450 U.S. 503, 512-13 (1981) (emphasis in original); *see also McNary*, 454 U.S. at 116 n.8 (explaining that there is no significant difference between the Tax Injunction Act and comity doctrine in determining

adequate of state remedies). That is the case here. As explained above, the plaintiffs each may raise their constitutional objections to the interest rate in the Tax Court. *See Furnitureland S., Inc.*, 364 Md. at 137-38. They may then appeal that decision to circuit court, the Maryland appellate courts, and eventually the Supreme Court. Indeed, that is precisely what happened in *Comptroller v. Wynne*. *See* 135 S. Ct. 1787, 1793 (2015) (outlining procedural history).

Although the plaintiffs might prefer a class action, a state administrative remedy "need not be the best remedy available or even equal to or better than the remedy which might be available" in court. *Lowe v. Washoe Cnty.*, 627 F.3d 1151, 1155 (2010) (internal quotation omitted). Thus, numerous federal courts have held that a State's procedure for resolving tax disputes is adequate even when it does not provide for a class action or similar "class-wide remedy." *Id.* at 1156; *see also Waldron v. Collins*, 788 F.2d 736, 738 (11th Cir. 1986); *Melof v. Hunt*, 718 F. Supp. 877, 885 (M.D. Ala. 1989); *Coleman v. McLaren*, 631 F. Supp. 749, 762 (N.D. Ill. 1985) *aff'd*, 796 F.2d 477 (7th Cir. 1986). In any event, the unavailability of a class action in Tax Court does not impose the same hurdle to relief as the plaintiffs seem to believe. As the *Wynne* litigation proves, a class action is not necessary; if one taxpayer appeals the Comptroller's decision through the Maryland courts, other taxpayers will benefit if the law is ultimately found to be unconstitutional. There is thus no reason to excuse exhaustion.[5]

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[5] In a footnote, the plaintiffs contend that their § 1983 claim falls into Maryland's so-called "constitutional exception" to the exhaustion requirement. (Pls.' Resp. at 10 n.42 (quoting *Harbor Island Marina, Inc. v. Board of Cnty. Comm'rs of Calvert Cnty.*;

Finally, even if exhaustion were not required for the plaintiffs' § 1983 claims, some of the plaintiffs and many of the putative class members have not even received a final decision from the Comptroller on their refund requests. (Compl. ¶¶ 35, 46, 47, 55.) At the very least, those plaintiffs cannot file suit until they have final decision from the Comptroller on their refund claims. *See, e.g.*, *Renaissance Centro Columbia*, 421 Md. at 484 (requiring a final decision before a plaintiff may challenge agency action in Maryland court).

III. THE PLAINTIFFS' TAKINGS CLAIM MUST ALSO BE DISMISSED.

The plaintiffs also claim that the Comptroller has effected an unconstitutional taking and that they are entitled to just compensation. This takings claim is essentially a § 1983 action for damages and thus must be dismissed for the same reasons as discussed above. *See McNary*, 454 U.S. at 116; *Bancroft Info. Grp.*, 91 Md. App. at 108. A finding that the refund scheme violates the Fourteenth Amendment as a taking will have the same consequences—and will be just as disruptive to the administration of the State's tax

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286 Md. 303, 308 (1979).) However, this exception has been "significantly limited" by later decisions, *Montgomery Cnty. v. Broadcast Equities, Inc.*, 360 Md. 438, 455, 758 (2000), and is now "an extremely narrow one," *Prince George's Cnty. v. Ray's Used Cars*, 398 Md. 632, 650 (2007). The exception does not apply, to take just a few examples, where the plaintiff does not challenge an *entire* statute in "all of its parts and all of its applications," where there are any factual issues to be resolved, or where the administrative remedy is "exclusive." *Id.* at 652-53 (citing *Broadcast Equities, Inc.*, 360 Md. at 456-57). Here, because the plaintiffs seek damages for refunds that have not yet been determined, there are factual issues to resolve. More importantly, the Tax Court is also the "exclusive" remedy for resolving tax disputes in Maryland, *Reiling*, 201 Md. at 288, and the plaintiffs do not challenge the entire statutory scheme governing interest on tax refunds. The constitutional exception thus does not apply.

regime—as a finding that the scheme violates the dormant commerce clause. Moreover, even outside the tax context, the Court of Appeals has "held on many occasions, when faced with a claim of an agency's unconstitutional taking of property, that such issues must still go through the administrative process, particularly when judicial review is provided." *Prince George's Cnty. v. Blumberg*, 288 Md. 275, 293 (1980).

Finally, even if exhaustion were not required for the takings claim raised here, a plaintiff in a takings suit must still have a ripe claim. *See Williamson Cnty. Reg'l Planning Comm'n v. Hamilton Bank of Johnson City*, 473 U.S. 172, 186-87 (1985) (explaining that a takings claim is not ripe for adjudication when there is no final agency decision and the potential for "administrative solutions" therefore remains (internal quotation omitted)). In other words, plaintiffs in takings cases must obtain a final agency decision before filing suit; otherwise, there is no way to determine for sure whether a taking has occurred, the extent of the taking, or the amount of just compensation.

Under Maryland law, the potential for "administrative solutions" remains until the Tax Court has issued a final decision. *Williamson Cnty.*, 473 U.S. at 187. The Tax Court reviews the Comptroller's decision *de novo*, Md. Code Ann., Tax-Gen. § 13-523, and on judicial review, the Maryland courts review the decision of the Tax Court, which is itself an administrative agency, and not the decision of the Comptroller, *see Comptroller v. Johns Hopkins Univ.*, 186 Md. App. 169, 188–89 (2009). Therefore, until the plaintiffs receive a final decision from the Tax Court, there is no way for this Court to determine the extent of the alleged taking for those plaintiffs, and the plaintiffs' takings claim must be dismissed. In fact, even if the Comptroller's decision were the final agency decision

that ripened the plaintiffs' takings claim, some of the plaintiffs have failed to obtain a final decision from the Comptroller on their refund requests. At the very least, those plaintiffs do not have a ripe claim.

CONCLUSION

The complaint should be dismissed.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I certify that on this 19th day of February, 2016, a copy of the Defendants' Reply Memorandum in Support of Motion to Dismiss was served by first-class mail on:

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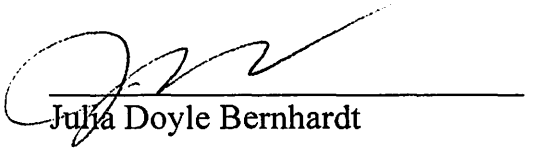

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