

Justices Get Chance To Shore Up Internal Consistency Test

By Maria Koklanaris

Law360 (August 2, 2019, 8:36 PM EDT) -- The U.S. Supreme Court could have the opportunity to draw a bright line on the internal consistency test by picking up a challenge to New York's denial of offsetting credits for taxes paid to another state on intangible income.

Shoe designer Sam Edelman and his wife are domiciled in Connecticut but are considered statutory residents of New York for spending more than 183 days in the state each year. They claim New York's taxation of their intangible income without an offsetting credit for taxes also paid to Connecticut on the same income violates the dormant commerce clause of the U.S. Constitution.

Lower courts have said that this double taxation of the Edelmans' intangible income does not violate the commerce clause, but the Edelmans have asked the justices to apply the internal consistency test, which generally prevents the same income from being taxed more than once, as it did in its 2015 holding in *Comptroller of the Treasury v. Wynne*.

As described in the *Wynne* opinion, the internal consistency test “looks to the structure of the tax at issue to see whether its identical application by every state in the union would place interstate commerce at a disadvantage as compared with commerce intrastate.”

If the justices agree to take the case, they could affirm *Wynne*'s finding that violating internal consistency also violates the commerce clause and that both lower courts and states should take heed, said Michael Lurie of Reed Smith LLP.

“I think they would send a message that internal consistency is a real test and has teeth to it,” said Lurie, who helped author a brief on behalf of the Edelmans. “This tax is clearly internally inconsistent. To courts they would say, ‘Our precedent really means what it says — apply the internal consistency test.’ To states they would say, ‘Don't have taxes that fail this test.’”



As the U.S. Supreme Court decides whether to take up a case regarding taxation of a couple's income by New York and Connecticut, the court likely will compare and contrast it with the *Wynne* case decided in 2015. (AP)

As it decides whether to take the case, the court will likely compare and contrast Edelman with Wynne. For the Edelmans and several amici, this is the key concern — they want Wynne to control. In Wynne, the court found the Maryland tax structure unconstitutional because it allowed credits against the state income tax for taxes Brian and Karen Wynne paid in other states, but did not allow a credit for local taxes paid. To the Edelmans and their amici, this is similar to what the Edelmans face.

However, the state of New York has emphasized differences between Edelman and Wynne, and won in the lower courts. One major difference is that in Wynne, the income in question was clearly sourced. That is not so in Edelman. Another question concerns discrimination. The Maryland scheme faced by the Wynnes was discriminatory, the justices found. Lower courts have agreed with New York that the Edelmans were not necessarily discriminated against just because they were taxed in two states.

But the Edelmans have been discriminated against, said Mitchell Newmark of Morrison & Foerster LLP. He said the court should look to internal consistency, decide that Wynne has been violated, and take the case. Newmark told Law360 that New York state does not get to decide when a domiciliary of Connecticut gains or loses protection from double taxation.

“Does a Connecticut domiciliary have any more or less constitutional protection depending on whether New York has a statutory residency standard of more than 300 days, 183 days or 50 days?” Newmark said. “How can the Constitution's protections be dependent on whether New York in its infinite wisdom wants to say you are here in New York, too? The Edelmans are, as are we all, deserving of an answer as were the Wynnes.”

In finding for New York against the Edelmans, lower courts found the controlling case to be one that predates Wynne by 17 years. In *Tamagni v. Tax Appeals Tribunal* of 1998, the New York Court of Appeals did not look to internal consistency. It found that New York's statutory residency law did not apply to an interstate market and thus did not violate the dormant commerce clause.

If the justices decide *Tamagni* still controls, it is highly unlikely they will grant certiorari, said Matthew E. Foreman of Matthew E. Foreman PC.

“They would think, we get what you're saying, but there's really no interstate commerce angle,” Foreman said. “You decided to live in state A and have a statutory residency in state B. That's on you; that's not commerce.”

However, Richard Pomp, professor of taxation at the University of Connecticut School of Law, said the justices should no longer look to *Tamagni*. He said *Tamagni*, as applied here, “is not very rigorous and not very sophisticated, and is pre-Wynne.”

That makes the Edelmans' petition worthy of a cert grant, Pomp said. But he emphasized that it's far from clear the court will view it that way. Pomp said the court might be concerned that the New York statute goes against Wynne and internal consistency, but may want to wait and see if other states confront questions of how to tax statutory residents, and how they handle it.

“I think the court will say not enough time has passed since Wynne and we have to allow time for states to figure this out,” Pomp said. “It's certainly a cert-worthy issue on the merits. But look how long it took the court to revisit *Quill*.” The 1992 decision in *Quill Corp. v. North Dakota* affirmed a physical presence standard for state sales and use taxation that stood until last year's *Wayfair* decision.

Another tax professor agreed that the justices would want to see the states work out the issue of double taxation of dual residents, or if they can't, to have Congress step in. Edward A. Zelinsky of Yeshiva University's Benjamin N. Cardozo School of Law said he was skeptical that the justices would decide that the internal consistency test in Wynne should push them to review the Edelman case.

He said he thought the justices would decide that “any relief should come politically, rather than from the courts.”

--Editing by Robert Rudinger and Tim Ruel.