IN THE SUPREME COURT OF OHIO

JOSH SCHAAD Plaintiff-Appellant, v. KAREN ALDER, et al., Defendants-Appellees	: : : : : : : : :	Case No. 2022-0316 On Appeal from the Hamilton County Court of Appeals, First Appellate District Court of Appeals Case No. C-2100349

BRIEF *AMICUS CURIAE* OF THE OHIO CHAMBER OF COMMERCE IN SUPPORT OF PLAINTIFF-APPELLANT JOSH SCHAAD

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TABLE OF CONTENTS

Page(s)

TABLE OF AUTHORITIES

Page(s)

Cases

Other Authorities

Rules

Constitutional Provisions

INTRODUCTION

Beginning in 2020, as a result of the COVID-19 pandemic, employers in Ohio and across the U.S. implemented work-from-home policies in response to state-mandated stay-at-home orders. Consequently, many employees who had previously physically worked in their employer's office were now performing services in a tax jurisdiction (whether a locality or a state) different from that of their employer, *e.g.,* working from home. As pandemic restrictions lifted, businesses sought to bring their workers back to the office, but many employees are demanding the continued flexibility to work remotely full (remote) or part time (hybrid).[1] So, as remote work becomes a more permanent part of the American employment landscape, uncertainty has arisen in how employers and employees address state – and especially local – income tax withholdings, payment, and liability. Individuals are generally subject to income tax in the jurisdiction where the income producing activity occurred; so, an employee who works in an employer's office is subject to that jurisdiction's tax. But, many employers are withholding local taxes based on the employer's location versus where the income producing activity occurred (*e.g.,* the home office). The issue before the Court is which municipality may tax the income of a nonresident versus withhold tax, consistent with Due Process. This important issue impacts many thousands of Ohio employees who worked at their employer's location prior to the pandemic but now work somewhere else.

STATEMENT OF INTEREST OF *AMICUS CURIAE* THE OHIO CHAMBER OF COMMERCE

Pursuant to S. Ct. Prac. R. 16.06, the Ohio Chamber of Commerce ("Ohio Chamber") submits this brief as *amicus curiae* in support of Plaintiff-Appellant Josh Schaad in the above-captioned matter.

[1] *See* Power, Tracey, *Remote work is here to stay. Are you ready to embrace the shift?* (December 10, 2021), available at https://www.benefitnews.com/opinion/remote-work-trends-are-on-the-rise (accessed July 19, 2022).

Founded in 1893, the Ohio Chamber is Ohio's largest and most diverse statewide business advocacy organization, representing businesses ranging in size from small, sole proprietorships to some of the largest U.S. companies. It works to promote and protect the interests of its more than 8,000 members while building a more favorable business climate in Ohio by advocating for the Ohio business community's interests on matters of statewide importance. By promoting its pro-growth agenda with policymakers and in courts across Ohio, the Ohio Chamber seeks a stable and predictable legal system which fosters a business climate where enterprise and Ohioans prosper.

Amicus has an institutional interest here because this Court's opinion would undoubtedly impact *Amicus*' business members operating in Ohio in a realm of uncertainty as to their local tax withholding obligations for employees working remotely as well as these remote workers' own local tax obligations. In addition, the outcome here could impact the taxation of businesses more broadly. Further, this Court's opinion may influence other tax jurisdictions across the nation on this issue, and may thus significantly impact tax administration affecting taxpayers and *Amicus'* business members across Ohio. A holding by this Court allowing a municipality to impose tax on the income of employees based solely on their employers' locations when the employees are performing services elsewhere could have far-reaching adverse, confusing, and inefficient impacts.

STATEMENT OF THE CASE AND FACTS

Amicus curiae assumes, for the purpose of this brief, that the factual and procedural background set out by the Court of Appeals in its decision is correct. *See generally* App. Op. ¶¶ 2-6. *Amicus curiae* therefore relies upon that background as set out by the Court of Appeals. In brief, this case involves legislation enacted to address remote work during the COVID-19 pandemic that provided that an employee who was working from home as a result of state-mandated stay-at-home order was deemed to be working at his employer's location for purposes of the municipal

income tax. Appellant, Josh Schaad, was one such employee, and attempted to seek a refund from the City of Cincinnati for amounts he earned from his Cincinnati-based employer while working outside the city in Blue Ash during much of 2020. The City of Cincinnati denied his request, and Mr. Schaad appealed, citing violations of his Due Process rights.

ARGUMENT AND LAW

The Due Process Clause of the Fourteenth Amendment of the United States Constitution requires the taxing authority to establish 1) "some definite link" between the taxing authority and the person or activity it seeks to tax and 2) "a rational relationship" between the income taxed and the income-producing activity. *Willacy v. Cleveland Bd. of Rev.*, 159 Ohio St.3d 383, 2020-Ohio-314, 151 N.E.3d 561, ¶22 (quoting *Miller Bros. Co. v. Maryland*, 347 U.S. 340, 345, 74 S.Ct. 535, 98 L.Ed.744 (1954)); *Willacy* at ¶22 (citing *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 273, 98 S.Ct. 2340, 57 L.Ed.2d 197 (1978)). Yet here, the municipality, with which the employee has no connection, has imposed tax on an employee's income from services performed outside of that municipality – based solely on their employer having an office there. Such a taxing structure is violative of the employee's Due Process rights. *See Willacy* at ¶22 (quoting *Miller Bros. Co.*, 347 U.S. at 345).

The Ohio General Assembly enacted emergency legislation in response to COVID-19 on March 28, 2020, Am. Sub. H.B. No. 197, Section 29 ("Section 29"), that, *inter alia*, designated the "principal place of work" for income tax purposes (that is, where the income would be deemed to be generated and thus taxed) as the *employer's* location– even when employees worked remotely in another location. Notably, as the General Assembly clarified for the 2021 tax year in Am. Sub. H.B. 110, Section 29 was intended to provide relief to employers who were suddenly faced with the obligation to withhold tax in many more jurisdictions than they were previously as a result of

their employees working remotely; it was *not* intended to change the municipality that could tax an employee's wages.[2] In other words, Section 29 was intended to address tax *withholdings*, not the ultimate *taxability* of income. This comports with well-settled Ohio law. *See Jones v. City of Massillon*, Ohio Bd. Tax App. No. 2018-2137, 2021 WL 1270305 (March 29, 2021) (finding that a city could only tax the portion of a nonresident's income earned for work performed within its borders).

However, prior to this clarification, some municipalities took the position that Section 29 permitted them retain the tax withheld by an employer on employees who were no longer working in the municipality (including the Plaintiff in this case).[3] In effect, this means that an employee residing in municipality A and performing work in municipality A, but employed by a business located in municipality B, was taxed by municipality B solely based on the employer being located in municipality B. The employee does not benefit from the tax-funded services in municipality B, but under Section 29, is forced to contribute to those services. Because there is no "definite link" between the municipality and the employee, or "rational relationship" between income taxed and the income-producing activity, as applied to Plaintiff, Section 29 thus violates the Fourteenth Amendment right of due process. Fourteenth Amendment, Section 1, U.S. Constitution ("[no]

[2] Am. Sub. H.B. No. 110, Sections 610.115 and 757.40 provide that for Tax Year 2021, Section 29 applied to tax withholding obligations only, and was not relevant to a determination of the employee's ultimate tax liability in a particular municipality. When the General Assembly enacted this legislation, the 2020 tax year was closed. As evidenced by the amended legislation, it is possible for Section 29 to be applied constitutionally; in this case, however, the municipality has overstepped its boundaries and has unconstitutionally withheld a refund from Plaintiff, as explained herein.

[3] This was also the mistake made by the City of Massillon in the *Jones* case. *See Jones*, Ohio Bd. Tax App. No. 2018-2137 at 4 ("Massillon's arguments conflate an employer's withholding rules with its authority to tax a nonresident individual. Just as an employer's lack of withholding does not alleviate the employee's income tax liability, neither does an employer's withholding requirement expand the tax due from an employee.").

State [shall] deprive any person of life, liberty, or property, without due process of law."); *Miller Bros.,* 347 U.S. at 345.

I. Proposition of Law No. 1: The Due Process Clause Prohibits a Municipality from Taxing Nonresident Income That is Unconnected to the Municipality When the Nonresident Employee's Services Performed to Earn That Income Occurred Outside of the Municipality.

The Due Process Clause allows municipalities to tax 1) income earned by residents of the municipality and 2) income earned by nonresidents "only if theirs is the jurisdiction 'within which the income actually arises and whose authority over it operates *in rem*.'" *Hillenmeyer v. Cleveland Bd. of Rev.*, 144 Ohio St.3d 165, 2015-Ohio-1623, 41 N.E.3d 1164, ¶42 (citing *Shaffer v. Carter*, 252 U.S. 37, 49, 40 S.Ct. 221, 64 L.Ed. 445 (1920)); *see also Willacy*, 159 Ohio St.3d 383, 2020-Ohio-314, 151 N.E.3d 561, at ¶23-24. The test imposed by this Court, and the United States Supreme Court, is that to satisfy Due Process, there must first be a "definite link" or "minimum connection" established between the local taxing authority and the taxed "person, property or transaction." *Willacy* at ¶22 (citing *Miller Bros. Co.*, 347 U.S. at 345). Accordingly, the local taxing authority here must show a "rational relationship" between the tax imposed and the activity which is taxed. *Willacy* at ¶22 (citing *Moorman Mfg. Co.*, 437 U.S. at 273).

Section 29 cannot authorize a municipality that taxes the income of a nonresident not performing work in the district without violating Due Process. While an individual can waive their constitutional right to due process, the Ohio Legislature cannot abrogate an individual's Due Process rights because they are guaranteed by the Constitution. *See Cleveland Bd. of Educ. v. Loudermill*, 470 U.S. 532, 541, 105 S.Ct. 1487, 84 L.Ed.2d 494 (1985) (quoting *Arnett v. Kennedy*, 416 U.S. 134, 167, 94 S.Ct. 1633, 40 L.Ed.2d 15 (1974)) ("The right to due process 'is conferred, not by legislative grace, but by constitutional guarantee.'").

A. Section 29 illegally mandates an apportionment that is not based on a rational relationship between the jurisdiction imputing the tax and the income-producing person, property, or transaction because the employee performs the work in another jurisdiction.

In enacting Section 29, the Ohio General Assembly impermissibly apportioned the entire taxable activity (*i.e.*, 100%) to the municipality in which none of the taxable income-producing activity took place. The purpose of apportionment is to fairly allocate the taxes collected between the locations in which the taxable activities occurred. When income is earned in multiple jurisdictions, apportionment ensures that each jurisdiction may only tax the portion of income that is rationally related to it, a constitutional requirement, whether because of where the income was earned or how it was earned. *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 169, 103 S.Ct. 2933, 2942, 77 L.Ed.2d 545 (1983) ("Having determined that a certain set of activities constitute a "unitary business," a State must then apply a formula apportioning the income of that business within and without the State. Such an apportionment formula must, under both the Due Process and Commerce Clauses, be fair."). Under Section 29, apportionment is improperly calculated because it allows a municipality to tax 100% of a nonresident's income, despite the income for services performed being earned in another taxing jurisdiction, and which does not fairly reflect the business transacted in the taxing municipality. *See Moorman Mfg.,* 437 U.S. at 274 ("[T]he States have wide latitude in the selection of apportionment formulas and…a formula-produced assessment will only be disturbed when the taxpayer has proved by 'clear and cogent evidence' that the income attributed to the State is in fact 'out of all appropriate proportions to the business transacted… in that State'"); *Hillenmeyer*, 144 Ohio St.3d 165, 2015-Ohio-1623, 41 N.E.3d 1164, at ¶39 (citing Fourteenth Amendment to the U.S. Constitution, Section 1 (stating that the income tax applied was extraterritorial because the city's "power to tax reaches only that portion of a nonresident's compensation that was earned by work performed in" that city)).

In the hypothetical of an employee working in municipality A, but municipality B taxing the employee, the properly apportioned tax would result in municipality A taxing 100% of the employee's income because all of the taxable work was performed in municipality A. *See Hillenmeyer* at ¶42 (citing *Shaffer*, 252 U.S. at 49); *see also Willacy*, 159 Ohio St.3d 383, 2020-Ohio-314, 151 N.E.3d 561, at ¶23. If however, the employee worked 60% in municipality A and 40% in municipality B, then the properly-apportioned tax would result in a similar divide of the employee's taxable income. Put simply, local jurisdictions cannot impose tax for services performed elsewhere.

It should also be noted that subjecting an employer to withholding requirements of a jurisdiction, cannot – consistent with Due Process – preclude an individual employee from receiving a refund from the jurisdiction on which taxes were withheld on the employee.

B. Under substantive due process, a municipality lacks jurisdiction to tax people, property, or transactions outside of its geographical boundaries and cannot rely on the employer's place of business as the constitutionally required connection to impose tax on the employee's income.

A municipality's power to tax income stems from the Home Rule Amendment of the Ohio Constitution; however, Due Process still "requires a municipality to have jurisdiction before imposing a tax." *Willacy* at ¶21. Though a municipality's power results from an act of the Ohio Legislature, the Ohio Legislature's power is constrained by each individual's constitutionally guaranteed Due Process rights. *See Crowell v. Benson*, 285 U.S. 22, 57, 52 S.Ct. 285, 76 L.Ed. 598 (1932) (finding that "[a] State may distribute its powers as it sees fit, provided only that it acts consistently with the essential demands of due process and does not transgress those restrictions of the Federal Constitution which are applicable to State authority."). The Home Rule Amendment allows municipalities "to adopt and enforce *within their limits* such local police, sanitary and other similar regulations, as are not in conflict with general laws." Ohio Constitution, Article XVIII,

Section 3 (emphasis added). One such limit is that the Ohio Legislature cannot abrogate a natural or legal person's due process rights.

Substantive due process rights include the limit imposed on taxing jurisdictions whether a state or a municipality, which can be found in *Wisconsin v. J.C. Penney Co.* and *Angell v. City of Toledo*. Both cases require the municipal income tax to pass the "fiscal relation" test. *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 444, 61 S.Ct. 246, 85 L.Ed. 267 (1940); *Angell v. City of Toledo*, 153 Ohio St. 179, 185, 91 N.E.2d 250, 253 (1950). Under these cases, to determine whether the tax complies with the Due Process Clause, "[t]he simple but controlling question is whether the state [here, the municipality] has given anything for which it can ask return." *J.C. Penney*, 311 U.S. at 444 ([ ] supplied); *Angell*, 91 N.E.2d at 253.

Suppose, for example, that an employee worked for a company located in municipality B but worked from home in municipality A. This employee would perform all work in municipality A, shop and take transportation in municipality A, and enroll her children in municipality A's schools. In this case, the employee would not have any relationship with municipality B; notably, her employer being located in municipality B does not connect the employee herself with municipality B. Because the employee cannot reap the benefits municipality B provides, it would be unfair, unjust, and an infringement on the employee's Due Process rights to be taxed by municipality B. *See Willacy*, 159 Ohio St.3d 383, 2020-Ohio-314, 151 N.E.3d 561 at ¶24. But if instead the employee worked in municipality B, commuted to and from municipality B, and performed taxable activities in municipality B, the employee would benefit from the benefits of municipality B, and it would not be an infringement of her Due Process rights to be taxed by municipality B. *See McConnell v. City of Columbus*, 172 Ohio St. 95, 173 N.E.2d 760 (1961) (holding that because the employee benefitted from the city's tax-funded "protections,

opportunities and benefits," there was a sufficient fiscal relationship that the imputed tax was proper).

Yet, in enacting Section 29, the Ohio General Assembly rejected this common sense (and constitutionally-mandated) approach and required the employee to be taxed regardless of where the employee actually performed their work, regardless of any benefit received (or in this case, not received), and in plain disregard for the employee's constitutional due process rights. To uphold the Court of Appeals would set a perilous and unlawful precedent.

II. Proposition of Law No. 2: This Court Should Not Abandon Long-Standing Due Process Precedent and Clear Guidance That Prohibits Municipalities from Taxing Beyond Their Limits.

Public policy strongly favors a reversal here. For decades, taxpayers have been able to rely on a bright-line rule – taxpayers owe income tax only to the jurisdiction with which that employee has a connection; and its corollary – a municipality can only tax income earned within its limits. *See Angell,* 153 Ohio St. 179, 185, 91 N.E.2d 250*; Willacy,* 159 Ohio St.3d 383, 2020-Ohio-314, 151 N.E.3d 561*; Hillenmeyer,* 144 Ohio St.3d 165, 2015-Ohio-1623, 41 N.E.3d 1164. Under this longstanding precedent rooted in Due Process, municipalities could tax *only*: income earned by residents who live in the municipality and income earned by nonresidents who work in the municipality. The live-or-work test is a common sense one, and it comports with Due Process; moreover, the fact that it has withstood decades of scrutiny has allowed taxpayers (both businesses and individuals) a high degree of certainty in understanding where they may owe tax on their income.[4]

The lower court's ruling flies in the face of that venerable precedent. The lower court has effectively held that a taxpayer's connection to a *third party* – his employer – allows a municipality

[4] As discussed *supra*, there is a difference between a taxing authority imposing a withholding obligation on an employer and imposing a tax on an employee; the latter of which is at issue here.

to impose an income tax on him, even when the taxpayer never avails himself of a single benefit of the municipality. Due process requires more than this indirect and tenuous thread. In today's interconnected world, it is not hard to imagine how municipalities could overstep the bounds of due process to look for any affiliation with nonresident taxpayers, no matter how miniscule.

Moreover, the lower court's ruling creates confusion for employers and employees trying to ascertain where they might be subject to tax. Employers are frequently part of a complex corporate structure; a parent company may be headquartered in one state, while subsidiaries are housed in another. A franchise may be locally owned and operated, but part of a national chain. There is barely a consensus on what constitutes a principal place of business for a company. Where is the "employer" located in these examples? Under the lower court's holding, any link between a company and a municipality could serve as an excuse for the municipality to assert tax on a nonresident employee. This uncertainty does not exist under the long established rule – a municipality could only subject a nonresident employee to tax on their income if they worked there. The line is clear and expectations settled. Those with unique circumstances, such as frequent travel or hybrid remote and in-office work arrangements, could either adjust their withholdings or seek refunds if the tax imposed did not reflect work performed and thus income earned in the municipality. Nonresident employers and employees alike did not need to be concerned with whether they had somehow submitted to a taxing jurisdiction without their knowledge or intent. Upholding the lower court would blur that bright line, if not erase it entirely.

Multi-state and multi-locality taxation is a huge compliance burden for businesses; in absence of federal legislation modernizing the tax system (*e.g.,* Remote and Mobile Worker Relief Act), companies are often left to interpret the tax statutes and regulations of dozens if not hundreds of jurisdictions. This compliance burden has increased in the wake of COVID-19, as workers have

continued to demand remote working arrangements, thus exposing employers to new tax withholding obligations and nexus concerns. Section 29 and the lower court's interpretation of it would muddy the waters even further, and would represent an unprecedented and unconstitutional extraterritorial expansion of municipal income taxes. Ohio taxpayers deserve clear and constitutional expectations when it comes to tax on their income.

The rule prior to the enactment of Section 29 was settled and comported with due process. There is no compelling reason to abandon it now. *Amicus* respectfully urge this Court to reverse the Court of Appeals.

CONCLUSION

Section 29, the City of Cincinnati's imposed tax on Mr. Schaad, and the lower courts' decisions upholding the imputed tax should be overturned because Mr. Schaad performed all taxable activities outside of the City of Cincinnati's jurisdiction; therefore Cincinnati's tax, pursuant to Section 29, is extraterritorial and contrary to the Due Process Clause. Section 29 unconstitutionally allows a tax and apportionment in favor of a municipality, unrelated to the income earned therein. Facilitating a municipality to impose tax on 100% of a nonresidents' income solely because their employer is located in the municipality violates due process, and is contrary to decades of clear precedent. This Court should uphold the venerable bright-line test that has governed municipal income tax in this state since its inception. For the foregoing reasons, *Amicus* respectfully requests that the Court overturn the Court of Appeals' judgment affirming the dismissal of the case.

Respectfully submitted,

/s/ Mark A. Loyd

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CERTIFICATE OF SERVICE

The undersigned hereby certifies that a copy of the foregoing brief in support of Plaintiff-Appellant Josh Schaad was served by electronic mail this 15th day of August, 2022 upon the following counsel:

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