ORIGINAL

IN THE SUPREME COURT OF OHIO

OHIO GROCERS ASSOCIATION, et al.,	:	**Case No. 2008-2018**
Plaintiffs-Appellees,	:	**Appeal from the Franklin County Court of Appeals, Tenth Appellate District**
v.	:	
RICHARD A. LEVIN, Ohio Tax Commioner	:	**Court of Appeals Case No. 07AP-813**
Defendant-Appellant.	:	

BRIEF OF *AMICI CURIAE* THE BUCKEYE INSTITUTE FOR PUBLIC POLICY SOLUTIONS AND THE TAX FOUNDATION IN SUPPORT OF PLAINTIFFS-APPELLEES OHIO GROCERS ASSOCIATION, et al.

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INTEREST OF *AMICUS CURIAE*

The Buckeye Institute for Public Policy Solutions is a non-profit research organization formed in 1994 to support public policies that advance liberty, individual rights, and a strong economy in Ohio. The Buckeye Institute for Public Policy Solutions is a nonpartisan research and educational institute devoted to individual liberty, economic freedom, personal responsibility and limited government in Ohio.

The Buckeye Institute develops ideas with the assistance of 45 scholars from 23 universities and colleges throughout Ohio, disseminates them through our publications, lectures and special events, and distributes them to policy makers and key opinion leaders to make meaningful change. The Buckeye Institute's work has made inroads in numerous areas: identifying regulations that stifle economic growth, demonstrating the benefits of market-based education reform, publicizing free market alternatives in health care, showing the savings that competition will bring to state and local governments, and identifying how to cut sales, income, property and business taxes and questionable government spending.

The Buckeye Institute's 1851 Center for Constitutional Law is dedicated to protecting Ohioans' control over their lives, their families, their property, and ultimately, their destinies. More pointedly, the 1851 Center has an interest in protecting Ohioans' rights to be free from unconstitutional taxation, and relatedly, in advancing statewide prosperity. *Amicus* thus has a strong interest in this Court's ruling on whether the state of Ohio imposes an excise tax on the purchase of food in Ohio: all Ohioans purchase food, and increasing the costs of such purchases leaves Ohioans less disposable income with which to carry out their owns wills.

The Tax Foundation is a non-partisan, non-profit research institution founded in 1937 to educate taxpayers on tax policy. Based in Washington, D.C., the Foundation's economic

and policy analysis is guided by the principles of neutrality, simplicity, transparency, and stability. The Tax Foundation makes information about government finance more understandable, such as with its annual calculation of "Tax Freedom Day," the day of the year when taxpayers have earned enough to pay for the nation's tax burden and begin earning for themselves.

The Tax Foundation educates the legal community and the general public about economics and taxpayer protections and advocates that judicial and policy decisions on tax law promote principled tax policy. Recent federal and state tax-related cases in which the Tax Foundation has participated as *amicus curiae* include *Department of Revenue of Kentucky v. Davis*, 128 S. Ct. 1801 (2008); *CSX Transportation, Inc. v. Georgia State Board of Equalization*, 128 S. Ct. 467 (2007); *DaimlerChrysler Corp. v. Cuno*, 547 U.S. 332 (2005); *Heatherly v. State*, --- S.E.2d ----, 363 N.C. 115 (2009), and *Bonner v. Indiana*, No. 49S02-0809-CV-525 (Ind. 2008).

This case involves an important issue of tax policy. By addressing the proper definition of "excise tax" as applied in this case, the opinion of this Court will not only have an impact on Ohio taxes, but its rationale will likely aid other states confronting similar questions. Therefore this decision and the rationale behind it will have a large impact upon deciding the legality of taxes throughout the country.

The Tax Foundation is in a unique position to aid this Court because it has conducted extensive research into taxes in general and excise taxes in particular, and the approaches taken by various courts, the academic community, and various legislative bodies. Accordingly, the Tax Foundation has an institutional interest in this case.

STATEMENT OF THE CASE AND FACTS

The Ohio Constitution authorizes "the General Assembly to enact 'excise and franchise taxes'," but "prohibits...transactional taxes on retail and wholesale food sales and purchases."[1] The Ohio Constitution provides that "no excise tax shall be levied or collected upon the sale of purchase of food for human consumption off the premises where sold."[2] Furthermore, it states that "no sales or other excise taxes shall be levied or collected (1) upon any wholesale sale or wholesale purchase of food for human consumption, its ingredients or its packaging."[3] These provisions were "aimed at 'consumer' purchases" and were intended to prohibit the levying of taxes and their burdens "upon food purchased by the public at the grocery store."[4] In sum, these constitutional provisions establish that the state is prohibited from enacting any transactional tax on the sale or purchase of food in Ohio.

Meanwhile, Ohio's Commercial Activities Tax imposes a tax upon Ohio's food suppliers that is based upon how much food they sell, is permitted to be passed on to the consumer, and is in fact passed on to the consumer in the form of higher prices of food in Ohio.

The parties and other *amici* have already supplied the Court with extensive briefings of the facts and procedural history of this case. These briefings include a sufficient description of what the CAT is, and how it operates. Accordingly, *amici* will defer to the facts outlined heretofore. This deference is given with the caveat that the history and operative

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1 Appellant's Brief, p. 12.

2 Ohio Const. art. XII § 3(C).

3 Ohio Const. art. XII §13.

4 *Cameron Coca-Cola Bottling Co. v. Tracy* (July 28, 1993), Franklin Co. C.P. 93CVH02-729 (Ex. 20, Appx. at A-178) at 25.

economic effects of excise taxes, as chronicled below, are facts, but are facts more appropriate for the Argument portion of this brief.

ARGUMENT

A. Courts must look beyond the label affixed by the legislature, and examine the operative effect of a tax when determining its type and effect.

No deference is due to the legislature's determination that Ohio's Commercial Activities Tax is a "franchise tax" when its operative effect is that of an excise tax. State and federal courts, including Ohio's, have historically looked beyond such labeling, instead examining how the charge actually operates. As Justice Brandeis wrote for the U.S. Supreme Court in 1921, "[t]he name by which the tax is described in the statute is, of course, immaterial."[5] Since that time, a litany of federal courts have reached this same conclusion: when ascertaining the nature or character of a tax, its "substance," "incidence," "operation," "essential nature," and "real object purpose and result," are determinative.[6]

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5 *Dawson v. Kentucky Distilleries & Warehouse Co.*, 255 U.S. 288, 292 (1921).

6 *See, e.g., Weiss v. McFadden*, 120 S.W.3d 545, 553 (Ark. 2003) ("[I]n the present case, the tax is not transformed into a lawful income tax just because the State asserts it is an income tax."); *Western Air Lines, Inc. v. Hughes County*, 372 N.W.2d 106, 109 (S.D. 1985) ("The name by which a tax is described in the statute is, of course, immaterial. Its character must be determined by its incidents. . . ."); *Emerson College v. City of Boston*, 462 N.E.2d 1098, 1105 (Mass. 1984) ("Ultimately, however, the nature of a monetary exaction 'must be determined by its operation rather than its specially descriptive phrase.'"); *Bishop v. District of Columbia*, 401 A.2d 955, 958 (D.C. App. 1979) ("As to the characterization of a tax, it is fundamental that the nature and effect of a tax, not its label, determine if it is an income tax or not."); *Weekes v. City of Oakland*, 579 P.2d 449, 467 (Cal. 1978) ("Although the instant tax is designated a 'license fee,' such declaration is not determinative. This court must look to substance and not mere form."); *Gaugler v. City of Allentown*, 189 A.2d 264, 265 (Pa. 1963) ("[T]he substance of the tax measure determines its true nature, rather than the label placed upon it."); *Gunby v. Yates*, 102 S.E.2d 548, 551 (Ga. 1958) ("The legislature's characterization of the amounts collectible by a public officer for services rendered as being fees is not controlling on the question of whether they constitute fees or taxes, if the burden imposed is devoid of the essential nature of fees."); *City of New Orleans v. Christian*, 87 So.2d 6, 8 (La. 1956) ("This court has held that the fact that an excise tax is denominated a license is of no importance in determining the true nature of the tax. The name by which a tax is described in the statute is immaterial, its character must be determined by its incidents."); *Commonwealth v. Baltimore Steam Packet Co.*, 68 S.E.2d 137, 146 (Va. 1951) ("But what it is called is not necessarily what it is. It is well settled that the name by which it is called is immaterial; that it is not a matter of labels; that the incidence of the tax provides the answer; that the operation of the statute and not its descriptive label

Courts of other states also look to the substance of a tax when analyzing its type, nature, and constitutionality. These courts hold that "the true economic impact of a tax is what ultimately determines its nature."[7] Another clear expression of this principle, in the analogous tax/fee analysis, is as follows: "[t]he tax/fee question is a legal determination, based on an independent review of the facts and regardless of the terminology used by the government."[8]

Most importantly, Ohio Courts definitively abstain from deferring to legislative nomenclature, instead examining the operative effect of a charge when typecasting it. In 1952, in *State, ex rel. Gordon, v. Rhodes*, the Ohio Supreme Court scrutinized whether revenues derived by a municipality from on-street parking meters were taxes or fees.[9] The court ruled that "[w]e recognize that simply labeling an assessment a fee does not preclude constitutional inquiry by this court. While there is no single dominant factor that mandates finding that the assessments are fees, a number of pertinent facts, taken in the aggregate, are persuasive."[10] The court further

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is what governs."); *Hukle v. City of Huntington*, 58 S.E.2d 780, 783 (W.Va. 1950) ("It is a well-nigh universal principle that courts will determine and classify taxation on the basis of realities, rather than what the tax is called in the taxing statute or ordinance."); *City of Louisville v. Sebree*, 214 S.W.2d 248, 253 (Ky. 1948) ("But the character of any tax is to be determined by its incidents, and the name by which it is described in the legislation imposing it is without significance."); *Flynn v. City and County of San Francisco*, 115 P.2d 3, 6 (Cal. 1941) ("The nomenclature is of minor importance, for the court will look beyond the mere title or the bare legislative assertion that the provision is for a license to see and determine the real object, purpose and result of the enactment."); *Smith v. Carbon County*, 63 P.2d 259, 260 (Utah 1936) ("The mere fact that the Legislature has characterized them as fees is not controlling if the burden sought to be imposed on estates is devoid of the essential characteristics of a fee."); *Jensen v. Henneford*, 53 P.2d 607, 610 (Wash. 1936) ("The Legislature may declare its intended purpose in an act, but it is for the courts to declare the nature and effect of the act. The character of a tax is determined by its incidents, not by its name."); *Sparling v. Refunding Bd.*, 71 S.W.2d 182, 186 (Ark. 1934) ("It may be well to state at the outset that the fact that the act designates the tax as 'a privilege or excise tax' does not necessarily make it so. . . .").

7 *Owens v. Fosdick,* 153 Fla. 17, 13 So.2d 700 (1943); *State ex rel. McKay v. Keller,* 140 Fla. 346, 191 So. 542 (1939).

8 *Issac v. City of Los Angeles* (1988), 66 Cal.App.4th 586, at 596.

9 *State, ex rel. Gordon, v. Rhodes* (1952), 158 Ohio St. 129, 48 O.O. 64, 107 N.E.2d 206.

10 *State, ex rel. Petroleum Underground Storage Tank Release Comp. Bd.* v. Withrow (1991), 62 Ohio St.3d 111, 579 N.E.2d 705.

concluded that "[w]e must examine *the substance* of the assessments and *not merely their form.*"[11]

In 1962, in *State, ex rel. Youngstown Sheet & Tube Co., v. Leach*, the Ohio Supreme Court again looked beyond the state's label, to the *operative effect* of the charge. In that case, the Court concluded that employer contributions to the Unemployment Compensation Fund were in fact taxes.[12]

In 1978, the Ohio Supreme Court again disregarded the label affixed by a local legislature that sought to cast unlawful taxes as lawful fees.[13] The Court looked to the *operative effect* and result of the charge in establishing the rule that "[w]ater charges that exceed the cost of the service constitute taxes.[14]

In 1990, the Supreme Court of Ohio yet again disregarded legislative nomenclature. In *Granzow*, the Court established a tax/fee distinction based upon the *substance* of the charge: "a 'fee' is in fact a 'tax' if it exceeds the 'cost and expense' to government of providing the service in question."[15] Several years later, in *Bldg. Industry Assn. of Cleveland v. Westlake*, the Court of Appeals for the Eight District of Ohio applied *Granzow* to find that a local ordinance was not a fee, but a tax.[16]

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11 *State, ex rel. Petroleum Underground Storage Tank Release Comp. Bd. v. Withrow* (1991), 62 Ohio St.3d 111, 579 N.E.2d 705, citing *Shkurti, supra,* 32 Ohio St.3d at 428, 513 N.E.2d at 1336. Emphasis Added.

12 *State, ex rel. Youngstown Sheet & Tube Co., v. Leach* (1962), 173 Ohio St. 397, 20 O.O.2d 33, 183 N.E.2d 369.

13 Cincinnati v. Roettinger (1922), 105 Ohio St. 145.

14 Cincinnati v. Roettinger (1922), 105 Ohio St. 145.

15 *Granzow v. Bur. of Support of Montgomery Cty.* (1990), 54 Ohio St.3d 35, 38.

16 *Bldg. Industry Assn. of Cleveland v. Westlake* (1995), 103 Ohio App.3d 546.

The next year, in *State, ex rel. Petroleum Underground Storage Tank Release Comp. Bd. v. Withrow,*[17] the Ohio Supreme Court disregarded the label of a charge, again looking to its operative effect instead. In that case, the Court concluded that a charge labeled an "assurance fund" "more closely resembles enforcement by the state of its taxing power."[18]

A strong policy rationale underlies these precedents, applies in this instance, and warrants that this Court look beyond the label of the tax and apply exacting scrutiny. If the Court deferred to legislative nomenclature, it would empower to the legislature to defy constitutional limitations, and exercise plenary taxing power. Such is the case here. The Tax Commissioner essentially argues that it may impose a "privilege of doing business in Ohio" tax that is measured by the amount of food sold, and that it may do so without violating the constitutional proscription against sales and excise taxes on food.

A simple illustration demonstrates this position to be subterfuge: imagine that Ohio's Constitution contained an absolute prohibition on income taxation, and that the tax commissioner sought to levy a tax on the "privilege of living in Ohio, as measured by income." Would this Court seriously entertain the argument that such a tax was anything other than an income tax?

Other states lend no credence to such a pretext. The State of Florida, for example, has such a constitutional prohibition on the taxation of income. Like Ohio, Florida looks beyond labels, to the substance of a tax.[19] In the 1930s, the City of Tampa attempted to impose a

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17 *State, ex rel. Petroleum Underground Storage Tank Release Comp. Bd. v Withrow* (1991), 62 Ohio St.3d 111, 579 N.E.2d 705.

18 Id.

19 Id.

"licensing fee" on attorneys as measured by the attorney's income.[20] The provision in dispute, much like the Ohio CAT, imposed a graduated tax, measured by earnings:

> When the gross receipts derived from the practice of the profession during the 12 months period ending September 30, 1938 was $2,500.00 or less_____$25.00. When the gross receipts for the said twelve months period was in excess of $2,500.00 the license tax shall be measured by an amount equal to $25.00 for the first $2.500.00, plus an amount equal to $10.00 for each additional $1,000.00, using said gross receipts as a measure.[21]

With Florida's constitutional prohibition against income taxes firmly in place, the Florida Supreme Court concluded that "The relator is an attorney and the receipts, either net or gross, cannot be classified as an excise tax, sales tax or tax on the privilege of practicing law within the meaning of Section 11 of Article IX whereby it is unlawful to levy on the income of citizens or residents of Florida on the part of the State of Florida."[22]

Just as Tampa's "license tax as measured by income" amounted to an unconstitutional income tax, Ohio's "tax on the privilege of doing business in Ohio as measured by gross receipts" is unconstitutional as applied to food. Tax receipts collected from Ohio grocers are a direct product of the amount of food sold by Ohio grocers. Concomitantly, as will be discussed *infra*, the Grocers pass the cost of this tax on to Ohioans, in the form of higher food prices. Resultantly, by measuring the tax as a function of the amount of food sold, the CAT taxes the sale of food in the same way that the city of Tampa sought to tax the sale of attorney labor. Thus, in *McKay*, the Florida Supreme Court nicely illustrates the folly of the Tax Commissioner's "as measured by" subterfuge. Label aside, the result of the CAT, in relation to

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20 *State ex rel. McKay v. Keller*, 140 Fla. 346, 191 So. 542.

21 Id.

22 Id.

food sales, is clearly inconsistent with the relevant provisions of Article XII of the Ohio Constitution.

The above precedents and policy considerations demonstrate that Ohio courts do not and should not defer to the label affixed by the state or local legislature when determining (1) the type of tax; or (2) the tax's constitutionality. Consequently, no deference is due to the state's label of this tax as a "franchise tax," "gross receipts tax," and/or "commercial activities tax." Instead this Court must inquire into the "substance" of the charge on food to determine whether it is a "sales or other excise tax * * * upon the sale or purchase of food." In so doing, it must necessarily conclude that the CAT, as applied to food, is precluded by Section 3(C), Article XII of the Ohio Constitution and Section 13, Article XII of the Ohio Constitution.

B. <u>In operation, the CAT, as applied to food, is an unconstitutional excise tax</u>.

The Court's analysis in this case necessitates a clear understanding of the term "excise tax." To this end, American history, case law, and economic understanding all provide needed guidance.

i. The history of excise taxes demonstrates that the CAT is an excise tax.

The Tax Commissioner's recitation of the history of Ohio's excise taxes[23] is incomplete. It neglects to note the historically disfavored status of excise taxes in the United States of America, and the historical recognition that any tax that ostensibly results in the consumer paying a higher price is an excise tax. The English Parliament first imposed excise taxes on items such as liquor, tea, coffee, soap, and salt in 1641, during the English Civil War, as

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[23] Appellant's Brief, pp. 6-8.

a temporary measure.[24] Parliament later infamously expanded such excise taxes to the American Colonies, thereby precipitating the American Revolution.[25] Because such taxes impacted the price of commodities, they were greatly unpopular: famous writer Samuel Johnson defined "excise" in his *Dictionary of the English Language* as "a hateful tax levied upon commodities, and adjudged not by common judges of property, but by wretches hired by those to whom the excise is paid."[26]

The first excise tax adopted by the United States government—indeed, the first federal tax of any kind—was the excise tax on whiskey adopted in 1791. Following the suppression of the Whiskey Tax Rebellion in 1794, where farmers had refused to pay the tax, additional taxes were imposed on carriages (1794), and later liquor, snuff, sugar refining, auction sales, and salt.[27] Mostly repealed by the Jefferson Administration, federal excise taxes were readopted and expanded in scope during the War of 1812, the Civil War, the Spanish-American War, World War I, the Great Depression, World War II, and the Korean War, leaving the federal system primarily with major excise taxes on liquor, tobacco, and gasoline, and minor ones on other items (such as transportation facilities). These taxes are recognized, in light of the above history and understanding, to be excise taxes, even though they often tax the producer of the product directly, and therefore the consumer, indirectly.

ii. Applicable precedent shows the CAT to be an excise tax.

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24 *See, e.g.*, Brenda Elvington, "Excise Taxes in Historical Perspective," *in* William F. Shughart II, TAXING CHOICE: THE PREDATORY POLITICS OF FISCAL DISCRIMINATION 33 (1997).

25 Id.

26 Samuel Johnson, DICTIONARY OF THE ENGLISH LANGUAGE (1785).

27 *See* Elvington, "Excise Taxes in Historical Perspective," 34-35.

The CAT tax, as applied to food, is, by definition, an unconstitutional excise tax. Historically, excise taxes (or sometimes simply "excises") are a class of taxes distinct from property taxes, income taxes, and poll taxes.[28] The United States Supreme Court has clarified that excise taxes are imposed on "consumption" (the purchase of commodities) but generally not remitted directly by the consumer: "[e]xcise is defined to be an inland imposition, sometimes upon the consumption of the commodity, and sometimes upon the retail sale; *sometimes upon the manufacturer, and sometimes upon the vendor.*"[29]

The CAT levies a monetary imposition upon vendors of food, and ostensibly, upon consumers. By legal definition, it is thus an excise tax.

iii. Principles of economics dictate that the CAT is an excise tax.

The CAT, as applied to food, is an unconstitutional excise tax because its costs are borne by consumers. Excise taxes may be imposed in the form of *general excise taxes* (such as Hawaii calls their sales taxes) or *selective excise taxes* (e.g., taxes on the sale of particular products), although the line between the two is unclear. Most sales taxes purport to tax the universe of consumption less exclusions, although the net result is that few sales taxes apply to

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[28] *Cf. Hylton v. United States*, 3 U.S. 171, 176 (1796) (Iredell, J., seriatim op.) (classifying federal taxes into the categories of (1) "direct taxes" on people or property, (2) "duties, imposts, and excises" on "articles," and (3) other indirect taxes); *Brushaber v. Union Pac. R.R. Co.*, 240 U.S. 1, 10-11 (1916) (describing the income tax as a "hitherto unknown power of taxation" but a direct tax on individuals).

[29] *Pacific Ins. Co. v. Soule*, 74 U.S. 433, 445 (1868), *citing* Bateman's Excise Law, 96; 1 Story's Constitution, § 953; 1 Blackstone's Commentary, 318; 1 Tucker's Blackstone, Appendix, 341. *See also Saviers v. Smith*, 101 Ohio St. 132, 137-138 (Ohio 1920) (defining excise tax as "a tax imposed on the performance of an act," the "engaging in an occupation, or. . .the enjoyment of a privilege."). Emphasis added.

even a majority of goods and services.[30] However, whether the tax starts by taxing everything and subtracts items out (such as with general sales taxes or gross receipts taxes, including the CAT), or lists each item individually (as in selective excise taxes), it falls under the category of excise taxation.

Typically, an excise tax is not paid directly by the consumer to the government.[31] Even though excise taxes are *legally* remitted by a collector, their cost is *substantively* borne, at least in part, by consumers of the taxed good or service.[32]

This observation is merely attendant to the greater economic understanding that all taxes are paid by people, regardless of who physically remits the check to the government. The actual economic incidence of taxes remitted by businesses falls upon one of three categories of actors: (1) owners or shareholders, in the form of reduced profits; (2) employees, in the form of lower wages; and (3) consumers, in the form of higher prices.[33]

In Ohio, gross receipts taxes are excise taxes.[34] Gross receipts taxes "tax all transactions" that generate the revenue that is used to determine the taxpayer's liability.[35] Just

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30 *See* John L. Mikesell, *State Retail Sales Tax Burdens, Reliance, and Breadth in Fiscal 2003*, State Tax Notes 125 (Jul. 12, 2004) (estimating that the median state sales tax in the U.S. applies to 43.3% of consumption, with Ohio's applying to 39.5% of consumption).

31 *See, e.g.*, United States Census Bureau, *2006 Government Finance and Employment Classification Manual*, Ch. 4 pg. 11 (2006) (defining excise tax as a tax on the "gross receipts of particular businesses"); Tax Foundation, *Federal Excise Taxes*, Project No. 40 (Jun. 1956), *available at* http://www.taxfoundation.org/files/pn40-1.pdf (defining excise tax as a tax on "a particular kind of commodity or service.").

32 *See generally* John R. McGowan, *Excise Taxes and Sound Tax Policy*, Tax Foundation Background Paper No. 18 at 4 (May 1997), *available at* http://www.taxfoundation.org/files/85a28cc81aa689fcf22192219331d87c.pdf.

33 *See, e.g.*, John Mikesell, *Gross Receipts Taxes in State Government Finances: A Review of Their History and Performance*, Tax Foundation Background Paper No. 53 (Jan. 2007), available at http://www.taxfoundation.org/files/bp53.pdf.

34 *See* App. Op. at 151, *citing State ex rel. Cleveland v. Kosydar* (1973), 36 Ohio St.2d 183, 184, 305 N.E.2d 803; *E. Ohio Gas Co. v. Limbach* (1986), 26 Ohio St.3d 63, 66-67, 26 Ohio B. 54, 498 N.E.2d 453.

as all excise taxes do, "gross receipts taxes have long been recognized as being non-neutral," in that they "distort the composition of goods produced in the economy, as well as the structure of firms that provide them."[36] In other words, gross receipts taxes impose additional costs on the commodities or services that they are levied against, forcing the market to compensate for those additional costs and resulting in an allocation of that tax burden.[37] It is generally accepted that the burden of a tax will typically fall "on those least able to alter their behavior in response to the tax."[38]

These general economic understandings were crystallized and applied specifically to Ohio's CAT by the only professional, degreed economist to testify in this case. In his September 8, 2006 Affidavit, Robert Lawson, Professor of Economics, concluded that (1) "[t]here is no relevant economic distinction between a conventional sales tax and the CAT when applied to the gross receipts from the sale of food;" (2) "[t]here is no relevant economic difference between the CAT and a conventional sales tax simply because the former is collected from the seller based upon aggregate gross receipts over a period of time and the latter is collected from the consumer on each separate transaction;" (3) the CAT will increase food prices to consumers, decrease net prices to sellers, and reduce quantities sold, in exactly the same way as a conventional sale tax on

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35 *See generally* Andrew Chamberlain, Patrick Fleenor, *Tax Pyramiding: The Economic Consequences of Gross Receipts Taxes*, Special Report No. 147, Tax Foundation, Dec. 2006 *available at* http://www.taxfoundation.org/files/sr147.pdf

36 Special Report No.147 at 6; *see also* John R. McGowan, *Excise Taxes and Sound Tax Policy*, Tax Foundation Background Paper No. 18 at 6 (May 1997), *available at* http://www.taxfoundation.org/files/85a28cc81aa689fcf22192219331d87c.pdf (stating that excise taxes inherently impose additional burdens on participants in competitive markets).

37 See id.

38 Tax Foundation, *Fiscal Fact* No. 101: Q & A on Carried Interest Debate, Sept. 7, 2007 *available at* http://www.taxfoundation.org/files/ff101.pdf.

the sale of food would have;" and (4) "the CAT and a conventional sales tax are economically indistinguishable."[39]

In *The Economics of the Commercial Activities Tax*, Mr. Lawson explained "the CAT is not 'just like a sales tax;' it is a sales tax. That is, there is no relevant economic distinction between a CAT and a conventional sales tax."[40] As Mr. Lawson echoes the general economic understandings articulated above, noting that "[w]hether the tax is levied at the point of sale and charged to the buyer or after the point of sale and charged to the seller is economically irrelevant."[41] Mr. Lawson further explains how, arithmetically, the CAT is identical to the general sales tax, and closes with the statement "I conclude that Ohio's CAT is a sales tax."[42]

In other words, the CAT inherently imposes its tax burden directly upon consumers because they are the parties least able to avoid it. In fact, the CAT itself acknowledges this result: it allows Ohio grocers and their suppliers to "recover the tax" by raising prices on the consumers.[43] Accordingly, the burden of paying the CAT falls on the consumer.

Indeed, it is impossible "for lawmakers to craft an economically neutral gross receipts tax" that will not somehow have an impact on the consumers involved in the taxed

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39 September 8, 2006 Affidavit of Robert Lawson.

40 Id.

41 Id.

42 Id., at p. 6.

43 R.C. 5751.02(B) ("Nothing in division (B) of this section prohibits a person from including in the price charged for a good or service an amount sufficient to recover the tax imposed by this section.")

transactions.[44] As a tax that substantively applies to Ohio grocers' sales of food, the CAT increases the cost of completing those individual transactions, and thus passes higher prices on to the consumers. Accordingly, the foregoing analysis demonstrates that the CAT is an excise tax, and excise taxes on food are prohibited by Article XII of the Ohio Constitution.

If the purpose of Ohio's constitutional prohibition against levying excise taxes on the sale of food was to leave food free from taxation, then the increased financial burden imposed by the CAT violates that intended purpose. Furthermore, if Ohio's constitutional prohibitions were "aimed at 'consumer' purchases" and were intended to prohibit the levying of taxes and their burdens "upon food purchased by the public at the grocery store,"[45], then the CAT undermines that purpose as well.

C. Ohio public policy considerations weight against levying a tax on food.

The extra-legal public policy arguments of the Tax Commissioner and its *Amici* are greatly dwarfed by policies against (1) imposing a regressive tax on Ohioans' food supply in the midst of an economic downturn; and (2) subsidizing the availability of food with one set of state government programs, while impairing it with another. The Tax Commissioner and its *Amici* make policy contentions that finding the CAT unconstitutional as applied to food would (1) "increase the burden on the rest of the taxpayers who remain subject to the tax;" (2) result in "a shortage of revenue for state and local governments to provide necessary services;" and (3)

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44 Special Report No. 147 at 10.

45 *Cameron Coca-Cola Bottling Co*, (July 28, 1993), Franklin Co. C.P. 93CVH02-729 (Ex. 20, Appx. at A-178) at 25.

"create a favored class of business taxpayers."[46] Not only do these critiques fail to account for the positive results of lower taxation of food, a commodity that every Ohioan must purchase, but they are greatly outweighed by regressive taxation of the indigent, and the policy inconsistency of taxing Ohioans to administer food availability programs on one hand while simultaneously taxing all food itself on the other hand.

i. The CAT is a regressive tax on food.

Having established that Ohio consumers pay the CAT, the Court can conclude that the CAT is "regressive," meaning that it impacts low income Ohioans to a greater extent than high income Ohioans. A "regressive" tax, as opposed to a "progressive" tax, is one that "imposes a greater burden (relative to resources) on the poor than on the rich—there is an inverse relationship between the taxpayer's ability to pay as measured by assets, consumption, or income."[47] The regressivity of a particular tax often depends on the propensity of the taxpayers to engage in the taxed activity relative to their income. Taxes like the Ohio CAT, and other excise taxes on food and other essential goods and services, are regressive because essentials such as food tend to comprise a higher percentage of the budget of a person or family with a lower income.

This understanding, as applied to food, is best expressed in a law of economics known as Engel's Law. Engel's Law simply observes the economic reality that "the proportion

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46 See generally, Appellant's Brief. See also Amici Brief of The Ohio Manufacturer's Association, et al. , p. 16.

47 See James, Simon (1998), A Dictionary of Taxation, Edgar Elgar Publishing Limited: Northhampton, MA; Hyman, David M. (1990), Public Finance: A cotemporary Application of Theory to Policy, 3rd, Dryden Press: Chicago, IL.

of income spent on food decreases as income increases, other factors remaining constant."[48] Put another way, an Ohioan who earns $200,000 and an Ohioan who earns $20,000 are likely to spend roughly equivalent amounts of their income on food, even as income increases. For the purposes of example, assume that the average Ohioan spends $5,000 per year on food, and that both earners mentioned above spend approximately $5,000 per year on food. A 1 percent excise tax on food will thus take $50 from each earner. However, that $50 represents a much greater portion of the $20,000 earner's income than of the $200,000 earner's income (.25 percent, as opposed to .025 percent).

Thus an excise tax on food, such as the CAT, is regressive, and more impactful on low-income Ohioans. Insofar as Ohioans agree that it is important to increase rather than restrict the indigent's access to food, the CAT's regressive nature if highly offensive to that important public purpose, and could not be indicative of the legislature's intent.

ii. Applying the CAT to food creates conflicts with other Ohio public policies.

Given the regressive nature of the CAT, as applied to food, Ohio's levying of a sales tax on food would conflict with numerous state policies that have been put in place to (1) ameliorate the effects of taxation on low-income Ohioans; and (2) enhance the access to food. There are a plethora of government policies on this front. As one example, the Ohio Department of Job and Family Services and Office of Family Stability maintain a "Food Assistance Policy" that helps indigent families pay for needed food.[49] Through this policy, the agencies issue an "Ohio Directions Card" or "Electronic Benefits Transfer" to indigent Ohioans who cannot afford

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48 See Merella, Vincenzo (2006), *Engel's Law and Commodity Differentiation.*

49 http://jfs.ohio.gov/ofam/cmandfsa.stm.

food.[50] This card is simply a commercial debit/ATM card that the State of Ohio issues to indigent families for the purchase of food. The card is to be used at Ohio grocery stores.

Meanwhile, a federal program known as The Food Assistance Program (TEFAP) "helps low-income people, including elderly people, by providing them with emergency food assistance at no cost."[51] The state of Ohio works off of this program through the Ohio Food Program (OFP), which is funded by the Ohio Department of Job and Family Services through an annual grant for the purchase and distribution of food products by the Ohio Association of Second Harvest Foodbanks to eligible households through the Ohio foodbank network. Under these programs, Ohio government purchases food, from Ohio grocers, for the indigent.[52] Finally, and perhaps most importantly, nearly one in ten Ohioans currently receives food stamps, and the state spends $121 million to administer the program.[53]

In other words, state government taxes all Ohioans to collect the funds necessary to implement and administer programs such as this, whose aims are to enhance the poor's access to food. At the same time, however, the CAT, when applied to food, raises the cost of food on those who can least afford it. Further, it results in the double-taxation of taxpayers, who pay the food tax as consumers, and pay higher taxes to support food programs that are more expensive because the CAT tax raises the purchase price of food purchased through various government programs.

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50 Id.

51 Id.

52 Id.

53 http://www.dispatch.com/live/content/local_news/stories/2008/03/22/foodstamps.ART_ART_03-22-08_A1_NN9NE83.html.

The legislature may not be presumed to have intended such absurd and inconsistent results. Accordingly, the Court should find that the CAT is unconstitutional as applied to food.

CONCLUSION

In conclusion, this Court owes no deference to the legislature's labeling of the CAT as anything other than an excise tax. History, legal definitions, and economic rules all establish that the CAT is an excise tax. Moreover, any policy arguments in favor of the CAT are outweighed by concerns over regressive taxation and the creation of absurd results, such as taxing the food that we, as a society, seek to make more available. As such, Article XII of the Ohio Constitution prohibits application of the CAT to Ohio's grocers.

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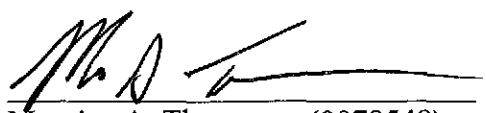

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