MULTISTATE TAX COMMISSION

Maximizing the synergies of multi-state tax cooperation

To: MTC Litigation Committee
From: Lila Disque, Counsel
Date: July 12, 2013
Subject: U.S. Supreme Court Update

Decisions

- **United States v. Windsor (Supreme Court Docket No. 12-307, opinion issued 6/26/13)**
  http://www.supremecourt.gov/opinions/12pdf/12-307_6j37.pdf

  Plaintiff Edith Windsor sued as surviving spouse of a same-sex couple that was married in Canada in 2007 and was resident in New York at the time of her spouse's death in 2009. Windsor was denied the spousal deduction for federal estate taxes under 26 U.S.C. § 2056(A) because Section 3 of the Defense of Marriage Act ("DOMA"), 1 U.S.C. § 7, defines the words "marriage" and "spouse" in federal law in a way that bars the Internal Revenue Service from recognizing Windsor as a spouse or the couple as married. Windsor's claim for a refund is at issue.

  The United States, initially named as the sole defendant, conducted its defense of the statute in the district court up to a point. On February 23, 2011, three months after suit was filed, the Department of Justice declined to continue defending the Act, and members of Congress took steps to support it. The Bipartisan Legal Advisory Group of the United States House of Representatives ("BLAG") retained counsel and took "the laboring oar in defense of the statute." The United States remained active as a party, switching sides to advocate that the statute be ruled unconstitutional. On June 6, 2012, the United States District Court for the Southern District of New York granted summary judgment in favor of Windsor.

  On appeal, United States Court of Appeals, Second Circuit, upheld the lower court's decision. It concluded that review of Section 3 of DOMA requires heightened scrutiny, since A) homosexuals as a group have historically endured persecution and discrimination; B) homosexuality has no relation to aptitude or ability to contribute to society; C) homosexuals are a discernible group with non-obvious distinguishing characteristics, especially in the subset of those who enter same-sex marriages; and D) the class remains a politically weakened minority. It further concluded the class is quasi-suspect (rather than suspect).

  To withstand intermediate scrutiny, a classification must be "substantially related to an important government interest." BLAG advanced two primary arguments for why Congress enacted DOMA. First, it cited "unique federal interests," which include maintaining a

consistent federal definition of marriage, protecting the fisc, and avoiding "the unknown consequences of a novel redefinition of a foundational social institution." Second, BLAG argued that Congress enacted the statute to encourage "responsible procreation." The Court of Appeals found DOMA's classification of same-sex spouses was not substantially related to an important government interest. Accordingly, it held that Section 3 of DOMA violates equal protection and is therefore unconstitutional.

In a 5–4 decision issued on June 26, 2013, the Supreme Court found Section 3 of DOMA to be unconstitutional, "as a deprivation of the liberty of the person protected by the Fifth Amendment." Without specifying an appropriate level of scrutiny, it found that under *Romer*, *Cleburne* and *Moreno*, a more convincing showing of an actual legitimate federal interest underlying the law was required than is usually demanded in rational basis cases. The Court explained that the states have long had the responsibility of regulating and defining marriage, and some states have opted to allow same-sex couples the protection and dignity associated with marriage. By denying recognition to same-sex couples who are legally married, federal law discriminates against them to express disapproval of state-sanctioned same-sex marriage.

- **Hollingsworth v. Perry (Supreme Court Docket No. 12-144, opinion issued 6/26/13)**
  http://www.supremecourt.gov/opinions/12pdf/12-144_8ok0.pdf

  After the California Supreme Court held that limiting marriage to opposite-sex couples violated the California Constitution, state voters passed a ballot initiative known as Proposition 8, amending the State Constitution to define marriage as a union between a man and a woman. A group of same-sex couples filed suit in federal court, challenging Proposition 8 under the Due Process and Equal Protection Clauses of the Fourteenth Amendment, and naming as defendants California's Governor and other state and local officials responsible for enforcing California's marriage laws. California's government officials refused to defend the law, so the District Court allowed the initiative's official proponents to intervene to defend it. After a bench trial, the court declared Proposition 8 unconstitutional and enjoined the public officials named as defendants from enforcing the law. Those officials elected not to appeal, but the proponents of the initiative did.

  The Ninth Circuit certified a question to the California Supreme Court: whether official proponents of a ballot initiative have authority to assert the State's interest in defending the constitutionality of the initiative when public officials refuse to do so. After the California Supreme Court answered in the affirmative, the Ninth Circuit concluded that petitioners had standing under federal law to defend Proposition 8's constitutionality. On the merits, the court affirmed the District Court's order, and subsequently denied rehearing en banc.

  The Supreme Court held that the proponents of the initiative did not have standing to appeal the district court's order.[1] After the District Court declared Proposition 8 unconstitutional and enjoined the state officials named as defendants from enforcing it, the issue of standing under Article III changed. The plaintiffs no longer had any injury to redress—they had won—

[1] Unlike in *Windsor*, where the court found standing. It is unclear why, but appears to be related to the fact that, unlike DOMA's proponents, the proponents of Prop 8 are neither agents nor public officials of the State of California.

and the state officials chose not to appeal. Proponents of the initiative did not have an injury that affected them in a "personal and individual way." Their "generalized grievance" was insufficient to confer standing. Furthermore, they could not be said to act as an agent of the state since an agent owes a fiduciary obligation to the principal, and the initiative's proponents held no such duty toward the people of California. The District Court's decision stands.

- **McBurney v. Young, (Supreme Court Docket No. 12-17, opinion Issued 4/29/2013)**
  http://www.supremecourt.gov/opinions/12pdf/12-17_d1o2.pdf

  The U.S. Supreme Court held that it was not unconstitutional under either the privileges and immunities or the commerce clauses for Virginia to provide the use of information databases (including property tax information) only to Virginia citizens, denying their use to out-of-staters, including data collection companies, and requiring those companies instead to obtain the data physically and in person.

  Two men who were residents of other states attempted to request records under Virginia's Freedom of Information Act (FOIA). However, Virginia's FOIA provides that "all public records shall be open to inspection and copying by any citizens of the Commonwealth," but it grants no such right to non-Virginians. The two filed suit alleging Virginia's FOIA violated the Privileges and Immunities Clause and the dormant Commerce Clause.

  The Petitioners claimed that Virginia's citizens-only FOIA provision violates four different "fundamental" privileges or immunities: the opportunity to pursue a common calling, the ability to own and transfer property, access to the Virginia courts, and access to public information. However, the court found the first three items on that list are not abridged by the Virginia FOIA. The fourth—framed broadly—is not protected by the Privileges and Immunities Clause; the right to access public information is not a "fundamental" privilege or immunity of citizenship. Regarding the dormant Commerce Clause, Virginia's citizens-only FOIA provision neither prohibited access to an interstate market nor imposed burdensome regulation on that market, and therefore did not violate the dormant Commerce Clause; Virginia merely created and provided to its own citizens copies of state records.

- **Dan's City Used Cars, Inc. v. Pelkey, (Supreme Court Docket No. 12-52, opinion issued 5/13/13)**
  http://www.supremecourt.gov/opinions/12pdf/12-52_l537.pdf

  Robert Pelkey brought suit under New Hampshire law against Dan's City Used Cars (Dan's City), a towing company. Pelkey alleged that Dan's City took custody of his car after towing it without Pelkey's knowledge, failed to notify him of its plan to auction the car, held an auction despite Pelkey's communication that he wanted to arrange for the car's return, and eventually traded the car away without compensating Pelkey for the loss of his vehicle.

  The question was how to interpret the preemptive scope of language in the Federal Aviation Administration Authorization Act (FAAAA) prohibiting state law "related to a price, route, or service of any motor carrier . . . with respect to the transportation of property." Specifically,

the issue in the case was whether the FAAAA preempted New Hampshire's statutory procedures by which an "authorized official" or the "owner ... of any private property ... on which a vehicle is parked without permission" may arrange to have the vehicle towed and stored. State supreme courts had split on this issue.

The New Hampshire Supreme Court concluded that Pelkey's state-law claims are "related to" neither the "transportation of property" nor the "service" of a motor carrier. Here, the claim concerned what the towing company did with the property after it was towed, that is, after it was transported. Nor was there any indication that Congress's intent was to displace laws other than laws aimed at generally regulating the interstate transportation industry. The Supreme Court agreed. Reading the statutory language in context, the Court unanimously determined that the FAAAA would not preempt any state law related to the "price, route, or service" of a motor carrier acting in any capacity, but only where that price, route or service directly involved the motor carrier's "transportation of property."

In addition, the FAAAA did not directly address the issue of how the vehicle should be disposed of, so holding that state law was preempted would place the issue beyond any governing law. The Court will hear a related case involving similar language in the Airline Deregulation Act in Northwest, Inc. v. Ginsberg next fall.

- **Wos v. E.M.A., (Supreme Court Docket No. 12-98, opinion issued 3/20/2013)**
  http://www.supremecourt.gov/opinions/12pdf/12-98_9ol1.pdf

  A child received a multi-million-dollar settlement in tort litigation against physicians for injuries suffered at birth. Federal law permits the state to take out of any such settlement the funds attributable to the expenses previously paid under Medicaid, but the Medicaid anti-lien provision prohibits a State from making a claim to any part of a Medicaid beneficiary's tort recovery not designated as payments for medical care. However, North Carolina had an irrebuttable statutory presumption that one-third of a tort recovery is attributable to medical expenses. The Court found this presumption was preempted by the federal law because rather than actually determining what portion of the settlement was awarded for medical, the state had created an arbitrary rule.

  In their dissent, Roberts, Scalia, and Thomas found the majority opinion had the "unfortunate consequence of denying flexibility to the States" in resolving policy questions of broad significance. The dissent was critical of the majority's failure to factor in the complexity of the federal law. Medicaid, noted the dissent, is a cooperative federal-state program. States contribute anywhere from 17-50% of the costs, but noted the dissent, "the books are thick with federal regulations that States must interpret and reconcile." The states are not told how to determine the portion of a settlement that is due to medical services, nor are they explicitly prohibited from using a rule such as the one at issue (but states must make efforts to recoup that portion or risk forfeiting federal funds). Nor is the rule here different from other similar rules states routinely impose on tort actions, the dissent noted.

Cert Granted

NONE YET

Cert Petition Filed

- **Madison County and Oneida County v. Oneida Indian Nation of New York** (Supreme Court Docket No. 12-604)
  http://www.scotusblog.com/case-files/cases/madison-county-v-oneida-indian-nation-of-new-york/

  An Indian tribe brought actions against counties to enjoin them from assessing property tax on tribe-owned property, acquired on the open market, and from enforcing those taxes through tax sale or foreclosure.

  The Court of Appeals' previous decision on appeal affirmed the judgment of the United States District Court for the Northern District of New York solely on the basis of tribal sovereign immunity from suit. However, while the case was pending before the Supreme Court, the Oneida Indian Nation ("OIN") notified the Court that it had voluntarily waived its tribal sovereign immunity from suit. In light of that development, the Supreme Court vacated the Court of Appeals' judgment in Oneida I and remanded for further proceedings.

  On remand, the court of appeals rejected the OIN's due process challenge to the foreclosure procedures employed by the Counties and ordered the district court to remand to state court the OIN's claim that the lands are immune from real property taxes under New York law. The court of appeals also affirmed the dismissal of the Counties' counterclaims seeking a declaration that the ancient Oneida reservation has been disestablished or diminished.

  The County petitioned for certiorari to resolve the following: whether the 300,000-acre ancient Oneida reservation in New York still exists, neither disestablished nor diminished, despite (1) the federal government's actions taken in furtherance of disestablishment (including, but not limited to, the 1838 Treaty of Buffalo Creek); (2) this Court's holding in City of Sherrill v. Oneida Indian Nation of New York that the Oneida Indian Nation of New York cannot exercise sovereignty over lands it purchases in the ancient reservation area; and (3) this Court's finding in that case that land in the ancient reservation area has not been treated as an Indian reservation by the federal, state or local governments for nearly two centuries. As of February 19, 2013, the Solicitor General is invited to file a brief in this case expressing the views of the United States.

Cert Denied

- **In Spirit Airlines, Inc. v. U.S. Department of Transportation, (Supreme Court Docket No. 12-656)**
  http://www.cadc.uscourts.gov/internet/opinions.nsf/B3C8FBE2AB1F6A9185257A45004EE709/$file/11-1219-1385164.pdf

Spirit Airlines challenged the Department of Transportation's requirement that the most prominent figure displayed on print advertisements and websites be the total price, inclusive of taxes. Spirit contended that strict scrutiny applied because they had “a First Amendment right to engage in political speech that informs [their] customer base of the huge tax burden that the federal government imposes on air travel."

The court found that even if the speech could not be characterized "merely as proposals to engage in commercial transactions,” it is nonetheless commercial in certain circumstances, for instance when it is an “advertisement[ ],” “refer[s] to a specific product,” and the speaker “has an economic motivation” for it. The combination of all these characteristics in the instant situation sufficed to classify the speech as "commercial speech."

The court found that where, as in this case, laws are “directed at misleading commercial speech,” and where they “impose a disclosure requirement rather than an affirmative limitation on speech,” an advertiser's rights are adequately protected as long as disclosure requirements are reasonably related to the State's interest in preventing deception of consumers. In the instant case, the government interest—ensuring the accuracy of commercial information in the marketplace—is clearly and directly advanced by a regulation requiring that the total, final price be the most prominent.

Based on its analysis, the Court of Appeals denied Spirit's request for review of the Department of Transportation's rule. The Supreme Court denied the petition for certiorari on April 1, 2013.

- **Keenan v. First California Bank (Supreme Court Docket No. 12-608)**
  http://cdn.ca9.uscourts.gov/datastore/memoranda/2012/07/02/09-55428.pdf

  The Ninth Circuit ruled in an unpublished opinion that a taxpayer cannot sue a bank under § 1983 for turning over Social Security payments (a violation of federal law) in response to a state tax levy.

  In 2005, the California Franchise Tax Board sent an Order to Withhold to First California Bank, based on its finding that Keenan owed taxes for tax years 1982, 1986, 1987, 1989, 1992, 1993, 1994, and 1996. Keenan explained that the bank account contained Social Security moneys and argued that under 42 U.S.C. § 407(a), transferring the Social Security funds to the Franchise Tax Board would be a violation of federal law.

  First California remitted the money to the Franchise Tax Board. Keenan sued the bank under 42 U.S.C. § 1983. On appeal, the Ninth Circuit affirmed the District Court's finding that First California was not acting under color of state law, and therefore was not liable. In order to demonstrate that a private party acted under color of state law, a plaintiff must be able to establish an additional nexus other than mere “governmental compulsion in the form of a generally applicable law.”

  Since First California was complying with an Order to Withhold from the Franchise Tax Board and the laws of the State of California, and Keenan was unable to demonstrate any additional nexus between First California and governmental authorities, the § 1983 claims against First California failed. The court did note, however, that although the claim against the bank could not be maintained, it was "deeply troubled by the apparent improper

confiscation of Social Security moneys by state tax authorities." The Supreme Court denied the petition for certiorari on January 14, 2013.

- **Shenandoah Sales & Service, Inc. v. Assessor of Jefferson Cty (Supreme Court Docket No. 12-628)**
  http://www.courtswv.gov/supreme-court/docs/spring2012/11-0248and11-0701.pdf

  A corporation disputing the Jefferson County Assessor's valuation of real estate failed to retain a lawyer to prosecute its appeals to the circuit court, and instead appeared through its vice-president. The circuit judge ordered the corporation to appear through a lawyer in circuit court and stated that the court would not accept pleadings or motions from the corporation that were not signed by a lawyer. The corporation did not retain a lawyer and the circuit court dismissed the corporation's appeals.

  In the Supreme Court of Appeals of West Virginia, the corporation's vice-president argued the circuit court erred by: (1) ruling that a corporation cannot be represented by a non-lawyer corporate agent in a circuit court; (2) failing to hold a hearing before dismissing both appeals; and (3) dismissing one of the appeals while there was a motion to disqualify the circuit judge pending. The court found that, although a corporation does not have to retain a lawyer to contest the jurisdiction of the court, in all other respects "[a] corporation is not a natural person but is an artificial entity created by law and for that reason in legal matters it must act through duly licensed attorneys." It held that a phrase in W. Va.Code § 11–3–25(b) allowing a non-lawyer agent to appeal a ruling of the board of equalization and review to the circuit court was a legislative encroachment on the Court's exclusive authority to define, regulate and control the practice of law.

  The Court of Appeals found no violation of due process on the part of the circuit court because the circuit court had given the corporation notice that it was engaged in the unauthorized practice of law and giving it a reasonable amount of time to correct the problem. It concluded that the circuit court's failure to stay the proceedings until the motion to disqualify was resolved was harmless error.

  The Supreme Court denied the corporation's petition for certiorari on January 22, 2013. A petition for rehearing was filed February 14, 2013. The petition was denied March 18, 2013.

Other

- ***Overstock.com v. New York Dept. of Taxn. and Fin.*, N.Y., 987 N.E.2d 621 (N.Y. 2013)**
  http://www.nycourts.gov/ctapps/Decisions/2013/Mar13/33-34opn13-Decision.pdf

  Amazon is an internet retailer based in Washington. It has no property or employees in New York. Overstock.com is an internet retailer based in Utah. It too, has no property or employees in New York. However, the two retailers entered into contracts with New York residents in which the resident placed the retailer's logo on its website, which if clicked, linked directly to the retailer's website. An individual earned a commission only if the customer clicked on the logo and subsequently made a purchase from the retailer. New York

enacted a law that these types of transactions subjected an e-tailer to a duty to collect sales tax on New York purchases.

Amazon and Overstock.com brought suit, alleging that the statute violated the Due Process Clause and the Commerce Clause, both on its face and as applied. The court found the New York statute did not violate the Commerce Clause on its face. A statute will not survive a Commerce Clause facial challenge if there is no set of circumstances under which the statute would be valid.

The statute imposes a tax collection obligation on an out-of-state vendor only where the vendor enters into a business-referral agreement with a New York State resident, and only when that resident receives a commission based on a sale in New York. Therefore, Amazon and Overstock.com had nexus with New York. Of equal importance to the requirement that the out-of-state vendor have an in-state presence is that there must be solicitation, not passive advertising. The Amazon Associates and Overstock.com Affiliate programs are not designed for the passive advertiser, but seek growth by reliance upon representatives who will look to solicit business. The obligations imposed by the state to collect the tax only arise when the paradigm shifts from advertising to solicitation. Here, there is a set of circumstances under which the statute would be valid, i.e., when a New York representative uses some form of proactive solicitation which results in a sale by Amazon, and a commission to the representative; and the representative has an in-state presence sufficient to satisfy the substantial nexus test.

However, the Appellate Court modified the lower court's decision by reinstating the as-applied challenges, finding that further discovery was required before those claims could be determined. Plaintiffs then entered into stipulations of discontinuance withdrawing their as-applied constitutional challenges with prejudice, which were deemed the final judgments. They filed appeals pursuant to CPLR 5601 (b)(1) and CPLR 5601 (d), bringing up for review the prior nonfinal Appellate Division order. The plaintiffs then decided to bypass their as-applied challenges and sought a reversal from the Court of Appeals by meeting its burden to prove that the Internet Tax is unconstitutional on its face. The Court rejected the facial challenges. The parties agreed that the only prong at issue was whether the statute satisfies the "substantial nexus" test. Under *Quill*, although an in-state physical presence is necessary, it need only be demonstrably more than a 'slightest presence' The Court found that "[a]ctive, in-state solicitation that produces a significant amount of revenue qualifies as 'demonstrably more than a "slightest presence,"' and upheld the tax.

Amazon.com and Overstock.com applied for and were granted an extension to file a petition for a writ of certiorari from June 26, 2013 to August 23, 2013.