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U.S. Supreme Court Update

TWO RECENT STATE TAX COURT DECISIONS

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***40** In this issue of the JOURNAL, we discuss the U.S. Supreme Court's recent decisions in two cases involving state and local taxes: *Nebraska v. Parker* (Docket No. 14-1406) and *Franchise Tax Board of the State of Californiav. Hyatt* (Docket No. 14-1175).

In *Parker*, the Court agreed with the U.S. Court of Appeals for the Eighth Circuit and held that an 1882 Act of Congress had not diminished the lands of the Omaha Tribe of Nebraska. Accordingly, taxpayers located on the disputed land (includingthe Nebraska village that brought the petition before the Court) remain subject to the Tribe's liquor license and taxing regulations, including a 10 percent sales tax on all liquor sales made on the Omaha Reservation.

In *Hyatt*, a case involving a Nevada taxpayer's lawsuit against the California Franchise Tax Board, a majority of the Court held that Nevada could not award higher damages in cases involving out-of-state agencies—*i.e.*, theCalifornia Franchise Tax Board—than the state could award in cases involving its own in-state agencies. The Court, however, split 4 to 4 (a result that remains more likely in the wake of Justice Antonin Scalia's death) on whether to overrule the lowercourt's ruling that there was no jurisdictional bar against a taxpayer bringing suit in a Nevada court against a California state agency. As a result, the Court effectively upheld its prior ruling in *Nevada v. Hall*, 440 U.S. 410 (1979), in which the Court found that states have jurisdiction to hear lawsuits filed by private citizens against other states.

We also note that as we go to press, two previously reported petitions remain pending before the Court.

Court Unanimously Upholds Omaha Tribe's Right to Enforce Liquor Taxes

As first reported in our last column, on 3/22/16, the Court ruled unanimously that the Omaha Tribe of Nebraska's (the ‘Tribe‘) Reservation was not diminished by an 1882 Act of Congress (the ‘1882 Act‘), and the Court therefore upheld theTribe's right to enforce liquor taxes in a largely non-Indian populated village (the Village of Pender) located on the disputed land.

The case, *Nebraska v. Parker*, Docket No. 14-1406, ruling below as *Smith v. Parker*, 774 F.3d 1166 (8th Cir. 2014), involves a decision by the U.S. Court of Appeals for the Eighth Circuit, which affirmed a district court's ruling that Congress did not intend to diminish the Tribe's reservation when passing the 1882 Act. Inan opinion by Justice Clarence Thomas, the Supreme Court unanimously upheld the Eight Circuit's ruling, finding that the ‘disputed land is within the reservation's boundaries.‘

**2 In upholding the Eighth Circuit's ruling, the Court looked to the 'well settled,' three-factor diminishment test announced in *Solem v. Bartlett*, 465 U.S. 463 (1984). As stated by Justice Thomas, the *Solem* factors include (1) the statutory text at issue, (2) the history surrounding the passage of the act, and (3) the subsequent demographic history of the land in question.

Text of 1882 Act does not 'evince[] an intent to diminish the reservation.'

Of the three *Solem* factors, Justice Thomas noted that the starting point for any diminishment analysis must be the statutory text, for '[t]he most probative evidence of diminishment is, of course, the statutory language used toopen the Indian lands' (quoting *Hagen v. Utah*, 510 U.S. 399 (1994)). And according to Justice Thomas, the language of the 1882 Act did not show any congressional intent to diminish the Tribe's lands.

In delivering the opinion of the Court, Justice Thomas explained that the '[c]ommon textual indications of Congress' intent to diminish reservation boundaries'—including an '[e]xplicit reference to cession,' 'anunconditional commitment from Congress to compensate the Indian tribe for its opened land,' or 'a statutory provision restoring portions of a reservation to 'the public domain''—were all absent from the 1882 Act. Instead, *41 '[t]he 1882 Act bore none of these hallmarks of diminishment.'

Rather than reducing the Tribe's lands, the 1882 Act 'merely opened the reservation land to settlement,' which, according to the Court, does not constitute diminishment. Thus, as stated by Justice Thomas, the petitioners 'failed at the firstand most important step [in a diminishment case].' That is '[t]hey cannot establish that the text of the 1882 Act evinced an intent to diminish the reservation.'

Other *Solem* factors 'cannot overcome the lack of clear textual signal that Congress intended to diminish the reservation.'

As stated above, the second and third *Solem* factors include the history of the legislative act at issue and the subsequent demographic history of the land in question.

According to the Court, the legislative history of the 1882 Act 'in no way 'unequivocally reveal[s] a widely held, contemporaneous understanding that the affected reservation would shrink as a result of the proposed legislation.' ' Therefore, the Court concluded that the petitioners were unable to present the necessary 'clear and plain' evidence of diminishment required under the Court's precedent.

In its arguments before the Court, the petitioners also emphasized the demographic history of the reservation, arguing that the Tribe was 'almost entirely absent from the disputed territory for more than 120 years.' But according to the Court, that'evidence of the changing demographics of disputed land is 'the least compelling' evidence in our diminishment analysis. ' Similarly, the Court found that 'evidence of the subsequent treatment of the disputed land by Government officials .. . ha[d] 'limited interpretive value.''

Court suggests a path for future challenges to tribal taxing authority.

**3 Despite its ruling in favor of the Tribe, the Court did recognize that '[p]etitioners' concerns about upsetting the 'justifiable expectations' of the almost exclusively non-Indian settlers who live on the land are compelling. ' Asrestated by the Court, the Tribe's liquor laws include both licensing requirements and the imposition of a 10 percent sales tax on liquor sales. These regulations, according to the Court, were imposed by the Tribe despite a 'longstanding absence' oftribal control over the disputed territory.

But, as restated by the Court, the settlers', albeit valid, 'justifiable expectations' about who would and would not assert jurisdiction over the disputed territory could not diminish reservation boundaries: 'Only congress has the power to diminisha

reservation.‘ And, as put forth by the Court, ‘[b]ecause petitioners . . . raised only the single question of diminishment, we express no view about whether equitable considerations of laches and acquiescence may curtail the Tribe's powerto tax.‘ Whether a different tribe imposing a different tax might violate these principles remains an open question. (For more background on the original petition filed in this case, see U.S. Supreme Court Update, 25JMT 43 (January 2016).)

Court Split on Whether States Have Jurisdiction to Hear Lawsuits Filed Against Other States

On 4/19/16, the U.S. Supreme Court issued its decision in *Franchise Tax Board of the State of California v. Hyatt*, Docket No. 14-1175, ruling below at 335 P.3d 125 (Nev. 2014). The justices in *Hyatt* were evenly divided as to whether the California Franchise Tax Board (‘FTB‘) could be sued by an individual taxpayer for damages in a Nevada state court. The split decisioneffectively affirms the ruling by the Nevada Supreme Court in the case below, which held that inventor Gilbert P. Hyatt's lawsuit against the FTB was not barred under principles of discretionary-function immunity and comity. The ruling also leaves in placethe Court's prior rule as announced in *Nevada v. Hall*, 440 U.S. 410 (1979), which held that sovereign immunity is not absolute when it comes to states vis-a-vis other states.

On the secondary question, however, of whether Nevada courts must apply the same damages cap in suits brought against agencies of sister states as those involving suits against Nevada state agencies, a majority of the justices agreed that failing to applythe damages cap in suits against other states' agencies—in this case, the FTB—would constitute a violation of the Full Faith and Credit Clause of the U.S. Constitution. Accordingly, although the FTB, and other state taxing agencies, will continueto face the possibility of ***42** being hauled into another state's courts, the High Court held that Nevada may not award any damages in favor of Mr. Hyatt in the present case in excess of Nevada's standard $50,000 damages cap without running afoul of the U.S. Constitution'sFull Faith and Credit Clause.

****4** Mr. Hyatt's dispute with the FTB stems from the agency's attempt to collect approximately $10 million in taxes on patent licensing fees earned by Mr. Hyatt in the 1990s. Following its audit, in which the FTB determined Mr. Hyatt to be a California resident,Mr. Hyatt sued the FTB in Nevada state court, claiming that the FTB's allegedly abusive audit and investigation techniques cost him business opportunities and inflicted emotional distress. In the case below, the Supreme Court of Nevada largely reversed a juryaward for Mr. Hyatt of $139 million in tort damages and $250 million in punitive damages, but the Nevada court held that the FTB was not immune from suit in Nevada and, therefore, could not escape all liability.

Justices divided on whether Nevada courts lack jurisdiction to hear suits brought against out-of-state agencies.

In a rule announced in *Nevada v. Hall*, 440 U.S. 410 (1979), the U.S. Supreme Court has previously held that one state can hear a private citizen's lawsuit against another state without the other state's consent. In *Hyatt*, the FTBexpressly asked the Court to review and overturn its prior holding. The FTB presented the following question for review in its original petition: ‘Whether *Nevada v. Hall* . . . , which permits a sovereign State to be hauled into the courtsof another State without its consent, should be overruled.‘

Writing for the Court, however, Justice Breyer stated that ‘[t]he Court is equally divided on this question, and we consequently affirm the Nevada courts' exercise of jurisdiction over California.‘ Thus, without announcing which justicesfell on which side of the issue, the Court effectively upheld its 37-year precedent as announced in *Nevada v. Hall.*

However, this was not the only question presented for review, and the Court was also asked by the FTB to consider whether ‘Nevada may refuse to extend to sister States hauled into Nevada courts the same immunities Nevada enjoys in those courts.‘In response to this question, a majority of the justices answered in the negative.

Court rules that withholding a damages cap in cases involving out-of-state agencies exhibits an impermissible 'policy of hostility.'

As restated by Justice Breyer in his opinion for a six-member majority of the Court, the FTB sought to 'reverse the Nevada court's decision insofar as it awards [Mr. Hyatt] greater damages than Nevada law would permit a private citizen to obtainin a similar suit against Nevada's own agencies.' On this issue, a majority of the Court held that 'Nevada's application of its damages law in this case reflects a special, and constitutionally forbidden, 'policy of hostility to the public Acts'of a sister State.' Accordingly, the Court, with two dissents, vacated the Nevada Supreme Court's decision as to the issue of damages 'insofar as the Nevada Supreme Court has declined to apply California law in favor of a special rule of Nevada lawthat is hostile to its sister States.'

****5** Although Justice Breyer admitted that the Court's prior precedent, including the Court's prior review of the current litigation (*see Franchise Tax Board of the State of California v. Hyatt*, 538 U.S. 488 (2003)), has held that the Full Faith and Credit Clause 'does not require one State to apply another State's law that violates its 'own legitimate public policy,'' the same analysis, according to Justice Breyer,does not apply when a state seeks to enforce a 'special rule of law applicable only in lawsuits against its sister States.'

As restated by Justice Breyer, Nevada ordinarily caps damages at $50,000 for lawsuits brought against state agencies. In the ruling below, however, the Nevada Supreme Court disregarded its standard rule, explaining that in the present case, 'California'ssystem of controlling its own agencies [failed] to provide 'adequate' recourse to Nevada's citizens.' Accordingly, the lower court reasoned that it would be against Nevada's public policy to apply the damages cap to the FTB's liabilityrelated to Mr. Hyatt's fraud and emotional distress claims and held that it had sufficient policy considerations for departing from its standard rule. A majority of the U.S. Supreme Court, however, disagreed with the Nevada court's analysis.

Nevada's ruling, according to Justice Breyer, was 'not only 'opposed' to California law [but] also inconsistent with the general principles of Nevada immunity law.' Thus, the Court held that 'Nevada's rule lacks [a]

'healthy regard for California's sovereign status' . . . [and] reflects a constitutionally impermissible 'policy of hostility toward the public Acts' of a sister State.' According to Justice Breyer, '[a] constitutionalrule that would permit this kind of discriminatory hostility is likely to cause chaotic interference by some ***43** States into the internal, legislative affairs of others.'

Accordingly, the Court ruled that the U.S. Constitution does not permit Nevada to award damages against California agencies under Nevada law that are greater than it could award against Nevada agencies in similar circumstances.

Dissent argues that Nevada has a 'sufficient policy interest' in favor of applying its own laws.

Chief Justice Roberts, who was joined by Justice Thomas, issued a dissenting opinion. According to the Chief Justice, '[t]he majority's approach is nowhere to be found in the Full Faith and Credit Clause. Where the Clause applies, it expresslyrequires a State to give *full* faith and credit to another State's laws. If the majority is correct that Nevada has no sufficient policy justification for applying Nevada immunity law, then California law applies. And under California law, the[FTB] is entitled to *full* immunity. Or, if Nevada has a sufficient policy reason to apply its own law, then Nevada law applies, and the [FTB] is subject to *full* liability.'

In reviewing Nevada's justifications for refusing to enforce the damages cap in question and thereby subjecting the FTB to full liability, Chief Justice Roberts found a sufficient policy reason for the state's departure from its ordinary rule. Accordingto the Chief Justice, '[a] State may not refuse to apply another State's laws where there are '*no* sufficient policy considerations to warrant such refusal.'' Conversely, however, '[w]here a State chooses adifferent rule from a sister State in order 'to give affirmative relief for an action arising within its borders,' the State has a sufficient policy reason for applying its own law, and the Full Faith and Credit Clause is satisfied.'

****6** In this case, Justice Roberts reasoned that 'the Nevada Supreme Court applied Nevada rather than California immunity law in order to uphold the 'state's policy interest in providing adequate redress to Nevada citizens'' who are harmed withinthe boundaries of their own state. The Chief Justice pointed to the various audit activities of the FTB that took place within Nevada to support his argument. And, according to Justice Roberts, 'there is no doubt that Nevada has a 'sufficient' policyinterest in protecting Nevada residents from such injuries.'

Thus, although the Chief Justice acknowledged that the Court's ruling 'seems fair,' he continued that 'for better or worse, the word 'fair' does not appear in the Full Faith and Credit Clause.' Instead, Justice Roberts argued that theCourt's decision is 'contrary to our precedent holding that the [Full Faith and Credit] Clause does not block a State from applying its own law to redress an injury within its own borders.' Accordingly, the Chief Justice respectfully dissented.(For more background on this case, including a detailed discussion of the underlying audit of Mr. Hyatt, see U.S. Supreme Court Update, 25 JMT 40 (July 2015).)

Petitions Still Pending

The following two petitions remained pending as the JOURNAL went to press.

Sprint Nextel asks Court to review NY preemption decision. In *Sprint Nextel Corp. v. New York*, Docket No. 15-1041, petition for cert. filed 2/18/16, ruling below as *People v. Sprint Nextel Corp.*, 26 N.Y.3d 98 (2015), Sprint Nextel Corporation ('Sprint') asks the Court to review a decision by the New York State Court of Appeals, in which New York's highest court held that: '(1) the New York Tax Law imposes sales tax on interstatevoice service sold by a mobile provider along with other services for a fixed monthly charge; (2) the statute is unambiguous; (3) the statute is not preempted by federal law (the Mobile Telecommunications Sourcing Act, 4U.S.C. 123(b)); (4) the [New York State] Attorney General's complaint sufficiently pleads a cause of action under the New York False Claims Act ((FCA) (State Finance Law 187 et seq.)); and (5) the damages recoverable under the FCA are notbarred by the Ex Post Facto Clause of the U.S. Constitution.'

Sprint now asks the U.S. Supreme Court to review the preemption issue: 'Whether New York law, which imposes sales tax on interstate mobile voice services only when it is bundled with other services, conflicts with the Mobile Telecommunications SourcingAct, 4 U.S.C. 123(b), and is therefore preempted.' (For more background on this case, including a detailed discussion of the underlying decision and the FCA complaint, seeU.S. Supreme Court Update, 26 JMT 40 (June 2016).)

Seminole Tribe of FL challenges state utility tax. In *Seminole Tribe of Florida v. Stranburg*, Docket No. 15-1064, petition for cert. filed 2/19/16, ruling below at 799 F.3d 1324 (11th Cir. 2015), the U.S. Court of Appeals for the Eleventh Circuit held that federal law prohibits and preempts Florida's commercial rent tax (the 'Rental Tax') from being imposed on the Seminole Tribe's leases of reservationland, but that Florida's tax on the gross receipts of utility service providers (the 'Utility Tax') does not violate federal Indian law, even when the tax is passed on to Indian customers, because the legal incidence of the tax falls on the utilitycompany and not on the Seminole Tribe. The Seminole Tribe now petitions the High Court to review the circuit court's ruling with regard to the Utility Tax, arguing that the lower court 'erroneously concluded that the legal incidence of the Utility Taxis on the utility company rather than on the Tribe' and therefore erroneously found the Utility Tax to be a permissible tax on the Tribe's activities.

****7** In its petition for certiorari, the Florida Seminole Tribe presents the following question for review: 'When a utility provider exercises a state-law right to expressly pass a utility tax to a federally recognized Indian tribe for utility services deliveredto the tribe's reservation and the tribe is therefore legally obligated to pay the tax, is the tax an impermissible direct tax on the tribe?' (For more background on this case, including a detailed discussion of the utility tax at issue, see U.S. SupremeCourt Update, 26 JMT 40 (June 2016).)

Justice Thomas noted that the starting point for any diminishment analysis must be the statutory text.

The ruling [in *Hyatt*] leaves in place the Court's prior rule as announced in *Nevada v. Hall*, 440 U.S. 410 (1979), which held that sovereign immunity is not absolute when it comes to states vis-a-visother states.

[T]he U.S. Constitution does not permit Nevada to award damages against California agencies under Nevada law that are greater than it could award against Nevada agencies in similar circumstances.

Sprint [asks] 'Whether New York law, which imposes sales tax on interstate mobile voice services only when it is bundled with other services, conflicts with the Mobile Telecommunications Sourcing Act . . . .'

The Seminole Tribe [argues] that the lower court 'erroneously concluded that the legal incidence of the Utility Tax is on the utility company rather than on the Tribe' [and therefore permissible].

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