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U.S. Supreme Court Update

U.S. SUPREME COURT UPDATE

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Supreme Court Set to Decide Three State and Local Tax Cases

***45** As regular readers of this column are well aware, the U.S. Supreme Court is set to decide the three state and local tax cases currently on its docket. These cases include a challenge to Maryland's credit against its personal income taxes for taxes paid toother states (*Comptroller of the Treasury v. Wynne*, Docket No. 13-485, cert. granted 5/27/14); a challenge involving the proper scope of the Tax Injunction Act (*Direct Marketing Ass'n v. Brohl*, Docket No. 13-1032, cert. granted 7/1/14);and a case in which Alabama has asked the Court to review the scope of the federal Railroad Revitalization and Regulatory Reform Act of 1976 (the ‘4R Act‘) (*Alabama Department of Revenue v. CSX Transportation, Inc.*, Docket No. 13-553,cert. granted 7/1/14). The Court has now heard oral arguments in each of these cases, and as the JOURNAL goes to press, we eagerly await the Court's decisions.

In the interim, we highlight a new petition for certiorari that involves state and local taxes. It asks the Court to consider whether the Employee Retirement Income Security Act of 1974 (‘ERISA‘) pre-emption provision (29U.S.C. § 1144(a), the ‘Pre-emption Provision‘) prohibits a Michigan tax (the Michigan Health Insurance Claims Assessment Act) on health insurance claims by carriers or third party administrators to healthcare providers for services renderedin Michigan for Michigan residents.

In addition, as we go to press, one previously reported state and local tax petition for certiorari remains pending before the Court, while another has been denied.

Finally, we note that the Court has set 3/4/15 as the date for oral arguments in *King v. Burwell.* The taxpayer in this case asks the Court to consider whether the Internal Revenue Service may permissibly promulgate regulations to extend tax-creditsubsidies to healthcare coverage purchased through exchanges established by the federal government under Section 1321 of the Patient Protection and Affordable Care Act (‘Obamacare‘).

ERISA Pre-emption Provision Challenge to Michigan Health Insurance Tax

In *Self-Insurance Institute of America, Inc. v. Snyder*, Docket No. 14-741, petition for cert. filed 12/18/14, ruling below at 761 F.3d 631 (6th Cir. 2014), the U.S. Court of Appeals for the Sixth Circuit affirmed a district court's ruling that the Michigan Health Insurance Claims Assessment Act (Mich. Comp. Laws §§ 550.1731–1734; the ‘MichiganAct‘)—which imposes a 1 percent tax, along with various reporting and record-keeping requirements, on all paid claims by carriers and third party administrators to healthcare providers for services rendered in Michigan for Michigan residents—isnot prohibited by ERISA's Pre-emption Provision (29 U.S.C. § 1144(a)).

****2** In its petition for review, the Self-Insurance Institute of America, Inc. (‘SIIA‘) argues (as it did in the proceedings below) that the Supremacy Clause of the U.S. Constitution (art. VI, § 2) and ERISA's Pre-emption Provision, prohibit theapplication of the Michigan Act to ERISA-covered entities (i.e., ERISA plan administrators).

The Michigan Act.

The Michigan Act (Mich. Comp. Laws §§ 550.1731-1741) imposes a 1 percent tax on all ‘paid claims‘ by ‘carriers‘ or ‘third party administrators‘ to healthcare providers for services rendered in Michigan to Michigan residents. “Carriers' include sponsors of ‘group health plan[s]’ set up under the strictures of ERISA.‘

The Michigan Act also requires every carrier and third-party administrator who pays the tax to submit quarterly returns with the Michigan Department of Treasury and to ‘keep accurate and complete records and pertinent documents as required by the department.‘

ERISA's Pre-emption Provision.

As explained by the Sixth Circuit in its decision upholding the Michigan Act, one of the purposes of ERISA is ‘to provide a uniform regulatory regime over employee benefit plans.‘ Accordingly, ‘ERISA contains a broad preemption provision that‘supersede[s] any and all State laws insofar as they . . . *relate to* any employee benefit plan’ that falls under the regulation of ERISA. (29 U.S.C. §1144(a)‘ (emphasis added).

The circuit court acknowledged that the Supreme Court considers the Pre-emption Provision ‘broadly worded and deliberately expansive‘ but also notes that the Court ‘has found providing useful guidance in this area to be difficult and defining‘relates to’ a ‘frustrating task.’‘ The circuit court ‘readily concur [s]‘ with the Supreme Court on this matter explaining that ‘the statutory text is simply ‘unhelpful’ because ‘[i]f ‘relateto‘ were taken to the furthest stretch of its indeterminacy, then for all practical purposes pre-emption would never run its course, for ‘[r]eally, universally, relations stop nowhere.’ ‘ (citations omitted).‘ The best guidance, accordingto the Sixth Circuit, that the Supreme Court has been able to provide is that ‘[a] law ‘relates to’ an employee benefit plan, in the normal sense of the phrase, if it has a connection with or referenceto such a plan.‘ (*Shaw v. Delta Air Lines, Inc.*, 463 U.S. 85 (1983).)

In the proceedings below, SIIA argued that the Michigan Act has an impermissible connection with employee benefit plans ***46** inasmuch as the Michigan Act: ‘(1) interferes with the administration of the plans; (2) imposes administrative burdens in additionto those prescribed by ERISA; and (3) interferes with the relationships between ERISA-covered entities.‘ The Sixth Circuit disagreed with all three of SIIA's contentions.

Before addressing each argument in turn, however, the Sixth Circuit initially noted that ‘[i]n determining whether a state law has an impermissible connection with ERISA plans, [the court] start[s] with the presumption thatCongress did not intend to preempt state laws, particularly in areas of traditional state concerns.‘ And, as stated by the court, state taxes (and any ancillary requirements) are ‘a type of law long recognized as an important ‘attribute of statesovereignty.’‘ As such, the court determined that ‘the presumption applies with special force in this case, and overcoming it ‘requires two showings . . . (1) the law at issue must mandate (or effectively mandate) something, and (2) that mandatemust fall within the area that Congress intended ERISA to control exclusively.’‘

No interference with ERISA plan administration.

****3** In responding to SIIA's specific contentions as to why the Michigan Act was impermissibly connected with ERISA employee benefit plans, the court ruled, first, that the Michigan Act did not interfere with the administration of such plans (i.e., uniform planadministration). The court found, '[i]n reality, the [Michigan] Act does not require a plan administrator to change how it administers the plan at all, and thus, this argument fails.' Rather, the court explains that Michigan Act's'definition of 'paid claims' applies, and the state's reporting and record-keeping requirements come into play, only when the carriers compute the tax, a function entirely divorced from plan administration.'

No creation of inappropriate administrative burdens.

Next, the court disagreed with SIIA's claim that the Michigan Act creates inappropriate administrative burdens. The court concluded that while Congress did intend for ERISA to preempt state laws requiring ERISA entities to file reports related to plans'financial stability, '[t]his basic conclusion . . . does not mean that Congress intended federal law to bar states from imposing additional administrative burdens unrelated to the plans' core functions. ' Because the Michigan Act's reportingand record-keeping requirements are meant only to ensure that carriers pay the correct amount of tax, the court found that the additional administrative work was unrelated to the processing of claims, and therefore permissible.

No interference with relationships between ERISA-covered entities.

The Sixth Circuit also held that the Michigan Act's residency requirement and permissive collection implementation provision do not interfere with the relationship between ERISA-covered entities.

SIIA argued that the Michigan Act's limitation of the tax to claims paid on behalf of Michigan residents effectively alters the relationship between plan administrators and plan beneficiaries, because the requirement forces the administrators to collectadditional information from beneficiaries—i.e., their residency status. For purposes of the Michigan Act, 'a Michigan 'resident' is an individual who is domiciled in the state of Michigan on the date that the service in question is performed.'(Mich. Admin. Code § 550.404(1).)

As regular readers of this column are well aware, domicile determinations are subjective, fact-specific (and oftentimes frustrating) inquiries. But section 550.404(3) of the Michigan Administrative Code—part of the Michigan Act—creates '[a]

rebuttable presumption . . . that an individual's home address, as maintained in the ordinary business records of a carrier or third-party administrator, indicates the domicile of that individual under this definition.' According to the court, '[b]ydefining residency by reference to the administrators' already-existing business records, Michigan leaves the relationship between ERISA-covered entities untouched,' and the court held that, therefore, Congress did not intend ERISA to preempt the MichiganAct's residency requirement.

****4** SIIA also argued that section 550.173a(2), which requires an administrator to develop and implement a methodology to collect the assessment of the tax, impermissibly interferes with the relationship between ERISA-covered entities. The court disagreed statingthat the Michigan Act 'does not force carriers and third-party administrators to change their plan documents. Therefore, there is no ERISA-preemption issue.'

Questions presented.

In its petition for review, SIIA contends that, in the ruling below, '[t]he circuit court invoked a strong presumption against the preemption of state taxing powers to read [ERISA's preemption provisions] narrowly despite Congress'sdeliberate choice of preemptive language whose breadth has been repeatedly emphasized by this Court, and Congress's express recognition that ERISA can and does preempt state tax laws.' Accordingly, SIIA presents two questions for review:

'Whether a state law that imposes new reporting, payment, recordkeeping, and audit requirements on ERISA plan administrators that arise directly from their processing of welfare benefit claims pursuant to ERISA 'relate[s] to' ERISA benefitplans and is therefore preempted under Section 514(a) [of ERISA].'

'Whether the broad preemption language in Section 514(a) can be judicially narrowed to accommodate a presumption against preemption of newly minted state laws that seek to exploitthe core functions of ERISA plan administration.'

Update on Docketed Cases

As previously reported in this column, the Court recently heard oral arguments in the three state and local tax cases on the Court's docket. As this issue of the JOURNAL goes to press, however, we still await the Court's decisions.

On 11/12/14, the Court heard oral arguments in *Comptroller of the Treasury v. Wynne*, Docket No. 13-485, cert. granted 5/27/14, ruling below at 431 Md. 147, 64 A.3d 453 (2013). This case involves a decision by the Maryland Court of Appeals (the state's highest court), finding that Maryland's income tax law, which provides a credit against Maryland state income tax for income taxespaid to other states, violates the Commerce Clause of the U.S. Constitution because the credit is not available to offset county-level income taxes.

The Maryland court analyzed the taxpayers' challenge to the statute under the dormant Commerce Clause test announced in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 51 L. Ed. 2d 326 (1977), whereby a state tax will pass constitutional muster if the tax: (1) applies to an activity with a substantial nexus with the taxing state; (2) is fairly apportioned; (3) does not discriminate againstinterstate or foreign commerce; and (4) is fairly related to the services provided by the state.

Focusing on the requirements of fair apportionment and no discrimination against interstate commerce, the Maryland court found that the lack of a credit against the county tax resulted in the tax failing under both prongs. (For more on this case, ***47** including a discussion of Maryland's income tax scheme and a discussion of the lower court's opinion in *Wynne*, see U.S. Supreme Court Update, 23 JMT 40 (February 2014). Fora discussion of the 11/12/14 oral arguments see U.S. Supreme Court Update, 24 JMT 39 (February 2015).)

****5** On 12/8/14, the Court heard oral arguments in *Direct Marketing Ass'n v. Brohl*, Docket No. 13-1032, cert. granted 7/1/14, ruling below at 735 F.3d 904 (10th Cir. 2013), *rem'g Direct Marketing Ass'n v. Huber*, DC Colo., No. 10-CV-01546-REB-CBS, 3/30/12, 2012 WL 1079175. In *Direct Marketing*, the U.S. Court of Appeals for the Tenth Circuit overturned adistrict court's ruling that a Colorado law imposing information notice and reporting requirements on remote retailers violated the Commerce Clause. The circuit court remanded the case to the district court for dismissal on procedural grounds, finding thatthe Tax Injunction Act ('TIA,' codified at 28 U.S.C. § 1341) precluded federal court jurisdiction over the claims.

The plaintiff, the Direct Marketing Association, now asks the Supreme Court to clarify the scope of the TIA's jurisdiction. (For more on this case, including a detailed discussion of the Colorado notice and reporting requirements, see U.S. Supreme CourtUpdate 24 JMT 40 (May 2014). For a discussion of the 12/8/14 oral arguments see U.S. Supreme Court Update, 25JMT 41 (March/April 2015).)

Finally, on 12/9/14, the Court heard oral arguments in *Alabama Department of Revenue v. CSX Transportation, Inc.*, Docket No. 13-553, cert. granted 7/1/14, ruling below as *CSX Transportation, Inc. v. Alabama Department of Revenue*, 720 F.3d 863 (11th Cir. 2013). In this case, Alabama has asked the Court to review the decision by the U.S. Court of Appeals for the Eleventh Circuit, which held that Alabama's failure to provide rail carriers with a tax exemption from thestate's sales and use taxes for their purchases of diesel fuel, while exempting both interstate motor carriers and water carriers, was discriminatory in violation of the federal Railroad Revitalization and Regulatory Reform Act of 1976 (the '4R Act,'codified at 49 U.S.C. § 11501). (For more background on this request for certiorari, including a discussion of Alabama's tax scheme at issue and the procedural history ofthe litigation, see U.S. Supreme Court Update, 23 JMT 40 (February 2014). For a discussion of the 12/9/14 oral arguments see U.S. Supreme CourtUpdate, 25 JMT 41 (March/April 2015).)

In addition to these three state and local tax cases, we also note that the Court has set 3/4/15 as the date for oral arguments in *King v. Burwell*, Docket No. 14-114, cert. granted 11/7/14, ruling below at 759 F.3d 358 (4th Cir. 2014). This controversial petition asks the Court to consider whether the Internal Revenue Service may permissibly promulgate regulations to extend tax-credit subsidies to healthcare coverage purchased through exchangesestablished by the federal government under Section 1321 of the Patient Protection and Affordable Care Act (‘Obamacare‘). Since the Court granted certiorari, over fifty amicus briefs have been filed with the Court, with more sure to follow. We willcontinue to provide updates on this case as they become available.

Petition Still Pending

****6** The following petition remained pending as the JOURNAL went to press.

Colorado legislators challenge state's Taxpayer Bill of Rights.

In *Hickenlooper v. Kerr*, Docket No. 14-460, petition for cert. filed 10/17/14, ruling below as *Kerr v. Hickenlooper*, 744 F.3d 1156 (10th Cir. 2014), petition for rehearing en banc denied, 759 F.3d 1186, the Court of Appeals for the Tenth Circuit affirmed a district court's ruling that a group of Colorado citizens, including current and former legislators,had standing to challenge Colorado's Taxpayer's Bill of Rights (‘TABOR‘) and that the legislators' challenge was not barred by the political question doctrine.

The plaintiffs seek injunctive and declaratory relief, claiming that TABOR's requirement that new taxes be subject to voter approval ‘undermines the fundamental nature of the state's Republican Form of Government‘ in violation of the Guarantee Clauseof the U.S. Constitution. Under TABOR, Colorado, with certain limited exceptions, ‘must have voter approval in advance for . . . any new tax, tax rate increase . . . , or a tax policy change directly causing a net tax revenue gain to any district.‘(Colo. Const. art. X, § 20, cl. 4(a).)

The legislators named Colorado Governor John Hickenlooper as defendant in their suit, and Governor Hickenlooper moved to dismiss the complaint, arguing that the plaintiffs lacked standing and that the political question doctrine required dismissal of allof the legislators' claims. But, according to the circuit court, the plaintiffs provided adequate proof that TABOR, by requiring a voter referendum on most tax issues, caused them injury. Thus, the plaintiffs had standing to challenge TABOR.

Moreover, under the *Baker v. Carr* test (see 369 U.S. 186 (1962)), the legislators' suit was not barred by the political question doctrine, as there were judicially discoverable and manageable standards for the litigation, and resolving the case would not require the court to improperlymake a policy determination. The circuit court's decision was strictly jurisdictional, however. The court stated that ‘merits of the case are not before us‘ and ‘stress[ed] that [its] decision on plaintiffs' Guarantee Clauseclaim is quite limited, leaving all issues other than standing, prudential standing, and the political question doctrine to the district court.‘

In his petition for certiorari, the governor challenges the circuit court's rulings on both the political question doctrine and standing. (For more background on this case, including the circuit court's decision, see U.S. Supreme Court Update, 24JMT 39 (February 2015).)

Petition Denied

The Court has denied certiorari in the following case.

In ***Houssels v. Pennsylvania***, Docket No. 14-638, petition for cert. denied 2/23/15, ruling below as *Wirth v. Commonwealth*, 95 A.3d 822, 2014 WL 2743554 (Pa. 2014), the Pennsylvania Supreme Court, with one dissent, affirmed a Commonwealth Court decision that nonresident limited partners, who invested in a Connecticut limited partnership that owned and operateda Pennsylvania skyscraper, realized gains from the foreclosure of the skyscraper that were properly subject to Pennsylvania income tax. Moreover, the Pennsylvania Supreme Court agreed with the Department of Revenue's determination that the petitioners couldnot use their investment losses in the partnership to offset the gain realized at the time of foreclosure.

****7** The petitioners had asked the Supreme Court to review the Pennsylvania court's rulings and to decide whether a limited partnership interest is a constitutionally sufficient nexus for state taxation and whether Pennsylvania's taxing laws subject nonresidentinvestors to unlawful and discriminatory taxes.

The Self-Insurance Institute of America, Inc. argues that the Supremacy Clause and ERISA's Pre-emption Provision prohibit the application of the Michigan Act to ERISA-covered entities.

The Sixth Circuit held that the Michigan Act's residency requirement and permissive collection implementation provision do not interfere with the relationship between ERISA-covered entities.

According to the circuit court, the [Colorado citizens] provided adequate proof that TABOR, by requiring a voter referendum on most tax issues, caused them injury.

The petitioners [in *Houssels*] had asked the Supreme Court whether a limited partnership interest is a constitutionally sufficient nexus for state taxation.

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