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U.S. Supreme Court Update

U.S. SUPREME COURT UPDATE

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U.S. Supreme Court Receives Two New Petitions in Property Tax Disputes

***38** In this issue of the JOURNAL, we cover two new petitions for certiorari filed with the U.S. Supreme Court involving equal protection and due process claims related to property tax disputes. The first, *Rite Aid Corp. v. Huseby* (DocketNo. 16-36), involves Rite Aid Corporation's claim that New York State's method of assessing property taxes on commercial properties financed with 'built-to-suit leases' violates taxpayers' rights to equal protection under the Fourteenth Amendmentof the U.S. Constitution.

In the second petition, *Pickett v. City of Frederick* (Docket No. 16-105), a Maryland property owner asks the U.S. Supreme Court to review a Maryland Court of Special Appeals decision foreclosing the owner's right to redeem his property aftera tax sale. Specifically, the property owner alleges that he was denied due process of law in the lower court proceedings when his case was adjudicated by a judge who lacked the 'objective standards of impartiality.'

As we go to press, we also note that four previously reported petitions (including two motions for leave to file bills of complaint) remain pending before the Court.

Rite Aid Claims NY State Property Tax Assessments Violate Equal Protection

In *Rite Aid Corp. v. Huseby*, Docket No. 16-36, petition for cert. filed 7/5/16, rulings below at *Rite Aid Corp. v Haywood*, 130 A.D.3d 1510 (N.Y. 4th Dep't 2015), *lv. to appeal denied*, 26 N.Y.3d 915 (2016) and *RiteAid Corp. v Huseby*, 130 A.D.3d 1518 (N.Y. 4th Dep't 2015), *lv. to appeal denied*, 26 N.Y.3d 916 (2016), Rite Aid Corporation ('Rite Aid') appeals two rulings from the New York State Appellate Division Fourth Department. In its rulings,the Fourth Department (with one dissent) reversed a trial court's reduction of the assessed property values of several parcels containing Rite Aid's retail drugstores. According to the Fourth Department, the lower court, in reducing the assessed value of theproperties, was wrong to accept Rite Aid's expert appraisals, as those appraisals improperly excluded 'the recent sale of the subject property as well as readily available comparable sales of national chaindrugstore properties in the applicable [net lease national drugstore] submarket.'

****2** Rite Aid, however, argues that it was proper to exclude these comparables from its appraisals since national chain drugstores, including Rite Aid's own stores, are often financed with what are known as 'built-to-suit leases.' According to

Rite Aid,because this financing method creates above-market rental rates, any use of such comparables in assessing property taxes artificially inflates the value of Rite Aid's properties and impermissibly discriminates against all taxpayers who choose to finance developmentswith built-to-suit leases vis-a-vis taxpayers who utilize more traditional financing methods.

Rite Aid's property tax assessment challenges.

In the cases below, Rite Aid sought review of real property tax assessments issued against several New York State commercial properties, which Rite Aid leased (i.e. triple-net-leased) from developers for use as retail drug stores. The properties at issuewere all financed using 'built-to-suit leases.' As explained by the courts below, this financing model allows developers to assemble several separate parcels of real property and combine them into a single plot, before leasing the combined developmentto a single tenant—in this case Rite Aid. As explained by the Fourth Department, these leases are a common financing method for national chain drugstores.

According to Rite Aid, however, these built-to-suit leases create above-market rental rates between the developer and the tenant since the lease is structured to include the premiums that were paid by the developer to acquire the various parcels of land,as well as the costs associated with assembly, demolition, and construction. As argued in Rite Aid's petition for certiorari, '[t]hese rents have no correlation to market rent because they are arbitrarily based on construction cost.'

Rite Aid's commercial properties were originally assessed by New York based on valuations that included the allegedly above-market rentals. Accordingly, Rite Aid challenged the assessments and, before the trial court, Rite Aid's expert appraiser argued thatby including Rite Aid's leases in the value of the company's retail drug stores, New York had over-assessed the properties.

The lower courts accepted Rite Aid's methodology. But, on appeal, the Fourth Department criticized the company's failure to use a valuation method that included 'readily available comparable sales of national chain drugstore properties' and concludedthat 'the failure of [Rite Aid's] expert to use the actual rent, negotiated at arm's length and without duress or collusion, as well as the ***39** failure to use similar rental comparables from the applicable market as evidence of value, demonstratesthe invalidity of the expert's conclusions.' Accordingly, the Fourth Department ruled that the trial court's decision to 'credit the appraisal of [Rite Aid's] expert was against the weight of the evidence' and, therefore, reversed thelower court's decision to reduce the assessed values of Rite Aid's properties.

Dissent argues that Fourth Department overstepped its boundaries.

****3** In both of the Fourth Department's rulings, a one-judge dissent was filed. According to the dissent, the New York Court of Appeals (New York State's highest court) has held that the Appellate Division 'may not set aside a finding of value made [bya lower court], unless such finding is based upon [an] erroneous theory of law or [an] erroneous ruling in the admission or exclusion of evidence, or unless it appears that the [lower] court . . . has failed to give to conflictingevidence the relative weight which it should have and thus has arrived at a value which is excessive or inadequate.'

In Rite Aid's case, however, the dissent argues that because Rite Aid's expert provided the trial court with 'a plausible reason for not relying on . . . data from other national retail pharmacies in the area'—*i.e.*, the above-marketnature of the commercial leases—it was improper for the Appellate Division to reverse the lower court's findings. Instead, the dissent claims that the majority should have declined to disturb '[t]he [lower] court's ultimate findingconcerning the value of the property [because it] is within the range of the expert testimony and supported by substantial evidence.'

Question presented.

Although Rite Aid did not raise any constitutional issues before the lower courts, Rite Aid now presents the U.S. Supreme Court with the following question for review: 'Was it a violation of the national drugstore taxpayer's constitutional right of

EqualProtection for the Appellate Division Fourth Department to reverse the trial court and reinstate the taxpayer's assessments which were based on the value of above market leases encumbering their stores, when all other taxpayers are assessed based on the valueof their real property alone.‘

Property Owner Asks Court to Review Maryland Judge's Failure to Recuse Himself in Property Tax Dispute

In *Pickett v. City of Frederick*, Docket No. 16-105, petition for cert. filed 7/21/16, ruling below at Case No. 0759, Maryland Court of Special Appeals, October 6, 2015, 2015 WL 5117649, Allan Pickett, a Maryland resident, asks the U.S. SupremeCourt to review a ruling of the Court of Special Appeals of Maryland in which the court affirmed a lower court's judgment permanently foreclosing Mr. Pickett's right to redeem a property following a tax sale. In his petition for certiorari, Mr. Picket allegesthat because the trial judge who issued the lower court's judgment foreclosing his right of redemption had also presided over an earlier condemnation mediation between Mr. Pickett and the City of Frederick (‘Frederick‘), the judge's involvement inthe subsequent redemption case posed an ‘unconstitutional risk of bias‘ that violated his right of due process of law under the Fourteenth Amendment of the U.S. Constitution.

The underlying property dispute.

According to the Maryland Court of Special Appeals, the case below was ‘the latest appeal in more than 10 years of litigation.‘ As explained by the court, Mr. Pickett was the historical owner of the property at issue, which, as a result of delinquentproperty taxes, was sold at a tax sale. Following the tax sale, the City of Frederick filed a complaint in Maryland circuit court to foreclose Mr. Pickett's right to redeem his property.

****4** Mr. Pickett, however, disputed the amount he would be required to pay in order to redeem the property. Thus, in response to the City's complaint, Mr. Pickett asked the circuit court to determine the correct redemption amount. The circuit court judge (who,as is explained in more detail below, previously served as a court-appointed mediator in a related condemnation proceeding) agreed to hold a hearing on the issue but eventually upheld the original redemption amount, which Mr. Pickett ultimately failed to pay.The circuit court therefore foreclosed Mr. Pickett's right of redemption and transferred the property to the City of Frederick.

In response to the circuit court's judgment foreclosing his right of redemption, Mr. Pickett appealed the lower court's ruling to the Maryland Court of Special Appeals. In his appeal, Mr. Pickett alleged several local property tax complaints (which he doesnot ask the U.S. Supreme Court to review in his petition for certiorari) and also asked the Court of Special Appeals whether ‘the failure of the trial judge who considered and issued the final order foreclosing equity of redemption to recuse himself basedon his earlier mediation between the parties [constituted] a denial of due process?‘

The trial judge's prior involvement in the dispute.

According to Mr. Pickett, the circuit court judge who foreclosed his right of redemption ‘should have recused himself from the proceedings because [he] had served as a court-appointed mediator between the parties in a separate condemnation ***40** case concerning the same property . . . prior to his appointment to the bench.‘ The Maryland Court of Special Appeals disagreed.

Citing to the Maryland Code of Judicial Conduct, the Court of Special Appeals noted that Maryland judges are to disqualify themselves in ‘any proceeding in which the judge's impartiality might reasonably be questioned, including the following circumstances:(1) The judge has a personal bias or prejudice concerning a party or a party's lawyer, or personal knowledge of facts *that are in dispute* in the proceeding.‘ Although the court acknowledged that the judge had previously served as a mediatorin a related condemnation case, the Maryland Court of Special Appeals held that ‘[Mr.] Pickett has not directed our attention to any specific fact in dispute in this tax foreclosure case that [the circuit court judge] may have had personalknowledge of as a result of his role as a mediator during the condemnation case 10 years ago.‘ And, ‘[w]ithout such evidence and given

the strong presumption of judicial impartiality,‘the Court of Special Appeals found that ‘any privileged knowledge [the circuit court judge] may have obtained from the parties during the condemnation case had no bearing on this tax foreclosure case.‘

Questions presented.

Citing to *Williams v. Pennsylvania*, 136 S. Ct. 1899 (2016), Mr. Pickett claims in his petition for certiorari that ‘due process of law requires adjudication by a judge who satisfies the objective appearance of impartiality. ‘ In lightof this principle, Mr. Pickett presents the Court with the following questions for review: [1] ‘Was the failure of the trial judge who considered and issued the judgement foreclosing a property owner's right of redemption to recuse himself dueto his earlier court-ordered and confidential mediation between the parties a denial of due process of law under the Fourteenth Amendment;‘ and [2] ‘When a trial judge fails to meet the objective standards of impartiality required by dueprocess, should prejudice be presumed from his failure to recuse or disqualify himself?‘

Petitions Still Pending

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

States challenge Delaware's right to claim MoneyGram's uncashed ‘official checks.‘

In *Delaware v. Pennsylvania and Wisconsin* (motion for leave to file a bill of complaint filed 5/26/16) and *Arkansas et. al. v. Delaware* (motion for leave to file a bill of complaint filed 6/9/16), Delaware and, in a separate filing, Arkansas (along with 20 other states) ask the U.S. Supreme Court to grant leave to file a complaint and to exercise exclusive and original jurisdiction over the states' complaints pursuant to Article III, Section 2, Clause 2 of the U.S. Constitution and Title 28, Section 1251(a) of the U.S. Code. (On 6/3/16, the State of Wisconsin also filed a brief and motion for leave to file counterclaim after Delaware submitted its complaint namingPennsylvania and Wisconsin as defendants.)

The underlying complaints relate to an ongoing dispute over the proper classification of (and priority rules applicable to) MoneyGram's ‘official checks.‘ In particular, the states disagree as to whether MoneyGram's official checks are properly classifiedas third-party bank checks (which would be subject to the federal common-law priority rules established in *Texas v. New Jersey*, 379 U.S. 674 (1965)) and escheat to MoneyGram's state of incorporation—Delaware—or, alternatively, whetherthe checks are more akin to money orders (which would be subject to special statutory priority rules under the Federal Disposition of Abandoned Money Orders and Traveler's Checks Act of 1974 (the ‘Act‘)) and escheat to the state of purchase —i.e.,Pennsylvania, Wisconsin, Arkansas, Texas, etc.

Although the dispute pits state against state over the proper classification of the official checks and the priority rules applicable thereto, the states do agree on one thing: that the Supreme Court is the exclusive forum that can and should hear the case.

The first state to file its motion for leave to file a bill of complaint was Delaware on 5/26/16. Delaware named Pennsylvania and Wisconsin as defendants in its suit and argues that the U.S. Supreme Court should hear its case because it ‘has no sufficientremedy except by invoking the Court's original jurisdiction in this proceeding.‘

In its bill of complaint, Delaware asks the Court specifically to (1) ‘[d]eclare that MoneyGram Official Checks are not ‘a money order, traveler's check, or other similar written instrument’‘ under the Act; (2) ‘[i]ssueits Decree commanding the State of Wisconsin and the Commonwealth of Pennsylvania not to assert any claim over abandoned and unclaimed property related to MoneyGram Official Checks;‘ and (3) ‘[i]ssue its Decree that all future sums payableon abandoned MoneyGram Official Checks should be remitted to the State of Delaware.‘

On 6/3/16, Wisconsin was the next state to get its papers before the Court, responding to Delaware's bill of complaint by filing a motion for leave to file counterclaim. In its counterclaim, Wisconsin agrees that the Court should exercise its exclusive jurisdiction,but requests that the Court (1) '[d]eclare the rights of Wisconsin with regard to unclaimed funds from Official Checks purchased in Wisconsin, which Delaware has wrongly seized;' (2) '[i]ssue an Order commanding Delaware tocease taking custody of funds from abandoned Official Checks purchased in Wisconsin;' and (3) '[i]ssue an Order commanding Delaware to pay Wisconsin damages in the amount of the unclaimed funds from abandoned Official Checks purchased inWisconsin.'

**6 *42 Wisconsin's counterclaim is a direct response to Delaware's bill of complaint. On 6/19/16, however, Arkansas, along with 20 other states (Arizona, Texas, Alabama, Colorado, Florida, Idaho, Indiana, Kansas, Kentucky, Louisiana, Michigan, Montana, Nebraska,Nevada, North Dakota, Ohio, Oklahoma, South Carolina, Utah and West Virginia) filed a separate motion for leave to file bill of complaint with the Court. These states also agree that the Court should exercise its original and exclusive jurisdiction over thedispute, but similar to Wisconsin's claims, the states allege that Delaware has wrongly claimed funds related to MoneyGram's official checks.

Specifically, Arkansas and its counterparts ask the Court to (1) '[d]eclare the rights of the Plaintiff States to the sums payable on unclaimed and abandoned MoneyGram official checks purchased in the Plaintiff States and unlawfully remittedto the State of Delaware;' (2) '[d]eclare the rights of the Plaintiff States to future sums payable on unclaimed and abandoned MoneyGram official checks purchased in the Plaintiff States;' and (3) '[i]ssue its decree commandingthe State of Delaware, its officers, citizens, and subdivisions, to: (a) deliver to the Plaintiff States sums payable on unclaimed and abandoned MoneyGram official checks purchased in those States and unlawfully remitted to Delaware; [and] (b) cease-and-desistall actions which interfere with and impede the authority of the Plaintiff States to take custody of sums payable on unclaimed and abandoned MoneyGram official checks purchased in those States. '(For more background on this case, including a detailed discussion of MoneyGram's 'official checks' and the general priority rules for unclaimed intangible personal property, see U.S. Supreme Court Update, 26 JMT 42 (September 2016).)

California taxpayer asks Court to review scope of Tax Injunction Act.

In *Huang v. City of Los Angeles,* Docket No. 15-1507, ruling below at 2006 WL 683269 (9th Cir. 2016), the U.S. Court of Appeals for the Ninth Circuit largely affirmed a district court's ruling that (1) certain business taxes assessed by the Cityof Los Angeles, as well as penalties added thereto for delinquent payment, qualify as 'taxes' under the Tax Injunction Act, such that the lower federal court lacked subject matter jurisdiction to hear a taxpayer's claim, and (2) that the Tax InjunctionAct also deprived the lower court of jurisdiction to hear the taxpayer's challenge to the methods by which the City of Los Angeles obtains information during its audits.

The taxpayer, Roger Huang, a general partner of a partnership that owns an apartment building near Dodger Stadium, argues that the Court should grant his petition to (1) resolve a circuit split as to whether the Tax Injunction Act deprives federal courtsof jurisdiction to hear challenges to a penalty imposed for failing to pay a tax and (2) address the Ninth Circuit's failure to follow the Supreme Court's recent precedent as announced in *Direct Marketing Ass'n v. Brohl,* 135 S. Ct. 1124 (2015),which, according to Huang, held that 'the Tax Injunction Act does not bar federal jurisdiction for challenges to the methods by which the government gathers the information it uses to calculate tax liability.'

**7 In his petition for certiorari, Huang presents the following questions for review: '(1) Whether a penalty imposed for failing to pay a tax is itself a 'tax' under the Tax Injunction Act,' and '(2) Whether the Tax Injunction Act deprivesfederal courts of jurisdiction to hear a taxpayer's challenge to the method by which the government obtains the information it uses to calculate tax liability.' (For more background on this case, including a detailed discussion of the lower court's findings,see U.S. Supreme Court Update, 26 JMT 42 (September 2016).)

Supreme Court continues to receive amicus briefs in Multistate Tax Compact litigation.

The Supreme Court continues to receive new amicus briefs in *Gillette v. California Franchise Tax Board*, Docket No. 15-1442, petition for cert. filed 5/27/16, ruling below at 363 P.3d 94 (Cal. 2015). Recent briefs have been filed by the Tax Foundation,the Council on State Taxation and the Tax Executives Institute (all filed 6/30/16).

In this case, which is the latest development in the protracted litigation involving various states' attempts to override the Multistate Tax Compact (the ‘Compact‘), Gillette, along with several other corporate taxpayers, asks the Court to reviewa decision by the California Supreme Court, in which California's highest court held that the Compact does not qualify as a binding reciprocal agreement.

The petition for certiorari argues, among other things, that review is warranted because the California Supreme Court erred in its holding that the Compact is not a binding contract and, therefore, subject to the U.S. Constitution's Contract Clause. Accordingto Gillette, having ‘held that the Compact is not binding, the California Supreme Court declined to decide whether a binding interstate compact that has not been approved by Congress takes precedence over other state law or whether California's departurefrom the Compact violates the Contract Clause.‘

Noting that the Compact is ‘a multistate agreement that addresses significant aspects of the state taxation of multistate businesses,‘ Gillette and its counterparts now ask the U.S. Supreme Court whether ‘the Multistate Tax Compact has the statusof a contract that binds its signatory states.‘ (For more background on this case, including a detailed discussion of the California court's ruling, see U.S. Supreme Court Update, 26JMT 43 (August 2016).)

Rite Aid sought review of real property tax assessments issued against several New York State commercial properties.

According to Mr. Pickett, the circuit court judge who foreclosed his right of redemption ‘should have recused himself . . . because [he] had served as a court-appointed mediator between the parties in a separate condemnation case . . ..‘

The states agree on one thing: that the Supreme Court is the exclusive forum that can and should hear the case [on the classification of MoneyGram's official checks].

The Supreme Court continues to receive new amicus briefs in *Gillette v. California Franchise Tax Board.*

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