UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF NEW YORK

SENECA NATION OF INDIANS,

Plaintiff,

v.

DAVID PATERSON, Governor of the State of New York, JAMIE WOODWARD, Acting Commissioner, New York State Department of Taxation and Finance, WILLIAM COMISKEY, Deputy Commissioner, Office of Tax Enforcement, New York State Department of Taxation and Finance, JOHN MELVILLE, Acting Superintendent, New York State Police, each in his or her official capacity,

Defendants.

Civil Action
No. 10-cv-00687-RJA

DEFENDANTS' MEMORANDUM OF LAW IN OPPOSITION TO THE SENECA NATION OF INDIANS' MOTION FOR PRELIMINARY INJUNCTION OR TEMPORARY RESTRAINING ORDER

PRELIMINARY STATEMENT

In June 2010, New York State enacted legislation designed to facilitate the enforcement and collection of cigarette taxes, including those on taxable reservation sales of cigarettes—*i.e.*, sales other than those intended for personal consumption by members of the reservation's governing tribe. The legislation requires its provisions to be enforced starting September 1, 2010, and contains a timetable for preparations designed to ensure that enforcement would commence on that date.

Under the amended Tax Law, cigarette wholesalers and stamping agents must prepay the tax for any cigarettes that will be sold in New York. To evidence this prepayment, a stamp must be attached to virtually all cigarette packages (with certain narrow exceptions not applicable here, *see* 20 N.Y.C.R.R. pt. 76). The new system mandates that no packages of cigarettes, including those intended for tribal consumption, may be sold in New York absent such a stamp (Smirlock Aff. ¶ 10). The amended Tax Law further provides, however, that qualified Indians and reservation cigarette sellers may generally purchase cigarettes tax-free from wholesalers and agents for tribal members' personal on-reservation consumption; the wholesalers and agents may then obtain refunds of the tax they prepaid. Thus, under the new system, tax collection occurs off the reservation and away from the tribes, and is the sole responsibility of State-licensed stamping agents and wholesalers, none of which are Indians or are located on Indian reservations (Woodard Aff. ¶ 22).

The new statute, and the regulations that New York's Department of Taxation and Finance (the "Department") have promulgated, provide several alternative mechanisms for shielding from tax the sale of cigarettes to tribal members for their own consumption, while still policing against the illegal sale of untaxed cigarettes to non-members. The statute and regulations afford the tribes an array of options for estimating the magnitude of such tax-exempt sales and for allotting to each tribe a corresponding number of cigarettes that can be purchased tax-free. These options were expressly designed to respect tribal self-government.

Tribes may elect to allocate their tax-exempt allotments themselves among their reservation retailers through a tax-exemption coupon system, or, in the alternative, they may receive their allotments through a prior approval system under which state-licensed wholesalers obtain the Department's approval for each tax-exempt sale of cigarettes to tribes and reservation retailers. Under either of these systems, tribes may submit evidence to the Department regarding the amount of their "probable demand" for cigarettes. The statute also provides that individual tribes may establish allotments of tax-free cigarettes outside the coupon or prior approval systems by entering into agreements with the State.

The Seneca Nation of Indians ("SNI") commenced this action for declaratory and injunctive relief seeking to prevent New York from implementing the 2010 statute and regulations. In particular, the SNI now moves for a preliminary injunction to delay implementation while this case is heard.

This Court should deny the SNI's motion. The SNI's various arguments all ultimately rest on its sweeping claim that the enforcement of New York's 2010 statute and regulations is precluded by the SNI's right under federal law to make its own laws and be ruled by them (*see* SNI Memorandum of Law in Support of Motion ["Memo"] at 31). This claim is wholly meritless. Federal and State laws recognize the SNI's legitimate interest in assuring an adequate supply of tax-free cigarettes for the consumption of the tribe and its members. But the SNI and its members have no right to continue selling unlimited quantities of unstamped and tax-free cigarettes to nonmembers. *See Wash. v. Confederated Tribes of Colville*

Indian Reservation, 447 U.S. 134, 154-59 (1980). Because the SNI has not shown that enforcement of New York's 2010 statute and regulations will interfere with its access to a sufficient quantity of tax-free cigarettes to meet its legitimate demand for reservation consumption, the SNI cannot demonstrate either a clear likelihood of success on the merits nor a judicially cognizable irreparable injury to any federally-protected right. Accordingly, this Court should deny the SNI's motion for a preliminary injunction.

STATEMENT OF THE CASE

A. New York's Cigarette Excise Tax

Article 20 of the New York Tax Law imposes an excise tax on cigarettes and tobacco. In particular, Tax Law § 471(1), contained in Article 20, imposes an excise tax on all cigarettes sold in New York, except that no such tax is imposed on cigarettes sold where New York does not have power to tax. Tax Law § 471(2) provides that the ultimate incidence of and liability for the cigarette excise tax is on the consumer. But the chain of taxation begins with New York State-licensed cigarette stamping agents, which purchase cigarettes from manufacturers. Agents advance the excise tax by purchasing cigarette excise tax stamps, which they affix to each pack of cigarettes as evidence that the excise tax has been paid. Sometimes agents act as wholesale dealers and sell cigarettes directly to retailers. Sometimes agents sell to wholesale dealers, who then sell to retailers. Either way, the excise tax is eventually passed through to the consumer as part of the cost of cigarettes.

Prepaid sales taxes are also reflected in the tax stamp, as required by Tax Law § 1103, and are passed through to the consumer in the same manner. (Smirlock Aff. ¶ 5.)

Although under federal law the State cannot tax on-reservation cigarette sales to members of the reservation's governing tribe for their own consumption, since 1976, the Supreme Court has repeatedly upheld the authority of states to tax "[o]n-reservation cigarette sales to persons other than reservation Indians." *Dep't of Taxation and Finance of N.Y. v. Milhelm Attea & Bros., Inc.*, 512 U.S. 61, 64 (1994); *see also Okla. Tax Comm'n v. Citizen Band Potawatomi Indian Tribe*, 498 U.S. 505 (1991); *Cal. State Bd. of Equalization v. Chemeheuvi Indian Tribe*, 474 U.S. 9 (1985); *Colville*, 447 U.S. at 150-62; *Moe v. Confederated Salish and Kootenai Tribes*, 425 U.S. 463, 481-83 (1976); *see also Matter of N.Y. State Dep't of Taxation and Finance v. Bramhall*, 235 A.D.2d 75, 85-86 (4th Dep't), *appeal dismissed*, 91 N.Y.2d 849 (1997) (rejecting challenges to motor fuel tax enforcement); *Snyder v. Wetzler*, 193 A.D.2d 329 (3d Dep't 1993), *aff'd*, 84 N.Y.2d 941 (1994) (rejecting claim by Seneca reservation retailer that he cannot be required to collect taxes on sales to nonmembers); *Ward v. State of New York*, 291 F. Supp. 2d 188, 199-206 (W.D.N.Y. 2003) (Indian reservation smoke shop owners are unlikely to succeed on the merits of their challenge to a state law barring them from shipping and transporting cigarettes to off-reservation customers).

The lengthy background of the State's efforts to collect the taxes due on cigarettes sold on reservations to non-tribe members is summarized in *City of N.Y.*

v. Milhelm Attea & Bros., Inc., 550 F. Supp. 2d 332, 337-38 (E.D.N.Y. 2008). What is relevant for present purposes is that, after the Supreme Court's 1994 *Attea* decision vindicating the State's taxing authority and an abortive enforcement attempt in 1997, the Department eventually adopted what came to be known as the policy of forbearance, allowing stamping agents to sell unstamped cigarettes without restriction to recognized Indian nations and reservation-based retailers (Woodard Aff. ¶ 4). This policy was formally announced in 2006 in Advisory Opinion TSB-A-06(2)M (Woodward Aff. Ex. A). That opinion stated that if the Department decided to change the forbearance policy, it would provide notice (Woodard Aff. ¶ 4).

On February 23, 2010, the Department formally provided such notice when it revoked the advisory opinion (Woodard Aff. Ex. B). However, at that time, preliminary injunctions in New York State court litigation involving SNI retailers and members prevented the Department from enforcing the Tax Law against on-reservation cigarette sales to non-members (Woodard Aff. ¶¶ 17-18).[1] *See Day Wholesale, Inc. v. State*, 51 A.D. 3d 383 (4th Dep't 2008).

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[1] The SNI suggests that the Department, through its Commissioner, has conceded that these injunctions prevent the enforcement of the newly amended Tax Law (Memo at 15). But the Commissioner's statements were merely descriptions of those injunctions, all of which predate the recent amendments. Contrary to the SNI's suggestion here, the Department's position is that these injunctions are no longer viable in light of the new tax regime and the Department's recently promulgated regulations. The Department filed a motion to vacate these injunctions in state court only in an abundance of caution to ensure that no conceivable obstacle remained in the way of the new tax regime's implementation on September 1. (Woodard Aff. ¶ 18.)

B. The 2010 Legislation

On June 21, 2010, the New York Legislature enacted legislation designed to facilitate enforcement of the Tax Law with respect to taxable on-reservation cigarette sales, and provided a timetable for preparing and commencing enforcement. *See* 2010 N.Y. Laws, ch. 134, pt. D ("Part D"), *as amended by* ch. 136, § 1 (Smirlock Aff. Ex. A-B). As set forth below, the legislation modified the coupon system in certain respects, and also provided an alternative mechanism for exempting non-taxable sales, giving each tribe the opportunity to choose between the two administrative mechanisms.

In Part D, the Legislature clarified that the cigarette excise tax is applicable to on-reservation cigarette sales to non-Indians and non-members of the tribe that occupies that reservation. The legislation also makes clear that the Indian tax exemption coupon system established by Tax Law § 471-e is just a mechanism for the delivery of quantities of tax-exempt cigarettes to Indian nations or tribes for personal use and consumption. Part D also establishes that all cigarettes sold by agents and wholesale dealers to an Indian reservation must bear a tax stamp, regardless of who is purchasing or will purchase the cigarettes. (Smirlock Aff. ¶ 9, Ex. A at 8.)

Part D, as amended by ch. 136, § 1 (Smirlock Aff. Ex. B), requires that within 60 days—that is, by August 20, 2010—the Department must "promulgate any rules and regulations and take any other actions necessary to fully implement" both the coupon system and the prior approval system, "including, but not limited to, the

establishment, issuance, and provision of Indian tax exemption coupons" (Smirlock Aff. Ex. A at 12). Part D also changed the role of the coupon system, permitting an Indian tribe to elect to participate in the Indian tax exemption coupon system rather than mandating participation (*id.* at 11). A tribe that elects to participate will receive coupons from the Department on a quarterly basis that it can use or distribute to reservation cigarette sellers in order to obtain tax-exempt cigarettes (*id.*). The amount of coupons provided to each Indian tribe is determined by the "probable demand" of the tribe for the year (*id.*). When an agent or wholesale dealer receives the coupons from a nation, tribe, or reservation cigarette seller, the agent or wholesale dealer can sell cigarettes to that entity in the amount represented by that quantity of coupons without collecting the tax. *See* Tax Law § 471-e(3). The agent or wholesaler would then submit the coupons to the Department for an expedited refund or credit of its prepaid tax. *See id.* §§ 471-e(4), 476. (*See generally* Smirlock Aff. ¶ 13.)

As an alternative to the coupon system, Part D also creates a prior approval system (Smirlock Aff. Ex. A at 9-10). Under new subsection 5 of Tax Law 471, when a tribe does not choose to participate in the coupon system, an agent or wholesale dealer can obtain from the Department prior approval for a particular sale of stamped tax-exempt products to a qualified purchaser from that tribe; in the aggregate, all such sales cannot exceed the tribe's probable demand amount. The prior approval system, like the coupon system, requires that all cigarettes sold by agents and wholesale dealers to an Indian reservation bear a tax stamp regardless

of who is purchasing the cigarettes (*id.* at 9; Smirlock Aff. ¶ 14). The Department is charged with establishing by regulation the manner and form of the prior approval system (Smirlock Aff. Ex. B).

C. The 2010 Regulations

On June 22, 2010, the Department adopted an emergency rule providing regulations to supplement the terms of the statute (Woodward Aff. Ex. C). This rule became effective that day upon filing with the Department of State. The rule adds a new regulation, 20 N.Y.C.R.R. § 74.6, that provides additional details for both the coupon system and the prior approval system. Both systems are designed to ensure that adequate quantities of stamped tax-exempt cigarettes will be available to Indian nations or tribes and their members based on their probable demand. (Woodard Aff. ¶¶ 7-8.)

The emergency rule also establishes specific methods and procedures that the Department will use to calculate probable demand under both the coupon and prior-approval systems (Woodward Aff. Ex. C at 5-7). Under this methodology, the probable demand for the SNI works out to 168,600 packs (16,860 cartons) each quarter, for a population of 7,243 (including children) (Woodard Aff. ¶ 19). An Indian tribe that believes that the probable demand calculated by the Department for a given year is inaccurate may contact the Department to explain why it believes the calculation is inaccurate. The Department will consider any evidence submitted by July 31 in determining the probable demand for the ensuing twelve-month period beginning September 1 (Woodward Aff. Ex. C at 7). Indian nations and

tribes have until August 15 each year to elect to participate in the Indian tax exemption coupon system. This election is made for the twelve-month period beginning September 1 and ending August 31. (*Id.* at 1-3.) The SNI has neither contested the Emergency Rule's probable demand calculation, nor elected to participate in the coupon system, despite the rule's clear deadlines (Woodard Aff. ¶¶ 10, 12).

Finally, the rule establishes that the Department will provide Indian tax exemption coupons on a quarterly basis to the recognized governing body of any Indian tribe located in New York that elects to participate in the Indian tax exemption coupon system (*id.* at 3).

Under § 202(6) of the State Administrative Procedure Act, the emergency rule is effective for 90 days, until September 19, 2010. The Department proposed the rule as a permanent rule on August 11, 2010, and also intends to readopt the emergency rule to extend it another sixty days, in order to ensure that it remains in effect until the proposed rule can be adopted as a permanent rule. (Woodard Aff. ¶ 7.)

To provide further guidance on the implementation of Part D and the emergency regulations, on July 29, 2010, the Department issued a technical memorandum (TSB-M) on the coupon and prior approval systems (Woodward Aff. Ex. D-E). A TSB-M is an informational statement explaining existing Department policies and/or outlining changes in the law, regulations, or Department policies. Each Indian nation or tribe, cigarette manufacturer, agent, and wholesaler has

been sent the TSB-M, and it also appears on the Department's web site. (Woodard Aff. ¶ 13.)

Both the coupon system and the prior approval system, as provided for in the 2010 legislation and regulations, are designed to ensure that Indian nations or tribes can obtain the amount of cigarettes necessary to satisfy the probable demand of the tribe and its members for cigarettes for on-reservation consumption without the nations or tribes or the tribal members having to pay any New York State tax on them.

The State financial plan anticipates that $110 million will be collected under §§ 471 and 471-e of the Tax Law as a result of the implementation of the new provisions during the current fiscal year (Woodard Aff. ¶ 23). The majority of this revenue (75%) is dedicated revenue that supports important health care programs that benefit all residents of the state (*id.*). The Department is currently on schedule for the coupon and prior approval systems to be implemented and operational as of September 1, 2010, the date that the Legislature mandated that the amended Tax Law begin to be enforced. Thus, it is of critical importance that no barriers to enforcement of the amended Tax Law remain.

D. The SNI's Tobacco Economy

The SNI claims that it is "an active and responsible regulator of the tobacco economy that exists in its Territories" (Memo at 7) and that it regularly partners with non-Indian regulators to keep contraband cigarettes out of tribal territory (Memo at 5-6). But this description of the Indian cigarette trade excludes two of its

most prominent features: the SNI's refusal to comply with either State or federal laws; and the SNI tobacco economy's reliance on tax evasion.

Recent litigation in this Court between SNI members and the federal government has highlighted these two features. On June 25, 2010, a member of the SNI and an SNI cigarette seller sued the federal government to prevent enforcement of the Prevent All Cigarette Trafficking Act of 2009 ("PACT Act"), Pub. L. No. 111-154, 124 Stat. 1087 (2010). *See* Complaint, Docket Entry #1, *Red Earth LLC v. United States*, No. 10-CV-530A (W.D.N.Y. June 25, 2010) (Arcara, J.). The PACT Act "requires retailers of cigarettes and smokeless tobacco who perform 'delivery sales' to comply with all state and local laws in the jurisdiction where those products are being delivered." *Red Earth LLC v. United States*, --- F.Supp.2d ---, 2010 WL 3061103, at *1 (W.D.N.Y. July 30, 2010).

In opposing the plaintiffs' request for a preliminary injunction, the United States presented a declaration by Ronald B. Turk, the Special Agent in Charge of the New York Field Division of the Bureau of Alcohol, Tobacco, Firearms, and Explosives. *See* Declaration of Ronald B. Turk ("Turk Decl."), Ex. C of Supplemental Memorandum of Law on Behalf of Defendant in Opposition to Plaintiffs' Motion for a Preliminary Injunction, Docket Entry # 28, *Red Earth*, *supra* (W.D.N.Y. July 6, 2010). Turk testified that the SNI has tolerated "large shipments of untaxed cigarettes" that were being sold on or from its territories without complying with the strict requirements of both State and federal law. *Id.* ¶ 9. In 2009, for example, over 10 million cartons of untaxed cigarettes were sold to the

SNI, even though the probable demand of the SNI's members is less than 70,000 cartons per year (Woodward Aff. ¶¶ 19-20). Moreover, the SNI has "refused to require these businesses to come into compliance," despite numerous requests by State and federal officials. Turk Decl. ¶ 10. As a result, most reservation cigarette sellers "are still involved in activities which deprive the States of substantial amounts of tobacco tax revenue; these activities are not conducted in accordance with the provisions of Federal law in that the sales are generally not reported to state taxation authorities as is required." *Id.*

The SNI's refusal to comply with applicable State and federal tax laws is no accident. As the Department of Justice observed in the *Red Earth* litigation, the SNI's tobacco economy relies "near exclusively [on] the evasion of State excise taxes and the refusal to affirmatively report . . . tax-free sales as required by federal law." Memorandum of Law in Opposition to Plaintiffs' Motion for a Preliminary Injunction at 11, Docket Entry # 25, *Red Earth*, *supra* (W.D.N.Y. July 1, 2010). In other words, the SNI's reservation cigarette sellers gain a competitive advantage by deliberately flouting applicable regulations and "market[ing] an exemption from state taxation to persons who would normally do their business elsewhere." *Colville*, 447 U.S. at 155. Far from presiding over a well-regulated tobacco economy, the SNI instead benefits from widespread noncompliance by the reservation retailers with the cigarette tax laws of the states and the federal government.

ARGUMENT

The SNI has moved in this Court for an emergency preliminary injunction or temporary restraining order preventing the State and the Department from enforcing the amended Tax Law on its legislatively mandated enforcement date of September 1, 2010. Ordinarily a party seeking injunctive relief need only show irreparable injury and either a probability of success on the merits, or sufficiently serious questions going to the merits. *See Motorola Credit Corp. v. Uzan*, 322 F.3d 130, 135 (2d Cir. 2003). As this Court has recently held, however, a party seeking to preliminarily "enjoin application of a governmental statute or regulation" must meet a higher standard: in addition to showing irreparable harm, it bears the burden of demonstrating "a *clear* likelihood of success on the merits." *Red Earth LLC*, 2010 WL 3061103, at *2 (emphasis added). "[T]his exception reflects the idea that governmental policies implemented through legislation or regulations developed through presumptively reasoned democratic processes are entitled to a higher degree of deference and should not be enjoined lightly." *Able v. United States*, 44 F.3d 128, 131 (2d Cir. 1995). A moving party must therefore make "a clear showing" of a clear likelihood of success on the merits in order to obtain the "extraordinary and drastic remedy" of a preliminary injunction. *Mazurek v. Armstrong*, 520 U.S. 968, 972 (1997) (quoting 11A C. Wright, A. Miller, & M. Kane, *Federal Practice and Procedure* § 2948, at 129-130 (2d ed. 1995)).

Here, the SNI has failed to show a clear likelihood of success on the merits. The new tax regime closely resembles cigarette taxing schemes that the Supreme

Court has previously upheld, and the SNI's claims of interference with its sovereignty and its licensed businesses are baseless.

New York is not infringing on the SNI's right to self-government. In *Colville*, the Supreme Court made clear that the tribes have no federal right to a cigarette economy based on "solely an exemption from state taxation." 447 U.S. at 155. Here, the SNI admits that it is marketing a claimed tax exemption (*see* Decl. of Jonathan Taylor in Support of Motion ["Taylor Decl."] ¶ 25 ("New York's exorbitant taxes . . . make tax-immune cigarettes valuable")). But no principles of federal Indian law, "whether stated in terms of pre-emption, tribal self-government, or otherwise, authorize Indian tribes thus to market an exemption from state taxation to persons who would normally do their business elsewhere." *Colville*, 447 U.S. at 155. Thus, although "the result of imposing [state] taxes will be to deprive the [SNI] of revenues which [it is] currently receiving," the State does not thereby infringe on the SNI's right to make its own laws and be ruled by them. *Id.* at 156. Even where, as the SNI alleges to be the case here (Memo at 3-7), its "tribal ordinances . . . comprehensively regulate the marketing of cigarettes by the tribal enterprises . . . the State does not interfere with the Tribes' power to regulate tribal enterprises when it simply imposes its tax on sales to nonmembers." *Id.* at 159.

Nor is New York impermissibly burdening the SNI. The collection burdens imposed by New York's law are imposed not on the Indian tribes but instead on non-Indian stamping agents and wholesalers, which prepay the cigarette tax and which must seek refunds for their tax-exempt probable demand sales to tribes and

tribal retailers. To the extent that the new law imposes any burdens at all on the SNI, they are trivial when compared to the burdens that the Supreme Court has permitted states to impose on tribes to facilitate the collection of legitimate state taxes. These approved burdens include requiring the tribes themselves to affix State tax stamps on cigarette packages, to collect taxes on sales to nonmembers, and to keep and make available for state inspection "extensive" records of both tax-exempt sales to tribal members and taxable sales to nonmembers. *See Attea*, 512 U.S. at 71-72; *Colville*, 447 U.S. at 159-60.

Finally, New York's requirement that virtually every pack of cigarettes be stamped, including those that will ultimately be sold tax free to tribes and reservation retailers, imposes no burden on the tribes or their members, who are entitled to purchase stamped cigarettes up to the probable demand amount without paying the tax. In addition, courts have upheld universal stamping/prepayment laws that require the tribes themselves to prepay the tax on exempt sales to members. *See, e.g., Keweenaw Bay Indian Community v. Rising*, 477 F.3d 881, 890-93 (6th Cir. 2007).

In addition to failing to show a clear likelihood of success on the merits, the SNI has not shown that it faces any threat of irreparable injury. Nor has it shown that issuing a preliminary injunction here would serve the public interest; to the contrary, enjoining the amended Tax Law would deprive the State of desperately needed revenues and harm the State's public health initiatives. As a result, this

Court should deny the SNI's motion for a preliminary injunction or temporary restraining order.

POINT I

THE SNI HAS NOT SHOWN A CLEAR LIKELIHOOD OF SUCCESS ON THE MERITS

The SNI's pre-enforcement "challenge to New York's regulatory scheme is essentially a facial one." *Attea*, 512 U.S. at 69; *see also id.* at 67-68 (noting that the lawsuit in *Attea*, like the SNI's action here, was filed "[b]efore New York's cigarette tax enforcement scheme went into effect"). To prevail on a facial challenge—"the most difficult challenge to mount successfully"—a plaintiff "must establish that no set of circumstances exists under which the [challenged legislation] would be valid." *United States v. Salerno*, 481 U.S. 739, 745 (1987). Here, the amended Tax Law provides three mechanisms for Indian tribes to avoid paying taxes on cigarettes that will be used by the tribes or their members: the coupon system, the prior approval system, and tax agreements negotiated between the State and individual Indian tribes. Moreover, the amended Tax Law gives Indian tribes total discretion to manage reservation cigarette sellers and their own members; for example, Indian tribes are free to implement any method of distributing tax-exemption coupons. Thus, the amended Tax Law must be sustained against the SNI's facial challenge if any of the three mechanisms, and any conceivable exercise of an Indian tribe's discretion, could be constitutional.

In addition, because "[c]laims of facial invalidity often rest on speculation," the Supreme Court has cautioned against arguments that rest upon "speculat[ion] about hypothetical or imaginary cases." *Wash. State Grange v. Wash. State Republican Party*, 552 U.S. 442, 450-51 (2008) (quotation marks omitted). Instead, a facial attack must be confined to any "alleged defects that inhere in the regulations as written." *Attea*, 512 U.S. at 69. In *Attea*, the Court held that this prohibition on speculative reasoning precluded any contest of the Department's probable-demand calculations; the Court accordingly "assume[d] that the allocations for each reservation will be sufficiently generous to satisfy the legitimate demands of those reservation Indians who smoked cigarettes." *Id.*; *see also id.* at 76-77. Thus, in this action, the SNI's facial attack on the amended Tax Law must be evaluated against the background assumption that, whatever mechanism it ultimately elects to adopt, it will receive an adequate allocation of tax-exempt cigarettes for its qualified members' consumption.[2]

Here, the SNI has failed to meet the stringent standards required to obtain a preliminary injunction based on a facial challenge to a state law. The key features of New York's new tax regime have already been approved by the Supreme Court. Moreover, the SNI has not shown that every conceivable application of the amended Tax Law is overly burdensome. Instead, a proper understanding of the coupon system, the prior approval system, and the tax agreement option shows that all

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[2] In addition, the SNI, like all other Indian tribes, had the opportunity to contest the Department's calculation of probable demand by July 31. It has chosen not to challenge that calculation. (Woodard Aff. ¶¶ 9-10.)

three systems impose a minimal burden on the SNI and its licensed businesses while still permitting the State to exercise its legitimate taxing authority over non-Indians.

A. Supreme Court Precedent Supports the Amended Tax Law's Cigarette Tax Regime.

New York's new cigarette tax regime has several key components: it imposes taxes only on cigarette sales to non-members; it allocates tax-exempt cigarettes to each Indian tribe based upon "probable demand"; and it permits each Indian tribe to elect to receive its allocation of tax-exempt cigarettes through a coupon system, a prior approval system, or a tax agreement. Each of these aspects has been approved by clearly established case law.

As the SNI recognizes (Memo at 27-28), a State may tax the sale of goods sold by Indians on Indian territory to non-members. *See Potawatomi*, 498 U.S. at 512. Here, the Tax Law imposes a cigarette tax within this permissible limit. *See* Tax Law § 471(1). To ensure that qualified Indians are not required to pay any tax, the Tax Law allocates a certain quantity of tax-exempt cigarettes to each Indian tribe based on the "probable demand" of that tribe's members. *Id.* § 471-e(2)(b). In *Attea*, the Supreme Court specifically upheld New York's "probable demand" system, holding that New York may "limit[] the permitted quantity of untaxed cigarettes based on the 'probable demand' of tax-exempt Indian consumers." *Attea*, 512 U.S. at 66.

The coupon system and the prior approval system also find support in the Supreme Court's cases. In fact, *Attea* upheld a coupon system that was far more intrusive than the system at issue here. In *Attea*, the Department itself was responsible for providing tax exemption coupons to reservation retailers, thereby circumventing the tribal government's authority over such entities. *Id.* at 66. Here, by contrast, the State leaves to Indian governments the authority to determine how to distribute coupons among the entities and individuals that they regulate.

Attea also upheld an approval system similar to the prior approval system at issue here. In *Attea*, the Department "preapprove[d] deliveries of tax-exempt cigarettes in order to ensure compliance with the quotas," *id.* at 76, and further required proof that the tax-exempt sale was directed at qualified Indian purchasers, *id.* at 66. Here, similarly, the Department ensures under the prior approval system that any tax-exempt sale is properly made to a qualified Indian purchaser and that the sale does not exceed the allocation of the Indian tribe in question (Woodward Aff. Ex. D at 6).

The SNI attempts to minimize the precedential effect of *Attea* by claiming that that case dealt only with the preemptive effect of the Indian Trader Statutes (Memo at 30). But *Attea* cannot be read so narrowly. The Court made clear that its decision relied on the principles of "tribal sovereignty" that it had earlier established in *Moe* and *Colville*. *See Attea*, 512 U.S. at 74 (noting that the "reasoning" in those cases, which "dealt most directly with claims of interference with tribal sovereignty," compelled the result in this case). And the Court upheld

New York's taxing regime in *Attea* by analogizing it to the regimes that it had similarly upheld in those earlier sovereignty cases. *See id.* at 73-76. Thus, while the specific question at issue in *Attea* concerned the Indian Trader Statutes, the principles underlying that decision apply equally to claims of Indian sovereignty and self-government.

B. The New Tax Regime Imposes Minimal If Any Burdens on the SNI.

The SNI's principal objection to the amended Tax Law is that the mechanisms by which the State enforces limitations on tax-exempt cigarette sales impose overly onerous burdens on the SNI that interfere with the tribe's sovereign right of self-government. The SNI further claims that these burdens will prevent its licensed cigarette sellers from engaging in tax-free commerce. To prevail on this facial challenge, the SNI must show that all of the mechanisms under the statute—the coupon system, the prior approval system, and tax agreements—are too burdensome. But SNI cannot make this showing here because the amended Tax Law in fact imposes almost the least burden that is possible while still ensuring that New York can legitimately tax cigarette sales to non-members.

1. The Coupon System

Under the coupon system, the Department provides each Indian tribe with coupons up to the tribe's quarterly allocation. The amended Tax Law imposes no further burdens on Indian tribes. Instead, the Tax Law leaves to the governing

bodies of each tribe the sovereign decision of how to distribute these tax-exemption coupons to their members and businesses.

Despite having complete freedom to deal with these coupons as it wishes, the SNI paradoxically claims that the coupon system interferes with tribal self-government in two ways. First, the SNI claims that the coupon system will "compel the [SNI] to abandon" its own stamp tax (Memo at 32). But New York's power to tax cigarette sales to non-members is not affected by any parallel regulatory scheme that the SNI may already have in place, "since each government is free to impose its taxes without ousting the other." *Colville*, 447 U.S. at 158.

Second, and more broadly, the SNI complains that under the coupon system it will have to establish an intricate bureaucracy to allocate the coupons among its members and on-reservation businesses (Memo at 32-33). As an initial matter, no such bureaucracy is mandated by the Tax Law itself, and the SNI's estimation of the number of "new laws and regulations" it will be required to develop (Memo at 32) is speculative. In addition, the SNI already licenses and regulates all retailers in its territories, and, as it admits, it already collects extensive data on all cigarettes sold under its jurisdiction (Memo at 4, 31-32). There is thus no reason to believe here, without additional evidence, that the SNI is incapable of devising some scheme to allocate the tax-exemption coupons.

More fundamentally, however, the SNI's complaint about needing to allocate tax-exemption coupons among its citizens and licensed businesses is at odds with its simultaneous claim of an inalienable right to "govern [itself] free of State

interference" (Memo at 24). The SNI's position here, apparently, is that it should not be responsible for "allocat[ing] the State's pre-determined quota among the Nation's numerous licensed stamping agents and retailers" (Memo at 20), and that the Department should be required to undertake, not only that task, but an entire laundry list of on-reservation regulation of Indian entities (Memo at 13-14). At the same time, the SNI contends that "the State may not assert jurisdiction over Indian tribes or their members residing in Indian country" (Memo at 23; *see also id.* 29) and that the State's regulations are effective only "up to the point where tribal self-government would be affected" (Memo at 31 (quoting *McClanahan v. State Tax Comm'n of Ariz.*, 411 U.S. 164, 179 (1973)).

The SNI cannot have it both ways. How to allocate a scarce resource (like the coupons) among tribal businesses and individuals would appear to be a prototypically governmental decision (*see* Memo at 20 ("The regulation of economic activity inside a sovereign's territory is a traditional governmental function.")), yet the SNI faults the State for not making that decision on the tribes' behalf. In other words, according to the SNI, the State cannot itself allocate tax-exemption coupons to Indian tribes or reservation cigarette sellers, since those entities are beyond the State's lawful jurisdiction; but the State also cannot leave such allocation to tribal governments. Under this conception of Indian self-government, in effect, the State may not limit the quantity of tax-exempt cigarettes on Indian territory at all.[3]

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[3] The SNI's argument makes clear that any harm to reservation businesses from the hypothetical absence of a coupon-allocation system (*e.g.*, Memo at 36-41)

That position is contrary to clearly established law. The Supreme Court has specifically held that New York may limit the quantity of tax-exempt cigarettes sold on Indian reservations according to a probable-demand formula. *See Attea*, 512 U.S. at 66. To exercise that concededly legitimate power, New York has provided for a coupon system that gives each Indian tribe a fair allocation of tax-exempt cigarettes. Rather than potentially infringe on tribal authority by dictating which Indian purchasers or retailers could receive such coupons, as it did in *Attea*, New York has instead decided to leave that question to the tribes themselves. Far from intruding on tribal prerogatives, that decision fully respects the tribes' interest in self-government.

2. The Prior Approval System.

Even if the coupon system did interfere with the SNI's right of self-government and with Indian businesses' right to sell tax-free cigarettes, the amended Tax Law must be upheld against a facial challenge because the alternative prior approval system imposes no burden at all on the SNI or its members and businesses. In fact, under that system, the only burdens are borne by non-Indian wholesalers, which are required to obtain the Department's approval before making tax-exempt sales to qualified Indian purchasers.

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derives, not from the amended Tax Law itself, but from the SNI's own "abdicat[ion] [of] its sovereign power over its members and territories" by refusing to "administer a tax-exempt cigarette quota" (Memo at 39).

The SNI does not claim in its motion for a preliminary injunction that the prior approval system itself imposes any burdens. Instead, it claims that the system would result in "severe market distortions" that would harm Indian businesses and that would require the SNI's government "to take drastic, and likely futile action, to address" (Memo at 33). But the "market distortions" that the SNI asserts are wholly speculative. For example, the SNI's economist contends that the Department's web site (which manages the prior approval system) could be hacked by wholesalers who may "enter[] fictitious personal information, collud[e] to corner all the quota, or any number of other imaginable workarounds" (Taylor Decl. ¶ 31(a)). The economist also suggests that the web site could be swamped by applications from "criminals, non-Seneca territory residents, retailers suspended or banned from Seneca tobacco trade, or all of the above" (*id.* ¶ 31(b)). And the economist asserts that the prior approval system "may . . . from time to time" attract "a predatory firm" that will arrogate to itself all of a tribe's quarterly allocation (*id.* ¶ 31(d)).

The economist provides absolutely no evidence, other than his own supposition, that any of these consequences are likely or even possible—and, indeed, his assertions are belied by the Department's own precautions (*e.g.*, Woodard Aff. ¶ 15). Such unsupported speculation is insufficient to support either a preliminary injunction or a facial challenge, let alone both at once. *See United States v. Raines*, 362 U.S. 17, 22 (1960) (laws should not be facially invalidated by "reference to hypothetical cases"); *RoDa Drilling Co. v. Siegal*, 552 F.3d 1203, 1210

(10th Cir. 2009) ("Purely speculative harm will not suffice" to sustain a preliminary injunction.).

In addition, even assuming that the prior approval system would alter the market for cigarettes on Indian territory, this so-called "distortion" would not invalidate the amended Tax Law. The Supreme Court has held that "a nondiscriminatory tax on non-Indian customers of Indian retailers doing business on the reservation" will be valid even if it has a "particularly severe" economic impact. *Colville*, 447 U.S. at 151 & n.26. Indian tribes have no entitlement to revenue from marketing a purported exemption from state cigarette taxes, and an otherwise valid state law does not interfere with tribal sovereignty even if it "deprive[s] the Tribes of revenues which they currently are receiving." *Id.* at 156.[4]

3. Tax Agreements.

As a final option, an Indian tribe that was dissatisfied with both the coupon system and the prior approval system could have entered into tax agreements with the State to supersede the Tax Law and regulations regarding the tribe's sale of cigarettes. This option highlights the degree to which the amended Tax Law respects Indian tribes' authority: rather than impose any particular system, however minimally burdensome, the new tax regime permitted a tribe to work with

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[4] The SNI also complains that there is no "backstop mechanism" whereby an individual Indian may claim an exemption from taxation (Memo at 39). But that statement is inaccurate. The Department's regulations permit a qualified Indian purchaser who wrongfully pays a cigarette tax to seek a refund. *See* 20 N.Y.C.R.R. § 77.1(b)(1).

the State to craft a customized solution that would be maximally compatible both with the tribe's idiosyncratic preferences and with the State's legitimate taxing authority.

The SNI has not shown that such an agreement would have been ineffective at addressing its concerns about the proper allocation of its probable-demand quota. For example, if the SNI had truly wished for the Department to decide, on the tribal government's behalf, how to allocate tax-exempt cigarette sales among reservation businesses, then it could and should have negotiated for an agreement with the State that would have implemented such a system.

Nor can the SNI contend that the State ever responded in bad faith to any request for an agreement. To the contrary, State officials, including the Governor, met repeatedly with SNI officials to address the persistent problem of untaxed cigarettes being sold to non-members on reservation territory (Kiernan Aff. ¶¶ 7, 11, 13, 16, 19, 26). And State officials regularly informed the SNI of the State's interest in resolving this problem through negotiated settlements (*id.* ¶¶ 4, 11, 27). Indeed, the Legislature extended the enforcement date of the amended Tax Law to September 1, 2010, "specifically to allow additional time to consummate negotiations" (*id.* ¶ 23).

But the State's efforts were for naught. The SNI has steadfastly declined to enter into any agreement with either State or federal officials to stop the illegal sale of untaxed cigarettes to non-members (*see also* Turk Decl. ¶ 10). Instead, the SNI has opposed nearly every attempt by the Legislature and the Department to enforce

the State's legitimate taxing power (Kiernan Aff. ¶ 27). In the absence of such an agreement, and in light of the Legislature's strict deadline of September 1, 2010, for the enforcement of the amended Tax Law, the Department must implement by that date the coupon system and/or prior approval system to ensure that the State can begin properly collecting the cigarette taxes that it is owed.

C. The SNI Has Shown No Likelihood of Success on Its Claim Based Upon Prepayment of Cigarette Taxes.

The SNI separately claims that the amended Tax Law improperly "require[s] the prepayment of cigarette tax to which New York has no lawful entitlement" (Memo at 41). The SNI's claim is limited to the cigarettes sold on the SNI's reservations to SNI members for their consumption, which New York is not authorized to tax. But the SNI's claim as to these cigarettes is unlikely to succeed on the merits for several reasons.

Preliminarily, the SNI has no standing to bring it. Under the new tax regime, only non-Indian wholesalers and stamping agents are required to prepay the tax on these cigarettes. By contrast, whether through the coupon system or the prior approval system, no tribe or qualified Indian retailer or member will be required to pay or prepay a cigarette tax on reservation purchases intended for tribal consumption, since a wholesaler is authorized to sell cigarettes tax-free up to the probable demand amount to those qualified purchasers. Because the SNI does not prepay any cigarette taxes on cigarettes within the probable demand amount for tribal consumption, it cannot complain here that requiring the non-Indian

wholesalers to do so is illegal. *See Ammex, Inc. v. United States*, 367 F.3d 530, 534 (6th Cir. 2004) (holding that the plaintiff had no Article III standing to sue when the tax was imposed on the plaintiff's suppliers, rather than the plaintiff itself).

Even if the SNI had standing to make the claim, which it does not, this claim could not support preliminary relief because the SNI has not shown a clear likelihood of success on this claim. The Sixth Circuit recently held that a State may require even Indian tribes to prepay cigarette taxes in order to ensure that non-members do not evade taxation. *See Keweenaw Bay Indian Community*, 477 F.3d at 891-92. And in *Potawatomi*, the Supreme Court approved off-reservation seizures of cigarettes from wholesalers, a far more drastic enforcement mechanism than simply requiring licensed stamping agents to stamp all cigarettes and apply for refunds for their tribal probable demand sales. *See Potawatomi*, 498 U.S. at 514; *see also Colville*, 447 U.S. at 161-62. It follows *a fortiori* that New York may require State-licensed wholesalers and stamping agents, which are not members of any Indian tribe, to prepay the taxes.[5]

Finally, New York's requirement that every package of cigarettes be stamped applies to the more than 100 million packs of cigarettes that pass through the SNI territories each year (Woodward Aff. ¶ 20). Only a tiny fraction of these cigarettes

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[5] The SNI suggests that the Supreme Court's decision in *Attea* frowned upon prepayment of taxes for cigarettes that ultimately would end up with tax-exempt Indian purchasers. But in *Attea* the Court was simply describing New York's tax regime (as it then existed), and emphasized this description only to correct the New York Court of Appeals' erroneous conclusion that New York's prepayment requirement was equivalent to the imposition of a sales tax on Indians. *See* 512 U.S. at 69, 75-76.

are necessary to satisfy the demand of Seneca smokers, who number no more than a few thousand (*id.* ¶ 19 (estimating the SNI's population at under 8,000)). Thus, even if the Court were to find, contrary to our arguments, that New York cannot require the stamping agents to pre-collect the tax on this tiny fraction, New York's pre-collection requirement would still be valid as to the rest of the 100 million packs of cigarettes and should be sustained as to them. *See Red Earth*, 2010 WL 3061103, at *18 (severing invalid provision of the PACT Act and sustaining the remainder).

In light of these precedents, and even ignoring its lack of standing, the SNI has not shown a clear likelihood of success on its claim that the amended Tax Law improperly requires the prepayment of cigarette taxes.

D. Federal Law Fully Supports the State's Taxing Authority Here.

Finally, the SNI suggests that the amended Tax Law contravenes federal law, which (according to the SNI) precludes State regulation of on-reservation cigarette sales (Memo at 25-26, 35). But the SNI mischaracterizes the federal government's position. "In fact, the federal government has been generally supportive of *state* regulation of cigarette sales." *Ward*, 291 F. Supp. 2d at 204. The Contraband Cigarette Trafficking Act, for example, bans large-scale sales of cigarettes that "bear no evidence of the payment of applicable State or local cigarette taxes" when, as here, "the State or local government requires a stamp, impression, or other indication to be placed on packages or other containers of cigarettes to evidence payment of cigarette taxes." 18 U.S.C. § 2341(2). And this

Court recently recognized that, with the PACT Act, "Congress intended to assist state and local governments in the collection of cigarette and smokeless tobacco excise taxes." *Red Earth*, 2010 WL 3061103, at *5. Thus, far from frowning on the State's taxing authority, the federal government has actively encouraged and aided States' efforts to enforce their tax laws by curtailing the illegal sales of untaxed cigarettes and collecting cigarette taxes from reservation sales to non-members.

Nor is there any basis for a claim that enforcement of the State's cigarette tax on reservation sales to nonmembers is preempted by federal statutes or treaties. In *Colville*, the Supreme Court rejected a claim that the Indian Self-Determination and Education Assistance Act of 1975, cited by the SNI here (*see* Memo at 25), preempted Washington's cigarette tax. *See Colville*, 447 U.S. at 155. Similarly, neither the 1794 Canandaigua treaty nor the 1842 Buffalo Creek treaty (*see* Memo at 3, 8, n.1 (referring to federal treaty rights)) bars New York's enforcement here. *See United States v. Kaid*, 241 Fed. App'x 747, 750-51 (2d Cir. Sept. 12, 2007) (summary order); *Lazore v. Comm'r of Internal Revenue*, 11 F.3d 1180, 1186-87 (3d Cir. 1993); *Bramhall*, 235 A.D.2d at 85; *Snyder*, 193 A.D.2d at 331.

POINT II

THE SNI HAS MADE NO SHOWING OF IRREPARABLE HARM

"To satisfy the irreparable harm requirement, [a plaintiff] must demonstrate that absent a preliminary injunction [it] will suffer an injury that is neither remote nor speculative, but actual and imminent, and one that cannot be remedied if a court waits until the end of trial to resolve the harm." *Grand River Enter. Six*

Nations, Ltd. v. Pryor, 481 F.3d 60, 66 (2d Cir. 2007) (internal quotation marks omitted). Here, the SNI claims that it will suffer irreparable harm in two ways: first, the new tax regime will "infringe[] upon [its] right of self-government" (Memo at 21); and second, "the entire Seneca tobacco economy" will lose business (Memo at 22). Both of these arguments are meritless.

As noted above, the SNI's claim of harm to its sovereignty misreads the statute and relies upon pure speculation. Under the new tax regime, no qualified Indian, reservation cigarette seller, or Indian tribe will be required to pay a cigarette tax at all on cigarettes purchased on their reservation for their own consumption. Instead, non-Indian wholesalers are required to sell cigarettes tax-free to qualified purchasers, and those wholesalers then shoulder the burden of obtaining a refund for any taxes that they have prepaid for those sales. Moreover, the coupon system, far from infringing on tribal sovereignty, in fact respects Indians' right of self-government by leaving to each tribe's governing body the decision of how to allocate a scarce economic resource among its people and businesses. And the prior approval system imposes no obligation or other burdens on Indian tribes at all.

The SNI has also not shown any imminent, non-speculative harm to its tobacco economy or to its licensed reservation businesses. The SNI's only claim here is that the prior approval system would cause severe market distortions (Memo at 21-22). Putting aside the fact that the prior approval system is but one of three mechanisms that an Indian tribe can elect, this assertion of harm rests on the

unsupported speculations of the SNI's economist, as noted earlier. Such speculation is insufficient to support a request for injunctive relief. *See Winter v. Natural Resources Defense Council, Inc.*, 129 S.Ct. 365, 375 (2008) ("Our frequently reiterated standard requires plaintiffs seeking preliminary relief to demonstrate that irreparable injury is *likely* in the absence of an injunction."); *City of Los Angeles v. Lyons*, 461 U.S. 95, 111 (1983) ("The speculative nature of Lyons' claim of future injury requires a finding that this prerequisite of equitable relief has not been fulfilled.").

The SNI's allegation of harm to its tobacco economy is meritless for another reason as well. The SNI forthrightly acknowledges that its tobacco economy is based upon its marketing of tax-free cigarettes (Taylor Decl. ¶ 25). And, indeed, for the past several decades the SNI has promoted an essentially unlimited quantity of tax-free cigarette sales on its territories, well beyond any conceivable demand by its members (Woodward Aff. ¶¶ 19-20). Thus, the SNI's claim of irreparable economic harm is based upon the anticipated curtailment of these unlimited tax-free sales and the concomitant loss of its businesses' major competitive advantage. But the Supreme Court has expressly found that no "principles of federal Indian law, whether stated in terms of pre-emption, tribal self-government, or otherwise, authorize Indian tribes thus to market an exemption from state taxation to persons who would normally do their business elsewhere." *Colville*, 447 U.S. at 155. Thus, the alleged harm to the SNI's tobacco economy is not a cognizable legal injury, and so cannot sustain the SNI's motion for a preliminary injunction.

POINT III

INJUNCTIVE RELIEF HERE WOULD NOT SERVE THE PUBLIC INTEREST

This Court should also deny the SNI's request for injunctive relief because a preliminary injunction or temporary restraining order here would not serve the public interest, but instead would harm it. The amended Tax Law imposes no taxes on the SNI or its members, and it does not interfere with the SNI's self-government or the economic interests of its members or businesses. Accordingly, enjoining the new tax regime would advance no cognizable public interest. Instead, such an injunction would frustrate the Legislature's clear intent to immediately begin collecting a concededly legitimate tax, and it would deprive the State of over a hundred million dollars in legitimate tax revenue, much of which is devoted to important health care programs (Woodard Aff. ¶¶ 23-24). Preventing the State from enforcing a legitimate cigarette tax also harms the State's interest in protecting public health by limiting cigarette consumption. *See Brown & Williamson Tobacco Corp. v. Pataki*, 320 F.3d 200, 217 (2d Cir. 2003); *see also City of N.Y. v. Golden Feather Smoke Shop, Inc.*, No. 08-3966, 2009 WL 2612345, at *23-*25 (E.D.N.Y. Aug. 25, 2009). The SNI does not dispute the State's right to tax on-reservation cigarette sales to non-members. Because its requested injunction would require the State to forgo these tax revenues and abdicate its public-health responsibilities, granting the injunction here would harm the public interest.

CONCLUSION

For the foregoing reasons, the Court should deny the SNI's motion for a preliminary injunction or temporary restraining order.

DATED: August 25, 2010
Albany, NY

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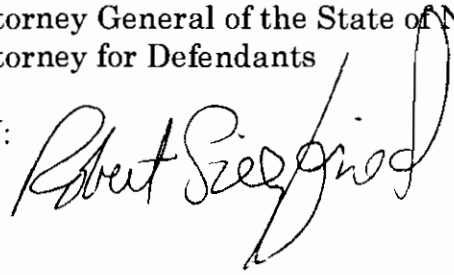
BY: 

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UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF NEW YORK

SENECA NATION OF INDIANS

Plaintiff,

10-CV-687(A)

v.

DAVID PATERSON, Governor of the State of New York, JAMIE WOODWARD, Acting Commissioner, New York State Department of Taxation and Finance, WILLIAM COMISKEY, Deputy Commissioner, Office of Tax Enforcement, New York State Department of Taxation and Finance, JOHN MELVILLE, Acting Superintendent, New York State Police, each in his or her official capacity,

Defendants.

CERTIFICATE OF SERVICE

I hereby certify that on August 25, 2010, I electronically filed the foregoing with the Clerk of the District Court using its CM/ECF system, which will forward the papers electronically to:

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