UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF NEW YORK

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| ST. REGIS MOHAWK TRIBE<br><br>Plaintiff,<br><br>v.<br><br>DAVID A. PATERSON, et. al.<br><br>Defendants. | ) | CIVIL ACTION NO.<br>8:10-CV-1026 (LEK/DRH) |

**MEMORANDUM IN SUPPORT OF PLAINTIFF'S APPLICATION FOR ORDER TO SHOW CAUSE WITH A TEMPORARY RESTRAINING ORDER**

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**MEMORANDUM IN SUPPORT OF PLAINTIFF'S APPLICATION FOR ORDER TO SHOW CAUSE WITH A TEMPORARY RESTRAINING ORDER**

The St. Regis Mohawk Tribe ("Tribe") submits this memorandum in support of its application for an order to show cause with a temporary restraining order which would prohibit the Defendants from enforcing the recent amendments to N.Y. Tax Law §§ 471 and 471-e, as well as the related regulations adopted by the Tax Department on June 22, 2010, regarding the distribution and sale of cigarettes to Indian reservations in New York. The new tax law and regulations are intended to address the collection of state taxes from non-Indians who purchase cigarettes from "qualified reservation retailers." The full implementation of this law will cause continuing and irreparable harm to the Tribe and its members 1) by infringing on the Tribe's sovereignty; 2) by imposing on tribal retailers, including the Tribe, a chaotic system for the distribution of tax exempt cigarette products with few safeguards for preventing abuse; and 3) by imposing an unprecedented economic burden on the Tribe and its members by directly interfering with the Tribe's and its retailers commercial dealings. The significant infringement of the Tribe's sovereignty and interference with tribal

government is alone enough to substantiate the irreparable harm that will come to pass if this law is enforced during the course of this litigation.

The law is entirely suspect and the Tribe has a substantial likelihood of success in establishing that this law violates both federal and state law. First, the State law and regulations which set out a coupon system, in effect, commandeer the Tribe to enforce State law in violation of tribal sovereignty and in violation of the State's own constitution.

There can be no doubt that requiring prior approval for the sale of cigarettes to tribal retailers by wholesalers will result in a chaotic distribution process with little oversight or control by the State. The State's prior approval plan interferes with commerce between the Tribe, tribal retailers, and State wholesalers by encouraging and even forcing the parties to engage in what amounts to legal hoarding. Such an impact on trade with sovereign nations is unprecedented.

The Law also discriminates against tribes, by allowing other governmental entities access to tax exempt cigarette products without imposing a similar draconian process for purchasing such products. The State could have no rational basis for making this distinction.

## FACTS

### A. Cigarette Sales and Regulatory Structure on the St. Regis Mohawk Tribe's Reservation.

The territory of the St. Regis Mohawk Tribe is located in northern New York, along the St. Lawrence River and the Canadian border. The Tribe's current reservation constitutes 14,000 acres spanning Franklin and St. Lawrence Counties. The Tribe and its members have a long history of entrepreneurship and there are 141 registered businesses, of which 30 are cigarettes retailers that employee 417 local residents. Declaration of Elliott Lazore, ¶ 3.

The Tribe has adopted a comprehensive regulatory system, which is intended to control cigarette prices while generating income to pay for essential government services. Exh. A and Exh. B to the Declaration of E. Lazore. It does so by licensing tobacco retailers and imposing a stamping requirement on all tobacco products sold by reservation retailers. All tobacco retailers must pay a Tribal Tobacco Fee to obtain a stamp, which is assessed at varying levels on all tobacco products. Exh. B to Decl. of Lazore. The Tribe has also enacted legislation that requires a certain markup over invoiced cost per carton of tobacco product. *Id.* The failure to abide by this minimum pricing regime can result in fines or suspensions of the offenders license to do business on the reservation. Exh. A to Decl. of Lazore, Section 4(l). Finally, the Tribe's regulations strictly prohibit both internet sales and tobacco sales to minors. Exh. A to Decl. of Lazore, Section 7.

The Tribe's Compliance Department is responsible for enforcement. Declaration of E. Lazore, ¶2. The Department is tasked with collecting the Tribal fees assessed on all tobacco products in the territory and it may levy fines and penalties for violations of tribal law. The Department has four employees. *Id.*

Significantly, while the Compliance Department ensures all Tribally licensed businesses strictly adhere to tribal laws, the Tribe does not regulate the transactions between the reservation retailers and wholesalers and the Tribe has no current structure to govern what may occur when a retailer orders cigarettes from a wholesaler. The relationship between the retailers and the wholesalers is strictly market based and the retailers are in control of the kinds of products that are brought to the reservation for retail sale. Nor does the Tribe regulate or otherwise take a governmental interest in the transaction between the retailer and the consumer. The Tribe's only interest is in making sure that once the cigarettes

arrive at the reservation they are properly stamped and that they are sold to all consumers at a minimum price. Under the regime, the Tribe has not heard any complaints or issues with regard to the ability of a tribal retailer to obtain sufficient tobacco products for retail sale or any complaints with regard to the ability of tribal members to obtain state tax-exempt cigarettes.

In 2008, the Tribe collected $2 million in fees. The fees the Tribe collects from sales of tobacco products in the territory go directly toward the operating budget of the Tribe and are used to support the many governmental programs and services the Tribe provides, including law enforcement, compliance, sanitation, the fire department, education, health services and environmental services. Declaration of M. Mitchell, ¶ 6.

In particular, the St. Regis Mohawk Tribal Police Department receives support from the money generated by these tobacco fees. The Tribal police department provides an invaluable service to both the Tribe and non-Natives as well. First, the Tribe's police department has been certified to act as state police in and near the Tribe's territory. See New York Indian Law, §114. In addition, the police department is an active and integral part of the International Border Enforcement Team (IBET), and the Franklin County Drug Task Force. Declaration of M. Mitchell, ¶ 7. The Tribe's Native officers are in the best position to aid in securing the United States-Canada border in our area because they have the most knowledge of our territory and the people who live here. Declaration of Michelle Mitchell, ¶ 6-7.

In addition to providing police services, the Tribe provides numerous essential government services such as health care, housing and education. Declaration of M. Mitchell, ¶ 8. Many of these 180 programs to require the Tribe to provide matching funds in order to

receive an allocation of required federal funding which would allow the Tribe to operate its programs effectively. The fees collected on tobacco sales provide matching funds for these essential government services and programs. *Id.*

**B. New York State Tax Law and Tax Exempt Products for Governmental Entities.**

New York imposes a tax on all cigarette products sold within the state with certain exceptions including sales to Indian tribes and other governmental entities. N.Y. Tax Law § 471 provides that:

> There is hereby imposed and shall be paid on all cigarettes possessed in the State by any person for sale, except that no tax shall be imposed in cigarettes sold under such circumstances that this state is without the power to impose such tax, including sales to qualified Indians for their own use and consumption on their nations' or tribes' qualified reservation, or sold to the United States or sold to or by a voluntary unincorporated organization of the armed forces of the United States operating a place for the sale of goods pursuant to regulations promulgated by the appropriate executive agency of the United States, to the extend provided in such regulations and policy statements of such an agency applicable to such sales.

The state regulations at N.Y. Comp. Codes. R. & Regs. tit. 20, § 76.2(d)(1) further define the right of the United States and related voluntary organizations to tax exempt products as follows:

> United States governmental entities and New York State governmental entities (as defined herein) may purchase cigarettes upon which the seller has not prepaid and precollected the cigarette tax by issuing to the seller of such cigarettes a signed government purchase order, a signed government purchase contract or an appropriate exemption document. For purposes of this subdivision, an appropriate exemption document must be made by the governmental entity claiming an exemption from tax, on its letterhead or on a printed form issued by it, identifying itself as an exempt United States governmental entity or as an exempt New York State governmental entity. An appropriate exemption document must also contain a statement to the effect that the cigarettes being purchased will be used or consumed exclusively by the subject governmental entity or, in the case of a United States entity, that such cigarettes will be resold to authorized purchasers.

> Such document must be signed and dated by a duly authorized representative of the governmental entity seeking an exemption from the cigarette tax.

For the tax exemption to apply to governments other than tribes, the cigarettes need to be "sold, used or consumed by such entities exclusively in the exercise of governmental functions or are used or consumed by authorized purchasers within the confines of a military reservation, facility or other Federal area." 20 N.Y.C.R.R. § 76.2 (a)(1). "Authorized purchasers" are defined as "any person authorized by the United States to make purchases from commissaries, ship's stores or voluntary unincorporated organizations of the armed forces of the United States." 20 N.Y.C.R.R. § 76.2(a)(2)(iii).

Thus, under state law, generally military personnel and any other persons authorized to purchase from military stores or voluntary organizations are tax exempt and the United States or its related governmental entities, may obtain as many tax free cigarettes as they like with only a simply statement that the cigarettes will be consumed by authorized persons. Such consumption must occur "within the confines of a military reservation, facility or other Federal area."

**C. History of New York State Tax Collection on Indian Reservations**

Tribe are treated differently under state law in their ability to exercise their right to a tax exemption. For many years, New York did not seek to impose its excise tax on cigarettes sold on Indian reservations and the tax exemption that inures to tribal members has been recognized in state law, § 471.

However, in 1988 the Department promulgated a regulatory scheme intended to ensure collection of State's cigarettes taxes from non-Indians who purchase their cigarette products from on-reservation sellers. The law was immediately challenged in *Dep't of Tax'n*

*& Fin. v. Milhelm Attea & Bros.*, 512 U.S. 61 (1994) ("*Attea*"). Although the United States Supreme Court upheld the regulations as to a particular facial challenge, after *Attea* was decided, the State did not implement the regulations but instead withdrew them. The Governor instituted what became known as the policy of "forbearance," in which the Governor concluded that the societal costs of implementing and enforcing the tax coupon system outweighed the need to collect the taxes. As explained in *New York Ass'n of Convenience Stores v. Urbach*,

> The record ... makes plain that the statutes cannot effectively be enforced without the cooperation of the Indian tribes. Because of tribal immunity, the retailers cannot be sued for their failure to collect the taxes in question, and State auditors cannot go on the reservations to examine the retailers' records.
>
> Additionally, the Department cannot compel the retailers to attend audits off the reservations or compel production of their books and records for the purpose of assessing taxes. In that regard, representatives of the Department engaged in extensive negotiations with the tribes in an effort to arrive at an acceptable agreement. Those efforts were largely unsuccessful and the vast majority of the Indian retailers refused to register with the Department. In further efforts to enforce the statute, the State attempted interdiction, i.e., interception of tobacco and motor fuel shipments and seizure of those shipments that were found to be in noncompliance with the Tax Law. That strategy resulted in civil unrest, personal injuries and significant interference with public transportation on the State highways. In our view, all of these factors provide a rational basis for the differential treatment of the parties.

*See New York Ass'n of Convenience Stores v. Urbach*, 181 Misc. 2d 589, 593, 694 N.Y.S.2d 885, 889 (N.Y. Sup. Ct. Albany Co. 1999), *aff'd*, 275 A.D.2d 520, 712 N.Y.S.2d 220 (3d Dep't 2000), *appeal dismissed*, 95 N.Y.2d 931, 744 N.E.2d 142, 721 N.Y.S.2d 606 (2000). It was on this ground that the Court decided the State had a rationale basis to treat tribal retailers differently than non-Indian retailers.

Despite the forbearance policy and the Governor's wise conclusion that enforcement of a tax law against reservation retailers was not feasible, the legislature acted several times in an attempt to create a tax collection system that it thought would be enforceable. In 2005, the State adopted as law a set of draft Tax Department regulations setting up a coupon system. However, that law did not go into effect until the Department to adopted regulations and took further action to implement it. The Department continued its policy of forbearance and did not implement the necessary regulations. The State courts agreed that the statute was not in effect until the Department acted and they upheld the right of reservation retailers to sell unstamped cigarettes, in the absence of an enforceable regulatory and statutory scheme addressing the calculation and collection of taxes arising from on-reservation sales of cigarettes. *See Day Wholesale v. New York*, 856 N.Y.S.2d 808 (4th Dept. 2008); *Cayuga Indian Nation of New York v. Gould*, 14 N.Y.3d 614, 629 (N.Y. Ct. App. 2010).

**D. Adoption of 2010 Tax Amendments**

On June 21, 2010, the New York Legislature enacted amendments to N.Y. Tax Law §§ 471 and 471-e, regarding the distribution and sale of cigarettes to Indian reservations in New York. The amendments are intended to address the collection of state taxes from non-Indians who purchase cigarettes from "qualified reservation retailers," while at the same time providing enough tax exempt product to meet the tribal member demand, as is required by federal law.

The statute does so by requiring that a state tax stamp be placed on all cigarettes that are to be sold to qualified reservation retailers, even if those cigarettes will be sold to tribal members who are exempt from paying the tax. The law attempts to guarantee access to tax-exempt cigarettes to tribal members by creating two tax exemption systems—the Indian tax

exemption coupon system or the prior approval system. Both systems are based on a probable demand calculation made by the Department. Under either system, the Department determines a quota of the quantity of tax-exempt cigarettes that may be sold to a tribe or retailers in each tribe's territory based on its determination of the probable demand of tribal members for such tax-exempt products. The probable demand calculation sets a specific number of packs that may be transferred to the territory of a tribe generally without the collection of the tax by a wholesaler from that tribe or retailer who purchased the product.

On June 22, 2010, the Department adopted Emergency Regulations to carry out the new tax scheme. 20 N.Y.C.R.R. § 74.6. On July 29, 2010, the Department also issued a guidance document to explain further how the system is intended to work. TSB-M-10(6)M, Cigarette Tax, TSB-M-10(8)S, Sales Tax ("Guidance"). Affidavit Marsha Schmidt, Exh. 6.

Under the state law and Emergency Regulations, the Tribe may obtain tax-exempt cigarettes in one of two ways the Indian tax exemption coupon system or the prior approval system.

1. Coupon System.

The Tribe may opt into the Indian tax exemption coupon system, set forth in § 471-e. Under this system, the Tribe would receive from the Department coupons equal to the number of tax-exempt cigarettes permitted to be transferred to the reservation under the probable demand quota system. The quota is to be distributed on a quarterly basis.

Once the Tribe obtains the coupons, it would be up to the tribal government to determine how to allocate the coupons among its various retailers. The Guidance, at page 4, states: "The Tax Department will not distribute Indian tax exemption coupons directly to reservation cigarette sellers."

As noted above, the Tribe currently has in force tribal laws that regulate the distribution and sale of cigarettes on the reservation. Exh. A & B to Decl. of Lazore. Tribal law requires that wholesalers and retailers of cigarettes be licensed, and that tribal stamps be affixed to cigarettes. *Id.* Tribal law prohibits the sale of cigarettes by unlicensed retailers, or the sale of products to which the tribal stamp is not affixed. *Id.* Although tribal law regulates retailers and wholesalers on the reservation, those regulations do not contemplate the implementation and administration of the State's coupon system, or in any way allocate the distribution of cigarettes. To implement the coupon system the Tribe would have no choice but to set up a comprehensive regulatory scheme to address the distribution of the coupons as follows (*See* Decl. of Lazore at ¶4):

a. The Tribe would first have to enact internal laws establishing institutions and procedures for administering and enforcing the State's coupon scheme, including development of regulations and procedures for determining the number of coupons to which a tribal retailer may be entitled from the allocation of coupons made by the State to the Tribe. Thus, the Tribe will have to request some evidence from the tribal retailer of the sales made by that retailer. This would require the collection and audit of sales data. Decl. of Lazore at ¶4.

b. If a retailer did not provide the required information, the Tribe would have to enforce the coupon system by withholding the coupons from the retailer for failure to provide the information. If a retailer provided the information, the Tribe would have to examine that evidence and make a determination as to allocation. The retailer may disagree with that assessment and then the Tribe would need to answer complaints from the retailer. Similarly, one retailer could object that another retailer received too many coupons and also file a

complaint with the Tribe. Thus, at minimum, the Tribe would have to implement regulations regarding disputes by retailers as to the amount of coupons allotted to it or to another retailer. *Id.*

c. The Tribe would also need to implement a system for monitoring the coupons including the development of record standards, and audits and investigations. The Tribe would have to enact internal tribal laws regarding appeals, records, and audits, among others. The Tribe would even be required to create an administrative body to implement the system. The Tribe does not currently have any such system or laws in place. *Id.*

d. If the Tribe finds that it does not have enough coupons, the burden would be on the Tribe to obtain evidence from its retailers regarding sales. Assuming that it could obtain this information (which is not at all certain), and the State disagreed with the evidence, the Tribe's only alternative would be to pursue legal remedies with the State on behalf of its tribal members. *Id.* N.Y. Tax Law § 471-e requires the Department to consider evidence submitted by the Tribe in calculating probable demand, but leaves the calculation to the Department. N.Y. Tax Law § 471-e(2)(b)(ii).

e. The Tribe would also be responsible for safeguarding the coupons. If the coupons disappeared, were counterfeited, or were otherwise misused, the burden would be upon the Tribe's law enforcement to investigate the matter. This could prove to be a very heavy burden for the Tribe's police force that already deals with border patrols and other tribal law enforcement problems. The Tribe may have to hire more officers to take care of the enforcement burden. *Id.*

Once the coupons are distributed, a reservation retailer may obtain stamped but tax-exempt cigarettes from a state-licensed wholesaler without payment of the tax by providing

an Indian tax exemption coupon. N.Y. Tax Law § 471-e, subdiv. 3(c). Because the tax has been prepaid, as required by state law and as evidenced by the tax stamp, the stamping agent or wholesaler must request a refund by submitting the coupons to the Department along with a refund claim form. *Id.* at § 471-e, subdiv. 4. The retailer would be left with the task of segregating or at least keeping track of how many purchased cigarettes are tax exempt from those that are not. Since all packs would be stamped, there will have to be some kind of internal method of counting tax exempt packs sold. This could mean the creation of a separate record keeping and inventory system.

2. Tribal Law and the Coupon System Adoption Process.

Because of the importance of the issue, under tribal law and custom, the Tribe would have to hold a referendum to determine if its members are willing to have the Tribe adopt the coupon system and the burdens it entails. Decl. of Mitchell at ¶ 4. Such a referendum would take at least three months. Under tribal law, the Tribal Council is required to provide 30 day advance notice of the referendum. *Id.* A minimum of three community meetings would have to be held. The vote would have to be held within 90 days of the Tribal Council's decision to have the referendum. *Id.*

On June 22, 2010, the Defendants announced that the deadline for a Tribe to accept the coupon system for the 2011 fiscal year was August 15, 2010. This timeline gave the Tribe no time to hold such a referendum nor was it given to determine the consequences if the coupons system was voted favorably or unfavorably. Because the Tribe had no time to exercise its sovereign right to self government, nor was it given the time to make a reasoned choice about its options in consultation with its membership, it was forced into the default prior approval system. Declaration of M. Mitchell at ¶ 5.

3. Prior Approval System.

Under the 2010 Amended Tax Law, if the Tribe does not opt into the coupon system, the prior approval system would apply. N.Y. Tax Law § 471(5). Under the prior approval system, the quota of tax-free cigarettes available for sales to Indians within the tribe's territory is also based on the Department's probable demand calculation. *Id.* However, in order for the system to work the Tribe or a reservation retailer must place an order for tax-exempt cigarettes with a wholesaler. The state-licensed stamping agent or a wholesaler must then obtain from the Department prior approval for the sale. N.Y. Tax Law § 471, subdiv. 5(b). As in the Indian coupon system, all tobacco products must bear a state tax stamp, notwithstanding that they are to be sold to tribal member purchasers, and the stamping agent or wholesaler must apply to the Department for a refund of the taxes that is prepaid when cigarettes are pre-approved for sale to the tribal retailer. *Id.* The approval for the sale is based on whether the Tribe's quota has yet to be completely distributed.

Like the Amended Tax Law, the Departmental Regulations did not set out the details of how the prior approval system would work except to state that the system "may include the use of an interactive Web application." Emergency Regulations, § 74.6(d)(3). Instead on July 29, 2010, the Department issued, TSB-M-10(6)M ("Guidance"), which describes itself as "informational." Exh. 6 to Schmidt Affidavit. The Guidance describes an internet-based interface that is also self-policing. According to the Guidance, when a wholesaler logs on to the web interface to request prior approval, that agent will enter the amount of cigarettes requested by a specific tribe or tribal retailer. The interface would then check to determine if there is room left in the quota for the sale. If the quota has not yet been reached, the wholesaler will be issued a confirmation number approving the sale. The website then

automatically deducts that amount from the Tribe's quota. Exh. 6 to Schmidt Affidavit, p. 5. The wholesaler then has 48 hours to complete the transaction. To do so, the wholesaler would report the name and address of the purchaser, the quantity sold, and an invoice number. Upon reporting the sale, the system generates a confirmation number to be used by the wholesaler in requesting a refund of the prepaid taxes.

In creating this system, the Defendants failed to include any measures that would ensure that neither a single wholesaler nor retailer could order the entire quota, therefore the system fails to take into account the potential for manipulation of the system to the detriment of the Tribe, its retailers and its member who are entitled to tax exempt products. With multiple wholesalers and retailers on the reservation, one wholesaler and/or one retailer could request the entire quota, thus freezing out all others who may wish to engage in the cigarette trade. The system encourages a race to the website where one wholesaler or retailer could claim the entire quota without repercussions. Nor does the system have any way to verify that the cigarettes are not being sold to a retailer who intends to transfer or sell the cigarettes on another reservation with a lower quota. The system is inadequate because it is simply a web-based mechanism for counting down the number of cigarettes sold under the quota until there are no more tax-exempt products left under the quota to be purchased. The result can be chaotic and even deceptive to those who might wish to participate.

This mechanism also fails to take into account that there is a potential for multiple and simultaneous transactions. The system assumes that one wholesaler will log in at a time. There is no detailed system for addressing the possibility that there will be many retailers seeking to purchase products from multiple agents under a single quota. It is unclear, for instance, what would happen if two different retailers place two different orders on the same

day from two different wholesalers. Until either wholesaler reports the transaction, neither will be aware of the other and neither will know if the quota will be reached. If the quota threshold has been reached, which retailer would get the products? If the wholesaler agrees to a sale and then later learns that the quota was reached by another reported purchase, would that wholesaler have breached the sale contract if he cannot deliver? What would be the penalty for the wholesaler who reported his sale second, and went over the quota even though there was no intent to do so because at the time of the sale, the quota had not been met?

Given the nature of the prior approval system and its tendency to chaos, the only way for the Tribe to ensure a fair allocation system on the reservation would be to adopt the coupon system, which would then force the Tribe to do what the State will not—manage the allocation system.

## ARGUMENT

### A. The Standard for Preliminary Injunction in the Second Circuit.

When seeking a preliminary injunction a movant must demonstrate 1) irreparable harm absent injunctive relief; 2) either a likelihood of success on the merits, or a serious question going to the merits to make them a fair ground for trial, with a balance of hardships tipping decidedly in the plaintiff's favor; and 3) that the public's interest weighs in favor of granting an injunction. *Metropolitan Taxicab Board of Trade v. City Of New York*, ___F.3d___, 2010 WL 2902501, *2 (2d Cir. 2010), *quoting Winter v. Natural Res. Def. Council, Inc.*, 129 S.Ct. 365, 374 (2008). If a moving party seeks a preliminary injunction that will affect government action taken in the public interest pursuant to a statutory or regulatory scheme, the injunction should be granted only if the moving party meets the more rigorous likelihood-of-success standard. *County of Nassau v. Leavitt*, 524 F.3d 408, 414 (2d

Cir. 2008). Only when the injunction would "alter rather than maintain the status quo," must the movant show "clear" or "substantial" likelihood of success. *Rodriguez v. Debuono,* 175 F.3d 227, 233 (2d Cir. 1999). Because the Tribe seeks the injunction to maintain rather than alter the status quo, the heightened "clear" or "substantial" likelihood of success on the merits does not apply. *See Malletier v. Dooney & Bourke, Inc.,* 454 F.3d 108, 114 (2d Cir. 2006) ("A prohibitory injunction is one that forbids or restrains an act… . A mandatory injunction, in contrast, orders an affirmative act or mandates a specified course of conduct.") (internal quotations omitted). This same standard applies to a request for a temporary restraining order. *Branham v. Daines,* 2010 WL 455413 at *2 (N.D.N.Y. 2010)

Irreparable harm is "the single most important prerequisite for the issuance of a preliminary injunction." *Rodriguez*, 175 F.3d at 233-34 (2d Cir. 1999) (citations omitted). The movant must demonstrate that the injury is "neither remote nor speculative, but actual and imminent, and that [it] cannot be remedied by an award of monetary damages." *Shapiro v. Cadman Towers, Inc.,* 51 F.3d 328, 332 (2d Cir. 1995). Adequate redress for the injury must not be attainable by a trial on the merits. *Kamerling v. Massanari,* 295 F.3d 206, 214 (2d Cir. 2002). Moreover, the harm must be so imminent as to be irreparable if a court waits until the end of trial to resolve the harm. "Only when the threatened harm would impair the court's ability to grant an effective remedy is there really a need for preliminary relief. Therefore, if a trial on the merits can be conducted before the injury would occur there is no need for interlocutory relief." *See* 11A Wright, Miller & Kane, Federal Practice and Procedure, §2948.1 at 144-49 (2d ed. 1995) (footnote omitted). Where a movant is found to be able to wait for the outcome of an appeal before obtaining preliminary injunctive relief, the irreparable harm he or she faces may not ordinarily be deemed "imminent" as required to

sustain a preliminary injunction. *Rodriguez,* 175 F.3d at 235.

Finally, "[w]henever a request for a preliminary injunction implicates public interests, a court should give some consideration to the balance of such interests in deciding whether a plaintiff's threatened irreparable injury and probability of success on the merits warrants injunctive relief." *Time Warner Cable of New York City v. Bloomberg L.P.*, 118 F.3d 917, 929 (2d Cir. 1997); *See Carey v. Klutznick*, 637 F.2d 834, 839 (2d Cir. 1980) (public interest does not always lie with the public agency as "the public interest also requires obedience to the requirements of the Constitution")

**B. The Tribe Will Suffer Irreparable Harm in the Infringement on Its Sovereignty and Federal Rights to Access to Tax Exempt Products.**

If the test for irreparable injury and imminent harm is to ask whether the plaintiff will be injured before a trial occurs or if the court can resolve the harm at the end of the case, then there is no doubt that the Tribe will suffer irreparable harm unless this court issues an injunction.

As it stands, between the time the Tribe filed this lawsuit and this motion, both a state court and federal district court had issued rulings, staying or enjoining the State from taking action to enforce the law. The State order prevented the State from implementing the law in its entirety and the Tribe was thereby protected from its implementation. The State order has now been lifted and the Tribe and its retailers are open to immediate enforcement of the prior approval system. Schmidt Affidavit ¶3-6.

With that order lifted, the law will be implemented and there is no turning back. The Tribe's sovereignty will be directly and immediately impacted and the Court would never be able to undo the infringement to tribal sovereignty. Without an injunction, the Tribe has two choices. First it would have to live with the prior approval system while this case goes

forward, with all its attendant problems, which, if the case lasts for a year or two, could result in wholesale destruction of the Tribe's retail businesses. The other option is that, during the course of the case, the Tribe can have a referendum to decide if it wishes to adopt the coupon system. If the Tribe did make that decision, concluding it is the lesser of two evils, the Tribe would have to gear up its own legislation and hiring to engage in a full scale regulatory enforcement scheme to carry out state law. So onerous is the coupon system that even the State declined to enforce it. See *Urbach* quotation above at p.7.

Federal courts have consistently held that a tribe need not wait until a tax enforcement regime actually impairs its sovereignty to obtain preventive relief. *See, e.g., Crow Tribe v. Montana*, 819 F.2d 895, 903 (9th Cir. 1987) ("The Tribe need not wait for mining to commence to challenge the taxes' application to coal mined within the Reservation boundaries"); *See Babbitt v. United Farm Workers Nat'l Union,* 442 U.S. 289, 298 (1979) (threatened injury need not have commenced in order to obtain preventive relief); *see also State of Arizona v. Atchison, Topeka, & Santa Fe R.R. Co.,* 656 F.2d 398, 402-03 (9th Cir. 1981) (declaratory judgment as to validity of tax may be entered even if the action began before tax law became effective).

Moreover, the infringement of tribal sovereignty constitutes irreparable injury that cannot be remedied by monetary damages and certainly cannot be resolved at the end of the case. In *Prairie Band of Potawatomi Indians v. Pierce,* 253 F.3d 1234, 1251 (10th Cir. 2001), the court issued a preliminary injunction where the state was attempting to enforce its motor vehicle registration laws where the tribe has already adopted its own code to address issues of tribal control over reservation access. The Court found that harm to tribal self-government is not "easily subject to valuation" and constitutes irreparable injury because "it

[can] not be adequately compensated for in the form of monetary damages." In *Kiowa Indian Tribe of Oklahoma v. Hoover*, 150 F.3d 1163, 1171-72 (10th Cir. 1998) the Court found irreparable harm where defendant corporation sought to seize tribe's assets and prohibit enforcement of tribe's laws. In *Winnebago Tribe of Nebraska v. Stovall,* 216 F. Supp. 2d 1226, 1233 (D. Kan. 2002), the court issued a preliminary injunction to prevent enforcement of motor fuel tax. The tribes argued not only economic harm by loss of revenue but also that the lost revenue would immediately impact essential governmental services. The tribes also established that the State actions amounted to an interference with their sovereign right to trade. *Stovall*, 216 F.Supp.2d at 1232. The Court found irreparable injury because the issues presented in the case concerned "the scope of tribal sovereignty, an issue that cannot be measured in dollars." *Id.* at 1233. *See also United States v. State of Michigan,* 534 F. Supp. 668 (W.D. Mich. 1982) (denial of tribe's contested treaty fishing rights meets irreparable harm standard).

The 2010 Amended Tax Law interferes with the sovereignty of the Tribe in a more intrusive manner than even that considered by the Tenth Circuit in *Pierce* and *Hoover*. Here, New York officials not only seek to enforce State laws in a manner that interferes with the Tribe's administration of its own Tobacco Ordinance and regulations within the Tribe's territory, but by implementing the coupon scheme the State statute also commandeers the Tribe's deliberative and governing bodies for the development of wholly new ordinances, regulations and procedures as well as establishing institutions and personnel to make them operational, all to implement the laws of the State of New York within the Tribe's territory and with respect to tribal members. Given the disputes likely to arise regarding such issues as the number of coupons distributed to tribal retailers, verification of coupon authenticity,

and other potential issues, implementation of the coupon scheme will create major impacts on the Tribe and its internal relations with tribal members and tribal retailers and it will require significant actions by the Tribe to enact internal tribal law and governance procedures to carry out the State's tax coupon scheme. Such unprecedented intrusion unquestionably "infringes unlawfully 'on the right of reservation Indians to make their own laws and be ruled by them.'" *White Mountain Apache v. Bracker*, 448 U.S. 136, 142 (1980) (quoting *Williams v. Lee*, 358 U.S. 217, 220 (1959).

As outlined above, the prior approval system is equally flawed since it will impose uncertainty and interferes with normal tribal commerce on the reservation by preventing legitimate purchases by tribal members. It does so by allowing the cigarettes to be hoarded by one retailer, and by potentially preventing all other tribal retailers equal access to products. This in turn could result in the closure of tribal businesses that have inadequate inventories. Unlike prior cigarette cases that looked to minimal burdens, e.g., *Attea*, this aspect of the statute burdens not just the Tribe but economic relations between tribal retailers and wholesalers in a way that will most certainly destroy businesses, not because the retailers have to collect the State taxes from non-Indians, but because the system can be easily rigged to allow a monopoly on the possession of tax exempt products that can be legitimately sold.

The imposition of the quota will also severely impact the revenues generated by the Tribe for governmental programs through the "minimum pricing" requirements under its Tobacco Ordinance. The Tribe requires and expects a specific amount of cigarettes to be sold by reservation retailers each year to reach its needed revenue. There can be no doubt that the limitation on the amount of tax exempt cigarettes to the reservation will be significantly reduced. For example, in 2009, the Tribe imposed its fees and minimum pricing

requirement on 724,930 cartons. Lazore Declaration, ¶ 3. The quota imposed by the State reduces that amount to 116,640 cartons, which is just 16% of the amount of tax exempt products currently available to reservation retailers.[1] See Declaration of Elliott Lazore at ¶ 3 and Exh. 6 to Schmidt Affidavit, p.2 setting out quota. The revenue generated by the Tribe to support essential tribal services and the loss of that revenue will cause significant harm to the Tribe and its members who depend on those services. Damages cannot compensate those who are harmed by the loss of services over the course of this case. These interferences with tribal self-government clearly constitute irreparable injury. *See Hoover,* 150 F.3d at 1171-72 (interference with the availability of tribal assets and the enforcement of tribal laws significantly interferes with tribal self-government); *see also Seneca-Cayuga Tribe v. Oklahoma,* 874 F.2d 709, 716 (10th Cir.1989) (finding irreparable injury where threatened loss of revenues and jobs created "prospect of significant interference with [tribal] self-government").

The Tribe then has been left with one of two bad choices, adopt the coupon system and its inherent governmental burdens, that should legitimately be carried by the State, or be subject to a prior approval system that can only result in excessive interference with normal commerce on the reservation to the detriment of the Tribe and its members. This immediacy of the threatened impairment of tribal sovereignty is sufficient to constitute "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." *Freedom Holdings v. Spitzer,* 408 F.3d 112, 114 (2d Cir. 2005) (internal quotations omitted). For the reasons stated above, the Tribe

[1] While products that are not tax exempt would be available to the retailers, given the likely unequal distribution of tax exempt cigarettes among tribal retailers, and the potential for tribal retailers to close their businesses because of the uncertainty of the availability of such products, the Tribe expects that many businesses will be shuttered, leaving a permanent reduction of revenue in its wake.

has carried its burden of meeting the showing of irreparable harm

### C. The Tribe Has a Likelihood of Success in Establishing that the State Law Violates Both Federal Protection of Tribal Sovereignty and the State Constitution's Prohibition on Delegation of Legislative Power.

The Tribe seeks to enjoin state governmental authorities from taking action to enforce an unconstitutional statute and regulatory system. Because Tribe seeks to restrain governmental action that violates the U.S. Constitution and federal law, and the State Constitution, the Tribe readily meets the "likelihood of success on the merits" standard.

#### 1. The Coupon System Violates Tribal Sovereignty.

The United States has recognized by treaty and federal law that Indian tribes are sovereign. The Indian Commerce Clause of the U.S. Constitution reserves to the federal government exclusive power over Indian tribes. U.S. Constitution, Art. I, § 8, Cl. 3. Under the Indian Commerce Clause, and the rule of federal law recognized as long ago as *Cherokee v. Georgia*, 30U.S. 1(1831), Indian tribes enjoy a protected right to self-government that may not be infringed upon by States. *Williams*, 358 U.S. at 219 (1959) ("the question has always been whether state action infringed upon the right of reservation Indians to make their own laws and be ruled by them"); *see also McClanahan v. State Tax Comm'n of Ariz.*, 411 U.S. 164, 173 (1973); *White Mountain Apache Tribe*, 448 U.S. at 142 (1982).

This principle underlies the general presumption that state law is inapplicable to on-reservation conduct involving only tribal members. *Nevada v. Hicks*, 533 U.S. 353, 362 (2001). The inapplicability of state law includes freedom from the imposition of taxes. The United States Supreme Court has ruled that "[e]nrolled tribal members who purchase cigarettes on Indian reservations are exempt" from state sales and excise taxes. *Attea,* 512 U.S. at 64 (1994). A Court's evaluation of "[w]hether the state taxes infringe on tribal

sovereignty depends on whether tribal self-government is affected." *Crow Tribe,* 819 F.2d at 902. The Supreme Court has held that a state may impose taxes on non-Indians on-reservation and that tribes and tribal retailers may be required to collect and remit such tax. In deference to tribal sovereignty however, the Court has permitted only minimal recordkeeping and tax remittance burdens on tribes and tribal retailers provided they are narrowly-tailored to prevent evasion of validly imposed state taxes on non-Indians. *Moe v. Confederated Salish and Kootenai Tribes of Flathead Reservation*, 425 U.S. 463, 483 (1976) (minimal burden to require an Indian tribal seller to collect a tax on a non-Indian); *Washington v. Confederated Tribes of the Colville Indian Reservation*, 447 U.S. 134, 159 (1980), (requiring tribal seller to keep detailed records of transactions was a minimal burden); *Attea*, 512 U.S. at 74 (1994) ("States may impose on reservation retailers minimal burdens reasonably tailored to the collection of valid taxes from non-Indians").

The 2010 Amended Tax Law does meet the minimal burden test. The State has established a tax-exempt coupon scheme that imposes excessive burdens and impermissibly interferes with the Tribe's sovereign authority such that the Tribe's self-government is significantly affected. In order for the coupon scheme to be implemented so as to make tax-exempt cigarettes available to the Tribe and its members, the Tribe would be commandeered by the State to enact internal laws establishing institutions and procedures for administering and enforcing the State's coupon scheme, including development of regulations and procedures for determining the number of coupons to which a tribal retailer may be entitled.

Not only will the Tax Law create major impacts on the Tribe and its internal relations with tribal members and tribal retailers, the entire financial burden for carrying out the State's coupon scheme falls on the Tribe. The Tribe has only four employees that work for its

compliance department. Decl. of Lazore at ¶ 2. That number would have to increase to at least twice its number. Because the Tribe is given the coupons to distribute, the Tax Law also burdens the Tribe with responsibility for safeguarding the coupons from disappearance, counterfeit, and other abuse. Investigation and enforcement of State tax coupon abuses will add heavy burdens to the Tribe's police force, which is at maximum capacity with border patrols and other tribal law enforcement problems. The Tribe will be forced to hire more officers to take care of the added enforcement burden.[2]

By analogy, this Court may consider the U.S. Supreme Court's view of instances where the Federal Government attempts to commandeer the State governments to carry out federal law. In *Printz v. United States,* 521 U.S. 898 (1997), the Court struck down the Brady Act as unconstitutional on the ground that it violated state sovereignty when it went so far as to require a state to use its own law enforcement personnel to enforce federal law.

Under the Brady Act, background checks were to be performed on gun buyers. The law required local law enforcement to perform the background checks until the federal government could get its system up and running. Under the law, the local law enforcement officer was required to determine if it would be a violation of the Act for a potential purchaser to possess a gun. While the Act did not require the law enforcement officer to take any particular action if he found a violation, if the enforcement officer relayed information to the gun dealer, he was required to put his reasons for that determination in writing to the purchaser and then destroy records in his possession regarding the purchase. *Printz,* 521 U.S. at 903-904.

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[2] It is unlikely that the State has the authority to directly enforce its law against tribal members because Congress severely limited the State's civil regulatory jurisdiction on-reservation. 25 U.S.C. § 233. The State's system can be read as a jurisdictional scheme by forcing the Tribe to enforce state law within reservation borders. This, too, strongly suggests the State has overstepped the boundaries of its taxing authority.

The *Printz* Court looked to a number of factors to find a violation of state sovereignty. First, the state was required to absorb the cost of implementing the regulatory program. Second, the state was being put into the "position of taking the blame for its burdensomeness and for its defects." *Id.* at 930. As an example, the Court noted that it would likely be the law enforcement officer and "not some federal official who will be blamed for any error ... that causes a purchaser to be mistakenly rejected." *Id.*

It is axiomatic that the Tribes are distinct sovereigns and that States have no authority in Indian country absent an act of Congress specifically allowing the extension of state authority. *Worcester v. Georgia,* 31 U.S. 515 (1832). In the area of taxation of non-Indians, a tribe may be asked by the State to bear a minimal burden in assisting with carrying out state law, but no more. *Attea,* 512 U.S. at 73. Those burdens cannot go so far as to "undermine tribal authority," *Williams v. Lee*, 358 U.S. at 223, and the requirements must be "reasonably necessary." *Colville,* 447 U.S. at 160.

The Tenth Amendment cases provide an apt illustration when the interest of two sovereigns collide and result in infringement. The commandeering of a state to enforce federal law can be readily applied to New York's tax coupon system, which commandeers the Tribe to enforce its laws. In fact, the State is foisting upon the Tribe a system it had previously concluded was unenforceable. *Urbach*, above at 7. Shifting that heavy burden on the Tribe is a clear violation of federal law, usurping tribal authority.

For the reasons stated above, the Tribe has a substantial likelihood to succeed on the merits that the 2005 Amended Tax Law's tax-exempt coupon scheme impermissibly infringes upon tribal sovereignty in violation of the doctrine that State action may not infringe

unlawfully "on the right of reservation Indians to make their own laws and be ruled by them." *Bracker,* 448 U.S. at 142.

**2. The Coupon System Violates the State Constitution's Prohibition on Unlawful Delegations of Authority.**

Article 3, § 1 of the New York Constitution states that: "The legislative power of this state shall be vested in the senate and assembly." This broad provision encompasses the concept that the State is not permitted to delegate certain legislative functions to other governmental or non-governmental entities.

Under the coupon system, the Tribe is provided the tax exemption coupons and delegated the power to make the system work. While the State may see it as allowing the Tribe to control its internal tribal affairs, it is in reality asking the Tribe to enforce State law through the enactment of tribal laws. How those tribal laws would intersect with state laws controlling the coupons and violation of the system is not clear.[3] But certainly, "[t]he Legislature cannot delegate the sovereign powers of the state to an administrative or executive authority of a foreign jurisdiction." *Darweger v. Staats*, 275 N.Y.S. 394, 403 (1934). While that a state administrative agency can be charged with the duty of carrying out a statute, once the legislative policy was outlined, "The Legislature should neither invite federal encroachment nor surrender to foreign agency, over which it has no control or supervision, powers given solely to it by the people." *De Agostina v. Parkshire Ridge Amusements, Inc.,* 278 N.Y.S. 622, 629 (1935). Significantly, the *De Agostina* court found that: "[I]f the state's power to delegate governmental functions to a foreign agency is

[3] For example, if the tribe adopted a law allowing exceptions to the coupon system under certain circumstances, would the tribal member have to follow state or tribal law? Would the State be permitted to prosecute a tribal member for following tribal law? Would the State have to accept the Tribe's internal laws regarding safety and control of the coupons? Would the State have to accept the Tribe's internal laws if the Tribe declared the misuse, counterfeiting or illicit trafficking of coupons a tribal misdemeanor?

sanctioned, there can be no legitimate limits to its exercise." *Id.* at 630. The state would then be subservient to a foreign entity not representative of the citizens of the state whose interests were being affected. *Id.*

In *Fink v. Cole*, 302 N.Y. 216 (1951), the legislative delegation of licensing power was at issue. The court described the relevant statute as delegating to The Jockey Club – a private corporation – the power to license horse owners, trainers, and jockeys at races. *Id.* at 224. The Jockey Club was authorized to grant such licenses at their discretion. *Id.* "In fact, in the exercise of the broad discretion vested in them in the issuance of licenses – essentially a sovereign power – the stewards are officers of The Jockey Club who are neither chosen by, nor responsible to the State government." *Id.* The court found that the delegation of licensing power to the Jockey Club "was such an abdication as to be patently an unconstitutional relinquishment of legislative power. . . ." *Id.* at 225.

In this case, the Tribe has been delegated the responsibility of carrying out an administrative function that would otherwise be the responsibility of the Department of Taxation and Finance. The Tribe is not and cannot be answerable to the State for whether this law is carried out properly and the State's attempt to rely on the Tribe violates the State Constitution.

### 3. The Prior Approval System Fails to Protect the Tribal Tax Exemption from Abuse and Therefore Violates Tribal Sovereignty.

When the State legislature adopted the prior approval system, it left the details to the Defendants to sort out. See N.Y. Tax Law §471 subdivision 5(b)("The department shall grant agents and wholesalers prior approval in a manner and form to be determined by the department as may be prescribed by regulations.") The Department failed to enact detailed regulations but rather left the details to the guidance document. The System devised by the

Department violates the Tribe's sovereignty largely because it interposes the tax department as an intermediary in the market transaction between the tribe and the wholesaler. In other words, in effect, the State has placed itself in the position of approving the contract for purchase between the tribe or its retailers, and the wholesaler. While the statute purports to regulate prior approval only as to wholesalers, it is clear that unless an on-reservation retailer places an order, the wholesaler has no need to obtain such approval. The system, therefore, will only work when there is a proposed transaction between the wholesaler and the tribe or retailer. The system therefore imposes a direct civil regulatory regime on the Tribe and tribal retailers whish in so doing directly and illegally interferes with the Tribe's on-reservation economy and its consensual relationship with non-Indian wholesalers.

It has to be assumed, however, that the State legislature intended to enact valid legislation by honoring the federal law requirement that tribal members have access to tax exempt products and that the legislature did not intend to violate the Tribe's internal relationship with its members. Sutherland, Statutes and Statutory Construction §45.11 ("It is presumed that the legislature acted with integrity and with an honest purpose to keep within constitutional limits.") In an ideal situation, the prior approval system could work in controlling tax-exempt supply if there is one reservation retailer and one wholesaler. But the regulations do not take into account the different economies on each reservation. On the Tribe's reservation, there are 30 retailers who deal with at least three different wholesalers. The Tribe is also a retailer but it is one of many. Because the regulations allow any wholesaler and any retailer to order as much product as they can afford under the quota, it is clear that there is no protection for all tribal retailers to obtain tax exempt products. As a result, the system could very well wreck havoc on the Tribe's reservation economy. In that

light, the regulatory system that interposes the State between a retailer and the wholesaler in their contractual relationship, while at the same time trying to allocate a quota with little or no oversight, simply cannot work. The regulations only serve to create interference in the transactions between the retailers and wholesaler and encourage a skewed allocation of the quota.

Commercial transactions within Indian country involve consensual relations with a tribe and are therefore within the jurisdiction of the tribe and are an aspect of tribal self-government. In *Montana*, 450 U.S. at 565-566, the Supreme Court laid down a general rule that "the inherent sovereign powers of an Indian tribe do not extend to the activities of nonmembers of the tribe." But one of the exceptions to the general rule against tribal authority over nonmembers was defined by *Montana*: "A tribe may regulate, through taxation, licensing, or other means, the activities of nonmembers who enter consensual relationships with the tribe or its members, through commercial dealing, contracts, leases, or other arrangements." *Id.* Thus, *Montana* recognized that a Tribe has a significant interest in commercial dealings with non-Indians largely because they impact the welfare of tribal members.

We acknowledge that the Supreme Court has addressed taxation issues separately holding that where an on-reservation transaction takes place between a non-tribal entity and a tribe or tribal members and the legal incidence of the tax rests on the non-Indian, a balancing test between state, federal and tribal interest must be applied to determine whether the State may regulate or apply its laws to that transaction. "This inquiry is not dependent on mechanical or absolute conceptions of state or tribal sovereignty, but has called for a particularized inquiry into the nature of the state, federal, and tribal interests at stake, an

inquiry designed to determine whether, in the specific context, the exercise of state authority would violate federal law" *White Mountain Apache*, 448 U.S. at 144-45 (1980); *Colville*, 447 U.S. at 154-57 (1980) (a state may impose a levy where the legal incidence of the tax rests on non-members, provided that the balance of federal, state, and tribal interests favor the State, and federal law is not to the contrary); *Moe*, 425 U.S. at 482-83 (since the incidence of Montana's cigarette sales tax falls on the consumer, the state may require the collection of the state tax for on reservation sales to non-members because it imposes no burden that frustrates tribal self-government).

While we acknowledge that the Supreme Court has held that States also have a "valid interest in ensuring compliance with lawful taxes that might be easily evaded through purchases of tax-exempt cigarettes on reservations," *Attea*, 512 U.S. at 73 (internal quotations and citations omitted), the Supreme Court also found that the State could do so only if the State's action placed only a "minimal burden" on the Tribe. *Id.*

Looking, not at the pre-approval system itself, but at the interference with both contractual relations and the market and commercial activities on the Tribe's reservation, the prior approval system is more than minimally burdensome. It interferes with the reservation economy to the point of the potential destruction of small businesses by the manipulation of the quota allocation. This is not a matter of the State law preventing the Tribe and its members from marketing a tax exemption. *See Colville*, 447 U.S. at 155. This is a matter of directly interfering with what is now a functioning market place where many small tribal businesses have equal access to the same products and trade in cigarettes is not dependent upon government approval of a contract, where such approval could result in a monopoly. No court has allowed such massive intrusion into a reservation economy.

A comparison of the facts involved in *Colville* and those in this case highlight the difference. As the Supreme Court explained in *Colville*, in all instances, the tribes were the sole purchasers of the cigarettes from the wholesalers. The Supreme Court found that the cigarettes remained the property of the tribes until sale. The Colville, Lummi, and Makah Tribes functioned as retailers, retaining possession of the cigarettes until their sale to consumers. The Yakima Tribe was a wholesaler to its licensed retailers. 447 U.S. at 144-145. Thus the Court did not address a situation where a reservation economy was made up of numerous small businesses purchasing directly from wholesalers would be directly impacted by State interference in contractual relationships.

Similarly, in *Attea*, the plaintiff was a wholesaler and the court focused on how prior approval would impact Attea as a wholesaler. The Court did not focus on the impact prior approval would have on the reservation economy. For example, the *Attea* Court declined to considered issues of prior approval and it did so from the perspective of the wholesaler, not the tribe and its retailers. "The associated requirement that the Department preapprove deliveries of tax-exempt cigarettes in order to ensure compliance with the quotas does not render the scheme facially invalid. This procedure should not prove unduly burdensome [to the wholesaler] absent wrongful withholding or delay of approval-problems that can be addressed if and when they arise." *Attea*, 512 U.S. at 77 (emphasis added). In fact, the Court dismissed the idea that allocation among retailers was an issue because it considered that problem from the perspective of the wholesaler, not the tribe or its retailers. *Id.* at 78. ("Possible problems involving the allocation of cigarettes among reservation retailers would not necessarily threaten any harm to respondent wholesalers, whose main interest lies in

selling the maximum number of cigarettes, however ultimately allocated.").[4]

The federal government has a long-standing interest in supporting economic growth and activity on-reservation through the development of small businesses. *See e.g.*, *California v. Cabazon Band of Mission Indians*, 480 U.S. 202, 216-17 (1987) (Congressional goal of supporting Indian self-government, including its "overall goal" of encouraging tribal self-sufficiency and economic development; 15 U.S.C. § 632(d) and 636(a)(Small Business Administration loan program for tribal businesses). While the federal government may not oppose the right of states to collect taxes from non-Indians using reasonable means, it has a very high interest that the State not destroy a reservation economy by using means that are not tested and will most likely result in the disruption of the market between retailers and wholesalers and between retailers and their customers, including the tribal members entitled to tax exempt products. That interference cannot be justified when the State has other options in collecting enforcing its tax scheme.[5]

Because of the system's significant interference with commercial and consensual relationships the tribe has a substantial likelihood of success in establishing that the Amended Tax Law and the regulations violate federal law.

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[4] The United States had objected to that particular system where New York as created "trade territories" that attempted to allocate each reservation's overall quota among retail outlets. The court found that the objection was also premature but noted that "[d]epending upon how they are applied in particular circumstances, these provisions may present significant problems to be addressed in some future proceeding." *Attea*, 512 U.S. at 77.

[5] For example, the state statute requires that non-Indians pay taxes on any products purchased and upon which a tax is owed. See N.Y. Tax Law §471-a and N.Y. Tax Law § 1112(1) which specifically addresses the payment by non-Indian consumers of taxes on goods purchased on Indian reservations: "Where property or services subject to sales or compensating use tax have been purchased on or from a qualified Indian reservation ..., the purchaser shall not be relieved of his or her liability to pay the tax due. Such tax due and not collected shall be paid by the purchaser directly to the department." The statute not only declares that the tax is owed but directs how it may be paid. The State has never tried to exercise that option.

**4. The Prior Approval System Creates the Likelihood that Tribal Members Will Not Have Access to Tax-Exempt Products.**

The Tribe has a clear likelihood of success on the merits in the proposition that the Defendants have created a situation where untaxed cigarettes may be unavailable to tribal members who are immune from such taxes in violation of federal law. The Supreme Court in *Attea* made it clear that a valid State tax collection scheme ensured that tax exempt products were made available to the tribal members and that New York could not precollect taxes that are otherwise not due. 512 U.S. at 76. The prior approval system fails to "leave ample room for legitimately tax exempt sales." *Id.* By allowing anyone to ask for the entire tax exempt quota, the system leaves open the very good possibility that no tax exempt products will be available to tribal members. This would place a tribal member in the position of having to purchase cigarettes and pay the tax and then ask for a refund. However, the prepayment of a tax that is not otherwise due and that New York has no legitimate interest in collecting and enforcing is a violation of federal law.

The *Attea* Court approved a precollection scheme that would apply to "cigarettes destined for nonexempt consumers." The Court approved this system only "assuming that the 'probable demand' calculations leave ample room for legitimately tax exempt sales." The Court noted that the approved scheme adopted by the State should "not require prepayment of any tax to which New York is not entitled." *Id.* at 76. That is, the Court would not approve any system that would require State pre-collection of taxes on sales to tribal members who are tax immune and then require the tribal member or to request a refund from the State on what would otherwise have been a non-taxable transaction.

The Supreme Court in *Attea* did not address the issue of an inadequate supply of legitimate tax exempt cigarettes for tribal purchasers but stated that such a situation "may

provide the basis for a future challenge." Certainly such a challenge would succeed as inadequate supply of tax exempt cigarettes for tribal purchasers leaves no alternative but for the imposition of a state tax whose legal incidence falls upon tribal members inside Indian Country. *See Oklahoma Tax Comm'n v. Chickasaw,* 515 U.S. 450, 458 (1995) (internal quotations omitted), which provides as follows:

> when a State attempts to levy a tax directly on an Indian tribe or its members inside Indian country, rather than on non-Indians, we have employed, instead of a balancing inquiry, a more categorical approach: [A]bsent cession of jurisdiction or other federal statutes permitting it,' we have held, a State is without power to tax reservation lands and reservation Indians. Taking this categorical approach, we have held unenforceable a number of state taxes whose legal incidence rested on a tribe or on tribal members inside Indian country. See, e.g., *Bryan v. Itasca County*, 426 U.S. 373 (1976)(tax on Indian-owned personal property situated in Indian country); *McClanahan*, 411 U.S. at 165-166 (tax on income earned on reservation by tribal members residing on reservation).

**D. The Tribe Has a Substantial Likelihood of Success in Establishing That If the Coupon System in Illegal, the Prior Approval System Must also be Struck Down Since it is Not Severable.**

Because the provisions of the Act governing tribal election to participate in the coupon system are invalid, the Court must determine whether those provisions can be severed from other parts of the statute. *National Advertising Co. v. Town of Niagara*, 942 F.2d 145, 148 (2d Cir. 1991). The Tribe maintains that the prior approval system cannot stand on its own and if the coupon system violates federal law, the entire system of tax collection set up in the 2010 Amended Tax Law must be declared in violations of federal and state law.

"Severability is a question of state law." *Id.* Under New York law, severance is appropriate only when the legislative body, foreseeing the partial invalidity, would have intended the provision to be severed, and when the remaining provisions can function as a

coherent whole. *Id.* (citing *People ex rel. Alpha Portland cement Co. v. Knapp*, 230 N.Y. 48, 129 N.E. 202 (1920)). The Second Circuit, applying New York law, has explained that "severance is inappropriate when the valid and invalid provisions are so intertwined that excision of the invalid provisions would leave a regulatory scheme that the legislature never intended." *Id.* (*citing New York State Superfund Coalition, Inc. v. New York State Dep't of Environmental Conservation,* 75 N.Y.2d 88, 94, 550 N.E.2d 155, 157, 550 N.Y.S.2d 879, 881 (Ct.App.1989)).

Here, the provisions providing for a tribe to elect to participate in the coupon system are so intertwined with other provisions for collection of the cigarette tax on on-reservation sales to non-tribal members that they cannot be severed, and all such provisions must fall. Before the New York Assembly enacted the 2010 amendments to Tax Law Sections 471 and 471-e, Section 471-e provided for the collection of the cigarette tax on on-reservation sales to non-tribal members through a coupon system. The coupons were never issued, however, and the state courts declared that that section was not effective and could not be enforced. *See Day Wholesale v. New York*, 856 N.Y.S.2d 808 (4th Dept. 2008); *Cayuga Indian Nation of New York v. Gould*, 14 N.Y.3d 614, 629 (N.Y. 2010).

In adopting the 2010 amendments to the Tax law, the legislature did not repeal the coupon system provisions in the law. Instead, the legislature retained those provisions, while amending them to provide that a tribe could elect the coupon system. N.Y. Tax Law § 471-e, subdiv. 2, para. (a); see also N.Y. Tax law §§ 471 subdiv. 1 & 5. *See also* 2010 New York Laws Chapt. 134, Part D, §6 (amending §471-e, showing changes to prior law). In addition to revising the law's provisions regarding the coupon system, the Assembly enacted new provisions implementing the prior approval system. N.Y. Tax Law § 471, subdiv. 5; *see also*

N.Y. Tax Law §§ 471, subdiv. 1. The prior approval provisions apply, however, if and only if a tribe does not elect to participate in the coupon system. The Legislature intended that tribes have a choice in taxing systems. The section of law implementing the prior approval section begins by stating "For any year that the recognized governing body of an Indian nation or tribe has not elected to participate in the Indian tax exemption coupon system established in section four hundred seventy-one-e of this article, paragraph (b) of this subdivision provides for the prior approval system . . . ." N.Y. Tax Law § 471, subdiv. 5. Other provisions in the law are to the same effect. *See* N.Y. Tax Law § 471 subdiv. 1 ("Indian tribes may elect to participate in the Indian tax coupon system . . . . If an Indian nation or tribe does not elect to participate in the Indian tax exemption coupon system, the prior approval system shall [apply].") ; N.Y. Tax Law § 471-e, subdiv. 1, para. (b) (providing that prior approval system will apply if tribe does not elect to participate in coupon system). The prior approval system, then, was intended by the Legislature to supplement, and not supplant, the coupon system.

The provisions in the New York Tax Law providing for the Indian tax exemption coupon system and the prior approval system are intertwined, and therefore the provisions implementing the prior approval system cannot be severed. *National Advertising Co. v. Town of Niagara*, 942 F.2d at 148-151 (refusing to sever intertwined provisions); *New York SMSA Limited Partnership v. Town of Clarkstown*, 603 F. Supp. 2d 715, 735 (S.D.N.Y. 2009) ("Severance of the invalid provisions, however, would create a confusing and unworkable statute"), *aff'd on other grounds*, 612 F.3d 97 (2d Cir. 2010); *New York State Superfund Coalition, Inc.*, 75 N.Y.2d at 94, 550 N.E.2d at 157, 550 N.Y.S.2d at 881 (where invalid standard was interwoven throughout the regulatory scheme, "judicial excision of that

provision to let the rest survive is inappropriate."); *Loew v. McNeill*, 170 Misc. 647, 10 N.Y.S. 2d 658, 660 (Sup. Ct. 1939) ("Since both parts of [an amendment to a statute] are so closely interdependent that one part cannot be permitted to stand alone without a complete disruption in the legislative scheme, the entire amendment is declared inoperative . . . .") *aff'd mem.* 279 N.Y. 806, 19 N.E. 2d 94 (1939).

Given the fact that the Legislature intended to create a choice, the Court cannot strip from statutory provisions implementing the prior approval system language stating that that system applies only if a tribe does not elect to participate in the void Indian tax coupon system as to do so would work a revision to the statute and frustrate the legislature's intent. *See National Advertising Co.*, 942 F.2d at 151 ("it is clear to us that the ordinance must be redrafted and that the Town of Niagara, not this court, should do it"); *Villas at Parkside Partners v. City of Farmers Branch*, 496 F.Supp.2d 757, 773-74 (N.D.Tex. 2007) ("The city asks the court to essentially rewrite the ordinance by stripping phrases that are inextricably intertwined to create a new ordinance that clearly frustrates the original legislative intent.").

The presence of a severance clause in the statute does not change the result.[6] Although a severance clause is relevant to the inquiry, it "is not dispositive," *National Advertising Co.*, 942 F.2d at 148, and an unconstitutional provision will not be severed even if the statute contains a severance clause where the unconstitutional provision is intertwined with other provisions of the law. *New York State Superfund Coalition,* 75 N.Y.2d at 94, 550 N.E.2d at 157, 550 N.Y.S.2d at 881 (objectionable provisions were not severable despite a severability clause).

[6] 2010 New York Laws, Ch. 134, Part D § 25.

**E. The Tribe Has a Substantial Likelihood of Success in Establishing That the State Law Violates the Equal Protection Clause of the U.S. Constitution.**

As explained above, the State law distinguishes between tribes as sovereigns and other governments and their related entities by imposing a draconian prior approval system on the Tribes before tax exempt products can be purchased.

The Equal Protection Clause of the Fourteenth Amendment provides that "no State shall ... deny to any person within its jurisdiction the equal protection of the laws." U.S. Const. amend. XIV, § 15. The clause "is essentially a direction that all persons similarly situated should be treated alike." *City of Cleburne v. Cleburne Living Center*, 473 U.S. 432, 439 (1985). Legislation that does not restrict a fundamental right or employ a suspect classification, like the social and economic legislation at issue in this case, is presumed valid as long as it is rationally related to a legitimate government interest. *Id.* at 440; *Romer v. Evans*, 517 U.S. 620, 631 (1996). While the government is entitled to deference when enacting social and economic legislation, the court must to substantively review the legitimacy of social and economic legislation. *Zobel v. Williams,* 457 U.S. 55 (1982). The question is whether any set of facts exist that may reasonably justify the challenged law. A law with a classification that is rationally related to a legitimate state interest will be upheld. *City of New Orleans v. Dukes*, 427 U.S. 297, 303 (1976). "Conversely, if this Court determines that the legislature acted arbitrarily or classified Plaintiff upon some ground not having a fair and substantial relation to the object of the act, such that similarly situated persons are treated differently, it must strike down the statute." *Consolidated Edison Co. v. Pataki*, 117 F.Supp.2d 257, 262 (N.D.N.Y. 2000) *citing Reed v. Reed*, 404 U.S. 71 (1971) and *F.S. Royster Guano Co. v. Virginia*, 253 U.S. 412, 415 (1920).

In this case, in the enactment of detailed statutory requirements and regulations, the legislature and the Defendants singled out and targeted nine tribes residing in the State, federally recognized sovereign nations, and concluded that they had to be treated differently than all other governmental entities in the State, even including unincorporated voluntary organizations and diplomatic missions, in the method by which they may obtain a supply of tax exempt cigarettes. *See* 20 N.Y.C.R.R. § 76.1 (general outline of exemption); 20 N.Y.C.R.R. § 76.2 (a)(1)(as applied to United States); 20 N.Y.C.R.R. § 76.4 (diplomatic missions and diplomatic personnel).

Notably, these entities are entitled to purchase as much tax exempt product with no quota, no limitations and no relationship to the potential consumption of the tax exempt populations. Nor are the purchases subject to prior approval. In addition, tax exempt products may be purchased for governmental use. Under § 76.2 Governmental Entities, the state regulations permit such entities to obtain tax-exempt cigarettes for "governmental functions" which appears to be in addition to and distinguished from those products necessary for the consumption by authorized purchasers.

The quota set for the Tribe, on the other hand, is a strict quota. The Tribe may to obtain cigarettes for "official use," but official use is undefined, and appears to be equate with tribal member demand, an equivalency not made for other governmental entities. See 20 N.Y.C.R.R. §74.6(e)(2)("In making a determination of probable demand, the department will take into consideration any evidence submitted by the recognized governing body of an Indian nation or tribe relating to such probable demand (e.g., a verifiable record of previous sales to qualified Indians or other statistical evidence) and/or relating to the amount needed for such nation's or tribe's official use.")

The distinction between the treatment of tribes and governmental entities appears to be based on the assumption that tax exempt cigarettes are somehow prone to abuse that military tax exempt cigarettes are not.

This is unlikely while the State has widely studied the issue of the misuse of tax exempt cigarettes on Indian reservations, the legislature has completely ignored any abuse that may occur on military bases or by diplomatic missions. For example, the military exemption clearly requires the consumption of tax-exempt cigarettes on base. But there is not a shred of evidence that this actually occurs and in fact, it is unlikely. It is more probable that military personnel not only take product out of the confines of the military reservation, but that they make such purchases for family and friends who are subject to the tax.

In two separate studies on cigarette tax evasion, it was found that tax exempt cigarette sales on military bases soar when state cigarette taxes rise because those without military store privileges ask family and friends to purchase tax exempt products for them. *See* Tax Foundation, *Special Report, California Schemin': Cigarette Tax Evasion and Crime in the Golden State*, p. 5, accessed September 14, 2010 at www.taxfoundation.org/files/sr145.pdf Exh. 4 to Schmidt Aff.; Mackinac Center for Public Policy, *Tax Exempt Sales on Military Bases in Michigan*, Dec. 3, 2008, accessed on September 14, 2010, at www.mackinac.org/archives/2008/s2008-12.pdf, Exh. 3 to Schmidt Aff. Such sales result in the loss of millions of dollars in tax revenues for impacted states. While the Defense Department attempted to address the situation is 2000 by ordering military stores to set prices at no less than 5 percent below the minimum price at the most competitive local market, the measure has only lessened the impact on lost revenue, not stopped it. Exh. 4, p. 5.

Nor does the statute or regulation take into account the differences even among the tribes. In 2009, the New York Association of Convenience Stores commissioned a report on additional tax revenue sources for New York State. The main purpose of the report was to assess the total demand for cigarettes by New York State residents and in turn, to estimate the number of cartons which were sold by conventional sources with the appropriate New York State tax stamp and the number of cartons which were purchased via "alternative distribution channels" by New Yorkers without paying the local excise tax. *See* Exh. E to Decl. of Lazore, *An Update – Additional Cigarette Tax Revenue Sources For New York State*. This report concluded that for fiscal year 2008-09, total untaxed sales through "alternative" channels, which includes tribal/internet sales, bootlegged sales, and cross-border sales, totaled 55,400,000 (fifty-five million, four hundred thousand) cartons of cigarettes. This is the equivalent of 554,000,000 (five-hundred, fifty-four million) packs of cigarettes packs. In comparison, the St. Regis Mohawk Tribe requires 717,084 cartons, which equates to approximately 1.4% of the total number of alternative channel marketed products set forth by the NYACS report. *See* Declaration of E. Lazore, ¶ 5. This number is miniscule in comparison to other so-called alternative channels suggesting that the Tribe and its retailers pose no real threat to the State tax revenue stream. *Id.* It is more likely that this is equivalent to the tax exempt products leaving military bases improperly—an amount for which the State turns a blind eye. But the State has lumped the Tribe in with other wrong doers assuming that each is equal in revenue impact while at the same time it has exonerated other tax exempt entities from any sort of accounting regime presumably based on an assumption that there is no problem in that quarter.

As this court held in *Consolidated Edison*, creating a statutory class that singles out

an individual or, as in this case a few tribes, is arbitrary particularly when it is highly likely that similar abuse or misuse may occur in similarly situated parties. 117 F.Supp.2d at 264. ("As long as the classification is reasonable, not arbitrary, and [rests] upon some ground of difference having a fair and substantial relation to the object of the legislation, so that all persons similarly circumstanced shall be treated alike," this Court will uphold it. However, as this Court has stated, if the classification is "so under-inclusive" that it bears no relation to the statute's purpose, the Court will strike it down." Citations and quotes omitted).

In this case, the State has focused exclusively on tribes for separate discriminatory treatment without even bothering to determine if other tax exempt entities are sources of purported misuse. On that ground, the statute violates Equal Protection.

**F. The Issuance of a Preliminary Injunction is in the Public Interest.**

Given the substantial harm that may occur to tribal sovereignty, the serious questions raised by the Tribe's complaint, and the substantial injury that would occur to the Tribe and its economy, and economy that benefits thousands of tribal members and New York state citizens, it would be in the public interest to issue a preliminary injunction to maintain the status quo while this case is being resolved. The State has not enforced its cigarette tax laws since 1994 and it is unlikely that there will be much difference to it if an injunction is issued until this case is resolved. On the other hand, an injunction will ensure that the Tribe's relationship with its retailers and the ability of retailers to obtain products for sale will be impinged to the point that the injury to the tribal economy is irreparable. A preliminary injunction has been issued in most every cigarette tax case that has been brought before the federal courts. *See e.g., Moe*, 425 US at 474; *Colville,* 447 US at 140; *Attea,* 512 US at 61.

**Conclusion**

Based on the above, the affirmations accompanying this memorandum and the exhibits attached thereto, this court is justified in issuing a temporary restraining order and preliminary injunction prohibiting the Defendants from enforcing the 2010 Amended Tax Law and Emergency Regulations.

Respectfully submitted,

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