UNITED STATES DISTRICT COURT
WESTERN DISTRICT OF MICHIGAN
NORTHERN DIVISION

KEWEENAW BAY INDIAN COMMUNITY, a federally-recognized Indian tribe, on its own behalf and as *parens patriae* for its members,

Plaintiff,

v

NICK A. KHOURI, Treasurer of the State of Michigan; WALTER FRATZKE, Native American Affairs Specialist of the Michigan Department of Treasury; RUTH JOHNSON, Secretary of State of Michigan; and CHRISTOPHER CROLEY, Detective/Sergeant of the Michigan State Police; DANIEL C. GRANO, Assistant Attorney General for the State of Michigan; and, TIMOTHY SPROULL, Detective of the Michigan State Police,

Defendants.

No. 2:16-cv-00121

HON. PAUL L. MALONEY

MAG. TIMOTHY P. GREELEY

DEFENDANTS' BRIEF OPPOSING PLAINTIFF'S MOTION FOR PARTIAL SUMMARY JUDGMENT REGARDING THE SALES AND USE TAXES

ORAL ARGUMENT REQUESTED

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CONCISE STATEMENT OF ISSUES PRESENTED

1. Do the Indian Trader Statutes categorically preempt the sales tax on retailers or the use tax on lessors that, respectively, sell or lease tangible personal property to the Community and its resident tribal members?

2. Does federal law categorically preempt the use tax when the Community and its resident tribal members use tangible personal property outside the tribe's Indian country?

3. Does Treasury's refund and exemption system violate equal protection?

4. Does Treasury's refund and exemption system violate due process?

5. If the court grants any portion of this motion, should the court deny the Community further relief under 28 U.S.C. § 2202?

CONTROLLING OR MOST APPROPRIATE AUTHORITY

Authority:

Moe v. Confederated Salish & Kootenai Tribes of Flathead Reservation, 425 U.S. 463 (1976).

Mescalero Apache Tribe v. Jones, 411 U.S. 145 (1973).

Steffel v. Thompson, 415 U.S. 452 (1974).

Wagnon v. Prairie Band Potawatomi Nation, 546 U.S. 95 (2005).

Washington v. Confederated Tribes of Colville Indian Reservation, 447 U.S. 134 (1980).

White Mountain Apache Tribe v. Bracker, 448 U.S. 136 (1980).

INTRODUCTION

Federal law bars a state from asserting "regulatory authority over tribal reservations and members" when federal law preempts state law or state law infringes on tribal sovereignty and self-governance. *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136, 142 (1980). The Department of Treasury recognizes both immunities from the sales tax levied on persons that sell tangible personal property at retail under the General Sales Tax Act, Mich. Comp. Laws § 205.51 *et seq*., and the use tax levied on persons that use, consume, or store tangible personal property in Michigan under the Use Tax Act, Mich. Comp. Laws § 205.91 *et seq*.

Treasury provides a system for the Community and its members to assert their federal immunities from the sales and use taxes by requesting an exemption letter before a purchase or a refund after the tax is paid. (Ex. 1, ¶ 19.) Treasury has also developed alternatives to submitting individual claims for certain repetitive sales or uses. (Ex. 1, ¶ 56.) These methods for obtaining refunds or exemptions are in addition to all other generally applicable tax exemptions, which the Community and its members are entitled to assert. (Ex. 1, ¶¶ 21-22.) This system gives effect to federal Indian tax immunities while protecting Treasury's interests in collecting revenue from non-Indian retailers and applying nondiscriminatory laws to the Community and its members for taxable activities outside of Indian country. The Community seeks to eliminate the refund and exemption system and to force Treasury to use an exemption certificate system to hamper Treasury's ability to collect lawful taxes.

The Community's legal arguments are meritless. Federal law does not categorically bar taxing all "Indian traders," i.e. the non-Indian retailers subject to the sales tax or lessors who collect the use tax. Nor does federal law categorically bar levying the use tax on the Community and its members who live in the tribe's Indian country (resident tribal members) when they use tangible personal property outside of Indian country because the use tax is not an annual personal

property tax that requires apportionment. Further, the refund and exemption system does not violate the Equal Protection and Due Process Clauses of the Fourteenth Amendment, U.S. Const., amend XIV, § 1, cl. 3 and cl. 4, because it does not adopt a racial classification and it is fundamentally fair.

Defendants respectfully ask this Court to deny the Community's motion and, instead, enter summary judgment in their favor on Counts I, V, VII, VIII, and the portion of Count XVII seeking an injunction related to those other sales and use tax counts. If the court grants any part of the Community's motion, the court should decline to enter the Community's proposed order because further relief under 28 U.S.C. § 2202 is not necessary and proper.

FEDERAL PREEMPTION IN INDIAN TAX CASES

Federal law preempts state law when a state levies "a tax directly on an Indian tribe or its members inside Indian country[.]" *Oklahoma Tax Comm'n v. Chickasaw Nation*, 515 U.S. 450, 458 (1995); *McClanahan v. State Tax Comm'n of Arizona*, 411 U.S. 164, 179-80 (1973). "Absent express federal law to the contrary," federal law does *not* preempt a nondiscriminatory state tax imposed on Indian tribes and their members outside of Indian country. *Mescalero Apache Tribe v. Jones*, 411 U.S. 145, 148-49 (1973). States may also tax non-Indians outside Indian country unless prohibited by Congress. *See Wagnon v. Prairie Band Potawatomi Nation*, 546 U.S. 95, 113 (2005). But when states seek to tax non-Indians for activities inside Indian country, courts employ 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." *Bracker*, 448 U.S. at 145. As these cases illustrate, an Indian tax preemption analysis examines "the 'who' and the 'where' of the challenged tax," which are factors that "have significant consequences." *Wagnon*, 546 U.S. at 101. The analysis focuses on the legal incidence of the tax, not economic burdens. *See id*. at 114-15.

STATEMENT OF FACTS

Treasury's Administration of the Sales Tax

The General Sales Tax Act imposes an annual 6% gross proceeds tax on "all persons engaged in the business of making sales at retail, by which ownership of tangible personal property is transferred for consideration . . . ." Mich. Comp. Laws § 205.52(1). The legal incidence of the sales tax falls on the retailer even though a retailer may "reimburse" itself for the amount of the tax. *See* Mich. Comp. Laws § 205.73(1); *Andrie Inc. v. Treasury Dep't*, 853 N.W.2d 310, 317 (Mich. 2014) ("a retail seller is 'not prohibited' from including sales tax in an item's price, but this leaves the retail seller the option to shoulder the sales tax burden itself").

Treasury does *not* levy the sales tax on retail sales made by the Community and its members under the following circumstances. (PageID.1697.)

[Sales Tax]

Community or Member as Retailer

Treasury recognizes that the sales tax does not apply to a person engaged in the business of making sales at retail (the retailer) if:

(1) the retailer is wholly owned by the Community or its member(s);

(2) the business is located inside the Community's reservation or trust lands (Indian country); and

(3) the transaction occurs within the Community's Indian country.

Treasury's procedure is that it will not require remittance of sales tax for an exempt transaction that meets all three of these factors. If the sales tax were remitted for an exempt transaction, Treasury will process and pay any timely request to refund the sales tax with the interest required by Mich. Comp. Laws § 205.30.

Text Box 1: Treasury Policy for Sales Tax When the Community or a Member is the Retailer

However, none of the refund and exemption claims in this case involve the Community or one of its members acting as a retailer. (Ex. 1, ¶ 52; Ex. 2, ¶ 23.)

All sales tax claims in this case involve Treasury's policy for the sales tax when the retailer is a non-Indian. (PageID.1697-1698.)

[Sales Tax]

Community or Member Not the Retailer

Treasury also recognizes that the sales tax does not apply when:

(1) the retailer is not wholly owned by the Community or its member(s);

(2) the transaction involves the Community's (not a member's) acquisition of tangible personal property that will be used for or otherwise serve an essential governmental function provided by the Community; and

(3) the transaction occurs within the Community's Indian country.

Treasury's procedure is that it will not require remittance of sales tax for an exempt transaction that meets all three of these factors. If requested, Treasury will provide the Community with an exemption letter for an exempt transaction. If sales tax were remitted for an exempt transaction, Treasury will process and pay a timely request to refund the sales tax with the interest required by Mich. Comp. Laws § 205.30.

Text Box 2: Treasury Policy for Sales Tax When the Community or a Member is Not the Retailer

Treasury is unaware of any sales tax claims at issue in this case involving a retailer licensed under the Indian Trader Statutes, 25 U.S.C. § 261 *et seq.*, or a purchase financed or approved by the Bureau of Indian Affairs. (Ex. 1, ¶ 53.) Additionally, Treasury does not tax licensed Indian traders selling at retail to a tribe or its members inside the tribe's Indian country. (Ex. 1, ¶ 16.)

Treasury's Administration of the Use Tax

The Use Tax Act levies a "specific tax" on "every person in this state . . . for the privilege of using, storing, or consuming tangible personal property in this state at a total combined rate

equal to 6% of the price of the property or services" specified in the act. Mich. Comp. Laws § 205.93(1); *see also* Mich. Comp. Laws § 205.92(b) (defining "use"). The consumer bears the legal incidence of the use tax, not the seller or lessor (collectively seller). *See* Andrie, 853 N.W.2d at 314. Mich. Comp. Laws § 205.94(1) provides an exemption from the use tax with evidence that the sales tax was "due and paid."

Treasury has explained how it administers the use tax in connection with the Community and its members. (PageID.1702.)

[Use Tax]

Use Solely Inside of the Community's Indian Country

Treasury recognizes that the use tax does not apply when:

(1) the purchaser is the Community or its qualified member(s);

(2) the tangible personal property transaction occurs inside the Community's Indian country; and

(3) the tangible personal property is used, stored, or consumed solely in the Community's Indian country.

Treasury's procedure is that it will not collect and/or require the remittance of use tax in circumstances that meet all three of these factors. If requested, Treasury will provide the Community or its members with an exemption letter for an exempt transaction. Additionally, if the use tax were remitted or collected for an exempt transaction, Treasury will process and pay a timely request to refund the use tax with the interest required by Mich. Comp. Laws § 205.30.

Text Box 3: Treasury Administration of the Use Tax When the Community's or its Member's Use is Solely Inside of Indian Country

Additionally, Treasury recognizes immunities from the sales and use taxes when the Community purchases tangible personal property that serves an essential governmental function, even if it is used both inside and outside of its Indian country. (Ex. 1, ¶ 15.)

Treasury's Informal Exemption and Refund Process and *Rising II*

More than a decade ago, the Community challenged the way Treasury administers the sales and use taxes. *See Keweenaw Bay Indian Cmty. v. Kleine*, 546 F. Supp. 2d 509 (W.D. Mich. 2008), aff'd in part, vacated in part sub nom. *Keweenaw Bay Indian Cmty. v. Rising*, 569 F.3d 589 (6th Cir. 2009) (*Rising II*). At the time, Treasury had an informal refund and exemption system for sales and use tax claims from "non-agreement" tribes, i.e., tribes without a tribal-state tax agreement. (PageID.1717, ¶ 21.)

The District Court in *Rising II* concluded that Treasury's process was "relevant and reasonably tailored to allow them [Treasury personnel] to make" the taxability determination. *Kleine*, 546 F. Supp. 2d at 525. But the Community had not submitted claims to Treasury and, therefore, the claims were not ripe, and the court declined to issue a declaratory judgment. *Id*. at 525-26. On appeal, the Sixth Circuit agreed that the sales and use tax claims were not ripe and should not be the subject of a declaratory judgment. *See Rising II*, 569 F.3d at 594. The Sixth Circuit vacated a portion of the District Court's decision concerning the Community's claim under 42 U.S.C. § 1983 regarding offsets and remanded for further proceedings. *Id*. at 594-96. On remand, the parties entered into a confidential stipulation for entry of a consent judgment that was filed under seal with the court.

Treasury's Current Exemption and Refund System and the Test Claims

Anticipating this litigation after *Rising II*, Treasury formalized how it handled sales and use tax exemption and refund claims from non-agreement tribes and their members. (Ex. 1, ¶ 19.) Treasury developed two forms, one for tribes and one for tribal members, that focus on the "who" and "where" elements of a claim. (PageID.1684-1685, 1687-1689.) The same form is used for a refund or exemption, and every claim receives individual review and a determination.

GRANTING OR APPROVING A CLAIM FOR A REFUND OR EXEMPTION LETTER

Refund or Exemption Denied – Treasury issues a denial letter.

Exemption Approved – Treasury issues an exemption letter to the retailer/taxpayer and, if titling is involved, an exemption letter to the branch of the Secretary of State's Office that will be processing the transaction.

Refund Approved – The Tax Processing Division issues a warrant or check for payment.

Supplemental Information Requested – Treasury may also request additional information or documentation to evaluate a claim. Treasury takes no further action on the claim until the filer responds with the requested information – those claims are neither approved nor denied.

Text Box 4: Treasury's Potential Responses to a Claim for a Sales or Use Tax Refund or Exemption Letter

Treasury subsequently placed the claim forms on the portion of its website that addresses Native American tax issues. (Ex. 1, ¶¶ 10, 23.) Treasury also posted information (guiding principles) concerning how it decides sales and use tax claims for refunds and exemptions. (PageID.1691.)

Beginning in 2012, the Community and four of its members (Susan LaFernier, Michael LaFernier, Sr., Elizabeth Mayo, and Scott Mayo – collectively, the Members) began submitting sales and use tax test claims to Treasury. (PageID.2031, 2035, 2039, 2043.) In the first few years, the Community, the Members, and Treasury all made multiple adaptations to how they submitted or responded to the claims. For instance, the Community and the Members developed form letters, and the Members moved from submitting groups of sales and use tax claims to single claims. (Exs. 4.s and 5.s.) Likewise, Treasury developed a series of form letters to promote consistent and faster administration of claims. (Ex. 1, ¶ 48.)

Treasury also created two alternatives for certain types of repetitive individual claims. Treasury adapted its secure utility website so that utility providers do not have to collect the use tax or reimburse themselves for the cost of the sales tax when providing services to exempt tribal units and tribal members. (Ex. 1, ¶ 57.) Treasury also developed multi-year (blanket) exemption letters for certain purchased or leased items. (Ex. 1, ¶ 58; Ex. 1.D.s.)[1]

The current version of the refund and exemption system is an interim step until the courts resolve the dispute with the Community concerning the circumstances when federal law preempts the sales and use taxes. (Ex. 1, ¶¶ 18, 24.) When the courts decide these issues, Treasury intends to reevaluate how the system gives effect to federal tax immunities for non-agreement tribes and their members and, if necessary, adapt it to meet federal law. (Ex. 1, ¶ 24.)

The Two Summary Charts

Treasury received 1,240 sales or use tax refund or exemption claims from the Community and the Members before the tribe filed this lawsuit in May 2016. (Ex. 2.A, claims #1-1240.) Even after suing, the Community and the Members continue to file claims. (Ex. 2.A, claims #1241-1345.) Treasury initiated informal discovery with the Community earlier this year to reconcile their records in the hope of providing the court with a single, reliable summary chart of all the claims. (Ex. 2, ¶ 27.) The Community filed this motion before completing the process.

The Community produced a chart (KBIC Summary Chart) with this motion that summarizes the sales and use tax test claims, but does not fully or accurately account for the claims or how Treasury decided them. (PageID.1649-1682.) Treasury has provided its own summary of the claims (Treasury Summary Chart), as well as two sets of tables (Basic Queries) that describe the claims. (Exs. 2.A, 2.B, 2.C.) Melissa Thelen's declaration identifies the

[1] A lower case "s" in an exhibit number means the document is being filed under seal.

differences between the parties' summary charts, including the information that the Community would have to provide to reconcile those differences. (Ex. 2, ¶¶ 34-38, and differences table.)

The following table provides a snapshot of the sales and use tax test claims in this case.

	Tribal Units 2012-2017	Members 2012-2017	TOTALS 2012-2017
Total Claims	1,031	314	1,345
Sales Tax Claims	877	225	1,102
Use Tax Claims	154	84	238
Neither Sales/Use Tax	0	5	5
Exemption Letters Issued	25	0	25
Claims Denied	952	231	1,183
Claims Approved	70	81	151
Treasury Waiting for Info	2	0	2
Refunds Issued	70	81	151

Table 1: Summary of Sales and Use Tax Claims for 2012-2017

LEGAL TEST FOR SUMMARY JUDGMENT

A party seeking partial summary judgment must demonstrate that "there is no genuine dispute as to any material fact and the movant is entitled to judgment as a matter of law" concerning the claims or defenses challenged. Fed. R. Civ. P. 56(a). A court reviews all the evidence in the record in the light most favorable to the nonmoving party. *See Matsushita Elec. Indus. Co. v. Zenith Radio Corp.*, 475 U.S. 574, 587 (1986). A court may only enter summary judgment against the nonmovant "after adequate time for discovery" and if the nonmovant "fails to make a showing sufficient to establish the existence of an element essential to that party's case and on which that party will bear the burden of proof at trial." *Celotex Corp. v. Catrett*, 477 U.S. 317, 322 (1986). However, the court may enter summary judgment in favor of a nonmovant if it grants notice of its intent to do so to the parities and gives them a reasonable time to respond. Fed. R. Civ. P. 56(f)(1); *see, generally*, *Smith v. Alford*, No. 1:13-CV-694, 2015 WL 6159397, at *5 (W.D. Mich. Oct. 20, 2015), aff'd (Oct. 5, 2016) (plaintiff was given notice and opportunity to respond to court's intent to enter summary judgment in favor of nonmovant).

ARGUMENT

I. The Indian Trader Statutes do not categorically preempt the sales tax on retailers or the use tax on lessors that, respectively, sell or lease tangible personal property to the Community and its resident tribal members.

The Community contends that the Indian Trader Statutes "categorically bar a state from imposing a tax, the legal incidence of which falls on an Indian trader, for sales, leases, or rentals of property to Indian tribes or tribal members within their Indian country." (PageID.1616.) The Indian Trader Statutes, 25 U.S.C. § 261 *et seq.*, regulate trade with reservation Indians. *See Warren Trading Post Co. v. Arizona State Tax Comm'n*, 380 U.S. 685, 688-89 (1965). In the 1800s, Congress granted the Commissioner of Indian Affairs authority to "appoint" traders and to regulate "the kind and quantity of goods and the prices at which such goods shall be sold to the Indians," subject to the President's authority to ban traders and goods. 25 U.S.C. § 261, § 263. The Bureau of Indian Affairs adopted rules that govern traders and their licensure, goods and premises on reservations, financial dealings, and other matters. *See* 40 C.F.R. § 140 *et seq.* Neither the statutes nor the rules specifically mention taxation.

A. Federal law does not bar Michigan from imposing the sales tax on non-Indian retailers selling to the Community and its members.

The Community argues that non-Indian retailers located *anywhere* are immune from the sales tax when they sell to the Community and its resident tribal members. The Community asks the court to eliminate the geographic (where) component of the preemption analysis and to overrule *Bracker*, 448 U.S. at 145, in which the Supreme Court explained the "particularized inquiry" into federal, state, and tribal interests courts use when states seek to tax non-Indians for

activities inside Indian country.[2] The Community incorrectly claims that *Warren Trading* and *Central Machinery Co. v. Arizona State Tax Comm'n*, 448 U.S. 160, 163 (1980) recognize a categorical bar when they actually applied the particularized inquiry explained in *Bracker*.

1. *Warren Trading* applied a particularized inquiry.

In *Warren Trading*, 380 U.S. at 686, the Warren Trading Post operated a retail location on the Navajo Indian Reservation pursuant to an Indian trader license. Arizona imposed a 2% gross proceeds tax on sales at retail. *Id*. at 686 n.1. Warren Trading claimed that it was exempt from the tax for its on-reservation sales to reservation Indians. *See id*. at 686 and n.1.

The Supreme Court noted several factors when considering whether the Indian Trader Statutes preempted Arizona's tax: (1) the statutes and regulations were comprehensive; (2) the tax was on a licensed trader's on-reservation sales; (3) the Department of Interior had interpreted the Indian Trader Statutes to "bar States from taxing federally *licensed* Indian traders on their sales to reservation Indians *on a reservation*"; and (4) the tax would burden the trader and the Indians though Arizona shouldered "no duties or responsibilities respecting the reservation Indians." *Warren Trading*, 380 U.S. at 686-91 (emphasis added). This last factor was at least partly a product of Congress's requirement that Arizona disclaim jurisdiction over Indian lands to gain statehood. *See McClanahan*, 411 U.S. at 175-76. The Supreme Court concluded that Arizona could not impose its tax on a "federally licensed Indian trader with respect to sales made to reservation Indians on the reservation." *Warren Trading*, 380 U.S. at 691.

The Community has presented no evidence that any of the sales tax claims involved a licensed Indian trader taxed for making sales to the Community and on the L'Anse Indian

[2] The "categorical bar" claims at issue do not require the court to engage in this particularized inquiry, which would be premature because it is the subject of expert testimony; expert reports are in-progress but not due for months, and discovery is ongoing. Fed. R. Civ. P. 56(d). (Ex. 7.)

Reservation. Nor has Treasury adopted a policy to tax a licensed Indian trader selling to a tribe or its resident tribal members inside Indian country. (Ex. 1, ¶ 16.) Further, in *Warren Trading*, the Supreme Court did not announce a categorical rule; it engaged in the fact-specific inquiry it would later explain in *Bracker*. *See Bracker*, 448 U.S. at 152 (citing *Warren Trading* as an example of the "reasoning" supporting a particularized inquiry).

When western states like Arizona disclaimed jurisdiction[3] over Indian country, they assumed few responsibilities toward their tribes and had lesser interests in taxation while the federal government assumed greater responsibilities and had higher interests in taxation. *See, e.g., Ramah Navajo Sch. Bd., Inc. v. Bureau of Revenue of New Mexico*, 458 U.S. 832, 839-43 (1982) (comparing federal interest in educating Indian children to state that had "declined to take any responsibility" for their education in a dispute over taxing a non-Indian contractor constructing a reservation school). But unlike Arizona and those other states, Michigan did not disclaim jurisdiction over Indian country to become a state. *See* Mich. Const. of 1835; Act Admitting Michigan to the Union, 5 Stat. 144 (Jan. 26. 1837); Enabling Act of 1836, 5 Stat. 49 (June 15, 1836). Today, Michigan provides significant services to the Community and its members supported by tax revenue, including revenue generated by the sales tax.

For instance, the Michigan constitution earmarks 73.33% of the sales tax and 33.33% of the use tax for the School Aid Fund, which pays for K-12 education. *See* Mich. Const. 1963, art. 9, § 8 and § 11. (Ex. 8.) In 2017-2018, the sales tax is estimated to contribute $5.77 billion and the use tax is estimated to contribute $558.8 million to the School Aid Fund's total revenue. (Ex.

[3] *See, e.g.*, Enabling Act of 1910, 36 Stat. 557, §§ 2 and 20 (June 20, 1910) (New Mexico and Arizona); Enabling Act of 1889, 25 Stat. 676, § 4 (Feb. 22, 1889) (North Dakota, South Dakota, Montana, and Washington); Enabling Act of 1906, 34 Stat. 267, ch. 3335, §§ 3, 25 (June 16, 1906) (Oklahoma and Indian Territory, New Mexico, Arizona); Enabling Act of 1894, 28 Stat. 107, ch. 38, § 3 (July 16, 1894) (Utah).

9.) The School Aid Fund then provides a foundation allowance of $7,631 per pupil in the Baraga Area and L'Anse Area Schools, which serve both Indian and non-Indian children who live on or near the Community's reservation. (Ex. 10.) These figures are just an introduction to issues defense experts will address. Still, they demonstrate that one of the core concerns in *Warren Trading* – that states not economically burden people they abandon – is not relevant in Michigan.

2. *Central Machinery* applied a particularized inquiry.

Central Machinery does not support a categorical bar. There, the Bureau of Indian Affairs financed and approved the sale of eleven tractors to a tribal enterprise that farmed its reservation and trust lands. *See Central Machinery*, 448 U.S. at 161 and 165 n.4. The seller was not a licensed Indian trader and did not have a permanent location on the reservation. *Id*. But its "salesman solicited the sale of these tractors on the reservation, the contract was made there, and payment for and delivery of the tractors also took place there." *Id*. Arizona attempted to levy the same tax addressed in *Warren Trading* on the tractor sales. *Id*. at 164 n.3.

Considering the same state and same tax at issue in *Warren Trading*, the Supreme Court concluded that federal law preempted the tax even though the seller lacked an Indian trader's license and permanent on-reservation location. *See Central Machinery*, 448 U.S. at 165. As the Supreme Court explained, the Indian Trader Statutes were intended to "protect Indians from becoming victims of fraud in dealings with persons selling goods" and that purpose "would be easily circumvented if a seller could avoid federal regulation simply by failing to adopt a permanent place of business on a reservation or by failing to obtain a federal license." *Id*. at 165.

The Community seizes on statements in *Central Machinery*, 448 U.S. at 165, that the Indian Trader Statutes apply to non-resident Indian traders, regardless of whether traders have a place of business on a reservation and regardless of how the Bureau of Indian Affairs administers the Indian Trader Statutes. (PageID.1618.) But the Supreme Court was identifying two federal

interests that were specific to the case. *Central Machinery*, 448 U.S. at 163-65, and 164 n.4. The Supreme Court places *Central Machinery* in the same category as *Bracker*, using both as examples of the "'particularized' examination" that applies when "the legal incidence of the tax [falls] on a nontribal entity engaged in a transaction with tribes or tribal members." *Arizona Dep't of Revenue v. Blaze Const. Co.*, 526 U.S. 32, 37 (1999) (quoting *Ramah*, 458 U.S. at 838).

The facts of this case also lead to a different result than in *Central Machinery*. There are no allegations of potential fraud here. The Community does not express any need for the protections of the Indian Trader Statutes under regulations that the National Congress of American Indians has called "an anachronistic and patriarchal burden on [tribal] economic development." (Ex. 11.) Nor is there any reason to fear that allowing Treasury to tax the non-Indian retailers would undermine the Bureau of Indian Affairs' regulatory authority. Unlike in *Central Machinery*, there is no evidence that the Bureau of Indian Affairs financed or approved any of the retail sales that have been taxed. (Ex. 1, ¶ 53.)

There has also been a sea change in commerce since *Central Machinery*. As the variety of claims in this case demonstrate, tribes and tribal members now have vastly expanded options for purchasing goods and services through the mail, by telephone, and over the internet. Retailers like QVC and Walmart are not attempting to avoid regulation by the Bureau of Indian Affairs when they choose their business locations. Moreover, unlike Indian traders who are the sole source of goods and credit on isolated reservations, these businesses sell to the public at-large and have no reason to single-out tribes and their members for fraud or misconduct.

These changes in commerce are so dramatic that, on December 9, 2016, the Bureau of Indian Affairs issued an advance notice of proposed rulemaking seeking comments on "whether there is a need for updated regulations addressing a modern approach to the Federal role

concerning trade occurring in Indian Country." 81 Fed. Reg. 89,016. If there were any doubt that *Central Machinery* applied the test explained in *Bracker*, these changed circumstances weigh heavily in favor of declining to issue a declaratory judgment holding that Treasury is categorically barred from taxing Indian traders who sell to the Community and its resident tribal members inside Indian country. *See Wilton v. Seven Falls Co*., 515 U.S. 277, 286 (1995) (recognizing "unique and substantial discretion" under the Declaratory Judgment Act).

3. Other courts recognize that *Warren Trading* and *Central Machinery* do not create a categorical bar.

Other federal courts have rejected the invitation to interpret the Indian Trader Statutes as a categorical bar to state taxes. In *Dep't of Taxation & Fin. of New York v. Milhelm Attea & Bros.*, 512 U.S. 61, 65-68 (1994), the Supreme Court explained, "Although language in *Warren Trading Post* suggests that no state regulation of Indian traders can be valid, our subsequent decisions have 'undermine[d]' that proposition." *Id*. at 71 (alterations in original). Rather, the cases holding that states may require even Indian retailers in Indian country to cooperate in collecting lawful state taxes on non-Indians "requires rejection of the submission" that the Indian Trader Statutes prohibit "any and all state-imposed burdens on Indian traders." *Id*. at 74.

In *Mashantucket Pequot Tribe v. Town of Ledyard*, 722 F.3d 457, 469 (2d Cir. 2013), the Second Circuit concluded that the Indian Trader Statutes did not preempt "Connecticut's generally-applicable personal property tax" on slot machines. The Tenth Circuit has upheld both New Mexico's gross receipts tax on non-Indian contractors working on a reservation and Kansas' motor fuel tax on non-Indian wholesalers over Indian Trader Statute arguments. *See Sac & Fox Nation of Missouri v. Pierce*, 213 F.3d 566, 580-83 (10th Cir. 2000); *see id*. at 582 (discussing *Mescalero Apache Tribe v. O'Cheskey* (*en banc*), 625 F.2d 967, 968-69 (10th Cir.1980)). Other than its misreading of *Warren Trading* and *Central Machinery*, the

Community does not cite another federal court applying the Indian Trader Statutes as a categorical bar to taxing Indian traders.

4. A categorical bar on taxing Indian traders conflicts with *Bracker*.

The Community recognizes that there is no categorical bar against taxing Indian traders, which is why it argues that the Supreme Court "did all the preemption analysis in *Warren Trading* – balancing or otherwise . . . ." (PageID.1629.) But *Bracker*, 448 U.S. at 142, expressly rejected a "rigid rule . . . to resolve the question whether a particular state law may be applied to an Indian reservation or to tribal members." Using facts concerning Arizona and an Arizona tax to determine preemption in *all* other cases is not 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." *Id*. at 145 (emphasis added). Simply applying the result in *Warren Trading* elsewhere deprives other states like Michigan of having its own "interest in exercising its regulatory authority over the activity in question . . . examined and given appropriate weight." *Ramah*, 458 U.S. at 838.

Further, the Supreme Court decided both *Central Machinery* and *Bracker* on the same day. There is no reason to believe that the Supreme Court intended to adopt conflicting legal principles – a categorical bar versus a particularized inquiry – in those two opinions. The Community ignores this conflict, arguing that *Central Machinery* would have applied *Bracker* in that case if the Supreme Court intended for a balancing test to govern preemption for Indian traders. (PageID.1629.) While it would have been convenient if *Central Machinery* mentioned *Bracker* by name, the Supreme Court actually engaged in the preemption test *Bracker* describes. *See Blaze*, 526 U.S. at 37. Thus, Treasury properly applies the *Bracker* test when a non-Indian engages in taxable activities inside Indian country to determine whether federal law preempts the sales tax because federal law does not categorically bar the tax.

5. The Community's other arguments on this issue have no merit.

The Community highlights three claims that it says are representative of Treasury's refusal to recognize the categorical bar against taxing Indian traders that sell to the Community and its members inside Indian country. (PageID.1624-25.) For the reasons stated above, there is no such categorical bar against taxing these sales by non-Indian retailers. Because this motion does not seek summary judgment of any *Bracker* claims, Treasury preserves its arguments about why the balance of those interests allows it to tax non-Indian retailers that sell to the Community and its members within Indian country. But there are a number of other features of the Community's Indian trader arguments that require a short response here.

First, the Community argues that the sales tax sourcing statute, Mich. Comp. Laws § 205.69(1), determines whether a sale occurs inside Indian country. The legislature enacted the provision to implement a streamlining agreement among participating states. *See* Streamlined Sales and Use Tax Agreement, adopted November 12, 2002 as amended through October 11, 2017, art. 1, § 102, available at <https://tinyurl.com/y8xbfp3h>. The Community is not a participating state, and the sourcing statutes identify when a sale occurs *in Michigan*, not when a sale occurs in Indian country. (Exs. 12.s and 13.s.) Treasury correctly looks at the facts surrounding a sale to determine if it occurs inside Indian country and is subject to *Bracker*. *See Central Machinery*, 448 U.S. at 164.

Second, the Community argues that Treasury's "excuse for denying these claims is presumably its conclusion that the purchases were not made" for an essential governmental function. (PageID.1625.) Treasury properly uses the *Bracker* test to determine whether federal law preempts the sales tax on non-Indian retailers making sales inside Indian country because federal law does not categorical bar the tax. Even when the balance of interests favor the state, Treasury does not tax the sale of items the Community purchases for essential governmental

functions in recognition that a state may not infringe on a tribe's right to sovereignty and self-governance. *See Williams v. Lee*, 358 U.S. 217, 220 (1959). (Ex. 1, ¶ 15.) Recognizing this exemption is simply evidence of Treasury's good-faith compliance with federal law.

Third, the Community contends that Treasury has not applied the essential governmental function exemption in a consistent manner, such as when deciding a claim for a Tribal Center vehicle. (PageID.1625-1626.) What the Community fails to note is that it submitted multiple claims for vehicles purchased for the Tribal Center, including the same pickup truck it used to make multiple trips to Nebraska to purchase untaxed, unstamped cigarettes. (Ex. 2.A, claims # 1137, 1338, 1339; Ex. 14.s.) The Community submitted the refund claim for the new Tribal Center vehicle the same week it filed this lawsuit, raising questions about where and how it intended to use the vehicle. (Ex. 2.A, claim # 1338; Ex. 15.s; Ex. 16.) Treasury requested additional information concerning how the Community intended to use the new vehicle. (Ex. 16, p. 4.) The Community waited five months to respond; but when it finally confirmed that the new vehicle would be used for essential governmental functions (not a commercial purpose), Treasury issued a refund for this vehicle like other Tribal center vehicles. (Ex. 15.s, pp. 10-11; Ex. 16, p. 1.) Treasury treats essential governmental function claims consistently.

Finally, the Community alludes to claims it did not submit to Treasury. *Rising II*, 569 F.3d at 595, holds that unsubmitted claims are not ripe.

B. Federal law does not categorically bar taxing non-Indian lessors, and how Treasury applies its state law guidance is outside the scope of this litigation.

Treasury expressly recognizes that federal law preempts the use tax when it falls on the Community or its members for uses inside Indian country, which is why there are so few use tax claims in this case. (PageID.1702.) The Community leases certain items that it uses at its casinos or hotel inside its Indian country, such as restaurant equipment, that are ordinarily

subject to the use tax. *See* Mich. Comp. Laws § 205.95(4) (lessor may elect to pay the sales tax on the original purchase or the use tax on the rental receipts). (Ex. 2A, claim # 114.) However, Treasury denied a series of use tax refund or exemption claims on the basis that, even though the Community or a Member was exempt, the lessor remained liable for the tax. (PageID.1627.)

The Community, relying on *Central Machinery*, argues that federal law categorically bars Treasury from taxing the lessors. (PageID.1626-1627.) For all the reasons stated above, *Central Machinery* applied a particularized inquiry to the specific facts of that case and does not impose a categorical bar against taxing Indian traders who are lessors.

The Community also argues that Treasury's guidance interpreting the use tax prohibits Treasury from imposing the use tax on the lessor when the lessee is exempt from the use tax. (PageID.1626.) The Community is correct that Revenue Admin. Bulletin 2015-25 provides that a lessor is not liable for the use tax if the lessee is exempt. (PageID.1740.) Treasury inadvertently overlooked this guidance and Mr. Fratzke is taking steps to address this issue outside the lawsuit. (Ex. 1, ¶ 64.)

However, ordering relief concerning these claims is not within the scope of this litigation. There are no claims in the third amended complaint that challenge Treasury's administration of the use tax under state law. The court may not order a refund of any use tax a lessor paid on the leased property because retroactive relief may not be granted in a case against state officials in their official capacity. *See Edelman v. Jordan*, 415 U.S. 651, 666 (1974). Any additional action on these claims under state law must be undertaken by the Treasury, which is charged with collecting taxes, making it the real party in interest, but immune from suit. *See Pennhurst State Sch. & Hosp. v. Halderman*, 465 U.S. 89, 106 (1984); Mich. Comp. Laws § 205.1(1).

Treasury also respectfully maintains that the court should decline to decide any issue involving lessor liability under state law because it would reward the Community for refusing to avail itself of state law remedies that would have resolved this issue years ago. *See* Mich. Comp. Laws § 205.21 and § 205.22. Revenue Admin. Bulletin 1988-39, Treasury's predecessor guidance, stated the same position as Revenue Admin. Bulletin 2015-25. (Ex. 1.F.) Gamesmanship is the only reason a taxpayer would want Treasury to perpetuate an inadvertent error rather than quickly obtaining a refund by challenging the denials in an appeal.

II. Federal law does not categorically bar the use tax when the Community and its resident tribal members use tangible personal property outside the tribe's Indian country.

The Community argues that Treasury improperly levies the use tax on the tribe and its resident members for tangible personal property that is "principally housed, stored or garaged within the Reservation" without apportioning the use tax to apply only to uses that occur outside of its Indian country. (PageID.1629-1630.) This argument involves only the use tax because the legal incidence falls on the consumer (the Community and its members) and it does not have an apportionment provision that excludes use inside of Indian country. However, the Community cites cases that all involve annual personal property taxes in name or function, while the Michigan use tax is a one-time excise tax that Treasury collects only for items that the Community and its resident tribal members use in Michigan outside of the tribe's Indian country.

A. Federal law prevents states from levying annual personal property taxes on property owned by tribes and tribal members that is used both inside and outside of Indian country unless the tax is apportioned.

In *Moe v. Confederated Salish & Kootenai Tribes of Flathead Reservation*, 425 U.S. 463, 469 (1976), Montana imposed a personal property tax that applied to resident tribal members' vehicles and other property. The tax was levied annually based on the vehicle's assessed value. *See Confederated Salish & Kootenai Tribes of Flathead Reservation, Montana v. State of Mont.,*

Dep't of Revenue, 392 F. Supp. 1325, 1326-27 (D. Mont. 1975). Until the resident tribal members paid the annual tax assessed each January 1, they could not pay the vehicle registration fee to obtain Montana license plates. *See id*. at 1326; *see also Moe*, 425 U.S. at 469 n.9. The District Court concluded that the annual taxable event for the resident tribal members occurred on the reservation and, as a result, federal law preempted the tax. *Salish & Kootenai*, 392 F. Supp. at 1327. The Supreme Court in *Moe* referenced these facts without repeating them and agreed that federal law preempted the tax. *See Moe*, 425 U.S. at 468-69, 480-81.

Washington fared no better than Montana when it defended its vehicle excise tax in *Colville*, 447 U.S. at 140. Washington levied a vehicle tax annually based on a percentage of the fair market value of vehicles tribal members owned and used both on- and off-reservation. *See id*. at 142-43, 163. The Supreme Court agreed that Washington could tax a use outside Indian country, but held that federal law preempted the tax because it was functionally no different from the tax in *Moe*. *See id*. In other words, because Washington levied the tax annually based on a percentage of the fair market value of the vehicle, the state was necessarily taxing the vehicle for the entire year, including time inside of Indian country. In conclusion, the court added, "Had Washington tailored its tax to the amount of actual off-reservation use, or otherwise varied something more than mere nomenclature, this might be a different case." *Id*. at 163-164. Thus, the Supreme Court recognized that apportioning a personal property tax ***or*** levying a tax that functions differently from an annual personal property tax avoids federal preemption.

More than a decade later, in *Oklahoma Tax Comm'n v. Sac & Fox Nation*, 508 U.S. 114, 119 (1993), the Supreme Court considered Oklahoma's vehicle tax, which was calculated as a percentage of the value of the vehicle when title was transferred and the vehicle used in the state. Oklahoma levied the vehicle tax in addition to the sales tax and coupled it with an annual

registration fee. *See id.* at 119, 127. Oklahoma also required tribal members to register their vehicles with the state, which conflicted with the tribal law requirement that all tribal members who "live and garage cars" within the tribe's territory have tribal registration/plates. *See id.*

While a tribal member owned a vehicle, Oklahoma considered all taxes and fees that tribal members failed to pay as delinquent, i.e., still owed to the state. *See Sac & Fox*, 508 U.S. at 120. When a non-Indian acquired title to the vehicle and applied for a state title and license plate, Oklahoma not only collected the current taxes and registration amounts, but also required the non-Indian to pay all delinquent taxes, delinquent registration fees, and a penalty. *See id.* Oklahoma made no similar attempt to collect delinquent taxes and fees or to impose a penalty when persons transferred titles to vehicles that had been licensed in other states. *See id.*

Oklahoma attempted to distinguish its vehicle excise tax from a personal property tax by arguing that it "'resembles a sales tax'" and was imposed on all vehicles that use state roads. *Sac & Fox*, 508 U.S. at 126. But the Supreme Court rejected the argument, saying that, as in *Moe* and *Colville*, the Oklahoma "excise tax and registration fee are imposed in addition to a sales tax; the two taxes are imposed for use both on and off Indian country; and the registration fees are assessed annually based on a percentage of the value of the vehicle." *Id*. at 127-28.

B. Federal law does not preempt Michigan's use tax because it is substantively different from taxes that require apportionment to avoid preemption.

The Use Tax Act does not have language specifically apportioning the use tax for tribes and their resident members for tangible personal property used both inside and outside Indian country. But the Use Tax Act does not require that type of apportionment provision because it is substantively different from the annual personal property taxes in *Moe*, *Colville*, and *Sac & Fox*.

An excise tax conditions the right to engage in a privilege on payment of a tax and is not a property tax. *See Sullivan v. United States*, 395 U.S. 169, 175 (1969) (a tax on the "privilege

of selling or buying property . . . [is] distinct from a tax on the property itself"); *Mkt. Place v. City of Ann Arbor*, 351 N.W.2d 607, 611-13 (Mich. App. Ct. 1984) (how to determine if a tax is a privilege tax or property tax). The Use Tax Act describes the use tax as a "specific tax" levied "for the privilege of using, storing, or consuming tangible personal property in this state,"[4] which is an excise tax. Mich. Comp. Laws § 205.93(1); *Elias Bros. Restaurants v. Treasury Dep't*, 549 N.W.2d 837, 838 n.1 (Mich. 1996) (use tax is as an excise tax). The Michigan Supreme Court long ago determined that the use tax is not a property tax. *See Banner Laundering Co. v. Gundry*, 298 N.W. 73, 76-77 (Mich. 1941).

The Michigan use tax is a real excise tax. The Michigan constitution provides for ad valorem property taxes separately from the use tax and imposes different limits on them. *See* Mich. Const. 1963, art. IX, § 6 (property tax, limit on amount), § 8 (sales and use taxes, limit on rate). Michigan does not levy the use tax *in addition* to the sales tax with evidence that the sales tax was paid. *See Andrie*, 853 N.W.2d at 315; *see also WMS Gaming, Inc. v. Dep't of Treasury*, 733 N.W.2d 97, 99 (Mich. App. Ct. 2007) ("It is the use in Michigan that is taxed under the use tax, precisely because it is not subject to the sales tax."). Rather, the two taxes are intended to be complementary and supplementary. *See Andrie*, 853 N.W.2d at 321.

The use tax is missing elements that would make it function like a personal property tax. It is not calculated based on the value (fair market or otherwise) of the tangible personal property. The amount of the use tax is calculated as 6% of the "price" of the property. *See* Mich. Comp. Laws § 205.93(1). Nor is the use tax levied annually. The statutory definition of a use does not incorporate time or duration elements, which means it is levied only once at the time of the use in Michigan. *See* Mich. Comp. Laws § 205.92(b). The time element was critical

[4] The use tax also applies to certain services not relevant to this issue.

in *Moe* and other decisions that followed. Because Montana applied the tax annually, it was necessarily taxing some portion of the time that the tribes and resident tribal members used the property within their own Indian country. *Salish & Kootenai*, 392 F. Supp. at 1327. But a one-time tax applied to a use outside of Indian country does not tax uses inside of Indian country.

Treasury does not simply assume that property will be used outside of Indian country when deciding to approve or deny a use tax refund or exemption claim; it asks that exact question on its forms and the claimant must certify the answer. (PageID.1684, line 11 and part 3; PageID.1687, line 16; PageID.1688, part 4.) Except the claims involving the inadvertent lessor liability error, the party filing the claim expressly indicates that the item is used *outside* of the tribe's Indian country by checking a box marked "Other Michigan Location" on Treasury's forms before Treasury will deny a refund or exemption. (ECF No. 129, Sealed Exs. 14, 18.) Thus, Treasury takes care to tax a use only outside of Indian country.

These distinctions between the Michigan use tax and the taxes preempted in *Moe*, *Colville*, and *Sac & Fox* are not mere nomenclature. As a result, Treasury may tax those uses that occur outside Indian country without an apportionment mechanism in the Use Tax Act, as the Supreme Court recognized in *Colville*, 447 U.S. at 163-64.

C. The Michigan use tax as applied to vehicles does not raise the concerns regarding discrimination at issue in *Sac & Fox*.

While *Sac & Fox* addressed federal preemption, the Supreme Court also highlighted facts suggesting it was concerned the Oklahoma vehicle tax was discriminatory or infringed on the right of tribal self-government. *See Sac & Fox*, 508 U.S. at 120. But the Use Tax Act does not single out tribes or tribal members. Nor does Treasury attempt to collect the preempted use tax from a new owner. (Ex. 1, ¶ 17.)

Further, the Community has its own vehicle registration and titling programs. (Ex. 17, ¶¶ 5-9.) The Department of State and the Community have entered into reciprocity agreements so that vehicles with the Community's license plate may travel on state roads and vice versa. (Exs. 17.A and 17.B.) The Department of State also seeks to cooperate with the Community to transfer state and tribal titles. (Ex. 17, ¶¶ 6-7; Ex. 17.C.) There is no conflict between state and tribal law in this case. Thus, the additional concerns that the Supreme Court likely had in *Sac & Fox* do not exist in Michigan and do not dictate the same result here.

D. *Chosa* is not precedent and is not persuasive.

The Community argues that in *Chosa v. Michigan Dep't of Treasury*, Opinion and Judgment, Final Conclusions issued April 20, 2005 (MTT Docket No. 283437), the Michigan Tax Tribunal ruled in favor of its theory that the use tax cannot be levied on vehicles that its members purchase and "garage" inside Indian country. (PageID.1621, 1729-1734.) The Tax Tribunal's Small Claims Division issued *Chosa* and it has not been designated as precedent. *See* Mich. Comp. Laws § 205.765. Additionally, the Tax Tribunal lacks jurisdiction to decide constitutional questions and its decisions are not binding on courts. *See New Michigan, L.P. v. City of Norton Shores*, No. 294678, 2011 WL 744938, at *2 n.1 (Mich. App. Ct. Mar. 3, 2011); *Elec. Data Sys. Corp. v. Twp. of Flint*, 656 N.W.2d 215, 222 (Mich. App. Ct. 2002). Nor is *Chosa* persuasive, because it failed to address the principles discussed in this brief.

III. Treasury's refund and exemption system does not violate equal protection.

The Equal Protection Clause makes plain that no state may "deny to any person within its jurisdiction the equal protection of the laws." U.S. Const. amend. XIV, § 1, cl. 4. The Community argues that Treasury discriminates against Indians based on race when it requires the tribe and its members to seek a refund or exemption, rather than allowing them to use an

exemption certificate to assert their federal tax immunities. (PageID.1632.) However, the Community's legal analysis is wrong and its factual allegations unfounded.

A. The rational basis test, not strict scrutiny, applies to this issue.

The Community argues that the refund and exemption system is subject to strict scrutiny because it applies only to Indians and, therefore, constitutes a racial classification. *See Ondo v. City of Cleveland*, 795 F.3d 597, 608 (6th Cir. 2015) (discussing equal protection review). But in *Moe*, 425 U.S. at 479, the Supreme Court plainly stated that federal law treats tribes and their members differently, not because of race or discrimination, but due to their unique historical relationship with Congress. *See id*. at 479-80. The *Moe* Court then explained, "'As long as the special treatment ***can be tied rationally*** to the fulfillment of Congress' unique obligation toward the Indians, such legislative judgments will not be disturbed.'" *Id*. at 480 (quoting *Morton v. Mancari*, 417 U.S. 535, 555 (1974)) (emphasis added). That is a rational basis test.

The Community argues that a rational basis test does not apply because Congress did not create the refund and exemption system and states do not have the same historical relationship with tribes. (PageID.1633.) But Treasury has created the refund and exemption system solely to give effect to tax immunities the *federal* government recognizes. The refund and exemption system applies only to tribes and their members because there are no other similarly situated groups, i.e., groups with sovereignty and a history that entitles them to the same tax immunities.

Treasury has no role in classifying who receives federal Indian tax immunities. The federal government determines which groups are Indian tribes. *See* Federally Recognized Indian Tribe List Act of 1994, Pub. L. 103-454, 108 Stat. 4791 (November 2, 1994); *see also Kahawaiolaa v. Norton*, 386 F.3d 1271, 1273 (9th Cir. 2004) ("[A]n American Indian tribe does not exist as a legal entity unless the federal government decides that it exists."). Tribes determine membership. *See Santa Clara Pueblo v. Martinez*, 436 U.S. 49, 55 (1978). In the

cases discussed in this brief, the Supreme Court determined when tribes and their members are immune. Treasury merely recognizes those underlying federal and tribal decisions. The rational basis test applies here because Treasury has not defined a suspect (racial) class when adopting the refund and exemption system.

B. Treasury's refund and exemption system passes the rational basis test.

A plaintiff with an equal protection claim subject to the rational basis test must "demonstrate that government action lacks a rational basis" by negating "every conceivable basis which might support the government action, or by demonstrating that the challenged government action was motivated by animus or ill-will." *Davis v. Prison Health Servs.*, 679 F.3d 433, 438 (6th Cir. 2012) (internal citations and quote marks omitted).

Treasury's Form 3372 is a sales and use tax certificate of exemption that does not refer to race, tribes, or tribal members. Treasury created Form 3372 for the generally applicable statutory exemptions under the General Sales Tax Act and the Use Tax Act, which is clear from the fact that the categories on the form match exemptions in those two acts. *See, e.g.*, Mich. Comp. Laws § 205.54t and § 205.94o (industrial processing exemptions). Tribes and tribal members are entitled to use Form 3372 when they meet those generally applicable criteria for the statutory exemptions. (Ex. 1, ¶ 22.)

Treasury only requires non-agreement tribes and their members to use the refund and exemption system when asserting federal Indian tax immunities. A "governing decisionmaker [may] actually articulate at any time the purpose or rationale supporting its classification." *Nordlinger v. Hahn*, 505 U.S. 1, 15 (1992). Treasury provides the refund and exemption system for non-agreement tribes and their members for several rational, non-discriminatory reasons.

1. Multiple, rational bases support the refund and exemption system.

First and most importantly, the refund and exemption system provides Treasury equal

footing in sales and use tax disputes with tribes that have sovereign immunity from suit. *See Oklahoma Tax Comm'n v. Citizen Band Potawatomi Indian Tribe of Oklahoma*, 498 U.S. 505, 514 (1991) (state concerns with tax enforcement in the face of tribal sovereign immunity from suit). (PageID.1727-1728.) Non-agreement tribes lack an agreement with Treasury with a limited waiver of sovereign immunity. (Ex. 1, ¶ 26.) The refund and exemption system allows Treasury to review a claim that a purchase is immune from the sales or use tax before tribal sovereign immunity complicates collection or enforcement. (Ex. 1, ¶ 26.)

Second, the refund and exemption system avoids shifting the burdens of determining whether federal law preempts a tax to individuals at the point of sale. (Ex. 1, ¶ 27.) Treasury uses Form 3372 for generally applicable, statutory tax exemptions that apply statewide to all qualifying individuals and entities. Those exemptions require documentation, but no geographic determinations. Determining whether federal law preempts a state tax requires more than checking tribal identification cards and calling the tribe to find out if property is located on a reservation or trust lands, as the Community contends. (PageID.1635.) The federal preemption analysis requires understanding a host of legal principles and relevant facts. Contrary to the Community's argument, Treasury also has every reason to remain involved in determining whether to approve or deny a claim because of the variety of non-exempt claims it receives. (Ex. 1, ¶ 31.)

Requiring this complex analysis at the point of sale is too high a burden to place on retailers and sellers, particularly because the Community and Treasury do not agree on the scope of federal Indian tax immunities or other key issues, like how the Ceded Area should be treated. Placing retailers and sellers in this position would: lead to inconsistent administration of federal Indian tax immunities, as well as the sales and use taxes; increase the burden on Treasury to

interact with retailers and sellers confused about whether to accept an exemption certification; and deny Treasury its role in protecting state interests in collecting tax revenue. (Ex. 1, ¶ 27.c.) The refund and exemption system avoids these issues by centralizing exemption decisions in Treasury. *See Armour v. City of Indianapolis, Ind.*, 566 U.S. 673, 682 (2012) ("administrative considerations can justify a tax-related distinction").

Third, Treasury's refund and exemption system plays a valuable function in coordinating and relieving the administrative burdens of having multiple state agencies consider tax issues. Under the current system, Treasury makes all refund and exemption decisions. (Ex. 17, ¶ 3.) The Department of State simply relies on Treasury's exemption letter or collects a tax and leaves the tribe or tribal member to seek a refund from Treasury. (Ex. 17, ¶ 3.)

Fourth, allowing non-agreement tribes and their members to use exemption certificates would shift the burden to Treasury to find taxable sales and uses. (Ex. 1, ¶ 28.) That approach is impracticable given the number of retailers and sellers that sell or lease property to tribes and tribal members and the costs of pursuing small amounts of revenue. (Ex. 1, ¶¶ 28, 31.)

Fifth, Treasury would gain little or no efficiency in its own operations if non-agreement tribes and their members could decide where and when to use exemption certificates. Treasury may have to consider whether to continue to provide a refund system to refund a tax when retailers or lessors do not accept the certificates or when tribes and tribal members do not have an exemption certificate available at the time of a purchase. (Ex. 1, ¶ 30.)

2. The Community does not negate any of the rational bases or provide evidence of animus or ill will.

The Community does not attempt to negate any of these reasons why Treasury reasonably requires a refund and exemption system. Nor does the Community propose how it would address Treasury's concerns with its proposal to use exemption certificates. Instead, it

argues that other states allow tribes to use exemption certificates. (PageID.1635.) But whether other states choose to handle federal Indian tax immunities differently has no bearing on Treasury's reasonable basis for adopting its refund and exemption system to address circumstances affecting taxation in Michigan. (Ex. 1, ¶ 32.)

The Community has not provided any evidence that the refund and exemption system is "motivated by animus or ill-will." *Davis*, 679 F.3d at 438. The Community claims that Treasury does not "trust" Indians to use exemption certificates, "apparently because of their race or ethnicity." (PageID.1635.) The Community cites a single letter in which Treasury indicated its lack of "comfort" with exemption certificates without "adequate safeguards." (PageID.1728.) The paragraph is expressly discussing tribal sovereign immunity from suit, which makes a limited waiver of tribal sovereign immunity the missing safeguard for non-agreement tribes. (PageID.1727-1728.) (Ex. 1, ¶ 11.) That is not evidence of discriminatory animus.

Treasury does not require non-agreement tribes and its members to use the refund and exemption system because of a lack of "trust" in Indians. In fact, section XII of each of the tribal-state tax agreements trusts the tribe to choose whether to use an exemption certificate for the sales and use tax or to rely on a refund system, both for itself and its members.[5] (Ex. 18, pp. 24-27.) The Community had a tax agreement with Treasury that allowed it to use a tax exemption certificate from 1977 until the end of 1999. (Ex. 19, p. 7; Ex. 20.) The Community has simply chosen not to enter into a new tax agreement with Treasury, or it would have this same opportunity to use exemption certificates today. (Ex. 1, ¶ 13.) The refund and exemption system does not unlawfully discriminate against the Community and its members. The system is

[5] Treasury's Native American web page, <https://tinyurl.com/yblkneew>, has all ten tribal agreements, including amendments.

constitutional because it "rationally furthers the purpose[s]" Treasury has in collecting tax revenue when not preempted by federal law, while minimizing and coordinating administrative burdens. *Massachusetts Bd. of Ret. v. Murgia*, 427 U.S. 307, 314 (1976).

C. Treasury's refund and exemption system also passes strict scrutiny.

If the court were to apply strict scrutiny to the refund and exemption system despite the absence of a racial classification by Treasury, the system would still be constitutional. "Under strict scrutiny, the government has the burden of proving that racial classifications are narrowly tailored measures that further compelling governmental interests." *Johnson v. California*, 543 U.S. 499, 505 (2005) (internal citations and quote marks omitted).

Treasury has compelling interests in avoiding tax fraud and avoidance, and collecting tax revenue to provide services to its Indian and non-Indian citizens and businesses when not preempted by federal law. (Ex. 1, ¶¶ 28, 31.) Tribal sovereign immunity from suit and the difficulties of collecting the sales or use tax for many individual transactions and uses present objective challenges to collecting sales and use tax revenue. (Ex. 1, ¶¶ 26, 28.) But Treasury makes available a series of options and approaches to addressing these issues while also respecting federal Indian tax immunities. (Ex. 1, ¶ 56.) This system is a narrow alternative.

The Community merely argues that the refund and exemption system has a disparate impact. (PageID.1632-1633.) There is no disparate impact. Non-Indians lack federal Indian tax immunities, all federally-recognized tribes in Michigan may voluntarily choose to enter into a tax agreement with Treasury, and the non-agreement tribes and their members are treated equally in the refund and exemption system. (Ex. 1, ¶¶ 10, 20.) Moreover, "disparate impact" standing alone is not an equal protection violation. *Vill. of Arlington Heights v. Metro. Hous. Dev. Corp.*, 429 U.S. 252, 264-65 (1977). There is no evidence of discriminatory intent behind the refund and exemption system. *See City of Cuyahoga Falls, Ohio v. Buckeye Cmty. Hope Found.*, 538

U.S. 188, 194 (2003). As a narrowly tailored approach to furthering the state's compelling interests, the refund and exemption system passes even strict scrutiny.

IV. Treasury's refund and exemption system does not violate due process.

While the Community mentions due process, it never actually briefs what the Due Process Clause, U.S. Const. amend. XIV, § 1, cl. 3, requires. Similarly, the Community mentions that the system "burdens and discourages the Community and its Members from exercising a categorical federal exemption," without providing any precedent suggesting that any such burden is illegal. (PageID.1632.) Instead, the Community mischaracterizes the refund and exemption system and Treasury's decisions. The Community should not be permitted to raise new legal arguments and authority in its reply brief to fix these fatal errors while preventing Defendants from responding in writing.

A. The refund and exemption system does not impose excessive burdens.

The process and burdens argument that the Community raises appears to be grounded in Supreme Court precedent holding that states may use systems to collect lawful state taxes not preempted by federal law because they are not, themselves, a tax subject to the federal preemption framework. *See Moe*, 425 U.S. at 483. Though not a due process analysis, the Supreme Court has held that states may enlist both tribes and non-Indians in attempting to collect lawful taxes if the administrative burden is not so excessive that it interferes with tribal sovereignty and self-governance or violates a federal statute. *See Milhelm*, 512 U.S. at 73; *Colville*, 447 U.S. at 151 (discussing *Moe* and explaining that a state may "impose at least 'minimal' burdens on the Indian retailer to aid in enforcing and collecting the tax").

Treasury has successfully defended a refund system in *Rising I* for the tobacco tax, and in *Rising II* for the informal system for the sales and use tax system. The result should be no different in this case. This sales and use tax refund and exemption system is designed to collect

the sales or use tax when a taxable activity occurs in Michigan outside of Indian country, *Mescalero*, 411 U.S. at 148-49, or when those taxes are levied on non-Indians for activities inside of Indian country and the balance of interests permits the tax, *Bracker*, 448 U.S. at 145.

The burdens associated with this system are minimal. The tribe or member submits a short form to Treasury that collects information about the purchaser, item, seller, and where the sale or use occurs with a receipt. (PageID.1684; 1687-1688.) Treasury will also consider any information the tribe or member submits, even if not requested. (Ex. 1, ¶ 36.) By allowing exemptions (unlike the tobacco tax refund system), a tribe or member never has to pre-pay the sales or use tax. Every claim receives individual consideration and an answer from Treasury: a denial letter, an exemption letter, a letter requesting supplemental information, or a refund. (Ex. 1, ¶¶ 33-47; Ex. 2.A.) State law also provides procedures to challenge denials. *See* Mich. Comp. Laws § 205.21 and § 205.22.

Additionally, Treasury staff have helped the Community reconcile its own claim records with Treasury claim records on multiple occasions. (PageID.1727.) (Ex. 2, ¶¶ 24-27.) And while human and computer errors do sometimes happen, Treasury has worked to fix them. (PageID.1727.) (Ex. 1, ¶ 60; Ex. 2, ¶ 43.c.) Though more formal than the system considered in *Rising II*, the current refund and exemption system is still designed to evolve with federal law, to offer efficient alternatives where available, and to have enough flexibility that Treasury can respond to individual concerns about claims.

As the very large number of sales tax claims at issue in this case show, the Community and its members are attempting to market their tax exemption to non-Indian retailers liable for the sales tax. For instance, 773 (57.5%) of all the claims at issue in this case were bills from SEMCO, a non-Indian natural gas company located in the Lower Peninsula. (Ex. 2.A.) SEMCO

is liable for the sales tax and reimburses itself for the economic burden of the tax by passing that cost to purchasers. *See* Mich. Comp. Laws § 205.73(1). The Community members who received the bills gave them to the Community, which paid the bills. (ECF No. 129, Sealed Ex. 12, p. 8.) Paying bills for impoverished tribal members is laudable. But the state has a strong interest in preventing tribes from marketing tax exemptions to non-Indian retailers. *See Barona Band of Mission Indians v. Yee*, 528 F.3d 1184, 1193 (9th Cir. 2008).

Nor are all the claims charitable. The Community may submit a claim when it is trying to avoid a retailer's delivery fee,[6] buying a pickup truck to transport untaxed cigarettes within the state, or ordering pizza. (Ex. 14.s; Ex. 21.s, p. 13; Ex. 22.s.) Apparently, the Community has issued and tried to use its own exemption certificate and its members have tried to use Form 3372 to avoid the refund and exemption system. (Ex. 1, ¶ 51; Ex. 1B; Ex. 23.A; Ex. 24.) These are just a few examples of why the minimal burdens imposed by the refund and exemption system are necessary to protect Treasury's interest in collecting state taxes.

B. The refund and exemption system does not violate procedural due process.

The Due Process Clause protects substantive and procedural rights, which are "distinct" categories. *Cleveland Bd. of Educ. v. Loudermill*, 470 U.S. 532, 541 (1985). The Community makes no effort to brief whether it is raising a substantive or procedural due process claim, nor what substantive right might be implicated in the refund and exemption system. As a result, Defendants address this argument without conceding the right to respond to the Community's arguments, should they ever be clarified.

[6] Treasury issued an exemption letter for these two police vehicles when the Community restructured the transaction to occur on the reservation because Treasury recognizes that activities like policing are essential governmental functions. (Ex. 21.s, p. 1.)

It would be easy to assume that this is a procedural due process argument because taxation can implicate property rights. *See McKesson Corp. v. Div. of Alcoholic Beverages & Tobacco, Dep't of Bus. Regulation of Florida*, 496 U.S. 18, 36 (1990). But retailers pay the sales tax, which means the Community and its members have not been deprived of a property right. Further, the Community is not arguing for different procedures – it wants Treasury to have no procedures, leaving the Community and its members to assert tax immunities as they see fit with exemption certificates Treasury may never see. There is no due process right to a more favorable procedure. *See Heller v. Doe by Doe*, 509 U.S. 312, 332 (1993) (quoting *Medina v. California*, 505 U.S. 437, 451 (1992)) (due process does not "'require a State to adopt one procedure over another on the basis that it may produce results more favorable to'" the plaintiff). Still, Treasury provides a pre-tax exemption process, a post-tax refund process, and methods to challenge both decisions. That is all that procedural due process requires under these circumstances. *See McKesson*, 496 U.S. at 36-37 (for taxation, due process requires pre- or post-deprivation process).

C. The refund and exemption system is fundamentally fair.

As far as Defendants can tell, the Community simply argues that the refund and exemption system is unfair. *See, generally, Lassiter v. Dep't of Soc. Servs. of Durham Cty., N. C.*, 452 U.S. 18, 24-25 (1981) (due process analysis seeks to "discover what 'fundamental fairness' consists of in a particular situation"). But to make this argument, the Community mischaracterizes the system and how Treasury has handled its claims.

1. Due process does not prevent Treasury from using form letters.

The Community complains that Treasury's denial letters do not include an analysis under federal law for every claim. (PageID.1612.) The Community provides no authority for the proposition that due process requires Treasury to provide individualized letters or an extensive

analysis for each claim. Using form letters promotes efficient use of Treasury staff time, faster responses to claims, and consistency when deciding similar claims. (Ex. 1, ¶ 48.) Even the Community and the Members use form letters to submit claims to Treasury. (Ex. 5.s, p. 3; Ex. 6.s, p. 3; Ex. 22.s, p. 3.)

Treasury's form letters cite the Supreme Court case providing the relevant preemption test, which provides sufficient information for the Community and the Members to discern the basis for Treasury's decision. (ECF No. 129, Sealed Ex. 7, p. 2; Sealed Ex. 8, p. 2.) The form letters for a *Bracker* balancing test do not repeat all state, federal, and tribal interests Treasury has considered, but Treasury actually considers a range of interests. (Ex. 1, ¶ 41.) The Community's criticism is actually that the form letters do not reflect the tribe's different view of federal law, which is not a due process issue.

2. Treasury decisions are consistent.

The Community argues that Treasury decides claims involving purchases from out-of-state sellers inconsistently because it treats some as use tax claims and others as sales tax claims. (PageID.1614.) The Community contends that there are 53 claims from out-of-state sellers, but only 28 of those claims were treated as a use tax. In other words, the Community claims that 25 claims (1.8% of the total) were incorrectly deemed sales tax claims instead of use tax claims.

A seller's residency does not solely determine whether the sales or use tax applies. *See* Mich. Comp. Laws § 205.52(1) and § 205.93(1). Treasury has confidential information, such as information concerning retailer sales tax licenses, that can be relevant to analyzing where a retail sale occurs. (Ex. 1, ¶ 39.) Treasury cannot reveal that information when it denies a claim. *See* Mich. Comp. Laws § 205.28(1)(f). (Ex. 1, ¶ 49.) There are also statutory presumptions relevant to identifying a tax. For instance, Treasury categorized a Member's refund claim for purchasing "household items" from Walmart.com as a sales tax. (Ex. 2A, claim # 50; Ex. 30.s.)

Walmart.com is presumed to make sales at retail in Michigan because it sells similar product lines under a similar name here. *See* Mich. Comp. Laws § 205.52b(1)(a).

Treasury's summary chart and the two sets of Basic Queries demonstrate that Treasury decides like claims consistently. (Exs. 2.A, 2.B, 2.C.) Even if Treasury incorrectly categorized some claims, such a low error rate is not a constitutional flaw, especially because Michigan law provided an opportunity to challenge every one of those decisions.

3. Treasury responds to all claims.

The Community suggests that Treasury does not respond to all claims, which the Treasury Summary Chart demonstrates is clearly wrong. (Ex. 2, ¶ 27; Ex. 2.A.) For instance, the Community argues that Treasury did not decide 3 of its 6 claims involving purchases from American Hotel Registry. (PageID.1614.) The Community submitted 8 refund claims for purchases from American Hotel Registry, Treasury approved the refunds, and the Community has cashed the 5 warrants paying all 8 refunds.[7] (Ex. 26.s). The Community also received payments for 3 additional claims it says Treasury did not refund.[8] (Ex. 27.s)

Similarly, the KBIC Summary Chart lists 21 claims without a response.[9] But Treasury approved and issued a refund for 8 of those claims.[10] (Ex. 28.A.s – Ex. 28.H.s). Treasury denied 2 of the claims.[11] (Ex. 29.A.s and Ex. 29.B.s). Treasury has been waiting for additional

[7] Ex. 2A, claims # 1244, 1250, 1262, 1264, 1265, 1272, 1280, 1306.

[8] KBIC Summary Chart lines # 72, 75, 199.

[9] KBIC Summary Chart lines # 16, 142, 143, 146, 147, 148, 167, 168, 173, 216, 246, 275, 295, 389, 1117, 1161, 1267, 1269, 1273, 1328, 1333.

[10] KBIC Summary Chart lines # 16, 173, 216, 246, 275, 1267, 1269, 1273; Ex.2.A, claims # 22, 165, 209, 245, 264, 1244, 1262, 1265.

[11] KBIC Summary Chart lines # 389, 1161; Ex. 2.A, claims # 389, 1158.

information for 2 claims.[12] (Ex. 30.s). Treasury did not receive 9 claims, which Treasury would need proof of mailing to demonstrate that the claims were submitted.[13] (Ex. 2, ¶ 37.) The problem is the Community's record-keeping, not the refund or exemption system.

4. Treasury decisions are timely, and its response time is decreasing.

The Community also suggests that Treasury does not respond to claims in a timely manner. But the KBIC Summary Chart reveals that the Community calculates time from the date on a claim form, which counts any delay before a claim is mailed and the time it is in transit to Treasury. Sometimes months elapse between the date on a claim form and when Treasury receives the claim.[14] The Community also counts time Treasury waits for supplemental information and the time it takes to receive a refund warrant or check in the mail. Those figures do not provide an accurate picture.

The "Tax Policy Received Date" and the "Date Denial or Other Letter Sent" columns on the Treasury Summary Chart columns provide the information needed to calculate how much time Treasury takes to decide claims. Between 2012 and 2107, it took Treasury an average of 26 days to issue a denial letter. Looking at 2014 through 2017 cuts the average time for a denial to 16 days. In 2017, it took an average of just 3.225 days from the date that Tribal Affairs received the claim for Treasury to send a denial letter.

While Treasury has not been collecting the same timing data for individual exemption letters, they are typically issued within a few days of when they are requested. (Ex. 31.s.) Treasury also automatically adds statutory interest to refunds, which would compensate for any

[12] KBIC Summary Chart lines # 1117, 1328; Ex.2.A, claims # 1122, 1327.

[13] KBIC Summary Chart lines # 142, 143, 146, 147, 148, 167, 168, 295, 1333.

[14] Ex. 2A, claim # 22, 26, 37, 115, 212, 230, 231, 234, 235, 1122, 1125, 1137, 1138, 1139, 1260.

delay. *See* Mich. Comp. Laws § 205.23(3). Plus, the utility website and blanket exemption letters immediately recognize immunity without processing individual claims.

Treasury has encountered problems processing refunds. (Ex. 2, ¶ 43.c.) But Treasury responded to the problem and, after 2014, total processing time for claims was cut almost in half. (Ex. 2.C, table 6.) There have also been two recent changes that may improve refund processing time. In October 2017, the State of Michigan rolled out the Statewide Integrated Governmental Management Application (SIGMA), a new computer system that replaces the different financial systems state departments have been using for many years. (Ex. 1, ¶ 61.a.) Tribal Affairs has also hired a new analyst to work on issues (including refunds) involving both agreement and non-agreement tribes and their members. (Ex. 1, ¶ 61.b.) The Community has not demonstrated that the refund and exemption is fundamentally unfair.

V. If the court grants any portion of this motion, it should deny the Community further relief under 28 U.S.C. § 2202.

The Community has presumed to submit a severe proposed order that would: decide this motion; enjoin Treasury from enforcing its sales and use taxes; and require Treasury to take a series of affirmative steps to implement an exemption certificate system for the tribe and its members. Even if the Community prevailed, this relief is not automatically available. *See Steffel v. Thompson*, 415 U.S. 452, 467 (1974) (declaratory judgment is an alternative to injunctions). Indeed, further relief is discretionary and available only when a declaratory judgment has been granted discretionary, the relief is both "necessary and proper," and the court has granted notice and a hearing. 28 U.S.C. § 2202.

If the court grants any part of the Community's motion, entering the proposed order is neither necessary nor proper, and certainly not without notice and a hearing. Treasury has acted in good faith when interpreting and applying the Indian tax immunity cases. The issues

presented to the court in this motion are complex and have been waiting for clarification for many years. Treasury also intends to reassess the refund and exemption system in light of the court's ruling to ensure it is in compliance with federal law. (Ex. 1, ¶¶ 18, 24.)

CONCLUSION AND RELIEF REQUESTED

For the reasons stated above, Defendants respectfully request that the court deny the Community's motion for partial summary judgment and enter summary judgment in their favor on Counts I, V, VII, VIII, and the related portion of Count XVII seeking an injunction.

Respectfully submitted,

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