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No. 13-1032

In the

Supreme Court of the United States

DIRECT MARKETING ASSOCIATION,
Petitioner,

v.

BARBARA BROHL,
IN HER CAPACITY AS EXECUTIVE DIRECTOR,
COLORADO DEPARTMENT OF REVENUE,
Respondent.

On Writ of Certiorari to the
Tenth Circuit Court of Appeals

BRIEF *AMICUS CURIAE* OF MULTISTATE TAX COMMISSION IN SUPPORT OF RESPONDENT

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October 24, 2014

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BRIEF OF MULTISTATE TAX COMMISSION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONERS

INTEREST OF THE *AMICUS CURIAE*

Amicus curiae Multistate Tax Commission ("the Commission") respectfully submits this brief in support of the Respondent, Barbara Brohl, in her capacity as Executive Director of the Colorado Department of Revenue, urging this Court to uphold the decision of the Tenth Circuit Court of Appeals.[1]

The issue before the court is whether the federal Tax Injunction Act ("TIA"), 28 U.S.C. § 1341, bars this suit from being heard in the federal courts. The Commission urges the Court to affirm the Tenth Circuit's ruling on the grounds that the language of the TIA, properly read, reaches the circumstances in this case, and a ruling to the contrary would impose harmful consequences on state tax administration and enforcement. In addition, principles of comity compel the conclusion that the federal courts should not interfere with legitimate state efforts to impose information reporting laws critical to the operation of the states' revenue laws.

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[1] No counsel for any party authored this brief in whole or in part. Only *amicus curiae* Multistate Tax Commission and its member states, through the payment of their membership fees, made any monetary contribution to the preparation or submission of this brief. This brief is filed by the Commission, not on behalf of any particular member state, other than the State of Colorado. Finally, this brief is filed with the consent of the parties.

The Commission was established by the Multistate Tax Compact, which became effective in 1967. *See United States Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452 (1978)(upholding the validity of the Compact). Today, forty-seven states and the District of Columbia participate in the Commission as compact, sovereignty, or associate members.

The purposes of the Compact are to facilitate proper determination of state and local tax liability of multistate taxpayers, promote uniformity or compatibility in significant components of state tax systems, facilitate taxpayer convenience and compliance in the filing of tax returns and in other phases of state tax administration, and avoid duplicative taxation. *Multistate Tax Compact*, Art. I.

The Commission's interest in this case arises from our goal of preserving a critical component of state sovereignty, that is, the ability to have important matters affecting state tax systems and the enforcement and collection of state taxes adjudicated in the state courts.

SUMMARY OF ARGUMENT

The Commission urges this Court to hold that the TIA bars this suit. The TIA removes from the federal courts the jurisdiction to hear cases that would "enjoin, suspend or restrain the assessment, levy or collection of any tax under State law . . ." 28 U.S.C. § 1341. The TIA "serves to minimize the frictions inherent in a federal system of government." *Empress Casino Joliet Corporation v. Balmoral Racing Club, Inc.*, 651 F.3d 722, 725 (7th

Cir. 2011)(holding that the TIA barred a suit by private plaintiffs against a private defendant alleging violations of the federal RICO Act in obtaining tax benefits from the state). The TIA is so important as a protective measure that it has been held to apply even to indirect federal efforts to restrain state tax assessment *Blangeres v. Burlington Northern, Inc.,* 872 F.2d 327, 328 (9th Cir. 1989); *Sipe v. Amerada Hess Corp.*, 689 F.2d 396, 404 (3d Cir. 1982); *California v. Grace Brethren Church*, 457 U.S. 393, 412 (1982). This is because the TIA codifies a long-accepted doctrine of judicial comity which counseled federal courts to refrain from interfering with the fiscal operations of state governments where the federal rights at issue could otherwise be preserved unimpaired. *Boise Artesian & Cold Water Co. v. Boise City*, 213 U.S. 276 (1909).

Different types of taxes rely on different collection systems, which are often particularly suited to the thing or activity being taxed. Property tax liabilities, for example, become a lien against the property and are regularly collected by the sale of that lien to third parties or foreclosure by the government. *See* Frank S. Alexander, *Tax Liens, Tax Sales, and Due Process*, 75 Ind. L.J. 747 (2000). In the case of cigarette taxes, because direct collection of the tax from the consumer would be ineffective, the collection of the tax instead depends upon the requirement that wholesalers purchase tax stamps for placement on each individual package before shipment. Congress recently enacted legislation to aid the states in their collection efforts. *See* The Prevent All Cigarette Trafficking Act of 2009, Pub. L. No. 111-154, 2010 S 1147, 15 U.S.C. § 376.

The TIA's scope should be interpreted in the context of the applicable state tax systems it was intended to protect, not by reference to terms used in the Internal Revenue Code. Properly interpreted in this context, the TIA would bar jurisdiction in this case. Moreover, principles of comity and federalism support this construction.

Use of third parties to provide essential information for tax reporting, and to collect tax imposed on others, are hardly uncommon mechanisms for enforcement in many tax systems. It may be obvious, but is worth noting, that a third-party collection obligation is never imposed without some kind of corresponding requirement for information reporting; it is hardly useful for a third party to collect the tax unless it also provides information to the taxpayer and the tax authority about the corresponding tax liability and the payment made. Lawmakers could reasonably conclude that failure to impose effective tax collection and reporting requirements on third parties in many situations would be a disservice to taxpayers who voluntarily comply with the law. So, for example, employers are subject to withholding and reporting obligations on wage income under federal income tax laws. 26 U.S.C. § 3401(a).

Where withholding or collection of the tax is not feasible, research has shown that imposing an information-reporting obligation by itself will still increase tax collection. *See* Internal Revenue Service Tax Gap for Tax Year 2006 – Overview, Jan. 6, 2012, and IR-2012-4 (2012)(estimating the net misreporting percentage, or NMP, defined as the net

misreported amount as a ratio of the true amount, is 8% for amounts subject to substantial information reporting but no withholding, as opposed to 56% for income where no withholding or information reporting is required).[2] Again, this type of requirement typically involves information reported by the third party to both the taxpayer and the taxing authority. Where the taxpayer relies on the third-party information to voluntarily comply (that is, to self-assess), this information-reporting obligation is not merely helpful, but is *essential* for tax collection. For example, partnerships, while exempt from tax, must provide information to partners for computation of their own tax on their share of partnership income. 26 U.S.C. §§ 701-704 and § 6063. Corporations electing to be treated as exempt "Subchapter S Corporations" have a similar reporting duty which enables their shareholders to report and pay tax on "pass-through" income of the corporation. 26 C.F.R. § 1.6012-2(h).

While such third party tax collection and reporting mechanisms are common and sometimes essential to the effective enforcement of other taxes, general consumption taxes stand out in terms of their dependence upon third-party sellers to collect and report the tax. No government that imposes a general consumption tax has discovered a way to dispense with this mechanism.[3] Consumption taxes,

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[2] http://www.irs.gov/uac/The-Tax-Gap (last visited Oct. 22, 2-14).

[3] *See* Organisation for Economic Cooperation and Development, Consumption Tax Aspects of Electronic Commerce—A Report from Working Party No. 9 on Consumption Taxes to the Committee on Fiscal Affairs, February 2001, explaining the

by their nature, are imposed on the day-to-day purchases by individuals, virtually none of whom maintain detailed records of those purchases, and many of whom (*e.g.*, minors) could hardly be required to do so. Without this information, compliance and enforcement would be nearly impossible. But sellers do maintain detailed records of sales for all sorts of reasons, including federal income tax compliance.

The Respondents do not suggest that a general consumption tax would function without this seller-collection and reporting mechanism. It is therefore unremarkable that in this country, where the only general consumption tax is the sales and use tax imposed solely by state and local governments, the states impose collection and reporting obligations on sellers. It should be equally clear that when imposing an information-reporting requirement is an essential element of collecting the tax, to enjoin the imposition of that requirement is to enjoin the collection of the tax.

Colorado has adopted this reporting mechanism to aid in the collection of its sales and use tax impositions. Sellers who are "retailers" and are "doing business" in the state have a statutory tax collection and reporting duty under state law. COLO. REV. STAT. §§ 39-26-102, 39-26-105 and 39-36-204(2). Under this Court's holding in *Quill v. North Dakota*, 504 U.S. 298 (1992), Colorado may not apply this tax

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difficulties with alternatives to seller-collection of consumption taxes imposed on electronic transactions.

collection duty to certain of DMA's members if they lack the requisite "substantial nexus" with the state. *Quill*, 504 U.S. at 313. But the state asserts that it may, consistent with *Quill*, impose information-reporting requirements without the obligation to calculate, charge and pay over the tax. As the circuit court recognized, the information-reporting requirements at issue here are no less an element of the tax collection system. *Direct Marketing Ass'n v. Brohl*, 735 F.3d 904, 912-914 (10th Cir. 2013). Therefore, a case challenging these information-reporting requirements is a case seeking to "enjoin, suspend or restrain . . . collection of any tax under State law," in violation of the TIA's jurisdictional bar.

Not only does the TIA's own language support a conclusion that Congress removed the jurisdiction to hear this suit from the federal courts, but such a ruling will not lead to the slippery slope that DMA fears. Brief of Petitioner at 52-54. It is not necessary for this Court to rule that any suit that may negatively affect tax collection, however indirectly, is barred from federal court. The Commission does not suggest that the TIA would bar a federal suit brought by a plaintiff with only an indirect or incidental connection to a tax assessment, collection or reporting obligation. A ruling in favor of DMA would subject states to suit over a number of common information-reporting requirements that have been deemed to be essential enough to be applied broadly as part of the states' tax collection systems.

Principles of judicial comity and federalism also support upholding the decision of the circuit court. First, while the TIA is similar in structure and effect to the Anti-Injunction Act ("AIA"), 26 U.S.C. § 7421(a), it was motivated not just by the need to efficiently administer taxes and provide for resolution of tax disputes, but also by a respect for the sovereign authority of state governments and the need to protect their tax systems from undue interference if the states are to fulfill their role in our federal system. *Fair Assessment in Real Estate Ass'n, Inc. v. McNary*, 454 U.S. 100, 111 (1981). Second, the role of comity and federalism principles in interpreting the TIA is well established. *Levin v. Commerce Energy, Inc.*, 560 U.S. 413 (2010).

ARGUMENT

I. The TIA Bars Federal Court Jurisdiction to Enjoin Application of the Information-reporting Requirements Imposed Under Colorado Law Upon Retailers Who, But for This Court's Ruling in *Quill,* Would Also be Required to Collect the Tax.

Forty-five states and the District of Columbia currently impose a general sales tax. Jerome R. Hellerstein & Walter Hellerstein, *State Taxation*, ¶ 12.02 (3rd ed. 2001 & Supp. 2014-2). Only Alaska, Delaware, Montana, New Hampshire and Oregon have no state level retail sales and use tax, although several Alaska municipalities rely on local sales

taxes. *Id.* Unlike many other countries, the United States lacks a national consumption tax.[4]

The retail sales tax is one of the predominant sources of state and local revenue. According to the US Census Bureau, general sales and gross receipts taxes yielded $255 billion in state revenue in 2013.[5] Colorado received $2.4 billion from general sales and gross receipts taxes in 2013. *Id.* These amounts represent 30.1 percent and 21.5 percent respectively of U.S. total and Colorado state tax collections.[6]

This Court has long recognized that the use tax, a complementary tax to the sales tax imposed on the instate use of taxable goods purchased out of state and collected by the out-of-state seller, is integral to the ability of a state to successfully impose its sales tax.

> The practical effect of [a use tax] system … is readily perceived. One of its effects must be that retail sellers in [the taxing state] will be helped to compete upon terms of equality

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[4] *See* Tax Reform and Consumption-Based Tax Systems: Hearing Before the H. Comm. on Ways and Means, 112th Cong. (2011) [hereinafter Ways and Means July 26 Hearing] (statement of Prof. Michael J. Graetz, Columbia Law School).

[5] U.S. Census Bureau 2013 Annual Survey of State Government Tax Collections, http://govs015webdev/govs/ftp2/statetax/2013stcreport.pdf (last visited Oct. 22, 2014).

[6] 2013 State Tax Collection by Source, Federation of Tax Administrators, http://www.taxadmin.org/fta/rate/13taxdis.html (last visited Oct. 22, 2014).

> with retail dealers in other states who are exempt from a sales tax or any corresponding burden. Another effect, … must be to avoid the likelihood of a drain upon the revenues of the state, buyers being no longer tempted to place their orders in other states in the effort to escape payment of the tax on local sales.

Henneford v. Silas Mason Co., Inc., 300 U.S. 577, 581 (1937). *Accord*, *Felt & Tarrant Mfg. Co. v. Gallagher*, 306 U.S. 62 (1939).

Colorado, like the 44 other states that impose a use tax, finds itself confronted with a dilemma. In order for the tax to be effective, retailers must play a role in the collection of the tax. Setting aside the question of the requisite nexus that a state must have over an out-of-state seller, this Court has long recognized that states may impose a collection and reporting obligation on out-of-state retailers where that collection obligation is integral to the states' ability to enforce the tax. *Silas Mason*, 300 U.S. 577 (1937), *Felt & Tarrant*, 306 U.S. 62 (1939). While this Court has recognized that the states have both the need as well as the authority under the due process clause and the Commerce Clause to impose a tax collection obligation on out-of-state sellers when they sell into the taxing state, *Gen. Trading Co. v. State Tax Comm'n of Iowa*, 322 US 335, 338 (1944)(holding that "to make the distributor the tax collector for the State is a familiar and sanctioned device"), the Court has also found that the dormant Commerce Clause prevents a state from enforcing that collection obligation on a seller that lacks the

requisite nexus to the state. *Nat'l Bellas Hess Inc. v. Dep't. of Revenue*, 386 U.S. 753 (1967) and *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992).

The dissenting opinions in both *Bellas Hess* and *Quill* accurately predicted the negative consequences of the holdings in those cases. The dissent in *Bellas Hess* expressed concern that to relieve certain out-of-state sellers from any tax collection obligation would "burden and penalize" competing retailers who would bear that obligation, 386 US 753, 763 (Fortas, J., dissenting). The dissent in *Quill* further expressed concern that the rule in *Bellas Hess* created an "interstate tax shelter." 504 US 298, 329 (White, J., concurring in part and dissenting in part). These concerns are founded on the implicit understanding that vendors play a critical role in collecting the tax, even though the tax itself is imposed on the purchaser, and is based in the recognition that the inability to rely on the vendor for enforcement of the tax likely renders that tax uncollectible.

If the cause for these concerns was not already self-evident, the empirical proof to support them has been established in the intervening years since *Quill*. In 2009, Professors Donald Bruce, William F. Fox and LeAnn Luna estimated that state and local sales and use tax losses as a result of electronic commerce purchases would range from $11.4 billion to $12.65 billion annually, with six-year aggregate losses from $52 to $56.3 billion. D. Bruce, W. Fox & L. Luna, *State and Local Government Sales Tax*

Revenue Losses from Electronic Commerce, 52 St. Tax Notes 537 (2009).[7]

This case involves an attempt by Colorado to address the compliance problem created by the explosive development of so-called "remote" commerce, particularly electronic commerce conducted over the Internet.[8] Unable to compel both a tax collection and an information-reporting obligation on remote sellers (that is, sellers without the requisite nexus under *Quill*), the state instead seeks to require those remote sellers to provide information to their Colorado customers and to the state Department of Revenue regarding purchases that may be subject to tax. COLO. REV. STAT. § 39-21-112(3.5). The members of DMA challenge the state's constitutional authority to require such information. The state does not contend that DMA cannot maintain such a challenge. The state does assert, however, that such a challenge is barred from being

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[7] The difficulties of cross-border enforcement of consumption taxes are hardly confined to the United States. The Organization for Economic Co-operation and Development, has thoroughly studied the problem of cross-border collection of consumption taxes and has concluded that with respect to consumer transactions, there is no good alternative to seller-collected tax, recommending that governments instead take steps to facilitate simplified approach to seller registration and compliance. OECD, Consumption Tax Aspects of Electronic Commerce—A Report from Working Party No. 9 on Consumption Taxes to the Committee on Fiscal Affairs, February 2001.

[8] Thad Rueter, *E-retail Spending to Increase 62% by 2016*, InternetRetailer (Feb. 27, 2012), http://www.internetretailer.com/2012/02/27/e-retail-spending-increase-45-2016.

heard in the federal district courts pursuant to the TIA.

The TIA provides that "the district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of such State." *Id.* The TIA bars this action because it is a suit that clearly seeks to enjoin (in fact, has succeeded in enjoining) requirements essential to the collection of tax, and imposed only for that purpose, upon retailers who belong to the general class of persons charged with tax collection duties under state law. Nothing in this Court's decision in *Hibbs v. Winn*, 542 U.S. 88 (2004) or the decisions of the lower courts cited by DMA would support federal jurisdiction in this case. Moreover, a ruling in favor of Colorado will not unduly expand the TIA's jurisdictional bar as DMA claims.

A. The Colorado Information-Reporting Requirements are Within the Authority of the State to Impose and are Essential to Sales and Use Tax Collection.

The Colorado information-reporting requirements are imposed solely for the purpose of aiding tax collection. First, the statute requires non-collecting remote retailers to notify each Colorado purchaser at the time of a sale that, although the retailer does not collect the tax, the purchaser is obligated to self-report Colorado use tax. COLO. REV. STAT. § 39-21-112(3.5)(c)(I) ("Transactional Notice"). Next, the statute requires a non-collecting retailer to send an annual notice to all Colorado customers

whose total purchases for the prior calendar year exceeded $500 ("Annual Purchase Summary"). The notice must list the dates and amount of each purchase for the year, and must again inform the purchaser of the obligation to self-report any use tax that is due. COLO. REV. STAT. § 39-21-112(3.5)(d)(I)(A)-(B). Finally, the statute requires the retailer to file an annual report with the Colorado Revenue Department containing the name, billing address, all shipping addresses, and the total amount of purchases of each of its Colorado purchasers. COLO. REV. STAT. § 39-21-112(3.5)(d)(II)(A) ("Customer Information Report").

Colorado's notice and reporting requirements are a reasonable exercise of the state's authority under the due process clause, U.S. Const. amend. XIV. This Court has held that it would be permissible under that clause for a state to impose the obligation to collect its use tax on remote sellers who lack a physical presence in the taxing state, although the state was precluded from doing so under the facts of that case pursuant to the dormant Commerce Clause. *Quill Corp. v. North Dakota,* 504 U.S. 298 (1992). The due process clause would therefore also allow Colorado to impose the more burdensome collection and reporting obligations on the remote retailers that are required by use tax collection, including accounting to the state for the calculation of tax that is due, the payment of any tax refunds to the consumers, and for all applicable exemptions from tax and non-taxable sales for resale. *See* COLO. REV. STAT. § 39-21-110, COLO. REV. STAT. § 39-21-112(1)-(3), COLO. REV. STAT. § 39-21-105, and COLO. REV. STAT. § 39-21-204. This Court

has made clear that the due process clause is not violated if the government's inquiry is within the authority of the agency, the agency's demand is not too indefinite and the information sought is reasonably relevant. *U.S. v. Morton Salt Co.,* 338 U.S. 632, 652 (1950). The information-reporting requirements are therefore within the state's regulatory authority.

Colorado's notice and information-reporting requirements reflect the well-recognized fact that information reporting by third parties is the single most effective tool to increase tax compliance. As the IRS notes in a recent "Tax Gap" report, "[r]eporting compliance is highest where parties other than the taxpayer are required to file information reports …" *Update on Reducing the Federal Tax Gap and Improving Voluntary Compliance* (US Treasury Department, July 8, 2009), Jt. App.at 43. The IRS notes that receipt of a W-2 from an employer "can lead to significant administrative simplification" and reduce the employee's burden by eliminating the need to gather records or perform computations. *Id.* at 43. The IRS recently implemented two third-party reporting requirements that are strikingly similar to the requirements of the Colorado statute. Starting in January 2011, organizations that process credit and debit card payments for merchants must annually report the amount of these payments to the recipient businesses and to the IRS. *Id.* at 44. Also starting in January 2011, brokerage firms must annually report cost basis and holding period information to customers and to the IRS in addition to gross proceeds from securities transactions. *Id.* The IRS states that "[t]hese information reports will make it

easier for taxpayers to compute the net amount of gain or loss and will have a significant effect on reducing misreported capital gains." *Id.*

B. The Sellers on Whom the Information-Reporting Requirements are Imposed are Part of the Same Class upon Whom General Tax Collection and Reporting Obligations are Imposed Under State Law.

The TIA bars federal court jurisdiction over claims that would enjoin or restrain "assessment, levy or collection of any tax *under state law* . . ." The language of the TIA does not restrict this jurisdictional bar to suits brought by taxpayers challenging their own taxes. Assuming the information-reporting requirements at issue are contained within the terms "assessment, levy or collection," DMA cannot reasonably contend that this suit does not violate the TIA's jurisdictional bar by seeking an injunction to prevent the enforcement of the requirements.

By its own terms, the TIA requires that "collection" must be understood in the context of the tax system established under state law. In asserting that this action is not barred by the TIA, DMA relies on the meaning of the term "collection" as defined in the Internal Revenue Code ("IRC") and as used in the AIA, thereby eliding the essential difference between the federal taxes governed by the AIA and the state tax issues of use tax collection that are implicated in this case. Brief for Petitioner at 38. Although the TIA is modeled after the AIA, it is

inappropriate to apply the IRC definitions to state sales or use taxes because the concept of "collection" has a materially different meaning in the sales and use tax collection context than it does in the IRC.

The definition of "collection" in the IRC refers to the various administrative and judicial methods that the IRS can employ to collect a tax liability from the taxpayer. 26 U.S.C. §6301 *et seq*. While all states have statutory procedures that authorize the revenue department to obtain the recovery of unpaid taxes, in the context of a state sales or use tax, the term "collection" has a broader meaning than it does under the IRC. The sales and use tax is, in the first instance, generally collected not by the state directly from the taxpayer-purchaser, but by the retail seller. Therefore, the term must be understood as referring to the retailer's role in charging, collecting, reporting and paying over the tax from the purchaser, and should not be confined to the ultimate enforcement mechanisms all states employ to recover any unpaid tax liability.

In the TIA, Congress recognized the distinction between federal and state tax procedures by barring the federal courts from enjoining, suspending or restraining "the assessment, levy or collection of any tax *under State law* ….." (*Emphasis added*.) When used in reference to law, the word "under" is synonymous with "pursuant to." *Macmillan Dictionary*, (thesaurus entry for "pursuant to something").[9]

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[9] http://www.macmillandictionary.com/us/thesaurus/american/pursuant#pursuant-to-something_1 (last visited Oct. 6, 2014).

Under the plain meaning of the TIA the term "collection" is to be determined "pursuant to State law." This is entirely sensible. If the TIA is to protect state authority to collect tax against the potential interference of lawsuits in federal court, then it must protect the methods by which the tax in question is actually collected—not just the methods that potential plaintiffs might argue should be protected.

Retailers in Colorado are required to collect and report sales and use tax. COLO. REV. STAT. §§ 39-26-105 and 39-36-204(2). But retailers who do not collect the tax are required, instead, to comply with the information-reporting requirements at issue in this case. COLO. REV. STAT. § 39-21-112(3.5)(c). Colorado sales and use tax statutes define "retailer" as "a person doing business in this state, known to the trade and public as such, and selling to the user or consumer, and not for resale." COLO. REV. STAT. § 39-26-102(8). The term "doing business" is defined as "selling, leasing, or delivering in this state, or any activity in this state in connection with the selling, leasing, or delivering in this state, of tangible personal property by a retail sale" and includes, but is not limited to, "soliciting, either by direct representatives, indirect representatives, manufacturers' agents, or by distribution of catalogues or other advertising, or by use of any communication media, or by use of the newspaper, radio, or television advertising media, or by any other means whatsoever . . ." COLO. REV. STAT. § 39-26-102(3).

DMA's members who assert a claim against the information-reporting requirements are

"retailers" and part of the general class upon which a general tax collection and reporting burden is imposed. This Court's decision in *Quill* may prevent the state from imposing this statutory tax collection obligation upon remote retailers, but it does not change the nature of the retailer's role in making taxable sales into the state and their essential connection to tax collection under the state's sales and use tax system.

The use of state law to give specific meaning to the operative terms of the TIA is completely congruent with the intent of the drafters to limit access to the federal courts in cases that challenge state tax procedures. Brief of Petitioner at App. 4-11. Therefore, it is state law and not federal law that determines the operative terms of the TIA. And Colorado law clearly provides that it is the retailer who generally has a duty to collect Colorado use tax. Separately imposing a less-burdensome information-reporting requirement does not separate that requirement from collection.

In sum, the term "collection" in this context refers to the system employed under Colorado law that relies on retailers to obtain the tax from the purchaser, either through both direct collection and reporting, or through the providing of information that will allow enforcement of collection from the purchaser by the state.

C. While DMA Envisions an Attempt by States to Shield Regulatory Rules from Federal Court Review Under the TIA, it Cannot Dispute that the Requirements in this Case Are Essential and Integral to Tax Collection.

The federal courts are capable of discerning between state requirements that are an essential element of tax collection, while not comprising the act of collection itself, and those requirements whose inclusion in the tax code are mere pretext and done to avoid federal court jurisdiction. Colorado did not set out to design a sales and use tax reporting system which would avoid federal court jurisdiction over challenges to those requirements. This Court is capable of drawing clear distinctions between state requirements that are covered by the TIA's jurisdictional bar because they are integral and essential to collection under the given state's tax system, and ones that are not, without resorting to a cramped construction of the act's terms, which would ultimately undermine its purpose.

DMA *amici* also outline a number of examples of tax enforcement tools that they claim are beyond the scope of the TIA's ban but would nevertheless be included if this court were to uphold the circuit court's decision in this case. *See, e.g.*, Brief of *Amicus Curiae* The Institute for Professionals in Taxation at 17-19. Yet the *amici* do not cite some of the more prevalent types of information reporting done by third parties currently under both state and federal law, which are much closer to the requirements at issue here, and which would be subject to federal

court challenge if the circuit court's ruling is reversed.

One previously-mentioned example is the requirement that partnerships and Subchapter S corporations prepare information returns that are then used by partners or shareholders to report and pay tax on the income passed through to them. The partnership or "S corporation" is exempt from tax under federal law generally and usually has no withholding or tax collection duty. 26 U.S.C. §§ 701 and 1363. Under state law, partnerships and S corporations may or may not have a duty to withhold tax on income earned by partners and shareholders. Hellerstein, *State Taxation* ¶ 20.06[5][a]. But it should not be the case that where the information-reporting requirement is accompanied by a tax-withholding requirement, the TIA's jurisdictional bar applies, and where it is not, the bar does not apply. In both cases, the information reporting is essential to the ability of the taxpayer to comply and the third party, the tax-exempt entity, is in the class of persons on whom a collection duty might be generally imposed.

Some examples of statutory systems completely dependent on third-party reporting include liquor, tobacco and fuel taxes. For instance, in Arizona, reporting obligations are imposed on both distributors and wholesalers, although only wholesalers generally pay the tax. *See* ARIZ. REV. STAT. ANN. §§ 42-3352, -3353 and -3354. Imposing a reporting obligation on distributors helps to ensure that wholesalers are reporting all taxable sales.

Fuel taxes imposed by states on carriers operating in multiple states are another example of taxes dependent upon third-party reporting. The states have adopted a kind of clearinghouse system in which the taxes are reported and paid to a "base jurisdiction" (a single state in which the carrier operates) and that jurisdiction collects tax on behalf of all states and conducts audits of its own carriers. The states then exchange information about taxes collected from carriers and also exchange reports filed so that the taxes can be credited to the jurisdiction in which the carrier operated. This system is governed by a detailed agreement among the states that defines each state's obligations under the system in which they are collecting, not just their own taxes, but the taxes imposed by other states, and are requiring information returns from carriers so that other states taxes can be properly determined. [10]

What these examples show is that there are instances in which the information-reporting obligation imposed on the third party may not accompany an obligation to directly pay over tax to the state that imposes that tax, but which are still essential to the tax system's ability to operate. Moreover, these examples demonstrate why any definition of the TIA's terms must be flexible enough to accommodate how states actually impose and collect taxes under state law. It is not reasonable to

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[10] International Fuel Tax Agreement, *Articles of Agreement*, http://www.iftach.org/manuals/2013/AA/Articles%20of%20Agreement%20Complete%20Document%20-%20FINAL%20July%202013.pdf (last visited Oct. 20, 2014)

conclude that the only action that the TIA's bar protects is the transfer of funds for a payment of tax liability to the state. The requirements at issue here were imposed for the legitimate purpose of collecting state taxes and were within the state's authority to impose under the due process clause; the Petitioner does not contend otherwise.

D. Colorado State Law Provides a "Plain, Speedy and Efficient Remedy" As Required by the TIA.

Colorado allows a "plain, speedy and efficient remedy" by which DMA's members may challenge the constitutionality of the notice and reporting requirements pursuant to remedies "tailor-made for taxpayers." *Hibbs v. Wynn,* 542 U.S. 88, 107. The statute provides for penalties for failure to provide the required notice or reports, which penalties will not be imposed if the retailer shows reasonable cause for the failure to provide the notice or report.[11] The retailer can raise the issue of reasonable cause by requesting a hearing before the state Department of Revenue pursuant to COLO. REV. STAT. § 39-21-103(8)(c) ("The executive director may modify the …

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[11] COLO. REV. STAT. § 39-21-112(3.5)(c)(II) (failure to provide required notice to purchaser at time of sale subject to five dollar penalty for each such failure); COLO. REV. STAT. § 39-21-112(3.5)(d)(III)(A) (failure to provide annual purchase report to purchaser subject to ten dollar penalty for each such failure); COLO. REV. STAT. §39-21-112(d)(III)(B)(failure to file annual statement with Department of Revenue subject to ten dollar penalty for each purchaser that should have been included in the statement). In each such case, the penalty will not be imposed if the retailer shows reasonable cause for such failure.

penalty … questioned at the hearing and may approve a refund"). Taxpayers may appeal an adverse decision pursuant to COLO. REV. STAT. § 39-21-105.[12] Alternatively, the taxpayer and the executive director may agree that "a question of law arising under the United States or Colorado constitutions" may proceed directly to the state district court, thereby bypassing the administrative hearing. COLO. REV. STAT. § 39-21-103(4.5).

The "plain, speedy and efficient remedy" requirement is to be interpreted narrowly in order to give effect to the TIA's purpose of imposing "a broad jurisdictional barrier" that "limit[s] drastically federal district court jurisdiction to interfere with so important a local concern as the collection of taxes." *Arkansas v. Farm Credit Services of Central Arkansas,* 520 U.S. 821, 825 (1997). In view of the purpose of the TIA to drastically limit federal court jurisdiction in state tax cases, this Court can and should read Colorado's "reasonable cause" provisions as providing retailers a remedy to challenge the constitutionality of the statute. Colorado's tax procedures for challenging tax assessments, including the assessment of penalties, provide the taxpayer-specific remedies as required by *Hibbs*. Under those procedures, they may choose to pay the penalty and seek a refund, or to appeal from the assessment of the penalty *ab initio.* Alternatively, if the taxpayer and the Department agree, remote

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[12] As argued in more detail at 25, infra, DMA's members are taxpayers under Colorado sales and use tax law, although they cannot be compelled to collect Colorado use tax in the absence of nexus.

retailers may proceed directly to state court to litigate a constitutional issue. This is all the TIA requires.

E. Because the Retailers Represented by DMA are Responsible under State Law for Providing the Means of Collecting Tax from Purchasers, the Cases They Cite do not Support their Position.

Colorado's information-reporting requirements are integral to the assessment and collection of use tax under state law. Contrary to DMA's assertion that its member retailers who lack nexus in the state are merely "outsiders" to the tax system (Brief for Petitioner at 49), those retailers are and have long been members of the general class of retailers that are unquestionably not "outsiders," but are tax collectors as well as taxpayers pursuant to the Colorado use tax law. "'Taxpayer' means any person obligated to account to the executive director of the department of revenue for taxes collected or to be collected under the terms of this article." COLO. REV. STAT. § 39-26-102(17). Under *Bellas Hess* and *Quill*, Colorado may not apply this definition to certain retailers who do not have some physical presence in the state, but that does not change the nature of the retailer's role or its connection to tax collection under the state's sales and use tax system.

It is because retailers are not "outsiders" that this Court's opinion in *Hibbs v. Winn* does not govern this case. *Hibbs* was an Establishment Clause challenge to an Arizona tax credit that provided for contributions made to parochial schools.

The plaintiffs neither claimed an entitlement to the credit nor sought to decrease state tax revenues in any way. Indeed, had they been successful, state tax revenues would have increased. In contrast, DMA seeks to enjoin a requirement essential to tax collection which applies to retailers that fall under the general class of sellers that are tax collectors and taxpayers under Colorado law. If their action is successful, state tax collections will be adversely affected because purchasers will not have information necessary to report the tax and the state will lack the information necessary to identify Colorado consumers who did not pay tax on their purchases.

Similarly, *Florida Bankers Ass'n v. United States Department of Treasury*, ___ F.Supp. 2d______, 2014 WL 114519 (D.C. Cir. 2014) upon which DMA relies, is plainly distinguishable from this case because neither the payer banks nor the foreign depositors were United States "taxpayers" under the interest reporting requirement at issue in that case. The government sought information regarding interest paid to foreign depositors so that it would have information to trade with foreign governments for information regarding interest paid to American depositors overseas. The interest information regarding foreign depositors required by the IRS was extremely attenuated from the government's objective of increasing compliance by American taxpayers with American tax laws. In contrast, Colorado seeks information from out-of-state Colorado taxpayers without which it is virtually impossible for the state to identify Colorado

consumers and to increase self-reporting of the use tax.

This case is also distinguishable from *United Parcel Service, Inc. v. Florez-Galarza*, 318 F.3d 323 (1st Cir. 2003). As was true of the banks and the foreign depositors in *Florida Bankers*, UPS was not a taxpayer under the Puerto Rico excise tax scheme nor was it part of a general class of persons upon whom Puerto Rico relied for tax collection. As the Court noted, the case was not a "prototypical" Butler Act or TIA case because the Puerto Rico delivery ban "targets third parties instead of those who owe the tax." 318 F. 3d at 331. In contrast, DMA's members are part of the class of taxpayers who owe use tax under Colorado law, although those members are excused from actually collecting the tax pursuant to this Court's decision in *Quill*. Furthermore, the injunction sought by UPS to bar the state from enforcing the delivery ban left the state free to collect the tax from package recipients. *Id.* The injunction DMA seeks would make it impossible for the state to collect the tax from Colorado consumers because the state would not have the information necessary to identify those consumers and, if necessary, to initiate audits.

In contrast, in *Wells v. Malloy*, 510 F.2d 74 (2d Cir. 1975), the license suspension provisions were hardly necessary for the state to identify the taxpayer; the fact the state was suspending the license indicated the state already knew who the taxpayer was. The license suspension provision was thus merely an indirect method of coercing compliance. 510 F.2d at 77. Again, Colorado has no

way of identifying the Colorado consumers who purchased property from DMA's members without the information required by the notice and information statute.

II. Comity and Federalism Principles Underpinning the TIA Should Inform the Determination of How to Apply the Act to the Circumstances of this Case.

DMA describes the TIA as serving a similar purpose to the Anti-Injunction Act, which prohibits suits in the federal court for the purpose of restraining the assessment or collection of any tax. Brief for Petitioner at 5. DMA also contends that the meaning of the TIA is best understood in light of the language, interpretation and application of the AIA as well as other statutes, including the Butler Act, 48 U.S.C. § 872 (limiting federal court jurisdiction in certain suits against Puerto Rico), and the Johnson Act, 28 U.S.C. § 1342 (limiting federal court jurisdiction in certain suits involving state public utility commissions) *Id.* at 6. These comparisons, however, gloss over both the history of the TIA and its important purpose in preserving an essential element of state sovereignty.

It is true that both state and federal taxes are generally imposed by way of administrative processes and procedures designed to allow challenges by private parties against the government, while at the same time, preserving the need of the government to enforce the law efficiently and without undue interference or disruption. Preserving these administrative processes and

procedures, (requirements to pay over taxes and claim refunds) and the legitimate governmental imperatives they serve, is clearly one purpose for limiting federal district court jurisdiction, whether it be over federal tax matters, or state tax matters. *Hibbs v. Winn*, 542 U.S. 88, 103 (2004). But the history of the TIA demonstrates that federal courts had concerns not just over short-circuiting state administrative processes, but also over the appropriateness of their granting equitable relief in cases where state tax matters are concerned. Brief for Petitioner at App. 21-23.

Moreover, unlike diversity jurisdiction, which provides citizens of different states a forum in which their challenge may be heard without an advantage to either, whether real or perceived, a suit against a government, whether federal or state, implicates sovereign immunity from suit, which, while embodied in the Eleventh Amendment, pre-dates the Constitution.

A. The History of the TIA and its Basis in the Principles of Comity Support the Conclusion that its Jurisdictional Bar was Meant to Apply in Cases Where an Essential Mechanism of State Tax Collection is at Issue.

This Court has held that the TIA's bar was meant to encompass declaratory judgments, even though the text of the TIA is silent on the issue. *Great Lakes Dredge & Dock Co. v. Huffman*, 319 U.S. 293, 299 (1943). Although the Act speaks only of suits "to enjoin, suspend, or restrain the assessment,

levy, or collection of any tax," the Court held that the declaratory judgment procedure might, in "every practical sense" operate to suspend collection of the state taxes until the litigation is ended. Therefore, the same considerations that "led federal courts of equity to refuse to enjoin the collection of state taxes, save in exceptional cases, require a like restraint . . ." *Id.* The Court further concluded that there was nothing in the enactment of the TIA that indicated congressional disapproval of the policy that had been adopted by the federal courts at that time of refraining from the exercise of their equitable jurisdiction in state tax cases. *Id.*

The reluctance of federal courts to exercise their equitable jurisdiction "is of peculiar force in cases where the suit . . . is brought to enjoin the collection of a state tax" in federal court. *Matthews v. Rodgers*, 284 U.S. 521, 525 (1932). Indeed, federal courts have long recognized that state courts may provide adequate remedies for plaintiffs asserting a federal right, and that these rights may be preserved without the interference of federal courts. *Id.* at 526. Such recognition does not support DMA's claim that access to federal courts is a paramount interest where state fiscal matters are concerned, or that there is any justification for a lack of confidence in the ability of state courts to be neutral and fair in such cases. Brief for Petitioner at 54. Nor is this a case in which diversity jurisdiction is implicated. Accordingly, neither DMA's citation to Justice Story's Commentaries concerning Article III of the Constitution and the provision granting jurisdiction to federal courts in controversies between citizens of different states, nor its citation to Justice Marshall's

opinion in *Bank of the United States v. Devaux*, 9 U.S. (5 Cranch) 61, 87 (1809) is on point when the controversy is not with a citizen of another state but with the state itself. *Id*. at 55-56.

This Court has recognized that TIA is best understood as a "partial codification" of this doctrine of comity, expressing federal reluctance to interfere in state affairs. *Nat'l Private Truck Council, Inc. v. Oklahoma Tax Comm'n*, 515 U.S. 582, 590 (1995); *Levin v. Commerce Energy, Inc.*, 560 U.S. 413, 414 (2010). Principles of comity warranted dismissal of a federal lawsuit by Ohio taxpayers challenging the tax benefits received by competitors in *Commerce Energy*, based on three factors which are equally applicable here. First, the issue did not involve any fundamental right or suspect classification; second, the plaintiffs were seeking to improve their competitive position *vis-à-vis* other taxpayers; and third, state courts were better positioned than their federal counterparts to correct any violation. 560 U.S. at 431. As in *Commerce Energy*, DMA raises no issue involving a fundamental right or suspect classification. A decision in favor of DMA would allow it to maintain, unimpeded, a competitive advantage over in-state competitors who must collect tax. As Colorado points out in its Response, these same in-state competitors lack the access to federal courts when contesting whether and how the state may impose its collection and reporting requirements. Respondent's Brief at 43. DMA is certainly attempting to improve its competitive position *vis-à-vis* other retailers. And finally, it is certainly possible in any case challenging multiple requirements, such as this one, for a court to

determine that some portion of the requirements are invalid. This would require an exercise of discretion about how the rest of the statute's requirements may be implemented, which mitigates against bringing the suit in federal court, where the basis for exercising such discretion is lacking.

B. Principles of State Sovereignty Also Support the Conclusion that the TIA Applies in this Case.

States are not just sovereign in name. Rather, under our federal system of government, states retain a "substantial portion of the Nation's primary sovereignty, together with the dignity and essential attributes inhering in that status." *Alden v. Maine*, 527 U.S. 706, 714 (1999). The founders considered sovereign immunity from suit essential to our federal system. *Id.* at 715. State sovereign immunity from suit does not flow from the grant of some right by the national government, but was retained by the states in the formation of that government, and is embodied in the Eleventh Amendment to the Constitution. *Id.* at 721-723. As this Court explained about the Eleventh Amendment in *Seminole Tribe of Florida v. Florida*, 517 U.S. 44, 54 (1996):

> Although the text of the Amendment would appear to restrict only the Article III diversity jurisdiction of the federal courts, 'we have understood the Eleventh Amendment to stand not so much for what it says, but for the presupposition . . . which it confirms. That presupposition, first observed over a century ago . . . has two parts: first,

> that each State is a sovereign entity in our federal system; and second, that it is inherent in the nature of sovereignty not to be amenable to the suit of an individual without its consent. *Internal quotations and citations omitted.*

This Court has recognized that the Supremacy Clause and the Eleventh Amendment of the Constitution are in tension and has provided a means for suits in equity to be brought by a private citizen against a state official for the ongoing violations of federal law under the doctrine of *Ex parte Young*, 209 U.S. 123 (1908). *Virginia Office for Protection and Advocacy v. Stewart*, 131 S.Ct. 1632, 1637-38 (2011). Nevertheless, state sovereign immunity from suit as embodied in the Eleventh Amendment retains its vitality and the Court has rejected claims that Congress possesses the power to abrogate that immunity under the Commerce Clause. *Id*. Moreover, while the exception in *Ex parte Young* has persisted, this Court has also expressed concern over any expansion of that exception. *Id*. at 1648 (Roberts, C.J., dissenting). The TIA was passed in response to and provides a bar against the jurisdiction that might otherwise be asserted under *Ex parte Young*. *Rosewell v. LaSalle Nat. Bank,* 450 U.S. 503, 522 (1981); *Perez v. Ledesma*, 401 U.S. 82, 104-115 (1971). Therefore, the same respect for state sovereign immunity and the role of the states in our federal system that counsels against the expansion of the exception under *Ex parte Young* also counsels against any expansion of federal court jurisdiction to hear a suit challenging the application of a state tax collection requirement.

CONCLUSION

The Commission urges this Court to affirm the judgment of the United States Court of Appeals for the Tenth Circuit that the TIA bars this suit. A contrary holding would impose harmful consequences on state tax administration and enforcement.

Respectfully submitted,

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October 24, 2014