

FILED
COURT OF APPEALS
DIVISION II

2019 JAN -3 PM 3: 21

NO. 52349-3-II

STATE OF WASHINGTON

BY 
DEPUTY

COURT OF APPEALS, DIVISION II
OF THE STATE OF WASHINGTON

ARUP Laboratories, Inc.,

Appellant,

v.

State of Washington, Department of Revenue,

Respondent.

BRIEF OF APPELLANT

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ORIGINAL

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I. INTRODUCTION

This court must determine whether ARUP¹ Laboratories, Inc. (“ARUP”), Appellant, is taxable under the Washington Business and Occupations tax (“B&O tax” or “gross receipts tax”) on gross receipts that ARUP receives for laboratory testing services performed in the Utah for Washington customers. ARUP contends that it is not subject to the gross receipts tax on receipts that it receives from Washington customers. The State of Washington, Department of Revenue (“DOR”), Respondent, disagrees and successfully argued that DOR was entitled to summary judgment that ARUP is taxable. Judge James Dixon of the Thurston County Superior Court entered the order on summary judgement for DOR on August 20, 2018.

At the trial court, ARUP argued that the tax was not due for five reasons. First, ARUP is an integral part of the state of Utah and thus, for legal purposes, ARUP is an arm of the state of Utah. The applicable tax imposing section applies to “persons,” and states are not included in the definition of “person.” Consequently, the tax does not apply on its face.

Second, ARUP’s laboratory services relate to tangible personal property. The gross receipts from services related to personal property are

¹ Pronounced A-R-U-P.

where the personal property “is located or intended/expected to be used or delivered.” This rule derives from the DOR’s administrative rule. Thus, even if ARUP is taxable, the gross receipts are allocated to Utah where the personal property “is located or intended/expected to be used or delivered.”

Third, because ARUP is an integral part of the University of Utah and its Medical School (“Utah Med School”), WAC 458-20-167 (“Rule 167”) should apply to exempt ARUP. Rule 167 exempts public universities from the gross receipts tax. Under the full and faith and credit clause, Washington must afford the same benefit to Utah that it affords to itself.

Fourth, if Rule 167 is interpreted to apply to only Washington State-created public universities, then such interpretation violates the Commerce Clause, because it violates the “internal consistency” test. It violates the test because the in-state university and the out-of-state university are taxed differently. The impermissible result is in-state universities are always exempt and out-of-state universities are always taxed even though they may be engaged in the same taxable activities.

Finally, because ARUP is an arm of the state of Utah, Washington’s tax refund system unlawfully forces ARUP/Utah into its courts to protect Utah’s interests. Utah enjoys sovereign immunity from

another state's jurisdiction unless it has agreed to Washington's jurisdiction, which it has not.

ARUP contends that the trial court erred because any one of ARUP's five reasons was sufficient to deny summary judgment to DOR and grant summary judgment to ARUP.

II. ASSIGNMENT OF ERROR

A. Assignment of Error

On August 20, 2018, the trial court erred by granting summary judgment to DOR and denying summary judgment to ARUP.

B. Issues Pertaining to Assignment of Error

1. Did the trial court err when it determined that ARUP's Laboratory serviced did not relate to tangible personal Property under WAC 458-20-19402(303)(b)?
2. Did the trial court err when it determined that ARUP as a non-profit entity is a "person" for purposes of the B&O tax?
3. Did the trial court err when it determined Rule 167 did not apply to ARUP as an arm of Utah?
4. Did the trial court err when it determined that Rule 167 met the requirements of the four-prong commerce clause test?
5. Did the trial court err when it determined that ARUP was not an arm of the state and sovereign immunity did not apply?

III. STATEMENT OF THE CASE

A. What the trial court considered and its decision.

Judge Dixon read the file and heard oral argument. The court concluded that DOR's rule, WAC 458-20-19402(303)(b) ("Rule 19402(303)(b)"), did not apply because ARUP's laboratory services did not relate to tangible personal property. Report of Proceedings (RP) at 40 and 41. The court also noted that although ARUP is closely affiliated with "the Utah state institution," ARUP is a "person" for purposes of the B&O tax. RP at 40. The court also found that the four-prong commerce clause test² had been satisfied, so there was no impermissible discrimination. RP at 41. Finally, it found sovereign immunity did apply because ARUP was a non-profit "person" and not an arm of Utah. RP at 41. This appeal follows the court's decision.

B. ARUP's formation and business activity

1. ARUP's management and control

i. Associated Regional & University Pathologists, Inc.

In 1983, the Associated University Pathologists (AUP), a non-profit, created and was the 100% sole shareholder of Associated Regional

² See *Complete Auto Transit, Inc. v. Brady*, 430 U. S. 274, 279, 97 S.Ct. 1076, 1079, 51 L.Ed.2d 326 (1977) (*Complete Auto*)

& University Pathologists, Inc., a for profit corporation (“Associated”³). CP at 175. AUP started Associated with a loan from the University of Utah Hospital. CP at 175-176. Associated began operating as a pathology laboratory in 1984. CP at 39. During the 2002-2003 time frame, the university president decided to take direct control of Associated, eliminating AUP as the sole shareholder. The University made this decision because there was a view by “the university leadership that [AUP]” was unnecessary because “[Associated] was part of the university.” CP at 176. After the University dissolved AUP, Associated continued to operate as it always had. CP at 177.

ii. Creation of ARUP, Inc.

Utah statutorily created and controls the University of Utah (“University”).⁴ The Utah Med School is statutorily part of the University.⁵ The University is a “component unit”⁶ of Utah. When a

³ Associated is sometimes referred in the record as ARUP, because that was the acronym for Associated’s full corporate name. As explained in the brief, Associated was reincorporated as a non-profit entity and the University changed the name to ARUP. See THIRD recital in Amended and Restated Articles of Incorporation. CP at 443. For purposes of clarity and to eliminate any confusion, this brief addresses Associated Regional & University Pathologists, Inc. as “Associated” and the reincorporated entity as “ARUP.”

⁴ UT Code, 53B-2-101

⁵ UT Code, 53B-17-Part 9

⁶ “Component unit” is a financial accounting term. Amendment of GASB Statement No. 14. CP at 665.

“separate entity,” the University in this case, has a significant relationship with a government entity, then it requires Utah to report the University’s financials as a component unit of the state if the University “raises and holds economic resources for the direct benefit of a governmental unit” under GASB.⁷ The University’s 2017 Audit Report from the State Auditor provides that the University has such a relationship and is treated as a “component unit” of Utah.⁸ CP at 295. Further, ARUP is also treated as a “component unit” of the University.⁹ CP at 362. ARUP is a component unit of the University and the University is a component unit of Utah. This GASB financial reporting establishes that ARUP raises and holds economic resources for the direct benefit of the University, and the University raises and holds economic resources for the direct benefit of Utah.

The University incorporated ARUP and it is ARUP’s sole voting member.¹⁰ CP at 425. According to the ARUP 2017 Annual Financial Report (audit performed by independent auditors, Deloitte & Touche),

⁷ *Id.*

⁸ University of Utah 2017 Financial Report. See caption *Report on the Financial Statements*.

⁹ ARUP 2017 Annual Financial Report. See paragraph 1 “Significant Accounting Policies”, subparagraph “Organization”. According to the subparagraph “Basis of Accounting” in that same paragraph, ARUP’s audit was done in accordance with GASB.

¹⁰ Art. III., § 3.1, Restated By-Laws (2009)

both the Congressional Joint Committee on Taxation and the IRS ruled that ARUP has been an “integral part of the State of Utah” since its formation in 1984.”¹¹ CP at 363. To comply fully with the IRS letter ruling,¹² the University reincorporated Associated under the Utah Revised Nonprofit Corporation Act, creating ARUP Laboratories, Inc. CP at 443-447 (see Art. IV, CP 444-445).

1) The IRS Private Letter Ruling

The IRS issued its private letter ruling on April 6, 2001 wherein it exempted Associated from federal income taxes under 26 U.S.C. § 115.¹³ The IRS found that promoting “public health and support of medical facilities are well-established functions of state and local governments and are essential governmental functions.”¹⁴ It further found that ARUP’s activities “are educational” and that the “income ... derives from the provisions of services that are established functions of state and local

¹¹ ARUP 2017 Annual Financial Report, (see caption “Taxes:”),

¹² Associated represented to the IRS that it would amend its articles and by-laws to meet the requirements of IRC § 115. See fourth full paragraph on CP at 580.

IRC § 115 provides:

Gross income does not include—

(1) income derived from ... the exercise of any essential governmental function and accruing to a State or any political subdivision thereof

¹³ IRS Letter Ruling, CP at 579-582.

¹⁴ *Id.* at 582

governments.”¹⁵ Finally, it held that these “are essential government functions” for purposes of IRC § 115.¹⁶

2) ARUP's Management

The University is the sole member of ARUP.¹⁷ CP at 425. ARUP's “management and direction” is controlled by the Board of Directors who the University appoints as ARUP's sole voting member. CP at 425.

The Board of Directors consists of ten members of which three must consist of (a) representative appointed by the President of the University of Utah; (b) the Chairman of the University of Utah Department of Pathology; and (3) the President of ARUP.¹⁸ CP at 426. The majority of directors “shall be employees, officers, or trustees of the University of Utah.” CP at 427.

2. The University's purpose for creating ARUP

ARUP's by-laws provide specifically that its goal is to serve Utah and the University.¹⁹ CP at 424-425. ARUP's purposes are many but one is to engage “in and conduct[] the business of a general clinical and surgical pathology laboratory as deemed necessary by the Department of

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ Art. III, §§ 3.1 and 3.2, Restated Articles of Incorporation

¹⁸ Art. IV., § 4.2(a), Restated Articles of Incorporation

¹⁹ Art. I, Restated By-Laws

Pathology of the University to support, supplement, and enhance its educational mission.”²⁰ CP at 444.

ARUP’s discrete purpose is to generate a larger number of test samples to improve research and teaching at the Utah Med School. The Utah Med School’s pathology faculty members found that the school could not retain well-regarded pathologists, in part, because the school had an insufficient number of unique samples from which the faculty could do academic quality research. CP at 173-174. The Utah Med School settled on a plan: the more samples that the medical school could get, the better research and teaching that the faculty could do. *Id.* With a revenue stream from the pathologists’ services, the University could also afford to pay the faculty more money to stay with the school. *Id.*

As a result, ARUP became a national laboratory and its laboratory services consist of testing tissue and other human samples by applying pathology protocols that determine if the samples bear evidence of infections or other biological disorders. Regarding Washington, ARUP occasionally sent one or more employees into Washington who would call on the local Washington customers to explain the specimen collection

²⁰ Art. III § III a., Restated Articles of Incorporation

process or to encourage them to use ARUP, including training on collecting and transporting samples. CP at 125.

Once the customer collected the samples, they would have the same transported to Utah by air. CP at 78 and 79. ARUP performs all testing activities in its Utah laboratories; no testing activities occur in Washington. CP at 126-127. ARUP's only Washington activities include ARUP employees who establish or maintain business relationships with Washington medical facilities.

After ARUP completes the testing, ARUP stores the samples in its Utah facilities, securely protecting the samples from contamination or spoilage. CP at 83-84. Samples are not returned to Washington. CP at 136. In some cases, the samples must be retested. CP at 83-84. Once ARUP completes the testing, it then securely sends the results to its customer's location through the internet and the customer typically accesses the information through computer equipment. CP at 67-68; 136.

As part of the testing functions, ARUP has medical students and Utah Med School residents performing pathology activities at ARUP; they work under the supervision of "full pathologists or certified pathologists, board-certified pathologists." CP at 127-128.

IV. SUMMARY OF ARGUMENT

ARUP argues five theories. Any one of these five theories results in a summary judgment in ARUP's favor, rendering the decision by the trial court in error. First, ARUP is not a "person" under the state revenue act, and thus is not taxable. Second, even if ARUP is a person for purposes of the revenue act, DOR's Rule 19402(303)(b) applies, and all gross revenue is sourced to Utah under the applicable apportionment formula, removing the same from Washington's jurisdiction to tax. Third, if ARUP is a taxable person, then Rule 167 should apply to ARUP under the full faith and credit clause. Fourth, if the full faith and credit clause does not apply, then imposing tax on ARUP renders Rule 167 unconstitutional under the Commerce Clause. Finally, if the court disagrees that any of the forgoing theories eliminates the gross receipts tax on ARUP, then the court should afford ARUP sovereign immunity protection, because ARUP is an arm of Utah.

V. STANDARD OF REVIEW

The appellate court reviews summary judgment orders de novo, performing the same inquiry as the trial court. *Sheikh v. Choe*, 156 Wn.2d 441, 447, 128 P.3d 574 (2006). "Summary judgment is appropriate only if the pleadings, affidavits, depositions, and admissions on file demonstrate the absence of any genuine issues of material fact and that the moving

party is entitled to judgment as a matter of law.” *Sheehan v. Cent. Puget Sound Reg'l Transit Auth.*, 155 Wn.2d 790, 797, 123 P.3d 88 (2005).

VI. ARGUMENT

The neither the parties nor the trial court found genuine issues of material fact. Consequently, it is not disputed whether it was proper for the trial court to decide the matter pursuant to cross motions for summary judgment. However, ARUP asks this court to review the trial court’s decision to determine if it properly granted the DOR’s motion as a matter of law. ARUP contends that the court failed to apply the law properly based on the undisputed facts and, rather, it should have granted ARUP’s motion for summary judgment.

ARUP first addresses Rule 19402(303)(b), because if the court agrees that this section of the rule applies, then the other four theories do not need to be addressed. ARUP will then explain its other four theories, each as alternative arguments.

A. Under Rule 19402(303)(b), ARUP’s revenue should be sourced to Utah where it performs the testing services.

Rule 19402(303) is particularly important in this case, because it determines how much of ARUP’s income should be apportioned to Washington. The application of Rule 19402(303)(b) or (c) is critical to

determining how ARUP should be taxed under Rule 19402(303). These subsections explain *where* ARUP's revenue was earned.

In Rule 19402(303)(b)(i), the state sources revenue to the state where the customer received the benefit of the taxpayer's service. RCW 82.04.462(3)(b)(i). The total Washington-sourced revenue is the numerator and the total worldwide income is the denominator. RCW 82.04.462(3)(a). Thus, if Rule 19402(303)(b) is applied, then the revenue is sourced to Utah and the numerator decreases Washington's share of ARUP's revenue. If Rule 19402(303)(c) applies, then the revenue is sourced to Washington and the numerator increases Washington's share of ARUP's income.

The DOR improperly applied its own rule, and the trial upheld that mistake. ARUP performs testing services on blood, tissue and digital images at its business location in Utah. Specimen samples are carefully transported to Utah, where ARUP applies its professional skills and laboratory equipment to the specimen samples. ARUP is then able to determine medical abnormalities, helping the customer diagnose and treat the customers' patients. CP at 171-172. After the samples are tested, they are not returned to Washington. If specimens are not destroyed in the testing protocol, ARUP stores the specimen in Utah.

There is no doubt that the specimen samples are tangible personal

property for tax purposes. This is true, because the legislature provided a sales tax exemption for blood, tissue, or blood and tissue banks or sales of human blood, tissue, organs, bodies, or body parts for medical research and quality control testing. *See* RCW 82.08.02805 and RCW 82.08.02806, respectively. These exemptions are unnecessary if body tissue and fluids are not tangible property. Without these exemptions, sales of blood or tissue, as examples, would otherwise be subject to sales tax as tangible personal property.

Because the sample specimen constitutes tangible personal property, ARUP turns to Rule 19402(303)(b) to source its income. This rule explains how a taxpayer must source revenue to particular states for services related to tangible personal property. It provides:

(b) If the taxpayer's service relates to tangible personal property, then *the benefit is received where the tangible personal property is located or intended/expected to be located.* (Italics supplied.)

(i) Tangible personal property is generally treated as located *where the place of principal use occurs.* ... (Italics supplied.)

(iii) The following is a nonexclusive list of services that relate to tangible personal property: ... (D) *Testing of the tangible personal property...* (Italics supplied.)

Rule 19402(303)(b)(iii)(D) specifically states that testing of tangible personal property is a “service that relate(s) to tangible personal property.” That is precisely what ARUP does; it applies pathology tests to specimen samples to determine if the cells bear evidence of infections or other biological disorders. There could be no clearer application of the rule; ARUP’s service “relates to tangible personal property.”

The DOR and the trial court instead applied Rule 19402(303)(c) that provides:

If the taxpayer's service does not relate to real or tangible personal property, the service is provided to a customer engaged in business, and the service relates to the customer's business activities, then the benefit is received where the customer's related business activities occur. The following is a nonexclusive list of business related services: (i) Developing a business management plan; (ii) Commission sales (other than sales of real or tangible personal property); (iii) Debt collection services; (iv) Legal and accounting services not specific to real or tangible personal property; (v) Advertising services; and (vi) Theater presentations.

The court erred when it applied Rule 19402(303)(c) as the controlling provision because the trial court believed, without expressly stating, that the customers wanted the test results, not the testing. RP at 40. It is really a default position when the other provisions do not apply. The court should have applied the more specific Rule 19402(303)(b), not the more general Rule 19402(303)(c).

The trial court's application was wrong for many reasons. First, section (303)(c) can apply only if the service does not relate to real or personal property. Contrary to the trial court's conclusion, the services relate to tangible personal property. ARUP's services are meaningless if they are unrelated to the sample specimen. Without ARUP's services, no one would know if bacteria or a virus was present, or some other medical disorder existed with the sample. Simply put, the tangible sample is worthless if ARUP does not perform its service on that sample. "Where a general statute includes the same matter as a specific statute and the two cannot be harmonized, the specific statute will prevail over the general. *Residents Opposed to Kittitas Turbines v. State Energy Facility Site Evaluation Council*, 165 Wn.2d 275, 309, 197 P.3d 1153 (2008)." *AOL, LLC v. Dep't of Revenue*, 149 Wn. App. 533, 542, 205 P.3d 159, 163 (2009). Here, both sections of the rule could be said to apply, but the trial court applied the most general rule option. That general provision is that the revenue is sourced to the location where the customer's business activities occur. The specific provision is that if the services relate to tangible personal property, then the revenue is sourced to the location where the tangible personal property is located. Thus, the specific provision in Rule 19402(303)(b) should prevail over the general provision in Rule 19402(303)(c).

Second, viewing the list of activities to which Rule 19402(303)(b) applies, it specifically includes “testing”. Rule 19402(303)(b)(iii)(D) provides that “The following is a nonexclusive list of services that relate to tangible personal property: ... (D) Testing of the tangible personal property...”. The language is plain and broad; there is nothing in that language or section that excludes pathology testing of specimens.

Furthermore, after a careful look at Rule 19402(303)(c), the court can see that the listed services in the general rule relate to *intangible* personal property such as marketing plans, debt collection, sales commissions, legal and accounting services, advertising services and theatre presentations. There is nothing in Rule 19402(303)(c) about testing tangible or intangible personal property, and it simply has no application here.

Third, if these rule sections present ambiguity or conflict, then the court should consider the rules of construction. ARUP turns to the principle of *eiusdem generis* that provides:

The principle requires that general terms appearing in a statute in connection with precise, specific terms, shall be accorded meaning and effect only to the extent that the general terms suggest items or things similar to those designated by the precise or specific terms. *In other words, the precise terms modify, influence or restrict the interpretation or application of the general terms* where both are used in sequence or collocation in legislative enactments. The *eiusdem generis* principle may not apply automatically in every

problem of statutory interpretation where precise, specific words are followed by general words. 50 Am. Jur. 246, § 250.

State v. Thompson, 38 Wn.2d 774, 777, 232 P.2d 87, 89-90 (1951) (italics supplied).²¹

Applying this principle to Rule 19402(303)(b) and (c), the court must construe the meaning of the general term “service” and whether it relates to tangible personal property. That general term can be construed by the precise terms to “modify, influence or restrict the interpretation or application of the general terms.” Here, the examples of services that are not related to tangible personal property are those services that are intangible in nature, e.g., planning, sales, debt collection, legal and accounting services, advertising and theater performance. They should influence the rejection of Rule 19402(303)(c) as the guiding provision because ARUP’s services **do not** relate to intangibles.

Because the customers want ARUP to test the sample specimen, Rule 19402(303)(b) has direct application. Applying this statutory construction principle to that rule, the question would then be whether ARUP’s services are related to tangible personal property. The precise term of “testing of the tangible personal property” influences the

²¹ Accord *Simpson Inv. Co. v. Dep't of Revenue*, 141 Wn.2d 139, 3 P.3d 741 (2000); *State v. K.L.B.*, 180 Wn.2d 735, 328 P.3d 886 (2014)

interpretation or application of the general term of “service relates to tangible personal property.” Instead, the trial court applied Rule 19402(303)(c), concluding that the benefit of the service was Washington where ARUP’s customer conducts business. RP at 40.

With all due respect to the trial court, its failure to apply Rule 19402(303)(b) in this case would render testing irrelevant for any purpose. This is true because in every case, when a customer hires a service provider to test tangible personal property, the customer will always want the test results where its business activities occur. No one would hire a service provider to test tangible personal property and then tell the provider not to share the results with them. That would appear to be the only time when that provision could ever apply, and it is absurd to suggest that is the likely intention of the customer. The well-settled principle of statutory construction is that the court should construe the law to give effect to all language. “We must construe statutes to give effect to all of the language and to render no portion meaningless or superfluous.” *AOL* at 542,163 (2009); *State v. J.P.*, 149 Wn.2d 444, 450, 69 P.3d 318 (2003). Thus, sourcing to Washington ignores the plain language of Rule 19402(303)(b) and reaches an absurd result.

Applying these principles to ARUP, because (1) the specimen is tangible personal property and (2) ARUP’s testing relates to tangible

personal property that is located, or expected to be located in Utah when principally used by ARUP in laboratory testing service, ARUP's service benefits its customers in Utah where the tangible personal property is located when it is tested. There is no intention or expectation that the tissue, blood or digital images will be ever be in Washington after ARUP performs its services un Utah.

There is no doubt where the tangible personal property will be used, and that is where the testing occurs in Utah. And there is no doubt where that tangible property will be in the future; it is either destroyed in the testing in Utah or it is locally stored at ARUP facilities in Utah. Under this rule, all income is sourced to Utah and the apportionment formula should reflect that conclusion.

To summarize, ARUP contends that the DOR improperly applied its own rule. ARUP performs testing services on blood, tissue and digital images at its location in Utah. Specimen samples are carefully transported to Utah. Applying its professional skills and laboratory equipment to the specimen samples, ARUP can determine medical abnormalities, helping the customer diagnose and treat the customers' patients. After the samples are tested, they are not returned to Washington. If specimens are not destroyed in the testing protocol, ARUP stores the specimen in Utah. There should be no doubt that the specimen samples are tangible personal

property for tax purposes and ARUP's services are related to tangible personal property. Summary judgment should have been granted to ARUP, not the DOR, and the trial court's decision should be reversed with directions to grant ARUP's motion for summary judgment.

B. The B&O Tax Applies Only to "Persons"; Utah is not a "Person" and ARUP is arm of Utah.

Alternatively, ARUP contends that the gross receipts tax does not apply to it, because ARUP is an arm of Utah. The service B&O tax applies to "every person". RCW 82.04.290(2). The B&O tax chapter defines "person." Conspicuously missing is the word "state." RCW 82.04.030. Thus, this statute is more important for what it does not say than for what it does say, because only "persons" are subject to tax, and if ARUP is an arm of Utah, then the four additional arguments made here after are relevant. If the court affirms the trial court that ARUP is not an arm of the state, then the four additional theories fail. Therefore, the critical question is whether ARUP is an arm of Utah. The trial court did not explain why ARUP was not an arm of Utah or distinguish ARUP from the entities described below in two Washington cases, holding that Harborview Hospital and the Association of University Physicians were arms of the state. RP at 40.

1. ARUP is an arm of the state and is not within the definition of “person” for tax purposes.

Utah created and controls the University and Utah appoints eight of the ten members of the Board of Trustees for the University. Two trustees are (1) the president of the university’s alumni association and (2) is the student body president. The Utah Med School is statutorily part of the University.

The University controls ARUP. The University is the sole member of ARUP. ARUP’s “management and direction” is controlled by the Board of Directors appointed by the University. A majority of the board members “shall be appointed from officers, employees, and trustees of the University”.

ARUP’s staff exceeds 3,000 employees of which at least 80 are medical directors. CP at 149. These medical directors are Utah Med School faculty members who are employed by the University. ARUP reimburses the University for their wages. *Id.*

ARUP’s budget is approved by either the University’s president or the University’s vice president for health sciences. CP at 250-251. Although ARUP’s audited financial statements are separately published, ARUP’s audited financial statements are reported to the University. In turn, the University consolidates ARUP’s audited financial information as a “component unit” of the University in its own financial statements under GASB.

ARUP's financial statement is also audited by independent auditors, Deloitte and Touche, LLP. The 2017 report describes the reasons why the University includes ARUP's financial report:

... Because the University appoints the majority of the two boards, is able to impose its will on these organizations, and the organizations almost exclusively benefit the University, the financial accountability criteria as defined by Governmental Accounting Standards Board (GASB) Statement No. 61, have been met and the two organizations are included as blended component units of the University. The component units of the University are ... ARUP Laboratories, Inc. (ARUP). Copies of the financial report of each component unit can be obtained from the respective entity. (Italics supplied.)

CP at 313 (under caption "A. Reporting Entity").

All net income accrues to the University and any "surplus funds from operations are paid to the University" and "shall be used for the educational mission of the University." CP at 445. The University determines the amount of the funds that will be distributed to the University from ARUP's surplus and how much it can keep growing the testing activities. CP at 160. ARUP's budgets are scrutinized, adjusted, and approved by the University. CP at 250.

To summarize, Utah created the University, the University created ARUP and is its sole member. The University controls the ARUP board members, the University is "able to impose its will on" ARUP, and ARUP "almost exclusively benefit[s] the University." ARUP's budget is approved by the University, adjusted by the University, and financial results are rolled up into the University's budget, as a "component unit" of

the state. There is no third party that is involved in the management and operation of ARUP. ARUP's budgets are approved by the University and any surplus funds go to the University for its educational mission. Thus, ARUP is more than "closely affiliated" with Utah as found by the trial court (RP at 40), ARUP acts by decision-makers appointed by Utah.

Further, any liability for ARUP's actions is divided into two categories. Utah covers the clinical staff (the about 80 or so medical directors who are part of the University faculty) from a state fund. CP at 253. ARUP covers the general medical liability for the technical staff (the people who prepare slides, physically perform lab tests, and conduct other testing processes). *Ibid.*

As for the University's purpose for ARUP, it is education; ARUP's goal is to locate as many unique specimen samples as possible. CP 248-249. Increasing the volume of samples increases the likelihood of getting a unique specimen. *Ibid.* The unique specimen provides greater chance for research and development (*e.g.*, new testing procedures), teaching, and publishing. *Ibid.*

This evidence definitively supports that (1) ARUP is performing a government function for Utah, (2) is operated and managed by Utah, and (3) provides no public benefit. Consequently, ARUP is an arm of Utah and is afforded the same status as Utah.

2. Washington case law supports ARUP's position that it is an arm of the state.

Washington's case law explains that an entity affiliated with the state is an arm of the state when it is "operated and managed" by the state. In a 1986 case involving tort claims, the Washington Supreme Court said:

The trial court found, based upon uncontroverted evidence, that Harborview is operated and managed by the University of Washington and all of its employees are employees of the University. *See also* RCW 36.62.290. Because the University of Washington is a state agency, Harborview, as operated and managed by the University, is an arm of the state. Its employees are state employees and claims against the University's operation at Harborview are paid from a fund held by the State Treasurer. *See* RCW 28B.20.253. It is clear that, in the context of this case, a § 1983 suit against Harborview is in legal effect a suit against the State and cannot, therefore, be maintained.

Hontz v. State, 105 Wn.2d 302, 310, 714 P.2d 1176, 1180 (1986).²² In this case, the court found that the Harborview Medical Center ("Harborview") employees and claims were paid from the state treasury and this was sufficient proof of the University of Washington's operation and management of Harborview. According to Harborview's website,²³ King County owns the hospital but has an agreement for the University of Washington to operate it:

In 1877, Harborview was founded as the six-bed King County Hospital in South Seattle. UW Medicine's management of Harborview has enabled the hospital to become a leading academic

²² See also *Houghton v. Board of Regents*, 691 F.Supp. 800 (1988), finding that the Burke Museum was an arm of the state because it was managed and operated by the University of Washington.

²³ From the UW Medicine website, <https://www.uwmedicine.org/harborview/about>, last viewed January 3, 2019.

medical center, ... UW Medicine physicians and staff continue to expand specialty care services based at Harborview with national experts in the centers of emphasis.

Harborview acts as an arm of the state as “a leading academic medical center” through the University of Washington’s operation and management.

Like Harborview, ARUP is part of a leading academic medical center and has a teaching function for the University, attracting a high volume of specimen, and hopefully, a higher number of unique specimens. Like Harborview, the clinical staff are employees of the University and the clinical staff, to the extent they create liability, the State of Utah uses its funds to pay any liability. Unlike Harborview that is owned by King County, the University is ARUP’s sole member and the University determines who is on the board King County determines Harborview’s Board, there’s no requirement in the UW Medicine By-Laws that any University of Washington employee be a Harborview trustee (CP at 633-655)), and all surplus funds belong to the University. Unlike ARUP, Harborview’s financial reporting is not part of University of Washington but is part of the King County reporting, according to the University of Washington.²⁴ CP 617. Thus, the Utah Med School and Utah exercise even more control over ARUP than the University of Washington does over the

²⁴ The Harborview Board of Trustees “determines major institutional policies and retains control of programs and fiscal matters.” See Note 13, Related Parties, CP 617, last viewed July 5, 2018. All of Harborview’s revenues and expenses are not recognized by the University of Washington in its financial statements, however some financial information is included. *Id.*

King County-owned Harborview.

Similarly, in 2015, the court entertained a medical malpractice case against the Association of University Physicians (“UWP”) and relied on the analysis from the *Hontz* case, as follows:

Generally, an entity operated and managed by a state agency for a state purpose is considered an arm of the State. For example, in *Hontz v. State*, the court recognized that for purposes of immunity from 42 U.S.C. § 1983 civil rights lawsuits, Harborview ‘Medical Center’ ‘is an arm of the State’ because it is operated and managed by UW, a state agency. (Footnote omitted.) The court concluded, “It is clear that, in the context of this case, a § 1983 suit against Harborview is in legal effect a suit against the State and cannot, therefore, be maintained.” (Footnote omitted.)

Hyde v. Univ. of Washington Med. Ctr., 186 Wn. App. 926, 930, 347 P.3d 918, 920 (2015).

The *Hyde* court looked at UWP’s articles of incorporation, bylaws, and operating agreement with the university, how it was owned and operated, how its income was distributed, and whether the UWP faculty would be deemed employees and agents of the University of Washington for professional liability purposes in determining UWP’s status as an arm of the state.²⁵

UWP’s purpose, in part, is to provide “additional sites of primary care practice and training for faculty, residents and students.”²⁶ CP at 601.

²⁵ *Hyde* at 931.

²⁶ “UW Medicine Neighborhood Clinics” (at bottom page)

Based on these facts, the court held that the University of Washington's operation and control of UWP made UWP an arm of the state.

The UW Medicine Board, created by the University of Washington Board of Regents, has responsibility for "planning and delivery of medical services, including oversight of physician services provided through the UWP."²⁷ CP 639. The UW Medicine Board has the responsibility to advise the University of Washington Board of Regents regarding physician services provided by UWP.²⁸ CP at 639-640. The University of Washington Board of Regents also determines the make-up of the UW Medicine Board.²⁹ CP 638. None need to be from the Board of Regents.

Like ARUP, the University subjects UWP to substantial control through the UW Medicine Board. However, unlike UWP, the ARUP Board consists primarily of University faculty representatives who can exert even more control over ARUP than the UW Medicine Board over UWP. The UW Medicine Board that has oversight over physician services provided by UWP; the ARUP board consisting of University faculty and other University representatives, exerts oversight as well. Because of the ARUP Board's

²⁷ UW Medicine, Board By-laws, Section 1.2.c.

²⁸ *Id.*, Section 1.2.e. and f.

²⁹ *Id.*, Section 1.1.

make-up, the University exerts its “will over ARUP as the University sees fit.”

Summarizing, although ARUP does not have identical facts to *Hontz* and *Hyde*, it doesn’t need identical facts to be an arm of the state entitled to the same treatment as the state of Utah. The question today is whether Utah exerts sufficient “management and operation” control over ARUP, even if it is separately incorporated, to be an arm of the state. ARUP’s facts support that it does, because Utah and the Utah Med School exert more control over ARUP than the University of Washington exerted over either Harborview or UWP. Thus, ARUP is *the* state for purposes of RCW 82.04.030 and ARUP is excluded from the definition of “person.” The tax that the DOR has asserted is not properly due.

C. The State of Washington’s Direct Taxation of the State of Utah is Impermissible under DOR’s Rule 167.

ARUP argued that Rule 167 applied to its situation and it should be exempt from the B&O tax, like Washington State-created schools. The trial court did not explain why Rule 167 did not apply, but merely concluded that ARUP was a person for B&O tax purposes. RP at 40.

Washington does not tax in-state universities. Rule 167 provides:

(3) Business and occupation tax.

Departments and institutions of the state of Washington are not subject to the B&O tax.... Private schools, student organizations, and school districts engaging

in utility or enterprise activities, and educational institutions which are not *departments or institutions of the state of Washington are subject to the B&O tax.* (Italics supplied.)

Rule 167 provides an example explaining this point:

Example 1. MN University is an educational institution created by the state of Washington. MN University operates a book store at which it sells text books, school supplies, and apparel to students and nonstudents. As an institution of the state of Washington, MN University is exempt from the B&O tax with respect to all sales, irrespective that sales are made to nonstudents. However, MN is required to collect and remit retail sales tax on its gross proceeds of sales made through its book store.

The rule also explains the requirements for qualification. Rule 167(2)(b) explains the definition of “educational institutions” and provides that the term includes institutions accredited by the U.S. Secretary of Education.

The University meets the rule; it is accredited by the Northwest Commission on Colleges and Universities (NCCU).³⁰ NCCU is recognized by the United States Department of Education.³¹ And as explained above, ARUP is a component unit of the University and an arm

³⁰ http://accreditation.utah.edu/wp-content/uploads/2013/03/4806_001.pdf, accreditation letter dated February 1, 2017.

³¹ <http://www.nwccu.org/>

of the state. Consequently, ARUP is entitled to a refund because ARUP has met Rule 167's requirements. However, if there is any doubt as to applying Rule 167 to ARUP, then failure to do so will violate the principles of full faith and credit.

1. Full Faith and Credit prevents the DOR from denying the B&O exemption to a non-Washington public university

In *Franchise Tax Board of California v. Hyatt (II)*, the United States Supreme Court granted review as to whether the Nevada Supreme Court erred, denying the Franchise Tax Board of California ("FTB") the immunities that would be available to Nevada agencies in Nevada courts in violation of the Full Faith and Credit Clause of the United States Constitution, U.S. Const. art. IV, § 1. *Franchise Tax Board of California v. Hyatt (II)*, ___ U.S. ___, 136 S. Ct. 1277, 194 L.Ed. 2d 431 (2016) (84 USLW 4210). The Court held that the Constitution does not permit "Nevada to award damages against California agencies under Nevada law that are greater than it could award against Nevada agencies in similar circumstances." *Id.* at 1281. The Court concluded that "[d]oing so violates the Constitution's requirement that Full Faith and Credit shall be given in each State to the public Acts, Records and judicial Proceedings of every other State." *Id.* The Court's decision in *Hyatt II* determined that the Full Faith and Credit Clause means that one state cannot hold another state liable for more than the liability that would be allowed for the forum state in its own courts. *Id.*

Courts around the country have adopted *Hyatt II* to other circumstances where one state treats another state differently than it would itself under its own laws. New Mexico applies *Hyatt II*, requiring “us to recognize the sovereign immunity of other states to the extent that sovereign immunity has been retained by this state under our law. Otherwise we would be espousing an impermissible special and discriminatory rule reflecting a policy of hostility to the public Acts of a sister State.”³² Similarly, California’s appeals court applied *Hyatt II* to find that the lower California court’s decision, declining to apply Oregon Tort Claims Act’s claims notice provision, was discriminatory under the Full Faith and Credit Clause “because the decision would create a special rule allowing a suit to proceed against Oregon State under circumstances that would preclude a comparable suit against a comparable California public entity.”³³ In sum, “viewed through a full faith and credit lens, a State that disregards its own ordinary legal principles [and applies a special rule of law applicable only in lawsuits against its sister States] is hostile to another State.” *Hyatt II* at 1282.

2. Washington exempts its own State Universities from the B&O Tax, a Public Act, and it should extend that treatment to ARUP under the Full Faith and Credit Clause

³² *Montano v. Frezza*, 2017-NMSC-015, ¶ 17, 393 P.3d 700, 705 (recognizing any immunity retained by Texas that was not inconsistent with the immunity retained by New Mexico).

³³ *Oregon State Univ. v. Superior Court*, 16 Cal. App. 5th 1180, 1186–87, 225 Cal. Rptr. 3d 31, 38 (Ct. App. 2017), *review denied* (Feb. 21, 2018).

Utah does not tax its universities and their component unit non-profits, like ARUP, according to ARUP's auditors:

Further, the Congressional Joint Committee on Taxation and the IRS ruled that ARUP had been an 'integral part of the State of Utah As such, ARUP is to be treated for all federal tax purposes as though it were the State of Utah. As a result of this ruling, certain income, activities, and holdings of the Company have been deemed to be exempt from state income, sales/use, property, and other taxes.

CP at 363.

Like Utah, Washington exempts its own universities from the B&O tax; RCW 82.04.410 exempts "county, city, town, school districts or fire district activity" from B&O tax. Rule 167 explains that exemption in detail. In *Hyatt II*, the Court found that "A statute is a "Public Act" within the meaning of the Full Faith and Credit Clause." *Hyatt II* at 1281. Here, the Washington B&O Tax statute is a public Act within the meaning of the Full Faith and Credit Clause. Under the Full Faith and Credit doctrine and *Hyatt II*, Washington may not hold another state liable for more than the liability that would be allowed for the forum state in its own courts. Consequently, if Washington does not tax its own public universities, then it should not tax Utah's public universities.

3. As a Component of the University of Utah, ARUP is an arm of Utah and Washington has found that its own entities like ARUP were arms of the state

ARUP is like UWP in *Hyde*, which a physician association owned and operated by the university to be an arm of the state under Washington

law. *Hyde* at 930 and 920 (“Generally, an entity operated and managed by a state agency for a state purpose is considered an arm of the State.”).

The court determined that the use of a separate nonprofit corporation does not preclude the entity from being considered as an arm of the State. *Id.* at 934. The court further observed:

UWP is a nonprofit corporation created under chapter 24.03 RCW “for the benefit of the University of Washington School of Medicine exclusively for charitable, educational and scientific purposes, and to aid in performing certain functions of and to carry out certain purposes of the University of Washington School of Medicine.” Its principal and income are devoted exclusively to these purposes. UWP is managed and directed by a board of trustees, which includes the chairs of each department of the UW medical school, plus 12 at—large trustees who are voting members of UWP elected by their colleagues and 3 community members who are appointed by the dean of the medical school. Upon dissolution, UWP's remaining assets will transfer to the university.

Id. at 931.

UWP physicians are faculty members of the UW School of Medicine. *Id.* Members are compensated by UWP in addition to their UW faculty salaries. *Id.* at 934. UWP retains all funds in excess of the annual operating expenses “for the benefit of the School of Medicine, as an Academic Support Fund to be used through the University by the School of Medicine for the educational, research and other institutional needs of the School of Medicine.” *Id.* And, UWP members are deemed agents of UW for professional liability purposes. *Id.*

Like UWP, ARUP is part of the University and thus an arm of the State of Utah. It is a nonprofit corporation created by the University and the University is the sole voting member. ARUP's CEO is a University faculty member and employee and reports to the University President.³⁴ CP 445. In turn, the University treats ARUP as "component unit" of the Utah for financial accounting purposes.³⁵ CP 295. ARUP was originally formed by the Department of Pathology of the Utah Med School to provide a space for pathologists to consult, do laboratory research, and teach, and in turn provide revenue back to the school to attract better pathologists. CP 173-174.

ARUP was organized "for the purpose of exercising essential government functions: conducting the business of "a general clinical and surgical pathology laboratory as deemed necessary to support, supplement, and enhance its educational mission" and "supporting and engaging in teaching and related scientific and medical research, both theoretical and applied, as deemed appropriate by the Department of Pathology." CP 173-174.

"ARUP... is the clinical practice of the Department of Pathology We perform laboratory testing on all types of bodily fluids or tissue samples from patients in all 50 states of the country." CP at 38. ARUP also runs the laboratory for the University of Utah Hospital and a blood

³⁴ Art. V., Restated Articles of Incorporation (2009)

³⁵ University of Utah, 2017 Annual Financial Report (under Auditor's Responsibility).

bank that services the University of Utah and several children's hospitals staffed by University of Utah faculty physicians. CP at 39. ARUP is composed of several different laboratory testing disciplines: chemistry, immunology, infectious disease, genetics, and anatomic pathology. CP 122. Each section is overseen by a medical director employed by the Department of Pathology. There are about 80 medical directors – who are University employees and faculty who oversee all ARUP's laboratory services (and ARUP reimburses the University for those services). CP 149. ARUP employs the medical technologists, technicians and support staff who assist with the laboratory testing; however, the University faculty members oversee it and conduct all the teaching. CP at 41-42. The director of the lab (chief medical officer) is also a University faculty member and employee. CP at 223.

From a research perspective, and from a teaching perspective, the more samples that pathologists have access to, the better the University of Utah's Department of Pathology will be able to teach its technologists and future pathologists. CP at 121. The more samples ARUP can obtain, the more diverse its study of infections, patient groups, and diagnoses is, the better the research and teaching for the University's pathologists, including Utah med school's medical students and medical residents. The diverse and abundant testing samples makes ARUP one of the best research and testing laboratories with some of the best pathologists in the country, which serves the University's mission of education and research. CP at 51. ARUP's affiliation with the University creates a "synergy that is

unique in the marketplace and that drives much of [its] success.” CP at 163. ARUP works closely with the University on potential legal liability matters, including settlements. CP at 233. Although ARUP has been able to pay for settlements out of its own revenue (which are, again, owned by the University), if it were ever faced with liability it could not settle with its own funds, the Utah would have to meet that obligation. CP at 233-234.

In sum, ARUP is a component of the University, a department or institution of Utah. Washington exempts its own departments and institutions from B&O tax, including its state universities. Because Washington exempts itself from B&O tax, comity requires that Washington exempt its sister state from B&O tax.

D. The State of Washington’s Direct Taxation of the State of Utah is Impermissible under the Commerce Clause.

Washington imposes its B&O tax on interstate commerce. Such a tax is constitutionally lawful if it complies with the Commerce Clause, U.S. Const. art. I, § 8, cl. 3. Imposing a B&O tax must comply with the four-prong test adopted by the Court: (1) apply to an activity with a substantial nexus with the taxing State; (2) are fairly apportioned; (3) do not discriminate against interstate commerce; and (4) are fairly related to the services the State provides. *Complete Auto*. Under the third and fourth prongs, the B&O tax cannot discriminate on its face or assess a tax that is not fairly related to the services that Washington provides.

1. Rule 167 would facially discriminate against interstate commerce under the third prong if it is not applied to the University of Utah.

In a B&O case that reached the U.S. Supreme Court, Washington taxed two discrete activities: manufacturing and selling. The Washington legislature, however, exempted the selling tax if the taxpayer had paid the manufacturing B&O tax, because in-state taxpayers that performed both activities in Washington, only paid the manufacturing tax and were exempt from the selling tax. Because out-of-state taxpayers only performed selling in Washington, they were always taxable on the selling activity. The Court struck down Washington's tax, stating:

We conclude that Washington's multiple activities exemption discriminates against interstate commerce The current B & O tax exposes manufacturing or selling activity outside the State to a multiple burden from which only the activity of manufacturing in-state and selling in-state is exempt. The fact that the B & O tax "has the advantage of appearing nondiscriminatory," see *General Motors Corp.*, 377 U.S., at 460, 84 S.Ct., at 1577 (Goldberg, J., dissenting), does not save it from invalidation....

Tyler Pipe, at 248, 2820, 199. The Court explained the requirement of "internally consistency," relying another Commerce Clause case as follows:

As we explained in *Armco*, our conclusion that a tax facially discriminates against interstate commerce need not be confirmed by an examination of the tax burdens imposed by other States:

"... In *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159, 169 [103 S.Ct. 2933, 2942, 77 L.Ed.2d 545] (1983), the Court noted that a tax must have

‘what might be called internal consistency-that is the [tax] must be such that, if applied by every jurisdiction,’ there would be no impermissible interference with free trade.

Tyler Pipe at 247, 2820, 1997.

Rule 167 only applies to in-state universities and colleges and exempts them from the B&O tax.³⁶ So, if a state school performs laboratory testing services, then Rule 167 exempts it. However, if ARUP performs the identical laboratory testing services, then it would never be exempt because it is not in-state. Thus, Rule 167 would facially discriminate against interstate commerce when the testing involves interstate activity like that involved in ARUP’s facts. To avoid this facial discrimination, Rule 167 should be read to apply to any state college or university.

2. Rule 167 would also violate the fourth prong if the rule is not applied to ARUP.

The trial court merely concluded that the rule met the *Complete Auto* requirements. RP at 40. Thus, the court did not explain why Washington can tax interstate commerce under *Complete Auto*. But, as explained by the Court:

It was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing the business.

³⁶ Rule 167 does not explain the source of the exemption, but ARUP assumes that state universities and colleges are exempt because they are not “persons” as explained above.

W. Live Stock v. Bureau of Revenue, 303 U.S. 250, 254, 58 S. Ct. 546, 548, 82 L. Ed. 823 (1938).

Washington is entitled to extract a fair share of tax from a business engaged in interstate commerce. However, that tax must be fairly related to the government services provided. Rule 167 fails to do so because it taxes only out-of- state universities and unfairly taxes only out-of-state businesses on the same activity. The Court explains what the fourth prong means:

... the fourth prong of the Complete Auto Transit test imposes the additional limitation that the measure of the tax must be reasonably related to the extent of the contact, *since it is the activities or presence of the taxpayer in the State that may properly be made to bear a "just share of state tax burden,"* [citations omitted.]

Commonwealth Edison Company v. Montana, 453 U.S. 609 at 625 and 626 (1981) (italics supplied). It went on to say:

When a tax is assessed in proportion to a taxpayer's activities or presence in a State, the taxpayer is shouldering its fair share of supporting the State's provision of "police and fire protection, the benefit of a trained work force, and 'the advantages of a civilized society.' " [citations omitted].

Commonwealth, 453 U.S. at 626 and 627 (italics supplied).

Washington schools have a substantial physical presence in Washington with substantial property for a full 365 days per year. They

receive funds from the legislature to assist in the state's mission to educate. They receive police and fire protection from public funds. They receive a trained work force provided by Washington. They are provided many state services from Washington's general fund

In contrast, however, ARUP has virtually no presence in Washington except an a few employees who visit Washington from time to time, certainly less than 365 days per year. CP at 137. It receives none of the services of an instate school. *Commonwealth* does not require Washington to itemize the available services and determine if the tax is fairly related to the services it provides. But when two taxpayers engage in identical activities and the instate taxpayer pays no tax but the out-of-state taxpayer pays tax, it must be that the value of the services it provides to the Washington colleges and universities should be the same value of services that it provides to ARUP. Here, Washington schools receive every state benefit but pay nothing for them. Utah's University receives very few state subsidies but pays B&O tax on 100% of its Washington receipts. A fair relationship is missing. The tax fails the fourth prong.

E. State of Washington's Direct Taxation of the State of Utah is Impermissible as a Violation of Utah's Sovereign Immunity.

ARUP also contends that is it protected by Utah's sovereign immunity. As explained above, ARUP functions as an arm of Utah. Also,

as explained above, Harborview and UWP have been given status as arms of the state and sovereign immunity because the University of Washington operated and managed their medical activities. ARUP should be afforded the same status as Harborview or UWP, and the trial court erred when it failed to apply sovereign immunity.

By way of background, sovereign immunity is a right that exists independent of the Constitution. The question is whether the state has a common law right to sovereign immunity regardless of the Constitution. The Court has generally followed the view that sovereign immunity derives from the common law. In 1999, the Court explained:

Rather, as the Constitution's structure, its history, and the authoritative interpretations by this Court make clear, the States' immunity from suit is a fundamental aspect of the sovereignty which the States enjoyed before the ratification of the Constitution, and which they retain today (either literally or by virtue of their admission into the Union upon an equal footing with the other States) except as altered by the plan of the Convention or certain constitutional Amendments.

Alden v. Maine, 527 U.S. 706, 713, 119 S. Ct. 2240, 2246–47, 144 L. Ed. 2d 636 (1999). Sovereign immunity is not reserved for actions by private citizens against the state; it also applies to “sovereigns against sovereigns,” to wit:

In *Blatchford v. Native Village of Noatak*, 501 U.S. 775, 779–782, 111 S.Ct. 2578, 2581–2583, 115 L.Ed.2d 686 (1991), we rejected the contention that sovereign immunity only restricts suits by

individuals against sovereigns, not by sovereigns against sovereigns. ...

Idaho v. Coeur d'Alene Tribe of Idaho, 521 U.S. 261, 268–69, 117 S. Ct. 2028, 2034, 138 L. Ed. 2d 438 (1997).

The Court did not limit sovereign immunity principles to circumstances when a citizen sued a state in the courts of that state, according to the Court. It stated:

The immunity of a truly independent sovereign from suit in its own courts has been enjoyed as a matter of absolute right for centuries. Only the sovereign's own consent could qualify the absolute character of that immunity.

Nevada v. Hall, 440 U.S. 410, 414, 99 S. Ct. 1182, 1185, 59 L. Ed. 2d 416 (1979). *Hall* involved a tort action against Nevada in California by a California resident for an accident that occurred in California. The issue of whether Nevada could be sued in California eventually reached the Court, and the Court held that Nevada could be sued in California. *Hall* is under attack in *Hyatt II*.

In *Hyatt II*, Hyatt sued the FTB in Nevada (intentional tort and bad-faith conduct) and won. Nevada rejected California's sovereign immunity claim. The FTB's position conflicted with *Hall*. In the predecessor case to *Hyatt II*, the Court split 4-4 on whether to overrule *Hall*, leaving *Hall* intact. California has asked the U.S. Supreme Court to review *Hyatt II*, and several states, including Utah and Washington, have

filed an amicus brief, encouraging the Court to accept the case and definitively rule on the sovereign immunity question. The petitioner and the amicus explain why sovereign immunity should be fully engaged, preventing a home state from forcing a foreign state to litigate in the home state's court.

Admittedly, ARUP's case is different from *Hyatt II*, because Utah is suing Washington to prevent Washington from taxing it. ARUP is litigating because it has been coerced in this way: (1) Washington can issue an estimated assessment if an audit target does not cooperate with the auditor,³⁷ (2) ARUP cannot challenge an estimated assessment if it did not cooperate with the auditor,³⁸ (3) Washington converted an unpaid estimated assessment into a tax lien by issuing a tax warrant,³⁹ and (4) then ARUP cannot substantively challenging the tax assessment. Thus, Washington coerces Utah to protect itself by cooperating with the audit and then forces ARUP to sue Washington in Washington's courts.

It is true that RCW 82.32.150 permits a taxpayer to seek an injunction. *Tyler Pipe Indus. V. State*, 96, Wn.2d 785,790, 638 P.2d 1213, 1216 (1982). In that case, the court held that the taxpayer's claim that

³⁷ RCW 82.32.100(1).

³⁸ RCW 82.32.070(1). In fact, a taxpayer who fails to comply with the production of books and records "is forever barred from questioning, in any court or proceedings, the correctness of any assessment.

³⁹ RCW 82.32.210(1)

paying the tax is inconvenient, but not an actual or substantial injury. Here, in ARUP's case, not only was the likelihood of obtaining an injunction was unlikely, because sovereign immunity did not apply under *Hall* but requiring ARUP to pay the tax would not have resulted in actual or substantial injury. Consequently, RCW 82.32.150 was of no assistance to ARUP.

California in *Hyatt II* appealed again the Court on March 12, 2018 (Case No. 17-1299) specifically seeking review of whether *Hall* should be overruled. On April 13, 2018, 44 states, including Washington, filed an amicus curiae brief. On June 28, 2018, the California petition was accepted for review. In the amicus brief, the 44 states observed:

Hall has “encourage[d] state courts to deny respect to the sovereign immunity of defendant sister states, in circumstances where such denial is at best questionable.” Donald Olenick, *Sovereign Immunity in Sister-State Courts: Full Faith and Credit and Federal Common Law Solutions*, 80 Colum. L. Rev. 1493, 1498 (1980). ... Nothing in the Constitution allows state courts to exercise jurisdiction over their sister States. The very idea denies States “the dignity that is consistent with their status as sovereign entities.” *Fed. Mar. Comm’n*, 535 U.S. at 760. *Hall*'s holding otherwise was erroneous.

Brief of Indiana and 43 Other States, *Franchise Tax Board v. Hyatt*, (Case No. 17-1299), p. 9. Appended as Appendix 1.

Based on the subsequent Court opinions on sovereign immunity, the states urge the Supreme Court to overturn *Hall*, because *Hall* denies the states the dignity of their sovereign immunity status. DOR should be consistent with

Washington's plea to overturn *Hall* and honor Utah's sovereign immunity regardless of whether *Hall* is overruled. Compelling ARUP to litigate in Washington courts through its refund statute, is also the denial of Utah's dignity of its sovereign immunity status. The U.S. Supreme Court has docketed this matter for argument on January 9, 2019.

VII. CONCLUSION

The trial court's granting of the DOR's motion for summary judgment should be reversed and ARUP's motion for summary judgment should be granted. First, Rule 19402(303)(b) applies and ARUP's gross receipts should be sourced to Utah where the tangible personal property is tested. Second, ARUP is an arm of Utah and not a taxable "person" for purposes of RCW 82.04.030. Third, Rule 167, which exempts public colleges and universities from the B&O tax, exempts ARUP, a component unit of the University of Utah, as required under the full faith and credit clause. Failure to do so violates the Commerce Clause as a facially discriminatory tax and one that fails to meet the fair relationship test. Fourth, imposing the tax on ARUP would violate Utah's right to its sovereign immunity. The trial court order granting summary judgment to the state should be reversed, the trial court's denial of ARUP's motion for summary judgment should be reversed, granting summary judgment to ARUP.

RESPECTFULLY SUBMITTED this 3rd day of January, 2019.

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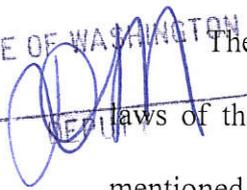
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CERTIFICATE OF SERVICE

STATE OF WASHINGTON

BY 

The undersigned certifies under the penalty of perjury under the laws of the State of Washington that I am now and at all times herein mentioned a resident of the State of Washington, over the age of eighteen years, not a party to or interested in the above-entitled action, and competent to be a witness herein.

On the date given below, I caused to be served the foregoing document on the following persons and in the manner listed below:

<p>Ms. Kelly Owings Mr. Joshua Weissman Assistant Attorney General Office of the Attorney General 7141 Cleanwater Lane SW P.O. Box 40123 Olympia, WA 98504-0123 kellyo2@atg.wa.gov joshuaw@atg.wa.gov CarrieP@Atg.wa.gov kyleeni@atg.wa.gov REVOlyFF@atg.wa.gov</p>	<p><input type="checkbox"/> Via Hand delivery <input checked="" type="checkbox"/> Via U.S. Mail, 1st Class, Postage Prepaid <input type="checkbox"/> Via Overnight Delivery <input type="checkbox"/> Via Facsimile <input checked="" type="checkbox"/> Via Email per E-Service Agreement</p>
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I hereby declare under penalty of perjury under the laws of the State of Washington that the foregoing is true and correct.

DATED at Tacoma, Washington this 3rd day of January, 2019.


Cindy Rochelle

Appendix 1

No. 17-1299

IN THE
Supreme Court of the United States

FRANCHISE TAX BOARD OF THE STATE OF CALIFORNIA
Petitioner,

v.

GILBERT P. HYATT,
Respondent.

**On Writ of Certiorari to the
Supreme Court of Nevada**

**BRIEF OF INDIANA AND 43 OTHER STATES AS
AMICI CURIAE IN SUPPORT OF PETITIONER**

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QUESTION PRESENTED

Whether *Nevada v. Hall*, 440 U.S. 410 (1979), which permits a sovereign State to be haled into another State's courts without its consent, should be overruled.

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INTEREST OF THE *AMICI* STATES

The States of Indiana, Alabama, Alaska, Arizona, Arkansas, Colorado, Connecticut, Delaware, Florida, Georgia, Hawaii, Idaho, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Montana, Nebraska, Nevada, New Jersey, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, and Wyoming respectfully submit this brief as *amici curiae* in support of petitioner. The *amici* States have a strong interest in protecting their sovereign immunity by overturning *Nevada v. Hall*, 440 U.S. 410 (1979). *Hall* is—and always has been—irreconcilable with the Court’s larger body of sovereign immunity decisions, and the *amici* States urge this Court to overturn it.

SUMMARY OF THE ARGUMENT

Forty years ago in *Nevada v. Hall*, 440 U.S. 410 (1979), this Court held that States could be subject to suit in the courts of their sister States. Petitioners along with 44 *amici* States now urge this Court to overrule *Hall*.

Nevada v. Hall was wrongly decided because state sovereign immunity is not limited to the text of the Eleventh Amendment. At common law, sovereign immunity, even in the courts of another sovereign, was assumed. The States did not relinquish that immunity when they ratified the Constitution. Instead, the

framers understood the Constitution to preserve the traditional sovereign immunity of the States. The Eleventh Amendment was enacted not to outline the boundaries of state sovereign immunity, but to restore its common law understanding. *Hall's* holding that state sovereign immunity is not protected in the courts of other States contravenes both this history and the Court's precedents.

Moreover, the numerous suits brought against States in other States' courts in the decades since *Hall* are an insult to state sovereignty. This insult is particularly harmful in the tax context, which goes to the core of state police power. *Hall* undermines the administrative review processes that States have set up to protect their sovereignty with respect to this important state function.

Finally, *stare decisis* should give way to overruling *Hall*. Not only was *Hall* wrongly decided, but no reliance interests weigh against reconsideration, as private plaintiffs do not structure their decisions or interests around the vulnerability of States to lawsuits in the courts of other States.

ARGUMENT

I. *Nevada v. Hall* Was Wrongly Decided

Nearly forty years ago, in *Nevada v. Hall*, 440 U.S. 410, 426–27 (1979), the Court held that the Constitution does not bar lawsuits against a State in the courts of another State. In doing so, it relied on the proposition that nothing “in Art. III authorizing the judicial power of the United States, or in the Eleventh

Amendment limitation on that power, provide any basis, explicit or implicit, for this Court to impose limits on the powers of” state courts to exercise jurisdiction over their sister States. *Id.* at 421. But that holding contravenes both the history of the Eleventh Amendment and this Court’s subsequent decisions on state sovereign immunity.

A. State sovereign immunity is not limited to the text of the Eleventh Amendment

The Court has long held that “the sovereign immunity of the States neither derives from, nor is limited by, the terms of the Eleventh Amendment.” *Alden v. Maine*, 527 U.S. 706, 713 (1999). On the contrary, “the States’ immunity from suit is a fundamental aspect of the sovereignty which the States enjoyed before the ratification of the Constitution, and which they retain today . . . except as altered by the plan of the Convention or certain constitutional Amendments.” *Id.* Sovereign immunity predates the Eleventh Amendment and, indeed, the Constitution itself.

1. Common law sovereign immunity originated in feudal England: “no lord could be sued by a vassal in his own court, but each petty lord was subject to suit in the courts of a higher lord.” *Nevada v. Hall*, 440 U.S. 410, 414–15 (1979). Only the king was completely immune from suit because “there was no higher court in which he could be sued.” *Id.* at 415. When the American colonies rebelled against the king, each State became a sovereign in its own right, and thus inherited sovereign immunity. See *Seminole Tribe of Fla. v. Florida*, 517 U.S. 44, 54 (1996).

At common law and at the time of the founding, a sovereign's immunity from suit, even in the courts of another sovereign, was assumed. William Blackstone explained that "no suit or action can be brought against the king, even in civil matters, because no court can have jurisdiction over him." 1 William Blackstone, Commentaries *235. Similarly, the leading treatise on international law at the time stated that "[o]ne sovereign cannot make himself the judge of the conduct of another." Emmerich de Vattel, *The Law of Nations or Principles of the Law of Nature Applied to the Conduct and Affairs of Nations and Sovereigns* 155 (Book II, Ch. 4, § 55) (J. Chitty ed., 1883).

Such was the prevailing understanding of sovereign immunity under the Articles of Confederation, as demonstrated by the decision of the Pennsylvania Court of Common Pleas in *Nathan v. Virginia*, 1 U.S. (1 Dall.) 77 (Pa. Ct. Com. Pl. 1781). There, a citizen of Pennsylvania sued the Commonwealth of Virginia in Pennsylvania state court over property located in Philadelphia Harbor. *Id.* at 77–78. The Attorney General of Pennsylvania weighed in, arguing "[t]hat a sovereign, when in a foreign country, is always considered by civilized nations, as exempt from its jurisdiction, privileged from arrests, and not subject to its laws." *Id.* at 78. The Virginia delegates to the Confederation Congress, led by James Madison, similarly argued that the case should be dismissed because it required Virginia to "abandon its Sovereignty by descending to answer before the Tribunal of another Power." James Madison, Letter from Virginia Delegates to Supreme Executive Council of Pennsylvania

(July 9, 1781), *reprinted in* 3 The Papers of James Madison 184 (William T. Hutchinson et al. eds., 1963). The court agreed and held that Virginia was immune from suit. *Nathan*, 1 U.S. (1 Dall.) at 80.

2. The States did not relinquish their sovereign status when they ratified the Constitution. “The leading advocates of the Constitution assured the people in no uncertain terms that the Constitution would not strip the States of sovereign immunity.” *Alden*, 527 U.S. at 716. Writing in support of ratification, Alexander Hamilton observed that “[i]t is inherent in the nature of sovereignty, not to be amenable to the suit of an individual *without its consent*.” The Federalist No. 81 (Alexander Hamilton). He argued that “there is no colour to pretend that the State governments would, by the adoption of [the Constitution], be divested” of their immunity and concluded that “to ascribe to the federal courts, by mere implication, and in destruction of a pre-existing right of the State governments, a power which would involve such a consequence, would be altogether forced and unwarrantable.” *Id.*

Even those Federalists that believed Article III abrogated state sovereign immunity in federal court did not go so far as to conclude that States could be sued in the courts of other States. Edmund Pendleton argued before the Virginia Convention that “[t]he impossibility of calling a sovereign state before the jurisdiction of another sovereign state[] shows the propriety and necessity of vesting [a federal] tribunal with the decision of controversies to which as state shall be a party.” 3 Elliot’s Debates 549.

Such episodes establish that “the Constitution was understood, in light of its history and structure, to preserve the States’ traditional immunity from private suits.” *Alden*, 527 U.S. at 724. Attorney General Edmund Randolph specifically recognized this principle in his report on the judiciary to the House of Representatives, delivered shortly after ratification: “as far as a particular state can be a party defendant, a sister state cannot be her judge.” 4 The Documentary History of the Supreme Court of the United States, 1789–1800 130 (Maeva Marcus, ed., 1992). Indeed, as the Court has recognized, “[t]he Constitution would never have been ratified if the States and their courts were to be stripped of their sovereign authority except as expressly provided by the Constitution itself.” *Atascadero State Hosp. v. Scanlon*, 473 U.S. 234, 238 n.2 (1985).

3. Notwithstanding the prevailing understanding of the framers, the Court held in *Chisholm v. Georgia*, 2 U.S. 419, 420 (1793), that a citizen of one State could invoke federal diversity jurisdiction against another State because such suits were permitted by the literal text of Article III. Justice Iredell dissented, “relying on American history, English history, and the principles of enumerated powers and separate sovereignty.” *Alden*, 527 U.S. at 720 (internal citations omitted).

The *Chisolm* decision “fell upon the country with a profound shock.” *Id.* (quoting 1 C. Warren, *The Supreme Court in United States History* 96 (rev. ed. 1926)). Just one day after the decision, the House of Representatives introduced a proposal to amend the

Constitution. *Id.* at 721. After a short recess, each chamber spent only one day discussing the Amendment before passing it. *Id.*

Congress enacted the Eleventh Amendment “not to change but to restore the original constitutional design.” *Id.* at 722. Moreover, “it is doubtful that if Congress meant to write a new immunity into the Constitution it would have limited that immunity to the narrow text of the Eleventh Amendment.” *Id.* at 723. For this reason, the Court has long held that “the scope of the States’ immunity from suit is demarcated not by the text of the Amendment alone but by fundamental postulates implicit in the constitutional design.” *Id.* at 729.

The Court’s post-Eleventh Amendment decision in *Hans v. Louisiana*, 134 U.S. 1 (1890), confirmed that understanding. In *Hans*, the Court held that sovereign immunity prevents individuals from asserting federal question jurisdiction against States, even though it is not specifically prohibited by the text of the Amendment. *Id.* at 14–15. *Hans* specifically relied on “the presumption that no anomalous and unheard-of proceedings or suits were intended to be raised up by the constitution.” *Id.* at 18. And the court has “since acknowledged that the *Chisholm* decision was erroneous.” *Fed. Mar. Comm’n v. S.C. State Ports Auth.*, 535 U.S. 743, 753 (2002). That is to say, “the Eleventh Amendment does not define the scope of the States’ sovereign immunity; it is but one particular exemplification of that immunity.” *Id.*

B. *Hall* contravenes this Eleventh Amendment history

Nevada v. Hall rests on the flawed premise that state courts may assert jurisdiction over their sister States unless some Constitutional text expressly limits such jurisdiction. 440 U.S. 410, 421 (1979). But that rationale has not survived the Court's more recent observations that sovereign immunity is not limited to the text of the Eleventh Amendment. *See, e.g., Fed. Mar. Comm'n v. S.C. State Ports Auth.*, 535 U.S. 743, 753 (2002); *Alden v. Maine*, 527 U.S. 706, 730 (1999); *Idaho v. Coeur d'Alene Tribe of Idaho*, 521 U.S. 261, 267–68 (1997); *Seminole Tribe of Fla. v. Florida*, 517 U.S. 44, 54 (1996).

The very purpose of Article III was to ensure the foreclosure of interstate conflicts that had plagued the nation by establishing a neutral forum to adjudicate these disputes. Richard H. Pierson, *Constitutional Law—State Sovereign Immunity—Nevada v. Hall*, 440 U.S. 410 (1979), 56 Wash. L. Rev. 289, 297 (1981). At the time of the Constitutional Convention, every State recognized the sovereign immunity of its sisters and the *in personam* jurisdiction of a state court was accordingly confined to its own citizens and residents. *Id.* at 298. Thus, the appropriate inference is that the inquiry should be whether anything in the Constitution *allows* jurisdiction of state courts over their sister States—not whether anything *forbids* it.

Hall's expectation that “prevailing notions of comity would provide adequate protection against the unlikely prospect of an attempt by the courts of one State

to assert jurisdiction over another,” *id.* at 419, has proved illusory. *Hall* has “encourage[d] state courts to deny respect to the sovereign immunity of defendant sister states, in circumstances where such denial is at best questionable.” Donald Olenick, *Sovereign Immunity in Sister-State Courts: Full Faith and Credit and Federal Common Law Solutions*, 80 Colum. L. Rev. 1493, 1498 (1980). Attempts by States to apply *Hall* have led to decisions that are “highly discriminatory” and “inconsistent with the traditional federal-system principles that the states are coequals and that the sovereignty of each state limits the powers of all others.” *Id.* at 1499. The Eleventh Amendment was enacted in order to preclude suits in any forum without the consent of the defendant State, Pierson, 56 Wash. L. Rev. at 298, a proposition this Court recognized in *New Hampshire v. Louisiana*, 108 U.S. 76, 91 (1883) (stating that federal jurisdiction under Article III is the exclusive remedy available to a citizen of another State).

Nothing in the Constitution allows state courts to exercise jurisdiction over their sister States. The very idea denies States “the dignity that is consistent with their status as sovereign entities.” *Fed. Mar. Comm’n*, 535 U.S. at 760. *Hall*’s holding otherwise was erroneous.

C. Later cases are in tension with *Hall*

Sovereign immunity cases since *Hall* have established what *Hall* rejected—sovereign immunity is derived from the history and structure of the Constitution and is antecedent to the text of both Article III

and the Eleventh Amendment. *Cf. Hall*, 440 U.S. at 426–27.

In *Seminole Tribe of Florida v. Florida*, the Court, overturning *Pennsylvania v. Union Gas Co.*, 491 U.S. 1 (1989), said that “we long have recognized that blind reliance upon the text of the Eleventh Amendment is to strain the Constitution and the law to a construction never imagined or dreamed of.” 517 U.S. 44, 69 (1996) (internal citations omitted). For this reason, the Court held that “the background principle of state sovereign immunity embodied in the Eleventh Amendment is not so ephemeral as to dissipate when the subject of the suit is an area . . . that is under the exclusive control of the Federal Government.” *Id.* at 72.

The very next year, in *Idaho v. Coeur d’Alene Tribe of Idaho* the Court again emphasized that the “recognition of sovereign immunity has not been limited to the suits described in the text of the Eleventh Amendment.” 521 U.S. 261, 267 (1997). Based on this principle, the Court held that a lawsuit brought by an Indian tribe against the State was barred by the Eleventh Amendment.

Later, in *Alden v. Maine*, 527 U.S. 706 (1999), the Court elaborated: “The generation that designed and adopted our federal system considered immunity from private suits central to sovereign dignity.” *Id.* at 715. The Eleventh Amendment was adopted “not to change” the Constitution “but to restore the original constitutional design.” *Id.* at 722. For this reason, “the sovereign immunity of the States neither derives

from, nor is limited by, the terms of the Eleventh Amendment.” *Id.* at 713. Ultimately, “as the Constitution’s structure, its history, and the authoritative interpretations by this Court make clear, the States’ immunity from suit is a fundamental aspect of the sovereignty which the States enjoyed before the ratification of the Constitution, and which they retain today.” *Id.*

Finally, in *Federal Maritime Commission v. South Carolina State Ports Authority*, 535 U.S. 743 (2002), the Court held that sovereign immunity barred the Federal Maritime Commission from adjudicating a private complaint against the South Carolina State Ports Authority, even though the text of the Eleventh Amendment applies only to Article III courts. The Court explained that “the Eleventh Amendment does not define the scope of the States’ sovereign immunity; it is but one particular exemplification of that immunity.” *Id.* at 753.

Seminole Tribe, *Coeur d’Alene*, *Alden*, and *Federal Maritime Commission* represent a fundamental course correction in the law of sovereign immunity—one that respects constitutional history and structure in a way that several earlier decisions, including not only *Union Gas* but also *Hall*, did not. Yet *Hall* remains as a vestige of the discarded doctrine, one that starkly contradicts other governing sovereign immunity precedents. The Court should overturn it.

II. State Sovereign Immunity Includes Immunity from Suits Brought in other States' Courts

A. Suits against States in other States' courts insult state sovereignty

The Court has held that “[t]he preeminent purpose of state sovereign immunity is to accord States the dignity that is consistent with their status as sovereign entities.” *Fed. Mar. Comm’n v. S.C. State Ports Auth.*, 535 U.S. 743, 760 (2002). Allowing States to be sued in the courts of other States contravenes that purpose.

First, it would be illogical to interpret the Eleventh Amendment to prohibit all non-consensual lawsuits against States in federal court, *see Hans v. Louisiana*, 134 U.S. 1, 18 (1890), yet allow those “anomalous and unheard-of” suits in state court. *Id.* Indeed, allowing a State to be sued in another State’s court would be a *greater* insult to state sovereignty than allowing a similar lawsuit in federal court. Federal courts were designed by the framers of the Constitution to provide a neutral forum. *Nevada v. Hall*, 440 U.S. 410, 437 (1979) (Rehnquist, J., dissenting).

Second, allowing state courts to exercise jurisdiction over sister States “would place unwarranted strain on the States’ ability to govern in accordance with the will of their citizens.” *Alden v. Maine*, 527 U.S. 706, 750–51 (1999). Lawsuits, especially those for money damages, implicate the “allocation of scarce resources among competing needs and interests”

which “lies at the heart of the political process.” *Id.* at 751. If the courts of other States are allowed to make such decisions, they will essentially decide what policy goals the defendant State should pursue and how it should pursue those goals. “If the principle of representative government is to be preserved to the States, the balance between competing interests must be reached after deliberation by the political process established by the citizens of the State, not by judicial decree” of another State’s court. *Id.*

This threat to state sovereignty is not merely hypothetical. At least five other tax cases have been brought against one State in a court of another State, including another lawsuit against California filed in Nevada, *see* Compl., *Schroeder v. California*, No. 14-2613 (D. Nev. Dec. 18, 2014), and yet another against California in Washington. *See* Compl., *Satcher v. California Tax Franchise Bd.*, No. 15-2-00390-1 (Wash. Super. Ct., Skagit Cty. June 17, 2015); Status Report, *Satcher*, No. 16-2-00194-0 (July 30, 2018). Massachusetts is currently being sued in Virginia state court over a recently promulgated sales and use tax regulation. Mass. Comm’r of Revenue’s Mem. of Points and Auths. in Supp. of his Mot. to Dismiss for Lack of Personal Jurisdiction at 4, *Crutchfield Corp. v. Harding*, No. CL17001145-00 (Va. Cir. Ct. Feb. 15, 2018). Similarly, Ohio has an appeal pending in the Kentucky Supreme Court concerning a commercial activity tax assessment. Motion to Transfer of Defs./Appellants State of Ohio & Joseph W. Testa, Tax Comm’r of Ohio at 1, *Great Lakes Minerals, LLC v. Ohio*, No. 2018-SC-000161-T (March 26, 2018) (granted unanimously, June 14, 2018). And South Dakota has been sued in

both North Dakota *and* Minnesota over a tax audit. Compl., *Agvise Labs., Inc. v. Gerlach*, No. 18-2018-CV-00460 (N.D. D. Ct. Mar. 26, 2018); Compl., *Agvise Labs., Inc. v. Gerlach*, No. 76-CV-18-80 (Minn. D. Ct. Mar. 7, 2018). Finally, Connecticut was sued in Texas state court by a taxpayer. Pls.' Original Pet., Req. for Declaratory J., Req. for Injunctive Relief & Req. for Disclosure, *Hendrick v. Conn. Dep't of Revenue Servs.*, No. DC 13-08568 (Tex. D. Ct. Aug. 6, 2013).

Outside the tax arena, Ohio also is a defendant in an Indiana state court case arising out of a motor vehicle collision. Order Denying Summ. J., *Chilton v. Ohio Dept. of Transp.*, No. 15D01-1404-CT-019 (Ind. Sup. Ct. Dec. 19, 2016). North Dakota is currently defending against a contract dispute in Minnesota state court. Compl., *Rosewood Hospitality, LLC v. N.D. Dept. of Soc. Servs.*, No. 62-CO-18-538 (Minn. D. Ct. Feb. 27, 2018). Rhode Island has a family law case in Connecticut state court. Compl., *Reale v. R.I.*, No. WWM-CV18-5008257-S (Conn. Sup. Ct. Nov. 17, 2017). And Texas recently defended a medical malpractice case in New Mexico state court. *Montano v. Frezza*, 339 P.3d 700 (N.M. 2017).

Every case brought against one State in a court of another State undermines the defendant State's sovereignty, both in terms of the insult to sovereign dignity and in terms of the required expenditure of sovereign resources to litigate the matter. *See Alden v. Maine*, 527 U.S. 706, 751 (1999). States must use scarce resources to meet a number of competing policy goals, and "it is inevitable that difficult decisions involving the most sensitive and political of judgments

must be made.” *Id.* Sovereign immunity “assures the states . . . from unanticipated intervention in the processes of government.” *Id.* at 750 (quoting *Great N. Life Ins. Co. v. Read*, 322 U.S. 47, 53 (1944)). In all cases, a limitation of immunity “carries with it substantial costs to the autonomy, the decisionmaking ability, and the sovereign capacity of the States.” *Id.*

B. The insult to state sovereignty is particularly harmful in the tax context

While any case brought against a State against its will is an insult to its sovereignty, the Court has also recognized that vitiating sovereign immunity when the power to tax is at stake is particularly harmful, as “the power to promulgate and enforce income tax laws is an essential attribute of sovereignty.” *Franchise Tax Bd. of Cal. v. Hyatt (Hyatt I)*, 538 U.S. 488, 498 (2003). “[T]axes,” the Court has recognized, “are the life-blood of government, and their prompt and certain availability an imperious need.” *Franchise Tax Bd. of Cal. v. U.S. Postal Serv.*, 467 U.S. 512, 523 (1984) (quoting *Bull v. United States*, 295 U.S. 247, 259–60 (1935)).

The taxing power of States is so important that Congress has limited the ability of the federal judiciary to restrain it. The Tax Injunction Act of 1937 prevents federal district courts from “enjoin[ing], suspend[ing] or restrain[ing] 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.” 28 U.S.C. § 1341. The purpose of the

Act is “to limit drastically federal district court jurisdiction to interfere with so important a local concern as the collection of taxes.” *Rosewell v. LaSalle Nat’l Bank*, 450 U.S. 503, 522 (1981). It “has its roots in equity practice, in principles of federalism, and in recognition of the imperative need of a State to administer its own fiscal operations.” *Tully v. Griffin, Inc.*, 429 U.S. 68, 73 (1976). Such a substantive limit on the power of federal courts demonstrates the core status of the taxing power to the States.

For their part, States often limit the processes their own taxpayers may use to challenge assessments and audits. Of the forty-three States that have some form of income tax, many have an administrative review process that taxpayers must complete before seeking judicial review of an audit or assessment. *See, e.g.*, Ind. Code § 6-8.1-5-1. Many States require a final administrative decision to be appealed to a special tax court, rather than a court of general jurisdiction. *See, e.g.*, Ind. Code § 33-26-3-1; Ala. Code § 40-29-90. *See generally* All St. Tax Guide (RIA). For sales and use taxes, similarly, many States require administrative review before challenging an audit or assessment in state court. In Indiana, for example, a taxpayer must first file a protest with Indiana Department of Revenue before appealing to the Indiana Tax Court. Ind. Code § 6-8.1-5-1. In Illinois, to take another example, the taxpayer has the option of either filing a protest with the Department of Revenue, 35 Ill. Comp. Stat. 120/5, paying the tax and then filing a claim for a credit with the Department, 35 Ill. Comp. Stat. 735/3-2, or paying the tax under protest and then filing an action in state court, 30 Ill. Comp. Stat.

230/1. *See generally* Am. Bar Ass'n, *Sales & Use Tax Deskbook* (30th ed. 2016–17). *See also* Am. Bar Ass'n, *Property Tax Deskbook* (22nd ed. 2017) (showing specialized administrative review procedures for property tax assessments).

Channeling tax claims into administrative review or specialized courts is one way States safeguard core taxation authority. Accordingly, in Nevada and California—the two States with direct ties to this case—bypassing administrative review and immediately seeking judicial review of an audit (or the tactics used during an audit) is not permitted. In Nevada, a taxpayer must complete administrative review *and* pay the tax bill before seeking judicial review of an audit. Nev. Rev. Stat. § 360.395. In California, a taxpayer may either: (1) file an appeal with the Office of Tax Appeals (without paying the underlying tax), but only after filing a protest of the audit assessment with the Franchise Tax Board and the denial of that protest, or (2) first pay the tax (except in a residency case) and then file a claim with the Franchise Tax Board for a refund. *See* Cal. Gov't Code § 15677; Cal. Rev. & Tax. Code § 19381. If the Franchise Tax Board denies the claim or does not act within six months, the taxpayer may file a suit for a refund in the Superior Court. Cal. Rev. & Tax. Code § 19381.

California law also prevents “instituting any judicial or administrative proceeding or action for or incidental to the assessment or collection of a tax,” or for any “act or omission in the interpretation or application of any law relating to a tax.” Cal. Gov't Code

§ 860.2. By suing California's tax authorities in Nevada courts while his administrative appeal remains pending, however, Hyatt has circumvented California's restrictions.

Hall thus undermines these administrative processes and the federal Tax Injunction Act by providing an end-run for plaintiffs around a State's tax enforcement system without requiring plaintiffs to abide by the carefully-crafted administrative procedures established by the taxing State. It also undermines the exercise of core state functions such as taxation, assessment, and audit by permitting a court from another State to overrule a State's policymaking and enforcement decisions. *Hall*, 440 U.S. at 425–27. By exercising jurisdiction over the taxation authority of another State, a forum-state court may make decisions that effectively determine what revenue goals the defendant State should pursue and how it should pursue them. Such lawsuits “place unwarranted strain on the States' ability to govern in accordance with the will of their citizens,” and inject another State's courts into “the heart of the political process” of a State. *Alden*, 527 U.S. at 750–51.

Worse still, the courts of the other State may be tempted to rule in a manner that benefits their own State's citizens, treasuries, and policy priorities. See, e.g., *Franchise Tax Bd. of Cal. v. Hyatt (Hyatt II)*, 136 S. Ct. 1277, 1279 (2016). As noted above, this case has already inspired other lawsuits in Nevada courts against FTB, which may force FTB to alter its enforcement policies.

To be sure, the Court in *Hyatt I* struggled to find a “principled distinction between [a State’s] interest in tort claims arising out of its university employee’s automobile accident, at issue in *Hall*, and [a State’s] interests in tort claims . . . arising out of its tax collection agency’s residency audit.” 538 U.S. at 498. But that only means that the Court should not create different standards for different types of claims. The point remains that this case demonstrates the degree to which *Hall* opened the door not only to suits that seek compensation for other States’ seemingly ordinary torts, but also for suits challenging other States’ core policy and enforcement determinations that the courts of the forum State may find objectionable.

III. *Stare Decisis* Should Not Prevent the Court from Overruling *Hall*

Where, as here, the Court must consider whether to overrule a prior decision, it must also grapple with the principle of *stare decisis*. However, “the rule of *stare decisis* is not an ‘inexorable command,’ and certainly it is not such in every constitutional case.” *Planned Parenthood of Se. Pa. v. Casey*, 505 U.S. 833, 854 (1992). Instead, the Court’s reconsideration of a prior holding must be “informed by a series of prudential and pragmatic considerations designed to test the consistency of overruling a prior decision with the ideal of the rule of law,” including (1) “whether the rule has proven to be intolerable simply in defying practical workability;” (2) “whether the rule is subject to a kind of reliance that would lend a special hardship to the consequences of overruling and add inequity to the cost of repudiation;” (3) “whether related

principles of law have so far developed as to have left the old rule no more than a remnant of abandoned doctrine;” and (4) “whether facts have so changed, or come to be seen so differently, as to have robbed the old rule of significant application or justification.” *Id.*

First, the sheer number of lawsuits against States in the courts of other States demonstrates the practical unworkability of *Hall*, particularly as it belies the sufficiency of the “comity” expectation articulated in *Hall*. See *supra* Parts I.A and II.A. This case alone represents the culmination of over twenty years of litigation and three trips to the Supreme Court. And it is far from the only case of its type. The State of Nevada—the very State whose courts chose to exercise jurisdiction in this case—both joined other States urging the Court to take this case to revisit *Hall* the last time around, Brief of Amici Curiae State of West Virginia and 39 Other States in Support of Petitioner, *Franchise Tax Bd. v. Hyatt*, 136 S. Ct. 1277 (2016) (No. 14-1175), and recently filed its own cert. petition asking the Court to overrule *Hall*. Petition for Writ of Certiorari, *Nevada Dep’t of Wildlife v. Smith*, No. 17-1348 (Mar. 21, 2018). The States’ nearly uniform opposition to *Hall* illustrates the need for a different outcome.

Second, *Hall* implicates no reliance interests. “The inquiry into reliance counts the cost of a rule’s repudiation as it would fall on those who have relied reasonably on the rule’s continued application.” *Casey*, 505 U.S. at 855. As should be obvious, potential plaintiffs do not structure their personal or economic interests or choices on the ability to sue another State

in the courts of their home State. Who contemplates the possibility of having a tort claim against a State where they do not live, let alone strategizes where they would bring such a hypothetical claim? Nobody. Similarly, States do not structure their court systems around the ability to entertain suits against other States, and they do not enact tort claim procedures with other States in mind. Indeed, after *Hyatt II*, state courts may not afford other States less protection from claims than they afford their home States. 136 S. Ct. at 1281. So, even if state courts wished to take specific account of how they would handle suits against other States in reliance on *Hall*, it is not clear what actions they could take.

Third, *Hall* is a “remnant of the abandoned doctrine” that the Eleventh Amendment defines the outer limits of state sovereign immunity. See Part I.C *supra*. The Court has long “recognized that blind reliance upon the text of the Eleventh Amendment is to strain the Constitution and the law to a construction never imagined or dreamed of.” *Seminole Tribe of Fla. v. Florida*, 517 U.S. 44, 69 (1996) (internal citations omitted). Overruling *Hall* is necessary to bring state immunity from suit in the courts of other States in line with the rest of this Court’s sovereign immunity doctrine.

Finally, although the facts and reasons underlying state sovereign immunity have not changed, the numerous lawsuits against States in other States’ courts has demonstrated the extent of *Hall*’s insult to state sovereignty. The “prevailing notions of comity” that

the Court invoked in *Hall* to protect States from such suits are insufficient. 440 U.S. at 419.

Just as the Court in *Seminole Tribe* overruled *Union Gas* because it was a “solitary departure from settled law, 517 U.S. at 66, so too should the Court overrule *Hall*. “[N]one of the policies underlying stare decisis require [this Court’s] continuing adherence to its holding.” *Id.* *Hall* “depart[s] from our established understanding of the Eleventh Amendment and undermine[s] the accepted function of Article III.” *Id.* Consequently, the time has come for this Court to overrule *Hall*.

CONCLUSION

The judgment should be reversed.

Respectfully submitted,

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