No. 22O150

In The
Supreme Court of the United States

STATE OF ARIZONA,
Plaintiff,

v.

STATE OF CALIFORNIA,
Defendant.

On Motion For Leave To File A Bill Of Complaint

Brief Of Amici Curiae DRI – The Voice Of The Defense Bar And The National Federation Of Independent Business Small Business Legal Center In Support Of Plaintiff's Motion For Leave To File A Bill Of Complaint

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STATEMENT OF INTEREST[1]

DRI – The Voice of the Defense Bar (www.dri.org) is an international membership organization composed of more than 23,000 attorneys who defend the interests of businesses and individuals in civil litigation. DRI's mission includes enhancing the skills, effectiveness, and professionalism of defense lawyers, promoting appreciation for the role of defense lawyers in the civil justice system, anticipating and addressing substantive and procedural issues germane to defense lawyers, and achieving fairness in the civil justice system. To help foster these objectives, DRI participates as *amicus curiae* at both the petition and merits stages in carefully selected Supreme Court cases presenting questions that significantly affect civil defense attorneys, their corporate or individual clients, and the conduct of civil litigation.

The National Federation of Independent Business Small Business Legal Center is a nonprofit, public interest law firm established to provide legal resources and be the voice for small businesses in the nation's courts through representation on issues of

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[1] Pursuant to Rule 37, *amici curiae* certify that no counsel for a party authored this brief in whole or in part and that no person or entity, other than amici, their members, or their counsel, has made a monetary contribution to the preparation or submission of this brief. Amici timely notified the parties of their intention to file this amicus brief and both parties have given their consent.

public interest affecting small businesses. The National Federation of Independent Business is the nation's leading small business association, representing members in Washington, D.C., and all 50 state capitals. Founded in 1943 as a nonprofit, nonpartisan organization, NFIB's mission is to promote and protect the right of its members to own, operate and grow their businesses.

NFIB represents small businesses nationwide, and its membership spans the spectrum of business operations, ranging from sole proprietor enterprises to firms with hundreds of employees. While there is no standard definition of a "small business," the typical NFIB member employs 10 people and reports gross sales of about $500,000 a year. The NFIB membership is a reflection of American small business.

The issue in this case – the ability of a state to tax nonresident corporate investors and seize their funds if the tax is not paid – is of fundamental importance to DRI, small businesses, and the civil defense bar. It is well established that a state's assertion of jurisdiction over nonresident corporate defendants implicates the fairness of the civil justice system. *Walden v. Fiore*, 571 U.S. 277, 283 (2014); *Daimler AG v. Bauman*, 571 U.S. 117, 126 (2014); *Goodyear Dunlop Tires Operations, S.A. v. Brown*, 564 U.S. 915, 918 (2011). Likewise, a state's extraterritorial assessments of taxes and seizures of property to pay those taxes when not voluntarily remitted concern Due Process. California is effectively exercising both its taxing powers and

police powers in Arizona and over non-California residents who lack minimum contacts with the state and thus could not be subjected to personal jurisdiction because they have never "purposefully avail(ed themselves) of the privilege of conducting activities within the forum State . . . ." *Hanson v. Denckla*, 357 U.S. 235, 253 (1958).

Based on the informed interest and relevant experience of its members, DRI has submitted several amicus briefs in recent years in cases presenting issues involving the appropriate constitutionally based limits to the exercise of personal jurisdiction over corporate defendants. See, e.g., *Bristol-Myers Squibb Company v. Superior Court of California*, __ U.S. __, 137 S.Ct. 1773 (2017), *Exxon Mobil Corp. v. Massachusetts*, __ U.S. __, 139 S.Ct. 794 (2019), and *China Terminal & Electric Corp. v. Willemsen*, __ U.S. __, 133 S.Ct. 984 (2013). Similarly, to fulfill its role as the voice for small business, the NFIB Legal Center frequently files amicus briefs in cases that will impact small businesses.

Given the extensive practical experience of DRI and NFIB Legal Center, they are well-suited to explain to the Court why the limits imposed on a state's taxing authority under Due Process and principles of federalism are important to businesses at every level. DRI members frequently defend domestic and international clients in litigation in state and federal courts. DRI members also routinely advise their domestic and international clients regarding the regulations and potential liability to

which they are subject under state and federal law. Likewise, NFIB Legal Center represents the interests of small businesses across all 50 states.

An important aspect of advising and representing businesses is knowledge regarding when a state is empowered to regulate or tax a business and when it may be haled into a state court. Companies make choices about where and how to conduct their affairs based, in part, on the regulatory and taxing environment. If a state is permitted to ignore this Court's longstanding limitations to a state's exercise of its taxing authority, corporate defendants will find themselves unpredictably subject to taxes and property seizures by states where they do not reside and as to which they have never purposefully availed themselves of the privilege of conducting business.

California's conduct in this case flouts traditional notions of Due Process and state sovereignty, undercuts or entirely abolishes traditional limitations to the reach of that sovereignty, and threatens to inject uncertainty into the well-established principles governing state sovereignty as part of Our Federalism.[2] DRI and

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[2] See *Younger v. Harris*, 401 U.S. 37, 44 (1971) ("[T]he notion of 'comity,' . . . is, a proper respect for state functions, a recognition of the fact that the entire country is made up of a Union of separate state governments, and a continuance of the belief that the National Government will fare best if the States and their institutions are left free to perform their separate functions in

(Continued on next page)

NFIB Legal Center thus have a vital interest in this case.

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their separate ways. This, perhaps for lack of a better and clearer way to describe it, is referred to by many as 'Our Federalism' . . . . ").

SUMMARY OF ARGUMENT

California's extraterritorial tax assessments and seizures on nonresident passive investors violate Due Process and principles of Our Federalism.

This Court has instructed that an entity subjects itself to a state's taxing power only where there exists "some minimum connection, between a state and the person, property or transaction it seeks to tax." *Miller Bros. Co. v. State of Md.*, 347 U.S. 340, 345 (1954). The "minimum connection" analysis, like the minimum contacts analysis for personal jurisdiction, mandates that there must be "'some act by which the defendant purposefully avail[ed] itself of the privilege of conducting activities within the forum State, thus invoking the benefits and protections of its laws." *Goodyear Dunlop Tires Operations, S.A. v. Brown*, 564 U.S. 915, 924 (2011), quoting *Hanson v. Denckla*, 357 U.S. 235, 253 (1958).

This Court has already addressed and rejected the idea that passive investment, standing alone, constitutes the minimum contacts necessary to comport with Due Process. *Shaffer v. Heitner*, 433 U.S. 186, 213 (1977). Moreover, the Court recognizes that the Due Process minimum contacts requirement is an integral part of Our Federalism. The federal system protects the several states against intrusions into their sovereignty by the federal government. At the same time, Our Federalism requires that the power of each sovereign state be prevented from expanding beyond its borders and infringing upon the sovereignty of a sister state.

Thus, not only do minimum contacts preserve Due Process by protecting defendants from "the burdens of litigating in a distant or inconvenient forum," they also "ensure that the States . . . do not reach out beyond the limits imposed on them by their status as coequal sovereigns in a federal system." *World-Wide Volkswagen Corp. v. Woodson,* 444 U.S. 286, 291-92 (1980).

It is important that this Court address and reaffirm the limitations on a state's authority to tax out-of-state residents by granting Arizona's motion for leave to file a bill of complaint and declaring California's "doing business" tax unconstitutional. Businesses must be assured that their mere status as passive investors will not render them liable for taxes and in danger of extraterritorial seizure of their assets.

ARGUMENT

California's so-called "doing business" tax scheme not only offends but upends "traditional notions of fair play and substantial justice" and well-established limits on state sovereignty through the extraterritorial assessment of taxes against nonresident passive investors in limited liability companies who lack minimum contacts with California, and an extraterritorial – indeed extrajudicial – seizure of funds if such taxes are not paid.

The issue in this case is of utmost importance to DRI members and NFIB Legal Center because it involves the coercive power of the state used against nonresident passive investors. The limits on a state's taxing power are mandated by the Due Process Clause, and indeed, our entire federal system.

A. California's extraterritorial tax assessments and seizures violate Due Process

As explained in Arizona's brief, Cal. Rev. Tax Code §§ 1941, 17948, and 23153(b)(3) impose a "doing business" tax on limited liability companies, limited liability partnerships, and corporations. Pl. Br., p. 5. The California Tax Board has asserted that *a mere ownership interest* in an LLC doing business in California equates to doing business in California, despite the recognized lack of presence or other activity in California. Pl. Br., pgs. 6-7; Complaint, Ex. A, Legal Ruling 2014-01. If an entity fails to pay the tax assessed, the Tax Board, acting under authority

purportedly granted by § 18670(a) and not through any court system, issues a seizure order to a bank or employer. Pl. Br., p. 9.

The question before the Court is whether a nonresident passive investor in an LLC, "by its acts or course of dealing, has subjected itself to the taxing power of [California]" such that the "doing business" tax comports with Due Process. *Miller Bros. Co. v. State of Md.*, 347 U.S. 340, 344 (1954). This Court has previously held that the answer depends on whether there exists "some minimum connection, between a state and the person, property or transaction it seeks to tax." *Id.* at 345. There must also be "a rational relationship between the tax and the values connected with the taxing State." *MeadWestvaco Corp. ex rel. Mead Corp. v. Illinois Dep't of Revenue*, 553 U.S. 16, 24 (2008) (citation and quotation marks omitted). In other words, the question is "whether the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the state," i.e., "whether the state has given anything for which it can ask return." *Id.* (citation and punctuation omitted). When a tax on an activity is involved, "there must be a connection to the activity itself, rather than a connection only to the actor the State seeks to tax." *Allied-Signal, Inc. v. Dir., Div. of Taxation*, 504 U.S. 768, 777-78 (1992).

The "minimum connection" analysis is akin to the minimum contacts analysis for personal jurisdiction. As is relevant here, the issue of whether passive interests constitute adequate minimum contacts to confer personal jurisdiction on an out-of-

state resident, and by implication, the power to tax, was addressed – and soundly rejected – in *Shaffer v. Heitner*, 433 U.S. 186 (1977). In that case, a shareholder's derivative action, the Delaware court asserted personal jurisdiction over present and former officers and directors of a Delaware corporation and its subsidiary based solely on their ownership of stock and other corporate rights. The court acted under a state statute that considered Delaware the situs of ownership of all stock in Delaware corporations. This Court observed that the property "is not the subject matter of this litigation, nor is the underlying cause of action related to the property." *Id.* at 213. Therefore, stock ownership did not "provide contacts with Delaware sufficient to support the jurisdiction of that State's courts over appellants. If it exists, that jurisdiction must have some other foundation." *Id.*

In its discussion, the Court noted that the criteria for making a finding that a corporation was "doing business" in the forum state involves basic fairness, that is, courts must attempt "to ascertain what dealings make it just to subject a foreign corporation to local suit." *Shaffer*, 433 U.S. at 203 (citation and quotation marks omitted). The Court instructed that the Due Process Clause "does not contemplate that a state may make binding a judgment in personam against an individual or corporate defendant with which the state has no contacts, ties, or relations." *Id.* at 204, quoting *International Shoe Co. v. Washington,* 326 U.S. 310, 319 (1945).

In an attempt to show that such minimum contacts were present, the appellee in *Shaffer* argued, among other things, "that by accepting positions as officers or directors of a Delaware corporation, appellants performed the acts required [to assert personal jurisdiction]," and "that Delaware law provides substantial benefits to corporate officers and directors," which "benefits were at least in part the incentive for appellants to assume their positions." 433 U.S. at 215-16. The appellee thus concluded that it was "'only fair and just' to require appellants, in return for these benefits, to respond in the State of Delaware when they are accused of misusing their power." *Id.* at 216.

This Court flatly disagreed that the appellants "purposefully availed themselves of the privilege of conducting activities within the forum State in a way that would justify bringing them before a Delaware tribunal." *Shaffer,* 433 U.S. at 216 (citation and punctuation omitted). The Court's straightforward reasoning is directly relevant here in determining whether California's tax scheme comports with due Process. It does not. The passive investors in LLCs doing business in California, like the stockholders in *Shaffer*, lack the minimum connections necessary for California to tax them. As this Court explained:

> Appellants have simply had nothing to do with the State of Delaware. . . . [I]t strains reason to suggest that anyone buying securities in a corporation formed in Delaware 'impliedly consents'

> to subject himself to Delaware's jurisdiction on any cause of action.

Shaffer v. Heitner, 433 U.S. at 216 (citation and punctuation omitted).

Also instructive is *Shaffer*'s lengthy discussion of the history of in personam, in rem, and quasi in rem jurisdiction. The Court's analysis of the evolution of jurisdiction led to the conclusion, without equivocation, that "all assertions of state-court jurisdiction must be evaluated according to the standards set forth in *International Shoe* and its progeny." *Shaffer*, 433 U.S. at 212. In other words, the Court extended "the standard of fairness and substantial justice set forth in *International Shoe*" – that is, an analysis of minimum contacts – to actions in rem and quasi in rem as well because "(t)he phrase, 'judicial jurisdiction over a thing', is a customary elliptical way of referring to jurisdiction over the interests of persons in a thing." *Shaffer*, 433 U.S. at 206, quoting Restatement (Second) of Conflict of Laws s 56, Introductory Note (1971). In short, the "the presence of the property alone would not support the State's jurisdiction." *Id.*, at 209.

The Courts of Appeals agree that passive interests standing alone do not constitute contacts sufficient to confer personal jurisdiction, and thus by implication, are not sufficient to confer taxing authority. See *Cent. States, Se. & Sw. Areas Pension Fund v. Reimer Express World Corp.*, 230 F.3d 934, 943 (7th Cir. 2000) ("We join other courts in finding that stock ownership in or affiliation with a

corporation, without more, is not a sufficient minimum contact."); *GCIU-Employer Ret. Fund v. Coleridge Fine Arts*, 700 F. App'x 865, 869 (10th Cir. 2017) (Finding "no legal authority for the proposition that the acquisition of a company that participates in a multiemployer pension plan is, by itself, sufficient to establish personal jurisdiction over the acquiring company and no reasoned argument to support the notion that such a rule would comport with due process."); *Barrett v. Lombardi*, 239 F.3d 23, 27 (1st Cir. 2001) ("The mere acceptance of shares transferred from within the forum state, without more, does not constitute a minimum contact sufficient to subject a foreign corporation to jurisdiction in that state's courts."); *Dean v. Motel 6 Operating L.P.*, 134 F.3d 1269, 1273-74 (6th Cir. 1998) ("[A] company does not purposefully avail itself merely by owning all or some of a corporation subject to jurisdiction."). See also *Transure, Inc. v. Marsh & McLennan, Inc.*, 766 F.2d 1297, 1299 (9th Cir. 1985) ("The existence of a parent-subsidiary relationship is insufficient to establish personal jurisdiction . . . .").

The importance of the minimum contacts standard to the health of the business environment cannot be overstated. In the context of personal jurisdiction, the Court has recognized that "[t]he Due Process Clause, by ensuring the 'orderly administration of the laws,' *International Shoe*, 326 U.S. at 319, gives a degree of predictability to the legal system that allows potential defendants to structure their primary conduct with some minimum assurance as to where that conduct will and will not render them liable to suit." *World-Wide Volkswagen*,

444 U.S. at 297. Thus, "[w]hen a corporation purposefully avails itself of the privilege of conducting activities within the forum State, it has clear notice that it is subject to suit there, and can act to alleviate the risk of burdensome litigation by procuring insurance, passing the expected costs on to customers, or, if the risks are too great, severing its connection with the State." *Id.* (citation and quotation marks omitted).

In this case, California's exercise of its taxing power and related seizures on nonresidents based on the attenuated "activity" of passive investment or the mere possession of an ownership interest in an LLC, not only violates Due Process but also thwarts the ability of DRI members and NFIB Legal Center to advise businesses regarding how to conduct operations so as to avoid tax liability and the unreasonable seizure of assets.

B. California's extraterritorial tax assessments and seizures do not comport with principles of Our Federalism

The Due Process minimum-contacts prerequisite to asserting personal jurisdiction or imposing a tax on an out-of-state resident is part of the larger concept of Our Federalism.

Our Federalism depends on a proper calibration and equilibrium between and among the states and federal government. This Court has repeatedly recognized that the "federalist structure of joint sovereigns preserves to the people numerous

advantages." *Gregory v. Ashcroft*, 501 U.S. 452, 458 (1991). Federalism "assures a decentralized government that will be more sensitive to the diverse needs of a heterogenous society; it increases opportunity for citizen involvement in the democratic process; it allows for more innovation and experimentation in government; and it makes government more responsive by putting the States in competition for a mobile citizenry." *Id.*, citing generally McConnell, Federalism: Evaluating the Founders' Design, 54 U.Chi.L.Rev. 1484, 1491-1511 (1987); Merritt, The Guarantee Clause and State Autonomy: Federalist for a Third Century, 88 Colum. L. Rev. 1, 2-10 (1988).

To this end, the Court has emphasized the importance of protecting the foundational structural protections of Our Federalism. See *Texas v. White*, 7 Wall. 700, 19 L.Ed. 227 (1869) ("the preservation of the States, and the maintenance of their governments, are as much within the design and care of the Constitution as the preservation of the Union and the maintenance of the National government").

This Court has protected the several states against intrusions into their sovereignty by the federal government. See e.g., *Printz v. United States*, 521 U.S. 898, 925 (1997); *Bd. of Trustees of the Univ. of Ala. v. Garrett*, 531 U.S. 356, 368 (2000); *Kimel v. Flo. Bd. of Regents*, 528 U.S. 62, 89 (2000); *Nat'l Fed'n of Indep. Bus. v. Sebelius*, 567 U.S. 519, 585 (2012). And it has protected the several states as to their essential functions. See e.g., *Mullaney v.*

Wilbur, 421 U.S. 684 (1975) (federal courts defer to states on interpretation of their state constitutions).

These benefits of Our Federalism require that the several states operate within the sphere of sovereignty that they have been constitutionally afforded; and that they not operate extraterritorially or beyond their sovereignty. Just as the jurisdiction, powers, and authority of the state and federal government vis-à-vis each other must be kept in proper equilibrium, so too, the power of each sovereign state cannot be permitted to intrude beyond its borders and impinge on the jurisdiction of a sister state.

One key tool for ensuring that the several states do not intrude beyond their territorial boundaries in the exercise of jurisdiction or the taxing power is the enforcement of limits that comport with Due Process. This Court has emphasized that, although jurisdictional standards have become more relaxed in light of advances in technology, transportation, and communications, such standards maintain their critical importance in the federal structure.

> [T]he requirements for personal jurisdiction over nonresidents have evolved from the rigid rule of *Pennoyer v. Neff*, 95 U.S. 714, 24 L.Ed. 565, to the flexible standard of *International Shoe Co. v. State of Washington*, 326 U.S. 310, 66 S.Ct. 154, 90 L.Ed. 95. But it is a mistake to assume that this trend

> heralds the eventual demise of all restrictions on the personal jurisdiction of state courts. See *Vanderbilt v. Vanderbilt*, 354 U.S. 416, 418, 77 S.Ct. 1360, 1362, 1 L.Ed.2d 1456. *Those restrictions are more than a guarantee of immunity from inconvenient or distant litigation. They are a consequence of territorial limitations on the power of the respective States*. However minimal the burden of defending in a foreign tribunal, a defendant may not be called upon to do so unless he has had the 'minimal contacts' with that State that are a prerequisite to its exercise of power over him.

Hanson, 357 U.S. at 250-51 (emphasis added).

Likewise, in *Shaffer*, the Court recognized that the minimum contacts requirement for asserting personal jurisdiction – or imposing a tax – is part of the larger concept of federalism.

> the inquiry into the State's jurisdiction over a foreign corporation appropriately focused not on whether the corporation was "present" but on whether there have been
>
> "such contacts of the corporation with the state of the forum as make it reasonable, in the context of our federal

> system of government, to require the corporation to defend the particular suit which is brought there."

Shaffer, 433 U.S. at 203, quoting *International Shoe*, 326 U.S. at 317. Again in *World-Wide Volkswagon*, the Court emphasized the connection between the minimum contacts requirement and federalism:

> The concept of minimum contacts . . . can be seen to perform two related, but distinguishable, functions. It protects the defendant against the burdens of litigating in a distant or inconvenient forum. And it acts to ensure that the States through their courts, do not reach out beyond the limits imposed on them by their status as coequal sovereigns in a federal system.

World-Wide Volkswagen, 444 U.S. at 291-92. In short:

> Even if the defendant would suffer minimal or no inconvenience from being forced to litigate before the tribunals of another State; even if the forum State has a strong interest in applying its law to the controversy; even if the forum State is the most convenient location for litigation, *the Due Process Clause, acting as an instrument of interstate federalism*, may sometimes act to divest

> the State of its power to render a valid judgment.

Id. at 294 (emphasis added).

Here again the justification for California's tax assessments on nonresidents – passive investment in a corporation – was soundly rejected in *Shaffer* both for failure to comply with the minimum contacts requirement of Due Process and as "inconsistent with that constitutional limitation on state power." *Shaffer*, 433 U.S. at 216-217.

CONCLUSION

It is important this Court address and reaffirm the limitations on a state's authority to tax out-of-state residents. Businesses must be assured that their mere status as a passive investor will not render them liable for taxes and in danger of an unconstitutional seizure of their assets. Moreover, action from this Court is needed now because forcing affected individuals and entities to litigate the issue in California courts adds insult to injury – just as California lacks the authority to assess taxes and seize assets from nonresidents in the absence of minimum contacts, so, too, its courts lack personal jurisdiction over them. If this Court does not act, some might chose to give in to the extortion rather than spend the additional funds to litigate in a foreign state.

Accordingly, this Court should exercise its original jurisdiction over this matter and grant Arizona's motion for leave to file its bill of complaint.

Respectfully submitted,

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