No. 10-662 NOV 16 2010

IN THE
Supreme Court of the United States

ASWORTH, LLC (f/k/a Asworth Corporation); HTF, LLC (f/k/a HT-Forum, Inc.); and D AVIATION SERVICES, LLC (f/k/a D Aviation Services, Inc.)

Petitioners,

v.

DEPARTMENT OF REVENUE, FINANCE AND ADMINISTRATION CABINET, COMMONWEALTH OF KENTUCKY (f/k/a Revenue Cabinet, Commonwealth of Kentucky)

Respondent.

ON PETITION FOR A WRIT OF CERTIORARI TO THE KENTUCKY COURT OF APPEALS

PETITION FOR A WRIT OF CERTIORARI

MARK F. SOMMER
JENNIFER Y. BARBER
GREENEBAUM DOLL & MCDONALD PLLC
3500 National City Tower
101 South Fifth Street
Louisville, KY 40202-3197
(502) 587-3570

JENNIFER S. SMART
Counsel of Record
GREENEBAUM DOLL & MCDONALD PLLC
300 West Vine Street
Suite 1100
Lexington, KY 40507-1665
(859) 288-4672
jss3@gdm.com

Counsel for Petitioners

233317

COUNSEL PRESS
(800) 274-3321 • (800) 359-6859

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QUESTIONS PRESENTED

1. Whether a State violates the Commerce Clause of the U.S. Constitution by subjecting an out-of-state corporate partner to income tax when the partner has no property or employees in the State and the partner's only connection with the State is the holding of passive investment interests in entities that have in-state business operations?

2. Whether a State violates the Due Process Clause of the U.S. Constitution by enacting non-curative tax legislation that retrospectively denies interest on overpayments of court-ordered tax refunds on a retroactive basis of up to 17 years?

RULE 29.6 STATEMENT

Asworth, LLC, formerly known as Asworth Corporation ("Asworth"), does not have a parent corporation nor any publicly held corporation that owns 10% or more of its stock.

HTF, LLC, formerly known as HT-Forum, Inc. ("HTF"), does not have a parent corporation nor any publicly held corporation that owns 10% or more of its stock.

D Aviation Services, LLC, formerly known as D Aviation Services, Inc. ("D Aviation"), does not have a parent corporation nor any publicly held corporation that owns 10% or more of its stock.

HTF and D Aviation are both 100% owned by Asworth.

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PETITION FOR A WRIT OF CERTIORARI

Petitioners respectfully petition this Court for a Writ of Certiorari to review the Opinion of the Kentucky Court of Appeals rendered on November 20, 2009.

OPINIONS BELOW

The Opinion of the Kentucky Court of Appeals is unreported and is reprinted in its entirety in Petitioners' Appendix ("Pet. App."). The Supreme Court of Kentucky's Order of August 18, 2010 denying Petitioners' Motion for Discretionary Review is also unreported and is reprinted at Pet. App. 46a. The Order of the Franklin Circuit Court is also unreported and is reprinted at Pet. App. 34a. The Order of the Kentucky Board of Tax Appeals is likewise unreported and is reprinted at Pet. App. 27a.

JURISDICTION

The Opinion for which certiorari is sought, issued by the Kentucky Court of Appeals, was rendered on November 20, 2009. Pet. App. 1a. Petitioners timely filed a Motion for Discretionary Review with the Supreme Court of Kentucky on December 18, 2009, which was denied on August 18, 2010. Pet. App. 46a. This Court has jurisdiction pursuant to 28 U.S.C. § 1257(a).

CONSTITUTIONAL AND STATUTORY PROVISIONS INVOLVED

The constitutional provisions involved are the Commerce and the Due Process Clauses of the U.S. Constitution.

The Commerce Clause provides: "the Congress shall have Power . . . To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes." U.S. CONST. art. I, § 8.

The Due Process Clause of the Fourteenth Amendment to the U.S. Constitution provides, in pertinent part: "[N]or shall any state deprive any person of life, liberty, or property, without due process of law." U.S. CONST. amend. XIV, § 1.

The Kentucky statutory provisions involved in this case are set forth at Pet. App. 47a, all of which are subservient to the constitutional sections cited here.

INTRODUCTION

A. Physical Presence – *Quill Corp. v. North Dakota*

This Petition for a Writ of Certiorari presents the important question of whether the Commerce Clause permits a state to impose income tax on an out-of-state corporate partner having no in-state physical presence, for no reason other than it is a passive investor in an entity that does business in the taxing state. For nearly 20 years, this question has been litigated in countless forums with conflicting outcomes. This Court should intervene to address whether states have the power and authority to reach across jurisdictional lines and subject out-of-state corporate partners to taxation when they maintain no property or employees in the taxing jurisdiction. This issue is as fundamental as the Commerce Clause and is of pressing significance to American business.

Many states are exceeding the constitutional limits of power as set forth in the Commerce Clause and as proclaimed by this Court, holding that physical presence is not a predicate to taxing income, in plain violation of this Court's holdings in *Nat'l Bellas Hess, Inc. v. Dep't of Revenue of Illinois*, 386 U.S. 753 (1967) and *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). Other states are following these dictates and the decisions of this Court, correctly holding that physical presence is required before states may subject out-of-state companies to income tax.

This issue has been litigated in appellate courts of at least 20 states and many lower forums with conflicting results. Simply put, the courts are in a state of chaos on whether physical presence is required as a constitutional predicate prior to taxation. Some courts, such as the court below in this case, have held that out-of-state partners are subject to state income taxation based solely on the holding of passive investment interests, even in the face of the partner having no physical presence in the taxing state. Other states have held to the contrary. Further, at least 35 states have enacted legislation, regulations or policies applying what state tax expert Professor Richard D. Pomp has referred to as a "metaphysical presence" test in income tax settings and stating that holding a partnership interest alone creates tax nexus. Many states are thus flouting this Court's physical presence requirement in *Quill*.

Beyond Kentucky, the lower court's decision will have significant impact on tax administration and enforcement in every state. The detrimental effect of the decision affects corporate taxpayers since it wrongly preempts and substitutes this Court's Commerce Clause "physical presence" standard with a Due Process "protection and benefits" standard. This Court's intervention is necessary to ensure that taxpayers, legislators, and administrators are appropriately advised regarding the valid constitutional parameters of state tax nexus or jurisdictional authority to tax. If not, and were the lower court's decision left to stand, virtually every out-of-state taxpayer receiving investment income from a company operating in another state will now be subject to that state's taxation.

As Justice White accurately predicted, it was a "sure bet" that the "vagaries of 'physical presence'" and the scope of the *Quill* Opinion "will be tested to their fullest in our courts." *Quill*, 504 U.S. at 331 (White, J., concurring in part and dissenting in part). As the *Quill* majority admitted, "our law in this area is something of a 'quagmire' and the 'application of constitutional principles to specific state statutes leaves much room for controversy and confusion and little in the way of precise guides to the states in the exercise of their indispensable power of taxation.'" *Quill,* 504 U.S. at 315-16. The avalanche of litigation on whether the physical presence rule governs income taxes or only sales and use taxes, post-*Quill*, demonstrates intervention is needed.

Many states, including Tennessee, Texas and Michigan, correctly analyzed *Quill* and held that this Court's affirmation of the physical presence rule in the sales and use tax setting did not equate to a rejection of that rule in other state tax (*e.g.*, income tax) settings.

Accordingly, these states held that non-resident companies with no in-state property, representatives or employees were not subject to state income or franchise taxes.

However, other states have misread *Quill*, holding that the physical presence rule is limited to sales and use taxes and does not apply to income taxes or other taxes. Tellingly, most states that upheld non-sales and use taxation without physical presence did so in cases involving companies that licensed intellectual property for in-state use by related companies, which raised the specter of sham transactions, no business purpose, and other common law doctrines. These cases are distinguishable from the instant situation, which involves no intangible property in Kentucky.

The lower court's decision in this case demonstrates that the departure from the physical presence rule is not limited to those types of cases; it is now being applied to traditional investment relationships. The lower court specifically recognized from the stipulated facts that Petitioners maintained no Kentucky property or employees — their sole connection with Kentucky was the receipt of passive investment income from non-Kentucky entities doing business there. Pet. App. 2a. This notwithstanding, the lower court questioned whether *Quill's* physical presence standard applies in the income tax context, concluding it "is unclear," and ruled that Petitioners' receipt of income from investments in entities with Kentucky operations was sufficient to meet substantial nexus under the Commerce Clause, *merely because the entities [not Petitioners] received protection and benefits from Kentucky*. Pet. App. 11a.

The lower court plainly erred by substituting this Court's Commerce Clause "substantial nexus" standard with the "purposeful availment" standard that defines the Due Process Clause so-called, "minimum contacts." *See Burger King Corp. v. Rudzewicz*, 471 U.S. 462 (1985). As this Court reiterated in *Quill*, the Commerce Clause's limits on state taxation are more restrictive than the "minimum contacts" needed to support personal jurisdiction under the Due Process Clause and are "animated by different constitutional concerns and policies." *Quill*, 504 U.S. at 312-13. As well-reminded in *Quill*, ". . . a corporation may have the 'minimum contacts' with a taxing State as required by the Due Process Clause, and yet lack the 'substantial nexus' with that State as required by the Commerce Clause." *Id.* at 313.

Here, the lower court relied solely upon an erroneous decision from an intermediate appellate court in Illinois holding that out-of-state limited partners are subject to income tax on income received from investments in in-state partnerships, despite having no actual physical presence in Illinois. *See Borden Chemicals and Plastics, LP v. Zehnder*, 726 N.E.2d 73 (Ill. App. 2000). In contrast, however, other state courts in similar fact patterns have held to the contrary. For example, the New Jersey Tax Court recently held in *BIS LP, Inc. v. Dir., Div. of Taxation*, 25 N.J.Tax 88 (N.J. Tax 2009), *appeal docketed*, No. A1172-09 (N.J. Super. Ct. App. Div. Nov. 9, 2009), that an out-of-state limited partner with no physical presence in a state cannot be constitutionally taxed by that state under the Commerce Clause, relying on this Court's decisions in *F.W. Woolworth Co. v. Taxation & Revenue Dep't*, 458 U.S. 354 (1982), and

ASARCO, Inc. v. Idaho State Tax Comm'n, 458 U.S. 307 (1982).

The decision below is one of the most far-reaching departures from the *Quill* physical presence rule to date by a state court, notwithstanding one of the narrowest and purest fact patterns for this Court to consider. If the lower court's decision is left to stand, any out-of-state owner receiving passive investment income from an entity located in a state in which the owner has no physical presence or any physical connection whatsoever, may now be subjected to income taxation jurisdiction by that state. By parity of reasoning, traditional dividend income earned by an out-of-state resident will now be taxable in the distributing state. This is not the law of this Court.

Much has changed in law, society, business, politics and the world during the nearly 20 years since this Court ruled in *Quill* that physical presence in a jurisdiction is a predicate to the constitutional imposition of a state tax. One thing, however, has been and remains constant: the continued disagreement everywhere but at this Court as to the applicability of the principles of *Quill* in state and local taxation. Consequently, this Court should now intervene to resolve these conflicts, foreclose another 20 years of controversy and uncertainty, and re-establish the limits on state taxation under the Commerce Clause as the framers of the Constitution intended.

B. "Modest" Retroactivity – *United States v. Carlton*

A second issue for the Court's consideration involves the retroactive, non-curative tax legislation enacted to the detriment of Petitioners and all other similarly situated taxpayers. In sanctioning this legislation, the lower court ignored the "modesty" requirement of *United States v. Carlton*, 512 U.S. 26 (1994), when analyzing this facially retroactive tax legislation. Justice Blackmun's *Carlton* Opinion, buttressed by the concurring Opinion of Justice O'Connor in *Carlton*, plainly requires a "modesty" analysis. For no other reason than this, the underlying Opinion, simply the latest of many state appellate court decisions to so find, should be reviewed and certiorari granted.

The period of retroactivity *is* a fundamental element to be considered by the judiciary when evaluating retroactive tax legislation; regardless of length, the term must be "modest." The singular point of law arising from *Carlton* traces to the overriding rule that the period of retroactivity must be "modest." As Justice Blackmun wrote for the majority therein, succinctly and plainly, ". . . Second, Congress acted promptly and established only a modest period of retroactivity." *Carlton*, 512 U.S. at 32.

So as to resolve an ever-widening split among the states and bring to a conclusion the plethora of state court litigation and almost continuous retroactive legislating underway, this Court should grant certiorari, hear the dispute, and plainly and unequivocally confirm, 16 years after *Carlton*, that the period of retroactivity in implementing otherwise constitutional, non-curative tax legislation, retroactive on its face, must be "modest."

The concerns of today's citizens as to retrospective tax legislation are the same as those of our founding forefathers in the late 1780s. Today's citizens expect, and in fact are entitled under the Constitution, to be governed by the law of the several states, which, when applied, is sound and fair under the microscope of the Due Process Clause. The national trend on this topic violates these core principles; review by this Court is warranted, necessary and requested.

During the debates leading up to this country's Constitution, the great leaders of our country *specifically addressed* their concern for what they termed "retrospective laws in civil cases." *See* DEBATES IN THE FEDERAL CONVENTION OF 1787 AS REPORTED BY JAMES MADISON, AUG. 28, 1787, H.Doc. No. 398, at 626, 69th Cong. 1st Sess. (1927); *see also* DEBATES IN THE FEDERAL CONVENTION OF 1787 AS REPORTED BY JAMES MADISON, AUG. 29, 1787, H.Doc. No. 398, at 632, 69th Cong. 1st Sess. (1927).[1]

Viewed from our cultural perspective and who we as a people truly are, the scrivener reports of James Madison are most telling — the dilemma faced today, hundreds of years since James Madison recorded such debates, is just as hearty and just as healthy. Now, however, it is time for this Court to once again speak with clarity and authority, and close the debate on this issue.

1. From a historical perspective, after debate and discussion, the specific reference banning and usurping the power of the states to enact retrospective laws in civil cases was struck, and the ban on legislation impeding contracts took its place. *See generally* U.S. CONST. art. I, § 10.

Retroactive taxation is the very essence of arbitrary action by a legislative body. The arbitrary, and thus punitive, nature of Kentucky's retroactive tax interest statutory changes in question is best demonstrated by briefly reviewing the undisputed facts.

The earliest tax refund at issue was for year 1993 and was filed in 1998; the first Petition of Appeal was filed in 2000 at the Kentucky Board of Tax Appeals ("Board"). After a hearing, the Board ruled in 2006 and ordered a refund payable to Petitioners of approximately $5.1 million, plus interest authorized by law. On first appeal, while reducing the refund award on a substantive issue, the Franklin Circuit Court not only affirmed much of the refund ordered and the interest thereon, but extraordinarily ordered that Kentucky immediately pay the refund. Rather than paying or moving for a Stay of the Order, Respondent appealed.

In conjunction with the Kentucky General Assembly and only weeks after the circuit court Order, Respondent proposed a Bill in 2008, which, on its face, not only changed the interest rate calculus[2] governing the refund within the Judgment in question herein, but also changed the date(s) upon which refund interest commenced to run (*i.e.*, it shortened the number of days of interest *and* reduced the rate of interest). 2008 Ky. Acts. ch. 132 §§ 8, 9, 10, 11, 15.[3]

2. Moving from a rate driven by the "prime rate" as reported by commercial banks, to a rate of prime rate less 2% on refunds and prime rate plus 2% on assessments.

3. *See also* 2009 Ky. Act. ch. 86 §§ 7, 8, 9, 10 & 15. Pet. App. 87a.

Not to be outdone by the plain text of the changes, the Kentucky General Assembly legislatively pronounced that there: (i) was an "emergency;" (ii) the Bill was effective immediately upon the Governor's signature; and (iii) the text "would govern, control and apply to any claim still pending before . . . the judiciary." Pet. App. 74a-86a. Thus, in one fell swoop, two Orders awarding tax interest to Petitioners were materially reduced, and the law in Kentucky was retroactively rewritten in a manner to statutorily justify same. This arbitrary legislative and executive branch action must stop.

Here, in the face of the facts now before this Court, the question is asked whether a 17 year retroactive change to settled tax law, absent any "curative" need,[4] is *per se* unconstitutional under the Due Process Clause and the *Carlton* "modesty" requirement thereunder.

Hearing the instant case allows the Court to clarify the principles of *Carlton* and its progeny, and provide clarity and much needed bright-lines in a dark and murky area of law. Settled expectations must ripen and mature, for if not now, the question posed becomes — when ever? Certiorari is most appropriate in this case.

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4. The legislative history documents, relied upon by the lower court, confirm this.

STATEMENT OF THE CASE

A. Factual Background

Petitioners' core facts are plain and clear; they have no "physical presence" in Kentucky. All relevant facts applicable to this Petition were stipulated and uncontroverted.

Petitioners maintained no offices, no employees, no places of business and had no real, tangible or intangible property in Kentucky — not even on a transitory basis. All were entities created under the laws of states other than Kentucky (*i.e.*, out-of-state companies); Asworth was a Nevada corporation and HTF and D Aviation were Delaware corporations. All maintained their principal places of business outside of Kentucky.

Petitioners' sole "connection" with Kentucky was that they were partners in two Tennessee-based partnerships that did business in Kentucky (Conwood Company, LP and Conwood Sales Co., LP (collectively "Conwood Companies")). The Conwood Companies were in the business of manufacturing and selling smokeless tobacco. Petitioners had no management, input or other type of control in or over the Conwood Companies, and simply held their interests in Conwood Companies as passive investment interests — Petitioners were pure holding companies. Respondent, Department of Revenue, Finance & Administration Cabinet (f/k/a Revenue Cabinet) is the administrative agency of the Commonwealth of Kentucky, whose responsibility it is to assess and enforce collection of various taxes, including corporation income taxes.

Petitioners filed original Kentucky corporation income tax returns and paid Kentucky corporation income tax calculated by using the standard three-factor apportionment formula of Ky. Rev. Stat. § 141.120, assimilating their individual property, payroll and sales metrics with those from the Conwood Companies to determine the amount of income properly subject to tax by Kentucky.

Respondent undertook a series of audits of Asworth[5] and issued corporation income tax assessments for tax years ending January 31, 1993 through January 31, 1996, contending that it should have apportioned additional income to Kentucky. Asworth disagreed, paid the tax and timely filed amended 1993-1996 returns pursuant to Ky. Rev. Stat. § 134.580, seeking refunds of corporation income tax overpayments on the basis that they had no nexus with Kentucky pursuant to, *inter alia*, the Commerce Clause and Ky. Rev. Stat. § 141.040. Petitioners later filed amended returns for tax years 1997 through 1999 on the same grounds. Respondent denied Petitioners' refund claims and the dispute moved on.

B. Proceedings Below

Petitioners appealed Respondent's denials of their refund claims to the Board. Petitioners contended that they had no physical presence in Kentucky and therefore

5. HTF and D Aviation were not audited by Respondent nor issued tax assessments.

did not have tax nexus with the state pursuant to, *inter alia*, the Commerce Clause and Kentucky statutory law.[6]

After a hearing on the merits, the Board agreed with Petitioners, finding no tax nexus with Kentucky under Ky. Rev. Stat. § 141.040 because Petitioners did not have any property or employees, and therefore did not have the required physical presence in Kentucky. By ruling on state grounds only, the Board did not reach Petitioners' constitutional assertions. By a January 2006 Order, the Board awarded refunds of all tax overpayments totaling $5.1 million, plus mandatory refund interest pursuant to Ky. Rev. Stat. § 131.183. Pet. App. 47a-50a.

On February 24, 2006, Respondent appealed the Board's Order to the Franklin Circuit Court. In December 2007, the court issued a split decision, holding that Petitioners had tax nexus under Kentucky's statutory scheme, the Commerce Clause and the Due Process Clause, but holding that the proper method of calculation of tax required the use of the three-factor apportionment and assimilation method (based on property, payroll and sales) to determine the amount of tax due to Kentucky. Pet. App. 42a-43a. The Franklin Circuit Court held that Petitioners had nexus, applying *Geoffrey, Inc. v. South Carolina Tax Comm'n*, 437

6. Petitioners also contended that they were not subject to tax under the Due Process Clause, and contended, in the alternative, that if they were subject to corporate income taxation by Kentucky, traditional three-factor apportionment methodology and assimilation of their apportionment factors with those of the Conwood Companies was constitutionally and statutorily required to determine the proper amount of income by Kentucky. These questions are not being put before this Court.

S.E.2d 13 (S.C. 1993), *cert. denied*, 510 U.S. 992 (1993) and *Borden Chemicals and Plastics, LP v. Zehnder*, 726 N.E.2d 73 (Ill. App. 2000). Pet. App. 42a. Because a refund still resulted, the circuit court took the extraordinary step of awarding immediate refunds of tax overpayments, plus refund interest pursuant to the version of Ky. Rev. Stat. § 131.183 in effect at the time. Pet. App. 44a.

On December 17, 2007, Respondent appealed the Order to the Kentucky Court of Appeals regarding the circuit court's findings on apportionment, and did not pay the ordered refund. Petitioners filed a cross-appeal regarding the court's findings on nexus and contended that the Commerce Clause and Due Process Clause prohibited Kentucky's imposition of corporate income tax under the facts before the Court because they did not have physical presence or sufficient minimum contacts in Kentucky. Petitioners subsequently filed an unopposed Motion for Leave to Correct Mathematical Error in Circuit Court's Order and to Allow Parties to Brief Issues Concerning House Bill 704 ("Motion").[7]

7. House Bill 704 was enacted in 2008 and retroactively amended Ky. Rev. Stat. § 131.183 [the statute relied upon by the Board and the circuit court to award interest to Petitioners], Ky. Rev. Stat. §§ 134.580 and 141.235 to change Kentucky's tax refund scheme to reduce the rate of interest paid on refunds from "prime rate" to "prime less 2%," and the calculation start date, so that interest on any tax refund would no longer be calculated beginning 60 days from the latter of the due date of the return or payment of the tax, but would begin to accrue on the date of the filing of an amended return requesting refunds. As a result, in all cases in which amended returns are filed after the due date of the original return and after the date of payment of the tax [which is nearly always], the amount of interest paid by Respondent on all refund claims, including those at issue here, are decreased. *See* 2008 Ky. Acts. ch. 132 §§ 8, 9, 10, 11 & 15.

Petitioners advised the court regarding another enactment, 2009 House Bill 216, which also retroactively amended the law, similarly to House Bill 704, which directly impacted and reduced the (refund) Judgment of Petitioners. *See* 2009 Ky. Acts. ch. 86 §§ 7, 8, 9, 10 & 15. By Order dated April 24, 2009, the court granted Petitioners' Motion and ordered briefing by the parties regarding all issues concerning House Bills 704 and 216 (collectively, "Bills").

The court ultimately rendered its November 2009 decision, affirming the circuit court's determination that Kentucky had statutory authority to tax Petitioners under Kentucky law and had constitutional authority to tax Petitioners under the Commerce Clause. Notwithstanding an assertion that *Quill's* physical presence rule as applied to income tax cases was "unclear," the court held that physical presence existed for Commerce Clause purposes based on Petitioners' receipt of income from the investment interests held in the Tennessee partnerships doing business in Kentucky. Pet. App. 11a.

The court also took judicial notice of the Bills, rejected Petitioners' contentions that *Carlton's* "modesty" requirement was violated by the severe retroactive nature of the Bills, and held that the Bills did not violate, *inter alia*, the Due Process Clause. As to the retroactive period, the court specifically held that *Carlton* "did not establish . . . a 'modesty requirement;' rather, the majority simply noted with favor that 'Congress acted promptly and established only a modest period of retroactivity.'" Pet. App. 20a.

On December 18, 2009, Petitioners timely filed a Motion for Discretionary Review with the Supreme Court of Kentucky, seeking review of the Court of Appeals' holdings. Petitioners' motion was denied on August 18, 2010.

REASONS FOR GRANTING THE PETITION

I. WITHOUT FURTHER REVIEW, THE KENTUCKY DECISION, WHICH ADDRESSES AN IMPORTANT FEDERAL QUESTION OF COMMERCE CLAUSE NEXUS, WILL STAND IN CONFLICT WITH DECISIONS OF OTHER STATE COURTS

Notwithstanding the Parties' Stipulations that Petitioners had no property or employees in Kentucky, the lower court in this case held through its minimalistic and erroneous analysis of the Commerce Clause that Petitioners had "physical presence" in Kentucky sufficient to subject them to corporate income tax based on Kentucky's protection and benefits provided to two Tennessee-based partnerships and Petitioners' passive investments in those partnerships. Pet. App. 11a.

The lower court's decision is at odds with several cases from sister states and represents the latest of a widening split of authorities. Attached for the Court's review is a map illustrating the split among Kentucky's sister states, representing 9 states following *Quill's* physical presence requirement in non-sales tax cases and 14 states rejecting *Quill* in non sales tax cases.[8] Pet.

8. Also attached is a Table of Authorities referenced in the map. Pet. App. 121a.

App. 120a. Further, at least 35 states have enacted legislation, regulations or policies specifically rejecting the physical presence test in income tax settings and stating that holding partnership interests alone creates tax nexus, again contrary to this Court's holding in *Quill.*[9]

The lower court below erroneously relied upon *Borden Chemicals and Plastics, LP v. Zehnder*, 726 N.E.2d 73 (Ill. App. 2000) (holding that limited partner had physical presence in Illinois for Commerce Clause purposes). However, the Illinois court's decision stands in stark contrast to the New Jersey Tax Court's decision in *BIS LP, Inc. v. Dir., Div. of Taxation*, 25 N.J. Tax 88 (N.J. Tax 2009), *appeal docketed*, No. A1172-09 (N.J. Super. Ct. App. Div. Nov. 9, 2009). In *BIS*, the court held that BIS, as a passive investor in a partnership with New Jersey operations, was not subject to New Jersey corporation business tax. *Id.* (citing *F.W. Woolworth Co.* and *ASARCO, Inc., supra*).[10]

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9. *See* 2010 SURVEY OF STATE TAX DEPARTMENTS, pp. 20-22; 42-43 (BNA State Tax ed., BNA) (2010); *See*, e.g., Ky. Rev. Stat. § 141.040 (effective 2005); Conn. Gen. Stat. § 12-214(a)(3); Iowa Code § 422.33(1); S.C. Code Ann. 12-6-530; Wis. Stat. § 71.23(2).

10. The lower court's decision in this case is also contrary to the Alabama state court's decision in *Lanzi v. Alabama Dep't of Revenue*, 968 So.2d 18 (Ala. App. 2006) (nonresident limited partner was not subject to Alabama income taxes under the Due Process Clause; Commerce Clause argument not reached by the court) and the Supreme Court of Missouri's decision in *Acme Royalty Co. v. Dir. of Revenue*, 96 S.W.3d 72 (Mo. 2002). Further, many lower courts and administrative tribunals have also considered, and are continuing to consider, this issue. *See Cerro Copper Prod., Inc. v. Alabama Dep't of Revenue*, No. F. 94-444, 1995 WL 800114 (Ala. Dep't of Revenue, Admin. Law Div.

(Cont'd)

The lower court's decision is also squarely at odds with the Texas Court of Appeals' decision in *Rylander v. Bandag Licensing Corp.*, 18 S.W.3d 296 (Tex. App. 2000). *Rylander* upheld *Quill's* physical presence rule and held that Texas could not impose the state's franchise tax, a tax on the privilege of doing business in the state, on an out-of-state corporation that did not have a physical presence; *i.e.*, meaning property or employees, in Texas. *See also Midland Cent. Appraisal Dist. v. BP America Prod. Co.*, 282 S.W.3d 215, 224 (Tex. App. 2009); *Peoples Gas, Light, and Coke Co. v. Harrison Cent. Appraisal Dist.*, 270 S.W.3d 208 (Tex. App. 2008). *But see INOVA Diagnostics, Inc. v. Strayhorn*, 166 S.W.3d 394, 402 (Tex. App. 2005), *cert. denied*, 547 U.S. 1072 (2006).

The lower court's decision is also contrary to the Tennessee Court of Appeals' published holding in *J.C. Penney Nat'l Bank v. Johnson*, 19 S.W.3d 831 (Tenn. App. 1999), *cert. denied*, 531 U.S. 927 (2000). The court in *J.C. Penney* held that Tennessee could not constitutionally tax the corporate earnings of non-resident corporations that had no physical presence, again, referring to real or tangible property or employees, in Tennessee. The court explained that no valid distinction could be made for Commerce Clause purposes between income-based taxes and sales and use taxes.[11]

(Cont'd)

Dec. 11, 1995; *see also In the Matter of the Petition of Wascana Energy Mktg. (U.S.), Inc.*, DTA No. 817866, 2002 WL 1726832 (N.Y. Div. of Tax App. Aug. 8, 2002) (Advisory Opinion).

11. *But see America Online, Inc. v. Johnson*, No. M2001-00927-COA-R3-CV, 2002 WL 1751434 (Tenn. App. Jul. 30, 2002) (not officially published and not citable in Tennessee).

The lower court's decision is also in conflict with the Michigan Court of Appeals' decisions in *Guardian Indus. Corp. v. Dep't of Treasury*, 499 N.W.2d 349 (Mich. App. 1993) and *Gillette Co. v. Dep't of Treasury*, 497 N.W.2d 595 (Mich. App. 1993), *cert. denied*, 513 U.S. 1103 (1995). Those decisions applied *Quill's* physical presence rule, requiring the existence of real or tangible property or employees, before imposition of Michigan's "single business tax."

Expressly contrary to *Quill* and the state court decisions applying its physical presence rule, some state appellate courts have held that physical presence is limited to sales and use taxes, and that the Commerce Clause authorizes taxation of non-resident out-of-state companies having no physical presence in a state. This traces to *Geoffrey, Inc. v. South Carolina Tax Comm'n*, 437 S.E.2d 13, 18 (S.C. 1993), *cert. denied*, 510 U.S. 992 (1993), where the court held that the physical presence rule set forth in *Quill* "had not been extended to other types of taxes," and held that "by licensing intangibles for use in [South Carolina]" by its affiliates, the Delaware corporation had a "substantial nexus" with South Carolina. *Id.* at 18 & n.4.

Several other state appellate courts followed South Carolina's lead, including *Couchot v. State Lottery Comm'n*, 659 N.E.2d 1225, 1230 (Ohio 1996), *cert. denied*, 519 U.S. 810 (1996) ("[t]here is no indication in *Quill* that the Supreme Court will extend the physical-presence requirement to cases involving taxation measured by income derived from the state."); *Buehner Block Co. v. Wyoming Dep't of Revenue*, 139 P.3d 1150, 1158 n.6 (Wyo. 2006) ("*Bellas Hess* and *Quill* have created the specialized jurisprudence . . . applicable to 'sales or use tax case[s]'"). *See also Kmart Properties, Inc. v. Taxation & Revenue Dep't of the State of New Mexico*, 131 P.3d 27, 35 (N.M. App. 2001), *writ quashed*, 131 P.3d 22, 35-36 (N.M. 2005); *Comptroller of the Treasury v. SYL, Inc.*, 825 A.2d 399, 415-416 (Md. 2003), *cert. denied*, 540 U.S. 984 (2003).

The ever growing judicial split is well known and acknowledged by state courts. *See Bridges v. Geoffrey, Inc.*, 984 So.2d 115, 127 (La. App. 2008), *writ denied*, 978 So.2d 370 (2008) (rejecting *Quill's* physical presence requirement and describing *J.C. Penney* and *Rylander* as not "persuasive"); *Geoffrey, Inc. v. Oklahoma Tax Comm'n*, 132 P.3d 632 (Okla. App. 2005), *cert. denied* (2006) (rejecting *Quill's* physical presence requirement and attempting to distinguish *J.C. Penney* and *Rylander*); *A & F Trademark, Inc. v. Tolson*, 605 S.E.2d 187, 196 n.9 (N.C. App. 2004), *cert. denied*, 546 U.S. 821 (2005) (rejecting *Quill's* physical presence requirement and attempting to distinguish *J.C. Penney*); *Gen. Motors Corp. v. City of Seattle*, 25 P.3d 1022, 1028 (Wash. App. 2001), *cert. denied*, 535 U.S. 1056 (2002) (rejecting physical presence standard and noting that the taxpayers "correctly argue that some state courts have extended the physical presence rule.").

The New Jersey and West Virginia Supreme Courts have specifically faced the split of states regarding the application of *Quill*. *See Lanco, Inc. v. Dir., Div. of Taxation*, 908 A.2d 176, 177 (N.J. 2006), *cert. denied*, 551 U.S. 1131 (2007) ("[s]ince the Court decided *Quill*, a split of authority has developed regarding whether the Supreme Court's holding was limited to sales and use taxes."). *See Tax Com'r of State v. MBNA America Bank, N.A.*, 640 S.E.2d 226, 231 (W.Va. 2006), *cert. denied*, 551 U.S. 1141 (2007) (stating that the issue of whether *Quill* applies to income and franchise taxes was a "major question left open by the Supreme Court's opinion."[12]; *see also Capital One Bank v. Com'r of Revenue*, 899 N.E.2d 76 (Mass. 2009), *cert. denied*, 129 S.Ct. 2827 (U.S. 2009); *Geoffrey, Inc. v. Com'r of Revenue*, 899 N.E.2d 87 (Mass. 2009), *cert. denied*, 129 S.Ct. 2853 (U.S. 2009).

The lower court endorsed a broad assertion of extraterritorial taxation power, disregarded well-reasoned court decisions and concluded that Kentucky could tax an investor receiving investment income from a separate and distinct entity operating in Kentucky for the sole reason that the in-state entity was receiving Kentucky's "protection and benefits." The lower court's decision thus brings the post-*Quill* chaotic state of affairs full circle, beginning with South Carolina's *Geoffrey* decision holding that physical presence was not needed for taxation for out-of-state companies in the context of intangible holding companies, through the lower court's holding that a state may tax an out-of-state company even where there is no intangible property in the state but merely receives distributive income from a business receiving "protection and benefits" from Kentucky.

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12. *See also Chase Manhattan Bank v. Gavin*, 733 A.2d 782 (Conn. 1999), *cert. denied*, 528 U.S. 965 (1999) (noting that *Quill* was not limited to sales and use tax related disputes, although it ultimately concluded that there was no Commerce Clause violation).

This pervasive ongoing split of authority among the lower courts constitutes substantial reason for this Court to grant review of this important case, and certiorari is warranted.

II. WITHOUT FURTHER REVIEW, THE KENTUCKY DECISION WILL EFFECTIVELY OBLITERATE THE PHYSICAL PRESENCE TEST SET FORTH IN *QUILL* AND SUBSTITUTE A "METAPHYSICAL" PRESENCE TEST

"The very purpose of the Commerce Clause [is] to ensure a national economy free from . . . unjustifiable local entanglements." *Nat'l Bellas Hess v. Dep't of Revenue of Illinois*, 386 U.S. 753, 760 (1967). This Court's decision noted the distinction between constitutional taxation of companies with property or employees in a state and unconstitutional taxation of companies with no property or employees in a state. *Id.* at 758. "[T]his basic distinction," this Court observed, "until now has been generally recognized by the state taxing authorities," and "is a valid one." *Id.* This Court therefore held that it "decline[d] to obliterate it." *Id.*

Later, this Court reaffirmed the physical presence standard and set forth a four-part test for proper state taxation under the Commerce Clause in *Complete Auto Transit v. Brady*, 430 U.S. 274 (1977). *Complete Auto* held that to satisfy the constitutional prerequisites, a tax: (1) must be "applied to an activity with a *substantial nexus* with the taxing state;" (2) must be "fairly apportioned;" (3) must "not discriminate against interstate commerce;" and (4) must be "fairly related to the services provided by the state." *Id.* at 279 (emphasis added). *See also Barclays Bank PLC v. Franchise Tax Bd. of California*, 512 U.S. 298, 310-311 (1994) (reaffirming *Complete Auto* standard).

In *Quill*, this Court plainly reaffirmed and highlighted the viability of the physical presence rule and noted that its holding was not limited to sales and use taxes. This Court observed:

> we have never intimated a desire to reject an established "bright-line" test. Although we have not, in our review of other types of taxes, articulated the same physical-presence requirement that *Bellas Hess* established for sales and use taxes, that silence does *not* imply repudiation of the *Bellas Hess* rule.

Quill, 504 U.S. at 314 (emphasis added). This Court went on to hold that ". . . the bright-line rule of *Bellas Hess* furthers the ends of the dormant Commerce Clause." *Id.* Accordingly, this Court specifically held that "substantial nexus" between a taxing State and an out-of-state corporation is met only where the corporation has a "physical presence" in the taxing state. *Id.*

Moreover, this Court recognized in *Quill* that the bright-line rule articulated in *National Bellas Hess* "furthers the ends of the dormant Commerce Clause" and it "encourages settled expectations and, in doing so, fosters investment by businesses and individuals." *Id.* at 314-16. It is critical to note that this Court, as explained in *Quill*, has *never* found "substantial nexus" in the absence of physical presence in matters brought before it. Further, this Court has never suggested that the meaning of "substantial nexus" varies depending on the type of tax involved. As Professor Pomp opined below in the Board hearing in this matter: "The Constitution does not distinguish between sales and use taxes and income taxes: there is only one nexus standard and the U.S. Supreme Court has endorsed physical presence." Pet. App. 114a. There is only one Constitution after all.

Such a shifting test, one requiring physical presence in sales and use tax cases while allowing "metaphysical presence" in income tax cases, would create unconscionable results. Indeed, this Court has applied "substantial nexus" principles arising from sales and use tax cases to disputes involving other types of state taxes. *See Tyler Pipe Indus., Inc. v. Washington State Dep't of Revenue*, 483 U.S. 232 (1987), *cert. denied*, 486 U.S. 1040 (1988). *Tyler Pipe* relied on *Scripto, Inc. v. Carson*, 362 U.S. 207 (1960), involving use tax issues, to determine if a taxpayer had substantial nexus with a state that subjected it to a business tax.

As this Court specifically held in *Quill*, 504 U.S. 298, 315 at n.8, a "slightest presence" or "minimal nexus" is *not* sufficient to establish nexus under the Commerce Clause. Indeed, as Justice White pointed out in *Quill*, "reasonable minds surely can, and will, differ over what showing is required to make out a 'physical presence' adequate to justify imposing responsibilities for use tax collection." *Quill*, 504 U.S. at 330, 331 (concurring in part and dissenting in part). Petitioners' passive investment holdings in Tennessee entities having Kentucky operations simply cannot as a matter of law rise to the level of "substantial nexus" under this Court's previous decisions and standing precedent.

In contrast, the lower court erred and juxtaposed Commerce Clause "substantial nexus" with the "purposeful availment" standard that defines "minimum contacts" under Due Process. *See Burger King Corp. v. Rudzewicz*, 471 U.S. 462, 775 (1985). Contrary to the lower court's decision, whether Petitioners receive "protection and benefits" from Kentucky is not the correct question to ask in a Commerce Clause analysis.

As this Court explained in *Quill*, the Commerce Clause and the Due Process Clause reflect very different concerns and thus use very different analyses:

> Due Process centrally concerns the fundamental fairness of governmental activity. Thus, at the most general level, the due process nexus analysis requires that we ask whether an individual's connections with a state are substantial enough to legitimate the state's exercise of power over him. We have, therefore, often identified "notice" or "fair warning" as the analytic touchstone of due process nexus analysis. In contrast, the Commerce Clause and its nexus requirement are informed not so much by concerns about fairness for the individual defendant as by structural concerns about the effects of state regulation on the national economy.

Quill, 298 U.S. at 312.

This Court has held that ". . . a corporation may have the 'minimum contacts' with a taxing State as required by the Due Process Clause, and yet lack the 'substantial nexus' with that State as required by the Commerce

Clause." *Quill*, 298 U.S. at 313. The lower court's substitution of due process "protection and benefits" for the Commerce Clause's requirement of "physical presence" "substantial nexus" per *Quill* was grave error, one of nation-wide consequence that materially harms and furthers the conflicts presented.

As Professor Pomp opined in this case:

> [B]y any principled measure of comparison, physical presence is to be preferred to metaphysical presence as a nexus standard. Physical presence is more consistent with a bright line test, more consistent with settled expectations, more likely to reduce litigation and foster interstate investment, less likely to discriminate against the service sector, less likely to lead to multiple taxation, more easily administered, and more compatible with the growth of electronic commerce.
>
> * * *
>
> [M]etaphysical presence is less a legal principle and more an invitation to chaos and multiple taxation, thus undercutting the very goals of the commerce clause that the concept of nexus is intended to further.

Pet. App. 114a.

Petitioners have absolutely *no* physical presence in Kentucky, as stipulated to by Respondent — no real, tangible or intangible property, no office and no employees located in Kentucky. Boiled down, the lower court's decision held that Petitioners have "metaphysical presence," as coined by Professor Pomp, and therefore "minimal nexus" in Kentucky — merely because Kentucky provided "protection and benefits" to two Tennessee-based entities in which Petitioners held passive investments from which they received income.

Under the lower court's reasoning, *all* companies will now be subject to state taxation so long as they receive income from an in-state company receiving "protection and benefits" from that state, presumably resulting in the taxation of, *inter alia*, passive dividend income of non-residents. As Professor Pomp opined below:

> An out-of-state corporate partner that is a passive investor in a partnership should be treated the same as an out-of-state shareholder in a corporation. Such a partner should be viewed as separate from the partnership just the way a shareholder is viewed as separate from a corporation. The activities of a traditional corporation are not attributed to its shareholders; similarly, the activities of the partnership should generally not be attributed to its partners. Consequently, an out-of-state partner that has no property or payroll of its own in Kentucky should not be viewed as having nexus with Kentucky just because the partnership has property or payroll in the State.

Pet. App. 119a. The lower court's flawed substitution of Due Process Clause analysis for Commerce Clause analysis is material, harmful and should be reviewed by this Court. Certiorari is warranted.

III. WITHOUT FURTHER REVIEW, THE LOWER COURT'S DECISION EVISCERATES THE "MODESTY" REQUIREMENT OF *CARLTON*, AND FURTHERS A SPLIT ON THE CONSTITUTIONAL STANDARDS TO GOVERN RETROACTIVE TAX LEGISLATION

In *United States v. Carlton*, 512 U.S. 26 (1994), with Justice Blackmun writing for a unanimous Court on the merits, this Court was clear that for retrospective amending legislation not to run afoul of the Due Process Clause, the involved Act must ". . . establish[ ] only a modest period of retroactivity." *Id.* at 32. If for no other reason than to bring to a conclusion the plethora of *Carlton*-related litigation, literally from all across the country,[13] this Court should grant certiorari and hear the dispute so as to plainly and unequivocally state that the period of retroactivity when implementing non-curative tax legislation made retroactive on its face must be "modest."

Carlton was hoped to be a solution to the retroactive tax legislation issue. However, far from avoiding or resolving disputes, many state court jurists see this constitutional predicate as *dicta*; others simply ignore it. The modesty requirement set forth in *Carlton* lead Justices Scalia and Thomas to aptly predict:

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13. *See Triple-S Mgmt., Corp. v. Mun. Revenue Collection Ctr.*, 130 S.Ct. 3498 (U.S. 2010) (involving an appeal to the Supreme Court of the Commonwealth of Puerto Rico concerning a period of retroactivity beyond 15 years).

> The reasoning the Court applies to uphold the statute in this case guarantees that *all* retroactive tax laws will henceforth be valid.

Id. at 40 (Scalia & Thomas, JJ., concurring) (emphasis in original).

Hearing the instant case affords the Court an opportunity to clarify *Carlton* and its progeny, and to offer bright-lines to ever growing competing lines of authorities and resolve an ever-widening split across the nation.

A. The Courts Of Kentucky And Other States Are Rejecting The Premise That *Carlton* Requires A "Modest" Period Of Retrospective Application

Over the past 16 years, dozens of cases across the country have addressed what has come to be known as the *Carlton* "modesty analysis." *See, e.g., Miller v. Johnson Controls, Inc.*, 296 S.W.3d 392, 399-400 (Ky. 2009), *cert. denied*, 130 S.Ct. 3324 (U.S. 2010). Some commentators and courts assert that as a matter of law, no "modesty" predicate underlies this Court's *Carlton* Due Process analysis. Quite the contrary, Justice Blackmun's words are clear, concise, and unequivocal — he could not have used fewer words.

Case law, some applying a *Carlton*-like modesty test and some not, is varied and diverse across the nation. The breadth of the split is apparent. In *Estate of Edward Kunze v. Com'r of Internal Revenue*, 233 F.3d 948, 954 (7th Cir. 2000), for example, the court relied on

Carlton's "modesty" requirement in upholding a statute with an eleven-month retroactivity period. *See also, e.g., Kitt v. United States*, 277 F.3d 1330, 1334-35 (Fed. Cir. 2002) (seven-month period); *Quarty v. United States*, 170 F.3d 961, 965-68 (9th Cir. 1999) (eight-month period); *Kane v. United States*, 942 F.Supp. 233, 234 (E.D. Pa. 1996) (eight-month period); *Gardens at W. Maui Vacation Club v. County of Maui*, 978 P.2d 772, 782-83 (Haw. 1999) (six-month period); *cf. Jefferson County Comm'n v. Edwards*, --- So.3d ---, 2010 WL 1946274, at *4, *9 (Ala. May 14, 2010) (citing *Carlton* as requiring a "modest" retroactivity period).

Still further, in *Montana Rail Link v. United States*, 76 F.3d 991 (9th Cir. 1996), the Ninth Circuit held that a shorter period of retroactivity would have been arbitrary, yet it did not specifically address the "modesty" issue. *Id.* at 993-994. *Enter. Leasing Co. of Phoenix v. Arizona Dep't of Revenue*, 211 P.3d 1 (Ariz. App. 2008), advocated leeway for retroactivity beyond one year when a legislature acts promptly. *Enterprise Leasing*, 211 P.3d at 6 (upholding a six-year retroactive period). An Alabama Court has found a two to three-year period "modest" in *Monroe v. Valhalla Cemetery Company, Inc.*, 749 So.2d 470, 474-475 (Ala. App. 1999), *cert. denied*, 529 U.S. 1022 (2000). A New York court has emphasized the need for flexibility when retroactive tax legislation is implemented in response to a federal constitutional infraction, and, in so holding, did not even mention or cite to *Carlton*. *See Moran Towing Corp. v. Urbach*, 1 A.D.3d 722, 724-725, 768 (N.Y.A.D. 2003). And in *Miller*, Kentucky's highest court stressed that what is modest depends on the circumstances and facts of the case, and disregarded the modesty test as an overriding element. *Miller v. Johnson Controls, Inc., supra.*[14]

Over only the last few months it has been demonstrated, once again, that the split continues. *See Zaber v. City of Dubuque*, --- N.W.2d ---, 2010 WL 2218625 (Iowa 2010) (five-year retroactive new tax was upheld; emphasis on "curative" nature used); *Ford Motor Credit Co. v. Michigan Dep't of Treasury*, No. 289781 (Mich. App. Jan. 12, 2010) (unreported), *petition for cert. filed*, (U.S. Oct. 12, 2010) (No. 10-481). (retroactive legislation abrogating a tax refund sanctioned).

Recognizing the ongoing rift as to the breadth and scope of *Carlton*,[15] in conjunction with the ongoing events in Congress concerning dozens of expiring (or expired) tax changes, this Court and countless others undoubtedly face yet another round of upcoming litigation concerning retroactive legislation without intervention by this Court.

14. Still other courts have opined on *Carlton* and its modesty provisions. *See Rivers v. State*, 490 S.E.2d 261, 277-79 (S.C. 1997) (holding two to three-year period not modest); *City of Modesto v. Nat'l Med. Inc.*, 27 Cal.Rptr.3d 215, 222 (Ca. App. 2005); *Buerer v. United States*, 141 F.Supp.2d 611, 614 (W.D.N.C. 2001) (minimizing the importance of the *Carlton* "modesty" text).

15. Commentators have written extensively on the topic of retroactive tax legislation; the progression is worthy of review. *See* Frederick A. Ballard, *Retroactive Federal Taxation*, 48 Harv. L. Rev. 592 (1935); Charles B. Hochman, The Supreme Court and the Constitutionality of Retroactive Legislation, 73 Harv. L. Rev. 692 (1960); Faith Colson, *The Supreme Court Sounds the Death Knell for Due Process Challenges to Retroactive Tax Legislation*, 27 Rutgers L.J. 243 (1995) and the authorities therein.

The period of retroactivity *is* a fundamental element to be considered by the judiciary when evaluating retroactive tax legislation; regardless of length, it must be "modest." The plain rejection of the *Carlton* modesty requirement by the lower court and the Kentucky Supreme Court in *Miller, supra,* demonstrates the need for this Court's intervention herein — *but for* clarity on this issue by way of granting certiorari herein, the prescient words of Justices Scalia and Thomas will continue to ring true. *See Carlton*, 512 U.S. at 39-42 (Scalia & Thomas, JJ., concurring).

This Court's progression of closely analyzing retrospective tax legislation is long and deep. *See, e.g., Untermyer v. Anderson*, 276 U.S. 440 (1928); *Cooper v. United States*, 280 U.S. 409 (1930); *Milliken v. United States*, 283 U.S. 15 (1931); *United States v. Hudson*, 299 U.S. 498 (1937); *Welch v. Henry*, 305 U.S. 134 (1938); *United States v. Darusmont*, 449 U.S. 292 (1981); *Pension Benefit Guar. Corp. v. R.A. Gray & Co.*, 467 U.S. 717 (1984); *United States v. Hemme*, 476 U.S. 558 (1986). While the facts certainly change from circumstance to circumstance, the scrutiny applied remains true under *Carlton*.

These cases and their holdings notwithstanding, as Justice O'Connor plainly noted in her concurrence in *Carlton*:

> In every case in which we have upheld a retroactive federal tax statute against due process challenge, however, the law applied retroactivity for only a relatively short period prior to enactment.

Carlton, 512 U.S. 26, 38 (O'Connor, J. concurring).

In contrast, the lower Kentucky court herein interpreted *Carlton* in a completely different manner and from a wholly different paradigm:

> The Corporations also contend that the four-year period[16] of retroactivity in this case fails to meet the "modesty requirement" of retroactive tax legislation under *Carlton*. However, contrary to the Corporations' assertion, the holding in *Carlton* did not establish such a "modesty requirement;" rather, the majority simply noted with favor that "Congress acted properly and established only a modest period of retroactivity."

Pet. App. 20a.

Certiorari is respectfully requested so that the Court may review the 17-year retrospective period called into question because of the Bills, and clarify the law so as to fill in the monumental divide across the country on the meaning and import of *Carlton's* "modesty" requirement.

B. When Retrospective Legislation Is "Non-Curative" In Nature, Due Process Should Require More, Not Less, "Modesty" For The Period Involved

Congress has for generations seen fit to enact curative legislation, so-called as it is designed to "fix an

16. This finding is flawed, in that, applied to Petitioners, the facial retrospective period approaches 17 years.

ill" or "cure an evil." The cases suggest that legislation designed to cure drafting errors in the drafting of tax legislation, and to close "loopholes" created in the legislative process, is an appropriate subject for retroactive treatment. *See, e.g.*, *Graham & Foster v. Goodcell*, 282 U.S. 409, 428 (1931) (stating that the power to enact curative statutes is unequivocally valid). This concept, too, seemingly applies to legislation designed to thwart circumstances of tax evasion. In *Untermyer, supra*, Justice Brandeis highlighted that the retroactive features of the challenged statute had "a special justification" because they were designed to prevent evasion of the tax. *Id.* at 450.

Alas, the *Carlton* case involved just such a curative legislative situation — an effort by Congress to correct what it asserted were unintentionally enacted "loopholes." In its starkest terms, a circumstance where Congress originally projected a tax break of $300 million, was in hindsight of mere months revised and projected at $7 billion — clearly a legislative effort to address the oft-referred to "law of unintended consequences." Designed to retroactively remedy what it saw and publicly asserted was a "patent abuse," Congress' Act at question in *Carlton* does in fact represent a rational method accompanying a legitimate governmental purpose when seen as the curative legislation it was.[17]

17. As to the "curative" nature thereof, *see* Briefs of Petitioner, United States of America, *United States v. Carlton*, 512 U.S. 26 (1994), reprinted at 1993 WL 638225 (U.S.), Reply Brief of Petitioner, United States of America, *United States v. Carlton*, 512 U.S. 26 (1994), reprinted at 1993 WL 13010930 (U.S.), making it clear that the Petitioner, United States, saw the case as only involving a curative-tax amendment designed to plug a loophole.

To state the obvious, retroactivity is disfavored under fundamental notions of justice. *Eastern Enterprises v. Apfel*, 524 U.S. 498, 532 (1998).[18] Accordingly, this Court has observed that "statutory retroactivity has long been disfavored" [*Landgray v. U.S.I. Film Prods.*, 511 U.S. 244, 268 (1994)], curative amendments being an exception. The Bills in question herein were not "curative," there was no fiscal crisis and accordingly there is no appropriate justification to override the modesty predicate of *Carlton*.

Retrospective amendments are in some instances a violation of the fundamental fairness citizens demand; no less than the credibility of our government is at stake. Trust in government is fundamental and axiomatic in a country of laws, not men. *See St. Regis Paper Co. v. United States*, 368 U.S. 208, 209 (1961) (Black, J., dissenting) ("It is no less good morals and good law that the Government should turn square corners in dealing with their Government."); *Federal Crop Ins. Corp. v. Merrill*, 332 U.S. 380, 387-88 (1947) (Jackson, J., dissenting) ("It is very well to say that those who deal with the Government should turn square corners. But there is no reason why the square corners should constitute a one-way street").

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18. *See also Harper v. Virginia Dep't of Taxation*, 509 U.S. 86 (1993) (Scalia, J., concurring) (noting that "original and enduring American perception of the judicial role sprang . . . from the jurisprudence of Blackstone, which viewed retroactivity as an inherent characteristic of the judicial power, a power 'not delegated to pronounce a new law, but to maintain and expound the old one.'") (quoting 1 W. Blackstone, *Commentaries* *69 (1765)).

The concerns today as to retrospective tax legislation are the same as that of our forefathers over 200 years ago when debating the Constitution. Clarity is needed. While we know that a 30 to 50-year period of retroactivity "is far from outside the bounds of retroactivity permissible" under due process analysis [*Eastern Enterprises v. Apfel*, 524 U.S. 498, 550 (1998)], the question remains, what period of retroactivity is not "modest?" Only certiorari will appropriately address this issue.

CONCLUSION

For the foregoing reasons, the Petition for Writ of Certiorari should be granted.

Respectfully submitted,

JENNIFER S. SMART
Counsel of Record
GREENEBAUM DOLL &
MCDONALD PLLC
300 West Vine Street
Suite 1100
Lexington, KY 40507-1665
(859) 288-4672
jss3@gdm.com

MARK F. SOMMER
JENNIFER Y. BARBER
GREENEBAUM DOLL &
MCDONALD PLLC
3500 National City Tower
101 South Fifth Street
Louisville, KY 40202-3197
(502) 587-3570

Counsel for Petitioners

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