FRANCHISE TAX BOARD OF THE STATE OF CALIFORNIA,

Appellant/Cross-Respondent,

vs.

CASE NO. 53264

GILBERT P. HYATT,

Respondent/Cross-Appellant.

______________________________/

FILED

JUL 20 2009

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AMICUS CURIAE BRIEF OF THE STATE OF UTAH

Joined in by the States of Arkansas, Colorado, Delaware, Florida, Idaho, Maine, Maryland, Missouri, Ohio, Oklahoma, North Dakota, Tennessee, Vermont, Virginia and Washington

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09-17734

IN THE SUPREME COURT OF THE STATE OF NEVADA

* * * *

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INTEREST OF AMICI

Amici are numerous sister States of Nevada and California. As such they have a vested interest in our federal system, the rights, powers and duties accorded to them as States, and in the interactions between all of the sister States. The outcome of this case will have a dramatic effect upon all of these items and are of vital interest to amici.

The United States is made up of fifty different States. Under our system of government, amici have an interest in retaining their sovereign rights to govern those who have transactions that come within their borders. Every State, in pursuit of its legitimate interests, necessarily conducts investigations which extend beyond its borders because there is free movement between the states. Transactions and relationships that affect their citizens can occur with individuals and entities outside of their borders. Affirming the astronomical judgment that resulted from various erroneous legal rulings and acts of the district court will force every State agency, including Nevada's own, to alter its processes to adjust for the vagaries of tort law regulation of 49 other States. To force these considerations on State agencies is to diminish the authority of their respective sovereign State governments and the laws governing within their respective spheres. This district court's actions, if affirmed, threaten the very fabric of our system of cooperative federalism. If this decision is allowed to stand, all States will be required to modify their conduct to accommodate the tort policies of each of their sister States – effectively mandating nationwide uniformity in laws, statutes, and public policies, and thereby undermining sovereignty of the States.

This case appears to be the first instance of an individual bringing a common-law tort lawsuit in one State based upon the tax audit activities of another State.[1] The

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[1] There is nothing about this case that limits it to income tax audits. As sovereign entities, the amici, as part of their normal governmental functions, conduct investigations of all types with respect to individuals, including residents, former residents, individuals who wish to become residents, and individuals that wish to enter into business relationships in, or with, people in their state. In each of these (continued)

filing of this lawsuit, by itself, was a concern to the States. When this case was considered by the United States Supreme Court discovery had not been completed, it had not yet gone to trial, and there was no verdict. Nonetheless, 37 States, Puerto Rico, and the Mariana Islands joined in amicus filings urging the United States Supreme Court to grant review of the case and to hold that such lawsuits should not be allowed. Those filings evidenced the fears of the States, collectively, of the treatment that any State administrative law enforcement activity might receive at the hands of a jury in the courts of a sister-State. The United States Supreme Court allowed the case to proceed on the basis that the Nevada courts had "sensitively applied principles of comity with a healthy regard for California's sovereign status." *Franchise Tax Board v. Hyatt,* 538 U.S. 488, 499 (2003).

The characterization by the United States Supreme Court of the Nevada judiciary's treatment of California set a benchmark for the application of comity and may have been accurate at the time of its consideration of this case, but it no longer is. The decision of the Nevada jury and the district court in this case did not adhere to that benchmark. The jury verdicts in this case, over $388 million in compensatory and punitive damages and over $100 million in pre-judgment interest, demonstrate that the fears of the states were well founded. The total judgment, which is in excess of $490 million, is staggering, and unprecedented with respect to the common law torts, invasion of privacy and infliction of emotional distress, that were alleged. This court and the United States Supreme Court allowed this case to proceed on the assumption that the trial of this case – as pled – would not violate the Constitutional principles embodied in the Full Faith and Credit Clause. The outcome and consequences flowing from it show that those core Constitutional principles were violated.

(continued) circumstances it may be necessary for a state to send its employees into another state to ascertain relevant information. Furthermore, if the verdicts and theories on which this case was argued by Plaintiff are allowed to stand, a state could be liable for damages even if its employees conduct all of their activities in their home state.

For most states, an award of this magnitude is budget busting even in the best of times. But beyond the verdict, is the fact that a suit brought in a sister State will almost invariably require the retention of local counsel in order for the party State to properly defend itself. The cost for outside counsel does not, of course, include the direct cost of the State's own employees who become involved in the defense of the lawsuit, or the indirect cost of diverting those employees from other functions. The prospect of becoming embroiled in litigation of this type in another state will necessarily have a chilling effect on the actions of state employees and state agencies. And not just those of a State's tax agencies. Any out-of-state investigatory activity by a State in performing any of its governmental functions could provide a basis for a similar lawsuit. The district court's actions, and outcome of this appeal, are of vital interest to amici and all other states.

STATEMENT OF FACTS

Amici hereby adopt the statement of facts in Appellant's Opening Brief.

SUMMARY OF ARGUMENT

State Sovereign Immunity is fundamental to our federal system. It is preserved by the granting of comity by which a court respects the sovereign interest of sister-States. In appropriate circumstances, where the actions of the forum State demonstrate "hostility" to the sister State, the principles of comity are institutionalized by the Full Faith and Credit Clause of the United States Constitution.[2] Dismissal of this action under either circumstance is necessary to preserve State Sovereign Immunity.

Before trial, the Franchise Tax Board (FTB) was fearful that the common-law tort action in this case was nothing more than an attempt to use the Nevada courts as a collateral attack on the California tax assessments. This was initially recognized as a potential problem by the Nevada courts in the preliminary rulings in this matter.

[2] Article VI, § 1, United States Constitution. "Full Faith and Credit shall be given each State to the Public Acts, Records, and other judicial proceedings of every other State."

However, the "bad faith" theory on which the case was tried by plaintiff Hyatt made it clear that the correctness of the California tax assessments was the central, and determinative, issue in the manner in which this case was tried. This did not adhere to the benchmark established by this court and the United States Supreme Court.

Under the proper application of the principles of comity, Nevada should apply the laws it applies to its own agencies, with the result that this lawsuit should be dismissed, or, at the very least, the jury's awards of damages, including punitive damages, should be reversed.

ARGUMENT

I. INTRODUCTION TO ARGUMENT

The gravamen of this matter are residency and tax audits conducted by the Franchise Tax Board of the State of California (FTB) of plaintiff Gilbert Hyatt for the year 1991 and part of 1992. Residency audits are, by their nature, invasive.

A fairly recent article in the Wall Street Journal, which provided advice on moving to a state with no income taxes, described a residency audit as subjectively feeling like a "tax colonoscopy." Tom Herman and Rachel Emma Silverman, *"Cutting the Risk of a State Audit When You Move,"* Wall St. J., August 29, 2007. The very first sentence of the article referred to Nevada as a potential tax haven: "No-income-tax states such as Florida, Nevada and Texas are looking increasingly attractive to people getting ready for retirement." Id. The article then advised wealthy readers: "But before moving to a tax haven, it's important to pay attention to the fine print of how to move. It's easy to make seemingly minor mistakes that can trigger a painful audit -- and a hefty bill -- from the high-tax jurisdiction you thought you had left behind." Id. The article gave "tips" on how to make sure a move is genuine. One tip was: "Don't leave . . . a safe deposit box in your former home state." Id. (In the present case, Hyatt maintained a safe deposit box in California long after he claimed to have moved to Nevada.) The article also described "red flags for auditors, " including "people with homes in more than one state, especially those with large incomes." Id. (Here, documentation showed that Hyatt's alleged sale of his California home, and his purchase of a Nevada home, occurred after his claimed move date.)

The Wall Street Journal article concluded with the following advice: "In your new home state, tax experts say it's important to make your move official. Register to vote, get a driver's license and register your car in the new state, and change your address on bills and important documents. Even so, establishing a legal residence in the eyes of the taxman is often based on subjective factors, including the intent of the taxpayer, which is why it's important to get advice from a tax-savvy adviser." Id. (In the present case, Hyatt took many of these steps, but most were long after his alleged move date; and he certainly had an impressive team of tax-savvy advisers.)

The invasive nature of an audit is particularly true when the object of the inquiry has been a resident of a state for a long period of time and the issue is the date on which the change in residency occurred. The primary determinative fact in cases of this type is normally the physical presence of the individual and what the individual was doing.[3] The analysis compares the amount of time and nature of activities in the former state of residence with the presence and activity in the claimed new state of residence. In this case virtually all of the audit activity, including all of the analysis and evaluation of the evidence, was performed in California. FTB's activities in Nevada were limited to investigative efforts aimed at gathering information relevant to the audit investigation.

The judgment resulted, in large part, from Hyatt's perception of the intrusive nature of the audit. His complaints concerning the audit and FTB's subsequent activities related to the audit (assessments and administrative appeal processing) led to

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[3] Under California law, "[w]hether or not the purpose for which an individual is in this State will be considered temporary or transitory in character will depend to a large extent upon the facts and circumstances of each particular case." 18 Cal. Admin. § 17014(b) (emphasis added).

the judgment, which has significant nationwide implications, and constitutional concerns, as discussed below.

II. THE PRINCIPLE OF STATE SOVEREIGN IMMUNITY UPON WHICH OUR FEDERAL SYSTEM OF GOVERNMENT IS BASED REQUIRES THAT THE JUDGMENT OF THE DISTRICT COURT BE REVERSED AND THIS CASE BE DISMISSED

A. State Sovereign Immunity

"It is an essential attribute of the States' retained sovereignty that they remain independent and autonomous within their proper sphere of authority." *Printz v. United States,* 521 U.S. 898, 928 (1997). "The essence of our federal system is that within the realm of authority left open to them under the Constitution, the States must be equally free to engage in any activity that their citizens choose for the common weal." *Garcia v. San Antonio Metropolitan Transit Authority,* 469 U.S. 528, 546 (1985). Taxation is clearly one of the areas of authority that is left open to the States, subject only to several Constitutional limitations, e.g., the Commerce Clause, the Due Process Clause of the Fourteenth Amendment and the Privileges and Immunities Clause.

There are a number of purposes and policies that underlie State Sovereign Immunity. First, a "preeminent purpose of State sovereign immunity is to accord States the dignity that is consistent with their status as sovereign entities." *Federal Maritime Comm'n v. South Carolina State Ports Authority*, 535 U.S. 743 (2002). Civil litigation instituted by private parties is an "affront to a State's dignity." *Id.* It is for this reason that all States place limits on, or requirements for, lawsuits to be brought against them in their own state courts.[4]

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[4] For example, Utah Code Annotated § 63G-7-201(1) "Except as may otherwise be provided in this chapter, each governmental entity and each employee of a governmental agency are immune from suit for any injury that results from the exercise of governmental function." Immunity is not waived with regard to "the collection and assessment of taxes." Utah Code Annotated § 63G-7-301(5)(h).

Private suits against non-consenting States present the "indignity of subjecting a State to the coercive process of judicial tribunals, regardless of the forum." *Alden v. Maine,* 527 U.S. 706, 750 (1999). *Alden* involved a suit brought in federal court, but its holding, "regardless of the forum," is equally, if not more, applicable to State courts. The federal government is a sovereign superior to States, while States are co-equal sovereigns. Thus, in a case such as this, where the lawsuit is filed in a state court against a non-consenting sister state agency, the policies and considerations of sovereign immunity are heightened and should be accorded similar respect and consideration.

A second reason for State Sovereign Immunity is that it serves "the important function of shielding state treasuries and thus preserving 'the States' ability to govern in accordance with the will of their citizens." *Federal Maritime*, 535 U.S. at 765. In addition to the indignity of having to defend this lawsuit against Hyatt's claims, California expended significant amounts of money defending this lawsuit, and will be required to pay $490 million if the district court's judgment is affirmed. In short, the shield to California's treasury provided by State Sovereign Immunity has been removed by the actions of the district court and the jury in this matter.

A necessary corollary to a State's Sovereign Immunity is that a limit must exist on a State's ability to act with respect to actions in other states. A State is only "competent to legislate" with respect to the subject matter of the alleged intentional torts taken that "injured one of its citizens <u>within its borders</u>." *Nevada v. Hall*, 440 U.S. 410, 424 (1979) (emphasis added); *Franchise Tax Board*, 538 U.S. at 494.[5] Tort

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[5] Hyatt may point to the fact that in its consideration of this case the United States Supreme Court stated that "[I]t is undisputed that at least some of the conduct alleged to be tortuous occurred in Nevada." *FTB v. Hyatt*, 538 U.S. at 495. This statement was made before the trial was held, before the actual evidence was presented to the jury, and before Hyatt's counsel argued the case to the jury. While there was conduct in Nevada that Hyatt may allege was tortuous, there is no specific finding to support that conclusion, other than the damage award for which the jury was allowed to consider all of California's actions.

law can be seen as a means of State regulation. *See BMW of North America, Inc. v. Gore,* 517 U.S. 559, 573, n.17 (1996). Thus, the territorial reach of one state's tort law can be no greater than any other exercise of lawmaking authority by that State. Here, there was no finding as to what injuries Hyatt suffered as a result of FTB's Nevada contacts made during the audit investigation or related to the single, or even two, trips made to Nevada by FTB's auditors. Rather, the bulk of the alleged harm Hyatt complained of to the jury related to lawful activities taken by FTB pursuant to California law and engaged in within the State of California. Thus, the jury's verdict, if allowed to stand, violates these basic principles.

One State cannot legislate for the other or be allowed to project its laws across state lines so as to preclude the other State from prescribing for itself the legal consequences of its acts within it. *Pacific Employers Insurance Co. v. Industrial Accident Comm'n*, 306 U.S. 493, 502 (1939). In effect, based on the actual issues that Hyatt was permitted to try in this case, the decision in this case, if affirmed, will result in Nevada projecting its determination across state lines and prescribing the consequences for lawful acts undertaken by California almost exclusively within California. This is legally prohibited by the United States Constitution.

A State may not expand the extraterritorial reach of its lawmaking authority in a manner that may force other States to alter or modify their conduct. *Brown-Forman Distillers, Corp. v. New York State Liquor Authority,* 476 U.S. 573, 584 (1986). Nor may a State extend to its residents extraterritorial protection from another State's exercise of its independent and autonomous lawmaking authority. *Bigelow v. Virginia,* 421 U.S. 809, 822-25 (1975); *Phillips Petroleum Co. v. Shutts*, 472 U.S. 797, 822 (1985). The award of damages by the Nevada jury and the district court in this case will be noted by every state, as is evidenced by the amici filing with the United States Supreme Court and this filing. State employees and agencies in determining the potential consequences of their actions will, if this judgment is allowed to stand, necessarily have to take into consideration the possibility of an out-of-state tort lawsuit and the awarding of damages, and therefore may alter or modify their conduct. The judgment in this case is an effort by Hyatt to have the Nevada courts give him extraterritorial protection from California's exercise of its right to tax and to audit.

Nothing in the Constitution supports the notion that a State, through its judiciary or otherwise, can intrude or pass judgment on another State's exercise of its independent lawmaking authority. That is exactly what the district court allowed a Nevada jury to do.[6] A forum state unconstitutionally "projects its laws across state lines" when its actions "may interfere with the ability of other States to exercise their own authority." *Brown-Forman,* 476 U.S. at 585. The district court's judgment, and the jury's verdict, are projecting Nevada laws across state lines and are interfering with California's ability to exercise its, California's, authority. This court should not allow that to happen.

B. The Legal Concepts Implementing State Sovereign Immunity

State Sovereign Immunity is principally enforced by the principle of comity. Comity is an accommodation policy, under which the courts of one State voluntarily give effect to the laws and judicial decisions of another State, out of deference and respect, to promote harmonious interstate relations. *Nevada v. Hall,* 440 U.S. at 424-27; *Mianecki v. District Court,* 99 Nev. 93, 98, 658 P.2d 422 (1983). The principle is appropriately invoked according to the sound discretion of the court acting without obligation. Here, the application of comity to California's Sovereign Immunity was required because this court had previously ruled upon the application of comity to this case. Moreover, the failure of the district court to extend comity under the circumstances of this case rose to the level of a violation of the Full Faith and Credit Clause of the United States Constitution.

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[6] Amici are informed that Hyatt's counsel in his closing argument asked the Nevada jury to be a "check and balance" upon the activities of FTB. Amici respectfully assert that this argument demonstrates "hostility" to the legitimate actions of another State in violation of the Full Faith and Credit Clause.

This court previously granted immunity for FTB's discretionary acts, dismissing plaintiff's negligence claims. Conversely, this court permitted Hyatt's intentional tort claims to stand.[7] These limitations, however, were not followed by the district court during the trial. In fact, the only matters that were tried to the jury related to FTB's discretionary conduct and were mostly related to lawful actions taken by FTB within the State of California. As a result, the district court violated this court's previous orders. But more importantly, from amici's standpoint, the district court's refusal to apply comity to California's Sovereign Immunity, based on the manner in which this case was tried, violated the Full Faith and Credit Clause of the United States Constitution. Comity is generally thought of as solely discretionary, but the concerns that underlie it gave rise to the inclusion of the Full Faith and Credit clause of the United States Constitution. U.S. Const. Article VI, § 1.[8] The Full Faith and Credit Clause "substituted a <u>command</u> for the earlier principles of comity." *Estin v. Estin,* 334 U.S. 541, 546 (1948) (emphasis added). The Full Faith and Credit Clause "made conflicts principles enforceable as a matter of constitutional command rather than leaving enforcement to the vagaries of the forum's view of comity." *Pacific Employers Insurance Co.,* 306 U.S. at 502. The Full Faith and Credit Clause alters "the status of the several states as independent foreign sovereigns, each free to ignore obligations created under the laws or by the judicial proceedings of the others . . . "

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[7] It is amici's understanding that subsequent to its April 2002 ruling, but prior to the trial of this matter, this court adopted a different standard for reviewing the discretionary actions of government employees. *Martinez v. Maruszczak,* 123 Nev. 433, 168 P.3d 720 (2007). Under this standard, the federal standard called the *Berkovitz-Gaubert*, test (the name is derived from two decisions of the United States Supreme Court, *Berkovitz v. United States*, 486 U.S. 531 (1988) and *United States v. Gaubert*, 499 U.S. 315 (1991)), the motivation of the agency or its employees are not considered. "Bad faith," which was the focus of Mr. Hyatt's case, should not have been presented to the jury, and they should not have been asked to decide whether it existed. This change in the legal standard, by itself, provides a sufficient basis to reverse the judgment of the district court.

[8] "Full Faith and Credit shall be given each State to the Public Acts, Records, and other judicial proceedings of every other State." U.S. Const. Article VI, § 1

Milwaukee County v. M.E. White Co., 296 U.S. 268, 277 (1935). Thus, the comity required by the Full Faith and Credit Clause is not voluntary, and is not an issue of State law. Indeed, the United States Supreme Court in this very case recognized that the limits imposed by the Full Faith and Credit Clause on application of comity principles by State courts were directly related to State sovereignty interests.

> States' sovereignty interests are not foreign to the full faith and credit command. But we are not presented here with a case in which a State has exhibited a "policy of hostility to the public Acts" of a sister State. *Carroll v. Lanza*, 349 U.S. 408, 413 (1955). The Nevada Supreme Court sensitively applied principles of comity with a healthy regard for California's sovereign status, relying on the contours of Nevada's own sovereign immunity from suit as a benchmark for its analysis.

Franchise Tax Board, 538 U.S. at 499.

Thus, at a minimum, comity as a matter of constitutional command requires the "healthy regard" by a forum State court of the "sovereign status" of a sister State. *See also Nevada v. Hall*, 440 U.S. at 424, footnote 24 (noting that the result might have been different in a case posing a "substantial threat to our constitutional system of cooperative federalism"). In the posture of this case in 2003, the United States Supreme Court believed that this Court met that minimum by recognizing FTB's sovereign immunity under California law to the extent that immunity was not antagonistic to the underlying policies of Nevada's sovereign immunity laws.

Based on these authorities, there are three principles under Full Faith and Credit that limit a forum State's authority to disregard the laws of a sister state: 1) a forum state may not act with hostility to the acts of a sister State by refusing to recognize laws that are not antagonistic to the polices of the forum state, *Franchise Tax Board*, 538 U.S. at 499; 2) a State may not project its laws into a sister State, *Pacific Employers*, 306 U.S. at 504-505; and 3) the forum State's laws may not be applied arbitrarily and unfairly to another State, at least to the extent that its application is contrary to the expectations of the parties at the time the challenged actions were taken, *Phillips*, 472 U.S. at 822. All of these principles were disregarded by the district court. The district court stripped FTB of its sovereign status and applied Nevada law applicable to *private parties* or non-sovereigns.

This is exemplified by the district court's refusal to extend comity to California's statute extending sovereign immunity to its state agency's against the imposition of punitive damages. In this instance, Nevada and California laws on punitive damages awards against sovereign State agencies are, respectively, identical and complimentary. Both states prohibit such awards. Cal. Gov't Code § 818; NRS 41.035(1). However, the Nevada district court opted to strip FTB of its sovereign status and applied the Nevada law applicable to <u>non-sovereigns</u>. As a matter of law, this action by the district court constituted an act of hostility to FTB in violation of the Full Faith and Credit Clause.[9] <u>See</u> *Hughes v. Fetter*, 341 U.S. 609 (1951).

Moreover, in violation of the second basic principle of the Full Faith and Credit Clause, the district court improperly allowed the tort claims to proceed under Nevada law that were within the exclusive lawmaking authority of California and which interfered with the pending administrative proceedings with regard to Hyatt's tax liability to California. The Full Faith and Credit Clause required the district court to recognize FTB's sovereign immunity under California law for all of Hyatt's claims that fell outside the lawmaking authority of Nevada. *Phillips,* 472 U.S. at 822; *Pacific Employers Ins. Co.*, 306 U.S. at 504-505.

Third, the district court arbitrarily allowed claims to proceed, and evidence to be introduced, that permitted the jury to disapprove of FTB's actions under California law and, indeed, to disapprove of laws of the State of California. At the time these

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[9] Similarly, the district court refused to extend comity to caps on compensatory damages against government agencies. California allows <u>no</u> damage awards against FTB, but Nevada allows awards of no more than $75,000 against its own government bodies. NRS 41.035(1). At the very least, Nevada's $75,000 cap on compensatory damages should have applied to FTB.

actions were taken, FTB had no expectation that its exercise of authority granted by California would subject it to liability under Nevada tort law. The Full Faith and Credit and Due Process Clauses of the United States Constitution required the district court to recognize California law and the lawfulness of FTB's exercise of authority under those laws. *Phillips,* 475 U.S. at 822. This lawsuit allowed the jury to consider actions taken in California, not just those in Nevada, effectively allowing the jury to judge and disapprove of FTB's lawful actions engaged in pursuant to the laws of the State of California. Nothing in the Constitution supports the notion that a State, through its judiciary or otherwise, can intrude or pass judgment on another State's exercise of its independent lawmaking authority. In fact, the Full Faith and Credit Clause forbids such intrusions or the passing of judgment by a sister State.

Consequently, the district court's actions in this matter exceeded the commands of the Full Faith and Credit Clause. Therefore, amici respectfully contend that the judgment of the district court must be reversed and this case dismissed.

III. ALLOWING THIS MATTER TO BE CLOAKED AS A TORT ACTION WHEN IT IS IN REALITY AN ATTACK UPON THE TAX LAWS AND PROCESSES OF ANOTHER STATE WILL HAVE DIRE CONSEQUENCES AND SHOW WHY THIS COURT SHOULD REVERSE THE JUDGMENT OF THE DISTRICT COURT AND DISMISS THIS CASE

By specifically noting that Mr. Hyatt's tax assessment claims would be determined under California procedures, the April 1999 ruling by then District Judge Saitta[10] that dismissed Hyatt's cause of action seeking a determination of Nevada residency was an acknowledgment that issues relating to FTB's tax and penalty

[10] "I do not believe Nevada has subject matter jurisdiction of plaintiff's claim, and that is the request to declare that, in fact, his residency was of Nevada, for purposes of the tax case only." 2 AA 00410-11.

assessments were within California's exclusive lawmaking sphere and, accordingly, outside of Nevada's lawmaking authority.[11]

California law is an expression of the policies approved by California citizens through their elected representatives. Neither a Nevada jury, nor the district court, has a "vote," or should have a "vote," on California policies. The position taken by the district court, that the ultimate issue of "bad faith" is divorced from the factual analyses and policy applications that led to it, is one of slicing shadows. A challenge to the analysis, whether under the rubric of tax or tort law, is an attack on FTB's conclusions.

To determine the permissibility of Nevada's regulation of FTB in this case, the "practical effect" of the district court's rulings "must be evaluated not only by considering the consequences" themselves, but also by considering how they may interact with the legitimate regulatory schemes of other states and what effect would arise if not one, but many or every other state adopted a similar approach. *Healy v. Beer Institute,* 491 U.S. 324, 336 (1989). FTB is an administrative agency with enforcement responsibilities delegated to it by the people of the State of California through their elected representatives. FTB's legitimate purpose is to assure the people of California that everyone owing the State taxes pays what is due. This same purpose and duty applies with respect to every other State, state agency and state employee. These purposes and duties exist not only with respect to taxes, but with respect to every other governmental function involving enforcement and investigatory activities.

The consequence of sustaining the district court's judgment will have dire consequences both fiscally, and, perhaps more importantly, also with respect to the States' enforcement processes. Such enforcement processes —quasi-prosecutorial— have long been recognized as unsuitable for review by courts and that, indeed, such

[11] As further demonstration that Hyatt intended this lawsuit to fundamentally question California's ability to tax him it should be noted that, in spite of District Court Judge Saitta's ruling, Hyatt's Second Amended Complaint filed shortly before trial includes as a cause of action a request for a declaration that he is a Nevada resident.

review "threatens to chill law enforcement by subjecting the prosecutor's motives and decision making to outside inquiry . . . " *Wayte v. United States,* 470 U.S. 598, 607 (1985). If the jury decision, and the judgment entered by the district court, is allowed to stand it will necessarily chill the law enforcement activities of every state when those activities involve investigating persons or transactions that occurred outside of the State. This is because every State government employee and every State government agency must consider the possibility of becoming embroiled in another State in a controversy such as that presented in this case and the possible consequences of an adverse determination.

Indeed, it was comparable concerns which appear to have motivated this court to adopt the *Berkovitz-Gaubert* test in *Martinez.* If the judgment entered by the district court is allowed to stand, it will necessarily chill government functions that involve investigating activities outside of a state, because every government employee and every government agency must consider the possibility of becoming embroiled in litigation in another state, and the possible consequences of an adverse determination.

Because this tort action involved questions of taxability and another state's administration of its tax laws, special considerations are involved, particular with respect to the presentation of the matter to a jury. As one academic commentator noted

> State tax administration policy should be set by elected officials and the employees who answer to them, not by jurors, particularly jurors from other states. Tax administration involves careful balancing of many political, fiscal, and legal considerations.[12] That balancing requires expertise, and it should be done through the democratic process. Jurors lack the needed expertise. . . . If they are out-of-staters, jurors lack a meaningful stake in the consequences of their decisions.[13]

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[12] Amici note the similarity in the author's phrasing and the second component of the "Berkowitz-Gaubert test" recently adopted by this Court, *Martinez v. Maruszczak,* 123 Nev. 433, 168 P.3d 720 (2007).

[13] Steve R. Johnson, "Extraterritorial Audits, Tax Competitors, and Narratives: *Hyatt,"* State Tax Notes, November 3, 2008, pg 283 at 288. Mr. Johnson is the E.L. Wiegand Professor of Law at the William Boyd School of Law, University of Nevada,

The special treatment to be accorded to taxation and tax collection procedures was highlighted in *Fair Assessment in Real Estate Association, Inc. v. McNary,* 454 U.S. 100 (1981), a case brought under 42 USCS section 1983 seeking damages for an alleged unconstitutional administration of a state property tax. The United States Supreme Court in holding that the 1983 action at issue in that case could not proceed in federal court stated:

> Special reasons justifying the policy of noninterference with state tax collection are obvious. The procedures for mass assessment and collection of state taxes and for administration and adjudication of taxpayers' disputes with tax officials are generally complex and necessarily designed to operate according to established rules. State tax agencies are organized to discharge their responsibilities in accordance with the state procedures. If federal declaratory relief were available to test state tax assessments, state tax administration might be thrown into disarray, and taxpayers might escape the ordinary procedural requirements imposed by state law. During the pendency of the federal suit the collection of revenue under the challenged law might be obstructed, with consequence damage to the State's budget, and perhaps with a shift to the state of taxpayer insolvency.

McNary, 454 U.S. at 108, Footnote 6.

These same considerations apply at least as equally to common-law tort claims brought in out-of-state courts challenging the assessment of taxes by a sister-State as tortuous. Administration of state taxes is complex, their adjudication and enforcement operate within established rules, and tax agencies are organized to discharge their responsibilities in accordance with state procedures. This lawsuit has thrown those procedures into disarray. One needs to look no farther than the delay occasioned by the Nevada Protective Order on the administrative determination of Mr. Hyatt's protest.[14]

Las Vegas. The article offers a number of other meaningful insights on the significance of this case and reasons why this Court should exercise comity to dismiss this action.

[14] Not only did the Protective Order delay the consideration of the protest but in addition, Mr. Hyatt's counsel in their briefs to the California State Board of Equalization has argued that in consideration of the FTB's assessment of taxes and penalties, the California State Board of Equalization is bound "to the testimony most favorable to Mr. Hyatt" and therefore must disregard any testimony by FTB witnesses in rebuttal. 92 AA 22940, 22944.

In addition, this lawsuit has caused disruption of California's revenue collection systems, as it would any State's. The United States Supreme Court went on in *McNary* to say

> To allow suits would cause disruption of the states' revenue collection systems . . . State tax collections officials would be summoned into federal court to defend their assessments against claims for refunds as well as prayers for punitive damages, merely on the assertion that the tax collected was willfully and maliciously discriminatory against a certain type of property.

454 U.S. at 114.

Evidence of such disruption is presented by this case. Employees of FTB were deposed. FTB attorneys, and attorneys of the California Attorney General's office, were required to appear in Nevada courts to defend California's procedures and assessments. The FTB was required to retain Nevada counsel to defend itself at great cost. The cost of state employee time, and lost revenues if those employees had been engaged in other endeavors, is staggering. Amici do not have the resources that California has. No other State, other than California, could have borne the costs to defend itself in this case. And even California will be unable to pay this judgment without curtailing other government programs. If the judgment of the district court is sustained it will have a chilling effect on the activities of every State, and not just in the administration of taxes.

The special considerations involving state taxes were clearly not taken into account by the district court, but this court should do so and dismiss this action.

IV. FOLLOWING THE BENCHMARK ESTABLISHED BY NEVADA LAW, AMICI RESPECTFULLY CONTEND THAT THIS COURT MUST EXERCISE ITS DISCRETION AND DISMISS THIS MATTER

The United States Supreme Court, in its 2003 opinion in this matter, observed that the Nevada Supreme Court had given a healthy regard for the sovereign status of California by "relying on the contours of Nevada's own sovereign immunity as a <u>benchmark</u> for its analysis." *Franchise Tax Board,* 538 U.S. at 499 (emphasis added). The decision of the Nevada jury and the district court in this case did not adhere to these benchmarks. If these benchmarks are followed, the damages awarded should be dismissed or reduced. Amici submit that proper application of the principle of comity, as articulated by Hyatt's counsel to the United States Supreme Court, should require this court to follow Nevada benchmarks and to apply those benchmarks to FTB.

Although there are many examples of the district court's failure to use Nevada's law applicable to its own state agencies as a benchmark for the evaluation of FTB's conduct, the primary example of the district court's failure in this regard is reflected in district court's erroneous determination to allow the jury to assess punitive damages against FTB, a state agency, and the district court's subsequent failure to vacate these damages after the trial.[15] As noted above, under Nevada law, punitive damages may not be imposed upon a Nevada governmental agency. NRS 41.035. California law also prohibits the imposition of punitive damages on a California government agency. Cal. Gov't Code § 818. The laws of both states are virtually identical. The district court erred by refusing to use Nevada's own statutory provision as "benchmark" to the analysis of punitive damages, and by refusing to extend comity to California's law, which was in no way antagonistic to Nevada's own policy. Rather, the district court chose to strip FTB of its sovereign status and apply Nevada laws applicable to purely private parties. Using the Nevada statute as a "benchmark," this Court should exercise is discretion under the principles of comity to dismiss the award of punitive damages.[16] Similarly, comity should be applied to the cap on compensatory damages, as noted earlier in this brief.

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[15] Separate from the issues of comity and Full Faith and Credit argued herein, amici would also note that the very size of the punitive damage award raises other constitutional issues which implicate State Sovereign Immunity. *BMW of North America, Inc., v. Gore,* 517 U.S. 559 (1996) and *State Farm Mutual Insurance v. Campbell,* 538 U.S. 408 (2003).

[16] In addition to the doctrine of comity, there is no common law authority for recognizing the liability of government entities for punitive damages. *City of Newport v. Fact Concerts, Inc.*, 453 U.S. 247, 260 (1981); *Foss v. Maine Turnpike Authority* 309 A.2d 339, 345-346 (Me. 1973); *Long v. City of Charlotte*, 293 S.E.2d 101, 113-115 (N.C. 1982)

CONCLUSION

The assessment of taxes, and manner in which they assessed, are properly the province of the state assessing them. California law provides Hyatt with all appropriate avenues of protection and redress. He is exercising those rights in California. Amici respectfully assert that no State should sit in judgment of the tax processes of a sister State. Nevada is not an exception to this standard. And Hyatt is not entitled to such special treatment.

Some of the consequences of allowing this judgment to stand include: 1) failure to apply principles of comity in accord with the expectations of the United States Supreme Court; 2) subjecting the exercise of a State's discretionary governmental functions to the review of a sister-state jury; 3) the chilling effect on state discretionary actions as a consequence of facing sister-state tort actions and judgments; 4) requiring a state to alter its processes to account for the tort regulations of 49 other states; 5) the use of tort actions to contest the performance of fundamental governmental functions; 6) interference with a State's administrative and judicial process by the actions of a sister-state court; 7) avoidance of the shield to which States are legitimately entitled as sovereigns, to protect their treasuries; 8) diverting State employees from normal functions to defend against out-of-state actions 9) interference with the taxing power of a State by a sister-state; 10) the awarding of punitive damages against governmental agencies; and 11) the potential for budgeting-busting judgments and administrative costs.

Hyatt has cloaked his challenge to a State's legitimate exercise of its taxing powers as a tort suit, so it could be brought in the forum of a sister state. The judgment in this case potentially will result in mortal injury to the concept of State Sovereign Immunity as it has existed for over 200 years. Such a fundamental change in the structure of our federal system should only be accomplished through an amendment to the United States Constitution. It should not be accomplished through a common-law tort suit.

Amici respectfully request that this Court, as expected by the United States Supreme Court, should show "sensitivity" to the "sovereign status" of California, *Franchise Tax Board,* 538 U.S. at 499, and reverse the verdicts of the jury and dismiss this case. Such outcome is the only one consistent with the principles of State Sovereign Immunity, the status of California and Nevada as co-equal sovereigns, and California's proper performance of its critical government functions.

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CERTIFICATE OF COMPLIANCE

I hereby certify that I have read this appellate brief, and to the best of my knowledge, information and belief, it is not frivolous or interposed for any improper purpose. I further certify that this brief complies with all applicable Nevada Rules of Appellate Procedure in particular NRAP 28(e), which requires every assertion in the brief regarding matters in the record to be supported by appropriate references to the record on appeal. I understand that I may be subject to sanctions in the event that the accompanying brief is not in conformity with the requirement of the Nevada Rules of Appellate Procedure.

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CERTIFICATE OF SERVICE

Pursuant to NRAP 25, I hereby certify that I served true and correct copies of the **Amicus Curiae Brief of the State of Utah** on this 20th day of July, 2009, by causing them to be delivered in the Unites States mail, enclosed in a sealed envelope, upon which first class postage was fully prepaid and affixed thereto, to the individuals listed below at their last known business address, as follows:

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