No. 24-333

IN THE

Supreme Court of the United States

THE WALT DISNEY COMPANY AND CONSOLIDATED SUBSIDIARIES,

Petitioner,

v.

THE TAX APPEALS TRIBUNAL OF THE STATE OF NEW YORK AND THE COMMISSIONER OF TAXATION AND FINANCE OF THE STATE OF NEW YORK,

Respondents.

On Petition for Writ of Certiorari to the New York Court of Appeals

BRIEF *AMICUS CURIAE* OF COUNCIL ON STATE TAXATION IN SUPPORT OF PETITIONER

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INTEREST OF *AMICUS CURIAE*

The Council On State Taxation ("COST") is a nonprofit trade association based in Washington, D.C. COST was originally formed in 1969 as an advisory committee to the Council of State Chambers of Commerce.[1] Today COST has grown to an independent membership of approximately 500 major corporations engaged in interstate and international business. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities.

COST members are extensively engaged in interstate and international commerce and share a vital interest in ensuring states do not impede the rights of all businesses engaged in both interstate and international commerce. To that end, it is important to COST members that states impose their taxes in a manner consistent with the protections provided by the U.S. Constitution's Commerce Clause.[2] This case provides the Court with the opportunity to clarify the Commerce Clause prohibition of states imposing discriminatory taxes against interstate and foreign commerce and to provide guidance with respect to the application of this Court's facial discrimination test when there is a discriminatory "geographic distinction" within a tax scheme. *Or. Waste Sys., Inc. v. Dep't of Envtl. Quality of Or.*, 511 U.S. 93, 100 (1994).

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[1] No counsel for any party authored this brief in whole or in part, and no person or entity aside from *amicus* and its counsel funded its preparation or submission. The parties received timely notice of *amicus*' intent to file this brief.

[2] Commerce Clause "regulate[s] commerce with foreign nations, and among the several states, and with the Indian tribes." U.S. Const. art. I, § 8, cl. 3.

From 2008 to 2010, the New York Department of Taxation and Finance, Division of Taxation ("Division of Taxation"), disallowed The Walt Disney Company's ("Petitioner") deduction from taxable income royalty payments received from foreign affiliates not subject to New York franchise tax while allowing such a deduction for royalty payments received from affiliates subject to New York franchise tax. The Division of Taxation denied the royalty payments deduction under former New York Tax Law § 208.9(o). The result of the Division of Taxation's action was the denial of Petitioner's refunds and the assessment of additional corporate franchise tax.

COST has a long history of submitting *amicus* briefs to this Court when significant state and local tax issues impacting businesses operating in interstate and international commerce are under consideration. COST has submitted *amicus* briefs in significant state tax cases considered by this Court including: *Comptroller of the Treasury of Maryland v. Wynne*, 575 U.S. 542 (2015); *Alabama Department of Revenue v. CSX Transportation, Inc.*, 575 U.S. 21 (2015); *Direct Marketing Ass'n v. Brohl*, 575 U.S. 1 (2015); *North Carolina Department of Revenue v. Kimberley Rice Kaestner 1992 Family Trust*, 139 S. Ct. 2213 (2019); and *Steiner v. Utah State Tax Commission*, 449 P.3d 189 (Utah 2019), *cert. denied*, 140 S. Ct. 1114 (2020). More recently, COST filed *amicus* briefs in *Ferrellgas Partners, L.P. v. Director, Division of Taxation*, 251 A.3d 760 (N.J. 2021), *cert. denied*, 142 S. Ct. 1440 (2022); *Washington Bankers Ass'n v. State of Washington, Department of Revenue,* 495 P.3d 808 (Wash. 2021), *cert. denied*, 142 S. Ct. 2828 (2022); and on the merits in *United States ex rel. Schutte v. SuperValu, Inc.,* 143 S. Ct. 1391 (2023); *Quad Graphics, Inc. v. North Carolina Department of Revenue*, 382

N.C. 356 (N.C. 2022), *cert. denied*, 143 S. Ct. 2638 (2023); and *MMN Infrastructure Services, LLC v. Michigan Department of Treasury*, 512 Mich. 594 (Mich. 2023), *cert. denied*, 144 S. Ct. 427 (2023).

As a long-standing business organization representing multijurisdictional taxpayers, COST is uniquely positioned to provide this Court with the analytical underpinnings for why the New York Court of Appeals affirming the Division of Taxation's denial of Petitioner's refund requests and the issuance of a corporate franchise tax deficiency violates the Commerce Clause and should be reviewed by this Court.

STATEMENT OF THE CASE

This case concerns a decision by the New York Court of Appeals holding the State's former corporate franchise tax statute, New York Tax Law § 208.9(o), did not discriminate against interstate and foreign commerce in violation of the Commerce Clause of the U.S. Constitution.[3] *In re Walt Disney Co. & Consol. Subsidiaries v. Tax Appeals Tribunal of the State*, Nos. 34, 35, 2024 NY Slip Op 02127 (N.Y. Apr. 23, 2024).[4]

Petitioner is a publicly-traded multinational, diversified entertainment conglomerate organized under the laws of Delaware. Petitioner's business includes the ownership, development, and use of intellectual property ("IP") assets through licensing to subsidiaries domestically and internationally. Internationally, Petitioner's foreign subsidiaries had licensing agreements with Petitioner, which permitted them to use Peti-

[3] U.S. Const. art. I, § 8, cl. 3.

[4] Consolidated with *International Business Machine Corp. & Combined Affiliates v. Tax Appeals Tribunal of the State.*

tioner's IP in exchange for royalty payments. These foreign subsidiaries had no business operations or activities in New York, and accordingly, did not file New York franchise tax returns. From 2008 to 2010, Petitioner paid taxes on its income allocatable to New York business activity, which represented between 5% and 6% of its total taxable income for the years at issue. During those years, Petitioner received royalty payments from foreign affiliates. For the 2009 and 2010 tax years, Petitioner deducted royalty payments received from all its foreign subsidiaries from its taxable income. It also subsequently filed an amended tax return for 2008 seeking a refund for foreign royalty income included in its taxable income. Petitioner was audited by the Division of Taxation, which denied its refund request and issued a notice of deficiency.

New York imposes a franchise tax on the allocated portion of the entire net income of a corporation earned in New York. New York Tax Law § 210.1. The starting point for the computation of New York taxable income is federal taxable income with certain modifications. In 2003, the statute was amended to enact a royalty expense addback which required taxpayers paying and deducting royalties to addback to federal taxable income royalties paid to a related member to the extent the royalties were deductible by the related member in calculating federal taxable income. New York Tax Law § 208.9(o)(2)(A). At the same time, the statute was also amended to allow taxpayers to deduct royalties received from related members.[5] New York Tax Law § 208.9(o). For the period at issue, Petitioner

[5] For purposes of both the royalty expense addback and the royalty exclusion provisions, the term "related member" was defined in relevant part as a corporation that owns at least 30% of the stock of another corporation. New York Tax Law § 208.9(o)(1)(A)-(B).

was subject to and filed New York corporate franchise tax returns. Pursuant to the statutory provision that permitted a taxpayer to exclude from New York taxable income royalties received from related parties, Petitioner deducted the royalty payments received from its foreign affiliates. The Division of Taxation denied Petitioner's exclusion of royalty income because its foreign affiliates paying the royalties were not subject to New York's corporate franchise tax.

The New York Tax Appeals Tribunal upheld the Division of Taxation's denial concluding Petitioner could deduct the royalty payments only if the related royalty payor was also a New York taxpayer. The New York Court of Appeals, Appellate Division, affirmed the Tax Appeals Tribunal holding the Division of Taxation's interpretation of the royalty income exclusion was not discriminatory under the Commerce Clause and the Foreign Commerce Clause of the U.S. Constitution. The New York Court of Appeals affirmed the Court of Appeals, Appellate Division, holding any burden on interstate or foreign commerce created by the New York tax scheme was incidental and did not violate this Court's dormant Commerce Clause protections related to discrimination and internal consistency. *See Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274 (1977). Because Petitioner's foreign subsidiaries did no business in New York and did not have a resulting filing requirement in New York, Petitioner was not allowed to deduct royalty income received by these non-New York foreign affiliates.

SUMMARY OF THE ARGUMENT

This case offers the Court an opportunity to provide guidance on the extent to which this Court's dormant Commerce Clause jurisprudence precludes discriminatory state taxation when the discrimination is based on a geographic determinant. Given the fundamental importance of *Kraft General Foods v. Iowa Department of Revenue and Finance*, 505 U.S. 71 (1992), to dormant Commerce Clause jurisprudence, it is critical for this Court to affirm *Kraft*'s precedential value in facial discrimination challenges to state taxes. This Court's intervention is especially pertinent in state tax discrimination challenges because these challenges predominantly stem from state courts self-reviewing their own state tax systems.

ARGUMENT

I. THE NEW YORK DECISION SIDESTEPS THIS COURT'S JURISPRUDENCE.

This Court has already provided in *Kraft* the constitutional framework which the New York Court of Appeals should have followed. Given the factual similarities between the case at hand and the facts presented in *Kraft*, the court should have reached the same result—New York's "foreign royalty addback" imposed on Petitioner violated the Commerce Clause. However, such was not the case.

The Commerce Clause of the United States Constitution provides that Congress shall have the authority to "regulate commerce . . . among the several states." U.S. Const. art. I, § 8, cl. 3. This affirmative grant of power has given rise to a concomitant negative or dormant implication—the states may not discriminate against interstate trade. *Assoc. Indus. v.*

Lohman, 511 U.S. 641, 646 (1994). The dormant element of the Commerce Clause thus prohibits economic protectionism on the part of states. States may not adopt measures designed to benefit in-state economic interests by burdening out-of-state competitors. *Id*. at 647. Thus, a state may not tax a transaction or incident more heavily when it crosses state lines than if it were to occur entirely within one state. *Id*. Nor may a state tax a transaction or incident more heavily when it crosses national borders than if it were to occur entirely within one state. Foreign commerce is afforded even greater protection than that afforded interstate commerce. *Kraft*, 505 U.S. at 79; *Japan Line, Ltd., v. Cnty. of Los Angeles*, 441 U.S. 434, 449 (1979).

The crux of this case, and the reason New York's "foreign royalty addback" provision is clearly invalid, lies with the fact that New York is treating royalty payments received from New York taxpayer affiliates who are doing business in the State more favorably than royalty payments received from non-New York taxpayer affiliates who are not doing business in the State.

The New York Court of Appeals' decision is inconsistent with *Kraft*. In *Kraft*, this Court addressed the inclusion of dividends from foreign subsidiaries in the tax base and found that Iowa facially discriminated against foreign commerce in violation of the Foreign Commerce Clause. Iowa, a separate reporting state, was not allowed to tax dividends from a controlled foreign corporation if it does not tax dividends from a controlled domestic corporation. The Court stated that: "[i]t is indisputable that the Iowa statute treats dividends received from foreign subsidiaries less favorably than dividends received from domestic

subsidiaries. Iowa included the former, but not the latter, in the calculation of taxable income." 505 U.S. at 75. The Court went on to determine that a state's preference for domestic commerce over foreign commerce is inconsistent with the Commerce Clause, even if the state's own economy is not a direct beneficiary of the discrimination: "[a]s the absence of local benefit does not eliminate the international implications of the discrimination, it cannot exempt such discrimination from Commerce Clause prohibitions." *Id*. at 80.

There are no significant differences between the facts and issues presented in *Kraft* and in this case. But the New York Court of Appeals attempts to distinguish *Kraft* based on New York's addback requirement which Iowa did not have in *Kraft*. *Disney*, 2024 NY Slip Op 02127, 6-7. Addback provisions are not a blanket panacea to a facially discriminatory corporate income tax scheme. And New York's discrimination based on a geographic determinant, placing a heavier burden on foreign commerce, is not cured by its addback provisions.

The concurrence also asserts that New York's tax scheme is permissible as a tax filing requirement. *Id.* at 10-12 (Wilson, C.J., concurring). The concurrence draws distinction between a tax provision that is a tax filing requirement and one "that imposes benefits or burdens depending upon where a business is located, where goods are produced, or where payments are made" with the former not creating an unconstitutional burden on interstate commerce. *Id.* at 10. But a New York tax return filing requirement is dependent on a taxpayer having business activities in the State. A business will not have a tax filing if it does not have business activities in the State. This aligns with what this Court in *Kraft* has illustrated as discriminatory—

"[t]he applicability of the Iowa tax necessarily depends not only on the domicile of the subsidiary, but also on the location of the subsidiary's business activities." 505 U.S. at 77.

This Court has addressed and struck down a similar New York tax scheme relating to a New York Domestic International Sales Corporation in *Westinghouse Electric Corp. v. Tully*, 466 U.S. 388 (1984). In *Westinghouse*, the State determined that a Domestic International Sales Corporation could receive a tax incentive only to the extent of its in-state business activity. This Court held that New York may not encourage the development of local industry by means of taxing measures that invite a multiplication of preferential trade areas within the United States. *Id*. In both *Westinghouse* and this case, New York is attempting to provide tax incentives only for businesses with in-state business activities, in violation of Commerce Clause protection.

II. THE NEW YORK DECISION FURTHER DIVIDES STATE COURTS.

Instead of following this Court's jurisprudence, the New York Court of Appeals justified its holding based on the Supreme Court of New Hampshire's decision in *General Electric Co., Inc. v. Commissioner, New Hampshire Department of Revenue Administration*, 914 A.2d 246 (N.H. 2006), *cert. denied*, 552 U.S. 989 (2007). In *General Electric*, the Supreme Court of New Hampshire rejected a Commerce Clause challenge to New Hampshire's tax deduction for dividends received from foreign subsidiaries that applied only to the extent that the foreign subsidiary conducted income-generating business. The New York Court of Appeals heavily relied on *General Electric* to conclude that New York's royalty addback provisions are not facially

discriminatory because there is "tax symmetry" in this case, where "there is no differential treatment on the corporate group level." 2024 NY Slip Op 02127, 7; *see General Electric*, 914 A.2d at 470. The New York Court of Appeals elaborates that there is no "differential treatment between companies that received the deduction and those that did not." *Id.* This kind of "symmetry," however, is not the appropriate analysis. The court's "tax symmetry" theory has not been adopted by this Court's jurisprudence. It is a fictious approach to support what would be discriminatory taxation of interstate and foreign commerce under this Court's case law. A tax imposed on a royalty-paying subsidiary doing business in New York, which provides New York with an independent basis for taxation, is different from a tax imposed on a royalty-paying subsidiary not doing business in New York. With the latter, New York has no independent basis for taxation.

Suggestions that this can be cured by a non-New York royalty-paying subsidiary volunteering to file New York tax returns is novel and unfounded. *Id.* at 12. A voluntary filing, where there is no legal basis for taxation, is not a "complementary" exaction that negates this discrimination. *See Or. Waste*, 511 U.S. at 100; *Armco, Inc. v. Hardesty*, 467 U.S. 638 (1984); 505 U.S. at 78 (the Court dismissing arguments that discriminatory taxation against foreign commerce can be avoided if a state "can force a taxpayer to conduct its foreign business through a domestic subsidiary" or if a taxpayer "changes the domicile of the corporations through which it conducts its business"). This unreasonable solution would also dismiss most, if not all, state tax discrimination challenges.

The New York Court of Appeals reliance on *General Electric* is also concerning because all other highest state courts evaluating comparable dividends received deduction constitutional challenges have held contrary to *General Electric*. Instead, *General Electric* is the "anomaly." Jerome R. Hellerstein et al., *State Taxation* ¶ 7.20[3][d][iii] (3d ed. 2001 & Supp. 2023). Courts in Mississippi, North Dakota, and California all found similar dividends received deduction limits unconstitutionally violated the dormant Commerce Clause. *Miss. Dep't of Revenue v. AT&T Corp.*, 202 So. 3d 1207 (Miss. 2016) (the Supreme Court of Mississippi held that Mississippi's dividend received exemption, which limited the exemption to dividends received from domestic affiliates doing business and filing income tax returns in Mississippi, violated the dormant Commerce Clause under this Court's internal consistency analysis); *D.D.I., Inc. v. State ex rel. Clayburgh*, 657 N.W.2d 228 (N.D. 2003) (the Supreme Court of North Dakota held that North Dakota's dividends received deduction to a dividend recipient, which is limited to the extent the dividend payor's income was subject to North Dakota corporate income tax, violated the dormant Commerce Clause under this Court's facial discrimination analysis); *Farmer Bros. Co. v. Franchise Tax Bd.*, 108 Cal. App. 4th 976 (2003), *cert. denied*, 540 U.S. 1178 (2004) (Court of Appeal of California held that California's dividends received deduction for only the portion of dividends received from another corporation when the dividends are in the payor corporation's measure of California franchise tax, alternative minimum tax, or corporation income tax violated the dormant Commerce Clause under this Court's facial discrimination and internal consistency analysis).

Rather than bolster the soundness of its legal analysis, the New York Court of Appeals' reliance on *General Electric* highlights the need for this Court to intervene. It exposes and deepens a conflict among state courts that this Court needs to address.

III. STATE TAX DISCRIMINATION CHALLENGES UNIQUELY NECESSITATE THIS COURT'S REVIEW.

State tax litigation is unique because it is subject to two constraints not existing in other areas of the law: the Tax Injunction Act and the comity doctrine. The Tax Injunction Act bars suits in federal courts to "enjoin, suspend or restrain the assessment, levy or collection" of state taxes, except where no "plain, speedy and efficient remedy" is available in a state court. 28 U.S.C. § 1341. Rarely have these conditions not been satisfied. Under the comity doctrine, "federal courts refrain from interfer[ing] … with the fiscal operations of the state governments . . . in all cases where the Federal rights of the persons could otherwise be preserved unimpaired." *Direct Mktg.*, 575 U.S. at 15 (quoting *Levin v. Com. Energy, Inc.*, 560 U.S. 413, 421 (2010)). This doctrine typically denies access to the federal courts. Both the Tax Injunction Act and the comity doctrine significantly constrain taxpayers' access to lower federal courts in state tax litigation. Indeed, such access is rare.

Such jurisdictional restrictions are unique to state tax controversies, and since 1988 when Congress eliminated mandatory review by this Court of state tax cases involving questions of federal law, petitions for writ of certiorari in state cases are subject to this

Court's discretionary review.[6] By contrast, other statutory or constitutional disputes involving environmental, health care, voting rights, educational issues and the like have no similar impediments or obstacles to federal review. In state tax controversies, taxpayers must rely almost exclusively on state courts to arbitrate federal constitutional challenges of state taxes.

In addition, state courts reviewing discrimination challenges of their own state tax systems require a remarkable level of self-control to ensure that they "avoid the tendencies toward economic Balkanization." *Hughes v. Okla.*, 441 U.S. 322, 325-326 (1979). This Court's review of this case is an essential check to ensure that the Commerce Clause limitations to state taxes are uniformly applied to avoid states imposing their own views on the Commerce Clause's restraints.

CONCLUSION

States have broad discretion in designing a tax structure. However, the tax structure cannot tax a transaction more heavily when it crosses state lines than when it occurs within the State, nor can that structure impose a tax which discriminates against interstate commerce by providing a direct commercial advantage to local business, or by subjecting interstate commerce to greater taxation. This Court already provided the controlling constitutional framework in *Kraft*. But the New York Court of Appeals' decision upholding the New York royalty addback tax scheme contravenes this Court's jurisprudence. For that

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[6] *See* P.L. 100-352, 102 Stat. 662 (June 27, 1988) (codified at 28 U.S.C. § 1254).

reason, this Court should grant review and reverse the judgment of the New York Court of Appeals.

Respectfully submitted,

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