ARIZONA COURT OF APPEALS

DIVISION ONE

SABAN RENT-A-CAR, LLC, et al., Plaintiffs/Appellees/ Cross-Appellants, v. ARIZONA DEPARTMENT OF REVENUE, Defendant/Appellant/ Appellee/Cross-Appellee, TOURISM AND SPORTS AUTHORITY, Defendant/Appellant/ Appellee/Cross-Appellee.	Court of Appeals Division One No. 1 CA-TX 16-0007 Maricopa County Superior Court No. TX2010-001089

ARIZONA DEPARTMENT OF REVENUE'S CROSS-APPEAL ANSWERING BRIEF TO SABAN RENT-A-CAR'S CROSS-APPEAL OPENING BRIEF

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INTRODUCTION*

Like Saban's state constitutional theory, its federal constitutional theory stretches the relevant constitutional provision so far that it leads to obviously absurd results. The core of Saban's dormant Commerce Clause argument rests on the premise that a state may never enact any tax that "falls, by design, in a predictably disproportionate way on out-of-state consumers." (Saban's Cross-OB at 99.) Accepting that premise effectively implies that no state or municipality anywhere may ever impose any tax of any amount on any car rental or other business that primarily serves tourists. Merely making explicit what Saban implicitly asks this Court to do reveals why Saban's request must be rejected.

Moreover, the law would not permit any other result. To the contrary, the United States Supreme Court has already explicitly rejected Saban's theory that "a state tax must be considered discriminatory for purposes of the Commerce Clause if the tax burden is borne primarily by out-of-state consumers." *Commonwealth Edison Co. v. Montana*, 453 U.S. 609,

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* This brief uses the same defined terms as the Department's prior briefs in this appeal, e.g., "Saban" refers to Plaintiffs/Appellees/Cross-Appellants. References to APP___ refer to the Department's Appendix attached to its Opening Brief.

618 (1981). Decisively, the Supreme Court refused to strike down the tax in that case for the same reason the superior court correctly rejected Saban's theory in this case: "the surcharge is not protectionist in nature" because "[i]t does not seek to deter or impede interstate commerce." [IR-161 at 4 (APP131).] *Cf. Commonwealth Edison*, 453 U.S. at 618 (explaining that the tax is administered under an "even-handed formula" and therefore is not "the type of differential tax treatment of interstate and intrastate commerce that the Court has found in other 'discrimination' cases.").

Faced with settled law fatal to its cross-appeal, Saban resorts to inventing new theories untethered from both the law and the underlying purposes of the dormant Commerce Clause. Saban claims, for example (at 93), that a court may conduct a facial analysis of a statute by examining something other than its text. Saban further claims (at 113) that a court may examine the effects of a statute without any evidence on the issue. But not only have courts universally rejected such theories, they have in some instances mocked them. (*See*, *e.g.*, Argument § II.C.1(a).) The Court should affirm the superior court's ruling that the AzSTA tax does not violate the dormant Commerce Clause.

STATEMENT OF FACTS AND CASE

The relevant facts and statement of the case are largely set forth in the Department's Opening Brief (at 14-23). Pertinent to the Commerce Clause issue, those involved with crafting the AzSTA legislation were aware that Arizona could not enact legislation that would violate the dormant Commerce Clause. They intended to draft legislation that complied with the dormant Commerce Clause. [IR-20 at 118 ("[T]he language was drafted as narrowly as possible because of the constitutionality issue. Under the Interstate Commerce clause, a resident cannot be deemed exempt.").]

The underlying purposes of the voter-approved Proposition were set forth in the Publicity Pamphlet, with the first purpose being to "promote tourism in Maricopa County":

> The Authority is established by law to: (i) promote tourism in Maricopa County; (ii) develop a multipurpose facility in Maricopa County for the use of a professional football franchise, a major college bowl sponsor, sports organization other than football (such as professional soccer, Pan Am and World Cup games, and NCAA championship basketball tournament games) and organizers of other events (such as trade shows, concerts and similar attractions); (iii) develop and renovate Cactus League baseball spring training facilities in Maricopa County with other governmental partners; and (iv) develop and improve youth and amateur sports facilities, recreational facilities and other community facilities in Maricopa County with other governmental partners.

[IR-20 at 125.] Nothing in the AzSTA legislation sought to protect a local industry from out-of-state competition. And nothing in the AzSTA legislation sought to encourage Arizonans to buy products from a local business at the expense of out-of-state competitors.

The AzSTA tax, codified at A.R.S. § 5-839, is lower if a "person leases or rents the motor vehicle as a temporary replacement motor vehicle," as compared to other rentals. A.R.S. § 5-839(B)(2). During the course of the litigation, the superior court required the parties to develop a record to determine whether and to what extent the surcharge, due to the temporary-replacement provision, "burdens customers from out of state over Arizona customers." [IR-161 at 4 (APP131).] That record shows that "the car rental companies are charging the same rate to all customers regardless of their reason for renting," i.e., the temporary-replacement provision has never been implemented. [*Id.*; *see also* IR-122 at 4 (APP142) (response to Interrogatory No. 2(a)).]

Notwithstanding that record, in the superior court Saban focused its dormant Commerce Clause challenge on the temporary-replacement provision. [*See* IR-21.] For example, Saban contended that the AzSTA tax "[o]n its face . . . purports to exclude in state residents from the burden of

the car rental tax by excluding in state residents from paying for car rental taxes under their most likely circumstance (rental of a car while their own vehicle is unavailable)." [IR-21 at 17.] Saban also "belatedly raise[d] a challenge to the tax on car rentals as a whole: because most car renters are from out of state, a tax on rental cars is discriminatory even without the differential rate for replacement cars." [IR-161 at 5 (APP132).]

The superior court rejected Saban's arguments. With respect to Saban's primary argument, the superior court found that "the surcharge is not protectionist in nature." [*Id.* at 4 (APP131).] It further found that the tax "does not seek to deter or impede interstate commerce; on the contrary, the promise of palatial sports facilities can only be realized by maximizing the amount that can be extracted from visitors without keeping them away." [*Id.*] Lastly, the superior court found that the car rental "companies have imposed the same tax on in-state and out-of-state renters, and on replacement-car and non-replacement car, customers alike," and thus the tax "raises no commerce clause issue." [IR-161 at 4-5 (APP131-132).]

With respect to Saban's "belatedly raise[d]" alternative argument concerning "the tax on car rentals as a whole," the superior court found

that argument waived. [*Id.* (Because this new issue would require "litigating from scratch[,] [t]the Court does not believe it is appropriate at this late date.").] The superior court also commented that it did not "find persuasive support for such an argument in relevant case law." [*Id.*] Saban has not challenged the superior court's waiver ruling in its cross-appeal.

After the superior court entered judgment, Saban timely filed a notice of cross-appeal. [IR-261.] This Court has jurisdiction under A.R.S. § 12-2101(A)(6).

ISSUES

1. The dormant Commerce Clause respects valid exercises of state and local taxing authority and invalidates taxes only if they interfere with certain aspects of interstate commerce. The AzSTA tax is facially neutral, it has a legitimate purpose, and there is no evidence that it has had any relevant adverse effects on interstate commerce. Should the Court nevertheless invalidate the AzSTA tax as a forbidden effort to interfere with interstate commerce?

2. May the Court summarily reject Saban's argument based on looking to "the tax on car rentals as a whole" [IR-161 at 5 (APP132)]

because the superior court found that argument waived and Saban has not challenged that waiver ruling on appeal?

STANDARD OF REVIEW

Because this case was decided on summary judgment and presents questions of law, the Court reviews the issues de novo. *See Maycock v. Asilomar Dev., Inc.*, 207 Ariz. 495, 498, ¶ 14 (App. 2004) (summary judgment); *id.* at 500, ¶ 24 (issues of law).

ARGUMENT

The Supreme Court set forth the modern dormant Commerce Clause principles for tax cases in *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 279 (1977). That case established a four-part test, which considers a tax's "practical effect, and . . . sustain[s] a tax against Commerce Clause challenge when the tax [1] is applied to an activity with a substantial nexus with the taxing State, [2] is fairly apportioned, [3] does not discriminate against interstate commerce, and [4] is fairly related to the services provided by the State." *Id.* (bracketed numbers added). Only the third factor of the *Complete Auto* test (discrimination against interstate commerce) is at issue in this appeal.

The AzSTA tax does not run afoul of this factor. As set forth below in Argument § I, nothing about the AzSTA tax in any way violates the dormant Commerce Clause. Saban's contention that the AzSTA tax is "protectionist" is conceptually flawed, and the core of its argument rests on a demonstrably false premise (i.e., that states may not enact taxes where out-of-staters pay the bulk of the tax).

As set forth in Argument § II, the doctrinal tests courts have developed for evaluating taxes under the dormant Commerce Clause confirm the AzSTA tax is not "discriminatory." In particular, the AzSTA tax is facially neutral, it does not have an improper purpose (and purpose alone would not suffice in any event), and there is no evidence that it has any discriminatory effects. The Court should thus affirm the superior court's ruling on the Commerce Clause.

I. The AzSTA tax is not the type of tax that a court may invalidate under the dormant Commerce Clause.

The core principles that underlie dormant Commerce Clause jurisprudence—which must provide the touchstone for the Court's analytic work—demonstrate unequivocally that the AzSTA tax does not run afoul of the dormant Commerce Clause.

A. The dormant Commerce Clause guards against economic protectionism, but it does not preclude all local regulation that in some way affects the flow of commerce.

The dormant Commerce Clause stems from the express grant of power to Congress to regulate commerce among the states. *See* U.S. Const. art. I, § 8, cl. 3 ("*Congress shall have Power* . . . [t]o regulate Commerce . . . among the several States[.]") (emphasis added). The central question in a dormant Commerce Clause challenge, therefore, is whether a state or local government has usurped the authority of Congress by doing what only the Congress has the power to do: i.e., "[t]o regulate Commerce . . . among the several States." *Id.*[1]

[1] Several Supreme Court Justices and many others have noted that the dormant Commerce Clause has no basis in the text of the Constitution, and therefore they believe the doctrine should be rejected entirely or at least as applied beyond the most quintessential interference with interstate commerce. Justice Scalia characterized the dormant Commerce Clause as "a *judicial fraud*." *Comptroller of Treasury v. Wynne*, 135 S. Ct. 1787, 1808 (2015) (Scalia, J., dissenting) ("The fundamental problem with our negative Commerce Clause cases is that the Constitution *does not contain a negative Commerce Clause*. It contains only a Commerce Clause. . . . The Clause says nothing about prohibiting state laws that burden commerce.") (Emphases added.) Others have reached similar conclusions. *See, e.g.*, *McBurney v. Young*, 133 S. Ct. 1709, 1720-21 (2013) (Thomas, J., concurring) (stating that "[t]he negative Commerce Clause has no basis in the text of the Constitution, makes little sense, and has proved virtually unworkable in application") (citation omitted).

At the root of the doctrine, state and local governments cannot directly regulate interstate commerce by projecting their laws into other jurisdictions and regulating beyond their borders. For example, California cannot impose a 5% royalty (paid to artists) on sales of art outside of California merely because the seller lives in California. *See*, *e.g.*, *Sam Francis Found. v. Christies, Inc.*, 784 F.3d 1320 (9th Cir. 2015) (en banc), *cert. denied*, 136 S. Ct. 795 (2016). To do so would regulate an art sale in New York by requiring a royalty to a North Dakota artist merely because the seller is a California resident. Accordingly, the law "regulates a commercial transaction that 'takes place wholly outside of the State's borders.'" *Id.* at 1323 (citation omitted).

But the dormant Commerce Clause regulates more than just direct interstate regulation. In particular, "[t]he modern law of what has come to be called the dormant Commerce Clause is driven by concern about 'economic protectionism.'" *Dep't of Revenue v. Davis*, 553 U.S. 328, 337 (2008) (citation omitted). Within this category, the classic dormant Commerce Clause violation is a protectionist import tariff. This is "the quintessential evil targeted by the dormant Commerce Clause." *Comptroller of Treasury v. Wynne*, 135 S. Ct. 1787, 1792 (2015); *see also Pharm.*

Research & Mfrs. of Am. v. Cty. of Alameda, 768 F.3d 1037, 1042 (9th Cir. 2014) ("[C]ases of this kind are legion.") (Quoting *West Lynn Creamery, Inc. v. Healy*, 512 U.S. 186, 194 (1994)). For example, Arizona cannot tax orange imports in order to prop up Arizona's citrus industry against competition from California growers.

At the same time, "not every exercise of local power is invalid merely because it affects in some way the flow of commerce between the States." *Nat'l Ass'n of Optometrists & Opticians v. Harris*, 682 F.3d 1144, 1148 (9th Cir. 2012) (citation omitted). To the contrary, the dormant Commerce Clause "respects federalism by protecting local autonomy." *Id.* "The law has had to respect a cross-purpose as well, for the Framers' distrust of economic Balkanization was limited by their federalism favoring a degree of local autonomy." *Davis*, 553 U.S. at 338 (comparing The Federalist Nos. 7 (A.

Hamilton), 11 (A. Hamilton), and 42 (J. Madison), *with* The Federalist No. 51 (J. Madison)).[2]

The law must be this way. If the rule were different, the dormant Commerce Clause would cripple state and local government because almost every governmental action affects interstate commerce in some way. Imposing a speed limit on a state highway affects interstate FedEx deliveries. Licensing requirements for doctors affect the interstate market for healthcare. Differences in sales tax rates affect interstate purchasing decisions, particularly near state borders. But no one seriously contends that those actions would violate the dormant Commerce Clause.

Indeed, courts have upheld:

- A flat fee "on trucks that undertake point-to-point hauls between Michigan cities," against a challenge that "trucks that carry *both* interstate and intrastate loads engage in intrastate business less than trucks that confine their operations to"

[2] Saban's focus on only some of the founders' statements (Saban's Cross-OB at 90 n.41) is incomplete because it ignores the important principle of federalism and local autonomy. *See* Federalist No. 51 ("In the compound republic of America, the power surrendered by the people is first divided between two distinct governments, and then the portion allotted to each subdivided among distinct and separate departments. Hence a double security arises to the rights of the people. The different governments will control each other, at the same time that each will be controlled by itself.").

Michigan, and thus the fee has an alleged discriminatory effect. *Am. Trucking Ass'ns, Inc. v. Mich. Pub. Serv. Comm'n*, 545 U.S. 429, 431 (2005).

- A reporting obligation on merchants who do not collect Colorado taxes (when only out-of-state merchants are exempt from tax collection). *Direct Mktg. Ass'n v. Brohl*, 814 F.3d 1129, 1141 (10th Cir.), *cert. denied*, 137 S. Ct. 591 & 593 (2016).

- An Arizona law prohibiting direct shipments of wine to consumers, with exceptions for (1) small wineries, and (2) small shipments "if the consumer is physically present at the winery when he buys the wine." *Black Star Farms LLC v. Oliver*, 600 F.3d 1225, 1227-28 (9th Cir. 2010).

- A discount on highway tolls for users of Massachusetts's toll transponder not available to users of New York's interoperable transponder. *Doran v. Mass. Tpk. Auth.*, 348 F.3d 315 (1st Cir. 2003).

Like the above examples (and others), the AzSTA tax is a paradigm example of a statute that does not run afoul of the dormant Commerce Clause. It "is not protectionist," and "does not seek to deter or impede interstate commerce." [IR-161 at 4 (APP131).] It thus in no way intrudes upon Congress's reserved power to regulate commerce or otherwise involves the type of protectionism abhorred by the dormant Commerce Clause.

To the contrary, as explained in the next section, the AzSTA tax encourages interstate commerce in a manner consistent with the dormant

Commerce Clause. It therefore does not violate the dormant Commerce Clause. *Cf. Commonwealth Edison*, 453 U.S. at 618 ("The premise of our discrimination cases is that '[t]he very purpose of the Commerce Clause was to create an area of free trade among the several States.'") (citation omitted).

B. Saban's attempt to shoehorn this case into the protectionist line of cases it cites shows why this case does not violate the dormant Commerce Clause.

In an effort to paint the AzSTA tax as impinging on the dormant Commerce Clause, Saban attempts to shoehorn this case into the line of economic protectionism cases where courts have been particularly hostile to state regulation. Those cases typically involve efforts to protect local business against the competitive forces of the national market (typically, lower-priced competitors).

For example, in *Bacchus Imports, Ltd. v. Dias*, 468 U.S. 263 (1984), upon which Saban heavily relies, Hawaii taxed alcohol but exempted certain alcohols (okolehao and pineapple wine) only if they were "manufactured in the State." *Id.* at 270 (citation omitted). (*See* Argument § II.A.3(a).) The Hawaii legislature intended to "promote" and "help in stimulating the local" industries and thus imposed a different tax rate on certain types of

alcohol produced in Hawaii versus the same type of alcohol produced outside Hawaii. 468 U.S. at 270 (quotation marks and citations omitted). The Court predictably held that "the legislation constitutes 'economic protectionism' in every sense of the phrase." *Id.* at 272.

In *C & A Carbone, Inc. v. Town of Clarkstown*, 511 U.S. 383 (1994), a New York town sought to protect and prop up a local trash transfer station by requiring all of the town's trash to be processed there, even though companies in other states were cheaper. *Id.* at 387. Again, the law's protection of the "local proprietor" gives the ordinance its "protectionist effect." *Id.* at 392.

In *Camps Newfound/Owatonna, Inc. v. Town of Harrison*, 520 U.S. 564 (1997), the Supreme Court faced a Maine law that gave a more-generous tax benefit to charities that benefitted Maine residents. *Id.* at 568. Limiting the tax benefit in that manner was protectionism, and "[p]rotectionism, whether targeted at for-profit entities or serving, as here, to encourage nonprofits to keep their efforts close to home, is forbidden under the dormant Commerce Clause." *Id.* at 588.

And in *West Lynn Creamery*, 512 U.S. at 189, the Court addressed Massachusetts's response to the fact that "Massachusetts dairy farmers

began to lose market share to lower cost producers in neighboring States." The State responded with a subsidy for Massachusetts-based dairies, paid for by a tax on milk (including milk produced out of state). *Id.* at 190-91. The Court again reiterated the principle that "[p]reservation of local industry by protecting it from the rigors of interstate competition is the hallmark of the economic protectionism that the Commerce Clause prohibits." *Id.* at 205. And it again struck down the protectionist law.

Virtually all of the cases upon which Saban heavily relies address import tariffs, the "quintessential evil targeted by the dormant Commerce Clause." *Wynne*, 135 S. Ct. at 1792. Out of necessity, Saban thus claims (at 88) that the AzSTA tax "serves functionally as an export tariff" designed to "protect[] Arizona's tourism industry." But the AzSTA tax is intended to promote Arizona tourism, and thus encourage the type of interstate commerce celebrated by the Commerce Clause. To say that the AzSTA tax "protects" the tourism industry (in the sense used in Commerce Clause cases) when that tax falls on the allegedly "protected" industry is nonsensical; you don't protect an industry by taxing it or its customers. Thus Saban's contention that tourists end up paying a majority of the tax *undercuts* its dormant Commerce Clause argument because the "protected"

industry depends on tourists. [*Cf.* IR-161 at 4 (APP131) (the AzSTA tax "does not seek to deter or impede interstate commerce" and cannot work by "keeping [visitors] away").]

In reality, the AzSTA tax is the opposite of the sort of economic protectionism addressed by the cases Saban cites. The majority of the cases Saban cites therefore have no bearing on this case other than to confirm this case is different.

C. Saban's theory rests on the false premise that States may not impose taxes where the tax burden is borne primarily by out-of-state consumers.

In addition, Saban's dormant Commerce Clause theory ultimately rests on a demonstrably false premise: that a State may not enact any tax that "falls, by design, in a predictably disproportionate way on out-of-state consumers." (Saban's Cross-OB at 99.) Indeed, over thirty years ago the Supreme Court in *Commonwealth Edison* explicitly rejected the foundation of Saban's theory: "that a state tax must be considered discriminatory for purposes of the Commerce Clause if the tax burden is borne primarily by out-of-state consumers." 453 U.S. at 618. In doing so, the Supreme Court upheld a tax on coal mined in Montana even though "90% of Montana coal is shipped to other states." *Id.* at 617. It expressed "misgivings about

judging the validity of a state tax by assessing the State's . . . 'exportation' of the tax burden out of State." *Id.* at 618. Although *Commonwealth Edison* all but controls the outcome of this case, and the parties extensively briefed it below [*see* IR-15, 21, 24], Saban says nothing about that case in its Opening Brief on Cross Appeal. That silence speaks volumes.

And, *Commonwealth Edison* is not the only authority confirming that the foundation of Saban's theory in this case lacks merit. In *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69, 88 (1987), a party "contend[ed] that the statute is discriminatory because it will apply most often to out-of-state entities." The Court noted that the "argument rests on the contention that, as a practical matter, most hostile tender offers [i.e., those affected by the statute] are launched by offerors outside Indiana." *Id.* The Court rejected that argument and held that the statute did not violate the dormant Commerce Clause. *See id.*

Other courts have reached the same conclusion when considering challenges to laws allegedly aimed at tourists. In *Valley Bank v. Plus Sys., Inc.*, 914 F.2d 1186, 1193 (9th Cir. 1990), plaintiffs challenged a law allegedly intended to "profit from out-of-state tourists[]." There, the law effectively enabled local Nevada banks to charge higher ATM fees to other banks'

customers, and an ATM network contended that those customers would likely be out-of-state tourists. *Id.* at 1188, 1193. Relying on *CTS*, the court concluded that "a state law is not 'discriminatory' under the commerce clause simply because it applies most often to out-of-staters." *Id.* at 1193.

Likewise, in *Airway Arms, Inc. v. Moon Area Sch. Dist.*, 446 A.2d 234, 242 (Pa. 1982), a state supreme court faced a tax on parking lots, where "the vast majority of patrons of the parking lots are traveling in air commerce," and 88.5% of them were traveling outside the state. Nevertheless, the court concluded that the tax was not discriminatory. "The tax burden in this case is borne according to the extent of use of the parking facilities and not on a distinction between patrons using interstate air commerce and patrons engaged in intrastate air commerce or local commerce." *Id.*

Courts have thus repeatedly and consistently rejected arguments like the ones Saban makes here. Tellingly, Saban cites no case striking down a tax merely because more out-of-staters than in-staters pay the tax (directly or indirectly).

Logically the law could not be any other way; otherwise States could *never* tax businesses that rely primarily on tourists for revenue (such as car rental agencies, hotels, and others). For this reason, as explained further in

Argument § II.D below, Saban's theory if accepted would send shockwaves across the country because numerous States and municipalities rely on taxes borne primarily by tourists. To accept Saban's theory would involve an "unwarranted departure from the rationale of [the Supreme Court's] prior discrimination cases." *Commonwealth Edison*, 453 U.S. at 619. The Court should decline Saban's invitation to significantly depart from the governing dormant Commerce Clause jurisprudence, and instead affirm the superior court's ruling on the dormant Commerce Clause.

II. The AzSTA tax cannot be subjected to strict scrutiny because it does not discriminate against out-of-state interests.

Despite these fundamental defects with Saban's theory, Saban claims that the AzSTA tax violates the dormant Commerce Clause by discriminating against out-of-staters. But "[t]he party challenging the statute bears the burden of showing discrimination." *Black Star Farms LLC v. Oliver*, 600 F.3d 1225, 1230 (9th Cir. 2010). "A statutory scheme 'can discriminate against out-of-state interests in three different ways: (a) facially, (b) purposefully [i.e., intent], or (c) in practical effect.'" *Nat'l Ass'n of Optometrists & Opticians v. Brown*, 567 F.3d 521, 525 (9th Cir. 2009)

(citation omitted). Contrary to Saban's contention, the AzSTA tax does not discriminate in any of these three ways.[3]

A. The AzSTA tax does not facially discriminate because it applies evenhandedly regardless of geography.

1. Section 5-839's text makes no geographic distinctions, which ends the facially discriminatory inquiry.

"[W]hen the Supreme Court has concluded a law facially discriminates against interstate commerce, it has done so based on statutory language *explicitly* identifying geographical distinctions." *Direct Mktg.*, 814 F.3d at 1141 (emphasis added). Evaluating facial discrimination thus requires starting (and ending) with the statute's plain text. In this case, the AzSTA tax's plain text does not facially discriminate against interstate commerce.

Nothing in § 5-839 (including the unused temporary-replacement provision) draws any geographical distinctions based on the location of either rental agencies or their customers. Thus in-state rental agencies (such as Saban) pay the same amount as out-of-state rental agencies (such

[3] Saban follows this same framework and in the same order, but groups facial discrimination and discriminatory intent together under the "purposefully" category. (*See* Saban's Cross-OB at 92-112 (heading (a) for facial discrimination; heading (b) for discriminatory intent).)

as Hertz or Avis). Moreover, rental agencies must pay the same tax without regard to the residency of their customers. Thus, the AzSTA tax does not facially discriminate against interstate commerce. *See, e.g.*, *Am. Trucking*, 545 U.S. at 434 (fee does not facially discriminate when "[t]he statute applies evenhandedly to all" affected companies); *Commonwealth Edison*, 453 U.S. at 618 ("But the Montana tax is computed at the same rate regardless of the final destination of the coal, and there is no suggestion here that the tax is administered in a manner that departs from this even-handed formula. We are not, therefore, confronted here with the type of differential tax treatment of interstate and intrastate commerce that the Court has found in other 'discrimination' cases."). Indeed, Saban concedes (at 97) that § 5-839 "utilizes seemingly neutral sounding words." That brings the facial inquiry to an end. The AzSTA surcharge cannot therefore be subjected to strict scrutiny under a "facially discriminatory" analysis.

2. Contrary to Saban's contention, a court may not find a statute facially discriminatory and subject it to strict scrutiny by going beyond the statute's plain text.

Recognizing that the AzSTA surcharge lacks any "statutory language explicitly identifying geographical distinctions," *Direct Mktg.*, 814 F.3d at 1141, Saban maintains (at 93) that a court may nevertheless find a statute

facially discriminatory (and thereby subject it to strict scrutiny without regard to its actual effects) in two other categories of cases. Under Saban's first theory, a statute facially discriminates if it uses neutral-sounding words "as proxies" to discriminate along state lines. (Saban's Cross-OB at 93.) Under its second theory, a court may (for reasons Saban never explains) "scrutinize[] the intent and effect [of a statute] to conclude its terms discriminate against interstate commerce." (*Id.* at 97.) In both instances, Saban contends, a court may look beyond the particular text of the statute in determining whether it facially discriminates (and is therefore subject to strict scrutiny).

But these two other types of "facial discrimination" cases do not exist. Decisively, Saban conflates *facial* discrimination with discriminatory *intent* and/or *effects*. If a statute uses a facially *neutral* proxy, then the only way to ascertain whether the statute nevertheless improperly discriminates along state lines is to examine the statute's *effects*. By definition, any discrimination that results from a *neutral* proxy will not show up on the statute's face; it will appear in the *effects*.

Similarly, if a court is going to actually "scrutinize[] the intent and effect [of a statute] to conclude its terms discriminate against interstate

commerce" (Saban's Cross-OB at 97), then it once again necessarily (and by definition) must look beyond the text and instead consider intent and effects (which is not a facial analysis). In its "facial discrimination" analysis, Saban even asks the Court (at 95-96) to use its "imagination" and "assume" certain things *about the statute's effects*. That is not how a facial analysis works.

Unsurprisingly, then, other courts have properly "decline[d] to look beyond the 'particular language' of the Statute in determining whether it is *facially discriminatory* because to do so would collapse the *facial* and *effects* analyses into one inquiry." *Brown & Williamson Tobacco Corp. v. Pataki*, 320 F.3d 200, 211–12 (2d Cir. 2003) (emphases added)). The Ninth Circuit, for example, recently rejected embracing an approach like the one Saban urges. *See Int'l Franchise Ass'n v. City of Seattle*, 803 F.3d 389, 400 (9th Cir. 2015), *cert. denied*, 136 S. Ct. 1838 (2016). Seattle imposed steeper minimum wage increases on large franchisees as compared to other employers. A franchise industry group argued that the franchise business model "is highly correlated with interstate commerce," meaning that most franchisors are from out-of-state (just like Saban contends that most rental cars are correlated with out-of-staters and replacement vehicle rentals are

correlated with in-staters). The Ninth Circuit rejected that argument, holding that distinguishing on that basis "does not constitute facial discrimination against out-of-state entities or interstate commerce." *Id.*

The Tenth Circuit likewise rejected such an argument. In *Direct Marketing*, Colorado imposed a reporting obligation on "retailers that sell goods to Colorado purchasers but do not collect Colorado sales or use taxes." 814 F.3d at 1141. By law, merchants with a physical presence in Colorado have to collect taxes, but merchants without a physical presence do not. *Id.* at 1132 (citing *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992)). Out-of-state merchants argued that Colorado imposed a reporting obligation on them but not on in-state merchants (who collected taxes and thus were not subject to the reporting obligation). The district court agreed, noting that the "veil" of facially neutral words could not overcome the obvious conclusion that Colorado treated the merchants differently (even though out-of-state merchants could voluntarily collect taxes and thus become exempt from the reporting requirements). *Id.* at 1140 (quoting district court). To top it off, the title of the statute was, "An Act Concerning the Collection of Sales and Use Taxes on Sales Made by *Out–Of–State Retailers*." *Id.* at 1141 (emphasis added). Nevertheless, the Tenth Circuit

rejected the notion of proxies and relied on the facially neutral text of the statute for its facially discriminatory analysis: "On its face, the law does not distinguish between in-state and out-of-state economic interests." *Id.*

The First Circuit reached the same conclusion in *Doran v. Massachusetts Turnpike Authority*, 348 F.3d 315 (1st Cir. 2003), which addressed highway tolls. Massachusetts offered a discount to cars with the Massachusetts "FAST LANE" transponder, but not to cars with transponders from other states' systems (such as New York's E-Z Pass), even though the transponders were interoperable and could be used on Massachusetts highways. *Id.* at 317. Out-of-staters argued that the discount treated in-staters differently from out-of-staters. Although FAST LANE was available to non-residents, the out-of-staters argued that "few non-residents" would take advantage of them, so of course the vast majority of FAST LANE users would come from Massachusetts. *Id.* at 321. The court rejected that proxy-based argument, ruling that the discount is not facially discriminatory because nothing prevents out-of-staters who already have an E-Z Pass transponder from also getting a FAST LANE transponder, so out-of-staters "are not 'penalized.'" *Id.* at 322.

Courts have thus repeatedly faced—and uniformly rejected—the type of "facial" arguments Saban advances here.

3. Contrary to Saban's suggestion, *Bacchus Imports* and *Camps Newfound* involved statutes that explicitly differentiated between interests along state lines.

Ignoring the cases that have rejected Saban's "broad approach," Saban instead showcases (at 93-100) two of its irrelevant protectionist cases: *Bacchus Imports* and *Camps Newfound*. It claims (at 93) these cases are examples of "decisions falling into the facial discrimination category" that involved regulations "not drawn explicitly along state lines." In fact, however, both cases are paradigm examples of ones involving regulations "drawn explicitly along state lines." Saban's illustrative cases—apparently the best examples it could find—do not support its expansive facial discrimination theory.

(a) *Bacchus Imports* involved a statute that discriminated explicitly along state lines.

Bacchus addressed tax exemptions for two kinds of locally produced alcohol. Hawaii taxed liquor, but expressly exempted "[o]kolehao *manufactured in the State*" and "[a]ny fruit wine *manufactured in the State*." Haw. Rev. Stat. § 244-4(6), (7) (Supp. 1983) (emphases added) (quoted in

Matter of Bacchus Imports, Ltd., 656 P.2d 724, 726 n.1 (Haw. 1982)). Although Saban quotes the full statutory text in a footnote (Saban's Cross-OB at 93-94 n.44), the main text of Saban's brief (at 94) omits the italicized portions—facial demarcations drawn explicitly along state lines.

In light of the statute's actual text, the Court had no need to search for proxies to find discrimination. Indeed, the Court emphasized that the tax exemption "applies only to *locally produced beverages*." 468 U.S. at 271 (emphasis added).

Ignoring the statute's actual language, Saban relies on a summary of *Bacchus* from a later case, *Amerada Hess Corp. v. Director, Division of Taxation, N.J. Department of Treasury*, 490 U.S. 66, 76 (1989). But *Amerada* did not rely on any kind of proxy theory either (in fact, it upheld the tax before it), so its discussion of *Bacchus* is classic dicta. Moreover, the discussion is incomplete and does not actually say that *Bacchus* held that a proxy can support finding facial discrimination. The Court should not rely on Saban's inaccurate extrapolation of *Amerada*'s incomplete summary of *Bacchus*.

Finally, even if *Bacchus* did rely on okolehao as a proxy for locally produced alcohol, it would be a perfect proxy, unlike the purported

proxies Saban relies on. The Supreme Court quoted the Hawaii Supreme Court as noting that "it had 'good reason to believe neither okolehao nor pineapple wine is produced elsewhere.'" *Bacchus*, 468 U.S. at 269. By contrast, Saban cannot claim *no* in-staters rent cars or that *no* out-of-staters rent cars as temporary replacement vehicles. Those supposed proxies thus are not perfect proxies, so a court would need to evaluate their *effects* on commerce (again demonstrating that Saban inappropriately conflates facial discrimination with discriminatory effects).

(b) *Camps Newfound* involved a statute that discriminated explicitly along state lines.

The statute in *Camps Newfound* likewise expressly discriminated along state lines. There, a Maine statute gave a less-generous tax benefit to charities "operated principally for the benefit of persons *who are not residents of Maine*." Me. Rev. Stat. tit. 36, § 652(1)(A) (Supp. 1996) (emphasis added) (quoted in *Camps Newfound*, 520 U.S. at 568). Thus, the Court held that "it is not necessary to look *beyond the text of this statute* to determine that it discriminates against interstate commerce." 520 U.S. at 575–76 (emphasis added).

Although the opinion also discusses the effects of the discriminatory tax benefit, the facial discrimination holding does not rely on that discussion. Saban claims (at 99) that parallels exist in the purported effects of the taxes at issue here and in *Camps Newfound* (e.g., Saban says, "the vast majority of the local business's customers are from out-of-state"). But the Supreme Court rejected applying cases addressing the relevance of the portion of out-of-state customers. Instead, it emphasized that "the Maine tax is facially discriminatory," so those cases do not apply. *Camps Newfound*, 520 U.S. at 579 n.13 (citing *Commonwealth Edison Co. v. Montana*, 453 U.S. 609 (1981); *CTS Corp. v. Dynamics Corp. of Am.*, 481 U.S. 69 (1987)). The Court addressed those issues in connection with the key disputes in the case, i.e., whether the dormant Commerce Clause even applied in a standard manner to summer camps (are campers "articles of commerce"?), to products "delivered and 'consumed' entirely within Maine," and to "charitable and benevolent institutions." *Camps Newfound*, 520 U.S. at 572, 583.

In sum, Saban's example cases do not justify subjecting the AzSTA tax to strict scrutiny.

B. The AzSTA tax does not have an improper purpose and a court may not strike down a tax on the basis of purpose alone.

Although Saban relies heavily on its allegation that the AzSTA tax had a discriminatory purpose, the purpose it ultimately points to—minimizing the tax burden on Arizona residents—is not *per se* improper under the Commerce Clause. Moreover, discriminatory purpose alone cannot violate the dormant Commerce Clause. The superior court, therefore, properly did not subject the AzSTA tax to strict scrutiny on the basis of the alleged discriminatory purpose.

1. The "purpose" Saban points to cannot by itself justify striking down the AzSTA tax.

As explained in Argument § I, for a statute to qualify as having an improper discriminatory purpose under the dormant Commerce Clause, it must be intended to discriminate in a manner invidious to the Commerce Clause, i.e., when a state regulates commerce in a manner that invades Congress's reserved power to do so. For this reason, judicial eyebrows typically get raised when, as in *Bacchus*, the relevant legislative history reveals a protectionist intent behind the legislation that runs afoul of the objectives of the dormant Commerce Clause.

Here, Saban contends the AzSTA tax generally (and the temporary-replacement provision in particular) has an improper purpose because it was designed so that "most of the tax burden" would "fall on out-of-state visitors." (Saban's Cross-OB at 106; *see also id.* at 102 (intended to "minimize the impact on the average Arizona resident") (citation omitted). However, as explained in Argument § I.C, a tax does not violate the Constitution merely because "the tax burden is borne primarily by out-of-state consumers." *Commonwealth Edison*, 453 U.S. at 618. Because a tax may, in at least some circumstances, lawfully burden "out-of-state consumers," intending for a tax to have that lawful effect cannot by itself qualify as an "improper" purpose under the dormant Commerce Clause. In other words, intending out-of-state consumers to bear the majority of a tax—the purpose Saban points to—cannot by itself be the type of improper discriminatory purpose that warrants striking down a law under the dormant Commerce Clause.

As for the *failed*, proposed temporary-replacement provision Saban emphasizes (that would have on its face discriminated on the basis of residency), that provision is irrelevant. Whatever the intent of the supporters of that provision may have had, it did not become part of the

legislation voters approved. Importantly, as Saban emphasizes, others involved in the AzSTA tax's design were keenly aware of potential Commerce Clause issues. Their side prevailed. They thus carefully crafted the AzSTA tax to promote tourism while *avoiding* any dormant Commerce Clause issues. [*See* IR-20 at 118.] Stated differently, they intended to create legislation that did not discriminate in a manner offensive to the Commerce Clause. Thus to the extent evidence of intent in this case matters (and it does not for the reasons set forth in the next section), the relevant evidence ultimately weighs in favor of upholding the AzSTA tax, not striking it down.

Decisively, in sharp contrast to this case, the cases Saban relies upon for its "purpose" analysis (at 100-101) involved a discriminatory purpose that squarely implicated the Commerce Clause's underlying objectives. The regulation in *S.D. Farm Bureau, Inc. v. Hazeltine*, 340 F.3d 583 (8th Cir. 2003) "prohibit[ed] corporations and syndicates, subject to certain exemptions, from acquiring or obtaining an interest in land used for farming and from otherwise engaging in farming in South Dakota." *Id.* at 587. Its purpose—to ensure that the state's agriculture industry "remain in the hands of family farmers and ranchers," *id.* at 594—ran directly contrary

to the Commerce Clause's foundational purpose. *See id.* at 593 (explaining that "the dormant Commerce Clause carries out the Framers' purpose to preven[t] a State from retreating into economic isolation or jeopardizing the welfare of the Nation as a whole, as it would do if it were free to place burdens on the flow of commerce across its borders that commerce wholly within those borders would not bear.") (internal quotation marks and citations omitted).

Similarly, the regulation in *Bacchus* gave a tax advantage to certain "locally produced beverages," 468 U.S. at 271 (i.e., classic economic protectionism), and the regulation in *SDDS, Inc. v. South Dakota*, 47 F.3d 263 (8th Cir. 1995), was "specifically designed and intended to hinder the importation of out-of-state waste into South Dakota," 47 F.3d at 268 (i.e., it intended to protect local interests by stifling interstate commerce). Both of these regulations thus likewise fit the dormant Commerce Clause paradigm.

As the superior court aptly observed, "the situation here differs." [IR-161 at 4 (APP131).] Here, the AzSTA tax was not designed to protect a local industry from out-of-state competition. Indeed, it was not intended to in any way (1) discourage anyone from coming to Arizona, or

(2) encourage Arizonans to buy products from a local business at the expense of other competitors. As the superior court recognized, it has nothing to do with "economic isolation" or otherwise burdening "the flow of commerce across its borders that commerce wholly within those borders would not bear." *Hazeltine*, 340 F.3d at 593 (citation omitted); [IR-161 at 4 (APP131 (the tax "does not seek to deter or impede interstate commerce")]. To the contrary, the AzSTA tax's primary objective is to promote Arizona's tourism industry, i.e., encourage out-of-staters to come to Arizona. That is something the dormant Commerce Clause applauds rather than abhors. There is thus nothing underlying the intent or purpose of the AzSTA tax that could justify subjecting it to strict scrutiny.

2. In addition, because a law without discriminatory effect does not usurp Congress's power to regulate interstate commerce, discriminatory purpose without discriminatory effect does not render a law unconstitutional.

Moreover, to violate the dormant Commerce Clause, a State must actually improperly regulate commerce. A failed "intent" to do so cannot by itself suffice. For example, a local government may hate outsiders, but without actually discriminating against them, that animosity does not usurp the Commerce Clause authority bestowed to Congress. For that

reason, discriminatory purpose alone cannot violate the dormant Commerce Clause.

Unsurprisingly, then, with one nonbinding exception that the Court should not follow, Saban cites no case that invalidated a law on the basis of discriminatory purpose alone. No binding authority has ever struck down a law on that basis, and for the Court to do so in this case would go well beyond the accepted contours of the dormant Commerce Clause. The Court should therefore reject Saban's request to strike down the AzSTA tax because of its purported "purpose."

(a) Discriminatory purpose alone does not render a law unconstitutional.

The superior court correctly noted that it could "find no support for the proposition that discriminatory intent standing alone violates the commerce clause." [IR-161 at 4 (APP131).] Indeed, nothing in the text of the Commerce Clause suggests that lawmakers' discriminatory purpose, standing alone, violates the U.S. Constitution.

True, many cases have repeated the three-part test for discrimination, which considers facial discrimination, discriminatory purpose, and discriminatory effect. *E.g.*, *Optometrists*, 567 F.3d at 525 ("A statutory

scheme 'can discriminate against out-of-state interests in three different ways: (a) facially, (b) purposefully, or (c) in practical effect.'") (citation omitted). But no binding authority from the U.S. Supreme Court or the Arizona Supreme Court (or even the Ninth Circuit) has ever struck down a law or tax on the basis of discriminatory purpose alone. In all controlling cases in which a court found discriminatory purpose, the court also found either facial discrimination or discriminatory effect. *See, e.g.*, *Bacchus*, 468 U.S. at 273 (relying on "both the purpose and effect" of the law).

In recent years, courts have increasingly noted that discriminatory purpose alone does not and should not violate the Constitution:

- "While courts routinely recite this test, there is some reason to question whether *a showing of discriminatory purpose alone* will invariably suffice to support a finding of constitutional invalidity under the dormant Commerce Clause." *All. of Auto. Mfrs. v. Gwadosky*, 430 F.3d 30, 36 n.3 (1st Cir. 2005) (citations omitted).
- "The Court finds it incongruous to say that a law violates the dormant Commerce Clause *merely by having a discriminatory purpose*. . . . If local lawmakers intend to discriminate in favor of local interests, but mistakenly pass a law that does not so discriminate, did those lawmakers violate the dormant Commerce Clause simply by their mistaken intentions? *The Court doubts it.*" *Puppies 'N Love v. City of Phoenix*, 116 F. Supp. 3d 971, 993 (D. Ariz. 2015).

- "[E]ven if the court were to find that the law was motivated by some discriminatory purpose, *that finding alone* would be unlikely to violate the Commerce Clause." *Int'l Franchise Ass'n v. City of Seattle*, 97 F. Supp. 3d 1256, 1272 n.14 (W.D. Wash.), *aff'd* 803 F.3d 389.

- "In no Commerce Clause case cited or disclosed by research has a statute or regulation been invalidated *solely because of the legislators' alleged discriminatory motives*." *Wal-Mart Stores, Inc. v. City of Turlock*, 483 F. Supp. 2d 987, 1013 (E.D. Cal. 2006) (and collecting citations).

- "[W]e decline to rule the TPT unconstitutional *based solely on the alleged discriminatory motives* of the city council members who supported it. . . . [¶] [T]he discrimination [the dormant Commerce Clause] prohibits is measured by the economic impact of a local regulation, not the evil motives of local legislators." *Burbank-Glendale-Pasadena Airport Auth. v. City of Burbank*, 64 Cal. App. 4th 1217, 1224 (1998).

(Emphases added.)

Common sense and the foundational premise of the dormant Commerce Clause compel the same conclusion. The Commerce Clause reserves for Congress the power "[t]o regulat[e] Commerce . . . among the several States." U.S. Const. art. I, § 8, cl. 3. If local lawmakers intend to regulate interstate commerce but *fail*, then that means they did not do the thing reserved for Congress (regulating commerce "among the several States"). Local governments usurping interstate power from Congress is the only justification for the dormant Commerce Clause. But in passing

unsuccessful discriminatory legislation, local governments do not tread on that power.

By contrast, if lawmakers intend to regulate commerce among states and they *succeed*, then that law necessarily would discriminate facially or in effect, rendering the "discriminatory purpose" redundant and unnecessary in striking down the discriminatory law.

Thus, despite dicta concerning discriminatory purpose, no binding authority justifies striking a local law on the basis of its alleged discriminatory purpose alone. The text and purpose of the Commerce Clause likewise do not justify that result. For these reasons, this Court must consider whether the AzSTA tax actually discriminates (and it does not).

(b) Saban's authority concerning discriminatory purpose does not hold otherwise, except in one limited and nonbinding case.

Saban identifies (at 101) one case striking down a law based solely on discriminatory purpose: *Hazeltine*, 340 F.3d at 593.[4] That case predates the recent view that intent is not enough. More fundamentally, the case

[4] Below, but not on appeal, Saban also relied on *Waste Management Holdings v. Gilmore*, 252 F.3d 316 (4th Cir. 2001) for this proposition. [IR-21 at 20.] That case suffers from the same problems as *Hazeltine*.

presupposes that discriminatory purpose alone renders a law unconstitutional. That proposition appears to have been uncontested in that case, and the opinion does not address how an *unsuccessful* intent to discriminate in any way robs Congress of the power to regulate interstate commerce. Moreover, and unlike the AzSTA tax, *Hazeltine* involved a classically protectionist law of the sort the dormant Commerce Clause guards against. The legislative history was "brimming with *protectionist* rhetoric." *Id.* at 594 (citation omitted; emphasis added) (citing legislative history stating, "[d]esperately needed profits will be skimmed out of local economies and into the pockets of distant corporations."). At bottom, *Hazeltine* is not binding on this Court and should not be followed.

Saban's other authorities do not support invalidating a law for discriminatory purpose alone. Saban relies (at 100-01) on *Bacchus*, but *Bacchus* expressly relied on "both the purpose and effect" of the law. 468 U.S. at 273; *see also id.* at 271 ("[T]he purpose of the exemption was to aid Hawaiian industry. Likewise, the effect of the exemption is clearly discriminatory . . . ."). Saban also quotes a summary of the *Bacchus* decision from *Amerada Hess*, 490 U.S. at 76. But *Amerada*'s summary of *Bacchus* is incomplete; *Bacchus* itself is the best guide to its holding.

Saban also cites *SDDS*, but *SDDS* (like *Bacchus*) did not rely on discriminatory purpose alone; it also observed that the law "is discriminatory in its effect." 47 F.3d at 270. Thus, the case did not address a law with discriminatory purpose but nondiscriminatory effect. And here, too, "the legislative history of the referred measure [was] brimming with protectionist rhetoric." *Id.* at 268.

Finally, Saban cites a treatise (at 101) for the premise that discriminatory intent alone suffices. (Citing Rotunda & Nowak, *Treatise on Constitutional Law*, § 11.8 at 246 (5th ed. 2012).)[5] Read in context, that section addresses whether a facially discriminatory law should be invalidated without moving to a balancing test. That issue is irrelevant to this case, and in any event the treatise's statement is, at best, an overstatement of the law. Moreover, even if the treatise actually purported to address whether discriminatory intent alone is enough, the treatise cites no case that could support the proposition.

[5] Citation updated to most recent edition.

C. Saban did not meet its burden of proving that the AzSTA tax has an impermissible discriminatory effect.

To prevail on a claim of discriminatory effect, Saban must have presented evidence of actual effects. It has no such evidence, and thus implicitly urges the Court not to require any. But the law does not permit a party to meet its burden of proof on this issue with speculation. Moreover, the limited evidence Saban relies upon confirms there is no dormant Commerce Clause problem in this case.

1. Saban must have evidence to meet its burden of showing that the AzSTA tax had discriminatory effects.

(a) Discriminatory effects arguments require actual evidence.

A plaintiff has the "burden . . . to offer[] substantial evidence of an actual discriminatory effect" to survive summary judgment. *Black Star Farms*, 600 F.3d at 1231 (quotation marks omitted); *accord Cherry Hill Vineyard, LLC v. Baldacci*, 505 F.3d 28, 37 (1st Cir. 2007). In upholding a state tax on intrastate trucking, the Supreme Court emphasized "the absence of record facts that empirically could show" a discriminatory effect. *Am. Trucking Ass'ns, Inc. v. Mich. Pub. Serv. Comm'n*, 545 U.S. 429, 435 (2005). Speculation will not do.

The federal appellate courts have encountered the lack of evidence on a discriminatory-effects claim so frequently that they have resorted to using colorful language in its absence. The Ninth Circuit explained, "[t]he proof of the pudding here must be in the eating, not in the picture on the box as seen through the partial eyes of the beholder." *Black Star Farms*, 600 F.3d at 1232. It further remarked, "In other words, prove it, or lose it." *Id.* Faced with another plaintiff who like Saban came to court without evidence, the First Circuit similarly held that a plaintiff who "offer[s] only prognostications woven from the gossamer strands of speculation and surmise" cannot meet its burden to show proof of discrimination. *Gwadosky*, 430 F.3d at 41.

In sum, speculation cannot replace actual evidence of discriminatory effects. *See Cherry Hill*, 505 F.3d at 39 ("Conjecture, however, cannot take the place of proof."). Consequently, "the mere fact that a statutory regime has a discriminatory *potential* is not enough to trigger strict scrutiny under the dormant commerce clause." *Id.* at 37 (emphasis in original). The evidence must be "significantly probative, not merely colorable." *Direct Mktg.*, 814 F.3d at 1142 (citation omitted).

(b) Contrary to Saban's contention, a "conceptual possibility" of discrimination cannot replace evidence of actual discriminatory effects.

Because Saban lacks any evidence of discriminatory effect, it invokes the premise that a "conceptual possibility" can substitute for evidence. Not so. Although Saban uses that or a similar phrase six times (at 113-16), no dormant Commerce Clause case actually uses the phrase and none of Saban's cited cases support the contention.

Saban relies on *West Lynn Creamery,* a case in which Massachusetts essentially taxed milk (produced both in- and out-of-state) and then rebated the tax back to in-state producers (including the taxes paid by out-of-state producers). 512 U.S. at 190-91. The Court concluded that "[t]he Massachusetts pricing order thus will *almost certainly* cause local goods to constitute a larger share, and goods with an out-of-state source to constitute a smaller share, of the total sales in the market." *Id.* at 196 (emphasis added; quotation marks and citation omitted). Because of the structure of the tax/rebate system, the Court could conclude with mathematical near-certainty that the tax would favor in-state producers. Moreover, unlike here, Massachusetts apparently did not contest the effects. The Court cataloged the State's four arguments, none of which

disputed the mathematical effects of the tax/rebate. *See id.* at 198. And to top it off, *West Lynn Creamery* is yet another classic protectionism case that has no relevance here.

Next, Saban relies on *C & A Carbone, Inc. v. Town of Clarkstown*, 511 U.S. 383 (1994). There, a town required trash to be processed at a specific waste transfer station in town. Although Saban contends that the Court did not require evidence, in fact the Court had ample evidence. The waste transfer station's "fee of $81 per ton exceeded the disposal cost of unsorted solid waste on the private market." *Id.* at 387. Consequently, a trash company tried to circumvent the law and process trash out of state. The town police, however, surveilled and intercepted trucks "destined for disposal sites in Illinois, Indiana, West Virginia, and Florida." *Id.* at 388. The Court had no need to speculate about the results because it already had actual facts about how the trash company reacted to the discriminatory law. And like *West Lynn Creamery*, there the government apparently did not contest those effects and the case addressed classic protectionism.

Saban again relies on *Bacchus Imports*, 468 U.S. 263. But like in *West Lynn Creamery* and *Carbone*, the government apparently did not dispute the

effects of the tax exemption for locally produced okolehao and pineapple wine.

Saban notes (at 113-15) that in these three cases, the Court did not demand evidence that the laws had been implemented. But no one contested that those laws were implemented. Here, it is undisputed that "the car rental companies are charging the same rate to all customers regardless of their reason for renting." [IR-161 at 4 (APP131).] The Court should decline Saban's invitation to assume, for example, that the temporary-replacement provision has had a forbidden economic impact when the evidence shows it has had no impact at all.

The Ninth Circuit has squarely rejected this sort of know-it-when-we-see-it approach to uncovering supposed pretextual discrimination. *See Valley Bank v. Plus Sys., Inc.*, 914 F.2d 1186, 1193 (9th Cir. 1990). There, a party (Plus) challenged a Nevada Law (SB 404). "Plus allege[d] that in practice SB 404 affects out-of-staters disproportionately to Nevadans, but Plus provide[d] no factual support for this assertion." *Id.* The court rejected that factual-argument-without-facts, explaining that "Plus's statement that SB 404's disproportionate impact is 'beyond dispute' is not enough to create a genuine factual issue on its claim that SB 404's

evenhandedness is superficial only." *Id.* (As discussed above (Argument § I.C), the court also rejected Plus's legal theory concerning the alleged disproportionate effect on out-of-staters.)

More recently, the Ninth Circuit again rejected the type of "conceptual possibility" of discrimination argument that Saban advances. *Black Star* observed that the plaintiff "ask[ed] [the court] without substantial evidentiary support to *speculate* and to *infer* that this scheme necessarily has the effect it fears. This leap of faith we will not take." 600 F.3d at 1232 (emphases added).

2. Saban has no evidence that the temporary-replacement provision has discriminatory effects, and the evidence shows just the opposite.

Saban suggests that the temporary-replacement provision has discriminatory effects, but it developed no evidence on that issue in the superior court, and thus cites no evidence in its discussion (at 116) of any actual effects on appeal. Saban's brief contains no citations to the record when discussing the supposed effects of that provision (at 116). It cites no evidence, for example, of any change in the ratio of out-of-state versus in-state renters before or after the AzSTA tax or any other potential method to

prove discriminatory effect between entities that are similarly situated. Saban thus has not met its burden.

Moreover, the evidence shows that the temporary-replacement provision has had no effect whatsoever on interstate commerce because it has never actually been implemented. As the superior court found, "the car rental companies are charging the same rate to all customers regardless of their reason for renting." [IR-161 at 4 (APP131); *see also* IR-122 at 4 (APP142 (response to Interrogatory No. 2(a))).] Thus, local residents have not received any benefit from the temporary-replacement provision.

Black Star considered an argument similar to Saban's. There, Arizona law, with two exceptions, prohibited direct shipments of wine to consumers. The exceptions permitted direct shipments (1) from "small winer[ies]," and (2) of two cases per year "if the consumer is physically present at the winery when he buys the wine." 600 F.3d at 1227-28. Like Saban's focus on the temporary-replacement provision, the plaintiffs in *Black Star* contended that "it should be *obvious*" that those exceptions had the effect of favoring local interests. *Id.* at 1232 (emphasis added). The Ninth Circuit slapped that argument down, emphasizing that "[c]onjecture cannot take the place of proof." *Id.* (citation and alterations omitted). Here,

of course, not only does Saban lack evidence to back up its conjecture, but the evidence shows that the temporary-replacement provision does not favor local interests. In the end, therefore, this case does not involve the "type of differential tax treatment of interstate and intrastate commerce that the Court has found in other 'discrimination' cases." *Commonwealth Edison*, 453 U.S. at 618.

Furthermore, even if the temporary-replacement provision could conceivably have an effect under some set of circumstances, it has not yet impacted interstate commerce at all. Particularly when, as here, the tax was enacted years ago, the plaintiff must present evidence that discrimination is happening *now*, not that discrimination might arise some day in the future. "Courts examining a 'practical effect' challenge must be reluctant to invalidate a state statutory scheme . . . simply because it *might* turn out down the road to be at odds with our constitutional prohibition against state laws that discriminate against Interstate Commerce." *Black Star*, 600 F.3d at 1232 (emphasis in original); *see also Gen. Motors Corp. v. Tracy*, 519 U.S. 278, 311 (1997) ("[W]e have never deemed a *hypothetical possibility* of favoritism to constitute discrimination that transgresses constitutional commands . . . .") (emphasis added; citation omitted).

3. Saban's argument about the allegedly large portion of out-of-state car renters is waived and is legally irrelevant.

The limited evidence Saban does cite (at 116-17) relates to its argument premised on the allegedly large portion of rental cars rented to out-of-state customers. But the superior court held that Saban had waived that argument by raising it too late, and Saban does not challenge on appeal the superior court's waiver ruling. The Court may thus summarily affirm the waiver ruling, and in any event the superior court correctly held that the argument is not supported by law.

(a) Saban waived its discriminatory-effect argument based on the portion of out-of-state renters.

The superior court held that "§ 5-839 does not violate the dormant Commerce Clause of the United States Constitution." [IR-254, ¶ 2.] The superior court gave two bases for that holding, as it relates to the overall share of out-of-state versus in-state renters.

First, the superior court held that Saban waived the argument by raising it too late:

> Perhaps recognizing the lack of discriminatory effect created by the surcharge, Plaintiffs belatedly raise a challenge to the tax on car rentals as a whole: because most car renters are from out of state, a tax on rental cars is discriminatory even without the differential rate for replacement cars. This would raise an

> entirely new issue requiring litigation from scratch. *The Court does not believe it is appropriate at this late date.*

[IR-161 at 5 (APP132) (emphasis added).] Second, the superior court held that "the Court [does not] find persuasive support for such an argument in relevant case law." [*Id.*]

Saban challenges the second basis on appeal, but does not challenge the superior court's alternative holding on waiver. The waiver ruling is, therefore, a "sufficient bas[i]s for the trial court's ruling," and therefore the Court should not entertain the merits of Saban's waived argument. *See A.D.R. Dev. Co. v. Greater Ariz. Sav. & Loan Ass'n*, 15 Ariz. App. 266, 267-68 (1971) (deeming it unnecessary to address a question raised on appeal because there were "other sufficient bases for the trial court's ruling" not challenged on appeal).

(b) Even if out-of-staters rent more cars than in-staters, that effect does not render the AzSTA tax unconstitutional.

The superior court correctly concluded that Saban's argument concerning the overall portion of out-of-state renters has no basis in law. [IR-161 at 5 (APP132) ("Nor does the Court find persuasive support for such an argument in relevant case law.").] As explained at the outset in

Argument § I.C, Saban's alternative theory—the core of its argument on appeal—is fundamentally flawed. A State may, as a matter of law, tax a product even if out-of-state customers purchase the lion's share of the product. *See Commonwealth Edison*, 453 U.S. at 618 (a tax does not violate the Commerce Clause merely because "the tax burden is borne primarily by out-of-state consumers."). In other words, the "effect" Saban points to is, as a matter of law, insufficient to justify subjecting the AzSTA tax to strict scrutiny. Thus the merits of Saban's waived argument do not help its case.

D. Ruling in Saban's favor would imply that taxes around the country are unconstitutional, contrary to settled law.

Common sense also shows why courts have universally rejected Saban's dormant Commerce Clause theory: it implies that no jurisdiction may impose a tax if tourists will pay the majority of the tax. That proposition has no support in law, and, if accepted, would have sweeping and disastrous effects for Arizona, and it would send shockwaves across the country.

Consider a simple example. Almost all transactions in Keystone, South Dakota involve tourists—its population is 337 people, but it's home

to Mount Rushmore, with more than 2 million visitors per year. That does not prohibit Keystone from imposing all sorts of taxes, so long as the 337 Keystone residents pay an equal tax rate as the millions of visitors.

Indeed, many jurisdictions have explicitly adopted a "tourism tax"—*and even called it that*. For example:

- Arkansas "levie[s] a *tourism tax*" on hotel rooms, campgrounds, various water sports activities, and "tourist attraction[s]." Ark. Code § 26-63-402.
- Maryland collects a "*tourism tax*" "on the retail sale of tourist-oriented goods and services." Md. Code, Econ. Dev. § 4-216.
- Tennessee collects a "*Tourist Accommodation Tax*" on the privilege of occupancy in a hotel. Tenn. Code title 7, ch. 4.
- Florida authorizes counties to establish "a *tourist impact tax*" for the privilege of renting hotel rooms. Fla. Stat. § 125.0108.
- Mississippi sends 80% of sales tax revenue "from the operation of a tourism project" to "the *Tourism Project Sales Tax* Incentive Fund." Miss. Code. § 27-65-75(2).
- Missouri authorizes lakefront counties to establish a "*tourism tax*" on hotel rooms, campgrounds, and houseboats. Mo. Rev. Stat. § 67.665(1). Missouri also authorizes certain other counties and cities to establish a "Convention and *Tourism Tax*." *Id.* § 66.390(1); *accord id.* § 92.327.
- New Jersey authorizes certain municipalities to "levy taxes upon predominantly *tourism related retail receipts*." N.J. Stat. § 40:54D-4(a).
- Illinois imposes a tax on the business of renting hotel rooms. 35 Ill. Comp. Stat. 145/3. Proceeds are paid in part to a fund

known as the "Local Tourism Fund," *id.* § 145/6. Another statute refers to the "Illinois *tourism tax* fund." 65 Ill. Comp. Stat. 5/8-3-13.

- Utah authorizes counties to establish taxes on hotel rooms and rental cars, and a "*tourism tax* advisory board" advises the county on how to spend the revenues. Utah Code § 17-31-8.

(Emphases added.)

It is thus widely recognized that state and local governments may take advantage of their natural and other resources (including those connected to tourism). As a result, just like Montana may tax coal even though non-Montanans paid 90% of the coal tax, governments may tax tourism-related goods and services even if out-of-staters pay the lion's share of those taxes.

To hold otherwise would cause a monumental and unjustified shift in the law. It would mean that rental car taxes nationwide are unconstitutional, even though the vast majority of States and many local jurisdictions impose a tax on car rentals. *See, e.g.*, Allison Hiltz, *Rental Car Taxes*, National Conference of State Legislatures (Mar. 18, 2015), http://www.ncsl.org/research/fiscal-policy/rental-car-taxes.aspx.

Indeed, Arizona has had a transaction privilege tax on those engaged in the

business of "automobile rental services" since 1935. (*See* Department's OB at 36.)

In enacting a tax with a temporary-replacement provision, the Arizona Legislature followed the lead of several other jurisdictions that already had similar provisions. *See, e.g.*:

- Haw. Rev. Stat. § 251-2(a) (exemption for a "vehicle to replace a vehicle of the lessee that is being repaired");
- Ind. Code § 6-6-9.5-8(b)(4) (exemption to county tax for a vehicle "provided to a person as a replacement vehicle");
- La. Stat. § 47:551(A) ("[N]or shall the tax apply to any individual or business who rents a vehicle as a replacement vehicle while his vehicle is being repaired . . . .");
- Utah Code § 59-12-603 (county tax does not apply to rentals "made for the purpose of temporarily replacing a person's motor vehicle that is being repaired");
- Wis. Stat. § 77.995 (exemption "for rental as a service or repair replacement vehicle").

Several more jurisdictions followed. *See, e.g.*:

- Nev. Rev. Stat. § 244A.810(2) (county tax "must not apply to replacement vehicles");
- N.M. Stat. § 7-14A-3.1 (tax "shall not apply to the lease of a temporary replacement vehicle");
- Tenn. Code § 67-4-1908 (metropolitan tax "shall not apply to any automobile rented as a replacement vehicle . . . while the renter's vehicle is being repaired").

Tellingly, although taxes like the one challenged here are common, Saban has identified no case striking down any such tax based on the dormant Commerce Clause.

In light of the longstanding nationwide practice of taxing rental cars (over eighty years in Arizona), to the extent any reform should occur in this area, it should be done legislatively, not by an Arizona appellate court. Indeed, in the past decade, four bills have been introduced in Congress to *limit* (not prohibit) state and local taxes on rental cars. *See* End Discriminatory State Taxes for Automobile Renters Act of 2015, H.R. 1528, 114th Cong. (2015); H.R. 2543, 113th Cong. (2013); H.R. 2469, 112th Cong. (2011); H.R. 4175, 111th Cong. (2009). So far, however, Congress is content with permitting States to tax rental cars without limits. In light of that, it would be an extraordinary exercise of judicial activism for this Court to now preclude Arizona from taxing rental cars. *Cf. Commonwealth Edison*, 453 U.S. at 637 (White, J., concurring) ("Congress has the power to protect interstate commerce from intolerable or even undesirable burdens. . . . Yet, Congress is so far content to let the matter rest . . . ."); *see also id.* at 628 n.18 (majority Op.) (citing failed federal legislation).

The details of these bills also show why judicial intervention makes no sense. For example, the 2015 failed bill defined 14 different terms, determined a threshold for comparing rental car taxes to other taxes, and selected the other taxes to use for comparison. The bill proposed a cap on rental car taxes based in part on the tax rate charged on "more than 51 percent of the rentals of other tangible personal property" in the jurisdiction. H.R. 1528, 114th Cong., § 3(a) (proposed 49 U.S.C. § 80505(a)(5)(A)). Because that cap is a policy choice, not a constitutional limit, it is not one courts should be making. Indeed, Saban's theory would not even permit a court to distinguish between a tax with a low rate and a tax with a high rate (or one with a temporary-replacement provision from one without that provision).

The Supreme Court expressly "decline[d]" "to prescribe a test for the validity of state taxes that would require state and federal courts, as a matter of federal constitutional law, to calculate acceptable rates or levels of taxation of activities that are conceded to be legitimate subjects of taxation." *Commonwealth Edison*, 453 U.S. at 628. It explained that "it is doubtful whether any legal test could adequately reflect the numerous and competing economic, geographic, demographic, social, and political

considerations that must inform a decision about an acceptable rate or level of state taxation, and yet be reasonably capable of application in a wide variety of individual cases." *Id.* These concerns apply with full force here, where courts would be ill-suited to determine arbitrary thresholds and comparable taxes for comparison.[6]

E. In light of the above, the Court may not subject the AzSTA tax to strict scrutiny and Saban provides no other basis for striking it down.

For all of these reasons, there is no basis for subjecting the AzSTA tax to strict scrutiny. Moreover, Saban does not identify any basis for reversing the Commerce Clause ruling if the Court does not apply strict scrutiny. Although in a footnote (Saban's Cross-OB at 79 n.38) Saban references another balancing test, *Pike v. Bruce Church, Inc.*, 397 U.S. 137,

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[6] If the temporary-replacement provision had been implemented and the Court found it problematic, the appropriate remedy would be to sever that provision, § 5-839(B)(2). An express severability clause applies to § 5-839. *See* 2002 Ariz. Sess. Laws 1257, 1303, ch. 288, § 60 ("[T]he provisions of this act are severable"). The provision would also be severable under common-law principles because (1) "the valid parts of [the] statute are effective and enforceable standing alone" (and indeed operate standing alone) and (2) the valid portions would have been enacted without the invalid portions (after all, the temporary-replacement provision has never been implemented, the AzSTA tax is working as intended, and no one is calling for repeal). *State Comp. Fund v. Symington*, 174 Ariz. 188, 195 (1993) (quotation marks and citation omitted).

142 (1970), it recognizes that *Complete Auto*, 430 U.S. at 279, typically applies in tax cases. Moreover, Saban does not dispute that the AzSTA tax passes the *Pike* test and the other three factors of *Complete Auto*. Accordingly, the Court should affirm the superior court's ruling on the Commerce Clause.

CONCLUSION

The superior court correctly found that the AzSTA tax "is not protectionist in nature," and does not violate the dormant Commerce Clause. [*See* IR-161 at 4-5 (APP131-132).] The Court should affirm that ruling.

RESPECTFULLY SUBMITTED this 15th day of September, 2017.

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