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# Federal Recent Developments

# FEDERAL RECENT DEVELOPMENTS

## UNITED STATES SUPREME COURT

TAXATION: State Tax Regulation of Cigarettes Sold on Reservations

*Department of Taxation & Fin. v. Milhelm Attea & Bros., Inc.*, 114 S. Ct. 2028 (1994)

Milhelm Attea & Brothers, Inc. (the Wholesalers) brought suit against the Department of Taxation and Finance of the State of New York (the Department). The Wholesalers sought to enjoin a regulatory scheme which required cigarette wholesalers to keep records of transactions[1] and which limited quantities of cigarettes sold to tax-exempt Indian retailers.[2] The Wholesalers claimed that the regulatory scheme was preempted by the federal Indian Trader Statutes.[3]

The United States Supreme Court held that "Indian traders are not wholly immune from state regulation that is reasonably necessary to the assessment or collection of lawful state taxes."[4] The Court further held that New York's regulatory scheme was not, on its face, unduly burdensome.[5]

The State of New York lacks authority to tax cigarettes sold on reservations to enrolled tribal members for their own consumption.[6] The State is entitled, however, to tax reservation cigarette sales to consumers who are not tribal members.[7] To insure that nonmember consumers did not escape the

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1. N.Y. COMP. CODES R. & REGS. tit. 20, § 336.6(g)(3-4) (1992).

2. *Id.* § 336.7.

3. 25 U.S.C. §§ 261-264 (1988). Section 261 provides:

> The Commissioner of Indian Affairs shall have the sole power and authority to appoint traders to the Indian tribes and to make such rules and regulations as he may deem just and proper specifying the kind and quantity of goods and the prices at which such goods shall be sold to the Indians.

*Id.* § 261. The *Milhelm Attea* Court explained in a footnote:

> [O]ther Indian Trader provisions state that persons who establish their fitness to trade with Indians to the BIA's satisfaction shall be permitted to do so, 25 U.S.C. § 262, authorize the President to prohibit the introduction of goods into Indian country and to revoke licenses, § 263, and impose penalties for unauthorized trading, § 264. BIA regulations under the statutes are codified at 25 C.F.R. §§ 140.1-140.26 (1993).

*Milhelm Attea*, 114 S. Ct. at 2034 n.7.

4. *Milhelm Attea*, 114 S. Ct. at 2036.

5. *Id.* at 2037.

6. *Id.* at 2031 (citing Moe v. Confederated Salish & Kootenai Tribes of Flathead Reservations, 425 U.S. 463, 475-81 (1976)).

7. *Milhelm Attea*, 114 S. Ct. at 2031 (citing Washington v. Confederated Tribes of Colville

state tax, the Department adopted a state tax regulation scheme which limited the quantity of untaxed cigarettes that wholesalers could sell to tax-exempt Indian retailers.[8]

The Department developed quotas for authorized sales which were calculated to parallel the "probable demand" of tax-exempt Indian consumers.[9] Sales quotas were to be based on data submitted from the tribe, or on per capita cigarette consumption rates of New York State residents.[10] Wholesalers who sold quantities beyond the quota were to assess the tribe or tribal retailer for the state tax.[11]

The Department's other regulations placed additional record-keeping burdens on the wholesalers. Under the regulations, wholesalers are required to obtain the Department's approval before selling untaxed cigarettes.[12] Further, wholesalers who planned to sell tax-exempt cigarettes to Indian tribes or reservation retailers bore the responsibility of ensuring that: (1) the buyer intends to distribute the cigarettes to tax-exempt consumers;[13] (2) the buyer takes delivery on the reservation;[14] and (3) the buyer holds a valid state tax exemption certificate.[15]

The United States Supreme Court observed that the Wholesaler's claim constituted a facial attack on the Department's regulations.[16] The Wholesalers challenged the Department's authority to impose the regulations, but the Wholesalers did not challenge specific features of the regulations themselves.[17] This conclusion led the Court to limit its review of the case in two ways: First, the Supreme Court proceeded with the assumption that the Department's quota on untaxed cigarettes would allow quantities of untaxed cigarettes sufficient to meet the legitimate consumption needs of Indians on the reservation.[18] Second, the Court declined to assess all features of the regulations and their impact on tribal sovereignty. Rather, the Court limited

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Reservation, 447 U.S. 134 (1980)).

8. The Department alleged that the volume of tax-exempt cigarettes sold on New York Indian reservations in 1987-88, if consumed exclusively by tax-exempt Indians, would represent a consumption rate 20 times that of average New York residents. The State estimated lost revenue of up to $65 million per year. *Id.* at 2031 (citing Record at 244-46, *Milhelm Attea* (No. 93-377) (affidavit of Jamie Woodward)).

9. N.Y. COMP. CODES R. & REGS. tit. 20, § 336.7(d)(i) (1992).

10. *Id.* §§ 336.7(d)(1), (d)(2)(ii).

11. *Id.* §§ 336.7(b)(2), (e).

12. *Milhelm Attea*, 114 S. Ct. at 2032.

13. N.Y. COMP. CODES R. & REGS. tit. 20, §§ 336.6(d)(1), 336.6(f)(1), 336.7(f)(1) (1992).

14. *Id.*

15. *Id.*

16. *Milhelm Attea*, 114 S. Ct. at 2033.

17. *Id.*

18. *Id.* at 2033.

its decision to whether the regulations conflicted with the Indian Trader Statutes.[19]

The *Milhelm Attea* Court explained that the Indian Trader Statutes were enacted with the purpose of preventing fraudulent behavior on the part of persons trading with Indians.[20] In a 1965 decision, *Warren Trading Post Co. v. Arizona Tax Commission*, the Supreme Court specified that federal legislation controlled Indian trading to the extent that all state regulation of Indian traders was invalid.[21]

The Supreme Court recognized that many of its decisions following *Warren Trading Post* had upheld state regulations and, in so doing, had "undermined" much of the *Warren Trading Post* principle.[22] The Court specifically referred to *Moe v. Salish & Kootenai Tribes of Flathead Reservations*,[23] *Washington v. Confederated Tribes of Colville Reservation*,[24] and *Oklahoma Tax Commission v. Citizen Band of Potawatomi Tribe*.[25]

In *Moe*, *Colville*, and *Citizen Band* the Supreme Court recognized the states' valid interest in ensuring compliance with lawful taxation. The Court distinguished between laws involved direct taxation of Indian traders for trade with Indians, and those which enforced lawful taxation of non-Indians.[26]

The Supreme Court concluded that, after balancing state, federal, and tribal interests, state regulation may be justified when the legislation protects legitimate state interest in taxation of non-Indians. The Court will inquire whether the burden placed on reservation retailers is minimal and appropriately tailored to the legitimate state interest in enforcing taxation of non-Indians.[27]

The *Milhelm Attea* Court noted that tax enforcement schemes were upheld in *Moe* and *Colville*, even though the schemes impacted reservation retailers directly. Consequently, the Court found it reasonable to impose similar schemes on non-Indian wholesalers: "It would be anomalous to hold that a

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19. *Id.* at 2033-34.

20. *Id.* at 2034.

21. Warren Trading Post Co. v. Arizona Tax Comm'n, 380 U.S. 685, 690 (1965) ("Congress has taken the business of Indian trading on reservations so fully in hand that no room remains for state laws imposing additional burdens upon traders.").

22. *Milhelm Attea*, 114 S. Ct. at 2034.

23. 425 U.S. 463, 483 (1976) (upholding Montana law requiring Indian tribal sellers to collect a cigarette tax validly imposed on non-Indians), *cited in Milhelm Attea*, 114 S. Ct. at 2034.

24. 447 U.S. 134, 155 (1980) (upholding Washington State cigarette tax regulatory scheme and rejecting argument that tribes could use tax exemption to create market from consumers who would normally do business elsewhere), *cited in Milhelm Attea*, 114 S. Ct. at 2034-35.

25. 498 U.S. 505, 514 (1991) (holding that the doctrine of sovereign immunity bars the State of Oklahoma from suing Tribes to recover cigarette taxes owed for transactions between tribal-owned smoke shop and non-Indians, but permitting Oklahoma to collect from wholesalers), *cited in Milhelm Attea*, 114 S. Ct. at 2035.

26. *Milhelm Attea*, 114 S. Ct. at 2035.

27. *Id.* at 2035-36.

State could impose tax collection and bookkeeping burdens on reservation retailers who are themselves enrolled tribal members, including stores operated by the tribes themselves, but that similar burdens could not be imposed on wholesalers, who often (as in this case) are not."[28]

Finally, the Supreme Court addressed the issue of whether the policy requiring reservation retailers to obtain tax-exempt certificates from the State invades the Bureau of Indian Affair's sole power to appoint Indian traders.[29] The Court found that the regulation did not vest authority to trade with Indians; it merely served to identify entities who were already selling cigarettes. Therefore, the regulation did not infringe upon the Bureau's power.[30]

DIMINISHMENT OF RESERVATION LAND: Effect of Opening Reservations to Non-Indian Settlement

*Hagen v. Utah*, 114 S. Ct. 958 (1994)

The issue before the Supreme Court in *Hagen* was whether the Uintah Indian Reservation had been diminished by Congress when the reservation was opened to non-Indian settlement in 1905. Hagen, an Indian, was charged with illegal possession of a controlled substance in Myton, Utah. Because Myton was within the original boundaries of the Uintah Indian Reservation, Hagen argued that the alleged offense occurred in "Indian country."[31] According to Hagen, the Utah state court, then, was without criminal jurisdiction.[32]

The trial court denied Hagen's motion. However, the state appellate court reversed, holding that Myton is in Indian country and, therefore, Utah's courts do not have jurisdiction.[33] The state appellate court based its conclusions on a Tenth Circuit decision which found that the Uintah Indian Reservation had not been diminished in 1905, when the land was opened to non-Indian settlement.[34] Ultimately, the state supreme court reversed, holding that the Uintah Reservation had been diminished by the 1905 opening of the reservation. The Utah Supreme Court found that the town of Myton is located outside of the reservation's boundaries, and Hagen was thus subject to the State's criminal jurisdiction for acts committed in Myton.[35] Hagen then

28. *Id.* at 2036.
29. *Id.* at 2037.
30. *Id.*
31. *See* 18 U.S.C. §.1151 (1994).
32. Hagen v. Utah, 114 S. Ct. 958, 964 (1994).
33. *Id.*
34. Hagen v. Utah, 802 P.2d 745 (Utah Ct. App. 1990) (relying on Ute Indian Tribe v. Utah, 773 F.2d 1087 (6th Cir. 1985) (en banc), *cert. denied*, 479 U.S. 994 (1986)).
35. Hagen v. Utah, 858 P.2d 925 (Utah 1992).

appealed his case to the United States Supreme Court, which granted certiorari to "resolve the direct conflict bewteen . . . the Tenth Circuit and the Utah Supreme Court on the question of whether the Uintah Reservation had been diminished.[36]

The *Hagen* Court found that under the General Allotment Act the President of the United States was authorized to divide communally owned tribal lands into individually owned parcels.[37] Land not conveyed to individual Indians — surplus land — was then available for sale to non-Indians.[38] Statutes which authorized the sale of surplus Indian lands to non-Indians, however, did not automatically diminish the reservation proper. The Supreme Court has held that some surplus land acts diminished reservations, while other surplus land acts did not.[39] To determine the effect of a particular act, a court must look to the language of the statute in question, as well as to the circumstances underlying the act's passage.[40]

The United States Supreme Court structured its *Hagen* analysis under two significant presumptions. First, that ambiguities are to be interpreted in favor of Indians, and second, that the diminishment of Indian reservations is an extreme measure, not to be taken lightly.[41] The United States Supreme Court then articulated three factors to consider in the determination of whether a reservation has been diminished through a surplus land act.[42]

The critical factor to be considered is the specific language of the act itself.[43] The second factor requires a review of the historical text surrounding the surplus land act.[44] Finally, the analysis should consider the characteristics of the people who populate the opened reservation lands.[45]

In *Hagen*, the United States Supreme Court reviewed legislation and proposed legislation from as early as 1894. The Court found that in 1894 and 1898 Congress directed the President to facilitate allotment of the Uintah's reservation lands.[46] These allotment efforts were ineffective, as was a 1902 land act pertaining to the Uintahs. The 1902 Act[47] authorized allotment of the Uintah's land, but only upon approval of the adult male members of the

36. *Hagen*, 114 S. Ct. at 964.
37. Act of Feb. 8, 1887, ch. 119, 24 Stat. 388.
38. *Hagen*, 114 S. Ct. at 961 (citing DeCoteau v. District County Court, 420 U.S. 425, 432 (1975)).
39. Solem v. Bartlet, 465 U.S. 463, 469 (1984).
40. *Id.* The relevant statute is Act of May 27, 1902, ch. 888, 32 Stat. 263.
41. *Hagen*, 114 S. Ct. at 965.
42. *Id.*
43. *Id.*
44. *Id.*
45. *Id.*
46. *Hagen*, 114 S. Ct. at 961.
47. Act of May 27, 1902, ch. 888, 32 Stat. 263.

Uintah tribe.[48] The 1902 Act directed that lands not allotted by a specific point in time were to be "restored to the public domain."[49]

The adult male members of the Uintah tribe never consented to allotment of their land as provided in the 1902 Act. However, in 1903, the Supreme Court decided *Lonewolf v. Hitchcock*,[50] which provided a mechanism by which reservation boundaries could be altered unilaterally by Congress.[51] Within months of the decision, Congress ordered the Uintah lands to be allotted unilaterally if the tribe did not consent to the allotments by June 1 of that year.[52] Congress specified that unallotted lands would be opened to non-Indians, as specified in the 1902 Act. A subsequent 1904 Act set aside funds to be used in implementing the purposes of the 1902 Act.[53]

Finally, in 1905, President Theodore Roosevelt issued a proclamation which directed that the unallotted lands in what had been the Uintah reservation were to be "restored to public domain." The proclamation ordered that the lands were to be opened to settlement under general homestead and townsite laws.[54]

The statutory references to the 1902 Act were significant to the Court's analysis in *Hagen*. The Court's decision would depend in part on whether the 1905 Act, which successfully resulted in the allotment of the Uintah lands, repealed the Act of 1902 by implication, or whether the provisions of the 1902 Act were incorporated into the 1905 Act. The 1902 Act referred to the public domain, whereas the 1905 Act did not: if the Court accepted that the text of the 1905 Act, without reference to the public domain, was not based on the Act of 1902, the statutory language at issue would be much less clear.

Hagen argued that the Act of March 3, 1905[55] repealed or at least superseded some parts of the 1902 Act, specifically the "restore to the public domain" language.[56] The Supreme Court disagreed with Hagen and stated that the intent of the 1902 Act to diminish the reservation survived the passage of the 1905 Act.[57] The Court pointed out that congressional action subsequent to the 1902 Act referred to the 1902 statute.[58] The 1905 Act was

48. *Id.*
49. *Id.*
50. 187 U.S. 553 (1903).
51. *Id.* at 567-68.
52. Act of Mar. 3, 1903, ch. 994, 32 Stat. 998.
53. Act of Apr. 21, 1904, ch. 1402, 33 Stat. 207.
54. Proclamation of July 14, 1905, 34 Stat. 3119, 3119-20.
55. Act of Mar. 3, 1905, ch. 1479, 33 Stat. 1069. The Act of 1905 deferred the opening time of surplus reservation lands as specified in the 1902 Act.
56. *Hagen*, 114 S. Ct. at 967.
57. *Id.*
58. *Id.*

also tied to the 1902 Act because the former dealt with the proceeds of the sale of the unallotted lands as provided for in the latter.[59]

Furthermore, in reviewing the historical evidence, the Supreme Court found clear evidence that the 1905 Act did not repeal the 1902 Act.[60] The Supreme Court relied on President Roosevelt's proclamation, in which he explained that the 1902 Act restored the unallotted lands to the public domain and that the subsequent acts including the 1905 Act extended the time for the opening of the lands.[61]

The phrase "public domain" was also central to the Supreme Court's analysis. The *Hagen* Court cited statutes enacted around the time of the 1902 Act as evidence that Congress considered Indian reservations as separate from the public domain.[62] Therefore, the Supreme Court in *Hagen* held that any unallotted reservation lands restored to the public domain "evidences a congressional intent with respect to those lands inconsistent with the continuation of reservation status."[63] In the view of the United States Supreme Court, Congress intended that the 1902 Land Act would diminish the Uintah Reservation.[64]

In continuing its analysis, the Supreme Court noted that the Uintah Valley was populated predominately by non-Indians[65] and concluded that a finding that the land in question was within Indian country would seriously burden the administration of state and local government.[66] Moreover, the Supreme Court found it significant that, since the time the reservation was first opened to non-Indian settlement, the State of Utah has exercised jurisdiction over the opened parts of the Uintah Valley.[67] The Supreme Court held that demographics, combined with the State's long term exercise of jurisdiction, demonstrated a "practical acknowledgment" that the reservation was diminished.[68] Consequently, the State of Utah properly exercised criminal jurisdiction for acts allegedly committed in the town of Myton, located beyond the boundaries of Indian country.[69]

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59. *Id.* at 967-68.
60. *Id.* at 969.
61. *Id.* at 969-70.
62. *Id.* at 966.
63. *Id.* at 967.
64. *Id.*
65. *Id.* at 970.
66. *Id.* (citing Solem v. Bartlet, 465 U.S. 463, 471-72 n.12 (1984)).
67. *Id.*
68. *Id.*
69. *Id.* at 970-71.