No. ___

IN THE

Supreme Court of the United States

JAMES DAWSON AND ELAINE DAWSON,

Petitioners,

v.

DALE W. STEAGER, AS STATE TAX COMMISSIONER OF WEST VIRGINIA,

Respondent.

On Petition For Writ Of Certiorari To The Supreme Court Of Appeals Of West Virginia

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

In *Davis v. Michigan Department of Treasury*, 489 U.S. 803, 815-16 (1989), this Court held that a state may not impose a heavier tax burden on federal employees than state employees, unless the discriminatory treatment is "justified by significant differences between the two classes." Such tax discrimination—even against a "subcategory" of federal employees—violates the doctrine of intergovernmental tax immunity and 4 U.S.C. § 111. *See Jefferson Cty., Ala. v. Acker*, 527 U.S. 423 (1999).

James Dawson worked as a deputy U.S. Marshal before being presidentially appointed as the U.S. Marshal for the Southern District of West Virginia. Mr. Dawson was enrolled exclusively in the Federal Employee Retirement System ("FERS"). He sought a West Virginia tax exemption for all of his FERS retirement income, but that exemption was ultimately denied.

Under West Virginia Law, Mr. Dawson is entitled to exempt *a portion* of his FERS income from his state taxable income. *See* W. VA. CODE §§ 11-21-12(c)(5) and 11-21-12(c)(8). In contrast, West Virginia law allows state law enforcement retirees to *entirely exempt* from their taxable income *all benefits* received from four West Virginia retirement plans. *See id.* § 11-21-12(c)(6). Federal law enforcement retirees like Mr. Dawson are not entitled to full exemptions, although it is undisputed that Mr. Dawson's job duties were not significantly different from those of the exempted state law enforcement officers.

After *Davis*, three state courts of last resort struck down tax laws that discriminate against federal em-

ployees, but three state courts of last resort have upheld such laws based on an extremely narrow and strained reading of *Davis*, while many other state courts of last resort have inconsistently ruled on related laws.

The question presented is:

Whether this Court's precedent and the doctrine of intergovernmental tax immunity bar states from exempting groups of state retirees from state income tax while discriminating against similarly situated federal retirees based on the source of their retirement income.

PARTIES TO THE PROCEEDING

James Dawson and Elaine Dawson were the petitioners before the Circuit Court of Mercer County, West Virginia, and the respondents below. Dale W. Steager, as State Tax Commissioner of West Virginia, was the respondent before the Circuit Court of Mercer County, West Virginia, and the petitioner below.

No corporations are involved in this proceeding.

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Petitioners James Dawson and Elaine Dawson respectfully submit this petition for a writ of certiorari to the Supreme Court of Appeals of West Virginia.

OPINIONS BELOW

The Supreme Court of Appeals of West Virginia's opinion is unreported, but is available at 2017 WL 2172006, and is reproduced at Pet.App.1a. The Circuit Court of Mercer County, West Virginia's order reversing the decision of the West Virginia Office of Tax Appeals is unreported and is reproduced at Pet.App.17a.

JURISDICTION

The Supreme Court of Appeals of West Virginia entered judgment on October 19, 2016. On August 9, 2017, Chief Justice Roberts extended the time for filing this petition to and including September 9, 2017. *See* No. 17A159. On August 29, 2017, Chief Justice Roberts further extended the time for filing this petition to and including September 19, 2017. *Id.* This Court has jurisdiction under 28 U.S.C. § 1257(a).

STATUTORY PROVISION INVOLVED

4 U.S.C. § 111(a) states:

> The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States, a territory or possession or political subdivision thereof, the government of the District of Columbia, or an agency or instrumentality of one or more of the foregoing, by a duly constituted taxing authority having jurisdiction, if the taxation does not discriminate against the officer or employee

because of the source of the pay or compensation.

STATEMENT OF THE CASE

A. Factual Background

1. This case concerns West Virginia's differential taxation treatment of a federal law enforcement officer's retirement benefits from similarly situated state law enforcement officers, whose retirement benefits are fully exempted from taxation.

Respondent James Dawson is a former Nicholas County, West Virginia, Deputy Sheriff, Deputy U.S. Marshal, and U.S. Marshal who retired from the U.S. Marshals Service on March 31, 2008. Pet.App.4a. While employed by the U.S. Marshals Service, Mr. Dawson was enrolled in the Federal Employee Retirement System ("FERS"), and he now receives retirement benefits from FERS. *Id.*

Under West Virginia law, Mr. Dawson is entitled to exempt at least $2,000 of FERS income from his state taxable income. *See* W. VA. CODE § 11-21-12(c)(5). When he reaches age 65, he may exempt up to $8,000. *See id.* § 11-21-12(c)(8).

2. On the other hand, West Virginia law allows the state law enforcement recipients of four West Virginia law enforcement retirement plans to exempt from their taxable state income *all of the benefits received* from those plans, without limitation. *See id.* § 11-21-12(c)(6) ("Section 12(c)(6)"). The four retirement plans covered by Section 12(c)(6) are: (1) Municipal Police Officer and Firefighter Retirement System ("MPFRS"); (2) the Deputy Sheriff Retirement System ("DSRS"); (3) the State Police Death, Disability and Retirement Fund ("Trooper Plan A"); and (4) the

West Virginia State Police Retirement System ("Trooper Plan B").[1]

3. Consistent with the exemption offered to similarly situated state law enforcement officers, on or about October 24, 2013, Mr. Dawson and his wife Elaine filed amended tax returns claiming a full adjustment exempting Mr. Dawson's FERS retirement income from state income tax pursuant to Section 12(c)(6) for the years 2010 and 2011. Pet.App.4a.

B. The Proceedings Below

1. On November 19, 2013, the Dawsons received letters from the West Virginia State Tax Department (hereinafter "the Tax Department") denying the exemption. Pet.App.18a. On or about January 10, 2014, the Dawsons appealed the Tax Department's

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[1] West Virginia taxes the income of retired local and state employees received from the Public Employees Retirement System ("PERS") and the State Teachers Retirement System ("TRS"), as well as from federal or military retirement systems. W. VA. CODE § 11-21-12(c)(5). West Virginia law permits, however, the recipients of PERS, TRS, or a general federal retirement to exempt up to $2,000 of retirement benefits from their taxable income. *Id.* The recipients of military retirement benefits are permitted to exempt up to $20,000. W. VA. CODE § 11-21-12(c)(7)(B). In addition, any taxpayer age 65 or older may exempt up to $8,000 from their taxable income, regardless of their source of income. W. VA. CODE § 11-21-12(c)(8).

Certain deputy sheriffs in West Virginia are enrolled in PERS, rather than DSRS, and thus do not receive a tax exemption under Section 12(c)(6). When DSRS was created in 1998, deputy sheriffs at that time had the option to join DSRS or remain in PERS. All deputy sheriffs hired after the creation of DSRS are enrolled in that system, however, and thus receive the full tax exemption of Section 12(c)(6).

denial by submitting a timely Petition for Refund to the West Virginia Office of Tax Appeals (hereinafter "OTA"). Pet.App.4a. On August 7, 2015, OTA affirmed the Tax Commissioner's denial of the Dawson's Section 12(c)(6) exemption. *Id.* at 5a.

2. The Dawsons appealed to the Circuit Court of Mercer County, West Virginia. *Id.* In an order dated March 31, 2016, the circuit court reversed the decision of OTA, holding that the denial of an exemption to Dawson violated 4 U.S.C. § 111 and the doctrine of intergovernmental tax immunity, and was contrary to this Court's decision in *Davis v. Michigan Department of Treasury*, 489 U.S. 803 (1989). Pet.App.24a-25a. The court held that the Supreme Court of Appeals of West Virginia's previous decision in *Brown v. Mierke*, 443 S.E.2d 462 (W. Va. 1994), did not apply to this case. Pet.App.22a.

In *Davis*, this Court held that a Michigan statute that exempted from taxation all retirement benefits paid by the state or its political subdivisions, but levied an income tax on retirement benefits paid by all other employers, including the federal government, violated the doctrine of intergovernmental tax immunity and 4 U.S.C. § 111. 489 U.S. at 805. Under the doctrine of intergovernmental tax immunity, the imposition of a "heavier tax burden on those who deal with one sovereign than is imposed on those who deal with the other must be justified by significant differences between the two classes." *Id.* at 815-16. Finding no significant difference between state and federal employees that justified their unequal tax treatment, this Court held that the Michigan taxing scheme violated "principles of intergovernmental tax immunity by favoring retired state and local gov-

ernment employees over retired federal employees." *Id.* at 817.

In *Brown*, the Supreme Court of Appeals of West Virginia held that Section 12(c)(6)—the same statute at issue here—did not violate the doctrine of intergovernmental tax immunity. 443 S.E.2d at 464. The court reasoned that this Court's holding in *Davis* did not apply to Section 12(c)(6) because the blanket tax exemption in *Davis* was intended to "discriminate against federal retirees" in violation of the doctrine of intergovernmental tax immunity. *Id.* at 466. On the other hand, according to the court, Section 12(c)(6) applied to a narrow class of former state employees and was intended only to "to give a benefit" to that "narrow class." *Id.* at 466. Therefore, the *Brown* court held that "no calculated scheme or plan exists" in Section 12(c)(6) "to discriminate against retired military personnel based on the source of their income." *Id.* at 467. The court upheld Section 12(c)(6).

After reviewing this West Virginia and United States Supreme Court precedent, the circuit court below held that this Court's decision in *Davis*, and not the West Virginia Supreme Court's decision in *Brown*, controlled. Pet.App.21a-22a. Unlike in *Brown*, where the military retiree plaintiffs failed to demonstrate that their job descriptions correspond to the job descriptions of the exempted state employees, here it is "undisputed" that "there are no significant differences between Mr. Dawson's powers and duties as a US Marshal and the powers and duties of the state and local law enforcement officers listed in [Section 12(c)(6)]." Pet.App.22a. Because *Davis* establishes that "a state tax law violates intergovernmental tax immunity if it treats state and local gov-

ernment employees more favorably than similarly situated federal government retirees," the circuit court determined that *Davis* and not *Brown* controlled. Pet.App.21a (citing *Davis*, 489 U.S. at 815, 816).

Applying *Davis* and its progeny, the circuit court noted that the state's discriminatory purpose in enacting Section 12(c)(6) was clear and improper. In fact, during oral argument, the state justified its discriminatory treatment of federal law enforcement officers by admitting that the purpose of Section 12(c)(6) was to "benefit the narrow class of *state* law enforcement officers" listed in the statute. Pet.App.23a. Thus, the inconsistent tax treatment was "unquestionably based on the source of one's retirement income and precisely the type of favoritism the doctrine of intergovernmental tax immunity prohibits." *Id.* The circuit court held that the state's intentional discrimination against federal employees in favor of state employees ran afoul of *Davis* and violated the doctrine of intergovernmental tax immunity. *Id.* at 23a-25a.

3. The Tax Commissioner appealed the circuit court's decision to the Supreme Court of Appeals of West Virginia. *Id.* at 1a. The court below reversed the circuit court's decision, holding that the statute did not violate the doctrine of intergovernmental tax immunity.

In so holding, the court departed from the reasoning of the circuit court and did not apply *Davis* and its progeny. The court determined that *Davis* did not apply to this case because in the Michigan statute at issue there was a blanket tax exemption for all state employees. *Id.* at 13a. But here, Section 12(c)(6)

does not afford a "blanket exception" to all state retirees; rather, it confers the tax exemption on a limited class of state law enforcement retirees. Pet.App.13a. Thus, the narrow scope of the discriminatory Section 12(c)(6) caused the court below to disregard this Court's intergovernmental tax immunity precedent entirely.

Instead, the court below determined that its prior decision in *Brown* controlled because Section 12(c)(6) exempts only a narrow class of state retirees. *Id.* at 14a-15a. The court emphasized that only a narrow group of state employees received the exemption, and thus concluded that the "intent of the exemption contained in Section 12(c)(6) was to give a benefit to a narrow class of state retirees" and not to discriminate against federal employees based on the source of their income. *Id.* at 15a. Mimicking its reasoning in *Brown*, the court below examined the "totality of the circumstances" and determined that Mr. Dawson received more favorable tax treatment than various other groups of non-similar state retirees. *Id.* at 15a-16a. Therefore, it upheld Section 12(c)(6), concluding that it was not intended to discriminate against former federal marshals. *Id.* at 16a.

This petition for certiorari followed.

REASONS FOR GRANTING THE PETITION

Review is warranted for four reasons.

First, the decision below exacerbates an existing division among state courts of last resort regarding whether this Court's decisions in *Davis*, 489 U.S. at 803, and *Jefferson County*, 527 U.S. at 434, and the

doctrine of intergovernmental tax immunity[2] bar states from exempting groups of state retirees from taxation while discriminating against similarly-situated federal retirees based on the source of their income.

Following *Davis*, three state courts of last resort have held that such discriminatory exemptions violate the doctrine of intergovernmental tax immunity. Conversely, three state courts of last resort have held post-*Davis* that states may exempt groups of state retirees from taxation while taxing similarly situated federal retirees, reasoning that *Davis* applies only to prohibit a blanket tax exemption for all state retirees, not an exemption for a limited group of state retirees. Furthermore, other cases decided after *Davis* evidence that this Court's intervention is necessary to define the precise parameters and scope of *Davis*.

Second, the decision below is directly contrary to this Court's decisions in *Davis* and *Jefferson County*. In *Davis*, this Court held that whenever a state statute is alleged to violate the doctrine of intergovernmental tax immunity by favoring state employees over similarly situated federal employees, the discriminatory treatment "must be justified by significant differences between the two classes." 489 U.S. at 816. Nothing in *Davis* suggests that its holding is limited to blanket tax exemptions granted to all state

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[2] This Court has held in *Davis* that "the retention of immunity in [4 U.S.C.] § 111 is coextensive with the prohibition against discriminatory taxes embodied in the modern constitutional doctrine of intergovernmental tax immunity." 489 U.S. at 813. Therefore, this petition treats the statutory section and the intergovernmental tax immunity doctrine as coextensive.

employees. To the contrary, in *Jefferson County*, this Court clarified that discriminating against even "a subcategory" of federal employees violates intergovernmental tax immunity. 527 U.S. at 443. Yet the court below erroneously reasoned that because the West Virginia law at issue was not a "blanket exemption" granted to "*all* state retirees," this Court's precedent on intergovernmental tax immunity did not apply. Pet.App.10a. This reasoning was erroneous, and other state courts of last resort have adopted this flawed reasoning in upholding discriminatory tax statutes.

Third, this is a recurring and important issue that this Court should address. Unsettled questions about the proper form of state tax schemes post-*Davis* have resulted in a split of authority and an explosion of litigation in state courts challenging restructured state tax schemes. Lacking specific guidance, state courts have reached different conclusions, which has resulted in inconsistent and ever-changing tax and benefits schemes across states. This uncertainty affects millions of federal, state, and local retirees nationwide. Furthermore, allowing states to impose "narrow" tax exemptions for swaths of state employees while strapping federal employees with the state tax burden imposes new financial risks for the burgeoning federal retiree population. Under the flawed reasoning of the court below, all states could adopt discriminatory tax exemptions favoring *limited groups of state employees* while taxing similarly situated federal employees to avoid challenges under *Davis* and the intergovernmental tax immunity doctrine. The "narrow class" of beneficiaries argument essentially suggests that taxing systems imposing

just a "small" discrimination are not prohibited by *Davis*.

Finally, this case presents an ideal vehicle to resolve this issue. It is undisputed that there are no significant differences between the exempted state law enforcement officers and federal marshals like Mr. Dawson; therefore, the question presented only requires the resolution of a legal issue. Pet.App.22a. Furthermore, the Supreme Court of Appeals of West Virginia's erroneous reasoning below and in *Brown* has been adopted by two other state courts of last resort in decisions upholding state tax statutes that clearly violate the doctrine of intergovernmental tax immunity, as set forth in *Davis*. This Court's intervention is necessary to avoid further reliance on these erroneous decisions.

I. THE DECISION BELOW DEEPENS AND PERPETUATES A POST-*DAVIS* SPLIT OVER WHETHER STATES MAY EXEMPT THE RETIREMENT INCOME OF STATE RETIREES WHILE TAXING THE RETIREMENT INCOME OF SIMILARLY SITUATED FEDERAL RETIREES

The decision below exacerbates a split of authority that persists post-*Davis* regarding whether states may exempt groups of state retirees from state tax while taxing similarly situated federal retirees.

Davis held that state tax statutes that "favor[] retired state and local government employees over retired federal employees" violate the principles of intergovernmental tax immunity. 489 U.S. at 817. In the aftermath of *Davis*, three state courts of last resort faithfully applied this Court's reasoning and

struck down tax statutes that favored groups of state retirees over federal retirees. On the other hand, three state courts of last resort have held post-*Davis* that states may exempt limited groups of state retirees while taxing similarly situated federal retirees. Courts that have upheld such discriminatory tax treatment justify it on the basis that *Davis* dealt with a blanket tax exemption for all state retirees, not an exemption for a limited group of state retirees. Therefore, according to those courts, *Davis* does not apply, one need not examine the federal *source* of the compensation under consideration, and the West Virginia Supreme Court's decision in *Brown* is instead instructive.

A. Three State Courts of Last Resort Have Held Post-*Davis* That States Are Not Able to Exempt Groups of State Retirees From State Income Tax While Not Exempting Similarly Situated Federal Retirees

After this Court's decision in *Davis*, three state courts of last resort have correctly held that state tax laws exempting state retirees from tax while not exempting similarly situated federal retirees violate the intergovernmental tax immunity doctrine or 4 U.S.C. § 111.

1. **Arkansas.** In *Pledger v. Bosnick*, Arkansas residents who were federal retirees and retirees from other states' agencies filed a lawsuit contending that provisions of the Arkansas tax code violated the doctrine of intergovernmental tax immunity. 811 S.W.2d 286, 288 (Ark. 1991), *abrogated on other grounds by State, Dep't of Fin. & Admin. v. Staton*, 942 S.W.2d

804, 806 (Ark. 1996). Specifically, the plaintiffs argued that tax provisions that fully exempted retirement income received by retirees from the Arkansas Public Employees, Teachers, State Highway Police, and State Highway Employees Retirement Systems, while allowing only a $6,000 exemption for all other retirees, discriminated against the plaintiffs based on the source of their income. *Id.*

The Arkansas Supreme Court agreed. Citing *Davis*, the court explained that the key question at issue was whether "the tax levied by the State of Arkansas discriminate[d] against the taxpayers because of the *source* of the pay or compensation." *Id.* at 291. Under *Davis*, if the court found that the Arkansas tax scheme discriminated "against retirees from the federal government . . . when compared to the treatment given retirees from the State of Arkansas" it "must find that the tax is in violation of the Constitutional Doctrine of Intergovernmental Tax Immunity." *Id.* The court said nothing about *Davis* being applicable only to challenges of blanket tax exemptions for state employees.

The court held that the tax levied upon the compensation of the military retirees and retirees from other states was "discriminatory" when compared to the tax "levied upon the compensation of the Arkansas civil service retirees." *Id.* at 292. In other words, "the tax discriminate[d] based upon the source of the payment, since the source of one payment is the State of Arkansas and the source of the military pay is the federal government." *Id.* Thus, the court held that the Arkansas tax ran afoul of *Davis* and violated principles of intergovernmental tax immunity.

2. **Colorado.** In *Kuhn v. State Department of Revenue of State of Colorado*, military retirees challenged portions of a Colorado taxing scheme that exempted $2,000 of military retirement benefits for retirees under the age of 55, but exempted $20,000 of retirement benefits for state and private retirees under the age of 55. 817 P.2d 101, 103 (Colo. 1991) (en banc) (citing Colo. Rev. Stat. §§ 39-22-104(4)(g), 39-22-104(4)(f)). The plaintiffs alleged that the taxing scheme violated 4 U.S.C. § 111 and the principles of intergovernmental tax immunity. *Id.* at 104. The State argued that the taxing scheme "did not discriminate based on the source of the income" and even if it did, "it was justified by significant differences between military retirement pay and other classes of retirement benefits." *Id.* at 106.

Relying on *Davis*, the Supreme Court of Colorado agreed with the plaintiffs, holding that the taxing scheme "did discriminate between taxpayers based on the source of their income." *Id.* at 108. The court explained that *Davis* "prohibit[s]" taxes "that discriminate between state and federal workers based on the source of the income" unless the inconsistent treatment is justified by significant differences between the classes. *Id.* at 107 (citing *Davis*, 489 U.S. at 816). The court said nothing to indicate that the holding in *Davis* is limited to blanket tax exemptions.

The court rejected the State's argument that discriminatory treatment was justified by the higher benefits received by retired military members than state retirees. *Id.* Indeed, the court stated that the financial argument was foreclosed by *Davis*, which "rejected" the "assertion that the fact that state re-

tirement benefits were 'less munificent' than federal benefits was a significant difference" that justified the disparate tax treatment. *Id.* at 109. Therefore, the court concluded that the state failed to show significant differences that justified the discriminatory tax scheme, and the tax scheme violated intergovernmental tax immunity and 4 U.S.C. § 111. *Id.*

3. **Missouri.** In *Hackman v. Director of Revenue*, taxpayers who had paid state income tax on federal military retirement benefits filed claims for a refund after this Court's decision in *Davis*. 771 S.W.2d 77, 79 (Mo. 1989). Missouri's taxation scheme allowed state retirees to exempt their retirement income from state income tax while not providing the same exemption to federal retirees. *Id.* Unlike the blanket tax exemption at issue in *Davis*, the Missouri taxing scheme provided narrow income tax exemptions throughout the tax code in the specific statutes that create the state's myriad retirement systems. *Id.* at 80. Nonetheless, the court reasoned that "the effect of Missouri's scattered retirement benefit exemption statutes is identical to that of Michigan's exemption statute for purposes of a *Davis* analysis." *Id.* In other words, although Missouri's tax code included several narrow statutory exemptions for subgroups of state employees—and not one large blanket exemption—*Davis* still controlled.

Citing *Davis*, the court determined (and the state conceded) that its taxing scheme violated "principles of intergovernmental tax immunity by favoring retired state and local government employees over retired federal employees." *Id.* (citing *Davis*, 489 U.S. at 817). The court struck down the taxing scheme.

B. Three State Courts of Last Resort Have Held Post-*Davis* That States Are Able to Exempt Groups of State Retirees From State Income Tax While Not Exempting Similarly Situated Federal Retirees

After this Court's decision in *Davis*, three state courts of last resort have erroneously held that state tax laws exempting groups of state retirees from state income tax while taxing similarly situated federal retirees did not violate the intergovernmental tax immunity doctrine or 4 U.S.C. § 111. To arrive at this conclusion, each of these courts has cited the West Virginia Supreme Court's *Brown* decision, which held that *Davis* does not control where states exempt a limited class of state employees from taxation, as opposed to providing a blanket tax exemption for all state employees.

1. a. **West Virginia**. In *Brown v. Mierke*, federal military retirees brought an action challenging Section 12(c)(6) (the same statute challenged by the Dawsons here), which provides for a modification reducing federal adjusted gross income for state income tax purposes by the entire amount a taxpayer receives from "pensions and annuities . . . under any West Virginia police, West Virginia firemen's retirement system or the West Virginia Department of Public Safety Death, Disability and Retirement Fund." 443 S.E.2d 462, 463 (W. Va. 1994). Federal tax law includes military pensions in adjusted gross income ("AGI"), and federal AGI constitutes AGI for the purposes of the West Virginia personal income tax, subject to certain exemptions. *Id.* Therefore, because they are counted in federal AGI, military pensions are likewise included in West Virginia AGI

and thus West Virginia personal income tax is imposed on military retirement pay. *Id.*

A disparity exists, however, between the tax exemptions provided to military retirees on one hand and West Virginia state retirees on the other. Subject to certain limited exclusions, military retirees are required to report their retirements as income on their tax returns. *Id.* By contrast, Section 12(c)(6) allows state retirees to exempt *all amounts* received from the West Virginia police, West Virginia firemen's retirement system or the West Virginia Department of Public Safety Death, Disability and Retirement Fund. W. VA. CODE § 11-21-12(c)(6). Because of this disparity, retired military personnel filed an action seeking to establish whether the West Virginia tax scheme violated 4 U.S.C. § 111 and the doctrine of intergovernmental tax immunity.

The Supreme Court of Appeals of West Virginia upheld the taxing scheme. Without legal support, the court explained that *Davis* did not control its analysis. Instead, because the "intent" of the West Virginia tax scheme was to "give a benefit to a very narrow class of former state and local employees" and not to "discriminate *against* federal retirees," the court held that *Davis* did not apply. *Brown*, 443 S.E.2d at 466. While acknowledging that focusing on who benefits from the exemption instead of who it excludes may "at first appear to be a distinction without a difference," the court relied on three facts to conclude that West Virginia did not intend to discriminate against retired military personnel. *Id.* *First*, the retired military personnel were treated more favorably than West Virginians who had retired from civilian occupations because they were allowed

some tax exemption of their retirement benefits. *Id.* at 467. *Second*, retired military personnel were treated equally with all persons retired from the West Virginia Public Employees Retirement System and the West Virginia Teachers Retirement System. *Id.* *Third*, along with state public employees and teachers, military retirees were treated "substantially more favorably" than persons retired from the West Virginia Judicial Retirement System. *Id.* From these facts, the court found it "difficult to infer that *any* of the pernicious dynamics that either the ancient doctrine of intergovernmental tax immunity or 4 U.S.C. § 111 are designed to remedy is implicated." *Id.* at 468.

Therefore, the court ignored *Davis* and upheld Section 12(c)(6).

b. In the decision below, the West Virginia Supreme Court again upheld Section 12(c)(6) against a challenge based on intergovernmental tax immunity and 4 U.S.C. § 111. Pet.App.16a. This time, however, the challenge was raised by Mr. Dawson—a former U.S. Marshal and deputy U.S. Marshal—who received retirement benefits from FERS. *Id.* at 4a. FERS income does not enjoy a complete exemption from taxation under West Virginia's state income taxation scheme. *See* § 11-22-12(c)(6); *see also* Pet.App.2a-3a. Mr. Dawson and his wife argued that the Tax Commissioner's preferential treatment of the retirement income of some state and local law enforcement officers was, in fact, discrimination against federal law enforcement officers in violation of 4 U.S.C. § 111. *Id.* at 4a-5a.

The court below disagreed. Drawing the same flawed distinction it drew in *Brown*, the court rea-

soned that West Virginia's "limited" tax exemptions differed from the taxing schemes invalidated by the Supreme Court in *Davis* and its progeny because "there is no intent in the West Virginia scheme to discriminate *against* federal retirees." Pet.App.10a. To determine the statute's intent, the court employed the same flawed reasoning that it used in *Brown*. *First*, the court reasoned that Mr. Dawson received more favorable tax treatment than state civilian retirees under West Virginia law. *Id.* at 15a. *Second*, unlike West Virginia civilian retirees, federal retirees are allowed to exempt $2,000 from their taxable income. *Id.* (citing W. VA. CODE § 11-21-12(c)(5)). *Third*, the court noted that Mr. Dawson also received more favorable tax treatment than retired state justices and circuit judges. *Id.* *Finally*, the court noted that Mr. Dawson received the same tax treatment as recipients of benefits from PERS and the Teachers Retirement System. *Id.*

In short, the court explained that Section 12(c)(6) gives a benefit to a "very narrow class of former state and local employees, and that benefit was not intended to discriminate against former federal marshals." *Id.* at 16a. Therefore, because the statute did not provide a blanket exemption for all state employees, the West Virginia Supreme Court again ignored *Davis* and upheld Section 12(c)(6).

2. **New Mexico.** In *Alarid v. Secretary of N.M. Department of Taxation and Revenue*, retired employees of the University of California and their spouses sought a refund for taxes paid on their retirement benefits between the years 1986 and 1989. 878 P.2d 341, 343 (N.M. 1994). The plaintiffs were New Mexico residents who worked at Los Alamos

National Laboratory, which was operated by the State of California through a contract with the federal government. *Id.* Therefore, although plaintiffs were residents of the state of New Mexico and worked in the state, they received retirement benefits through the State of California. *Id.*

During the same time period the plaintiffs were taxed on their retirement income, the retirement income of former employees of the New Mexico state educational institutions was exempt from state taxation. *Id.* Because the exemption for state educators did not extend to the employees of the National Laboratory, the plaintiffs claimed that the taxing scheme violated the intergovernmental tax immunity doctrine. *Id.* at 343-44.

The New Mexico Supreme Court disagreed, holding that the tax on plaintiff's retirement income did not violate the intergovernmental tax immunity doctrine. *Id.* at 345-46. Citing the West Virginia Supreme Court's decision in *Brown*, the court reasoned that granting narrow tax exemptions to state employees does not pose the same concerns as the blanket exemptions struck down in *Davis*: "[t]he fact that the State has chosen to exempt from state tax one limited class of state retirees does not mean Plaintiffs are being illegally discriminated against." *Id.* (citing *Brown*, 443 S.E.2d at 462). The court determined that the plaintiffs were in the same position as the majority of New Mexico citizens whose retirement incomes were also taxed. *Id.* at 347. Therefore, the court reversed the lower court's grant of summary judgment in favor of plaintiffs and held that the taxation scheme did not violate the doctrine of intergovernmental tax immunity. *Id.*

3. **Massachusetts.** In *Cooper v. Commissioner of Revenue*, Massachusetts taxpayers who paid state income tax on federal military pension income brought claims for abatement of that tax under 4 U.S.C. § 111 and the doctrine of intergovernmental tax immunity. 658 N.E.2d 963, 963 (Mass. 1995). Among other claims, they argued that a Massachusetts statutory "grandfather" provision violated 4 U.S.C. § 111 because it exempted "income from a noncontributory annuity or pension allowance received on account of service in a police or fire department of a town by a person . . . who was in the employ of such . . . department at the time of the establishment of the contributory retirement system in 1936 and 1937." *Id.* at 965. Because the statute exempted only the retirement income of certain state police or fire personnel and did not extend to similarly situated federal employees, the taxpayers argued that it violated 4 U.S.C. § 111. *Id.*

The court disagreed. It reasoned that because the tax provision at issue favored a "small and dwindling class" of state retirees, it could not constitute "discrimination against federally funded benefits." *Cooper*, 658 N.E.2d at 965 (citing *Brown*, 443 S.E.2d at 462; *Alarid*, 878 P.2d at 341). Therefore, the court relied upon the West Virginia and New Mexico Supreme Courts' precedent and ignored *Davis* because the tax statute at issue was not a blanket tax exemption for all state employees. The court held that the statute favored a group of state retirees not because their "source of the pay or compensation is the Commonwealth rather than the Federal government," but because of "the basis of occupation (police and firefighters) and the date of first employment (before

1938)." *Id.* (internal quotations omitted). The court upheld the discriminatory tax statute. *Id.*

C. Other Cases That Have Addressed Related Post-*Davis* Tax Issues Likewise Deepen the Split of Authority

The *Davis* decision left many questions unanswered regarding how states should conform their tax schemes to comply with this Court's holding. The Court explained that the issue "could be resolved either by extending the tax exemption to retired federal employees (or to all retired employees), or by eliminating the exemption for retired state and local government employees." *Davis*, 489 U.S. at 818. But the Court left to the states the ultimate decision of how to comply with its "mandate of equal treatment." *Id.*

1. In the aftermath of *Davis*, certain states have established taxation schemes that are plainly inconsistent with the rationale of *Davis* and its progeny. In some cases, states allow tax exemptions or deductions for only specific types of contributions made to retirement plans. *See, e.g.*, *Kerr v. Killian*, 84 P.3d 446 (Ariz. 2004) (state exempted state employee mandatory contributions to retirement plans "picked up" or paid by a state employer but did not exempt federal, mandatory employee contributions to plans); *Filios v. Comm'r of Revenue*, 615 N.E.2d 933 (Mass. 1993) (state exempted from taxation "contributory" state retirement benefits, which were 90% employer provided and 10% employee provided, but imposed tax on federal employer-provided military retirement compensation); *Witte v. Dir. of Revenue*, 829 S.W.2d 436 (Mo. 1992) (en banc) (state allowed deduction for

contributions made by individual earners to public retirement funds but did not allow deduction for mandatory contributions to federal Civil Service Retirement System). Unlike in *Davis*, these taxing schemes do not expressly discriminate against federal retirees based on the source of their income. Yet the *practical effect* of these schemes is to tax federal employees less favorably than state employees.

The dispositive factor in these cases was that the statutes did not discriminate against federal employees based on "who pays" them, but instead taxed a specific type of contribution to a retirement plan. *See Kerr*, 84 P.3d at 455 ("[T]he difference is not who pays the employees, but the voluntary choice made by the employer as to whether the contributions should be picked up."); *Filios*, 615 N.E.2d at 936 ("The Commonwealth does not impose the tax based on the source of the income[.]"); *Witte*, 829 S.W.2d at 441 ("Section 143.141 does not single out employees of the state and its political subdivisions for favorable tax treatment[.]"). Therefore, three state courts of last resort have upheld tax statutes that, in practice, tax state employees more favorably than federal employees. This is plainly contrary to *Davis*.

2. a. In response to *Davis*, other states eliminated tax *exemptions* for state and local government retirees and simultaneously increased state retirement *benefits* to compensate state retirees for the loss of the tax exemption. *See generally*, WALTER HELLERSTEIN, JOHN A. SWAIN, STATE TAXATION ¶ 22.04[3][a][i] (3d ed. 2017) (hereinafter "STATE TAXATION") (discussing states that increased state employee retirement benefits in response to *Davis*). Litigation ensued, as federal retirees challenged these

benefits increases as "tax rebates in disguise" under the doctrine of intergovernmental tax immunity. Courts split as to the legality of such benefits increases.

b. Four state courts of last resort held that an increase in state employee retirement benefits enacted after the repeal of statutes exempting their retirement income did not violate the doctrine of intergovernmental tax immunity. *See Ragsdale v. Dep't of Revenue*, 895 P.2d 1348 (Or. 1995); *Ward v. South Carolina*, 590 S.E.2d 30 (S.C. 2003); *Thompson v. Utah State Tax Comm'n*, 112 P.3d 1205 (Utah 2004); *Weiss v. McFadden*, 148 S.W.3d 248 (Ark. 2004). These courts generally reasoned that this Court's decision in *Davis* and the doctrine of intergovernmental tax immunity relate only to discrimination *in taxation* based on the source of income—they do not "deprive a state of its sovereignty to establish the level of its employees' compensation[.]" *Ward*, 590 S.E.2d at 32; *Thompson*, 112 P.3d at 1207 ("[W]e find nothing in *Davis* even remotely suggesting that a state cannot compensate its employees at whatever rate it sees fit[.]"). Therefore, because the state statutes at issue only added retirement *benefits*—and did not expressly address taxation—the courts did not apply *Davis* and upheld the benefits increases.

c. On the other hand, two state courts of last resort held that state increases in state retiree benefits in response to *Davis* violated the doctrine of intergovernmental tax immunity. *See Vogl v. Dep't of Revenue*, 960 P.2d 373 (Or. 1998); *Sheehy v. Pub. Employees Ret. Div.*, 864 P.2d 762 (Mont. 1993). In *Vogl*, the Supreme Court of Oregon—without overruling its contrary decision in *Ragsdale*—held that a statu-

tory increase in state retiree benefits violated the doctrine of intergovernmental tax immunity because the benefit increase was more narrowly tailored to directly compensate the state retirees for the nullified tax exemption than the benefits increase in *Ragsdale*. 960 P.2d at 376, 379-81, 393. Similarly, in *Sheehy*, the Supreme Court of Montana held that a statutory increase in state employee retirement benefits violated the doctrine of intergovernmental tax immunity and 4 U.S.C. § 111. 864 P.2d at 767-68. The court concluded that the adjustment in benefits was actually a "partial tax rebate denominated otherwise in an attempt to evade the requirements of federal law[.]" *Id.*

The Oregon and Montana Supreme Courts viewed the benefits increases as tied expressly to attempts to circumvent *Davis*, not merely as an increase in compensation benefits. *See Vogl*, 960 P.2d at 380 ("[A]s the state moves closer to replacing the lost net income on a dollar-for-dollar basis, the fact that the increase is in fact a tax rebate, rather than a general increase in compensation to 'make up' for lost net income, becomes more apparent."); *Sheehy*, 864 P.3d at 768 ("Rather than comply with 4 U.S.C. § 111 . . . the legislature chose to equalize the burden by taxing all retirement benefits, subject to the phase-out exemption discussed above. Within the same legislative enactment, the legislature provided for an adjustment payment to state retirees who are Montana residents. The State's argument that the two portions of the bill are not related defies logic."). Therefore, because the benefits increases were actually discriminatory tax rebates in disguise, they violated the doc-

trine of intergovernmental tax immunity as outlined by this Court in *Davis*.

3. These cases confirm that state courts are having difficulty applying *Davis* and its progeny and that this Court's intervention is essential to clarify their parameters and scope. Furthermore, this Court should clarify that ignoring *Davis* and "favoring retired state and local government employees over retired federal employees" is impermissible and violates the doctrine of intergovernmental tax immunity—even where states craft creative taxing schemes to mask that illegal purpose. *Davis*, 489 U.S. at 817.

II. THE DECISION BELOW DIRECTLY CONFLICTS WITH THIS COURT'S DECISIONS IN *DAVIS* AND *JEFFERSON COUNTY*

The decision below is directly contrary to this Court's precedent. Indeed, this Court held in *Davis*, 489 U.S. at 817, and reiterated in *Jefferson County*, 527 U.S. at 442-43, that a state may not tax a federal retiree's pension and other retirement benefits less favorably than the retirement benefits of similarly situated state retirees. The decision below acknowledged this precedent, but then erroneously determined that it did not apply because *Davis* dealt with a blanket tax exemption for all state employees, and the West Virginia statute at issue (Section 12(c)(6)) exempted only a subset of state employees. Pet.App.10a. This distinction is erroneous.

1. This Court broadly held that taxes favoring retired state and local government employees over similarly situated retired federal employees violate the doctrine of intergovernmental tax immunity.

In *Davis*, this Court's holding was clear: "the imposition of a heavier tax burden on those who deal with one sovereign than is imposed on those who deal with the other" must be justified by demonstrating that the disparate treatment is the result of "significant differences between the two classes." 489 U.S. at 816-17. In that case, the Michigan taxing scheme at issue exempted retirement benefits received from the state or its political subdivisions, but did not exempt federal retirement benefits. *Id.* at 806. The state attempted to justify the discriminatory treatment by arguing that the state has an interest in hiring qualified civil servants and that the state retirement benefits are "less munificent" than those offered by the federal government. *Id.* at 816.

This Court disagreed that the manufactured "differences" warranted the unequal tax treatment. *First*, the Court stated that the state's goal of hiring qualified candidates was "beside the point," because it was a *reason for* the preferential treatment of state employees, not a *significant difference* between state and federal employees. *Id.* *Second*, the Court rejected the notion that differences in value between state and federal retirement benefits justified preferential tax treatment for state employees. *Id.* at 816-17. It reasoned,

> [a] tax exemption truly intended to account for differences in retirement benefits would not discriminate on the basis of the source of those benefits . . . ; rather, it would discriminate on the basis of the amount of benefits received by the individual retirees.

Id. at 817. Because the state was unable to show that significant differences between state and federal retirees justified the unequal tax treatment, this Court held that the taxing scheme violated principles of intergovernmental tax immunity. *Id.*

In *Jefferson County*, this Court reiterated its holding in *Davis*. 527 U.S. at 442-43. Although this Court ultimately determined that the occupational tax at issue did not violate the doctrine of intergovernmental tax immunity, it again explained that "a state tax exempting retirement benefits paid by the State but not those paid by the Federal Government" violates the doctrine of intergovernmental tax immunity. *Id.* at 442. This Court cautioned—"[s]hould Alabama or Jefferson County authorities take to exempting state officials while leaving federal officials (or *a subcategory of them*) subject to the tax, that would indeed present a starkly different case" violating the doctrine of intergovernmental tax immunity. *Id.* at 443 (emphasis added). The key is whether the tax discriminates against federal employees "based on the federal *source* of their pay or compensation." *Id.* at 442-43.

2. The decision below is directly contrary to *Davis* and its progeny. Indeed, the court below upheld a West Virginia tax exemption that applied only to four state law enforcement retirement plans while not extending the same exemption to similarly situated federal law enforcement officials. Pet.App.16a.

While acknowledging this Court's decision in *Davis*, the court below chose to disregard it. Instead, it determined—without supporting authority—that *Davis* does not apply to state laws that exempt only a "*narrow* class" of state retirees while discriminating

against similarly situated federal retirees. *Id.* at 10a. It implied that small tax discriminations are permissible. But nothing in *Davis* supports that conclusion. In fact, this Court in *Jefferson County* clarified that the principles of intergovernmental tax immunity apply even when a "subcategory" of federal officials are taxed unequally to their state counterparts. 527 U.S. at 443.

Furthermore, the court below reasoned that the tax exemption was not *intended to discriminate* against Mr. Dawson, but instead was intended to "*benefit* . . . a narrow class of state retirees." Pet.App.15a. However, this reasoning is circular and could be used to support any discriminatory taxing scheme—including the scheme invalidated in *Davis*—that intends to *benefit* a group of state employees while not extending it to federal employees. In *Davis*, this Court did not apply a test whether a given tax provision was "intended" to burden federal employees. Rather, this Court looked to the "source of those benefits."

Finally, the court below erroneously avoided the question whether significant differences could justify the disparate treatment, determining that it was unnecessary to reach that question. However, it was "undisputed" in this case that "there are no significant differences between Mr. Dawson's powers and duties as a U.S. Marshal and the powers and duties of the state and local law enforcement officers listed in [Section 12(c)(6)]." Pet.App.22a. Thus, under the proper analysis, Dawson could not be treated differently from the similarly situated state law enforcement retirees whose income is entirely exempt.

Accordingly, the decision below, which upholds a state taxing scheme that favors state retirees and discriminates against similarly situated federal retirees based solely on the source of their income, contravenes clear precedent of this Court and should be reversed.

III. THE QUESTION PRESENTED IS RECURRING AND IMPORTANT

The West Virginia Supreme Court's decision is at odds with this Court's precedent and with decisions of other state courts of last resort. Since *Davis*, litigation regarding the proper structure of tax exemptions and benefits for state and federal employees has exploded in state courts across the country. The result has been inconsistent and ever-changing tax exemption schemes for government retirees nationwide. Without this Court's intervention, the growing population of both federal and state retirees who budget based on a fixed income will be subjected to continued uncertainty.

1. The issue presented in this case has consistently arisen in state courts after *Davis*. In response to this Court's *Davis* decision, states took varied approaches to restructuring their tax laws to achieve equal treatment between state and federal retirees. *See supra* Section I; *see also* Dan T. Coenen & Walter Hellerstein, *Suspect Linkage: The Interplay of State Taxing and Spending Measures in the Application of Constitutional Antidiscrimination Rules*, 95 MICH. L. REV. 2167, 2178-79 (1997) (discussing various approaches to retirement taxation and benefits schemes taken by states after *Davis*); STATE TAXATION ¶ 22.04[3][a] (same). This rush to change state

tax and benefits schemes in response to *Davis* resulted in varied tax treatment for retirees depending on their state of residence. *See, e.g.*, NATIONAL ACTIVE AND RETIRED FEDERAL EMPLOYEES ASSOCIATION, STATE TAX TREATMENT OF FEDERAL ANNUITIES (Apr. 2017), https://www.narfe.org/pdf/StateTaxRoundupTaxYear2015.pdf (giving state-by-state breakdown of taxation of federal annuities).

As a result of these widespread changes, a "nationwide outpouring of litigation" ensued where federal retirees challenged the various revised state tax and benefits schemes. *See* STATE TAXATION ¶ 22.04[3][a] (discussing "considerable litigation" in response to *Davis*). Indeed, a review of the caselaw shows that there are 58 state court of last resort decisions that discuss "intergovernmental tax immunity" and cite *Davis*. This litigation surge resulted in a split of authority and inconsistent treatment of federal and state retirees across states. *See supra* Section I.

2. Open questions regarding the proper structure for state retirement tax and benefits schemes affect a large segment of the U.S. population. For example, as of 2014, there were over 1.5 million federal retirees living in states that tax federal retirement income, and that number continues to grow. *See* Janet Kopenhaver, *Population of Federal Employees by Congressional District and County (2014)*, EYE ON WASHINGTON, http://eyeonwashington.com/few_map_2014/index.html (last visited Sept. 18, 2017); *see also* CONGRESSIONAL BUDGET OFFICE, CIVIL SERVICE RETIREMENT AND DISABILITY FUND - CBO MARCH 2012 BASELINE, https://www.cbo.gov/sites/default/files/112th-congress-2011-2012/dataandtechnicalinforma

tion/43067_CivilServiceRetirementDisabilityFund.pdf (last visited Sept. 18, 2017) (projecting approximately 10% growth in number of federal retirees between 2012 and 2022). Furthermore, in 2014, state and local governments employed around 7.4 million full-time equivalent workers (approximately 232 public employees for every 10,000 Americans). When teachers and others working in education are included in the 2014 total, it more than doubles to about 16.2 million non-federal public employees nationwide. *See* Governing.com, *States With Most Government Employees: Totals and Per Capita Rates*, http://www.governing.com/gov-data/public-workforce-salaries/states-most-government-workers-public-employees-by-job-type.html (last visited Sept. 18, 2017). Open questions regarding the proper structure of state tax and benefits schemes related to public retirement income and ever-growing tax disparities between states affect millions of retirees across the United States and require resolution.

3. Finally, allowing a state like West Virginia to perpetuate a tax statute that discriminates against federal employees in favor of state employees creates troubling precedent. As the population of federal retirees continues to increase, cash-strapped states may choose to follow the lead of West Virginia, Arizona, and Massachusetts and impose taxes that favor small groups of state retirees while taxing similarly situated federal retirees to cover state costs. But this discriminatory taxation of federal employees to pad states' coffers is exactly the behavior that the doctrine of intergovernmental tax immunity prohibits. *Davis*, 489 U.S. at 814 (explaining that "private entities or individuals who are subjected to discrimi-

natory taxation on account of their dealings with a sovereign" are entitled to "receive the protection of the constitutional doctrine" of intergovernmental tax immunity). This Court's intervention is necessary to ensure that discriminatory tax statutes like Section 12(c)(6) are not used to increase states' revenue at the expense of the federal government and its employees.

IV. THIS CASE PRESENTS AN IDEAL VEHICLE TO DECIDE THIS IMPORTANT QUESTION

This petition presents an ideal vehicle to decide the question presented. *First*, it is undisputed that there are no significant differences between the state law enforcement officers exempted under Section 12(c)(6) and federal marshals like Mr. Dawson. Pet.App.22a. There is no factual dispute for this Court to resolve, and the intergovernmental tax immunity question presented is purely a question of law.

Second, the West Virginia Supreme Court's erroneous determination that this Court's holding in *Davis* is limited only to *blanket tax exemptions* for state employees has been erroneously relied upon by other state courts of last resort. Indeed, both the New Mexico Supreme Court and the Massachusetts Supreme Court have expressly cited the West Virginia Supreme Court's *Brown* decision to uphold state tax exemptions for *narrow groups* of state employees that discriminate against similarly situated federal employees. *See Alarid*, 878 P.2d at 345-46; *Cooper*, 658 N.E.2d at 965. This case presents an opportunity for this Court to correct the West Virginia Supreme Court's misstatement of the holding in *Davis*

before other state courts rely on *Brown* or the decision below to uphold a discriminatory taxing scheme that violates the doctrine of intergovernmental tax immunity.

CONCLUSION

The petition for a writ of certiorari should be granted. In the alternative, because the decision below is so plainly contrary to this Court's precedent, summary reversal is warranted.

Respectfully submitted,

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SEPTEMBER 19, 2017

APPENDIX

APPENDIX A

STATE OF WEST VIRGINIA
SUPREME COURT OF APPEALS

Dale W. Steager, as
State Tax Commissioner of West Virginia,
Respondent Below, Petitioner

vs) No. 16-0441 (Mercer County 15-C-326)

James Dawson and
Elaine Dawson,
Petitioners Below, Respondents

MEMORANDUM DECISION

The Tax Commissioner for the State of West Virginia, petitioner Dale W. Steager,[1] by counsel Katherine Schultz and L. Wayne Williams, appeals a March 31, 2016, order of the Circuit Court of Mercer County. In that order, the circuit court held that a tax exemption available only to beneficiaries of certain state retirement plans unlawfully discriminated against certain federal retirees. The taxpayer-respondents, James and Elaine Dawson, by counsel Michael W. Carey and David R. Pogue, filed a

[1] Mr. Steager replaced Mark W. Matkovich as Tax Commissioner in January 2017.

response in favor of the circuit court's order. The Tax Commissioner filed a reply.

The Court has considered the parties' briefs and oral arguments, as well as the record on appeal. Upon consideration of the standard of review and existing precedent, the Court finds no substantial question of law. This case satisfies the "limited circumstances" requirement of Rule 21(d) of the Rules of Appellate Procedure and is appropriate for a memorandum decision rather than an opinion. A memorandum decision reversing the circuit court's order is therefore appropriate under Rule 21 of the Rules of Appellate Procedure.

Since 1939, Congress has permitted states to tax the income and the retirement benefits of former United States government employees. However, Congress allows state taxes upon federal retirement benefits only "if the taxation does not discriminate . . . because of the source of the pay or compensation." 4 U.S.C. § 111 [1998].

West Virginia imposes taxes upon the government-provided retirement income of most local, state and federal employees who reside in this state. West Virginia taxes the income of retired local and state employees received from the West Virginia Public Employees Retirement System ("PERS") and the State Teachers Retirement System ("TRS"); it also taxes the income of retired federal employees received from any federal or military retirement system. W.Va. Code § 11-21-12(c)(5) [2006]. However, West Virginia law permits the recipients of PERS, TRS, or a general federal retirement to exempt up to $2,000 of retirement benefits from their

taxable income. *Id.*[2] The law permits recipients of military retirement benefits to exempt up to $20,000. W.Va. Code § 11-21-12(c)(7)(B). Furthermore, any taxpayer aged 65 or older may exempt up to $8,000 from their taxable income, regardless of the source of that income. W.Va. Code § 11-2112(c)(8).

At issue in this case is a unique tax exemption contained in West Virginia Code § 11-21-12(c)(6) ("Section 12(c)(6)"). Section 12(c)(6) allows the recipients of four small West Virginia retirement plans to exempt from their taxable state income all the benefits received from those plans. According to the Tax Commissioner, the recipients comprise approximately two percent of all state government retirees. The four retirement plans are the Municipal Police Officer and Firefighter Retirement System ("MPFRS"); the Deputy Sheriff Retirement System ("DSRS"); the State Police Death, Disability and Retirement Fund ("Trooper Plan A"); and the West Virginia State Police Retirement System ("Trooper Plan B").[3]

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[2] W.Va. Code § 11-21-12(c)(5) provides, in pertinent part, that a taxpayer may exempt from adjusted gross income "the first two thousand dollars of benefits received under any federal retirement system to which Title 4 U.S.C. § 111 applies[.]"

[3] W.Va. Code § 11-21-12(c)(6) provides:

> (c) *Modifications reducing federal adjusted gross income.* -- There shall be subtracted from federal adjusted gross income to the extent included therein: . . .
>
> (6) Retirement income received in the form of pensions and annuities after the thirty-first day of December, one thousand nine hundred seventy-nine, under any West Virginia police, West Virginia

The taxpayer in this case is James Dawson, who worked most of his career as a deputy U.S. Marshal before being presidentially appointed U.S. Marshal for the Southern District of West Virginia. Mr. Dawson retired from the U.S. Marshals Service on March 31, 2008. During his employment, Mr. Dawson was enrolled exclusively in the Federal Employee Retirement System ("FERS"), and he now receives benefits from FERS. The Tax Commissioner agrees that Mr. Dawson is entitled to exempt at least $2,000 of FERS income from his state taxable income; when he reaches the age of 65, he may exempt up to $8,000. *See* W.Va. Code §§ 11-21-12(c)(5) and -12(c)(8).

For tax years 2010 and 2011, Mr. Dawson and his wife Elaine filed amended tax returns claiming an adjustment exempting Mr. Dawson's FERS retirement income from state income tax pursuant to Section 12(c)(6). The Tax Commissioner refused to allow the Dawsons to claim the exemption.

The Dawsons appealed, and in a hearing before the Office of Tax Appeals asserted that there is no significant difference between state, local, and federal law enforcement officers. Accordingly, the Dawsons contended that the Tax Commissioner's preferential treatment of the retirement income of some (but not

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> Firemen's Retirement System or the West Virginia State Police Death, Disability and Retirement Fund, the West Virginia State Police Retirement System or the West Virginia Deputy Sheriff Retirement System, including any survivorship annuities derived from any of these programs, to the extent includable in gross income for federal income tax purposes[.]

all) state and local law enforcement officers pursuant to Section 12(c)(6) was, in fact, discrimination against federal law enforcement officers prohibited by 4 U.S.C. § 111. The Tax Commissioner countered that, under the totality of the circumstances, the Section 12(c)(6) exemption was not designed to discriminate against federal retirees; rather, the intent of the exemption is to give a benefit to a very narrow class of former state and local employees. The Office of Tax Appeals rejected the Dawsons' argument and affirmed the Tax Commissioner's denial of the Section 12(c)(6) exemption.

The Dawsons appealed to the Circuit Court of Mercer County, and the parties repeated their arguments. In an order dated March 31, 2016, the circuit court reversed the decision of the Office of Tax Appeals. The circuit court concluded that the Tax Commissioner's denial of the Section 12(c)(6) exemption to the Dawsons violated 4 U.S.C. § 111. The Tax Commissioner now appeals the circuit court's order.

The issues raised by the parties involve the interpretation of Section 12(c)(6), and an assessment of whether it conflicts with 4 U.S.C. § 111. "Where the issue on an appeal from the circuit court is clearly a question of law or involving an interpretation of a statute, we apply a *de novo* standard of review." Syllabus Point 1, *Chrystal R.M. v. Charlie A.L.*, 194 W.Va. 138, 459 S.E.2d 415 (1995). *See also*, Syllabus Point 1, *Appalachian Power Co. v. State Tax Dep't of W.Va.*, 195 W.Va. 573, 466 S.E.2d 424 (1995) ("Interpreting a statute or an administrative rule or regulation presents a purely legal question subject to *de novo* review."). We review the factual findings and

conclusions of the Tax Commissioner under a clearly wrong and abuse of discretion standard. Syllabus Point 5, *Frymier-Halloran v. Paige*, 193 W.Va. 687, 458 S.E.2d 780 (1995). "The 'clearly wrong' and the 'arbitrary and capricious' standards of review are deferential ones which presume an agency's actions are valid as long as the decision is supported by substantial evidence or by a rational basis." Syllabus Point 3, *In re Queen*, 196 W.Va. 442, 473 S.E.2d 483 (1996).

The Tax Commissioner asserts that the circuit court erred in holding that Section 12(c)(6) was an intentionally discriminatory tax against federal marshals. The Tax Commissioner argues that the circuit court failed to take into account the fact that there is no evidence in the record to suggest that Section 12(c)(6) was intended to discriminate against employees or former employees of the federal government. Viewing West Virginia's tax scheme in totality, the Tax Commissioner contends that the record shows there was no calculated scheme or blanket plan to discriminate against retired federal marshals based on the source of their income. As we explain below, we agree and reverse the circuit court's holding.

In *Davis v. Michigan Dept. of Treasury*, 489 U.S. 803 (1989), the United States Supreme Court analyzed 4 U.S.C. § 111 and discussed its roots in the doctrine of intergovernmental tax immunity. The doctrine traces back to *McCullough v. Maryland*, 17 U.S. 316 (1819), the seminal case where the Supreme Court recognized that Congress was constitutionally empowered to create a "Bank of the United States," and held that the state of Maryland could not impose

a discriminatory tax on the Bank. "Chief Justice Marshall's opinion for the Court reasoned that the Bank was an instrumentality of the Federal Government used to carry into effect the Government's delegated powers, and taxation by the State would unconstitutionally interfere with the exercise of those powers." *Davis*, 489 U.S. at 810.[4]

"[I]ntergovernmental tax immunity is based on the need to protect each sovereign's governmental operations from undue interference by the other." *Id.* at 814. Prior to 1939, the "salaries of most government employees, both state and federal, generally were thought to be exempt from taxation by another sovereign under the doctrine of intergovernmental tax immunity." *Id.* "This rule 'was based on the rationale that any tax on income a party received under a contract with the government was a tax on the contract and thus a tax "on" the government because it burdened the government's power to enter into the contract.'" *Id.* at 811 (quoting *South Carolina v. Baker*, 485 U.S. 505, 518 (1988)). However, Congress enacted the "Public Salary Tax Act of 1939" (of which 4 U.S.C. § 111 is a part) "to impose federal income tax on the salaries of all state and local government employees," *Davis*, 489 U.S. at

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[4] The intergovernmental tax immunity doctrine is founded upon the Supremacy Clause (Article VI) of the United States Constitution which provides, in part: "This Constitution, and the laws of the United States which shall be made in pursuance thereof; and all treaties made, or which shall be made, under the authority of the United States, shall be the supreme law of the land[.]"

810, and also to expressly permit states to tax the salaries of federal employees. *Id.* at 811.[5]

The Supreme Court found, however, that Congress "did not waive all aspects of intergovernmental tax immunity[.]" *Id.* at 812. The final clause of 4 U.S.C. § 111 provides, "The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States . . . if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation." This clause prohibits "state taxes that discriminate against federal employees on the basis of the source of their compensation." *Davis*, 489 U.S. at 811. The Supreme Court concluded that this clause embodies "the modern constitutional doctrine of intergovernmental tax immunity." *Id.* at 813. Under the doctrine, if a heavier tax burden is imposed upon a class of individuals who deal with the federal government than is imposed upon those individuals who deal with state government, then "the relevant inquiry is whether the inconsistent tax treatment is directly related to, and justified by, 'significant differences between the two classes.'" *Id.* at 815-816 (quoting *Phillips Chemical Co. v. Dumas Independent School Dist.*, 361 U.S. 376, 383 (1960)).

In *Davis*, the Supreme Court considered a Michigan state tax scheme under which "the retirement benefits of retired state employees are

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[5] Congress adopted the Public Salary Tax Act contemporaneously with the Supreme Court's decision in *Graves v. New York ex rel. O'Keefe*, 306 U.S. 466 (1939), which held that a state could levy non-discriminatory income taxes upon a federal employee. *Davis*, 489 U.S. at 811-812.

exempt from state taxation while the benefits received by retired federal employees are not." *Davis*, 489 U.S. at 806. The Supreme Court specifically identified the state scheme as a "blanket exemption[.]" *Id.* at 817. The Supreme Court had "no difficulty" concluding that federal retirement benefits are a form of compensation protected from discrimination under 4 U.S.C. § 111. *Id.* at 808-809. More importantly, the Supreme Court concluded that the blanket state tax exemption was precluded by 4 U.S.C. § 111 because it "violates principles of intergovernmental tax immunity by favoring retired state and local government employees over retired federal employees." *Id.* at 817.

Several years later, this Court was presented with an opportunity to apply *Davis* and 4 U.S.C. § 111 to the exemption contained in Section 12(c)(6). In *Brown v. Mierke*, 191 W.Va. 120, 443 S.E.2d 462 (1994), the taxpayers were retirees from the armed forces of the United States who received military pensions.[6] As recipients of a military pension, the Tax Commissioner agreed that the taxpayers were entitled to exempt at least $2,000 of pension income from their state taxable income; if they were over age 65, they could exempt up to $8,000. 191 W.Va. at 121, 443 S.E.2d at 463 (citing W.Va. Code §§ 11-21-12(c)(5) and -12(c)(9)).[7] The taxpayers, however,

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[6] In *Barker v. Kansas*, 503 U.S. 594 (1992), the Supreme Court held that federal military retirement benefits are protected from discrimination under 4 U.S.C. § 111.

[7] Subsequent to our decision in *Brown*, and effective after the 2002 tax year, the recipients of military retirement income may exempt up to $20,000 from their taxable income. W.Va. Code § 11-21-12(c)(7)(B).

claimed they were entitled to exempt *all* of their pension income from state taxation under Section 12(c)(6). The taxpayers argued, "West Virginia's exemption of certain firefighters' and police officers' retirement benefits renders the tax of military pensions prohibited and discriminatory." 191 W.Va. at 123, 443 S.E.2d at 465.

This Court rejected the taxpayers' argument in *Brown*. We noted that in cases where the Supreme Court had found a state tax exemption improperly discriminated against federal retirees under 4 U.S.C. § 111 – such as the Michigan exemption for all state retirees in *Davis* – the state had afforded a blanket exemption to *all* state retirees. Our analysis of Section 12(c)(6) turned on the fact that West Virginia's tax law "exempts a *narrow* class of state employees from state taxation while taxing federal employees." 191 W.Va. at 124, 443 S.E.2d at 466 (emphasis added).

Applying *Davis*, we recognized in *Brown* that "the test of whether a state tax scheme violates 4 U.S.C. § 111 is whether there exists substantial differences between the two classes that justify the discrimination." *Id.* We concluded, however, that West Virginia's limited, multi-tiered series of tax exemptions differed from the "schemes invalidated by the Supreme Court in that there is no intent in the West Virginia scheme to discriminate *against* federal retirees; rather, the intent is to give a benefit to a very narrow class of former state and local employees." *Id.* Summarizing the law, we found in Syllabus Point 2:

> Challenges to a state tax scheme under 4 U.S.C. § 111 can succeed only when one purpose of the challenged scheme is shown to discriminate against the officer or employee because of the *source* of pay or compensation. In determining whether such discrimination exists, a court will look to the totality of the circumstances to ascertain whether the intent of the scheme is to discriminate against employees or former employees of the federal government.

191 W.Va. at 121, 443 S.E.2d at 463.

The *Brown* Court upheld Section 12(c)(6) and found it did not violate 4 U.S.C. § 111 and the doctrine of intergovernmental tax immunity. The ruling turned on the totality of the circumstances. First, the record in *Brown* indicated that (as of 1991) 1,624 retired police and firefighters were exempt from taxation by Section 12(c)(6) – "about four percent of all state and local retirees in West Virginia." 191 W.Va. at 121, 443 S.E.2d at 463. Furthermore, an analysis of the entire scheme of tax exemptions showed no intent to discriminate against former employees of the federal government:

> [T]hree facts conclusively demonstrate that no calculated scheme or plan exists to discriminate against retired military personnel based on the source of their income: (1) retired military personnel are treated *more* favorably than West Virginians who have retired from civilian occupations; (2) retired military personnel are treated equally with all persons retired from the West Virginia Public Employees Retirement System and the West Virginia

> Teachers Retirement System; and (3) along with state public employees and teachers, military retirees are treated *substantially more favorably* than persons retired from the West Virginia Judicial Retirement System.

191 W.Va. at 125, 443 S.E.2d at 467. As further evidence of a lack of discriminatory intent, the Court noted:

> That the judges of this Court, statewide elected officials with rather substantial personal political followings and not a few friends in the West Virginia Legislature, are taxed at a substantially *higher* rate than retired members of the Armed Forces of the United States, and both military retirees and the majority of retired state employees are taxed at *lower* rates than West Virginians retired from private sector occupations renders it extraordinarily difficult to infer that *any* of the pernicious dynamics that either the ancient doctrine of intergovernmental tax immunity or 4 U.S.C. § 111 are designed to remedy is implicated.

191 W.Va. at 125-26, 443 S.E.2d at 467-68.

We now turn to the circumstances of this case. Section 12(c)(6) exempts from state taxation the retirement income of many state and local firefighters and law enforcement officers, but not federal marshals. The taxpayer, Mr. Dawson, asserts that there are no significant differences between the powers and duties of state and local law enforcement officers and those of federal marshals. Mr. Dawson contends that this inconsistent tax treatment is proscribed by 4 U.S.C. § 111 because, as the Supreme

Court said in *Davis*, it is not "directly related to, and justified by, significant differences between the two classes." 489 U.S. at 815-816.

The Tax Commissioner counters that the exemption at issue in *Davis* was a global or blanket exemption: the *Davis* tax exemption applied to all state retirees but no federal retirees. In this case, the tax exemption in Section 12(c)(6) applies to a narrow but diverse class of state retirees. Of 53,184 total state government retirees in 2010, less than two percent are eligible for the exemption. For example, the Tax Commissioner showed that in 2010, only 260 retired deputy sheriffs (less than 0.5% of all state retirees) received a pension from the DSRS and were entitled to use the Section 12(c)(6) exemption. An unknown number of other deputy sheriffs, all of whom started working before the DSRS was established in 1998, cannot use the Section 12(c)(6) exemption because they are among the 22,040 retirees receiving a pension from PERS. The Tax Commissioner also showed some state retirement plans provide cost of living increases (like Trooper Plan A or Plan B) while some do not (like MPFRS or DSRS). Some state retirees have contributed to and therefore receive social security (DPRS) while some do not (Trooper Plans A and B). Further, the exemption in Section 12(c)(6) applies to firefighters, but not to emergency medical technicians or paramedics.[8] The Section 12(c)(6) exemption also

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[8] Individuals who provide emergency medical services may receive retirement benefits from PERS or, if employed after 2008, the Emergency Medical Services Retirement System ("EMSRS"). *See* W.Va. Code § 16-5V-1 *et seq*.

does not apply to law enforcement officers employed by the Department of Natural Resources[9] or by the Capitol Police.[10]

It is well settled that tax exemptions are strictly construed against the taxpayer. Where a person claims an exemption from a law imposing a tax, the law is strictly construed against the person claiming the exemption. Syllabus Point 2, *State ex rel. Lambert v. Carman*, 145 W.Va. 635, 116 S.E.2d 265 (1960) ("Where a person claims an exemption from a law imposing a license or tax, such law is strictly construed against the person claiming the exemption."); Syllabus Point 3, *Owens-Illinois Glass Co. v. Battle*, 151 W.Va. 655, 154 S.E.2d 854 (1967) ("Where a person claims an exemption from a law imposing a tax, such law must be construed strictly against the person claiming the exemption."). Under Syllabus Point 2 of *Brown*, the Dawsons were required to establish that the tax scheme established by Section 12(c)(6) discriminates against a federal retiree because of the source of his or her income. However, in determining whether such discrimination exists, this Court "will look to the totality of the circumstances to ascertain whether the intent of the scheme is to discriminate against

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[9] *See* W.Va. Code § 20-7-1 *et seq*. (establishing natural resources police officers and setting duties and powers).

[10] The Capitol Police is formally known as the "Division of Protective Services." *See* W.Va. Code § 15-5D-2 [2002] ("The state facilities protection division within the department of military affairs and public safety shall hereafter be designated the division of protective services. The purpose of the division is to provide safety and security at the capitol complex and other state facilities.").

employees or former employees of the federal government." *Id.*

In light of the totality of the circumstances, and the totality of the structure of West Virginia's tax and retirement scheme, Section 12(c)(6) did not discriminate against Mr. Dawson. The intent of the exemption contained in Section 12(c)(6) was to give a benefit to a narrow class of state retirees. The record conclusively demonstrates that Mr. Dawson received more favorable tax treatment than state civilian retirees, whose status as retirees affords them no special exemption. Unlike state civilian retirees, federal retirees like Mr. Dawson are allowed to exempt $2,000 from their taxable income. W.Va. Code § 11-21-12(c)(5). Mr. Dawson also received more favorable tax treatment than retired state justices and circuit judges, who likewise are afforded no exemption for their state retirement income.[11] Most importantly, Mr. Dawson received the same tax treatment as the former state employees who make up as the vast majority of all state retirees: recipients of benefits from PERS and the Teachers Retirement System. Additionally only some law enforcement officers (such as deputy sheriffs

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[11] Most retired circuit judges and supreme court justices receive benefits from the Judges' Retirement System and cannot use the exemption applicable to recipients of PERS benefits in W.Va. Code 11-21-12(c)(5). However, family court judges, as well as a handful of former circuit judges and justices, are members of PERS and *can* use the exemption. *See* W.Va. Code § 51-9-5 [1987] (permitting circuit judges and justices to elect PERS coverage); W.Va. Code § 51-2A-6(g) [2011] (providing family court judges are not eligible to participate in the Judges' Retirement System).

receiving benefits from DSRS) are permitted to rely upon the Section 12(c)(6) exemption, while others (such as deputy sheriffs receiving benefits from PERS) are not.

When this Court first upheld Section 12(c)(6) in *Brown* in 1994, the number of retirees who qualified for the exemption comprised four-percent of all state-pension recipients. In the years at issue in this case, the number who qualify for the exemption has diminished to two percent of all state-pension recipients. Similar to what we found in *Brown*, the total structure of West Virginia's system for taxing personal income does not discriminate against retired members of the United States Marshals Service in violation of 4 U.S.C. § 111. Section 12(c)(6) gives a benefit to a very narrow class of former state and local employees, and that benefit was not intended to discriminate against former federal marshals.

The circuit court erred in finding that Section 12(c)(6) was contrary to 4 U.S.C. § 111. Accordingly, the circuit court's March 31, 2016, order must be reversed.

Reversed and remanded.

ISSUED: May 17, 2017

CONCURRED IN BY:

Chief Justice Allen H. Loughry II
Justice Robin Jean Davis
Justice Margaret L. Workman
Justice Menis E. Ketchum
Justice Elizabeth D. Walker

APPENDIX B

16-0441
COPY

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APR 01 2016
NIA
JULIE BALL
CLERK CIRCUIT COURT
MERCER COUNTY

IN THE CIRCUIT COURT OF MERCER COUNTY, WEST VIRGINIA

JAMES DAWSON and ELAINE F. DAWSON,
Petitioners,
v.

MARK W. MATKOVICH, as ACTING STATE TAX COMMISSIONER OF WEST VIRGINIA,
Respondent.

CIVIL ACTION NO. 15-C-326

RECEIVED
APR 4 2016
Attorney General Office
Tax Division

ORDER GRANTING APPEAL AND REVERSING THE DECISION OF THE WEST VIRGINIA OFFICE OF TAX APPEALS

This matter came before the Court for oral argument on March 14, 2016, pursuant to W.Va. Code §11-10A-19, W. Va. CSR §121-1-82, and Rule 2 of the West Virginia Rules for Administrative Appeals. The petitioners appeared in person and by

counsel, David Pogue. The Respondent appeared by counsel, Katherine Schultz.

Background and Procedural History

This matter is an appeal from an Order of the Office of Tax Appeals ("OTA"), which was itself an appeal from a decision by the West Virginia State Tax Department ("Tax Department"). Petitioner James Dawson ("Dawson"), a retired federal law enforcement officer, attempted to exempt his retirement income from state income tax pursuant to W.Va Code §11-21-12(c)(6), but the Tax Department denied the exemption. Dawson and his wife then filed a Petition for Refund before the OTA and a corresponding motion for summary judgment. After conducting a hearing on the matter, the OTA concluded it did not have the power to grant the relief sought. Accordingly OTA denied the Dawsons' motion for summary judgment and dismissed their appeal.

The Dawsons then appealed to this Court pursuant to the Administrative Procedures Act, W.Va Code §29A-5-4(g). On appeal they argue the OTA incorrectly applied the test established in *Brown v. Mierke*, 191 W.Va. 120,443 S.E.2d 462 (1994) instead of the test set forth by the United States Supreme Court's decision in *Davis v. Michigan Dept. of Treasury*, 489 U.S. 803 (1989). Under the *Davis* standard, W.Va Code §11-21-12(c)(6) violates 4 U.S.C. §111 and the constitutional doctrine of intergovernmental tax immunity by favoring retired state and local law enforcement officers over retired federal law enforcement officers. According to the Dawsons, the OTA also erred by relying on

differences between the pay scales of federal and state law enforcement officers to uphold the validity of §11-21-12(c)(6).

The Tax Department, on the other hand, submits that because Mr. Dawson is a retired US Marshal instead of a retired West Virginia law enforcement official, he does not meet the criteria set forth in §11-21-12(c)(6) and cannot claim the exemption set forth in that statute. The Tax Department further argues that the OTA properly applied *Brown* instead of *Davis*, because the West Virginia Supreme Court rendered its decision in *Brown* after the United States Supreme Court decided *Davis*.

Standard of Review

West Virginia Code §29A-5-4(g) governs this Court's review the administrative decision of the Office of Tax Appeals ("OTA"). W. Va. Code §11-10A-19. Factual findings made by the Tax Department receive deference; Questions of law are reviewed *de novo*. The Court shall reverse, vacate or modify the order or decision of the agency if the substantial rights of the petitioners have been prejudiced because the administrative findings, inferences, conclusions, decision or order are:

(1) in violation of constitutional or statutory provisions; or

(2) in excess of the statutory authority or jurisdiction of the agency; or

(3) made upon unlawful procedures; or

(4) affected by other error of law; or

(5) clearly wrong in view of the reliable, probative ad substantial evidence on the whole record; or

(6) arbitrary or capricious or characterized by abuse of discretion or clearly unwarranted exercise of discretion.

W.Va Code §§29A-5-4(g). Guided by this standard, the Court has carefully considered the Memoranda of Law, oral argument, and pertinent legal authorities, and concludes the OTA decision must be reversed.

Analysis

West Virginia Code §11-21-12(c)(6) provides that the following shall be subtracted from a resident individual's adjusted gross income for tax purposes:

> Retirement income received in the form of pensions and annuities after the thirty-first day of December, one thousand nine hundred seventy-nine, under any West Virginia police, West Virginia Firemen's Retirement System or the West Virginia State Police Death, Disability and Retirement Fund, the West Virginia State Police Retirement System or the West Virginia Deputy Sheriff Retirement System, including any survivorship annuities derived from any of these programs, to the extent includable in gross income for federal income tax purposes.

W.Va. Code §11-21-12(c)(6).

Under the doctrine of intergovernmental tax immunity "[t]he imposition of a heavier tax burden on [those who deal with one sovereign] than is imposed on [those who deal with the other] must be justified by significant differences between the two

classes." *Davis*, 489 U.S. at 815, 816. Thus, a state tax law violates intergovernmental tax immunity if it treats state and local government employees more favorably than similarly situated federal government retirees, unless the inconsistent tax treatment is directly related to, and justified by, significant differences between the two classes. *See*, *Id; Barker v. Kansas*, 503 US 594,598 (1992).

Despite this clear precedent established by United States Supreme Court, the OTA instead applied *Brown v. Mierke*, 443 S.E.2d 462 (W.Va. 1994), claiming this West Virginia Supreme Court decision governs all claims of intergovernmental tax immunity in West Virginia. *Brown*, however, involved the determination of whether military retirees – a federal occupation which did not have a state counterpart identified in §11-21-12(c)(6) – were entitled to the state tax exemption. The fact that "the retirees failed to demonstrate that their job descriptions during any substantial part of their active service corresponded to the job descriptions of municipal firefights, municipal police officers, or state police officers" was a pivotal fact upon which our Court distinguished *Brown* from *Davis*. See, *Brown*, 443 S.E.2d 465.

The *Brown* Court further concluded that when a court is determining if discrimination exists, it is to look to the totality of the circumstances to ascertain whether the intent of the scheme was to discriminate against employees or former employees of the federal government as opposed to merely favoring state employees. Syl. Pt. 2, *Brown*, 443 S.E.2d at 465. Then, despite there being no such hurdle imposed by *Davis* and its progeny, the *Brown* Court deemed

§11-21-12(c)(6) non-violative of the intergovernmental tax immunity doctrine as applied to military retirees. *Brown* does not apply to the case at bar.

To begin, it is axiomatic that state courts are bound by the decisions of the United States Supreme Court. And the United States Supreme Court has held, in no uncertain terms, that when a state tax statute is alleged to violate the constitutional doctrine of intergovernmental tax immunity by favoring state employees over similarly situated federal employees, the proper inquiry is whether the inconsistent tax treatment is directly related to, and justified by, significant differences between the two classes. *See*, *Davis*, 489 U.S. at 816; *Barker*, 503 U.S. at 598. It is undisputed in the present matter that there are no significant differences between Mr. Dawson's powers and duties as a US Marshal and the powers and duties of the state and local law enforcement officers listed in §11-21-12(c)(6). Thus, unlike the military retirees in *Brown* who "failed to demonstrate that their job descriptions during any substantial part of their active service corresponded to the job descriptions of municipal firefighters, municipal police officers or state police officers..."[1] the job responsibilities of a US Marshall *are* substantially similar to the job responsibilities of state law enforcement officers. It is these pivotal similarities between the duties of state and federal law enforcement counterparts that bring this matter squarely within the purview of *Davis*.

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[1] *Brown*, 442 S.E.2d at 465.

Furthermore, the outcome in *Brown* may have been correct under the specific facts of that case, because §11-21-12(c)(6) only applies to law enforcement officers and firefighters, neither of which the *Brown* petitioners were. Hence, the reason they did not receive the exemption was because they were not law enforcement officers or firefighters. Mr. Dawson, however, *is*, but since he is a retired *federal* law enforcement officer rather than a retired *state* or *local* law enforcement officer who could receive social security benefits,[2] the OTA denied him the §11-21-12(c)(6) exemption.

During oral argument the respondent justified its decision, explaining that the Legislature crafted §11-21-12(c)(6) specifically to benefit the narrow class of *state* law enforcement officers. This type of inconsistent tax treatment is, however, unquestionably based on the source of one's retirement income and precisely the type of favoritism the doctrine of intergovernmental tax immunity prohibits. *See*, *Davis*, *supra*.

To the extent the OTA concluded that §11-21-12(c)(6) is constitutional based on the income differential between state and local law enforcement

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[2] Since the non-precedential decision of the Monongalia Circuit Court in *Dodson v. Palmer*, C.A. No. 00-C-AP-10 (2000) the OTA has only denied the exemption in §11-21-12(c)(6) to those federal law enforcement officers who are eligible to collect social security benefits, and has done so based solely on the false belief that the state and local law enforcement officers listed in §11-21-12(c)(6) are not eligible to collect social security benefits. In the pending matter, the OTA erroneously based its decision on the fact Mr. Dawson had paid into social security and could receive social security.

officers and their federal counterparts, this, too, was in error. The United States Supreme Court rejected this very notion in *Davis*, reasoning that

> [w]hile the average retired federal civil servant receives a larger pension than his state counterpart, there are undoubtedly many individual instances in which the opposite holds true. A tax exemption truly intended to account for differences in retirement benefits would not discriminate on the basis of the source of those benefits...rather, it would discriminate on the basis of the amount of benefits received by individual retires.

Davis, at 817. Had the West Virginia's Legislature intended 11-21-12(c)(6) to account for differences in income instead of differences in the source of income, it easily could have do so.

It is for these reasons, the Court concludes the underlying decision was affected by error of law, and the OTA's final decision violated the constitutional doctrine of intergovernmental tax immunity.

Ruling

1. The OTA erred in concluding that the West Virginia Supreme Court's decision in *Brown* rather than the United States Supreme Court's decision in *Davis* and its progeny control the outcome of this case.
2. West Virginia Code §11-21-12(c)(6), as applied in the case at bar, violates 4 U.S.C. §111 and the doctrine of intergovernmental tax immunity by favoring retired state and local law enforcement officers over retired federal law enforcement officers.

3. The OTA further erred to the extent it relied on differences between the pay scales of federal and state law enforcement officers to uphold the validity of §11-21-12(c)(6), and *Dodson v. Palmer*, C.A. No. 00-C-AP-10 (2000) to justify its exclusion of Mr. Dawson from exemption.
4. The OTA's decision is hereby **REVERSED**.
5. The circuit clerk shall provide a copy of this Order to counsel of record and remove the case from the docket.

ENTERED the 31 day of March 2016.

/s/ William J. Sadler
William J. Sadler, Judge 9th Circuit