

UNITED STATES DISTRICT COURT  
WESTERN DISTRICT OF MICHIGAN

KEWEENAW BAY INDIAN  
COMMUNITY, a federally-recognized  
Indian tribe, on its own behalf and as *parens*  
*patriae* for its members,

Plaintiff,

v.

ROBERT J. KLEINE, Treasurer of the State  
of Michigan; JAY RISING, former Treasurer  
of the State of Michigan; MICHAEL  
REYNOLDS, Administrator of the Collection  
Division of the Michigan Department of  
Treasury; WALTER A. FRATZKE, Native  
American Affairs Specialist of the Michigan  
Department of Treasury; and TERRI LYNN  
LAND, Secretary of State of Michigan,

Defendants.

Case No. 2:05-cv-0224

Hon. Gordon J. Quist

**DEFENDANTS' BRIEF IN**  
**OPPOSITION TO PLAINTIFF'S**  
**SECOND MOTION FOR**  
**SUMMARY JUDGMENT**

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**I. INTRODUCTION**

The Keweenaw Bay Indian Community (the Community) has filed this second motion for summary judgment of Counts I, II, and V. These counts relate to the 1993 and 1994 sales and use tax assessments by the State of Michigan and the offsets that occurred for those assessments in 1996 and 2005. The Community argues that the 1993 and 1994 assessments were not permitted by federal law, making both the assessments and the subsequent offsets to pay the assessments invalid. The Community, however, merely rehashes the arguments presented in its first motion for summary judgment and ignores the terms of the 1977 Tax Agreement, under which the Community agreed to pay the taxes in question, thereby waiving any rights under federal law to object to those taxes. The Community also makes unfounded assertions concerning sales taxes involving the Community as a retailer.

In addition, the Community contends that the 2005 offsets were improper because they involved federal funds that could not be offset under the Purpose Law, 31 U.S.C. §1301(a), or under the United States Treasury Offset Program created under the Debt Collection Improvement Act, 31 U.S.C. §3716. The Community's arguments largely rest on its assurance that no further authority need be provided because the principles it cites are "well-settled" or "axiomatic," terms that should prompt a skeptical review of this motion from the first instance. In reality, the Community's arguments are, at best, nothing more than a series of unsupported assumptions and misinterpretations of statutes that it has never before relied upon in its Complaint or in response to discovery. At worst, its brief is a studied attempt to direct the Court's attention away from the fact that Community has no valid claims concerning the 2005 Offsets.

Summary judgment in favor of the Community must be denied and summary judgment granted in favor of Defendants as argued in their briefs. Defendants incorporate by reference their previous summary judgment briefs without restating them fully in order to focus on the Community's newest arguments. In particular, Defendants refer the Court to the lengthy statement of facts with extensive documentary support in the Brief In Support of Defendants' Second Motion for Summary Judgment (Brief in Support of Defendants' Second Motion) (October 31, 2007), p 1-17, as well as the statement of law concerning when summary judgment should be denied in Defendants' Response to Plaintiff's [First] Motion for Summary Judgment (Defendants' Response to Plaintiff's First Motion) (November 22, 2006), p 9.

**II. THE COURT NEED NOT AND SHOULD NOT RULE ON THE VALIDITY OF THE 1993 AND 1994 SALES AND USE TAX ASSESSMENTS OR THE 1996 AND 2005 OFFSETS**

The Community contends that Defendants have raised their waiver and *Ex Parte Young*, 209 U.S. 123; 28 S.Ct. 441; 52 L.Ed. 714 (1908), arguments in relation to the 1993 and 1994 tax assessments because they cannot prevail on the merits. See Community's Memorandum in Support of Second Motion for Partial Summary Judgment (Community's Brief), p 15. That simply is not true, as explained in the following sections.

**A. Sovereign Immunity Protects States And Their Officials From Most Claims**

It bears repeating that the *Ex Parte Young* doctrine is an exception to a state's Eleventh Amendment sovereign immunity that permits only a very narrow class of claims pled against a state official acting in his official capacity that relate to *ongoing violations* of federal law and seek only *prospective injunctive relief*. See *Green v. Mansour*, 474 U.S. 64, 68; 106 S.Ct. 423; 88 L.Ed.2d 371 (1985). Counts I, II, and V (as well as other counts) go well beyond the limited scope of this exception by asking this Court to adjudicate past actions and grant monetary relief

in the form of tax refunds for the offsets. See *Big Horn County Elec. Co-op., Inc. v. Adams*, 219 F.3d 944, 954 (9th Cir., 2000) (holding that a refund of taxes improperly collected by a tribe is retrospective relief and not permitted under *Ex Parte Young*). While each of these counts seeks a declaration that Defendants are not entitled to take any further offsets to satisfy the 1993 and 1994 tax assessment, this question is moot: no future offsets need or could be taken concerning those assessments because the State of Michigan has already taken offsets to satisfy their full amounts. See *Papasan v. Allain*, 478 U.S. 265, 277-278; 106 S.Ct. 2932; 92 L.Ed.2d 209 (1986) (emphasizing that the Eleventh Amendment bars suit against a state official for conduct that occurred in the past and is not ongoing); see also *Green, supra* at 68 (holding that “compensatory or deterrence interests are insufficient” to justify permitting retrospective or monetary relief in the face of sovereign immunity). Nor has the Community even alleged that any further offsets based on these assessments are ongoing or imminent. Accordingly, the Community is not entitled to summary judgment on these counts because they raise claims grounded in past events and Defendants are therefore immune from them.

Defendants’ request that the Court decide this sovereign immunity issue before reaching the merits of the Community’s argument is not merely a strategic preference. Under *Nair v. Oakland County Community Mental Health Authority*, 443 F.3d 469, 476 (6th Cir., 2006), Defendants’ “litigation conduct,” *i.e.*, their choice to make immunity a “threshold defense” by moving for summary judgment on that ground more than a year ago (January 8, 2007), weighs heavily in favor of resolving that issue before addressing the merits of this case. Sovereign immunity presents the narrowest ruling with the broadest dispositive effect that the Court can make in this case involving such a lengthy complaint. See *id.* at 477 (addresses the merits because the defendant had asserted sovereign immunity only as an alternative theory, not a

threshold defense, and because the merits provided a narrower and more “straightforward” ground on which to resolve the case). Therefore, Defendants respectfully maintain that the Court should rule on the sovereign immunity defense before reaching the merits of these three Counts.

**B. The Community Has Waived All Claims Made in Counts I And II**

Likewise, waiver presents a narrow and efficient ground on which to resolve the counts concerning the 1993 and 1994 assessments and the offsets that occurred in 1996. While the Community has submitted a number of affidavits in response to the waiver argument, these affidavits do not contradict the essential facts Defendants have outlined regarding the substance of the representations made regarding the legitimacy of the 1993 and 1994 tax assessments and the Community’s desire to use them as a bargaining chip in tax agreement negotiations between 1997 and 2002. These affidavits only spin the meaning of, and authority for, the conduct by the Community and its representatives conceding that the 1993 and 1994 taxes were due and would be paid when a new tax agreement was negotiated. See Brief in Support of Defendants’ Second Motion, p 29-30. Not even current President LaFernier or former President Dakota deny in their affidavits that these representations were made. See Affidavits of Susan J. LaFernier, ¶9, and Fred Dakota, ¶14 filed In Support of Plaintiff’s Second Motion for Summary Judgment.

Even if the Court were not persuaded that the individual representations made by Gerald Hays and others concerning the Community’s conceded liability for these taxes were sufficient to constitute a waiver, the Community has not disputed Defendants’ evidence that it received notice in writing of its right to appeal the 2002 determination concerning the assessments and 1996 offsets, but failed to appeal. See Exs. BB, CC, DD attached to Brief in Support of Defendants’ Second Motion. The Community is not entitled to use the current litigation as a

collateral challenge to taxes for which it has already waived its right to object. Therefore, summary judgment in the Community's favor should be denied.

**III. THE 1993 AND 1994 SALES AND USE TAX ASSESSMENTS WERE LAWFUL AND THE COMMUNITY IS THEREFORE NOT ENTITLED TO HAVE SUMMARY JUDGMENT ENTERED IN ITS FAVOR FOR COUNTS I AND II**

According to the Community, the 1993 and 1994 tax assessments were invalid because a state government cannot impose a tax when its legal incidence falls on a Native American tribe for conduct within Indian Country unless Congress grants authority to impose the tax. Community's Brief, p 11. Because the assessments were invalid, the Community contends, so were the 1996 and 2005 Offsets that collected those assessments. *Id.*

Defendants agree that, subject to the exception discussed below, a Native American tribe is generally immune from the legal incidence of a state tax for conduct within its own Indian Country unless Congress grants the state the authority to impose the tax. *McClanahan v. State Tax Comm'n. of Arizona*, 411 U.S. 164, 170-171; 93 S. Ct. 1257; 36 L. Ed. 2d 129 (1973). However, Native American tribes may waive their rights not to be taxed under federal law in an express and unequivocal manner just as they may waive any other rights associated with their sovereignty. See *Merrion v. Jicarilla Apache Tribe*, 455 U.S. 130, 148; 102 S.Ct. 894; 71 L.Ed.2d 21 (1982) (acknowledging that, like other governments, a tribe may waive its "sovereign power through contract"). The only requirement is that the waiver of the sovereign right be "clear." *Oklahoma Tax Comm'n v. Citizen Band Potawatomi Tribe of Okla.*, 498 U.S. 505, 509; 111 S.Ct. 905; 112 L.Ed.2d 1112 (1991); see also *Merrion*, *supra* (stating that a tribe's sovereign rights must be "surrendered in unmistakable terms"). The Community has presented no authority suggesting that this ability to waive its sovereign powers excludes the right to consent to pay or collect taxes; its desire to negotiate a new tax agreement between 1997 and 2002

suggests that the Community itself maintains that, as a sovereign, it may decide to waive certain rights if doing so would be advantageous.<sup>1</sup>

The 1977 Tax Agreement, which was undeniably in effect for the 1993 and 1994 tax years, was a clear waiver of the Community's rights – whatever they may be – to refuse payment of the sales and collection of use taxes based on the Community's sovereignty. See 1977 Tax Agreement, attached as Ex. A to Complaint; see also Ex. C attached to Brief in Support of Defendants' Second Motion. Under the plain language of the 1977 Tax Agreement, the Community agreed that "all persons making retail sales within the exterior boundaries of the L'Anse Federal Indian Reservation must obtain a Michigan Sales Tax License." *Id.* at 4. The Community was not exempt from this requirement as evidenced by the fact that under the Tax Agreement the KBIT-C store owned by the Community was required to "become licensed for sales tax upon acceptance of this agreement." *Id.* at 3. The 1977 Tax Agreement also acknowledged that this requirement that "all persons" have a sales tax license would apply to future businesses the Community operated by referring to the only future business in contemplation at that time, which was the gasoline station to be operated by the Community. *Id.*

A sales tax license is the routine statutory method by which the State of Michigan

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<sup>1</sup> There is no question that states can enter into enforceable, negotiated agreements with tribes. *Nevada v. Hicks*, 533 U.S. 353, 393; 121 S.Ct. 2304, 150 L.Ed.2d 398 (2001) ("State governments may enter into consensual relationships with tribes, such as contracts for services or shared authority over public resources."). In fact, states and tribes can enter into enforceable agreements divvying up the most basic public resource – tax revenues. See *Citizen Band*, *supra* at 514 ("States may also enter into agreements with the tribes to adopt a mutually satisfactory regime for the collection of this sort of tax.") As the Supreme Court noted, these agreements are based on specific federal authority delegated to tribes to negotiate with state and local governments found in 25 U.S.C. § 476. Given the myriad grey areas in Indian tax law, allowing states and tribes to negotiate their respective rights and obligations for paying and collecting taxes can only be seen as sound public policy. The alternative is to require courts to assume full responsibility for every last detail of tribal-state tax law.

obligates a retailer to abide by all the provisions of the Sales Tax Act and the Use Tax Act, which includes the obligations to pay sales tax, collect use tax, and undergo audit. See Brief in Support of Defendants' Second Motion, p 2-3 (explaining relationship between M.C.L. §§ 205.53(2), 205.95(1), and 205.20). The Community did in fact apply for a sales tax license. See Ex. A attached to Brief in Support of Defendants' Second Motion.

The concluding section of the 1977 Tax Agreement, page 35, also acknowledged that its purpose was "to develop a *fair and workable policy* with respect to the interrelationship between the *taxing authority and responsibility* of the State of Michigan and those rights possessed by *members* of the Keweenaw Bay Indian Community to be exempt from the assessment of *certain* state taxes pursuant to treaty and other federal rights." Emphasis added. This language directly establishes that the purpose of the 1977 Tax Agreement was not merely to establish tax exemptions, but also necessarily the circumstances under which the Community agreed to pay or collect taxes. The Community was required to collect and pay tax, of course, only on "taxable sales" as defined by the Tax Agreement.<sup>2</sup> See 1977 Tax Agreement, p 2 (formula for excluding certain sales from refund because they were deemed nontaxable).

There are no magic words to be invoked to waive sovereign rights and allow a tribe to engage in commerce with non-tribal entities. See *Sokaogon Gaming Enterprise Corp. v. Tushie-Montgomery Associates, Inc.*, 86 F.3d 656, 659-660 (7<sup>th</sup> Cir., 1996) (rejecting argument that

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<sup>2</sup> In *Rising I*, the federal courts approved of the similar pre-payment and refund system that the State imposed on the Community for tobacco taxes in the period after the 1977 Tax Agreement expired, noting that pre-payment of a tax later refunded did not mean that a tax had been imposed. See *Keweenaw Bay Indian Community v. Rising*, No. 2:03-CV-111(W.D. Mich., Sept. 12, 2005) (opinion), available at 2005 WL 2207224, \*7-10. If such a scheme does not violate federal Indian law without the Community's express agreement for the tobacco tax, then the Community's written agreement to abide by a similar scheme for the sales and use taxes must also be permissible under federal Indian law.

waiver of sovereign immunity had to be stated explicitly as an “archaically, paternalistic purpose of protecting the tribe against being tricked” and making it more difficult to enter into “advantageous business transactions”); see also *C & L Enterprises, Inc. v. Citizen Band Potawatomi Indian Tribe of Oklahoma*, 532 U.S. 411, 121 S.Ct. 1589; 149 L.Ed.2d 623 (2001) (citing with approval statement in *Sokaogon, supra* at 660, that there is no authority for the proposition that a tribe must use the words “sovereign immunity” when waiving that immunity). Rather, it is enough for a tribe to agree clearly to conduct that it otherwise could not be forced to undertake because of its sovereign immunity. To suggest that the Community operated under the 1977 Tax Agreement for approximately 20 years but that it never waived immunity which would have allowed the State of Michigan a mechanism to actually receive taxes due is specious.

The Community evidently has anticipated that Defendants would raise this argument that the 1993 and 1994 tax assessments were valid under the 1977 Tax Agreement, which is why it has submitted a number of affidavits with attachments to its brief. These documents create red herrings for the Court, suggesting that the State should have refrained from auditing the Community during a time of internal turmoil, that the Community’s Chief Financial Officer had no authority to agree that the audits were accurate, that certain members of the Community understood the 1977 Tax Agreement to mean one thing or another, etc. Perhaps the only relevant information in these attachments is where the Community asserts that its Tribal Council was the body authorized to waive its sovereign immunities and its Tribal Council did pass a resolution authorizing the 1977 Tax Agreement. See Second LaFernier Affidavit, ¶6 and attached Tribal Council Resolution. Thus, there is no question that the 1977 Tax Agreement clearly and with the backing of the appropriate governmental body waived the Community’s immunity with respect to the 1993 and 1994 taxes to be paid or collected under the Agreement.

More importantly, the fact that the Community has submitted these documents should not be taken as evidence that summary judgment should be granted for the Community because the 1977 Tax Agreement failed to waive the Community's sovereign rights. As a contract, the 1977 Tax Agreement must be interpreted according to its plain language. See, generally, *Aetna Cas. & Sur. Co. v. Dow Chemical Co.*, 28 F.Supp.2d 440, 444 (E.D.Mich., 1998) (describing rules of contract construction). The Community's obligation to pay or collect the 1993 and 1994 sales and use taxes that were the basis for the assessments and offsets is apparent in the text of the 1977 Tax Agreement.

The Community's numerous affidavits are insufficient to establish as a matter of law that there was no waiver of sovereign immunity and that the 1993 and 1994 tax assessments were invalid as a result. First, the Community and the State operated under the terms of the 1977 Tax Agreement for almost twenty years, which conclusively proves that the Community did waive its sovereign rights regarding the taxes and had agreed to pay or collect the taxes and receive the refunds under the Agreement.<sup>3</sup> Second, the affidavits that the Community has filed speak to the affiant's personal understanding, not what the parties' understanding of the 1977 Tax Agreement, and they also disclaim the authority to speak on behalf of the Community on the question of waiver. See, e.g., Affidavit of Fred Dakota, ¶4, 8-11, 13 (personal "point of view" regarding the Agreement), ¶¶14-15 (conceding that his opinion did not bind the Community); see also Second LaFernier Affidavit, ¶8. These affidavits are not legally relevant to understanding the meaning of the contract. While Defendants do not believe that trial will be necessary in this

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<sup>3</sup> Contrary to the Community's suggestion, whether the State has entered into tax agreements *with other parties* drafted in a different manner than the 1977 Tax Agreement is irrelevant to understanding its meaning and effect. Community's Brief, p 15, n 12. This document is inadmissible and should not be considered. Fed. R. Evid. 402.

case because of its own motions for summary judgment, it would be improper to grant summary judgment to Defendants in relation to the 1993 and 1994 assessments and subsequent offsets based on the Community's claim that it did not waive sovereign immunity.

**IV. THE COMMUNITY IS NOT ENTITLED TO HAVE SUMMARY JUDGMENT ENTERED IN ITS FAVOR FOR COUNT V CONCERNING THE 2005 OFFSETS**

Since the State of Michigan took the 2005 Offsets, Defendants have consistently maintained that those offsets were taken pursuant to the State's common-law rights of a creditor, not pursuant to statute. For instance, when Defendant Fratzke wrote to the Community's attorney, John Baker, on June 28, 2005, he not only articulated this common-law right, he cited authority for it:

In general, the State has the right to offset funds in its possession in order to satisfy liabilities due and owing to it. See *Whispering Pines AFC Home, Inc. v. Department of Treasury and Department of Mental Health*, 212 Mich. App. 545; 538 N.W.2d 452; 1995 Mich. App. [Ex. MM, attached to Brief in Support of Defendants' Second Motion.]

The Community acknowledged that this is the claimed basis for the 2005 Offsets in its Complaint at paragraph 44. This right to common-law offsets is recognized in long-standing precedent that follows *United States v. Munsey Trust Co.*, 332 U.S. 234, 239; 67 S.Ct. 1599; 91 L.Ed. 2022 (1947). See Brief in Support of Defendants' Second Motion, p. 24 and Reply Brief in Support of Defendants' Second Motion for Summary Judgment (December 28, 2007), p. 3 (discussion and additional authority). The Community has never cited authority that overrules this precedent or holds that the common-law right was abrogated by statute. Rather, as explained below, the Community merely cites statutes that address some element of federal appropriations and federal offsets, without making the requisite demonstration that these statutes apply to Defendants and have the effect of barring common-law offsets. Therefore, summary judgment

in the Community's favor should be denied.

**A. The Community Failed To Plead A Claim Upon Which Relief Can Be Granted Concerning The 2005 Offsets In Count V**

Paragraph 81 of the Complaint states the Community's theory of liability in Count V, explaining, "The 2005 Offsets of federal program funds are invalid as a matter of federal law and violate the Supremacy Clause in Article VI of the United States Constitution because such offsets violate the terms and purpose of the federal statutes and regulations to which the federal program funds relate and violate general federal law restrictions on federal appropriations." There is no more explanation of the legal basis for this theory, not even a single citation to either of the statutes on which the Community relies to move for summary judgment.

In *Lillard v. Shelby County Bd. of Educ.*, 76 F.3d 716, 726 (6th Cir., 1996), the Sixth Circuit explained the minimum standard that applies to pleading a claim:

A complaint need not set down in detail all the particularities of a plaintiff's claim, but must simply give the defendant *fair notice of what the plaintiff's claim is and the grounds upon which it rests*. It is plain that, although liberal, *the standard does require that a plaintiff plead more than bare legal conclusions*. In practice, a . . . complaint must contain either direct or inferential allegations respecting all the material elements to sustain a recovery under some viable legal theory. [Emphasis added, text omitted in original, internal citations and quote marks omitted.]

Count V was inadequate to state a claim because it substantively consists of a single sentence that utterly fails to articulate the "federal law" that the 2005 Offsets allegedly violated and, therefore, was an alleged violation of the Supremacy Clause. See, generally, *Morgan v. Church's Fried Chicken*, 829 F.2d 10, 12 (6th Cir., 1987) (stating that a court need "not accept as true legal conclusions or unwarranted factual inferences" in similar analysis of a motion to dismiss under Fed. R. Civ. P. 12(b)(6)). Even considering the facts that were pleaded concerning

the 2005 Offsets in the introductory sections of the Complaint, there was nothing there or in the conclusory sentence in ¶81 that hinted at the legal basis for Count V. Whether that was because the Community had yet to develop its legal theory or because it was leaving itself options is immaterial. Defendants were denied the fair notice to which they are entitled and for this reason alone, summary judgment in favor of the Community should be denied.<sup>4</sup>

Additionally, Defendants cannot be said to have been fairly apprised of the basis for Count V outside of the Complaint. In March 2007, Defendants served their second set of discovery requests on the Community. Interrogatory 23 asked the Community to

[i]dentify all factual and legal grounds on which you rely to support the assertion made in paragraph 81 . . . that the 2005 Offsets violate the terms and purposes of the federal statutes and regulations referenced and the general federal law restrictions on federal appropriations. **Include specific references to all statutes and regulations and restrictions** and fully describe how Plaintiff would apply that law to the relevant facts to show the offsets violate the terms and purposes of those statutes and regulations and restrictions. [See **Ex. A**, Excerpts from Community's Response to Second Discovery Requests, p 39 (emphasis added).]

To answer Interrogatory 23 the Community referred back to its answer to Interrogatory 22. See **Ex. A**, p 39. The answer to Interrogatory 22, however, does not provide a single citation to any of the statutes or other authority that the Community now asserts in its Memorandum in Support of Second Motion for Partial Summary Judgment (Community's Brief). See **Ex. A**, p. 36-38.

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<sup>4</sup> The Community's failure to cite any authority in support of its proposition that these statutes barred the State of Michigan from taking the 2005 Offsets is further evidence that Defendants are entitled to qualified immunity for the 42 U.S.C. §1983 claim against them in Count VI. Without authority that these statutes abrogate the common-law right to offset and elevating the offset issue to a constitutional level, the Community cannot establish that Defendants violated a clearly established constitutional right. See *Higgason v. Stephens*, 288 F.3d 868, 876 (6th Cir., 2002) (articulating qualified immunity test). Additionally, the Community's failure or refusal to identify these statutes in discovery denied Defendants the opportunity to address the argument more fully in their Second Motion for Summary Judgment. Finally, the fact that it took the Community this long to enunciate some legal basis for its asserted claim establishes that the so-called "rights" it claims were violated are far from "clearly established."

Rather, the answer to Interrogatory 22 is a rambling statement of conclusory assertions repeated verbatim for each type of funds that were offset. The Community merely said that the funds for each program “must be used for the purposes specifically prescribed in the federal law governing the program” and “Defendants had no legal authority to withhold the funds from the Community.” See **Ex. A**, p. 36-38. Not once did the Community cite the Purpose Law, 31 U.S.C. §1301(a), a statute concerning federal appropriations, any section of the Debt Collection Improvement Act in its answer to Interrogatory 23 or 22, or any case law concerning common-law offset rights.

**B. Even If Properly Pleaded, The 2005 Offsets Did Not Violate The Purpose Law, 31 U.S.C. §1301(a)**

The Community contends that the 2005 Offsets violated the Purpose Law, 31 U.S.C. §1301(a), which states, “Appropriations shall be applied only to the objects for which the appropriations were made except as otherwise provided by law.” According to the Community, the funds that were offset in 2005 were earmarked for the Community and “[t]he Community was required under federal law to use the federal funds to administer tribal government programs and to provide direct benefits to Community members and other Native Americans in the Community’s service area.” Community’s Brief, p. 16 (emphasis added).

Defendants have no position concerning whether the Community was restricted in how *it* spent the money Congress appropriated. However, if the spending obligation that follows federal appropriations were imposed *on the Community* under 31 U.S.C. §1301(a), it leaves unanswered why Defendants were at all obligated to take or refrain from any particular action under the statute. The only hint that the Community gives is that the money could not be spent on the “Michigan Department of Treasury” because Treasury is not a beneficiary of any of these

federal programs. Community's Brief, p. 16-17. However, the Community did *not* spend the money on the "Michigan Department of Treasury" and Defendants do not claim that the State of Michigan or Department of Treasury were beneficiaries of the funds under the individual federal programs. Rather, the State of Michigan was the creditor for Community's tax debt and it exercised its common-law right to offset the funds as they passed through its computerized system before the funds reached the Community and could be expended by the Community.

The primary goal of 31 U.S.C. §1301(a) is to prevent power struggles over money and the budget process within the federal government. See, generally, *American Federation of Government Employees, AFL-CIO, Local 1647 v. Federal Labor Relations Authority*, 388 F.3d 405, 408-409 (3rd Cir., 2004) (explaining background of Appropriations Clause in litigation involving 31 U.S.C. §1301(a) and reimbursement of civilian employee expenses at Department of Defense facility); *F.D.I.C. v. Hurwitz*, 384 F.Supp.2d 1039, 1093 (S.D.Tex., 2005) ("Congress specifies the amount, purpose, and time for spending appropriated funds. Even if a deal between agencies may save money or generate other benefits, *agencies may spend appropriated funds only as Congress says.*") (emphasis added); *Cobell v. Norton*, 263 F.Supp.2d 58, 65 (D.D.C., 2003) (ordering defendant federal agencies to continue paying costs of federal master out of general fund money appropriated by Congress). Allowing a state to enforce its common-law right to offset debts does nothing to interfere with the obedience Congress requires of the agencies that receive earmarked appropriations.

The Community does not cite a single case holding that a common-law offset of federal funds by a state to satisfy a tax debt violates 31 U.S.C. §1301(a). Nor does it posit any interpretation of the text of 31 U.S.C. §1301(a) that would bar an offset by a state. The text of 31

U.S.C. §1301(a) says nothing about offsets by any federal or state agency, much less when federal funds may be offset by states to satisfy state tax debts. This statute is directed at executive agencies that spend appropriated funds, and prohibits them from ignoring the directions of Congress in that regard. Once an agency has disbursed the funds, the statute has no application. Accordingly, the Community is not entitled to have summary judgment granted in its favor for Count V on this unpleaded theory.

**C. Even If Pleaded Properly, The 2005 Offsets Did Not Violate The Debt Collection Improvement Act, 31 U.S.C. §3716**

The Community argues that Congress passed § 3716 of the Debt Collection Improvement Act (DCIA), 31 U.S.C. § 3716, in order to “authorize the United States Department of Treasury (Treasury) to offset federal payments for the purpose of collecting delinquent debts owed to the United States or to States” and to prohibit such offsets in certain circumstances. Community’s Brief, p 17-19. The Community argues that because the *federal government* would have been prohibited from taking the 2005 Offsets by the DCIA, it is “axiomatic under the Supremacy Clause of the U.S. Constitution that state governments are also forbidden to offset these exempt federal program funds.” *Id.* at 19. In this instance, however, “axiomatic” must be read to mean “having no support whatsoever in the case law, statutory language, or federal regulations.”

Here, even if the Community is correct that the federal government could not have taken the offsets in question (it is less than clear that this is the case), saying that it is “axiomatic” that states would also be barred from taking offsets is not a persuasive legal argument. See *Meridia Prods. Liab. Lit. v. Abbott Labs.*, 447 F.3d 861, 867-868 (6th Cir., 2006) (emphasizing that parties must adequately develop arguments and citing authority to the effect that arguments mentioned in passing and without authority are deemed waived). The Community has pleaded

no authority to support its argument because there is none. As a result, the Community has failed to carry its burden as the movant for summary judgment. See, generally, *Aetna Cas. and Sur. Co. v. Dow Chemical Co.*, 28 F.Supp.2d 421, 435 (E.D. Mich., 1998) (failure to “set forth *the law* and the facts relevant to the issue” grounds for denying summary judgment) (emphasis added).

More importantly, whether acting intentionally or negligently, the Community has failed to inform the Court that 31 U.S.C. § 3716 – the very section on which it relies for its argument – states in subsection (d), “Nothing in this section is intended to prohibit the use of any other administrative offset authority existing under statute or common law.” In other words, Congress clearly intended to preserve the common-law rights of offset already exercised by governments when it enacted the DCIA. The Community does not provide any authority to dispute that Michigan has a common-law right of offset and should be denied summary judgment for that reason.

Nor should the Court accept even the Community’s overview of the scope and effect of the DCIA and the United States Treasury Offset Program (TOP) authorized under the DCIA because it is critically deficient. TOP is used solely by the Financial Management Service to offset nontax debts owed to the United States. See 31 U.S.C. § 3701(a)(8) (defining “nontax”); 31 U.S.C. § 3701(d) (excluding tax debts from “administrative offset”); 31 U.S.C. § 3711(g)(1) (requiring only “a nontax debt or claim owed to the United States [that] has been delinquent for a period of 180 days” to be referred to Treasury for collection); 31 U.S.C. § 3716(6) (allowing “administrative offset” of “legally enforceable nontax debt”); 31 C.F.R. § 285.4(b) (defining “debt” to exclude tax debt); see also **Ex. B**, FMS, *Congressional Staff Handbook: Debt*

*Collection* (March 2006) <<http://www.fms.treas.gov/news/handbook/index.html#debt>>, p 11 (“FMS serves as the government’s central debt collection agency, managing the government’s non-tax delinquent debt portfolio. One of the key tools used by FMS to collect delinquent debt is the Treasury Offset Program[.]”). While Treasury developed a special program to collect state income tax debts in 2000 that offsets federal income tax refunds, it has no program to collect debts that are for other types of state taxes. See 31 C.F.R. § 285.8(b); see also **Ex. B**, p 11.

The Community should have known that tax debts are excluded from the DCIA not only because it is so prominently stated in the statutes and regulations, but because it is also listed in the table that lists program payments exempt from offset that the Community cites in its brief at page 18-19. See FMS, Debt Management Services, *Treasury Offset Program Payments Exempt from Offset By Disbursing Officials* (June 2006) <<http://fms.treas.gov/debt/dmexmpt.pdf>> (exempting “[p]ayments under the tariff laws” governed by Treasury). The Community’s theory that Defendants are liable for the 2005 Offsets because they are bound to follow the same requirements imposed on the federal government in the DCIA (specifically 31 U.S.C. § 3716) and administrative rules must fail because, among other reasons, the DCIA would never apply to this type of debt.

The Community’s argument that Congress intended to limit a state’s ability to collect debts independent of the processes outlined in the DCIA – and the “administrative offset” provisions in particular – is also meritless because the DCIA does not provide the exclusive method for collecting even nontax debts owed to the United States, as 31 U.S.C. § 3716(d) suggests. In other words, the Community’s theory is simply that the State would have been prevented from doing what the federal government could not do under the DCIA. However,

because the DCIA does not limit the manner in which the federal government collects the debts owed to it, it cannot limit the manner in which states attempt to collect debts owed to them. For instance, the DCIA refers to several other methods of debt collection that make it unnecessary to send the debt to Treasury for collection. See 31 U.S.C. §3711(g)(2)(A); see also 31 U.S.C. §3711(g)(9). The federal agencies may even collect the debts through an “internal offset” of their own funds without sending the debt to Treasury for collection. See 31 C.F.R. § 285.12(d)(1)(v) and (d)(4). Even after Treasury is asked to collect the debt it may seek collection through other methods and agencies. See 31 U.S.C. §3711(g)(4). Once these other methods fail to collect the debt, then Treasury “*may* collect the claim by administrative offset.” 31 U.S.C. § 3716(a) (emphasis added). Reviewed as a whole, the DCIA sets forth an expansive menu of options for collecting debts that does not limit the federal government and, therefore, should not be interpreted to limit state governments.

Furthermore, the fact that a state must formally enter into a reciprocal agreement to collect debts owed to the United States before Treasury will attempt to collect the state’s debt is evidence that whatever limits might exist in the DCIA and the “administrative offsets” under TOP do not apply to limit state collection practices by the operation of law. See 31 U.S.C. § 3716(h)(1)(B). Rather, states must formally agree to be bound by any such limitations in the DCIA. *Id.* However, the State of Michigan has never entered into a reciprocal agreement that would bind them to follow the DCIA or its debt collection requirements, including requirements for an “administrative offset” under TOP. In fact, when the State of Michigan took the offsets in 2005, not one of the fifty states had any such reciprocal agreement. See **Ex. C**, Government Accounting Office, *Financial Management: State and Federal Governments Are Not Taking Action to Collect Unpaid Debt through Reciprocal Agreements*, GAO-05-697R (August 25,

2005) <<http://www.gao.gov/htext/d05697r.html>>, p 2. Because Michigan had not entered into a reciprocal agreement under the DCIA, Defendants cannot be held liable even if they did not follow the requirements or limits that might exist in the DCIA. In any event, even if Michigan had entered into a reciprocal agreement, it would have been intended only to ensure that Treasury obtains the “benefit” of having the state collect federal debts and to prevent “duplicative efforts” at debt collection, not to limit Michigan’s ability to collect its own debts with its own methods. See 31 C.F.R. § 285.1(c).

Finally, if this Court were to conclude that the DCIA and TOP somehow applied to Defendants, it would still have to deny summary judgment in favor of the Community because its argument that the 1993 and 1994 tax assessments are not “legally enforceable” has no merit. According to the Community, the State of Michigan could not take the 2005 Offsets because the 1993 and 1994 tax assessments were not a “legally enforceable debt” under its theory that they were barred by federal law and not permitted under the 1977 Tax Agreement. As noted above, that argument fails because the tax assessments were permitted under the 1977 Tax Agreement. More importantly, the Community fails to inform the Court that the DCIA regulations define the term “legally enforceable debt” as follows:

Legally enforceable refers to a characteristic of a debt and *means there has been a final agency determination that the debt, in the amount stated, is due, and there are no legal bars to collection by offset.* Debts that are not legally enforceable for purposes of this section include, but are not limited to, debts subject to the automatic stay in bankruptcy proceedings or debts covered by a statute that prohibits collection of such debt by offset. For example, if a delinquent debt is the subject of a pending administrative review process required by statute or regulation, and if collection action during the review process is prohibited, the debt is not considered legally enforceable for purposes of this section. . . . [31 C.F.R. § 285.12(c)(3)(i).]

Under this definition, the 1993 and 1994 tax assessments were “legally enforceable” in 2005

because the Michigan Department of Treasury had already issued its final determination concerning the assessments in 2002 and there were no other pending proceedings to challenge that determination, not even with respect to the interest that the State had charged.

Irrespective of the documents that the Community has filed in support of this motion, summary judgment cannot be granted in the Community's favor on Count V because it does not state a claim on which it could ever be entitled to judgment as a matter of law. See Fed. R. Civ. P. 56(c) ("The judgment sought should be rendered if the pleadings, the discovery and disclosure materials on file, and any affidavits show that there is no genuine issue as to any material fact and that the *movant is entitled to judgment as a matter of law.*") (emphasis added). In other words, by failing to state a claim in the Complaint, the Community has made it impossible to determine what elements it must prove with its documentary evidence in order to be entitled to summary judgment. See, generally, *Winfield Collection Ltd. v. Gemmy Industries Corp.*, 311 F.Supp.2d 611, 613-614 (E.D. Mich., 2004) (discussing analytical relationship between evidence submitted in support of motion for summary judgment and the "essential element[s] of the cause of action"). The Community is not entitled to use this omission to its advantage.

V. **CONCLUSION**

Defendants respectfully request that this Court deny summary judgment to Plaintiffs and, instead, grant summary judgment in their favor, along with any other relief it believes just and equitable.

Respectfully submitted,

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