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IN THE UNITED STATES DISTRICT COURT

FOR THE EASTERN DISTRICT OF CALIFORNIA

STATE OF CALIFORNIA, ex rel. ROB BONTA, in his official capacity as Attorney General of the State of California, Plaintiff, **v.** **AZUMA CORPORATION, et al.,** Defendants.	2:23-cv-00743-KJM-DB **REPLY BRIEF IN SUPPORT OF DEFENDANTS' MOTION TO DISMISS**

This case turns on whether the facts elevate the State's interests in licensing Indians in Indian country above the federal and tribal interests in protecting tribal sovereignty and economic development. The State has not alleged sufficient facts to state a claim for relief that is plausible on its face. *Ashcroft v. Iqbal*, 556 U.S. 662, 677 (2009) (the facts pleaded must show the claim is more than just possible). The allegations do not contain facts which enable the Court to decide, under *White Mountain Apache Tribe v. Bracker*, 448 U.S. 136 (1980), that the State may overcome the presumption that its laws do not apply to Indians operating in Indian country. Instead, the State offers a "legal conclusion couched as a factual allegation" that the Tribal Retailers are consumers because they do not hold a State license. *Iqbal* at 678. Nor does the Complaint allege that the Defendants are engaged in third-party delivery services for Azuma, or that Azuma owes a tax. After stripping away the State's conclusory statements, it failed to state a claim on which relief can be granted.

Further, the State has not carried its burden to establish that the Court has subject matter jurisdiction to determine the rights of Indians in this case. *McNutt v. General Motors Acceptance Corp. of Indiana, Inc.*, 298 U.S. 178, 189 (1936) (the party invoking federal jurisdiction carries the burden throughout the case). The Defendants each enjoy tribal sovereign immunity, those sued in their individual capacities enjoy qualified official immunity and the Tribal Retailers enjoy the sovereign immunity of their respective Indian tribes.

For both reasons above, the Court should grant the Motion to Dismiss.

ARGUMENT

I. Defendants' Conduct Does Not Fall Within § 376a Regulations.

The State's First Claim alleges that the Defendants violate the PACT Act's provisions regulating delivery sales pursuant to 15 U.S.C. § 376a.[1] But the State's conclusory allegations fail to establish that this statute applies to the Defendants. Section 376a regulates "delivery sales," which are remote sales to "consumers." §§ 376a, 375(4), 375(5). §§ 376a(a)-(d) (regulating delivery sellers) & 376a(e) (regulating third-party delivery services). Thus, the State's burden is to allege

[1] Hereafter, code references are to Title 15 of the United States Code unless otherwise stated.

facts that the Defendants engage in delivery sales to consumers (§§ 376a(a)-(d)) or provide third-party delivery services for a delivery seller (§ 376a(e)(2)).

a. Defendants do not engage in delivery sales.

A delivery sale includes both a delivery seller and a consumer. §§ 375(5) & 375(6). The Complaint alleges that the "Defendants are 'delivery sellers'" that deliver cigarettes to Tribal Retailers who the State alleges are "consumers." Complaint ¶¶ 67, 69, 70. The State's recitation of the elements in 376a, coupled with conclusory statements that Azuma's deliveries are to a consumer, cannot survive this Motion to Dismiss. *Iqbal*, 556 U.S. at 678.

The State alleges that an unlicensed Tribal Retailer is a consumer, without offering facts that the State's licensing regime applies to Tribal Retailers which are otherwise exempt from the definition of a consumer. The PACT Act defines a "consumer" as not including "any person lawfully operating as a manufacturer, distributor, wholesaler, or retailer of cigarettes or smokeless tobacco." § 375(4)(B). The State asserts, without analysis, that the Defendants bear the burden of proving the Tribal Retailers are lawfully operating to exempt them from the definition of a consumer. Opposition p. 26:10-14. The State's assertion is betrayed by the text of the statute. The definition of consumer is a conjunctive test which requires proof of two elements: that the purported consumer "purchases cigarettes" *and* is not "lawfully operating as a manufacturer, distributor, wholesaler, or retailer of cigarettes." § 375(4)(A)-(B).[2] The State must establish that there is a consumer as an element of its claim, and it is therefore the State's burden to prove that the Tribal Retailers are not lawfully operating under *applicable* law.

The State has not alleged a factual basis for applying its licensing statutes to the Tribal Retailers as Indians purchasing and selling cigarettes in their own Indian country (see below). Ultimately, Azuma's sales to Tribal Retailers are not delivery sales and are not subject to the regulations and prohibitions at § 376a. Therefore, the State's First Claim should be dismissed.

[2] The definition states: "The term 'consumer' (A) means any person that purchases cigarettes or smokeless tobacco; and (B) does not include any person lawfully operating as a manufacturer, distributor, wholesaler, or retailer or cigarettes or smokeless tobacco."

b. Defendants are not third-party delivery services.

The State also makes conclusory allegations that the "Defendants" violate § 376a(e)(2), which regulates third-party delivery services.[3] Complaint ¶ 75. The State does not allege that the Defendants engage in third-party deliveries *for* Azuma. Rather, the State alleges that the Defendants *are* the delivery seller and its agents. Complaint ¶¶ 68, 65-66, 75. The delivery seller cannot violate § 376a(e)(2), which only applies to third parties that deliver packages *for* a delivery seller on the PACT Act list. § 376a(e)(2); *see also* § 376a(e)(9)(D) (exempting common carriers from subsections (a)-(d)); § 376a(d) (regulating deliveries made by delivery sellers). The State's First Claim should be dismissed because the State has not alleged that the Defendants act in a third-party capacity.[4]

II. The Tribal Retailers Are Not Consumers Under the PACT Act.

With allegations that obfuscate what activity is allegedly conducted by who and where, the State attempts to create a "consumer" where none exists. But the State must allege with sufficient clarity why State licensing laws apply to the Tribal Retailers before it can plausibly assert that their alleged noncompliance makes them "consumers" under the PACT Act.

The State begins its Opposition argument by asking this Court to apply its "comprehensive statutory scheme" involving licensing, preemptions, recordkeeping, assurances, and other obligations (Plaintiff's Opposition to Defendant's Motion to Dismiss ("Opposition") pp. 1:11-5:10) to Indian "manufacturers, importers, wholesalers, distributors, and retailers" (Opposition p. 3:4-6). *See* Opposition p. 12:24-27. This broad-brush approach is not consistent with "well-settled" law. Opposition p. 12:25. Rather, it violates the presumption that states cannot impose their policy priorities on Indian tribes operating in Indian country through civil regulation of otherwise lawful

[3] More broadly, § 376a(e)(2) applies to third parties that participate in the delivery of a package. For brevity, reference herein is to "delivery services" as a term that encompasses all third parties that make deliveries.

[4] The State also sued the individual defendants in their capacity as elected officials of the Alturas Indian Rancheria ("AIR"). However, the Complaint does not allege that AIR or the individual defendants in their official capacity on behalf of AIR deliver packages for Azuma. Nor does the State allege how Defendants Del Rosa or Rose complete any delivery in their individual capacity, rather than in a capacity as agents of Azuma.

activity. *Okla. Tax Com'n v. Sac and Fox Nation*, 508 U.S. 114, 128 (1985) ("we presume against a State having the jurisdiction to tax within Indian country"); *see also Confederated Salish & Kootenai Tribes of Flathead Reservation v. Moe,* 392 F.Supp. 1297, 1307 (D. Mont. 1974) (the State may not require a Tribal Retailer "to possess its cigarette dealer's license") (aff'd 425 U.S. 463 (1976)).

a. The State has not alleged facts that show the Tribal Retailers are not lawfully operating in their own Indian country.

A bedrock principle of federal Indian law is that states cannot impose civil regulatory schemes on Indian tribes and tribal members operating within their own Indian country. *See California v. Cabazon Band of Mission Indians,* 480 U.S. 202 (1987). The State agrees that whether a state regulation infringes on tribal sovereignty "depends on *who* is being regulated… and *where* the activity to be regulated takes place." Opposition, p. 11:12-14; *Big Sandy Rancheria Enters. v. Bonta,* 1 F.4th 710, 725 (9th Cir. 2021). The Court must engage in a "particularized inquiry" into whether the Tribal Retailers (the who) are subject to the State's comprehensive regulations while operating in their own Indian country (the where). *Id*. (quoting *Bracker,* 448 U.S. at 145).

A decision evaluating one set of facts cannot be used to "determine whether, in [another] context, the exercise of state authority would violate federal law." *Bracker* at 145. Disregarding the Supreme Court's decision, the State attempts to import *Big Sandy*'s conclusions as a presumption that the Tribal Retailers are not lawfully operating. *See, e.g.*, Opposition pp. 14:5-7 & 23:22-24:4. However, *Big Sandy* addressed a tribally owned distributor *operating outside of its own Indian Country,* and thus subject to non-discriminatory State law. *Big Sandy* at 726. In sharp contrast, the State's PACT Act claims here depend on whether the Tribal Retailers, *who operate within their own Indian Country*, are subject to the State's licensing scheme. As *Big Sandy* recognized, an entirely different "analytical framework" applies in this alternative context. *Id*. at 725.

The Tribal Retailers purchase and sell cigarettes in their own Indian country and "state law is generally inapplicable." *Id*. (citing *Bracker* at 144). The State cannot apply its licensing regime to this on-reservation conduct. *Moe,* 392 F.Supp. at 1307. Requiring the Tribal Retailers to obtain State licenses would "hinder the [parent Tribe's] ability to govern its territory and members by

prohibiting" the Tribal Retailers from purchasing off-directory and tax-exempt cigarettes inside their own Indian country. *Cf. Big Sandy* at 729 and 730 (applying the Directory Statute to "sales activities *off the Rancheria*"). Likewise, the State's requirement that Tribal Retailers, operating in their own Indian Country, purchase cigarettes only from a State-licensed distributor (Opposition p. 3:6-7) constitutes an invalid attempt to regulate Indians in Indian Country. Even if this requirement could be considered the regulation of a non-Indian in Indian Country, it is only valid if the State's interests outweigh federal and tribal interests under the *Bracker* balancing test. *Okla. Tax Comm'n v. Chickasaw Nation*, 515 U.S. 450, 459 (1995); *Big Sandy*, 1. F.4th at 725 ("[W]hen a state 'asserts authority over the conduct of non-Indians engaging in activity on the reservation,' courts must conduct 'a particularized inquiry into' and balance the 'state, federal and tribal interests at stake.") (quoting *Bracker*, 448 U.S. at 145). In applying *Bracker*, the State's interests do not outweigh the tribal interests within a market created by, and incident to, the tribes' gaming enterprises. Complaint, Exhibit L, ECF 1-12 at p. 5; Ferris Decl., ECF 23-4 at ¶ 10. *See, e.g., Cabazon*, 480 U.S. at 219-220; *Wash. v. Confederated Tribes of Colville Indian Reservation*, 447 U.S. 134, 156 (1980) (tribal interests are "strongest when the revenues are derived from value generated on the reservation by activities involving the Tribes and when the taxpayer is the recipient of tribal services.").[5]

The State has not met its burden of alleging facts that establish the Tribal Retailers are not lawfully operating under *applicable* law, and its First Claim should be dismissed. Regardless, to the extent the State asks this Court to apply *Bracker* to its proposed licensing of the Tribal Retailers, those entities must be able to defend themselves as parties to this case so that they can bring their own arguments based on actual experience, instead of relying on Defendants to guess what tribal interests are at stake and what burdens they face. Because the Tribal Retailers cannot be joined under Rule 19, the claim should be dismissed.

[5] Even if the balance of interests could favor the State under the *Bracker* test, the comprehensive licensing regime alleged by the State—avoiding its conclusory statements—does not evidence a minimal burden for the collection of valid taxes on non-Indians. Rather, the license requirements alone are unlawful as applied in this context. Defendants' Opposition, ECF 23 at pp. 21-24.

III. The CCTA Does Not Apply to Azuma's Transportation of its Own Cigarettes.

The State alleges that the Defendants transport "contraband cigarettes" in violation of the CCTA. Complaint ¶ 79. The CCTA applies to the transportation of cigarettes when a state tax is owed but not paid. 18 U.S.C. §§ 2342(a) & 2341(2). The State's allegations are based on the incorrect conclusion that State law applies. The State cannot tax products that are only transported across State land.

a. The Commerce Clause precludes the State's proposed tax based on transportation of Azuma's products.

The Commerce Clause prohibits states from taxing goods that are merely being transported through the State. Interjurisdictional taxes on goods are prohibited under the Commerce Clause unless, *inter alia*, there is a substantial nexus with the taxing state, the tax is fairly related to the services the state provides, and the tax does not discriminate against interjurisdictional commerce. *See South Dakota v. Wayfair, Inc.*, 138 S.Ct. 2080, 2091 (2018).[6] This constitutional prohibition applies with the same force to jurisdictional boundaries between tribal nations and states as it applies to jurisdictional boundaries between states. U.S. Const., art. I, sec. 8, cl. 3 (reserving to Congress the power "to regulate commerce with foreign nations, among states, and with the Indian tribes.") (emphasis added).

The substantial nexus test parallels the minimum contacts test under the Due Process Clause. *Wayfair*, 138 S.Ct. at 2091, 2093. More specifically, some part of the sale must be consummated within the State before a sales (or other) tax on the goods is valid. *See Okla. Tax Com'n v. Jefferson Lines, Inc*., 514 U.S. 175, 184 (1995). There is no substantial nexus in this case because no part of the sale occurs outside of Indian country.

The tax must also apply to conduct fairly related to the services the State provides. While the State may impose a tax for services related to such transportation (e.g., taxes funding roadwork), that is not the type of tax the State seeks to apply. Rather, the State is attempting to apply a tax to the goods themselves and not simply the transportation of those goods. As explained in *Jefferson*

[6] Although *Wayfair* dealt with vastly different facts, it reformed the substantial nexus test and is cited as the most current Supreme Court precedent.

Lines, if Azuma's products were transported across several states which applied the same tax on the goods carried, the goods themselves would be unconstitutionally subjected to more than one State's tax. *Id*. at 185.

Finally, the tax must not discriminate against interjurisdictional commerce. The State does not apply a tax to goods that are merely transported through the State in interstate commerce. *See* 18 Cal. Code Regs. §§ 1620(a)(2)(B) (sales tax does not apply to out-of-State orders "sent by the purchaser directly to the retailer at a point outside this state"); *see also McDonnell Douglas Corp. v. Franchise Tax Bd*., 26 Cal.App.4th 1789, 1796 (2d D.C.A. 1994) (deliveries of products in California but destined for use outside of California are not taxable). A discriminatory tax on Indian sellers that send orders directly to a retailer in Indian country is unconstitutional.

b. No tax is owed before Azuma delivers its products, and the CCTA does not apply.

The CCTA prohibits the transportation of "contraband" cigarettes. The State improperly substitutes the word "contraband" for "untaxed" throughout its Complaint and Opposition. These terms are not synonymous, because the CCTA defines contraband cigarettes as only those that, *inter alia*, (a) "bear no evidence of the payment of *applicable* State or local cigarette taxes" **and** (b) are not in the possession of "a person holding a permit… as a manufacturer of tobacco products… or an agent of such person." 18 U.S.C. § 2341 (emphasis added).

The State admits that Azuma holds the required manufacturing permit, Complaint ¶¶ 8 & 41, and the individual Defendants are agents of Azuma. Complaint ¶¶ 10, 65-66; 75. Escrow payments are not a tax, *HCI Distribution, Inc. v. Hilgers*, --- F.Supp.3d ---, 2023 WL 3122201, *6 (D. Neb. 2023),[7] and the State concedes its other cigarette taxes attach "to the first taxable use, sale, or consumption," Opposition p. 2:2-3; *see id.* at *13-14 (discussing *King Mountain Tobacco Co., Inc. v. McKenna*, 768 F.3d 989 (9th Cir. 2014)).[8] The State also does not allege facts on which the

[7] If the escrow payments are a tax, they are "categorically barred." *Id*. at *5.

[8] The State's reliance on *City of New York v. Gordon*, 1 F.Supp.3d 94 (S.D.N.Y. 2013) is misplaced. Because unlike in *Gordon*, where the cigarettes were contraband while in the possession of the seller, Azuma's cigarettes are not contraband while in its possession, and Azuma does not lose possession of the cigarettes until it makes its own deliveries to the Tribal Retailers. 18 U.S.C. § 2341(2)(A).

Court could conclude that Azuma's cigarettes are sold to non-Indians that leave Indian country and might be taxable.[9] The State cannot establish under either prong that Azuma's untaxed cigarettes are contraband, so Azuma's transportation of untaxed cigarettes does not violate the CCTA. The State's Second Claim should be dismissed.

IV. The Tribal Retailers and Their Parent Indian Tribes Are Necessary and Indispensable Parties to This Litigation Under Rule 19.

The State's burden to prove that there is a consumer will require this Court to issue a decision that affects the rights and obligations of the Tribal Retailers. The State must prove (1) that the State may lawfully require Tribal Retailers to obtain a State license, (2) that the State may require Tribal Retailers to purchase cigarettes only from a State-licensed entity, and ultimately (3) that the Tribal Retailers are operating unlawfully. These questions also strongly implicate the interests of the Tribal Retailers' parent Indian tribes, which exercise sovereign governmental and regulatory jurisdiction over the Tribal Retailers. None of the Defendants are sued in any retail capacity, and each of the Tribal Retailers is owned by another sovereign, so the State cannot plausibly claim that their interests are already protected by the Defendants.

Rule 12(b)(7) allows a defendant to assert that an absent person is necessary and indispensable; it does not require the absent person to appear for itself to claim an interest.[10] *See Provident Tradesmen Bank & Trust Co. v. Patterson*, 390 U.S. 102, 110-111 (1968) and *Republic of Philippines v. Pimentel*, 553 U.S. 851, 861 (2008) (Court may dismiss a suit *sua sponte* where a sovereign indispensable party cannot be joined). The State does not contest that the Tribal Retailers enjoy sovereign immunity. Therefore, the Court must dismiss the State's First Claim because it

[9] To the contrary, the State attaches to its Complaint information demonstrating that Azuma's cigarettes are sold at tribally owned casinos in Indian Country, Complaint, Ex. L, ECF 1-12 at p. 3. "[W]hen the complaint is accompanied by attached documents, such documents are deemed part of the complaint and may be considered in evaluating the merits of a Rule 12(b)(6) motion." *Durning v. First Boston Corp.*, 815 F.2d 1265, 1267 (9th Cir.), *cert. denied*, 484 U.S. 944 (1987).

[10] The State's suggestion that the absent parties must claim an interest to be protected by Rule 19 is contrary to law. *See American Greyhound Racing v. Hull*, 305 F.3d 1015 (9th Cir. 2002); *Shermoen v. U.S.*, 982 F.2d 1312 (9th Cir. 1992); *McShan v. Sherrill*, 283 F.2d 462 (9th Cir. 1960); *compare United States v. Bowen*, 172 F.3d 682, 689 (9th Cir. 1999) (a party *with notice* that *chooses* not to claim an interest may not be necessary and indispensable).

cannot join the Tribal Retailers and/or their parent Indian tribes. *See Pimentel*, 553 U.S. at 8617 (requiring dismissal where a sovereign indispensable party cannot be joined).

V. The Defendants Have Immunity from State Suit.

a. The individual Defendants are immune in their capacity as elected government officials.

The State concedes that *Ex parte Young* applies only to acts of government officials that violate federal law. Opposition p. 22:3-5. But the State does not allege that Del Rosa or Rose perform any act in the scope of their official duties as elected members of AIR's government which violates federal law. *See* Complaint ¶ 64. The simple fact that AIR's Business Committee has regulatory control over Azuma does not turn governmental acts into acts of the purportedly regulated entity, Azuma (or vice versa). The State merely conflates the two without explanation.

b. Azuma is immune as an arm of the tribe.

Although the State agrees that determining whether Azuma is an arm of the Tribe is "a multi-factor" test, it only disputed Defendants' evidence regarding one of the five *White* factors. *White v. Univ. of Cal.*, 765 F.3d 1010, 1025 (9th Cir. 2014). Opposition p. 14:18, *et seq.* The State thus concedes that the Defendants have satisfied the other four factors. In the one factor disputed by the State, it disparages AIR's reinvestment of Azuma revenues in business opportunities, but federal courts have already agreed that development of a tribal economy for a California Indian tribe establishes a valid financial relationship under the *White* factors. *See Breakthrough Mgmt. Grp. Inc. v. Chukchansi Gold Casino and Resort*, 629 F.3d 1173, 1195 (2010). As stated in the Del Rosa Declaration, AIR reinvests Azuma revenues into other tribal economic development opportunities. *Cf.* Opposition p. 15:8-9, 17-19 (claiming the Defendants only reinvest in Azuma and do not show where its profits go). The Plaintiff's weak attempt to address only one factor by mischaracterizing the facts demonstrates that Azuma is immune to suit as an arm of the Tribe.

CONCLUSION

For the reasons stated herein, the State's federal claims should be dismissed. Upon dismissal of the federal claims, the Court should decline to exercise supplemental jurisdiction over the State's state-law claims.

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Respectfully submitted,

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