

CSX, the 4-R Act, and the State of Alabama



All Taxpayers are Equal, but Some
Taxpayers are More Equal Than Others

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Presented at:

46th Annual Conference and Committee Meetings
Multistate Tax Commission
July 22-24, 2013 San Diego, California

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Railroads sue Alabama in Federal Court

- CSX Transportation, Inc., sought a preliminary injunction and a determination that the application of the state's sales and use tax laws to CSX's purchase, storage, and use of diesel fuel violated the Federal Railroad Revitalization and Regulatory Reform Act of 1976 (the "4-R Act")
- Norfolk Southern Railway Company also brought an identical action against the state
- State and CSX agreed that the outcome of Norfolk control the outcome of CSX
- Injunction is denied in Norfolk and Norfolk appeals to the 11th Circuit

AL sales tax / excise tax law

- Alabama imposes a 4% tax on the retail sale of tangible personal property and the storage, use, or consumption of tangible personal property in the state, including diesel fuel. § 40-23-2(1) & 61 (a), Ala. Code 1975.
- Alabama imposes a \$0.19 / gallon excise tax on purchases of diesel fuel for on-road use. Purchases of diesel fuel that are subject to the excise tax are exempt from the sales and use taxes. § 40-17-2(1) & 220(j), Ala. Code 1975.

Alabama sales tax / excise tax as applied to diesel fuel

Entity	4% sales / use tax	\$0.19/gallon motor fuel excise tax
Railroads	Purchase, storage, consumption, or use	Exempt
Motor carriers	Exempt, provided that excise tax is paid	Purchase
Intrastate water carriers	Purchase, storage, consumption, or use	Exempt
Interstate water carriers	Exempt	Exempt

Federal 4-R Act

- Passed by Congress in 1976
- Designed to restore the financial stability of the railway system
- Key to achieving the goals of the Act was a prohibition on discriminatory state taxation of railroads, in particular railroad property

4-R Act Anti-discrimination provisions

Section 11501(b) The following acts unreasonably burden and discriminate against interstate commerce, and a State, subdivision of a State, or authority acting for a State or subdivision of a State may not do any of them:

- (1)** Assess rail transportation property at a value that has a higher ratio to the true market value of the rail transportation property than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction has to the true market value of the other commercial and industrial property.
- (2)** Levy or collect a tax on an assessment that may not be made under paragraph (1) of this subsection.
- (3)** Levy or collect an ad valorem property tax on rail transportation property at a tax rate that exceeds the tax rate applicable to commercial and industrial property in the same assessment jurisdiction.
- (4)** Impose another tax that discriminates against a rail carrier providing transportation subject to the jurisdiction of the Board under this part.

What does it mean to discriminate?

Federal Circuit Courts are split on the definition of the appropriate class for comparison

	Functional Approach	Competitive Approach
Circuits	Fifth, Seventh, Ninth	Eighth, Eleventh
Members of Class	Commercial and industrial users	Railroads, motor carriers, water carriers
Statutory interpretation approach	Language of (b)(1)-(3) used to inform reading of (b)(4).	(b)(4) read independently. 4-R Act designed to ensure railroads remain competitive
Key considerations	Is the tax a broad-based tax? Are a sufficient number of local entities included in tax? Does burden of tax fall almost exclusively on railroads?	Are railroads treated less favorably than their main competitors?

Norfolk, 550 F.3d 1306 (11th Cir. 2008)

- Question was whether the state's exemptions for motor carriers and water carriers from the sales / use tax on diesel fuel are discriminatory under the 4-R Act
- Eleventh Circuit held that exemptions from a generally applicable tax were not subject to challenge under the 4-R Act
- Eleventh Circuit relied heavily on Dep't of Revenue v. ACF Indus., Inc., 510 U.S. 332 (1994)

ACF Industries

- Property tax exemption case
- SCOTUS held that “a State may grant exemptions from a generally applicable ad valorem property tax without subjecting the taxation of railroad property to challenge under [§ 11501(b)(4) of the 4-R Act]
- Stated another way, § 11501(b)(4) does not prevent states from exempting nonrailroad property, but not railroad property, from ad valorem taxes of general application

ACF Industries

Keys to ACF Industries decision

- The 4-R Act specifically addresses taxes, but does not address exemptions
- States' traditional power to provide exemptions to property tax
- Common for states to exempt certain commercial property at the time of enactment of the 4-R Act
- “Principles of federalism”

ACF Industries applied to Norfolk

- Alabama's sales and use tax is a generally applicable tax – no targeting of railroads
- Nothing in the plain language of the 4-R Act that it was intended to reach tax exemptions of any type
- SCOTUS did not limit the ACF Industries holding to ad valorem taxes, so it also applies to sales and use taxes
- As with property tax exemptions, sales and use tax exemptions were commonplace at the time of the enactment of the 4-R Act
- Principles of federalism

Back to CSX

- Federal district court dismissed the CSX case based on the outcome of Norfolk
- CSX appealed to the 11th Circuit, which affirmed based on Norfolk
- CSX then petitioned SCOTUS for certiorari, which SCOTUS granted, framing the question as:

“Whether a State’s exemptions of rail carrier competitors, but not rail carriers, from generally applicable sales and use taxes on fuel subject the taxes to challenge under 49 U.S.C. § 11501(b)(4) as ‘another tax that discriminates against a rail carrier.’”

SCOTUS – never mind ACF

- Eleventh circuit misunderstood ACF Industries
- ACF Industries concerned a challenge under subsection (b)(4) to a property tax exemption that was granted to non-railroad entities
- Court reasoned that allowing this challenge under subsection (b)(4) was inconsistent with the express provisions of subsections (b)(1) – (3) allowing such exemptions
- “Structural analysis” in ACF Industries is not applicable in determining whether a non-property tax can be challenged as discriminatory under subsection (b)(4)

SCOTUS – never mind ACF

Viewing § 11501(b)(4),

- Section 11501(b)(4) is a catch-all, designed to encompass any non-property tax
- Look to the “ordinary meaning” of the word discrimination – “failure to treat all persons equally when no reasonable distinction can be found between those favored and those not favored”
- Charging one group of taxpayers a lesser rate of tax, or exempting them from a tax, when the groups are similarly situated, constitutes discrimination under § 11501 (b)(4) against the group paying the higher rate, absent sufficient justification

SCOTUS – implications, stated and unstated

- Exemptions from non-property taxes can be challenged as discriminatory under the 4-R Act
- SCOTUS did not address what would constitute justification of disparate treatment of groups of taxpayers or whether the court could consider the state's broader taxing scheme
- SCOTUS declined to address whether the “similarly situated groups of taxpayers” was properly represented by the functional approach or the competitive approach”

District Court on remand

- Competitive approach defines correct comparison class
- Burden of proof is on CSX to show discriminatory effect of exemptions
- Court will look beyond the tax at issue to compensatory taxes in determining whether exemptions for competitors are justified

District Court on remand – state wins!

Sales and use tax exemptions do not discriminate against railroads

Motor Carriers

- Motor carriers pay fuel excise tax, which is roughly equivalent to the sales and use tax

Water Carriers

- CSX offered no evidence as to discriminatory effect of the exemption for interstate water carriers
- Interstate water carriers are not similarly situated to railroads because of potential constitutional concerns

11th Cir. after remand – taxes are hard

- Competitive approach defines the correct comparison class
- Burden shifts to the state to justify exemptions once the railroad has made a prima facie case of discrimination
- Build a box around the sales and use tax; do not look outside the box
- Too complex to consider other components of a state's tax scheme

Railroad's competitors received favorable treatment via sales and use tax exemptions; therefore, the exemptions violate the 4-R Act.

Supreme Court Again (CSX II)

- Main opinion authored by Scalia, 7-2 (Ginsburg and Thomas dissent)
- CSX was correct on the comparison class issue. Comparison class can consist of CSX competitors, not all general and commercial taxpayers, as the State had urged

Supreme Court Again (CSX II)

- BUT, the State was right when it suggested the motor fuel tax motor carriers pay *could* justify otherwise prohibited discrimination
- Case was remanded to 11th Circuit to determine whether the motor fuels tax justifies the discrimination suffered by CSX in paying sales tax on diesel fuel

Supreme Court Again (CSX II)

- Difficulty of carrying out the inquiry is no excuse; it's a difficulty imposed by the language of (b)(4).
- Potential offset by sales tax cannot be a justification when considering water carriers, which pay neither tax.
- Remanded to 11th Circuit to examine State's other arguments re: water carriers

Supreme Court Again (CSX II)

- Thomas continues his dissent from the prior case
- He believes (b)(4), as a catchall provision, should have used the same comparison class as (b)(1) through (b)(3), and would have ruled for the State

Supreme Court Again (CSX II)

- Next steps:
 - 11th Circuit Remand
 - Whether motor fuels tax imposed on motor carriers can immunize sales tax imposed on railroads
 - Whether State's arguments regarding water carrier total exemption are reasonable

Case Citations

Functional Approach

Kansas City S. Ry. v. McNamara, 817 F.2d 368, 374 (5th Cir. 1987).

Kansas City S. Ry. v. Koeller, 653 F.3d 496 (7th Cir. 2011).

Atchison, Topeka, and Santa Fe Ry. v. Arizona, 78 F.3d 438 (9th Cir. 2011).

Competitive Approach

Burlington Northern, Santa Fe Ry. v. Lohman, 193 F.3d 984 (8th Cir. 1999).

CSX Opinions and Other Important Cases

Department of Revenue of Oregon v. ACF Indus., Inc., 510 U.S. 332 (1994).

Norfolk Southern Ry. v. Alabama Dep't of Revenue, 550 F.3d 1306 (11th Cir. 2008).

CSX Transp., Inc. v. Alabama Dep't of Revenue, 131 S.Ct. 1101 (2011)

CSX Transp., Inc. v. Alabama Dep't of Revenue, 892 F.Supp.2d 1300 (N.D. Ala. 2012).

CSX Transp., Inc. v. Alabama Dep't of Revenue, 2013 WL 3286156 (11th Cir. 2013).

CSX Transp., Inc. v. Alabama Dep't of Revenue, SCOTUS, slip op., March 14, 2015