

# Significant Kentucky Tax Cases in 2020

## Dentons SALT Insights

What's going on with Kentucky tax cases in 2020? Let us take a look...

### **Should the U.S. Supreme Court Consider *Testa v. Great Lakes Minerals*?**

The issue here is whether a Kentucky taxpayer can contest an out-of-state assessment in Kentucky. So far the answer is no, but the taxpayer is asking the United States Supreme Court to weigh in.

The Kentucky Supreme Court provided the background for its holding in *Ohio and Testa v. Great Lakes Minerals, LLC*, 597 S.W.3d 169 (Ky. 2019), *reh'g denied* (Apr. 30, 2020):

Great Lakes ... is a mineral processing company that sells minerals to buyers at its Greenup County, Kentucky plant. Great Lakes maintains that it sells its products in Kentucky; all transactions, including payment and delivery of goods, occur in Kentucky; Great Lakes does not have a physical presence in Ohio; and Great Lakes neither directly nor indirectly delivers its products to the State of Ohio.

From a taxpayer's perspective, one can sympathize with Great Lakes. It's a 100% Kentucky company and neither directly nor indirectly delivers its products to Ohio. Why then Great Lakes asks should it be forced to go to Ohio to contest an assessment? From Ohio's perspective, the State of Ohio imposes its CAT tax and provides procedures to contest a CAT assessment issued by Ohio:

Stated very simply, Ohio has created a commercial activity tax (CAT) that taxes persons who do business and have a substantial nexus to Ohio. O.R.C.2 5751.02(A). Ohio's Department of Taxation (Department) may issue a CAT assessment to an out-of-state business for outstanding liability to Ohio arising from transactions with an Ohio company. Businesses are provided administrative remedies to protest CAT assessments to the Tax Commissioner of Ohio, then the Ohio Board of Tax Appeals, and then the Ohio appellate courts. O.R.C. 5751.09; O.R.C. 5717.02; ORC 5717.04.

Great Lakes petitioned the United States Supreme Court in July 2020 to grant *certiorari* to review the Kentucky Supreme Court's published decision. Interestingly, the Kentucky Supreme Court heard the appeal directly from Greenup Circuit Court where Great Lakes sued the State of Ohio and Joseph W. Testa, Ohio's Tax Commissioner, in his official and individual capacities. Great Lakes sought: (1) a declaratory judgment that it is not subject to Ohio's CAT; (2) monetary relief pursuant to 42 U.S.C. § 1983 for the forced collection of taxes not owed, in violation of the Ohio and United States Constitutions; and (3) a determination that it would be inequitable to require Great Lakes to defend an action in Ohio, a foreign state. Ohio and Testa moved to dismiss Great Lake's Complaint, which the Circuit Court denied, and so, Ohio moved to transfer the case directly to the Kentucky Supreme Court, which

considered the appeal of Ohio and Testa, focusing on sovereign immunity and comity and thus not reaching the merits of Great Lakes' claims.

The Kentucky Supreme Court, citing *Franchise Tax Bd. of California v. Hyatt*, 139 S. Ct. 1485 (2019), held that "the State of Ohio is protected by sovereign immunity, and Great Lakes' claims against it should have been dismissed." Citing to *Kentucky v. Graham*, 473 U.S. 159 (1985), the Court held that, "Testa is entitled to the same sovereign immunity that protects the state of Ohio, and therefore Great Lakes' claims against him in his official capacity should have been dismissed." The Court then turned to whether immunity protected Commissioner Testa in his personal capacity. It held, "[W]e believe that Ohio's state courts are better suited to efficiently evaluate and apply Ohio law to this issue. Should the case progress further, Ohio's courts would also be better suited to evaluate the facts, and to consider whether Testa caused the deprivation of a constitutional right while acting under the color of Ohio state law. Accordingly, relying on the principle of comity, we hereby dismiss Joseph Testa in his personal capacity."

Great Lakes' Petition for Certiorari to the United States Supreme Court asks three questions. Two of the questions focus on Great Lakes' claims against the Ohio Tax Commissioner and the Kentucky Supreme Court's holding that dismissed them, *i.e.*, whether a state's sovereign immunity extends to a state official sued in their individual capacity and whether comity supports a dismissal. Should the United States Supreme Court take up this case, it would generally open the door to in-state lawsuits against out-of-state tax officials. That would upend the status quo.

Great Lakes' other question asks, "Whether an individual or business that does not have sufficient minimum contacts to be subject to the jurisdiction of a foreign state may seek declaratory or injunctive relief within their home state." Great Lakes describes the underlying action as "a Kentucky action for Declaratory and other equitable relief to determine whether a Kentucky company has minimum contacts or a substantial nexus with the State of Ohio to be subject to a foreign tax." Great Lakes argues, "To allow a Kentucky court to determine the minimum contacts issue now, rather than years from now, benefits all parties by preventing unnecessary years of litigation costs."

The taxpayer's Petition distinguishes this case from the *Hyatt* decision, arguing that Great Lakes should be permitted to defend itself in Kentucky:

The Court's decision in *Franchise Tax Bd. of California v. Hyatt*, 129 S.Ct. 1485 (2019) clearly prohibits an individual or business from using the courts of its home state to offensively seek monetary redress against another state, but the question in this case is whether an individual or business can file a defensive equitable action to prohibit unconstitutional wrongs being committed against it in its home state. The equitable resolution and decision based upon the precedent of each of the states involved and the federal courts, is that Great Lakes should be permitted to defend itself in Wurtland, Kentucky.

The United States Supreme Court accepts state cases that have decided an important federal question in a way that conflicts with the decisions of state high courts or federal courts of appeal or with its decisions. It seems that the issues in this case are important, given that the Kentucky Supreme Court granted a direct appeal. But, do they conflict with other decisions? Great Lakes argues that they do. On the other hand, Ohio believes otherwise and indicated that it would not respond to Great Lakes' *certiorari* petition.

The United States Supreme Court accepts very few cases for review. Will the Court accept this case? Should they? What do you think?

### **Property Tax Evidentiary Rules 101**

In *Kroger Ltd. P'ship I v. Boyle Cty. Prop. Valuation Adm'r*, No. 2019-CA-000935-MR, 2020 WL 4722042 (Ky. App. Aug. 14, 2020), the Kentucky Court of Appeals considered Kroger's appeal of the assessment value of one of its stores for real property tax purposes and in so doing laid out evidentiary rules for a real property tax case at the Kentucky Claims Commission.

As to evidence, Kroger offered the expert testimony and appraisal report of a certified property appraiser employing two approaches to value the property: the sales comparison approach and the income approach. The PVA presented testimony of the PVA who relied on a summary report prepared by the Kentucky Department of Revenue using a cost approach.

The Court of Appeals opined that the PVA's valuation is an evidentiary presumption that must be presumed correct unless rebutted by competent evidence. Once Kroger presented such evidence, *i.e.*, the expert testimony and appraisal report, the presumption disappeared. Kroger not only presented evidence supporting a contrary value, but also presented evidence which cast doubt on the assumptions relied upon in the PVA's assessment. Kroger's evidence was sufficient to rebut the statutory presumption of the validity of the PVA's assessment. Nevertheless, Kroger retained the ultimate burden of proof and risk of non-persuasion to establish the value of the property. As long as the PVA relied upon a properly supported valuation, the Commission was not obligated to accept the valuation provided by Kroger's expert. However, the Court of Appeals agreed with Kroger that the PVA failed to carry its burden of going forward with evidence to establish that the PVA's valuation of Kroger's property was competent and reliable. Accordingly, the Court held for Kroger.

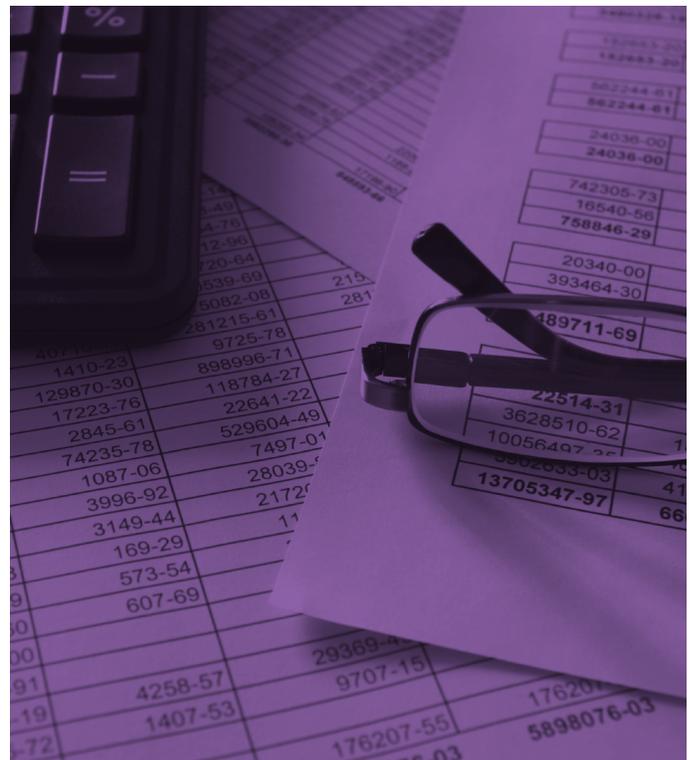
In *Kroger v. Boyle PVA*, the Court of Appeals provides a concise summary of evidentiary rules applied to a typical real property tax dispute.

### **Judges Get Sued Too - Dep't of Revenue v. Shepherd, No. 2019-SC-000104-MR (Ky. Feb. 20, 2020)**

The Kentucky Department of Revenue filed a petition for a writ of prohibition in the Court of Appeals to prohibit the Franklin Circuit Court from requiring KDOR to disclose what KDOR considered to be confidential taxpayer information. In the underlying case, a Kentucky non-profit mutual ownership corporation that manages, operates, acquires, and owns housing units sued a utility seeking a declaratory judgment that the non-profit was exempt from state sales tax on utilities. The utility requested a Technical Advice Memorandum (TAM) from KDOR but KDOR issued a Private Letter Ruling (PLR) instead, finding that the utility services were commercial, not residential, so that the utilities were not tax exempt. The non-profit served KDOR with a complaint and sought the TAM request letter. KDOR sought a protective order which the Circuit Court initially denied but then after KDOR sought a writ from the Court of Appeal, vacated its own order as moot, since the non-profit had obtained the KDOR-related documents from the utility. Because of this, the Court

of Appeals denied KDOR's petition for writ as moot. But, KDOR appealed to the Kentucky Supreme court arguing that exceptions to the mootness doctrine applied. The Kentucky Supreme Court, however, held that neither the capable of repetition, yet evading review nor the public interest exceptions applied.

One can discern from this case that KDOR will strongly resist turning over what it considers to be taxpayer information. Interestingly, had KDOR issued a TAM instead of a PLR, KDOR would have presumably posted the TAM on its website. And, under KDOR Revenue Procedure KY-RP-19-03 (Oct. 1, 2019), a redacted version of the PLR would have been posted on KDOR's website, though this would not have been the case for PLR's issued prior to October 1, 2019.



### **Kentucky Supreme Court Review Requested in Rent-A-Center (denied) and Ridge (pending)**

Cases continue to wind their way up from the Kentucky Court of Appeals to the Kentucky Supreme Court. The Kentucky Supreme court declined to review *Dep't of Revenue, Fin. & Admin. Cabinet v. Rent-A-Ctr. E., Inc.*, No. 2017-CA-001653-MR, 2019 WL 3059900 (Ky. App. July 12, 2019), *review denied* (July 1, 2020); that case involved a taxpayer's use of the methodology of a settlement agreement with KDOR. The Kentucky Supreme Court is still considering whether it will review *Ridge v. Fin. &*

*Admin. Cabinet, Dep't of Revenue*, No. 2018-CA-001517-MR, 2019 WL 3850790 (Ky. App. Aug. 16, 2019); the *Ridge* case involves the question of whether Kentucky can tax the severance income of a Tennessee-resident former employee who was based in Kentucky when employed.

### **Tax Cases Worth Watching**

There are several property tax cases winding their way through the Kentucky Claims Commission, the Circuit Courts and the Court of Appeals. It seems like property taxes are an area in which taxpayers and Property Valuation Administrators are finding themselves in disagreement.

Manufacturing sales tax exemptions are always a hot issue. Currently, the Court of Appeals is considering *Century Aluminum pf Kentucky, GP v. Dep't of Revenue*, No. 2020-CA-0301, which concerns the manufacturing supplies exemption. The case is currently being briefed.

Most of the time, taxpayers and the government agree on what is and how much is subject to tax, what is exempt, what the procedures are, etc. And, when they do not initially agree, in many, indeed in most, instances, taxpayers and tax authorities can find common ground to come to an agreement. But, in those few instances in which they do not agree, there are a civil ways and venues to resolve them, and these disputes are often quite interesting.

This is a modified version of Mark A. Loyd's regular column, *Tax in the Bluegrass*, "Significant Kentucky Tax Cases in 2020" which appeared in Issue 4, 2020 of the Kentucky CPA Journal.



## STATE AND LOCAL TAX TEAM



**Mark A. Loyd**  
Chair, Tax Department  
[mark.loyd@dentons.com](mailto:mark.loyd@dentons.com)



**Scott Clark**  
Partner  
[scott.clark@dentons.com](mailto:scott.clark@dentons.com)



**Bailey Roesse**  
Partner  
[bailey.roesse@dentons.com](mailto:bailey.roesse@dentons.com)



**Brett J. Miller**  
Partner  
[brett.miller@dentons.com](mailto:brett.miller@dentons.com)



**Stephanie Bruns**  
Managing Associate  
[stephanie.bruns@dentons.com](mailto:stephanie.bruns@dentons.com)



**Jeffrey T. Bennett**  
Partner  
[jeff.bennett@dentons.com](mailto:jeff.bennett@dentons.com)



**Brad Hasler**  
Partner  
[bradley.hasler@dentons.com](mailto:bradley.hasler@dentons.com)



**Kelli A. Wikoff**  
Partner  
[kelli.wikoff@dentons.com](mailto:kelli.wikoff@dentons.com)



**Kimberly M. Nolte**  
Associate  
[kimberly.nolte@dentons.com](mailto:kimberly.nolte@dentons.com)

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