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## Kentucky, 49 Other States and Friends of the Court File Briefs in Supreme Court Municipal Bond Taxation Case

On July 19, 2007, the State of Kentucky filed its brief in *Davis v. Kentucky Department of Revenue of the Finance and Administration Cabinet*, urging the U.S. Supreme Court to reverse a Kentucky appellate court's early 2006 ruling, based on the "dormant" Commerce Clause of the U.S. Constitution, holding unconstitutional a statute exempting municipal bond interest from Kentucky's income tax only if the municipal bonds are issued in Kentucky. Kentucky's brief argues that state sovereignty differentiates each state from every other state and from private participants in commercial transactions for purposes of the Commerce Clause, and permits each state to use its tax statutes to lower the borrowing costs on bonds issued by such state and its political subdivisions, without requiring that a state provide similar tax advantages for municipal bonds issued by or in other states.

Tax statutes similar to the challenged Kentucky statute are in effect in 42 states (4 of those states exempt some but not all in-state municipal bonds, but tax all out-of-state municipal bonds), and a Supreme Court affirmance of the Kentucky court's decision in *Davis* would lead to the invalidation of such statutes. Accordingly, both public and private participants in the municipal bond industry are following the case closely, and various such participants, or associations representing such participants, filed friend-of-the-court, or *amicus*, briefs on July 19th in support of Kentucky's position and the current structure of the municipal bond market. Such *amicus* briefs were filed by:

- **The State of North Carolina, joined by 48 other states.** This filing is noteworthy, as the plaintiffs in the *Davis* case argue that Kentucky-type statutes discriminate against public issuers trying to sell their bonds to residents of other states.

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The briefs submitted by Kentucky and the 49 other states indicate that all 50 states, including states that have no state income tax or that do not tax in-state bonds differently from out-of-state bonds, support the challenged taxation practice, or at least a state's right to implement a tax that favors its own municipal bond issuers.

- **The National Association of State Treasurers.** NAST previously filed an *amicus* brief urging the Supreme Court to review the lower court decision in *Davis* because of its importance to the municipal bond market. NAST has now filed a brief on the merits of the case, supporting Kentucky and Kentucky-type tax statutes.
- **The Government Finance Officers Association.** The GFOA filed a brief supporting Kentucky on behalf of itself, **the National Governors Association, the National League of Cities, the National Conference of State Legislatures, the National Association of Counties, the Council of State Governments, the U.S. Conference of Mayors, the International Municipal Lawyers Association and the International City/County Management Association.**
- **The Multistate Tax Commission.** The MTC is the administrative agency of the Multistate Tax Compact and includes 47 states in its membership. The Multistate Tax Compact exists for the purposes of facilitating equitable taxation of multistate taxpayers and promoting uniformity and compatibility among state tax systems.
- **The Securities Industry and Financial Markets Association.** SIFMA represents over 650 securities firms, banks and asset managers.
- **Nuveen Investments, Inc.** Nuveen sponsors open-end and closed-end single-state municipal bond mutual funds for 23 states, including Kentucky. Its *amicus* brief asserts that an affirmance of the Kentucky court decision would adversely impact single-state funds, and virtually all of the other briefs submitted suggested that single-state funds would largely disappear from the municipal bond market if states are constitutionally required to give out-of-state municipal bonds identical tax treatment as in-state municipal bonds.
- **Churchill Tax-Free Fund of Kentucky, Hawaiian Tax-Free Trust, Narragansett Insured Tax-Free Income Fund, Tax-Free Fund for Utah, Tax-Free Fund of Colorado, Tax-Free Trust of Arizona, Tax-Free Trust of Oregon,**

**Hawaii Municipal Fund, Hawaii Intermediate Fund, The Idaho Tax-Exempt Fund, Ocean State Tax-Exempt Fund, Bishop Street Hawaii Municipal Bond Fund and Westcore Colorado Tax-Exempt Fund.** These 13 single-state municipal bond funds include seven from the Aquila Group of Funds, four single-state funds from the First Pacific fund group, and four single-state funds that are unaffiliated with the other represented funds.

- **Dupree Mutual Funds.** Dupree operates eight single-state municipal bond funds in Kentucky, Tennessee, Alabama, Mississippi and North Carolina.

In addition to the eight *amicus* briefs filed in support of Kentucky, the **National Federation of Municipal Analysts (NMFA)** filed an *amicus* brief in support of neither party. Unlike the other *amicus* briefs, NFMA's brief does not address the constitutional law question presented by the *Davis* case, but instead is intended to inform the Supreme Court about the structure of the existing municipal bond market and the potential impact on the municipal bond market, state issuers and investors of a decision invalidating Kentucky-type state tax statutes. The brief asserts that such an invalidation would cause billions of dollars of losses to holders of municipal bonds issued in high-tax "specialty" states and would adversely affect market access by smaller municipal issuers.

Briefs from the Davises, the taxpayers challenging the constitutionality of Kentucky's tax statute, and from parties interested in filing *amicus* briefs in support of the Davises' position, are due on August 23rd, unless they seek and are granted an extension. Thereafter, the State of Kentucky will have the opportunity to file a reply brief to the Davises' brief within 35 days after the Davises file their brief.

Oral arguments on the case are expected to take place in October, although the Supreme Court has not yet scheduled a date for such arguments. The Supreme Court's decision in the case is expected no later than the end of term in June 2008, and more likely in early 2008.

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*If you wish to discuss the contents of this advisory, or for assistance with issues raised by the legal developments that are the subject of this advisory, please contact the Mintz Levin lawyers listed below or any other member of Mintz Levin's Public Finance section.*

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