IN THE SUPREME COURT OF IOWA

SUPREME COURT NO. 54 / 01-0011

RACING ASSOCIATION OF CENTRAL IOWA,
DUBUQUE GREYHOUND ASSOCIATION,
DUBUQUE RACING ASSOCIATION, LTD.,
and IOWA WEST RACING ASSOCIATION

Plaintiffs-Appellants,

vs.

MICHAEL FITZGERALD, TREASURER,
STATE OF IOWA,

Defendant-Appellee.

APPEAL FROM THE DISTRICT COURT
OF POLK COUNTY
THE HONORABLE SCOTT D. ROSENBERG

PETITION FOR REHEARING IN THE SUPREME COURT OF IOWA

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PROOF OF SERVICE

On the _____ day of June, 2002, the undersigned did serve the within Petition for Rehearing on all other parties to this appeal by mailing two copies thereof to respective counsel for said parties at their addresses of record.

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PETITION FOR REHEARING

Contrary to decades of precedent, the Court's 4-3 opinion is based on a factual analysis that is wholly inappropriate in an equal protection case, that intrudes into matters long left to legislative judgment, and is, in significant part, simply inaccurate. On a constitutionally unnecessary platform of contemporary facts not available to the legislature, the majority constructs a straw-man needed for the conclusion: there is no reason for the taxing scheme, unless the legislature meant to "drive the racetracks out of business." Then, discounting this justification as an illegitimate government interest and finding "no other basis for upholding the law," the Court knocks down the straw-man in favor of a radically new and different approach to equal protection analysis with neither precedent nor analytical justification.

The opinion engages in a factual dialogue to determine that: the rates "will seriously jeopardize the racetrack's viability"; the rates "do nothing to further the economic viability of the racetracks"; the rates are "disabling the industry" -- all leading to the conclusion that the rates are set up to "drive the racetracks out of business" and the judicial directive that the legislature must set a rate both racetracks and riverboats "can bear." Such a factual dialogue impermissibly intrudes into judgments reserved for the legislature and confuses constitutional review of a "confiscatory tax" under Due Process with the appropriate review of the classifications under Equal Protection. The dialogue leads to conclusions that are inaccurate, but that are, nevertheless, used as justification for the opinion that the legislature in 1994 could not have rationally made such classifications.

This intrusion into the legislative realm is fraught with logical pitfalls. When the legislature enacted the tax rates in 1994 gambling was in its infancy. There were only four riverboats in Iowa in 1994 - docked at Davenport, Clinton,

Dubuque, and Sioux City. Yet the opinion measures the constitutionality of the statute against "facts" drawn from the present day (eight years later) and against "facts" predicted into 2004 (ten years later), when the tax rate would have peaked. If constitutionality is to be measured by the "facts" as they unfold over time, equal protection analysis will become hostage to the economic success or failure of business. Could statutes be constitutional when enacted, yet drift into unconstitutionality as the economy fluctuates?

It is inappropriate for the courts to direct the legislature to set a rate that both racetracks and riverboats "can bear." This policy choice is simply out of judicial reach. The legislature could set the tax rate for both racetracks and riverboats at 36% or 38% or 40%, thus obviating an equal protection challenge yet failing to lower the tax rate that concerned the court in the first place.

The dissent got it right. The test has always been and must remain: could the legislature have rationally classified racetracks and riverboats differently for tax purposes? Every reasonable basis for upholding the legislative classification must be negated. The opinion throws taxing schemes into turmoil. No current tax, exemption, or credit is beyond the reach of unpredictable judicial oversight. This lack of guidance and predictability is at the heart of the problem with the opinion. The term "textbook example" fits this case; legislators, legal scholars and elected officials are scratching their heads and will continue to puzzle over this decision as they try to apply it in the future.

The Court should grant the motion for rehearing and reverse its decision.Respectfully submitted,

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ARGUMENT

THE OPINION TURNS ON FACT FINDINGS THAT ARE IMPERMISSIBLE, THAT INTRUDE INTO MATTERS OF LEGISLATIVE JUDGMENT AND THAT ARE INACCURATE.

A. The opinion relies on impermissible fact finding.

Even though the rational basis for a statutory classification is not measured by evidence, the opinion includes extensive fact findings which propel the opinion to an unfounded conclusion about legislative purpose and ultimate rejection of the rational basis for distinctions between racetracks and riverboats. It is settled that

> [B]ecause [the courts] never require a legislature to articulate its reasons for enacting a statute, it is entirely irrelevant for constitutional purposes whether the conceived reason for the challenged distinction actually motivated the legislature . . . a Legislative choice is not subject to courtroom fact finding and may be based on rational speculation unsupported by evidence or empirical data . . . .

FCC v. Beach Communications, 508 U.S. 307, 315, 124 L.Ed.2d 211, 222, 113 S.Ct. 2096, 2101 (1993) (emphasis added). "Only by faithful adherence to this guiding principle . . . is it possible to preserve to the legislative branch its rightful independence and its ability to function." Lehnhausen v. Lake Short Auto Parts, 410 U.S. 356, 365, 35 L.Ed.2d 351, 358, 93 S.Ct. 1001, 1006 (1973).

Violation of this "guiding principle" led the United States Supreme Court to summarily reverse the Ohio Supreme Court without oral argument in Central State Univ. v. American Assoc. of University Professors, 526 U.S. 124, 119 S.Ct. 1162, 143 L.Ed.2d 227 (1999) (per curium). Noting the lower court had held that the record lacked any "shred of evidence" to support a statute exempting workload standards for professors at public universities from collective bargaining, the

Supreme Court reversed emphasizing that lack of evidence "does not detract from the rationality of the legislative decision." Id. at 128, 119 S.Ct. at 1164, 143 L.Ed.2d at 231.

Rather than abide by the "guiding principle" so recently enforced by the United States Supreme Court, the opinion in this case veers off course making extensive findings of fact upon which the opinion concludes that the statute is unconstitutional. Fact findings about the tax rates include: the rates "will seriously jeopardize the racetrack's viability"; the rates do "nothing to further the economic viability of the racetracks"; the rates "frustrate the legislative purpose in permitting the racetracks to operate"; and the rates are "disabling the [racetrack] industry." Racing Assoc. of Central Iowa et al. v. Fitzgerald, No. 54/01-0011, slip op. at 12 - 13 (Iowa Sup. Ct. June 12, 2002).

Reliance on these facts to assess the constitutionality of a tax statute creates an anomaly in equal protection jurisprudence. "Rational speculation" to support legislative classifications has been now displaced by fact finding. Worse, the constitutionality of a statute enacted eight years ago has been measured by the current and future economics of the gambling industry. No legislature in1994 could have predicted what the revenues from slot machines would be years later. The constitutionality of state laws must be measured by whether the legislative choice was based on "rational speculation."

The rational basis test has never required the State to prove that legislation works; rather, the rational basis test only requires the State to show the legislation had a conceivable rational basis. This opinion dramatically departs from the test.

B. The opinion improperly focuses on the adverse impact of the tax on the racetracks which intrudes into legislative judgment.

The opinion relies heavily on the adverse impact of the tax on the racetracks. This is at odds with precedent and wrongly intrudes into matters

vested in the judgment of the legislature. Courts must not pass on the reasonableness of a tax by assessing its impact on a particular business. In City of Pittsburgh v. Alco Parking Corp. et al., 417 U.S. 369, 94 S.Ct. 2291, 41 L.Ed.2d 132 (1974), the United States Supreme Court rebuffed a challenge to the 20% tax on gross receipts from parking or storing automobiles and stated that the Court "has consistently refused either to undertake the task of passing on the 'reasonableness' of a tax that otherwise is within the power of Congress or of state legislative authorities, or to hold that a tax is unconstitutional because it renders a business unprofitable." Id. at 373, 94 S.Ct. at 2294, 41 L.Ed.2d at 136. This is true *even when the impact of a tax may be to destroy a particular business.* Magnano Co. V. Hamilton, 292 U.S. 40, 44, 78 L.Ed. 1109, 1114, 54 S.Ct. 599, 601 (1934).

Reliance on the size of the tax and the potential for an adverse impact on the racetracks to hold the statute unconstitutional runs contrary to these settled authorities. The standards for reviewing substantive due process and equal protections claims are the same. Exira Community School District v. Iowa et al., 512 N.W.2d 787, 793 (Iowa 1994); Kent v. Polk County Board of Supervisors, 391 N.W.2d 220, 224-25 (Iowa 1986).

Disregarding the admonition of these cases, the opinion emphasizes that racetracks pay "eighty percent more taxes than they would as riverboats" and "eventually the thirty-six percent tax on gross receipts will seriously jeopardize the racetracks' viability." Racing Assoc. of Central Iowa, at 11-12. Actually the tax is paid on *adjusted* gross receipts, that is receipts after reduction for amounts paid out in winnings. The slot machines are required to pay out to gamblers between 80% and 100% of the amount wagered. 491 IAC 11.9(2). A distribution of 90 % would make the tax rate only 3.6 % of gross receipts.

Although the opinion seems to express outrage over the tax on racetracks,

in two important contexts racetracks have immense advantages over other Iowa businesses. Most Iowa businesses pay either 5 or 6 % in sales tax on gross receipts. In addition few, if any, businesses in Iowa or the United States have the profit potential of large gambling operations protected by limited licensing.

Further, the opinion observes that the higher tax on racetracks ends up "helping the riverboat industry" by hurting the racetrack industry and directs the legislature to "tax racetracks and riverboats at a rate they both can bear." Racing Assoc. of Central Iowa, at 11-12. Thus, the opinion resolves any competitive "edge" riverboats may have over racetracks by striking the higher tax rate and mandating that the legislature arrive at a tax that allows both enterprises to thrive.

This legislative directive improperly expands the judicial role and intrudes into legislative policy. City of New Orleans v. Dukes, 427 U.S. 297, 303, 96 S.Ct. 2513, 2517, 49 L.Ed.2d 511, 517 (1976) (judiciary not a superlegislature to judge wisdom of legislative policy). Whether the tax rate "frustrates the racetrack's responsibility to distribute money to local government and charitable organizations" or "frustrates the racetrack's ability to contribute to the overall economy of this state" or may end up "helping the riverboat industry" by hurting the racetrack industry, Racing Assoc. of Central Iowa, at 11-12, are matters for legislative, not judicial, concern.

C. The opinion relies on facts that are inaccurate.

Even if fact findings were appropriate in assessing the rational basis for the tax rate and did not intrude into legislative judgment, the fact findings in the opinion are simply inaccurate.[1] The record does not contain many facts concerning the fiscal status of the racetracks, because that is not an appropriate

[1]On a procedural matter, the opinion erroneously refers to a cross appeal by the State. Racing Assoc. of Central Iowa, at 5, 15. No cross appeal was ever filed.

judicial inquiry for the reasons set forth above. There are vague assertions of hard times by the plaintiffs. The financial numbers in the record indicate the contrary.

At the time the motions were submitted to the district court, Prairie Meadows estimated annual adjusted gross receipts of $149,453,670 for future years. At the current tax rate of 32%, the tax is $47,115,174. (App. 131) Prairie Meadows would retain $102,338,496 for simple operating expenses and public purpose expenditures (subsidizing horse racing, contributing to Polk County and making other charitable contributions).[2] Similarly, the figures at Bluffs Run show gross receipts of $123,000,000, taxes at the highest rate of $43,450,000 and a pool of money amounting to $79,550,000 for simple operating expenses and public purpose expenditures. (App. 145) These figures overwhelm any general statement that the racetracks are in trouble.

Prairie Meadows planned to spend money for improvements -- $6 million from 1998 to 2002 and $14 million from 2003 through 2006, even though the tax rate would have peaked in 2004. Spending $20 million from cash flow for facility improvements, with no need to borrow, is not the sign of a failing company.

Further, Prairie Meadows planned to increase purses to horse owners from $10,312,251 in 1998 to $16,595,606 in 2002, even as the racetrack approached the top tax rate. A pool of $102,000,000 allows Prairie Meadows to do this.

The only racetrack to raise the possibility of closure is Dubuque Greyhound Park and Casino -- but it does not attribute the possibility solely to the tax rate. Market maturity and losses in greyhound operations are cited as factors. (App. 140) Moreover, the Dubuque Racing Association (DRA) holds the licenses to operate *both* Dubuque Greyhound Park and Casino and the Greater Dubuque

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[2]Prairie Meadows does not make payments for facility debt, because it pays cash for capital improvements.

Riverboat Entertainment Company. (App. 52) The decision to close would only shift slot machine consumers from the racetrack to the riverboat - operated by the same nonprofit corporation. DRA would remain in operation.

The sole basis in the record for ascribing to the legislature the purpose to "drive the racetracks out of business" appears to be a footnote attributing to a state representative from a "riverboat county" an amendment that would have increased the tax rate for racetracks to 40% of gross receipts. Racing Assoc. of Central Iowa, at 4. The subject intent of individual legislators is irrelevant to equal protection analysis - even if this intent could be inferred from such a slender thread. See Willis v. City of Des Moines, 357 N.W.2d 567, 571 (Iowa 1984). Imputing a Machiavellian motive to the legislature from this minor fact is disrespectful to an equal branch of government.

D. The opinion abandons traditional equal protection analysis.

The opinion disregards facts which demonstrate the financial viability of the racetracks and elects to rely on contrary suggestions in the record in support of its conclusions. It has never been the role of the judiciary to resolve factual conflicts when applying the traditional equal protection analysis under either the Iowa Constitution or the United States Constitution. Abandoning the traditional equal protection analysis of tax statutes, the opinion imposes wholly new restrictions on the legislature when enacting tax classifications. This Court has said

> [i]t is not sufficient that the court may regard the reason for the classification a poor one. The differences upon which the classification is based need not be great or conspicuous. An iron rule of equal taxation is neither attainable or necessary. [citations omitted]

Moorman v. G.D. Bair, 254 N.W.2d 737, 753 (Iowa 1977), aff'd, 437 U.S. 267, 98

S.Ct. 2340, 57 L.Ed.2d 197 (1978), *quoting from*, Dickinson v. Porter, 240 Iowa 393, 400-401, 35 N.W.2d 66, 72 (1949). Even minor differences in classifications have been found to satisfy equal protection. See e.g. Moorman, 254 N.W.2d at 741 (different treatment of income from manufacturing plants based on location); Hearst Corp. v. Iowa Dep't of Revenue and Finance, 461 N.W.2d 295, 306 (Iowa 1990), *cert. denied*, 499 U.S. 983, 111 S.Ct. 1639, 113 L.Ed.2d 735 (1991) (different tax treatment for newspapers and magazines).

Hearst illustrates how rational speculation should be applied by the courts under an equal protection analysis. Assessing whether a sales tax on magazines, but not newspapers, violates equal protection, this Court relied on the interest in enhancing the general knowledge and literacy of citizens and in avoiding problems that would arise by forcing newspaper carriers to collect sales tax to support the classification. Id. at 306. Without fact finding and without second- guessing the legislature, this Court accepted the reasons asserted as sufficient to support the classifications and concluded the classifications were rationally related to a legitimate government purpose. Id. at 305-06.

Spinning 180 degrees from Hearst, the opinion searches for similarities between racetracks and riverboats and disregards distinctions. Racing Assoc. of Central Iowa, at 7 - 8. In fact, the only similarity between racetracks and riverboats is that they both offer slot machines. Focusing so intently on slot machines seems to have turned the analysis of the opinion away from a traditional equal protection framework.

This Court's opinion in Hearst would dictate a contrary result. Just as newspapers and magazines are different despite the fact that they both may contain the same types of news or entertainment articles, riverboats are different from racetracks in nearly every other way. Just as the legislature wanted to subsidize newspapers to keep them cheap, the legislature could have lightened the tax load

on riverboats to encourage them to set up business and remain in the State. Indeed, immediately prior to enactment of the 1994 tax statute, between 1992 - 93, three riverboats left the state. (App. 52) Just as the legislature determined that newspapers were better served to carry out the interest of enhancing the knowledge of the public, the legislature could have determined that riverboats were more important to economic development than racetracks. Any one of these reasons serves as a constitutionally sufficient rational basis for the tax rate.

CONCLUSION

This Court rarely grants rehearing and for good reason. The rehearing process exists to catch the very rare mistakes the Court might make before a decision becomes final. It is our belief that this decision is one of those very rare mistakes -- one with significant fiscal consequences. For this reason, the Attorney General has personally signed a petition for rehearing for the first time in his long tenure.

The Petition for Rehearing should be granted and the decision should be reversed. In the event that the decision is not reversed, the district court on remand should be directed to address the retroactive application of the decision in formulating a remedy - an issue not briefed to this Court.