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MELVIN MILLIGAN and KIM LAWTON-MILLIGAN, Plaintiffs, v. DIRECTOR, DIVISION OF TAXATION, and DIRECTOR, DIVISION OF STATE LOTTERY, Defendants.	TAX COURT OF NEW JERSEY DOCKET NO. 007048-2011 DOCKET NO. 001337-2012 DOCKET NO. 000524-2013 DOCKET NO. 000046-2014 DOCKET NO. 000202-2015

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In 2009, the Legislature enacted a statute reversing a decades-long policy of not imposing New Jersey gross income tax on New Jersey lottery winnings. An amendment to N.J.S.A. 54A:6-11, adopted on June 29, 2009, imposes the tax on "New Jersey lottery winnings from a prize in an amount exceeding $10,000 . . . ." The amendment took effect immediately and applies "to taxable years beginning on or after January 1, 2009." L. 2009, c. 69, §5. The question before the court is whether the State, consistent with its obligation to turn square corners, may assess gross income tax on installments of lottery winnings received in 2009 and later years from a prize won in 2000.

For the reasons explained more fully below, the court concludes that the State may not impose gross income tax on winnings from a 2000 New Jersey lottery prize received in installments in 2009 and later years. It is undisputed that the State enacted a lottery to generate income, entered the marketplace to sell lottery tickets and, in 2000, when plaintiff Melvin Milligan purchased his winning ticket, made a deliberate effort to generate ticket sales by affirmatively representing to the public in its advertisements and on its website that New Jersey lottery winnings are not subject to State income tax. These representations, in effect, became part of the contractual agreement between the State and Mr. Milligan as the bearer of a ticket entitling him to a 2000 New Jersey lottery prize. Having induced the purchase of lottery tickets with assurances that lottery winnings would not be subject to State income tax, and having offered the payment of lottery winnings in installments over a twenty-six year period, the State may not impose the tax on the proceeds of any prize won prior to the January 1, 2009 effective date of the amendment to N.J.S.A. 54A:6-11. To hold otherwise would ignore the State's obligation to act with integrity when engaging in financial transactions with members of the public.

I. Findings of Fact and Procedural History

Plaintiff Melvin Milligan is a resident of New Jersey. In June 2000, he purchased a Big Game Lottery ticket from an authorized Division of State Lottery merchant. Mr. Milligan held the winning ticket for the June 9, 2000 drawing entitling him to a prize of $46 million.

Mr. Milligan did not know he held the winning ticket until almost a year later when, on June 7, 2001, he validated the ticket after watching the local news and learning that the winning ticket for the June 9, 2000 drawing had still not been claimed. Later that day, Mr. Milligan informed his wife, plaintiff Kim Lawton-Milligan, of his good luck. The couple discussed the two payment options offered by the Division of State Lottery to collect the prize. Plaintiffs could elect

the cash option and receive an immediate lump sum payout of $23,748,052, or elect the annuity option and receive fixed annual installments of approximately $1.7 million, net federal income tax withholdings, per year for 26 years. They had 60 days to make the election.[1]

On June 12, 2001, the Division of State Lottery received Mr. Milligan's validated ticket. The agency processed, verified and declared the ticket to be genuine the following day. A representative of the Division contacted Mr. Milligan to discuss the procedure for collecting the prize winnings and to schedule a press conference with Acting Governor DiFrancesco and Virginia E. Haines, then Executive Director of the Division of State Lottery. At the June 15, 2001, press conference, William T. Jourdain, Controller of the Division of State Lottery, approached plaintiffs and said that the "good thing about The Big Game" is that there was no State tax on the lottery prize. At the time of the press conference, plaintiffs had not yet elected their payment option.

Shortly after the press conference, the couple decided that the annuity payments, which would provide a constant revenue stream for a significant number of years, was the best option for their family. In making their decision the couple was influenced by their desire to provide a stable source of revenue for their child, who required continuing medical care.[2]

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[1] Mr. Milligan's winning ticket indicated that he chose the lump sum payment option. He does not recall whether he affirmatively elected that option or if it was the default automatically generated when he purchased his ticket. The parties agree that, technically speaking, during the 60-day election period, plaintiffs were deciding whether to change the election to annual annuity payments.

[2] Plaintiffs allege that they consulted an attorney and an accountant for tax and estate planning advice before making the annuity payment election and that those professionals advised plaintiffs that their lottery winnings would not be subject to State income tax. Plaintiffs also allege that they relied on these representations when making their payment election. These and other allegations support plaintiffs' claim that the assessment of income tax on the installment payments they receive in 2009 and later years would constitute a manifest injustice. See Oberhand v. Director, Div. of Taxation, 193 N.J. 558 (2008). The parties agreed that the court would reserve decision on plaintiffs' manifest injustice claims because discovery with respect to those claims is not complete. The court issued an opinion today in a companion case applying the manifest injustice doctrine to preclude the taxation of the winnings of taxpayers who won a New Jersey

On June 18, 2001, Controller Jourdain directed Tim Patton, an official at the State Division of Investment, to initiate the purchase of United States Treasury securities to fund Mr. Milligan's lottery prize. Mr. Jourdain specified that the "25 annual installments" would be for "$1,769,000, per year, beginning in May, 2002, and ending in May, 2026." Three days later, on June 21, 2001, plaintiffs met with Executive Director Haines to sign and finalize the necessary paperwork. That same day, plaintiffs received an initial installment check in the amount of $1,278,000. With the check, plaintiffs received a letter dated June 21, 2001 from Executive Director Haines confirming the terms of the Division of State Lottery's agreement with plaintiffs.

The agreement stated, in relevant part, that

> [t]he total amount of your annuity prize is $46,000,000.00, which is comprised of an initial payment amount of $1,775,000.00 and twenty five (25) annual installment payments of $1,769,000.00 each. The check which you receive today will be in the net amount of $1,278,000.00, which is your initial payment of $1,775,000.00 less twenty eight percent (28%) federal withholding tax of $497,000.00 which the lottery is required to deduct in accordance with the energy policy act of 1992.
>
> Your remaining twenty five (25) installment payments will be for the net amount of $1,273,680.00, which is your annual installment amount of $1,769,000.00 less twenty eight percent (28%) federal withholding tax of $495,320.00.
>
> Please be informed that the twenty eight (28%) federal tax deduction may not be sufficient to satisfy your federal tax obligation; therefore, I recommend that you contact your local office of the Internal Revenue Service to assist you, or seek legal or financial advice as soon as possible.
>
> [(emphasis added).]

lottery prize prior to the January 1, 2009. See Leger v. Director, Div. of Taxation, __ N.J. Tax __ (Tax 2016).

There is no mention in the June 21, 2001 letter of the withholding of New Jersey gross income tax from plaintiffs' installment payments. This is so because at the time of the June 9, 2000 drawing, and when Mr. Milligan subsequently claimed his prize in 2001, N.J.S.A. 54A:6-11 provided that New Jersey lottery winnings were not subject to New Jersey gross income tax. At those times, the statute stated that gross income subject to the tax "shall not include lottery winnings from the New Jersey lottery." N.J.S.A. 54A:6-11 (2000).

In 2000, the Division of State Lottery advertised in its brochures and on its website that New Jersey residents who won a lottery prize were not required to pay New Jersey gross income tax on their winnings. Division of State Lottery officials candidly admitted that these representations were intended to generate lottery ticket sales and to exploit a perceived business advantage over neighboring States. This was especially true with respect to New Jersey residents who work out of State. In 2000, while New Jersey excluded lottery winnings from State income tax, nearby States taxed lottery winnings. Controller Jourdain acknowledged that the Division of State Lottery hoped to entice New Jersey residents who worked in other States to purchase lottery tickets when they returned home to New Jersey, rather than in the State in which they worked.

In addition, Rule 21(b) of the Big Game Rules provided that "[a]ll winners, tickets, and transactions are subject to New Jersey Lottery rules and regulations, and State Law." At the time that Mr. Milligan purchased his ticket, won the $46 million prize, claimed his prize, and elected the annuity option, State law provided that New Jersey lottery winnings were not subject to gross income tax.

In 2009, the Legislature, as part of the annual State budget process, identified the need to raise over $1 billion in revenue. As part of this effort, various bills intended to raise revenue from New Jersey lottery winnings were introduced in the Legislature. A bill amending N.J.S.A. 54A:6-

11 to provide that New Jersey Lottery "winnings from a prize in an amount exceeding $10,000 shall be included in gross income" subject to tax was enacted into law on June 29, 2009. L. 2009, c. 69. According to L. 2009, c. 69, §5, the amendment to N.J.S.A. 54A:6-11 "shall take effect immediately and apply to taxable years beginning on or after January 1, 2009."[3]

In 2009, plaintiffs received an annual annuity payment of $1,273,680.00, after the withholding of federal income tax. On April 5, 2010, plaintiffs filed a joint New Jersey gross income tax return for tax year 2009. In order to avoid fees, penalties and interest, they reported the annual installment of New Jersey lottery winnings received in 2009 as taxable gross income and paid the tax due.

On August 9, 2010, plaintiffs filed an amended joint New Jersey gross income tax return for tax year 2009. This return excluded from taxable gross income the installment of lottery winnings they received in 2009. The amended return stated that plaintiffs disputed application of the amendment to N.J.S.A. 54A:6-11 to the 2009 installment and sought a refund of the $160,406 in gross income tax they paid on the installment.

By letter dated October 22, 2010, the Division of Taxation disallowed plaintiffs' amended income tax return and refund claim for tax year 2009.

On or about December 8, 2010, plaintiffs submitted a Notice of Protest and Request for Hearing with the Division of Taxation. An administrative hearing was held at the Division of Taxation on or about January 7, 2011.

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[3] When N.J.S.A. 54A:6-11 was amended to extend the gross income tax to certain lottery winnings, the Legislature also enacted legislation temporarily increasing gross income tax rates for taxpayers with taxable income exceeding $400,000, and temporarily suspending property tax deductions for certain taxpayers with income exceeding $150,000. See L. 2009, c. 69. A Fiscal Note estimated a total of more than $1 billion in new revenue from the three measures.

By letter dated February 2, 2011, the Director, Division of Taxation rejected plaintiffs' administrative appeal and issued a Final Determination upholding the denial of plaintiffs' refund request for tax year 2009.

On April 29, 2011, plaintiffs filed a Complaint in this court challenging the Director's February 2, 2011 Final Determination. Plaintiffs allege that application of the gross income tax to the lottery winnings installment plaintiffs received in 2009 constitutes a breach of contract, violates the square corners doctrine, constitutes a manifest injustice, and violates the State and federal Constitutions. Plaintiffs seeks a reversal of the Director's denial of their refund claim, a declaratory judgment that application of the amendment to N.J.S.A. 54A:6-11 to their lottery winnings is unconstitutional and illegal, and the award of compensatory damages, attorney's fees, and costs of suit.

Plaintiffs followed a similar course of action with respect to tax years 2010 through 2014, first filing gross income tax returns including the lottery winnings installments they received in those years in taxable gross income and subsequently filing amended returns excluding the installment payments from taxable income and requesting a refund. Each year the Director denied plaintiffs' refund request.

On January 25, 2013, plaintiffs filed a Complaint challenging the Director's denial of their refund claim for tax years 2010 and 2011.

On February 19, 2014, plaintiffs filed a Complaint challenging the Director's denial of their refund claim for tax year 2012.

On February 11, 2015, plaintiffs filed a Complaint challenging the Director's denial of their refund claim for tax year 2013.

Plaintiffs also challenged the application of the gross income tax to their lottery winnings installments in another forum. On June 6, 2011, plaintiffs filed a Complaint in the Superior Court, Law Division, Bergen County, alleging breach of contract and other claims similar to those raised in their Tax Court Complaints. The Superior Court Complaint named both the Director, Division of Taxation and the Division of State Lottery as defendants.

On November 4, 2011, the Hon. Brian R. Martinotti, J.S.C., transferred plaintiffs' Superior Court Complaint to this court. See N.J.S.A. 2B:13-2(b)("The Tax Court shall have jurisdiction over actions cognizable in the Superior Court which raise issues as to which expertise in matters involving taxation is desirable, and which have been transferred to the Tax Court pursuant to the Rules of the Supreme Court.").[4]

On February 23, 2015, this court denied the Division of State Lottery's motion to dismiss the allegations against it in the Complaint first filed in the Superior Court.

On March 2, 2015, this court entered an Order consolidating plaintiffs' four Tax Court actions and the matter they initiated in the Superior Court.

On June 3, 2016, plaintiffs moved for summary judgment on all claims in all matters.

On June 14, 2016, plaintiffs amended their motion to exclude a request for summary judgment on their manifest injustice claims, reserving the right to proceed with those claims in the event they do not prevail their other claims.

On June 24, 2016, the Director, Division of Taxation and the Director, Division of State Lottery, in separate filings, opposed plaintiffs' motion and cross-moved for summary judgment on all claims, except plaintiffs' allegations of manifest injustice.

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[4] Judge Martinotti also granted plaintiffs leave to file a late Notice of Contract Claim pursuant to N.J.S.A. 59:13-6 and held that a May 12, 2011 notice from plaintiffs was sufficient to satisfy plaintiffs' notice obligations under the Contractual Liability Act, N.J.S.A. 59:13-1 to -10.

On July 8, 2016, plaintiffs filed opposition to defendants' cross-motion.

On July 22, 2016, the court heard oral argument from counsel.

II. Conclusions of Law

Summary judgment should be granted where "the pleadings, depositions, answers to interrogatories and admissions on file, together with the affidavits, if any, show that there is no genuine issue as to any material fact challenged and that the moving party is entitled to a judgment or order as a matter of law." R. 4:46-2. In Brill v. Guardian Life Ins. Co., 142 N.J. 520, 523 (1995), our Supreme Court established the standard for summary judgment as follows:

> [W]hen deciding a motion for summary judgment under Rule 4:46-2, the determination whether there exists a genuine issue with respect to a material fact challenged requires the motion judge to consider whether the competent evidential materials presented, when viewed in the light most favorable to the non-moving party in consideration of the applicable evidentiary standard, are sufficient to permit a rational factfinder to resolve the alleged disputed issue in favor of the non-moving party.

The court finds that there are sufficient undisputed material facts in the motion record to determine whether the Director's interpretation of the amendment to N.J.S.A. 54A:6-11 is entitled to be affirmed and to determine plaintiffs' claims under the square corners doctrine.

A. Whether the Amendment to N.J.S.A. 54A:6-11 Applies to the Installments of Lottery Winnings Plaintiffs Received in 2009 and Later Years from their 2000 Lottery Prize.

As a threshold matter, plaintiffs challenge the Director, Division of Taxation's interpretation of the amendment to N.J.S.A. 54A:6-11. They argue that the amendment was not intended to extend the gross income tax to lottery winnings received in 2009 and later years from a prize awarded prior to January 1, 2009. According to plaintiffs, it is the date that the "prize" is awarded that controls application of the effective date provision of the amendment, in light of the fact that it is a "prize in an amount exceeding $10,000" that triggers taxation of the winnings under

the amended statute. This reading of the effective date provision of the amendment to N.J.S.A. 54A:6-11 would require reversal of the Taxation Director's denial of plaintiffs' refund claims for each tax year at issue. Plaintiffs' argument is based on what they describe as the unambiguous language of the statute. In addition, plaintiffs argue that if the court concludes that the effective date provision is ambiguous, the legislative history supports their interpretation of the statute, requiring reversal of the Taxation Director's determinations.

Defendants, on the other hand, advance the argument that both the plain language of the statute and its legislative history are in accord with the Taxation Director's interpretation of the amendment as applying to any lottery "winnings" received on or after January 1, 2009, regardless of when the underlying lottery prize was awarded. In the Director's view, it is "winnings" that are taxable and receipt of those winnings in a tax year beginning January 1, 2009 or later falls within the effective date of the amendment.

The court's analysis of the parties' positions has as its foundation the familiar principle that the Director, Division of Taxation's interpretation of tax statutes is entitled to a presumption of validity. "Courts have recognized the Director's expertise in the highly specialized and technical area of taxation." Aetna Burglar & Fire Alarm Co. v. Director, Div. of Taxation, 16 N.J. Tax 584, 589 (Tax 1997)(citing Metromedia, Inc. v. Director, Div. of Taxation, 97 N.J. 313, 327 (1984)). The scope of judicial review of the Director's decision with respect to the imposition of a tax "is limited." Quest Diagnostics, Inc. v. Director, Div. of Taxation, 387 N.J. Super. 104, 109 (App. Div.), certif. denied, 188 N.J. 577 (2006); International Business Machines Corp. v. Director, Div. of Taxation, 26 N.J. Tax 102, 107-08 (Tax 2011). The Supreme Court has directed courts to accord "great respect" to the Director's application of tax statutes, "so long as it is not plainly unreasonable." Metromedia, supra, 97 N.J. at 327. See also GE Solid State, Inc. v. Director, Div.

of Taxation, 132 N.J. 298, 306 (1993)("Generally, courts accord substantial deference to the interpretation an agency gives to a statute that the agency is charged with enforcing.").

The Gross Income Tax Act provides that taxable income shall consist of sixteen distinct categories. N.J.S.A. 54A:5-1. Plaintiffs do not dispute that lottery winnings fall into one of two categories of taxable income. According to N.J.S.A. 54A:5-1,

> New Jersey gross income shall consist of the following categories of income:
>
> (g) Gambling winnings.
>
> * * *
>
> (l) Amounts received as prizes and awards, except as provided in N.J.S. 54A:6-8 and N.J.S. 54A:6-11 hereunder.
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> [N.J.S.A. 54A:5-1.]

Because N.J.S.A. 54A:5-1(l) specifically refers to N.J.S.A. 54A:6-11, the provision providing a partial exclusion from taxable gross income for lottery winnings, it is readily apparent that category (l) includes lottery winnings in gross income subject to tax. The subparagraph's reference to N.J.S.A. 54A:6-11 would otherwise be superfluous. See Gabin v. Skyline Cabana Club, 54 N.J. 550, 555 (1969)("It is a cardinal rule of statutory construction that full effect should be given, if possible, to every word of a statute. We cannot assume that the Legislature used meaningless language."). The Taxation Director also considers lottery winnings to be "gambling winnings" as defined by N.J.S.A. 54A:5-1(g), a net category of income. The Division permits taxpayers to offset lottery winnings with gambling losses incurred in the same year when calculating taxable gambling winnings under N.J.S.A. 54A:5-1(g).

Regardless of the category of taxable income to which lottery winnings are correctly attributed, the statutory language that is controlling here is the 2009 amendment to N.J.S.A. 54A:6-11 and its effective date provision. After amendment, the statute reads

> Gross income shall not include lottery winnings from the New Jersey Lottery, except that New Jersey Lottery winnings from a prize in an amount exceeding $10,000 shall be included in gross income.
>
> [N.J.S.A. 54A:6-11.]

According to L. 2009, c. 69, §5, the amendment to N.J.S.A. 54A:6-11 "shall take effect immediately and apply to taxable years beginning on or after January 1, 2009."

Statutory construction begins with the statute's plain language. Merin v. Maglaki, 126 N.J. 430, 434 (1992). "A statute should be interpreted in accordance with its plain meaning if it is clear and unambiguous on its face and admits of only one interpretation." Board of Educ. v. Neptune Twp. Educ. Ass'n, 144 N.J. 16, 25 (1996)(quotations omitted). "[T]he best approach to the meaning of a tax statute is to give to the words used by the Legislature their generally accepted meaning, unless another or different meaning is expressly indicated." Public Serv. Elec. & Gas Co. v. Township of Woodbridge, 73 N.J. 474, 478 (1977)(quotations omitted). "'The duty of the Director, and this court, is to give meaning to the wording of the statute and, where the words used are unambiguous, apply its plain meaning in the absence of a legislative intent to the contrary.'" Vassilidze v. Director, Div. of Taxation, 24 N.J. Tax 278, 291 (Tax 2008)(quoting Sutkowski v. Director, Div. of Taxation, 312 N.J. Super. 465, 475 (App. Div. 1998)).

Both interpretations of the statute offered by the parties are reasonable. The effective date provision of the amended statute, L. 2009, c. 69, §3, provides that the limitation to exclusion from taxable income applies to "taxable years beginning on or after January 1, 2009." A "'[t]axable year' means the calendar or fiscal accounting period for which a tax is payable under this act."

N.J.S.A. 54A:1-2(k). "There is hereby imposed a tax for each taxable year (which shall be the same as the taxable year for federal income tax purposes) on the New Jersey gross income as herein defined of every individual . . . ." N.J.S.A. 54A:2-1. Individual taxpayers calculate income for New Jersey gross income tax purposes based on the calendar year.

To the extent that lottery winnings are "gambling winnings" within the meaning of N.J.S.A. 54A:5-1(g), those "winnings" were received by plaintiffs in installments in 2009, 2010, 2011, 2012 and 2013. Plaintiffs reported their income on a calendar year basis for each tax year. Each installment of winnings received by plaintiffs was received in a taxable year beginning on or after January 1, 2009. As this court recently explained, "[b]oth the plain language and overall structure of the GIT Act lead to the conclusion that the tax is an annual assessment, based on discrete events that take place during the tax year." Murphy v. Director, Div. of Taxation, 26 N.J. Tax 432, 443 (Tax 2012), aff'd, 27 N.J. Tax 293 (App. Div. 2013). Under this reading of the statute, it is the receipt of the "winnings" in a tax year that began on or after January 1, 2009 that is the taxable event embraced by the amendment to N.J.S.A. 54A:6-11.

On the other hand, one could reasonably interpret the statute to provide that it is a "prize in an amount exceeding $10,000" that triggers the inclusion of the winnings in taxable gross income. The Division of State Lottery rules for the Big Game (subsequently renamed the Mega Millions) are drafted with the premise that the "prize" is the amount won by the holder of a winning ticket. For example, Rule 14 provides that a ticket holder may elect a payment option "[a]t the time a prize is claimed." In addition, the letter from the State Lottery Executive Director to plaintiffs describes their "prize" as being $46,000,000.00, the full amount awarded at the June 9, 2000 lottery drawing. Both Controller Jourdain and the Executive Director of the State Lottery confirmed at their depositions that the Division of State Lottery considers plaintiffs' "prize" to be

the total amount they won at the June 9, 2000 drawing. Under this view of the statute, the amendment to N.J.S.A. 54A:6-11 applies only to winnings from prizes awarded on January 1, 2009 or later and not to Mr. Milligan's 2009 installment of winnings from the lottery prize he won in 2000.[5]

The legislative history of the amendment to N.J.S.A. 54A:6-11 does not provide definitive assistance in resolving the question of which of these reasonable interpretations of the statute was intended by the Legislature. See DiProspero v. Penn, 183 N.J. 477, 492-493 (2005)("[I]f there is ambiguity in the statutory language that leads to more than one plausible interpretation, [the court] may turn to extrinsic evidence, 'including the legislative history, committee reports, and contemporaneous construction.'")(quoting Cherry Hill Manor Assocs. v. Faugno, 182 N.J. 64, 75 (2004)). There is an absence of explicit discussion in the legislative history of the taxation of annuity installment payments received on or after January 1, 2009 from prizes awarded prior to January 1, 2009. The distinction between the date on which a lottery prize is awarded and the date on which the winnings from that prize are received appears not to have been the focus of debate by the Legislature.

In addition, the Office of Legislative Services ("OLS") is an agency of the Legislature established "to aid and assist the Legislature in performing its functions . . . ." N.J.S.A. 52:11-55. Among its statutory objectives, the OLS is to "[p]rovide, upon request, legal, fiscal, research,

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[5] Notably, although the Taxation Director argues that it is plaintiffs' receipt of winnings in 2009 that triggers the statute, a Technical Bulletin issued by the Division of Taxation on July 14, 2016, just days before oral argument on the parties' cross-motions, acknowledges that it is the prize amount that is the operative factor in determining whether the gross income tax is imposed. In Technical Bulletin TB-20-R, the Division states that "the prize amount (over $10,000) is the determinative factor of taxability, rather than the total amount of lottery winnings over the year. For example, if a person won the New Jersey Lottery two times in the same year and the winning prize amounts were $5,000.00 and $6,000.00, these winnings are not subject to New Jersey gross tax [sic]." This supports plaintiffs' interpretation of the effective date provision of the statute.

information and administrative services and assistance for the Legislature, its officers, committees, commissions, members and staff." N.J.S.A. 52:11-58(b)(1). Martin Poethke, an OLS fiscal analyst, prepared a Fiscal Note to accompany A4102, the bill which ultimately was enacted as the amendment to N.J.S.A. 54A:6-11. As noted above, in addition to the lottery prize amendment, A4102 included other amendments to the Gross Income Tax Act designed to raise revenue. The Fiscal Note includes an estimate that A4102, if enacted "would increase State gross income tax revenues by $1,011,000,000 in Fiscal Year 2010," including "$8 million from the application of the gross income tax to certain lottery prize winnings, which will recur annually." Mr. Poethke testified that he did not perform an independent corroboration of the amount attributable to the taxation of lottery winnings, which was considered de minimus compared to the over $1 billion projected to be raised by the other provisions of A4102. A Statement of the Assembly Budget Committee accompanying A4102 provides that the $8 million estimated revenue from the taxation of lottery winnings would "fluctuat[e] with annual changes in prize winnings."

Plaintiffs argue that the Fiscal Note and Mr. Poethke's testimony support their position that the Legislature did not intend to extend the tax to installments of lottery winnings received on or after January 1, 2009 from prizes awarded prior to that date. This is so, plaintiffs argue, because when the Fiscal Note and Assembly Budget Committee Statement were prepared, the annual installment payments of lottery winnings to be awarded in 2009 and later years from prizes won prior to January 1, 2009, and the gross income tax those installment payments would generate, would have been easily quantifiable and not dependent on "annual changes in prize winnings."[6]

[6] Plaintiffs point out that application of the amendment to N.J.S.A. 54A:6-11 to plaintiffs alone will generate approximately $130,000 in tax revenue annually. In 2009, there were approximately 2,400 taxpayers in lottery winnings annuity status. Even if those taxpayers paid just $3,334 a year in income tax, the amendment to N.J.S.A. 54A:6-11 would generate more than $8 million in revenue ($3,334 x 2,400 = $8,001,600). Plaintiffs argue that in light of the fact that

Plaintiffs urge the court to adopt their view of the meaning of the amendment to N.J.S.A. 54A:6-11 because the tax statutes must "be construed most strongly against the government and in favor of the taxpayer where there is doubt or ambiguity." Sutkowski v. Director, Div. of Taxation, 312 N.J. Super. 465, 475 (App. Div. 1998); see also Fedders Fin. Corp. v. Director, Div. of Taxation, 96 N.J. 376, 385 (1984)("[W]hen interpretation of a taxing provision is in doubt, and there is no legislative history that dispels that doubt, the court should construe the statute in favor of the taxpayer."). The Taxation Director counters that N.J.S.A. 54A:6-11, in effect, creates an exemption from taxation and should therefore be narrowly construed. "Taxation is the rule and exemption is the exception to the rule.'" Sidman v. Director, Div. of Taxation, 18 N.J. Tax 636, 645 n.1 (Tax 2000) (quoting AT&T Co. v. Director, Div. of Taxation 13 N.J. Tax 534, 543 (Tax 1993)); accord Reck v. Director, Div. of Taxation, 345 N.J. Super. 443, 449 (App. Div. 2001), aff'd, 175 N.J. 54 (2002). N.J.S.A. 54A:6-11 might also be viewed as an exclusion of otherwise taxable revenue from taxable income. Exclusions too are narrowly construed against the taxpayer. Sa v. Director, Div. of Taxation, 26 N.J. Tax 377, 383 (Tax 2012).[7]

It is clear that absent N.J.S.A. 54A:6-11, all New Jersey lottery winnings would be included in taxable income either as "gambling winnings" under N.J.S.A. 54A:5-1(g) or "prizes" under

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their tax liability is more than 40 times higher than that baseline amount, the legislative history and revenue projects clearly could not possibly have included anticipated revenue from installment payments on lottery prizes awarded prior to January 1, 2009.

[7] Assembly Bill No. A2069, introduced in 2010, would amend N.J.S.A. 54A:6-11 to provide that taxable income includes lottery winnings "from a prize awarded pursuant to a drawing on or after July 1, 2009." This bill would codify plaintiffs' interpretation of the statute. Assembly Bill No. A2196, introduced in 2014, would repeal the 2009 amendment to N.J.S.A. 54A:6-11, restoring the full exclusion from taxable gross income for New Jersey lottery winnings beginning July 1, 2013. Each of these bills was sponsored by a single member of the Legislature. Similar bills with various effective dates were introduced but have not been enacted into law. No bill proposing to further amend N.J.S.A. 54A:6-11 was voted on by either house of the Legislature after the 2009 amendment at issue here. The bills, therefore, are not useful evidence of legislative intent.

N.J.S.A. 54A:5-1(l). Whether N.J.S.A. 54A:6-11 is viewed as creating an exemption from taxation or an exclusion from taxable income, the statute, and its effective date provision, must be construed narrowly against the taxpayer.

The court cannot conclude that the Legislature unequivocally intended to extend the gross income tax to all lottery winnings received on or after January 1, 2009, regardless of the date on which the underlying prize was awarded. Nor can the court conclude that that the Legislature unequivocally meant to extend the gross income tax only to winnings from lottery prizes awarded on or after January 1, 2009. The court finds, however, that any ambiguity that might exist in the statute must be read in favor of taxation of the income, and surely does not overcome the deference to which the Director is entitled when he interprets a tax statute. Because the Director's interpretation of the amendment to N.J.S.A. 54A:6-11 and its effective date provision is not "plainly at odds with" the statute, see ADVO, Inc. v. Director, Div. of Taxation, 25 N.J. Tax 504, 511 (Tax 2010), it must be upheld.[8]

B. Whether Taxation of Plaintiffs' Lottery Winnings is barred by the Square Corners Doctrine.

Having determined that the Director's interpretation of the amendment to N.J.S.A. 54A:6-11 must be upheld, the court is confronted with the question of whether that interpretation of the statute, when applied to plaintiffs, comports with the State's obligation to act with integrity under

[8] The court notes that the motion record contains evidence of initial confusion on the part of officials at the Division of State Lottery and the Division of Taxation with respect to the meaning of the effective date provision of the amendment to N.J.S.A. 54A:6-11. It does not strike the court as unusual that Executive Branch officials charged with the administration of a newly enacted statute might engage in a discussion of the meaning of the new law and how it will be applied. In addition, the record demonstrates that within a few days after enactment of the amendment to N.J.S.A. 54A:6-11, the Taxation Director took the position that the statute applies to all lottery winnings received on or after January 1, 2009, regardless of the date on which the prize was awarded. These post-enactment developments are not convincing evidence that the statute is ambiguous.

the square corners doctrine. The square corners doctrine is a long-established legal principle limiting Executive Branch action which would otherwise be authorized by law.

The Supreme Court explained the scope of the square corners doctrine in F.M.C. Stores Co. v. Borough of Morris Plains, 100 N.J. 418, 426-27 (1985). The Court's directive was clear:

> We have in a variety of contexts insisted that governmental officials act solely in the public interest. In dealing with the public, government must "turn square corners." Gruber v. Mayor and Twsp. Com. of Raritan Tp., 73 N.J. Super. 120 (App. Div.), aff'd., 39 N.J. 1 (1962). This applies, for example, in government contracts. See Keyes Martin v. Director, Div. of Purchase and Property, 99 N.J. 244 (1985). Also, in the condemnation field, government has an overriding obligation to deal forthrightly and fairly with property owners. See Rockaway v. Donofrio, 186 N.J. Super. 344 (App. Div. 1982); State v. Siris, 191 N.J. Super. 261 (1983). It may not conduct itself so as to achieve or preserve any kind of bargaining or litigational advantage over the property owner. Its primary obligation is to comport itself with compunction and integrity, and in doing so government may have to forego the freedom of action that private citizens may employ in dealing with one another.
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> [Id. at 426-27.]

The currency of the square corners doctrine in the area of taxation was highlighted by the Court:

> [S]tatutory provisions governing substantive standards and procedures for taxation, including the administrative review process, are premised on the concept that government will act scrupulously, correctly, efficiently, and honestly. It is to be assumed that the [taxing authority] will exercise its governmental responsibilities in the field of taxation conscientiously, in good faith and without ulterior motives.
>
> [Id. at 427.]

"One of the hallmarks of the 'turn square corners' doctrine is that its application is not dependent upon a finding of bad faith." CBS Outdoor, Inc. v. Borough of Lebanon Planning Bd., 414 N.J. Super. 563, 586-87 (App. Div. 2010); accord Gastime, Inc. v. Director, Div. of Taxation, 20 N.J. Tax 158 (Tax 2002). The circumstances under which the doctrine will be applied to limit

government action are not static. Equitable relief under the doctrine "cannot be exercised or withheld rigidly, but [is] always subject to the guiding principles of fundamental fairness." New Concepts For Living, Inc. v. City of Hackensack, 376 N.J. Super. 394, 404 (App. Div. 2005).

Courts have not hesitated to apply the doctrine to preclude the assessment of tax where taxpayers made financial decisions relying on representations by State officials regarding how tax laws will be applied, only to have those officials change position later. A recent Appellate Division opinion serves as a good example of how the doctrine may limit the State's authority to assess a tax.

In Residuary Trust A v. Director, Div. of Taxation, 28 N.J. Tax 541 (App. Div. 2015), the Division of Taxation issued advice in 1999 in the State Tax News, its bi-monthly newsletter, that no tax would be assessed in the circumstances in which the taxpayer found itself seven years later. The taxpayer filed a return for tax year 2006 consistent with the Division's 1999 published advice. In 2009, the Division issued a notice assessing tax against the taxpayer, taking a position "at variance with the clear guidance it had provided . . . taxpayers" and asserting "for the first time" that the taxpayer's circumstances supported the assessment of tax. Id. at 547.

The Appellate Division affirmed this court's reversal of the tax assessment under the square corners doctrine. As the court succinctly explained:

> The square corners doctrine is particularly important in the field of taxation, because trusts, businesses, individuals and others must be able to reliably engage in tax planning and, to do so, they must know what the rules are. It is fundamentally unfair for the Division to announce in its official publication that, under a certain set of facts, a trust's income will not be taxed, and then retroactively apply a different standard years later.
>
> [Id. at 548 (citations omitted).]

Similarly, in Lowe's Home Centers, Inc. v. City of Millville, 25 N.J. Tax 591 (Tax 2010), this court applied the square corners doctrine to preclude a city from negating a tax exemption agreement with a taxpayer who redeveloped blighted property. In that case, after the property was redeveloped, the municipal tax assessor made a written representation to the taxpayer that the deadline for applying for the exemption was July 1. The taxpayer submitted its application on June 30, before the deadline identified by the assessor. The exemption was approved. Id. at 596-97. Two and a half years later, the municipality attempted to rescind the exemption because the actual deadline for the exemption application was June 26, contrary to the tax assessor's advice to the taxpayer, making the application late. Id. at 597.

Despite the fact that the application was submitted after the correct deadline, this court precluded revocation of the exemption. In reaching its decision, the court noted that the taxpayer reasonably relied on the tax assessor's representation when submitting its exemption application on June 30, and had relied on the availability of the exemption when deciding to undertake redevelopment of the troubled property. In addition, the municipality had secured the benefits of the economic development that was the basis of the award of the exemption. The court held that allowing revocation of the exemption after the taxpayer had redeveloped the area and relied on the assessor's representation of the application deadline, albeit incorrect, "would seriously undermine the [economic development] statute's purpose by introducing an element of uncertainty to the development planning process." Id. at 605.

In addition, the court held that revocation of the exemption would "permit [the municipality] to gain the benefit of its bargain with [the taxpayer] while depriving the property owner of the tax benefits that motivated the construction" of the property. Id. at 605-06. The court concluded that the taxing authorities

> fell short of the standards of fairness and fair dealings that taxpayers have a right to expect from public officials. Proper administration of our tax laws . . . demand[s] consistency and fairness from municipal officers in their dealings with property owners.
>
> [Id. at 606.]

This observation is equally true with respect to State tax officials.

Here, there is no dispute that in 2000 officials from the Division of State Lottery actively and intentionally represented to the public that winnings from the New Jersey lottery are not subject to gross income tax. These representations were made with the purpose of generating the sale of lottery tickets and resulting income for the State. It was perfectly reasonable for Mr. Milligan and all purchasers of lottery tickets to rely on these representations. More importantly, after Mr. Milligan claimed his lottery prize, he was given a 60-day period to make an election between an immediate lump sum payment of his winnings or the payment of his winnings in a series of installments stretching over many years. Common sense would suggest that the exclusion of New Jersey lottery winnings from State income tax was one factor considered by Mr. Milligan when making his election. The record convincingly demonstrates that the fact that New Jersey lottery winnings were not subject to State income tax was acknowledged by State officials during the election period and was incorporated in the State Lottery Executive Director's letter to Mr. Milligan detailing the sum certain he would receive each year.

In the circumstances before the court, the State was, in effect, a market participant. State officials raised revenue for public coffers by generating the sale of lottery tickets in a competitive environment. Those officials sought a business advantage by advertising that New Jersey lottery winnings are not subject to the State income tax. See McCauley v. State, 19 N.J. Tax 581, 584-85 (Tax 2001)(noting that the "presumed purpose of the exemption of State Lottery winnings is N.J.S.A. 54A:6-11" was "the encouragement of ticket sales.") When purchasing his ticket Mr.

Milligan surely had a right to expect that the State would abide by the terms of the deal it was offering the public: if you hold a winning lottery ticket you will receive the lottery prize free from State income tax. It does not take extended legal analysis, complex explanations of the details of a statute, or an in-depth exploration of judicial decisions to reach the common sense conclusion that the State should live up to the representations it makes in the marketplace.

The contractual nature of the relationship between plaintiffs and the State further supports this conclusion. Although the court reserves decision on plaintiffs' breach of contract claims, it is critical at this juncture to note that in 1993, a trial court judge recognized precedents from other jurisdictions holding that "the relationship arising out of the lottery system is primarily contractual in nature." Driscoll v. State, 265 N.J. Super. 503, 510 (Law Div. 1993)(citing Valante v. Rhode Island Lottery Comm'n, 544 A.2d 586, 589 (R.I. 1988); Hair v. State, 2 Cal. App. 4th (1991); Aguimatang v. California State Lottery, 234 Cal. App. 3d 769 (1991); Brown v. California State Lottery Comm'n, 232 Cal. App. 3d 1335 (1991); Thao v. Control Data Corp., 790 P.2d 1239 (Wash. App. 1990)). "A ticket holder is said to have accepted an offer upon purchasing the lottery tickets at the licensed agency." Id. at 510.

"From a contractual perspective, the terms of the contract are subject to the lottery law, and the rules and regulations promulgated pursuant to that authority." Ibid. (citing Karafa v. New Jersey State Lottery Comm'n, 129 N.J. Super. 499, 502 (Chan. Div. 1974)(denying claim to lottery prize by person who misplaced winning ticket and could not satisfy regulation requiring presentation of ticket to claim prize)); accord Triano v. Division of State Lottery, 306 N.J. Super. 114, 124 (App. Div. 1997). "The rights and obligations of the contracting parties arising out of a lottery ticket purchase cannot, therefore, contravene the rules and regulations of the" Division of State Lottery. Driscoll, supra, 265 N.J. Super. at 510; see also NBCP Urban Renewal v. City of

Newark, 17 N.J. Tax 59, 73 (Tax 1997)("Statutes in existence at the time a contract is executed are implicitly part of the contract."), aff'd, 17 N.J. Tax 505 (App. Div. 1998). The State's interaction with Mr. Milligan is more than a casual exchange. By virtue of having established a lottery and having sold Mr. Milligan a winning ticket, the State imposed on itself the obligation to act fairly and with compunction when called upon to fulfill its bargain with lottery winners. For those winners of lottery prizes awarded prior to January 1, 2009, that bargain includes the receipt of winnings without the imposition of New Jersey gross income tax.[9]

Having determined that plaintiffs are entitled to relief under the square corner doctrine, the court need not reach the constitutional claims raised by plaintiffs. "Ordinarily, we will not reach a constitutional issue if a case can be decided on narrower grounds." Residuary Trust A, supra, 28 N.J. Tax at 545 (citing Randolph Town Center, LP v. County of Morris, 186 N.J. 78, 80 (2006); A.Z. v. Higher Educ. Student Assistance Auth. 427 N.J. Super. 389, 395 (App. Div. 2012)). The court, therefore, reserves decision on plaintiffs' claims under the federal and State Constitutions.

The court would be remiss, however, were it not to address the holding in Klebanow v. Glaser, 80 N.J. 367 (1979), given the apparent similarity of the facts before the Court in that case to those in the present matter. In Klebanow, a taxpayer moved from New York to New Jersey in

[9] Both defendants deny the existence of a contract. The Taxation Director also argues that if a contract exits his entity is not a party to the agreement, having played no role in the promotion or sale of the winning ticket to Mr. Milligan. The court concludes that it need not resolve these and other contentions to decide plaintiffs' square corners claims, as it is sufficient at this juncture in the court's analysis to recognize the legal precedents that the bearer of a winning lottery ticket has a relationship that is contractual in nature with the State. The equitable square corners doctrine does not require specific findings of breach of contract on the part of a particular State entity or official to justify the award of relief. The doctrine is flexible enough to limit official action that would bestow upon the State an untoward advantage in a contractual setting without assigning liability on any individual government entity or actor. For example, although the Taxation Director did not make any representations to plaintiffs regarding the taxation of lottery winnings, the representation of State Lottery officials to plaintiffs provide an ample basis for the award of equitable relief against all State defendants.

November 1974. A few months later, in January 1975, the taxpayer sold securities, realizing capital gains of more than $11 million. The taxpayer claimed that he moved to New Jersey in specific reliance on the fact that at the time of the move New Jersey did not tax capital gains, intending to conduct his transaction in the State to avoid tax. Id. at 369-70. At the time of the sale, however, there were bills pending in the Legislature which, if enacted, would have imposed a tax on capital gains from transactions occurring after December 31, 1974. Id. at 370.

On August 4, 1975, the Governor approved legislation imposing a tax on capital gains. The act provided that it was to "take effect immediately and shall be applicable with respect to unearned income earned, received or constructively accrued or credited to the taxpayer on or after January 1, 1975." Ibid. (citing L. 1975, c. 172, §25). After the Director, Division of Taxation assessed tax on the gain from the January 1975 transaction, the taxpayer appealed, arguing that the assessment violated the Fifth and Fourteenth Amendments of the United States Constitution. His challenge ultimately was heard by the Supreme Court, which summarized the taxpayer's argument as follows:

> Plaintiff contends that the retroactive effect of the statute as applied to him is unconstitutional, arguing that when an individual voluntarily enters into a transaction relying on the nontaxability of the event, a subsequently adopted statute cannot constitutionally create tax consequences where none previously existed.
>
> [Id. at 370.]

After examination of several United States Supreme Court precedents, our Court observed that

> in the income tax area retroactivity does not per se constitute a deprivation of property without due process. Retroactivity, at least with respect to income realized in the year in which the act was passed, has been validated irrespective of whether the statute created a new tax or increase tax burdens by revising an existing law. It has been upheld even though the taxpayer may not have been aware of its immanency and even though the triggering event may have

> occurred because of some voluntary action or inaction on the part of the taxpayer.
>
> [Id. at 373 (footnote omitted).]

The Court recognized that when the statute at issue was enacted the State was "in the throes of a fiscal crisis" brought about by the State's need to comply with the Court's recent holding in Robinson v. Cahill, 63 N.J. 196 (1973), regarding the State's public school funding obligations under the State Constitution. Id. at 376. The Governor identified those who benefit from transactions resulting in capital gains as "segments of the economy that are able to bear the additional burden" of raising the revenue necessary to meet the State's pressing financial needs. Ibid. In addition, the Court noted that the taxpayer "should have been aware that serious consideration was being given to some form of income tax long before the sale of his stock." Id. 377. The Court's holding was plainly fact specific:

> We are satisfied that under the totality of circumstances and events existing here – the paramount governmental interest in obtaining adequate revenues, the extensive fiscal implications for the State in a financial crunch, apportionment of the cost of government equitably, the public controversy and numerous income tax bills which had been introduced in the Legislature subsequent to the decision in Robinson v. Cahill, supra – the limited retroactive effect of the statute does not violate the Fourteenth Amendment of the Federal Constitution. We see no reason to reach a different conclusion in interpreting the comparable provision of the New Jersey Constitution (1947), Art. 1, par. 1.
>
> [Id. at 377.]

On first review, the facts in Klebanow appear quite similar to those presently before the court. A closer examination, however, reveals crucial factual differences. Foremost among those differences is the State had no involvement in the private financial transaction at issue in Klebanow. This contrasts sharply with the transaction giving rise to the taxable event in the present case. As discussed at length above, State officials, as active participants in the lottery market,

made affirmative representations to the public, including Mr. Milligan, that New Jersey lottery winnings were not subject to State income tax. Those representations were made with the admitted purpose of generating lottery sales and to exploit a perceived business advantage over neighboring States where lottery winnings were subject to tax. In addition, plaintiffs and the State have a relationship that is contractual in nature and in which the State agreed to provide plaintiffs with a sum certain every year over a period of 25 years. That sum certain, although expressly subject to withholdings for federal income tax purpose, is calculated based on the understanding that plaintiffs' installment payments would be free from State income tax. Another critical distinction is that at the time that Mr. Milligan purchased his winning lottery ticket in 2000, and at the time that he claimed his prize and elected the multi-year annuity payment option in 2001, no bills were pending in the Legislature to reverse the long-standing exclusion of New Jersey lottery winnings from taxable income. It was not until 2009, nine years after Mr. Milligan purchased his lottery ticket, that the Legislature first considered extending the gross income tax to some New Jersey lottery winnings.

Each of these factual distinctions supports this court's conclusion that the retroactive extension of the State income tax to Mr. Milligan's lottery winnings is barred by the square corners doctrine. While the Court in Klebanow examined the underlying constitutional authority of the State to impose an income tax retroactively, the Court did not have occasion to opine on the limits that are imposed on State action by the square corners doctrine. Thus, to the extent that Klebanow stands for the proposition that the State could, under circumstances different from those presented here, retroactively impose an income tax, the Court's holding does not limit the vitality of the square corners doctrine where the State's taxing power is used to bring about an untoward advantage to the State.

The court is well aware of the limitations on its authority in the area of State fiscal policy. "The power to raise revenue or to tax is among the most fundamental of governmental powers." In re: Commissioner of Ins. Orders A-92-189 and A-92-212, 137 N.J. 93, 98 (1994)(citing In re: Commissioner of Ins., 132 N.J. 209, 226 (1993)). As this court recently explained,

> [i]t is not the province of the judiciary to determine public policy. The elected representatives in the other branches of government are charged with the responsibility of formulating the State's public policy, including management of the public fisc.
>
> [Kite v. Director, Div. of Taxation, 29 N.J. Tax 75, 90 (Tax 2016), appeal pending.]

This court is hesitant to intrude on the prerogatives of the other branches of government, particularly with respect to the enactment of revenue raising measures during times of fiscal crisis. The parties and this court have no quarrel with well-established precedents bestowing on the Legislature and the Governor ample power to decide which of the many forms of income will be taxed. There can be no doubt that that power includes the ability to decide that New Jersey lottery winnings will be subject to gross income tax. Indeed, no party makes the argument that New Jersey lottery winnings from prizes awarded after the June 29, 2009 amendment of N.J.S.A. 54:6-11 may not be subject to income tax.

It is, however, the judiciary's obligation to apply legal precedents that limit the ability of the other branches of government to use their considerable powers in ways that trespass on the State's obligations to deal fairly with members of the public with whom it has entered financial arrangements. That obligation is violated when the State seeks to tax lottery winning from prizes awarded prior to January 1, 2009, where all participants in the financial transaction that resulted in the award of the lottery prize understood that the winnings would not be subject to State income tax.

In light of these findings of fact and conclusions of law, this court will enter an Order in each of the above-listed matters granting plaintiffs' motion for summary judgment, in part, and denying defendants' cross-motion for summary judgment, in part. Plaintiffs will be granted summary judgment in their favor with respect to their request for an Order declaring that assessment of gross income tax on installments of lottery winnings from the June 9, 2000 lottery prize received by plaintiffs on or after January 1, 2009 is prohibited by the square corners doctrine. Defendants will be denied summary judgment with respect to the same issue. The court reserves decision on both plaintiffs' motion for summary judgment and defendants' cross-motion for summary judgment on the remainder of the claims raised in the Complaints.