10-10-2011

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by Steve R. Johnson

The interaction of morality and money produces interesting results. One manifestation is legislation in some states and proposals in others to impose higher taxes on "gentlemen's show lounges" (OK, I mean strip clubs) and other venues of adult entertainment.

In 2010 and 2011 two state supreme courts passed on the legality of different forms of those taxes, upholding them against challenges that they infringed on free speech/free expression rights protected by the First Amendment of the U.S. Constitution. This installment of the column considers those two decisions: the February 2010 Utah decision in *Bushco v. Utah State Tax Commission*[1] and the August 2011 Texas decision in *Combs v. Texas Entertainment Association, Inc.*[2]

It is virtually certain that there will be additional litigation along these lines in the years to come. More states and localities will consider and enact similar measures. Those efforts will be fueled in part by America's moral ambivalence about erotic entertainment and in part by governments' never-ending quest for revenue in fiscally challenging times, and the states will be emboldened by the *Bushco* and *Combs* decisions. The adult entertainment industry can be counted on to challenge many or most of the enactments.[3]

Bushco *and* Combs *were correctly decided under current law.*

The first and second parts below describe *Bushco* and *Combs*, respectively. The third part generally describes relevant First Amendment doctrines. The fourth part applies those doctrines to *Bushco* and *Combs* and concludes that these cases were correctly decided under current law.

Bushco

In 2004 the Utah Legislature enacted a tax on sexually explicit businesses and escort services.[4] It imposes a 10 percent gross receipts tax on businesses whose employees or independent contractors either perform services while nude or partially nude for at least 30 days per year or provide companionship to another individual in return for compensation. Funds generated by the tax are dedicated to treatment programs for convicted sex offenders and investigation of Internet crimes against children.

A group of strip clubs and escort service agencies challenged the tax on First Amendment grounds.

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[1]*Bushco v. Utah State Tax Comm'n*, 225 P.3d 153 (Utah 2010), *cert. denied sub nom. Denali, L.L.C. v. Utah State Tax Comm'n*, 131 S. Ct. 455 (2010). (For the decision, see *Doc 2009-25835* or *2009 STT 224-25*.)

[2]*Combs v. Texas Entertainment Ass'n, Inc.*, __ S.W. 3d __, 2011 WL 3796572 (Texas Aug. 26, 2010). (For the Texas Supreme Court decision, see *Doc 2011-18326* or *2011 STT 167-28*.)

[3]The Texas statute at issue in *Combs* was expected to raise $44 million but has raised only $15 million thus far because strip clubs refused to pay the tax during the pendency of the litigation. Manny Fernandez, "Strip Club 'Pole Tax' Is Upheld in Texas," *available at* http://www.nytimes.com/2011/08/27/us/27texas.html?_n=1&pagewanted=print (Aug. 26, 2011).

[4]Utah Code Ann. sections 59-27-101 to 59-27-108 (2008).

The lower court upheld the tax on summary judgment. Over a dissent, the Utah Supreme Court affirmed.[5]

The *Bushco* plaintiffs maintained that the tax is content based. The Utah Supreme Court majority disagreed. It held that the tax is facially neutral because its application does not depend on the content of any protected speech and the record did not reflect that suppressing protected speech is the predominant purpose of the tax.[6] In particular, the majority said that the tax is triggered by nudity, which — because it "is not an inherently expressive condition" — is unprotected conduct instead of protected speech.[7]

Viewing the tax as a content-neutral regulation of conduct that burdens protected speech only incidentally, the majority applied intermediate scrutiny under the *O'Brien* standard. Under that standard, government regulation of conduct is upheld if:

- the measure is within the legislature's power to enact;
- the regulation furthers a substantial governmental interest;
- that interest is unrelated to suppression of protected speech; and
- any incidental effect it has on protected expression is not greater than essential to furthering the governmental interest.[8]

The majority concluded that all four prongs were satisfied.

In particular, the majority identified raising revenue to provide treatment for sex offenders as a substantial state interest, having "the twin goals of rehabilitation and prevention of future offenses."[9] Also, the majority believed that "any burdens the Tax imposes on protected expression are de minimis" — in part because establishments can avoid the tax "simply by having their erotic dancers use G-strings and pasties" and in part because "the exemption period allows business to use nudity as a means of expression for up to 30 days each calendar year without being subject to the Tax."[10]

One justice dissented. In his view, the statute entails a content-based tax on First Amendment expressive speech. Accordingly, strict scrutiny, not the *O'Brien* test, would apply. To the dissenter, strict scrutiny could not be satisfied because the statute is not a narrowly tailored measure to advance a compelling state interest.[11]

Combs

In 2007 the Texas Legislature enacted the Sexually Oriented Business Fee Act.[12] The act imposes on each "sexually oriented businesses" a "fee" of $5 for each entry by a customer who is admitted into the business. A business is sexually oriented if it is a nightclub, bar, restaurant, or similar commercial enterprise that:

- provides for an audience of two or more individuals live nude entertainment or live nude performances; and
- authorizes on-premises consumption of alcoholic beverages.

Under the act, nude means "(A) entirely unclothed; or (B) clothed in a manner that leaves uncovered or visible through less than fully opaque clothing any portion of the breasts below the top of the areola of the breasts, if the person is female, or any portion of the genitals or buttocks."[13] The business has discretion to determine how it derives the money required to pay the fee, so the business can choose whether to bear the incidence of the levy itself, raise admission fees on patrons, raise food or beverage charges, or pass the costs on to the entertainers. The first $25 million collected is to be credited to a state sexual assault program fund, and the remainder is to be used to provide medical insurance premium payment aid to low-income persons.

A sexually oriented business and an association representing sexually oriented businesses sued for declaratory and injunctive relief on the ground that the levy violates free speech rights. After a bench trial, the trial court held that:

- "erotic nude/topless dancing is protected expression under the First Amendment";
- the fee constitutes a content-based tax on such expression;
- a strict scrutiny standard applied;
- the state failed to meet its burden under that standard of showing "that the [tax] is necessary to serve a compelling state interest and [is] narrowly tailored for that purpose"; and

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[5]The escort service portion of the measure was invalidated because escort was defined in an unconstitutionally vague manner. 225 P.3d at 171. Our focus will be on the portion of the statute pertaining to strip clubs.

[6]225 P.3d at 159-63.

[7]*Id.* at 161 (quoting *Pap's A.M. v. City of Erie*, 529 U.S. 277, 289 (2000)).

[8]*United States v. O'Brien*, 391 U.S. 367, 377 (1968).

[9]225 P.3d at 167.

[10]*Id.* at 168-69.

[11]*Id.* at 172-76 (Durham, C.J., dissenting in part).

[12]Texas Bus. & Com. Code sections 102.051 to 102.056.

[13]The Utah legislation at issue in *Bushco* contained similar anatomical detail. Utah Code Ann. section 59-27-102(3); *cf. Ernoznik v. City of Jacksonville*, 422 U.S. 205, 213 (1975) (similar detail in an ordinance — held unconstitutional — aimed at some drive-in movie theater exhibitions). The state comptroller of public accounts narrowed the scope of the Texas levy by adopting a regulation exempting businesses holding occasional events such as wet T-shirt contests. Texas Admin. Code 3.722(c)(3).

- even should the tax be seen as content-neutral, it would fail the intermediate scrutiny standard that would then apply.[14]

Accordingly, the trial court held that the act violates the federal Constitution; it permanently enjoined the state from collecting the tax; and it granted the plaintiff attorneys' fees.[15]

A divided appellate court affirmed the trial court's decision. The majority saw the levy as a content-based tax directed at constitutionally protected expression through nude dancing. This was fatal because the state conceded that the levy could not withstand strict scrutiny.[16] The dissent thought that an intermediate scrutiny standard applied and was satisfied.[17] In contrast, the majority thought that the statute would fail even under that standard.[18]

The Texas Supreme Court, citing *Bushco*, unanimously reversed.[19] It maintained that the tax is not aimed at the expressive content of nude dancing but rather "at the secondary effects of the expression in the presence of alcohol."[20] The trial court had found that the state "presented persuasive trial evidence supporting a possible link between the business activity subject to the tax and the secondary effects addressed by the sexual assault program fund."[21] A principal legislative sponsor of the legislation, along with two organizations, filed an amicus brief with the supreme court asserting the link between "the dangerous combination of alcohol and live nude entertainment" and "an increased tendency for sexual violence."[22]

Accordingly, the Texas Supreme Court — as had the Utah Supreme Court — held that *O'Brien* provides the governing standard.[23] That standard was satisfied, the Texas court held, in part because the tax need not interfere with the expressive elements of nude dancing. First, "an adult entertainment business can avoid the fee altogether by not allowing alcohol to be consumed." Second, "the ban could be avoided simply by using pasties and G-strings." Third, "we think a $5 fee presents no [great] burden on nude dancing."[24] In short, the court thought any restriction on expression to be de minimis.

Current Doctrine

When considering threats to First Amendment rights, one usually thinks of other forms of governmental action. Yet taxes can be subject to First Amendment challenge. For example, the U.S. Supreme Court invalidated a Minnesota use tax imposed on the cost of paper and ink products consumed in production of large newspapers because the levy and its selective exemptions violated the First Amendment by significantly burdening freedom of the press.[25] In the main, First Amendment challenges to state and local taxes are evaluated under the same standards as challenges to other governmental actions.

Those standards are complex, however, and their application and evolution often are hard to predict. Sometimes free speech cases in the U.S. Supreme Court produce no majority opinion but only a patchwork of pluralities, concurrences, and dissents.[26]

The First Amendment provides that government "shall make no law . . . abridging the freedom of speech," but not all speech is treated equally. The Supreme Court has held that obscenity is a type of speech unprotected by the First Amendment.[27] Sexually oriented expression is not automatically obscene.[28] Nude dancing has been held to be protected,[29] but only barely.[30]

The Court has held that a jurisdiction may prohibit nude dancing entirely for the purpose of "protecting societal order and morality" and that measures to do so are aimed at conduct and effects, not at any message conveyed.[31] When the statute is animated predominately by concern with the secondary

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[14]*Texas Entertainment Ass'n, Inc. v. Combs*, 2008 WL 2307196 (Texas Dist. 2008).

[15]*Id. further op.* 2008 WL 2307197 (Texas Dist. 2008). Having resolved the case on federal constitutional grounds, the trial court found it unnecessary to reach the plaintiff's state constitutional claims.

[16]287 S.W.3d 852, 864 (Texas App. 2009).

[17]*Id.* at 870 (Puryear, J., dissenting).

[18]*Id.* at 864, n.12.

[19]Although the levy is called a "fee" by the statute, the appellate court concluded it really is a tax. The supreme court assumed it to be a tax, but this classification question was not central to the court's analysis. *See* 2011 WL 3796572, at *2.

[20]*Id.* at *7.

[21]2008 WL 2307197.

[22]Brief of Amici Curiae Representative Ellen Cohen and Texas Ass'n Against Sexual Assault & Texas Legal Services Center, No. 09-0481, at 4. Typically, evidence offered in litigation by legislators regarding the intent of the legislature in enacting a statute is given little weight by the courts. *E.g., Bread Political Action Committee v. FEC*, 455 U.S. 577, 582 n.3 (1982).

[23]Slip op. at *8.

[24]*Id.*

[25]*Minneapolis Star & Tribune Co. v. Minnesota Comm'r of Revenue*, 460 U.S. 575 (1983).

[26]*E.g., City of Erie v. PAP's A.M.*, 529 U.S. 277 (2000); *Barnes v. Glen Theater, Inc.*, 501 U.S. 560 (1991).

[27]*Roth v. United States*, 354 U.S. 476 (1957).

[28]*Id.* at 485.

[29]*Schad v. Borough of Mt. Ephraim*, 452 U.S. 61 (1981).

[30]"Nude dancing . . . is expressive conduct within the outer perimeter of the First Amendment, though we view it as only marginally so." *Barnes, supra*, 501 U.S. at 566 (plurality opinion); *cf. Young v. American Mini-Theaters, Inc.*, 427 U.S. 50, 70-71 (1976) (finding adult movies to be low-value speech, so that "the State may legitimately use the content of these materials as the basis for placing them in a different classification").

[31]*Barnes, supra*, 501 U.S. at 568 & 571 (plurality opinion); *see also City of Erie, supra* note 7.

effects of adult entertainment — such as crime, quality of life, and area deterioration — the regulation is content neutral (not content based), thus is subjected to less exacting scrutiny.[32]

Application of Doctrine

As a policy matter, I am not entirely happy with *Bushco* and *Combs* because they:

- uphold tax increases;
- invite pretextual governmental behavior (that is, encourage governments to say that measures really motivated by conventional morality instead are prompted by concern about secondary effects); and
- depend on the Supreme Court's changeable and sometimes disingenuous utterings in this area.

Nonetheless, as a matter of current doctrine, I think that *Bushco* and *Combs* were correctly decided. The combined effect of several doctrines of deference make it hard to successfully challenge legislative judgments in this area.

First, there is the notion that — revenue raising being fundamental to government — legislatures are allowed great leeway in how to tax. As the Supreme Court said:

> The States have a very wide discretion in the laying of their taxes. When dealing with their proper domestic concerns, and not . . . violating the guaranties of the . . . Constitution, the States have the attribute of sovereign powers in devising their fiscal systems to ensure revenue and foster their local interests. . . . The state may impose different specific taxes upon different trades and professions and may vary the rate of excise upon various products. It is not required to resort to close distinctions or to maintain a precise, scientific uniformity.[33]

Second, the states' traditional powers of regulation are heightened when, as in *Combs*, liquor is in the picture. The Supreme Court has upheld regulation of nude dancing in establishments serving alcohol, saying that the "broad sweep of the Twenty-first amendment has been recognized as conferring something more than normal state authority over public health, welfare, and morals."[34]

Third, legislative judgments regarding secondary effects are accorded great respect. Is it true that erotic performances or the mixture of those performances with alcohol increases sexual violence, crime, or other untoward consequences? The record is by no means clear. There are studies on both sides, and those studies are controversial.[35]

That being so, it is important that the factual record on which the restriction is predicated may be thin, indeed virtually nonexistent.[36] It is exceedingly difficult to challenge as empirically unsound a legislative conclusion that erotic dancing (or erotic dancing in conjunction with alcohol) leads to adverse secondary effects.

Some states and localities that wish to tax adult entertainment venues more heavily may be deterred from doing so by the realization that costly litigation is highly likely. If they are willing to bear those costs, however, they probably will prevail. Unless the U.S. Supreme Court substantially liberalizes current doctrine — something that does not seem likely any time soon[37] — future challenges to these taxes are likely to meet the same fate as in *Bushco* and *Combs*. ☆

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[32]*City of Renton v. Playtime Theater, Inc.*, 475 U.S. 41, 47 (1986). That position conflicts with the Court's acknowledgement in *Young, supra* note 30, a decade earlier that such restrictions are content based.

[33]*Allied Stores of Ohio, Inc. v. Bower*, 358 U.S. 522, 526-27 (1959). That is especially so because "courts as institutions are poorly equipped to evaluate with precision the relative burdens of various methods of taxation." *Minneapolis Star, supra* note 25, 460 U.S. at 589.

[34]*California v. LaRue*, 409 U.S. 109 (1972); *see also id.* at 118 (stating that states can constitutionally conclude "that certain sexual performances and the dispensation of liquor ought not to occur [in the same place]"); *City of Newport v. Iacobucci*, 479 U.S. 92 (1986).

[35]*See, e.g.*, Erwin Chemerinsky, *Constitutional Law Principles and Policies* 1050-1052 (4th ed. 2011); Nadine Strossen, *Defending Pornography* (1986).

[36]*E.g., City of Erie, supra* note 7, 529 U.S. at 296-302 (plurality opinion); *Barnes, supra* note 26, 501 U.S. at 585 (Souter, J., concurring in the judgment). *But see, City of Erie*, 529 U.S. at 317 (Stevens, J., dissenting); *id.* at 310 (Souter, J. dissenting) (repudiating his view in *Barnes*).

[37]The Court's recent decisions have generally been protective of the First Amendment. However, although the Court has held that new categories to which the First Amendment does not apply should not be invented lightly, it has reaffirmed traditional exceptions and limitations as to depictions of sexual conduct. *See e.g., Brown v. Entertainment Merchants Ass'n*, 131 S. Ct. 2729, 2734 (2011).