California: US Supreme Court refuses to hear multistate tax compact appeal

David M. Kall | Tuesday, October 18, 2016

Last December, the California Supreme Court issued its opinion in the case *Gillette Co. v. Franchise Tax Bd*. With the decision, the court put to rest any question as to whether lawmakers had the authority to deny Gillette, Proctor & Gamble, and Kimberly-Clark, among others, the option of choosing whether to use the Multistate Tax Compact's (Compact) apportionment formula, rather than one provided under California state law that would have resulted in a greater tax liability. The court held that lawmakers indeed have the authority to eliminate the Compact's election provision, meaning that the companies could not collect the $34 million in refunds to which they argued they were entitled.

The plaintiffs disagreed, and took their suit to the United States Supreme Court. In their May 27, 2016, *petition* asking the Court to hear their case, they argued that the Compact was designed, in part, to help companies that operate in multiple states avoid duplicative taxation. The possibility of duplicative taxation stems from the fact that states have different apportionment formulas to determine the percentage of the company's income tax is taxable by that state, which carries with it "complexity, burdensome compliance costs, and the risk of [multi-state companies] being taxed on more than 100 [percent] of their income."

The Compact "directly addressed" these concerns, according to the petition. Quoting its language, the petitioners asserted that the Compact is intended to "[f]acilitate proper determination of State and local tax liability of multistate taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes"; "[p]romote uniformity or compatibility in significant components of tax systems"; "[f]acilitate taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration"; and "[a]void duplicative taxation."

Many opined that the Court would not take the case. For example, in May, Bloomberg quoted the legal counsel for the Multistate Tax Commission (MTC), who did not think the suit posed a substantial federal question, and that it was not "essential" because "the decision was limited to what the compact was not – it is 'not a compact that required congressional approval… at that point, 'every issue becomes a state issue.'"

Gillette was one of several so-called Compact cases, and the MTC's counsel suggested that appeals of all of them would become moot if the Court decided not to hear it. The other Compact cases are the following:

- Minnesota's *Kimberly-Clark Corp. v. Comm'r of Revenue*, in which the Minnesota Supreme Court denied Kimberly-Clark's refund claim, affirming the lower court's decision;
- Michigan's *Gillette Commercial Operations N. Am. v. Dep't of Treasury*, a consolidated appeal in which the Court of Appeals also affirmed the trial court's conclusion that precluded the plaintiffs from using

the Compact's apportionment formula rather than the statutory one;

- Texas' *Graphic Packaging Corp. v. Hegar*, in which the Court of Appeals likewise concluded that the taxpayer could not use the three-factor apportionment formula; and
- Oregon's *Health Net, Inc. v. Or. Dep't of Revenue*, in which the Oregon Tax Court decided that Health Net Inc. did not have the right to the compact election on its state tax obligations.

At the Supreme Court, the Tax Foundation was one entity that filed a friend-of-the-court brief, in support of the companies seeking refunds. The crux of the argument was this:

> "Allowing California to unilaterally amend a compact it has adopted, rather than seeking to amend it or withdrawing from it, will undermine the entire concept of interstate compacts as binding agreements among states and strip the states of an incredibly important tool used to foster interstate cooperation. The U.S. Supreme Court has in the past recognized the importance of such agreements and the unique role they play in fostering cooperation among states, and should act to protect them from destruction. "

The State of Ohio was another supporter of the petitioners. In its amicus brief, which pointed out that Ohio has not signed on to the Compact, the Buckeye State nevertheless asserted an interest in the outcome because it is a party to other, similar multi-state compacts. Additionally, the authors professed that the California Supreme Court had committed two errors in its analysis that "create confusion about the proper standards for analyzing interstate compacts and could affect other agreements among the States." Accordingly, "Ohio has an interest in ensuring that interstate agreements are evaluated by clear, uniform standards."

On October 11, 2016, the United States Supreme Court denied the petition.

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