



MULTISTATE TAX COMMISSION

Maximizing the synergies of multi-state tax cooperation

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September 5, 2013

To: Governors, legislators, and tax administrators of states that are party to the Multistate Tax Compact

RE: Letter of August 28, 2013 from the NCSL Executive Committee Task Force on State and Local Taxation

You may have received a letter dated August 28, 2013, from the NCSL Executive Committee Task Force on State and Local Taxation. This letter attached a memorandum from Stephen P. Kranz of McDermott Will & Emery regarding “Issues Raised by State Membership in Multistate Compact.” The letter and the memorandum are inaccurate in their representations of the Multistate Tax Compact and incomplete in their information regarding the current litigation related to Article III of the Compact. Simply put, although the Commission would not normally respond to a communication of this nature, the effect of the inaccuracies and lack of complete information is so misleading that we are compelled to do so.

INACCURACIES ADDRESSED

Q. Can your state be bound by rules “even when those rules have not been legislatively adopted by the state”?

A. No (setting aside federal rulemaking for purposes of this discussion). Moreover, your state’s laws create and sustain the Commission. Your state’s top tax official is a member of the Commission established by the Compact that your state’s legislature adopted and your state’s governor signed into law.

Q. Can the Commission adopt or do anything that imposes rules on your state or binds your state’s legislature with respect to tax policy or binds your state’s executive branch with respect to tax administration?

A. Again, despite the representations in the letter and memorandum, the answer is no. Article VII of the Compact is the article that provides for the Commission’s uniformity work. The very last section of Article VII provides that states consider any such regulation (by convention, any uniformity proposal) for adoption “in accordance with its own laws and procedures.” Therefore, your state—not the Commission—determines which rules will apply to your state. The Commission simply adopts recommendations for uniform tax administration. The U.S. Supreme Court agrees: “[E]ach State retains complete freedom to adopt or reject the

rules and regulations of the Commission.” *U.S. Steel Corp. et al. v. Multistate Tax Commission*, et al., 434 U.S. 452 (1978).

So no state is “at risk” of anything with respect to the uniformity activities of the Commission. The Commission consists of the head of each state agency charged with the administration of income taxes or sales and use taxes for those states which have adopted the Multistate Tax Compact (Compact, Art. VI). As an intergovernmental state tax agency, the Commission has, from its inception in 1967, always functioned as an adjunct to your state’s tax agency in an advisory role. The U.S. Supreme Court called it in *U.S. Steel* in 1978: There never was any “delegation of sovereign power” to the Commission. We work for you and your state.

INCOMPLETE INFORMATION CORRECTED

Q. What is at issue in *Gillette Co. v. Franchise Tax Bd.*, 209 Cal. App. 4th 938 (2012) and those other cases?

A. The core issue in those cases is an election that most states adopted when they adopted the Multistate Tax Compact. This election, contained in Article III, on its face allows multistate taxpayers to follow Article IV of the Compact, which contains the Uniform Division of Income for Tax Purposes Act (UDITPA), or the state’s laws, if different, with respect to allocation and apportionment. As Compact states began to deviate from UDITPA with respect to allocation and apportionment, they used various methods to disable the election. *Gillette* deals specifically with California’s method of disabling the election, and the other cases deal with the viability of the election as it related to those specific states’ laws and history.

The issue common to all of these cases is whether or not the Compact is a binding contract among the party states that may not be unilaterally modified (e.g., through some lawmaking to disable the Article III election). The taxpayers in these cases are asserting that this is so, and that they are entitled to the election. The states assert that the Multistate Tax Compact is not a regulatory or boundary compact that requires it to be absolutely binding on all the states that are party to it, but rather an advisory compact allowing some individual state variation acceptable to the other Compact states. The Commission’s legal staff has been active in their support for the states facing these cases, and will continue to be so.

There are several cases beyond the administrative stage; the letter and memorandum highlighted the only two where the taxpayers prevailed. *Gillette* is the furthest along, with briefing nearly done in the California Supreme Court. The taxpayers won at the appellate court level in *Gillette*. Also pending at the state supreme court level is the first of three Michigan cases, *Int’l Bus. Mach. Corp. v. Dep’t of Treasury*, No. 306618 (Mich. Ct. App., Nov. 20, 2012). The state prevailed at the appellate level. Two other Michigan cases are being appealed from a lower court level, one a taxpayer win, *Anheuser-Busch, Inc. v. Mich. Dep’t of Treasury*, No. 11-85-MT (Mich. Ct. Cl., June 6, 2013), and the other a state win omitted from the letter and memorandum you received, *Lorillard Tobacco Co. v. Mich. Dep’t of Treasury*, No. 11-93-MT (Mich. Ct. Cl., Oct. 22, 2012). Cases in Texas and Oregon are pending at the trial court level, *Graphic Packaging Corp. v. Combs*, District Court of Travis County, Tex., 353rd Judicial

District, No. D-1-GN-12-003038; and *Health Net, Inc. v. Or. Dept. of Rev.*, Or. T.C., No. TC 5127.

CONCLUSION

The litigation regarding the Article III election is a significant matter for Compact states. Because of its significance, we do encourage you to discuss these matters with your state's top tax and legal officials, and not rely on self-serving advice from private industry interests.

The Commission's staff is also ready to address any questions and concerns you may have and continue to serve your state's interests as it has been doing for more than 45 years. Please do not hesitate to contact Joe Huddleston, Executive Director, or Shirley Sicilian, General Counsel, at jhuddleston@mtc.gov or ssicilian@mtc.gov, respectively, or by calling the Commission at 202-650-0300.

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