

# Multistate Tax Compact Article III Background and Issues

MTC Litigation Committee Meeting  
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*Shirley Sicilian*

*General Counsel*

*Multistate Tax Commission*

# History

- 1957 – UDITPA (Uniform Law Commission)
- 1959 – *Northwestern States Portland Cement*  
358 U.S. 450 (1959)
- 1959 – PL 86-272 (15 U.S.C. § 381)
  - Pre-emption
  - Willis Committee
- 1967 – State Enactments
  - UDITPA
  - Compact
  - Both
- Model Multistate Tax Compact
  - Effective after enactment by seven states in August 1967

# Multistate Tax Compact

Overarching

- **Article I.** Purposes
- **Article II.** Definitions

Income

- **Article III. Elements of Income Tax Laws**
  - Taxpayer Option, State and Local Taxes
  - Taxpayer Option, Short Form
  - Coverage

Sales

- **Article IV. Division of Income (UDITPA)**
- **Article V.** Elements of Sales and Use Tax Laws
  - Tax Credit
  - Exemption Certificates. Vendors May Rely

Commission

- **Article VI.** The Commission
- **Article VII.** Uniform Regulations and Forms
- **Article VIII.** Interstate Audits
- **Article IX.** Arbitration

Operation

- **Article X.** Entry Into Force and Withdrawal
- **Article XI.** Effect on Other Laws & Jurisdiction
- **Article XII.** Liberal Construction; Severability

# Multistate Tax Compact

- **Suggested Enabling Act:** “The ‘Multistate Tax Compact’ is hereby enacted into law and entered into with all jurisdictions legally joining therein, *in the form substantially as follows*: ...”
- **Article I (Purposes)**
  1. Facilitate proper determination of State and local tax liability of multistate taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes.
  2. *Promote uniformity or compatibility* in significant components of tax systems.
  3. Facilitate taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration.
  4. Avoid duplicative taxation.

# Multistate Tax Compact

## Art. IV [UDITPA]

- Which industries covered
- How apportionment performed
  - “Business/Non-Business” income
  - Apportionment
    - Formula – (3 factor equal-weighted)
    - Factor definitions
    - Numerator sourcing
  - Allocation
- Distortion relief

# Multistate Tax Compact

## Art. III.1

- “Any taxpayer ....may elect to apportion and allocate his income in the manner provided by the laws of such States or by the laws of such States and subdivisions without reference to this compact, *or may elect to apportion and allocate in accordance with Article IV. [UDITPA]*”
- “... This election *for any tax year* may be made *in all party States* or subdivisions thereof *or in any one or more* of the party States or subdivisions thereof without reference to the election made in the others.  
...”

# Multistate Tax Compact

- **Art. X.2** “Any party State may withdraw from this compact by enacting a statute repealing the same. ...”
- **Art. XII** “severable”
- **Art. XII** “shall be liberally construed to effectuate its purposes”

# State Enactments

- 1970 – Commission list 20 States where “Compact has been enacted as a uniform law”
- 1967 to 1973 – seeking Congressional consent
- 1972 – Florida Resolution
- 1978 – *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 U.S. 452 (1978)
- 1978 – *Moorman Mfg. Co. v. Bair*, 437 U.S. 267 (1978)

# California

- Timeline
  - 1966: UDITPA
  - 1973: Compact
  - 1993: “Notwithstanding [the Compact], all business income shall be apportioned to this state [using double-weighted sales]”

# Compact States

- Forty-seven Commission member states
- Nineteen Compact member states

- 10** {
- 6 states have little deviation (AK, HI, MT, NM, ND, KS)
  - 3 states don't have corporate income tax (SD, WA, (TX))
  - 1 state allows election (MO)

- 9** {
- 3 states omit or limit Article III.1 directly (CO, MI, MN)
  - 3 states modified Article IV.9 (AL, AR, UT)
  - 3 states limit Art. III.1 by separate statute (DC, OR, ID,[CA])

# California

- Timeline
  - 1966: UDITPA (CR&TC §§ 25120-25139)
  - 1973: Compact (CR&TC § 38006)
  - 1993: “Notwithstanding [the Compact], all business income shall be apportioned to this state [using double-weighted sales]” (CR&TC § 25128)
  - 2006: TPs amend returns and file for refunds

# Issues

- Did the State modify?
- Can the State modify?
  - Is it a “Compact?”
  - If Compact, how interpreted?
    - Plain Language?
    - Course of Performance?
    - Consistent with Compact Purposes?

# California – *Gillette*

- Trial Court – found for State
- Court of Appeals – found for Taxpayer
  - Multistate Tax Compact is a contract  
(*Seattle Master Builders*, 786 F.2d 1359 (9th Cir. 1986)(three prong test))
  - Compact’s terms do not allow modification  
(course of performance irrelevant)
  - State may not impair obligations of contracts  
(Contract Clause, U.S. Const., art. I, § 10)
  - Reenactment rule prohibits modification by reference anyway  
(Cal. Const., art. IV, § 9)
- Supreme Court – will review, CoA decision “depublished”

# California – *Gillette*

- What's next?
  - California Supreme Court
    - State's opening brief due March 18
    - Amicus Briefs (members, MTC)
  - SB 1015
    - Compact repealed, June 2012
    - “Doctrine of election” applies
    - Likely subject of future litigation
  - US Supreme Court?

# Michigan – *IBM*

- Timeline

- 1969: UDITPA and Compact enacted
- 1975: SBT enacted
  - » conforms to UDITPA, but not an income tax
  - » 1991-2007: progressive increases in SBT sales weighting enacted, from 40% to 92.5%
- 2008: MBT enacted
  - » income and modified gross receipts tax
  - » 100% sales factor
- 2009: TPs amend returns, begin filing refund claims
- 2011: Compact Art.III amended
  - » “... except that beginning Jan. 1, 2011 any taxpayer subject to the MBT or CIT shall apportion and allocate in accordance with the provisions of that act and shall not apportion or allocate in accordance with article IV” (MLC 205.581)

# Michigan – *IBM*

- Trial court – found for State
- Court of Appeals – found for State
  - Multistate Tax Compact is not a contract
  - Compact Art.III.1 not required (compare Art. III.2)
  - MBT repealed Compact by implication
  - Concurrence: UDITPA Sec. 18 overrides Art. III
  - Amicus briefs (Michigan Manufacturers Assoc., MTC)
- Michigan Supreme Court – Leave to appeal requested

# Michigan – *IBM*

- What's next?
  - Decision by MI SC on whether to grant leave to appeal expected in April/May 2013
  - If MI SC grants leave, final decision, after briefing and oral argument, expected around December 2013
- Other cases:
  - *Lorillard* – pending before MI Court of Appeals; awaiting oral argument
  - Additional cases pending in MI Tax Tribunal or Court of Claims
  - Additional cases at Department level

# Oregon – *Health Net*

- *Health Net, Inc. and Sub's v. DOR*, Oregon Tax Court, No. 120649D (filed July 2, 2012)
  - 1965: UDITPA
  - 1967: Compact
  - 1993 (retroactive to 1991): “In any case in which the provisions of [Oregon’s separate UDITPA statutes] are inconsistent with the provisions of [the Compact], the provisions of [Oregon’s separate UDITPA statutes] shall control.” Or. Rev. Stat. § 314.606

# Texas – *Graphic Packaging*

- *Graphic Packaging Corp. v. Combs* , Dist. Court of Travis County, Texas, 353rd Jud. Dist., No. D-1-GN-12-003038 (filed Sep. 27, 2012)
  - 1981: Compact
  - 2011: “The apportionment provision in TTC Chapter 141, related to the Multistate Tax Compact (MTC), does not apply to the revised Texas franchise tax and entities may not elect to use the MTC's three-factor apportionment formula in lieu of the formula specified in Texas Tax Code Chapter 171.” Policy Letter Ruling 201007003L (2010)

# Implications

- Considerations for Taxpayers
- Considerations for Compact States