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## ***Gillette files Answer Brief on Merits – Submits previously uncovered documents***

July 22, 2013

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### ***In brief***

On July 16, 2013, Gillette filed an answer brief on the merits before the Supreme Court of California in the matter of *Gillette Company and Subsidiaries v. California Franchise Tax Board*. Of significant note are the numerous documents submitted for the record that were only recently discovered.

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### ***In detail***

In July 2012, the California Court of Appeal in *Gillette Company and Subsidiaries v. California Franchise Tax Board* struck down the Franchise Tax Board's attempt to override the Multistate Tax Compact on three independent bases: 1) Compact law superseded subsequently enacted conflicting state law; 2) federal and state constitutions prohibit states from passing laws that impair contracts; and 3) the FTB's construct of the effect of subsequent state law runs afoul of the reenactment clause of the California constitution.

In January 2013, a petition for review was granted and opening briefs were filed in April. On July 16, 2013, an answer brief on the merits was filed by the taxpayers with the California Supreme Court. Of significant note are the accompanying

exhibits submitted into the record of previously uncovered historical documents that relate to the enactment, interpretation, and application of the Multistate Tax Compact.

#### ***Exhibits***

Seven documents were submitted to the court related to the proceedings. Most of the documents were prepared in the 1960s by the Council of State Governments (CSG), the governmental agency that drafted the Multistate Tax Compact. [Exhibit N](#), a CSG memo written on December 20, 1966, directly addresses the issue at the heart of the *Gillette* case. The memo states “[f]or almost a year a Multistate Tax Compact has been in the process of development under the auspices of the Council of State Governments . . . . The basic objective of the compact is to provide solutions and additional

facilities for dealing with a number of tax problems of multistate businesses, notably the ones identified by the Willis Subcommittee of the House Committee on the Judiciary . . . . One of the principal measures for improvements – i.e. simplification of taxpayer compliance and elimination of the possibility of double taxation – in the income tax field is the Uniform Division of Income for Tax Purposes Act . . . . The compact would permit any multistate taxpayer, at his option, to employ the Uniform Act for allocations and apportionments involving party states of [sic] their subdivisions. Each party state could retain its existing division of income provisions but it would be required to make the Uniform Act available to any taxpayer wishing to use it.”

A January 20, 1967, Summary and Analysis document prepared by the CSG re-emphasizes the commitment to an apportionment election. Submitted as [Exhibit S](#), the document states once again the ability of any taxpayer “at his option, to employ the Uniform Act for allocations and apportionments.” The Summary and Analysis document notes the ramifications of the *Northwest Portland Cement* case, including the enactment of Public Law 86-272 and the formation of the Willis Subcommittee, which promoted enactment of federal legislation that would have created uniformity at the cost of restricting state taxing power. The CSG document notes that “[u]niformity in State laws is generally considered to be a desirable objective, but a balance must be struck between a required uniformity and State and local independence. The ability of States to vary their policies to meet their own particular needs and the specific preferences of their inhabitants is a cardinal virtue of the American form of government. . . . On the other hand, multistate taxpayers are often willing to forego the advantages of uniformity in order to benefit from particular State and local policies that may serve both their

needs and those of the governmental units in question. The Multistate Tax Compact provides that the Uniform Act will be available in all party states to any multistate taxpayer wishing to use it. Consequently, taxpayers will be able to have the benefits of uniformity whenever they want it.”

### ***Brief***

In its brief, Gillette claims California’s 1993 law change to double weight the sales factor was an invalid attempt to alter an interstate compact. Gillette claims that party states may not unilaterally amend compacts piecemeal through subsequent legislation. Gillette further argues that the Compact election is mandatory for party states and the lack of Congressional approval of the Compact does not change the fundamental nature and precedence of the Compact. Gillette notes that the express terms of the Compact are unambiguous and, as such, do not permit an interpretation that would allow for a partial repeal of certain provisions. To permit such an interpretation would render Article VIII, which allows a state to opt out of the audit provisions, superfluous. In addition, because its terms are unambiguous, extrinsic evidence is

unnecessary. Thus, the FTB’s arguments concerning subsequent party conduct must be rejected. However, if the court were to consider extrinsic evidence, the contemporaneous drafting history would be most probative of the parties’ intent. This history is reflected in the exhibits submitted along with the brief, including the memoranda from the Council of State Governments.

Michael Herbert observes, “What is striking in these documents is the clear benefit the states received from entering into the compact. They retained their sovereignty over state apportionment. They did not surrender it.”

Gillette also noted that permitting a partial repeal of the Compact will have ramifications beyond state tax issues, as it would jeopardize many California interstate compacts, such as compacts addressing juveniles and adult offenders.

Finally, Gillette noted that the 1993 law change violated the contract clause of the US and California constitutions and the constitutional reenactment rule.

## ***Let’s talk***

To discuss how this issue might affect your business, please contact our authors:

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