On September 11, 2014, Michigan Governor Rick Snyder signed S.B. 156, which purports to repeal the state’s adoption of the Multistate Tax Compact (the Compact) retroactive to January 1, 2008. Mich. Pub. Acts 2014, No. 282 (S.B. 156). As explained by the Senate Fiscal Agency’s Bill Analysis, “the bill would prevent the State from paying approximately $1.1 billion in MBT refunds . . . as a result of a recent Michigan Supreme Court decision.” The referenced decision is the IBM case, in which the court upheld a taxpayer’s right to elect to use the Compact’s equally weighted three factor apportionment formula for the 2008 tax year. Int’l Bus. Machines Corp. v. Dep’t of Treasury, 496 Mich. 642 (July 14, 2014), mot. for reh’g pending (filed Aug. 4, 2014).

How did we get here and where could this saga lead? This Legal Alert provides context for these questions.

**Michigan’s Enactment of the Compact and the IBM Decision**


Under the MBT, taxpayers began electing to apportion their income using the Compact Election in lieu of the MBT’s statutory single sales factor formula. As Compact Election claims mounted, on May 25, 2011, the Legislature amended its adoption of Article III of the Compact, purporting to repeal the availability of the Compact Election effective for tax years beginning on or after January 1, 2011. Mich. Laws 2011, Pub. Act No. 40 (H.B. 4479). The 2011 Legislature did not completely repeal the state’s adoption of the Compact, nor did it attempt to repeal the Compact Election provision retroactively.

In July of this year, the Michigan Supreme Court upheld IBM’s right to make the Compact Election under both components of the MBT for the 2008 tax year. The court held that the Legislature did not repeal the availability of the Compact Election when it enacted the MBT in 2007, despite the MBT’s single sales factor tax.
formula, because “[r]epeals by implication are rare” and “if the Legislature had intended to repeal [the Compact], it would have done so explicitly,” IBM at *6. The court was also persuaded that the Legislature’s 2011 repeal of the Compact Election provision “is evidence that the Legislature had not impliedly repealed the provision [earlier].” Id.

Sutherland Observation: IBM was decided solely on statutory construction grounds and held that state law authorized the Compact Election. As such, it did not need to reach the question at issue in California’s Gillette case\(^1\) – whether the Compact is a binding interstate compact that would trump a later-enacted statute – although the dissent would have found it not to be a binding compact. In another case that remains pending on appeal, the Michigan Court of Claims adopted the Gillette reasoning and held that the Compact was binding until repeal. See Anheuser-Busch, Inc. v. Michigan Dep’t of Treasury, Case No. 11-85-MT (Order and Opinion, Mich. Ct. of Claims June 6, 2013) (Collette, J.), appeal docketed (Mich. App. No. 316743).

Michigan’s Reaction to IBM: Deny, Deny, Deny

On August 4, 2014, the Michigan Department of Treasury asked the court to reconsider its decision in IBM, estimating that it would potentially owe a “budget-busting” $1.1 billion of tax refunds, plus interest, if the decision stands. While that request for reconsideration remains pending, the Legislature swiftly (and without hearing or floor debate) intervened and enacted S.B. 156 on September 11, 2014. S.B. 156 provides that:

1. The entire Compact “is repealed retroactively and effective beginning January 1, 2008;” and

2. The retroactive repeal of the Compact “is to express the original intent of the legislature” when it enacted the MBT in 2007 and again when it repealed the Compact’s election provision prospectively in 2011.\(^2\)

In other words, the expressed intent of S.B. 156 is to clarify in 2014 that the 2011 legislation clarified that the 2007 legislation intended to repeal Michigan’s 1970 adoption of the Compact, in its entirety, for the purpose of eliminating the availability of the Compact Election. Governor Snyder praised the Legislature for enacting legislation that “eliminates a loophole” in the 1970 statute. As a result of the repeal, Michigan joins a growing number of states that have repealed the Compact (e.g., California, the District of Columbia, Minnesota, Oregon, and Utah) and is the only state to have attempted to do so retroactively.

Sutherland Observation: Retroactively repealing the Compact more than six years into the past raises a host of issues. One might question
how a legislature, whose membership has materially changed over the course of six years, can “express the original intent” of a prior legislature. A six-year period of retroactivity also calls into question the law’s constitutionality under the Due Process Clause. See United States v. Carlton, 512 U.S. 26 (1994). While the Michigan Court of Appeals has upheld retroactive denials of tax refunds in the past, it is unclear what Michigan courts will do when confronted with what can reasonably be viewed as a legislative overruling of a judicial decision while numerous taxpayers’ cases remain pending. See Gen. Motors Corp. v. Dep’t. of Treasury, 290 Mich. App. 355 (2010). Moreover, under the reasoning of Gillette, a state legislature could not repeal its adoption of the Compact on a retroactive basis, as “any repealing legislation must be prospective in nature, because [Article X of the Compact provides that] it cannot ‘affect any liability already incurred by or chargeable to a party State prior to the time of such withdrawal.’” Gillette, 147 Cal. Rptr. 3d at 614. Finally, taxpayers should be aware that Michigan law provides that refund claims challenging the constitutionality of tax laws must be filed within 90 days from the date set for filing a return. MCL § 205.27a(7).

Conclusion

For those who thought the IBM decision would finally resolve the Compact Election question in Michigan, think again. Michigan’s retroactive repeal of the Compact is almost certain to be challenged and adds a host of new issues to be evaluated by taxpayers in this continuing game of “now you see it – now you don’t.”


2 Other portions of the tax legislation have a retroactive period back only to January 1, 2010.

If you have any questions about this Legal Alert, please feel free to contact any of the attorneys listed under ‘Related People/Contributors’ or the Sutherland attorney with whom you regularly work.