IN THE SUPREME COURT OF THE STATE OF OREGON

HEALTH NET, INC. and SUBSIDIARIES, Plaintiffs-Appellants, vs. **DEPARTMENT OF REVENUE, State of Oregon,** Defendant-Respondent.	Tax Court (Regular Division) Case No. TC 5127 S063625

BRIEF OF *AMICI CURIAE* THE STATES OF TEXAS, ALASKA, ARKANSAS, CALIFORNIA, HAWAII, IDAHO, MICHIGAN, MINNESOTA, MISSOURI, MONTANA, NORTH DAKOTA, UTAH, AND WASHINGTON, AND THE DISTRICT OF COLUMBIA IN SUPPORT OF DEFENDANT-RESPONDENT

On Appeal from the Judgment of the Oregon Tax Court
The Honorable Henry C. Breithaupt

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June 2016

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I. IDENTITY AND INTEREST OF *AMICI CURIAE*

The States of Texas, Alaska, Arkansas, California, Hawaii, Idaho, Michigan, Minnesota, Missouri, Montana, North Dakota, Utah, and Washington, and the District of Columbia ("*amici* states") have an interest in this case because it involves the proper construction and application of the Multistate Tax Compact.

The *amici* states include the following members of the Compact, which have enacted the Compact in their statutory laws: Alaska, Arkansas, Hawaii, Idaho, Missouri, Montana, North Dakota, Texas, Utah, and Washington, and the District of Columbia. Through their Compact membership, those jurisdictions govern the Multistate Tax Commission, the intergovernmental agency created by the Compact to address multistate taxation issues and preserve members' sovereign authority over their tax policies. The *amici* states also include California, Michigan, and Minnesota, which are former members of the Compact and current members of the Commission. Those states participate in the Commission's activities, meetings, or programs.

The *amici* states appear to address the meaning of the Compact from the perspective of current Compact and Commission members and to discuss the proper analysis of interstate compacts, such as this one, that neither require nor receive congressional approval.

II. STATEMENT OF THE CASE

The *amici* states adopt the Statement of the Case as set forth by the Department of Revenue in its Respondent's Brief at 1-5.

III. SUMMARY OF THE ARGUMENT

The *amici* states fully concur with the Department of Revenue's position that the Multistate Tax Compact is not a binding compact that contractually precludes its members from disallowing the apportionment election in Article III.1 and enacting an exclusive apportionment formula. In support of affirming the Tax Court's judgment, the *amici* states will emphasize several points to supplement the Department's arguments.

The fact that the Multistate Tax Compact is labeled a "compact" and uses the compact form does not necessarily mean that it is a binding regulatory compact. Considered as a whole, the Compact is in the nature of a non-binding advisory compact that includes model laws.

That conclusion is reinforced by examining one untenable consequence of Health Net's competing view of the Compact. Under Health Net's construction, each Compact state contracted away its power to tax the part of a taxpayer's tax base that the taxpayer removes from the state's jurisdiction by electing the Compact's apportionment formula under Article III.1. But that interpretation would clash with those Compact states' constitutions that prohibit

contractual suspensions of taxation power—a conflict that the Compact's drafters expressly sought to avoid.

Moreover, because states do not easily cede their sovereignty as a general matter, it is settled that any relinquishing of sovereign power must be expressed in unmistakable terms. Here, the Compact does not address what happens when a state apportionment method by its very terms cannot be elective because state law expressly makes it exclusive. That lack of unmistakable language must mean that the states reserved the power to enact exclusive apportionment laws. Other construction aids support that reading, such as the states' longstanding course of performance and comparisons to other compacts' language.

Even if Health Net could establish that the Compact's apportionment election is contractually binding, that provision would not automatically trump the Compact states' apportionment laws. Because the Compact neither required nor received congressional approval, its preeminence over its members' state laws hinges on the constitutional prohibition against impairing contractual obligations. Under the United States Constitution, only a substantial impairment that is not reasonable and necessary to accomplish an important public purpose is invalid. Health Net is simply wrong in suggesting that interstate compacts are governed by a special federal standard that renders any impairment unconstitutional.

Under the proper test, the constitutionality of an alleged contractual impairment depends heavily on the extent to which the impairment upsets relevant reliance interests. This factor favors the Compact states. The Compact members have construed the Compact to allow them to adopt and enforce exclusive apportionment formulas for over forty years. States have relied on that construction in choosing to join and remain in the Compact, and those with exclusive formulas have factored them into their revenue estimates and budget appropriations. By contrast, Health Net is neither a party nor a third-party beneficiary of the Compact. And even if Health Net were a beneficiary, it could not reasonably rely on the Compact's taxpayer-election provision because a state can withdraw from the Compact unilaterally at any time. Under these circumstances, even if Health Net could credibly claim some contractual right under the Compact, that right was not unconstitutionally impaired.

IV. RESPONSE TO ASSIGNMENT OF ERROR

The *amici* states adopt the Response to Assignment of Error as set forth by the Department of Revenue in its Respondent's Brief at 5-6.

V. ARGUMENT

A. Compact States May Disallow the Apportionment Election Because the Multistate Tax Compact Is Not A Binding Regulatory Compact.

Health Net claims that Oregon cannot preclude taxpayers from invoking Article III.1 of the Multistate Tax Compact, which provides that a multistate

taxpayer "may elect to apportion and allocate his income in the manner provided by the laws" of a Compact state or "may elect to apportion and allocate in accordance with [the three-factor apportionment formula] in Article IV." ORS 305.655, Art III.1. But the Compact does not contractually bar its members from disallowing Article III.1's apportionment election in their respective tax laws. The Compact is in the nature of an advisory compact containing model laws, not a binding regulatory compact that carries the preemptive force that Health Net assigns to it.

1. The compact label and form do not make the Compact contractually binding.

Contrary to the assertions of Health Net and its *amici*, *see* Appt Br 20-21; ICJ Br 7-9; COST Br 17-19, the use of the "compact" label or the compact form does not resolve whether the Compact contractually obligates its members to maintain the operation of Articles III.1 and IV in state law. Only "*in some contexts*" is a compact "a contract between the participating states." *McComb v. Wambaugh*, 934 F2d 474, 479 (3d Cir 1991) (emphasis added).

Interstate compacts are generally classified into three categories—"boundary," "regulatory," and "advisory"—but only the first two potentially create a binding contract. Caroline N. Broun, *et al.*, *The Evolving Use and the Changing Role of Interstate Compacts: A Practitioner's Guide* 12-15 (2006). Boundary compacts "establish official borders between states" "with a high degree of finality." *Id.* at 12, 13. And in many regulatory compacts, "the

member states have collectively and contractually agreed to reallocate governing authority away from individual states to a multilateral relationship." *Id.* at 21-22.

By contrast, "nonbinding" advisory compacts "are more akin to administrative agreements between states," which "lack formal enforcement mechanisms." *Id.* at 13, 14. "[A]dvisory compacts cede no state sovereignty nor delegate any governing power to a compact-created agency." *Id.* at 14. And they "generally do not require congressional consent." *Id.* As discussed below the Compact most closely fits this advisory-compact category.

2. The Compact does not exhibit the indicia of a binding regulatory compact.

The United States Supreme Court has identified three "classic indicia" of a binding regulatory compact: (1) the establishment of a joint regulatory body; (2) state enactments that require reciprocal action to be effective; and (3) the prohibition of unilateral repeal or modification of its terms. *See Ne. Bancorp, Inc. v. Bd. of Governors of Fed. Reserve Sys.*, 472 US 159, 175, 105 S Ct 2545, 86 L Ed 2d 112 (1985); *see also Seattle Master Builders Ass'n v. Pac. Nw. Elec. Power & Conservation Planning Council*, 786 F2d 1359, 1363 (9th Cir 1986), *cert den*, 479 US 1059 (1987). As the California Supreme Court recently held, the Compact does not exhibit any of these characteristics. *Gillette Co. v. Franchise Tax Bd.*, 62 Cal 4th 468, 478-83, 363 P3d 94 (2015), *pet for cert filed* (US May 27, 2016) (No. 15-1442).

a. The Commission is not a joint regulatory body.

The first trait of a binding regulatory compact is creation of a "joint organization for *regulatory* purposes," *Seattle Master Builders*, 786 F2d at 1363 (emphasis added); *see also Ne. Bancorp*, 472 US at 175. By contrast, an advisory compact "cede[s] no state *sovereignty* nor delegate[s] any *governing* power to a compact-created agency." Broun, *Interstate Compacts* at 14 (emphases added).

The Compact does not create a joint regulatory body. *Gillette*, 62 Cal 4th at 481-83. It forms the Multistate Tax Commission, ORS 305.655, Art VI, but that agency does not qualify. As the United States Supreme Court noted in a case challenging the Compact's validity: "Nor is there any delegation of sovereign power to the Commission; each State retains complete freedom to adopt or reject the rules and regulations of the Commission." *U.S. Steel Corp. v. Multistate Tax Comm'n*, 434 US 452, 473, 98 S Ct 799, 54 L Ed 2d 682 (1978); *see also* ORS 305.655, Art VII.3 (providing that the Commission shall submit regulations to the states to "consider any such regulation for adoption in accordance with its own laws and procedures"). Aside from drafting non-binding rules, the Commission's other powers also evince an advisory compact. *Compare* ORS 305.655, Art VI.3 (granting the Commission power to "[s]tudy state and local tax systems," "[d]evelop and recommend proposals," and "[c]ompile and publish information"), *with* Broun, *Interstate Compacts* at 13

(explaining that advisory compacts "are designed not to actually resolve an interstate matter, but simply to study such matters"). The Commission conducts audits only upon request. ORS 305.655, Art VIII.2. And its arbitration functions are inoperative. *See U.S. Steel*, 434 US at 493 (White, J., dissenting).[1]

b. The Compact provisions do not require reciprocal action to be effective.

The second feature of a binding regulatory compact is the inclusion of "state enactments which require reciprocal action for their effectiveness." *Seattle Master Builders*, 786 F2d at 1363; *see also Ne. Bancorp*, 472 US at 175. For example, the Interstate Compact for Adult Offender Supervision provides a mechanism for Oregon parolees to serve their parole in other compact states, and vice-versa. *See* ORS 144.600, Art I. That agreement requires reciprocal action to be effective because, among other things, a "sending" state "transfer[s] supervision authority" over a parolee to a "receiving" state, which in turn must allow a sending state's officials to enter the receiving state to "retake" an offender for a parole violation. *See id.*

The Multistate Tax Compact does not similarly require reciprocal action to effect its substantive terms. *Gillette*, 62 Cal 4th at 478-80. The Compact "does not purport to authorize the member States to exercise any powers they could not exercise in its absence." *U.S. Steel*, 434 US at 473. Absent the

[1] Since *U.S. Steel*, the Commission has not enacted a regulation activating the arbitration provision.

Compact, each state administers its tax laws, including the apportionment of its business tax base, without reference to or consideration of other states' laws. *See Moorman Mfg. Co. v. Bair*, 437 US 267, 278-79, 98 S Ct 2340, 57 L Ed 2d 197 (1978) (noting that states enact differing apportionment formulas "based on political and economic considerations that vary from State to State"). The Compact does nothing to change that. A Compact state can allow a taxpayer to exercise Article III.1's option and use Article IV to apportion its business income regardless of how other states tax or apportion that income or whether those states are even Compact members. ORS 305.655, Art IV.2-3 (noting that the only condition on Article IV's application is that the taxpayer's income be "taxable" in another state).

Health Net fails to rebut this point by arguing that the Compact required enactment by seven states to become effective. *See* Appt Br 21-23. Enactment by seven states allowed the Compact to "enter into force," ORS 305.655, Art X.1, which, for example, authorized the Commission's creation and funding, *id.*, Art VI. But the mere fact that states took the joint action necessary to establish an advisory body without regulatory power is not evidence of a binding regulatory compact. And nothing in *Northeast Bancorp* (or any other case cited by Health Net) suggests otherwise.

c. The Compact does not prohibit unilateral repeal or modification.

The third characteristic of a binding regulatory compact is "conditional consent" that prohibits a member state from unilaterally repealing or modifying its participation. *Seattle Master Builders*, 786 F2d at 1363; *see also Ne. Bancorp*, 472 US at 175. This Compact contains neither condition. *Gillette*, 62 Cal 4th at 480-81.

The Compact expressly provides that a state "may withdraw from this compact by enacting a statute repealing the same." ORS 305.655, Art X.2. Withdrawal does not affect any previously incurred liability—*e.g.*, dues, payments for audits, *id.*, Art VI.4, VIII.2—but even the existence or non-payment of those liabilities does not prevent or delay withdrawal. *Id.*, Art X.2.

Health Net attempts to rebut this point by reciting the ordinary process for enacting legislation and claiming that those steps impose a relevant limitation on a member's ability to leave the Compact. Appt Br 21-23. But regardless of the procedure involved, withdrawal remains wholly "unilateral" under the Compact—there are no conditions that qualify or postpone a state's decision to withdraw, such as notice to other states or the Commission. ORS 305.655, Art X.2. And merely enacting a repealing statute is not itself a condition that makes withdrawal somehow less than unilateral; a state would have the power to do that even in the absence of a compact provision. *Caruthers v. Myers*, 344 Or 596, 602, 189 P3d 1 (2008) ("Either the legislature

or the people acting through the initiative may repeal or amend existing state statutes.").

The Compact also does not prohibit a state from unilaterally modifying its participation. While no provision explicitly *allows* a state to unilaterally modify its participation, that silence favors a construction that states may do so. The "well-established" presumption is that, "absent some clear indication that the legislature intends to bind itself contractually," an enacted law does not create contractual rights. *Nat'l R.R. Passenger Corp. v. Atchison, Topeka & Santa Fe Ry.*, 470 US 451, 465-66, 105 S Ct 1441, 84 L Ed 2d 432 (1985). That presumption surely informs *Seattle Master Builders*' framing of this inquiry: the issue is whether a compact renders a state "*not free* to modify * * * its participation unilaterally," not whether a compact affirmatively allows modification. 786 F2d at 1363 (emphasis added).

3. The Compact is in the nature of an advisory compact with model laws.

Because the Compact lacks the indicia of a binding regulatory compact, it must be more in the nature of an advisory compact. The usual traits of advisory compacts are all present: it "lack[s] formal enforcement mechanisms"; it aims to "study" state tax systems, not "resolve" conflicts among them; it "cede[s] no state sovereignty nor delegate[s] any governing power to a compact-created agency"; and it "do[es] not require congressional consent." Broun, *Interstate Compacts* at 13-14.

The Compact's structure and terms show that Articles II through V constitute model tax laws contained within that advisory compact. The Compact inserts those articles into its text without any language requiring members to maintain those provisions unchanged in their laws or any means of compelling them to do so. *See* ORS 305.655, Arts II-V. What prefaces those provisions instead is the "Purposes" article, which describes the Compact as "[f]acilitat[ing]" the determination of multistate taxpayers' tax liability and "[p]romot[ing]" uniformity in tax systems—words that are hortatory, not mandatory. *Id.*, Art I. Indeed, the Compact's sole method of implementing those tax-law elements is through the Commission's draft regulations, which are "advisory only." *U.S Steel*, 434 US at 457. Moreover, Article IV's text *is* a uniform law—the Uniform Division of Income for Tax Purposes Act. ORS 305.655, Art IV. And the Commission's first annual report recounted that the Compact had "been enacted as a uniform law" by 15 states. Multistate Tax Commission, *First Annual Report* 12 (1969), *available at* http://www.mtc.gov/The-Commission/Annual-Report (accessed June 16, 2016). Because "[u]niform acts do not constitute a contract between the states," the Compact members "may make changes to fit individual state needs." Broun, *Interstate Compacts* at 16. Accordingly, Oregon was free to restrict the application of Articles III.1 and IV in Oregon law.

4. *U.S. Steel* did not assume that the Compact is a binding contract.

Health Net nonetheless asserts that the United States Supreme Court has already confirmed that the Compact is binding in the *U.S. Steel* case. Appt Br 26. According to Health Net, the Court "assumed that the Compact was a valid, binding compact (otherwise the case and its analysis would have been entirely superfluous)." Appt Br 26. That assertion is both wrong and irrelevant.

The Court certainly did not assume that the Compact was "valid"; that was the very question presented for review. Corporations facing audits by the Commission filed suit to declare the Compact unconstitutional on the ground that the Compact's lack of congressional consent violated the Compact Clause. *U.S. Steel*, 434 US at 458, 458 n 7; *see* US Const, Art I, § 10, cl 3 ("No State shall, without the Consent of Congress * * * enter into any Agreement or Compact with another State * * *."). The Court rejected that challenge, holding that the Compact Clause does not apply to the Compact because it does not "enhance the political power of the member States in a way that encroaches upon the supremacy of the United States." *U.S. Steel*, 434 US at 472. The Court also rejected claims that the Compact violated the Commerce Clause and the Fourteenth Amendment. *Id.* at 478-79.

The Court also did not assume that the Compact was contractually binding. No such assumption is explicit—the words "binding" and "contract" appear nowhere in the majority opinion. *See U.S. Steel*, 434 US at 454-79. Nor

does the Court's analysis depend on any implicit assumption that the Compact is binding. The challenges to the Compact were based specifically on the Commission's performance of audits and its regulations. *Id.* at 473-79. Health Net concedes that, even under its view of the Compact, the Compact's audit provisions are not binding. Appt Br 29 (stating that the Compact "allows party states not to enact Article VIII's audit provisions"). Presumably Health Net would also concede that, under any reading, the Commission's regulations are likewise not binding. ORS 305.655, Art VII.3 ("Each such state and subdivision shall *consider any such regulation for adoption* in accordance with its own laws and procedures." (emphasis added)); *U.S. Steel*, 434 US at 457 (explaining that "[e]ach member State has the power to reject, disregard, amend, or modify any rules or regulations promulgated by the Commission"). And, again, the Court emphasized that Compact states had not delegated any sovereign authority to the Commission. *Id.* at 473.

In any event, even if *U.S. Steel* could somehow be read to have implicitly assumed that the Compact was binding for purposes of its analysis, that assumption would not foreclose a court from considering the question on the merits when it is squarely presented. *Brecht v. Abrahamson*, 507 US 619, 631, 113 S Ct 1710, 123 L Ed 2d 353 (1993); *see also Ariz. Christian Sch. Tuition Org. v. Winn*, 563 US 125, 145, 131 S Ct 1436, 179 L Ed 2d 523 (2011) ("The Court would risk error if it relied on assumptions that have gone unstated and

unexamined."). Accordingly, under the analysis discussed above, this Court should conclude that the Compact is not a binding regulatory compact.

B. The Compact Could Not Function as a Binding Regulatory Compact Because the Election in Article III.1 Would Then Be Invalid Under Many of Its Members' State Constitutions.

Aside from the absence of any of the classic indicia of a binding regulatory compact, the Compact cannot be construed as a contractually binding agreement because that construction would render the election provision in Article III.1 of the Compact unconstitutional in many of its current and former member states—a conflict that the Compact's drafters expressly sought to avoid.

Nearly half of all states have constitutional provisions that prohibit the state from suspending its power of taxation by contract.[2] Among those states are fourteen current and former Compact members, including half of the current members.[3]

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[2] *See* Alaska Const, Art IX, § 1; Ariz Const, Art IX, § 1; Ark Const, Art 16, § 7; Cal Const, Art XIII, § 31; Ga Const, Art VII, § 1; Haw Const, Art VII, § 1; Ill Const, Art IX, § 1; La Const, Art VII, § 1; Mich Const, Art IX, § 2; Minn Const, Art X, § 1; Miss Const, Art 7, § 182; Mo Const, Art X, § 2; Mont Const, Art VIII, § 2; NY Const, Art XVI, § 1; NC Const, Art V, § 2; ND Const, Art X, § 2; Okla Const, Art X, § 5; Pa Const, Art VIII, § 6; SD Const, Art XI, § 3; Tex Const, Art VIII, § 4; Wash Const, Art 7, § 1; Wyo Const, Art 15, § 14. In addition, Colorado's constitution provides that "[t]he power to tax corporations and corporate property, real and personal, shall never be relinquished or suspended." Colo Const, Art X, § 9.

[3] The current members with this constitutional restriction are Alaska, Arkansas, Hawaii, Missouri, Montana, North Dakota, Texas, and Washington.

Yet, under Health Net's view of the Compact as a binding contract, those current and former members violated their own constitutions by joining the Compact. According to Health Net, those states contracted away the power to tax that portion of a taxpayer's tax base that the taxpayer removes from the state's taxing authority by electing Article IV's apportionment method over an alternative exclusive method provided by state law. Stated differently, Health Net is claiming a contractual right to subject less of its income to a state's taxing authority than the state's law might otherwise provide.

Because Health Net's construction of the Compact would run afoul of the constitutions of nearly half of the states, it is not one that the Compact's drafters could have intended. *See Jefferson Branch Bank v. Skelly*, 66 US 436, 448, 17 L Ed 173 (1862) (observing that states "may contract by legislation to release the exercise of taxing a particular thing, corporation, or person" "unless prohibited in terms by State constitutions"). Indeed, because the Compact operates within a member state only to the extent that the state enacts the Compact as a statute, ORS 305.655, Art X.1, the Compact's drafters expressly recognized that its provisions could not conflict with any Compact state's constitution, *see id.*, Art XII (providing that any Compact provision declared to be contrary to a state constitution is severable).

Colorado, which prohibits the suspension of taxation power generally, is also a current member. The former members with this restriction are California, Illinois, Michigan, Minnesota, South Dakota, and Wyoming.

That analysis controls here even though the Oregon Constitution lacks a prohibition against contractual suspensions of the taxing power. Regardless of its own constitutional limitations, Oregon could not have validly contracted with other states to adopt a compact provision that would violate those states' constitutions. It is likewise no answer that the Compact states did not permanently or irrevocably surrender their taxation power, but merely obligated themselves to provide the taxpayer election until they withdrew from the Compact. Most Compact states' constitutions prohibit contractual "suspensions" as well as "surrenders" of the taxing power, *see supra* n 2, so that even a temporary relinquishment of the authority to tax a taxable portion of a taxpayer's income would be invalid.

C. The Compact Does Not Unmistakably Bar Its Members from Enforcing an Exclusive Apportionment Method.

Beyond specific state constitutional prohibitions against contractual suspensions of taxation authority, there remains the "well-established principle that States do not easily cede their sovereign powers." *Tarrant Reg'l Water Dist. v. Herrmann*, __ US __, __, 133 S Ct 2120, 2132, 186 L Ed 2d 153 (2013) (applying that principle to an interstate compact). Under that principle, "neither the right of taxation, nor any other power of sovereignty, will be held * * * to have been surrendered, unless such surrender has been expressed in terms too plain to be mistaken." *Jefferson Branch Bank*, 66 US at 446. The unmistakable terms necessary to support Health Net's position are not found in the Compact.

Article III.1 states that a taxpayer "may elect to apportion and allocate his income in the manner provided by the laws of [a Compact] state * * * without reference to this compact, or may elect to apportion and allocate in accordance with [the three-factor apportionment formula in] Article IV." ORS 305.655, Art III.1. The Compact does not address the circumstance in which state law mandates exclusive use of one apportionment method, as ORS 314.606 does. Nor does the Compact anywhere preclude a state from adding that sort of exclusive condition to the laws to which Article III.1 refers. For all that Article III.1 reveals, the taxpayer takes the state laws as it finds them. So what happens when the state law that Article III.1 purports to treat as optional is, by its very terms, not optional? The Compact doesn't say.

Thus, as the Department notes, the Compact does not unambiguously express the member states' intent to contract away their authority to adopt an exclusive apportionment formula. Respt Br 12-16. That ambiguity alone warrants a construction that the member states reserved that authority. *See Tarrant Reg'l Water Dist.*, 133 S Ct at 2133 (explaining that "States rarely relinquish their sovereign powers, so when they do we would expect a clear indication of such devolution, not inscrutable silence"); *see also United States v. Winstar Corp.*, 518 US 839, 877-78, 116 S Ct 2432, 135 L Ed 2d 964 (1996) (plurality op.) (noting that "unmistakability was needed for waiver [of a sovereign power], not reservation").

Moreover, "other interpretive tools" support the Department's position that the Compact does not bar its members from adopting exclusive apportionment methods. *See Tarrant Reg'l Water Dist.*, 133 S Ct at 2132. The parties' "'course of performance under the Compact is highly significant' evidence of [their] understanding of the compact's terms." *Id.* at 2135 (quoting *Alabama v. North Carolina*, 560 US 330, 346, 130 S Ct 2295, 176 L Ed 2d 1070 (2010)). As the Department explains, the Compact members' 1972 resolution ratifying Florida's repeal of Articles III and IV, as well as the later unopposed disabling of Article III.1's taxpayer election by eleven Compact members, reflect the member states' common, long-held view that the Compact does not preclude them from imposing an exclusive apportionment method. Respt Br 20-25. Also, comparisons to other compacts' text can shed light on the parties' intent. *Tarrant Reg'l Water Dist.*, 133 S Ct at 2133. Unlike this Compact, other compacts to which Oregon belongs explicitly state that the compact supersedes any conflicting state statute. *See, e.g.*, ORS 144.600, Art XIV(a)(2) ("The laws of the State of Oregon, other than the Oregon Constitution, that conflict with this compact are superseded to the extent of the conflict."); ORS 417.030, Art XIII.A.2 ("All compacting states' laws other than state Constitutions and other interstate compacts conflicting with this compact are superseded to the extent of the conflict.").

D. Health Net Cannot Prevail Merely by Showing a Conflict Between Article III.1 of the Compact and State Law.

Even if Health Net could establish that the Compact is a binding regulatory compact, that would not be the end of the matter. As just discussed, the Compact does not prescribe a rule of decision for a court to apply when there is a conflict between a Compact provision and state law. Nor does the Compact otherwise contain any mechanism for enforcing its provisions against its member states. Because Congress has not approved this Compact, it is not a federal law that preempts state law by virtue of the Supremacy Clause. *See Tarrant Reg'l Water Dist.*, 133 S Ct at 2130 n 8. And, of course, this is not an instance in which a compact state has brought an original action against another compact state for an alleged breach of their agreement. *E.g.*, *Alabama*, 560 US at 338.

To prevail, then, Health Net must establish that, by disallowing Article III.1's taxpayer election, ORS 314.606 violates federal and state constitutional guaranties against laws impairing the obligation of contracts. US Const, Art I, § 10, cl 1; Or Const, Art I, § 21. Contrary to Health Net's assertions, a state is not constrained as a matter of *common law* from legislating inconsistently with a non-congressionally-approved compact. Nor is Health Net correct that *any* conflict between a state law and an interstate compact qualifies as an unconstitutional impairment under the federal Contract Clause.

1. Health Net bears the heavy burden of showing that state law unconstitutionally impairs contractual obligations under the Compact.

When Congress approves an interstate compact, it "transforms" the compact into federal law. *Cuyler v. Adams*, 449 US 433, 440, 101 S Ct 703, 66 L Ed 2d 641 (1981). Under the Supremacy Clause, then, an approved compact "pre-empts any state law that conflicts with the Compact." *Tarrant Reg'l Water Dist.*, 133 S Ct at 2130 n 8.

By contrast, a non-approved compact operates only as a state statute and, in some cases, a binding contract among states. *See* Norman J. Singer & J.D. Shambie Singer, 1A *Sutherland Statutes and Statutory Construction* § 32:5 (7th ed 2009). As a statute, the compact may be superseded by later-enacted state laws under "the doctrine of implied repeal" or rules that "give effect to the latest in time." *Id.* § 32:6.

When the compact also creates a binding contract, however, the compact *may* take precedence over a conflicting, later-enacted statute *if* the statute's effect on the compact violates the Contract Clause, US Const, Art I, § 10, cl 1, which prohibits laws impairing contractual obligations. *Green v. Biddle*, 21 US 1, 92, 5 L Ed 547 (1823) (holding that a statute abrogating a compact violated the Contract Clause); *Gen. Expressways, Inc. v. Iowa Reciprocity Bd.*, 163 NW2d 413, 419-21 (Iowa 1968) (evaluating a potential conflict between a statute and a compact under contract-clause principles); Singer & Singer, 1A

Sutherland Statutes and Statutory Construction § 32:3 (describing compacts as "deriv[ing] binding force" from the Contract Clause), § 32:8 (explaining that a state's authority to abrogate a non-congressionally-approved compact is limited by "the constitutional prohibition against impairing the obligation of contract"); Broun, *Interstate Compacts* at 22 (explaining that "[a] compact controls over a state's application of its own law through the Supremacy Clause [in the case of congressionally approved compacts] and the Contracts Clause"); Vincent V. Thursby, *Interstate Cooperation: A Study of the Interstate Compact* 79 (1953) ("A State is prohibited by the contract impairment clause of the Constitution from impairing its compacts with other states.").[4]

Health Net agrees that a non-approved compact may preempt a state law that unconstitutionally impairs a contractual obligation under the compact. Appt Br 44-49. But Health Net implies that, independent of the Contract Clause, all compacts supersede state law by virtue of a common-law rule that a state contractually cedes its sovereign authority to legislate inconsistently with a

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[4] *See also* Jill Elaine Hasday, *Interstate Compacts in a Democratic Society: The Problem of Permanency*, 49 Fla L Rev 1, 3 (1997) ("[A]s with other contracts, the Contracts Clause of the United States Constitution protects compacts from impairment by the states. Although a state cannot be bound by a compact to which it has not consented, a compact takes precedence over the subsequent statutes of signatory states."); Matthew S. Tripolitsiotis, *Bridge Over Troubled Waters: The Application of State Law to Compact Clause Entities*, 23 Yale L & Pol'y Rev 163, 174 (2005) (explaining that, because an interstate compact may be a contract protected against impairment by the Contracts Clause, "[t]his logical scheme gives compacts preeminence over the subsequent legislation of signatory states").

compact it has joined. *See id.* at 38-43. If that is Health Net's contention, the Court should reject it, for four reasons.

First, the blanket assertion that a state cedes its sovereign authority by joining a compact begs the question. "Once entered, the terms of the compact and any rules and regulations authorized by the compact can, *to the extent provided in the agreement*, supersede any substantive state laws that may be in conflict * * *." Broun, *Interstate Compacts* at 22 (emphasis added). Again, unlike other compacts, no term in this Compact provides that it supersedes state law or that its members are contractually obligated to maintain Articles III.1 and IV in their state laws unchanged.

Second, Health Net never explains how the *common law* could strip a state legislature of its sovereign authority to enact tax laws. As this Court has explained, that sort of limitation generally must be found in a federal or state constitutional provision. *See MacPherson v. DAS*, 340 Or 117, 127, 130 P3d 308 (2006) (observing that "limitations on legislative power must be grounded in specific provisions of either the state or federal constitutions" and "even implied limitations must find their source in some constitutional provision"); *State v. Moyle*, 299 Or 691, 699, 705 P2d 740 (1985) ("In principle, legislative power to select the objectives of legislation is plenary, except as it is limited by the state and federal constitutions.").

Third, if Health Net were correct that, as a matter of common law, all interstate compacts automatically supersede conflicting state law, it is difficult to understand why any state, court, or scholar would have ever looked beyond that principle to establish a compact's preemptive effect. Under Health Net's logic, express provisions that a compact supersedes conflicting state laws (*e.g.*, ORS 144.600, Art XIV(a)(2); ORS 417.030, Art XIII.A.2) are wholly superfluous, because those compacts' supremacy over state law is already self-evident as a matter of "ceded sovereignty." Likewise, no court need ever have invoked the Supremacy Clause or the Contract Clause to determine a compact's preeminence over state law, as the United States Supreme Court has done. *E.g.*, *Tarrant Reg'l Water Dist.*, 133 S Ct at 2130 n 8 (Supremacy Clause); *Green*, 21 US at 92 (Contract Clause). Indeed, as a matter of constitutional avoidance, the Court should not have relied on those Clauses if Health Net's supposed common-law rule were in effect. *Cf. Escambia Cnty. v. McMillan*, 466 US 48, 51, 104 S Ct 1577, 80 L Ed 2d 36 (1984) (per curiam) (noting that "normally" courts "will not decide a constitutional question if there is some other ground upon which to dispose of the case"). And, of course, the extensive scholarship cited above about the "binding force" that interstate compacts derive from the Contract Clause would be so much spilled ink.

Finally, as the Tax Court thoroughly explained, Health Net's asserted common-law rule that all non-congressionally-approved compacts

automatically supersede state law rests on misreadings and unwarranted extensions of statements extracted from a handful of cases. ER-229-235. The *amici* states will not repeat that discussion here, but two cases cited by Health Net bear further mention.

Although Health Net cites the *General Expressways* case as authority for its suggested common-law rule, Appt Br 41, that case actually supports the Department's position. The sentence selectively quoted by Health Net states in full:

> Although it is true valid contracts of the State cannot be *impaired by the Legislature*, and we agree with the trial court that the uniform compact is a valid state contract, we do not interpret this legislation as an attempt to unilaterally alter the terms of the compact previously entered into by the board pursuant to the authority provided in chapter 326 in 1959.

Gen. Expressways, 163 NW2d at 419 (emphasis added). The court later explained that it adopted that interpretation of the legislation at issue to avoid a construction that would render the law "unconstitutional" under the Contract Clause. *Id.* at 421. Again, though, applying that rule of construction would have been unnecessary if Health Net were correct that a non-approved compact already supersedes state law as a non-constitutional, common-law matter.

Health Net's reliance on *In re O.M.*, 565 A2d 573 (DC App 1989), *cert den*, 494 US 1086 (1990), is also misplaced. Appt Br 42-43. That case is inapposite for two straightforward reasons. First, the *O.M.* court expressly

stated: "This case does not present, as appellant argues, the issue of whether an interstate compact which is not federal law may or must be enforced by the courts." 565 A2d at 579. Of course, that is precisely the issue in this appeal. Second, the court added that "the courts of the District of Columbia, including this court, have been expressly commanded by Congress to enforce the Compact according to its terms." *Id.* (citing D.C. Code § 32-1104). Accordingly, the *O.M.* court was required to follow that legislatively mandated rule of decision. *Id.* By contrast, in this case there is no legislative command—in the Compact or elsewhere—to enforce the Compact's provisions over conflicting state law. Indeed, the Oregon Legislature has mandated the opposite. ORS 314.606.

2. A conflict between state law and the Compact does not automatically violate the federal Contract Clause.

Under the federal Contract Clause, an actual conflict between the Compact and Oregon's exclusive apportionment formula would not automatically render the latter provision invalid. Although *Green v. Biddle* applied the rule that "any deviation" from a contract, "however minute, or apparently immaterial," violated the federal Contract Clause, 21 US at 84, the United States Supreme Court has since considerably relaxed the constitutional standard. "[A] finding that there has been a technical impairment is merely a preliminary step in resolving the more difficult question whether that impairment is permitted under the Constitution." *U.S. Trust Co. v. New Jersey*,

431 US 1, 21, 97 S Ct 1505, 52 L Ed 2d 92 (1977). As the Department explains, evaluating whether a state law invalidly impairs a contractual obligation under the federal Contract Clause now requires application of a multi-factor test to consider whether the law effects a substantial impairment that lacks a legitimate public purpose and does not reasonably adjust rights and responsibilities. Respt Br 41-47.

Health Net wrongly maintains that this modern Contract Clause analysis does not apply to interstate compacts. Appt Br 45-46. Health Net apparently believes that *Green* not only established that a compact (like other contracts) is subject to the Contract Clause, but that it also created a special Contract Clause standard applicable only to compacts, which has remained frozen in time even as the Supreme Court's Contract Clause test for other contracts has evolved into a more complex inquiry. *See id.* Nothing in *Green* suggests that distinction. To the contrary, the very basis for *Green*'s holding is that, under the Contract Clause, a compact should be treated like any other contract. 21 US at 92 (observing that the Contract Clause "embraces all contracts * * * whether between individuals, or between a State and individuals" and that "a State has no more power to impair an obligation into which she herself has entered, than she can the contracts of individuals"). And the Supreme Court has since confirmed that "[t]he Contract Clause is not an absolute bar to subsequent modification of a State's own financial obligations" under a compact. *U.S.*

Trust, 431 US at 25. Consistent with that holding, the Court should conduct a modern federal Contract Clause analysis in this case.

E. Comparing the Reliance Interests Implicated by the Compact Shows That Any Contractual Impairment Does Not Violate the Federal Contract Clause.

As the Department explains, Health Net cannot complain of impairment to any contractual obligations under the Compact because it is neither a party to nor a third-party beneficiary of the Compact. *See* Respt Br 25-29. And, in any event, in evaluating whether a state law unconstitutionally impairs a contract, a court must examine the extent to which the alleged impairment affected the relevant reliance interests. *Id.* at 42-43. Indeed, "[i]n determining whether an impairment is substantial and so not 'permitted under the Constitution,' of *greatest* concern appears to be the contracting parties' *actual* reliance on the abridged contractual term." *City of Charleston v. Pub. Serv. Comm'n*, 57 F3d 385, 392 (4th Cir), *cert den*, 516 US 974 (1995) (quoting *U.S. Trust*, 431 US at 21) (emphases added). A comparison of the relative reliance interests in this case conclusively shows that, to the extent a state's imposition of an exclusive apportionment formula actually impaired an obligation under the Compact, that impairment was not substantial, and thus not unconstitutional.

Even if taxpayers were an intended third-party beneficiary of the Compact, Health Net cannot demonstrate any reliance by taxpayers on Article III.1's election provision. The Compact reserves to states the right to withdraw

from the Compact unilaterally at any time without notice. ORS 305.655, Art X.2. Thus, even assuming that taxpayers believed that Article III.1 guaranteed a right to elect an apportionment formula that varied from other state law, they could not have reasonably relied on that belief in their tax planning knowing that the legislature could repeal the Compact at will. *See City of Charleston*, 57 F.3d at 392-93 (noting that a relevant factor in the reliance analysis is whether "the original contract * * * indicated that the abridged term was subject to impairment by the legislature").

History refutes any substantial taxpayer reliance on Article III.1 after states adopted exclusive apportionment formulas. In this case, Health Net did not attempt to avail itself of the taxpayer election until seventeen years after Oregon made its apportionment formula exclusive. *See* Respt Br 2-4. The same pattern has occurred in other states: although many Compact states began adopting exclusive apportionment formulas in the late 1980s and early 1990s, *id.* at 22-24, taxpayers have not invoked their allegedly superior right to elect an apportionment formula under Article III.1 until recently.

By contrast, in choosing to join and remain in the Compact, the member states have necessarily and significantly relied on their shared, longstanding interpretation that the Compact does not preclude the adoption of exclusive income-apportionment formulas. As the Department explains, in 1972 the Compact states unanimously ratified Florida's repeal of Articles III and IV as

being consistent with the Compact. *Id.* at 21-22. Since then, many Compact states have similarly imposed exclusive apportionment formulas that negate any taxpayer option under Article III.1. *Id.* at 22-24. State tax authorities have inevitably factored those mandatory formulas into their revenue estimates, which state legislatures have then used in appropriating funds and setting budget priorities. The states' reliance on their mutual reading of their Compact for a task as important as managing statewide fiscal affairs, and for such an extended period of time, dwarfs any recently asserted reliance that may be claimed by entities like Health Net that are not parties to the Compact.

VI. CONCLUSION

The judgment of the Tax Court should be affirmed.

DATED this 16th day of June, 2016.

Respectfully submitted,

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WITH WORD-COUNT AND FONT-SIZE REQUIREMENTS

I certify that this brief complies with the word-count limitation in ORAP 5.05(2)(b) and that the word count of this brief (as described in ORAP 5.05(2)(a)) is 6,778 words.

I certify that the font size in this brief is Times New Roman 14-point for both the text of the brief and footnotes, as required by ORAP 5.05(4)(f).

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