No. 09-981

IN THE

Supreme Court of the United States

JOHNSON CONTROLS, INC.; ET AL.,

Petitioners,

v.

JONATHAN MILLER, SECRETARY OF THE FINANCE AND ADMINISTRATION CABINET OF THE COMMONWEALTH OF KENTUCKY; COMMONWEALTH OF KENTUCKY, DEPARTMENT OF REVENUE,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF KENTUCKY

BRIEF IN OPPOSITION

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QUESTIONS PRESENTED

The questions presented are:

1. Does the Due Process Clause, as interpreted by *McKesson Corp. v. Div. of Alcoholic Beverages*, 496 U.S. 18 (1990), and *Reich v. Collins*, 513 U.S. 104 (1994), require a State to consent to suits in its own courts brought to recover mere tax overpayments made under a state tax statute that is neither unconstitutional under the Constitution of the United States nor unlawful under some overriding federal statute via the Supremacy Clause?

2. Does the Due Process Clause, as interpreted in *United States v. Carlton*, 512 U.S. 26 (1994), require that retroactive tax legislation be enacted no later than "the first possible legislative session" following the legislature's identification of the "legitimate legislative purpose" sought to be achieved by the retroactive legislation?

3. Does the Equal Protection Clause require that tax statutes apply in the same way to all members of a "similarly situated" group of taxpayers, or to none?

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STATEMENT

To avoid a massive loss of public revenues threatened by the use of retroactive "unitary" (rather than "separate") corporate income tax returns for pre-1995 years, the Kentucky General Assembly in 2000 enacted two retroactive tax statutes.

One statute, KRS 141.200(18), prohibits the use of unitary returns, and requires separate corporate entities to file separate tax returns for pre-1995 years.

The other statute, KRS 141.200(17), revokes the Commonwealth's consent to unitary return refund suits brought to recover alleged tax overpayments for pre-1995 years.

Both statutes were made retroactively effective for tax returns filed or refund claims made after December 22, 1994, for "all taxable years ending before December 31, 1995," *i.e.,* pre-1995 tax years.

Both statutes were enacted as new subsections of KRS 141.200, a statute which since 1942 has prescribed the types of tax returns that must be filed by corporations in Kentucky.[1] The opinions of the Kentucky courts sometimes use the term "H.B. 541," which refers to the House Bill enacted by the Ken-

[1] *See* 2000 Ky. Acts ch. 543, § 1. [Pet. App. 122-123].

tucky General Assembly in 2000, as shorthand for the statutes.

The two new subsections are currently codified as KRS 141.200(17) and KRS 141.200(18).[2] KRS 141.200(17) is the retroactive revocation of the Commonwealth's consent to suit. KRS 141.200(18) is the retroactive prohibition on the use of unitary returns to compute taxable income and tax liability.[3]

A casual observer might wonder why the 2000 Kentucky General Assembly made the amendments retroactively effective for all pre-1995 years, but not for 1995 or any subsequent year. The answer is that the 1996 Kentucky General Assembly had already prohibited the use of unitary returns for 1995 and all subsequent years. [4]

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[2] *See* 2000 Ky. Acts. ch. 543, § 1 (initial codification); 2005 Ky. Acts ch. 168, § 15 (subsequent re-codification).

[3] The Petition refers to the statutes as KRS 141.200(9) and KRS 141.200(10), as they were initially codified. The opinion of the Kentucky Supreme Court consistently refers to the statutes as they are currently codified, as does this Brief in Opposition.

[4] *See* 1996 Ky. Acts ch. 239, §§ 1 — 3, *initially codified as* KRS 141.120(11), *subsequently codified as* KRS 141.200(7), *see* 2000 Ky. Acts ch. 543, § 1, *and subsequently re-codified as* KRS 141.200(15), *see* 2005 Ky. Acts ch. 168, § 15. The constitutionality of the 1996 legislation, which was made retroactive "for taxable years ending on or after December 31, 1995," and is currently codified at KRS 141.200(15), has never been challenged.

A. Kentucky Tax Terms of Art

Consideration of the Petition requires a working understanding of (i) the difference between a "separate" corporate income tax return and a "unitary" corporate income tax return, and (ii) the difference between a tax "overpayment" and a "refund claim."

In a "separate" corporate income tax return, a single corporation reports its own (and only its own) revenues, expenses, and apportionment factors, and computes its own (and only its own) taxable income (or loss) and tax liability. *See* KRS 141.200(2)(c) (statutory definition of "separate return").

In a "unitary" corporate income tax return, a group of corporations organized as separate legal entities (typically a common parent corporation and some or all of its subsidiaries) which allegedly conduct a "unitary" business, combine their separate revenues, expenses, and apportionment factors, and compute a "unitary" taxable income (or loss) and tax liability.[5] Unitary returns are therefore sometimes

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[5] A third and completely different type of return is the federal "consolidated" corporate return. The members of the "consolidated" group are determined solely by mathematical stock ownership, regardless of the business conducted by each corporation, and include the common parent and each subsidiary which is at least 80% owned by the common parent. There is no requirement that the parent and any of its subsidiaries conduct a "unitary" business. A "unitary" or "combined" return is strictly a state tax law concept. The Internal Revenue Code permits qualifying corporations to elect to file a consolidated

called "combined" returns by tax cases, tax treatises, and the Petition.

A tax "overpayment" is defined under Kentucky law as "the excess of the tax payments made over the correct tax liability determined under the terms of the applicable statute without reference to the constitutionality of the statute." KRS 134.580(1)(b).

The importance of the term "tax overpayment" is that Kentucky's general tax refund statute, KRS 134.580(2), under which all of Petitioners' refund claims have been made, only authorizes a refund or credit of an "overpayment of tax." A separate Kentucky statute, KRS 134.590(1), provides for refunds of taxes "paid under a statute held unconstitutional." The Kentucky Supreme Court has construed these two statutes to be mutually exclusive. *Revenue Cabinet v. Gossum*, 887 S.W.2d 329, 334-335 (Ky. 1994). (KRS 134.580 "is limited" to "tax overpayments" as defined and does not "apply to situations where the constitutionality of a statute is at issue").

This point is crucial: under Kentucky law, a suit to recover a tax "overpayment" under KRS 134.580, such as the refund claims asserted by Petitioners, by definition does not and cannot involve a tax paid under a statute held to be unconstitutional.

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return, but the federal tax law has never permitted separate corporations to combine their income in a "unitary" return based on the conduct of a "unitary" business.

The *Gossum* case itself held that refund claims for state taxes paid under a Kentucky statute which exempted state employee retirement payments from the Kentucky income tax, but not federal employee retirement payments (and which therefore violated "the federal constitutional doctrine of intergovernmental tax immunity," *see Davis v. Michigan Dep't of Treasury*, 489 U.S. 803 (1989)), could not be brought under KRS 134.580 (which provides a four year statute of limitations) but had to be brought under KRS 134.590 (which provides a shorter two year statute of limitations). 887 S.W.2d at 334-335.

A "refund claim," like a complaint in a civil action, merely states the taxpayer's contention that a tax "overpayment" has been made. Taxpayers often make refund claims by filing an "amended return" for the tax year. But an amended return filed after the due date for the original return (*e.g.,* April 15, 2010 for 2009 tax returns) does not replace or supersede the original return. *Koch v. Alexander*, 561 F.2d 1115 (4th Cir. 1977) (amended returns "showing a smaller liability than initially reported are generally treated as claims for refunds"); Rev. Rul. 57-601, 1957-2 CB 614 (amended return filed after due date is merely refund claim).

Using a "unitary" return to compute taxable income and tax liability, does not automatically increase or decrease taxable income or tax liability, or generate a tax "overpayment" or a tax "underpayment," versus the aggregate results of using "separate" returns for each member of the alleged unitary group. The type of tax return, like any tax accounting method, merely affects the computation of taxable income and tax liability. Whether an “overpay- “overpayment” or “underpayment” exists depends on whether (i) the actual tax payments made by the taxpayer for the year, exceed (or are less than) (ii) the taxpayer’s correctly computed tax liability determined under the applicable substantive law.

B. Separate Returns by Separate Corporations

KRS 141.200(17) and KRS 141.200(18) were not written on a clean legislative slate.

Kentucky’s first income tax law, enacted in 1936, required separate corporations, whether or not affiliated, to file separate income tax returns. Ky. Stat. § 4281b-18, 1936 Ky. Acts 3rd Ex. Sess. ch. 7, § 18, provided that “every corporation doing business” in Kentucky “shall make a return,” and mandated that “corporations which are affiliated shall each make separate returns.”

When the Kentucky Revised Statutes were enacted in 1942, the fundamental requirement of separate returns by separate corporate entities was carried over in KRS 141.200(1), which provided: “corporations that are affiliated must each make a separate return.” *See* Ky. Rev. Stat. § 141.200(1) (1st ed. 1942).

C. 1966 UDITPA Changes

Prior to 1966, Kentucky's corporate income tax law sought to tax a corporation on its income from "sources" in Kentucky, because the basic federal constitutional rule is that a State cannot tax income that is not in some way connected to property or transactions or business conducted in the taxing State.

This focus on the geographic "source" of income invited metaphysical disputes about "where" income was earned, and was ill-suited to an economy dominated by large corporations with nationwide businesses. In 1966, the Kentucky General Assembly adopted a more modern and practical approach, recommended by the Multistate Tax Commission and the National Conference of Commissioners on State Laws, of dividing corporate income into "business" and "non-business" income. "Business income" was defined, generally, as income "from transactions and activity in the regular course of a trade or business" of the corporation, and "non-business income" was defined as "all income other than business income."

Under this approach, "business income" is "apportioned" or divided among the States according to a three factor property, payroll, and sales formula used to compute an "apportionment factor," and items of "non-business income" are "allocated" to specific States using a set of mechanical rules. The general effect is that if a corporation's "apportionment factor" for State *X* is 15% (roughly indicating that 15% of its "business income" is attributable to operations in State *X*, as measured by its relative property, payroll, and sales in State *X* versus all States), then 15% of its income is "apportioned" to State *X* and subject to taxation under State *X's* laws. The other 85% of its "business income" is "apportioned" to other States.

The 1966 legislation, patterned after the Uniform Division of Income for Tax Purposes Act, was incorporated into Chapter 141 (the income tax statute) of the Kentucky Revised Statutes by 1966 Ky. Acts ch. 176.

But — and this is a very significant "but" — the 1966 legislation made no change whatsoever to the provisions of KRS 141.200(1) — the statutory requirement of a "separate return" from "each" corporation. The "apportionment" provisions of the 1966 legislation were separately codified as KRS 141.120, generally referred to as the "apportionment statute."

D. Department of Revenue Positions

From 1972 until 1988, the Kentucky Department of Revenue interpreted KRS 141.120 — the new apportionment statute — as authorizing the use of unitary returns to compute the combined tax liability of the members of a group of corporations conducting a "unitary" business.

In 1988, the Department of Revenue determined that its prior interpretation of KRS 141.120 had been erroneous, and announced in Revenue Policy 41P225 (the state equivalent of an IRS revenue ruling) that separate returns should be filed by a parent and each of its subsidiaries, unless a subsidiary was a mere "paper corporation with limited viable activities."

The Department's correction of what it considered to be an erroneous interpretation of the apportionment statute was entirely proper. *Automobile Club of Michigan v. Comm'r*, 353 U.S. 180, 183 (1957) (IRS not precluded in 1945 from revoking erroneous 1934 and 1938 revenue rulings; doctrine of equitable estoppel "is not a bar to the correction by the Commissioner of a mistake of law"); *Delta Air Lines, Inc. v. Commonwealth*, 689 S.W.2d 14, 20 (Ky. 1985) ("erroneous interpretation of the law [by an ad-administrative agency] will not be perpetuated"; Revenue Department has "affirmative responsibility" to "abandon" an "erroneous policy when it discover[s] its error"); *Revenue Cabinet v. Lazarus, Inc.*, 49 S.W.3d 172, 175 (Ky. 2001) (Revenue Cabinet cannot "change the [statutory] law by mistake").

E. 1994 *GTE* Case and 1996 Legislation

Revenue Policy 41P225 sparked a number of lower court lawsuits in which taxpayers challenged the Department's position, and contended under various theories that unitary returns were permitted or required under Kentucky law.

The fundamental statutory construction dispute was not settled until 1994 when the Kentucky Supreme Court, in *GTE v. Revenue Cabinet*, 889 S.W.2d 788 (Ky. 1994), construed KRS 141.120 (the apportionment statute) to require a group of corporations that conduct a "unitary" business to file a "unitary" return in Kentucky. The *GTE* decision finessed the conflict between KRS 141.200(1), the statute which requires separate returns by "each" corporation, and its construction of KRS 141.120, by reading the former statute's use of the term "corporation" to mean what the *GTE* Court called a "unitary corporation" comprised of the parent and its unitary subsidiaries.

The *GTE* case was decided on December 22, 1994. The Kentucky General Assembly was not then in session, and did not meet again until 1996, because at the time the Kentucky Constitution only allowed the General Assembly to meet in "regular session" for 60 days in even numbered years.[6]

At the first available opportunity after *GTE* was decided, the Kentucky General Assembly in its 1996 regular session abrogated *GTE* by amending KRS 141.120 (the statute construed in *GTE)* to provide that "nothing in this section shall be construed as allowing or requiring the filing of a combined return under the unitary business concept," and by

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[6] The Kentucky Constitution was amended in 2000 to allow 30-day sessions in odd numbered years, the first of which was convened in 2001.

making the amendment retroactively effective for 1995 and all future taxable years.[7]

After the 1996 General Assembly adjourned, it became apparent that the Commonwealth still faced substantial exposure for unitary return refund claims. A number of parent-subsidiary groups, including Petitioners, contended that they had conducted a "unitary" business during pre-1995 years, and were therefore permitted under *GTE* to make unitary return refund claims for those pre-1995 years for which refund claims were not otherwise barred by the statute of limitations.[8] These unitary return refund claims for pre-1995 were not affected by the 1996 legislation, which only applied to 1995 and subsequent years.

F. 1998 Budget Bill

None of the decisions of the Kentucky courts below turned on the precise amount of the refund claims made by Petitioners and others, or on the dates the refund claims were made, or on the specific years for which tax overpayments were alleged to have been made. The opinion of the Franklin Circuit Court, a trial court of general jurisdiction, states that by the end of 1995, the Kentucky Department of Revenue "estimated" the total exposure at "about $50,000,000." As additional claims were filed, the

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[7] *See* KRS 141.200(11), *added by* 1996 Ky. Acts Ch. 239 § 1, § 3.

[8] KRS 134.580, Kentucky's general tax refund statute, requires that refund claims be made within four years after the due date of the return, including extensions.

Department of Revenue increased its estimate of the exposure to $160,000,000 in October 1996 and "almost $200,000,000 at the end of June 1998." Pet. App. 196.

Exactly when or how this estimated exposure was communicated by the Department of Revenue to the leadership of the Kentucky General Assembly is not revealed by the opinions of the Kentucky courts. This comes as no surprise: the Kentucky General Assembly was not in session from April 1996 until January 1998.

What we do know, however, is that "in response [to these estimates], to avoid a huge loss to the general fund, at the next legislative session, 1998, the General Assembly included in the 1998-2000 budget bill, a measure which prohibited the Revenue Cabinet from paying any post-*GTE* refund claims," *i.e.,* unitary return refund claims filed after December 22, 1994. Pet. App. 29 (concurring opinion of Schroeder, J.).

In Kentucky parlance, the "budget bill" is the appropriations bill enacted by the General Assembly in its biennial "regular session" to authorize expenditures of public monies during the two fiscal years (July 1 through June 30) following the "regular session." Under the Kentucky Constitution, monies held in the State Treasury may not be legally expended unless "appropriated" by the General Assembly. *See* Ky. Const. § 230; *Fletcher v. Stumbo*, 163 S.W.3d 852 (Ky. 2005).

Although the biennial "budget bill" is mostly a soporific listing of authorized line item expenditures for highways, schools, social services, government operations, and public works, the General Assembly is constitutionally permitted to include within the "budget bill" substantive provisions which temporarily suspend or change the effect of a specified provision of the permanent Kentucky Revised Statutes for two years. *See Armstrong v. Collins,* 709 S.W.2d 437 (Ky. 1986).

In reviewing the tortured path of KRS 141.200(17) and KRS 141.200(18), the Kentucky Supreme Court concluded that "the General Assembly was not apprised of, or at least was not able to address, these problems [the $200,000,000 refund claim exposure] until late in the 1998 regular session, when it was well into the budgeting process." Pet. App. 7. Since the General Assembly met only "every other year then, the first chance to deal with the problem with direct legislation would come two years later," *i.e.,* in 2000. *Id.* "[T]o at least temporarily patch the problem," the General Assembly "inserted a provision in the 1998 Budget Bill barring the state treasury from paying out any refunds" under "the theory announced in *GTE*." Pet. App. 7-8. But because "the Budget Bill would only be in effect for two years," the "problem would have to be addressed fully in 2000." Pet. App. 8.

The temporary legislative fix in the 1998 budget bill, enacted as 1998 H.B. 321 § 33, provided that "notwithstanding KRS 134.580 [the general tax refund statute], no taxpayer shall be refunded" any tax overpayment "attributable to the filing" of a unitary return for a pre-1995 year "after December 22, 1994." This prohibition on the payment of unitary return refunds was probably an excess of virtue, because the 1998 budget bill had not appropriated any funds for the payment of such claims. But before the constitutionality of this stopgap measure could be determined by an appellate court, the prohibition "expired on its own terms in 2000," Pet. App. 104 (Circuit Court Opinion), when the two year 1998 budget bill expired.

G. 2000 Enactment of KRS 141.200 (17) and KRS 141.200(18)

We now come to 2000, when "the General Assembly finally had a chance to deal directly with the emerging problem," according to the Kentucky Supreme Court, which had no difficulty concluding that "there can be no question that the legislature acted to correct what it viewed as a mistake in *GTE's* interpretation of the law, that it had a legitimate governmental purpose (raising and controlling revenue), and that the statute rationally furthers this purpose." Pet. App. 20.

Justice Schroeder's concurring opinion, which says the statute was enacted "to prevent a massive loss to the state treasury as a result of the *GTE* decision," Pet. App. 31, quotes the principal sponsor of the 2000 legislation, who emphasized that the retroactive amendments were necessary to avoid having to slash funding for education and social services.

> "If we don't do this [pass H.B. 541], it could cost us up to $190,000,000. . . These corporations that are involved did not plan their business based on filing the way that they are now attempting to come back and get refunds . . . . But now they want to come back and raid the state treasury . . . to the tune of $190,000,000. And that's what this bill is all about . . . [I]f we don't do it, then we better figure out how to cut the budget $190,000,000." Transcript of Hearing on H.B. 541, House Appropriations and Revenue Committee, February 22, 2000, (remarks of Chairman Moberly), *quoted at* Pet. App. 31 n.2.

The 2000 General Assembly responded by enacting KRS 141.200(17) and KRS 141.200(18),[9] the statutes challenged here.

Both statutes were expressly made retroactive to 1994 and prior years.[10] The retroactive reach of the statutes was essential: the unitary method re-

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[9] *See* 2000 Ky. Acts. ch. 543, § 1, *initially codified as* KRS 141.200(9) and KRS 141.200(10), *and subsequently re-codified as* KRS 141.200(17) and KRS 141.200(18), *see* 2005 Ky. Acts ch. 168, § 15.

[10] *See* KRS 446.080(3) (General Assembly may make statute retroactive if "expressly so declared").

fund claims that jeopardized the Commonwealth's treasury were all made by filing retroactive unitary returns after the 1994 *GTE* decision, for 1994 and prior years.

Both statutes only apply to retroactive unitary returns. That is, the statutes only apply if the group members initially filed separate returns, and then switched to a retroactive unitary return. If a corporate group filed a unitary return or made a unitary return refund claim, on or before December 22, 1994, neither statute applies.

H. Retroactive Unitary Returns and Mere Tax "Overpayment" Claims

We refer to the unitary returns filed by Petitioners and other parent-subsidiary groups after the *GTE* decision as "retroactive" unitary returns rather than as "amended" returns, because none of the Petitioners filed a timely unitary return by the due date for 1994 or any prior year.[11] These retroactive unitary returns were labeled as "amended" returns, but you can't amend a tax return that has never been filed. As the Kentucky Supreme Court observed, Petitioners "sought to amend their returns by substituting" unitary returns for previously filed separate returns. Pet. App. 4.

None of the Petitioners claims to have made a tax overpayment under a Kentucky tax statute that

[11] Each of Petitioners' unitary returns was, however, filed within the four year statute of limitations for refund claims.

violates the Constitution of the United States or that is otherwise unlawful under some federal statute. Each refund claim is based exclusively on the use of a retroactive unitary return under KRS 141.120 as construed by the *GTE* case, frozen in time and unaffected by the 1996, 1998, and 2000 legislation.

All the refund claims in question were brought exclusively under KRS 134.580, Kentucky's general tax refund statute, which expressly does not apply to claims for refund of taxes "in any case in which the statute may be held unconstitutional," *see* KRS 134.580(6).

Petitioners' refund claims are therefore mere tax overpayment refund claims, based on using one type of tax return rather than another type of tax return, to compute tax liability. The tax overpayments allegedly made by Petitioners, can no more be said to have been made under an unconstitutional or unlawful tax statute, than a taxpayer who mistakenly uses straight line rather than accelerated depreciation, or who incorrectly computes the amount of a deduction, or who erroneously interprets the substantive tax law, can be said to have paid taxes under an unconstitutional or unlawful tax statute.

Stated another way, the tax overpayments allegedly made by Petitioners are in no way caused by or attributable to any feature of the Kentucky corporate tax law alleged to be unconstitutional or otherwise unlawful under federal law. All of the tax overpayments alleged to have been made by Petitioners are attributable solely to Petitioners' using separate returns, rather than unitary returns, to compute the taxable income and tax liability initially paid for the years in question.[12]

The Kentucky Department of Revenue disallowed each of the Petitioners' refund claims on the merits, *i.e.*, because the alleged unitary group failed to establish that it conducted a unitary business under the facts of its particular case and applicable law. Pet. App. 106 n.3 (Franklin Circuit Court Opinion).

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[12] The federal tax refund statutes do not distinguish between refund suits brought to recover taxes paid under an unconstitutional statute, and refund suits brought to recover taxes erroneously or incorrectly paid under a constitutional statute. 28 U.S.C. § 1346(a)(1), the Congressional waiver of the United States' sovereign immunity, gives the federal district courts jurisdiction to entertain suits against the United States for "the recovery of any internal-revenue tax alleged to have been erroneously or illegally assessed or collected, or any penalty claimed to have been collected without authority or any sum alleged to have been excessive or in any manner wrongfully collected under the internal-revenue laws." Using the federal statutory terminology, "a tax is overpaid when a taxpayer pays more than is owed, for whatever reason or no reason at all," *United States v. Dalm*, 494 U.S. 596, 609 n.6 (1990). The term "overpayment" under the federal statutes thus covers more conceptual territory than it does under Kentucky law, and "encompasses 'erroneously,' 'illegally,' or 'wrongfully' collected taxes, as those terms are used in 28 U.S.C. § 1346(a)(1)," *id.,* and would include taxes paid under an unconstitutional statute. The taxpayer in *United States v. Carlton*, for example, claimed to have overpaid estate tax liability because a deduction otherwise allowable to the estate had been retroactively repealed in violation of the Due Process Clause, and sued under § 1346(a)(1) to recover the tax.

REASONS FOR DENYING THE PETITION

The Kentucky Supreme Court's decision is a comprehensive and well reasoned application of correctly stated principles of rational basis review of retroactive tax statutes under the Due Process Clause and of statutory classifications in economic legislation under the Equal Protection Clause.

I. Petitioners' tax overpayment claims are barred by well settled principles of state sovereign immunity which do not need to be rehashed on certiorari.

The Petition's first reason for granting the writ is the startling assertion that "Petitioners possessed a due process right to pursue refund claims for overpaid taxes," and that KRS 141.200(17) "deprive[s] Petitioners of this due process right by precluding the Petitioners from pursuing their refund claims," Pet. 13. The "refund claims for overpaid taxes" to which the Petition refers means the refund claims made by the Petitioners under KRS 134.580, and necessarily refers to mere tax "overpayments" computed under a constitutional tax statute.

In other words, the Petition contends that the Due Process Clause requires a State to consent to suits in its own courts brought to recover mere tax overpayments made under a state tax statute that is neither "unconstitutional" under the federal Constitution nor "unlawful" under some overriding federal statute via the Supremacy Clause.

It may be helpful to clear away the conceptual underbrush.

Under Kentucky law, a taxpayer has no "right" to sue the Commonwealth to recover an alleged tax overpayment, unless the General Assembly has consented to the suit. *E.g., Department of Revenue v. Jack Cole Co.*, 474 S.W.2d 70, 72 (Ky. 1971) (refund suit "cannot be sustained because [taxpayers] cannot sue the Commonwealth without legislative consent"). "[T]he right to a refund of illegally or improperly collected taxes does not derive from the common law, but is a matter of legislative grace." *Revenue Cabinet v. Gossum*, 887 S.W.2d 329, 334 (Ky. 1994), *quoting Dep't of Conservation v. Co-De Coal Co.,* 388 S.W.2d 614 (Ky. 1964). *Accord, Hurry Up Broadway Co. v. Shannon*, 102 S.W.2d 30, 31 (Ky. 1937) (absent consent to refund suit, taxpayer "would be without any right whatsoever to collect such taxes from the Commonwealth . . . such right being a purely statutory one").

The federal rule is the same. *United States v. Dalm*, 494 U.S. 596 (1990), holds that "under settled principles of sovereign immunity" a taxpayer cannot sue the National Government to recover tax overpayments without consent, *id.* at 608, and that even the Supreme Court cannot "go beyond the authority Congress has given us in permitting [tax refund] suits against the Government," because "if any principle is central to our understanding of sovereign immunity, it is that the power to consent to such suits is reserved to Congress," *id.* at 610

So much for the notion that a taxpayer has a "due process right" to sue a State to recover a tax overpayment without consent.

KRS 141.200(17) retroactively revokes the Commonwealth's consent to unitary return refund suits, such as those brought by Petitioners, by providing that "no claim for refund" made for a pre-1995 year by a retroactive unitary return filed after December 22, 1994, "shall be effective or recognized for any purpose." The Kentucky Supreme Court has construed this language and held that "the plain meaning" of KRS 141.200(17) is that "the legislature withdrew its consent, specifically, to be sued for a refund under a combined return based on the unitary business plan." Pet. App. 11.[13]

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[13] The construction of KRS 141.200(17) by the Kentucky Supreme Court "become[s] a part of the statute" for purposes of review by this Court. *Wheeling Steel Corp. v. Glander*, 337 U.S. 562, 566 (1949); *Allied Stores of Ohio, Inc. v. Bowers*, 358 U.S. 522, 526 (1950). The 2007 Kentucky General Assembly made its intention pluperfectly clear by retroactively amending the general tax refund statute to provide that "notwithstanding any provision of the Kentucky Revised Statutes to the contrary, the Commonwealth hereby revokes and withdraws its consent to suit in any forum whatsoever on any claim for recovery" of "any tax overpayment" for a pre-1995 year based on a retroactive unitary return filed after December 22, 1994. The 2007 legislation applies to "all claims for such taxable years pending in any judicial or administrative forum." *See* KRS 134.580(9). The 2007 legislation is a virtual carbon copy of the federal legisla-

Perhaps the Petition means that KRS 141.200(17), which retroactively revoked the Commonwealth's consent to unitary method refund suits, unconstitutionally snatched from Petitioners some "due process right" they had in the Commonwealth's prior consent to suit.

There is very little gas in this conceptual tank.

It has been settled constitutional law for over 150 years that a State may retroactively revoke its consent to suit, even after the cause of action has arisen and even after suit has been filed. *Beers v. Arkansas*, 61 U.S. 527, 529-530 (1857) (retroactive revocation of consent to suit on bonds issued by the State unless certain procedural requirements satisfied; *held*, because consent to suit "is altogether voluntary on the part of the sovereignty, it follows that it may prescribe the terms and conditions on which it consents to be sued . . . and may withdraw its consent whenever it may suppose that justice to the public requires it;" State legislature "might have repealed the prior law [granting consent] altogether, and put an end to the jurisdiction of their courts in suits against the state, if they had thought proper to do so").

Beers v. Arkansas is no hoary precedent fallen into desuetude. Its holding has been repeatedly reconfirmed and relied upon by the Court in many

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tion upheld in *Edwards v. U.S. Dept. of Energy*, 200 Fed. Appx. 382, 389 (6th Cir. 2006), *cert. den.* 127 S.Ct. 1913 (2007).

modern cases, including *Raygor v. Regents of University of Minnesota,* 534 U.S. 533, 543 (2002), and *Alden v. Maine,* 527 U.S. 706, 746 (1999), within the last 15 years. *College Savings Bank v. Florida Prepaid Postsecondary Educ. Expense Bd.,* 527 U.S. 666 (1999), quoted *Beers'* key holding that a State's "decision to waive [sovereign] immunity, however, 'is altogether voluntary on the part of the sovereignty,'" and reaffirmed that "a State may, absent any contractual commitment to the contrary, alter the conditions of its waiver and apply those changes to a pending suit." 527 U.S. at 675-676.

The sovereign's consent to suit is not a property right protected by the Due Process Clause; *ergo*, revocation of consent to suit invades no constitutionally protected interest.

Justice Brandeis' opinion for a unanimous Court in *Lynch v. United States*, 292 U.S. 571 (1934), confirms that the Petitioners had no constitutionally protected interest in the Commonwealth's prior consent to suits to recover alleged tax overpayments, and therefore have no tenable argument that the retroactive revocation of consent to suit in KRS 141.200(17) violated any rights vouchsafed by the Due Process Clause. *Lynch* upheld retroactive revocation of Congress' consent to sue the United States on war risk insurance policies, with an unlimited period of retroactivity. "Although consent to sue was . . . given when the policy issued Congress retained power to withdraw the consent to sue at any time. [C]onsent to sue the United States is a privilege accorded, not the grant of a property right protected by the Fifth Amendment." 292 U.S. at 581.

Justice Douglas' opinion for a unanimous Court in *Maricopa County v. Valley Nat'l Bank*, 318 U.S. 357 (1943), upheld retroactive revocation of consent to suit against a federal agency, with an unlimited period of retroactivity. "Such consent, though previously granted, has now been withdrawn. And the power to withdraw the privilege of suing the United States knows no limitations." 318 U.S. at 362.

Subsequent decisions of the federal Courts of Appeals have unflinchingly followed *Lynch* and *Maricopa County*. *E.g., United States v. Lindsey*, 202 F.2d 239, 240 (1st Cir. 1953) ("consent to sue the United States is a privilege which is revocable at any time"); *Laycock v. United States*, 230 F.2d 848, 850 (9th Cir. 1956) ("well settled that the power to withdraw" consent "knows no limitations"); *Juda v. United States*, 13 Cl. Ct. 667, 689 (Cl. Ct. 1987) ("unbroken line" of decisions); *Heller v. United States*, 776 F.2d 92, 98 (3d Cir. 1985) ("Congress' power to remove a right to sue the government is absolute."); *Clinton County Comm'rs v. EPA*, 116 F.3d 1018, 1026 (3d Cir. 1997) (legislature's power to withdraw the privilege of suing the sovereign "knows no limitations"); *Edwards v. U.S. Dept. of Energy*, 200 Fed. Appx. 382, 389 (6th Cir. 2006), *cert. den.* 127 S.Ct. 1913 (2007) (power to withdraw consent "knows no limitations"); *Anolok v. United States*, 873 F.2d 369, 374 (Fed. Cir. 1989) ("no indication in any later

[Supreme Court] decision that *Lynch* is any other than an accurate statement of the law").

Petitioners contend that this "due process right to pursue their refund claims," *i.e.,* to sue the Commonwealth in its own courts, was established by *McKesson Corp. v. Div. of Alcoholic Beverages & Tobacco*, 496 U.S. 18 (1990), and *Reich v. Collins*, 513 U.S. 422 (1998)." Pet. 15.

Neither *McKesson* nor *Reich* may properly be freighted with the "due process right" claimed by the Petition, and the decision of the Kentucky Supreme Court in no way conflicts with either *McKesson* or *Reich*. Both *McKesson* and *Reich* differ from this case in three fundamental respects.

First, both *McKesson* and *Reich* involved state tax statutes which violated the federal Constitution. Neither involved a mere tax overpayment claim, such as a claim that a taxpayer has overpaid tax liability by computing a depreciation deduction using straight line rather than accelerated depreciation, or (as here) a claim that the taxpayer has overpaid tax liability by computing taxable income using a separate return rather than a unitary return.

In *McKesson*, the Florida Supreme Court had already determined that a Florida state tax statute (which imposed a discriminatory tax on out-of-state beverages but not on in-state citrus beverages) violated the dormant Commerce Clause, under *Bacchus Imports, Ltd. v. Dias,* 468 U.S. 263 (1984). *See*

496 U.S. at 22. In *Reich*, a Georgia state tax statute taxed pension income received by federal retirees but exempted pension income received by state government employees. It was uncontested that the Georgia statute and similar statutes of "numerous States" violated the "constitutional intergovernmental tax immunity doctrine," under *Davis v. Michigan Dep't of Treasury*, 489 U.S. 803 (1989)). *See* 513 U.S. at 108.

Thus both *McKesson* and *Reich* are statements of the constitutional common law of remedies, *i.e.,* what remedies are constitutionally required or permitted choices when a state court with subject matter jurisdiction considers what remedies may or must be fashioned when a taxpayer has paid taxes under a state statute determined to be unconstitutional. This inquiry starts with the basic constitutional principle, quoted by both *McKesson* and *Reich*, that "a denial by a state court of a recovery of taxes exacted in violation of the laws or Constitution of the United States by compulsion is itself in contravention of the Fourteenth Amendment," *McKesson*, 496 U.S. at 34; *Reich*, 513 U.S. at 109 (*both quoting Carpenter v. Shaw*, 280 U.S. 363, 369 (1930)). But where, as here, no claim is made that any taxes have been "exacted in violation of the laws or Constitution of the United States," neither *McKesson* nor *Reich* gains any conceptual traction.

Second, in both *McKesson* and *Reich*, the defendant States had consented to the refund suits in their own courts by the plaintiff taxpayers, thereby waiving state sovereign immunity. As the Court pointedly observed in *McKesson*, “the Florida courts accepted jurisdiction over this suit which sought monetary relief” from the State, 496 U.S. at 26, and Florida “concede[s] that the State waived any sovereign immunity from suit through [the state statute’s] authorization of a state-court refund action,” 496 U.S. at 49 n.34. Georgia in *Reich* had similarly waived its state sovereign immunity by statutorily authorizing refund suits to recover “illegally assessed” taxes, which the Court found to be an “obvious” consent to suits to recover “state taxes assessed in violation of federal law.” 513 U.S. at 111.

The state courts in *McKesson* and *Reich* had subject matter jurisdiction to entertain the claims asserted against Florida and Georgia. Both States had waived state sovereign immunity. But neither *McKesson* nor *Reich* says anything about the scope of state sovereign immunity when it has not been waived, or about the constitutional power of a State to retroactively revoke a prior waiver.

Third, both *McKesson* and *Reich* base their analyses on the proposition that exaction of a tax is a deprivation of property within the meaning of the Due Process Clause, and at the most hold that a State must provide “meaningful backward-looking relief to rectify any unconstitutional deprivation,” *McKesson*, 496 U.S. at 32, or “a clear and certain remedy for taxes collected in violation of federal law,” *Reich*, 513 U.S. 108. Assuming *arguendo* that these holdings have any vitality beyond cases like *McKesson* and *Reich* where state sovereign immunity has been waived, they do not have any staying power here: the Kentucky corporate income tax law has not been held to be unconstitutional or to otherwise violate federal law.

A mistake by a taxpayer in determining his tax liability does not transmogrify a constitutionally valid state tax statute into an "unconstitutional deprivation" of property or an exaction of a tax "in violation of federal law."

II. The Court has already provided ample "guidance" on "the due process limits of retroactive legislation."

The Petition's second reason for granting certiorari starts by asking the Court to "offer guidance to States and taxpayers on the due process limits of retroactive legislation" Pet. 19, but ends by asking the Court "to establish that retroactive legislation violates due process when a state legislature fails t:o enact the legislation at the first possible legislative session," Pet. 24. Presumably this Due Process Clause requirement would shackle Congress as well.

The Court has already provided all the "guidance" needed on the permissible reach of retroactive legislation in three prior decisions. *United States v. Carlton*, 512 U.S. 26, 30-31 (1994) ("test of due process" for "retroactive economic legislation" is "met simply by showing that the retroactive application of the legislation is itself justified by a rational legislative purpose." *Accord*, *Pension Benefit Guaranty*

Corp. v. R.A. Gray & Co., 467 U.S. 717, 729-730 (1984); *Usery v. Turner Elkhorn Mining Co.*, 428 U.S. 1, 16-17 (1976).

The Petition fails to make any showing that the *Carlton* test has bemused the lower courts, or has led to decisions by different courts that cannot easily be reconciled as slightly different applications of a properly stated rule of law. Indeed, the Petition admits that "lower courts have followed" *Carlton* albeit "in different ways," Pet. 21, the operative word being "followed."[14]

The Petition then abruptly veers into cold and deep water by advancing the propositions that "due process should limit state legislatures to enacting retroactive legislation only at the first opportunity to do so," and that "it is fundamentally irrational" for a state legislature "to understand that a revenue or tax problem exists that can only be remedied through retroactive legislation, and fail to enact the legislation at the first possible legislative session." Pet. 24.

These propositions are much too extravagant to be seriously maintained, or to warrant the Court's consideration on certiorari. What property interest

[14] The Petition at 23 n.3 quarrels with the Kentucky Supreme Court's factual determination that the Kentucky General Assembly enacted KRS 141.200(17) and KRS 141.200(18) "at the first available opportunity, as it became aware of the issues," 296 S.W.3d at 401, asserts that "the undisputed evidence" before the trial court was to the contrary. This argumentative reference to the record is neither correct nor a good reason for granting certiorari.

protected by the Due Process Clause requires retroactive economic legislation to be enacted "at the first possible legislative session," or not at all?

Any such use-it-or-lose-it limitation on a legislature's constitutional power cannot be squared with *Carlton's* express holding that "a taxpayer has no vested right in the Internal Revenue Code" protected by the Due Process Clause, 512 U.S. at 33, or reconciled with the precedents on which *Carlton* relied. *See, e.g., Millikin v. United States*, 283 U.S. 15 (1931) (sustaining statute increasing federal estate tax on gifts made in contemplation of death, applicable with an unlimited period of retroactivity to all gifts made prior to enactment); *Usery v. Turner Elkhorn Mining Co.*, 428 U.S. 1 (1976) (sustaining federal statute imposing liability on employers for black lung benefits, applicable with an unlimited period of retroactivity for all prior employees). Decisions of three Courts of Appeals would also have to be disapproved.[15]

We cannot imagine that the Due Process Clause does not constrain the unlimited retroactive effect of the Court's decisions,[16] yet cabins the consti-

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[15] *E.g., Montana Rail Link, Inc. v. United States*, 76 F.3d 991 (9th Cir. 1996) (four to six year period of retroactivity); *Honeywell, Inc. v. United States*, 973 F.2d 638 (8th Cir. 1992) (ten years); *Wilgard Realty Co.*, 127 F.2d 514 (2d Cir.) cert. den. 317 U.S. 655 (1942) (15 years); *accord*, *Fife v. CIR*, 82 T.C. 1 (1984) (unlimited period of retroactivity).

[16] All the Court's decisions are "the controlling interpretation of federal law and must be given full retroactive effect in all cases still open on direct review and as to all events, regardless of whether such events predate or postdate our announcement of

tutional lawmaking power of Congress and the States within a retroactive period no greater than "the first possible legislative session" following the legislature's identification of the "legitimate legislative purpose" sought to be achieved by retroactive economic legislation.

The *GTE* case was a statutory construction case. Like any statutory construction decision, its result (except with respect to the parties to the final judgment, *see Plaut v. Spendthrift Farm, Inc.*, 514 U.S. 211 (1995)) and precedential effect could be changed or nullified by a subsequent amendment of the statute construed. The Petitioners never had any interest in the *GTE* decision protected by the Due Process Clause. "No person has a vested interest in any rule of law, entitling him to insist that it shall remain unchanged for his benefit." *New York Central Railroad Co. v. Sarah White*, 243 U.S. 188, 198 (1917). "Our cases have clearly established that a person has no property, no vested interest, in any rule of the common law." *Duke Power Co. v. Carolina Envir. Study Group, Inc.*, 438 U.S. 59, 88 n.32 (1978) (citing many cases).

The Petition fails to explain why any of these bedrock precedents needs to be reconsidered.

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the rule." *Harper v. Virginia Dep't of Taxation*, 509 U.S. 86, 97 (1993).

III. The Equal Protection Clause does not require all-or-nothing economic legislation.

The Petition's third reason for granting the writ is that the Court "should establish" that the Equal Protection Clause "precludes a State from treating similarly situated taxpayers differently based solely on the date" their income tax refund claims are filed "and the order in which "those claims [are] processed by a state agency." Pet. 25.

In discussing this third reason, the Petition lumps KRS 141.200(17) and KRS 141.200(18) into one undifferentiated statute the Petition calls "the 2000 Amendments." This conflation of two independently operative statutes discombobulates the analysis. If either statute is sustained, Petitioners' refund claims will be precluded, either by the substantive tax law or by state sovereign immunity.

If the retroactive prohibition of unitary returns under KRS 141.200(18) is upheld, then no Petitioner has overpaid its correct tax liability, determined using separate returns. If no tax overpayment has been made, no refund must be paid.

If the retroactive revocation of consent to unitary return refund suits under KRS 141.200(17) is upheld, then no Petitioner may sue the Commonwealth in a Kentucky court to recover an alleged tax overpayment computed using unitary returns. If state sovereign immunity bars the suit, the merits of the claim are immaterial.

We cannot agree with the Petition's assertion that "this case involves similarly situated taxpayers being treated differently as a result of the 2000 Amendments." Pet. 26. This assertion mischaracterizes both statutes, which apply equally to all corporate taxpayers.

The "different treatment" of "similarly situated taxpayers" decried by the Petition is a function of the effective date of the two statutes, not of any legislative classification among taxpayers.

All tax legislation must have an effective date. The Tax Reform Act of 1986 did not violate the Equal Protection Clause by disallowing depreciation deductions generated in years after 1986 as "passive losses," while permitting depreciation deductions generated in 1986 and prior years to fully shelter ordinary income, even though the deductions were generated by exactly the same depreciable property on either side of the effective date of the law.

If the different treatment of "similarly situated taxpayers" caused by the effective date of tax legislation violates the Equal Protection Clause, no tax legislation could ever withstand an Equal Protection Clause challenge.

The Petition mistakes an effective date for a legislative classification, and a tautology for a constitutional issue. The Court long ago determined that a tax statute with a retroactive effective date no more offends the Equal Protection Clause than a tax statute with a prospective effective date. *Welch v. Henry*, 305 U.S. 134 (1938), held that a 1935 state tax law retroactively taxing dividends received in 1933, was not "a denial of equal protection because retroactive. If the 1933 dividends differed sufficiently from other classes of income to admit of the taxation, in that year, lapse of time did not remove that difference so as to compel equality of treatment when the income was taxed at a later date," 305 U.S. at 144.

In other words, if tax legislation would not violate the Equal Protection Clause if made effective prospectively, it does not violate the Equal Protection Clause if made effective retroactively. There is no Equal Protection issue lurking here.

If we focus on KRS 141.200(17) — the retroactive revocation of consent to unitary return refund suits — then it appears that Petitioners want the Court to "establish" that the Equal Protection Clause requires a sovereign State to consent to all types of tax refund suits, or to none. But "to the extent [a State] has chosen to consent to certain classes of suits while maintaining its immunity from others, it has done no more than exercise a privilege of sovereignty concomitant to its constitutional immunity from suit." *Alden v. Maine*, 527 U.S. 706, 758 (1999). *Cf. California v. Arizona*, 440 U.S. 59, 65 (1979) ("It is clear, of course, that Congress could refuse to waive the Nation's sovereign immunity in all cases or only in some cases.").

If we focus on KRS 141.200(18) — the retroactive prohibition on the use of unitary returns — then it appears that Petitioners want the Court to "establish" that the Equal Protection Clause requires a retroactive tax statute to apply to all prior transactions or years, or to none. But the Equal Protection Clause "does not compel [state] legislatures to prohibit all like evils, or none," *U.S. v. Carolene Products Co.,* 304 U.S. 144, 151 (1938). Grandfather clauses have been routinely upheld against Equal Protection Clause attacks. *E.g., City of New Orleans v. Dukes*, 427 U.S. 297 (1976) (upholding prohibition of French Quarter pushcart vendors which exempted vendors in operation for eight years: "rather than proceeding by the immediate and absolute abolition of all pushcart food vendors, the city could rationally choose initially to eliminate vendors of more recent vintage. This gradual approach to the problem is not constitutionally impermissible."); *United States R.R. Retirement Bd. v. Fritz*, 449 U.S. 166, 177 (1980) (upholding abolition of double retirement benefits for railroad employees which exempted persons hired prior to specified date: "because Congress could have eliminated windfall benefits for all classes of employees, it is not constitutionally impermissible for Congress to have drawn lines between groups of employees for the purpose of phasing out those benefits"). The Petition offers no reason why these precedents need to be revisited.

The Petition fails to make any showing, or even to suggest, that it was unreasonable or irrational for the Kentucky General Assembly to have concluded that the lion's share of a predicted $200,000,000 revenue loss was attributable to retroactive unitary returns filed after the date of the *GTE* decision, and therefore to have made the prohibition effective with respect to such returns. That failure is fatal to the Petition's contention that KRS 141.200(18) suffers some Equal Protection Clause infirmity that needs doctoring on certiorari.

CONCLUSION

The Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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