

1           IN THE SUPREME COURT OF THE UNITED STATES

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3   MEADWESTVACO CORPORATION,                               :

4   SUCCESSOR IN INTEREST TO                               :

5   THE MEAD CORPORATION,                                   :

6                               Petitioner                               :

7                               v.   :   No. 06-1413

8   ILLINOIS DEPARTMENT OF                                 :

9   REVENUE, ET AL.   :

10   - - - - - x

11   Washington, D.C.

12   Wednesday, January 16, 2008

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14                               The above-entitled matter came on for oral  
15   argument before the Supreme Court of the United States  
16   at 11:17 a.m.

17   APPEARANCES:

18   BETH S. BRINKMANN, ESQ., Washington, D.C.; on behalf  
19       of the Petitioner.

20   BRIAN F. BAROV, ESQ., Assistant Attorney General,  
21       Chicago, Ill.; on behalf of the Respondents.

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P R O C E E D I N G S

(11:17 a.m.)

CHIEF JUSTICE ROBERTS: We will hear argument next in Case 06-1413, MeadWestvaco v. The Illinois Department of Revenue.

Ms. Brinkmann.

ORAL ARGUMENT OF BETH S. BRINKMANN

ON BEHALF OF THE PETITIONER

MS. BRINKMANN: Mr. Chief Justice, and may it please the Court:

The ruling of the Illinois Appellate Court in this case radically expanded the Court's operational-function tax. The State tax at issue violates the principles of constitutional limitations on state taxing authority for at least two reasons. First, the factors relied on by the appellate court here for functional -- for operational function would mean that ownership and investment would meet that standard. But that's what this Court rejected in Allied-Signal.

A State does not have the authority to reach out to tax all investments owned by a company that does business in the State. The operational function demands more. It applies --

JUSTICE GINSBURG: You are saying to me, Ms. Brinkmann -- we talk about an asset, an investment.

1 This was one company. This -- it's strange to talk  
2 about unitary basis or investment. This is a division  
3 of one company. And we are talking about a sale of  
4 assets. Not the sale of stock of a subsidiary.

5 So what more is there than this is one  
6 company, it sells some of its assets?

7 MS. BRINKMANN: Well, Your Honor, the fact  
8 that it's a division does not mean that it meets either  
9 the operational-function test or the unitary-business  
10 test. A long line of cases from this Court tell us  
11 that. It --

12 JUSTICE GINSBURG: Do we have any cases --  
13 do we have any decisions that go against the state  
14 taxing authority that involve divisions as opposed to  
15 subsidiaries?

16 MS. BRINKMANN: No, but the Exxon case  
17 involved divisions, and it went in favor of the state  
18 taxing authority. But the Court applied a  
19 straightforward, unitary business analysis to that.  
20 And, Your Honor, this dates back to the Adams Express  
21 case of 1897.

22 The Court in that case said it's not  
23 ownership. It's about the use, the unitariness of use,  
24 not of ownership. Mobile followed on that. Mobile  
25 talked about the fact that it's not the corporate form

1 that mattered. It pointed out that that could have  
2 little to do with the underlying determination of  
3 apportionment, which depends upon whether it's a  
4 discrete business enterprise.

5 And then following on the heels of that  
6 analysis in Mobil, the Court applied it to the Exxon  
7 case that involved divisions. That was a vertically  
8 integrated corporation. It's very different from the  
9 facts of this case, and it reached a different result.

10 Moreover, the Woolworth case involved  
11 subsidiaries. Three out of the four of them were 100  
12 percent wholly owned.

13 JUSTICE STEVENS: Can I go back to sort of a  
14 fundamental question I'm not quite sure I know the  
15 answer to. Supposing we don't have corporations here,  
16 but an individual resident of New York owned this whole  
17 business and a big bunch of it was activities in  
18 Illinois, and he sold the business. Would Illinois have  
19 the authority to impose any tax on that transaction?

20 MS. BRINKMANN: If it was a capital gain,  
21 Your Honor, on the sale of investment, the Court's  
22 longstanding cases teach that it is the domicile that  
23 taxes that commercial gain.

24 JUSTICE STEVENS: I'm assuming it's not the  
25 domicile. The owner lives in New York. The business is

1 all over the country, but does millions of dollars of  
2 business in Illinois. And they sell the whole business.  
3 Would the owner be subject to any tax of any kind in  
4 Illinois on that transaction? Could he constitutionally  
5 be subjected to any tax?

6 BRINKMANN: If there was -- the domiciliary  
7 State generally is the State which has the authority to  
8 tax an income on a capital gain --

9 JUSTICE STEVENS: Assume it's not the  
10 domiciliary State.

11 MS. BRINKMANN: But what the Court explained  
12 in Mobil, for example, if it is under the unitary  
13 business principle, then the State in which --

14 JUSTICE STEVENS: Could we get an answer  
15 without reference to cases? Do you think Illinois would  
16 have the authority to impose a tax on that transaction?

17 MS. BRINKMANN: If the -- there was  
18 sufficient nexus to the company doing business --

19 JUSTICE STEVENS: Millions of dollars of  
20 business in Illinois, that's my assumption.

21 MS. BRINKMANN: Yes, they would be able to  
22 tax the ongoing business activity in that State.

23 JUSTICE KENNEDY: No.

24 JUSTICE STEVENS: Could they tax the sale of  
25 the business?

1 JUSTICE KENNEDY: I have the same --

2 MS. BRINKMANN: The sale of the business  
3 would be to the domicile of the seller. They would be  
4 able to --

5 JUSTICE STEVENS: You're saying only the  
6 domicile could impose a tax?

7 MS. BRINKMANN: Yes, unless, as the Court  
8 recognized in Mobil, there is this unitary business  
9 exception, because the State's ability to tax begins at  
10 the starting point at the territorial limitations of the  
11 State. And the Court has --

12 JUSTICE STEVENS: But if they owned a truck  
13 instead of a business, they could tax that transaction,  
14 I suppose?

15 JUSTICE SCALIA: You can't have a unitary  
16 business -- a person who is a unitary business. I mean,  
17 a person can't be unitary with Exxon. I mean, when you  
18 speak of a unitary business you're talking about a  
19 corporation which, you know, is unitary with another  
20 corporation.

21 MS. BRINKMANN: That's the area --

22 JUSTICE SCALIA: Once you put it into a  
23 personal taxation scheme, it seems to me the whole  
24 unitary business notion has no application at all.

25 MS. BRINKMANN: Well, I agree with you, Your

1 Honor. But it does come back to the taxing, the right  
2 of the domicile State to tax on a sale --

3 JUSTICE GINSBURG: What is -- what does the  
4 domicile State -- we have Ohio. But you say as a matter  
5 of constitutional law, not State tax policy, as a matter  
6 of constitutional law, the only State that has authority  
7 to tax the capital gain is Ohio?

8 MS. BRINKMANN: That's right, Your Honor,  
9 unless --

10 JUSTICE GINSBURG: Does Ohio -- would Ohio  
11 give credit for the tax that its sister State thinks is  
12 due? What is, in fact, Ohio's tax law in this respect?  
13 Does Ohio give credit to taxes paid by other States --  
14 to other States?

15 MS. BRINKMANN: Ohio would allocate the  
16 entire gain as a capital gain on an intangible that was  
17 sold in the State of Ohio. That would be allocated in  
18 its entirety to Illinois.

19 Now, what the Court has recognized is that  
20 default principle sometimes gives way when that gain has  
21 had enough connection to business activity in another  
22 jurisdiction. That's where these issues arise, because  
23 there are States taxing multi- state activities. And  
24 that's --

25 JUSTICE GINSBURG: Can I have an answer to a



1 very simple question? If Illinois claimed the tax,  
2 would Ohio give credit for the tax paid in Illinois?

3 MS. BRINKMANN: Not if Ohio had the  
4 constitutional right to allocate that tax to Ohio, as it  
5 does.

6 JUSTICE GINSBURG: Do we know what -- what  
7 Ohio does in these situations?

8 MS. BRINKMANN: Yes. It allocates it to the  
9 State of Ohio. The only exception for that would be in  
10 a situation, not the facts here, but if that capital  
11 gain either served an operational function to the  
12 business activities that were conducted in another  
13 State, then that State would have a right to apportion  
14 it and tax its portion of that or if the operational  
15 function applied. And that is because the activity now  
16 has transformed from just a capital gain that's  
17 connected to the domiciliary State of the seller to a  
18 business income because it is part of this unitary  
19 business. That's why the other State has a right to  
20 apportion.

21 JUSTICE ALITO: What has Ohio done --

22 MS. BRINKMANN: That's not the situation  
23 here.

24 JUSTICE ALITO: What has Ohio done up to  
25 this point with respect to this transaction?

1 MS. BRINKMANN: Under Ohio's laws this would  
2 be allocated to that State.

3 CHIEF JUSTICE ROBERTS: To Ohio?

4 MS. BRINKMANN: Yes, because it's a capital  
5 gain on a sale of an investment.

6 CHIEF JUSTICE ROBERTS: Ms. Brinkmann, you  
7 begin your brief by saying this, a paper company, that  
8 happens to own a data processing company. Why couldn't  
9 you equally say this is a data processing company that  
10 happens to own a paper company?

11 MS. BRINKMANN: No, Your Honor. This has  
12 been a paper company since 1846.

13 CHIEF JUSTICE ROBERTS: Well, and  
14 Lexis/Nexis has been a data processing company since  
15 whenever.

16 MS. BRINKMANN: But under the Court's  
17 unitary --

18 CHIEF JUSTICE ROBERTS: It's not the  
19 oldest -- whichever is oldest isn't the one that gets to  
20 be regarded as the dominant partner, is it?

21 MS. BRINKMANN: No. But when you do the  
22 analysis, you're looking at the taxpayer, which is Mead  
23 Corporation. And it clearly has a --

24 CHIEF JUSTICE ROBERTS: Is General Electric  
25 a light bulb company or, since it owns NBC, a media

1 company.

2 MS. BRINKMANN: I would have to know many  
3 more facts in order to answer that questions, Your  
4 Honor. But I -- and I don't mean to be evasive --

5 JUSTICE GINSBURG: Why isn't the answer  
6 both? Why isn't the answer both, just as here it is  
7 both a paper or office supply company and a Lexis/Nexis,  
8 electronic data company?

9 MS. BRINKMANN: It's an analytical construct  
10 that we're doing here. We're looking at the taxpayer  
11 who is being taxed, the Mead Corporation. So you look  
12 at its business that's being conducted in Illinois.  
13 They have a unitary paper company that's vertically  
14 integrated that's doing business activities in Illinois.

15 CHIEF JUSTICE ROBERTS: Well, that's because  
16 they sell paper in Illinois?

17 MS. BRINKMANN: Yes.

18 CHIEF JUSTICE ROBERTS: Well, Lexis sells  
19 data services in Illinois, too.

20 MS. BRINKMANN: Yes. But when you're  
21 looking -- and for both purposes, Your Honor, for State  
22 tax on the operating income of both of those businesses,  
23 Illinois does have a right to apportion those taxes.  
24 And those taxes were paid without objection by both of  
25 those businesses.

1                   We're talking about a tax on a different  
2 event, on a capital gain on a sale of the business in  
3 Ohio.

4                   CHIEF JUSTICE ROBERTS: Well, why doesn't --  
5 I mean, you just said, as I understand it, Illinois has  
6 the right to tax Lexis under business activities in  
7 Illinois. Illinois would argue the reason it has a  
8 capital gain is partly because they were doing business  
9 in Illinois and so we should be entitled to part of that  
10 capital gain. Almost -- I mean, it seems to me it would  
11 be pretty easy if they get to tax 2 percent of Lexis's  
12 business, well then maybe they should get 2 percent of  
13 the capital gain when it's sold or tax 2 percent.

14                   MS. BRINKMANN: Your Honor, that is a  
15 belated argument that the State of Illinois has raised  
16 in this Court. It did not present an argument to the  
17 Illinois appellate court based on Lexis/Nexis's  
18 connection to Illinois. It raises a host of  
19 jurisdictional, procedural and substantive bars.

20                   Under the rules of Illinois, as we point out  
21 in our reply brief, that argument is waived. This comes  
22 to the Court from a State court, not a Federal court of  
23 appeals. Because of that waiver, it's an independent  
24 and adequate state ground.

25                   Moreover, that argument wasn't raised in the

1 brief in opposition, either.

2 JUSTICE GINSBURG: They're raising it in --  
3 in support of the judgment. So if it's novel, but it  
4 supports the judgment, then at least shouldn't the  
5 Illinois courts have a chance to look at it and say, oh,  
6 that's what we really meant, we just got -- explained it  
7 the wrong way?

8 MS. BRINKMANN: Well, that would certainly  
9 be a matter for the Illinois court rather than for this  
10 Court, Your Honor. But in addition, I think any  
11 disposition on the merits of that issue would be a  
12 ruling by this Court that would be trumping that  
13 independent and adequate State ground waiver.

14 Moreover, this argument wasn't raised in the  
15 brief in opposition, either. And the Court's precedent,  
16 of course, and practice would not be to address that.  
17 Particularly in this case, it denied notice to the amici  
18 who would be affected by this argument.

19 But turning to the substance of it --

20 JUSTICE KENNEDY: I think this is part of  
21 the substance. I thought that as part of one of your  
22 answers you said that Ohio is free to allocate part of  
23 this capital gains tax to Illinois? Did I hear you say  
24 that, because I don't understand that?

25 MS. BRINKMANN: No, Your Honor, I'm sorry.

1 I apologize if I misspoke. Ohio would allocate, I mean,  
2 take the entire gain for itself as the domicile State of  
3 the seller --

4 JUSTICE KENNEDY: I see.

5 MS. BRINKMANN: -- of the investment. In  
6 other factual scenarios, if it turns out that that asset  
7 actually was not an investment and in fact had enough  
8 connection to the business activities in Illinois  
9 because it was really the supplier of the raw materials,  
10 or the two examples that this Court has given as  
11 operational functions is the interest on the bank  
12 account, which is the working capital, or the -- the  
13 futures hedging against the raw material of corn.

14 CHIEF JUSTICE ROBERTS: Well, isn't it kind  
15 of like futures hedging? I mean, you've got a paper  
16 company and then you've got something that is sort of  
17 the paperless aspect, and they can look at it and say,  
18 well, we're kind of hedging our paper business by  
19 investing heavily in something that's supposedly going  
20 to take away the need for paper.

21 MS. BRINKMANN: No, Your Honor. Under the  
22 operational function test, it has to be a much closer  
23 nexus to the operating, the operations of the paper  
24 company; and short of that operational function -- or if  
25 it were part of the unitary business, the domiciliary

1 State would allocate. And if I could turn --

2 JUSTICE KENNEDY: Are you saying this is a  
3 passive investment?

4 MS. BRINKMANN: Yes, Your Honor.

5 JUSTICE SOUTER: How can you call it a  
6 passive investment, not only when there was -- I think  
7 undisputedly -- as -- as much interest and activity in  
8 Nexis's business planning by the Mead people? But to my  
9 mind even more importantly, when in fact Mead, I think a  
10 couple of times, merged with -- with Nexis -- with Lexis  
11 -- when that provided a tax advantage, by -- by giving  
12 them loss carryforwards that reduced their taxes. Why  
13 isn't it fair to -- to say under the operational  
14 function test that if -- if the company is -- if Nexis  
15 is -- is mergeable with Mead when it produces a tax  
16 advantage and is certainly in a very operational sense  
17 functional then, because it's saving them a lot of  
18 money -- and that's, that has nothing to do with passive  
19 investment. If it's usable in a merger scenario there,  
20 it ought when the -- when the tide turns be -- be  
21 regarded as close enough in operational function to be  
22 taxable when the gain comes in.

23 MS. BRINKMANN: Your Honor, that's contrary  
24 to the Court's long-standing recognition that something  
25 that enriches the taxpayer is not necessarily part of

1 the unitary business's operational function.

2 JUSTICE SOUTER: That's -- that's right.

3 But weren't the enrichment cases in which income was  
4 being generated by an investment? The investor, of  
5 course, was the -- was the taxpayer company, and it  
6 simply reaped the benefits of a profitable investment.  
7 That's something very different from merging  
8 corporations, then unmerging them, and then merging them  
9 again to provide not merely enrichment, but great tax  
10 savings; and if they are operationally close enough to  
11 produce great tax savings, why shouldn't they be treated  
12 as operationally close enough when in fact they -- they  
13 produce a capital gain?

14 MS. BRINKMANN: Because that isn't the  
15 operational connection that justifies a State --

16 JUSTICE SOUTER: The gain alone certainly is  
17 not. If they had absolutely done nothing but make their  
18 investment and wait to see whether the ship came in, I  
19 would understand your argument. But between the  
20 investment and the return of the ship, they were merging  
21 these corporations back and forth for -- for their --  
22 for Mead's tax advantage. And that seems to me to take  
23 it out -- take the facts of this case out of the sort of  
24 the paradigm of the -- the operational or the  
25 nonoperational function cases.



1 MS. BRINKMANN: Your Honor, I think not, if  
2 we look at Allied-Signal, we look at Woolworth, and we  
3 look at ASARCO. Allied-Signal was a sales and  
4 investment -- and getting back to the point about the  
5 argument really was waived about the connection with  
6 Lexis/Nexis in Illinois, those were the same facts in  
7 Allied-Signal. The investment there was --

8 JUSTICE GINSBURG: It was a sale of stock in  
9 that case, wasn't it?

10 MS. BRINKMANN: Yes.

11 JUSTICE GINSBURG: It was the sale of a  
12 subsidiary. And here we have a sale of assets of one  
13 company, and that's why it's so hard for me to see this,  
14 as, why are we talking about unitary or not? There is  
15 only one company; it's Mead.

16 MS. BRINKMANN: In Allied-Signal, the  
17 investment there was also doing business within the  
18 State. In the Exxon case, there were divisions to which  
19 this Court applied the entire unitary business  
20 principle, because what the Court has said repeatedly in  
21 Mobil, in Exxon, in all these cases, it's not the  
22 corporate form; it is whether there is a discrete  
23 business enterprise; and ASARCO speaks to this.

24 JUSTICE GINSBURG: You told me that there  
25 was no case that the tax -- taxing authority lost that

1 involved divisions of a single company and sale of  
2 assets, rather than the sale of stock.

3 MS. BRINKMANN: That's correct. We have  
4 four or five cases here. One of them does involve  
5 divisions, Exxon, but in that case it was a vertically  
6 integrated corporation, and the State prevailed in that  
7 case, but it did not change the analysis that applied.

8 JUSTICE GINSBURG: Well, we're talking about  
9 what Due Process permits States to do, and you're asking  
10 us to declare a restriction that, as far as I know, has  
11 never been declared in any case.

12 MS. BRINKMANN: It has, Your Honor. It goes  
13 back to principles that ownership do -- does not  
14 determine; simply because there is a business operating  
15 in the State, the State does not have the right to tax  
16 every investment that's owned by that. That dates back  
17 to 1897.

18 JUSTICE GINSBURG: It's not just that it's  
19 an investment, it's not just that it's holding on to the  
20 shares in another company. It's both of these are  
21 ongoing businesses, Lexis/Nexis and Mead, and they are  
22 both generating income, and all along Illinois has been  
23 taxing the income of both of them, right?

24 MS. BRINKMANN: Yes, the operating income  
25 within the State's apportioned. But if you look to the

1 business activity of the taxpayer Mead, operating in  
2 Illinois, it is that nexus on which Illinois is claiming  
3 that they have a right to tax here. And if we look at  
4 the Woolworth case, for example, I think that is also  
5 instructive. Those were four subsidiaries. Three of  
6 them were 100 percent wholly owned, and the Court  
7 expressly said we recognize they are wholly owned  
8 subsidiaries. These could be integrated divisions, and  
9 they said, that is not significant, if they are  
10 independent, different business enterprises.

11 JUSTICE GINSBURG: Weren't those foreign  
12 corporations?

13 MS. BRINKMANN: Yes, Your Honor.

14 JUSTICE GINSBURG: So running them as -- as  
15 a single company would have been a little harder.

16 MS. BRINKMANN: Well, no, in fact there were  
17 also some foreign subsidiaries, I believe, involved in  
18 the ASARCO case, for example, Your Honor, and the same  
19 analysis applied -- you know, whether it was vertically  
20 integrated and whether or not it met -- the unitary  
21 business test goes back to three core principles, and  
22 this Court has said at least four if not five times that  
23 the unitary business principle is the linchpin of  
24 apportionment. That is whether or not there is  
25 functional integration.

1 JUSTICE SOUTER: Don't we start -- I don't  
2 mean to cut off your argument, but don't we start with  
3 the assumption that this is not a unitary business?  
4 Wasn't that the finding of the trial court which was not  
5 disturbed on appeal?

6 MS. BRINKMANN: That's right, Your Honor.  
7 That's right.

8 JUSTICE SOUTER: You can say it if you want,  
9 but I wanted to make sure --

10 MS. BRINKMANN: There is no virtual  
11 integration; there is no sharing of centralized  
12 management; there's no economies of scale. We think  
13 this is unassailable in the stipular record --

14 JUSTICE BREYER: Am I thinking about that  
15 part correctly? I -- I found this difficult. I go back  
16 to the railroad; that seems the easiest case. You have  
17 a railroad in 50 States, and Illinois finds it very hard  
18 to evaluate its -- evaluate its value, its railroad  
19 property in Illinois, because the value of that depends  
20 on service everywhere. So the court says that's the  
21 unitary principle; and really what you're supposed to  
22 look at is whether when you look at the supposedly  
23 separate part of the business, does that separate part  
24 of the business contribute to the whole thing? So that  
25 if you were in fact trying to say what is Illinois doing

1 without considering that separate part, it would be  
2 tough to do.

3 I mean, that's the underlying theme.

4 MS. BRINKMANN: We would --

5 JUSTICE BREYER: And if that's so, there is  
6 no second test. I mean, I grant you there is language,  
7 but really what people have done is they've said, we are  
8 here in a special situation because we have an interest  
9 in another company, and that's a special part of our  
10 business, and has nothing to do with the rest of the  
11 business. And then the argument is no, it does have  
12 something to do with the rest of the business. And if  
13 it does, like it provides you with working capital, it's  
14 just like the railroad track in California vis-a-vis  
15 Illinois.

16 MS. BRINKMANN: It's contributing to the  
17 business.

18 JUSTICE BREYER: And if it doesn't, it  
19 doesn't. So now, if that's right, then it's the form of  
20 analysis rather than the result that's wrong in the  
21 court below. Because they start talking about two  
22 separate tests and then people argue whether the second  
23 should swallow up the first, and at that point I get  
24 totally lost. It's fairly long, but I'd appreciate your  
25 evaluating what I've just said.

1 MS. BRINKMANN: Well, Your Honor, there --  
2 on this record, there's no question that the Lexis/Nexis  
3 cannot meet the unitary business test.

4 JUSTICE GINSBURG: Yes, there is, Ms.  
5 Brinkmann. The Illinois appellate court never got to  
6 that question. Illinois argued all along this is a  
7 unitary business. The only one who said it wasn't was  
8 this trial court, and the Illinois intermediate  
9 appellate court says, well, we don't have to deal with  
10 that because if you use the other label, operational  
11 function, that comes out all right, too.

12 But this argument was certainly the number  
13 one argument that Illinois was making. It lost only in  
14 the trial court on -- on it. And the appellate court  
15 said we don't have to get to it. So I think your answer  
16 to Justice Souter really wasn't accurate because it  
17 isn't --

18 MS. BRINKMANN: Well, our position is on the  
19 record here, Your Honor, the stipulated record, that  
20 it's unassailable. But we do --

21 JUSTICE GINSBURG: All we know is that a  
22 trial judge said that was so.

23 MS. BRINKMANN: And then that's our  
24 position, obviously, on the record, Your Honor; but we  
25 agreed this was properly raised in the appellate court,

1 as opposed to the other argument which was not. And  
2 this also was mentioned in the brief in opposition, as  
3 opposed to their other argument, which was not.

4 So we do think the Court could reach this  
5 argument, and we maintain that on this record the  
6 linchpin of apportionment giving the right of a State --  
7 and this is a right to extend beyond its territory.

8 The Court has already let it go beyond its  
9 territory to get to something outside the State if it's  
10 part of the unitary business -- the railroad case, the  
11 express case.

12 And in that situation there are three  
13 factors, none of which can be met on this record. There  
14 was no shared, centralized management, none. There was  
15 no integrated functions, none. And there were no  
16 economies of scale. Lexis/Nexis did not even get a  
17 discount on any paper they bought from Mead. They were,  
18 you know, minor customers of each other.

19 JUSTICE GINSBURG: Maybe when we're talking  
20 about Due Process and Commerce Clause limitations on  
21 what States can tax, we ought to ask ourselves if those  
22 three -- is that it? If we're trying to measure, is  
23 there a sufficient relationship between Lexis/Nexis,  
24 Mead, and the State of Illinois to make it fair for them  
25 to tax?

1                   And you say, oh, yes. Each year when  
2 they're making income, when they are a going concern,  
3 Illinois can get a piece of it. But when the assets are  
4 sold, assets that would have generated income for  
5 Illinois year after year, but when those assets are  
6 sold, Illinois can get nothing to represent -- to  
7 substitute for that stream of income that it would have  
8 gotten.

9                   MS. BRINKMANN: No. It will continue to get  
10 income tax on an apportioned basis before and after.

11                   JUSTICE GINSBURG: But Lexis/Nexis is gone.

12                   MS. BRINKMANN: Well, Lexis/Nexis continues  
13 to operate. It's now owned by Reed Elsevier. So it  
14 would continue to pay an apportioned income tax.

15                   It's a different event here, Your Honor. It  
16 is the sale of an investment that occurred in Ohio. And  
17 as the domicile State, Ohio has provided benefits to the  
18 corporate headquarters, to management --

19                   JUSTICE GINSBURG: Suppose it had been  
20 Delaware, and there was nothing there in Delaware except  
21 it was a Delaware corporation.

22                   MS. BRINKMANN: That's not the commercial  
23 domicile, Your Honor. There is a distinction in all of  
24 these cases between the State of incorporation and the  
25 commercial domicile. The commercial domicile --



1 CHIEF JUSTICE ROBERTS: Ms. Brinkmann, one  
2 thing that concerns me is how this will complicate the  
3 process. I think, with respect to ordinary income, the  
4 States work this out, and they figure we get 5 percent  
5 because we have 5 percent of the presence or business,  
6 whatever.

7 Now, they're going to have that, and they're  
8 going to have an overlay on that. They're going to say,  
9 well, it's 5 percent; but, you know, we sold this asset  
10 that doesn't have any connection to Illinois; and that's  
11 part of the income we've got. So you don't get quite 5  
12 percent of all.

13 And another -- Illinois is going to come  
14 back and say, well, yes, but you sold this other one;  
15 and, as to that one, you've got sufficient connection  
16 with Illinois. It seems to me it's going to be  
17 impossible to sort this out.

18 MS. BRINKMANN: Your Honor, this has been  
19 going on since at least 1992 in the Allied-Signal case.  
20 The lower courts, the State courts, except for the court  
21 in this case, have been able to apply that easily.

22 In order to take the expansive view of  
23 Illinois here, you would be undermining Allied-Signal,  
24 which had the same facts as in this case, not to mention  
25 ASARCO, Woolworth.

1           And I would just say, before I could reserve  
2 the remainder of my time, Allied-Signal was the case in  
3 which this Court was faced with new arguments raised by  
4 the States, at argument. You went back and had  
5 resupplemental briefing and reargument, and questioned  
6 in your questions to those parties whether or not ASARCO  
7 and Woolworth should be revisited and overruled.

8           So the Allied-Signal case took into account  
9 all of these concerns and came back with a ringing  
10 affirmation of the linchpin of an apportionability for  
11 state taxation being the unitary-business test with the  
12 operational-function aspect.

13           JUSTICE KENNEDY: I don't like to intrude on  
14 the white light, but if I could just ask one question.

15           If the unitary-tax argument has been  
16 preserved and is met and if there's a finding that they  
17 are unitary, does Illinois have the right to tax the  
18 sale, or to -- to a portion of it?

19           MS. BRINKMANN: We think that the finding is  
20 that it is not unitary.

21           JUSTICE KENNEDY: No, no. Assume -- assume  
22 it is unitary. Can Illinois then, in your view, have a  
23 part of -- tax part of the gain on the sale?

24           MS. BRINKMANN: Yes, if it were unitary, but  
25 we think there's no way this record could meet the

1 standards compared to Woolworth, ASARCO. In all those  
2 cases, they were much closer. Thank you.

3 CHIEF JUSTICE ROBERTS: Thank you, Ms.  
4 Brinkmann.

5 Mr. Barov.

6 ORAL ARGUMENT OF BRIAN F. BAROV  
7 ON BEHALF OF THE RESPONDENTS

8 MR. BAROV: Mr. Chief Justice, and may it  
9 please the Court:

10 Illinois is not attempting to tax income  
11 earned outside its borders. To the contrary, the income  
12 it seeks to tax here is income earned by Mead on its  
13 electronic publishing business, Lexis, which conducted  
14 substantial business in Illinois.

15 Mead paid taxes on the income that the  
16 electronic publishing business earned. Yet, it now  
17 contends that the Constitution bars it from taxing any  
18 of the gains it realized on the sale of Lexis, even  
19 though Illinois undeniably contributed --

20 JUSTICE KENNEDY: Well, if you did not  
21 proceed on the unitary business there, let's take that  
22 off the table. It seems to me that Lexis's presence in  
23 Illinois is quite irrelevant.

24 MR. BAROV: No, Your Honor. It's --

25 JUSTICE KENNEDY: It seems to me that, under

1 your theory, you could tax the sale, even if Lexis were  
2 not in Illinois at all, just because Mead is.

3 MR. BAROV: If this - if they were unitary,  
4 yes, then Lexis's presence in Illinois would be  
5 irrelevant to this case, if they met the  
6 unitary-business doctrine.

7 JUSTICE BREYER: That's not the question. I  
8 thought that the -- I agree with the same question  
9 Justice Kennedy had. Suppose that I'm a Massachusetts  
10 company that sells tables, and I sell some tables in  
11 Illinois. And one day I take some of the money, and I  
12 buy an iron mine in New Mexico. And then I sell the  
13 iron mine. And Illinois, not Massachusetts, wants to  
14 impose a tax. And suppose there is no connection  
15 whatsoever between the iron mine and anything else but  
16 for four, which are the four listed on page 13a:

17 One, that I have contributed capital support  
18 to the iron mine.

19 Two, I approve the major capital  
20 expenditures of the iron mine, sitting in my office in  
21 Massachusetts.

22 Three, sometimes -- and this is a tougher  
23 one -- I call the iron mine a division of my table  
24 company.

25 And, four, I sometimes retain tax benefits

1 and control over the extra cash of the iron mine, but  
2 I'm not using it in my day-to-day work.

3 Now, are those four things alone sufficient  
4 for Illinois to tax the sale of my iron mine? That, it  
5 seems to me, is the way they presented it. Maybe it is  
6 a unitary business really, but I guess we have to send  
7 it back for that.

8 MR. BAROV: Under -- under those bare facts,  
9 probably there would be not a sufficient connection.

10 JUSTICE BREYER: All right. Then why isn't  
11 that the end of this case? That's what they said it  
12 was. That's what they said, perhaps wrongly, that this  
13 isn't a unitary business. And, therefore, we are left  
14 with those four facts, and why not send it back and say  
15 you haven't reached the unitary-business question; go  
16 reach it?

17 MR. BAROV: Because, Your Honor --

18 JUSTICE KENNEDY: And if I can just add on  
19 to that same question: If you're going to have the  
20 unitary-tax theory, that's -- that's very helpful. But  
21 if we take the unitary-tax theory off the table, it  
22 seems to me that you are confusing the law by having  
23 some midway test. I don't know what your theory is,  
24 that -- in relation to this part of Justice Breyer's  
25 question.

1 MR. BAROV: There's a two-part answer to  
2 that question -- those questions, Your Honor.

3 First, there's a second avenue of State  
4 taxation that's been well recognized by this Court for  
5 at least 80 years, which is that if a business conducts  
6 business in a State, a State has a tax -- has the right  
7 to tax a share of that business. And that's all  
8 Illinois did here. When it apportioned the income in  
9 this case, it apportioned the income only based on  
10 Lexis's in-State Illinois presence. So under that  
11 avenue alone, the tax is constitutional.

12 The second --

13 JUSTICE KENNEDY: But Mead didn't receive --  
14 pardon me -- Lexis didn't receive the money for the  
15 sale, Mead did.

16 MR. BAROV: Right.

17 JUSTICE KENNEDY: Unless, again, if Mead's  
18 presence or nonpresence is simply irrelevant to what  
19 happened here, absent a unitary theory.

20 MR. BAROV: No, Your Honor. Mead received  
21 the tax -- the gain for the sale because Lexis was a  
22 division of Mead, and the only tax-paying -- the only --  
23 there is no -- there was no legal entity known as  
24 "Lexis" at the time that Lexis was sold. It was assets  
25 -- it was assets owned by the Mead Corporation.

1           Now, Mead received the benefit -- the gain  
2 on the sale because Mead was the only tax-paying entity  
3 in this case. So Mead was conducting a business in  
4 Illinois called "Lexis," and, therefore, Illinois could  
5 tax at least --

6           JUSTICE KENNEDY: Do you think that if there  
7 had been a separate corporation and that Lexis was a  
8 subsidiary corporation and the subsidiary was -- it was  
9 sold, that, again, absent a finding of unitary, Illinois  
10 then could have had a tax?

11           MR. BAROV: Yes. Illinois could have taxed  
12 based on the --

13           JUSTICE KENNEDY: All right. So, then, the  
14 asset stock doesn't make any difference?

15           MR. BAROV: But the -- but the point, Your  
16 Honor, is that Lexis had a presence in Illinois. It was  
17 conducting business in Illinois. That, alone, gave  
18 Illinois the power to tax a share of the income --

19           JUSTICE KENNEDY: That gets back to Justice  
20 Stevens's initial hypothetical. If you live in New York  
21 and you have an investment in a company that does a lot  
22 of business in Illinois and you in New York, a resident  
23 individual, sell that stock, under your theory Illinois  
24 could tax it.

25           MR. BAROV: No. Illinois can't tax that

1 State because there is no relationship -- there has to  
2 be some relationship, you know, between Illinois and the  
3 tax-paying activity and the taxpayer.

4 In Justice Breyer's hypothetical there was  
5 none. But there is a -- but let me, if I can, address  
6 that prong of the analysis, also.

7 Here there was a much closer connection  
8 between Lexis and Mead than simply that of a passive  
9 investment. It wasn't just that Mead helped Lexis buy,  
10 make, handle acquisitions. They were involved in the  
11 actual acquisitions themselves, in purchasing and  
12 contracting to make those acquisitions.

13 Mead was involved in many of the -- in  
14 controlling lots of their capital investment, its -- and  
15 its -- it was also involved in manipulating excess -- in  
16 their excess cash. And there is a whole -- there was a  
17 host of facts that supported a closer relationship  
18 between Mead and Lexis than simply that, that passive  
19 investment.

20 So whether -- even if you are looking at it  
21 from the operational-function point of view, there was  
22 -- there was a -- a sufficient connection between Lexis  
23 and Mead beyond that of Justice Breyer's hypothetical.

24 JUSTICE ALITO: If you traded places with  
25 Ohio, how would you have treated this transaction under



1 your tax laws?

2 MR. BAROV: Under our tax laws --

3 JUSTICE ALITO: Say that Mead was domiciled  
4 in Illinois but Lexis/Nexis operated in Ohio, would you  
5 have just taken -- would you have allocated or would you  
6 have claimed that -- the right to tax the entire capital  
7 gain?

8 MR. BAROV: This would have probably, I  
9 think, Your Honor -- I believe this would have been  
10 apportioned as business income under Illinois law.

11 JUSTICE GINSBURG: Do you know what -- or  
12 did you know what Ohio did in the --

13 MR. BAROV: I don't know what Ohio did.  
14 They -- Mead has never cited anything in the record to  
15 support the contention that it has been -- that it was  
16 allocated all to Ohio. My understanding of Ohio law at  
17 the time was they -- they have the same business-income  
18 test, basically, that Illinois does.

19 JUSTICE GINSBURG: Well, what would you say  
20 -- I mean, we talk about apportioning income and  
21 allocating income, allocating to the commercial  
22 headquarters.

23 What in an enterprise like this would you  
24 say is allocated to the commercial headquarters as  
25 opposed to being apportioned among all the States?

1                   MR. BAROV: Different States have different  
2 rules, Your Honor, and these are State-law rules, not  
3 constitutional rules, about allocation and  
4 apportionment. Some States will allocate an intangible  
5 capital gain like this to their own domicile State.

6                   Other States will apportion it based on the  
7 share of income that is done in the State.

8                   Again, I don't know what Ohio did. But the  
9 point is that's a rule -- that's a State-law rule of  
10 choice, not a rule of -- a constitutional rule. I think  
11 this Court has been pretty clear in the Mobil Oil case  
12 that these -- those -- that doesn't have a  
13 constitutional significance.

14                   That when a State, a domicile State, and a  
15 State where a source -- which is the source of income,  
16 when those conflict, in fact, this Court has signaled  
17 that apportionment is the default rule. And that the  
18 source State actually would have -- the source State  
19 would win that confrontation.

20                   JUSTICE SOUTER: Mr. Barov, I just want to  
21 go back to an earlier answer to see how far you would go  
22 with the position that you took.

23                   Assume that, exclusive of Nexis, Mead is the  
24 same kind of unitary corporation as under -- under  
25 everybody's understanding now. Assume, also, as you

1 suggested in a hypo, that Lexis was doing business in  
2 Illinois. So that at least a -- a portion of its own  
3 activity could be taxed in Illinois. And assume, third,  
4 that the relationship between Mead and Lexis is simply  
5 one of passive investment. Mead simply bought a lot of  
6 stock, maybe 100 percent of the stock at the right time;  
7 and, otherwise, it kept hands off. And at this point  
8 Mead now -- now sells.

9 On -- on your theory, would -- would the  
10 State of Illinois be able to tax a portion of the  
11 capital gain?

12 MR. BAROV: Yes, they would, Your Honor.  
13 But they would be limited in how much of that capital  
14 gain they could apportion. They would apportion it  
15 limited to the amount of income that arose in Illinois.  
16 And that's what the auditor did in this case.

17 JUSTICE SOUTER: Well, but that would be, in  
18 effect, the portion of the Nexis business, total  
19 business that took place in Illinois, total sales, total  
20 payroll, however you do it.

21 MR. BAROV: Right, and then that would be  
22 put -- that would be put into --

23 JUSTICE SOUTER: Okay. But the only point I  
24 wanted to be clear on to understand your position is  
25 that purely passive investment would be enough to

1 trigger your theory?

2 MR. BAROV: Yes, it would be.

3 JUSTICE SOUTER: Okay.

4 MR. BAROV: It is, Your Honor.

5 CHIEF JUSTICE ROBERTS: Counsel, why isn't  
6 your friend correct that you have waived any argument  
7 based on the presence of Lexis in Illinois?

8 MR. BAROV: Your Honor, two reasons:

9 First, under the -- they have cited  
10 basically two basis grounds for waiver, one under  
11 Illinois law and under this Court's rules. But they  
12 misstate Illinois law in the -- on the waiver regard.

13 The cases and rules they cite to stand for a  
14 simple proposition that a point not raised in a brief  
15 before a particular court can't be raised on oral  
16 argument. But what the Illinois Supreme Court has been  
17 clear on "otherwise" is that an argument, even if it's  
18 not raised in the appellate court, as long as it's  
19 raised in the trial court in support of a judgment, may  
20 be raised in a reviewing court on further review.

21 I can provide a couple of cites, Your Honor.

22 JUSTICE GINSBURG: And -- and I'm not  
23 following your argument, because I thought that the  
24 argument that this was a unitary enterprise was made in  
25 the Illinois appellate court, and the appellate court

1 recognizes that it was made, and said we are not going  
2 to reach it because we have this operational-function  
3 test?

4 MR. BAROV: Yes, Your Honor. That's --  
5 that's correct.

6 CHIEF JUSTICE ROBERTS: Well, but that's --  
7 they are very different from your current argument,  
8 which you emphasize that whether they are unitary or  
9 not, Lexis/Nexis was in Illinois.

10 MR. BAROV: That's correct, Your Honor.

11 CHIEF JUSTICE ROBERTS: Okay. Now, as to  
12 that argument, at least I am very reluctant to overturn  
13 a State court on an argument that they didn't have an  
14 opportunity to consider. And whether it's technically  
15 waived because you raised it in the trial court or not,  
16 it certainly was not an argument you made to the  
17 Illinois appellate courts.

18 MR. BAROV: That's correct, Your Honor. And  
19 -- but I think, as this Court set forth in Caterpillar  
20 v. Lewis, it is a predicate to the intelligent  
21 resolution of this case.

22 CHIEF JUSTICE ROBERTS: Well, it wasn't in  
23 Allied-Signal. In Allied-Signal the asset that was sold  
24 was in New Jersey, and that was totally irrelevant to  
25 how we treated the issue in that case.

1                   MR. BAROV: Certainly, Your Honor. But New  
2 Jersey was taking a very different position in that  
3 case. They were making a much broader argument than we  
4 are making here. They were trying to overturn the  
5 entire unitary doctrine.

6                   And so they may have -- they may have chosen  
7 not to make that argument. It may very well have been  
8 in that case that ASARCO's apportionment factors in that  
9 case were so minimal that it wasn't worth their making  
10 that argument.

11                   But, for whatever reason, they weren't  
12 interested in taxing based on the source alone.

13                   But here, as the facts show, Illinois did  
14 tax. We taxed Lexis, or the gain on Lexis, pursuant to  
15 Lexis' in-state apportionment factors.

16                   JUSTICE STEVENS: May I ask this question  
17 just -- it shows my ignorance, but if the  
18 unitary-business approach to taxation was not applied in  
19 this case, how did you compute the amount of the tax?

20                   MR. BAROV: It was computed -- what the  
21 department did in this case is it -- it took the entire  
22 gain that put -- that went into Mead's apportionable tax  
23 base. But, then, in order to find the Illinois-Lexis  
24 share of the gain, he looked at the -- he looked at  
25 Lexis's Illinois sales and Illinois's -- Lexis's

1 Illinois payroll and pulled that amount out, which was  
2 about four percent of the gain, and put that into Mead's  
3 --

4 JUSTICE STEVENS: So you use a different  
5 formula from the normal three-factor formula to compute  
6 the tax?

7 MR. BAROV: Right. You use a different  
8 formula. You use a two-factor formula, but it was just  
9 related to Mead's sales, not to --

10 JUSTICE KENNEDY: But it seems to me that  
11 those factors are wholly irrelevant to the fact of sale.  
12 It's just whimsical. It has nothing to do with the  
13 sale.

14 The reason we use apportionment in other  
15 cases is, just as in Justice Breyer's railroad example,  
16 there is no other way to tell, and so forth.

17 But here the presence of Lexis in Illinois  
18 is wholly accidental with reference to what went on in  
19 the sale.

20 MR. BAROV: No, Your Honor, it wasn't. I  
21 mean Lexis did considerable business in Illinois, and  
22 the auditor was isolating Illinois's business in  
23 attempting to accurately value the amount of gain that  
24 should be attributable to Mead based on Lexis's Illinois  
25 presence.

1 CHIEF JUSTICE ROBERTS: Well, that's why  
2 it's even more dramatic to me that you didn't raise the  
3 argument based on the Lexis connection to Illinois.  
4 That's the basis on which your auditor is claiming these  
5 taxes; and, yet, you don't even raise it before the  
6 Illinois appellate court as a ground for being able to  
7 reach the Lexis/Nexis income.

8 MR. BAROV: -- the trial court -- actually  
9 the appellate court ruled on whether the State law tests  
10 had been met at the time. And when it went up on appeal  
11 we -- we prevailed in the appellate court based on  
12 operational -- I'm sorry, in the trial court, based on  
13 the court's finding the operational function had been  
14 met. That's how the appellant framed the issue, and the  
15 case sort of turned on really Illinois State law's  
16 interpretation of Allied-Signal. But, you know, at this  
17 point the -- the facts and the law are clear and a  
18 decision --

19 JUSTICE STEVENS: In the Illinois courts,  
20 they did argue that as a matter of Federal  
21 constitutional law the tax is impermissible, didn't  
22 they?

23 MR. BAROV: Correct, yes. Yes, they did.  
24 At this point, Your Honor, I mean, to render a decision  
25 that doesn't take into account the facts of the case,



1 the economic reality, accordingly would be artificial.

2 CHIEF JUSTICE ROBERTS: We couldn't do  
3 anything more if we said you haven't waived it, we  
4 couldn't do anything more than send it back. You're  
5 telling us Lexis has this presence in Illinois, but we  
6 have nothing in the record about that.

7 MR. BAROV: Yes, it is in the record. The  
8 auditor's -- I mean, the stipulation itself shows that  
9 Lexis was in Illinois. And the Illinois appellate court  
10 made a finding that the presence of Lexis -- Mead to tax  
11 Nexis with Illinois was undisputed. So the Illinois  
12 appellate court recognized that Lexis had a taxing --  
13 adequate taxing connection with Illinois.

14 CHIEF JUSTICE ROBERTS: Where is that?

15 MR. BAROV: That is -- I don't have the page  
16 cite handy, Your Honor, but the appellate court did make  
17 a finding that it was undisputed that the --

18 CHIEF JUSTICE ROBERTS: I just -- usually  
19 appellate courts don't make findings. That's why I'm  
20 curious --

21 MR. BAROV: I'm sorry. Made a statement.

22 JUSTICE GINSBURG: Was there any sort of  
23 stipulation between the parties to say what each, what  
24 Lexis/Nexis was doing in Illinois, what Mead was doing  
25 in Illinois?

1                   MR. BAROV:  There was, there was a long  
2 stipulation, yes, Your Honor, and plus there was  
3 exhibits attached to the stipulation, which are  
4 reflected in our briefs, that discuss in detail what  
5 Mead and Lexis were both doing, at least their  
6 relationship to each other.

7                   JUSTICE GINSBURG:  Let me ask you about the  
8 theory that both the trial court and the intermediate  
9 appellate court went on, this operational function test,  
10 which has been brought up in a few of our cases, but I  
11 don't know any that was decided.  Did we ever have any  
12 case that turned on the operational function test to  
13 hold for the State taxing authority?

14                   MR. BAROV:  No, Your Honor.  But in  
15 Allied-Signal there was -- examples were given of  
16 certain --

17                   JUSTICE GINSBURG:  Yes.  But one of the  
18 problems with applying it as you urge here is that that  
19 would just override -- why would anyone go to the  
20 trouble of making a case under the so-called unitary  
21 business test, because the operational function test  
22 would be much easier to meet?  So --

23                   MR. BAROV:  I guess on that point I would  
24 disagree with you a bit, Your Honor.  I think there are  
25 very -- they're different types that look at different

1 relationships. So one doesn't -- while the same facts  
2 can support them in instances, you can have situations  
3 where a business is unitary but not operational or --  
4 I'm sorry, an asset is operational, but isn't  
5 necessarily --

6 JUSTICE BREYER: What? What? What could it  
7 be? That is -- as I read this, I thought, well, there  
8 is no separate test. It's just there's a certain  
9 situation that comes up fairly commonly where someone  
10 claims that an asset of a company was really quite  
11 separate, and therefore when they get income from it or  
12 they sell it it has nothing to do with my business. And  
13 the answer is: It did have something to do with your  
14 business, you used the working capital and so forth, in  
15 which case it's part of the business. So how -- how is  
16 it -- how is it different from that?

17 MR. BAROV: I agree, Your Honor.

18 JUSTICE BREYER: Well, if you agree with  
19 that, do you really agree, because if you agree with  
20 that there's no such separate test, this court was wrong  
21 to consider it separately, the lower court, and they  
22 should have reached the question they didn't reach,  
23 which was is this whole thing one single business, which  
24 is normally called the unitary business test?

25 MR. BAROV: Your Honor, on that point I

1 disagree.

2 JUSTICE BREYER: Good. All right.

3 MR. BAROV: I think there is -- I mean,  
4 they're both ways of reaching the overall unitary  
5 principle, whether you can show the intangible flow of  
6 assets -- of value between a company -- I can give you  
7 an example, say, of a company that would be unitary but  
8 where the operational function analysis wouldn't apply  
9 is the Container Corp. Type fact pattern, where you have  
10 a domestic -- a domestic parent providing value out to  
11 the foreign subsidiaries, but there is nothing sort of  
12 flowing back to the domestic parent. They're not really  
13 using those subsidiaries in the domestic business. But  
14 nevertheless, there is enough value being thrown out  
15 that it passed the unitary threshold.

16 The unitary -- the unitary -- I'm sorry.  
17 The operational function analysis or test or principle,  
18 whatever you want to call it, arises in the examples  
19 given in Allied-Signal. As you said, you've got  
20 something which isn't really part of the rest of your  
21 business, but you're using it in that business to  
22 support it way beyond just a passive investment.

23 And this -- in this case, that's how Mead  
24 was using Lexis. They were using it to support their,  
25 the value of their multiple, their multi-state business,

1 by manipulating -- by making capital contributions,  
2 manipulating corporate structures, and bringing back  
3 that tax and net loss carryforwards, which increased the  
4 value, which increased their business activities.

5 So this case actually is that -- is that --  
6 falls within that paradigm also. It's not unlike any --  
7 like either of those hypotheticals in Allied-Signal, not  
8 unlike the use of working -- investment of working  
9 capital.

10 So, yes, both -- the test, while there are  
11 facts that overlap them, they can show that there are  
12 different relationships.

13 JUSTICE GINSBURG: So say you -- but you  
14 would be asking us, if you were going to go on that  
15 operational function, to take two examples that were  
16 given in Allied-Signal that are quite different from  
17 what's involved here, and to make that a doctrine when  
18 you recognize that we have never used that theory to  
19 hold for a State taxing authority in the context of a  
20 multi-state enterprise?

21 MR. BAROV: Your Honor, I don't think you  
22 have to create a separate doctrine again. I think these  
23 are both considered different ways of showing the  
24 intangible flow of value, the significant links between  
25 a business that give rise to constitutional

1 apportionment. And whether they're considered separate  
2 analyses -- they have been described by some academics  
3 as corollaries of each other. It's certainly, given  
4 this Court's signals in Allied-Signal, I think it's  
5 certainly appropriate where the facts arise to make the  
6 constitutional finding based on the operational function  
7 that an asset serves in a business.

8 JUSTICE STEVENS: May I ask this question.  
9 Does the record tell us whether other States have sought  
10 to tax the capital gain on this transaction?

11 MR. BAROV: No, it does not, Your Honor.

12 JUSTICE STEVENS: As far as we know,  
13 Illinois is out on its own here?

14 MR. BAROV: I don't know, Your -- I don't  
15 know the answer to that, Your Honor. I hope not.

16 In any event, Your Honor --

17 JUSTICE SCALIA: You'd not wager, however,  
18 right?

19 MR. BAROV: In any case, Your Honor, as you  
20 said, as I've said, there are two possible ways that --  
21 two different constitutional paths or theories that we  
22 can go down in this case to meet the -- that allows  
23 Illinois to apportion.

24 Independent of the operational links, Mead  
25 can tax the gain on Lexis simply because Lexis conducted

1 business in Illinois. A state may tax a nonresident's  
2 investment income based on its investment in a separate  
3 business, and that's exactly what Illinois -- that's  
4 another way to uphold the Illinois appellate court's  
5 decision.

6 JUSTICE GINSBURG: If Illinois -- if Ohio  
7 is, in fact, taxing the whole gain at its full rate on  
8 the theory that this entire income should be allocated  
9 to Ohio, then you do have an element of double taxation,  
10 right?

11 MR. BAROV: That's possible, Your Honor, but  
12 it's -- first, there is no -- there's no evidence that  
13 Ohio in fact did that. But I think the Mobil Oil case  
14 should have disposed of that, that contention, because  
15 this Court rejected a similar argument that the mere  
16 possibility of taxation by a domiciliary State  
17 foreclosed taxation by a State where the business was  
18 present.

19 And under Mobil Oil, when a resident State's  
20 claim and a source State's claim conflict, this Court  
21 indicated that the resident State's claim must yield to  
22 that of the source State. So there should be no issue  
23 of multiple taxation in this case.

24 Just -- Chief Justice Roberts, just to go  
25 back to your question, it's page 11A of the pet. app.

1 where the appellate court said: "Mead does not dispute  
2 that Lexis/Nexis had the requisite connection or nexus  
3 with Illinois."

4 CHIEF JUSTICE ROBERTS: I thought -- I've  
5 been looking, too. I thought 18A does say that they had  
6 \$46 million of sales attributable to Lexis/Nexis.

7 MR. BAROV: Right. Certainly. There was  
8 hundreds of millions of dollars of sales in Illinois.  
9 So that's really not an issue in this case.

10 CHIEF JUSTICE ROBERTS: No, only 46 million.

11 MR. BAROV: I'm sorry.

12 CHIEF JUSTICE ROBERTS: It said 46, not  
13 hundreds of millions.

14 MR. BAROV: I'm sorry. In 1994, yes, that's  
15 correct.

16 The -- and again there's -- both Mead and  
17 Lexis -- as both Mead and Lexis had adequate  
18 constitutional connection here, there is no basis not to  
19 sustain --

20 JUSTICE SCALIA: You're taxing Mead, not  
21 Nexis/Lexis?

22 MR. BAROV: Correct. That's correct.

23 JUSTICE SCALIA: So what relevance is it  
24 that Nexis/Lexis has business in Illinois?

25 MR. BAROV: It's --



1 JUSTICE SCALIA: I mean that's fine if  
2 that's who you're taxing.

3 MR. BAROV: Well, it's relevant if, only if,  
4 this Court finds that there was no operational  
5 relationship between Lexis and Mead. Then Lexis's  
6 presence in Illinois becomes relevant because in that  
7 case, whether you look at this as a separate business  
8 conducted by Mead or whether it was even a passive  
9 investment of Mead's, Illinois can still tax it in the  
10 manner that it did by -- by isolating the values of  
11 Lexis's -- that Lexis earned in Illinois.

12 JUSTICE KENNEDY: And that is different --

13 JUSTICE SCALIA: I might say that I don't  
14 follow that. It seems to me what you can establish from  
15 the fact that it did a lot of business in Illinois is  
16 that can you tax it and -- but I don't see how.

17 JUSTICE GINSBURG: There was no "it" to tax,  
18 right?

19 MR. BAROV: That 's correct. There was no  
20 "it" to tax and under this court's well-established case  
21 law, International Harvester, J.C. Penney, a State can  
22 tax a nonresident on an investment in that State as well  
23 as the tax is properly prorated to the amount of income  
24 that rose within that State.

25 JUSTICE GINSBURG: At the time of this sale

1 of Lexis/Nexis assets, there was only one taxpayer; it  
2 was Mead.

3 MR. BAROV: That's correct, Your Honor.  
4 There was one taxpayer and it was Mead. That was the  
5 only party that could have been taxed. That's correct.

6 So here, in this case, Mead is taking an  
7 all-or-nothing approach to taxation but this could --  
8 this disregards the connections between Mead's  
9 electronic publishing business in Illinois. And the  
10 Court should decline to rule in their favor. In fact --

11 JUSTICE SCALIA: Do you have any case like  
12 that where your ability to tax a surviving corporation  
13 has to do with, not whether the surviving corporation  
14 itself has sufficient contacts with the State, but  
15 whether some other corporation that has disappeared now  
16 but that merged into it had sufficient -- it seems to me  
17 you have to establish connection with the taxpayer. Not  
18 -- not with somebody from whom the taxpayer made some  
19 money.

20 MR. BAROV: You have to establish a  
21 connection with the taxpayer's activities in the taxing  
22 State. That's the constitutional touchstone. So if  
23 Mead -- whether Mead was running a business in Illinois  
24 or investing in Illinois or had a unitary business that  
25 operated in Illinois, those -- that's the -- that

1 provides a sufficient link.

2 JUSTICE SCALIA: That's fine.

3 MR. BAROV: So that provides the taxing --  
4 the ability --

5 JUSTICE SCALIA: But that isn't established  
6 by the mere fact that Lexis/Nexis did business there.  
7 Ultimately you have to come down to connecting it to  
8 Mead, either by your unitary business doctrine or by  
9 this functional doctrine that you're relying on.

10 MR. BAROV: No, Your Honor. Under  
11 International Harvester, I think that the Court made it  
12 very clear that even a passive investment can be taxed  
13 by a State. If Mead -- Mead can be taxed -- even if  
14 LEXIS was a passive investor and Mead was only investing  
15 in Illinois, Illinois could still tax Mead on the value  
16 of its investment that arose in Illinois. And so Mead  
17 realized the gain. Mead is the taxpayer. Mead can be  
18 taxed as long as the tax is properly prorated to the  
19 Illinois presence, which it was in this case.

20 JUSTICE KENNEDY: But the proration, it  
21 seems to me -- that should have nothing to do with the  
22 extent of Lexis in Illinois --

23 MR. BAROV: Exactly.

24 JUSTICE KENNEDY: -- nor does it have to do  
25 with the extent of Mead in Illinois.

1 MR. BAROV: Well, no, Your Honor. It's --  
2 under this -- then under this Court's precedent, that  
3 you're looking for the source State, the activity of the  
4 business was conducted in the source State. Now, in  
5 this case it happened that the amounts are fairly close  
6 to each other. So if there is any question about it,  
7 there's no -- you know, there is no constitutional  
8 problem that arises out of that. But clearly this -- I  
9 mean it's settled precedent that a State can tax based  
10 on income -- the income that arose in that State and  
11 that's what happened here.

12 Indeed, to accept Mead's contention which  
13 also would create a constitutional loophole that for  
14 income in ae State's marketplace helped create but which  
15 a State cannot recover, the Illinois court's decision  
16 permitting Illinois to tax a fraction of the gain should  
17 be affirmed.

18 And if the Court has no other questions --

19 JUSTICE SCALIA: Can you tax me on stock --  
20 on stock that I own on companies that do business in  
21 Illinois?

22 MR. BAROV: In the abstract, yes, you could,  
23 Your Honor.

24 JUSTICE SCALIA: Do you know any State that  
25 tries to do it.

1 MR. BAROV: No, Your Honor, but again, Your  
2 Honor --

3 JUSTICE SCALIA: That's extraordinary. I  
4 don't know of any tax that a State could possibly  
5 impose, that no State has imposed.

6 (Laughter.)

7 MR. BAROV: Your Honor, this is -- but Your  
8 Honor, International Harvester is the perfectly precise  
9 fact pattern where this Court upheld a tax on a -- on  
10 investors, on the shareholder's investment in a State in  
11 which they were not present, so -- but in this case Mead  
12 had an independent tax presence also in Illinois. So  
13 that issue just doesn't arise in this case.

14 CHIEF JUSTICE ROBERTS: Thank you, Counsel.  
15 Ms. Brinkmann, you have three minutes.

16 REBUTTAL ARGUMENT OF BETH S. BRINKMANN

17 ON BEHALF OF THE PETITIONER

18 MS. BRINKMANN: I have four very quick  
19 points, Your Honor. Two go into this new, very  
20 breathtaking argument that the State is making based on  
21 Lexis/Nexis's presence to the State. Concerning  
22 Illinois law, if you look Repondents' brief in  
23 opposition, on page 12 at note 4, they cite the same  
24 Illinois law we do, trying to argue that we had waived  
25 arguments in the brief in op, so we are on pretty solid

1 ground there. I think it's their cert page, they were  
2 agreeing with us on what the Illinois law meant.

3 On the substance of it, I think Justice  
4 Scalia and Justice Kennedy brought out the weaknesses.  
5 Their position would lead to taxes on all stock sales.  
6 Any State where an investment was doing business could  
7 then reach out and apportion the gain on that. And as  
8 far as International Harvester and J.C. Penney, those  
9 were tax on the investment, not the investor. And the  
10 dissent -- that was the dispute -- the majority. It was  
11 the incident of the tax fell on the invest -- the  
12 investment that was doing business in the State.

13 The State concedes, Your Honor, on Justice  
14 Ginsburg's, the distinction between -- the sale of  
15 assets and the sale of stocks that you were concerned  
16 about. On page 43, they concede and I think it's very  
17 well recognized through Mobil and Exxon and Woolworth  
18 that "apportionment has nothing to do with the form a  
19 business organization takes."

20 CHIEF JUSTICE ROBERTS: Ms. Brinkmann, your  
21 final point.

22 MS. BRINKMANN: Finally I would point out,  
23 on the question you asked -- I think it was Justice  
24 Ginsburg -- what Illinois would do in this.  
25 Interestingly --

1 JUSTICE GINSBURG: Ohio.

2 MS. BRINKMANN: -- the record in this case  
3 at -- it's not in the joint appendix, but it's at C-851.  
4 It's Exhibit 1, to the stipulation of facts. It  
5 indicates that interest and dividends allocable are  
6 allocable to Illinois if the commercial domicile is in  
7 Illinois.

8 JUSTICE SCALIA: Illinois or Ohio, were you  
9 talking about?

10 MS. BRINKMANN: This is the Illinois return,  
11 and the question was what Illinois would do? And they  
12 say commercial domicile, we get your interest and  
13 dividends.

14 CHIEF JUSTICE ROBERTS: Ms. Brinkmann, on  
15 the waiver point -- I'm looking at page 18a -- it not  
16 only says that Lexis/Nexis contributed \$46 million from  
17 its presence in Illinois; it begins the sentence by  
18 saying "as the Department notes, \$46 million of Mead's  
19 income came from Lexis/Nexis activities in Illinois."  
20 So that doesn't sound like a waiver of that point to me.

21 MS. BRINKMANN: At one point, after they got  
22 through the unitary business and operational functional  
23 analysis, there was an argument about whether it was  
24 grossly disproportionate, and that's where some of that  
25 information came. It was never in the context of this

1 legal --

2 CHIEF JUSTICE ROBERTS: Initially, it's  
3 about the context in which -- what I regard as an  
4 important fact -- was raised, whether it was raised in  
5 the context of an argument on unitary business or  
6 whether or not they went too far, but the stubborn fact  
7 is still there.

8 MS. BRINKMANN: There are facts, Your Honor,  
9 but the Illinois law is very clear; it's rule 341(h)(7)  
10 and (i) which applies to applee. If you don't raise a  
11 point in the appellate court, it is waived. That's an  
12 independent and adequate State ground. And it's a very  
13 breathtaking argument, as Justice Scalia pointed out,  
14 that also wasn't brought forth in the brief in  
15 opposition. Thank you, Your Honor.

16 CHIEF JUSTICE ROBERTS: Thank you. The case  
17 is submitted.

18 (Whereupon, at 12:18 p.m., the case in the  
19 above-entitled matter was submitted.)

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