Nos. 12-56067, 12-56068, 12-56077 (consolidated)

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

SAM FRANCIS FOUNDATION, ET AL.,
Plaintiffs-Appellants,
v.
CHRISTIE'S, INC.
Defendant-Appellee.

SAM FRANCIS FOUNDATION, ET AL.,
Plaintiffs-Appellants,
v.
EBAY, INC.,
Defendant-Appellee.

ESTATE OF ROBERT GRAHAM, ET AL.,
Plaintiffs-Appellants,
v.
SOTHEBY'S, INC.,
Defendant-Appellee.

Appeal from the United States District Court for the Central District of California, No. 2:11-cv-08605-MWF-FFM, No. 2:11-cv-08622-MWF-PLA, No. 2:11-cv-8604-MWF-FFM, The Honorable Jacqueline H. Nguyen

---

BRIEF FOR THE STATE OF CALIFORNIA AS *AMICUS CURIAE* SUPPORTING APPELLANTS AND REVERSAL

KAMALA D. HARRIS
Attorney General of California
EDWARD C. DUMONT
Solicitor General
MARK J. BRECKLER
Chief Assistant Attorney General
ROBERT W. BYRNE
Senior Assistant Attorney General

AIMEE FEINBERG (SBN 223309)
Deputy Solicitor General
GAVIN G. MCCABE
Supervising Deputy Attorney General
455 Golden Gate Avenue, Suite 11000
San Francisco, CA 94102
Telephone: (415) 703-2545
E-mail: Aimee.Feinberg@doj.ca.gov

TABLE OF CONTENTS

Page

TABLE OF CONTENTS
(continued)

Page

TABLE OF AUTHORITIES

Page

CASES

TABLE OF AUTHORITIES
(continued)

Page

TABLE OF AUTHORITIES
(continued)

Page

TABLE OF AUTHORITIES
(continued)

Page

INTEREST AND AUTHORITY

These consolidated cases involve whether application of the California Resale Royalties Act (CRRA) under circumstances alleged in plaintiffs' complaints would amount to impermissible extraterritorial regulation by the State in violation of the dormant Commerce Clause. The Court has ordered that this matter be reheard to consider the application of the extraterritoriality principle in this case in light of statements in two prior cases, also involving California laws: *Rocky Mountain Farmers Union v. Corey*, 730 F.3d 1070 (9th Cir. 2013), and *Association des Éleveurs de Canards et D'Oies du Québec v. Harris*, 729 F.3d 937 (9th Cir. 2013). *See* Dkt. 85 (directing briefing on whether statements in these cases indicated "a conflict in our case law regarding the applicability of *Healy v. Beer Inst.*, 491 U.S. 324 (1989)"). California has a direct and substantial interest in these issues, and in particular in any articulation by the *en banc* Court of principles for use in addressing allegations that a state statute "directly controls commerce occurring wholly outside the boundaries of [the] State." *Healy*, 491 U.S. at 336. The Attorney General submits this brief on behalf of the State pursuant to Rule 29(a) of the Federal Rules of Appellate Procedure and Ninth Circuit Rule 29-2(a).

SUMMARY OF ARGUMENT

The Supreme Court has held that a state law is impermissibly "extraterritorial" only if it directly controls wholly out-of-state commerce. Applying this principle, the Court has only rarely found a state law invalid. Although the Court has struck down laws that tie in-state prices to those charged outside the State, it has rejected arguments that the dormant Commerce Clause disables States from regulating in-state commerce, even if the regulation might have effects outside the State.

This Court's decisions in *Rocky Mountain* and *Éleveurs* correctly applied the Supreme Court's articulation of the extraterritoriality doctrine. In *Rocky Mountain*, the Court properly held that California's Low Carbon Fuel Standard directly regulated only the State's own market. Likewise, in *Éleveurs*, the Court recognized that a state law regulating in-state sales of foie gras did not control commerce in other States. The fact that California's regulations might motivate out-of-state businesses to change certain practices in order to compete in California's markets did not violate the Commerce Clause. These holdings are consistent with a line of cases from this and other courts of appeals that have upheld state laws regulating in-state commerce.

In their as-applied challenge to the CRRA, defendants do not advance claims like those considered in *Rocky Mountain* and *Éleveurs*. The challenges in those

cases asserted that California's regulation of its own market had impermissible extraterritorial effects. In contrast, defendants here argue that the CRRA, by its own terms, directly regulates sales of art that occur wholly out of state. This contention is incorrect, because the CRRA does not prescribe the terms or conditions of any sale. It does not, for example, prescribe prices for art owned by California residents or restrict where art sales can take place. Rather, the statute imposes financial obligations on California residents once a sale is complete. A State does not violate the dormant Commerce Clause by imposing such obligations on its own residents.

Even if the CRRA is viewed as regulating art sale transactions involving California sellers, as defendants contend, the district court still erred in striking it down and dismissing plaintiffs' complaints. Courts have recognized that the dormant Commerce Clause is not offended when a State's law is applied to a transaction that occurs in part within the regulating State. At this early stage of the litigation, no facts have been developed that would show that any transactions at issue in plaintiffs' complaints do not take place at least partly in California. Accordingly, even under defendants' theory, it was error to dismiss the case at the pleadings stage.

Because defendants' as-applied challenge to the CRRA fails, the Court need not reach the issue of severability. If the Court concludes otherwise, the additional

authorities presented below confirm that any unconstitutional applications of the law should be severed and the remaining applications left intact.

ARGUMENT

I. A STATE LAW IS "EXTRATERRITORIAL" ONLY IF IT DIRECTLY REGULATES WHOLLY OUT-OF-STATE COMMERCE

A. The Supreme Court Has Rarely Invalidated State Laws As "Extraterritorial"

The Commerce Clause grants Congress the authority "[t]o regulate Commerce . . . among the several States." U.S. Const. art. I, § 8, cl. 3. Although the Clause speaks only of Congress, the Supreme Court has read it to embody implicit limitations on state regulation. *E.g.*, *McBurney v. Young*, 133 S. Ct. 1709, 1719 (2013). This negative or "dormant" aspect of the Clause is "driven by a concern about economic protectionism—that is, regulatory measures designed to benefit in-state economic interests by burdening out-of-state competitors." *Id.* (internal quotation marks omitted). Its application is not intended "to cut the States off from legislating on all subjects relating to the health, life, and safety of their citizens, though the legislation might indirectly affect the commerce of the country." *Huron Portland Cement Co. v. City of Detroit*, 362 U.S. 440, 443-444 (1960).

The Supreme Court has generally analyzed dormant Commerce Clause challenges using a "two-tiered approach." *Brown-Forman Distillers Corp. v. N.Y. State Liquor Auth.*, 476 U.S. 573, 578 (1986). A state statute that either

discriminates against or "directly regulates" interstate commerce will normally be struck down. *Id.* at 579. If, however, a statute "regulates evenhandedly" and "has only indirect effects on interstate commerce," it will be sustained so long as the state interest underlying the law is legitimate and the local benefits of the law are not "clearly exceed[ed]" by any burden on interstate commerce. *Id.* (citing *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970)).

The defendants in these cases have brought an as-applied challenge to the CRRA, alleging that the statute cannot constitutionally require remittance of royalties with respect to sales made on behalf of California sellers but in auctions held outside of California. Defendants argue that any such requirement would "directly regulate[]" an out-of-state sale, and thus be impermissibly "extraterritorial." In that regard, the Supreme Court has explained that "the 'Commerce Clause . . . precludes the application of a state statute to commerce that takes place wholly outside of the State's borders.'" *Healy*, 491 U.S. at 336. A state statute may not "directly control[] commerce occurring wholly outside the boundaries of a State," either by its terms or in "practical effect." *Id.*

The Supreme Court has rarely invalidated a statute as extraterritorial. In *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 519 (1935), the Court struck down a New York milk-pricing statute that prohibited in-state dealers from selling milk purchased in other States for a price lower than that set by New York. While that

statute was unconstitutional in light of its protectionist intent, *id.* at 527, the Court's opinion also observed that "New York ha[d] no power to project its legislation into Vermont by regulating the price to be paid in that state for milk acquired there," *id*. at 521. Fifty years later, the Court in *Brown-Forman* invalidated a New York price-affirmation statute that had the effect of requiring distillers to seek approval from New York regulators before selling liquor outside New York at a price lower than the price they had posted for use in that State. *See* 476 U.S. at 575-576, 582. And in *Healy*, the Court struck down a similar Connecticut price-affirmation law on the ground that, among other things, it had "the practical effect of controlling Massachusetts prices." 491 U.S. at 338.

In contrast, the Court has rejected Commerce Clause challenges to state statutes that did not involve tying in-state and out-of-state prices, even when they were characterized as seeking to regulate out-of-state commerce. In *CTS Corp. v. Dynamics Corp. of America*, 481 U.S. 69 (1987), for example, the Court upheld an Indiana anti-takeover law that prevented either in-state or out-of-state entities from acquiring control of Indiana corporations without approval from a majority of disinterested shareholders. *Id.* at 73-74, 94. Noting that the law "applie[d] only to corporations incorporated in Indiana," the Court rejected Commerce Clause challenges, including challenges concerning the law's application to tender offers made by out-of-state offerors and involving out-of-state shareholders. *Id.* at 93.

Similarly, in *Edgar v. MITE Corp.*, 457 U.S. 624 (1982), the Court did not apply extraterritoriality principles in invalidating an Illinois law that allowed a state official to block any tender offer for a corporation that bore one of several relationships to the State. *Id.* at 626-627. By its terms, the statute could prohibit a potential buyer "from making its offer and concluding interstate transactions not only with [target] stockholders living in Illinois, but also with those living in other States and having no connection with Illinois." *Id*. at 642 (plurality opinion). Four Justices analyzed the law as one "purport[ing] to regulate directly and to interdict interstate commerce, including commerce wholly outside the State." *Id*. at 643 (plurality opinion). The Court majority, however, held the statute unconstitutional only because it burdened out-of-state commerce without sufficient offsetting local benefits. *Id*. at 643-646 (applying balancing test under *Pike v. Bruce Church*); *cf. CTS*, 481 U.S. at 81 (noting that *Edgar* plurality's reasoning on different point "did not represent the views of a majority of the Court" (footnote omitted)).

Most recently, in *Pharmaceutical Research & Manufacturers of America v. Walsh*, 538 U.S. 644, 669 (2003), the Court rejected an extraterritoriality challenge to a Maine program designed to reduce drug prices for certain state residents. The Maine law required pharmaceutical companies selling drugs in Maine through a public program to agree with the State to rebate part of the normal retail price. *Id*. at 654. The State would use the rebated funds to subsidize discounted sales to

qualified residents. *Id*. Manufacturers that failed to enter into rebate agreements would, under some circumstances, have sales of their drugs through the Medicaid program subjected to pre-authorization requirements. *Id*. at 654-655. The manufacturers argued that the Maine program was unconstitutional under *Baldwin* and *Healy*, because they were not based in Maine and largely sold their products to distributors and wholesalers outside the State. *See id.* at 656, 669. They characterized the Maine program as "regulation of the terms of transactions that occur elsewhere." *Id*. at 669.

The Court rejected the analogy to its earlier cases:

> [U]nlike price control or price affirmation statutes, the Maine Act does not regulate the price of any out-of-state transaction, either by its express terms or by its inevitable effect. Maine does not insist that manufacturers sell their drugs to a wholesaler for a certain price. Similarly, Maine is not tying the price of its in-state products to out-of-state prices. The rule that was applied in *Baldwin* and *Healy* accordingly is not applicable to this case.

Id. (internal quotation marks and citation omitted). Thus, while the prospect of being required to pay rebates might have influenced the terms on which manufacturers sold their products to out-of-state distributors, or reduced the ultimate net benefit of those sales, the Maine law did not impermissibly dictate the terms of such transactions, directly or by "inevitable effect." *See id.*[1]

[1] As this Court suggested in *Éleveurs*, the Supreme Court's decision in *Walsh* could be read as limiting *Healy* and *Baldwin* to statutes regulating prices. 729 F.3d at 950-951. Comparative price-control statutes like those at issue in *Healy*, *Baldwin*, (continued…)

These cases demonstrate that only laws that apply to, or directly control, commerce occurring wholly outside the State will be considered invalid extraterritorial regulation.

B. This Court and Others Have Correctly Recognized That a State's Regulation of In-State Commerce Does Not Become Extraterritorial Merely Because It May Affect Business Decisions Made Out of State

This and other courts of appeals have regularly and correctly followed the Supreme Court's guidance in sustaining States' authority to regulate in-state activities and markets—even if the regulation leads out-of-state actors to alter their conduct in response. Thus, for example, in *Rocky Mountain*, this Court correctly rejected an extraterritoriality challenge to California's Low Carbon Fuel Standard,

---

(…continued)
and *Brown-Forman* arguably impose unique burdens on interstate commerce. There is, however, no need to resolve that question in this case. The Court can reaffirm the result in *Éleveurs* and resolve plaintiffs' appeal without deciding whether *Healy* is confined to the context of price regulations. *See* Section I.B (discussing *Éleveurs*); Section II (discussing Resale Royalties Act).

Notably, two members of the *Walsh* Court would have rejected the Commerce Clause challenge for even broader reasons. Concurring in the judgment, Justice Scalia reasoned that "the negative Commerce Clause, having no foundation in the text of the Constitution and not lending itself to judicial application except in the invalidation of facially discriminatory action, should not be extended beyond such action and nondiscriminatory action of the precise sort hitherto invalidated." 538 U.S. at 674-675. Similarly, Justice Thomas concurred in the judgment on the ground that "the negative Commerce Clause has no basis in the text of the Constitution, makes little sense, and has proved virtually unworkable in application." *Id.* at 683 (internal quotation marks and alterations omitted).

which limits the average carbon-intensity of fuel sold for use within the State. 730 F.3d at 1101-1106. The Court recognized that California's standard might lead some fuel producers, including some out-of-state fuel producers, to make different business decisions in order to obtain price premiums or increase their competitiveness in California's market. *See id*. at 1101. Those indirect effects were permissible, however, because California's standard—unlike the law in *Healy*—controlled only its own market. *See id.* at 1102-1103.

The Court rejected a similar extraterritoriality challenge in *Éleveurs*, involving California's prohibition on the in-state sale of products made by force-feeding birds. 729 F.3d at 949-951. In affirming the denial of a preliminary injunction to block enforcement of the law, the Court recognized that the statute did not have the kind of practical effects held unlawful in *Healy*. *Id.* Among other things, the statute did not set prices for products, tie in-state prices to those charged elsewhere, require out-of-state producers to change their production methods for products sold in other States, or subject producers to conflicting regulation. *Id.*

These two decisions are consistent with many others in which this Court has rejected challenges to laws regulating in-state conduct that were claimed to have impermissible effects on commerce in other States. For example, in *Pharmaceutical Research & Manufacturers of America v. County of Alameda*, 768 F.3d 1037 (9th Cir. 2014), the Court turned back an extraterritoriality challenge to

a county ordinance that required drug manufacturers that sold prescription drugs in the county, including those manufacturers based outside the county, to provide for the in-county collection and disposal of unused drugs. *Id.* at 1043-1044. Relying on *Éleveurs*, the Court explained that "there is nothing unusual or unconstitutional per se about a state or county regulating the in-state conduct of an out-of-state entity when the out-of-state entity chooses to engage the state or county through interstate commerce." *Id.*

Similarly, in *Greater Los Angeles Agency on Deafness, Inc. v. Cable News Network, Inc.*, 742 F.3d 414 (9th Cir. 2014), the Court held that California's Disabled Persons Act could properly be applied to require CNN to provide closed-captioning when videos on its website are accessed by California viewers. *Id.* at 432-433 (rejecting CNN's argument that plaintiffs' claim had no probability of prevailing). Such a requirement did not have the "practical effect" of controlling wholly out-of-state conduct because, "[e]ven though CNN.com is a single website, . . . CNN could enable a captioning option for California visitors to its site, leave the remainder unchanged, and thereby avoid the potential for extraterritorial application" of the law. *Id.* at 433. Moreover, even if the company changed "'its entire website in order to comply with the California law, this [would] not mean that California [was] regulating out-of-state conduct.'" *Id.* (quoting *Nat'l Fed'n of the Blind v. Target Corp.*, 452 F. Supp. 2d 946, 961 (N.D. Cal. 2006)); *see also*

Valley Bank of Nev. v. Plus Sys., Inc., 914 F.2d 1186, 1191 (9th Cir. 1990) (rejecting claim that Nevada statute regulated extraterritorially by requiring non-Nevada banks to impose, collect, and pay fees charged by Nevada ATMs when the banks' customers withdrew money from Nevada ATMs); *Pac. Merchant Shipping Ass'n v. Goldstene*, 639 F.3d 1154, 1179 (9th Cir. 2011) (rejecting extraterritoriality challenge to California regulations requiring ocean-going vessels calling at a California port to use cleaner-burning fuels while within certain distance of California coast).

The only decision in which this Court has found a state statute to have impermissible extraterritorial effects under *Healy* involved the unique context of Nevada's attempt to regulate a national sports league. In *NCAA v. Miller*, 10 F.3d 633 (9th Cir. 1993), the Court struck down a Nevada law requiring the NCAA (but no in-state entity) to provide enhanced procedural protections to Nevada schools or students accused of a rules infraction. *Id.* at 637-638. The Court held that this mandate would, as a practical matter, impermissibly require the NCAA to apply Nevada's rules in proceedings involving no Nevada party, because of the NCAA's unique need for national uniformity in disciplinary proceedings. *Id.* at 638-639; *cf. Valley Bank*, 914 F.2d at 1192 (pre-*NCAA* case distinguishing Commerce Clause challenges to rules of professional sports leagues, on the ground that "[d]ecisions in sports cases . . . deal with the unique entity of the national professional sports

league and have not been applied in other factual settings"). Under those unusual circumstances, Nevada's law operated in effect as a direct control on the NCAA's wholly out-of-state activities and thus exceeded the scope of the State's jurisdiction. *See NCAA*, 10 F.3d at 639.[2]

This Court's decisions in cases involving the regulation of in-state commerce are consistent with those of other circuits. In *National Electrical Manufacturers Association v. Sorrell*, 272 F.3d 104 (2d Cir. 2001), for example, the Second Circuit upheld Vermont's labeling law for light bulbs sold in the State, explaining that the law did not "inescapably require manufacturers to label all lamps wherever distributed." *Id.* at 110. "To the extent the statute may be said to 'require' labels on lamps sold outside Vermont, then, it is only because the manufacturers are unwilling to modify their production and distribution systems to differentiate between Vermont-bound and non-Vermont-bound lamps." *Id.* Similarly, in *Cotto Waxo Co. v. Williams*, 46 F.3d 790, 794 (8th Cir. 1995), the Eighth Circuit upheld Minnesota's prohibition against the sale of petroleum-based

[2] In *Union Pacific Railroad Co. v. California Public Utilities Commission*, 346 F.3d 851 (9th Cir. 2003), this Court held that a state regulation of train configurations had extraterritorial effect because it would require trains traveling through other States to be configured according to the State's standards, and such state regulations could lead to a patchwork of inconsistent standards governing interstate train trips. *Id.* at 871-872. The Court, however, invalidated the regulation under *Pike*'s balancing test; it did not treat it under *Healy* as a prohibited regulation of wholly out-of-state conduct. *See id.* at 870, 872.

sweeping compounds. Although Minnesota's regulation of its own market "affected Cotto Waxo's participation in interstate commerce," it was not impermissibly extraterritorial because, unlike the laws at issue in *Brown-Forman* and *Baldwin*, Minnesota's regulation was "itself . . . indifferent to sales occurring out-of-state." *Id.* [3] These decisions by this and other courts are consistent with the Supreme Court's recognition that States' regulation of in-state activities may have effects out of state and that such effects rarely rise to the impermissible level of controlling wholly out-of-state commerce.

II. THE DISTRICT COURT'S JUDGMENT THAT THE CALIFORNIA RESALE ROYALTIES ACT OPERATES EXTRATERRITORIALLY SHOULD BE REVERSED

Applying the extraterritoriality principle in this case, the district court's judgment should be reversed. In urging the contrary result, defendants disclaim arguments like those considered in *Rocky Mountain* and *Éleveurs*, which involved allegations that California's regulation of its own market had impermissible

[3] *See, e.g*, *Int'l Dairy Foods Ass'n v. Boggs*, 622 F.3d 628, 647 (6th Cir. 2010) (rejecting extraterritorial challenge to Ohio law regulating the content of labels on dairy products because "unlike the price-affirmation statutes [in *Healy* and *Brown-Forman*], which directly tied their pricing requirements to the prices charged by the distillers in other states, [Ohio's] labeling requirements have no direct effect on [milk processors'] out-of-state labeling conduct"); *Alliance of Auto Mfrs. v. Gwadosky*, 430 F.3d 30, 41 (1st Cir. 2005) (rejecting extraterritoriality argument that Maine's regulation of its auto markets "transform[ed] Maine prices into national minimum prices"); *Hampton Feedlot, Inc. v. Nixon*, 249 F.3d 814, 819 (8th Cir. 2001) (rejecting extraterritoriality challenge to Missouri law that "only regulates the sale of livestock sold in Missouri").

extraterritorial effects on commerce occurring in other States. Christie's Supp. Br. (Dkt. 93) 1, 9-10; Sotheby's Supp. Br. (Dkt. 94) 1, 6-10. Instead, defendants here assert that the CRRA, by its terms, directly regulates sales that take place wholly outside of California. In particular, defendants find fault with two provisions of the CRRA as applied to the facts alleged in the complaints: (1) California Civil Code section 986(a)'s imposition of a royalty obligation on California art sellers (the California-resident provision) and (2) section 986(a)(1)'s related obligation that sellers' agents withhold and transmit owed royalties on behalf of their principals. For the reasons explained below, defendants' arguments either fail or cannot be resolved on the present record.

A. The California-Resident Provision Does Not Regulate Extraterritorially

The district court erred in holding, on defendants' motion to dismiss, that the California-resident provision operates extraterritorially. Contrary to defendants' view, the CRRA does not regulate art sales transactions, because it does not prescribe or limit terms or conditions for such transactions. Rather, it imposes post-sale financial obligations on California sellers and their agents. Under the dormant Commerce Clause, States may impose financial obligations, such as the obligation to pay CRRA royalties, on their own residents. But even if the CRRA is viewed as regulating art sales transactions, no facts have been developed at this

early stage of the litigation that would show that the transactions at issue occur wholly out of State.

1. The California-Resident Provision Permissibly Imposes Post-Sale Financial Obligations on In-State Residents, Rather Than Prescribing Terms or Conditions for Sales of Art

The CRRA provides that "[w]henever a work of fine art is sold and the seller resides in California . . . , the seller or the seller's agent shall pay to the artist of such work of fine art or to such artist's agent 5 percent of the amount of such sale." Cal. Civ. Code § 986(a). This language says nothing about the terms or conditions on which a sale of art must be conducted. It requires only a payment by the seller, for the benefit of the artist, after the sales transaction is completed.

This Court's decision in *Morseburg v. Balyon*, 621 F.2d 972 (9th Cir. 1980), confirms the point. There, the Court concluded that the CRRA, rather than impairing the right to transfer a work of art, "creates a right in personam against a seller of a 'work of fine art.'" *Id.* at 977. Although royalty laws may affect art owners' decisions whether to sell their works, the Court explained, such laws "[t]echnically speaking[,] . . . in no way restrict the transfer of art works." *Id.* at 977; *see also id.* at 978; *id*. at 979 (characterizing CRRA as creating "an unbargained-for obligation to pay a royalty to the creator of that work or the Arts Council upon resale").

States may impose obligations like the CRRA's royalty payment on their own residents. When a state obligation applies only to the State's own residents, there is little reason for concern about the State overstepping Commerce Clause boundaries. *See Healy*, 491 U.S. at 336 (noting Commerce Clause concern "with the autonomy of individual States within their respective spheres"). Thus, for example, in *CTS Corp.*, the Supreme Court found no dormant Commerce Clause concern with an Indiana anti-takeover law that applied only to Indiana corporations with a significant number of Indiana shareholders. 481 U.S. at 93. Unlike the anti-takeover law struck down in *Edgar*, "every application of the Indiana Act [would] affect a substantial number of Indiana residents." *Id.*; *cf. McBurney*, 133 S. Ct. at 1720 (dormant Commerce Clause not implicated by State-created program that provides benefit to state residents). In addition, outside of the Commerce Clause context, the Supreme Court has held that a State may apply its laws to its own residents, even when those residents are outside the State's boundaries. *See Skiriotes v. Florida*, 313 U.S. 69, 76-77 (1941) (upholding conviction of Florida resident under Florida statute prohibiting certain conduct beyond State's territorial waters).

Although the CRRA is not a tax, for purposes of analyzing state authority under the dormant Commerce Clause it is broadly similar in that it imposes on a California resident an obligation to remit a payment, and that obligation arises after

a sale at a price in excess of the amount the resident paid for the item sold. *See* Cal. Civ. Code § 986(a), (b)(4). In the tax context, it is a "well-established principle" that a State may "tax *all* the income of its residents, even income earned outside the taxing jurisdiction"—including, for example, capital gains on sales made outside the State. *See Oklahoma Tax Comm'n v. Chickasaw Nation*, 515 U.S. 450, 462-463 (1995) (emphasis in original) (footnote omitted). It is not clear why a State that may tax a resident's income from such a sale would lack the constitutional authority to require the same resident to pay the royalty provided by the CRRA.

In sum, the California-resident provision does not regulate the sales of art. Its imposition of a post-sale financial obligation on in-state residents raises no dormant Commerce Clause concern.

2. Even if the California-Resident Provision Is Viewed as Regulating Art Sales Transactions, It Was Error To Dismiss Plaintiffs' Complaints

Even if the CRRA's California-resident provision were viewed as regulating sales of art, the district court's judgment still should be reversed. At this early stage of the litigation, no facts have been developed that would permit the conclusion that applying the CRRA to the facts alleged in plaintiffs' complaints would amount to impermissible extraterritorial regulation.

When considering whether a State's law may be applied to resolve a dispute over a particular transaction, courts have recognized that the dormant Commerce Clause is not offended by applying the State's law when the transaction occurs in part within the regulating State. This is so because a State exceeds its authority under the Commerce Clause only if a law "directly controls commerce occurring *wholly outside* [its] boundaries." *Healy*, 491 U.S. at 336 (emphasis added). Thus, for example, in *Gravquick A/S v. Trimble Navigation International, Ltd.*, 323 F.3d 1219 (9th Cir. 2003), this Court held that the California Equipment Dealers Act could be applied to a contract between a California equipment manufacturer and an overseas buyer. *Id.* at 1224. Although the Court's analysis rested in part on the fact that the parties chose California law to govern their contract, its dormant Commerce Clause analysis emphasized that the contract involved a California party and was performed in part in California. *See id.* (law did not "directly regulate the actions of parties located in other states," but "regulate[d] contractual relationships in which at least one party is located in California"). As the Court explained, "[a]pplying California law to a contract that is performed only partially outside of California does not violate the Commerce Clause." *Id.*; *cf. Watson v. Employers Liab. Assurance Corp.*, 348 U.S. 66, 73 (1954) (when "a contract affects the people of several states, each may have interests that leave it free to enforce its own contract policies") (discussing Full Faith and Credit Clause).

Other courts have agreed that the extraterritoriality principle does not divest States of jurisdiction over transactions that occur partly in the regulating State. *See, e.g.*, *A.S. Goldmen & Co., Inc. v. N.J. Bureau of Sec.*, 163 F.3d 780, 787 (3d Cir. 1999) (upholding application of New Jersey law forbidding in-state broker from selling certain securities to out-of-state buyers, even though the sales would have been lawful in the buyers' home states); *Quik Payday, Inc. v. Stork*, 549 F.3d 1302, 1308-1309 (10th Cir. 2008) (Kansas law regulating interstate loan transactions with Kansas residents did not operate extraterritorially); *Kearney v. Salomon Smith Barney*, 39 Cal. 4th 95, 106-107 (2006) (application of California law to phone calls originating out of state but directed to Californians while in California did not violate dormant Commerce Clause under *Healy* because, *inter alia*, the calls "quite clearly did not take place wholly outside California's borders" (internal quotation marks and alterations omitted)). Moreover, contrary to Christie's and Sotheby's view (Auction Houses Br. (Dkt. 44-3) 16-17), a State's law may be applied in a dispute over a transaction even if aspects of the transaction other than the offer and acceptance occur within the State. *See Quik Payday*, 549 F.3d at 1308 (observing that Kansas could properly apply its consumer-lending regulations to an out-of-state payday lender, even if the Kansas borrower was not in the State when undertaking the loan transaction, because "other aspects of the transaction are very likely to be in Kansas—notably, the transfer of funds to the

borrower would naturally be to a bank in Kansas"); *see also S.D. Meyers, Inc. v. City & Cnty. of San Francisco*, 253 F.3d 461, 469 (9th Cir. 2001) (upholding city ordinance's requirement that companies contracting with the city provide domestic partnership benefits to workers with "direct contact with the City," even if both they and their employer are not physically within city limits).

Here, because no facts have been developed regarding the details of the transactions alleged in the complaints, it cannot be determined at this stage of the litigation whether any of the transactions at issue is properly characterized as occurring "wholly outside" the boundaries of California for purposes of the dormant Commerce Clause. *See Healy*, 491 U.S. at 336. Resolution of defendants' as-applied challenges requires a remand for the parties to develop facts relevant to the extraterritoriality inquiry.[4]

Defendants have likewise not shown that applying the CRRA to the facts alleged in this case would subject art sellers to inconsistent regulation. Because,

[4] Decisions from other circuits do not lead to a contrary result. *See* Auction Houses' Br. 17, 19-20. *Midwest Title Loans, Inc. v. Mills*, 593 F.3d 660 (7th Cir. 2010), *Dean Foods Co. v. Brancel*, 187 F.3d 609 (7th Cir. 1999), and *Carolina Trucks & Equipment, Inc. v. Volvo Trucks of North America, Inc.*, 492 F.3d 484 (4th Cir. 2007), were decided, not on the pleadings, but on a developed factual record. *See Midwest Title Loans, Inc. v. Ripley*, 616 F. Supp. 2d 897, 900-901 (S.D. Ind. 2009) (setting forth stipulated facts developed on summary-judgment record); *Dean Foods*, 187 F.3d at 610 (noting district court's "extensive fact-finding"); *id.* at 618 (describing testimony about the transactions); *Carolina Trucks*, 492 F.3d at 487 (appeal followed a jury trial).

according to the auction houses (Br. 6), no other State has enacted a similar royalty law, there are no other regulatory mandates with which the CRRA could conflict. *See Sorrell*, 272 F.3d at 112 (no regulatory conflict where "no other state even regulates" the subject of Vermont's law, "much less does so in conflict with Vermont's approach"); *S.D. Meyers*, 253 F.3d at 470 ("the [Supreme Court] has never invalidated a state or local law under the dormant Commerce Clause based upon mere speculation about the possibility of conflicting legislation"). Moreover, even if more than one State with a sufficient relationship to the parties or transaction imposed royalty obligations on a single art sale, there is no reason to believe that it would be impossible to comply with both States' laws. *See Boggs*, 622 F.3d at 647 (rejecting extraterritoriality challenge on ground that, *inter alia*, compliance with the state regulation did not "raise the possibility that [affected entities] would be in violation of the regulations of another state," which was "the key problem with the New York statute in *Brown-Forman*").

B. Defendants Have Not Demonstrated that Section 986(a)(1)'s Collection Obligations Operate Extraterritorially

There is likewise no basis to dismiss plaintiffs' complaints based on objections to the CRRA's separate requirement that sellers' agents withhold and transmit owed royalties. *See* Cal. Civ. Code § 986(a)(1). This provision does not purport to regulate out-of-state art sales. Rather, by assigning to sellers' agents the administrative obligation to withhold and pay royalties on behalf of sellers, the

CRRA effectively adds a contractual term to the California seller-agent agreement: in addition to selling the work of art on the seller's behalf, the agent shall also set aside and transmit owed royalties. For the reasons explained above, a State's authority to apply its laws to a contract of this kind depends on facts concerning the contract itself that have not been developed at this early stage of the litigation. *See supra* at 19-21.

For all of these reasons, the district court erred in holding that the application of the CRRA to the circumstances alleged in plaintiffs' complaints would violate the dormant Commerce Clause.

III. IF THE COURT REACHES THE ISSUE OF SEVERABILITY, IT SHOULD DISALLOW ONLY ANY UNLAWFUL APPLICATIONS OF THE STATUTE

Defendants' as-applied challenge to the CRRA fails, and there is therefore no need for the Court to reach the issue of severability. In light of the Court's questions regarding severability at the panel argument, however, the State presents below authorities and argument, not advanced by the parties, that further demonstrate why, if the Court concludes that any applications of the CRRA are unconstitutional, only those applications should be disallowed.

First, under California law, when a party challenges an application of a law as unconstitutional, "the statute should be upheld if, after deletion of the invalid application, a workable statute remains." *Walnut Creek Manor v. Fair Employment & Hous. Comm'n*, 54 Cal. 3d 245, 266 (1991) (internal quotation

marks and alterations omitted); *see also People v. Kelly*, 47 Cal. 4th 1008, 1048 (2010) (the "appropriate remedy" when an application of a statute is unlawful is to "disapprove, or disallow, *only the unconstitutional application* of [the law], thereby preserving any residuary constitutional application with regard to the other provisions," when the Legislature would have preferred such a result had it foreseen the invalid applications (emphasis in original)). The analysis in these authorities demonstrates that, if the Court concludes that some applications of the CRRA are unconstitutional, the appropriate remedy is to disallow only those unlawful applications—not to excise the allegedly offending text or to strike down the entire statute.

Second, the CRRA's legislative history refutes defendants' claim that the Legislature would not have enacted a law that imposed royalty obligations only with respect to in-state sales. *See* Auction Houses Br. 54-58; EBay Br. (Dkt. 46) 45-46. When the Senate added the California-resident language, it did so as part of a change that broadened the law to cover not only sales by galleries, auction houses, and museums (as the Assembly bill had provided) but also those by private sellers. *See* Excerpts of Record (ER) 745 (Assembly bill); ER 761 (Senate); ER 784-785 (Conference Committee report); *see also* ER 718 (Assembly Ways and Means Committee Analysis noting that "[s]ince the [Assembly] bill only applies to galleries, museums and auctioneers, sales between private individuals

would apparently not apply"). Defendants' sole support for their contrary theory—that the Legislature added the California-resident language to prevent the art-sales market from leaving the State—is a letter from an outside third party to three individual members of the Legislature. *See* ER 577-578. Such a document is irrelevant to determining the Legislature's intent. *See Metro. Water Dist. of S. Calif. v. Imperial Irr. Dist.*, 80 Cal. App. 4th 1403, 1425-1426 (2000) (because "a court will generally consider only those materials indicative of the intent of the Legislature *as a whole*," letters to individual legislators expressing opposition to a bill "generally should not be considered" (emphasis in original)).[5] Moreover, precisely the same criticism was leveled against the bill even after it included the California-resident language. *E.g.*, ER 815. Defendants therefore have not and cannot overcome the presumption in favor of severability.

[5] In addition to the February 1976 letter at ER 577-578, Defendants cite two other documents that they claim reveal a concern about limiting the CRRA's royalty obligation following in-state sales. Auction Houses Br. 58; EBay Br. 46 (both citing ER 605-606, 837). Because both of these documents were authored by non-legislators, after the bill was adopted, neither sheds light on the Legislature's intent in passing the law.

CONCLUSION

The judgment of the district court should be reversed.

Dated: November 24, 2014

Respectfully submitted,

KAMALA D. HARRIS
Attorney General of California
EDWARD C. DUMONT
Solicitor General
MARK J. BRECKLER
Chief Assistant Attorney General
ROBERT W. BYRNE
Senior Assistant Attorney General

/S/ Aimee Feinberg
AIMEE FEINBERG
Deputy Solicitor General

GAVIN G. MCCABE
Supervising Deputy Attorney General
Attorneys for the State of California

CERTIFICATE OF COMPLIANCE

I certify that the attached brief is proportionately spaced, uses a 14-point Times New Roman font, and contains 6,133 words as counted by the Microsoft Word program, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

Dated: November 24, 2014

/S/ Aimee Feinberg
AIMEE FEINBERG
Deputy Solicitor General

CERTIFICATE OF SERVICE

I hereby certify that I electronically filed the document entitled **BRIEF FOR THE STATE OF CALIFORNIA AS *AMICUS CURIAE* SUPPORTING APPELLANTS AND REVERSAL** with the Clerk of the Court for the United States Court of Appeals for the Ninth Circuit on November 24, 2014 using the CM/ECF system. All case participants will be served electronically by the CM/ECF system.

Dated: November 24, 2014

/S/ Aimee Feinberg
AIMEE FEINBERG
Deputy Solicitor General