APPENDIX

APPENDIX A

IN THE
SUPREME COURT OF THE STATE OF UTAH

ROBERT C. STEINER AND WENDY STEINER-REED,
Appellants and Cross-Appellees,
v.
UTAH STATE TAX COMMISSION,
Appellee and Cross-Appellant.

No. 20180223
Filed August 14, 2019

On Direct Appeal

Third District, Salt Lake
The Honorable Noel S. Hyde
No. 170901774

Attorneys:

Peter W. Billings, William H. Adams, Nora K. Brunelle, David P. Billings, Salt Lake City, for appellants and cross-appellees

Sean D. Reyes, Att'y Gen., Stanford E. Purser, Deputy Solic. Gen., Erin T. Middleton, Asst. Solic. Gen., John C. McCarrey, Mark E. Wainwright, Asst. Att'y Gens., Salt Lake City, for appellee and cross-appellant

---

ASSOCIATE CHIEF JUSTICE LEE authored the opinion of the Court, in which CHIEF JUSTICE DURRANT, JUSTICE HIMONAS, JUSTICE PEARCE, and JUSTICE PETERSEN joined.

ASSOCIATE CHIEF JUSTICE LEE, opinion of the Court:

¶1 The Utah State Tax Commission disallowed certain tax deductions claimed by Robert and Wendy Steiner on their tax returns. The Steiners filed a challenge to that determination in the tax court. In that forum, the Steiners asserted that the United States Constitution, specifically the Dormant Commerce Clause and the Dormant Foreign Commerce Clause,[1] mandated that Utah allow their claimed deductions relating to (1) income earned in the United States but outside of Utah and (2) income earned in foreign countries. The Steiners also cited the Utah Code section 59-10-115(2), in support of their latter claim. The tax court agreed in part. It allowed the second set of deductions but disallowed the first.

¶2 Both parties appealed. We affirm in part and reverse in part. We agree with the State and hold that neither set of deductions is mandated by the United States Constitution. Nor are the deductions required by the Utah Tax Code.

---

[1] Throughout this opinion we refer to both the "Dormant Commerce Clause" and the "Dormant Foreign Commerce Clause." We refer to them this way, despite the fact that we cannot find either such clause in our copy of the United States Constitution, for the sake of simplicity and concision.

¶3 Our constitutional analysis is in line with our 2015 decision in *DIRECTV v. Utah State Tax Commission,* 2015 UT 93, 364 P.3d 1036. There we noted the lack of any textual or originalist mooring for the doctrine that has built up around the concept of dormant commerce, while also lamenting the lack of any "clear, overarching theory" in the decisions of the United States Supreme Court in this field. *Id.* ¶ 45. We acknowledged, of course, our duty to follow controlling precedent from that court. But we emphasized the difficulty of "anticipat[ing] expansions of the law" in this field "into new territory" not yet explored by the Supreme Court. *Id.* And in the absence of clear direction (in text, history, or precedent), we declined to make a guess about the direction the case law might take in the next case that comes before the Supreme Court. *Id.*

¶4 We resolve this case on this basis. We find no controlling precedent from the United States Supreme Court that mandates a decision striking down the challenged Utah tax provisions on dormant commerce grounds. And we uphold their constitutionality on that basis.

I

¶5 The Steiners filed joint tax returns as Utah residents in tax years 2011, 2012, and 2013. Although their income included earnings from various sources, the only component at issue on appeal is the tax on business income earned by Robert Steiner (Steiner).

¶6 Steiner is a shareholder of Steiner, LLC, which is taxed as an S corporation.[2] He is also a beneficiary of the G.A. Steiner Trust (the Trust), which is the majority shareholder of Steiner, LLC. The Steiners' income from Steiner, LLC during the relevant period included both amounts passed directly to Steiner by virtue of his direct stake in Steiner, LLC and amounts attributable to Steiner as a beneficiary of the Trust.

¶7 Steiner, LLC is the sole shareholder of Alsco, Inc. Alsco is a textile rental business, which along with its subsidiaries does business in the United States and around the world. Alsco and all of its subsidiaries that do business in the United States have elected to be taxed as Qualified S Subsidiaries. Thus, all of the income derived from these entities is passed through to Steiner, LLC. Steiner, LLC, in turn, passes the income through to its individual shareholders, including Steiner. Such income is accordingly reflected on the Steiners' joint tax returns. Most of Alsco's foreign subsidiaries have elected to be taxed as partnerships for U.S. tax purposes. Ninety-nine percent of the income from each subsidiary is passed through to Alsco as a partner. This income goes through the same pass-through waterfall and ends up on the Steiners' joint tax returns as well.

---

[2] That means that Steiner, LLC itself does not pay any federal or state-level tax. *See* 26 U.S.C. § 1363; UTAH CODE § 59-10-1403(1). All of its income passes through to individual shareholders' tax returns (in proportion to their ownership interest). 26 U.S.C. § 1366; UTAH CODE § 59-10-1403.1(2). The individuals then pay taxes on the amount passed through to their individual returns. 26 U.S.C. § 1366.

¶8 On their federal tax returns during the relevant years the Steiners claimed, and received, a tax credit for the taxes they had paid to foreign jurisdictions. On their Utah tax returns, the Steiners claimed a state tax credit for taxes they paid to other states. These credits are explicitly allowed by the Utah Tax Code. UTAH CODE § 59-10-1003. But the Steiners also claimed an "equitable adjustment" under Utah Code section 59-10-115 — an adjustment excluding foreign income from their Utah taxable income.

¶9 The Utah State Tax Commission[3] audited the Steiners' tax returns. The Commission disallowed the "equitable adjustment" for foreign income. But it also recalculated the state tax credit and determined that the Steiners were entitled to a larger credit than they had claimed.

¶10 The Steiners filed a Petition for Redetermination challenging the Commission's disallowance of the equitable adjustment for foreign income. In a subsequent amendment to their petition, the Steiners also challenged Utah's state tax credit system. They asked the Commission to make a determination that only the portion of Steiner, LLC's income that is apportioned to Utah should be included in taxable income for Utah

[3] Some of the actions in this case were undertaken by subdivisions of the Commission (specifically the Auditing Division). Because the distinctions are not relevant, we refer to all of the entities collectively as the Commission for the sake of simplicity.

purposes.[4] The Steiners also raised constitutional challenges to Utah's tax scheme in their petition.

¶11 The Commission conducted a formal hearing on the Steiners' petition and later issued a final decision in which it upheld the original audit determination and denied the Steiners' new apportionment claim. The Commission lacked jurisdiction to hear the constitutional claims and thus declined to address them.

¶12 After this adverse ruling, the Steiners paid the assessed tax deficiency (plus statutory interest) pursuant to Utah Code section 59-1-611. They then appealed to the third district tax court for a "de novo" review of the Commission's determination. *See* UTAH CODE § 59-1-601. In the tax court, both parties moved for summary judgment. The tax court first ruled that Utah's tax treatment of income earned in other states did not run afoul of the Dormant Commerce Clause. Specifically, the court held that the Dormant Commerce Clause did not require apportionment of the Steiners' income and that Utah's tax credit system satisfied the requirements of that clause. The court went on to rule that the Steiners were entitled to claim an equitable adjustment for their foreign business income. The court's ruling in this regard, although ultimately based on statutory grounds, was driven by constitutional concerns. In particular, the tax court

---

[4] Apportionment involves allocation of corporate business income to Utah by comparing a corporation's Utah-specific presence with its overall payroll, property, sales, and so forth. UTAH CODE § 59-7-311. Only the proportion of income attributable to Utah is then taxed by Utah.

believed that the Dormant Foreign Commerce Clause mandated that Utah allow foreign business income to be deducted. The tax court thus remanded the case to the Commission so it could apply the equitable adjustment to the Steiners' income. Both parties filed notices of appeal to this court pursuant to Utah Code section 59-1-608.

II

¶13 The Commerce Clause grants Congress the authority to regulate interstate commerce. U.S. CONST. art. I, § 8, cl. 3. "By negative implication," the United States Supreme Court has held that "this provision also limits the states' authority in this realm." *DIRECTV v. Utah State Tax Comm'n,* 2015 UT 93, ¶ 13, 364 P.3d 1036. "So even if Congress has not spoken on an issue of interstate commerce, states are prevented from encroaching on Congress's authority — hence the term 'dormant' or 'negative' Commerce Clause." *Id.* We must decide how to apply this negative implication to the Utah Tax Code.

¶14 This case presents three distinct questions for our resolution: (1) whether the Dormant Commerce Clause requires Utah to apportion a residency-based income tax instead of simply granting a credit for taxes paid to other states; (2) whether the Dormant Foreign Commerce Clause requires Utah to allow a deduction for income earned in foreign countries; and (3) whether Utah's "equitable adjustment" statute, Utah Code section 59-10-115(2), mandates a deduction for foreign income.

¶15 We answer each of these questions in the negative, explaining our reasoning below. But before

diving into the specifics, we lay out some background on our general jurisprudential approach to dormant commerce issues.

A

¶16 Decades ago the United States Supreme Court likened its case law under the Dormant Commerce Clause to a "quagmire." *Nw. States Portland Cement Co. v. Minnesota,* 358 U.S. 450, 458 (1959). That was an apt metaphor at the time. It seems even more so today.

¶17 The Supreme Court's body of dormant commerce jurisprudence has multiplied several-fold in the decades since the *Portland Cement* case. But "[n]ot much has changed . . . , except perhaps to add more room for controversy and confusion and little in the way of precise guides to the States in the exercise of their indispensable power of taxation." *DIRECTV,* 2015 UT 93, ¶ 44 (citation and internal quotation marks omitted). This is unfortunate. The lower courts are operating largely in the dark in this important field of constitutional law. "Yet we must of course decide the cases that come before us, mindful of our role as a lower court to follow controlling precedent from the U.S. Supreme Court." *Id.*

¶18 In carrying out our duty, however, "we are reluctant to extend dormant Commerce Clause precedent in new directions not yet endorsed" by the Supreme Court. *Id.* ¶ 45. Because the high court's rulings in this area have proceeded on an *ad hoc* basis lacking "any clear, overarching theory," we have noted the difficulty of the task of a lower court in attempting to "anticipate expansions of the law

into new territory." *Id.* And with this in mind, we have warned of the perils of a lower court reading tea leaves in this field.

¶19 We have acknowledged, of course, the Supreme Court's prerogative to place limits on the "longstanding police powers of state and local governments to regulate business." *Id.* ¶ 46. But in light of the *ad hoc* nature of that court's precedents, we have warned that "it should be the U.S. Supreme Court" that leads the way in charting new territory in this field. *Id.*

¶20 We follow this same approach here. We will, of course, faithfully apply controlling precedent. But we decline to extend that precedent into new territory — even in ways that might seem logical in other jurisprudential realms. We do that not out of any disrespect for the United States Supreme Court, but in our best attempt at judicial humility in a constitutional field marked more by haphazard policy judgments than any unifying legal theory. In such a field it would seem presumptuous to make our own guess about the next move the high court might make as it extends its precedent. And we will thus leave it to that court to mark the next extension in this field.

B

¶21 Like many states, Utah taxes its residents on all of their income, regardless of where it is earned. But Utah also grants its residents credits for taxes they have already paid to other states. This ensures that Utah residents' income is not subject to taxation by both Utah and another state.

¶22 The Steiners nevertheless contend that this taxation scheme violates the Dormant Commerce Clause because it taxes a disproportionate share of the income they earned outside of Utah. They are mistaken. We hold that Utah's provision of credits for income taxes already paid to other states satisfies the dormant commerce requirements set forth in controlling precedent.[5]

¶23 The seminal case in this area is *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274 (1977). *Complete Auto* is the origin of the four-part test used to assess state taxes for compliance with the Dormant Commerce Clause. But the *Complete Auto* framework was altered by the Supreme Court's more recent decision in *Comptroller of the Treasury of Maryland v. Wynne,* 135 S. Ct. 1787 (2015). In light of the complexity of the case law in this area, we first outline the evolution of Dormant Commerce Clause jurisprudence prior to *Wynne.* We next explain how *Wynne* changed the governing framework. Finally, we apply *Wynne* to conclude that Utah's tax scheme is constitutional.

1

¶24 The modern framework for evaluating the validity of state taxes under the Dormant Commerce Clause has its origins in *Complete Auto,* 430 U.S. 274. In that case the high court overruled the

---

[5] The tax court granted summary judgment in favor of the Commission on this issue. We review summary judgment decisions for correctness, granting no deference to the lower court's legal conclusions. *Salt Lake Cty. v. Holliday Water Co.,* 2010 UT 45, ¶ 14, 234 P.3d 1105.

previously governing analytical approach established in *Freeman v. Hewit,* 329 U.S. 249 (1946), and *Spector Motor Service v. O'Connor,* 340 U.S. 602 (1951). Those cases established what was known as the "Spector Rule" — that "a tax on the 'privilege' of engaging in an activity in the State may not be applied to an activity that is part of interstate commerce." *Complete Auto,* 430 U.S. at 278. The *Complete Auto* Court discarded the Spector Rule on the ground that it represented a "triumph of formalism over substance." *Id.* at 281.

¶25 Apart from its expressed dissatisfaction with the formalist nature of the Spector Rule, the *Complete Auto* Court offered very little in the way of an analytical explanation of its basis for a new legal framework in this field. Instead the Court just made brief note of four claims that the taxpayer had *not* made in that case. *Id.* at 287. The Court stated, almost in passing, "that no claim is made that the activity is not sufficiently connected to the State to justify a tax, or that the tax is not fairly related to benefits provided the taxpayer, or that the tax discriminates against interstate commerce, or that the tax is not fairly apportioned." *Id.*

¶26 This offhand statement was eventually elevated into a "test." *See D.H. Holmes Co. v. McNamara,* 486 U.S. 24, 30 (1988). To pass Dormant Commerce Clause scrutiny under this "test," a state tax must: (1) apply to an activity with a substantial nexus to the state, (2) be fairly apportioned, (3) not discriminate against interstate commerce, and (4) be fairly related to the services the state provides. *Id.* Only the fair apportionment prong is at issue in this appeal.

¶27 The Supreme Court has further subdivided the fair apportionment prong into two parts — internal consistency and external consistency. *Container Corp. of Am. v. Franchise Tax Bd.,* 463 U.S. 159, 169 (1983). Internal consistency requires an analysis of the inherent characteristics of the state tax system. Under this analysis we assume that every state uses Utah's tax system, and assess whether, in this hypothetical world, there is systematic discrimination against interstate commerce. *Wynne,* 135 S. Ct. at 1801-02. External consistency, on the other hand, requires that state taxes "reflect a reasonable sense of how income is generated." *Container Corp.,* 463 U.S. at 169. To evaluate this question, a court must assess "whether the State has taxed only that portion of the revenues from the interstate activity which reasonably reflects the in-state component of the activity being taxed." *Goldberg v. Sweet,* 488 U.S. 252, 262 (1989). This essentially requires states to apportion income, and tax only that part of the income attributable to in-state activity.

¶28 Prior to *Wynne* there was considerable uncertainty regarding the continued vitality of both of these two components. *See, e.g., Okla. Tax Comm'n v. Jefferson Lines, Inc.,* 514 U.S. 175, 196 (1995) (declining to require external consistency of sales taxes for sake of "simplicity"); Walter Hellerstein, *Is "Internal Consistency" Dead?: Reflections on an Evolving Commerce Clause Restraint on State Taxation,* 61 TAX. L. REV. 1, 26 (2007). Despite this confusion, neither test has been expressly overruled by the Supreme Court. With this in mind, the Steiners assert that Utah's tax scheme, as applied to

them, must satisfy *both* the internal and external consistency tests. If the tax fails to do this, in their view, it does not survive the Dormant Commerce Clause challenge.

¶29 To see why this assertion is mistaken, we have to take a detailed look at the *Wynne* decision.

2

¶30 *Wynne* was a challenge brought by individual taxpayers against Maryland's tax statutes. The Wynnes sought two important extensions to the Supreme Court's then-existing Dormant Commerce Clause jurisprudence. First, they wanted the Court to apply the clause to an individual (rather than a corporation) for the first time. Second, they wanted the Court to apply the clause to a residency-based income tax — also for the first time.

¶31 Like the Steiners, the taxpayers in *Wynne* were shareholders of an S corporation. *Wynne,* 135 S. Ct. at 1793. The Wynnes were residents of Maryland. *Id.* At the time of that case, Maryland imposed two levels of state taxation — first, a state income tax, which Maryland levied at a graduated rate; and second, a county income tax, which varied based on geography but was levied at a flat rate. *Id.* at 1792. Despite the differing nomenclature, both taxes were collected directly by the state of Maryland. *Id.* Maryland allowed taxpayers to claim a credit for taxes paid to other states, but only against the "state" tax — not the "county" tax. *Id.* Maryland residents were thus subject to double taxation on their income earned in other states. Income was taxed by the other state via that state's taxation

regime and Maryland via its flat rate county tax. Maryland also taxed the income of nonresidents. *Id.* Nonresidents paid the state income tax on all income they earned within Maryland. *Id.* They also had to pay a "special nonresident tax" instead of the county tax. *Id.* This tax was equivalent to the lowest county income tax rate. *Id.* The Wynnes claimed that this system violated the Dormant Commerce Clause.

¶32 The Supreme Court agreed. As a threshold matter the Court noted that "it is hard to see why the dormant Commerce Clause should treat individuals less favorably than corporations." *Id.* at 1797. It thus concluded, with little analysis, that individuals are also protected by the Dormant Commerce Clause — even though the Court had previously never explicitly held as much. [6] The Wynnes, as shareholders of an S corporation, accordingly fell within the ambit its protection.

¶33 The Court then went on to assess the substance of the Maryland tax. But in doing so, it sailed past the four-part *Complete Auto* test and

---

[6] The *Wynne* case is a departure from the Court's previous position that an individual's residence in a state subjected him, in full, to that state's taxation regime. Indeed, as the principal dissent noted, "the sheer volume and consistency of [the Court's] precedent confirms . . . the degree to which this Court has — until now — endorsed the well-established principle . . . that a State may tax its residents' worldwide income, without restriction arising from the source-based taxes imposed by other States and regardless of whether the State also chooses to impose source-based taxes of its own." *Comptroller of the Treasury of Md. v. Wynne,* 135 S. Ct. 1787, 1818 (2015) (Ginsburg, J., dissenting) (citation and internal quotation marks omitted).

assessed the Maryland tax only on internal consistency grounds. Although the Court noted that the Maryland Court of Appeals applied the full *Complete Auto* test, *id.* at 1793, it did not endorse or apply the full test anywhere in its opinion. Nor did it state that it was simply unnecessary to apply the remaining prongs because one of the prongs was dispositive. Instead, it at least implicitly treated internal consistency as a standalone constitutional test. The continuing vitality of the *Complete Auto* test is thus in serious doubt.[7]

¶34 *Wynne* also introduced uncertainty into the fair apportionment prong. As discussed above, *supra* ¶ 27, the fair apportionment requirement consists of two subparts — internal consistency and external consistency. The *Wynne* Court first concluded that Maryland's tax failed the internal consistency test. The Court imagined a simplified world in which every state had the same taxation system as Maryland. *Id.* at 1803. The Court then

> [a]ssume[d] further that two taxpayers, April and Bob, both live in State A, but that April earns her income in State A whereas Bob earns his income in State B. In this circumstance, Bob will pay more income tax than April solely because he earns income interstate. Specifically, April will have to pay a 1.25% tax only once, to State A. But Bob will have to pay a 1.25% tax twice: once to State A,

---

[7] We flag this point without conclusively resolving it. We need not decide whether *Wynne* dispensed with *Complete Auto* because only the fair apportionment prong is at issue in this case.

> where he resides, and once to State B, where he earns the income.

Id. at 1803-04. Based on this hypothetical, the Court determined that the Maryland tax systematically discriminated against interstate commerce and thus failed the internal consistency test. *Id.* at 1803. And in light of this failure, the Court held that Maryland's tax failed to survive the Dormant Commerce Clause challenge. *Id.*[8]

¶35 So far so good. Because Maryland's tax failed the internal consistency test, the Supreme Court need not have reached the external consistency test since a failure on either prong would have been determinative. But the Court went on to propose a potential solution to Maryland's problem. Significantly, the Court's proposed solution is one that would fail the external consistency test.

¶36 The *Wynne* Court suggested that Maryland could fix the problem with its tax code by eliminating the special nonresident tax, but continuing to tax all of its residents' income regardless of source. *Id.* at 1806. Yet this solution would fail the external consistency requirement. The proposed system would allow Maryland to levy the county tax on 100 percent of its residents' income generated outside of Maryland. Maryland would apportion none of this income to other states. Crucially, *it would not even have to grant a credit for taxes paid to other states* (as

---

[8] This despite the fact that the Court had upheld internally inconsistent state taxes before. *See, e.g., Am. Trucking Ass'ns v. Mich. Pub. Serv. Comm'n,* 545 U.S. 429, 437 (2005); *Shaffer v. Carter,* 252 U.S. 37, 57 (1920). So much for consistency.

long as it didn't tax nonresidents).[9] This "would seem to squarely violate the external consistency test," which requires states to apportion income such that it "reflect[s] a reasonable sense of how income is generated." *Dormant Commerce Clause — Personal Income Taxation* — Comptroller of the Treasury of Maryland v. Wynne, 129 HARV. L. REV. 181, 186-87 (2015) (internal quotation marks and emphasis omitted). This tax system does not even come close to "slicing [the] taxable pie among [the] States in which the taxpayer's activities contributed to taxable income." *Jefferson Lines,* 514 U.S. at 186. Maryland would be entitled to tax the out of state "slice" simply because the taxpayer resided in Maryland. But slicing the tax pie is the quintessential point of external consistency.

¶37 The *Wynne* Court thus went out of its way to endorse a tax regime violative of the external consistency test. Whatever life external consistency might have left, it is highly unlikely that it continues to apply in the context of an individual taxpayer's challenge to a state's taxation system.[10]

---

[9] As long as Maryland taxes only residents, the tax system is internally consistent. If every state taxed based only on residency (and not based on the source of the income), there would be no discrimination against interstate commerce. A person living in State A would pay only State A taxes, and a person living in State B would pay only State B taxes. There would be no differing tax burden based on the interstate nature of the income.

[10] Although we are unaware of any judicial opinions reaching this precise conclusion, there is significant scholarly commentary along these lines. *See, e.g.,* Mackenzie Catherine Schott, Comment, *Inconsistency with the Internal Consistency*

¶38 To summarize, *Wynne* struck down Maryland's tax system solely on the basis of internal consistency. The Court did not apply the *Complete Auto* test. And it strongly implied that tax systems that fail external consistency would nonetheless pass constitutional muster.

¶39 The task that remains, then, is to assess Utah's tax scheme under the guidelines laid out in *Wynne*.

3

¶40 We can distill several principles from *Wynne* that bear on the Steiners' first claim: (1) As shareholders of an S corporation, the Steiners are entitled to bring a Dormant Commerce Clause challenge; (2) Utah's tax regime *must* satisfy the internal consistency test; and (3) Utah's tax regime need not satisfy the external consistency test. The Steiners' challenge will rise and fall, then, on a showing of internal inconsistency in Utah's tax code.

¶41 We uphold the constitutionality of the Utah tax scheme at issue under these principles. Because Utah's tax system is internally consistent, we hold

---

Test, 77 LA. L. REV. 947 (2017) (arguing that *Wynne* established internal consistency as a standalone constitutional test); Edward A. Zelinsky, *The Enigma of* Wynne, 7 WM. & MARY BUS. L. REV. 797, 809-10 (2016) (noting that *Wynne* "can be read as presaging a future formal repudiation of the external consistency test"); *Dormant Commerce Clause — Personal Income Taxation* — Comptroller of the Treasury of Maryland v. Wynne, 129 HARV. L. REV. 181, 188 (2015) (asserting that *Wynne* demonstrates that the Supreme Court is "hesitant to apply the [external consistency] test").

that the Steiners' Dormant Commerce Clause challenge fails on the merits.

¶42 For the years in question, Utah taxed its residents' state taxable income at a rate of 5 percent. UTAH CODE § 59-10-104 (2013). Utah residents who paid income taxes in other states could take a credit against their Utah taxes in the amount of taxes they paid to other states, up to the amount that they would have paid under Utah's tax rate. *Id.* § 59-10-1003. Nonresidents were also taxed at the same rate of 5 percent, but only on their income earned in Utah. *Id.* § 59-10-103(1)(w), -104(2), -116.

¶43 This arrangement satisfies *Wynne's* internal consistency test. If every state adopted the same tax system as Utah, there would be no discrimination against interstate commerce. April and Bob (our hypothetical taxpayers) — who are both residents of State A — pay the same tax even though April earns her income in State A and Bob earns his in State B. April will pay a 5 percent tax to State A on her income because she resides there. Bob will pay a 5 percent tax to State A because he resides there and a 5 percent tax to State B because he earns income there, but he will receive a credit in State A for the 5 percent tax paid to State B. Like April, he will be taxed only once on his income. Bob does not shoulder a higher tax burden even though he earns his income in interstate commerce.[11] This conclusion is bolstered

---

[11] It is true that some states have a 0 percent income tax, and no credit against Utah taxes is thus available for income earned in those states (because no taxes are paid to those states). But this is immaterial to the analysis. Internal consistency analyzes only the effects of a state's *own* tax system. The fact that a

by the *Wynne* majority's statement that "Maryland could cure the problem with its current system by granting a credit for taxes paid to other States." 135 S. Ct. at 1806. This is exactly what Utah does.

¶44 Utah's tax code thus satisfies the internal consistency test. In *Wynne,* the Supreme Court declined to require anything else of Maryland's tax. We accordingly apply *Wynne* and conclude that a state tax levied against individuals need satisfy only the internal consistency test to pass Dormant Commerce Clause scrutiny. [12] It would be an extension of *Wynne* to require that these taxes also satisfy external consistency. If the Supreme Court wishes to mandate such an extension, it is of course free to do so. But we will not do so here.

C

¶45 The Steiners also assert a challenge to Utah's tax code under the Dormant Foreign Commerce Clause.[13] They contend that Utah's failure to grant a

---

given state's system might generate odd results because of its interaction with the systems of *other* states is irrelevant. *See Okla. Tax Comm'n v. Jefferson Lines, Inc.,* 514 U.S. 175, 185 (1995).

[12] As discussed previously, only the fair apportionment prong of the *Complete Auto* test is at issue before us. So although a fair reading of *Wynne* is that it may have discarded that test entirely, we need not decide the issue. It is enough for our purposes to conclude that after *Wynne,* "fair apportionment" means the same as "internal consistency" in this context.

[13] The Dormant Foreign Commerce Clause is analogous to the Dormant Commerce Clause. But whereas the latter is derived by negative implication from the Commerce Clause, the former finds its footing (or lack thereof) in the Foreign Commerce Clause.

credit for taxes already paid to foreign countries impermissibly discriminates against international commerce. The tax court agreed and allowed the Steiners to deduct their foreign income under the equitable adjustment statute so as to avoid what it viewed as an otherwise unconstitutional result. We reverse. There is no Supreme Court case in which that Court has struck down a state tax on the foreign income of an individual or an S corporation. We decline to break new ground here — if the Dormant Foreign Commerce Clause is going to be extended to individuals "it should be the United States Supreme Court that makes that decision." *DIRECTV v. Utah State Tax Comm'n,* 2015 UT 93, ¶ 46, 364 P.3d 1036. The protections of the Dormant Foreign Commerce Clause have been extended only to corporations. And even if the clause did apply to the Steiners, the requirements are met here. Accordingly, we hold that Utah's tax system does not run afoul of the Dormant Foreign Commerce Clause.[14]

1

¶46 No Supreme Court case considering the Dormant Foreign Commerce Clause has involved an individual taxpayer (or S corporation shareholder). They have all involved C [15] corporations. [16] The

---

[14] We review the tax court's grant of summary judgment for correctness. *Salt Lake Cty. v. Holliday Water Co.,* 2010 UT 45, ¶ 14, 234 P.3d 1105.

[15] C corporations file corporate tax returns and pay federal and state corporate-level taxes on the entity's business and non-business income. 26 U.S.C. § 11; UTAH CODE § 59-7-101 *et seq.*

[16] *See Barclays Bank PLC v. Franchise Tax Bd. Of Cal.,* 512 U.S. 298 (1994); *Itel Containers Int'l Corp. v. Huddleston,* 507

Supreme Court has never indicated that a state — taxing an *individual* based on his residency in that state — could run afoul of the Constitution by failing to grant a tax credit against taxes levied by foreign countries. Under the principles we articulated in *DIRECTV* that alone is enough to end the inquiry. We could conclude otherwise only by transplanting *Wynne* into the Court's foreign commerce clause jurisprudence. But we find no established basis for *Wynne* to be extended into this area.

¶47 As discussed above, *Wynne* established — for the first time — that a state tax levied against an individual who resided in that state was subject to the Dormant Commerce Clause. *Supra* ¶ 32. Justice Alito, writing for the Court, noted that "it is hard to see why the dormant Commerce Clause should treat individuals less favorably than corporations." *Comptroller of the Treasury of Md. v. Wynne,* 135 S. Ct. 1787, 1797 (2015). Crucially, however, the Court applied a different doctrinal framework to the individual taxpayers in *Wynne* than the one previously applied to corporations.

¶48 *Wynne* adopted the internal consistency test as a freestanding constitutional requirement. *Id.* at 1803. In its previous cases, however, the Court applied this test as one part of the broader *Complete Auto* framework. *See, e.g., D.H. Holmes Co. v.*

U.S. 60 (1993); *Kraft Gen. Foods, Inc. v. Iowa Dep't of Revenue & Fin,* 505 U.S. 71 (1992); *Wardair Canada, Inc. v. Fla. Dep't of Revenue,* 477 U.S. 1 (1986); *Container Corp. of Am. v. Franchise Tax Bd.,* 463 U.S. 159 (1983); *Mobil Oil Corp. v. Comm'r of Taxes of Vt.,* 445 U.S. 425 (1980); *Japan Line, Ltd. v. Cty. Of Los Angeles,* 441 U.S. 434 (1979).

McNamara, 486 U.S. 24, 30 (1988). And what's more, the failure of a tax to pass the internal consistency test was not previously fatal. *See, e.g., Am. Trucking Ass'ns v. Mich. Pub. Serv. Comm'n,* 545 U.S. 429, 437 (2005); *Shaffer v. Carter,* 252 U.S. 37, 57 (1920). Thus despite the Court's insistence that individuals are entitled to be treated no "less favorably" than corporations under the Dormant Commerce Clause, it is clear that they can be treated differently. Crucial distinctions between individuals and corporations continue to exist as a doctrinal matter. Logically, then, individuals and corporations may also be subjected to differing analytical frameworks under the Dormant Foreign Commerce Clause. But the Supreme Court has provided no guidance whatsoever to lower courts regarding how to treat individuals in the context of *foreign* commerce. So even if we were inclined to conclude that state taxes of individual residents are subject to Dormant Foreign Commerce Clause scrutiny, we would be completely at sea. We would have no idea what test to apply or how to apply it.[17]

¶49 "Our hesitance to extend the law of dormant commerce is reinforced by a practical problem: The extension advocated by the [Steiners] would open a

---

[17] This difficulty is exacerbated by the fact that the governing Dormant Foreign Commerce Clause framework is not identical to the domestic framework. *See, e.g., Itel Containers Int'l Corp.,* 507 U.S. at 73 (noting that *Complete Auto* framework is the "domestic commerce clause test"). We thus do not know (1) how the assessment of an individual tax would work as a practical matter; or (2) how it would work as a doctrinal matter. We see no basis for stumbling through these nesting layers of unknowns until the Supreme Court lights the way.

can of worms." *DIRECTV,* 2015 UT 93, ¶ 46. This practical problem is amply illustrated by the Steiners' own briefing. In seeking to extend *Wynne* to foreign commerce, the Steiners attempt to apply the internal consistency test. As discussed, this test requires analyzing a hypothetical world in which all jurisdictions have the challenged tax scheme. We then would assess if interstate commerce suffers from systematic discrimination in this alternate world. But this test is quite impossible to apply in an international setting. *Wynne*'s internal consistency analysis contemplated only state-level taxes within a uniform federal system. And the international income earned by the Steiners is subject to multiple levels of foreign taxation — local, subnational, and national. It would make no sense to universalize Utah's tax system to conduct a *Wynne* analysis — Utah is a single, subnational taxing jurisdiction. There is no proper basis to compare the effect of its tax system with the effect of those of foreign jurisdictions encompassing multiple levels of taxation.

¶50 In light of this uncertainty, we decline to "veer[] from a principle of interstate and international taxation repeatedly acknowledged by [the Supreme Court]: A nation or State 'may tax *all* the income of its residents, even income earned outside the taxing jurisdiction." *Wynne,* 135 S. Ct. at 1813 (Ginsburg, J. dissenting) (quoting *Okla. Tax Comm'n v. Chickasaw Nation,* 515 U.S. 450, 462-63 (1995)). Although the Supreme Court has chosen to depart from this settled rule in the context of domestic taxation, it has given no indication of its intent to extend that approach to state taxation of

foreign commerce. "And since a move in that direction would require subjective line-drawing that would take us far afield of the Court's current approach, we doubt that it will." *DIRECTV,* 2015 UT 93, ¶ 46. We reverse the tax court and hold that Utah may tax the entirety of the Steiners' foreign income based on their residency in the state.

2

¶51 Although the Supreme Court has never articulated a test for a residence-based individual income tax, Utah's tax is consistent with the broader dormant foreign commerce principles the Court has hinted at. First, Utah's tax code interacts with the federal tax code in a manner that leads to evenhanded treatment of foreign commerce. Second, we can infer that Congress approves of Utah's tax system and has thus authorized it.

¶52 The "foreign commerce clause cannot be interpreted to demand that a State refrain from taxing any business transaction that is also potentially subject to taxation by a foreign sovereign." *Itel Containers Int'l Corp. v. Huddleston,* 507 U.S. 60, 74 (1993). Indeed, "absolute consistency, even among taxing authorities whose basic approach to the task is quite similar, may just be too much to ask." *Container Corp. of Am. v. Franchise Tax Bd.,* 463 U.S. 159, 192 (1983). There is always some risk of double taxation in the international realm. Mitigation of this risk, however, would require complex negotiation with foreign nations — negotiations that the State of Utah is legally and practically ill-equipped to tackle.

¶53 This is a further indication of the need for leeway for states in the exercise of their taxing authority in the shadow of the Foreign Commerce Clause. *See id. at* 192 n. 31 (noting that "California . . . is in no position to negotiate with foreign governments," and thus that the risk of double taxation was no reason to invalidate the tax). Utah's residency based individual tax may possibly subject the Steiners to a double tax on some of their income. But this alone may not be a basis for invalidating the Utah tax.

¶54 This conclusion is strengthened by the way in which Utah's tax system interacts with the federal system. The United States government has entered into a multitude of complex tax treaties with foreign nations. The federal government, consistent with these treaties, provides residents with a credit for foreign taxes already paid on foreign-sourced income. 26 U.S.C. §§ 901-09. The rules governing these tax credits are understandably extremely complex. Crucially, these treaties and rules often allow a credit against federal tax for both foreign national and subnational taxes. Richard D. Pomp and Michael J. McIntyre, *GATT, Barclays, and Double Taxation,* 8 STATE TAX NOTES 977 (1995). If the State of Utah were to also grant a foreign tax credit, foreign-sourced income would be granted the windfall of a double tax credit. This would systematically favor foreign commerce over domestic commerce. And we see no basis for the conclusion that the Dormant Foreign Commerce Clause requires such a result.[18]

---

[18] It is true that the Supreme Court has previously stated that there is "no authority . . . for the principle that discrimination

¶55 Congress seems to agree. Despite the fact that dozens of states decline to grant a credit for foreign taxes, Congress has never acted to prohibit the practice or to preempt these laws in any way. Normally we would hesitate to infer anything from Congressional inaction. But the Supreme Court has specifically stated that Congress may "passively indicate that certain state practices" do not violate the Dormant Foreign Commerce Clause. *Barclays Bank PLC v. Franchise Tax Bd. of Cal.,* 512 U.S. 298, 323 (1994).[19] "[I]f a state tax merely has foreign resonances, but does not implicate foreign affairs, we cannot infer, absent some explicit directive from Congress" that the states must conform their taxes to federal practice. *Container Corp. of Am.,* 463 U.S. at 194 (internal alterations, quotation marks, and citations omitted).

---

against foreign commerce can be justified if the benefit to domestic subsidiaries might happen to be offset by other taxes imposed not by [the State], but by . . . the Federal Government." *Kraft Gen. Foods,* 505 U.S. at 81. But this was before the Court articulated the principle of passive congressional approval. The interaction between federal and state statutes is important for assessing if Congress has *sub silentio* approved a state law.

[19] The Court made this statement in the context of evaluating whether a tax impaired the ability of the federal government to operate uniformly. This is ostensibly one of two additional prongs (along with the *Complete Auto* factors) in evaluating taxes under the Dormant Foreign Commerce Clause. But it has broader applicability. If Congress may "passively" approve of state laws for one part of the test, there is no reason its passive approval should not be attributed to the law as a whole. After all, it seems implausible that Congress would intend to signal approval for just one part of a judicially invented six-part test.

¶56 The lack of an explicit Congressional directive may thus come close to tacit approval of these state laws. And the Court has repeatedly stated that Congress can authorize state action that would otherwise violate the Dormant Commerce Clause. *See, e.g., Camps Newfound/Owatonna, Inc. v. Town of Harrison,* 520 U.S. 564, 572 & n.8 (1997); *Maine v. Taylor,* 477 U.S. 131, 138 (1986). Regardless of any judicially jury-rigged multipart tests, then, this Congressional approval immunizes Utah's tax code from judicial scrutiny under the Dormant Foreign Commerce Clause.

D

¶57 Lastly, the Steiners argue that the equitable adjustment statute in Utah's tax code allows them to deduct their foreign income from their Utah tax base as a statutory matter. Applying principles of constitutional avoidance, the tax court agreed and read the relevant section to allow the deduction. We reverse. We hold that the equitable adjustment statute does not apply in this instance.

¶58 As in all cases of statutory interpretation, we begin with the text. *See Olsen v. Eagle Mountain City,* 2011 UT 10, ¶ 9, 248 P.3d 465 (affirming "our commitment to interpreting statutes according to the 'plain meaning of their text"). [20] The equitable

---

[20] We have previously suggested that statutes granting tax credits "must be narrowly construed against the taxpayer." *Ivory Homes, Ltd. v. Utah State Tax Comm'n,* 2011 UT 54, 1110, 266 P.3d 751. Yet we have also said that we "construe tax imposition statutes liberally in favor of the taxpayer." *Id.* ¶ 31. This dichotomy presents a difficult line-drawing problem, as it is not always apparent whether a given statutory provision is

adjustment statute reads, in relevant part: "[t]he commission shall allow an adjustment to adjusted gross income of a resident or nonresident individual if the resident or nonresident individual would otherwise . . . suffer a double tax detriment under this part." UTAH CODE § 59-10-115(2)(b). The question presented concerns the meaning of the phrase "double tax detriment under this part."

¶59 The Steiners contend that if any of their income is taxed twice, then they have suffered a "double tax detriment." Thus, they argue, the fact that their foreign-source income is taxed by both Utah and a foreign country entitles them to take advantage of the statute and adjust the income they report to Utah.

¶60 It's true that the Steiners have suffered a "double tax detriment" by being taxed by both Utah and a foreign country. But the statute doesn't call for adjustments for any double tax detriment—it calls for an adjustment only if the taxpayer suffers "a

---

better viewed as a matter of a tax "credit," on one hand, or as an element of the basis for the threshold imposition of the tax, on the other. The logic of the distinction is likewise a bit slippery. We have endorsed the notion of narrow construction of tax credits on the ground that such are a matter of legislative "grace." *See id.* ¶ 10. But there is a sense in which all tax provisions are a matter of grace, as the taxing authority could always go further in imposing a greater tax.

We flag this problem as a matter deserving greater attention in a future case. We need not resolve it here, however, as it has always been clear that the first order of business in a matter of statutory interpretation is to credit the ordinary meaning of the words enacted into law by the legislature. And here we conclude that such meaning cuts squarely against the Steiners.

double tax detriment *under this part." Id.* (emphasis added). The words "under this part" are crucial. And "under this part" necessarily refers to the part of the tax code to which section 115 belongs — part 1 of title 59, chapter 10, entitled "Determination and Reporting of Tax Liability and Information" of the State's Individual Income Tax Act. *See id.* §§ 59-10-101-137. The clear import of that phrase is that an equitable adjustment is available only if the Utah tax code itself imposes double taxation.[21]

¶61 This is fatal to the Steiners' position. Utah has not taxed their foreign income twice — it has only taxed it once. The second tax detriment they suffered was at the hands of a foreign sovereign. They cannot therefore take advantage of the equitable adjustment statute. We reverse the tax court and hold that the equitable adjustment statute applies only when Utah itself imposes double taxation.

III

¶62 "The principle of *dormant* commerce . . . is not rooted in a *clause,* but in a negative implication of one." *DIRECTV v. Utah State Tax Comm'n,* 2015 UT 93, ¶ 45, 364 P.3d 1036. For that reason there is a "dearth of any textual or historical foundation for a court to look to" in this field. *Id.* The problem is compounded when we search for principled guidance in precedent from the United States Supreme Court,

---

[21] The tax court's invocation of the constitutional avoidance canon was thus erroneous. That canon is applicable only where the statute is "genuinely susceptible to two constructions." *Utah Dep't of Transp. v. Carlson,* 2014 UT 24, ¶ 24, 332 P.3d 900 (quoting *Almendarez-Torres v. United States,* 523 U.S. 224, 238 (1998)). Here the statute is unambiguous.

as that Court itself has long acknowledged that its case law in this field is a bit of a "quagmire," *Nw. States Portland Cement Co. v. Minnesota,* 358 U.S. 450, 458 (1959), and its recent decisions "add more room for controversy and confusion and little in the way of precise guides to the States in the exercise of their indispensable power of taxation." *DIRECTV,* 2015 UT 93, ¶ 44 (citation and internal quotation marks omitted).

¶63 This is the legal backdrop for our decision in this case. The Steiners have raised some plausible arguments and identified some potential policy concerns with the tax regime enacted by the State of Utah. But in the absence of any clear anchors in text, history, or precedent, we are left with little more than a request that we second-guess the policy judgment of our state legislature — based on speculation about how a rather haphazard body of case law may ultimately play out in the future.

¶64 We do not see this as our role.[22] We uphold the constitutionality of the Utah tax provisions at issue on the ground that the Steiners have identified no basis in controlling precedent for striking them down. We also hold that they have fallen short in

---

[22] *See DIRECTV v. Utah State Tax Comm'n,* 2015 UT 93, ¶ 46, 364 P.3d 1036 (noting our "hesitance" to "limit[] the longstanding police powers of state and local governments to regulate business"); *see also Comptroller of Treasury of Md. v. Wynne,* 135 S. Ct. 1787, 1810 (2015) (Scalia, J., dissenting) (suggesting that the dormant commerce "doctrine does not call upon us to perform a conventional judicial function," but "instead requires us to balance the needs of commerce against the needs of state governments" — "a task for legislators, not judges").

their attempt to identify a statutory basis for their challenge to these provisions.

APPENDIX B

IN THE THIRD JUDICIAL DISTRICT COURT
SALT LAKE COUNTY, STATE OF UTAH
TAX COURT DECISION

ROBERT C. STEINER & WENDY STEINER-REED,
Petitioners / Plaintiffs,

v.

UTAH STATE TAX COMMISSION,
Respondent / Defendant.

RULING AND ORDER ON CROSS-MOTIONS FOR SUMMARY JUDGMENT

Case No. 170901774

Judge Noel S. Hyde

Filed 01/30/2018

The matter before the court is a challenge to Utah's tax structure as it relates to the business income of shareholders of S corporations. At issue is the tax structure's impact on foreign and interstate commerce. Petitioners have made both facial and as-applied challenges to Utah's tax structure.[1] The

[1] "[W]e will find the statute unconstitutional only if petitioners can demonstrate that the statute is either facially unconstitutional or unconstitutional as applied. In making this determination, we will resolve any reasonable doubt in favor of constitutionality." *Elk Lodges No. 719 (Ogden) & No. 2021*

success of those challenges turns on whether the current statutory structure is capable of a constitutional interpretation. If a reasonable constitutional reading of the statutes is available, the facial challenge will fail. However, even if the tax structure is facially sufficient, if its application to Petitioners in this case fails to meet constitutional standards, then the as-applied challenge may succeed. To determine whether a reasonable constitutional interpretation exists, the court must evaluate controlling Utah and federal constitutional precedent as it relates to the circumstances of this case.

FACTS

The Steiners were Utah residents during the years that the income tax was assessed. *Pet. Mot.* at 4 ¶ 1. Their income came from Steiner, LLC, a Nevada subchapter-S Corporation. *Id.* at ¶ 2; *Id.* Ex. A at 3. The business income from Steiner, LLC passes through to its shareholders, and the Steiners are shareholders of Steiner, LLC. *Id.* at ¶ 2, 3. About 2% of the corporation's income is generated from activities within Utah; about 98% comes from its interstate activities and foreign business subsidiaries. *Id.* at 11. When the Steiners filed their 2011, 2012, and 2013 taxes, they claimed the available state tax credit on income earned and taxed in other states. *Id.* at 8 ¶ 12. The Steiners also claimed equitable adjustments, under Utah Code Ann. § 59-10-115, and removed all foreign business income from their Utah taxable income, even though

---

(Moab) v. Dep't of Alcoholic Beverage Control, 905 P.2d 1189, 1202 (Utah 1995) (citation omitted).

that income was reported on their federal return. *Id.,* Ex. A at 2. Utah does not provide a tax credit for income earned in foreign jurisdictions or income earned in states without an income tax. *Id.* at 8 ¶ 12, 13. The Utah State Tax Commission ("the Commission"), denied the equitable adjustments and assessed a deficiency on the business income in the Steiners' taxes for 2011, 2012, and 2013, totaling approximately $1.3 million. *Id.* at 8-9, ¶ 14, 15.

The Steiners' appealed the deficiency determination to the Commission. *Id.* at 9-10, ¶ 16-19. The Commission ruled against Petitioners, holding that the Steiners did not qualify for an adjustment under Utah Code Ann. § 59-10-115, and noting that the Commission lacked authority to determine the constitutional questions. *Id.* at 10, ¶ 19-20. Petitioners appealed and asked to have the case decided in Tax Court. Both parties have moved for summary judgment and agree that the case presents no disputed issues of material fact. *Id.* at 3; *Resp. Mot.* at 1.

DISCUSSION

States have the power to tax the income of their residents under the Due Process clause of the Fourteenth Amendment to the U.S. Constitution. However, the power to tax all the income of the state's residents is limited by the Commerce Clause. *See, Comptroller of Treasure of Maryland v. Wynne,* 135 S.Ct. 1787, 1798-99 (2015). The United States Constitution grants Congress power "To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes." U.S. Const. Art. I, § 8, cl. 3. "Although the Clause is

framed as a positive grant of power to Congress, `[the Supreme Court has] consistently held this language to contain a further, negative command, known as the dormant Commerce Clause, prohibiting certain state taxation even when Congress has failed to legislate on the subject.'" *Wynne,* 135 S.Ct. at 1794 (quoting *Okla. Tax Comm'n v. Jefferson Lines, Inc.,* 514 U.S. 175, 179 (1995)). The Utah Supreme Court has acknowledged that "even if Congress has not spoken on an issue of interstate commerce, states are prevented from encroaching on Congress's authority—hence the term 'dormant' or 'negative' Commerce Clause." *DIRECTV v. Utah State Tax Comm'n,* 2015 UT 93, ¶ 13. Notwithstanding references to interstate commerce in many of the Commerce Clause decisions of the Supreme Court, the standards and limitations that apply to state taxation of interstate commerce also apply, under the foreign Commerce Clause of the U.S. Constitution, to state taxation of foreign commerce. In *Kraft General Foods, Inc. v. Iowa Dept. of Revenue and Finance,* 505 U.S. 71 (1992), the Supreme Court held that foreign commerce is due even greater protection from discrimination than interstate commerce. *Id.* at 79.

Commerce Clause challenges are subject to strict scrutiny when the challenged laws "directly discriminate against interstate commerce—by 'facial' discrimination or discrimination that is apparent in its effect and discriminatory purpose." *DIRECTV,* 2015 UT at ¶ 14 (citing *Or. Waste Sys. Inc. v. Dep't of Envtl. Quality,* 511 U.S. 93, 99 (1994)). A tax structure that discriminates based on the geographic location of the business or its activities is subject to strict scrutiny. *Id,* at ¶¶ 23-26. A law to which strict

scrutiny applies may only be upheld if "it serves a 'legitimate local purpose' that 'could not be served as well by available nondiscriminatory means.'" *Id,* at ¶ 14 (citing *Maine v. Taylor,* 477 U.S. 131, 139 (1986)). Alternatively, a balancing test may apply when the tax law's discriminatory effect is merely incidental, and the law may be invalidated only if the burden on interstate commerce outweighs the local benefit. *Id.,* at ¶ 15 (citing *Pike v. Bruce Church, Inc.,* 397 U.S. 137, 142 (1970)). However, when a tax law affects foreign commerce, a court may find a discriminatory violation based only on a burden on foreign commerce, regardless of any finding of a local benefit. *Id.* The court will evaluate the foreign commerce issues in the present case under a strict scrutiny analysis to ensure that foreign commerce receives the heightened level of protection required in *Kraft.*

Because the present case involves taxation of the shareholders of an S corporation, it is also significant to note that in *Wynne,* the U.S. Supreme Court determined that Commerce Clause protections afforded to C corporations also apply to S corporations and their shareholders. *See Wynne,* 135 S.Ct. at 1792, 1797-98. In *Wynne,* the Court held that Maryland's personal income tax structure violated the Commerce Clause because it denied shareholders of an S corporation a credit for corporate income taxes paid in other states. *Id.* at 1792-93. The Court ruled that the interstate business income was impermissibly taxed twice because it was subject to two states' tax schemes. *Id.* at 1792. Respondent's argument that applying this holding from *Wynne* to the present case would be an unwarranted extension

of *Wynne* is not persuasive. Likewise, that the Supreme Court may not have specifically contemplated the consequences of its ruling in *Wynne* when applied to the circumstances now before this court does not allow the court to disregard the Court's ruling. Based upon *Wynne,* constitutional limitations on Utah's taxation of corporate business income apply to taxation of S corporation income. Respondent provides no persuasive authority for the argument that *Wynne* must be restricted to questions involving interstate taxation and that the case has no application to issues involving foreign commerce.

The U.S. Supreme Court has ruled that to survive a Commerce Clause challenge, a tax must meet the following four-prong test: "the tax is applied to an activity with a substantial nexus with the taxing State, is fairly apportioned, does not discriminate against interstate commerce, and is fairly related to the services provided by the State." *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274, 279 (1977). Petitioners argue that, as currently interpreted and applied by Respondent, Utah's tax structure violates the second and third prongs of this *Complete Auto* test. Each prong will be addressed in turn.[2]

Discrimination

States may not "impose a tax which discriminates against interstate commerce either by providing direct commercial advantage to local business, or by

---

[2] Because Petitioners do not argue that the first and fourth prongs of the *Complete Auto* test are violated in this case, those prongs will not be addressed further in this opinion. *Pet. Mot.* at 16; *Resp. Mot.* at 17; *Resp. Mot.* at 25.

subjecting interstate commerce to the burden of multiple taxation." *DIRECTV,* 2015 UT at ¶ 22 (citing *Wynne,* 135 S.Ct. 1787, at 1794 (quoting *Nw. States Portland Cement Co. v. Minnesota,* 358 U.S. 450, 458 (1959))) (quotations omitted). Consistently, the Utah Supreme Court has held that "the dormant Commerce Clause's strict prohibition on discrimination is implicated by laws treating different interests differently *because* one set of interests has a distinct geographic connection to the home state and others lack it." *DIRECTV,* 2015 UT at ¶ 34.

The U.S. Supreme Court has held tax structures unconstitutional when those structures "had the potential to result in the discriminatory double taxation of income earned out of state." *Wynne,* 135 S.Ct. at 1801-02. The Court explained, "[a]lthough we did not use the term in those cases, we held that those schemes could be cured by taxes that satisfy what we have subsequently labeled the 'internal consistency' test." *Id.*[3]

---

[3] Initially, the Court in *Container Corp. of America v. Franchise Tax Board,* 463 U.S. 159, 169 (1983), stated, "The first...component of fairness in an apportionment formula is what might be called internal consistency—that is the formula must be such that, if applied by every jurisdiction, it would result in no more than all of the unitary business's income being taxed." Later in *Oklahoma Tax Comm'n v. Jefferson Lines, Inc.,* 514 U.S. 175, 185 (1995), internal consistency was still used as part of the fair apportionment prong, but the Court was starting to look for discrimination under internal consistency. The test's purpose was to "see whether [a tax's] identical application...would place interstate commerce at a disadvantage as compared with commerce intrastate." *Id.*

To determine internal consistency, a hypothetical test is applied, which assumes that every jurisdiction has the same tax structure. The purpose of this test is to "`look[] to the structure of the tax at issue to see whether its identical application by every State in the Union would place interstate commerce at a disadvantage as compared with commerce intrastate.' *Id.* at 1812, (quoting *Jefferson Lines,* 514 U.S. at 185). If applying the tax as structured would result in discrimination against interstate or foreign commerce, the tax is not internally consistent.

The issue presently before this court involves the taxation of business income earned out-of-state by an S corporation whose shareholders are resident in Utah. Utah taxes business income at a rate of 5%. *Pet. Mot.* at 18; *See also Resp. Mot.* at 24 (citing Utah Code Ann. §§ 59-10104(1), -103(w)(i), -103(1)(a), -114). Utah also allows residents who earn income out-of-state to take a credit for taxes paid in other states. However, Utah does not allow residents to take a credit for taxes paid in foreign jurisdictions. Utah's tax structure also provides for equitable adjustments. The equitable adjustment provisions will be addressed separately in this decision and are not considered here. Assuming that every jurisdiction, including all other states and foreign jurisdictions, has a tax structure identical to Utah's current structure, the question is whether this tax structure discriminates against interstate or foreign commerce.

Hypothetically, the court considers the following three circumstances: Business A is resident in Utah and earns income in Utah; Business B is resident in Utah, but earns income from Colorado; and Business

C is also resident in Utah, but earns income from Germany. Under Utah's current tax structure as it relates to business taxes and available business tax credits, Business A pays tax on the Utah business income at the current rate of 5%. Business B's Colorado business income is taxed in Utah at 5%. However, because it is assumed that Colorado also taxes business income earned there at 5%, Business B can claim the tax credit for the taxes paid on income in Colorado. Thus, Business B does not pay taxes on the Colorado income in Utah and the Colorado income is only taxed once. Business C's German business income is taxed in Utah at 5%. Germany is presumed, hypothetically, to also tax the income earned there at 5%. However, Utah's tax structure does not permit Business C to take a tax credit for the 5% tax paid in Germany on the business income also taxed in Utah. Therefore, Business C, hypothetically, pays a double tax on the business income earned in Germany.

This hypothetical analysis shows that Utah's tax structure is internally consistent as applied to interstate business taxation, which conclusion is acknowledged by both Petitioners and Respondent in this case. However, Utah's tax structure is not internally consistent as applied to taxation of foreign business income. Utah does not provide a credit or other adjustment for foreign taxes paid, so the business income is subject to double taxation, once by the foreign jurisdiction and a second time by Utah. The court rules that, absent consideration of equitable adjustments, this discrimination violates the foreign Commerce Clause.

Respondent argues unpersuasively that Utah need not make any accommodation for foreign business income because Congress has already spoken on the issue, and through a federal tax credit, found in IRC §§ 901-909, and various tax treaties has addressed the problem of double taxation of foreign business income. However, a tax credit for federal taxes does not provide relief from state taxes.[4] In addition, none of the cases cited by Respondent supporting this argument involves a state attempting to tax foreign business income. *Havana Elec. Ry., Light & Power Co. v. Comm'r,* 34 B.T.A. 782 (1936); *Riggs Nat. Corp. & Subsidiaries v. C.I.R.,* 163 F.3d 1363 (D.C. Cir. 1999); *Procter & Gamble Co. v. United States,* 2010 WL 2925099 (T.C. 2010). These cases actually support Petitioners' argument that a federal tax credit provides relief on federal taxes only. The existence of a federal foreign tax credit, therefore, does not resolve the discrimination that may result when states tax foreign business income.

Similarly, federal tax treaties have only addressed how the federal government's tax structure interacts with foreign entities and their citizens. In making the argument that tax treaties have addressed and resolved the issues relating to double taxation of foreign business income by states, Respondent relies primarily on the United States Model Income Tax Convention from November 2006. *Resp. Supp. Auth. 1.* Article 23 of the model treaty provides relief from double taxation, but is only applicable at the federal

---

[4] Utah Code Ann. § 59-10-110 (2017) states that taxpayers may not apply federal tax credits when calculating their income for state taxes.

level. *See Resp. Supp. Auth. 2,* at 8, 74. Article 24 does focus on non-discrimination relating to foreign nationals residing in the U.S., and is applicable to the states. *Id.* at 2, 78-79. However, the model treaty nowhere addresses or authorizes the double taxation by the states of foreign business income. This lack of direction is not a statement from Congress on the propriety of any state tax structure relating to foreign commerce. The dormant foreign Commerce Clause has application in precisely this situation. The absence of a provision in the model treaty requiring states to grant credits for foreign taxes paid does not open the door for states to tax foreign business income in such a way that results in double taxation. Respondent's argument that the foreign Commerce Clause does not apply is rejected.

Apportionment

A tax must be fairly apportioned "to ensure that each State taxes only its fair share of an interstate transaction." *Oklahoma Tax Comm'n v. Jefferson Lines, Inc.,* 514 U.S. 175, 184 (1995) (quotations and citation omitted). To determine whether a state tax is fairly apportioned, the court applies what is referred to as an external consistency test. "External consistency ... looks ... to the economic justification for the State's claim upon the value taxed, to discover whether a State's tax reaches beyond that portion of value that is fairly attributable to economic activity within the taxing State." *Id.* at 185. However, external consistency must work in harmony with the principle that states can tax based on residency; the external consistency test has not been applied to invalidate an income tax based on residency.

To the extent that Petitioners' argument is a request to either directly or implicitly invalidate Utah's residence-based business income tax, the request is denied. Even though cases applying the external consistency test and requiring some formula of apportionment focus on the activity or transaction taxed, no cases have been presented to this court which compel the conclusion that a resident of a state may avoid taxation by the state of any amount of business income simply because the business was not conducted in the state. The taxable activity or transaction that is the focus of a residence-based income tax is residency, itself.

There is "a well-established principle of interstate and international taxation—namely, that a jurisdiction... may tax *all* the income of its residents, even income earned outside the taxing jurisdiction." *Oklahoma Tax Comm'n v. Chickasaw Nation,* 515 U.S. 450, 462-463 (1995). The Court has explained, "[that] the receipt of income by a resident of the territory of a taxing sovereignty is a taxable event is universally recognized. Domicil itself affords a basis for such taxation." *New York ex rel. Cohn v. Graves,* 300 U.S. 308, 312-313 (1937). Residency, itself, provides a valid and sufficient connection to the state for business income tax purposes, and a residence-based business income tax may be imposed so long as the tax avoids the pitfalls of discrimination and double taxation.

Petitioners' arguments that the tax structure is improper because it may result in a tax liability greater than the total business income generated in the State of Utah or in an effective tax rate that is disproportionately high in relation to the business

income generated in the state do not persuade the court that the tax structure is externally inconsistent. Utah may tax the business income of its residents, but the tax may not result in double taxation when viewed together with taxes imposed by other states or foreign entities. Thus, if the business income earned in other states or foreign jurisdictions is not taxed at all in those jurisdictions, Utah may impose its residence-based tax on such income. Even if the effective tax rate when compared to business income generated in Utah is disproportionately high, the business income of Petitioners is still only taxed once, and the tax structure would still comply with Commerce Clause requirements. The court rules in this case that Utah's current business tax structure does not violate the apportionment prong of the *Complete Auto* test.

Equitable Adjustments

Utah's tax statute includes an equitable adjustment provision. Utah Code Ann. § 59-10115 requires the Commission to approve equitable adjustments if the taxpayer "would otherwise suffer a double tax detriment." Petitioners have argued that they should have been able to make the equitable adjustment to their income to eliminate earnings from states that do not impose an income tax, and to avoid a double tax detriment related to their foreign business earnings. Respondent opposes this interpretation of the statute. Regarding the adjustment to eliminate income earned in states that do not impose an income tax, the court is not persuaded by Petitioners' argument. Because such income has not been the subject of any income tax, it

is properly subject to the state's residence-based tax. Also, because there is no double taxation, equitable adjustments are not required.

With respect to foreign business earnings, the court reviews the equitable adjustment provisions to determine whether such provisions can be interpreted to meet constitutional requirements. As it does so, the court is mindful of the principles of statutory interpretation which require the court to "construe a challenged statute to avoid constitutional infirmities wherever possible." *Elk Lodges No. 719 (Ogden) & No. 2021 (Moab) v. Dep't of Alcoholic Beverage Control,* 905 P.2d 1189, 1202 (Utah 1995) (citing *Society of Separationists, Inc. v. Whitehead,* 870 P.2d 916, 920 (Utah 1993)). Courts generally avoid analyzing constitutional issues if it can be avoided by statutory interpretation. *See Utah Dept. of Transp. V. Carlson,* 2014 UT 24, ¶ 24. When it is unavoidable, the courts will "prefer a constitutional reading of a statute over an unconstitutional interpretation thereof." *Elk Lodges,* 905 P.2d at 1202 (citing *Chris & Dick's Lumber & Hardware v. Tax Comm'n of Utah,* 791 P.2d 511, 516 (Utah 1990)).

Petitioners argue that the plain reading of the statute provides a way for taxpayers to make equitable adjustments to their income. The statute reads:

> 2) The commission shall allow an adjustment to adjusted gross income of a resident or nonresident individual if the resident or nonresident individual would otherwise: . . .

(b) suffer a double tax detriment under this part.

Utah Code § 59-10-115 (West 2017); *see also, Pet. Mot.* at 32, (quoting Utah Code § 59-10-115 (West 2008)).

In response, Respondent argues first, that the equitable adjustment provision has never been interpreted to apply to double taxation on foreign business income. *See Pet. Mot.* at 33; *Pet. Mot.,* Ex. A at 9-10 *(citing Utah State Tax Commission Findings of Fact, Conclusions of Law, and Final Decision, Appeal No.* 08-0590 (August 5, 2010); *Utah State Tax Commission Order, Appeal No.* 05-1787 (September 5, 2006); *Utah State Tax Commission Initial Hearing Order, Appeal No.* 12-915 (April 15, 2014); *Utah State Tax Commission Findings of Fact, Conclusions of Law, and Final Decision, Appeal No.* 14-373 (November 11, 2015); and *Utah State Tax Commission Initial Hearing Order, Appeal No.* 15-1332 (June 27, 2016)). However, the fact that the equitable adjustment provision has not yet been interpreted in a constitutionally permissible way does not preclude its being so interpreted now.

The courts do not "defer to an agency's statutory interpretation unless the legislature has explicitly, or implicitly, granted the agency discretion to interpret the statutory language at issue." *Belnorth Petroleum Corp. v. State Tax Com 'n of Utah,* 845 P.2d 266, 268 (Utah Ct. App 1993); *see also LPI Services v. McGee,* 2009 UT 41, ¶ 7. Because the Utah Legislature has directed, in Utah Code Ann. § 59-1-610 (2017), that no deference is to be given to conclusions of law made by the Commission, and also based upon the

Commission's own confirmation that it lacks authority to address or determine the constitutionality of Utah's tax structure, this court is not bound by past agency interpretations of the equitable adjustment provisions of Utah's tax statutes.

Respondent next argues that the Legislature intended the equitable adjustments provision to cover only double taxes imposed by Utah. "It is a long-held position of the Commission that the Utah Legislature only intended to address double taxation by the State of Utah ... and that the Legislature did not intend to address foreign income or income from states that assess no tax." *Resp. Mem. Opp'n* at 33; *see also Pet. Mot,* Ex. A at 9-10. Questions of legislative intent are not given substantial weight by the court if the suggested interpretation would result in an unconstitutional application of the statute, and an at-least-equally-plausible interpretation permits a constitutional application. The Commission's interpretation finds no support in a plain-language reading of the statute. The equitable adjustment provision of the tax code is included in that part which authorizes Utah to tax its residents' income. The statute is directed, generally, to concern about double taxation, and is not restricted to circumstances where the State of Utah imposes a tax twice. The language of the statute is equally applicable to circumstances where the State of Utah imposes a tax on income that has already been taxed by another jurisdiction. Taxation by the State of Utah of business income that has already been taxed in another jurisdiction meets squarely the definition of double taxation, and there is no plausible

argument that the taxation in question is not being imposed by the State of Utah.

Finally, Respondent argues that if the Legislature wanted this statute to be read to address double foreign taxation, it would have expressly referred to foreign business income. *Resp. Mem. Opp'n* at 33. The court is not persuaded. *Kraft* requires that foreign commerce receive at least the same protection as interstate commerce. If the statute were drafted to expressly preclude adjustments for foreign income, as Respondent argues, then the statute would be unconstitutional on its face. Because the court must construe the statute to be constitutional, if possible, and because Respondent's suggested interpretation would be facially unconstitutional, the court must interpret the equitable adjustment provisions to permit an adjustment for foreign business income taxed in the foreign jurisdiction. The court is not in a position to rewrite any provision of Utah's tax code. The court can only interpret the provisions that are presently subject to challenge and determine whether they meet constitutional standards on their face or as applied.

CONCLUSION

In summary, the tests for internal and external consistency have been met by Utah's tax structure for local and interstate business income, and the Commission is affirmed on the facial and as-applied challenges regarding such business income. However, in applying the standards set forth in *Kraft,* the court must be even more vigilant to ensure that Utah's tax structure does not impose an

improper burden on foreign commerce. Therefore, because Utah's tax structure as currently applied to the taxation of foreign business income passed through to the shareholder of an S corporation may result in double taxation of that income, such double taxation of foreign business income is a discriminatory burden on foreign commerce which violates the foreign Commerce Clause of the U.S. Constitution.

The absence of a credit or other adjustment for foreign business income already taxed in a foreign jurisdiction cannot pass muster under the internal consistency test. By denying the equitable adjustment claimed by Petitioners regarding foreign business income already taxed in a foreign jurisdiction, the tax structure as currently applied is invalid based on that discrimination, even though the tax structure is externally consistent because it is a residence-based tax. Therefore, the portion of the Commission's decision which relates to the determination of Petitioners' tax liability relating to foreign business income is vacated, and the case is remanded with instruction to apply the equitable adjustment provision so as to avoid double taxation of Petitioners' foreign business income. Any effort to address a potential change in the tax statutes to permit a credit for taxes paid on business income generated in foreign jurisdictions is left to the consideration of the Legislature.

ORDER

The Tax Commission's decision is affirmed as to the interstate business income claim, and reversed

and remanded with respect to the foreign business income claim.

Dated this 30th day of January, 2018.

/s/ Noel S. Hyde
Noel S. Hyde
District Court Judge

APPENDIX C

BEFORE THE UTAH STATE TAX COMMISSION

ROBERT C. STEINER AND WENDY STEINER-REED,
Petitioners,

v.

AUDITING DIVISION OF THE UTAH STATE TAX COMMISSION,
Respondent.

FINDINGS OF FACT, CONCLUSIONS OF LAW, AND FINAL DECISION

Appeal No. 15-235

Tax Type: Income Tax

Tax Years: 2011, 2012 and 2013

Judge: Phan

Presiding:

Michael Cragun, Commissioner
Robert Pero, Commissioner
Rebecca Rockwell, Commissioner
Jane Phan, Administrative Law Judge

Appearances:

For Petitioner:

Peter Billings, Attorney at Law
William Adams, Attorney at Law

Nora Brunelle, Attorney at Law
Robert Steiner

For Respondent:

John McCarrey, Assistant Attorney General
Mark Wainwright, Assistant Attorney General
Angie Hillas, Income Tax Audit Manager
Kim Ferrell, Corporate Franchise Tax Audit Manager

STATEMENT OF THE CASE

This matter came before the Utah State Tax Commission for a Formal Hearing on May 10, 2016, in accordance with Utah Code §59-1-501 and §63G-4-201 et seq. Based upon the evidence and testimony presented at the hearing, the Tax Commission hereby makes its:

FINDINGS OF FACT

1. Petitioners ("Taxpayers") timely filed an appeal of Utah individual income tax audit deficiencies issued against them for tax years 2011, 2012 and 2013 and the matter proceeded to this Formal Hearing.

2. The Notices of Deficiency and Audit Change had been issued on January 12, 2015 for each year at issue.[1] The amounts of audit deficiencies imposed with interest calculated to the notice payment dates are as follows:

---

[1] Exhibit 1.

Year	Audit Tax	Interest
2011	$377,585	$21,310.28
2012	$448,258	$16,382.91
2013	$407,875	$6,749.49

Year	Penalty	Total as of Notice Date[2]
2011	$0	$398,895.28
2012	$0	$464,640.91
2013	$0	$414,624.49

3. Although Respondent ("Division") had made some small changes in the audits which were in the Taxpayer's favor, the tax deficiency resulted from the Division's disallowance of the equitable adjustments the Taxpayers had claimed for each tax year on their Utah Resident Individual Income Tax Returns.

4. It was the equitable adjustments that were at issue in this hearing. The equitable adjustments were subtractions that the Taxpayers made from their Utah taxable income, although they were income amounts that the Taxpayers had included in their federal adjusted gross income. The equitable adjustments were claimed on Line 8 (Subtractions from Income) of their Utah Individual Income Tax Returns[3] and were as follows:

---

[2] Interest continues to accrue on any unpaid balance.

[3] Exhibits 2-4.

2011	$7,372,280
2012	$9,066,691
2013	$8,209,333

5. With their 2011 Utah Individual Income Tax Return, the Taxpayers provided an attachment to Form TC-40A[4] in which they explained the equitable adjustment as follows:

> Adjustments have been made to exclude the foreign source business taxable income included in the Taxpayers' federal taxable income from the Taxpayers' Utah taxable income. Utah is prohibited by the Commerce Clause in Article I, Section 8 of the United States Constitution from imposing a tax on the Taxpayers' foreign source business taxable income since doing so would discriminate against foreign commerce. Utah law unfairly attempts to tax foreign source income differently from the taxation of domestic source income taxed in other states. The Taxpayers receive a credit for income taxes paid to another state; however, since no such credit is allowed for foreign tax imposed on foreign source income, the Utah Tax on the Taxpayers' foreign source income (before foreign income tax) is discriminatory and therefore unconstitutional.

---

[4] Exhibit 2, pg. 000019.

A similar statement was provided with the Taxpayers' returns for 2012 and 2013.[5]

6. The Taxpayers were Utah resident individuals for tax years 2011 - 2013.

7. Robert Steiner (when referred to individually, Mr. Steiner will be referred to as "Taxpayer") is a shareholder directly of Steiner, LLC, which is a Nevada limited liability company that has elected to be classified as an S corporation for federal and Utah tax purposes. Taxpayer is also one of several income beneficiaries of the G.A. Steiner Trust. The G.A. Steiner Trust is the majority shareholder (87%) of Steiner, LLC. The G.A. Steiner Trust for the benefit of the Taxpayer has elected to be a Qualified Subchapter S Trust ("QSST") for federal tax purposes. The Taxpayer is deemed to be the shareholder of Steiner, LLC with respect to the shares owned by the Robert Steiner portion of the G.A. Steiner Trust. As the shareholder of an S corporation, the Taxpayer included his allocable share of the income of Steiner, LLC on his federal income tax returns and they were part of his federal adjusted gross income for the years in question.

8. Steiner, LLC is a holding company that is the sole shareholder of Alsco, Inc., a Nevada corporation ("ALSCO"). ALSCO has elected to be classified as a Qualified S Subsidiary ("QSSUB") for federal and Utah tax purposes. Thus, for tax purposes, ALSCO is a disregarded entity and its business is considered to be the business of Steiner, LLC. All of Steiner, LLC's business income is from ALSCO. ALSCO is engaged

---

[5] Exhibits 3 & 4.

in the textile rental business both directly and through wholly owned subsidiaries in the United States and several foreign countries.[6] All of the ALSCO subsidiaries that are engaged in business in the United States have elected to be classified as QSSUBs. Substantially all of the income of the textile rental business, both domestic and foreign, is "flow through income" that is allocated to the shareholders of Steiner, LLC for federal and Utah tax purposes, and the shareholders are responsible for the payments of the federal and Utah income tax liability on the Steiner, LLC income.

9. Roughly 2% or less of Steiner, LLC's business income was apportioned to Utah during the years in question and roughly 98% to other states and foreign countries. ALSCO has facilities in 30 states and thirteen or fourteen countries. It has 17,300 employees worldwide and 430 employees in Utah. ALSCO's general office is located in Utah.

APPLICABLE LAW

A tax is imposed on the state taxable income of a resident individual under Utah Code §59-10-104(1)[7].

Utah Code §59-10-103(1)(w) defines "state taxable income" as follows, in pertinent part:

> (i) Subject to Section 59-10-1404.5, for a resident individual, means the resident

---

[6] Exhibit 1.

[7] The Commission cites to the 2012 version of the Utah Code on provisions of substantive law, which is similar for all three tax years at issue.

> individual's adjusted gross income after making the:
>
> (A) additions and subtractions required by Section 59-10-114; and
>
> (B) adjustments required by Section 59-10-115...

Utah Code §59-10-103(1)(a)(i) provides that "adjusted gross income" for a resident individual "is as defined in Section 62, Internal Revenue Code."

During the audit years,[8] Utah Code §59-10-115 provided for an equitable adjustment in some limited situations as follows:

> (1) The commission shall allow an adjustment to adjusted gross income of a resident or nonresident individual if the resident or nonresident individual would otherwise:
>
> (a) receive a double tax benefit under this part; or

---

[8] After the audit period, effective beginning with the 2017 tax year, this statute was revised to add an equitable adjustment on foreign source taxable income for certain pass-through entity taxpayers where the income is from heavy gauge metal tank manufacturing. The new provision at Utah Code Subsection 59-10-115(3)(a) (2017) provides: "For a pass-through entity taxpayer generating taxable income primarily from establishments classified in Code Section 3342, Metal Tank (Heavy Gauge) Manufacturing, of the 2002 or 2007 North American Industry Classification System of the Federal Executive Office of the President, Office of Management and Budget, an adjustment described in Subsection (2) includes net foreign source taxable income generated from Metal Tank (Heavy Gauge) Manufacturing establishments."

(b) suffer a double tax detriment under this part.

(2) In accordance with Title 63G, Chapter 3, Utah Administrative Rulemaking Act, the commission may make rules to allow for the adjustment to adjusted *gross* income required by Subsection (1).

Utah Code §59-10-1003 provides for credit for taxes paid to another state as follows:

(1) Except as provided in Subsection (2), a claimant, estate, or trust may claim a nonrefundable tax credit against the tax otherwise due under this chapter equal to the amount of the tax imposed:

(a) on that claimant, estate, or trust for the taxable year;

(b) by another state of the United States, the District of Columbia, or a possession of the United States; and

(c) on income:

(i) derived from sources within that other state of the United States, District of Columbia, or possession of the United States; and

(ii) if that income is also subject to tax under this chapter.

(2) A tax credit under this section may only be claimed by a:

(a) resident claimant;

(b) resident estate; or

(c) resident trust.

(3) The application of the tax credit provided under this section may not operate to reduce the tax payable under this chapter to an amount less than would have been payable were the income from the other state disregarded.

(4) The tax credit provided by this section shall be computed and claimed in accordance with rules prescribed by the commission.

Utah Code §59-1-1417 provides for burden of proof and statutory construction as follows:

(1) In a proceeding before the commission, the burden of proof is on the petitioner except for determining the following . . .

(2) Regardless of whether a taxpayer has paid or remitted a tax, fee, or charge, the commission or a court considering a case involving the tax, fee, or charge shall:

(a) construe a statute imposing the tax, fee, or charge strictly in favor of the taxpayer; and

(b) construe a statute providing an exemption from or credit against the tax, fee, or charge strictly against the taxpayer.

DISCUSSION

The relevant facts were not substantially in dispute at this hearing. The issue is a question of law and primarily the issues raised by the Taxpayers are constitutional. As noted by the Taxpayers' representative "the Taxpayers' position is really quite simple: Utah cannot constitutionally tax business income attributable to activities outside of Utah. And Section 59-10-115 can and must be construed to avoid the unconstitutional result of the Division's position." [9] The Taxpayers are Utah residents for Utah individual income tax purposes and are not contesting that the State of Utah may tax their dividend and investment income, which they refer to as nonbusiness or portfolio income. Their contention is with the ALSCO business income that passes through to the Taxpayers' individual returns and is included in their federal adjusted gross income. They are arguing that it is unconstitutional for the State of Utah to tax the Taxpayers' business income attributable to activities outside of Utah, even though it is income included in the Taxpayers' federal adjusted gross income. The Taxpayers argue at the hearing that the same constitutional principles apply to not only the income attributable to foreign countries, but also income attributable to states with no income tax. [10] They distinguish the states that tax income from states

---

[9] Petitioners' Pre-Hearing Reply Brief, pg. 3.

[10] The Taxpayers had not taken the position regarding the income attributable to states that do not assess tax on their Utah returns for the audit years, so this position was not reflected in the audit deficiency amounts.

that do not because Utah does allow a credit for individual income taxes paid to another state, so this credit is available for states that assess tax. Basically, the Taxpayers argue that most of the ALSCO business income does not relate to Utah and Utah should only be able to tax business income attributable to Utah.

The Taxpayers point out that under Utah law, a corporation that is domiciled in Utah that is taxed as a C corporation, is subject to a Utah tax only on its business income that is attributable to its business activities in Utah.[11] The Taxpayers represent that if Steiner, LLC was taxed as a C corporation, most of the income would be attributable to business activities conducted outside of Utah." The Taxpayers represent that if their Steiner, LLC income was taxed like a C corporation and only the income attributable to Utah was subject to Utah tax, the tax amount would be substantially less for each year. They state for example, in tax year 2011 the tax on the Steiner, LLC income attributable to the Taxpayers under the Division's position would be $388,506 of Utah individual income tax, while if the

[11] In Taxpayers' Prehearing Brief, pg. 8, these differences were stated as follows for each tax year: for 2011, of the $10,783,466 which was the Taxpayers' share of Steiner, LLC Business Income, $10,551,190 was attributable to non-Utah sources; for tax year 2012, of the $12,937,828 Taxpayers' share, $12,704,313 was attributable to non-Utah sources; and for 2013, of the $14,236,670 Taxpayers' share, $14,018,578 was attributable to non-Utah sources.

tax was calculated like a C corporation, it would only be $11,051.[12]

The Taxpayers cite to the recent United States Supreme Court decision in *Comptroller of Treasury of Md. v. Wynne,* 135 S.Ct. 1787 (US 2015), and argue that it supports the position that "if a tax on a C corporation violates the Commerce Clause, then the same tax imposed on an individual also violates the Commerce Clause."[13] *Wynne* was a case involving individual income tax provisions in Maryland and a Maryland resident individual who was the shareholder in an S corporation that was engaged in business in Maryland and other states. Maryland allowed its residents to claim a credit for taxes paid to other states against their Maryland "state" individual income tax, but did not allow the credit against what was called the "county tax." Although this second tax was referred to as the "county tax" it also was collected by the state, but the tax rate was based on the county in which the person resided. In *Wynne* the Court notes the result of not allowing a credit for taxes paid to other states against the county tax was "that some of the income earned by Maryland residents outside the State is taxed twice. Maryland's scheme creates an incentive for taxpayers to opt for intrastate rather than interstate economic activity." The Court goes on to find, "We . . .

---

[12] See Taxpayers' Prehearing Brief, pg. 9. For tax year 2012, this difference asserted by the Taxpayers was from $472,792 to $11,821 and for tax year 2013, the difference was from $506,761 to $11,051.

[13] Petitioners' Pre-Hearing Reply Brief, pg. 2.

hold that this feature of the State's tax scheme violates the Federal Constitution." *Id.* at 1792.

The Taxpayers point out that in reaching its decision in *Wynne,* the Court had stated, "We have long held that States cannot subject corporate income to tax schemes similar to Maryland's, and we see no reason why income earned by individuals should be treated less favorably." *Id.* at 1792. It is the Taxpayers' position that *Wynne* makes it clear that taxes imposed by a state on resident individuals are subject to the same constitutional restrictions as taxes imposed on a corporation and that a state tax on income taxable to a resident shareholder from activities by the S corporation in other jurisdictions is subject to the limitations imposed under the Commerce Clause.[14] The Taxpayers argue that Utah's individual income tax as it pertains to the Taxpayers, violates the Commerce Clause of the United States Constitution under the four part test set out in *Complete Auto Transit, Inc. v. Brady,* 430 U.S. 274 (1977). The Taxpayers also argue that the Utah tax law as it pertains to the Taxpayers, violates the Foreign Commerce Clause of the United States Constitution based on the decisions in *Container Corporation of America v. Franchise Tax Board,* 463 U.S. 159 (1983) and *Kraft General Foods, Inc. v. Iowa Dep't of Revenue and Finance,* 505 U.S. 71 (1992).

The Taxpayers argue that Utah Code Sec. 59-10-115 is a safety valve to solve these asserted constitutional flaws in the Utah Individual Income Tax Act. The Taxpayers acknowledge that the

---

[14] See Petitioners' Pre-Hearing Brief, pg. 13.

Division's interpretation of Utah Code Sec. 59-10-115 does not allow for an equitable adjustment in this matter because it is the Division's position that the equitable adjustment under Utah Code Sec. 59-10-115 is limited to situations where income is taxed twice by the State of Utah. However, the representatives for the Taxpayers argue the Taxpayers position to allow the equitable adjustment based on a double tax detriment from a different taxing jurisdiction is a plausible reading of the statute and that all the Taxpayers need to do is show that their alternative and constitutional reading is plausible and if plausible, the Commission must adopt it over the Division's reading which they assert is unconstitutional.[15]

It was the Division's position that the Taxpayers are asking that the Commission invalidate Utah Code Secs. 59-10-104 and 59-10-103 which impose an income tax on the state taxable income of Utah resident individuals and specifically define "state taxable income" to be the individual's federal "adjusted gross income." It was not disputed in this matter that the Taxpayers were Utah resident individuals during the tax years at issue and the income they are arguing that should be excluded from Utah income tax was income that the Taxpayers had included on their federal returns in their federal adjusted gross income. The Division argues that although an equitable adjustment is provided under Utah Code Sec. 5910-115 to adjusted

---

[15] The Taxpayers' representatives cite to *Elks Lodges No. 719 (Ogden) & No. 2021 (Moab) v. Dep't of Alcoholic Beverage Control,* 905 P.2d 1189, 1202 (Utah 1995).

gross income, it is only if the individual would otherwise "suffer a double tax detriment ***under this part*** (emphasis added)." The Division points out that "this part" refers to Part 1 of Chapter 10, Individual Income Tax Act. The Division indicates that the Tax Commission has uniformly interpreted this provision to limit the equitable adjustment to situations where the individual would be taxed twice by the State of Utah under Part 1 of the act, and did not allow the adjustment in situations where the individual was taxed only once by the State of Utah, but also taxed by a foreign jurisdiction or by another state on the same income. The Division cites to *Utah State Tax Commission Findings of Fact, Conclusions of Law and Final Decision, Appeal No. 08-0590* (August 5, 2010);[16] *Utah State Tax Commission Order, Appeal No. 05-1787* (September 5, 2006); *Utah State Tax Commission Initial Hearing Order, Appeal No. 12-915* (April 15, 2014); *Utah State Tax Commission Findings of Fact, Conclusions of Law, and Final Decision, Appeal No. 14-374* (November 11, 2015).[17]

---

[16] The Petitioners in *Appeal No. 08-0590* appealed the Commission's ruling to the Utah Third District Court, which upheld the Tax Commission's decision disallowing the equitable adjustment for income that was subject to tax in Canada. *See XXXX v. Utah State Tax Comm'n,* Case No. 100917302. The District Court ruling was appealed to the Utah Supreme Court, which sent the matter to the Utah Court of Appeals where it was eventually settled. *See XXXX v. Utah State Tax Comm 'n,* Case No. 20120708 (Utah Ct. App).

[17] See also *Utah State Tax Commission Initial Hearing Order Appeal No. 15-1332* (June 27, 2016). These and other decisions issued by the Utah State Tax Commission are available for review in a redacted format at tax.utah.gov/commission-office/decisions.

The Division's position is consistent with how the Utah State Tax Commission has interpreted and applied Utah Code Secs. 59-10-104, 59-10-103(1) and 59-10-115 in Utah for many years. Under Utah law, apportionment factors do not apply to a Utah resident individual for income tax purposes. Utah Code Secs. 59-10-104 and 59-10-103(1) impose a tax on a resident individual's state taxable income which is based on the individual's federal "adjusted gross income." Utah law does provide an equitable adjustment under Utah Code Sec. 59-10-115 to the federal adjusted gross income if the resident individual would receive a double tax detriment under Part 1 of the Utah Individual Income Tax Act. The Taxpayers' argument that they should be allowed to take an equitable adjustment on income that was also subject to tax by foreign jurisdictions has been specifically rejected by the Tax Commission over the years in the decisions noted above. The Tax Commission has been consistent in its application of these provisions. Under Utah Code Sec. 59-1-1417, the Commission must construe a statute providing an exemption or credit strictly against the taxpayer and the equitable adjustment is similar to an exemption or credit. The Taxpayers expansion of the equitable adjustment provided at Utah Code Sec. 59-10-115 to their income is not a plausible interpretation and without specific limitations would have a substantial impact on Utah's Individual Income Tax Act.

In order to find that the Taxpayers are entitled to take an equitable adjustment, the Tax Commission would have to expand the equitable adjustment beyond what the Utah Legislature has specifically

allowed at Utah Code Sec. 59-10-115.[18] The Tax Commission declines to do so, especially in light of the fact that the Utah Legislature has recently considered Utah Code Sec. 59-10-115 with respect to foreign source income and revised that section in a very limited and specific manner. Beginning with tax year 2017, the Utah Legislature adopted Utah Code Subsection 59-10-115(3) which enacts an equitable adjustment for taxable income of a pass through entity taxpayer in one specific industry, that being the heavy gauge metal tank industry. Certainly the Utah Legislature could have made this change more broadly applicable but chose not to do so. Additionally, if prior to this revision, Utah Code Sec. 5910-115 had been intended to be applied as broadly as the Taxpayers are arguing at this hearing, the provision allowing the adjustment for the metal tank industry would not have been necessary because it would already have been available for all industries generally on the foreign source pass through income.

Ultimately the Division is correct on the point that the Taxpayers' are requesting relief that would first require the Tax Commission to do something it lacks jurisdiction to do, invalidate Utah individual income tax provisions. The Utah Supreme Court has previously held that the Utah State Tax Commission lacks authority to determine the constitutionality of

---

[18] See *MacFarlane v. Utah State Tax Commission,* 2006 UT 25, ¶19, "(While we recognize the general rule that statutes granting credits must be strictly construed against the taxpayer, the construction must not defeat the purpose of the statute.)' The best evidence of that intent is the plain language of the statute." (Citing *Jensen v. Intermountain Health Care, Inc.,* 679 P.2d 903, 906 (Utah 1984).

Utah laws. *See Nebeker v. Tax Comm'n,* 2001 UT 74; 35 P.3d 180 (2001). Regardless, the Division points out that the State of Utah's individual income tax statutes already comply with the Court's decision in *Comptroller of Treasury of Maryland v. Wynne,* 135 S.Ct. 1787 (2015), because Utah allowed the credit for taxes paid to other states while Maryland did not provide for such a credit. The Taxpayers' arguments based on the decision in *Wynne* go far beyond what the Court actually held in that case. The Tax Commission should decline to expand its longstanding interpretation of Utah Code Sec. 59-10-115 or invalidate other provisions of the Utah Individual Income Tax Act based on the Taxpayers' assertions regarding the application or effect of the Court's holding in *Wynne.*

CONCLUSIONS OF LAW

1. The Utah Individual Income Tax Act imposes an income tax on the "state taxable income" of Utah resident individuals. Utah Code Subsection 59-10-104(1). "State taxable income" is specifically defined as the individual's federal adjusted gross income subject to certain additions, subtractions and adjustments. Utah Code Subsections 59-10-103(1)(a) & (w). These provisions tax the resident individual on income included in his or her federal adjusted gross income whether it comes from sources outside of Utah or sources from within the state. Utah law does allow under Utah Code Sec. 59-10-1003 a credit for taxes paid to other states and that has been allowed in this matter.

2. The Utah Legislature has provided an adjustment under Utah Code Sec. 59-10-115 to the

federal adjusted gross income if the resident individual suffers "a double tax detriment under this part." The Tax Commission consistently interpreted this equitable adjustment to apply only to situations where the individual would have been taxed twice on the same income by the state of Utah under the Part 1 of the Individual Income Tax Act and has not allowed this adjustment when the individual would be taxed once by Utah and also by a different government jurisdiction. *See Utah State Tax Commission Findings of Fact, Conclusions of Law and Final Decision, Appeal No. 08-0590* (August 5, 2010); *Utah State Tax Commission Order, Appeal No. 05-1787* (September 5, 2006); *Utah State Tax Commission Initial Hearing Order, Appeal No. 12-915* (April 15, 2014); *Utah State Tax Commission Findings of Fact, Conclusions of Law, and Final Decision, Appeal No. 14-374* (November 11, 2015); and *Utah State Tax Commission Initial Hearing Order Appeal No. 15-1332* (June 27, 2016). The Taxpayers argue they should be allowed to take this adjustment on income they included in their federal adjusted gross income, but which they argue was business income attributable to other states or countries. The Taxpayers' position is contrary to the statutory provisions and the Commission's consistent application of these provisions. The Utah Legislature has not expanded this adjustment generally to income attributable to foreign sources or income from states that do not assess an individual income tax.

3. The Taxpayers argument that their interpretation of Utah Code Sec. 59-10-115 is "plausible" and under *Elks Lodges No. 719 (Ogden) & No. 2021 (Moab) v. Dep't of Alcoholic Beverage*

Control, 905 P.2d 1189, 1202 (Utah 1995) should be upheld over the Division's interpretation is unpersuasive. The Taxpayers expansion of the equitable adjustment provided at Utah Code Sec. 59-10-115 to their income is not a plausible interpretation and without specific limitations would have a substantial impact on Utah's Individual Income Tax Act. The Utah Legislature has not provided an equitable adjustment or a credit applicable in this matter. In order to find for the Taxpayers, the Tax Commission would have to expand the credit beyond what the Utah Legislature has allowed and should decline to do so, especially in light of the fact that the Utah Legislature has recently looked at the statute, made a limited revision, but did not expand it in the manner the Taxpayers are requesting.

4. The Taxpayers argue that the imposition of Utah Individual Income Tax on business income they attribute to sources outside of Utah violates the Commerce Clause of the U.S. Constitution. The Utah State Tax Commission lacks authority to invalidate provisions of the Utah Individual Income Tax Act based on the constitutionality of Utah laws. *See Nebeker v. Tax Comm'n,* 2001 UT 74; 35 P.3d 180 (2001). Regardless, the Taxpayers' arguments based on the United States Supreme Court's decision in *Comptroller of Treasury of Md. v. Wynne,* 135 S.Ct. 1787 (US 2015) go far beyond what the Court actually held in that case.

After review of the facts and applicable law in this matter, the Taxpayers' appeal should be denied.

/s/ Jane Phan
Jane Phan
Administrative Law Judge

DECISION AND ORDER

Based on the foregoing, the Tax Commission denies the Taxpayers appeal pertaining to the individual income tax audit deficiencies for tax years 2011, 2012 and 2013. It is so ordered.

DATED this 15 day of November, 2016.

/s/ John L. Valentine	/s/ Michael J. Cragun
John L. Valentine	Michael J. Cragun
Commission Chair	Commissioner
/s/ Robert P. Pero	/s/ Rebecca L. Rockwell
Robert P. Pero	Rebecca L. Rockwell
Commissioner	Commissioner

Notice of Appeal Rights and Payment Requirement: Any balance due as a result of this order must be paid within thirty (30) days of the date of this order, or a late payment penalty could be assessed. You have twenty (20) days after the date of this order to file a Request for Reconsideration with the Tax Commission Appeals Unit pursuant to Utah Code Ann. §63G-4-302. A Request for Reconsideration must allege newly discovered evidence or a mistake of law or fact. If you do not file a Request for Reconsideration with the Commission, this order constitutes final agency action. You have thirty (30) days after the date of this order to pursue judicial review of this order in accordance with Utah Code Ann. §59-1-601 et seq. and §63G-4-401 et seq.

APPENDIX D

STATUTORY PROVISIONS INVOLVED

1. **Utah Code § 59-10-103 provides in pertinent part:**

Definitions

(1) As used in this chapter:

* * * * *

(w) "Taxable income" or "state taxable income":

(i) subject to Section 59-10-1404.5, for a resident individual, means the resident individual's adjusted gross income after making the:

(A) additions and subtractions required by Section 59-10-114; and

(B) adjustments required by Section 59-10-115;

(ii) for a nonresident individual, is an amount calculated by:

(A) determining the nonresident individual's adjusted gross income for the taxable year, after making the:

(I) additions and subtractions required by Section 59-10-114; and

(II) adjustments required by Section 59-10-115; and

(B) calculating the portion of the amount determined under Subsection (1)(w)(ii)(A) that

is derived from Utah sources in accordance with Section 59-10-117;

* * * * *

2. **Utah Code § 59-10-116 provides:**

Tax on nonresident individual--Calculation--Exemption

(1) Except as provided in Subsection (2), a tax is imposed on a nonresident individual in an amount equal to the product of the:

(a) nonresident individual's state taxable income; and

(b) percentage listed in Subsection 59-10-104(2).

(2) This section does not apply to a nonresident individual exempt from taxation under Section 59-10-104.1.

3. **Utah Code § 59-10-117 provides in pertinent part:**

State taxable income derived from Utah sources

(1) For purposes of Section 59-10-116, state taxable income derived from Utah sources includes state taxable income attributable to or resulting from:

* * * * *

(b) the carrying on of a business, trade, profession, or occupation in this state;

* * * * *

4. **Utah Code § 59-10-1003 provides:**

Tax credit for tax paid by individual to another state

(1) Except as provided in Subsection (2), a claimant, estate, or trust may claim a nonrefundable tax credit against the tax otherwise due under this chapter equal to the amount of the tax imposed:

(a) on that claimant, estate, or trust for the taxable year;

(b) by another state of the United States, the District of Columbia, or a possession of the United States; and

(c) on income:

(i) derived from sources within that other state of the United States, District of Columbia, or possession of the United States; and

(ii) if that income is also subject to tax under this chapter.

(2) A tax credit under this section may only be claimed by a:

(a) resident claimant;

(b) resident estate; or

(c) resident trust.

(3) The application of the tax credit provided under this section may not operate to reduce the tax payable under this chapter to an amount less than would have been payable were the income from the other state disregarded.

(4) The tax credit provided by this section shall be computed and claimed in accordance with rules prescribed by the commission.