No. ________

In The
Supreme Court of the United States

MMN INFRASTRUCTURE SERVICES, LLC,

Petitioner,

v.

MICHIGAN DEPARTMENT OF TREASURY,

Respondent.

On Petition For Writ Of Certiorari To The Michigan Supreme Court

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

This case concerns a state's attempt to tax a company's value based on de minimis, temporary contacts when that company is already subject to tax on such value in another state, an issue of national importance affecting interstate commerce, extraterritorial taxation, and a split among state courts of last resort.

Minnesota Limited, Inc., was a Minnesota company with a Minnesota headquarter and substantial assets in Minnesota. The corporation had almost no assets in Michigan. In 2011, Petitioner Vectren Infrastructure, n/k/a MMN Infrastructure Services, LLC, purchased Minnesota Limited in an asset sale. The gain on the sale of the enterprise made up \$51 million of the company's \$55 million income, about 93%, which the company rightly attributed to out-of-state economic activity.

The enterprise sale occurred at the end of March, resulting in a three-month "short tax year" filing. During those three months, its offseason, Minnesota Limited was engaged in the cleanup of an oil spill in Michigan. The State of Michigan used those anomalies to claim 70% of the taxable value *of the entire company*, refusing to apportion the enterprise-sale income to out-of-state activity. The Michigan Supreme Court's 4–3 decision upholding that tax assessment raises two questions for this Court's review:

1. Whether, to comply with the requirements of fair apportionment and the prohibition on extraterritorial taxation, a state must include in its state tax

QUESTIONS PRESENTED—Continued

apportionment formula the factors of a business giving rise to income to be taxed.

2. Whether factor representation includes a temporal element.

PARTIES TO THE PROCEEDING AND CORPORATE DISCLOSURE STATEMENT

Petitioner MMN Infrastructure Services, LLC (MMN), is the successor-in-interest to Vectren Infrastructure Services Corp. (Vectren), the plaintiff below, which itself was the successor-in-interest to Minnesota Limited, Inc.

Minnesota Limited, Inc., was converted to a limited liability company, Minnesota Limited, LLC, on March 31, 2011, the date of the sale of the company. Vectren, an Indiana corporation, was the sole shareholder, and transferred its interest to a wholly owned subsidiary, Vectren Utility Service, Inc., an Indiana corporation.

On February 3, 2020, PowerTeam Services, LLC, a Delaware limited liability company, acquired all issued and outstanding common stock of Vectren from Vectren Utility Service, Inc. Vectren was converted (with a name change) to a limited liability company, MMN, on April 6, 2020. The current sole member of MMN is Artera Services, LLC f/k/a PowerTeam Services, LLC. PowerTeam Services, LLC changed its name to Artera Services, LLC, on July 27, 2020.

Respondent is the Michigan Department of Treasury.

LIST OF ALL PROCEEDINGS

Michigan Supreme Court, Case No. 163742, *Vectren Infrastructure Services Corp. v. Department of Treasury*, Opinion issued July 31, 2023.

Michigan Supreme Court, Case No. 163742, *Vectren Infrastructure Services Corp., successor-in-interest to Minnesota Limited, Inc. v. Department of Treasury*, Order issued March 23, 2022.

Michigan Court of Appeals, Case No. 35462, *Vectren Infrastructure Services Corp., successor-in-interest to Minnesota Limited, Inc. v. Department of Treasury*, Opinion issued September 30, 2021.

Michigan Court of Claims, Case No. 17-000107-MT, *Vectren Infrastructure Services Corp., successor-in-interest to Minnesota Limited, Inc. v. Department of Treasury*, Opinion issued May 25, 2021.

Michigan Supreme Court Order, Case No. 161422, *Vectren Infrastructure Services Corp., successor-in-interest to Minnesota Limited, Inc. v. Department of Treasury*, Order issued November 25, 2020.

Michigan Court of Appeals, Case No. 35462, *Vectren Infrastructure Services Corp., successor-in-interest to Minnesota Limited, Inc. v. Department of Treasury*, Opinion issued March 12, 2020.

Michigan Court of Claims, Case No. 17-000107-MT, *Vectren Infrastructure Services Corp., successor of Minnesota Limited, Inc. v. Department of Treasury*, Opinion issued August 14, 2018.

TABLE OF CONTENTS

TABLE OF CONTENTS—Continued

TABLE OF CONTENTS—Continued

Page

TABLE OF AUTHORITIES

Page

CASES

TABLE OF AUTHORITIES—Continued

TABLE OF AUTHORITIES—Continued

Page

Constitutional Provisions

Statutes

TABLE OF AUTHORITIES—Continued

Page

OTHER AUTHORITIES

DECISIONS BELOW

The opinion of the Michigan Supreme Court is not yet reported but is available at 2023 WL 4874684 and reprinted at App. 1. The first opinion of the Michigan Court of Appeals is reported at 331 Mich. App. 568 and reprinted at App. 164, and the second opinion of the Michigan Court of Appeals is reported at 339 Mich. App. 117 and reprinted at App. 143. The first opinion of the Michigan Court of Claims is not reported but is available at 2018 WL 10563275 and is reprinted at App. 183, and the second opinion of the Michigan Court of Claims is not reported but is available at 2021 WL 3923834 and reprinted at App. 149.

STATEMENT OF JURISDICTION

Petitioner timely files this petition from the Michigan Supreme Court's July 31, 2023 decision. This Court has jurisdiction under 28 U.S.C. § 1257(a).

PERTINENT CONSTITUTIONAL AND STATUTORY PROVISIONS

The Commerce Clause of the United States Constitution, U.S. Const., art. I, § 8, cl.3 provides: "The Congress shall have Power to regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes[.]"

The Due Process Clause of the Fourteenth Amendment to the United States Constitution, U.S. Const., amend. XIV, § 1, provides: "[N]or shall any State deprive any person of life, liberty, or property, without due process of law. . . ."

Michigan Compiled Law § 208.1309 states:

(1) If the apportionment provisions of this act do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for or the treasurer may require the following, with respect to all or a portion of the taxpayer's business activity, if reasonable:

> (a) Separate accounting.
>
> (b) The inclusion of 1 or more additional or alternative factors that will fairly represent the taxpayer's business activity in this state.
>
> (c) The use of any other method to effectuate an equitable allocation and apportionment of the taxpayer's tax base.

(2) An alternate method may be used only if it is approved by the department.

(3) The apportionment provisions of this act shall be rebuttably presumed to fairly represent the business activity attributed to the taxpayer in this state, taken as a whole and without a separate examination of the specific elements of either tax base unless it can be demonstrated that the business activity attributed to the taxpayer in this state is out of all

appropriate proportion to the actual business activity transacted in this state and leads to a grossly distorted result or would operate unconstitutionally to tax the extraterritorial activity of the taxpayer.

(4) The filing of a return or an amended return is not considered a petition for the purposes of subsection (1).

INTRODUCTION

The Michigan Supreme Court's 4–3 decision shatters this Court's judicial teachings regarding fair apportionment and extraterritorial taxation, *see Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113 (1920); *Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell*, 283 U.S. 123 (1931); *Norfolk & Western Ry. Co. v. Missouri State Tax Comm'n*, 390 U.S. 317 (1968), while exacerbating existing conflicts with state courts of last resort over how to tax the income of companies that do business in multiple states. Certiorari is warranted.

When a unitary business does business in multiple states, a taxing state may calculate the taxes owed to it by "apportioning" income to that state. To do this, the state uses an apportionment formula. Historically, states used an equally weighted, three-factor formula, consisting of a property factor, a payroll factor, and a sales factor. First, the state calculates a ratio for the company's property, payroll, and sales based on in-state versus total business activity. Next, the state calculates the average of the ratios. Finally, the average is multiplied by the entity's income subject to apportionment. The result is the amount of business income to be taxed by the state.

Take a simple example based on a hypothetical company based in State Y that does business in State Z, which uses all three apportionment factors. If 10% of the company's sales are to State Z customers, 3% of the company's real and personal property is in State Z, and 2% of the company's payroll is paid to State Z residents, then 5% of the company's apportionable base income [(10 + 3 + 2) / 3] may be attributed to State Z and is subject to State Z's business tax.

As this Court has recognized, the Commerce and Due Process Clauses place limits on how much a state can tax that hypothetical company. For example, if Michigan was State Z and tried to tax 70% of the company's income rather than 5%, the rational relationship between the tax and Michigan business activity would be destroyed, and a court must invalidate it.

Yet that is exactly what happened here. Minnesota Limited built a large business with substantial assets, employees, and contracts in Minnesota. While the company sporadically performed work in Michigan, that activity constituted a small fraction of its business.

In spring 2011, the two shareholders of Minnesota Limited sold the company to Petitioner in an asset sale, with Vectren becoming Minnesota Limited's successor-in-interest, responsible for business taxes owed from January 1 to March 31, 2011. Minnesota Limited reported a $51 million gain on the sale, roughly 93% of the company's $55 million taxable income for that short-year period. The remaining $4 million of income earned that year was from its daily operations. Michigan, like many states, uses an apportionment formula that has only one factor—the sales ratio. Because most of Minnesota Limited's assets were located outside of Michigan, the company computed its sales factor by putting the $51 million as well as sales revenue from daily operations in the denominator, and including only the enterprise value from assets located in Michigan at the time of the sale as well as sales revenue from Michigan daily operations in the numerator, like this:

$$\text{Sales ratio} = \frac{\text{Value of Michigan assets + revenue from Michigan operations}}{\text{Total value of assets + revenue from operations everywhere}}$$

The result was that 14.986% of the company's sales for the 2011 short tax year was attributable to Michigan. And even that number was artificially inflated by an oil-spill cleanup that Minnesota Limited was contracted to undertake in Michigan in late 2010 to early 2011, the company's normal offseason, resulting in a sales ratio that was "over four times the company's attribution of sales to Michigan prior to" that contract. App. 86 (Zahra, J., dissenting).

Respondent Michigan Department of Treasury, in an approach which defied this Court's binding precedence, determined that it could tax the entirety of Minnesota Limited's enterprise value from the sale while at the same time excluding the enterprise value from the apportionment formula. It computed the sales ratio like this:

$$\text{Sales ratio} = \frac{\text{Revenue from Michigan operations}}{\text{Revenue from operations everywhere}}$$

By ignoring the sale of the company and taking advantage of the one-time bump in the company's Michigan activity due to the oil spill cleanup, the Department's calculated sales ratio attributed 69.9571% of the company's total income to Michigan. In other words, even though Minnesota Limited was built, maintained, and located almost entirely in Minnesota, and even though Michigan had virtually nothing to do with Minnesota Limited's enterprise value, Michigan claimed the right to tax *70% of the company's enterprise sale proceeds*. App. 10 ("Treasury determined that the sales factor should have been 69.9571% [and] the apportioned tax base should have been $38,316,659.").

The dissenting Michigan Supreme Court Justices understood that the majority's ruling raised constitutional concerns, stating "[i]f the United States Constitution's prohibition on disproportionate taxation of out-of-state activity is to retain viable force, this tax cannot withstand constitutional scrutiny." App. 71 (Zahra, J., dissenting). Indeed, "[i]f the Department's tax apportionment is permitted, this state and others will continue to extend their reach further and further into out-of-state activities." *Ibid.* "States will compete for more and more dollars flowing outside their borders. This will come at the cost of state sovereignty and the consistent and predictable administration of interstate commerce." *Ibid.*

The glaring inequity is unprecedented and unworkable; if every state where a company had some sporadic activity tried to tax 70% of the enterprise value, interstate commerce itself would be jeopardized. Moreover, Michigan is the only state on record to refuse to consider where enterprise value was generated. And while several other states properly recognize that this Court's precedent requires what Michigan did not do, even among these states, there are different approaches which would merit clarification by this Court.

The first question presented is whether factors of a business giving rise to income to be taxed must be represented in a state's apportionment formula. Here, Michigan taxed Minnesota Limited's enterprise value but failed to consider the state to which most that income was attributable: Minnesota. Instead, Michigan excluded the enterprise value amount entirely from the sales factor computation. Conversely, Wisconsin, Maine, Mississippi, and Rhode Island unequivocally require factor representation and have struck down formulas that lack it. Minnesota and New Mexico question whether factor representation is constitutionally required. And Maryland and Tennessee refuse to extend factor representation beyond subsidiary dividends. Michigan is the only state to refuse to even consider an alternative apportionment formula with factor representation to avoid distortion.

The second question presented is whether factor representation must include a temporal element. Here, Minnesota Limited's sales ratio was distorted by the fact that it was only reporting income from January 1 to March 31 in the applicable tax year, the company's offseason. Had Michigan accounted for the fact that the company generates most of its sales over the summer months in states outside of Michigan, Michigan's calculation of the sales ratio would have looked very different. In contrast, Maine has held in similar circumstances that the taxing authority should look at recent full-year apportionment ratios to ensure the short-year ratio is not out of whack.

This case is an ideal vehicle to resolve those conflicts. The material facts are not in dispute, and the Michigan Supreme Court's majority and dissenting opinions clearly frame the constitutional issues at stake. Moreover, this Court has long recognized the Constitution's limitations on a state's power to tax—a necessary bulwark against economic Balkanization among the states. The decision below is not only wrong, but dangerous, opening the door to "increasing taxation by the States well beyond their territorial borders" to the disfavor of a "sound and consistent system of interstate commerce." App. 131 (Zahra, J., dissenting).

There is an essential need for the Court's guidance. If every state, based on the tiniest contact, sought to tax enterprise value, such action would impede interstate commerce. A tax system is unsustainable where there is no rational connection between a company's tax burden and its activity within a taxing state and where, instead, a state uses a small subset of in-state activities to tax a company's enterprise value achieved nearly wholly from out-of-state activities. The Michigan Supreme Court majority justified its unprecedented approach based on a speculative projection of how company assets might possibly be used in Michigan in the future, which is wholly arbitrary. App. 125 (Zahra, J., dissenting). If Michigan is permitted to do this, other states also seeking greater tax revenue will follow. Such speculation will incentivize other states to create and impose apportionment formulae that "completely fail to consider whether the profits from the sale were in any 'just sense attributable to transactions within' " the state. App. 136 (Viviano, J., dissenting).

Accordingly, the Court should grant the petition, resolve the conflicts, and reverse the Michigan Supreme Court. Alternatively, and at a bare minimum, the Court should summarily reverse because Michigan's tax assessment does not comport with any reasonable construction of the Commerce and Due Process Clauses.

STATEMENT OF THE CASE

I. Court precedent limits state power to tax

Recognizing the difficulty that interstate businesses present for state tax authorities, this Court has "developed the unitary business principle." *MeadWestvaco Corp. v. Ill. Dep't of Revenue*, 553 U.S. 16, 25 (2008). Under that principle, "a State need not isolate the intrastate income-producing activities from the rest of the business but may tax an apportioned sum of the corporation's multistate business if the business is unitary." *Id.* (cleaned up).

But the unitary business principle has clear constitutional limits. "The Commerce Clause and the Due Process Clause impose distinct but parallel limitations on a State's power to tax out-of-state activities." *MeadWestvaco*, 553 U.S. at 24. Specifically, "[t]he Due Process Clause demands that there exist some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax, *as well as a rational relationship between the tax and the values connected with the taxing State*." *Id.* (emphasis added) (cleaned up). Separately, the Commerce Clause, "forbids the States to levy taxes that discriminate against interstate commerce or that burden it by subjecting activities to multiple or *unfairly apportioned* taxation." *Id.* (emphasis added) (citations omitted).

"The broad inquiry subsumed in both constitutional requirements is whether the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the state. . . ." *MeadWestvaco*, 553 U.S. at 24–25 (cleaned up).

II. Taxpayer was Minnesota-based, with limited business in Michigan

Minnesota Limited, an S-corporation, was a family-owned business in Big Lake, Minnesota, where most of its facilities were located. Reuben Leines, father of Christopher Leines and Paulette Britzius, started the business in 1966. App. 72. Minnesota Limited constructed oil and gas pipelines to transport natural gas, crude oil, and petroleum products, and primarily performed its services in Minnesota and the upper Midwest, i.e., Wisconsin, Iowa, and North and South Dakota. App. 73. The company rarely performed work in Michigan and had no facilities there. App. 79; 110. For the decade preceding the sale of the Company in 2011, its average sales to Michigan were 6.9% of total company sales, and Michigan sales never exceeded 18.3% in any year. App. 47.

Chris and Paulette succeeded Reuben as owners in the late 90's. App. 7. By the time Chris and Paulette sold their shares of the business in 2011 due to Paulette's health, the company had 700 employees. App. 165. Vectren allocated the purchase price as follows: approximately $34.4 million to tangible assets (construction, transportation, and office equipment and certain buildings), approximately $22.8 million to intangible assets, and approximately $16.6 million to goodwill. App. 83.

In 2010, the year before the sale, a new customer, Enbridge, selected Minnesota Limited to perform a hazardous material clean-up project. This was Minnesota Limited's largest ever project in Michigan which took place during the company's 2010 to 2011 off-season. App. 45.

Minnesota Limited sent ten employees and five pieces of equipment to Michigan to perform the Enbridge project; all other equipment was rented, and local laborers hired. App. 79. When the business was sold, the only Michigan work Minnesota Limited had outstanding was the tail end of the Enbridge project. App. 82.

III. Proceedings below

As S-corporation shareholders, Chris and Paulette reported their gain on federal and state returns prepared by a tax professional and paid their taxes due. App. 187. For the Michigan Business Tax filing, Petitioner sought to use an alternative apportionment formula, as the standard formula resulted in an unreasonable 70% of the enterprise value sourced to Michigan. App. 87–88. Michigan denied the request and excluded *all* the gain from the sales factor calculation. As a result, the ratio apportioning income to Michigan soared from 14.99% to 70%. App. 55. This was due to not only the removal of the gain from the sales factor, but also use of the short year during which Minnesota Limited was engaged in the Michigan cleanup while its other operations were idle. Yet Michigan did *not* remove the enterprise value from the tax base. App. 151.

Michigan issued a Final Assessment, asserting that Petitioner must use the standard apportionment formula rather than an alternative method. Petitioner filed an action in the Michigan Court of Claims, asserting that application of the standard apportionment formula resulted in extraterritorial taxation, was unfair apportionment, and failed to recognize how the gain was earned—predominantly in states other than Michigan. App. 11–12.

On cross-motions for summary disposition, the Court of Claims disagreed with Petitioner's apportionment argument. The Court of Claims noted that the "sale was expressly reported to the shareholders as a sale of the S-Corp's assets," and that "the §338(h)(1) election controls the outcome of this case." App. 191. Yet, the Court of Claims failed to apply this finding to source the enterprise value based on the location of Petitioner's assets at the time of the sale. App. 194. The Court of Claims inaccurately stated "while plaintiff generally frames its argument in this manner [that the apportionment formula as applied to the sale was out of all appropriate proportion to the business and activities conducted in Michigan], the crux of plaintiff's contention is really with the computation of its tax base. App. 192. This misconstruction of the pleadings was further emphasized by the Court of Claims when it summarized, "this type of argument is not concerned with the result or constitutionality of the apportionment formula, but it is simply a disagreement with the computation of [Plaintiff's] tax base." *Ibid*.

Petitioner's request for alternative apportionment was dismissed.

The Michigan Court of Appeals reversed, holding that application of the statutory formula "would result in the imposition of a tax in violation of the Commerce Clause," and that the use of an alternative formula "would be necessary to avoid the constitutional violation." App. 171. In doing so, the Court of Appeals affirmed these well-established principles of when alternative apportionment is required:

1. An apportionment formula must determine the portion of income "fairly attributed to in-state activities";

2. Fairness "must actually reflect a reasonable sense of how the income is generated";

3. A state may not tax more than its fair share of interstate commerce; and

4. A taxpayer may rebut the presumption that the statutory apportionment is fair by showing by "clear and cogent evidence" that the business activity transacted in this state leads to a grossly distorted result, or alternatively, the apportionment formula would operate unconstitutionally to tax the extraterritorial activity of the taxpayer. App. 172–175.

The Court of Appeals concluded that Petitioner had "presented clear and cogent evidence that the statutory formula, as applied, attributed business activity to Michigan "out of all appropriate proportion to the actual business actively transacted in the state" and led to a grossly distorted result and operated to unconstitutionally tax extraterritorial activity. App. 178. The court recognized that "the value of the business and its assets was built up over many years and attributable to activity in many states." App. 173. And the court observed that "much of the activity and assets involved in the Sale never had any connection to Michigan." *Ibid*. In sum, the "majority of the activities making up [Minnesota Limited's] fair market value at the time of the Sale had occurred outside Michigan's borders." App. 179.

Michigan filed an Application for Leave to the Michigan Supreme Court. App. 144. Instead of reviewing, the Court issued an November 25, 2020 order vacating the Court of Appeals' decision and remanding to the Court of Appeals to address the issue of the lack of factor representation, as well as issues not the subject of this Petition. App. 162. The Court of Appeals remanded to the Court of Claims.

The Court of Claims, without a hearing, issued its opinion on remand on May 25, 2021, adopting Michigan's position without analyzing whether such interpretation would have an unconstitutional effect. App. 149. Having retained jurisdiction, on September 30, 2021, the Court of Appeals issued its published opinion after remand, reaffirming its earlier decision that held Michigan's application of the standard apportionment formula was unconstitutional and that, "[a]n alternate method of apportionment must be adopted." App. 148. The court remanded to the Court of Claims "with directions to determine an appropriate apportionment method if the parties are unable to agree upon one." *Ibid*.

Michigan filed a second Application for Leave to the Michigan Supreme Court, which granted oral argument on the application and requested briefing as to (1) whether the taxpayer established that "the business activity attributed to it in this state 'is out of all appropriate proportion to the actual business activity transacted in this state and leads to a grossly distorted result' "; (2) whether application of the statutory formula runs afoul of the Due Process and Commerce Clauses; and (3) whether remand to determine an alternate method of apportionment conflicts with MCL 208.1309(2). App. 141–142.

The Michigan Supreme Court issued its Opinion on July 31, 2023, and reversed in a 4–3 decision. The court held that (1) the income from the sale was properly attributable to Michigan under the MBTA, and (2) the MBTA formula, as applied, did not impermissibly tax income outside the scope of Michigan's taxing powers. App. 2–3. The majority agreed with the State's position that the proceeds from the sale of the business should not be included in the sales factor, and that no constitutional distortion was evident. App. 59. The majority justified this result by speculating that the company's assets could be used in Michigan in the future. App 64. Having conclusively and finally resolved the federal question presented, the court remanded to the Court of Claims for further proceedings. App. 68.

Justice Zahra issued a blistering dissent joined by Chief Justice Clement and supported by Justice Viviano, emphasizing why the Majority validated an unconstitutional apportionment scheme. App. 71 (Zahra, J., dissenting); App. 132 (Viviano, J., dissenting). He explained, "Constitutional principles drawn from Due Process and the Commerce Clause support the notion that states cannot regulate, control, or otherwise make illegal actions or behavior that occur wholly outside of the state. This rule protects individuals from shifting and competing laws, provides consistency and predictability in out-of-state activities, and preempts reprisals and capricious government behavior." App. 93.

Justice Zahra concluded the tax ran afoul of these principles as Michigan claimed 70% of MLI's value is subject to tax even though MLI "had no real property, physical assets, permanent labor, or intangible property permanently located in Michigan." App. 79; 100. The company "had no physical structures, it had no facilities, and it had no warehouses in the state." App. 101. "The infrastructure and physical structures by which the corporation was run, i.e., the company's base of operations, was located entirely outside of Michigan. Yet no apportionment was given to account for these dispersed, out-of-state physical properties." App. 102.

Justice Zahra highlighted that "[w]hile Michigan could tax a reasonable apportionment of value provided within the state by the equipment, such as through property taxes or other consumption taxes, Michigan cannot apply a 70% allocation of equipment sales occurring wholly outside of its jurisdiction," App. 103, "when the company owned 1,195 pieces of equipment and only five pieces were in Michigan." App. 102. In addition, Michigan cannot tax labor that occurs outside of its boundaries. Only 10 out of 600 employees entered the state during the tax measurement period. App. 105.

Judge Zahra also criticized the majority for ignoring the available record and relying heavily on presumptions on how the purchased equipment could be used in the future. App. 117–118; 121. "This is confounding given that almost none of ML's historical activities occurred in Michigan, including in the immediate years leading up to the sale." App. 122. He emphasized Michigan's tax calculation resulted in a 400% increase in the calculated sales ratio—a more than 900% increase over the company's recent sales history in Michigan. App. 115. And he concluded that the application of Michigan's formula was unconstitutional. *Ibid*.

REASONS FOR GRANTING THE WRIT

I. The Michigan Supreme Court's decision exacerbates a substantial conflict among the lower courts over the proper apportionment of a multi-state business's income.

This Court has expressly left open questions concerning the necessity of factor representation in state tax apportionment. While Justice Stevens would have decided the issue in *Mobil Oil Corp. v. Commissioner of Taxes of Vermont*, 445 U.S. 425 (1980), *see id.* at 461 (Stevens, J., dissenting) ("Unless the sales, payroll, and property values connected with the production of income by the payor corporations are added to the denominator of the apportionment formula, the inclusion of earnings attributable to those corporations in the apportionable tax base will inevitably cause [the corporation's] income to be overstated."), the majority declined. And in *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159, 169–70 (1983), while the Court explained that the factors used must reflect a reasonable sense of how income is generated, it stopped short of requiring factor representation in apportionment.

Since those decisions, the Court has denied certiorari in several cases that have sought guidance on factor representation. The resulting vacuum has led to inconsistent application of this Court's fair apportionment tests under the Due Process and Commerce Clauses of the Constitution.

The 4–3 decision below exacerbates the conflict among the states over the proper apportionment of a multistate business's income. Michigan is the only state on record to refuse to even consider an alternative apportionment formula with factor representation to avoid distortion. Wisconsin, Maine, Mississippi, and Rhode Island unequivocally require factor representation and have struck down formulas that lack it. Minnesota and New Mexico question whether factor representation is constitutionally required. And

Maryland and Tennessee refuse to extend the concept beyond subsidiary dividends. Other states have recognized the inherent rationality of factor representation but have not ruled on the extent to which it is required. The Court should grant the petition and resolve the conflict.

A. The asymmetry of including gain in the tax base, while excluding such gain from the apportionment factor, violates the constitutional requirement of fair apportionment.

The Due Process Clause of the Fourteenth Amendment and the Commerce Clause of the U.S. Constitution, U.S. Const., art. I, § 8, cl.3, impose distinct but parallel limitations on a state's power to tax out-of-state activities. As noted above, in *MeadWestvaco*, this Court summarized these limitations as requiring "a rational relationship between the tax and the values connected with the taxing State" and prohibiting "unfairly apportioned taxation." 553 U.S. at 24 (citations omitted).

These limitations mandate that a state may not, when imposing an income tax, "tax value earned outside of its borders." *ASARCO Inc. v. Idaho State Tax Comm'n*, 458 U.S. 307, 315 (1982). The fundamental requirement is there must be "a 'minimal connection between the interstate activities and the taxing State,' and there must be a rational relation between the income attributed to the taxing State and the intrastate value of the corporate business." *Allied-Signal, Inc. v. Director, Div. of Tax'n*, 504 U.S. 768, 772 (1992) (citations omitted).

In apportioning the income of a multistate business, a state must apply an apportionment formula that "under both the Due Process and Commerce Clauses [is] fair." *Container Corp.*, 463 U.S. at 169. A component of fairness in an apportionment formula is a requirement of external consistency, that requires that "the factor or factors used in the . . . formula must actually reflect a reasonable sense of how income is generated." *Id. Accord*, *e.g.*, *Okla. Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175, 185 (1995).[1] External consistency looks to the economic justification of whether "a State's tax reaches beyond that portion of value that is fairly attributable to economic activity within the taxing State." *Id.*

None of the enterprise gain which Michigan seeks to tax is included in the statutory apportionment formula, resulting in both a lack of any rational sense of how the income was generated and extraterritorial taxation. As Michigan includes only income from direct-to-consumer sales (i.e., income from daily operations) in its formula and excludes all the gain from the sale of the business enterprise (whether real, tangible, or intangible), there is no factor representation to link Michigan's purported "apportioned share" of the

[1] Petitioner does not contest the component of internal consistency, which looks to determine if the formula, if applied by all jurisdictions, would result in no more than all a business's income being tax. *Container Corp.*, 463 U.S. at 169.

income to the activities which gave rise to the income. While recognizing that inclusion of the enterprise value may not produce a precise value attributable to Michigan, the *absence of any representation* cannot comport with this Court's established notions of fairness since it results in an unapportioned tax on interstate commerce. *See J.D. Adams Mfg. Co. v. Storen*, 304 U.S. 307, 310–11 (1938) (tax on income without proper consideration of the location of the property sold was unconstitutional); *Miller Bros. Co. v. Md.*, 347 U.S. 340, 343 (1954) (where no jurisdiction to property exists, the imposition of a tax on such property would be ultra vires and void).

It is patently unfair for Michigan to tax greater than 95% of tangible assets, 100% of real property and facilities, and 100% of intangibles—all of which were located out of state and lacked any meaningful connection with the State. None of the enterprise value attributed to these assets was due to economic value created from Michigan activities, making Michigan's apportionment formula contrary to Due Process. While the dissent made this clear, the majority cannot show why its result is fair.

The state courts that have considered this asymmetry are in conflict. In *Tambrands, Inc. v. State Tax Assessor*, 595 A.2d 1039 (Me. 1991), Maine sought to tax dividends received by the taxpayer from foreign subsidiaries without including any part of the subsidiaries' activity in that state's apportionment factors. On review, the Maine Supreme Court struck down the tax and held that excluding the business activity of the foreign affiliates created an impermissible distortion: "The ineluctable result is that more of the business activity of the unitary business is attributed to Maine than is the actual case. Thus, the income taxable by Maine under the Assessor's formula does not truly reflect Tambrands' connection with Maine and fails to meet the test of fairness required by the due process clause." *Id.* at 1044. The court made clear that the state could not constitutionally include the subsidiary income in the taxpayer's tax base yet apportion the company's Maine tax liability by ignoring the subsidiary-income factors when calculating the apportionment ratio. *Id*. at 1044–45.

The Rhode Island Supreme has reached the same conclusion. In *Homart Development Co. v. Norberg*, 529 A.2d 115 (R.I. 1987), the taxpayer received income from several partnerships in addition to earning income from its own operations within and without Rhode Island. Like Maine, Rhode Island included the partnership income in the company's tax base but excluded the partnership-income factors when calculating the apportionment ratio.

The Rhode Island Supreme Court held that this created "a manifestly inherent distortion of the amount of business activity conducted in this state," considering that the partnerships did no business in Rhode Island. *Id*. at 120. The court recognized that the distributive share income arose from the partnerships' business activities outside Rhode Island and excluding that activity from the apportionment formula is therefore manifestly inequitable. *Id*. at 121 ("[t]he inclusion of this income in Homart's net income calculation for apportionment purposes necessarily requires that the payroll, property, and receipt factors that gave rise to it be included in the apportionment equation also").

The Mississippi Supreme Court has held similarly. In *Mississippi Department of Revenue v. Comcast of Georgia/Virginia, Inc.*, 300 So.3d 532 (Miss. 2020), the tax agency's assessment failed to account for the apportionment factors of the taxpayer's unitary subsidiaries in apportioning its capital tax base. As a result, Mississippi sought to tax about 340% more out-of-state value than the alternative apportionment method offered by the taxpayer. The court ruled the lack of factor representation resulted in a distortion in favor of the state by overattributing income. *Id*. at 541. "Such a mismatch does not reflect a rational relationship between the values being taxed and the activities giving rise to the values." *Ibid*.

The same is true in Wisconsin. Consider *American Telephone & Telegraph Co. v. Wisconsin Department of Revenue*, 422 N.W.2d 629 (Wis. Ct. App. 1988), review denied, 428 N.W.2d 554 (Wis. 1988). Observing that the taxpayer's apportionable income included $500 million from Wisconsin operations and $3 billion of intangible income from subsidiaries—most of which did no business in the state—the Wisconsin Court of Appeals held that the state's decision to exclude the intangible-income factors from the apportionment formula "does not reflect a reasonable sense of how AT&T's income is generated and taxes value earned outside the borders of Wisconsin, contrary to . . . the due process and commerce clauses of the United States Constitution." *Id*. at 636. The State was required to include the intangible income in the apportionment formula if it wanted to tax it.

In contrast, the Supreme Court in Minnesota (where Minnesota Limited had its commercial domicile) has questioned whether symmetry between a tax base and the factors used to apportion is constitutionally required. In *NCR Corp. v. Commissioner of Revenue*, 438 N.W.2d 86 (Minn. 1989), the Minnesota Supreme Court upheld a tax on foreign dividends despite the State's decision to exclude the foreign-dividends factor from the apportionment formula. The court held that the 23% disparity between the state's apportionment formula and the taxpayer's formula was within the acceptable constitutional margin of error and "certainly does not approach the disparity the Supreme Court of the United States found constitutionally unacceptable in *Hans Rees*." *Id*. at 93.

Similarly, in *NCR Corp. v. Taxation & Revenue Department*, 856 P.2d 982 (N.M. Ct. App. 1993), which involved identical facts, the New Mexico Court of Appeals—without any discussion or analysis of whether the factors used to apportion the taxpayer's income accurately represented its activity in the state—ruled that the taxpayer had not met its burden of proving that the tax was unfairly apportioned under the test specified in *Container Corp*. *Id*. *Accord*, *e.g.*, *Caterpillar, Inc. v. N.H. Dep't. of Revenue*, 741 A.2d 56 (N.H. 1999).

Adding to this chaos and inconsistency are the rulings of the state court of last resort in Maryland and the intermediate appellate court in Tennessee, which have refused to require factor representation outside the subsidiary dividend context. In *NCR Corp. v. Comptroller of Treasury, Income Tax Division*, 544 A.2d 764 (Md. 1988), the Maryland Comptroller sought to include dividends and royalties from foreign affiliates in the tax base without those factors' representation in the apportionment formula. The Court of Appeals (now the Maryland Supreme Court), rejected the taxpayer's due-process challenge with respect to royalties, ruling that licensing trademarks to affiliates is no different from licensing trademarks to unrelated parties. Thus, there is no more basis for factor representation than there would be for the sale of machinery to an unrelated party. *Id*. at 781 (remanding for the Comptroller to consider whether gross distortion existed with respect to the dividends).

Likewise, in *H.J. Heinz Co., L.P. v. Chumley*, No. M2010-00202-COA-R3CV, 2011 WL 2569755, at *1 (Tenn. Ct. App. June 28, 2011), the intermediate appellate court in Tennessee declined to require factor representation for investment partnership income. Although the court was "not insensitive to the logic of Justice Stevens' dissent in *Mobil Oil*," it held that "the nature of the income addressed in *Mobil Oil* is distinguishable from the disputed income in this case." *Id*. at *12.

In providing still a different, and inconsistent approach, Pennsylvania's and South Carolina's Supreme

Courts recognize the inherent value of factor representation but do not require it unless the asymmetry produces a gross distortion in comparison to the statutory formula. In *Unisys Corp. v. Commonwealth, Board of Finance and Revenue*, 812 A.2d 448 (Pa. 2002), the Pennsylvania Supreme Court noted that this Court's focus in applying the external consistency test has been the degree of disparity between taxation under the state's formula and some more neutral baseline measure. *Id*. at 461. Because the taxpayer failed to establish such distortion, the taxpayer had not met its burden of proving an unfair apportionment. *Id*. at 465–66.

And in *NCR Corp. v. South Carolina Tax Commission*, 439 S.E.2d 254 (S.C. 1993), the taxpayer challenged the lack of factor representation for royalty and interest income. After first ruling that fair apportionment does not require full inclusion of the subsidiaries' factors and remanding to determine what proportion of the subsidiaries' activity was used to generate royalty and interest income, the South Carolina Supreme Court held that a 28% disparity between the statutory formula and a baseline comparison was not an unconstitutional distortion. *Id*. at 257.

In sum, the state courts that have addressed the issue of factor representation have been wildly inconsistent when requiring that factors giving rise to the taxable base income be fairly represented in that state's apportionment formula so that the formula is related to how the income was earned or related to the activities conducted in the state. This alone shows the essential importance of clarification by this Court at this time.

Moreover, irrespective of the conflict among other state high courts, it is essential for this Court to reject the unprecedented overreach by Michigan here. No state has gone as far as Michigan and ignored out-of-state value entirely in determining what is a fair apportionment on the sale of a business. Instead, Michigan, by excluding the enterprise value from the apportionment formula, failed to consider *at all* the historical activities giving rise to the income as well as the activities conducted outside of the state which were predominantly responsible for the creation of the value that Michigan seeks to tax.

Leading academic commentators have recognized that asymmetry between the tax base and the apportionment formula may establish that a tax assessment is unconstitutional. *E.g.*, Jerome R. Hellerstein & Walter Hellerstein, State Taxation, ¶9.15[2] (3d ed. 1998); Professor Richard Pomp, Report of the Hearing Officer, Multistate Tax Compact Article IV [UDITPA] Proposed Amendments, p. 104 (Oct. 25, 2013) ("[i]t would be sheer serendipity if apportioning the gain in the year of sale without including the gross receipts [in the factor] would reach the correct answer"). And that makes sense. Whether it be subsidiary earnings, dividends, intangible income, or proceeds from an asset sale, if a state includes that income in a company's taxable base, then the state's apportionment formula must also account for that value so that out-of-state income can be appropriately apportioned.

This Court should grant the petition, reverse the Michigan Supreme Court's decision, and hold that symmetry is required to satisfy the Commerce and Due Process Clauses. Such a holding means that when a state includes a category of income in a company's taxable base—such as enterprise value—then that value must also be represented in the state's apportionment formula to account for income generated by out-of-state activity.

B. Distortion is further enhanced when gain is apportioned without reference to the span of time in which the value was created.

This Court's guidance is separately needed to determine if factor representation includes a temporal element. As Justice Zahra explained in his dissent, "The horizon of time [ ] matters. . . . Here, the Department calculates the tax by taking a short, three-month period, calculating the direct to consumers sales for only that period, and attributing that percentage of sales to the sale of all assets in the company. . . . That is not only grossly disproportionate in value, but severely temporally skewed." App. 110.

"[T]hrough the development of ML's company history, its brand name, experience in the field, and consumer value were derived almost entirely from outside Michigan," Justice Zahra continued. App. 109. "Yet the [Treasury] Department did not consider . . . the broader scope of time that would adequately capture

ML's economic activity in the state." App. 110. That is distortive.

A comparison of the record below to a decision of Maine's highest court illustrates the differing approaches and the need for this Court to hold definitively that the Constitution requires states to take temporal representation into account. In *State Tax Assessor v. Kraft Foods Group, Inc*., 235 A.3d 837 (Me. 2020), the taxpayer challenged the use of a single sales factor to apportion gain from the sale of an entire line of business. In rejecting the taxpayer's argument for alternative apportionment, the court noted that the sales factor *in the year of the sale* was consistent with the percentages computed in years past and that the state only sought to tax a small percentage (approximately 0.7%) of the profit realized. *Id*. at 846.

In stark contrast here, the Michigan Department of Treasury used an aberrational year to apportion 70% of Minnesota Limited's income, then applied that formula to all enterprise value, even though most of the company's value had nothing at all to do with Michigan. That's the only way Michigan could arrive at a 70% sales ratio for a company that does very little work in Michigan. The resulting gross distortion could be corrected by representing in the sales factor the average of the Michigan sales for all the years in which Minnesota Limited did business. Indeed, any apportionment that looks only to the year of sale is inherently arbitrary.

II. The Michigan Supreme Court's decision also conflicts with numerous decisions of this Court.

In *Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell* and *Norfolk & Western Railway v. Missouri State Tax Commission*, this Court struck down taxes that were "out of all appropriate proportion to the business transacted . . . in that state" and that have "led to a grossly distorted result." *Hans Rees' Sons*, 283 U.S. at 135; *Norfolk*, 390 U.S. at 326. The principle that a tax is unconstitutional if it results in gross distortion was first stated by this Court in *Underwood Typewriter Co. v. Chamberlain*, 254 U.S. 113 (1920).

The taxpayer in *Underwood Typewriter* earned income through a series of transactions beginning with the manufacture of products in Connecticut and ending with sale of these products in other states. In rejecting the taxpayer's due process challenge to application of Connecticut's formulary apportionment, the Court held that the taxpayer failed to meet its burden of showing the apportionment of its income was inherently arbitrary or produced an un-reasonable result. 254 U.S. at 121. The taxpayer "has not even attempted to show this; and for aught that appears the percentage of net profits earned in Connecticut may have been much larger." *Ibid*.

Fifteen years later, in *Hans Rees' Sons*, the Court reiterated that "evidence may always be received which tends to show that a State has applied a method, which, albeit fair on its face, operates so as to reach profits which are in no just sense attributable to transactions within its jurisdiction," and found that the evidence lacking in *Underwood* was present. 283 U.S. at 134. The state assigned 80% of the taxpayer's income to North Carolina using the statutory apportionment method, while the taxpayer offered evidence proving that the average income from North Carolina operations was 17%. Based on this showing, the Court held that "the statutory method, as applied to the appellant's business for the years in question operated unreasonably and arbitrarily, in attributing to North Carolina a percentage of income out of all appropriate proportion to the business transacted by the appellant in that State." 283 U.S. at 135.

In *Norfolk*, the Court considered application of an apportionment that resulted in more than twice the assessment of tax compared to the previous year. "[O]ur cases certainly forbid an unexplained discrepancy as gross as that in this case. Such discrepancy certainly means that the impact of the state tax is not confined to intrastate property even within the broad tolerance permitted. The facts of life do not neatly lend themselves to the niceties of constitutionalism; but neither does the Constitution tolerate any result, however distorted, just because it is the product of a convenient mathematical formula which, in most situations, may produce a tolerable product." 390 U.S. at 327. The Court held that the State made no effort to offset the distortion and voided the tax.

In those cases, the question presented was whether the result of the statutory formula represented a gross distortion of the taxpayer's actual business in the taxing State. Here, the challenged regime is even more distortive due to the asymmetrical relationship between the tax base and the apportionment formula, the lack of a rational relationship "both on its face and in its application" to the "values connected with the taxing State," *id.* at 325, and the limited temporal measurement period. No numerical comparisons are necessary, though they are in abundance in Judge Zahra's dissent: where there is a *substantive* divergence between the elements of the tax base and the elements of the apportionment formula, the result is distortive. App. 114–115 (Zahra, J., dissenting). This occurs when the income sought to be taxed was earned over decades of hard work in other states, yet Michigan seeks to apportion 70% of that income based on a measurement period of three months of direct-to-consumer activities. App. 121–122 (Zahra, J., dissenting).

In *Goldberg v. Sweet*, 488 U.S. 252 (1989), this Court noted that "the central purpose behind the apportionment requirement is to ensure that each State taxes only its fair share of an interstate transaction." *Id.* at 260–61. While no specific apportionment formula is mandated, any formula that is used must guarantee that "the State has taxed only that portion of revenues from the interstate activity which reasonable reflects the in-state component of the activity being taxed." *Id.* at 262.

Indeed, this Court has long made clear that states cannot regulate or control actions that occur wholly outside the state. *Nat'l Pork Producers Council v. Ross*, 143 S. Ct. 1142, 1156 (2023). This rule protects against shifting and competing laws, provides consistency and predictability in out-of-state activities, and preempts capricious government behavior.

State actions controlling taxation are treated similarly, and states are precluded from applying "a state statute to commerce that takes place wholly outside of the State's borders." *Healy v. Beer Inst., Inc.* 491 U.S. 324, 336 (1989) (citation omitted). When reviewing a state statute affecting interstate commerce, the burden imposed cannot be excessive in relation to the benefits received from the state. *Pike v. Bruce Church, Inc.*, 397 U.S. 137, 142 (1970).

By imposing tax on income received for 95% of tangible property located outside of Michigan, 100% of the real property and facilities located outside Michigan, and 100% of the intangibles located outside of Michigan, Michigan has asserted extraterritorial jurisdiction over property located and used elsewhere to an excessive level no court has ever seen: a 2,100% increase from post-2000 sales history and a 900% increase from recent sales activity. As a result, Michigan far exceeded the inherent limits of its state power. App. 131 (Zahra, J., dissenting). *Accord Shaffer v. Heitner*, 433 U.S. 186, 197 (1977).

To allow such exercise of extraterritorial taxation violates the long-standing constitutional principles this Court has recognized. *E.g.*, *Miller Bros.*, 347 U.S. at 342 ("No principle is better settled than the power of a State, even its power of taxation, in respect to property, is limited to such as is within its jurisdiction.") (citation omitted); *Container Corp.*, 463 U.S. at 164 (a state cannot "tax value earned outside its borders") (citation omitted); *Trinova Corp. v. Mich. Dep't of Treasury*, 498 U.S. 358, 374–84 (1991) (states may not constitutionally "tax burdens and import tax revenues" when analyzing the economic value of sales and assets within a jurisdiction).

III. This case is an ideal vehicle to resolve confusion and provide critical clarity regarding the issues presented.

Inherent in the Michigan Supreme Court's majority opinion is that *where* a company accrues its corporate value is essentially irrelevant when taxing the income when the company is sold. This is in direct conflict with the jurisprudential underpinnings of this Court's decisions in *Hans Rees' Sons, Inc.*, 283 U.S. at 135, *Container Corp.*, 463 U.S. at 169, and *Trinova Corp.*, 498 U.S. at 374–84. State courts of last resort have also addressed this issue and adopted disparate approaches inconsistent with each other. This has led to a lack of uniformity, administrative difficulties, increasing uncertainty, and continued protests, appeals, and litigation. The Court last declined to address this issue in *Unisys Corp. v. Commonwealth, Board of Finance & Revenue*, 812 A.2d 448 (2002), and uncertainty and chaos has continued. This issue is ripe for consideration.

Unlike the taxpayer in *Mobil Oil*, Petitioner has squarely disputed the fairness of Michigan's taxing regime due to the lack of factor representation. While this Court referenced such symmetry in *Container Corp.*, where the use of a three-factor formula allowed representation of the activities from which the income sought to be tax arose, the state courts have not consistently adhered to the Court's view and further guidance is needed to address this recurring question.

If Michigan's asymmetry is allowed to stand, it will have a major effect not only in Michigan but in every state. "Without federal court intervention to limit such behavior, more consistent and aggressive tax assessments in this state and other are likely to be issued." Zahra, J., dissenting, App. 71. States will continue to extend their tax collection efforts beyond their boundaries in violation of the principles of interstate commerce. Zahra, J., dissenting, *Ibid*. Businesses large and small will be caught in a lopsided world of disproportionate and extraterritorial taxation, resulting in the recognized "economic Balkanization" which the Constitution works to prevent. *Hughes v. Okla.*, 441 U.S. 322, 325 (1979).

Moreover, this is an ideal vehicle for the Court to decide the questions presented. There are no meaningful facts disputed. The record is sufficient. And the Michigan Supreme Court's majority and dissenting opinions clearly frame the conflict that should be resolved.

At a bare minimum, the Court should grant the petition and summarily reverse. In no event should the Court allow a decision to stand that taxes company income based upon activity that bears almost no relation whatsoever to the taxing state.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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