No. 23-443

IN THE

Supreme Court of the United States

MMN INFRASTRUCTURE SERVICES, LLC, SUCCESSOR IN INTEREST TO VECTREN INFRASTRUCTURE SERVICES CORP.,

Petitioner,

v.

MICHIGAN DEPARTMENT OF TREASURY,

Respondent.

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

BRIEF OF THE INSTITUTE FOR PROFESSIONALS IN TAXATION AS *AMICUS CURIAE* IN SUPPORT OF PETITIONER

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases **Page(s)**

Constitutional Provisions

Codes, Statutes, and Rules

Other Authorities

IDENTITY AND INTEREST OF *AMICUS CURIAE*

Pursuant to Supreme Court Rule 37, the Institute for Professionals in Taxation (IPT) respectfully submits this brief *amicus curiae* in support of Petitioner MMN Infrastructure Services, LLC.[1]

Founded in 1976, IPT is a non-profit educational organization whose 6,000-plus members represent approximately 1,200 corporations, firms, and taxpayers throughout the United States and Canada. IPT's membership includes small businesses as well as most of the Fortune 1000 companies and spans the spectrum of business and industry sectors, including agriculture, manufacturing, retail, communications, finance, transportation, and energy. In addition to fostering professionalism among its members, IPT's mission is to promote the uniform and equitable administration of state and local taxation, minimize the costs of tax administration and compliance, and promote equitable and non-discriminatory taxation of multistate businesses.

IPT files this brief *amicus curiae* to communicate the broad interest in this case by both taxpayers and their advisers across the United States. Specifically, the circumstances under which alternative apportionment is required under constitutional mandates directly affect the uniform and equitable

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[1] Pursuant to this Court's Rule 37.6, amicus states that no counsel for any party authored this brief in whole or in part, and no person or entity other than the amicus and respective counsel made any monetary contributions to the preparation or submission of this brief.

administration of state and local taxation and IPT's goal to promote equitable and non-discriminatory taxation of multistate businesses.

SUMMARY OF ARGUMENT

This case is to alternative apportionment as the seminal case *Allied-Signal, Inc. v. Dir., Div. of Tax'n*, 504 U.S. 768, 773 (1992) is to the inclusion of income in an apportionable state tax base, as explained below. As in *Allied-Signal*, this case cries out for the clarity only this Court can give.

If a corporation engages in a multi-state business, each state may only tax its fair share of the corporation's total income. *See, e.g.*, *Hans Rees' Sons, Inc. v. North Carolina ex rel. Maxwell*, 283 U.S. 123 (1931). To determine that fair share, this Court has endorsed a process, called "apportionment," whereby a corporation multiplies its total income by one or more fractions that reflect the portion of the corporation's total activity occurring in the taxing state. *Container Corp. of Amer. v. Franchise Tax Bd.*, 463 U.S. 159 (1983). An apportionment formula is generally expressed as a percentage, using a factor or factors based on a type of business activity (*i.e.*, sales, property, payroll), applied to total income to calculate the income taxable by the taxing state. That process is fair, in a constitutional sense, so long as the result produces a "rough approximation" of the corporation's income earned in the taxing state. *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 273 (1978). But if in a particular case the application of the ordinary apportionment fractions does not accomplish this result, the apportionment method violates the constitution and a deviation from the standard formula, *i.e.*, alternative apportionment, is required. *Hans Rees'*, 283 U.S. at 135–136.

Here, the Michigan Supreme Court paid lip service to the Court's fair apportionment precedent, but then proceeded to ignore it. Although a bare 4-3 majority of the Michigan Supreme Court found the Michigan tax is fairly apportioned, the three dissenting justices and the unanimous panel of the Michigan Court of Appeals—found that it is not fairly apportioned. This dissonance merits this Court's scrutiny.

For the three-month period ending March 31, 2011, Minnesota Limited had income of $55 million, comprising a gain of $51 million on the sale of its business assets and $4 million in daily operational income. Pet. at 4-5. Michigan applied its statutory single sales factor apportionment formula, which excluded the proceeds, and generated an apportionment factor of 70%. Pet. at 6. Had the proceeds been included, the sales factor would have been just 15% (with 70% exceeding 15% by 4.7 times). Pet. at 5. For context, during the preceding decade Taxpayer's average Michigan sales factor was 7%, and Minnesota Limited's sales factor in 2010 was 40%. Pet. at 11; *Vectren Infrastructure Servs. Corp. v. Dep't of Treasury*, No. 163742, 2023 WL 4874684, at *26 (Mich. July 31, 2023).

The $51 million gain included in the tax base is almost 13 times as much as the $4 million in operational income, yet the proceeds of the gain are not reflected in the apportionment factor. Additionally, the 70% sales factor for the three-month period greatly exceeds the 7% historical percentage of business the taxpayer derived from Michigan (by 10 times). Even comparing Taxpayer's most recent annual period sales factor of 40%, the excess is a multiple of 1.75. Clearly, 2011 was an outlier.

This Court evaluates the constitutionality of an apportionment scheme using the standards articulated in *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159 (1983) and *Hans Rees' Sons, Inc. v. Maxwell*, 283 U.S. 123 (1931). Under those standards, the application of Michigan's standard apportionment formula here results in gross distortion that requires alternative apportionment.

First, the income statutorily apportioned to Michigan is out of all appropriate proportion to the business transacted in that state by Minnesota Limited. This is because although the gain makes up the vast majority of the tax *base*, none of the proceeds are reflected in the apportionment *factor*. Likewise, from a temporal perspective, gain realized from over ten years of business operations is being taxed using an apportionment factor derived from only three-months of activity. As applied, Michigan's tax scheme creates a material disconnect between the income apportioned to the state and the business transacted therein.

Second, the statutory apportionment formula as applied to Minnesota Limited creates unconstitutional distortion because it unreasonably and arbitrarily attributes a percentage of income (70%) to Michigan out of all appropriate proportion to the business transacted by Minnesota Limited in Michigan, whether that is 15% (including the gain proceeds), 7% (historical), or 40% (the prior twelve months, *i.e.*, 2010).

Michigan's failure to deviate from its standard statutory apportionment formula notwithstanding the impermissible distortion it caused, and the Michigan Supreme Court's blessing of same, concerns taxpayers and tax advisors across the country. Given the many types of multistate businesses, the standard apportionment formula does not always adequately capture a business's activity in a given state, such that alternative apportionment is constitutionally necessary and required by the Due Process and Commerce Clauses. When an outlier case like this is allowed to stand, it erodes the trust of taxpayers and their advisors in these constitutional protections. This case will also raise continued questions for taxpayers and their advisors as to whether states will apply their standard apportionment formulas or allow for alternative apportionment. The issue reaches beyond Michigan and this taxpayer.

This Court should step in to provide clarity and to stop the state's overreach, as it did in *Allied-Signal*.

ARGUMENT

I. Alternative Apportionment Issues Are Important and Widespread to Many Taxpayers Across the Nation.

Taxpayer requests for alternative apportionment are common and becoming more common in the modern national economy. As this Court has already reflected, "The Internet's prevalence and power have changed the dynamics of the national economy." *South Dakota v. Wayfair, Inc.*, 585 U.S. ----, 138 S. Ct. 2080, 2097, 201 L. Ed. 2d 403 (2018). As business operations grow more complex in nature – regional, national and international operations – taxpayers increasingly seek out alternative apportionment to ensure their unique circumstances are taxed equitably in a given jurisdiction.[2] Taxpayers and taxing jurisdictions must evaluate each request and, especially without clear guidance from this Court, litigate this issue to the furthest extent, just like the taxpayer here. *Id.*

States, as noted, may also seek alternative apportionment, and in an increasingly confusing legal landscape, what was once a tool developed to ensure taxpayers are taxed fairly has instead become an additional method for states to extract more revenue. Indeed, states have been generally more successful litigating their own alternative apportionment claims than taxpayers.[3] Altogether this has resulted in a lack of uniformity and the ensuing uncertainty has only increased the burden on taxpayers across the Nation. Only this Court can resolve the ambiguity for taxpayers in all jurisdictions within the United

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[2] *See* Craig Ridenour, CPA, and Brian Kirkell, J.D., *Alternative Apportionment: Fairness Is Not the Only Factor*, THE TAX ADVISER (March 1, 2013), https://www.thetaxadviser.com/issues/2013/mar/redenour-salt-mar2013.html.

[3] Glenn C. McCoy Jr., J.D., and Pietro M. Stuardi, CPA, Holtz Rubenstein Reminick LLP, New York City, *Alternative Apportionment: Tough for the Taxpayer, (Too) Easy for the States*, THE TAX ADVISER (October 1, 2012), https://www.thetaxadviser.com/issues/2012/oct/clinic-story-13.html; *see also* Christopher T. Lutz, Robert P. Merten III, and Nicholas J. Kump, *Trends and Developments in Alternative Apportionment of State Income*, 84 STATE TAX NOTES 559 (May 8, 2017).

States, and additional clarity can only help in this complex legal area.

II. This Case Provides an Appropriate Vehicle to Provide Clarity and Direction as to when the Constitution Requires Alternative Apportionment to Correct Gross Distortion Caused by a Lack of Factor Representation and Temporal Elements of a State's Standard Apportionment Formula.

A. This Court's Due Process Clause and Commerce Clause jurisprudence in *Container* and *Hans Rees'* requires alternative apportionment to correct gross distortion.

The application of a taxing jurisdiction's (here, Michigan's) standard apportionment formula to any given taxpayer's activities in that jurisdiction must comport with requirements of the Due Process and Commerce Clauses.[4] These Clauses "do not allow a State to tax income arising out of interstate activities—even on a proportional basis—unless there is … a rational relationship between the income attributed to the State and the intrastate values of the enterprise." *Container Corp. of Am. v. Franchise*

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4 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…." 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[.]"

Tax Bd., 463 U.S. 159, 165–66 (1983) (citations omitted). State apportionment formulas "must, under both the Due Process and Commerce Clauses, be fair." *Id.* at 169. This Court has stated:

> The Constitution does not "invalidat[e] an apportionment formula whenever it may result in taxation of some income that did not have its source in the taxing State ...." … Nevertheless, we will strike down the application of an apportionment formula if the taxpayer can prove "by 'clear and cogent evidence' that the income attributed to the State is in fact 'out of all appropriate proportions to the business transacted in that State,' or has 'led to a grossly distorted result,'…."

Container, 463 U.S. at 169-170 (citations omitted)([ ] in original).

This Court has developed standards that all taxing jurisdictions must meet for the application of an apportionment formula to be constitutional. *See Container*, *supra*; *Hans Rees' Sons, Inc. v. Maxwell*, 283 U.S. 123 (1931).

Container and *Hans Rees'* hold that if the taxpayer "…demonstrate[s] that there is no rational relationship between the income attributed to the state and the intrastate values of the enterprise," then alternative apportionment is constitutionally required. *Container Corp.*, 463 U.S. at 180 (citation omitted). A taxpayer can meet this burden "by proving that the income apportioned to [the state] under the statute is 'out of all appropriate proportion to the business transacted by [the taxpayer] in that state.'" *Id.* at 180-81 (quoting *Hans Rees'*, 283 U.S. at 135) ([ ] added).

Moreover, "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." *Hans Rees'*, 283 U.S. at 134. A taxpayer meets this burden by showing that the state's statutory method causes gross distortion "as applied to the [taxpayer's] business for the years in question [and] operated unreasonably and arbitrarily, in attributing to [the state] a percentage of income out of all appropriate proportion to the business transacted by the appellant in that state." *Id.* at 135 ([ ] added). In *Hans Rees'*, the evidence showed that "for the years 1923, 1924, 1925, and 1926, the average income having its source in the manufacturing and tanning operations within the State of North Carolina was seventeen per cent., while under the assessments in question there was allocated to the state of North Carolina approximately 80 per cent…." *Id.* at 134 (internal quotation marks omitted).

Alternative apportionment is required when a state's method of apportionment cannot be sustained because its "rigid application" leads to a "grossly distorted result." *Norfolk & Western Ry. Co. v. Missouri State Tax Comm'n*, 390 U.S. 317, 326 (1968). In *Norfolk*, the state's mileage formula was struck down for yielding a "grossly distorted result." Specifically, the state's mileage formula "resulted in postulating that N & W's rolling stock in Missouri constituted 8.2824% of its rolling stock. But appellants showed that the rolling stock usually employed in the State comprised only about 2.71% by number of units (and only 3.16% by cost-less-depreciation value) of the total N & W fleet." *Id.* at 327.

If allowed to stand, this case will be an outlier among alternative apportionment jurisprudence and sow confusion among states, taxpayers, and their advisors as to what standards must be applied in reviewing alternative apportionment requests.

B. Taxpayers need clarity regarding the standards under which alternative apportionment is constitutionally required.

In addressing the apportionment factor issue, the Michigan Supreme Court erred when it applied a line of cases that address whether income should be included in the tax base but which did not address the application or composition of an apportionment factor to that tax base.

Allied-Signal, Inc. v. Dir., Div. of Tax'n, 504 U.S. 768, 773 (1992) addressed: "(1) whether the unitary business principle remains an appropriate device for ascertaining whether a State has transgressed its constitutional limitations; and if so, (2) whether … [it is constitutional] to include in petitioner's apportionable tax base certain income that … was not generated in the course of its unitary business." *Id.* at 773. Indeed, *Allied Signal* did not address the apportionment of the tax base. *Id.* at 790.

Similarly, *Mobil Oil Corp. v. Comm'r of Taxes of Vermont* did not analyze the application or composition of a state's apportionment formula. 445 U.S. 425 (1980). Instead, therein this Court addressed the question of whether dividends paid from foreign subsidiary corporations of a unitary business could be included in a state's tax base. *Id.* at 427. Indeed, *Mobil Oil* held, "[w]e need not, and do not, decide what the constituent elements of a fair apportionment formula applicable to such income would be." *Id.* at 449.

The Michigan Supreme Court's misplaced reliance on *Allied Signal* and *Mobil Oil* exemplifies the confusion among state courts regarding the law with respect to alternative apportionment as it pertains to constitutionally-required factor representation and temporal matching. This Court should use this case as a vehicle to clear the muddied waters and provide the guidance states, taxpayers, and their advisors require.

C. The temporal element was a point of dispute among the justices in the Michigan Supreme Court's 4-3 decision and should be addressed by this Court.

The dispute among the Michigan Supreme Court justices further evidences the need for this Court to provide clarity and direction as to under what circumstances the Constitution requires alternative apportionment to correct gross distortion. As Justice Zahra's dissent makes clear, the temporal element was a point of contention among the justices: "The horizon of time considered by the Department also 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." *Vectren Infrastructure Servs. Corp. v. Dep't of Treasury*, No. 163742, 2023 WL 4874684, at *41 (Mich. July 31, 2023) (Zahra, J. dissenting) (emphasis added). According to Justice Zahra, "That is not only grossly disproportionate in value, but severely temporally skewed." *Id.*

Dissenting justices identified the disconnect between the gain on the sale of all business assets and the use of the statutory direct sales factor for a three-month period. In no way did that apportionment factor fairly reflect Minnesota Limited's activities in Michigan:

> Not "every unitary business" sells all of its corporate rights, property, employee contracts, and intellectual property that it has built over decades through out-of-state activity, recoups a massive amount of income through an out-of-state corporate sale, and receives a 70% tax apportionment on that entire body of income to a state with little connection to the company's activities, ***based solely on a comparatively small amount of direct-to-consumer sales from a narrow three-month period of time*** when the company was performing an offseason contract in response to an environmental emergency. The tax imposed here does not fairly capture a reasonable valuation of ML's in-state activities, even giving a degree of room for the state to perform proper attribution.

Id. (emphasis added) (citations omitted). The dispute among the justices, evidenced in Justice Zahra's dissenting opinion, reflects the fundamental uncertainty concerning temporal issues and the potential for gross distortion in apportionment. Before this decision, multistate taxpayers had comfort that isolated business events with some minimal connection to a state would not grossly distort the amount of income attributable to that state, due to the availability of alternative apportionment vis á vis, *e.g.*, *Hans Rees'*; this case unsettles those clear expectations. Now, when multistate taxpayers and their advisors evaluate where and how they must file their income tax returns, they now must wonder whether jurisdictions emboldened by this opinion will seize upon minimal state contacts. This case can be anticipated to spawn needless litigation of alternative apportionment issues without this Court's intervention.

D. Failure to address whether a temporal element of factor representation exists allows an unconstitutional windfall to certain states.

If this Court does not address the temporal element of factor representation, the door will remain open for states to arbitrarily extract income taxes, in violation of the Due Process and Commerce Clauses. As illustrated here, the 70% apportionment of income gained over a ten-plus year period is simple happenstance springing from the three-month period ending March 31, 2011. Mere timing and the administrative convenience of the taxable year should not be the sole basis for allowing a state to tax 70%

rather than 15% of a business's entire income. As with *Allied-Signal,* wherein this Court refused New Jersey's invitation to hold that notwithstanding the unitary business principle, all income is apportionable, this Court should reject Michigan's invitation to allow the application of an apportionment formula that yields a grossly distorted attribution of income to Michigan.

Indeed, the gross distortion here is substantially similar to that in *Hans Rees'*. There, the evidence showed "that for the years 1923, 1924, 1925, and 1926, the average income having its source in the manufacturing and tanning operations within the State of North Carolina was seventeen per cent…." *Hans Rees' Sons v. State of N. Carolina ex rel. Maxwell*, 283 U.S. 123, 134 (1931). However, "under the assessments in question there was allocated to the state of North Carolina approximately 80 per cent. of the appellant's income" whereas the taxpayer submitted "[a]n analysis … showing that the percentage of its income attributable to North Carolina, for the years in question, did not in any event exceed 21.7 per cent." *Id.* ([ ] added). There, in light of such circumstances, this 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." *Id.* at 135. If in *Hans Rees'*, 80% statutorily apportioned income was considered impermissible relative to 17% actual operational income, how can 70% statutorily apportioned income relative to 15% actual operational income be constitutionally distinguishable in Michigan?

Should this Court not address this issue, similar bare application of a taxing state's standard apportionment formula in one-off circumstances will lead to unconstitutionally arbitrary taxation beyond a state's fair share of income.

States already have political incentive to export tax burden beyond their borders, thus generating revenues without paying the political toll of raising taxes. Allowing the Michigan Supreme Court's ruling to stand will only incentivize, "more … aggressive tax assessments in this state and others…." *Vectren Infrastructure Servs. Corp. v. Dep't of Treasury*, No. 163742, 2023 WL 4874684, at *29 (Mich. July 31, 2023) (Zahran, J., dissenting).

CONCLUSION

The Constitution protects actors engaged in interstate commerce from state tax overreach. The Supreme Court is the arbiter of those protections.[5]

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[5] "It is emphatically the province and duty of the judicial department to say what the law is. Those who apply the rule to particular cases, must of necessity expound and interpret that rule. If two laws conflict with each other, the courts must decide on the operation of each." *Marbury v. Madison*, 5 U.S. (1 Cranch) 137, 177 (1803); *see also* Federalist No. 78, at 525 (Alexander Hamilton) (J. Cooke ed. 1961) ("The interpretation of the laws is the proper and peculiar province of the courts. A constitution is, in fact, and must be regarded by the judges, as a fundamental law. It therefore belongs to them to ascertain its meaning….").

When states, like Michigan here, aggressively implement their taxing power by unwaveringly applying their standard apportionment formula in a way that leads to outcomes that are out of all proportion and grossly distort actual business activities within a state, it is incumbent on this Court to intervene, not just for this taxpayer but for all taxpayers.

This Court must nip in the bud Michigan's rigid application of its statutory apportionment formula, just like the *Allied-Signal* Court did to stop New Jerey's rigid inclusion of all income in the apportionable tax base.

This rigid approach must be stopped before it spreads.

Respectfully submitted,

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