No. 23-443

IN THE
Supreme Court of the United States

MMN INFRASTRUCTURE SERVICES, LLC,

Petitioner,

v.

MICHIGAN DEPARTMENT OF TREASURY,

Respondent.

On Petition for a Writ of Certiorari to the Michigan Supreme Court

BRIEF FOR *AMICUS CURIAE* AMERICAN COLLEGE OF TAX COUNSEL IN SUPPORT OF PETITIONER

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BRIEF OF
AMERICAN COLLEGE OF TAX COUNSEL
AS *AMICUS CURIAE*
IN SUPPORT OF PETITIONER

The American College of Tax Counsel (the "College") respectfully submits this brief as *amicus curiae* in support of Petitioner MMN Infrastructure Services, LLC.[1]

STATEMENT OF INTEREST

The College is a nonprofit professional association of tax lawyers in private practice, in law school teaching positions, and in government, who are recognized for their excellence in tax practice and for their substantial contributions and commitment to the profession. The purposes of the College are:

- to foster and recognize the excellence of its members and to elevate standards in the practice of the profession of tax law;
- to stimulate development of skills and knowledge through participation in continuing legal education programs and seminars;

[1] Pursuant to Supreme Court Rule 37.6, counsel for *amicus curiae* states that no counsel for a party authored this brief in whole or in part, and no party or counsel for a party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amicus curiae*, its members, or its counsel made a monetary contribution to its preparation or submission. Counsel for the College provided timely notice of the College's intent to file this brief.

- to provide additional mechanisms for input by tax professionals in development of tax laws and policy; and
- to facilitate scholarly discussion and examination of tax policy issues.

The College is composed of approximately 700 Fellows recognized for their outstanding reputations and contributions to the field of tax law and is governed by a Board of Regents consisting of one Regent from each federal judicial circuit, two Regents at large, the Officers of the College, and the last retiring President of the College. This *amicus curiae* brief is submitted by the College's Board of Regents and does not necessarily reflect the views of all members of the College, including those who are government employees, academics, and law school professors, some of whom may appear separately before the Court as *amicus curiae* in this case.

The College has submitted briefs as *amicus curiae* in this Court on several occasions, including recent briefs on the merits in *Moore v. United States*, Docket No. 22-800, *Bittner v. United States*, 598 U.S. 85 (2023), and *N. Carolina Dep't of Revenue v. Kimberley Rice Kaestner 1992 Family Trust*, 139 S. Ct. 2213 (2019).

The College submits this *amicus curiae* brief because the decision below is emblematic of threats to the consistent application of this Court's precedents under the Fourteenth Amendment and the Commerce Clause prohibiting the arbitrary and unreasonable state taxation of business enterprise values that are fairly attributable to other States. "Fair apportionment" of income from multistate activities is mandatory. The opinion below does not respect the qualitative analysis required for evaluation of a claim that the statutorily imposed apportionment formula impermissibly distorts the income tax base. If imitated by other States, the predictability and constitutionality of state tax systems would be undermined and burdens on interstate commerce improperly increased.

SUMMARY OF ARGUMENT

1. This Court's precedents are clear that, while States have great flexibility in fashioning formulas for apportioning the income or property of a multistate enterprise, *see Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 273 (1978), any such "formula must bear a rational relationship, both on its face and in its application, to . . . values connected with the taxing State." *Norfolk & W. Ry. Co. v. Missouri St. Tax Comm'n*, 390 U.S. 317, 325 (1968). *Norfolk & Western* teaches that, in evaluating the application of an apportionment formula to an individual taxpayer, state revenue agencies and courts must give attention to "the peculiarities of a given enterprise." *Id.*

The bare-majority decision of the Michigan Supreme Court failed to live up to this standard. It used atypical operating sales from a three-month stub period to allocate gains from the sale of the taxpayer's business as a whole, which gains had accrued elsewhere over many years. The Court should grant the writ to reaffirm the standards for giving due attention to specific taxpayer circumstances to prevent state taxation of extraterritorial values. The importance of such individualized attention is heightened by the increasing predominance of single-factor apportionment formulas, which by definition take account of only one of the "peculiarities of a given enterprise."

2. The case before the Court is an excellent vehicle for revisiting and reaffirming the Court's principles because the competing analyses of the majority and dissenting opinions in the Michigan Supreme Court provide such divergent approaches to the "rational" in evaluating the business and economic factors before it. The multiple decisions below on the agreed facts illustrate the need for the Court to revisit the core principles that ensure fair apportionment.

ARGUMENT

I. The Court's Well-Established Norms for Assessing the Fairness of Apportionment Are Increasingly Being Tested in State Courts and Require This Court's Reaffirmation.

A. Regardless of the presumptive validity of any statutory apportionment formula, Due Process and Commerce Clause concerns place limits on the application of such formulas and require fairness to the individual taxpayer as well as structural respect for interstate commerce and reciprocal limitations on state sovereignty.

Under the Due Process Clause of the Fourteenth Amendment,[2] a State's income tax must

[2] U.S. Const. amend. XIV, § 1.

be based on a "rational relationship between the income attributed to the State and the intrastate values of the enterprise." *Mobil Oil Corp. v. Comm'r of Taxes of Vt.*, 445 U.S. 425, 436-37 (1980), *quoted at* Pet. App. 17. This requirement is intended to prevent a State from "project[ing] the taxing power of the state plainly beyond its borders." *Norfolk & W. Ry. Co. v. Missouri St. Tax Comm'n*, 390 U.S. 317, 325 (1968) (quoting *Nashville, C. & St. L. R. Co. v. Browning*, 310 U.S. 362, 365 (1940) (quotation marks omitted)). It also serves to protect the specific taxpayer from an "unreasonable" or "arbitrary result in its case." *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 274, 275 (1978).

Similarly, the Commerce Clause[3] requires that "the factor or factors used in the apportionment formula must actually reflect a reasonable sense of how income is generated." *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 169 (1983). *See* Pet. App. 18. This "external consistency" test 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." *Okla. Tax Comm'n v. Jefferson Lines, Inc.*, 514 U.S. 175, 185 (1995).

This Court's cases provide a well-established framework for evaluating whether an apportionment formula satisfies the Constitutional requirements both "on its face and in its application." *Norfolk & Western*, 390 U.S. at 325. The Petition does not

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[3] U.S. Const. art. I, § 8, cl. 3.

challenge the facial validity of the Michigan formula at issue. This case involves its application. *See* Petition at 7-8. The lower courts need this Court's guidance on the appropriate standard for reviewing as-applied challenges to single-factor formulas.

Specifically, in this case, Michigan used atypical operating sales in Michigan during a three-month stub period as a percentage of operating sales nationwide during that stub period to allocate gains from the sale of the business accrued in other years and realized elsewhere. Although this Court has not addressed apportionment problems raised by gains from the sale of a business, Michigan's tax in this case "reaches beyond that portion of value that is fairly attributable to economic activity within the taxing State." *Jefferson Lines*, 514 U.S. at 185.

In *Hans Rees' Sons, Inc. v. N. Carolina ex rel. Maxwell*, 283 U.S. 123 (1931), the Court stated that a taxpayer may always present evidence that the "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." *Id.* at 134. The Court's review of the evidence convinced it that the otherwise unobjectionable statutory method exceeded the State's authority under the Fourteenth Amendment in the case at hand by "operat[ing] 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.

Similarly, in *Norfolk & Western*, the Court's conclusion on review of the record was that it showed "that rigid application of the mileage formula led to a grossly distorted result." 390 U.S. at 326. Norfolk & Western had just entered the Missouri market in the year in question by leasing the track of another railroad. The lessor railroad had a materially different and less specialized traffic market than that of Norfolk & Western in its legacy business in other states. The Court found "that the record is totally barren of any evidence relating to enhancement" of the value of the Missouri property from the combination, "or to any other factor which might offset the devastating effect of the demonstrated discrepancy." *Id.* at 327.

These quotations are the qualitative descriptors used by the Court to express how the attribution of multistate income or property to the taxing State was unreasonable and arbitrary in that particular case. Given that Michigan law adopted these descriptors as the statutory thresholds for entitlement to relief from the statutory formula, *see* Pet. App. 6 (quoting Mich. Comp. Laws §208.1309(3)), it should follow that the analytical methods of the Court that led to those descriptors be considered in evaluating a taxpayer's claim under the statute. This step was pointedly omitted from the Michigan Supreme Court's majority opinion. Instead, the Michigan Supreme Court evaded this Court's qualitative reasoning by relying on the expedient of the limited taxing period. The majority said this Court's analysis in *Hans Rees* and *Norfolk & Western* depended conceptually on the "snapshot of the business transacted during a tax year." *See* Pet. App. 62-63. That argument is expressly contradicted by the *Norfolk & Western* opinion, as shown below.

To recapitulate the *Norfolk & Western* analysis: that case involved application of a Missouri property tax to an interstate railroad's rolling stock. The apportionment formula attributed value of rolling stock to the State in accordance with the percentage of the railroad's total miles of track that lay within the State. 390 U.S. at 320-21. In other words, the value of one thing was apportioned to the State in accordance with a ratio derived from the geographic location of another thing. The Court had approved the use of a road mileage ratio to postulate the value of property that uses the road "in various contexts." *Id.* at 326. However, in *Norfolk & Western*, the Court determined that the formula, as applied, produced a grossly distorted result. In reaching this conclusion, the Court noted, among other things, the large increase in value assigned to the in-state property leased by the railroad as compared to the value assigned to the same property in the lessor's hands in the prior year. *Id.* at 326-27. The Court rejected the State's contention that the leased property had an enhanced value on account of its combination with the taxpayer's other operations, observing such enhanced value was merely "assumed," without evidence or particularized quantification. *Id.* at 328-29. Given the lack of evidence, the Court found the difference in value from one year to the next to be an "unexplained discrepancy" to a "gross" degree. *Id.* at 327.

The Court's approval of a single-factor apportionment formula in *Moorman*, decided ten years later, took nothing away from its holding in *Norfolk & Western*. The Court in *Moorman*, in fact, applied the same standard of proof to the taxpayer's claim as it had to the State's claim in *Norfolk &*

Western. In *Moorman*, "[the taxpayer] contends that we should proceed *on the assumption* that at least some portion of the income from Iowa sales was generated by Illinois activities." 437 U.S. at 272 (emphasis added). Because the taxpayer chose not to make an as-applied challenge or demonstrate a causal link between the Illinois activities and profits from Iowa sales, the Court rejected the contention as "speculative." *Id.*

The integrity of the law in this area would benefit substantially from renewal and reinforcement of this Court's consistent analysis in the current case.

B. The dramatic increase in States' reliance on single-factor formulas to apportion taxable income has opened the door to an increased risk of distortion, and that risk makes careful application of the constitutional framework more critical.

Since *Moorman*, the "single sales factor" has recently become the most common approach in formulary apportionment. *See* Tax Foundation, Apportionment (State Primary Apportionment Factors for Tax Year 2020), https://taxfoundation.org/taxedu/glossary/apportionment/ (29 of 45 States with corporate income taxes used only a gross-sales factor in 2020, and most others weighted sales more heavily than other factors). The landscape of apportionment of interstate income has shifted substantially since *Container* affirmed the merits of a multi-factor formula in 1983, and the consequences of this shift, especially when gain from the sale of a business is realized in a single tax year, merit this Court's review.

Although a single-factor apportionment formula may be presumptively valid, it bears keeping in mind that the choice of factor is a legislative one and hence a political one. State policy and legislative statements have been quite open about the goal of single sales factor apportionment – giving a boost to local business by reducing the tax burden associated with buildings and personnel. For example, Maryland:

> For corporations that are based in Maryland, placing more weight on the sales factor can provide tax relief because those corporations generally own significantly more property and incur more payroll costs in the State. In addition, placing more weight on the sales factor tends to place a larger percentage of an out-of-state corporation's income within the taxing jurisdiction of the State.

Maryland Economic Development and Business Climate Commission, *Report of the Maryland Economic Development and Business Climate Commission, Phase II: Taxes* 37-38 (2016). *See also* Shirley Sicilian & Joe Huddleston, The US States' Experience with Formulary Apportionment, in Richard Krever, et al., The Allocation of Multinational Business Income: Reassessing the Formulary Apportionment Option, ch. 2, at 52 (Wolters Kluwer, updated 2020) ("Reducing the weight given to property and payroll reduces a potential tax disincentive of locating capital investment and jobs in the state. A formula that uses only the sales factor eliminates that potential.”).

Given these explicit goals of single sales factor apportionment, the scrutiny this Court has always required to ensure that the statutory formula does not produce distortion in individual cases becomes all the more imperative.[4]

The susceptibility of single-factor apportionment to produce distortion is exacerbated by the tendency of state courts to read this Court’s statement that a single-factor formula is “presumptively valid,” *Moorman*, 437 U.S. at 273, as meaning that such formulas are “conclusively valid” regardless of application. For example, in a case bearing similarities to the present Petition, *State Tax Assessor v. Kraft Foods Group, Inc.*, 235 A.3d 837 (Me. 2020), the Supreme Court of Maine relegated the taxpayer’s constitutional claim of distortion to a footnote, saying:

> We have considered Kraft’s remaining argument that alternative apportionment is constitutionally required pursuant to the Due Process and Commerce Clauses of the United States Constitution, and we conclude that it is not persuasive *because* the

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[4] *See* Walter Hellerstein, “Distortion of Income in a Single-Factor Sales Formula World,” 96 Tax Notes State 729 (May 11, 2020) (reviewing the history of distortion analysis in the Court’s cases and raising the question whether modern single-factor formulas pose a greater constitutional risk to State income tax systems).

> Supreme Court has "repeatedly held that a single-factor formula is presumptively valid."

Id. at 842 n.6 (quoting *Moorman*, 437 U.S. at 273) (emphasis added). A crucial distinction for the *Moorman* decision was that, unlike this appeal, the taxpayer did not identify evidence for the claimed distortion in that case.

The Court should grant the writ requested in this matter because the force of its teaching in *Norfolk & Western*, *Moorman*, and *Hans Rees* has been greatly diluted over time, at the same time when that teaching has become more important given the application of statutory single-factor apportionment formulas to business sales and other "one-off" circumstances, as the Michigan Supreme Court described the facts in this case. *See* Pet. App. 7.

II. The *Vectren* Opinions Below Demonstrate a Divergence in Approaching the Question "How Income Is Generated" and Present an Ideal Vehicle for Guidance on Application of Established Norms.

The opinions in *Norfolk & W. Ry. Co. v. Missouri St. Tax Comm'n*, 390 U.S. 317, 325 (1968), and *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 273 (1978), establish that state courts cannot rely on mere "assumptions" or "speculation" in the face of evidence in the record when determining whether the factors used in an apportionment formula "actually reflect a reasonable sense of how income is generated." *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 169 (1983). This case presents an excellent opportunity to revisit and reaffirm this important guidance, because the opinions in the Michigan Supreme Court's decision embody such divergent pathways through the evidence.

The College submits that the dissents by Justices Zahra, Pet. App. 26-131, and Viviano, Pet. App. 132-40, represent a measured and reasoned examination of the evidence in the case while the four-Justice majority opinion is marred by an imbalanced review of the record and, as Justice Zahra notes, Pet. App. 125, 127, an unwarranted, "speculative" projection of future business value in Michigan.

The reasoning in the majority opinion is simply not consistent. It begins with acknowledgment that the case is highly unusual, dealing "with a complex asset sale of a unitary business operation . . . and the one-off ramifications when that asset sale coincided with large Michigan sales." Pet. App. 7. Though the majority notes that this "coincidence" is significant, it then takes pains to explain why it is reasonable to exclude the proceeds of the asset sale from the statutory sales factor: "the sale of ML to Vectren was *not the same thing* as selling a product or service (such as oil spill cleanup or pipeline maintenance services)." Pet. App. 9 (emphasis added). Having acknowledged these "peculiarities of [the] given enterprise" at a superficial level, the thrust of the majority's apportionment analysis proceeds in an entirely different direction. The majority held that the asset sale proceeds were just an aspect of a unitary business that was appropriately sourced to Michigan by a factor "that accurately measures sales." Pet. App. 56.

Responding to the claim that excluding the asset sale proceeds from the sales factor caused a failure to recognize reasonably "how the income was generated," which is the core constitutional issue, the majority said: "This is nothing more than a gripe about which factors are or are not included in the formula." Pet. App. 57. For support, the majority cited to *Moorman* as an example of decisions that did not invalidate single-factor formulas, *see id.* n.23, but *Moorman* does not support the majority's analysis. The majority failed to acknowledge that the taxpayer's challenge to Iowa's formula in *Moorman* relied only on an assumption that its out-of-state activities contributed to profits from in-state sales and not on a record of evidence.[5]

The core of the majority's justification for ascribing 70% of the net income from the asset sale to Michigan lay in the majority's citation of a "nonexhaustive summary of relevant evidence" that cited only to ML's connections with Michigan and not to the balance of ML's business. *See* Pet. App. 45-46. It was this slice of the record, and the majority's reliance on it to ascribe "a potential further growth market" for the company in Michigan, that prompted the dissent's accusation of "pure speculation." Pet. App. 127 (Zahra, J., dissenting).

The dissent by Justice Zahra, by contrast, appears to consider meticulously the entirety of the taxpayer's undisputed evidence. *See* Pet. App. 72 n.5

[5] *See also* Pet. App. 24-25, 54 n.21 (discussing *Moorman* without acknowledging that the taxpayer did not make an evidentiary case in support of its distortion claim).

(enumerating the sources of evidence in the record), 74 n.6 (carefully explaining the calculation of sales ascribed to Michigan), 75-76 (cataloguing assets and personnel of the taxpayer in geographic terms), 79-82 (describing the oil spill remediation project that boosted Michigan sales during the short tax year), 101-09 (bringing all the facts to bear on the question of where to attribute value within the multistate enterprise). *See also* Pet. App. 106 n.52 (analyzing contributing factors in ML's valuation). In the College's view, the dissent is accurate in noting that "the majority opinion largely leaves unaddressed the substantial record of value explained in this opinion." Pet. App. 121-22.

Given this stark contrast in frame of reference between the slim majority and the carefully reasoned dissents in the court below, the case presents itself as an ideal opportunity not only to reinforce the analytical framework erected in *Norfolk & Western* and *Moorman* in light of the trend to single-factor formulas, but also to teach again that a system of fair apportionment depends on a fair judicial supervision of revenue agencies, because the courts are the guarantors of the constitutional values at stake.

CONCLUSION

For the foregoing reasons, the College respectfully requests that the Court grant the writ requested by Petitioner.

Respectfully submitted,

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