

No. \_\_\_\_\_

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In The  
**Supreme Court of the United States**

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IDAHO STATE TAX COMMISSION,

*Petitioner,*

v.

NOELL INDUSTRIES, INC.,

*Respondent.*

—————◆—————  
**On Petition For A Writ Of Certiorari To The  
Supreme Court Of The State Of Idaho**

—————◆—————  
**PETITION FOR WRIT OF CERTIORARI**

—————◆—————  
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## QUESTION PRESENTED

Previously, this Court considered whether a unitary-business relationship could be determined from the superficial aspects of a corporation. *Mobil Oil Corp. v. Commissioner of Taxes of Vermont*, 445 U.S. 425, 439, 100 S. Ct. 1223, 1232, 63 L. Ed. 2d 510 (1980). This Court answered that superficial attributes were not determinative of unity. *Id.* Instead, this Court ruled that a unitary relationship is presumed unless the corporation proved by affirmative evidence that it was a “discrete business enterprise.” *Id.* at 439–442, 100 S. Ct. at 1232–1234.

Today, State courts are wrestling with nearly the same question: should superficial aspects of a pass-through entity’s business determine unity? Courts in Idaho, New Jersey, and Tennessee have wrestled with this question. See *Noell Industries Inc. v. Idaho State Tax Commission*, 167 Idaho 367, 470 P.3d 1176 (2020), reh’g denied (Aug. 14, 2020) at App. 1-46; *BIS LP, Inc. v. Dir., Div. of Taxation*, 26 N.J. Tax 489 (Super. Ct. App. Div. 2011); and *Blue Bell Creameries v. Roberts*, 333 S.W.3d 59 (Tenn. 2011). These decisions have produced a split among the states: the Tennessee court extended the *Mobil* ruling to pass-through entities while the Idaho and New Jersey courts have not. This split in state court cases prompts the question of this case, which is:

Does this Court’s ruling in *Mobil* apply to pass-through entities?

## **PARTIES TO THE PROCEEDING**

All parties to the proceedings below are named in the caption. Noell Industries, Inc. was historically called “Blackhawk Industries, Inc.” at all times relevant to the facts of this case.

## **RELATED CASES**

- *Noell Industries Inc. v. Idaho State Tax Commission*, CV01-18-02355, Idaho Fourth Judicial District Court, and for the County of Ada. Judgment entered February 15, 2019.
- *Noell Industries Inc. v. Idaho State Tax Commission*, 167 Idaho 367, 470 P.3d 1176 (2020), reh’g denied (Aug. 14, 2020). Judgment entered May 22, 2020. Petition for rehearing denied August 14, 2020.

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**PETITION FOR A WRIT OF CERTIORARI**

The Idaho State Tax Commission respectfully petitions this Court for a writ of certiorari to review a judgment of the Supreme Court of Idaho.

**OPINIONS BELOW**

The opinion of the Supreme Court of Idaho is available at *Noell Industries Inc. v. Idaho State Tax Commission*, 167 Idaho 367, 470 P.3d 1176 (2020), reh'g denied (Aug. 14, 2020). The Idaho Supreme Court opinion is reproduced at App. 1–46. The state trial court's decision is unreported and is reproduced at App. 47–89.

**JURISDICTION**

The Idaho Supreme Court issued its decision on May 22, 2020. App. 1–46. The Idaho State Tax Commission timely petitioned the Idaho Supreme Court to rehear the matter. The petition for rehearing was denied on August 14, 2020. This Court has jurisdiction to consider the Idaho Supreme Court's decision under 28 U.S.C. § 1257(a).





## **STATUTES AND CONSTITUTIONAL PROVISIONS INVOLVED**

The Fourteenth Amendment to the United States Constitution provides: “No State shall . . . deprive any person of life, liberty, or property, without due process of law.” U.S. Const. amend. XIV, § 1 (the Due Process Clause).

Idaho Code section 63-3027 states, in part:

The Idaho taxable income of any multistate or unitary corporation transacting business both within and without this state shall be computed in accordance with the rules set forth in this section:

(a) As used in this section, unless the context otherwise requires:

(1) “Business income” means income arising from transactions and activity in the regular course of the taxpayer’s trade or business and includes income from the acquisition, management, or disposition of tangible and intangible property when such acquisition, management, or disposition constitutes integral or necessary parts of the taxpayer’s trade or business operations. Gains or losses and dividend and interest income from stock and securities of any foreign or domestic corporation shall be presumed to be income from intangible property, the acquisition, management, or disposition of which constitutes an integral part of the taxpayer’s trade or business; such presumption may only be

overcome by clear and convincing evidence to the contrary.

...

(f)(3) Capital gains and losses from sales of intangible personal property are allocable to this state if the taxpayer's commercial domicile is in this state, unless such gains and losses constitute business income as defined in this section.

...

(i)(1) Notwithstanding the election allowed in article III.1 of the multistate tax compact enacted as section 63-3701, Idaho Code, all business income shall be apportioned to this state under subsection (j) of this section by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus two (2) times the sales factor, and the denominator of which is four (4), except as provided in paragraph (2) of this subsection.

Idaho Income Tax Administrative Rule 340 states, in part:

In Idaho, the unitary business principle shall be applied to the fullest extent allowed by the U.S. Constitution. The unitary business principle shall not be applied to result in the combination of business activities or entities under circumstances where, if it were adverse to the taxpayer, the combination of such

activities or entities would not be allowed by the U.S. Constitution.

IDAPA 35.01.01.340(02)(b).

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## STATEMENT OF THE CASE

### I. INTRODUCTION

While this Court has never explicitly applied the holding in *Mobil Oil Corporation v. Commissioner of Taxes of Vermont*, 445 U.S. 425, 100 S. Ct. 1223, 63 L. Ed. 2d 510 (1980) to pass-through entities, there is no reason that ruling should not be applicable to them. In *Mobil*, this Court ruled that superficial attributes of a business, such as corporate form or other generic descriptors of the business, did not determine unity. *Mobil* at 439, 100 S. Ct. at 1232. Instead, the Court looked at the “underlying economic realities” of the business. *Id.* The Court held that there was presumption of a unitary relationship and that the taxpayer could overcome the presumption by providing affirmative evidence that it operated as a “discrete business enterprise.” *Exxon Corp. v. Wisconsin Dep’t of Revenue*, 447 U.S. 207, 223–224, 100 S. Ct. 2109, 2120, 65 L. Ed. 2d 66 (1980) quoting *Mobil* at 439, 100 S. Ct. at 1232.

Applying the *Mobil* ruling to pass-through entities is consistent with the underlying due process principles animating this Court’s unitary-business test. See *MeadWestvaco Corp. ex rel. Mead Corp. v. Illinois Department of Revenue*, 553 U.S. 16, 25, 128 S. Ct.

1498, 1505, 170 L. Ed. 2d 404 (2008) (stating that the unitary-business tests should serve the broader inquiry of “whether the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the state”). Applying the *Mobil* ruling also prevents businesses from using new business structures to elude fairly apportioned state taxation. *Allied-Signal, Inc. v. Dir., Div. of Taxation*, 504 U.S. 768, 786, 112 S. Ct. 2251, 119 L. Ed. 2d 533 (1992) (noting that using “new methods of finance and new forms of business” does not make a business immune from apportionment). Finally, applying the ruling evenly ensures that pass-through entities and corporations are subject to the same due process standards.

The consequence of not applying this *Mobil* ruling to pass-through entities is apparent from the case at hand. The Idaho Supreme Court ignored *Mobil* when it determined that the inactivity of a holding company proved a diversity of business enterprise. In so doing, the Idaho Supreme Court has effectively created a holding-company exception to this Court’s unitary-business test and thus created a class of businesses that are immune from a state’s fairly apportioned tax. This ruling creates a shelter for certain businesses that is not immediately available to other businesses or individuals without a change in business form. It also deprives Idaho of revenue that, but for this shelter, it would otherwise fairly tax consistent with the Due Process Clause.

This Petition should be granted. The tension between the inconsistent state court decisions and the

uneven application of the *Mobil* decision calls for this Court's attention. The Court should affirmatively apply its ruling in *Mobil* to pass-through entities. Specifically, and as in *Mobil*, this Court should find that a pass-through entity, just as with corporations, must prove by affirmative evidence that it is a "discrete business enterprise" from what it owns to even "raise the question of nonapportionability." *Mobil* at 439 & 442, 100 S. Ct. at 1232 & 1234. If a pass-through entity fails to do so, the state should be entitled to conclude that a unitary-business relationship exists. *Id.*

## **II. FACTS AND PROCEEDINGS BELOW**

### **A. The Blackhawk Family of Businesses.**

Respondent is a holding company headquartered in Virginia that held ownership interest in only two subsidiaries: (1) Blackhawk Products Group Unlimited, LLC ("Blackhawk, LLC") and (2) Blackhawk Real Estate Holdings, LLC ("Blackhawk Real Estate"). Blackhawk, LLC was in the business of producing, marketing, and selling tactical gear. This tactical gear business produced the revenue of the entire enterprise. The Blackhawk businesses used Blackhawk Real Estate to hold real estate necessary to the Blackhawk businesses. Blackhawk Real Estate produced only losses. Respondent was known as Blackhawk, Inc. at all times relevant to this matter including at the time of the sale of Blackhawk, LLC in 2010.

Respondent had no independent purpose to exist other than to hold an interest in the Blackhawk family

of businesses. It held no interest in any business unrelated to the Blackhawk businesses and had no investments. Respondent derived 99% of its gross revenue from Blackhawk, LLC. The remainder of its revenue was from interest earned from bank deposits. Respondent's only corporate officers were also officers of Blackhawk, LLC. In particular, Michael Noell—founder of the tactical gear business—was President of both companies. In this role, he oversaw and directed both companies.

Respondent had no substantial business activity. The company held required board meetings and coordinated the taxes of its two subsidiaries. It also shared the same legal and accounting services as its subsidiaries. It primarily existed as a mechanism to allow Michael Noell, founder of the Blackhawk business and 100% owner<sup>1</sup> of Respondent, to continue to manage the company he founded and directed.

In the years leading up to the sale, Blackhawk, LLC built up a substantial presence in Idaho and reported income tax to the state. It located its Westcoast operations center and a large warehouse in Boise, Idaho. Its tax returns indicated that Blackhawk, LLC had more than 40% of all of its property located in Idaho and 13% of its workforce in the state. It is undisputed that Blackhawk, LLC benefitted from the

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<sup>1</sup> In 2009, Mr. Noell conveyed about one-third of his interest in Respondent to a grantor-retained annuity trust organized by Mr. Noell.

protections and opportunities afforded to it by the State of Idaho.

The Blackhawk businesses reported their income tax to Idaho through the Respondent's tax returns. Respondent filed its tax returns indicating that it was unitary with its two subsidiaries and indicating that the income Blackhawk, LLC produced from its ordinary business transactions was apportionable business income. In the years preceding the sale and in the year of the sale, Respondent reported itself as transacting business in the State of Idaho.

In 2010, Respondent sold its 78.54% membership interest in Blackhawk, LLC for \$120 million. Following the sale, Respondent reported all income derived from the ordinary transaction of its tactical gear business in 2010 as being apportionable business income in Idaho. However, Respondent reported the income arising from the sale of Blackhawk, LLC as nonbusiness income. It did not apportion any of the income arising from the sale to Idaho, instead allocating all the capital gain to Virginia.

From the time Blackhawk, LLC was organized in 2004 until the time that Respondent sold its subsidiary in 2010, all of Respondent's activities, slight as they were, were conducted in furtherance of the Blackhawk family of businesses.

### **B. Idaho’s Corporate Income Tax Law.**

By design, Idaho’s income tax on multistate businesses is intended to be as broad as may be permitted under the Constitution. Idaho’s statutory framework is a common one—Idaho uses a lightly modified version of the model Uniform Division of Income for Tax Purposes Act (“UDITPA”). Under its statute, Idaho taxes a multistate business on the “business income” that arises from “any multistate or unitary corporation transacting business both within and without this state.” Idaho Code § 63-3027. Idaho’s formulation of UDITPA allows Idaho to tax multistate businesses to the fullest extent of the Due Process Clause as interpreted by this Court. IDAPA 35.01.01.340(02)(b) (“In Idaho, the unitary business principle shall be applied to the fullest extent allowed by the U.S. Constitution.”)

### **C. Administrative and Judicial Proceedings.**

This case began as an audit and administrative appeal before the Idaho State Tax Commission (the Petitioner). On its tax returns, the Respondent asserted that the income derived from selling Blackhawk, LLC was nonbusiness income not apportionable to Idaho. As a result of the audit and administrative appeal, the Commission ultimately determined that the income produced from the sale of Blackhawk, LLC was business income that could be fairly apportioned and taxed by Idaho.

Respondent appealed the Petitioner’s decision to Idaho’s state district court. In this *de novo* proceeding



before the District Court, Respondent alleged that it was not a business and thus could not be unitary with its subsidiary business. It contended that it was not taxable on the capital gain recognized from the sale of Blackhawk, LLC. Before both the Idaho District Court and the Idaho Supreme Court, it argued that—because it lacked business operations—it was immune from Idaho’s fairly apportioned state taxation and may only be taxed by its home state, Virginia.

In response, Petitioner argued that the evidence of a lack of business activity presented by Respondent did not establish that it was a discrete business enterprise from Blackhawk, LLC. Petitioner argued that consistent with the *Mobil* decision, Respondent’s failure to prove a discrete business enterprise required that Petitioner be deemed unitary with Blackhawk, LLC. Petitioner further argued that, pursuant to *Mobil*, Idaho could apportion and tax a share of Respondent’s capital gain.

The Idaho Supreme Court rejected Respondent’s argument that it was not a business. The Idaho Court found that Respondent was in the business of being a holding company. It characterized Respondent as “being part of a commonly controlled group” with its two subsidiaries. App. 27. The Court stated that as the parent company of the group, “Noell Industries’ primary function was holding its interest in the two business entities over several years, relying primarily on Blackhawk for its income.” App. 17. The Court continued:

. . . Noell Industries was merely a holding company. It held interests in only two business entities: Blackhawk and a Virginia company that leased real property to Blackhawk. Once Noell Industries transferred its net assets to Blackhawk in exchange for a majority interest, Noell Industries ceased most—if not all—of its business activity, notwithstanding its representation as an ‘investment’ company on its tax returns. . . . Indeed, by selling Blackhawk, Noell Industries lost its primary source of income in exchange for the financial betterment of \$120 million.

App. 21. In short, the Idaho Court determined that Noell Industries was in the business of being a holding company, rejecting the premise of Respondent’s argument that it could not be taxed as it was not a business.

The Idaho courts also rejected Petitioner’s argument concerning *Mobil*. Both the Idaho District Court and Idaho Supreme Court dismissed the holding from *Mobil*. The Idaho District Court incorrectly attributed the *Mobil* ruling to a Tennessee case, *Blue Bell Creameries v. Roberts*, 333 S.W.3d 59 (Tenn. 2011). In this round-about way, it criticized this Court’s ruling as “jettison[ing] the unitary business principle.” App. 82. It continued to state that the Tennessee court showed a “lack of thoughtful analysis” by applying the *Mobil* ruling. App. 82. Finally, it incorrectly stated that the *Mobil* ruling had not been applied outside of Tennessee. App. 82.

The Idaho Supreme Court similarly avoided discussing the *Mobil* ruling. The Idaho Supreme Court signaled that it was aware of *Mobil* by citing to it for the proposition that “the unitary-business principle is ‘the linchpin of apportionability in the field of state income taxation.’” App. 14 quoting *Mobil* at 439, 100 S. Ct. at 1232. However, the Court failed to directly cite to the case again. Instead, and just as with the District Court, the Idaho Supreme Court discussed and dismissed the *Blue Bell* case. App. 25–26. The Idaho Supreme Court decision effectively ignored this Court’s *Mobil* ruling.

In its place, the Idaho Supreme Court found that Respondent’s evidence of a lack of business activity meant that it could not be unitary with Blackhawk, LLC. The Idaho Court found that its lack of activity meant that it did not have “employees, payroll, [and] offices.” The court reasoned that without “employees, payroll, or offices,” it was impossible for Respondent to share “centralized management, oversight, or headquarters,” with Blackhawk, LLC. App. 27. The Idaho Court further reasoned that a holding company without substantial business activity could not exert “shared control” or have shared “operations” with its subsidiary companies. App. 27.

The Idaho Court concluded that since Respondent was “a shell holding company” and because its only formal transactions were to form its subsidiaries and sell its subsidiaries, Respondent’s relationship with its subsidiaries “showcase[d] substantial independence

rather than the level [of] interdependence required to manifest unity.” App. 27.



## **REASONS FOR GRANTING THE PETITION**

There are two broad reasons for this Court finding that the *Mobil* decision applies to pass-through entities: (1) Applying *Mobil* to pass-through entities is consistent with the Constitutional principles underlying this Court’s unitary-business test and (2) it would resolve a state court split on the applicability of the *Mobil* ruling to pass-through entities.

### **I. Applying *Mobil* to Pass-Through Entities is Consistent With this Court’s Due Process Case Law.**

This Court’s decision in *Mobil* is a core component of the unitary-business principle. It is not an aberration or a sidelight to this Court’s unitary-business principle case law. It is the piece of this Court’s case law that ensures that the unitary-business test is substantively applied and used in a manner consistent with the Due Process Clause. As such, *Mobil* should be just as applicable to pass-through entities as it is to corporations.

**A. This Court Created the Unitary-Business Test to Serve Broader Due Process Clause Considerations.**

The Constitution permits a state to impose a tax “when the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the state—that is, whether the state has given anything for which it can ask return.” *MeadWestvaco* at 25, 128 S. Ct. at 1505 (internal quotation marks omitted). In describing this expansive taxing power, this Court has stated that the Due Process Clause requires “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.* at 24, 128 S. Ct. at 1505.

In interpreting this requirement, the Court has identified a practical concern with how this abstract Constitutional principle applies to businesses operating in multiple states. *Allied-Signal* at 777–778, 112 S. Ct. at 2258. The Court has found it difficult to determine with specificity where the income of a multistate business is produced. *Id.* Such difficulty creates “complications and uncertainties” for taxpayers and the taxing state. *Id.* at 778, 112 S. Ct. at 2258. To avoid these complications, this Court has created the “unitary-business principle:” the concept that a “State [may] tax a corporation on an apportionable share of the multistate business carried on in part in the taxing State.” *Id.*

Rounding out this concept more completely, this Court has provided guidance on when a business unit<sup>2</sup> is engaged in a “multistate business carried on in part in the taxing State.” *Id.* This Court’s unitary-business test measures the flow of value between multiple business units to determine whether the business units are sufficiently interrelated to be considered part of a single enterprise. As this Court has explained, “a relevant question in the unitary business inquiry is whether ‘contributions to income [of the subsidiaries] result[ed] from functional integration, centralization of management, and economies of scale.’” *Container Corp. of Am. v. Franchise Tax Bd.*, 463 U.S. 159, 178, 103 S. Ct. 2933, 2947, 77 L. Ed. 2d 545 (1983) quoting from *F. W. Woolworth Co. v. Taxation & Revenue Dep’t of State of N.M.*, 458 U.S. 354, 364, 102 S. Ct. 3128, 3135, 73 L. Ed. 2d 819 (1982) and *Mobil* at 438, 100 S. Ct. at 1232. These factors evidence a “unitary relationship” and serve as a practical application of a state’s right to apportion income under the Due Process Clause.

Taken all together, the abstract construction of what the Due Process Clause requires and its corresponding practical applications are meant to serve—not frustrate—the broader inquiry: “whether the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the

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<sup>2</sup> The phrase business unit, while awkward, is intentional. As this Court’s standard looks past formal corporate divisions, it is possible for a single business organization to have separate lines of business that constitute distinct unitary businesses. *Mobil* at 440, 100 S. Ct. at 1233.

state. . . .” *MeadWestvaco* at 25, 128 S. Ct. at 1505 (internal quotation marks omitted). To this end, the Court has been careful to keep this area of law flexible so that it can be applicable to “new methods of finance and new forms of business” as they evolve. *Allied-Signal* at 786, 112 S. Ct. at 2263. The aim of any application of this Court’s state-and-local-tax due process case law to the facts of a case should be to reach a conclusion “logically consistent with the underlying principles motivating the approach.” *Id.* at 769, 112 S. Ct. at 2254, quoting *Container* at 167, 103 S. Ct. at 2941.

**B. *Mobil* Ensures that any Application of the Unitary-Business Principle Serves Such Broader Considerations.**

Through its decision in *Mobil*, this Court ensures that any application of the unitary-business principle serves underlying due process considerations. In *Mobil*, this Court rejected calls to introduce rigidity to its unitary-business principle. In that case, the Court was urged by “various *amici*” to treat the formal “division between parent and subsidiary . . . as a break in the scope of unitary business.” *Mobil* at 440, 100 S. Ct. at 1233. Those *amici* argued that the business structure alone was a sufficient “break” in unity to make “the receipt of dividends . . . a discrete ‘taxable event’ bearing no relation” to the taxing state. *Id.*

This Court rejected the argument that such formal division can make a business immune from fairly apportioned state taxation. This Court stated that

“[s]uperficially, intercorporate division might appear to be a more attractive basis for limiting apportionability,” however “the form of business organization may have nothing to do with the underlying unity or diversity of business enterprise.” *Id.* The Court noted that “[h]ad appellant chosen to operate its foreign subsidiaries as separate divisions of a legally as well as a functionally integrated enterprise, there is little doubt that the income derived from those divisions would meet due process requirements for apportionability.” *Id.* at 440–441, 100 S. Ct. at 1233. This Court continued, “One must look principally at the underlying activity, not at the form of investment, to determine the propriety of apportionability.” *Id.* at 440, 100 S. Ct. at 1233.

Ultimately, this Court held that neither Mobil’s business structure nor its self-characterization of having a “holding company function” evidenced a lack of a unitary business. *Id.* The Court found that—in accordance with the concepts underlying the unitary-business principle—it is the taxpayer’s obligation to show a lack of a unitary relationship. *Id.* at 439–440, 100 S. Ct. at 1232–1233. The Court reasoned that “[i]n the absence of any proof of discrete business enterprise” the state was “entitled to conclude” that a unitary relationship existed. *Id.* The Court ruled that the taxpayer in that matter “had failed to sustain its burden of proving any unrelated business activity on the part of its subsidiaries and affiliates that would raise the question of nonapportionability.” *Id.* at 442, 100 S. Ct. at 1234.

The *Mobil* ruling has been favorably cited to by this Court in later cases. In *Exxon*, this Court stated:



“The court looks to the ‘underlying economic realities of a unitary business,’ and the income must derive from ‘unrelated business activity’ which constitutes a ‘discrete business enterprise. . . .’” *Exxon* at 223–224, 100 S. Ct. at 2120, quoting *Mobil* at 439, 100 S. Ct. at 1232. Likewise in *Allied-Signal*, this Court said: “It remains the case that ‘[i]n order to exclude certain income from the apportionment formula, the company must prove that “the income was earned in the course of activities unrelated to [those carried out in the taxing] State.”’” *Allied-Signal* at 787, 112 S. Ct. at 2263, quoting *Exxon* at 223, 100 S. Ct. at 2120.

Fundamentally, this Court’s decision in *Mobil* requires that a court always examines a business’s economic substance and considers how that substance relates to the activity performed in the taxing state. By ensuring such a substantive review of business activity and its relation to the taxing state, the *Mobil* ruling enables the broader inquiry of “whether the taxing power exerted by the state bears fiscal relation to protection, opportunities and benefits given by the state.” *MeadWestvaco* at 25, 128 S. Ct. at 1505 (internal quotation marks omitted).

**C. As a Core Component of the Unitary-Business Principle, *Mobil* Should Apply to Pass-Through Entities.**

There is no reason for why this Court’s holding in *Mobil* should not be applicable to pass-through entities in the same way that it applies to corporations. Just as

with corporations, applying the *Mobil* ruling to pass-through entities ensures that the substance of the entity's underlying business activity is compared with the business being conducted in state. It also ensures that it is this substantive comparison, and not some latent attribute of the business's form, that determines apportionability.

It is appropriate for this Court to apply this ruling to pass-through entities. Regardless of business form, the analysis this Court required in *Mobil* plays the same role in guiding courts to enter decisions "logically consistent with the underlying principles motivating the [unitary-business] approach." *Allied-Signal* at 769, 112 S. Ct. at 2254, quoting *Container* at 167, 103 S. Ct. at 2941. Failing to apply *Mobil* to pass-through entities only serves to frustrate and limit this Court's unitary-business principle.

**D. Failing to Apply *Mobil* to Pass-Through Entities Would Produce an Uneven Application of this Court's Unitary-Business Test.**

This Court has been careful when interpreting the due process requirements placed on a state's ability to tax income so that the restraints apply broadly and evenly to all forms of business. *Allied-Signal* at 786, 112 S. Ct. at 2263. This Court has expressly stated that the unitary-business principle should apply to "new methods of finance and new forms of business" as they evolve. *Id.* It has also stated that "the form of business

organization may have nothing to do with the underlying unity or diversity of business enterprise.” *Mobil* at 440, 100 S. Ct. at 1233.

Taken all together, it is apparent that the intent of the Court is to make the unitary-business principle broadly applicable to all businesses, regardless of form. This intent would be upended if the *Mobil* ruling, a core component of the unitary-business principle, was not applicable to a category of businesses. By not applying *Mobil* to pass-through entities, this Court would develop a new and distinct branch of case law that would lead to an inconsistent application of the Due Process Clause. In short, pass-through entities and corporations would develop separate Due Process Clause standards for when they are taxable by a state which would inevitably lead to a pass-through entity escaping a tax that would otherwise apply to a corporation, or vice versa.

Such an uneven application of this Court’s unitary-business test would unnecessarily interfere in how businesses structure themselves and constitutes an erosion of a state’s income tax base. As there is no compelling reason to treat these categories of businesses differently from one another, the risks that come from allowing inconsistencies in the unitary-business principle to propagate far outweigh any benefit.

**E. The Idaho Supreme Court Decision Undermines the Due Process Clause.**

By ignoring *Mobil*, the Idaho Supreme Court’s decision frustrates the unitary-business principle and undermines the Due Process Clause. In its decision, the Idaho Court did not require that the Respondent provide evidence that its business activity was discrete from the activity of its subsidiary. To the contrary, the Idaho Court looked only to superficial evidence of inactivity and the form of the Respondent’s business investment to divine the absence of a unitary relationship between Respondent and its subsidiary. App. 27.

The Idaho Court took the definitional elements of a shell holding company—the lack of activity, lack of employees, lack of payroll, and lack of offices—and made this the basis for concluding that Idaho could not fairly apportion Respondent’s capital gain. App. 27. Just as with the *amici* in *Mobil*, the Idaho Court failed to “look principally at the underlying activity” and instead looked “at the form of investment, to determine the propriety of apportionability.” *Mobil* at 440, 100 S. Ct. at 1233. And unlike this Court’s decision in *Mobil*, the Idaho Court allowed the form of the investment to determine the apportionability of the income.

The decision of the Idaho Supreme Court is generally inconsistent with this Court’s more flexible and robust approach to determining apportionability. The exact business structure used by the Respondent in this case, a corporate holding company with two subsidiary pass-through limited liability companies, has

never come before this Court on state-and-local-tax due process grounds. Moreover, this Court has never directly considered the applicability of the unitary-business principle in a pass-through entity situation. But undoubtedly, and contrary to the Idaho Supreme Court decision, this Court's due process case law is flexible enough to apply to these "new forms of business." *Allied-Signal* at 769, 112 S. Ct. at 2254, quoting *Container* at 167, 103 S. Ct. at 2941. It was inappropriate for the Idaho Supreme Court to use Respondent's business structure to determine the case.

As in *Mobil*, the error of the Idaho Court's rationale comes into focus when looking past the business structure to the underlying business activity. As this Court has stated, "[t]he form of business organization" selected by Respondent "may have nothing to do with the underlying unity or diversity of business enterprise." *Mobil* at 440, 100 S. Ct. at 1233. Had Respondent chosen to operate the three legs of its commonly controlled group as "separate divisions of a legally as well as a functionally integrated enterprise, there is little doubt that the income derived from" the sale of the tactical gear division "would meet due process requirements for apportionability." *Mobil* at 440-441, 100 S. Ct. at 1233.

Consistent with *Mobil*, and with the evidence that was before the Court, the Idaho Supreme Court should have determined that neither Respondent's business structure nor its self-characterization of being a holding company evidenced a lack of a unitary business. Instead, it would have been more appropriate for the

Idaho Court to conclude that evidence detailing its corporate form is not affirmative evidence of a discrete business enterprise. In keeping with the holding in *Mobil*, the Idaho Court should have ruled that the taxpayer in this matter “had failed to sustain its burden of proving any unrelated business activity on the part of its subsidiaries . . . that would raise the question of nonapportionability.” *Mobil* at 442, 100 S. Ct. at 1234.

When viewed as a whole, the Idaho Supreme Court fundamentally misunderstood what it was doing when applying this Court’s due process jurisprudence. Instead of pursuing an inquiry into the relationship between two business units to determine whether Idaho’s attempt to tax the income bore a relationship to the “protection, opportunities and benefits given by the state,” the Idaho Court instead attempted a rote application of this Court’s unitary-business test. *MeadWestvaco* at 25, 128 S. Ct. at 1505 (internal quotation marks omitted). Such an attempt was bound to fail as any application of this Court’s due process case law should be tailored to the facts of the case and “logically consistent with the underlying principles motivating the approach.” *Allied-Signal* at 769, 112 S. Ct. at 2254, quoting *Container* at 167, 103 S. Ct. at 2941.

The consequence of the Idaho Supreme Court decision is that a “shell holding company” is immune from a state’s right to fairly apportion and tax income arising from interstate commerce. App. 27. The Idaho Supreme Court has attempted to limit its decision by stating that the “decision rests on a fact-intensive

inquiry based on the extensive—and largely undisputed—findings of the district court.” App. 29. However, this claim is belied by the simple and generic facts upon which the Idaho Court rests its opinion. The shell holding company of this case was not unitary because it was a shell holding company and because it lacked business activity. If the shell holding company of this case, one that is so maximally dedicated to the in-state business that it holds, cannot have its income fairly apportioned and taxed by Idaho, it is difficult to conceive of one that could.

As a result, Idaho now has a split unitary-business test, with certain forms of businesses being held to a different constitutional standard than others. Shell holding companies that mimic the attributes of Respondent will likely elude taxation under circumstances that would result in taxation for business that are not so organized. Such an uneven application of this Court’s case law produces unfair and inconsistent results that are detrimental to taxpayers and the state. By creating this inconsistency, the Idaho Supreme Court’s holding undermines the Due Process Clause.

## **II. Extending *Mobil* to Pass-Through Entities Would Resolve a Split Between State Courts.**

Just as with Idaho, New Jersey did not extend the logic of this Court’s *Mobil* decision to pass-through entities. *BIS LP, Inc. v. Dir., Div. of Taxation*, 26 N.J. Tax 489 (Super. Ct. App. Div. 2011). In that matter, the state of New Jersey argued that BIS, a partner in a

partnership, was unitary with the business performed by the partnership and could have its share of the partnership income fairly apportioned and taxed by New Jersey. *Id.* at 492–493. The partnership conducted business in New Jersey, “performing banking information solutions” in the state. *Id.* at 492. New Jersey sought to lay a fairly apportioned tax on the income arising from this in-state business activity that was routed into the hands of BIS which was headquartered out of state. *Id.* at 491–492.

BIS seems to have no discernible business activity separate from the partnership it was engaged in. BIS was a 99% limited partner in the partnership. *Id.* The other partner, BISYS, owned a 1% share of the partnership but was designated as the general partner. *Id.* These two entities appear to have been operated by the same group of executives. *Id.*

In contravention of this Court’s case law, New Jersey determined this case by looking primarily “at the form of investment, to determine the propriety of apportionability.” *Mobil* at 440, 100 S. Ct. at 1233. In its decision, the court did not perform any substantial review of BIS’s business to determine if its business activity was discrete from the partnership it was engaged in. Indeed, the evidence presented in that case all tended toward indicating that BIS did not have business activity discrete from the partnership. The court noted that “the partnership interest was BIS’s only or most substantial asset, and it produced BIS’s income.” *BIS* at 498. It also noted that BIS and its partner shared executives. *Id.* at 496. As in the case



presently before this Court, it appears that BIS lacked substantial independent business activity from its related entity.

Despite there being no evidence of a discrete business enterprise, the New Jersey court was persuaded that the partners were not unitary because of the labels used to describe them. BIS was described as “an investment company.” *Id.* at 500. Its partner was described as a “banking information data processing” business. *Id.* The New Jersey court failed to look beyond the labels used, and determined that

there was no functional integration nor economies of scale because BIS and [the other partner] were engaged in different businesses: BIS was an investment company (as the Director now concedes), and Solutions’ business was banking information data processing. Sharing a mailing address and certain corporate officers does not show that there was centralized management for Solutions and BIS.

*Id.* In short, the New Jersey court—just like the Idaho court—used the form of BIS’s investment to determine its apportionability. The court failed to apply the logic of *Mobil* in this case and failed to consider the broader inquiry of “whether the state has given anything for which it can ask return.” *MeadWestvaco* at 25, 128 S. Ct. at 1505 (internal quotation marks omitted).

New Jersey brought this latter failure to the court’s attention. New Jersey, citing to *MeadWestvaco*, asked the court to consider this case in a manner

consistent with the underlying due process principles. *BIS* at 499. It argued that an overly “formalistic application of the unitary business principle gives short shrift to the United States Supreme Court’s” due process case law. *Id.*

The court ignored New Jersey’s request. It seemed to not understand that the unitary-business test is not an end unto itself. In response to New Jersey’s urging, it merely recited elements of this Court’s unitary-business test as expressed in *Allied-Signal* and *Woolworth*. *Id.* at 499–500. In so doing, the court demonstrated the same kind of inversion that occurred in Idaho: this Court’s unitary-business test, intended to serve the due process’s broader inquiry, was used to avoid making such an inquiry.

In contrast to New Jersey and Idaho, Tennessee, in its decision in *Blue Bell Creameries v. Roberts*, 333 S.W.3d 59 (Tenn. 2011),<sup>3</sup> struck the right balance by relying on the *Mobil* ruling in its decision. In that matter, the Tennessee high court was asked a very similar question to the one Respondent presented to the Idaho courts: can a holding company that lacks substantial business activity be unitary with an operational company. *Blue Bell* at 62. Just as in the matter before this Court, the “only underlying activity generating income” for the holding company, BBC USA, was the sale and distribution of the product produced by the

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<sup>3</sup> A Tennessee appellate court also applied the *Mobil* standard to a later Tennessee case, *H.J. Heinz Co., L.P. v. Chumley*, No. M2010-00202-COA-R3CV, 2011 WL 2569755, at \*1 (Tenn. Ct. App. June 28, 2011).

operating company. *Id.* at 71. Similarly, just as with Respondent, BBC USA was a legally separate business entity that did not conduct any business operations of its own. *Id.* And just as in the present case, the taxpayer contended that BBC USA could not be unitary as its lack of activity made the application of the unitary-business principle impossible. *Id.* at 71–72

But where the Idaho Supreme Court failed to appropriately apply this Court’s controlling decisions, the Tennessee Supreme Court succeeded. Unlike the Idaho court, the Tennessee court correctly identified this Court’s holding as expressed in *Mobil*. In its analysis of this issue, the Tennessee high court correctly observed:

To determine whether two separate business entities form a unitary business, we must look beyond the superficial divisions between parent corporations and their subsidiaries to the “underlying activity” generating the income. See *Mobil Oil Corp. v. Comm’r of Taxes*, 445 U.S. 425, 440–441, 100 S. Ct. 1223, 63 L. Ed. 2d 510 (1980). To be an unrelated business activity, the separate business entity must constitute a “discrete business enterprise” from the taxpayer. *Exxon Corp.*, 447 U.S. at 223–224, 100 S. Ct. 2109.

*Id.* at 71. It proceeded to apply this standard, determining that BBC USA has not provided any “clear and cogent evidence showing that [it] operates a business enterprise that is discrete from” the operating company. *Id.* at 72. The Tennessee Court ruled that

Tennessee was entitled to conclude that the two entities were unitary as the taxpayer failed to meet the burden “the United States Supreme Court has placed . . . on the taxpayer challenging [a] tax assessment to demonstrate that the tax is unconstitutional.” *Id.* at 72, citing *Butler Bros. v. McColgan*, 315 U.S. 501, 507, 62 S. Ct. 701, 86 L. Ed. 991 (1942).

The Idaho Supreme Court, New Jersey intermediate court, and Tennessee Supreme Court decisions are in direct conflict with each other. Idaho and New Jersey both demonstrate a profound misunderstanding of how this Court’s due process case law should be applied. The effect of Idaho’s and New Jersey’s decisions is to subvert and disrupt the Constitution’s due process standards. In both cases, had the taxpayer operated its business as a single entity “there is little doubt that the [capital gain] income derived . . . would meet due process requirements for apportionability.” *Mobil* at 440–441, 100 S. Ct. at 1233. Consistent with *Mobil*, what these courts should have done is ignore the form and superficial aspects of the business and get back to the basic due process question of whether the state has provided something “for which it can ask return.” *MeadWestvaco* at 25, 128 S. Ct. at 1505 (internal quotation marks omitted).

This Court’s attention to this matter is required to ensure that multistate corporate taxpayers across the country are subject to the same uniform, constitutional principles wherever they are. Likewise, it is important for this Court to hear this matter to align

the States behind the same constitutional unitary-business standard.

Petitioner respectfully requests that this Court hear this matter and affirmatively apply its *Mobil* holding to pass-through entities.

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**CONCLUSION**

The Petition for Writ of Certiorari should be granted.

Respectfully submitted,

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