In the
Supreme Court of Ohio

Patton R. Corrigan,	:	Case No. 2014-1836
Appellant,	:	
vs.	:	On Appeal from the Ohio Board of Tax Appeals
Joseph. W. Testa, Tax Commissioner of Ohio	:	BTA Case No. 2012-3244
Appellee.	:	

REPLY BRIEF OF APPELLANT PATTON R. CORRIGAN

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

ARGUMENT

In Appellant's first Brief, the taxpayer argued that Ohio may only tax a non-resident's income to the extent that the taxpayer's income was earned in Ohio, and that Revised Code Section 5747.212 unconstitutionally attempts to tax income that is not earned in Ohio – specifically, a non-resident's capital gain on the sale of an ownership interest in a business that has some income earned in Ohio. Appellee Tax Commissioner's Brief, for reasons discussed below, has not shown either that Ohio may constitutionally tax a non-resident's income that is not earned in Ohio, or that an apportioned share of this taxpayer's capital gain on the sale of his interest in Mansfield Plumbing, LLC is income earned in Ohio and thus taxable by Ohio under this rule of constitutional law. Accordingly, we ask this Court to hold that Revised Code Section 5747.212, either facially or as applied to Appellant's tax refund claim, is unconstitutional.

Proposition of Law No. 1

The Due Process and Commerce Clauses of the United States Constitution prohibit a state from taxing the income of a non-resident unless that income is earned within the taxing state.

The Tax Commissioner's Brief fails to show that Ohio may tax non-residents income, except where the tax is "*upon incomes accruing to nonresidents from their property or business within the state, or their occupations carried on therein*". *Shaffer v. Carter*, 252 U.S. 37, 52 (1920) (emphasis added). The foregoing principle means that "[a] state may tax such part of the income of a non-resident as is fairly attributable either to property located in the state or to events or transactions which, occurring there, are subject to state regulation". *International Harvester Co. v. Wisconsin Department of Taxation*. 322 U.S. 435, 441 - 442 (1944). The Tax Commissioner has cited no cases overturning the above formulations; in fact, all of the authorities cited by the Tax Commissioner are consistent with the principle that a non-resident is taxable only upon income earned in the taxing state, meaning that the income is attributable either to property within the state or "events or transactions which, occurring [in the taxing state], are subject to [the taxing state's] regulation." *Id.*

The principle Ohio cases discussed in the Commissioner's Brief held that Ohio could tax income that clearly was earned from property in Ohio or from events or transactions which occurred in Ohio and thus are subject to Ohio's regulation. This Court held that Ohio lottery winnings are earned in Ohio and thus may constitutionally be taxed by Ohio in *Couchot v. State Lottery Comm'n*, 74 Ohio St.3d 421 (1996). Since Federal law prohibits the sale of Ohio lottery tickets outside of Ohio without Ohio's consent, an Ohio lottery ticket may only be purchased within Ohio. *See* 18 U.S.C. 1301. In fact, the taxpayer in *Couchot* purchased and redeemed the winning lottery ticket within Ohio. *Couchot,* 74 Ohio St.3d at 425. This Court, in *Couchot,* acknowledged the U.S. Supreme Court's admonition that Ohio's power to tax a non-resident extends to " 'such part of the income of a non-resident as is fairly attributable either to property located in the state or to events or transactions which, occurring there, are subject to state regulation . . .' ". *Id.* at 422 (quoting *International Harvester Co. v. Wisconsin Dept. of Taxation*, 322 U.S. 435, 441 - 442 (1944). Following this quote, this Court reasoned that "The Ohio lottery is an event exclusively within the power, dominion, and control of Ohio. . . . Only Ohio can generate, collect, and distribute the funds comprised by its lottery." 74 Ohio St.3d at 422. Since the taxpayer's Ohio lottery winnings resulted from "events or transactions which, occurring [in Ohio], are subject to

[Ohio] regulation," this Court's conclusion that Ohio may tax a non-resident's Ohio lottery winnings is consistent with the rule that Ohio may tax non-residents only on income from property within the state or from events or transactions occurring in Ohio.

A key part of the Tax Commissioner's argument is the assertion that Ohio may tax a non-resident's income under the theory that Ohio has given something "for which it can ask return," even if the income is not earned in Ohio. Appellee's Br. at 1, citing *Couchot*, 74 Ohio St.3d at 417 (quoting *Wisconsin v. J.C. Penney Co.*, 311 U.S. 435, 445 (1945). But neither *Wisconsin v. J.C. Penney* nor *Couchot* reaches this extreme conclusion. *Couchot,* as noted above, also cited and relied on the principle that Ohio may tax income resulting from property within Ohio or from events or transactions occurring in Ohio that are subject to Ohio's regulation. The U.S. Supreme Court's decision in *J.C. Penney* describes the general principle that a state's taxing power hinges on whether the state "has given anything for which it can ask return," but uses this principle to support the more specific rule upon which it decided that case: that the challenged statute taxed income " 'derived from property located and business transacted in' " Wisconsin, which made that income subject to Wisconsin's taxing authority. *See J.C. Penney*, 311 U.S. at 443 (quoting from the challenged Wisconsin tax statute). The tax challenged in *J.C. Penney* was upheld because "its measure as well as its incidence was related to" transactions in the taxing state. *Id.* at 446. More recent decisions of the U.S. Supreme Court adhere to this same rule that a state may only tax a non-residents income that derives from property or transactions in the taxing state. *See, e.g., MeadWestvaco Corp. v. Wisconsin Department of Revenue*, 563 U.S. 16, 19 (2008) ("The Due Process and Commerce Clauses forbid the states to tax 'extraterritorial values.' ") (*quoting from Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. 159, 164 (1983)). There are no U.S. Supreme Court decisions qualifying or overruling the specific rule that "[u]nder both the Due Process and Commerce Clauses of the Constitution, a state may not, when imposing an income tax, tax value earned outside its borders." *Container Corp.*, 463 U.S. at 164.

The Tax Commissioner's Brief also relies heavily on the *Johnson* case, decided by the Louisiana Supreme Court before *MeadWestvaco*. *Johnson v. Collector of Revenue*, 246 La. 540, 165 So.2d 466 (1964), *on rehearing;* Appellee's Br. at 14 – 15. As shown in Appellee's discussion of the *Johnson* case, however, that case involved the taxability of a gain realized by a shareholder on a transaction with the corporation in which the shareholder realized a gain on Louisiana land that had appreciated in value. Appellee's Br. at 14 – 15; *Johnson,* 165 So.2d 572 – 574. By contrast, Mr. Corrigan's gain was realized not in a transaction with Mansfield Plumbing LLC, but rather from a sale to another non-Ohio resident, and did not involve his receiving or realizing a gain on property located in Ohio. *See* Appellee's Br. at 3. Similarly, the Oregon court's decision in *Kulik*, like this Court's decision in *Agley*, involved the question of whether a pass-through entity owner is subject to a state's tax on "gross income of a non-resident derived from sources within this state." *Kulik v. Dept. of Revenue,* 290 Or. 507, 624 P.2d 93 (1981); Appellee's Br. at 15 - 16. The *Valentino* and *Prince* cases cited by Appellee similarly involved a non-resident shareholder's taxability on their distributive share of the income that the business which they owned earned within the taxing state. *See Valentino v. Franchise Tax Bd.*, 105 Cal.Rprtr. 304 (2001); *Prince v. State Dept. of Revenue*, 55 So.3d 273 (Ct. of Civil Appeals of Alabama 2010). None of these state cases deviates from the principal that a state may only tax a non-resident on income that is earned within the taxing state.

In short, Appellee's Brief and the authorities cited therein fail to refute the proposition of law that Mr. Corrigan, as a non-resident of Ohio, can only be taxed by Ohio on income which he earned in Ohio. As shown in the next section, the gain which Mr. Corrigan realized on the sale of his interest in Mansfield Plumbing LLC is not income earned in Ohio for purposes of this rule, and thus Ohio's assessment of income tax for his Federal taxable gain on that sale is unconstitutional.

<u>Proposition of Law No. 2</u>

R.C. 5747.212 violates the Due Process and Commerce Clauses of the United States Constitution because it attempts to tax a non-resident on income that is not earned within Ohio.

Just at the Tax Commissioner has failed to show that Ohio may tax Mr. Corrigan, a non-resident, on income he did not earn in Ohio, the Commissioner has not shown that Mr. Corrigan's Federal gain on the sale of his interest in Mansfield Plumbing LLC is income earned in Ohio under the case law construing the limits on Ohio's constitutional power to tax non-residents. Thus, R.C. 5747.212 is unconstitutional at least as it applies to Ohio's attempt to tax Mr. Corrigan's gain on the sale of his interest in Mansfield Pluming LLC.

As discussed earlier, income is earned within a state for purposes of constitutional limits on a state's power to tax if that income "is fairly attributable either to property located in the state or to events or transactions which, occurring there, are subject to state regulation". *International Harvester*, 322 U.S. at 441 – 442. The issue here is not income tax nexus – i.e., whether Mr. Corrigan is subject to an Ohio income tax -- but rather whether his gain from the sale of his interest in Mansfield Plumbing LLC is earned within Ohio and thus taxable by Ohio. There is no dispute that Mr. Corrigan would have been taxable by Ohio on his distributive share of Mansfield Plumbing LLC's Ohio income had it had positive earnings while he was an owner, or that he would have been subject to Ohio income tax on any compensation he received for services performed in Ohio as a manager (equivalent to a corporate director) of the LLC. In both of these situations, Mr. Corrigan would have had income earned in Ohio that it could tax. But, for reasons shown below, Mr. Corrigan's income from his sale of his interest in Mansfield Plumbing LLC is not income earned in Ohio and thus not taxable by Ohio.

There are two accepted methods for a state to determine the amount of taxable income earned within that state: "geographic accounting" (sometimes called "separate geographic accounting" or "separate accounting"), which attempts to isolate the income earned within each state; and apportionment, which allocates a portion of the taxpayer's total multistate income to the taxing state based on the ratio of certain in-state values to the total values for the enterprise. *See ASARCO Inc. v. Idaho State Tax* Com'n, 458 U.S. 307, 316 (1982). If and only if a taxpayer is engaged in a "unitary business," a state may determine the amount of the taxpayer's taxable income earned within that state by means of factor apportionment. *Id.; Allied-Signal, Inc. v. Director, Div. of* Taxation, 504 U.S. 768, 772 – 773 (1992). But "the linchpin of apportionability in the field of state income taxation is the unitary business principle." *Mobil Oil Corp v. Commissioner of Taxes of* Vermont, 445 U.S. 425, 439 (1980). If the taxpayer's business operations "formed part of a single unitary business," the state may compute the taxable income within that state using an apportionment method; otherwise, the state must use a geographic accounting method to determine the income earned in that state. *ASARCO*, 458 U.S. at 316.

Ohio determined the portion of Mansfield Plumbing, LLC's income (or, in this case, loss) that was earned in Ohio using a typical three-factor apportionment formula that apportions to Ohio a portion of the LLC's total income wherever earned based on the ratio of the LLC's Ohio payroll, property, and sales to the LLC's total payroll, property and sales. *See* R.C. 5733.05(B)(2), 5747.212. The theory underlying this is that Mansfield Plumbing was engaged in a single, unitary business in all of the states and countries in which it has payroll, property and sales, and that the LLC had income-producing activity (specifically, property, payroll, and sales) located both inside and outside of Ohio that contributed to the combined income of the unitary business. *See Mobil*, 445 U.S. at 438. We do not dispute that Mansfield Plumbing, LLC is engaged in a unitary business (manufacturing and selling "sanitary ware," Tr. 20 lines 6 - 9), and thus that Ohio may calculate its Ohio taxable income using an apportionment method. But, Mansfield Plumbing LLC was not engaged in a unitary business with its owners. The owners did not directly engage in the business of manufacturing and selling plumbing products, and did not own any other companies engaged in that business. Tr. 29 -30, lines 21 – 5 (Mr. Corrigan did not deal directly with customer or suppliers, and did not give direction to any employees except through the company president); Tr. 30 – 33. Lines 21 – 25 (other businesses owned partly by Mr. Corrigan were in different lines of business from Mansfield Plumbing, LLC, did not supply product to each other, and "have nothing to do with one another.") Yet, the method that R.C. 5747.212 attempts to apply to Mr. Corrigan's gain from sale of his LLC interest is an apportionment method, and one using apportionment factors based on the Ohio activities of Mansfield Plumbing, rather than the Ohio activities of Mr. Corrigan. *See* R.C.5747.212(B).

Apportioning a share of Mr. Corrigan's capital gain to Ohio is, as noted above, permissible only if that gain were attributable to a unitary business. It is not income earned in the course of a unitary business simply because Mansfield Plumbing LLC, the asset that Mr. Corrigan and his fellow investors sold, is engaged in a unitary business. Unlike the operating income of Mansfield Plumbing, LLC, this gain is the personal gain of the owner, not a gain of the business which is passed through to the owners. Mansfield Plumbing LLC did not buy or sell an interest in itself (distinguishing this situation from that of the taxpayer in *Johnson, supra,* 246 La. 540, 165 So.2d 466). Nor was the gain realized from a transaction taxed as a sale of the Mansfield Plumbing's assets, with the gains passed through to the LLC owners in the same manner as operating income (distinguishing this situation from that of the taxpayer in *Prince, supra,* 55 So.3d 273).

The Tax Commissioner's Brief argues that "the state may properly 'look through' the form of the business organization (in this case, Mansfield's organization as a limited liability company) and attribute Mansfield's Ohio business activities, property and income to Mr. Corrigan directly . . . because, for purposes of doing business, Mansfield Plumbing, LLC is merely a 'legal fiction'". Appellee's Br. at 9. While the Tax Commissioner relies on *Agley v. Tracy*, 87 Ohio St.3d 265, 268, 1999-Ohio-61 for this proposition, *Agley* in fact does not state that a corporation's business activities and property are attributable to its shareholders; rather, it holds that a shareholder's proportionate share of the corporation's income earned in Ohio may be taxed by Ohio, even though the shareholders themselves "did not personally participate in any business activities in Ohio." *Agley*, 87 Ohio St.3d at 268. *Agley* also does not stand for the proposition that a shareholder's income, other than that passed through from a business that has Ohio earnings, is taxable by Ohio merely because the shareholder's Ohio pass-through income is taxable. It certainly does not stand for the proposition that the shareholder's income may be attributable to the corporation (or limited liability company), or that the shareholder's (or LLC member's) income other than that passed through from the corporation (or LLC) may be taxed by Ohio based on the Ohio apportionment factors calculated for the corporation/LLC.

The Tax Commissioner's Brief completely misunderstands, and misapplies, the concept of "unitary business" and its significance to the present controversy. The Commissioner states that he "is not attempting to avail himself of the 'unitary business' principle. Instead, the Commissioner treated the income Mr. Corrigan earned from his majority ownership of his Mansfield business as a 'discrete business enterprise,' subject to Ohio apportionment using only the Mansfield business's property, payroll, and sales figures. . . . Only if the Commissioner . . . had sought to combine Mr. Corrigan's gains from his Mansfield business with his income from other interstate businesses or sources would the 'unitary business; principle come into play." Appellee's Br. at 28 – 29. The Commissioner cannot both say that Mr. Corrigan's income from sale of his business interest is apportionable to Ohio, and that he "is not attempting to avail himself of the 'unitary business' principle", because the U.S. Supreme Court has held that only income from a unitary business is apportionable. *See ASARCO*, 458 U.S. at 316. Mr.

Corrigan's income is apportionable to Ohio only to the extent that the apportioned income derives from a unitary business. As shown above, Mr. Corrigan's pass-through income (had their been any net income) derived from the LLC's Ohio taxable income which was part of a unitary business (manufacturing and selling "sanitary ware"), and thus may validly be apportioned. But, as shown below, Mr. Corrigan's income from his sale of an interest in the LLC is not a part of the same unitary business in which the LLC is engaged, and thus is not apportionable to Ohio. Since R.C. 5747.212 attempts to apportion to Ohio income that may not constitutionally be apportioned to Ohio, it is unconstitutional at least as applied to Mr. Corrigan and, we will show, facially as well.

MeadWestvaco shows that a taxpayer's gain from sale of a business is not apportionable to a state just because the operating income from the business that was sold could be apportioned to that taxpayer. The taxpayer in *MeadWestvaco* sold its Lexis operating division – not even a separate legal entity at the time of the sale – and realized a gain on that sale. *MeadWestvaco*, 553 U.S. at 20, 22. The *MeadWestvaco* Court held that Illinois could not tax an apportioned part of the taxpayer's gain on the sale of Lexis unless Lexis was part of a unitary business with the selling taxpayer. *Id.* at 30. Just like the corporate seller in *MeadWestvaco,* Mr. Corrigan is not engaged in a unitary business with Mansfield Plumbing LLC. "Where, as here, the asset in question is another business, we have described the 'hallmarks' of a unitary relationship as functional integration, centralized management, and economies of scale." *Id.* The testimony described above (Tr. 29 – 33) amply demonstrates that there is no functional integration between Mr. Corrigan's other business activities and Mansfield Plumbing, and no opportunities for economies of scale since the other businesses were in completely different lines of business and had no interaction with Mansfield Plumbing. As for "centralized management," the record does not show that Mansfield Plumbing was more subject to "centralized management" by its largest shareholder, Mr. Corrigan, than Lexis was to "centralized management" by its sole owner. In both cases, for example, a local management team managed the business that was later sold on a day-to-day basis. See *MeadWestvaco*, 553 U.S. at 21 – 22; Tr. 28, lines 11 – 19.

Mansfield Plumbing's existence as a separate, distinct business from Mr. Corrigan's other investments is no legal fiction: Mansfield's business existed, albeit in a different legal form, before Mr. Corrigan's acquisition of a controlling interest, and it continued to exist after he sold his interest. Tr. 25 - 27, lines 8 – 15; Tr. 33, lines 8 – 25; Tr. 34 – 35, lines 9 – 2. Mr. Corrigan testified that he and his fellow investors "decided to acquire [Mansfield Plumbing] in the form of an LLC . . . and hold it for investment purposes for a later sale." Tr. 33, lines 17 – 20. This is important because the U.S. Supreme Court has held that the sale of a business is not apportionable where, as here, the business served an investment function in the selling taxpayer's business, rather than an operational function. "The conclusion that the asset served an operational function was merely instrumental to the constitutionally relevant conclusion that the asset was a unitary part of the business being conducted in the taxing State rather than a discrete asset to which the State had no claim." *MeadWestvaco*, 553 U.S. at 29 – 30. To Mr. Corrigan, his interest in Mansfield Plumbing LLC served an investment, rather than an operational, function with regard to any business he himself was conducting. It was, therefore, not part of a unitary business with Mansfield Plumbing, and not apportionable to Ohio under *MeadWestvaco*.

We acknowledge, as the Tax Commissioner argues, that the *MeadWestvaco* opinion declined to address an alternative argument for upholding Illinois' assessment: "that Lexis did substantial business in Illinois and the Lexis' own contacts with the State suffice to justify the apportionment of Mead's capital gain." *MeadWestvaco,* 553 U.S. at 31. While the U.S. Supreme Court declined to address this theory, it also does not appear to have been adopted by the Illinois courts on remand or, as far as we can tell, by any other court. The failure of the Court to reject this argument outright in *Meadwestvaco* certainly affords no basis for this Court to accept it here.

In short, Mr. Corrigan was not engaged in a unitary business with Mansfield Plumbing LLC, and his investment in that LLC was not an asset of a unitary business which earned income within Ohio. As such, the income from the disposal of the investment (as distinct from the Ohio taxable income that passed through to Mr. Corrigan while he owned it) is not apportionable to Ohio. Since R.C. 5747.212 attempts to apportion part of this income to Ohio, notwithstanding that it is not an asset of a unitary business that Ohio may apportion, it is unconstitutional as applied to Mr. Corrigan.

The cases and arguments advanced by the Tax Commissioner do not undermine this conclusion. *Couchot*, as discussed above, addresses the Ohio taxability of payments made by the Ohio Lottery to its winners – not gains by lottery ticket holders on out of state sales of lottery tickets. *Couchot*, 74 Ohio St.3d at 418. Nothing in the *Couchot* decision would subject to Ohio income tax gain from the sale of a lottery ticket (a bearer instrument until it is redeemed) outside of Ohio by a non-Ohio resident. The example just given is more similar to the situation here: Mr. Corrigan, a non-Ohio resident, sold his interest in the LLC that owned Mansfield Plumbing to another non-Ohio resident, with no evidence that Ohio was involved in the actual sale of his interest.

The specific requirements of R.C. 5747.212 (that the taxpayer sold an interest in a business which itself had Ohio taxable income, and that the taxpayer owned a twenty percent or greater voting interest) do not show a constitutionally sufficient basis for taxing Mr. Corrigan's gain, and the specific facts here no not provide a constiutionally sifficient basis for Ohio to tax this gain. The statute does not require that the interest sold be part of a unitary business, and in fact Mr. Corrigan's gain was not a gain from an asset that is part of a unitary business. In contrast to the *Geoffrey* case cited by the Comissioner, Mr. Corrigan's ownership interest was not an asset used by Mansfiled Plumbing to earn income in Ohio: it was an asset which gives him certain rights with respect to Mansfield Pluming LLC and its income. *See Geoffrey, Inc. v. South Carolina Tax Comm.*, 313 S.C. 15, 437 S.E.2d 13 (S.Car. 1993) (tradenames and trademarks were actually used by the taxpayer in South Carolina to earn income there, so that royalty income from the use of those assets in South Carolina was taxable by that State). And, of course, it is irrelevant for constitutional purposes that, as Appellee complains, in the absence of R.C. 5747.212 neither Mansfield Plumbing nor its shareholders would be subject to Ohio income tax for years during which Mansfield Plumbing lost income. Mansfield Plumbing was subject to Commercial Activity Tax, property taxes, and sales taxes for its Ohio operations, and would have been subject to income tax as well had it had gains during this period. And, had Mansfield Plumbing been a C corporation, it would not have been subject to any tax on its Ohio income since repeal of the Corporation Franchise Tax.

We agree with the Tax Commissioner that "mobilia sequunter personam" is no longer the only consitutionally permissible basis for a state to tax income from an intangible, but disagree with his conclusion that it is no longer relevant. Further, none of the other constitutionally permitted methods for allocating or apportioning income from an intangible is present here, or is effectively utlized in R.C. 5747.212. For example, if an intangible asset is used directly by a business to earn income in a state, the state may tax the income generated from the use of that intangible asset in the state. *See Geoffrey*, 313 S.C. 15, 437 S.E.2d 13. Mr. Corrigan's LLC interest was not used in Ohio to generate income, and particulary was not used in Ohio to generate his income from the sale of that interest. As discussed at length above, income from intangible assets may be apportioned to a state if the income is earned from an asset used in a unitary business. *See MeadWestvaco*, 553 U,S, at 27. But, as shown above, the income Mr. Corrigan realized from the sale of his LLC interest was not income from an asset used in a unitary business and thus may not be apportioned to Ohio. And, of course, income that is earned in a state may be taxed by the recipient of that income, even if the taxpayer receives that Ohio income by virtue of the ownership of an intangible asset such as a lottery ticket. *See Couchot*, 74 Ohio St.3d at 420, fn. 5. And, even if one of these alternative grounds for taxing Mr. Corrigan's gain were present here, R.C. 5747.212 relies only on the apportionment ground, without the constitutionally essential requirement that the asset whose income is apportioned be an asset used in a unitary business.

Mr. Corrigan's gain on the sale of his interest in the LLC was "value outside its borders" that Ohio may not tax consistent with the Due Process and Commerce

Clauses. *Container Corp.*, 463 U.S. at 164. It did not result from property in Ohio (one of the ways that income may be earned in Ohio), since there is no basis for situsing his interest to Ohio. See *Shaffer v. Carter*, 252 U.S. 37, 52 (1920); *International Harvester Co.,* 322 U.S. at 441 - 442. It was an interest in a non-Ohio LLC, sold by a non-Ohio resident to another non-Ohio domiciliary. It was not an asset used to earn income in Ohio, but rather an ownership interest in a business that, based on its Ohio apportionment fraction, can attribute about 1/3 of its taxable income or loss to Ohio operations. There is no evidence that the sale occurred in Ohio, and no requirement in the statute that the sale occur here. Thus, the sale was not subject to regulation or control by Ohio, and thus cannot be said to result from a transaction that, occuring here, is subject to Ohio's regulation. *See International Harvester Co.,* 322 U.S. at 441 - 442. Ohio's only connection to the LLC itself, aside from its business operations here, is that the LLC is registered with the Ohio Secretary of State as a foreign LLC that may do business in Ohio. Tr. 25 lines 8 – 15; Appellant's Exs. 1 & 2. The ownership of the LLC requires no approval by the State of Ohio, and is only known to the state of Ohio through the LLC's tax filings, which disclose the owners and their distributive shares of income or loss. Appellee's Br. at 4; R.C. 5747.08(D). We cannot, on this basis, say that the income from the sale of the LLC interest resulted from property in Ohio or from transactions occuring in Ohio, and thus cannot say that the income from the sale of the LLC interest was earned in Ohio. *See International Harvester,* at 441 - 442. If the income from the sale was not earned in Ohio, then Ohio may not tax a non-resident on this income. *Id.*

R.C. 5747.212 is unconstitutional as applied to Mr. Corrigan's gain at issue because, as shown, it attempts to tax income that is not constitutionally apportionable to Ohio (since it results from the sale of a business that is not part of a unitary business with the seller) and that is not otherwise income "earned within Ohio" and thus subject to its income tax jurisdiction. Thus, the Tax Commissioner's Final Determination should be overturned, and Mr. Corrigan should receive the refund that he claimed for paying a portion of the taxes he was assessed under R.C. 5747.212. In the next section, we discuss further why R.C. 5747.212 is not only unconstitutional as applied, but is facially unconstitutional.

Proposition of Law No. 3

R.C. 5747.212 is facially unconstitutional, not just unconstitutional as applied to Mr. Corrigan, because it asserts a power to only income that Ohio cannot tax Without violating the Due Process and Commerce Clauses

It is constitutional for Ohio to apportion for its income tax purposes the gain from the sale of business if the seller does business with Ohio and the business that is sold is part of a unitary business with the seller. *MeadWestvaco*, 553 U.S. at 30. And, in fact, Ohio statutes other than 5747.212 do just that. If Mr. Corrigan, or any other taxpayer that is not a C corporation, has business income, Ohio can and will tax that taxpayer's income that is apportioned to Ohio based on a three-factor apportionment formula. *See* R.C. 5747.01(B), 5747.02(A), 5747.21. Mr. Corrigan would have Ohio business income if he had "income, including gain or loss, arising from transactions, activities, and sources in the regular course of a trade or business", including "income, gain, or loss from real property, tangible property, and intangible property if the acquisition, rental, management, and disposition of the property constitute integral parts of the regular course of a trade or business operation" provided that the business has property, payroll, or sales in Ohio. R.C. 5747.01(B), 5747.20. Further, Ohio-taxable "'Business income' includes income, including gain or loss, from a partial or complete liquidation of a business". R.C. 5747.01(B). In short, Ohio's income tax laws, without regard to R.C. 5747.212, would tax Mr. Corrigan on an apportioned share of his gain from the sale of his interest in Mansfield Plumbing if Mr. Corrigan himself were engaged in a regular course of business in Ohio and Mansfield Plumbing was an asset of that business.

What, then, does R.C. 5747.212 add? It asserts a power to tax income from a taxpayer who is not engaged in a regular course of a trade or business in Ohio, and who is not a resident of Ohio, if that income is earned from the sale of an interest in a business entity that itself has income that is taxable by Ohio. Since it applies to non-residents only, it is constitutional only to the extent that it taxes income that is earned in Ohio, including income that it is constitutional to apportion to Ohio. But, as shown above, it is constitutional to apportion income from the sale of a business to Ohio only if the business sold is in a unitary business with the business selling it. If the business sold is in a unitary business with the selling business, and that unitary business has property, payroll, or sales in Ohio, it is probable that the statutes described in the previous section would both make the selling business subject to Ohio income tax and subject an apportioned share of the gain on the sale to Ohio income tax. If the business sold is not a unitary business with property, payroll, or sales in Ohio, then it would not be constitutional for Ohio to apportion a share of the gain on the sale to Ohio for tax purposes. *See MeadWestvaco*, 553 U.S. at 30. Thus, statutes other than R.C. 5747.212 would subject the gain, or an apportioned share of that gain, to Ohio for state income tax purposes in those situations where it is constitutional to levy such a tax. Since R.C. 5747.212 goes beyond those statutes by asserting a power to tax a gain from the sale of a business ownership interest by a non-resident who is not doing business in Ohio and is not in a unitary business with a business that is doing business in Ohio, it goes beyond the other section of Ohio's income tax laws only in situations where Ohio lacks the constitutional power to tax. As such, it is facially unconstitutional, and should be struck down by this Court.

Conclusion

For the foregoing reasons, we repeat our request that this Court find both that R.C. 5747.212 is unconstitutional as applied to Mr. Corrigan's capital gain from sale of his interest in Mansfield, and is facially unconstitutional because it is plainly designed to assess taxes on non-residents in violation of the Commerce and Due Process Clauses.

Respectfully submitted,

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Patton R. Corrigan

CERTIFICATE OF SERVICE

I certify that a true and correct copy of the foregoing *Brief of Appellant Patton R. Corrigan* was served, via email attachment and via U.S. postage prepaid mail, this 28th day of April, 2015, upon the following:

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Appendix

Statutes Cited in Reply Brief Only

R.C. 5733.05(B)

(B) The sum of the corporation's net income during the corporation's taxable year, allocated or apportioned to this state as prescribed in divisions (B)(1) and (2) of this section, and subject to sections 5733.052, 5733.053, 5733.057, 5733.058, 5733.059, and 5733.0510 of the Revised Code:

(1) The net nonbusiness income allocated or apportioned to this state as provided by section 5733.051 of the Revised Code.

(2) The amount of Ohio apportioned net business income, which shall be calculated by multiplying the corporation's net business income by a fraction. The numerator of the fraction is the sum of the following products: the property factor multiplied by twenty, the payroll factor multiplied by twenty, and the sales factor multiplied by sixty. The denominator of the fraction is one hundred, provided that the denominator shall be reduced by twenty if the property factor has a denominator of zero, by twenty if the payroll factor has a denominator of zero, and by sixty if the sales factor has a denominator of zero.

The property, payroll, and sales factors shall be determined as follows, but the numerator and the denominator of the factors shall not include the portion of any property, payroll, and sales otherwise includible in the factors to the extent that the portion relates to, or is used in connection with, the production of nonbusiness income allocated under section 5733.051 of the Revised Code:

(a) The property factor is a fraction computed as follows:

The numerator of the fraction is the average value of the corporation's real and tangible personal property owned or rented, and used in the trade or business in this state during the taxable year, and the denominator of the fraction is the average value of all the corporation's real and tangible personal property owned or rented, and used in the trade or business everywhere during such year. Real and tangible personal property used in the trade or business includes, but is not limited to, real and tangible personal property that the corporation rents, subrents, leases, or subleases to others if the income or loss from such rentals, subrentals, leases, or subleases is business income. There shall be excluded from the numerator and denominator of the fraction the original cost of all of the following property within Ohio: property with respect to which a "pollution control facility" certificate has been issued pursuant to section 5709.21 of the Revised Code; property with respect to which an "industrial water pollution control certificate" has been issued pursuant to that section or former section 6111.31 of the Revised Code; and property used exclusively during the taxable year for qualified research.

(i) Property owned by the corporation is valued at its original cost. Property rented by the corporation is valued at eight times the net annual rental rate. "Net annual rental rate" means the annual rental rate paid by the corporation less any annual rental rate received by the corporation from subrentals.

(ii) The average value of property shall be determined by averaging the values at the beginning and the end of the taxable year, but the tax commissioner may require the averaging of monthly values during the taxable year, if reasonably required to reflect properly the average value of the corporation's property.

(b) The payroll factor is a fraction computed as follows:

The numerator of the fraction is the total amount paid in this state during the taxable year by the corporation for compensation, and the denominator of the fraction is the total compensation paid everywhere by the corporation during such year. There shall be excluded from the numerator and the denominator of the payroll factor the total compensation paid in this state to employees who are primarily engaged in qualified research.

(i) Compensation means any form of remuneration paid to an employee for personal services.

(ii) Compensation is paid in this state if: (I) the recipient's service is performed entirely within this state, (II) the recipient's service is performed both within and without this state, but the service performed without this state is incidental to the recipient's service within this state, (III) some of the service is performed within this state and either the base of operations, or if there is no base of operations, the place from which the service is directed or controlled is within this state, or the base of operations or the place from which the service is directed or controlled is not in any state in which some part of the service is performed, but the recipient's residence is in this state.

(iii) Compensation is paid in this state to any employee of a common or contract motor carrier corporation, who performs the employee's regularly assigned duties on a motor vehicle in more than one state, in the same ratio by which the mileage traveled by such employee within the state bears to the total mileage traveled by such employee everywhere during the taxable year.

(c) The sales factor is a fraction computed as follows:

Except as provided in this section, the numerator of the fraction is the total sales in this state by the corporation during the taxable year or part thereof, and the denominator of the fraction is the total sales by the corporation everywhere during such year or part thereof. In computing the numerator and denominator of the fraction, the following shall be eliminated from the fraction: receipts and any related gains or losses from the sale or other disposal of excluded assets; dividends or distributions; and interest or other similar amounts received for the use of, or for the forbearance of the use of, money. Also, in computing the numerator and denominator of the sales factor, in the case of a corporation owning at least eighty per cent of the issued and outstanding common stock of one or more insurance companies or public utilities, except an electric company and a combined company, and, for tax years 2005 and thereafter, a telephone company, or owning at least twenty-five per cent of the issued and outstanding common stock of one or more financial institutions, receipts received by the corporation from such utilities, insurance companies, and financial institutions shall be eliminated. As used in this division, "excluded assets" means property that is either: intangible property, other than trademarks, trade names, patents, copyrights, and similar intellectual property; or tangible personal property or real property where that property is a capital asset or an asset described in section 1231 of the Internal Revenue Code, without regard to the holding period specified therein.

(i) For the purpose of this section and section 5733.03 of the Revised Code, receipts not eliminated or excluded from the fraction shall be sitused as follows:

Receipts from rents and royalties from real property located in this state shall be sitused to this state.

Receipts from rents and royalties of tangible personal property, to the extent the tangible personal property is used in this state, shall be sitused to this state.

Receipts from the sale of electricity and of electric transmission and distribution services shall be sitused to this state in the manner provided under section 5733.059 of the Revised Code.

Receipts from the sale of real property located in this state shall be sitused to this state.

Receipts from the sale of tangible personal property shall be sitused to this state if such property is received in this state by the purchaser. In the case of delivery of tangible personal property by common carrier or by other means of transportation, the place at which such property is ultimately received after all transportation has been completed shall be considered as the place at which such property is received by the purchaser. Direct delivery in this state, other than for purposes of transportation, to a person or firm designated by a purchaser constitutes delivery to the purchaser in this state, and direct delivery outside this state to a person or firm designated by a purchaser does not constitute delivery to the purchaser in this state, regardless of where title passes or other conditions of sale.

(ii) Receipts from all other sales not eliminated or excluded from the fraction shall be sitused to this state as follows:

Receipts from the sale, exchange, disposition, or other grant of the right to use trademarks, trade names, patents, copyrights, and similar intellectual property shall be sitused to this state to the extent that the receipts are based on the amount of use of that property in this state. If the receipts are not based on the amount of use of that property, but rather on the right to use the property and the payor has the right to use the property in this state, then the receipts from the sale, exchange, disposition, or other grant of the right to use such property shall be sitused to this state to the extent the receipts are based on the right to use the property in this state.

Receipts from the sale of services, and receipts from any other sales not eliminated or excluded from the sales factor and not otherwise sitused under division (B)(2)(c) of this section, shall be sitused to this state in the proportion to the purchaser's benefit, with respect to the sale, in this state to the purchaser's benefit, with respect to the sale, everywhere. The physical location where the purchaser ultimately uses or receives the benefit of what was purchased shall be paramount in determining the proportion of the benefit in this state to the benefit everywhere.

(iii) Income from receipts eliminated or excluded from the sales factor under division (B)(2)(c) of this section shall not be presumed to be nonbusiness income.

(d) If the allocation and apportionment provisions of division (B) of this section do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may request, which request must be in writing and must accompany the report, a timely filed petition for reassessment, or a timely filed amended report, or the tax commissioner may require, in respect to all or any part of the taxpayer's allocated or apportioned base, if reasonable, any one or more of the following:

(i) Separate accounting;

(ii) The exclusion of any one or more of the factors;

(iii) The inclusion of one or more additional factors that will fairly represent the taxpayer's allocated or apportioned base in this state.

An alternative method will be effective only with approval by the tax commissioner.

Nothing in this section shall be construed to extend any statute of limitations set forth in this chapter.

(e) The tax commissioner may adopt rules providing for alternative allocation and apportionment methods, and alternative calculations of a corporation's base, that apply to corporations engaged in telecommunications.

R.C. 5747.01(B)

(B) "Business income" means income, including gain or loss, arising from transactions, activities, and sources in the regular course of a trade or business and includes income, gain, or loss from real property, tangible property, and intangible property if the acquisition, rental, management, and disposition of the property constitute integral parts of the regular course of a trade or business operation. "Business income" includes income, including gain or loss, from a partial or complete liquidation of a business, including, but not limited to, gain or loss from the sale or other disposition of goodwill.