

In the
Supreme Court of Ohio

T. RYAN LEGG IRREVOCABLE TRUST,	:	
	:	Case No. 2015-0917
Appellant/Cross-Appellee,	:	
	:	Appeal from Ohio Board of Tax Appeals
v.	:	
	:	BTA Case No. 2013-A-1469
JOSEPH W. TESTA,	:	
TAX COMMISSIONER OF OHIO,	:	
	:	
Appellee/Cross-Appellant.	:	

APPELLEE TAX COMMISSIONER'S MERIT BRIEF

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INTRODUCTION

The appellant T. Ryan Legg Irrevocable Trust (“Legg Trust” or “Trust”) sold its shares of stock in Total Quality Logistics, Inc. (“TQL”) during tax year 2006, but contests and refuses to pay Ohio income tax on the capital gain.¹ The Tax Commissioner properly assessed the Trust for its income tax liability on the capital gain, because the book value and location of TQL’s physical assets were “available” to the Trust and therefore the capital gain qualified as a “qualifying trust amount” to be included in the Trust’s Ohio taxable income pursuant to R.C. 5747.01(BB)(2)(a) and (6).

On appeal, the Ohio Board of Tax Appeals (“Board” or “BTA”) affirmed the Tax Commissioner’s final determination. See, *T. Ryan Legg Irrevocable Trust v. Testa*, BTA Case No. 2013-1469 (May 5, 2015), unreported, at 4 (“*BTA Decision and Order*”). The BTA correctly concluded that the book value and location of TQL’s physical assets are “available” to the Trust within the meaning of R.C. 5747.01(BB)(2)(a) and (6), and therefore, the BTA upheld the Trust’s Ohio income tax assessment liability for the 2006 tax year. This Court should affirm.

The book value and location of TQL’s physical assets were “available,” *i.e.* “ascertainable,” to the Trust as a matter of law. The Trust (including its trustee) enjoyed the right to inspect TQL’s books and records because the Trust was a 32.5% shareholder in the company. As this Court has explained, Ohio corporate law, namely R.C. 1701.37(C), provides

¹ The income at issue is the capital gain that the Legg Trust received from selling its shares of TQL stock, in the amount of \$18,614,242. The assessment also included other investment income that the Trust has not contested (and failed to pay tax on) in the amount of \$393,388, resulting in \$19,007,630 of total income for the Trust in 2006. The Commissioner imposed tax on Ohio’s “fair share” apportioned amount of that total income, *i.e.* $\$19,007,630 \times 0.918630 = \$17,508,352$. See, the Commissioner’s audit changes, at pages 85-86 of his statutory transcript of evidence certified to the BTA pursuant to R.C. 5717.02, T.Supp. 87-88.

that any and all shareholders have the right to examine the books and records of the company they own. *Alcan Aluminum v. Limbach*, 42 Ohio St.3d 121, 124 (1989).

Since the Trust acquired 32.5% of TQL stock under a Purchase Agreement in December 2005, the book value and location of TQL's physical assets were "available," *i.e.* ascertainable, to the Trust. See Purchase Agreement, at T.Supp. 297-408. Similarly, as a 50% shareholder prior to the Purchase Agreement, Mr. Legg, who is the Trust's grantor, also had access to TQL's books and records including the book value and location of TQL's physical assets.

Indeed, as the BTA expressly found, the Trust actually used the book value and location of TQL's physical assets to provide the Commissioner with the Trust's 91.8% Ohio apportionment ratio based upon the Trust's property, payroll, and sales factors. *BTA Decision and Order*, at 4. As a matter of fact and law, then, the book value and location of TQL's physical assets were "available" to the Trust. Against this foundation, the Trust's arguments to the contrary must fail, leaving the inescapable conclusion that Ohio's fair share of the gain is indeed apportionable to Ohio as a "qualifying trust amount." See, the Commissioner's Proposition of Law No. 1 below.

Moreover, even if the Trust could somehow establish that the book value and location of TQL's physical assets were not "available" to the Trust (which is directly refuted in law and fact), there are several alternative grounds for upholding the Commissioner's treatment of the Trust's income, as the BTA recognized in its decision below. See the Commissioner's Proposition of Law No. 2 below.

Further, the Trust's challenges to the constitutionality of the Commissioner's assessment and to the Ohio statutes fail for both substantive and jurisdictional reasons. Contrary to the Trust's suggestion, Ohio may constitutionally tax its apportionable share of the Trust's income

under the Due Process Clauses of the Ohio and U.S. Constitutions and the Commerce Clause of the U.S. Constitution. *Agley v. Tracy*, 87 Ohio St.3d 265, 266-67 (1999); *Couchot v. State Lottery Comm'n*, 74 Ohio St.3d 417, 421 (1996).

In fact, through extensive activity in Ohio, as the Trust's self-reported 91.831% apportionment ratio based upon property, payroll, and sales in Ohio demonstrates, the Trust has availed itself to Ohio's "benefits, protections, and opportunities" through TQL. The Trust extensively benefitted its Ohio resident beneficiaries, namely Mr. Legg and his family. The Due Process and Commerce Clause challenges therefore fail because the Trust is inextricably intertwined with Ohio and maintains close connections here. In addition, the Trust's Commerce Clause challenge fails because it was abandoned in the notice of appeal to this Court and may not be resurrected through briefing. *Deerhake v. Limbach*, 47 Ohio St.3d 44 (1989). See, the Commissioner's Proposition of Law No. 3.

Likewise, the Trust's Equal Protection challenge to R.C. 5747.01(BB)(4)(c) fails on its face because the Trust's notice of appeal failed to identify any class of similarly situated taxpayers, but instead merely complained of differential treatment of investors in S corporations and C corporations under Ohio tax law. But investors in electing S corporations differ fundamentally from investors in entities that have not elected "pass-through" status as S corporations. Simply put, "[t]he Equal Protection Clause does not forbid classifications. It simply keeps governmental decisionmakers from treating differently persons **who are in all relevant respects alike** (emphasis added)." *Park Corp. v. Brook Park*, 102 Ohio St.3d 166, 2004-Ohio-2237, ¶ 19, quoting *Nordlinger v. Hahn*, 505 U.S. 1, 10 (1992). An investor who chooses to invest in a corporation that has elected S corporation status is not similarly situated to

an investor that invests in a C corporation that has not elected “pass-through” status. See, the Commissioner’s Proposition of Law No. 4

Finally, the Legg Trust’s appeal to this Court fails for an independent jurisdictional reason: the Trust’s notice of appeal to the BTA is properly dismissed because the attorney who filed the appeal, Mark Loyd, lacked the requisite authorization to file the appeal from the trustee. Accordingly, because the BTA notice of appeal was invalid, the appeal to this Court is likewise invalid. As this Court has long held, the trustee of a trust has the exclusive authority to approve litigation on the Trust’s behalf. *Schofield v. Cleveland Trust Co.* 149 Ohio St. 133, 144 (1948) (“[t]he successor trustee *alone* was the proper person to bring an action to recoup funds which had been wrongfully and illegally diverted from the trust estate[.]”), citing Ohio General Code § 11244 (current Ohio Civ. R. 17(a)) (emphasis added); R.C. 5808.16 (X) (powers of trustee to prosecute a legal action).

In this case, the trustee of the Legg Trust did not give Mr. Loyd authority to file the petition for reassessment with the Commissioner or the BTA notice of appeal. Mr. Loyd argued before the BTA that the trustee has now “ratified” the filings, but he does not contest that the trustee did not provide authority at the time of filing. Mr. Loyd also has not provided an excuse for failing to obtain authority from the trustee at the time of filing. In addition, Mr. Loyd has not presented any probative and reliable evidence that the filings were actually ratified. Since the pleadings were not properly filed, the Trust failed to timely perfect its appeal rights and this appeal should be dismissed. R.C. 5747.13; R.C. 5717.02. In its decision below, the BTA unreasonably and unlawfully denied the Commissioner’s motion to dismiss the notice of appeal. The BTA’s decision is unreasonable and unlawful in this regard and this Court should dismiss

this appeal if the BTA and Commissioner are not affirmed on the merits. See, the Commissioner's Proposition of Law No. 5.²

STATEMENT OF THE CASE AND FACTS

A. Statement of Relevant Facts

T. Ryan Legg and his advisors created the appellant Legg Trust through a trust agreement on November 14, 2005, just weeks before the TQL stock sale at issue. See, Legg Trust Agreement, Ex. 1, at 1, T.Supp. 409-433.³ From its inception until January 28, 2008, U.S. Trust Co. served as the trustee of the Trust. Charles Schwab Bank took over as trustee on January 28, 2008 and served in that capacity until its removal on June 5, 2009. Ex. 17, at 1, Supp. 4. An unrelated entity, UBS Trust, then took over as trustee from June 5, 2009 through August 31, 2015, when UBS Trust merged with and into the current trustee, Reliance Trust Company of Delaware. T. Supp. 287; Ex. 17, at 3.

Total Quality Logistics, or TQL, is a Subchapter S corporation under the Internal Revenue Code that is and always has been an Ohio company headquartered in Cincinnati, Ohio. T. Ryan Legg and Kenneth Oaks began TQL in 1997 together as equal 50-50 partners, with Mr. Legg serving as CEO from the company's inception until late 2005. Hr. Tr. 60-61, T.Supp. 163; Hr. Tr. 66-67, T.Supp. 163-164. In February 2006, through a complex transaction involving

² This Court need not, however, consider this subject-matter jurisdictional ground defect, if it affirms the BTA's decision on substantive grounds. See, *Hafiz v. Levin*, 120 Ohio St.3d 449, 2008-Ohio-6788, ¶ 15, fn. 1 (having determined that the taxpayer's challenge based on its reading of a tax statute was substantively erroneous, the Court declined to consider jurisdictional issues).

³ For purposes of this brief, the statutory transcript of evidence that the Commissioner certified to the Board of Tax Appeals pursuant to R.C. 5717.02 will be referenced as "S.T. ___." Citations to the hearing transcript from the evidentiary hearing before the BTA will be referenced as "Hr. Tr. ___." The appendix to this brief will be referenced as "Appx. ___." The appellant's first supplement to the record will be referenced as "Supp. ___" and the Commissioner's second supplement will be referenced as "T. Supp. ___."

several trusts, Mr. Legg sold his 50% share in TQL to Mr. Oaks for \$28 million, which resulted in a nearly \$19 million capital gain for the Legg Trust. Hr. Tr. 87-88, T.Supp. 170; see also, the Purchase Agreement, Ex. F, at 110, T.Supp. 408 (“Stock Power”). The Commissioner now seeks to tax Ohio’s apportioned fair share of the income arising from that stock sale.

At the hearing before the BTA, Mr. Legg testified that the stock sale served the sole purpose of transferring his 50% interest in TQL to his 50% business partner, Mr. Oaks. Hr. Tr. 74, T.Supp. 167 (Legg testimony); see also, Hr. Tr. 213, T.Supp. 201 (testimony of attorney Kevin Ghassomian). Rather than transfer the shares directly to Mr. Oaks, Mr. Legg chose to first transfer the shares through a network of newly-created trusts. Tax avoidance is the purpose for creating the trusts. Mr. Legg and his accountant John Michel each testified that they are not aware of any business purpose for routing the shares through a network of trusts rather than directly to Mr. Oaks. Hr. Tr. 88, T.Supp. 170 (Legg testimony); Hr. Tr. 247-48, T.Supp. 210 (Michel testimony).

Through one document, a complex Purchase Agreement, Mr. Legg sold 100 TQL shares representing his 50% interest to Mr. Oaks for roughly \$28 million. 65 of the 100 shares, or 32.5% of TQL’s shares, flowed through the appellant T. Ryan Legg Irrevocable Trust (“Legg Trust” or “Trust”) to the “Oaks Stock Trust.” Ex. F, at 1, T.Supp. 1 (Purchase Agreement). The other 35 shares, or 17.5% of TQL, flowed through the similarly-named Legg Irrevocable Trust (“Legg Trust 2”) to the “Oaks Stock Trust.” Ex. F, at 1, T.Supp. 1. Mr. Oaks was the beneficiary of the Oaks Stock Trust.

On its 2006 Ohio tax return, the Trust recognized \$19,007,630 in income, including a \$18,614,242 capital gain arising from the TQL stock sale, but allocated the income entirely outside of Ohio. S.T. 85-86, 96-100, T.Supp. 87-88, 98-102 (Ohio Form 1041). Mr. Michel, the

Trust's tax preparer, actually had access to the TQL books and records when he prepared the Trust's 2006 Ohio income tax return. Hr. Tr. 226, 241, T.Supp. 205, 209. *BTA Decision and Order*, at 4. Indeed, upon audit, he actually used the very books and records at issue to calculate a three-factor Ohio apportionment ratio for the Trust, which again was approximately 92% because the Trust is so closely intertwined with Ohio. *BTA Decision and Order*, at 4.

B. Procedural Posture

Upon audit of the Trust's Ohio tax return, the Commissioner determined that the Trust's 2006 income including the gain from the sale of TQL stock is indeed apportionable to Ohio. Accordingly, on May 26, 2009, the Commissioner issued an assessment for the deficiency, including tax, interest, and penalty. S.T. 44, T.Supp. 46 (notice of assessment).

On June 20, 2009, Mr. Loyd and attorney Kevin Ghassomian, allegedly on behalf of the Trust, filed a petition for reassessment with the Commissioner, arguing that the book value and location of TQL's physical assets were *not* available to the Trust. S.T. 7-43, T.Supp. 9-45 (petition for reassessment). The petition incorrectly reflects that the trustee of the Trust is Charles Schwab Bank, when UBS Trust was actually the trustee of the Trust at that time. S.T. 8, T.Supp. 10; T. Supp. 287 ("Removal and Appointment of Trustee"). Mr. Loyd and Mr. Ghassomian did not obtain authority to file the petition for reassessment from the actual trustee at that time, UBS Trust. Mr. Loyd now argues that UBS Trust "ratified" the filing of the petition for reassessment and the BTA notice of appeal. As for the content of the petition, the Trust raised statutory and constitutional issues, many of which are presently before this Court.

On March 29, 2013, after reviewing the issues raised in Mr. Loyd's and Mr. Ghassomian's petition for reassessment, the Commissioner issued his final determination upholding the assessment. S.T. 1, T.Supp. 3(final determination). Citing *Alcan Aluminum v.*

Limbach with approval, the Commissioner determined that the Trust's gain from the stock sale was apportionable to Ohio as a "qualifying trust amount" under R.C. 5747.01(BB)(2)(a) because the TQL's books and records were unquestionably "available," *i.e.* ascertainable, to the Legg Trust as a matter of law and fact. S.T. 2, T.Supp. 4.

As an alternative basis for upholding his assessment, the Commissioner held that the Trust's gain is apportionable to Ohio under R.C. 5747.01(BB)(4)(c)(ii), even if the gain is not a "qualifying trust amount." That is because the gain arose from the Trust's sale of a pass-through entity. R.C. 5747.01(BB)(4)(c)(ii) provides for the apportionment of nonresident trust income arising from the sale of a "section R.C. 5747.212 entity," defined therein to include pass-through entities. Since TQL elected S Corporation status for the 2006 tax year, the Trust gain from the sale of TQL stock is subject to apportionment under that statute.

On May 28, 2013, Mr. Loyd appealed to the BTA, once again without authority from the trustee, UBS Trust. Because Mr. Loyd did not have authority to file the BTA notice of appeal or petition for reassessment on behalf of the Trust, the Commissioner filed a motion to dismiss the appeal. The content of Mr. Loyd's notice of appeal restated the statutory arguments in his petition for reassessment regarding the availability of TQL's books and records. In addition, Mr. Loyd maintained constitutional arguments regarding the alleged retroactivity of R.C. 5747.01(BB)(4)(c)(ii), as well as Due Process and Equal Protection challenges.

On May 21, 2014, following extensive written discovery, the BTA held a hearing on the Commissioner's motion to dismiss and, separately, a hearing on the merits of Mr. Loyd's notice of appeal. During the hearing on the motion to dismiss, Mr. Loyd refused to testify or to represent that he had authorization from the trustee of the Legg Trust to file the petition and notice of appeal. Hr. Tr. 40-48, T.Supp. 158-160. The BTA unreasonably and unlawfully

quashed subpoenas directed to Mr. Loyd and his then-co-counsel Bailey Ruese, but sustained a subpoena issued to Mr. Ghassomian. Hr. Tr. 26, T.Supp 155.

On May 5, 2015, the BTA issued its ruling on the motion and the merits of the Trust's appeal. The BTA first denied the motion to dismiss, surprisingly on the basis that Mr. Loyd's identification of the incorrect trustee on the petition and notice of appeal were "typographical errors." *BTA Decision and Order*, at 2. The BTA's ruling is clearly unreasonable and unlawful because Mr. Loyd did not even argue that he had authority to file at the time of filing or that the filings contained a typo. Instead, Mr. Loyd argues that the trustee "ratified" the filings.

The BTA proceeded to rule on the merits, finding that the Trust's gain on the sale of TQL stock gave rise to taxable Ohio income. In so ruling, the BTA identified three alternative bases for its decision. First, the BTA found that "the book value of TQL assets was available to the trust" and "utilized by the trust's tax preparer." *BTA Decision and Order*, at page 4. Relying on *Alcan Aluminum* and the definition of "available" in R.C. 5747.01(BB)(6), the BTA held that the gain constitutes an apportionable "qualifying trust amount" under R.C. 5747.01(BB)(2)(a).

As an alternative, the second basis for the BTA's holding is that the Trust had [modified] business income pursuant to the statutory definition of "business income." R.C. 5747.01(B) provides that business income includes a "partial or complete liquidation of a business," as through the Legg Trust's liquidation of its TQL stock. *BTA Decision and Order*, at 4. Thirdly, the BTA held that since Mr. Legg was a beneficiary of the Trust and resided in Ohio "from 2001 to mid-2006," the Trust resides in Ohio for Ohio income tax purposes. See, R.C. 5747.01(BB)(I)(3) (defining "resident" for trust purposes). As a result, its income, including the gain at issue, is taxable in Ohio pursuant to R.C. 5747.01(BB)(4)(c)(i).

On June 3, 2015, the Trust filed its notice of appeal to this Court contesting the BTA's decision and order. The Trust argues, among other things, that TQL's books and records were not "available" to the Trust. On June 15, 2015, the Commissioner timely filed a notice of cross-appeal because the BTA erred in failing to dismiss the appeal on the basis that Mr. Loyd lacked authority to file the petition for reassessment or the BTA notice of appeal on the Trust's behalf.

Any further facts, particularly those regarding the motion to dismiss, will be included in the Argument section that follows.

ARGUMENT

Proposition of Law No. 1:

Under R.C. 5747.01(BB)(2) and (6), a trust's capital gain income from the sale of stock in an Ohio corporation is a "qualifying trust amount" properly apportionable to Ohio when the trust is a 32.5% shareholder and the book value and location of the corporation's physical assets are actually "available" to the trust.

The Legg Trust's gain from the sale of its 32.5% interest in TQL is apportionable to Ohio as a "qualifying trust amount" under R.C. 5747.01(BB)(2)(a) because TQL's books and records, including the book value and location of its physical assets, were "available" to the Trust. For background, Section A initially lays out the statutory framework for Ohio taxation and apportionment of trust income.

Section B then explains that TQL's books and records were "available" to the Trust by virtue of the Trust's status as a TQL shareholder. The Trust's ability to ascertain TQL's books and records as a shareholder alone is sufficient reason to find that the records were "available" to the Trust and uphold the Commissioner's final determination. R.C. 5747.01(BB)(6) (defining "available"); *Alcan Aluminum v. Limbach*, 42 Ohio St.3d 121, 124 (1989).

The Trust's case is particularly weak because TQL's books and records were more than just ascertainable to the Trust; *the Trust actually used them*. Indeed, Section C details the extensive factual record upon which the BTA relied to determine that TQL's books and records were actually available to and used by the Trust. *BTA Decision and Order*, at 4. Section D concludes with an explanation that the Commissioner used a three-factor formula of property, payroll, and sales factors to apportion the Trust's qualifying trust amount to Ohio, which more accurately reflects the Trust's activity in Ohio than a default single-factor formula.

- A. For purposes of allocating and apportioning trust income under Ohio law, trust income may be characterized as a “qualifying trust amount,” “modified business income,” “qualifying investment income,” or “modified nonbusiness income.” R.C. 5747.01(BB).**

Ohio law provides special allocation and apportionment statutes for trusts, as opposed to individuals, estates, pass-through entities and other types of entities. In state and local tax law parlance, the word “allocate” refers to statutory mechanisms that trace income to the state of its source and include the income in full when determining of the income tax. But due to the reality of multistate and international commerce, income sometimes is not traceable to any one state. When income cannot be traced to one particular state, the word “apportion” refers to a statutory formula (often one reflecting payroll, property, and sales factors) that may be applied to a business's income to fairly reflect the income tax attributable to a particular state.

Under the allocation and apportionment statutes for trusts, the first inquiry into trust capital gain income is whether the income is a statutorily defined “qualifying trust amount.” See, R.C. 5747.01(BB) (“Any gain or loss that is not a qualifying trust amount is modified business income, qualifying investment income, or modified nonbusiness income, as the case may be.”). If the trust's capital gain income is indeed a “qualifying trust amount,” then the

income is apportionable to Ohio, normally through a single-factor formula that takes into account the qualifying investee's assets in Ohio and everywhere. R.C. 5747.01(BB)(4)(b).

If trust income is not a qualifying trust amount, then it may fall into one of three other categories dictating the proper allocation or apportionment methodology, as follows: modified business income, qualifying investment income, or modified nonbusiness income. R.C. 5747.01(BB). Modified business income means a trust's "business income" (as defined in R.C. 5747.01(B)) less any qualifying trust amounts. R.C. 5747.01(BB)(1). Qualifying investment income, briefly stated, refers to trust income that is passed through to a trust via its interest in pass through entity, such as a distributive share of income from a Subchapter S corporation. R.C. 5747.012(A). Modified nonbusiness income is the residual income that is not a qualifying trust amount, qualifying investment income, or modified business income. R.C. 5747.01(BB)(3).

B. Pursuant to R.C. 5747.01(BB)(2)(a), the Trust's capital gain income from the sale of TQL stock is a "qualifying trust amount" because the book value and location of TQL's physical assets in Ohio and everywhere were "available" to the Trust.

The Trust's capital gain income from its sale of TQL stock is apportionable to Ohio because it is a "qualifying trust amount" under Ohio income tax statutes for trusts. Specifically, R.C. 5747.01(BB)(2)(a) defines qualifying trust amount as follows:

(2) "Qualifying trust amount" of a trust means capital gains and losses from the sale, exchange, or other disposition of equity or ownership interests in, or debt obligations of, a qualifying investee to the extent included in the trust's Ohio taxable income, but only if the following requirements are satisfied:

(a) The book value of the qualifying investee's physical assets in this state and everywhere, as of the last day of the qualifying investee's fiscal or calendar year ending immediately prior to the date on which the trust recognizes the gain or loss, is available to the trust.

(b) [Pursuant to R.C. 5747.011(B), the trust held a greater than five per cent interest in the qualifying investee] for the trust's taxable year in which the trust recognizes the gain or loss.

(Emphasis added and bracketed language substituted).

Thus, the Trust's capital gain income is a qualifying trust amount if, in the conjunctive, it satisfies two requirements: *first*, the book value of the "qualifying investee's" physical assets are available to the trust; and *second*, the trust held at least a 5% share of the qualifying investee.

The parties agree that the second requirement is satisfied in this case. The Trust held a 32.5% interest in TQL, which is a "qualifying investee" as defined in R.C. 5747.01(BB)(5)(a), thereby far surpassing the 5% threshold under R.C. 5747.01(BB)(2)(b). The question presented here is whether the first prong of the statute is satisfied; namely, whether the book value of the qualifying investee's, *i.e.* TQL's, physical assets are "available" to the Trust.

1. **The book value and location of TQL's physical assets are "available" to the Trust under R.C. 5747.01(BB)(6), which clearly and unambiguously provides that "available" means "able to learn of the information."**

Pursuant to R.C. 5747.01(BB)(6), "available" is defined as follows:

'available' means information is such that a person is able to learn of the information by the due date plus extensions, if any, for filing the return for the taxable year in which the trust recognizes the gain or loss. (Emphasis added).

R.C. 5747.01(BB)(6) effectively codifies, for trust income tax purposes, this Court's holding in *Alcan Aluminum v. Limbach*, 42 Ohio St.3d 121, 124 (1989). The Court in *Alcan* addressed a situation just like this one, but in the Ohio corporation franchise tax context. The taxpayer, Alcan Aluminum ("Alcan"), realized a capital gain from the sale of its 50% interest in another company, F.A. Kohler Company. Under the Ohio corporate franchise tax, specifically R.C. 5733.051, Alcan was required to apportion its capital gain income in accordance with the

ratio of F.A. Kohler's physical assets in Ohio to F.A. Kohler's physical assets everywhere, *if the book value of F.A. Kohler's physical assets in Ohio and everywhere were available to Alcan*. If the books and records were not available to Alcan, a three-factor formula of Alcan's property, payroll, and sales would have applied.

Since F.A. Kohler held all its physical assets in Ohio, Alcan's Ohio apportionment factor was 1.0 if the books and records of F.A. Kohler were available to Alcan. In an effort to reduce tax liability through a lower Ohio apportionment ratio, Alcan argued that it did not have access to F.A. Kohler's records even though Alcan held a 50% ownership stake in the company.

This Court rejected Alcan's argument, holding that available means "ascertainable" to Alcan. *Alcan*, 42 Ohio St.3d at 124. And, since *any* shareholder of an Ohio corporation has access to the books and records of the corporation pursuant to Ohio corporate law, specifically R.C. 1701.37, Alcan could ascertain the book value of F.A. Kohler's physical assets in Ohio and everywhere. As a consequence, Alcan was required to apply a 1.0 Ohio apportionment factor to its capital gain income based upon the location of F. A. Kohler's physical assets in Ohio.

The "availability of physical assets" issue in *Alcan* is materially the same issue as here to determine whether the Trust's capital gain income is a "qualifying trust amount" under R.C. 5747.01(BB)(2). In other words, the definition of "available" matters to determine whether trust income is a qualifying trust amount apportionable to Ohio. R.C. 5747.01(BB)(2)(a). If the Trust is "able to learn of" the book value of TQL's physical assets in Ohio and everywhere, the Trust's capital gain is a qualifying trust amount apportionable to Ohio.

The Trust, as a 32.5% shareholder, clearly had access to the TQL books and records pursuant to R.C. 1701.37(C). As in *Alcan*, R.C. 1701.37(C) still provides that *any* shareholder of an Ohio corporation may examine the books and records of such corporation. 42 Ohio St.3d at

123. Under Purchase Agreement, the Trust acquired a 32.5% ownership share in TQL. Ex. F, p. 1, T.Supp. 1 (Purchase Agreement). Just as with any shareholder of an Ohio corporation, the Trust, as a 32% shareholder, of course had available to it the statutory right to examine the book value of TQL's physical assets. The Trust's income is thus taxable as a matter of law.

2. The Trust's attempts to distinguish *Alcan* are without merit. Further, the Trust's misplaced reliance on the BTA's *Random House v. Tracy* decision only reaffirms *Alcan*.

The Trust attempts to distinguish *Alcan* because the taxpayer in the case, *Alcan*, was a 50% shareholder in F.A. Kohler, whereas the Trust was a 32.5% shareholder in TQL. See, Trust merit brief, at 23. But any shareholder has the right to examine a company's books, as expressly provided in R.C. 1701.37(C). R.C. 1701.37(C) expressly provides that “[a]ny shareholder of the corporation . . . shall have the right to examine . . . [the corporation's] books and records[.]” (Emphasis added). And, a 32.5% stake in a company is a large stake in TQL in any event. By the Trust's line of reasoning, minority shareholders in Ohio corporations would have no ability to monitor internal affairs, contrary to well-established law.

The Trust's attempts to distinguish *Alcan* on the basis of the different statutes interpreted in each case are unavailing. R.C. 5747.01(BB)(2)(a) and (6) are clear and unambiguous, just as the Court in *Alcan* explained that the statute at issue there, R.C. 5733.051, “is not ambiguous.” *Alcan*, 42 Ohio St.3d at 123. This Court should not examine the “underlying legislative intent” as the Trust suggests because the statute is clear and unambiguous. Trust merit brief, at 20-21.

Even if this Court does consider the statute to be ambiguous, it should not be construed in the taxpayer's favor, as the Trust asserts. In *UBS Financial Services, Inc. v. Levin*, this Court explained that ambiguities in apportionment statutes should not be resolved in favor of the taxpayer because they are not tax imposition statutes that “define subjects of taxation.” 119 Ohio

St.3d 286, 2008-Ohio-3821, ¶¶ 32-35. Rather, “[a]ny particular construction of the apportionment [statute] might cut in favor of a taxpayer in one case but against a taxpayer in the next.” *Id.* at ¶ 33.

Further, apportionment statutes are remedial in nature and must be construed to effectuate their remedial purpose of determining Ohio’s “fair share” of a trust’s income. *Id.* at ¶ 35 (approving of the Commissioner’s construction of the statute because it “more closely realizes the ‘object sought to be attained’ by the apportionment) (citing to R.C. 1.49(A), *Rio Indal, Inc. v. Lindley*, 62 Ohio St.2d 283, 285 (1980), and *Champion Spark Plug Co. v. Lindley*, 70 Ohio St.2d 82, 85-86 (1982)).

In sum, R.C. 5747.01(BB)(2)(a) is not a tax imposition statute and ambiguities should not be construed in the taxpayer’s favor. Instead, as an apportionment statute, it is a remedial statute and therefore must be construed to most closely realize the object sought to be attained by the apportionment. That remedial purpose is to fairly determine Ohio’s “fair share” of trust income, as the Commissioner has done in this case.

Should this Court decide to entertain the Trust’s discussion of “legislative intent,” it may be quickly dismissed as without merit. In its merit brief, at page 21, the Trust suggests that, in *Alcan* and in this case, income will be allocated wholly outside of Ohio as nonbusiness income if the books and records at issue are not “available.” However, in *Alcan*, the consequence of “non-availability” was simply to apportion the dividend income using Alcan’s three-factor formula of property, payroll, and sales factors rather than a single-factor formula of F.A. Kohler’s assets. *Alcan*, 42 Ohio St.3d at 122. In other words, there was no question that some income could be apportioned to Ohio in *Alcan*. Similarly here, if TQL’s books and records are somehow not available, the capital gain income is still “modified business income” or “modified nonbusiness

income” taxable in Ohio. There is no “legislative intent” in R.C. 5747.01(BB) or the corporation franchise tax statute at issue in *Alcan* to allocate income outside of Ohio.

In a last ditch effort to find some legal authority to support its position, the Trust relies upon *Random House v. Tracy*, BTA Case No. 1991-A-1329. See, Trust merit brief, at 23-25. But by citing *Alcan* with approval, the *Random House* case is just additional authority for the Commissioner that defines “available” to mean “ascertainable.” In a short decision, the BTA in *Random House* considered whether Random House, Inc., a book publisher headquartered in New York, could allocate royalty payments outside Ohio for Ohio corporation franchise taxpayers. Under R.C. 5733.051(G)-(H), such payments are indeed allocable outside Ohio if the taxpayer could not ascertain the location of the royalty payor’s activities. Because Random House presented credible testimony that it could not ascertain such information from the payors, the BTA held that the location of the payor’s activities were unavailable to Random House.

The issue presented in the *Random House* BTA decision is in sharp contrast in pertinent respects with the *Alcan* issue that this Court addressed. When a shareholder has a capital gain from the sale of an equity stake in another company, as was the case with *Alcan*, and here, the books and records are necessarily ascertainable to the shareholder/taxpayer and therefore “available” pursuant to Ohio corporate law, R.C. 1701.37(C). The payee of royalty payments, by contrast, does not necessarily have access to the payor’s books and records. In short, *Random House* serves only to reaffirm that “available,” as applied to the present context, means ascertainable, a standard easily satisfied under the present facts.

Accordingly, *Alcan* and R.C. 5747.01(BB)(6) require the Commissioner to apportion the Trust’s capital gain income from the sale of its TQL stock to Ohio as a “qualifying trust amount”

under R.C. 5747.01(BB)(2)(a) because the location of TQL's physical assets are "available" to all TQL shareholders, including the Trust.

- C. Even if the Trust's status as a TQL shareholder is somehow insufficient in making the books and records "available," there is overwhelming evidence in the record to support the Board's dispositive factual findings that the Trust could, and did, gain access to TQL's books and records.**

The BTA relied upon a strong evidentiary record in holding that the Trust held a legal right to TQL's books and records (which include the book value and location of TQL's physical assets in Ohio and everywhere) and actually used the records to complete the Trust's tax return. *BTA Decision and Order*, at 4. Expressly, the Board found that "the book value of TQL assets was available to the trust" and "utilized by the trust's tax preparer" to complete the Trust's Ohio tax return. *Id.*; see also, Hr. Tr. 226, 241, T.Supp. 205, 209. These reasonable and lawful factual findings are dispositive that the Trust's gain was a "qualifying trust amount" under R.C. 5747.01(BB)(2) and (6) that is properly apportionable to Ohio. R.C. 5717.04; *Satullo v. Wilkins*, 111 Ohio St.3d 399, 2006-Ohio-5856, ¶ 14 (reasonable and lawful standard of review).

- 1. The Trust actually had access to the location of TQL's physical assets and the Trust's accountant, John Michel, used the records upon audit to complete apportionment schedules for the Trust's Ohio tax return.**

Mr. Michel, the Trust's tax preparer, testified that indeed he actually had access to TQL's books and records when he prepared the Trust's tax return for 2006. Hr. Tr. 226, 241, T.Supp. 205, 209. He further explained at BTA hearing that he used TQL's books and records to calculate the Ohio apportionment ratio for the Trust. Upon audit, Mr. Michel used TQL's books and records to provide the Commissioner with Ohio Form IT-2023 for the Trust's 2006 Ohio tax return containing a three-factor apportionment ratio, which is roughly 92%. Hr. Tr. 24, T.Supp. 154. The information for the property factor that Mr. Michel provided includes the information for the book value and location of TQL's physical assets in Ohio and elsewhere.

See also, apportionment schedules, at S.T. 90-93, T.Supp. 92-95. There is no question that the book value and location of TQL's physical assets are available to the Trust and that the Trust actually used the information.

The Trust's bald assertion in briefing that "the Trust never received [the book value of] TQL's physical assets" is just plain wrong. Trust merit brief, at 8. Mr. Michel can and did provide the information, and he did so on behalf of the Trust. Hr. Tr. 241, T.Supp. 209. Mr. Michel's cover letter to the Commissioner accompanying the apportionment schedules even states that he is submitting the schedules "on behalf of the above-referenced taxpayer [the Legg Trust.]" S.T. 129, T.Supp. 131.

Because the facts so plainly support the Commissioner's and the BTA's findings that the books and records were available to the Trust, the Trust has impermissibly attempted to add documents to the evidentiary record on appeal to this Court. See, U.S. Trust Affidavit, at Supp. 1-2. Specifically, the Trust's first supplement to the record filed with this Court wrongly includes an "Affidavit of U.S. Trust Company of Delaware" that this Court should not consider because that document was not introduced into evidence in the BTA proceedings.⁴ *RNG Properties, Ltd. v. Summit Cty. Bd. of Revision*, 140 Ohio St.3d 455, 2014-Ohio-4036, ¶ 22 (rejecting documents submitted on appeal that were not included in the BTA's record). The affidavit was also never subject to cross-examination because that document was provided after the BTA hearing and the affiant, a Managing Director of U.S. Trust Co., did not appear at hearing to provide testimony.

⁴ The Trust first produced the affidavit *after* the BTA hearing in this case through a pleading that it styled a "motion to dismiss," but is more accurately described as an out-of-rule surreply to the Commissioner's motion to dismiss. If the Trust's "motion to dismiss" were granted, they would lose the appeal. The Commissioner timely filed with the BTA a "motion to strike and for additional relief" in response. However, the BTA did not rule on the Trust's "motion to dismiss" and the Commissioner's response.

But even if this Court were to now consider the affidavit, it would not advance the Trust's case as the Trust claims. Trust merit brief, at 12-13. The affidavit's false statement that TQL never provided the book value and location of TQL's physical assets to the Trust is obviously not from the personal knowledge of the affiant. As discussed, the records were actually provided to the Trust on or before July 15, 2008, when the Trust provided the data to the Commissioner. S.T. 90-93, 129, T.Supp. 92-95, 131. At that time U.S. Trust Co. was not the trustee; instead Charles Schwab Bank was the trust at that time. Ex. 17, Supp. 1.

The problems with the affidavit extend even further. If, in fact, U.S. Trust Co. did not receive the information, it was because they failed to ask for the information, not because the location of TQL's physical assets were "unavailable." There is no evidence in the record that U.S. Trust was aware of the Ohio tax controversy. It is therefore hardly surprising if TQL did not provide U.S. Trust Co. with the books and records.

Had Mr. Legg and/or the Trust's advisors inquired into the availability of TQL's books and records at the time the Trust's Ohio tax return was initially filed, they also would have received the records. But they did not ask. See, testimony of Legg, Michel, and John Dovich, at Hr. Tr. 118, 241-42, 133-34, T.Supp. 177, 209, 181, respectively. Mr. Legg could have even told his advisors of the physical location of TQL's physical assets in Ohio and everywhere because he had personal knowledge. Hr. Tr. 111, T.Supp. 176. As a matter of law, moreover, Mr. Legg had access to the books and records pursuant to R.C. 1701.37(C) as a 50% TQL shareholder prior to the stock sale. Still further, Mr. Legg had access to the books and records as CEO of TQL until late 2005.

Clearly, TQL's books and records were *actually* available to the Legg Trust. The Board's finding that the records were available and actually used by the Trust is reasonable, lawful, and dispositive in the Commissioner's favor.

2. In addition, the Trust held contractual rights under the Legg Trust Agreement that gave it access to TQL's books and records.

The Trust and Mr. Legg enjoyed contractual rights that enabled them to access the location of TQL's physical assets through TQL's books and records. John Dovich, investment advisor to the Trust and Trust advisory committee member, agreed during his BTA testimony that the Trust has the right to inspect TQL's books and records. Mr. Dovich specifically agreed that the Legg Trust Agreement gave the Trust's "advisory committee," of which he was a member, the right to inspect TQL's books and records. Hr. Tr. 132, T. Supp. 181; Ex. 1, at 22 ("Inspection of the Records of the Businesses"), T.Supp. 430. Kevin Ghassomian, another advisor to the Trust, also served on the Trust's advisory committee and enjoyed the right to inspect TQL's books and records. Of course, the Trust was able to provide this inspection right through the Legg Trust Agreement because the Trust itself had inspection rights to TQL's records as a TQL shareholder.

Despite the overwhelming evidence that the Trust can and did access TQL's books and records, the Trust maintains that through another agreement, the Purchase Agreement, it is actually precluded from accessing the records. Trust merit brief, at 19-20. But that is not true. The Purchase Agreement simply provides the Trust with *additional* rights to the TQL books and records, after the closing of the sale from the Legg Trust to the Oaks Stock Trust.

Section 2.1 of the Purchase Agreement provides that if certain "Monetization Events" occur after the "Closing Date" of February 3, 2006 and prior to February 28, 2010, the "Seller," namely Mr. Legg and the Trust, have additional inspection rights to TQL's records. See,

Purchase Agreement, Ex. F, at 2, T.Supp. Based upon the Purchase Agreement, the BTA determined that the sale closed on February 3, 2006. *BTA Decision and Order*, at 3; Ex. F, at 110 (“Stock Power”), T.Supp. 298. Under Section 2.2 of the Purchase Agreement, “Monetization Events” include major TQL stock sales or sales of substantially all of TQL’s assets.

The Trust argues that the Purchase Agreement precludes the Trust from obtaining access to TQL’s books due to contractual language that grants the Trust an additional right to TQL’s books *after the Trust sells its shares*. See, Ex. F, at 3, T.Supp. 299 (Section 2.5). There is limiting language if “a Monetization Event has not occurred,” but that limiting language refers only to a limitation on the additional contractual right that the Trust obtained even after it sold its shares, *i.e.* after February 3, 2006. See, Ex. F, at 2, T.Supp. 298 (Section 2.2).

The fundamental point is familiar: the Legg Trust was a 32.5% TQL shareholder that enjoyed and actually exercised its right to inspect TQL’s books and records. Moreover, Ohio corporate law is clear that all shareholders enjoy the right to inspect a company’s books and records. R.C. 1701.37(C) uses the mandatory, not permissive, language “shall” in conferring the inspection right upon shareholders, as follows: “Any shareholder of the corporation . . . shall have the right to examine . . . [the corporation’s] books and records[.]” In other words, the Legg Trust agreement could not and did not vitiate the Trust’s right to inspect TQL’s records.

There is no question that the book value and location of TQL’s physical assets were available to the Trust and that the Trust in fact used that information. Given such availability, the Trust’s capital gain income on the sale TQL shares is apportionable to Ohio as a qualifying trust amount.

D. Pursuant to R.C. 5747.01(BB)(4), the Commissioner used an alternative three-factor formula to apportion the Trust's qualifying trust amount to Ohio.

A trust's qualifying trust amount is normally apportioned to Ohio based upon the ratio of the location of the "qualifying investee's," *e.g.* TQL's, physical assets in Ohio and everywhere. R.C. 5747.01(BB)(4)(a). But here, with the benefit of property, payroll, and sales figures in Ohio and everywhere, which Mr. Michel provided upon audit, the Commissioner used a three-factor formula apportionment method. Indeed, R.C. 5747.01(BB)(4) authorizes the Commissioner to use an alternative apportionment method in situations where, as here, such deviation is in the interests of equity and fairness.⁵

Unlike other situations, TQL's property, payroll, and sales data in Ohio and everywhere were provided to the Commissioner upon audit by Mr. Michel. Upon review of these figures presented on Ohio Forms IT 2023 for 2004, 2005, and 2006, TQL had roughly \$500 million in Ohio sales from 2004 to 2006 and several million dollars in Ohio payroll. S.T. 90-96, T.Supp. 92-98. Taking these factors into account is simply a more accurate reflection of TQL's Ohio activity than a single-factor property factor. In fact, many states and the Uniform Division of Income for Tax Purposes Act apply similar three-factor apportionment formulas precisely for this reason. *See e.g.* UDITPA, § 9, Appx. 179. With the benefit of this information, the Commissioner applied a three-factor apportionment formula using three year averages of payroll, property, and sales.

⁵ The pertinent language in R.C. 5747.01(BB)(4) is not designated under a subdivision of the statute. For purposes of clarity, the pertinent language is the following: "If the allocation and apportionment of a trust's income under divisions (BB)(4)(a) and (c) of this section do not fairly represent the modified Ohio taxable income of the trust in this state, the alternative methods described in division (C) of section 5747.21 of the Revised Code may be applied in the manner and to the same extent provided in that section."

The Trust contends that, because the Trust is organized under Delaware laws, “[a]ppportioning to Ohio all of the tax on the capital gain related to the sale of TQL stock grossly distorts *i.e.*, does not fairly reflect, the lack of connection with Ohio with the Trust and the stock sale.” Trust merit brief, at 38. However, the Trust seems to be under the mistaken impression that the Commissioner used a 1.0 apportionment ratio. Trust notice of appeal, at 3. The Commissioner actually used a 0.918, or roughly 92%, apportionment ratio based upon the three-year average of TQL’s property, payroll, and sales factors. S.T. 85-86, T.Supp. 87-88.

The Trust has never provided the apportionment ratio that it believes to be correct. As a result, the Trust has never, before the BTA or this Court, specified error sufficient to invoke the BTA’s or the Court’s jurisdiction over the “issue.” See, R.C. 5717.04; R.C. 5717.02; *Holiday Inns v. Limbach*, 48 Ohio St.3d 34, 37 (1990); *Hatchadorian v. Lindley*, 21 Ohio St.3d 66, 71 (1986) (taxpayer must show “manner and extent” of the claimed error). Further, it is a matter of pure speculation that the Trust’s alleged apportionment ratio is lower than the 92% actually applied; that is, a new apportionment ratio may actually result in additional liability for the Trust.

Based upon the foregoing, the Trust’s capital gain income for 2006 is a qualifying trust amount that should be apportioned to Ohio based upon the three-year average of a three-factor property, payroll, and sales formula pursuant to R.C. 5747.01(BB)(4) and R.C. 5747.212.

Proposition of Law No. 2:

A trust’s capital gain on the sale of its entire 32.5 percent interest in the stock of a corporation making a Subchapter S corporation election under the Internal Revenue Code is apportionable to Ohio as “modified Ohio taxable income” under R.C. 5747.01(BB)(4) even if the income is not a “qualifying trust amount” under R.C. 5747.01(BB)(2).

The Legg Trust’s gain from the sale of its TQL stock is apportionable or allocable to Ohio under R.C. 5747.01(BB) regardless of whether it is a “qualifying trust amount” under

R.C. 5747.01(BB)(2). That is, *as an alternative* to finding that the Trust has a “qualifying trust amount,” the income may be apportioned to Ohio as “modified Ohio taxable income” under R.C. 5747.01(BB)(4). By statute, “modified Ohio taxable income” includes “modified business income” and “modified nonbusiness income,” as defined in R.C. 5747.01(BB)(1) and (3).

The BTA found that that there are alternative bases for upholding the Commissioner’s final determination. *BTA Decision and Order*, at 3-5. Section A below discusses the first of these alternative bases, specifically that the Trust’s gain is apportionable to Ohio as “modified business income.” The Trust’s gain arose from the “partial or complete liquidation of a business” such that it falls within the definition of “business income” under R.C. 5747.01(B), which definition extends to trust income as “modified business income” through R.C. 5747.01(BB)(1). *BTA Decision and Order*, at 4-5.

The Trust’s gain is also apportionable or allocable to Ohio as “modified nonbusiness income” even if the income is not a qualifying trust amount or modified business income. Section C explains that the Trust’s gain is taxable in Ohio as “modified nonbusiness income,” regardless of whether the Trust is a resident or nonresident trust. R.C. 5747.01(BB)(4)(c). Since the Trust is a resident trust, as the Board found, then its nonbusiness income should actually be *allocated* in full to Ohio pursuant to R.C. 5747.01(BB)(4)(c)(i) under this alternative theory.

Accordingly, even *assuming arguendo* that the Trust’s gain is not a “qualifying trust amount,” the income is still apportionable to Ohio as “modified Ohio taxable income” for a variety of alternative reasons.

A. Even if the Trust's capital gain income is not a qualifying trust amount, the income is still apportionable to Ohio as "modified business income" under R.C. 5747.01(BB)(1).

Items of income that are not a "qualifying trust amount" may nonetheless be classified as modified business income. The Trust misconstrues the Board's findings when it argues that the Board held that the Trust's gain is both a qualifying trust amount and modified business income. Trust merit brief, at 26. The Board simply provided alternative bases for its central holding that Ohio law requires the taxation of the Trust's gain.

R.C. 5747.01(BB)(1) provides that "modified business income" means the business income included in a trust's Ohio taxable income after such taxable income is first reduced by the qualifying trust amount." (Emphasis added). Thus, if a trust's income is not a qualifying trust amount, then the analysis turns to whether the income is "business income." The definition of business income is provided in R.C. 5747.01(B), which reads, in pertinent part:

"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. (Emphasis added).

Here, the Trust's capital gain is business income as a "partial or complete liquidation of a business." Mr. Legg transferred his 50% interest in TQL to the Trust on December 5, 2005, just days after the Trust was created on November 14, 2005, and for the sole purpose of liquidating his interest in the company through a sale to his business partner Kenneth Oaks. Hr. Tr. 88. The Trust, in turn, liquidated its interest in TQL on February 1, 2006. *BTA Decision and Order*, at 5; Ex. F, at 110, T.Supp. 408 (Purchase Agreement). Due to the liquidation, the Trust has modified business income under R.C. 5747.01(BB)(1) apportionable to Ohio even if the income is not a qualifying trust amount.

The Trust counters that it is not a “business” within the meaning of R.C. 5747.01(B) and that “TQL was not partially or fully liquidated.” Trust merit brief, at 26-27. For support, the Trust misguidedly relies heavily upon a case that was superseded by the relevant statutory language, namely *Kemppel v. Zaino*, 91 Ohio St.3d 420, 423 (1994). That is, the relevant “partial or complete liquidation” statutory language in R.C. 5747.01(B) was a legislative response to *Kemppel* that superseded *Kemppel*’s central holding that the liquidation of a business constitutes nonbusiness income.⁶ Still, the Trust maintains that the “sale of stock” is not business income under the “anti-*Kemppel*” language. The Trust argues that only “the dissolution of a corporation or partnership via the sale of its assets” is business income, “not the sale of stock by a stockholder.” Trust merit brief, at 28.

But the General Assembly has expressly provided that the sale of stock *is* business income. In the same bill where the General Assembly enacted the “anti-*Kemppel*” language, it enacted R.C. 5747.212 and amended R.C. 5747.21 to provide a special apportionment formula for individual’s or corporate entity’s sale of stock in a pass-through or closely-held entity. R.C. 5747.212 provides for the apportionment, not allocation, of capital gain income from the sale of stock in a pass-through or closely held entity. Moreover, as amended, R.C. 5747.21 provides that “all items of business income” shall be apportioned pursuant to a three-factor formula in the Ohio corporation franchise tax statutes, “[e]xcept as otherwise provided under R.C. 5747.212[.]” That means that the capital gain income described in R.C. 5747.212 is a type

⁶ Through Am. Sub. S. B. 261, 124th G.A. (2002), Appx. 194-198, the Ohio General Assembly expanded the definition of “business income” under R.C. 5747.01(B) to include the following language: “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.” The new statutory language has the effect of legislatively superseding the end result in *Kemppel* because liquidation income is now characterized as business income rather than nonbusiness income.

of “business income,” namely a gain on the sale of a pass-through entity. Since such capital gain income is “business income” to an individual under R.C. 5747.212, then it should similarly be “modified business income” to a trust under R.C. 5747.01(BB)(1).

Therefore, as an alternative basis for apportioning the income to Ohio, the Trust’s gain is apportionable to Ohio as “modified business income.”

B. Even if the Trust’s capital gain income is neither a qualifying trust amount nor modified business income, then Ohio is still required to tax the income as “modified nonbusiness income.”

If the Trust’s gain on the sale of its TQL stock is not a “qualifying trust amount” or “modified business income,” then it is nonetheless “modified nonbusiness income” apportionable or allocable to Ohio. Pursuant to R.C. 5747.01(BB)(3), “modified nonbusiness income” is the residual of a trust’s income after excluding other types of trust income.

If the Trust’s gain is “modified nonbusiness income,” then Ohio must tax the gain. R.C. 5747.01(BB)(4)(c)(ii) is clear and unambiguous that, *even if the Trust is somehow a non-Ohio resident trust*, the Trust’s gain from the sale of stock in a pass-through entity, *i.e.* TQL, is apportionable to Ohio. If the Trust is a resident Trust, as the BTA expressly held, then the Trust has even greater tax liability than was assessed because the income is allocable 100% to Ohio as resident trust income (rather than the 92% apportionment ratio applied).

1. Even if the Trust is a nonresident trust, its gain from the sale of stock in TQL is apportionable to Ohio under R.C. 5747.01(BB)(4)(c)(ii) because TQL is a pass-through entity making the Subchapter S corporation election.

The Trust’s gain on the sale of its TQL stock is apportionable to Ohio even if this Court determines that the Trust is a nonresident trust with “modified non-business income.” R.C. 5747.01(BB)(4)(c)(ii) clearly and unambiguously provides that trust income from the sale of stock in a pass-through entity (included in the statutory definition of a “R.C. 5747.212 entity”)

is apportionable to Ohio. Since TQL is an S corporation, which is a pass-through entity, the Trust's gain from the sale of TQL stock is apportionable to Ohio. The Trust has never contested the plain meaning of R.C. 5747.01(BB)(4)(c)(ii). See, Trust merit brief, at 39.

The Trust argued before the BTA that R.C. 5747.01(BB)(4)(c)(ii) is unconstitutionally retroactive, but has abandoned that argument on appeal to this Court. Trust merit brief, at 39; *Deerhake v. Limbach*, 47 Ohio St.3d 44 (1989). In its appeal to this Court and merit brief, the Trust now argues that the Trust's gain is "nonbusiness income under R.C. 5747.01(C) and R.C. 5747.20(B)(2)(c). Trust merit brief, at 29-30; Trust notice of appeal, at 2. But the statutes that the Trust now relies upon are applicable only to individuals and estates, not trusts. R.C. 5747.20(B)(2)(c) apportions income for purposes of the nonresident credit provided in R.C. 5747.05. In turn, R.C. 5747.05 expressly provides that the nonresident credit provided therein "shall be allowed against the income tax * * * for individuals and estates[.]" Ohio statutes separately address trust income, primarily through R.C. 5747.01(BB).

The Trust's "Proposition of Law No. II" is therefore wholly without merit. The Trust's claim that its income is "nonbusiness income under R.C. 5747.01(C)" is entirely misplaced and cannot entitle it to relief. Even if the Trust were treated as an individual rather than a trust, its income from the sale of TQL would be apportionable to Ohio under a special apportionment statute for an individual's sale of equity in a pass-through entity, namely R.C. 5747.212.

Should the Trust attempt to resurrect its argument that R.C. 5747.01(BB)(4)(c)(ii) is unconstitutionally retroactive as applied to the gain at issue here, this Court should nevertheless reject it. The language at issue in the statute was enacted pursuant to a legislative amendment effective March 30, 2006, Am. Sub. H.B. 530, 126th G.A (2002), Appx. 199-201. The language at issue is the following underlined language is R.C. 5747.01(BB)(4)(c)(ii).

(c)(ii) With respect to a trust or portion of a trust that is not a resident as ascertained in accordance with division (I)(3)(d) of this section, the amount of its modified nonbusiness income satisfying the descriptions in divisions (B)(2) to (5) of section 5747.20 of the Revised Code, except as otherwise provided in division (BB)(4)(c)(ii) of this section. With respect to a trust or portion of a trust that is not a resident as ascertained in accordance with division (I)(3)(d) of this section, the trust's portion of modified nonbusiness income recognized from the sale, exchange, or other disposition of a debt interest in or equity interest in a section 5747.212 entity, as defined in section 5747.212 of the Revised Code, without regard to division (A) of that section, shall not be allocated to this state in accordance with section 5747.20 of the Revised Code but shall be apportioned to this state in accordance with division (B) of section 5747.212 of the Revised Code without regard to division (A) of that section.

The Trust may argue that the underlined language is unconstitutionally retroactive as applied to the Trust's stock sale. Specifically, the Trust may argue that the February 1, 2006 stock sale may not be subject to a law change effective March 30, 2006, even though the law change occurred during the taxable year. But that is incorrect because "antecedent facts," *i.e.* facts that occurred prior to the effective date of the statutory amendment, may be applied to determine current period tax liability.

For example, the Ohio corporate franchise tax itself fundamentally relies on such antecedent facts to determine current liability. The corporate franchise tax was imposed on the privilege of doing business in the current tax year and measured under either the "net worth" method or the "net income" method, each of which requires application of antecedent facts from the preceding taxable year to determine the taxpayer's prospective liability for the current tax year. R.C. 5733.01; R.C. 5733.05; R.C. 5733.06; *Bank One Dayton, N. A. v. Limbach*, 50 Ohio St. 3d 163, 167 (1990); *East Ohio Gas Co. v. Limbach*, 26 Ohio St. 3d 63, 67 (1986).

Even more telling, this Court has, repeatedly blessed the application of antecedent facts to determine current tax liability. Most recently, the Court in *J.M. Smucker, L.L.C. v. Levin*, 113 Ohio St.3d 337, 2007-Ohio-2073, upheld this principle in personal property context as follows:

*** [I]n valuing inventory in the current tax year, the "inventory valuation statutes may draw on the antecedent fact of holding inventory" during the prior year.

Id., at ¶22. (Emphasis added and internal citation omitted); *see also Schoenrade v. Tracy*, 74 Ohio St. 3d 200, 203-204 (1995); *Dery v. Lindley*, 57 Ohio St.2d 5 (1979).

In *United Eng. & Foundry Co. v. Bowers*, the Court held that "[a] statute is not retroactive merely because it draws on antecedent facts for a criterion in its operation." 171 Ohio St. 279, 282 (1960). There, a law change in October 1955 required personal property taxpayers to begin listing inventory that was previously exempt as "for storage only." The taxpayer attempted to exclude inventory for months prior to the law change, from January to September 1955 (at that time personal property was listed on a monthly basis). In refuting the taxpayer's retroactivity challenge, this Court blessed the Commissioner's listing of the inventory for all months – in other words, his use of antecedent facts to determine current liability.

The situation here with the Legg Trust is no different than the application of antecedent facts to law changes in *United Eng.*, *Schoenrade*, and *Dery*. The law change went into effect during the Trust's 2006 taxable year and draws upon events occurring at any time during that tax year, including the February 1, 2006 transaction at issue. Just as in *United Eng.*, the law change draws upon events occurring during the entire taxable year, including the portion of the taxable prior to the effective date of the law. Furthermore, the Ohio tax return at issue was not even filed until October 4, 2007, over 18 months after the transaction and the law change.

Therefore R.C. 5747.01(BB)(4)(c)(ii) is not unconstitutionally retroactive as applied to the Trust's stock sale and the Trust's gain is apportionable to Ohio under its plain meaning.

2. **If the Trust's gain from the TQL stock sale is "modified nonbusiness income," then the income should be allocated 100% to Ohio because the Trust is an Ohio resident trust.**

The Trust is an Ohio resident trust and Ohio provides for fully allocating resident trust income to Ohio. R.C. 5747.01(I)(3) defines "resident" for purposes of the Ohio income tax as applied to trusts.

R.C. 5747.01(I)(3) provides, in pertinent part:

- (I) "Resident" means any of the following ***
 - (3) A trust that, in whole or part, resides in this state. ***

For the purposes of division (I)(3) of this section:

(a) A trust resides in this state for the trust's current taxable year to the extent, as described in division (I)(3)(d) of this section, that the trust consists directly or indirectly, in whole or in part, of assets, net of any related liabilities, that were transferred, or caused to be transferred, directly or indirectly, to the trust by any of the following: ***

(ii) A person who was domiciled in this state for the purposes of this chapter when the person directly or indirectly transferred assets to an irrevocable trust, but only if at least one of the trust's qualifying beneficiaries is domiciled in this state for the purposes of this chapter during all or some portion of the trust's current taxable year

Thus, the Trust is an Ohio resident trust if: (1) the Trust consists of assets transferred to it by an Ohio domiciliary; and (2) the Trust has a qualifying beneficiary domiciled in Ohio.

First, the Trust has assets transferred to it by an Ohio domiciliary because Mr. Legg, an Ohio domiciliary in 2006, transferred TQL shares to the Trust under the Purchase Agreement. Ex. F, T.Supp. 297. "Domicile 'is generally defined as a legal relationship between a person and

a particular place which contemplates two factors: first, residence, at least for some period of time and, second, the intent to reside in that place permanently or at least indefinitely.” *Cunningham v. Testa*, 2015-Ohio-2744, ¶ 12, quoting *Schill v. Cincinnati Ins. Co.*, 141 Ohio St.3d 382, 2014-Ohio-4527, ¶ 24 (defining “common law domicile”).

Mr. Legg clearly had Ohio as his domicile in 2006 as he maintained a home in Ohio and intended to return to Ohio when he was away. In fact, Mr. Legg voted in Hamilton County, Ohio in the November 2006 general election and maintained a home with his family in Cincinnati, Ohio. Ex. S, T.Supp. 292-294 (certified voter records); Hr. Tr. 68-70, T.Supp. 165-166 (testimony of Mr. Legg); Ex. X, T.Supp. 295-296 (auditor records showing that T. Ryan and Denise Legg sold their Cincinnati home July 2007); Hr. Tr. 71, 266-67, T.Supp. 166, 214-215. The Trust has not contested that Mr. Legg indeed intended to return to his family in Ohio when he was away during 2006. The first prong is satisfied because Mr. Legg is the transferee who transferred assets, namely TQL shares, to the Trust.

Second, the Trust has a qualifying beneficiary domiciled in Ohio due to Mr. Legg and his family as well. R.C. 5747.01(I)(3)(c) identifies a “qualifying beneficiary” as a “potential current beneficiary” under I.R.C. 1361(e)(2). I.R.C. 1361(e)(2) defines a potential current beneficiary as follows:

For purposes of this section, the term “potential current beneficiary” means, with respect to any period, any person who at any time during such period is entitled to, or at the discretion of any person may receive, a distribution from the principal or income of the trust[.] (Emphasis added).

The Legg Trust Agreement identifies Mr. Legg and his family as the primary beneficiaries of the Trust. Ex. 1, at 6, T.Supp. 414 (Legg Trust Agreement). And, Mr. Legg’s wife was also an Ohio domiciliary during 2006. Ex. 1, at 6, T.Supp. 414. Thus, the Trust has

beneficiaries domiciled in Ohio, and “qualifying beneficiary” is defined pursuant to I.R.C. 1361(e)(2) to include Mr. Legg and his family. The second prong of the residency inquiry under R.C.5747.01(I)(3) is satisfied.

Accordingly, the Legg Trust was an Ohio resident trust during 2006 for purposes of the Trust’s income including the capital gain income from the sale of its TQL stock. Further, if the Court determines that the Ohio resident Legg Trust has modified nonbusiness income pursuant to R.C. 5747.01(BB)(3), the income should be allocated in full to Ohio pursuant to R.C. 5747.01(BB)(4)(c)(i), resulting in additional tax liability for the Trust.⁷

For these reasons, the Trust’s gain from the sale of its TQL stock is apportionable or allocable to Ohio even if this Court determines that the gain is not a “qualifying trust amount” under R.C. 5747.01(BB)(2)(a).

Proposition of Law No. 3:

Ohio may tax its fair share of a trust’s gain from the sale of an Ohio corporation incorporated, headquartered, and doing business in Ohio under the Due Process Clauses of the Ohio and U.S. Constitutions.

This Court has already held that Ohio may constitutionally tax income generated against a backdrop of the “benefits, protections, and opportunities” that Ohio provides. *Agley v. Tracy*, 87 Ohio St.3d 265, 266-67 (1999). As the Court held in *Agley*, “[t]he Due Process Clause ‘requires some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.’” *Id.*, citing *Miller Bros. Co. v. Maryland*, 347 U.S. 340 (1954).

In holding that Ohio may tax individual income generated through a company doing business in Ohio, the *Agley* Court held:

⁷ The BTA has the authority to “modify” the Commissioner’s final determinations under R.C. 5717.03. *Key Services v. Zaino*, 95 Ohio St.3d 11, 16 (2002).

[t]he determination of state taxing power generally involves the flexible application of several factors, such as the state's power, dominion, or control over that which it seeks to tax; the benefits, protections, and opportunities afforded by the state; and the social and governmental costs incurred by the state. In turn, these factors will play out differently depending upon the nature of the tax imposed and the activities of the taxpayer or tax-generating source. (Emphasis added.)

Agley, 87 Ohio St.3d at 266-267. Further, “[i]n the *International Harvester* case, the United States Supreme Court summarized the law by stating 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 and which are within the protection of the state and entitled to the numerous other benefits which it confers.’” *Couchot v. State Lottery Comm.*, 74 Ohio St.3d 417, 422, (1996), quoting *International Harvester Co. v. Wisconsin Dept. of Taxation*, 322 U.S. 435 (1944).

Because the Trust has a strong connection to Ohio and is in fact inextricably intertwined, Ohio may constitutionally tax the Trust's capital gain income from the sale of TQL stock. The Trust's gain is generated from the value that TQL created through its extensive activity in Ohio. TQL had millions of dollars in property, payroll, and sales in Ohio during 2004, 2005, and 2006. Due to such extensive activity, the three year average of the Trust's Ohio apportionment ratio is very high, roughly 92%. Furthermore, Mr. Legg, the grantor of the Legg Trust, was an Ohio resident during the 2006 tax year and during years prior. Given such extensive activity in Ohio, the Trust has benefitted from Ohio's “benefits, protections, and opportunities extensively” and is constitutionally subject to tax under controlling U.S. and Ohio Supreme Court precedent.

In its brief, the Trust further contends that the Commissioner's apportionment is unfairly apportioned to Ohio under the dormant Commerce Clause doctrine. But the Trust abandoned its arguments under the dormant Commerce Clause in its notice of appeal to this Court and the

arguments are now jurisdictionally barred for failure to “set forth the errors complained of” as R.C. 5717.04 requires. *Deerhake v. Limbach*, 47 Ohio St.3d 44 (1989).

Moreover, the arguments were not raised in the notice of appeal for good reason – they are without merit. The Trust is a resident trust that enjoyed substantial benefits from Ohio and its marketplace, as its gain was generated from the value that TQL developed through its extensive activity in Ohio. *Agley*, at 266-67; *Couchot*, 74 Ohio St.3d at 421. Accordingly, this Court should not consider the Trust’s Commerce Clause challenge and reject the Trust’s challenges under the Due Process Clauses of the Ohio and U.S. Constitutions.

Proposition of Law No. 4:

R.C. 5747.01(BB)(4)(c) does not violate the Equal Protection Clauses of the Ohio and U.S. Constitutions where an investor in an S corporation is treated differently than an investor in a C corporation because such investors are not similarly situated and such differential treatment rationally furthers the State’s legitimate interest in raising and stabilizing revenue.

The Trust raised an Equal Protection challenge that is predicated on a ruling under an alternative theory that the Commissioner has presented to support his final determination and assessment. Namely, the Trust contends that if the Commissioner and BTA are affirmed on the basis that the Trust’s gain from the sale of TQL stock is “modified nonbusiness income” allocable or apportionable to Ohio, then there is an Equal Protection violation. Otherwise, the Trust has posited a hypothetical question that is not subject to this Court’s review. But the Trust’s claim fails even if this Court makes the predicate findings to reach this issue. Ohio may treat investors in S corporations differently than investors in C corporations without running afoul of the Equal Protection Clause.

The Ohio General Assembly may pass laws that differentiate among classes of citizens. “The Equal Protection Clause does not forbid classifications. It simply keeps governmental

decisionmakers from treating differently persons who are in all relevant respects alike.” *Park Corp. v. Brook Park*, 102 Ohio St.3d 166, 2004-Ohio-2237, ¶ 19, quoting *Nordlinger v. Hahn*, 505 U.S. 1, 10 (1992).

In respect of the legislative-democratic process, courts give great deference to legislatively enacted laws when reviewing a statute on equal protection grounds. *Id.* “As a general rule ‘legislatures are presumed to have acted within their constitutional power despite the fact that, in practice, their laws result in some inequality.’” *Huntington Natl. Bank v. Limbach*, 71 Ohio St.3d 261, 262 (1994), quoting *McGowan v. Maryland*, 366 U.S. 420, 425-26 (1961); *GTE N., Inc. v. Zaino*, 96 Ohio St.3d 9, 11, 2002-Ohio-2984, ¶ 22. Courts are particularly deferential to the legislative process where the law at issue relates to the taxing power of the state, which is “fundamentally a legislative responsibility.” *Hillenmeyer v. Cleveland Bd. of Rev.*, Slip Opinion No. 2015-Ohio-1623, ¶ 30.

The starting point for any Equal Protection claim is to determine whether the entities the claimant seeks to compare are in fact similarly situated. Persons who are not similarly situated may be treated differently, without such differential treatment invoking Equal Protection review. *Vacco v. Quill*, 521 U.S. 793, 799 (1997) (noting that Equal Protection “embodies a general rule that States must treat like cases alike but may treat unlike cases accordingly”) (internal citation omitted); *GTE North, Inc.*, 96 Ohio St.3d at 11.

Investors in Subchapter S corporations are not similarly situated to investors in Subchapter C corporations. As an initial matter, the distinction is subject to an election, such that any corporation meeting threshold requirements may elect to be an S Corporation if it desires. When S corporation status is elected, however, the corporation, including its investors, must take the bitter with the sweet. Under the Internal Revenue Code, S Corporations benefit

because they are generally taxable only at the investor level, not the corporate level, but are subject to other limitations. Non-Ohio resident trusts are simply investors that experience tax consequences from the S corporation election; under Ohio law, that includes the treatment of capital gain income from the sale of S corporation shares. The Trust has not identified similarly situated taxpayers and the Equal Protection challenge fails on that basis alone.

Even assuming *arguendo* that investors of S corporations and C corporations are similarly situated, this Court should reject the Equal Protection challenge because the classification rationally furthers the State of Ohio's interest in raising and stabilizing tax revenue. *Park Corp*, 102 Ohio St.3d 166, ¶¶ 28-32, citing with approval *Fitzgerald v. Racing Assn.*, 539 U.S. 103 (2003). "Unless a classification warrants some form of heightened review because it jeopardizes exercise of a fundamental right or categorizes on the basis of an inherently suspect characteristic, the Equal Protection Clause requires only that the classification **rationaly further a legitimate state interest.**" *Nordlinger*, 505 U.S. at 2 (emphasis added). "The Equal Protection Clause does not impose an 'iron rule of equality.'" *Ohio Apt. Assn. v. Levin*, 127 Ohio St.3d 76, 86, 2010-Ohio-4414, ¶ 51. If Ohio taxation on a capital gain could be avoided simply by incorporating a trust in another state and transferring shares to it before the stock sale, it would be very difficult for the State to raise and stabilize revenue. Thus, R.C. 5747.01(BB)(4)(c) does not violate the Equal Protection Clauses of the Ohio and U.S. Constitutions even if the Court makes the predicate findings to reach this issue.

Proposition of Law No. 5:

The trustee of a trust has exclusive authority to authorize litigation on behalf of a trust and may not ratify the filing of pleadings, if at all, unless there is a justifiable excuse for the failure to authorize litigation prior to filing.

The BTA erred in failing to dismiss this appeal pursuant to the Commissioner’s motion to dismiss because the trustee of the Trust did not approve the filing of the Trust’s notice of appeal to the BTA or petition for reassessment before the Commissioner. The BTA unreasonably and unlawfully denied the Commissioner’s motion to dismiss due to “typographical errors” on the pleadings. But the pleadings plainly did not contain typos. The Trust’s identification of the incorrect trustee on the pleadings could not be typos because Mr. Loyd does not contest that he lacked authority to file at the time of filing; rather, he argued before the Board that the trustee has “ratified” the filings.

Since the filings were not properly filed, this Court should dismiss this appeal because the Commissioner, BTA, and derivatively this Court, lack jurisdiction over the matter. R.C. 5747.13; R.C. 5717.02; see also, *Cousino Constr. Co. v. Wilkins*, 108 Ohio St.3d 90, 2006-Ohio-162, ¶ 40 (rejecting a BTA finding of “typographical errors”). Section A below explains that only the trustee of a trust may authorize litigation and that Mr. Loyd did not obtain authorization to file from the trustee of the Trust at the time of filing. Instead, T. Ryan Legg authorized the filings, even though he is not the trustee and may not authorize litigation on behalf of the Trust. Section B then turns to five deficiencies with Mr. Loyd’s “ratification” defense.

- A. This appeal must be dismissed because the trustee did not authorize it. T. Ryan Legg, who is not the trustee, provided invalid authority for Mr. Loyd to file the petition for reassessment with the Commissioner and the BTA notice of appeal.**

The trustee of the Trust has the exclusive authority to approve litigation on the Trust’s behalf. *Schofield v. Cleveland Trust Co.* 149 Ohio St. 133, 144 (1948) (“[t]he successor trustee

alone was the proper person to bring an action to recoup funds which had been wrongfully and illegally diverted from the trust estate[.]”), citing Ohio General Code § 11244 (current Ohio Civ. R. 17(a)) (emphasis added); R.C. 5808.16 (X) (powers of trustee to prosecute a legal action).

But the trustee of the Trust did not authorize the filing of the petition for reassessment with the Commissioner or the BTA notice of appeal. The only evidence in the record on the matter is the uncontroverted testimony of David D. Ebersole that Mr. Legg provided the authority, albeit invalid, for the filings.⁸ Mr. Loyd made the idea that TQL’s books and records were not “available” from whole cloth and there is no reason to think, let alone evidence showing, that the trustee authorized such arguments. At BTA hearing, Mr. Legg additionally confirmed through his own sworn testimony that he alone pays the legal fees for this litigation. Hr. Tr. 97-98, T.Supp. 172. Since the pleadings were not properly filed, the Trust’s appeal rights have not been timely perfected and this appeal should be dismissed. R.C. 5747.13; R.C. 5717.02.

B. UBS Trust, which was the trustee of the Trust as the time of filing the petition for reassessment and BTA notice of appeal, may not, and did not, “ratify” the filings.

Mr. Loyd argued that the trustee “ratified” the filings during the Board’s proceedings. But that argument fails because there is no evidence of ratification or any justifiable excuse for lacking authority at the time of filing. There are at least five reasons that Mr. Loyd’s ratification defense fails, as detailed below.

⁸ Mr. Ebersole provided his testimony by affirming his affidavit attached to the Commissioner’s motion to dismiss at the BTA hearing on the motion. See, Ebersole Affidavit, T.Supp. 251-293; Hr. Tr. 38, 158. The affidavit attests to conversations between Mr. Ebersole and Mr. Loyd and his co-counsel while this appeal was pending before the BTA. The attorney examiner ruled at hearing that the affidavit was “already in the record.” Hr. Tr. 38-39, T. Supp. 158.

1. **The trustee may not ratify this litigation pursuant to Civ. R. 17(A) because Mr. Loyd has unclean hands with respect to his failure to obtain authority to file at the time of filing.**

In support of his ratification argument, Mr. Loyd has argued that the BTA has equitable jurisdiction through Ohio Civ. R. 17(A), Appx. 111, which provides as follows:

Real party in interest. * * * No action shall be dismissed on the ground that it is not prosecuted in the name of the real party in interest until a reasonable time has been allowed after objection for ratification of commencement of the action by, or joinder or substitution of, the real party in interest. * * * (Emphasis added).

Through his “ratification” argument, Mr. Loyd argues that he should be permitted to invoke the Commissioner’s and BTA’s jurisdiction as follows: first, by knowingly filing a petition for reassessment and BTA notice of appeal without authority from the real party in interest, here the trustee of the Legg Trust, and second, by alleging, without any probative and reliable evidence, that the trustee ratified the filings long after the appeal windows under R.C. 5747.13 and R.C. 5717.02 have closed.

That is simply not the law, especially given that ratification under Civ. R. 17(A) is an equitable rule and the BTA does not have equitable jurisdiction. Further, there is no injustice in this case, which matters because ratification under Civ. R. 17(A) is an equitable rule to be applied only where required in the interests of justice. *Ohio Central Railroad System v. Mason Law Firm Co.*, 182 Ohio App.3d 814, 2009-Ohio-3238, Appx. 64-75. In *Ohio Central Railroad System*, the Tenth District Court of Appeals expressly held:

When determination of the correct party to bring the action was not difficult and when no excusable mistake was made, the last sentence of Rule 17(a) is inapplicable and the action should be dismissed.

Id. at ¶¶ 39-40 (emphasis added and internal citations omitted); *see also Wells Fargo Bank, N.A. v. Sessley*, 188 Ohio App.3d 213, 220-21, 2010-Ohio-2902, Appx.76-88. Thus, ratification

under Civ. R. 17(A) is not available to parties who have unclean hands for making an inexcusable mistake by knowingly failing to obtain authority for filing from the real party in interest.

Here, Mr. Loyd has no excuse, let alone a justifiable one, for failing to obtain authority from UBS Trust to file the petition and BTA notice of appeal, even though UBS Trust was the trustee at the time of filing. T. Supp. 287; Ex. 17, at 3. Mr. Loyd's unclean hands are particularly evident in this case because he and his colleague Kevin Ghassomian did not attempt to obtain authority for the petition for reassessment until the Commissioner raised the issue. Rather than obtain authority from UBS Trust, Mr. Loyd and Mr. Ghassomian indicated on the petition for reassessment that "Charles Schwab Bank" was the trustee by identifying the address for the Trust as follows: "T. Ryan Legg Irrevocable Trust c/o Charles Schwab Bank." S.T. 7-8 (petition), T.Supp. 9-10.

Charles Schwab plainly was not the trustee of the Trust when the petition was filed on July 20, 2009; instead the trustee of the Trust was UBS Trust. Charles Schwab was removed as trustee on June 5, 2009, several weeks prior to the filing of the petition for reassessment. Supp. 4. Furthermore, Mr. Loyd made no effort to correct his petition through the BTA notice of appeal, or even obtain authority for the BTA notice of appeal. Instead, Mr. Loyd simply stated in the BTA notice of appeal that "U.S. Trust Company" was the trustee "[a]t all times relevant herein," with reference apparently to 2006. BTA notice of appeal, at 2, Appx. 2.

In other words, Mr. Loyd did not properly identify the trustee to the Commissioner through his petition for reassessment. Nor did he attempt to correct the error or notify the Commissioner until the Commissioner inquired into the matter for several weeks during the proceedings before the BTA and eventually filed a motion to dismiss. See, the uncontroverted

affidavit of David D. Ebersole, T.Supp. 251-293. Simply put, Mr. Loyd may not ratify this litigation because he has unclean hands and there is no injustice to remedy through ratification.

2. Mr. Loyd has not provided *any* probative and reliable evidence to show that UBS Trust, as trustee of the Legg Trust, actually attempted to ratify this litigation.

There is no evidence, let alone probative and reliable evidence, that the trustee ever actually attempted to ratify the petition and BTA notice of appeal. The Commissioner subpoenaed and noticed for deposition Mr. Loyd and his then-co-counsel Bailey Roesse to testify at the hearing on the motion to dismiss, but they refused to testify and the Board unreasonably and unlawfully quashed their subpoenas. UBS Trust was not timely identified as trustee of the Trust, such that the Commissioner could not timely request a subpoena directed to UBS Trust representatives in accordance with the BTA's rules. Ebersole Affidavit, at ¶ 11, T.Supp. 254.

Rather than testify or provide testimony from someone else, Mr. Loyd "marked for purposes of identification," *but did not introduce into evidence*, a letter allegedly from UBS Trust Officers Seane Baylor and Richard Kemp. Hr. Tr. 40, 48, T.Supp. 158, 160. Because the letter was not introduced, it was not admitted into evidence at the BTA's hearing on the Commissioner's motion to dismiss. Hr. Tr. 48. Thus, it is not a part of the evidentiary record before this Court.

The letter is also highly objectionable. Hr. Tr. 40-41, T.Supp. 158 (objections). The letter does not state that it is based upon personal knowledge, but nonetheless asserts that UBS Trust ratified the present litigation. The letter also refers to "UBSTC," UBS Trust Co., rather than use the first person pronoun "I" that would suggest the letter is from personal knowledge. Even if the letter were admitted into evidence, the letter is not probative and reliable evidence because it is not from personal knowledge. Ohio Evid. R. 602, Appx. 120-122; *State ex rel.*

Sekermestrovich v. Akron, 90 Ohio St.3d 536, 538 (2001); see also Civ. R. 56(E). Also, the letter was not subject to cross-examination by the Commissioner because UBS Trust and the UBS Trust officers were not present at the BTA hearing.

The letter further fails to state whether the signers reviewed any documents pertaining to the litigation or was aware of any details of the present tax controversy. The letter's signers simply recite that some unidentified person at UBS Trust "ratified actions" taken by Mr. Loyd in this litigation. However, it does not identify those actions, or any underlying facts. There is no suggestion that UBS Trust knows what actions it is attempting to ratify or the subject matter of this appeal, or that it has reviewed the petition or BTA notice of appeal. Hr. Tr. 15, T.Supp. 152. The Commissioner also objected to the letter as hearsay, perhaps multiple levels of hearsay. Barton A. Hubbard, as counsel for the Commissioner, stated at hearing with respect to the UBS Trust letter that the source of the statements in the letter and affidavit are almost certainly Mr. Loyd himself. Hr. Tr. 30, T.Supp. 152 ("they put the words in the mouth of the trustee"). Mr. Loyd has never asserted anything contrary to Mr. Hubbard's statements on this point. Accordingly, the letter is not reliable and probative evidence based upon personal knowledge, nor included in the record, and this Court should not consider it.

Likewise, this Court should not consider an "affidavit" from UBS Trust that Mr. Loyd submitted to the Board through the Trust's written response to the Commissioner's motion to dismiss, which was filed after the BTA's hearing on the motion. The "affidavit" shares the same defects discussed with respect to the UBS Trust letter, including that it was not included in the Board's record and may not be considered on appeal. *RNG Properties, Ltd.*, at ¶ 22. Thus, there is no probative evidence before this Court that UBS Trust even attempted to ratify this litigation and this case must be dismissed. *Olentangy Local Schools Bd. of Ed. v. Delaware Cty.*

Bd. of Rev., 125 Ohio St.3d 103, 2010-Ohio-1040, ¶ 15; *Satullo v. Wilkins*, 111 Ohio St.3d 399, 2006-Ohio-5856, ¶ 14.

3. **Mr. Loyd may not ratify this litigation where, as here, the party attempting to ratify the litigation, namely UBS Trust, is not aware of the actions it is ratifying or the subject matter of the litigation.**

Black letter agency law places additional limitations on the ratification doctrine that likewise foreclose ratification in this case. Pursuant to Ohio law and the Restatement of Agency (3d), the ratifying party must be aware of the actions being ratified. *Wells Fargo Bank v. Sessley*, 188 Ohio App.3d 213, 222, 2010-Ohio-2902; Restatement of Agency, at § 4.06, Appx. 184-189 (“A person is not bound by a ratification made without knowledge of material facts involved in the original act when the person was unaware of such lack of knowledge.”). There is no evidence here that UBS Trust has any knowledge concerning the subject matter of this appeal, or that UBS Trust has reviewed any pleadings. When Mr. Hubbard, as the Commissioner’s counsel, expressly stated at the BTA hearing on the motion to dismiss that the UBS Trust officers who signed the letter (that is not part of the record) most likely have no knowledge of the subject matter of this appeal, Mr. Loyd maintained his silence. Hr. Tr. 15, T.Supp. 152. Due to UBS Trust’s lack of knowledge, then, UBS Trust may not ratify this appeal.

4. **Mr. Loyd may not ratify this litigation where, as here, such ratification would affect the rights of third parties including the Tax Commissioner and Board of Tax Appeals.**

As an additional limitation on the ratification doctrine, ratification is “not effective unless it precedes the occurrence of circumstances that would cause the ratification to have adverse and inequitable effects on the rights of third parties. These circumstances include *** a specific time that determines whether a third party is deprived of a right or subjected to a liability.” Restatement of Agency (3d), § 4.06; *Wagner v. City of Globe*, 722 P.2d 250, 255 (Ariz. 1986);

Gemstar Ltd. v. Ernst & Young, 901 P.2d 1178, 1190-91 (Ariz. App. 1995). In other words, ratification is not effective where it adversely affects the rights of third parties.

Mr. Loyd's attempted ratification here is not effective because it adversely affects the rights of third parties, including the Tax Commissioner and the Board of Tax Appeals. In the interests of administrative efficiency, judicial efficiency, and enabling the Commissioner's to assert all lawful bases for his assessment and final determination, among other reasons, ratification is not effective to cure defecting petitions for reassessment and BTA notices of appeal. See, *Ohio Central Rail. Sys. v. Mason Law Firm*, 182 Ohio App.3d 814, 2009-Ohio-3238, ¶ 33 (identifying the equitable purposes for Civ. R. 17(A)); *CNG Dev. Co. v. Limbach*, 63 Ohio St.3d 28, 31-32 (1992) (identifying jurisdictional requirements that go to the core of procedural efficiency).

5. Ratification pursuant to Civ. R. 17(A) is not possible because, as a creature of statute, the BTA does not have equitable jurisdiction.

Most fundamentally, as a creature of statute, the BTA does not have equitable jurisdiction and this Board may not invoke such jurisdiction. *American Restaurant & Lunch v. Glander*, 147 Ohio St. 147 (1946); *Steward v. Evatt*, 143 Ohio St. 547 (1944). In fact, this Court has already stated that Civ. R. 17 is not binding on the BTA. In *Brown v. Levin*, this Court recognized that the Ohio Rules of Civil Procedure are binding on this Board only to the extent that they are discovery rules consistent with the Board's own discovery rules. 119 Ohio St.3d 335, 2008-Ohio-4081, ¶ 30. Since Civ. R. 17(A) is not a discovery rule, Civ. R. 17(A) is not binding on this Board and in no way provides this Board with equitable jurisdiction.

Equitable jurisdiction is precisely what Mr. Loyd is attempting to invoke through his argument that UBS Trust "ratified" this litigation. But the General Assembly, not the BTA, has the authority to determine the Board's jurisdiction. This Court has held on numerous occasions

that BTA notices of appeal and, derivatively, petitions for reassessment must satisfy strict jurisdiction requirements to invoke the BTA's jurisdiction. See, e.g. *CNG Dev.*, 63 Ohio St.3d at 31-32; *American Fiber Systems v. Levin*, 125 Ohio St.3d 374, 2010-Ohio-1468 (2010); see also *Ohio Bell Telephone Company v. Levin*, 124 Ohio St.3d 211, 2009-Ohio-6189 (2009).

Similarly, in the real property tax exemption context, this Court held that the Commissioner did not have jurisdiction over an application for exemption where a trustee holding title to real property did not properly apply for exemption. In *Columbus City School District Bd. of Ed. v. Wilkins*, this Court held that the Commissioner lacks jurisdiction over an application for exemption where the property owner does not identify itself as the trustee of the trust that holds title to real property for which exemption is sought. 106 Ohio St.3d 200 (2005).

There is no legislative authority for taxpayers to ratify appeals before the BTA, and Mr. Loyd may not invoke the BTA's jurisdiction with equitable arguments or reference to Civ. R. 17. Mr. Loyd was not an "authorized agent" of UBS Trust when he filed the petition for reassessment, as R.C. 5747.13(B) requires. Mr. Loyd himself is not a "taxpayer" that may file a BTA notice of appeal in this case, as R.C. 5717.02 requires. In a phrase, this appeal must be dismissed because the Trust did not meet the strict jurisdiction requirements for filing a petition for reassessment under R.C. 5747.13 or for filing a BTA notice of appeal under R.C. 5717.02.

This Court should dismiss this appeal and reverse the BTA's unreasonable and unlawful decision to deny the Commissioner's motion to dismiss.

CONCLUSION

Based upon the foregoing, this Court should affirm the BTA's decision and order upholding the merits of the Commissioner's reasonable and lawful final determination. In the alternative, this Court should dismiss the Trust's appeal for failure to timely file a petition for reassessment with the Tax Commissioner or notice of appeal with the BTA.

Respectfully submitted,



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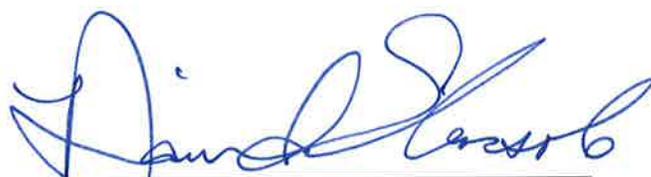
Joseph W. Testa, Tax Commissioner of Ohio

CERTIFICATE OF SERVICE

I hereby certify that the foregoing Appellee Tax Commissioner's Merit Brief was served upon the following by email on this 10th day of November, 2015:

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