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In the Supreme Court of Ohio

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

REPLY BRIEF AMICUS CURIAE OF THE OHIO CHAMBER OF COMMERCE IN SUPPORT OF APPELLANT PATTON R. CORRIGAN

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REPLY BRIEF AMICUS CURIAE OF THE OHIO CHAMBER OF COMMERCE IN SUPPORT OF APPELLANT PATTON R. CORRIGAN

I. INTRODUCTION

Ohio personal income tax should not be assessed against a nonresident investor when an investment in an entity operating in Ohio is sold unless the entity can be disregarded and the entity's activities can be attributed directly to the nonresident investor. R.C. 5747.212 is an anti-abuse statute and not a statute of general application for all closely-held entities operating in Ohio. Otherwise, the Ohio statute would (1) improperly subject income that is taxable in the state of residence to a second level of tax, (2) deny the investor Due Process, (3) interfere with interstate commerce, and (4) present a strong deterrent to investments in Ohio by nonresidents.

II. LAW AND ARGUMENT

A. Other States Do Not Tax The Gain Of A Nonresident Investor.

Appellee's brief asserts that the taxpayer seeks a new or creative means to avoid a properly-assessed tax. This argument is based on a series of misstatements of the law that attempt to assure the Court that the Tax Commissioner's position is not unusual and is within

constitutional bounds. This conclusion, however, could not be further from the truth. The tax that the Tax Commissioner seeks to impose would cause a significant departure from accepted principles for income sharing among the states for tax purposes and would run afoul of constitutional limitations.

Appellee's brief first creates the impression that other states tax a nonresident's gain from the sale of an interest in an entity doing business in the state. In fact, the opposite is true. The rule is that states do not tax this type of gain. The Tax Commissioner seeks authority to impose tax on a nonresident's investment beyond that approved by any court. In fact, the cases cited in the Brief of Appellee at 14 *contradict* the assertion that a "uniform body of case law supports" the Tax Commissioner. Rather, all four cases fall within this Court's finding in *Agley v. Tracy*, 87 Ohio St.3d 265, 719 N.E.2d 951 (1999). *Compare Johnson v. Collector of Revenue*, 246 La. 540, 165 So.2d 466 (1964) (shareholders owe tax on liquidation and distribution of Louisiana assets); *Kulick v. Dept. of Revenue*, 290 Ore. 507, 624 P.2d 93 (1981) (pro rata distributive share of nonresident of entity income from a pass-through entity operating in-state subject to tax); *Valentino v. Franchise Tax Bd.*, 105 Cal.Rptr.2d 304 (2001) (same); *Prince v. Dept. of Revenue*, 55 So.3d 273 (Ala. Civ. App. 2010) (gain from the deemed sale of assets by Alabama entity with the profits distributed to the nonresident shareholders taxable in Alabama). None of the cases concern income earned by an investor when selling the entity.

Further, *Prince* turned on the conclusion of the Alabama court that the transaction was a deemed sale of assets with the gain recognized *by the entity* rather than a stock sale. 55 So.3d at 280-281. No such election is present in the current appeal. Notably, if the stock sale would have itself been taxable, then the Alabama Court would not have had to address the question of whether the transaction should be treated as a deemed sale of assets by the entity rather than a

stock sale. The implication of the analysis in *Prince* is that a stock sale would not have been taxable. In any case, *Prince* like the other decisions cited, do not support the Tax Commissioner, much less present a uniform body of case law supporting the taxation of a nonresident's sale of an investment.

The few cases that even consider taxation of the gain on the sale of an interest in an entity show just the opposite. In *In re Baum,* for example, the New York State Tax Appeals Tribunal found that, under New York law, the election to treat a sale of stock as an asset sale by the entity was not effective.[1] N.Y. DTA Nos. 820837, 820838, 2009 WL 427425, at *6 (Feb. 12, 2009). Because the federal election was not recognized for New York tax purposes, the transaction was treated as a stock sale. The Tax Tribunal then expressed the proper treatment of the stock sale of an interest in a pass-through entity (S corporation) as follows:

> As stated at the outset, this is a simple stock sale. Thus, petitioners' gain from the sale of stock in SBS [SBS International of New York, Inc., an S corporation] is not included as New York source income to them [the shareholders], since they are nonresident individuals.

In re Baum, 2009 WL 427425, at *7.

Appellee's Brief also misleads when it asserts that 41 states have statutes that impose a tax similar to Ohio and tax this type of gain. The state laws referenced in the Brief of Appellee at page 34 address the taxation of distributive shares of income from the pass-through entities, however, and do not sanction sourcing the gain from the sale of an interest in the entity per the factors of the entity.

The Tax Commissioner's suggestion that because most states, like Ohio, use federal adjusted gross income as the tax base, that other states tax this type of investment income is also wrong. The calculation of the tax base says nothing about how that tax base is sourced among the

[1] Thereafter the New York law was changed to recognize the election.

states, which is the issue here. Other states do not source the investor's gain away from the investor's state of residence and, thus, do not tax this type of gain, despite strong similarities in the tax bases before sourcing the gain within and outside the state.

Curiously, the Tax Commissioner cites two cases that support sourcing gains from intangibles in the form of dividends and capital gains to the state of domicile and that prohibit treating the income as apportionable. *Allied-Signal, Inc. v. Director, Div. of Taxation*, 504 U.S. 768, 788-790, 112 S.Ct. 2251, 119 L.Ed.2d 533 (1992) (gain from the sale of stock not part of the apportionable base when investor and investee are not in the same unitary business and the transaction serves an investment purpose and not an operational purpose) and *ASARCO Inc. v. Idaho State Tax Comm.*, 458 U.S. 307, 307-308, 102 S.Ct. 3103, 73 L.Ed.2d 787 (1982) (dividends paid from non-unitary payer allocable to domicile of payee and not part of apportionable income; capital gains not treated differently from dividends). Application of the unitary principles expressed in these cases (and other cases as well) compel treating Mr. Corrigan's sale of his investment in Mansfield Plumbing Products LLC ("Mansfield Plumbing") as allocable to Connecticut and not apportionable to Ohio. (*See* Reply Brief of Appellant).

That R.C. 5747.212 is unique to Ohio does not require a finding that it is unconstitutional. The unique nature of R.C. 5747.212, as sought to be applied by the Tax Commissioner, however, should at a minimum raise concerns that the statute overreaches. The Tax Commissioner's refusal even to admit to the Court that R.C. 5747.212 is unique also wholly undermines the Tax Commissioner's plea that he is trying only to enforce Ohio's "fair share" of the tax.

The Tax Commissioner repeatedly argues that because Ohio provided benefits to the entity, Ohio has a constitutionally permissible claim on the separate and distinct gain earned by

the nonresident investor's sale of an interest in the entity. The Tax Commissioner's claim to the income of the entity does not extend to the gain from the sale of the investment. The Tax Commissioner never addressed the basis for his linking the benefits provided to the entity to empower him to tax Mr. Corrigan's gain on his investment. Moreover, the Tax Commissioner makes no effort to explain why Connecticut, Mr. Corrigan's state of residence and the accepted jurisdiction for sourcing this type of income, does not have a superior claim to the investment income from the sale of an interest in the entity because of the benefits it has provided Mr. Corrigan as a resident of that state. Mr. Corrigan's income has not escaped taxation.[2] All of this income has been taxed because Connecticut, as the state of residency, has already taxed the gain in recognition of the benefits Connecticut has conferred on Mr. Corrigan as one of its residents.

This principle of assigning investments to the investor's state of residency applies equally when an Ohio resident invests in out-of-state entities. Ohio receives all of the gain from investments earned by its residents who own entities operating outside Ohio because of the benefits Ohio provides to the resident investor, even though Ohio provides no benefits to the entities operating outside Ohio.

B. Strict Construction Of A Statute Providing For Apportionment Is Required, And Any Ambiguity Must Be Resolved In Favor Of The Taxpayer.

The Tax Commissioner cites the wrong authorities when he argues that the nonresident credit is to be strictly construed against the taxpayer. (Brief of Appellee, 33). While deductions, exemptions and exclusions from the tax base are construed against the taxpayer, the same is not true for the methods of sourcing income in and out of the state. The nonresident credit is not a reduction in tax but the method by which the income is assigned among the states. To the extent income qualifies for the nonresident credit, it remains taxable, but in another state and not Ohio.

---

[2] Connecticut law, contrary to the assertion of the Tax Commissioner, does not yield to Ohio's taxation of this income. (*See* discussion, infra, at Part D.1.).

The nonresident credit takes the taxpayer's income and assigns to Ohio the part of that income that is sourced in Ohio. In this case, the Tax Commissioner seeks to use the apportionment factors of Mansfield Plumbing to apportion to Ohio Mr. Corrigan's investment gain on the sale of an interest in the entity. As a result, the nonresident credit is the mechanism being used to source this income in and out of Ohio. Because the issue here is whether the apportionment was proper, and no exemption is claimed from taxation, any ambiguity in the construction of the tax statute in determining how to source income is resolved in favor of the taxpayer. *See Gulf Oil Corp. v. Kosydar*, 44 Ohio St.2d 208, 339 N.E.2d 820 (1975), paragraph one of the syllabus (applying standard of review for apportionment cases); *Storer Communications, Inc. v. Limbach,* 37 Ohio St.3d 193, 195, 525 N.E.2d 466 (1988) (same).

C. Due Process Is Violated If An Entity's Activities Are Attributed To An Investor For Sourcing Income From The Sale Of An Interest In The Entity, Absent A Basis For Disregarding The Separate Existence Of The Entity.

1. The Tax Commissioner Cannot Look Through An Entity To Source Gain From The Sale Of An Interest In That Entity By The Investor In The Normal Course.

As a threshold matter, the Tax Commissioner limits his arguments to the situation in which the entity being sold is a pass-through entity—in this case a limited liability company. R.C. 5747.212, however, is not limited to pass-through entities but also includes closely-held C corporations, *i.e.*, entities that are taxed at the entity level and whose income is not passed through to the investors before taxation. While the Tax Commissioner may wish to avoid the issue, the sole determinant for his application of the R.C. 5747.212 look-through to the activities of the separate legal entity is whether the entity is closely-held, and not whether the entity is a pass-through entity for tax purposes.

The Tax Commissioner seeks to disregard all closely-held entities' separate existence for tax purposes based solely on the fact that the entities are closely-held. The Tax Commissioner

proceeds with his look-through approach absent the existence of any of the factors that this Court has found necessary before disregarding an entity's separate existence in the non-tax context. (*See* Brief of Amicus Curiae, 4). The Tax Commissioner's view would be comparable to the General Assembly decreeing that no closely-held entity could claim the benefit of limited liability solely because the entity is closely-held, and despite the entity's adherence to the organizational requirements necessary for the entity to enjoy a separate legal status.

The fact that a tax is involved rather than an action in tort or contract does not sanction the abandonment of the accepted rules for recognizing the separate legal status of an entity. The Tax Commissioner bases his authority to pierce the legal entity status in the tax area on this Court's decision in *Agley*, but the Tax Commissioner is stretching the finding of that case beyond what the Court decided.

First, the Court in *Agley* specifically declared that the corporation was a "separate legal entity for purpose of doing business." 87 Ohio St.3d at 268.[3] In *Agley,* the Court focused on the income earned by the entity, which income could have been taxed to the entity, if it had not passed through to the owners. The Court concluded that under the pass-through entity concept, the entity's income would be taxable only if it could be taxed to the investor. The Court's decision is entirely consistent with the U.S. Supreme Court's holding in *Wisconsin v. J.C. Penney* that the entity's income could be taxed in the investor's hands under these circumstances without running afoul of constitutional limits. *See* 311 U.S. 435, 61 S.Ct. 246, 85 L.Ed. 267 (1940). Nothing in the *Agley* or the *J.C. Penney* cases suggests that the separate nature of the entity was extinguished; only that the entity's operating income could be taxed as income of the investor when the income was passed through and the entity was not taxed.

[3] We have added the phrase "for purpose of doing business" that the Tax Commissioner wants added. (*See* Brief of Appellee, 9-10). That addition has no impact on the analysis.

An entity's operating income is wholly different than an investor's gain from the sale of an interest in the entity. In Ohio, the pass-through entity reports its annual operating income to the Tax Commissioner. *See* R.C. 5747.08(D), (I) (in the context of the composite return). Further, the taxation of that operating income applies to the investor only once the entity's income is attributed to the investor by the entity as the investor's distributive share. In contrast, Mr. Corrigan's gain from the sale of an interest in the entity would never be reported by the entity itself. The gain from the sale of an interest in the entity is not income to the entity. It would only be reported by the investor on the investor's personal return.

The principle that a shareholder/member is distinct from the investee entity is an important principle of commerce. Most often, the focus of this distinction is the limitation on the investor's liability for acts of the entity. This distinction should also exist for tax purposes. The decision in *Agley* authorized the taxation of the entity's income in the nonresident investor's hands to prevent the avoidance of tax on the income that the state certainly would have authority to tax in the entity's hands. To take the *Agley* decision and expand it to permit an investor's gain on the sale of an interest in an entity to be taxed is not supportable.

The key distinction between the taxation of the operating income (inside income) earned by the entity addressed in *Agley* and the investor's gain (the outside gain) from the sale of an interest in an entity is expressed by the Supreme Judicial Court of Massachusetts in *Commr. of Revenue v. Dupee,* 423 Mass. 617, 623, 670 N.E.2d 176 (1996). Like Ohio, Massachusetts taxes the operating income of the pass-through entity. But when the Massachusetts Department of Revenue sought to expand those principles to tax the gain from the sale of an interest in the entity, the highest court in Massachusetts rejected the Department of Revenue's reading of that state's statue in a manner that is instructive in this case in Ohio. *Id.*

It is true, as the Ohio Tax Commissioner states, that the Massachusetts Court applied the Massachusetts statute, not the U.S. Constitution. The fact that no decision addresses the constitutionality of taxing a nonresident for the personal gains from the sale of an out of state investment, however, merely shows that the states competing with Ohio do not tax this type of gain and, thus, the constitutional issue does not arise.

The Massachusetts Supreme Court's conclusions, however, are sound tax policies and reflect the principles that govern the relationship among the states competing for income generated by multistate companies and nonresidents' sale of investments. These conclusions also reflect the distinction between the taxation of income earned by the entity operating in state and the income recognized by the nonresident investor in the event of a sale of the investment. No state has questioned the reasoning of the Massachusetts Court. For his part, the Tax Commissioner offers no rationale to challenge the conclusions of the Massachusetts court.

2. The Attribution Of Mansfield Plumbing's Apportionment Factors To Mr. Corrigan's Sale Of An Interest In The Entity Violates Due Process.

a. Principles Of Personal Jurisdiction Are Applicable To Determining The Geographic Reach Of A State's Taxing Authority.

Because no federal or state courts have confronted a statute like R.C. 5747.212, this Court properly can look at the application of the Due Process principles in comparable contexts, both tax and non-tax. Disregarding the separate nature of a legal entity, absent a basis to pierce the entity's veil, constitutes a violation of the investor's right to Due Process.

Contrary to the Tax Commissioner' arguments, issues relevant to long-arm jurisdiction are comparable to issues implicated by a state's effort to expand its taxing jurisdiction. For general jurisdiction purposes, a plaintiff cannot compel the appearance of a person or entity into court based on the activities of a separate affiliate of the entity, such as a separate entity in which

the potential defendant invests. In *Daimler AG v. Bauman*, plaintiffs allegedly had been harmed by a Daimler affiliate in Argentina. ___ U.S. ___, 134 S.Ct. 746, 187 L.Ed. 624 (2014). The U.S. Supreme Court found that the California court could not exercise general jurisdiction over Daimler when the alleged tort was perpetrated by a Daimler-affiliated entity, even though another affiliated entity had extensive contacts with California. The Supreme Court limited the ability to use the affiliate to confer jurisdiction to those situations in which the in-state affiliate was the alter-ego of the tortfeasor or the in-state entity was the tortfeasor's agent. Here, the Tax Commissioner makes no effort to assert the alter-ego theory. And, the Record presents no basis to support piercing the separate existence of Mansfield Plumbing.

The Tax Commissioner does suggest that the activities of Mansfield Plumbing may bind Mr. Corrigan and cites authorities that attribute the activities of officers, employees and agents (collectively "Agents") to the legal entity. (Brief of Appellee, 19-20). The attribution of the actions of the Agents to the entity, however, does not operate in reverse. The actions of the legal entity are not attributed to the Agents or the shareholders.

Otherwise, the limitations of liability conferred by a separate corporate existence would cease to exist, and shareholders could be sued in any jurisdiction in which their investments did business. Such is not the case. "Jurisdiction over officers, directors, and shareholders of corporation cannot be based solely on jurisdiction over the corporation itself." *State ex rel. DeWine v. S&R Recycling, Inc.*, 195 Ohio App.3d 744, 2011-Ohio-3371, 961 N.E.2d 1153, ¶ 24 (7th Dist.), citing *Dombroski v. Wellpoint, Inc.*, 119 Ohio St.3d 506, 2008-Ohio-4827, ¶ 16; *In re Blue Flame Energy Corp.*, 171 Ohio App.3d 514, 2006-Ohio-6892, 871 N.E.2d 1227, ¶ 31 (10th Dist.); *accord Shaffer v. Heitner*, 433 U.S. 186, 217, 97 S.Ct. 2569, 53 L.Ed.2d 683 (1977) (Powell, J., concurring) ("[N]either the statutory presence of appellants' stock in Delaware nor

their positions as directors and officers of a Delaware corporation can provide sufficient contacts to support the Delaware courts' assertion of jurisdiction in this case."). This conclusion is consistent with fundamental agency principles.

Thus, while the activities of the Agents of Mansfield Plumbing are attributed to Mansfield Plumbing, the activities of Mansfield Plumbing are not attributed to its agents, much less attributed to Mr. Corrigan as an investor. The gain from the sale of an interest in the entity is not properly assignable to Ohio based on the activities of Mansfield Plumbing.

b. The Incidence Of The Tax On The Entity Is Distinct From The Incidence Of The Tax On The Sale Of The Investment.

The Tax Commissioner appears to assume that production of income by the entity can be equated with Mr. Corrigan's gain from the sale of an interest in the entity for purposes of sourcing the sale. The two types of income, however, are different and that difference means that the use of the entity's factors for sourcing Mr. Corrigan's personal gain is not appropriate.

The difference in the two taxable events (sale of an interest in the entity versus production of income by the entity) is illustrated by a case that addressed the Commerce Clause. In *Fulton Corp. v. Faulkner*, the issue was a Commerce Clause challenge to a credit, which increased by the amount of the subsidiary's income that was taxed in North Carolina, against an intangible tax on the in-state parent corporation measured by its investment in its subsidiary. 516 U.S. 325, 116 S.Ct. 848, 133 L.Ed.2d 796 (1996). In essence, the more the subsidiary invested in North Carolina, the less intangible tax the parent paid; and the less the subsidiary invested in North Carolina, the more intangible tax the parent paid. *Fulton* held that this resulted in unconstitutional discrimination against interstate commerce. *Id.* at 325-326.

The usefulness of *Fulton* to the present case in the Due Process context is the U.S. Supreme Court's recognition that taxation of an investee-subsidiary's income-generating

activities is distinct and not relatable to the tax arising from the ownership of the investment. Just as North Carolina could not use the tax on the subsidiary to defend a claim of discrimination against the parent because of the different incidences of the two taxes, the Tax Commissioner should not be permitted to apportion using the factors for sourcing an investee's operating income as the means of sourcing an investor's sale of an investment, a tax incident distinct from the taxation of an investee's income.

Although intangible tax and income tax were at issue in *Fulton* and two income taxes are at issue in the present case, the distinction between taxing the investor and taxing the investee remains the same. Because taxation of Mr. Corrigan's gain as an investor is different than the taxation of the internal operating income of Mansfield Plumbing as the investee, using the investee's apportionment factor improperly sources Mr. Corrigan's gain on the investment.

Instead of allocating the gain based on the investor's activities and his relationship to his state of residence, as should have been done, the Tax Commissioner purports to apportion the gain based solely on the investee's activities. This proposition is exactly equivalent to the state purporting to tax an investor's gain from the sale of Ford Motor Company stock by reference to the underlying activities of Ford Motor Company. Using the factors of Ford Motor Company, however, is never the basis for sourcing shareholders' sales of Ford Motor Company stock. The Tax Commissioner's sourcing method is equally inapplicable to the investor in Mansfield Plumbing, notwithstanding the fact that Mansfield Plumbing is closely-held.

The use of Mansfield Plumbing's sourcing factors—absent a reason to pierce Mansfield Plumbing's separate corporate existence—is the wrong method to assign Mr. Corrigan's personal gain. The Tax Commissioner's effort to expand R.C.5747.212 beyond those occasions when the investor is abusing the existence of the separate entity is overreaching and should not be upheld.

D. The Tax Commissioner's Application Of R.C. 5747.212 Interferes With Interstate Commerce, And The Resident Credit Does Not Save It.

1. Interstate Commerce Is Burdened Because Connecticut Need Not And Does Not Give Credit Based On Ohio's Tax On This Income.

The Tax Commissioner's construction of R.C. 5747.212 interferes with interstate commerce because an investment from outside Ohio is subject to greater tax upon disposition than the same investment made by an Ohio resident into an Ohio entity. If the Tax Commissioner is successful in this appeal, Mr. Corrigan will pay tax on the same income in Connecticut and Ohio. If he had been an Ohio resident, Mr. Corrigan would pay the tax on his personal gain only once. The only way to avoid the double taxation for the nonresident investor is to avoid investing in Ohio. Such a barrier to interstate investing burdens interstate commerce in a meaningful way.

The extra tax for cross-border investments is prevented by application of the resident credit. That is, the state of a person's residency yields the income for tax purposes for income properly sourced to another state. That is why the tax on the pass-through income of the entity is not also taxed by Connecticut; the state of residence gives the credit for the income properly taxed in Ohio.

The problem here is that Connecticut (and other states do the same) denies the resident credit for the taxation of intangibles. The Tax Commissioner insists that the Connecticut credit is available but he provides no authority for his bald assertion. In addition to the regulation already referenced in the initial Amicus Brief at 8-9, the relevant 2004 Form CT 1040, Connecticut Resident Income Tax Return and Instructions most relevant to the resident credit read as follows:

> **What is Income Derived From or Connected With Sources Within a Qualifying Jurisdiction**[4]
>
> - Compensation that is received for personal services performed in a qualifying jurisdiction;

[4] Ohio would be a qualifying jurisdiction.

- Income from a business, trade, or profession carried on in a qualifying jurisdiction;
- Gambling winnings from a state-conducted lottery. See **Informational Publication 2003(21)**, *Connecticut Income Tax Treatment of State Lottery Winnings Received by Residents and Nonresidents of Connecticut*; **or**
- Income from real or tangible personal property situated in a qualifying jurisdiction.

> Income from intangibles, such as stocks and bonds, is not considered derived from or connected with sources within a qualifying jurisdiction **unless** the income is from property employed in a business, trade, or profession carried on in that jurisdiction.

(Emphasis sic; footnote added). Appx. 1-3, Excerpt of 2004 Form CT-1040, Connecticut Resident Income Tax Return & Instructions, 22.[5]

The ownership interest in a limited liability company is the exact counterpart to the ownership of stock. Mr. Corrigan did not employ the income from his gain from the sale of an interest in the entity in the conduct of a business, trade, or profession that he carried on in Ohio. Therefore, Connecticut would not provide a resident credit for any taxation by Ohio on his gain from the sale of his investment.

2. The Taxation Of Nonresidents' Investment Gains Violates The *Complete Auto Transit* Test.

Contrary to the Tax Commissioner's attempt to limit the scope of briefing, an Amicus Curiae is not limited to addressing the substantial nexus prong of the four-part test of *Complete Auto Transit, Inc. v. Brady*, 430 U.S. 274, 97 S.Ct. 1076, 51 L.Ed.2d 326 (1977).[6] While courts will not hear new *issues* or *claims* raised by an Amicus Curiae, the same is not true of alternative

[5] Full instructions are available at http://www.ct.gov/drs/lib/drs/forms/2004forms/incometax/ct-1040booklet.pdf.

[6] Under *Complete Auto Transit*, a state tax survives a challenge under the dormant Commerce Clause if it does the following: (1) applies to an activity with a substantial nexus with the taxing state; (2) is fairly apportioned; (3) is not discriminatory towards interstate or foreign commerce; and (4) is fairly related to the services provided by the State. 430 U.S. at 274.

arguments in support of pending issues or claims. In this case, Mr. Corrigan preserved the Commerce Clause issue. Mr. Corrigan could raise alternative arguments under the Commerce Clause in support of a preserved issue. *See Goodyear Tire & Rubber Co. v. Limbach*, 61 Ohio St.3d 381, 382, 575 N.E.2d 146 (1991) (taxpayer can raise additional arguments so long as the issue was preserved).

This distinction between issues raised and alternative arguments also is applicable in the case of an amicus brief. "Although an amicus brief is ordinarily limited to arguing issues raised by the parties, an amicus may present different arguments than the parties relating to those issues." *Lewis v. Harris*, 378 N.J. Super. 168, 185, fn. 2, 875 A.2d 259 (2005), citing *Keating v. State*, 157 So.2d 567, 569 (Fla.App.1963). This distinction is necessary to save amicus briefs from redundancy:

> A significant distinction is apparent as between 'issues' and 'theories' in support of a particular issue * * *. [A]micus is not confined solely to arguing the parties' theories in support of a particular issue. To so confine amicus would be to place him in a position of parroting 'me too' which would result in his not being able to contribute anything to the court by his participation in the cause.

Keating, 157 So.2d at 569.

In the case of the Commerce Clause and the four-part test of *Complete Auto Transit,* the four prongs work together and not separately. Thus, if no nexus exists for the income being taxed by the state, then that taxing scheme discriminates against interstate commerce and fails to properly apportion the income. Likewise a taxing scheme that fails to properly apportion income does so by purporting to tax income over which that state lacks substantial nexus. Because the four prongs of *Complete Auto Transit* work together to identify different aspects of state activities that interfere with interstate commerce, the Court, the parties and Amicus Curiae are not limited to addressing the Commerce Clause issue only through the lens of substantial nexus.

On the merits of the Commerce Clause claim, the states have an obligation to prevent double taxation in this context. In *Maryland State Comptroller v. Wynne*, a majority of the Maryland Court of Appeals found that the Maryland tax scheme that granted a resident credit against only part of the state tax violated the Commerce Clause by interfering with interstate commerce. 431 Md. 147, 64 A.3d 453 (2013), *cert. granted*, ___ U.S. ___, 134 S.Ct. 2660, 189 L.Ed.2d 208 (2014). The Maryland Court of Appeals addressed the problem of double taxation in the context of that state's resident credit. The same dangers arise here when a nonresident credit is read to permit double taxation for cross-border investments.

The majority opinion of the Maryland Court of Appeals provides:

> The limitation of the credit for payments of out-of-state income taxes to the State portion of the Maryland income tax can result in significantly different treatment for a Maryland resident taxpayer who earns substantial income from out-of-state activities when compared with an otherwise identical taxpayer who earns income entirely from Maryland activities. In particular, the first taxpayer may pay more in total state and local income taxes than the second. This creates a disincentive for the taxpayer—or the S corporation of which the taxpayer is an owner—to conduct income-generating activities in other states with income taxes. Thus, the operation of the credit with respect to the county tax may affect the interstate market for capital and business investment and, accordingly, implicate the dormant Commerce Clause.

Id. at 164-165, citing *Fulton*, 516 U.S. 325 (North Carolina property tax on intangibles that taxed investments in out-of-state businesses at a higher rate violated the Commerce Clause); *Boston Stock Exchange v. State Tax Comm'n*, 429 U.S. 318, 332, 97 S.Ct. 599, 50 L.Ed.2d 514 (1977).

Maryland appealed to the United States Supreme Court and at this writing, the Supreme Court has not ruled. Maryland is arguing that the state of residency need not provide any credit for income sourced to another state. The Wynnes are arguing that the resident credit is necessary to prevent violation of the Commerce Clause.[7]

[7] We cannot predict how the U.S. Supreme Court will decide *Wynne,* but it is difficult to see how that decision will support the Ohio Tax Commissioner's position in this case.

E. R.C. 5747.212 Is Intended As An Anti-Abuse Statute Applicable Only When Necessary To Prevent Improper Avoidance Of Tax.

The initial Amicus Brief proposed an alternate construction limiting R.C. 5747.212's look-through to the investee's apportionment factors only when the legal entity should be disregarded. (Brief of Amicus Curiae, 13-14). The Tax Commissioner responded that because only constitutional challenges were raised, not a statutory interpretation challenge, an alternate construction of the statute could not be entertained. (Brief of Appellee, 31-32).

The trigger for the proffered alternate construction, however, is the constitutional impairment. An alternative construction seeks to avoid the need to strike down the statute on constitutional grounds. Courts have a duty to liberally construe statutes 'to save them from constitutional infirmities.'" *Mahoning Edn. Assn. of Dev. Disabilities v. State Emp. Relations Bd.*, 137 Ohio St.3d 257, 2013-Ohio-4654, 998 N.E.2d 1124, ¶ 13, quoting *Desenco, Inc. v. Akron*, 84 Ohio St.3d 535, 538, 1999-Ohio-368, 706 N.E.2d 323. The Court is not relieved of that duty even when a party did not address the alternative by pleadings. *See Descenco*, 84 Ohio St.3d at 538 (requiring courts to "uphold [the] constitutionality" of a statute when "possible"). The judicial duty and authority to consider an alternative construction to avoid the constitutional infirmity is not conferred on the Court by the parties and is not limited by the pleadings.

Here, reading R.C. 5747.212 as an anti-abuse statute would avoid the constitutional concerns. And, the Tax Commissioner explicitly concedes the premise for the alternate construction when he describes the application of the statute:

> Indeed, for the purpose of determining whether Ohio may validly exercise its taxing power, the State may properly 'look through' the form of the business organization (in this case Mansfield's organization as a limited liability company) and attribute Mansfield's Ohio business activities, property and income to Mr. Corrigan directly.

(Brief of Appellee, 9).

Amicus agrees that the Tax Commissioner should be permitted to disregard the entity, but only when the circumstances are such that the entity properly can be disregarded. The Tax Commissioner's view is that R.C. 5747.212 permits him to look through *every* closely-held entity. Amicus submits that the General Assembly did not intend to provide the Tax Commissioner such a blunt instrument to use against taxpayers that have faithfully attended to the requirements of operating a separate legal entity.

The Tax Commissioner's other examples are consistent with an anti-abuse construction. Amicus agrees that a lottery winner setting up an entity just to hold the winning ticket should be subject to having the entity disregarded. Another example of an abusive arrangement would be if an individual dropped an asset, such as Ohio real estate, into a limited liability company just before sale. These sales would properly be subject to tax, as those actions were taken for the purpose of tax avoidance.

The Tax Commissioner also fails to cite the principal use of R.C. 5747.212. If a closely held business attempts to cast off the apportionment factors (property, payroll and sales) just before a liquidation and distribution, the Tax Commissioner can compel the taxpayer to use three years' worth of apportionment factors to avoid distorting the portion of the gain properly apportioned to Ohio and can follow the gain through to the investor. The use of three years of apportionment factors and the application of the statute to all closely-held corporations shows that this statute is an anti-abuse statute and not one of general application. On the facts of this case, with no evidence of abuse or tax avoidance, R.C. 5747.212 has no role.

III. CONCLUSION

The Tax Commissioner's application of R.C. 5747.212 will hurt the Ohio investment market, which is dependent on nonresidents as well as residents. Investors are entitled to

protection from the overreaching effort of the Tax Commissioner to assign income to Ohio that is not properly sourced here. Interstate commerce is entitled to protection from the burden of double taxation applicable only when the investment crosses state borders. Finally, the investment market in Ohio is entitled to protection from the Tax Commissioner's overly-aggressive application of the statute. The Tax Commissioner's action, if upheld in this case, can be expected to hurt the Ohio investment market when nonresident investors learn of the distinct disadvantage in investing in closely-held entities operating in Ohio.

The decision of the BTA should be reversed. R.C. 5747.212 should be applied only in instances of abuse or tax avoidance to avoid constitutional infirmities, or the statute should be struck down as unconstitutional.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I hereby certify that on this 28th day of April, 2015 a true copy of the foregoing Reply Brief Amicus Curiae was served by electronic and ordinary mail upon J. Donald Mottley, Taft Stettinius & Hollister LLP, 65 East State Street, Suite 1000, Columbus, Ohio 43215, Counsel for Appellant and Michael DeWine, Attorney General of Ohio, c/o Barton A. Hubbard, David D. Ebersole and Raina M. Nahra, Assistant Attorneys General, 30 East Broad Street, 25th Floor, Columbus, Ohio 43215, Counsel for Appellee, Joseph W. Testa, Tax Commissioner of Ohio.

s/ Edward J. Bernert
Edward J. Bernert

2004 FORM CT-1040

Connecticut Resident Income Tax

Return and Instructions

This booklet contains:

- Form CT-1040
- Schedule CT-1040WH
- Form CT-1040 EXT
- Form CT-1040ES
- Taxpayer Questionnaire
- Tax Tables
- Tax Calculation Schedule

Dear Customer:

Each year, the Connecticut Department of Revenue Services (DRS) strives to create quality products that give you, the taxpayer, the information you need to make tax filing as easy as possible. We listen to taxpayer suggestions for improving our products and seek new procedures to make processing returns more efficient.

This year, you will notice extensive changes to the layout of the income tax forms. The new design is a result of innovative technology being used to process paper returns, as well as efforts to provide you with a cleaner, easier format. While the larger spacing has increased the number of pages of the return, it also increases readability and will help reduce the number of filing and processing errors.

This booklet also contains information about electronic filing methods that make filing and paying taxes even easier. I encourage you to review the filing criteria for *WebFile* and *Telefile* on Page 4. If you qualify and expect to receive a refund, you could see that money in your bank account in only four days.

At DRS, our goal is to provide taxpayers with excellent customer service and a user-friendly approach to tax administration. If you have questions about Connecticut taxes or filing this return, you can reach DRS Taxpayer Services staff by e-mail, phone, or letter. The back cover of this booklet provides all the ways you can access this Agency including the DRS Web site, which is available anytime, to provide you with access to forms, publications, and information.

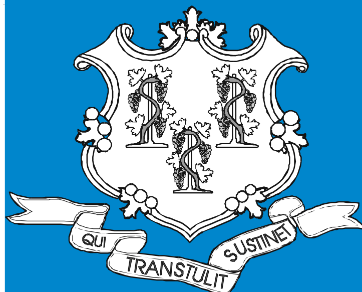
As always, we welcome your comments and ideas about how we can improve the way we do business.

Sincerely,

Pam Law

Commissioner of Revenue Services

Taxpayer information is available on our Web site:
www.ct.gov/DRS

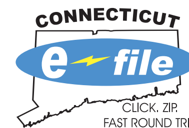


Connecticut WebFile Program

File **Form CT-1040** or **Form CT-1040 EXT** over the internet using ***WebFile***. ***WebFile*** is free and secure.

Connecticut fed/state e-file Program

File your federal and Connecticut returns together using ***e-file***!



For more information on these programs, visit: www.ct.gov/DRS

Department of Revenue Services walk-in locations and telephone numbers are listed on the back cover.

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7. Subtract the amount of any interest income from notes, bonds, or other obligations of the State of Connecticut, which interest income is included in federal adjusted gross income.

Do **not** use Line 49 to subtract income subject to tax in a qualifying jurisdiction (see *Schedule 2 - Credit for Income Taxes Paid to Qualifying Jurisdictions,* below) or income of a nonresident spouse (see *Special Rules for Married Individuals* on Page 14).

Line 50 - Total Subtractions

Add Lines 40 through 49. Enter the total on **Form CT-1040**, Line 50.

Schedule 2 - Credit for Income Taxes Paid to Qualifying Jurisdictions

Important: You **must** first complete **Form CT-1040**, *Schedule 3 - Credit for Property Taxes Paid on Your Primary Residence and/or Motor Vehicle,* before completing *Schedule 2*. See instructions on Page 25.

Am I Eligible for the Credit for Income Taxes Paid to Qualifying Jurisdictions

If you are a **resident** of Connecticut and if any part of your income was taxed by a **qualifying jurisdiction**, you may be able to claim a credit against your Connecticut income tax liability for qualifying income tax payments you have made.

Taxpayers seeking a credit for alternative minimum taxes paid to another jurisdiction must complete **Form CT-6251**, *Connecticut Alternative Minimum Tax Return-Individuals*, to calculate their alternative minimum tax credit.

What is a Qualifying Jurisdiction

A *qualifying jurisdiction* includes another state of the U.S., a local government within another state, or the District of Columbia. A *qualifying jurisdiction* does not include the State of Connecticut, the U.S., or a foreign country or its provinces (for example, Canada and Canadian provinces).

What are Qualifying Income Tax Payments

Qualifying income tax payments are income taxes that you actually paid on income:

- Derived from or connected with sources within the qualifying jurisdiction; **and**
- Subject to tax in the qualifying jurisdiction.

What is Income Derived From or Connected With Sources Within a Qualifying Jurisdiction

- Compensation that is received for personal services performed in a qualifying jurisdiction;
- Income from a business, trade, or profession carried on in a qualifying jurisdiction;
- Gambling winnings from a state-conducted lottery. See **Informational Publication 2003(21)**, *Connecticut Income Tax Treatment of State Lottery Winnings Received by Residents and Nonresidents of Connecticut*; **or**
- Income from real or tangible personal property situated in a qualifying jurisdiction.

Income from intangibles, such as stocks and bonds, is not considered derived from or connected with sources within a qualifying jurisdiction **unless** the income is from property employed in a business, trade, or profession carried on in that jurisdiction.

What Payments Do Not Qualify

- Income tax payments made to a qualifying jurisdiction on income that was not derived from or connected with sources within the qualifying jurisdiction (such as wages not derived from or connected with sources within the qualifying jurisdiction);
- Income tax payments made to a qualifying jurisdiction on income not included in your Connecticut adjusted gross income;
- Income tax paid to a jurisdiction that is not a qualifying jurisdiction, including a foreign country or its provinces (for example, Canada and Canadian provinces);
- Alternative minimum tax paid to a qualifying jurisdiction;
- Income tax paid to a qualifying jurisdiction if you claimed credit on that jurisdiction's income tax return for income tax paid to Connecticut; **or**
- Penalties or interest on income taxes you paid to a qualifying jurisdiction.

What Limitations Apply to the Credit

The total credit is limited to whichever of the following amounts is least:

- The amount of income tax paid to the qualifying jurisdiction;
- The portion of Connecticut income tax due on the Connecticut adjusted gross income that is sourced in the qualifying jurisdiction; **or**
- The amount of your Connecticut income tax entered on **Form CT-1040**, Line 6.

How Do I Calculate the Credit

You **must** first complete your income tax return(s) in the qualifying jurisdiction(s). Then, complete *Schedule 2 - Worksheet* on Page 23, to determine the amount to enter on *Schedule 2 - Credit for Income Taxes Paid to Qualifying Jurisdictions*, Line 53.

The allowed credit must be separately computed for each qualifying jurisdiction. Use separate columns for each qualifying jurisdiction for which you are claiming a credit. **Attach a copy of all income tax returns filed with qualifying jurisdictions to your Connecticut income tax return or the credit will be disallowed.**