

THE STATE OF SOUTH CAROLINA
In the Supreme Court

APPEAL FROM THE ADMINISTRATIVE LAW COURT
Carolyn C. Matthews, Administrative Law Judge

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S.C. Supreme Court

CarMax Auto Superstores West Coast, Inc,Respondent/Petitioner,
v.
South Carolina Department of Revenue,Petitioner/Respondent.

**AMICUS CURIAE BRIEF OF COUNCIL ON STATE TAXATION
("COST") IN SUPPORT OF PETITION FOR WRIT**

Burnet R. Maybank, III
Nexsen Pruet, LLC
1230 Main Street, Ste 700 (29201)
PO Drawer 2426
Columbia, SC 29202
Phone: 803-540-2048
Fax: 803-727-1472
Cell: 803-960-3024
E-mail:
bmaybank@nexsenpruet.com

Alexandra E. Sampson
Reed Smith LLP
1301 K Street, N.W.
Suite 1100 – East Tower
Washington DC
Phone: 202-414-9486

ATTORNEYS FOR COUNCIL ON STATE
TAXATION ("COST")

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INTEREST OF THE AMICUS

The Council on State Taxation (“COST”) is a nonprofit trade association based in Washington, D.C. COST was formed in 1969 as an advisory committee to the Council on State Chambers of Commerce. Today COST has grown to an independent membership of nearly 600 major corporations engaged in interstate and international business. COST’s objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multi-jurisdictional business entities. COST members do business in South Carolina and own and lease property in South Carolina.

South Carolina apportions the income of multistate corporate taxpayers by using a set of rules based upon the Uniform Division of Income for Tax Purposes Act (“UDITPA”). UDITPA has been adopted by a majority of other states as well, and the states that have adopted UDITPA often look to court decisions in their sister states when called upon to interpret this uniform law. How UDITPA is administered and applied in South Carolina is, therefore, of vital interest and importance to COST and its members. COST is concerned that the holding of the Administrative Law Court (“ALC”) in this case will not only negatively impact how South Carolina administers income tax on COST members but also will negatively impact how other states administer their tax laws and that, if allowed to

stand, the decision in this case will inevitably lead to the very lack of uniformity and uncertainty that UDITPA was designed to prevent.

COST submits this *amicus curiae* brief to stress the overall importance of this case and to aid this Court in understanding how the decision of the ALC—allowing the South Carolina Department of Revenue (the "Department") to deviate from statutory rules in a very common situation—undermines the certainty that accompanies uniform multistate apportionment and equates to unstable and indiscriminate taxation by the State of South Carolina. The South Carolina legislature long ago adopted UDITPA in its statutes. It was designed to use a uniform measure to determine how much income from a taxpayer doing business in multiple states is apportioned and subject to tax in South Carolina. Those statutes apply in virtually every circumstance and with every taxpayer so that the multistate income can be uniformly and consistently divided, consistent with the other states that have adopted UDITPA. In a few circumstances, promulgated regulations can vary the statutory rules in those instances where a group of taxpayers or an entire industry has unique facts. It is only in the rarest and most unusual circumstances that the Department can justifiably vary from the standard apportionment methodology provided for in South Carolina's statutes and rules. The ALC decision below threatens to disrupt this long-standing South Carolina structure. In essence, the decision below arms the Department with the

power to deviate from the strict statutory scheme not just in rare and unusual circumstances, but even in situations where the facts are commonplace.

Additionally, COST and its members have an interest in promoting efficiencies and controlling costs in litigation such that taxpayers can avoid an extended, time-consuming and expensive process that results in substantial financial burdens and delayed resolutions for taxpayers.

ARGUMENT

Review of the ALC's decision by this Court is warranted in this case because of the potentially widespread impact the decision could have on the consistency and reliability of South Carolina's corporate income tax laws. The importance of this case goes far beyond the application of a rarely imposed statutory exception to a single interstate taxpayer. The latitude the ALC granted the Department to deviate from the standard statutory apportionment formulae will have a significant impact on taxpayers across South Carolina. Of equal, if not greater, importance is the fact that that action of the Department threatens the consistency and uniformity that the South Carolina legislature has sought to achieve in the area of state taxation of interstate commerce.

Additionally, when appropriate, an appellate court should enter judgment or enter a factual finding where there is no evidence in the record upon which a lower court could rule in favor of one of the parties. In the alternative, if an

appellate court does remand such a case, then it should provide appropriate guidance or instructions to the ALC to avoid multiple appeals and trips back to the ALC. COST and its members have an interest in avoiding such inefficiencies, burdensome expenses and delayed resolutions to cases.

I. THERE IS NO BURDEN OF PROOF ISSUE

There is no longer a burden of proof issue in this case. The Court of Appeals properly held that the Department, as the proponent of an alternative method authorized by § 12-6-2320(A)), had the burden of proving that (1) the standard apportionment formula did not fairly represent the taxpayer's business activity in this state, and (2) the method chosen by the Department was reasonable. Although the Department at one time took a different position in the case, both parties now agree that this is the proper standard.

In its Petition for Writ of Certiorari, the Department attempts to create a burden of proof issue where none exists by arguing that the Court of Appeals erred in stating that the alternative formula chosen by the Department must be "not only appropriate, but more appropriate than any other competing methods." First, the Department argues that this language misstates the law in South Carolina. Additionally, the Department appears to argue that CarMax West had a duty to come forward with another competing method. Neither argument has credence or justifies this Court issuing a writ of certiorari.

The Court of Appeals appears to have quoted the language that the Department questions from *Media General Communications v. S.C. Dept. of Revenue*, 388 S.C. 138, 694 S.E.2d 525 (2010), a case in which both parties agreed that the standard method was not fair and agreed that the combined reporting method proposed by the taxpayer did fairly represent those activities. In that case, because the Department did not propose another method, the Court adopted the taxpayer's method. The Court did not address the burden of proof at all. Thus, Media General has no bearing on this case, which involves a taxpayer that is relying on the standard apportionment method and who is not proposing any other competing method. The only competing method in this case is the statutory method and that method is, therefore, the method that the Department must show fails to represent the taxpayer's activities in this state. To the extent that the Court of Appeals' language could be interpreted as requiring that the Department prove that its method was not only more appropriate than the statutory method but also more appropriate than any other conceivable method, it is harmless and irrelevant to the burden of proof question at hand where the taxpayer has relied on the statutory method and has not proposed an alternative method.

In addition, to the extent the Department is asserting that CarMax West had a duty to come forward with another competing method, the law provides no

support for this argument. Section 12-6-2320 allows a taxpayer to rely on the standard apportionment method. If the Department disagrees, then it must show that the standard method does not fairly represent the extent of that taxpayer's business activities in this State and that its alternative is reasonable. See S.C. Code Ann. §12-6-2320(A) There is simply no requirement that the taxpayer propose another competing method, and CarMax West had a clear right and, in fact, duty under the statute, to use the standard method, which it has done and seeks to defend.

II. THE COURT SHOULD ENTER JUDGMENT IN FAVOR OF CARMAX WEST VERSUS REMANDING THE CASE TO THE ALC WHERE THERE IS NO EVIDENCE THAT COULD SUPPORT THE DEPARTMENT 'S POSITION.

COST and the taxpayers it represents have an interest in streamlining the litigation process, reducing inefficiencies and litigation costs, and avoiding duplicative or unnecessary litigation and appeals that delay final resolution. Where a lower court makes an error of law in its decision, an appellate court should usually remand the case to the lower court to allow it to apply the correct law to the facts of the case. However, an exception to this general rule should be made where, as in this case, there is no evidence in the record upon which the lower court could find in favor of one of the parties. In such a case, the appellate court should simply enter judgment and not remand the case to the lower court thus promoting efficiencies, reducing costs for all parties, including taxpayers,

and avoiding further delay to the final resolution. *See* S.C. Code Ann. § 1-23-610(B) (which provides that an appellate court may reverse a decision of the ALC if it is "clearly erroneous in view of the reliable, probative, and substantial evidence on the whole record."); *Sierra Club v. South Carolina Dep't of Environmental Control*, 387 S.C. 424, 431, 693 S.E.2d 13, 16 (2011).

As set forth in CarMax West's Petition in this matter, the Department presented no evidence of distortion in this case. The only "evidence" cited by the Department in support of distortion were two facts- that CarMax West had less taxable income than its related company, CarMax East, and that CarMax West's tax bill was lower under the standard formula than it would be under the Department's method. Neither of these assertions has any relevance to the questions at issue, i.e. does the standard method fairly represent the extent of CarMax West's activities in South Carolina and is the Department's alternate method a fair reflection of those activities.

A. Sound Tax Policy Supports Alternative Apportionment being Used in Limited Circumstances.

Sound tax policy supports the requirement that alternative apportionment be used in limited circumstances. The ALC Order correctly notes that the statutory authority of the Department to require an alternative method is triggered *only* if the standard formulas contained in Title 12, Chapter 6 fail to fairly represent the extent of the taxpayer's business activity in South Carolina.

However, the ALC Order then fails to apply the correct “fair representation” standard. South Carolina alternative apportionment law is modeled after the alternative formula contained in UDITPA. This standard was evoked by Prof. William Pierce, UDITPA’s principal draftsman, who stated that the equitable apportionment provision should be limited to the “unusual case:”

Of course, departures from the basic formula should be avoided except where reasonableness requires. Nevertheless, some alternative method must be available to handle the constitutional problem *as well as the unusual cases*, because no statutory pattern could ever resolve satisfactorily the problems for the multitude of taxpayers with individual business characteristics. (Emphasis added.)

W. Pierce, 'The Uniform Division of Income for State Tax Purposes,' 35 Taxes 747, 781 (1957).

The Multistate Tax Commission Regulations take a similar position.

MTC Reg. IV.18.(a) provides:

[UDITPA §] 18 permits a departure from the allocation and apportionment provisions of [UDITPA] *only in limited* and specific cases. [UDITPA § 18] may be invoked only in specific cases where *unusual fact situations* (which ordinarily will be unique and nonrecurring) produce incongruous results under the apportionment and allocation provisions contained in [UDITPA]. (Emphasis added.)

The Department's ad hoc deviation from the statutory apportionment formula in this case is truly unprecedented. To Amicus's knowledge, this case represents the only time that a state tax administrator has ever used the alternative apportionment clause of a UDITPA-based formula to randomly sever a viable arm of a business in order to increase a state's tax liability. Such a radical departure from the way in which other states have routinely interpreted an identical provision should not be allowed to stand without this Court's scrutiny.

South Carolina adopted a modified version of the UDITPA and accompanying regulations in order to join other states in applying a standard statutory apportionment formula. The goal of UDITPA, and the South Carolina statutes modeled on it, is to provide consistent and uniform rules across the nation to ensure that each state taxes only an appropriate portion of a corporation's income in order to avoid duplicative taxation. Uniform rules are intended to address virtually every situation, and deviation from the rules should be used in the rarest of circumstances. As the primary technical drafter of UDITPA noted:

There are completely compelling reasons for giving the [alternative apportionment] provisions a narrow construction. Under a broad construction the purposes of obtaining uniformity through the adoption of the Uniform Act would be defeated. If a choice of methods is permitted, different administrators in different states inevitably will choose different methods. As a result, even if all the states imposing taxes on or measured by income

should adopt the Uniform Act, the chaotic condition heretofore existing would continue to exist.

Keesling and Warren, California's Uniform Division of Income for Tax Purposes Act, 15 UCLA L. Rev. 156, 171 (1967) (emphasis added). The ad hoc approach, if allowed to stand, will open the door to the “chaotic condition” that UDITPA seeks to ameliorate.

The drafters of the UDITPA made it clear that the alternative apportionment provisions were “designed to permit the use of methods different than those prescribed in the Act only in unusual cases and in cases where the application of the specifically prescribed methods might be held unconstitutional.” *Id.* While the distortion requirement has often been interpreted to be satisfied at a level of less than what is unconstitutional, the intent of the UDITPA drafters is clear—the provision should be used sparingly.

Other states that have invoked the alternative apportionment methodology have done so under much different circumstances than those at issue here. The use of alternative apportionment by either taxpayers or administrators in other states has typically been limited to very narrow circumstances. Some early equitable apportionment cases arose out of attempts by taxpayers or tax administrators to utilize alternative apportionment based solely on large disparities between tax liability under separate accounting and apportionment. *See, e.g., Donald M. Drake v. Dep't of Revenue*, 500 P.2d 1041 (Or. 1972)

(rejecting administrator's attempt to impose separate accounting on in-state portion of unitary business based on profits); *Amoco Prod. Co. v. Arnold*, 518 P.2d 453 (Kan. 1974). Alternative apportionment has also been invoked to exclude amounts from an out-of-state capital gain, an issue which would have been more appropriately addressed based on unitary business principles. *See, e.g., Stan Musial & Biggies, Inc. v. State*, 363 So.2d 375 (Fla. Dist. Ct. App. 1978); *Roger Dean Enterprises Inc. v. State*, 387 So.2d 358 (Fla. 1980) (holding that alternative apportionment is inapplicable to exclude gain).

Courts have hesitated to allow either taxpayers or administrators to invoke alternative apportionment whenever economists might disagree on the appropriateness of the standard apportionment formula. *See, e.g., Colgate-Palmolive Co., Inc. v. Bower*, Ill. Cir. Ct. No. 01 L 50195, 2002 WL 31628400 (2002) (denying Section 18 claim that a fourth factor representing contribution of international trademarks should be added to formula); *Pacific Coca-Cola Bottling Co. v. Dep't of Revenue*, 773 P.2d 1290 (Or. 1989) (denying factor adjustment for value of trade names, finding that value already reflected in costs of tangibles); *NCR Corp. v. Comptroller of the Treasury*, 544 A.2d 764 (Md. 1988) (denying factor relief claim for foreign-source income absent gross disparity in tax liability). The courts recognize that without any limitations based on exceptionality, relief petitions and litigation would certainly increase in frequency.

The case here is very similar to many of the other cases where the expanded use of alternative apportionment was justifiably curtailed. Simply stated, no circumstances warrant the use of alternative apportionment in this case. Neither side contends that application of the standard apportionment formula produced an unconstitutional result. Neither was there any substantive showing that the standard UDITPA formula failed to fairly represent the extent of CarMax's activities in South Carolina because of some unusual circumstances. No unusual circumstances existed. To the contrary, the standard applicable formula operated in this case precisely as it was intended to by the drafters of UDITPA and—more to the point—by the South Carolina Legislature.

The Department essentially determined that the taxpayer had different types of receipts and income—retail and intangibles—and that some of that income and receipts should not be reported on a South Carolina return. Every multistate taxpayer has different types of receipts and income and consequently could be subject to a similar ad hoc determination. As the Minnesota Supreme Court recently noted in a decision that prevented the Minnesota Tax Commissioner from deviating from its statutory tax rules: “[t]he Commissioner clearly dislikes the tax consequences that occur under the relevant statutes, but it is for the legislature, not the Commissioner, to change the law that creates such consequences.” *HMN Fin., Inc. v. Comm’r of Rev.*, 782 N.W.2d 558 (Minn. 2010).

B. Deviation From the Standard Formula Without Any Prior Guidance by the Department Violates the APA, Is Fundamentally Unfair and Runs Counter to Sound Tax Policy.

South Carolina's standard statutory and regulatory apportionment rules—like those in other states—are designed to uniformly address virtually every factual situation. However, as discussed above, the rules do allow for limited deviations from the standard formulae on a specific taxpayer basis, but only where there are unusual and nonrecurring fact patterns. The Department refused to follow the standard statutory apportionment formulae in this case, not because the facts were unusual and nonrecurring, but because the Department was dissatisfied with the amount of tax produced by the standard formulae. The Department cannot disregard its statutory obligation to provide advance guidance through rule making in order to increase tax revenue.

There is certainly nothing unusual about the structure of West. The Findings of Facts specifically note that West's structure "shares features with the structures of other multi-state taxpayers who divide their retail operations into 'East' and 'West' operations and similarly benefit from this structure in the form of tax savings" Findings of Fact No. 6. It is unpleasant for taxpayers who must rely on written guidance and interpretations to witness the Department acknowledge that a particular structure is commonplace while at the same time invoke a special rule aimed at unusual, taxpayer-specific circumstances.

The typical state administrative procedure act contains two separate sets of procedures—one for rulemaking and one for adjudication. While agencies delegated authority to issue rules and to decide individual cases normally have broad discretion as to the means by which they may make particular law, they are bound by their state act to follow scrupulously the procedures appurtenant to whatever means of lawmaking they actually choose in a particular instance.

The Department promulgates rules through regulations issued in accordance with the South Carolina's administrative procedures act. Code §1-23-10 *et seq.* and Code §12-4-320(1). Also, the Department announces general statements of position for guidance through advisory opinions which are not regulations and do not have the force of law. See Code §§1-23-10(4) and 12-4-320. The legislature obviously recognized that the Department would need to exercise a great deal of discretion in furtherance of its duty to enforce the tax laws of the State, and that in exercising its discretion taxpayers need to be advised of all rules utilized by the Department to enforce the tax laws of the State. To conclude, as the Department does, that it need not go through the rulemaking process (or offer any other guidance) ignores the affirmative statutory duties placed on the Department by the legislature.

In *CBS, Inc. v. Comptroller*, 575 A.2d 324 (Md. 1990), the Maryland Supreme Court, addressing a situation not that different from the one here, held that the tax administrator may enact certain tax policies only prospectively, and

then only by formal rulemaking. *CBS* dealt with the manner in which a taxpayer apportioned advertising receipts of national broadcasting companies. For a number of years, CBS computed its Maryland income tax pursuant to the three-factor formula. The taxpayer and the tax administrator stipulated that the taxpayer's method of apportionment "was reviewed during the audits of prior years . . . and no adjustment . . . was ever proposed." *Id.* at 325. Despite this prior history of acquiescence in the taxpayer's method of apportionment, "when the 1980 and 1981 returns were audited, the Appellant for the first time insisted on the application" of a new apportionment method. *Id.* The question presented was whether the tax administrator's new policy required formal rulemaking. The Court found that "the effect of the tax administrator's audit was to announce a substantially new generally applicable policy with respect to apportionment of the network advertising income of national broadcasting corporations." *Id.* at 330.

The Court explicitly rejected the tax administrator's assertion that the alternative apportionment authority granted to the tax administrator, which is identical to the South Carolina provision at issue here, gave the administrator the authority to enact this new policy without formal rulemaking. Referring to *Metromedia, Inc. v. Dir., Div. of Taxation*, 478 A.2d 742 (N.J. 1984), the Maryland Supreme Court noted: "it does not follow that, because [an agency] has statutory discretion, the manner in which this discretion is exercised is not governed by the standards that determine whether rulemaking or adjudication

must be followed in a given case.” *CBS*, 575 A.2d 328. The Court held that the tax administrator’s new policy could not be effected through ad hoc adjudication, but only prospectively pursuant to the formal rulemaking procedures of the Maryland Administrative Procedure Act. As a result, the Appellant’s position could not be applied retroactively.

The Maryland Supreme Court’s reasoning in *CBS* seamlessly flows into the analysis to the South Carolina Administrative Procedure Act, which also requires that a change or implementation of policy by a state agency be accomplished by promulgating a regulation. It is inequitable for the Department to invoke such a unique apportionment regime on a common scenario through the adjudicatory process. Rather, it should have promulgated rules so that all similarly situated taxpayers are aware of and have the ability to fully understand the Department’s intent to sever parts of a company at the time a taxpayer files its return.

The importance of clear regulatory guidance that is available to all taxpayers prior to the time they file a return cannot be overstated. The ability to make reasonably accurate forecasts of state tax liability is an essential element of informing one’s investors. Such forecasts of a taxpayer’s total state tax liability cannot be made without reasonably fixed standards. The standard South Carolina rules for apportionment are designed to provide certainty through fixed standards. When a tax is imposed without regard to the recognized standards – as was the

assessment here – sound business decisions based upon expected tax liabilities becomes impossible.

In sum, the Department presented no evidence to the ALC that would support a deviation from the standard formula and, therefore, the Court should simply enter judgment in favor of the taxpayer. A remand on this issue would only burden the taxpayer and the State of South Carolina with unnecessary expenses and delay a final resolution in this matter.

III. THE COURT SHOULD ENTER A FACTUAL FINDING THAT CARMAX WEST IS A UNITARY BUSINESS VERSUS REMANDING THE CASE TO THE ALC TO MAKE THAT DETERMINATION WHERE THE EVIDENCE AT TRIAL WAS UNCONTESTED ON THAT ISSUE.

Similar to I above, where the evidence regarding an issue is uncontested but the lower court simply failed to make a finding (in this case, because the Court did not think it relevant), the appellate court should simply enter a factual finding versus remanding the case to the ALC so that taxpayers do not bear unnecessary costs and have final resolution further delayed. Both the ALC and the Court of Appeals failed to rule that CarMax West operates a unitary business despite the evidence being uncontested on this issue at trial. *See* App. pp. 1083-1086, Appellant's Brief, and p. 1158, Appellant's Reply Brief. The Department introduced no evidence to show that CarMax West was not operating a unitary business, and, in fact, its auditor agreed that all CarMax entities were a unitary

business. *Id.* There is simply no reason to remand this case to the ALC on this issue when there is no evidence upon which a lower court could find that CarMax West did not operate a unitary business.

II. IF THE COURT DETERMINES THAT REMAND IS PROPER, THEN IT SHOULD PROVIDE INSTRUCTIONS OR GUIDANCE TO THE ALC AS DOING SO WILL AVOID MULTIPLE APPEALS.

In the alternative to I, II and III above, if this Court believes that a remand is necessary in this case, then the Court should instruct the ALC to consider whether CarMax West is a unitary business and, if so, consider whether the Department's effort at a form of separate accounting is appropriate for such a business. The ALC Order correctly notes that in order to deviate from the South Carolina income tax standards, the standard formula must fail to fairly represent the extent of the taxpayer's business activity in South Carolina and the requested alternative method must be reasonable. The Department's requested alternative method seeks to divide a unitary business and therefore may be viewed as a form of separate accounting. Thus, the ALC should be instructed to consider whether separate accounting is reasonable where the taxpayer operates a unitary business.

While separate accounting is a method expressly permitted by Section 12-6-2320(A)(1), it should not be used to separate the elements of a unitary business, and South Carolina law is clear on this point. *See Exxon Corp. v. S.C. Tax Comm'n*, 273 S.C. 594, 258 S.E.2d 93 (1979). Additionally, this Code Section

also expressly allows a taxpayer to petition for use of an alternative method, which the DOR is required to grant under the same standards as involved in this case. Accordingly, the policy question that will be before the ALC is whether it makes for good tax and public policy to allow taxpayers -- as well as the Department -- involved in a unitary business to petition for separate accounting.

Hellerstein & Hellerstein, *State Taxation*, at ¶ 8.03, pg. 8-38, describes separate accounting as follows:

Separate accounting is a technique of carving out of the taxpayer's overall business the activities taking place, the property employed, and the income derived from sources within a single state and by accounting analysis ascertaining the profits attributable to that portion of the business; Accordingly, separate accounting is based on the theory that the business of a multistate taxpayer can be divided into separate compartments so that its activities within the taxing state can be segregated from its activities elsewhere and accounted for separately.

After noting that "Over the years, separate accounting has been the focus for increased criticism," (pg. 8-40), the Treatise severely criticizes the separate accounting method for the following reasons:

Separate accounting, as a method of dividing the income of a unitary business among the states, suffers from three inherent defects. First, it is fearfully expensive, since adequate underlying data cannot be furnished without maintaining the books of account in a manner that will show the details of the taxpayer's business, operations, and transactions on a state-by-state basis. Moreover, it has been suggested that "a system of separate accounts for

branches or subsidiaries is, in the majority of cases, impracticable."

Second, the Achilles heel of separate accounting lies in the construction of the imputed prices at which goods are deemed purchased and sold between various branches or subsidiaries of the enterprise.

* * * *

The third inherent defect in separate accounting, as applied to a unitary business, goes to the merits of the method. As in *Alice in Wonderland*, it operates in a universe of unreality. For the essence of the separate accounting technique of dividing the income of a unitary business is to ignore the interdependence and integration of the business operations conducted in the various states, and to treat them, instead, as if they were separate, independent, and nonintegrated. (pgs. 8-41 and 8-43)

Taxpayers have frequently asserted separate accounting as a basis to invalidate standard income tax based assessments. Such challenges have been uniformly unsuccessful. Hellerstein states (§ 8.15[1] pgs. 8-240, -241, -243, -244, -245, -247) the following:

Taxpayers typically rely on separate accounting computations as the basis for their contention that the state's formula misapportions income to the taxing state, citing *Hans Rees' Sons, Inc. v. North Carolina*. [283 U.S. 123 (1931)]

* * *

As the ensuing discussion reveals, however, subsequent [United States Supreme Court] decisions have eroded—if not altogether repudiated—the central proposition for which *Hans Rees* stands.

* * *

In subsequent decisions, the [Supreme] Court has reiterated the view that separate accounting evidence does not—as a matter of federal constitutional law—"impeach the validity or propriety" of the apportionment of the income of a unitary business.

* * *

Three years later in *Container* [Corp. of Am. v. Franchise Tax Bd., 463 U.S. 159 (1983)], involving a constitutional challenge to California's worldwide combined reporting regime, the Court reiterated the view that the results of separate accounting evidence did not undermine the validity of the formulary apportionment of the income from a unitary business:

* * *

Despite the Court's apparent rejection of separate accounting evidence as theoretically irrelevant to the propriety of formulary apportionment of the income of a unitary business, the Court nevertheless felt compelled to respond to the taxpayer's claim that the separate accounting evidence demonstrated distortion, by revealing a disparity between the income attributed to the state by formula and the income attributed to the state by separate accounting. In rejecting the taxpayer's contention, the Court observed:

But we have seen no evidence demonstrating that the margin of error (systematic or not) inherent in the three-factor formula is greater than the margin of error (systematic or not) inherent in the sort of separate accounting urged upon us by appellant. Indeed, it would be difficult to come to such a conclusion on the basis of the figures in this case: for all of appellant's statistics showing allegedly enormous distortions caused by the three-factor formula reveal that the percentage increase in taxable income attributable to California between the methodology employed by appellant and the methodology employed by appellee comes to

approximately 14%, a far cry from the more than 250% difference which led us to strike down the state tax in *Hans Rees' Sons, Inc.*, and a figure certainly within the substantial margin of error inherent in any method of attributing income among the components of a unitary business.

* * * *

After considering the Court's decision in *Exxon* [Corp. v. Wisconsin Dept. of Revenue, 447 U.S. 207 (1980)], *Container*, and *Trinova*, [Corp. v. Michigan Dept. of Treasury, 498 U.S. 358 (1991)], *only the most sanguine taxpayer would harbor the hope that the Supreme Court may still be moved by separate accounting evidence to invalidate the application of a three-factor formula to the income (or other tax base) of a unitary business.* (Emphasis added.)

Hellerstein discusses several recent cases in which the taxpayer asserted that a separate accounting analysis moved distortion. In ¶ 8.15[4] (Supplement pgs. 8-71-72, Hellerstein states:

In *Pennzoil Co. v. Department of Revenue*, the Oregon courts considered the question of whether the inclusion in Pennzoil's apportionable tax base of the proceeds from one of the largest tort settlements in Corporate history—the \$3 billion payment that Pennzoil received from Texaco for settlement of a lawsuit for wrongful interference with Pennzoil's contract to acquire Getty Oil Company—gave rise to unconstitutional distortion. Pennzoil asserted that the inclusion of the settlement proceeds in the apportionable tax base, which, according to Pennzoil, increased its Oregon income by 1,877 percent, resulted in unconstitutional distortion. The Oregon Tax Court rejected this argument on several grounds.

* * *

Second, the Tax Court dismissed—again, quite

properly—the suggestion that Pennzoil's separate accounting evidence, which showed a loss in Oregon, demonstrated that the attribution of an extraordinary amount of income to the state was unconstitutionally distortive. In the absence of a demonstration that the source of the gain was not part of the taxpayer's unitary business—something that Pennzoil, in the Tax Court's view, was unable to establish, the law is well settled that separate accounting cannot impeach the validity of a reasonable apportionment.

In affirming the Tax Court's decision, the Oregon Supreme Court observed:

Our answer to Pennzoil's argument mirrors the Tax Court's. First, we disapprove of the separate accounting method that Pennzoil advocates. Indeed, the difficulty in applying a separate accounting method to a multistate business is the very reason for apportionment and the unitary business principle.

Lastly, Hellerstein (§ 9.20(3)(a), pg. 9-245-246) states:

[a] Separate Accounting as Basis for Equitable Apportionment

An Oregon construction company that worked on projects in California, Oregon, and Washington, sought to be taxed on a unitary basis, since the Oregon projects were profitable and the California projects showed losses. The Department of Revenue resisted and applied separate accounting to the company's income, relying on the UDITPA equitable apportionment provision.

The court, however, found no basis for the resort to special accounting, and took the position that the equitable apportionment provision should be narrowly construed, quoting from Keesling and Warren:

"There are completely compelling reasons for giving the relief provisions a narrow construction. Under a broad construction the purposes of obtaining uniformity through the adoption of the Uniform Act would be defeated. If a choice of methods is permitted, different administrators in different states inevitably will choose different methods. As a result, even if all the states imposing taxes on or measured by income should adopt the Uniform Act, the chaotic condition heretofore existing would continue to exist." We agree with the conclusion of the Tax Court that the use of any method other than apportionment should be exceptional and the party the taxpayer or the Department of Revenue--who seeks to invoke the applicability of ORS 314.670 has the burden of proof.

* * *

In most states, the taxpayer cannot establish a right under the equitable apportionment provision to substitute separate accounting for the formula merely by showing that separate accounting produces a lower tax. (Emphasis added.)

See also, Citizens Utils. Co. of Ill. v. Department of Revenue, 488 N.E.2d 984 (1986) (the court rejected the taxpayer's claim of unconstitutional distortion of income based on the allegation that the use of formula apportionment increased its tax liability 213% over the amount determined by separate accounting).

Instructions by this Court to the ALC regarding the need to consider unitary business law and related tax policy issues will ensure that the ALC

considers the relevant facts and law on remand, will promote judicial economy and will avoid unnecessary expenses and multiple proceedings and appeals.

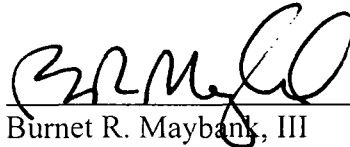
III. WHERE A CASE IS REMANDED DUE TO A LEGAL ERROR BY THE ALC, THE COURT SHOULD INSTRUCT THE ALC TO MAKE NEW FINDINGS BASED ON THE EVIDENCE IN THE RECORD AND SHOULD NOT ALLOW A FULL RE-TRIAL.

As previously stated, COST and the taxpayers it represents have an interest in reducing burdensome litigation expenses where possible and obviously the State of South Carolina shares that interest as it affects both parties equally. To that end, this Court should make it clear in its instructions to the ALC that the Court of Appeals' order for the ALC to reconsider all issues should be based on the facts in the record and is not an order for a new trial. Under South Carolina law, when a case is remanded back to the trial court, a party may not submit additional evidence unless the appellate court grants the party leave to do so. *Parker v. S.C. Public Serv. Comm'n*, 288 S.C. 304, 342 S.E.2d 403 (1986) (finding Supreme Court's remand to Public Service Commission "for such further *consideration* as may be proper in light of the views expressed herein" was an instruction for the Commission "merely to review the evidence which was admitted in the record" and did not allow the Commission to consider additional evidence, as no party should get two bites at the apple); *Piedmont Natural Gas Co., Inc. v. Hamm*, 301 S.C. 50, 389 S.E.2d 655 (1990) (holding that remand to Public Service Commission "to substantiate the record" was an order to review

the evidence already presented not to take additional evidence). As CarMax West has pointed out in its Petition, the Department agreed at trial that it should bear the burden of proof. *See* Appellant's Brief at App. p. 1078 (citing App. 464, lines 3-9). It should have presented any evidence it needed to meet this burden at trial. It would be unfair to now require the parties to bear the burden and expense of another trial. *Lewis v. Lewis*, 392 S.C. 381, 709 S.C. 650 (2011) (reversing Court of Appeals decision, which found that the value of the marital home was not supported by the record and which remanded the case with instructions that invited the lower court to accept additional evidence, and noting that "Given Respondent's incomplete presentation at trial, it would be fundamentally unfair to Petitioner to give Respondent a second bite at the apple"); *Sierra Club v. South Carolina Dep't of Environmental Control*, 387 S.C. 424, 693 S.E.2d 13 (2011) (remanding case to ALC with instructions to apply its factual findings to the proper regulations, which the ALC had not addressed in its order). Therefore, if this case is remanded, then the Court should instruct the ALC that its reconsideration of the issues while applying the correct burden of proof should be done based on the record and no new evidence or testimony shall be allowed.

CONCLUSION

COST respectfully urges this Court to grant CarMax's Petition for Writ of Certiorari and deny the Department's Petition for Writ of Certiorari. Review is appropriate for all the reasons detailed in CarMax's Petition, and, for the reasons explained in this brief, review is especially appropriate because the decision, if allowed to stand, will jeopardize and undermine the uniformity, fairness, and consistency of state taxation that South Carolina law was designed to offer to multi-state taxpayers and will result in significant and unnecessary expenses and delay for the taxpayer and the State of South Carolina.



Burnet R. Maybank, III
NEXSEN PRUET, LLC
1230 Main Street, Suite 700 (29201)
Post Office Drawer 2426
Columbia, South Carolina 29202
803-771-8900

Alexandra E. Sampson
REED SMITH LLP
1301 K Street, N.W.
Suite 1100 East Tower
Washington, DC
202-414-9486

Attorneys for Council on State Taxation

Columbia, South Carolina
January 29, 2013

THE STATE OF SOUTH CAROLINA
In The Supreme Court

APPEAL FROM THE ADMINISTRATIVE LAW COURT

Carolyn C. Matthews, Administrative Law Judge

Case No. 09-ALJ-17-0160-CC

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SC Supreme Court

v.

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CERTIFICATE OF COUNSEL

The undersigned certifies that this Brief of Amicus Curiae by the Council on State
Taxation ("COST") complies with Rule 211(b), SCACR.


Burnet R. Maybank
NEXSEN PRUET, LLC
1230 Main Street, Suite 700 (29201)
Post Office Drawer 2426
Columbia, South Carolina 29202
803-771-8900

Alexandra E. Sampson
REED SMITH LLP
1301 K Street, N.W.
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PROOF OF SERVICE

I certify that I served the **Amicus Curiae Brief of Council on State Taxation (“COST”) in Support of Petition for Writ** on the Petitioner and Respondent by depositing copies of it in the United States Mail, postage prepaid, on Jan 29, 2013 addressed to their attorneys of record as follows:

Counsel Served:

**Attorneys for the South Carolina
Department of Revenue:**

Milton Kimpson, Esq.
Harry A. Hancock
South Carolina Department of Revenue
P.O. Box 12265
Columbia, SC 29211

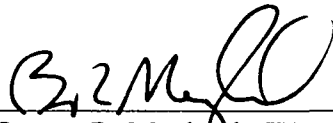
**Attorneys for CarMax Auto
Superstores West Coast, Inc.**

John C. von Lehe, Jr.
Bryson M. Geer
Nelson Mullins Riley & Scarborough,
LLP
151 Meeting Street, Suite 600
Charleston, SC 29401

**Attorneys for South Carolina State
Chamber of Commerce**

Robert L. Widener
Erik P. Doerring
McNair Law Firm, P.A.
PO Box 11390
Columbia, SC 29211

A. Mattison Bogan
Nelson Mullins Riley & Scarborough,
LLP
1320 Main Street, 17th Floor
Columbia, SC 29201



Burnet R. Maybank, III
NEXSEN PRUET, LLC
1230 Main Street, Suite 700 (29201)
Post Office Drawer 2426
Columbia, South Carolina 29202
803-771-8900

Alexandra E. Sampson
REED SMITH LLP
1301 K Street, N.W.
Suite **1100** East Tower
Washington, DC
202-414-9486

Attorneys for Council on State Taxation

Columbia, South Carolina
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