No. 12-401

IN THE

Supreme Court of the United States

KIMBERLY-CLARK CORPORATION AND
KIMBERLY-CLARK WORLDWIDE, INC.,
Petitioners,

v.

ALABAMA DEPARTMENT OF REVENUE,
Respondent.

On a Petition for a Writ of Certiorari to the Alabama Court of Civil Appeals

MOTION OF TAX EXECUTIVES INSTITUTE, INC. FOR LEAVE TO FILE AS *AMICUS CURIAE* AND BRIEF OF *AMICUS CURIAE* IN SUPPORT OF THE PETITIONERS

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October 26, 2012

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MOTION OF TAX EXECUTIVES INSTITUTE, INC. FOR LEAVE TO FILE A BRIEF AS *AMICUS CURIAE* IN SUPPORT OF THE PETITIONERS

Pursuant to this Court's Rule 37.2, Tax Executives Institute, Inc. hereby moves for leave to file the accompanying brief as *amicus curiae* supporting petitioners. The consent of the counsel for petitioners has been obtained and is on file with the clerk. Counsel for respondent declined to give consent.

Tax Executives Institute ("TEI" or "the Institute") is a voluntary, nonprofit association of corporate and other business executives, managers, and administrators who are responsible for the tax affairs of their employers. TEI was organized in 1944 under

the laws of the State of New York and is exempt from taxation under section 501(c)(6) of the Internal Revenue Code (26 U.S.C.). The Institute is dedicated to promoting the uniform and equitable enforcement of the tax laws, reducing the costs and burdens of administration and compliance to the benefit of both the government and taxpayers, and vindicating Commerce Clause protections and the constitutional rights of business taxpayers.

The members of the Institute represent a cross section of the business community. The multijurisdictional companies represented by the Institute's membership are significantly affected by state business taxes, and especially the rules governing the allocation and apportionment of income among the various States. As a result, nearly all Institute members will be affected by the resolution of this case, which addresses the treatment of a particular type of income received by a taxpayer. If the decision of the Alabama courts stands, taxpayers throughout the Nation will suffer the ensuing uncertainty, an increase in the cost and burden of compliance, and the enhanced potential for duplicative taxation. As individuals who must contend daily with the interpretation and administration of the Nation's tax laws, the Institute's members have a vital interest in the proper disposition of this case.

In view of its interests and unique perspective on these issues, Tax Executives Institute respectfully requests that this Court grant it leave to participate as *amicus curiae* by filing the accompanying brief in support of the petition for a writ of certiorari.

Respectfully submitted,

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BRIEF OF TAX EXECUTIVES INSTITUTE, INC. AS *AMICUS CURIAE* IN SUPPORT OF THE PETITIONERS

INTEREST OF *AMICUS CURIAE*

Pursuant to Rule 37 of the Rules of this Court, Tax Executives Institute, Inc. submits this brief as *amicus curiae* in support of the petition for a writ of certiorari.[1] Tax Executives Institute ("TEI" or "the

[1] Pursuant to Rule 37.6, *amicus* Tax Executives Institute, Inc. states that no counsel for a party has written this brief in whole or in part and that no person or entity, other than *amicus*, its members, or its counsel, has made a monetary contribution to the preparation or submission of this brief. Tax Executives Institute timely notified the parties of *amicus's* intent to file

Institute") is a voluntary, nonprofit association of corporate and other business executives, managers, and administrators who are responsible for the tax affairs of their employers. TEI was organized in 1944 under the laws of the State of New York and is exempt from taxation under section 501(c)(6) of the Internal Revenue Code (26 U.S.C.). The Institute is dedicated to promoting the uniform and equitable enforcement of the tax laws, reducing the costs and burdens of administration and compliance to the benefit of both the government and taxpayers, and vindicating Commerce Clause protections and the constitutional rights of business taxpayers.

The members of the Institute represent a cross section of the business community. The multijurisdictional companies represented by the Institute's membership are significantly affected by the rules governing state taxes generally, and especially those governing the allocation and apportionment of income among the various States. As a result, nearly all Institute members will be affected by the resolution of this case, which addresses the treatment of a particular type of income received by a taxpayer. If the decision of the Alabama courts stands, taxpayers throughout the Nation will suffer uncertainty, an increase in the cost and burden of compliance, and the enhanced potential for duplicative taxation. As individuals who must contend daily with the interpretation and administration of the Nation's tax laws, the Institute's members have a vital interest in the proper disposition of this case.

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this brief. Petitioners consented in a letter filed with the clerk; respondent declined to give consent.

The continuing expansion of commerce across borders has made the division of the tax base among competing jurisdictions one of the most critical issues affecting state taxation of multistate businesses almost since the country's founding. Early on, States and taxpayers struggled to identify and define the constitutional limits on States' ability to tax businesses present in multiple jurisdictions. As railroads and transportation companies crisscrossed the American landscape in the mid-1800s, States applied varying systems of apportioning and taxing those businesses based on a ratio of their activity within a given State relative to their activity everywhere. The resulting apportionment ratio or percentage was multiplied by the business's tax base to arrive at that part of a taxpayer's business a State could subject to tax.

Well over a century ago, this Court confirmed the constitutionality of States' use of apportionment formulas even observing that "[i]t may well be doubted whether any better mode of determining" the tax base attributable to a particular State exists. *State R.R. Tax Cases*, 92 U.S. 575, 608 (1875). While certain income is so divorced from a company's general business operations that the Constitution requires it be excluded from the apportionable tax base, the Constitution requires that all income generated by a taxpayer's "unitary business" be subject to apportionment to avoid double taxation.[2] Thus, this

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[2] Although the terms "allocation" and "apportionment" are often used interchangeably in respect of the division of income among various jurisdictions, "allocation" properly refers to the "attribution of a particular type of income to a designated state, [and] 'apportionment' refers to the division of the tax base by formula." JEROME R. HELLERSTEIN & WALTER HELLERSTEIN,

Court held that the taxability of a non-domiciliary taxpayer's out-of-state business turned on the application of the "unit rule" or the unitary business principle — on whether the out-of-state income sought to be taxed was "unitary" with, or functionally related to, the taxpayer's in-state activities. *Id.* In *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425, 439 (1980), the Court encapsulated its prior holdings by declaring the unitary business principle to be the "linchpin of apportionability in the field of state income taxation."

Regrettably, the decision of the Alabama courts sheers off that linchpin. By ruling that certain income (gain from the sale of assets integral to the taxpayer's operations) should be allocated fully to Alabama rather than apportioned among the States, Alabama arrogated a larger share of income than was its due. Unchallenged, this decision will place taxpayers throughout the United States at risk of multiple taxation on income earned as part of their unitary businesses. "Taxation by apportionment and taxation by allocation to a single situs are theoretically incommensurate, and if the latter method is constitutionally preferred, a tax based on the former cannot be sustained." *Mobil*, 445 U.S. at 444-45, *citing Standard Oil v. Peck*, 342 U.S. 382, 384 (1952). The reverse is also true. Because allocation and apportionment are different ways of doing the same thing — assigning income to jurisdictions — they represent an example of mutual exclusivity or, to borrow a term from logic, exclusive disjunction. Income can be apportioned or it can be allocated but it cannot be fully allocated to a single State while

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STATE TAXATION, PART IV: CORPORATE FRANCHISE, NET INCOME, AND CAPITAL STOCK TAXES ¶ 9.01 (3d ed. 2012).

being apportioned by other States without violating the constitutional protections shielding multistate businesses from "multiple or unfairly apportioned taxation." *MeadWestvaco Corp. v. Illinois Department of Revenue*, 553 U.S. 16, 24 (2008).

The decision of the Alabama courts will exacerbate the risk of multiple taxation as States contort the unitary business principle. States have not infrequently had difficulty applying the unitary business principle consistently, and this case continues the trend. The resulting confusion unnecessarily burdens interstate commerce, robbing multistate taxpayers of the certainty needed to plan and conduct their business affairs and forcing them to engage in prolonged and costly legal battles against state tax administrators thereby imposing an "unreasonable clog upon the mobility of commerce." *See Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 527 (1935).

ARGUMENT

I. BACKGROUND

Kimberly-Clark Corporation ("KC") has long manufactured paper-related consumer products including diapers, paper towels, and toilet paper. In 1962, KC purchased timberland and a pulp mill located in Alabama ("the Coosa Properties") from which it harvested trees and produced pulp used in the manufacture of its products for the next 34 years.

During the 1990s, KC decided to reduce its reliance on self-produced raw materials, and to obtain those raw materials instead from third-party vendors. As part of that strategy, KC sold the Coosa Properties to Alliance Forest Products, Inc. ("Alliance") for $600

million in 1997.[3] Since pulp from the Coosa Properties constituted a majority of KC's pulp production, it entered into a five-year supply contract with Alliance. Pursuing this same strategy, KC sold timberland and pulp manufacturing properties throughout the country during the late 1990s.

Because the assets sold were used continuously in its business for 34 years, KC treated the gain from the sale of the Coosa Properties as unitary business income on its 1997 Alabama corporate income tax return. Accordingly, as with all its unitary business income, KC apportioned the gain to Alabama and other States in which it did business based on its apportionment percentages in those States. After auditing KC's tax return, the Alabama Department of Revenue ("the Department") recharacterized the gain as nonbusiness income from the sale of real property, which under Alabama law is to be allocated in full to Alabama, the State in which the real property is located. Since KC treated the gain as apportionable business income in other States — a treatment endorsed by those States — the Department's assessment subjected KC to multiple taxation on the gain from its sale of the Coosa Properties.

KC challenged the Department's assessment, arguing that under both Alabama law and the Due Process and Commerce Clauses of the U.S. Constitution the gain was apportionable business income. The Alabama administrative law judge ("ALJ") agreed with the first argument, holding that the gain was

[3] As of the date of the sale, the Coosa Properties had been transferred to a wholly-owned second tier subsidiary of KC named Kimberly-Clark Worldwide, Inc. ("KCW") (*i.e.*, KC owned 100 percent of Kimberly-Clark Tissue Company, which in turn owned 100 percent of KCW).

apportionable under Alabama's definitions of business and nonbusiness income, and thus found no need to address KC's constitutional arguments. The Montgomery County Circuit Court reversed the ALJ's decision, finding that the gain from the Coosa Properties sale was nonbusiness income allocable in full to Alabama. The Alabama Court of Civil Appeals reversed, finding that the gain was apportionable. On appeal to the Alabama Supreme Court, that decision was itself reversed with the court determining that the gain constituted nonbusiness income allocable in full to Alabama.

None of the opinions, however, addressed the merits of KC's constitutional arguments, but rather focused on the character of the gain from the Coosa Properties sale under Alabama's statutory definitions of business and nonbusiness income. Accordingly, KC petitioned the Alabama Supreme Court for a rehearing, requesting that the court review those constitutional claims. After the court declined to do so, KC filed a motion with the Circuit Court to remand the case to the ALJ for consideration of its constitutional arguments. The Circuit Court denied KC's motion and, on appeal, the Alabama Court of Civil Appeals affirmed, finding that the Alabama Supreme Court's holding on the application of state law definitions obviated the need to address the constitutional arguments since "[t]here is … no constitutional requirement that *nonbusiness* income be apportioned." Pet. App. at 12a.

II. THE DECISION OF THE ALABAMA COURTS IGNORES THE CONSTITUTIONAL REQUIREMENT THAT UNITARY BUSINESS INCOME BE APPORTIONED AMONG THE STATES AND NOT ALLOCATED IN FULL TO ANY STATE

By allocating KC's gain on the sale of the Coosa Properties fully to the State of Alabama, the Alabama Department of Revenue ignored the limits imposed by the Due Process and Commerce Clauses on States' ability to tax multistate businesses. U.S. Const. art. I, § 8, cl. 3; U.S. Const. amend. XIV, § 1. Nearly 150 years ago, as railroads crisscrossed the national landscape, States grappled with the intricacies of taxing these first multistate businesses. Rather than imposing their property taxes on the value of the iron and timbers physically located within their borders, the States moved toward valuing the entire business enterprise and devised a system for apportioning that value among the various States based on factors such as the ratio of miles of track in the State to the miles of track everywhere. In *State R.R. Tax Cases*, 92 U.S. 575 (1875), the Court affirmed the use of this "unit rule" (or the unitary business principle) under which railroads could be taxed on the apportioned value of their property nationwide that was used in their unitary businesses.

The Court reasoned that the taxpayer's "unitary" property in each State contributed to and enhanced the value of the property of the whole enterprise. As the Court explained in *Adams Express Co. v. Ohio State Auditor*, 165 U.S. 194, 222 (1897), "while the unity which exists may not be a physical unity, it is something more than a mere unity of ownership. It is a unity of the use, not simply for the convenience

or pecuniary profit of the owner, but existing in the very necessities of the case — resulting from the very nature of the business."

This approach in these early unitary cases shifted —

> the constitutional inquiry from the niceties of geographic accounting to the determination of the taxpayer's business unit. If the value the State wished to tax derived from a "unitary business" operated within and without the State, the State could tax an apportioned share of the value of that business instead of isolating and taxing the value of only the property physically present in the State. Conversely, if the value the State wished to tax derived from a "discrete business enterprise," then the State could not tax even an apportioned share of that value.

MeadWestvaco Corp. v. Illinois Department of Revenue, 553 U.S. 16, 26 (2008) (citations and internal quotations omitted).

Eighty-three years later, in *Mobil Oil Corp. v. Commissioner of Taxes*, 445 U.S. 425 (1980), the Court encapsulated its prior holdings by declaring that "the linchpin of apportionability in the field of state income taxation is the unitary-business principle," *id.* at 439, and describing a unitary business as one marked by "functional integration, centralization of management, and economies of scale." *Id.* at 438.[4]

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[4] The unitary business principle holds that the local tax base is calculated by first defining the scope of the unitary business of which the taxed enterprise's activities in the taxing jurisdiction form one part, and then apportioning the total income of the unitary business between the taxing jurisdiction and the rest of the world based on a formula "taking into account

In *Allied Signal, Inc. v. Director, Division of Taxation*, 504 U.S. 768, 780 (1992), the Court explained that the "unitary business rule is a recognition of two imperatives: the States' wide authority to devise formulae for an accurate assessment of a corporation's intrastate value or income; and the necessary limit on the States' authority to tax value or income that cannot in fairness be attributed to the taxpayer's activities within the State."

In *MeadWestvaco*, the Court observed, "[a]s the unitary business principle has evolved in step with American enterprise, courts have sometimes found it difficult to identify exactly when a business is unitary." *MeadWestvaco*, 553 U.S. at 27.[5] That is certainly *not* the case here. All parties agree that the Coosa Properties were an integral part of KC's business for decades before it decided to sell them along with a number of other similar properties over the course of a few years. To say that the sale of the Coosa Properties did not give rise to (apportionable)

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objective measures of the corporation's activities within and without the jurisdiction." *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159, 165 (1983).

[5] The Court has commented that dividing income among the several States resembles "slicing a shadow." *Container Corp.*, 463 U.S. at 192. Absolute consistency among taxing authorities "may just be too much to ask," *id.*, but there are constitutional limits on a State's use of an apportionment formula, especially in respect of income derived from multistate commerce. In other words, a balance must be struck between a State's need for revenue and the taxpayer's legitimate right to protection from parochial authorities. *See Boston Stock Exchange v. State Tax Commission*, 429 U.S. 329, 318 (1977) (the Court has a duty "to make the delicate adjustment between the national interest in free and open trade and the legitimate interest of the individual States in exercising their taxing powers").

business income of a unitary enterprise would be as wrong as for a railroad in the late 1800s to argue that gain from the sale of the tracks used to transport its rail cars did not relate to its unitary business.

Allocation and apportionment of the same income violates the Commerce Clause because it discriminates against interstate commerce by subjecting activities to multiple and unfairly apportioned taxation. *MeadWestvaco Corp.,* 553 U.S. at 24, *citing Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159, 170-71 (1983); *Armco, Inc. v. Hardesty*, 467 U.S. 638, 644 (1984). "Taxation by apportionment and taxation by allocation to a single situs are theoretically incommensurate, and if the latter method is constitutionally preferred, a tax based on the former cannot be sustained." *Mobil*, 445 U.S. at 444-45, *citing Standard Oil v. Peck*, 342 U.S. 382, 384 (1952). In other words, because allocation and apportionment are different ways of doing the same thing — assigning income to jurisdictions — they represent an example of mutual exclusivity or, to borrow a term from logic, exclusive disjunction. Income can be apportioned or it can be allocated but it cannot simultaneously be fully allocated to a single State and apportioned by other States.

Alabama's debasement of the unitary business principle would convert the potential for duplicative taxation into reality. Letting the decision below stand would vitiate the unitary business principle, allowing States to expand or contract the definition at will in order to subject multistate businesses to multiple taxation on income from any substantial transaction.[6] Indeed, there is no normative basis for

[6] The Chief Justice of the Alabama Supreme Court recognized this effect in her dissent stating "that the majority opinion will

sanctioning the allocation and apportionment (or, indeed, the multiple allocation) of the same income. *Mobil*, 445 U.S. at 444-45.

The decision of the Alabama courts will exacerbate the existing risk of multiple taxation as States contort the unitary business principle in the absence of clear guidance. States have frequently had difficulty applying the unitary business principle, and the decision of the Alabama courts continues that trend. The resulting confusion unnecessarily burdens interstate commerce by forcing multistate taxpayers to not only cope with complex state corporate income and franchise tax law but also to engage in prolonged and costly legal battles against state tax administrators thereby imposing an "unreasonable clog upon the mobility of commerce." *Baldwin v. G.A.F. Seelig, Inc.*, 294 U.S. 511, 527 (1935).

Alabama should not be permitted to ignore the constraints of the Due Process and Commerce Clauses by eschewing the unitary business rule and allocating income to itself that was clearly earned as part of KC's unitary business.

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probably result in more revenue for the State of Alabama," and that the taxpayers "have already paid the corporate tax attributable to the income from the sale of these assets to the other states in which they do business, and this decision will thus result in a double payment." Pet. App. 36a.

CONCLUSION

For the foregoing reasons, the Court should grant the petition for a writ of certiorari and reverse the decision below.

Respectfully submitted,

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