Summary of SC93162, *MINACT Inc. v. Director of Revenue*
On review from the administrative hearing commission, Commissioner Sreenivasa Rao Dandamudi
Argued and submitted November 14, 2013; opinion issued April 15, 2014

Attorneys: The director was represented by Solicitor General James R. Layton and Deputy Solicitor General Jeremiah J. Morgan of the attorney general's office in Jefferson City, (573) 751-3321; and MINACT was represented by James W. Erwin and Janette M. Lohman of Thompson Coburn LLP in St. Louis, (314) 552-6000.

Overview: The director of revenue seeks review of an administrative hearing commission decision determining that the income from a trust established by an out-of-state company with operations in Missouri to fund a deferred-compensation plan is "non-business income" that is not subject to taxation in Missouri. In a unanimous decision written by Judge Richard B. Teitelman, the Supreme Court of Missouri reverses the decision and remands (sends back) the case. The trust income meets the test for "business income" subject to taxation in Missouri because company established the trust for the current operational purpose of attracting and retaining key employees to sustain its current business operations.

Facts: MINACT Inc. is a Mississippi corporation with operations in several states, including Missouri. It manages job corps centers pursuant to its contract with the federal government. In 1988, it established a "non-qualified" federal deferred-compensation plan under which all income from plan investments is part of MINACT's taxable income, and the company does not receive a deduction for its contributions to the plan. In 1994, MINACT established a "rabbi trust" to fund the plan and meet its future liabilities to plan participants. To qualify as a rabbi trust, the employer must be the grantor of a trust used to fund a non-qualified deferred-compensation plan and must report the trust's earnings as income on the employer's federal income tax return. Trust assets and income only can be used to pay benefits owed to employees under the deferred-compensation plan. In its 2007 Missouri corporate income-tax return, MINACT reported nearly $668,000 in "non-business" income, about $455,500 of which was income from the rabbi trust. MINACT reported and allocated all trust income to Mississippi maintaining that all its trust income was non-business income not subject to apportionment and Missouri taxation. The Missouri director of revenue determined the trust income was business income subject to apportionment and taxation in Missouri. MINACT sought review in the administrative hearing commission, which determined the trust income was non-business income. The director seeks review.

REVERSED AND REMANDED.

Court en banc holds: Because the trust income is "business income" used for the current operational purpose of attracting and retaining key employees, it is subject to apportionment in Missouri. A taxpayer such as MINACT with tax liabilities in multiple states must apportion “business income” to the various states in which it conducts business, while “non-business income” is paid to the state in which the taxpayer resides. Under sections 32.200 through 32.240, RSMo, business income is apportioned to Missouri using a formula calculating the percentage of a company’s income attributable to Missouri based on the company’s property, personnel and sales in Missouri. One of the tests Missouri uses to determine whether income is business or non-business is the “functional test,” which determines whether a gain is attributable to an activity – namely, the acquisition, management and disposition of property – that constitutes an integral part of the taxpayer’s regular business. Because the trust income satisfies this functional test, it is “business income.” MINACT did not establish the plan and trust for an altruistic or non-business purpose, and the trust income is not a passive investment that serves no present, integral operational purpose. Rather, MINACT created the trust specifically to provide a retirement incentive to attract and retain key employees to sustain its current business operations.