IN THE
SUPREME COURT
STATE OF MISSOURI

No. 85180

Tubular Steel Industries, Inc.,
Appellant,

v.

DIRECTOR OF REVENUE, STATE OF MISSOURI,
Respondent.

ON PETITION FOR REVIEW
FROM THE MISSOURI ADMINISTRATIVE HEARING COMMISSION
THE HONORABLE KAREN A. WINN, COMMISSIONER

BRIEF FOR RESPONDENT

JEREMIAH W. (JAY) NIXON
Attorney General

VICTORINE R. MAHON
Assistant Attorney General
Missouri Bar No. 32202
Broadway State Office Building
221 West High Street, 8th Floor
Post Office Box 899
Jefferson City, Missouri 65102
(573) 751-0330 Telephone

(573) 751-8796 Facsimile

ATTORNEYS FOR RESPONDENT
DIRECTOR OF REVENUE

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STATEMENT OF FACTS

A. Tubular Steel Industries, Inc., and its operations

The facts in this case were submitted by a joint stipulation (L.F. 12).[1] Tubular Steel, Inc., is an operating company in business as a distributor of steel tubing (L.F. 13). It is owned 100 percent by the Appellant in this case - Tubular Steel Industries, Inc. (Tubular) (L.F. 13). Tubular, in turn, is owned by TSI Holding Company (TSI Holding), which is an appellant in a related appeal *TSI Holding Co. v. Director of Revenue*, No. 85179 (L.F. 13). Tubular is a Missouri corporation that operates solely as an investment-holding company (L.F. 13). All of Tubular's assets are cash and investments in subsidiaries, municipal bonds, mutual funds, and real estate (L.F. 13). Tubular has investments in Missouri (L.F. 13). Tubular also has invested in entities that are not located in Missouri, have no assets in Missouri, and do no business here (L.F. 13).

B. Tubular's 1993 and 1994 Missouri franchise tax return

Tubular has never filed a franchise tax return in any state other than Missouri (L.F. 13). On its original Missouri franchise tax returns for 1993 and 1994, Tubular reported its assets as being employed entirely in Missouri (L.F. 13). Tubular filed amended returns for those years on or about December 16, 1994, because Tubular's accountants determined that

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[1] While the facts generally are not in dispute, the page numbers used by Tubular to reference the record do not correspond with the page numbers of the Legal File on file with the Missouri Supreme Court.

the asset allocation formula on the Missouri franchise tax return form did not, in their opinion, fairly allocate Tubular's assets (L.F. 13).

On its amended returns, Tubular apportioned all of its assets with the exception of its investments in subsidiaries; those investments were not included in either the numerator or the denominator (L.F. 13). In the numerator, Tubular included its cash and inter-company dividend receivables as being in Missouri (L.F. 13-14). In the denominator, Tubular listed all of its assets, except for its investments in subsidiaries, which were not included in either the numerator or denominator (L.F. 13-14). Tubular computed Missouri apportionment percentages as 29.2738 percent for 1993 and 33.6515 percent for 1994 (L.F. 14; Stip. Ex. A - L.F. 20).

The Secretary of State rejected the amended returns, precipitating a phone call on January 17, 1995, between the Secretary of State's Assistant General Counsel and Tubular's accountant (L.F. 14). The Assistant General Counsel agreed to review the matter and said he would confer with someone else at the Secretary of State's Office and return a call to the accountant (L.F. 14). On January 4, 1996, the Secretary of State issued Missouri franchise tax refunds to Tubular in the amounts reflected on Tubular's amended Missouri franchise tax returns for 1993 - 1994 (L.F. 15).

On its amended returns, Tubular apportioned its assets by including in the numerator all assets, in which Tubular invested, that were located in Missouri, had assets in Missouri, or did business in Missouri and included in the denominator all assets (L.F. 12). Tubular added to the numerator its cash and inter-company dividend receivables (L.F. 12-13). For

example, with respect to investments in municipal bonds for non-Missouri municipalities, Tubular included such investments in the denominator, but not in the numerator (L.F. 13). Tubular did not include its investments in affiliated companies in calculating its apportionment percentages; those investments were neither in the numerator nor the denominator (L.F. 13).

C. Tubular's 1995 Missouri franchise tax return

On or about April 11, 1995, Tubular filed its 1995 franchise tax return using the same allocation methodology used in the amended 1993 and 1994 returns, demonstrating a Missouri apportionment percentage of 45.7275 percent (L.F. 15). The Secretary of State accepted that return as filed (L.F. 15).

D. Tubular's 1996 - 2000 Missouri franchise tax returns

Tubular filed Missouri franchise tax returns for 1996 through 2000 using the allocation of assets methodology that Tubular used on its amended Missouri franchise tax returned for 1993 - 1994 (L.F. 15). Tubular reported apportionment percentages of 35.0803 percent for 1996 (L.F. 85); 43.3025 percent for 1997 (L.F. 87); and 18.918 percent for 1998 (L.F. 89). The Secretary of State did not accept Tubular's apportionment of assets and on September 13, 1999, the Secretary of State mailed an assessment notice to Tubular, reporting a total amount due of $6,374.93, including the following:

Tax year	Additional Tax	Interest	Penalty	Amount Due
1996	$1,133.44	$335.23	$283.36	$1,752.03

1997	$1,122.35	$234.36	$497.50	$1,854.30
1998	$1,930.58	$243.12	$594.90	$2,768.60

(Stip. Ex. 0 - L.F. 138). Tubular protested the assessment by letter dated October 6, 1999 (L.F. 16).

On May 11, 2000, the Director of Revenue rejected and returned Tubular's 2000 Missouri franchise tax return (L.F. 16). The explanation on the notice states: "Alternative method of apportionment as accepted by the office of the secretary of state for years 1993, 1994, & 1995. Years 1996 through 1998 are currently being reviewed by the General Counsel's office." (L.F. 16; Stip. Ex. Q - L.F. 140). A second rejection notice dated June 5, 2000, instructed: "Please resubmit original documents with copy of approval of alternative method." (L.F. 17; Stip. Ex. Q - L.F. 140).

On October 12, 2001, the Director issued her final decision, upholding the assessment but abating the penalties (L.F. 17; Stip. Ex. S - L.F. 144 - 149). Tubular thereafter filed its petition for a review by the AHC (Stip. Ex. T - L.F. 150).

E. Administration of the Missouri franchise tax

Prior to January 1, 2000, the Missouri franchise tax was administered by the Secretary of State (L.F. 17). Effective January 1, 2000, the Director of Revenue was charged with administering the Missouri franchise tax (L.F. 17).

On August 28, 1995, the Secretary of State promulgated Regulation 15 CSR 30-150.170 with an effective date of March 30, 1996 (L.F. 18; Stip. Ex. X - L.F. 158). The Secretary of State amended on October 21, 1998, Regulation 15 CSR 30-150.170

effective April 30, 1999 (L.F. 18). The amended version became Regulation 12 CSR 10-9.200 on January 1, 2000 (L.F. 18; Stip. Ex. Y - L.F. 160).

Neither the Director nor the Secretary of State has published any documents, other than Regulation 12 CSR 10-9.200, setting forth a requirement that a taxpayer receive written approval of the Director or Revenue or the Secretary of State prior to using an alternate method for apportioning assets for Missouri franchise tax purposes (L.F. 18). Neither the Director of Revenue nor the Secretary of State has published any documents referencing any standards by which a taxpayer may receive written approval from the Director or the Secretary of State to utilize an alternate method of apportionment of assets for Missouri franchise tax purpose (L.F. 18). The Director of Revenue and the Secretary of State, respectively, have published instructions to assist taxpayers in completing Missouri franchise tax returns (L.F. 18 - 19). The instructions (Stip. Ex. AA) are located in the Legal File, starting at page 162.

When the Secretary of State administered the Missouri franchise tax, the Secretary of State generally accepted Missouri franchise tax returns using alternate methods of apportionment evidenced by a written approval letter, unless and until such alternate methods were reviewed by a staff attorney and revoked by the Secretary of State at the attorney's suggestion (L.F. 19). During the period in which the Director of Revenue administered the Missouri franchise tax, the Director disregarded any agreements in prior tax years in determining whether an alternate method of apportionment is acceptable for subsequent tax years (L.F. 19).

F. The Administrative Hearing Commission's decision

On March 3, 2003, the AHC entered its decision (L.F. 174). The AHC ruled that Tubular was liable for Missouri franchise tax for years 1996 - 1998 as the Director of Revenue had assessed, that it was not entitled to use an alternate method of apportionment, and that it had not obtained written approval for an alternate method of apportionment (L.F. 174 - 189). The AHC reasoned:

> " The intent of Section 147.010 is only to apply to situations in which a corporation does business in more than any other state.
>
> " Tubular does not conduct business in any other state.
>
> " Even if the Secretary of State had provided approval for an alternate apportionment method for 1993 and 1994, Tubular has nothing to show that it had approval for the years at issue.

(AHC Decision 174-189, 12-13, 17). Tubular thereafter filed its appeal to this Court.

STANDARD OF REVIEW

In reviewing the decision of the Administrative Hearing Commission (AHC) which upheld the Director's assessment, this Court's interpretation of the revenue laws is de novo. *Southwestern Bell Yellow Pages v. Director of Revenue,* 94 S.W.3d 388, 390 (Mo. banc 2002). The Court will uphold the AHC's decision if authorized by law and supported by competent and substantial evidence upon the whole record. *Id*. (citing § 621.193, RSMo; *Southwestern Bell Telephone Co. v. Director of Revenue,* 78 S.W.3d 763, 765 (Mo. banc 2002) (citations omitted)).

POINT I

FRANCHISE TAX MEASURED BY TUBULAR'S INVESTMENTS OUTSIDE MISSOURI

A. Section 147.010, RSMo, does not require Tubular to apportion its Missouri franchise tax base.

The Missouri General Assembly enacted a franchise tax that not only imposes an excise on the privilege of doing business in Missouri, *see State ex rel. Marquette Hotel Investment Co. v. State Tax Commission,* 282 Mo. 213, 221 S.W. 721, 722 (Mo. banc 1920), but provides a corporate entity with the opportunity to apportion its franchise tax base if "it *employs* a part of its outstanding shares in business in another state or country." § 147.010.1[2] (emphasis added). In such case, the corporation "shall be deemed to have employed in this state that proportion of its entire outstanding shares and surplus that its property and assets employed in this state bears to all its property and assets wherever located."

§ 147.010.1, RSMo While the phrase "employs a part of its outstanding shares in business in another state or county" is not clearly defined in statute or case law, certainly the phrase means something more than merely owning securities in an out-of- state entity. If it means something more than that, then Tubular is not entitled to apportion its franchise tax base under § 147.010.1, RSMo.

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[2] Unless otherwise noted, references are to Revised Statutes of Missouri 1994; however, § 147.010, RSMo 2000, also is included in the Respondent's Appendix.

A cardinal rule of statutory construction is to ascertain the intent of the lawmakers and to give effect to that intent. *Cub Cadet Corp. v. Mopec, Inc.*, 78 S.W.3d 205 (Mo.App., W.D. 2002). Legislative intent and the meaning of words used in the statute may be derived from the general purposes of the legislative enactment. *Id.* As stipulated by the parties, Tubular is in the business of holding investments, including mutual funds and municipal bonds. The business of the corporation is managed, directed and controlled from within the State of Missouri. Tubular has no tangible assets outside our state. Tubular does not operate the type of business or the municipality in which it invests. Yet that is what Tubular insists Missouri's law allows. In short, Tubular "employs" all its outstanding shares and surplus in Missouri because its business operations are exclusively in Missouri. All of Tubular's intangible assets, such as minority shares of stocks and municipal bonds, wherever located, bear a direct relationship to its business operations here in Missouri.

If a franchise tax is truly a tax for the privilege of doing business in Missouri, *State ex rel. Marquette Hotel Investment Co. v. State Tax Commission*, then the intent of the legislature is effectuated if the measurement of the tax includes all property that has a relationship to the privilege granted. Tubular's power to act as an investment-holding company is authorized by the State of Missouri. It would make no sense to grant a domestic investment-holding corporation the privilege of operating its business in Missouri, granting the corporation the protections of this state, and then allow the same company to exploit that privilege and avoid its franchise tax simply by limiting its investments to out-of-state stocks and bonds.

Tubular's interpretation of the § 147.010.1 would render parts of the statute meaningless. For instance, the statute directs a corporation to calculate its apportionment percentage for the purpose of Chapter 147, RSMo, as follows:

> [S]uch corporation shall be deemed to have employed in this state that proportion of its entire outstanding shares and surplus that its property and assets *employed* in this state bears to all of its property and assets wherever located.

§ 147.010.1, (emphasis added). To interpret the statute in the fashion proposed by Tubular, the word "employed," as italicized above, simply would have no importance or meaning. Another rule of statutory construction, however, is that a "statute must be harmonized and every word, clause, sentence, and section thereof must be given some meaning." *Sermchief v. Gonzales*, 660 S.W.2d 683, 688-89 (Mo. banc 1983).

Reading each of the words in § 147.010.1, as having some meaning, the apportionment of Tubular's out-of-state investments from the company's Missouri franchise tax base is unauthorized because all of Tubular's assets are investments that are "employed" here. The imposition of the franchise tax based on all of Tubular's holdings is appropriate because all of its securities holdings have a fair relationship to the value of the franchise enjoyed by Tubular in this State. The stocks and bonds are the very essence of its business and naturally form a part of Tubular's capital that is used and employed in Missouri.

B. *Union Electric Co. v. Morris*, 222 S.W.2d 767 (Mo. 1949), does not authorize the taxpayer to apportion out its investments in foreign entities.

Contrary to Tubular's contention, this case is not factually on point with *Union Electric Co. v. Morris*, 222 S.W.2d 767 (Mo. 1949). Indeed, it the factual distinctions between this case and *Union Electric*, which demonstrate that the decision of the AHC was correct and should be affirmed.

Union Electric, a Missouri utility company, held 100 percent of the stock in two Illinois utility corporations. The wholly owned foreign subsidiaries did no business in Missouri and owned no assets in this state. This Court concluded that Union Electric's stock in the subsidiaries could be excluded from its Missouri franchise tax base because the subsidiaries were not used in business in Missouri and were not a part of the parent corporation's "property and assets in this state." 222 S.W.2d at 772. The holding in *Union Electric*, advances the purpose of a franchise tax, which is designed to tax only the right of a corporation to do business in Missouri, as opposed to some other state. *See State ex rel. Marquette Hotel Investment Co. v. State Tax Commission*, 221 S.W. at 722.

Union Electric, however, does not stand for the proposition that all investments in all foreign corporations are to be excluded from a domestic corporation's Missouri franchise tax base. This Court considered, but specifically rejected such bright-line rule, noting that the words used in the franchise tax statute "cannot be determined independent of the particular context in which they are used and the subject matter under discussion." 222 S.W.2d at 770. While this Court determined within the context of *Union Electric* that the

Missouri utility's shares of stock in its two wholly owned foreign subsidiaries were not employed in business in this state, the Court recognized that this may not be the appropriate holding in every case of foreign investment. As the Court specifically commented, "There is no suggestion that the shares of stock in question were used in respondent's Director's business, or that it was in the business of buying or selling stocks." 222 S.W.2d at 770. The clear inference is that if Union Electric was an investment-holding company, such as Tubular, it would not have been allowed to apportion out its investments in foreign corporations.

C. No double taxation

The Director also vigorously disputes Tubular's assertion that the Director's construction of § 147.010, RSMo, will result in multiple taxation of the same assets and that this is not what the legislature could have intended (Appellant's brief 19-20). First, there is no evidence in the stipulated record that the mutual funds or municipalities in which Tubular invests are subject to franchise taxation in the other states. It is unlikely that any jurisdiction imposes franchise tax on a municipality, and at least a part of Tubular's investments are in municipal bonds (L.F. 12). In Missouri, there are several classes of corporation that are exempt from franchise tax, including not-for-profit corporations. § 147.010.2. The parties' stipulated facts clearly indicate, however, that Tubular pays no franchise tax in any other state (L.F. 12). So there certainly is no double taxation as to Tubular.

Second, "[t]he [franchise] tax is not a property tax, but an excise levied upon the privilege of transacting business in this state as a corporation." *Missouri Athletic Ass'n v. Delk, Inv. Corp.*, 20 S.W.2d 51, 55 (Mo. 1929). The tax is on the privilege for the amount of business a corporation conducts within the state. *Id.* One measure of determining the amount of franchise tax, thus attempting by formula to arrive at a reasonable approximation of the value of the business done in Missouri, is to consider a company's assets and property employed within the state. But not every jurisdiction imposes its franchise tax in such manner. Some states determine the amount of franchise tax to be paid by a corporate entity through its earnings. *For example, in Education Films Corp. v. Ward,* 282 U.S. 379, 51 S.Ct. 170, 75 L.Ed 400 (1931), the United States Supreme Court considered and rejected a challenge to the validity of a New York franchise tax statute that measured the tax according to income, including income earned from tax-exempt federal bonds.[3] Due to

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[3] Tubular cites *Boatmen's Bancshares, Inc. v. Director of Revenue,* 757 S.W.2d 574, 576 (Mo. banc 1988), as support for its argument that the AHC's decision in the instant case will result in double taxation since in Missouri, each subsidiary pays its own franchise tax based upon the par value of its outstanding stock and surplus and thus, is taxed on investments in and advances to it by the parent (Appellant's brief 7). As this Court specifically noted, however, in other jurisdictions, such as Texas, a corporation's surplus includes investments in its subsidiaries. Thus, *Boatmen's Bancshares, Inc.*, only highlights the jurisdictional differences in franchise taxation.

the diversity in state franchise tax schemes, one cannot legitimately assert that Missouri's consideration of out-of-state investments in measuring the amount of franchise tax due, will result in any double taxation on any investment.

D. The Commission's Decision

1. Interstate offices and franchise tax returns

Some of the rationales cited by the AHC for upholding the Director's franchise tax assessment against Tubular was the corporation's lack of physical office outside Missouri and the fact that Tubular files no franchise tax returns in any other state (L.F. 174-189). Tubular contends that these two factors are irrelevant, noting that there is no statutory requirement that such facts be demonstrated as a precursor to franchise tax apportionment (Appellant's brief 21). The Director agrees that there is no such statutory requirement, and the AHC did not suggest that such facts must be demonstrated before a corporation may apportion its franchise tax base under § 147.010. But that does not mean such facts are irrelevant. Tubular's lack of offices and franchise tax liability in other states is evidence that supports the finding that it performs no business activity in other states and therefore *employs* all of its outstanding shares and surplus in Missouri.

2. Municipal bonds

The AHC held that Tubular's investments in municipal bonds in out-of-state municipalities did not entitle Tubular to apportion its franchise tax base because Tubular made its investment while in Missouri and received its return in Missouri (L.F. 120-21). Tubular contends that this holding of the AHC is contrary to *Household Finance*

Corporation v. Robertson, 364 S.W.2d 595 (Mo. banc 1963)(Appellant's brief 25). But Tubular misunderstands that decision.

Household Finance Corp., involved a Delaware company with its principal place of business in Chicago. The company owned a number of subsidiaries doing business in Missouri, which were in the business of loaning money. This Court determined that the foreign parent corporation's investments and cash advances to its Missouri subsidiaries were not the parent's "property and assets [employed] in this state" but were the assets of its subsidiaries. 364 S.W.2d at 607. This was the converse of the situation in *Union Electric Co.,* in which the stock of two foreign subsidiaries owned by a Missouri parent corporation was held not to be a part of the parent corporation's "property and assets in this state." 222 S.W.2d at 772. While at first blush, *Household Finance Corp.,* might appear to support Tubular's position, a thorough review of this Court's rationale, and its discussion of the earlier *Union Electric* case, supports the Director's position and the AHC's decision that the municipal bonds should not be apportioned out of Tubular's franchise tax base.

In *Household Finance,* this Court turned to the word -"employed"- that Tubular wants to eliminate:

> Considering the Union Electric opinion in its entirety, we understand it to declare that the physical property of the Illinois corporations was not located in this state and neither was it employed by Union Electric in its business; and neither was it property and assets of Union Electric *in this state for the purpose contemplated in § 147.010*....[W]e do not understand it to hold, as

> plaintiff contends, that if the physical property were in fact employed in Union Electric's business in Missouri, it nevertheless should not be included in computing Union Electric's franchise tax on grounds that the situs of the physical assets represented by the shares of stock was not also in Missouri. Rather do we understand the opinion to hold that the franchise tax imposed under § 147.010 is to be measured by and computed upon the value of its *property and assets employed in business in this state.*

Household Finance Corp., 364 S.W.2d at 602 (emphasis in the original). It makes no difference that municipal bonds (or the mutual funds) might be an investment in an out-of-state entity. The situs of the security is not controlling. Rather, it is the value of the property and assets employed by Tubular's business in Missouri that are in issue. Tubular's business is located solely in Missouri. The investments are made from Missouri. Tubular operates in Missouri. The municipal bonds, irrespective of their location, are still employed in Tubular's business in this state and are properly included in evaluating Tubular's Missouri franchise tax base.

3. Investments in mutual funds

Tubular next argues that the AHC erred in distinguishing *Union Electric* on the basis that it involved wholly owned subsidiaries (Appellant's brief 23-24). Tubular contends that nothing in *Union Electric Co.,* or in § 147.010, indicate that the percentage of ownership in another business entity is determinative (Appellant's brief 23-24). The fallacy of this argument is that by the AHC did not rule that the percentage of ownership

was a *determinative* factor. Rather, the AHC found that Union Electric, as a parent company, had "a degree of control over those subsidiaries such that the court regarded it as employing a portion of its own outstanding shares in business in another state." (AHC decision at decision page 11). Tubular can hardly claim a substantial degree of control over an out-of-state municipality or the corporations in which it invests through a mutual fund.

In any event, the percentage of ownership issue is red herring. Regulations in effect during the pendency of this dispute allow a parent corporation to deduct from its tax base on line 2b of the franchise tax form, that portion of the corporation's surplus invested or advanced to a subsidiary corporation, provided the parent owns at least 50 percent of the voting stock. 12 CSR 10-9.200(1)(C), 2000 (formerly 15 CSR 30-150.170, 1996, and as amended 1999). If Tubular had owned at least 50 percent of the voting stock in all of the out-of-state corporations in which it invests, this case would not be before the Supreme Court of Missouri today. The issue, therefore, is not and never has been the *percentage* of the stock Tubular owns in an out-of-state corporation. If the shares of stock owned in an out-of-state corporation are *employed* in connection with Tubular's investment-holding business in this state, then Tubular's franchise tax base should include such securities. On the facts of this case, it cannot be said that Tubular has *employed* its outstanding shares in business outside of Missouri.

POINT II

SECRETARY OF STATE'S ALLEGED APPROVAL

A. The Director's regulation is fair.

Tubular next addresses (Appellant's brief 27) whether in apportioning its franchise tax base it is required to follow the formula set forth in state regulations - 15 CSR 30-150.170 (now 12 CSR 10-9.200) - or whether it may use an alternate formula. Tubular contends that it must be allowed to apportion by an alternate method because the Secretary of State's Office had approved such method, the approval was withdrawn only after Tubular filed its franchise tax returns for the relevant tax periods, and neither the Director nor the AHC questioned the fairness, accuracy, or precision of the alternate methodology (Appellant's brief 27). This all assumes, of course, that Tubular is even allowed to apportion its franchise tax base, a point that the Director does not concede.

Whenever a corporation of sufficient worth operates in more than one state and employs a part of its outstanding shares and assets in another state or country, § 147.010, requires the corporation to pay its annual franchise tax based on the outstanding shares and surplus that <u>are</u> employed in this state. To assist a corporation in calculating the apportionment percentage for its franchise tax base, the Department of Revenue promulgated 12 CSR 10-9.200 (previously 15 CSR 30-150.170). The corporation is directed to calculate the value of all inventory, land, and fixed assets located in Missouri, together with the accounts receivable that are attributable to Missouri, and divide that

amount by all inventory, land, fixed assets and accounts receivable, wherever located. 12 CSR 10-9.200(2)(E).

If a corporation has no land, fixed assets, accounts receivables, or inventory, the normal apportionment calculation will result in a zero figure. Thus, the company assets are not apportioned and its Missouri franchise tax is based on all of its assets, except those that might be advanced to its subsidiaries. 12 CSR 10-9.200(2)(E) While Tubular baldly asserts that this result is "not fair, accurate or precise" (Appellant's brief 26), it is the same apportionment method described in *Household Finance Corp.*

In *Household Finance Corp.,* the State Tax Commission computed additional tax based on an additional $6,150,993.02 in Missouri assets it found due to these three adjustments: (1) Missouri cash was increased from $111,017.16 to $1,138,879; (2) the taxpayer's $560,000 investment in its subsidiaries operating in Missouri was added to Missouri assets; and (3) the taxpayer's advances of $4,563,132 to the same subsidiaries were added to Missouri assets. 364 S.W.2d at 598-99. The State Tax Commission recomputed the Missouri cash for 1959 by multiplying the taxpayer's total cash of $26,602,884.74 by 0.042812. This percentage was the ratio of Missouri loans receivable and tangible assets to total loans receivable and tangible assets. 364 S.W.2d at 598. This Court held that the cash employed by the taxpayer in its business in this state, irrespective of its location, must be included in determining the amount of franchise tax owed. 364 S.W.2d at 603. But the Court also upheld the apportionment method used by the State Tax Commission. *Id.* Consequently, the apportionment percentage was computed based on

assets other than cash (loans receivable and tangible assets). This Court had the opportunity, but did not express dissatisfaction with this method of computing the apportionment ratio.

The rationale for excluding cash from the computation of the apportionment ratio in *Household Finance Corp.*, was that its location did not accurately reflect the taxpayer's business and could easily be manipulated:

> For example, can the statute mean that either a domestic or foreign corporation engaged in the business of making loans in St. Louis, Missouri, may avoid payment of a portion of the franchise tax imposed under § 147.010 merely by keeping the cash thus employed by it in East St. Louis, Illinois, and drawing thereon as its Missouri commitments required? We think it can not. We hold that the corporation franchise tax imposed under § 147.010 requires that the cash employed by plaintiff in business in this state, irrespective of its location, shall be included in computing the amount of the tax annually accruing under § 147.010.

364 S.W.2d at 603. Similarly, the location of Tubular's investments, like the location of cash in *Household Finance Corp.*, is not determinative of where Tubular is engaged in business and it is not unfair, inaccurate or imprecise to exclude investments, such as Tubular's investments in out-of-state entities, from the calculation of an apportionment ratio.

Tubular erroneously describes the Commission's decision and the Director's position as simply being: "all assets are includable in the tax base unless a taxpayer has certain types of assets [accounts receivable, inventories or land and fixed assets]." (Appellant's brief 28). It also paints its own argument with a broad stroke, posturing that its alternate method of computing an apportionment ratio fairly reflects the proportion of the taxpayer's outstanding shares and surplus that its property and assets employed in this state bears to all of its property and assets wherever located (Appellant's brief 28). Neither statement is correct.

The Commission's decision and the Director's position are not so inflexible as to close the door in every instance to the use of an alternate method for computing the apportionment ratio. The alternate method is available in the appropriate circumstances. As was required by 15 CSR 30-150.170(2)(E)4, 1996 (Stip. Ex. Q), and is now required by 12 CSR 10-9.200, 2000 (Stip. Ex. R), a corporation must demonstrate "good cause" and obtain approval from the Secretary of State to use the alternate method of computation. Such good cause has not been demonstrated here because Tubular does not "employ" any part of its outstanding shares in business in another state or country, as is required by § 147.010. Rather, all of its outstanding shares are employed here in Missouri because all of Tubular's business activities are centered in this state.

What distinguishes this case from *Union Electric Co.,* is the very nature of the Tubular's business. The inter-relationship between the out-of-state and in-state activities is a critical factor. In *Union Electric Co.,* a multi-state business enterprise was conducted in

a way that some of its business operations outside Missouri were wholly independent of and did not contribute to the business operations within this state. On such facts, it is "fair" to exclude such outside activity from Missouri franchise tax because the functions between the parent company and its subsidiaries are independent. Tubular's investments in out-of-state business entities, however, are intertwined with its business as a Missouri investment-holding company and these investments contribute markedly to the value of the business transacted in Missouri and the privilege granted. On these facts, it cannot be said that Tubular "employs" its stock and surplus anywhere except in Missouri.

B. The Secretary of State did not approve the alternate method of computing the apportionment ratio for the tax years in issue.

Regulation 15 CSR 30-150.170(E), effective March 20, 1996, provided that a corporation having assets employed both within and without Missouri may calculate the apportionment ratio by using lines 3a through 3d and line 4 of the franchise tax form. This regulation and the franchise tax form provided for the apportionment ratio to be calculated based on inventories, land, fixed assets, and accounts receivables; but not other intangible assets. Other intangibles are not included in either the numerator or the denominator in determining the appropriate apportionment ratio. The regulation further provided, however, that a corporation may seek approval from the Secretary of State to use an alternate method of apportionment for good cause:

> A corporation may, upon approval by the secretary of state and for good cause shown, use an alternate method of apportionment that fairly reflects

> the "proportion of its entire outstanding shares and surplus that its property and assets employed in this state bears to all of its property and assets wherever located" (Section 147.010, RSMo).

15 CSR 30-150.170(E), effective March 30, 1996.

Tubular contends that in accordance with this regulation it obtained prior approval from the Secretary of State to use such an alternate method of apportionment for 1996 through 1998 (Appellant's brief 30). Tubular asserts that the Secretary of State's issuance of franchise tax refunds for 1993 and 1994, and its acceptance of Tubular's 1995 return, constitutes approval (Appellant's brief 30). Tubular avers that each of the returns (1993, 1994 and 1995) used the alternate formula (Appellant's brief 30). Tubular argues that even if the Secretary of State is permitted to withhold its approval in later years, the auditor did not issue his report revoking the apportionment method until May 3, 1999, constituting an attempt to retroactively revoke approval (Appellant's brief 29-30).

Accepting a return with an alternate formula for 1993, 1994 and 1995 does not constitute approval for a future year. In effect, Tubular's argument is that the Director is estopped from collecting taxes that are due because Tubular detrimentally relied on the Secretary of State's past actions or inactions with respect to returns filed in prior years. The doctrine of estoppel generally is not applicable to acts of a governmental body; it is jealously withheld and only sparingly applied against governmental bodies and public officials acting in their official capacity when necessary to prevent manifest injustice. *Contel v. Missouri, Inc v. Director of Revenue*, 863 S.W.2d 928 (Mo.App., W.D. 1993).

Though the result may be harsh, taxpayers have no vested right to rely even upon an erroneous interpretation of a statute exempting them from taxation. *Bartlett & Co. Grain v. Director of Revenue,* 649 S.W.2d 220, 224 (Mo. 1983)*; St. Louis Country Club v. Administrative Hearing Commission,* 657 S.W.2d 614, 616 (Mo. banc 1983).

To establish estoppel, Tubular must prove: 1) a statement or representation, 2) an act by a party based on reliance of the statement or representation, and 3) an injury as a result of the reliance. *Missouri Highway & Transportation Commission v. Myers,* 785 S.W.2d 70, 78 (Mo. banc 1990). In addition, to prevail against the government, the taxpayer must prove that a government official committed an act of affirmative misconduct. *Farmers' & Laborers' Ins. Ass'n v. Director of Revenue,* 742 S.W.2d 141, 143 (Mo. banc 1987). As noted by this Court in *Lynn v. Director of Revenue,* 689 S.W.2d 45 (Mo. 1985), statements made by a Department of Revenue employee that a taxpayer's business was exempt from sales tax could not bind future directors of the Department nor limit the state's right to collect sales taxes that were properly owing. Tubular has shown no affirmative misconduct on the part of the government. The Director seeks only to collect taxes properly due. The Director is no more estopped in this case from rejecting Tubular's alternate apportionment method than was the Director in *Lynn.*

Tubular's argument is analogous to that made by the taxpayer and rejected by this Court in *J. C. Nichols Co. v. Director of Revenue,* 796 S.W.2d 16 (Mo. banc 1990), in which the taxpayer wrote the Director of Revenue, telling the Director that the taxpayer would continue to follow its historical accounting method unless the taxpayer heard

otherwise. The Director did not respond and the taxpayer continued to file its income tax returns using its accounting method. For the most part, the returns were accepted and some subsequent audits even yielded a refund. But when the Director in a later tax year sent a notice of deficiency, the taxpayer balked, contending that the Director had approved its historical accounting method. The Supreme Court held that the alternative accounting method that purported to segregate income and deductions with respect to interstate transactions was not an unfettered right, and that an affirmative approval of the Director of Revenue was required prior to use of an alternative accounting method. 796 S.W. 2d at 20.

The statute in *J. C. Nichols*,(§ 143.461.2, RSMo 1986) required the taxpayer to "petition the director of revenue in writing" for approval and for the director to notify the corporation if the alternate method was approved. While the regulation in issue in this case, 15 CSR 30-150.170, did not require written petition,[4] it contemplated prior affirmative approval before a corporation could use an alternate method of apportionment. Tubular's accountant agreed the Secretary of State did not issue a letter of approval or in any other way formalize an approval of Tubular's alternate apportionment method (Stip. Ex. R - L.F. 141). The regulation permitted a corporation to use an alternate method only

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[4] The amended version of 15 CSR 30-150.170, now 12 CSR 10-9.200, effective April 10, 1999, now specifies that to obtain written approval to use an alternate method of apportionment, the tax payer must submit a written request prior to the date of the franchise tax report.

"upon approval from the Secretary of State and for good case shown . . . . ." 15 CSR 30-150.170(2)(E)4. Similar to *J.C. Nichols,* the taxpayer can not infer from mere silence that the Director (or Secretary of State) has approved the alternate method and a Director's decision to settle a dispute with a taxpayer for one year, can not be read as an approval of an alternate method for subsequent years.

For the periods at issue (1996 through 1998), § 147.120.5, allowed the Secretary of State three years after a franchise report was filed in which to mail a notice of assessment. There is no allegation that the notices of assessments were untimely (Stip. Ex O - L.F. 138). The assessments were based on the finding by the auditor (as agent for the Secretary of State) that Tubular had used its own method of apportionment without the Secretary of State's approval. The notices confirmed the Secretary of State's position that approval had not been granted. Tubular can not logically contend that the Secretary of State gave tacit approval of its alternate method in light of these assessments notices.

CONCLUSION

The Administrative Hearing Commission appropriately applied the law to the facts in affirming the Director's assessment of franchise tax under § 147.010, RSMo. In view of the foregoing arguments and cited authorities, the Director requests that the decision of the Administrative Hearing Commission be affirmed.

Respectfully submitted,

JEREMIAH W. (JAY) NIXON
Attorney General

VICTORINE R. MAHON
Assistant Attorney General
Missouri Bar No. 32202
Broadway State Office Building
221 West High Street, 8th Floor
Post Office Box 899
Jefferson City, Missouri 65102
(573) 751-0330 Telephone
(573) 751-8796 Facsimile

ATTORNEYS FOR RESPONDENT DIRECTOR OF REVENUE

CERTIFICATE OF COMPLIANCE WITH RULE 84.06(B) AND (C)

The undersigned hereby certifies that on this 15th day of August 2003, two true and accurate copies of the foregoing brief, and one disk containing the foregoing brief, were mailed, postage prepaid, to:

Edward F. Downey
Riverview Office Center
221 Bolivar Street, Ste. 101
Jefferson City, Missouri 65101

Juan D. Keller
Derek B. Rose
211 North Broadway, Ste. 3600
St. Louis, Missouri 63101

The undersigned certifies that the foregoing brief complies with the limitations contained in Supreme Court Rule No. 84.06(b) and that the brief contains 6590 words.

The undersigned further certifies that the labeled disk, simultaneously filed with the hard copies of the brief, has been scanned for viruses and is virus-free.

_____
Assistant Attorney General