No. 48578

IN THE

Supreme Court of Illinois

GTE AUTOMATIC ELECTRIC, INCORPORATED, Plaintiff-Appellant, vs. **ROBERT H. ALLPHIN, as Director of Revenue of the State of Illinois,** Defendant-Appellee.	Appeal from the Appellate Court of Illinois, First District. — There heard on appeal from the Circuit Court of Cook County, Illinois. — Honorable **Daniel A. Covelli,** Presiding Judge.

BRIEF OF AMICUS CURIAE

WILLIAM D. DEXTER,
General Counsel,
Multistate Tax Commission,
Bank of Olympia Building,
Olympia, Washington 98501,

Attorney for Multistate Tax Commission and Named States.

EUGENE F. CORRIGAN,
Executive Director,
Multistate Tax Commission,
1790 30th Street,
Boulder, Colorado 80301,

Of Counsel.

KEENAN PRINTING COMPANY (312) 372-0066 365

PARTICIPATING AMICI CURIAE

William J. Baxley
Attorney General
State of Alabama

Bruce E. Babbitt
Attorney General
State of Arizona

Richard R. Heath
Director, Finance and Administration
State of Arkansas

Evelle J. Younger
Attorney General
State of California

Wayne L. Kidwell
Attorney General
State of Idaho

Frank Kelley
Attorney General
State of Michigan
Richard R. Roesch
Assistant Attorney General

James F. Senechal
Chief Counsel
Department of Revenue
State of Montana

Antonio Anaya
Attorney General
State of New Mexico

Allen I. Olson
Attorney General
State of North Dakota
A. R. Hausauer
Special Assistant Attorney General

Lee Johnson
Attorney General
Oregon Department of Justice
Theodore De Looze
Chief Tax Counsel

Slade Gorton
Attorney General
State of Washington
Richard H. Holmquist
Chief Counsel

INDEX

TABLE OF AUTHORITIES

Table of Cases:

STATUTES

IN THE

Supreme Court of Illinois

GTE AUTOMATIC ELECTRIC, INCORPORATED, Plaintiff-Appellant, vs. **ROBERT H. ALLPHIN, as Director of Revenue of the State of Illinois,** Defendant-Appellee.	Appeal from the Appellate Court of Illinois, First District. — There heard on appeal from the Circuit Court of Cook County, Illinois. — Honorable **Daniel A. Covelli,** Presiding Judge.

BRIEF OF AMICUS CURIAE

I.

STATEMENT OF INTEREST

This brief is submitted to permit the Multistate Tax Commission (hereinafter referred to as the Commission) and those of its member states which appear as amicus curiae to supplement the arguments of the appellee in this cause.

The Commission is the official administrative agency of the Multistate Tax Compact entered into by 21 states as full members and by 13 states as associate members.[1]

The Commission and the member states that have joined in this brief are vitally interested in the substantive issues in this cause. The language of the Uniform Division of Income For Tax Purposes Act (UDITPA) has been enacted by all the member states as well as 13 additional states for purposes of division of their respective income tax bases among the states which have jurisdiction to tax. The substantive questions in this cause concern an interpretation and application of the language of UDITPA and is a case of first impression in this country.

Pursuant to Article VII of the Multistate Tax Compact, the Commission is authorized to promulgate uniform rules and regulations interpreting UDITPA which become operative in member states if and when the member states adopt them in accordance with their own methods and procedures. The Commission approved revised uniform

---

1. The legislatures of 21 states have enacted the Multi-State Tax Compact, thereby making those states regular members of the Commission. Those states are: California, South Dakota, Kansas, Washington, Texas, New Mexico, Nevada, Oregon, Missouri, Nebraska, Arkansas, Idaho, Hawaii, Colorado, Wyoming, Utah, Montana, North Dakota, Michigan, Alaska and Indiana. One state, Alabama, has enacted the Compact subject to congressional legislative consent. Pending enactment of such consent, Alabama is considered to be an associate member state. Twelve other states are associate members at the request of the respective Governors. Those states are: Arizona, Georgia, Louisiana, Maryland, Massachusetts, Minnesota, New Jersey, Ohio, Oklahoma, Pennsylvania, Tennessee and West Virginia.

allocation and apportionment regulations on February 21, 1973. Those regulations interpret UDITPA for administrative purposes. Arkansas, California, Idaho, Nebraska, New Mexico, North Dakota, Oregon and Utah have adopted the regulations and other states are unofficially following the regulations in material part pending their adoption. On July 15, 1974, Illinois published proposed regulations which conform substantially with those of the Commission. These regulations embody an interpretation of the UDITPA language which is at issue in this cause.

It is important that the language of UDITPA be given a rational and uniform interpretation to carry out the purpose of the 29 states adopting its language in the first instance, which is to provide for uniformity and full accountability in the division of income for state and local income tax purposes. The Commission and the member amicus curiae states which have joined in this brief are concerned with appellant's position that the language of UDITPA (adopted for income tax allocation and apportionment purposes by Illinois) should be construed to defeat its manifest purpose by unwarranted exemption of income attributable to so-called "drop shipments." It is the purpose of this brief to demonstrate to the court the principle that the concept of full accountability of the income of the appellant to the states which have jurisdiction to tax is within the manifest intent of the Illinois legislature in adopting the UDITPA language and that proper rules of statutory construction require that this intent be given judicial approval.

II.

ISSUES PRESENTED FOR REVIEW

The brief of amicus curiae are limited to the substantive issues in this case. Simply stated, those issues are:

1. Are the receipts from appellant's sales, consummated by delivery by appellant's suppliers from Illinois sources to appellant's customers located in states in which appellant is not taxable, properly included in appellant's Illinois numerator of the sales factor of the apportionment formula? If not, are these receipts properly excluded from both the numerator and denominator of the sales factor?

2. Are the receipts from appellant's sales to its out-of-state customers located in states in which the appellant is not subject to tax and delivered to such customers by appellant's out-of-state suppliers located in states in which appellant is not subject to tax properly included in appellant's Illinois numerator of the sales factors the apportionment formula? If not, are these receipts properly excluded from both the numerator and denominator of the sales factor?

III.

STATEMENT OF THE CASE

In its declaratory action, the appellant requested this court to determine whether or not two classes of sales receipts are to be included in the Illinois numerator in the sales factor of the UDITPA apportionment formula. The first class of sales which we will deal with in this brief are the sales that presumably the appellant made to its customers located in states which do not have jurisdiction to impose an income tax on appellant where the goods are delivered directly from the appellant's suppliers in Illinois to the customers. The second class of sales for inclusion or exclusion in the Illinois numerator of the sales factor under UDITPA are the sales presumably to the appellant's out-of-state customers from appellant's out-of-state suppliers where both the customers and suppliers are located in states which do not have jurisdiction to impose an income tax on the appellant. These two classes of sales differ only in one particular, namely, the location of appellant's suppliers from which the goods are shipped to the appellant's customers, that is, whether within the state of Illinois or without the state of Illinois.

Under the language of UDITPA, it is the appellee's position and that of the Commission and the amicus curiae member states that the receipts from such sales should be included in the Illinois numerator of the sales factor UDITPA apportionment formula. An alternative position of the Commission and the member amicus curiae states is that the sales in question should be excluded both from the numerator and denominator of the sales factor under UDITPA. On the other hand, the appellant takes the position that the Illinois numerator should not include

any receipts from these classes of sales and that all the receipts from these classes of sales should be included in the denominator of the sales factor under UDITPA. Since these receipts are not includable in the numerator of any other state, appellant asks that UDITPA be interpreted to provide a tax loophole in the sales factor of the apportionment formula.

Under the regulations promulgated by the Commission, the position is taken that the receipts from the sales in question should be included in the Illinois numerator of the sales factor. The purpose of this brief is to demonstrate to this court why we believe the Commission regulations under UDITPA properly require the inclusion of the receipts in question in the Illinois numerator of the sales factor; or, in the alternative, to demonstrate why we believe that the receipts from these classes of sales should be excluded from both the numerator and the denominator of the sales apportionment factor.

IV.

STATUTES AND REGULATIONS INVOLVED

The questions at issue are whether or not the receipts from the sales in question are "in this state" (Illinois) as that term is defined by the following language in section 16 of UDITPA (Article IV, section 16 of the Multistate Tax Compact; Ill. Rev. Stat. ch. 120, § 3-304):

> "(b) Sales of tangible personal property are in this state if:
>
> (i) the properties delivered are shipped to a purchaser, other than the United States Government, within this state regardless of the FOB point or other conditions of the sale; or
>
> (ii) the property is shipped from an office, store, warehouse, factory or other place of storage in this state and either the purchaser is the United States Government or the person is not taxable in the state of the purchaser."

In addition, section 18 of UDITPA (Article IV, section 18 of the Multistate Tax Compact; Illinois Income Tax Law § 3-304(e)) provides:

> "18. If the allocation and apportionment provisions of this Article do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for or the administrator may require, in respect to all or any part of the taxpayer's business activity, if reasonable:
>
> (a) separate accounting;
>
> (b) the exclusion of any one or more of the factors;
>
> (c) the inclusion of one or more additional factors which will fairly represent the taxpayer's activity in this State; or

(d) the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income."

In reference to the first class of receipts here considered, namely, receipts from sales from Illinois suppliers of the appellant, the regulations of the Commission provide:

"(6) If the taxpayer is not taxable in the state of purchaser, the sale is attributable to this state if the property is shipped from an office, store, warehouse, factory, or other place of storage in this state." (Multistate Tax Commission Reg. IV. 16. (a) (6), Multistate Tax Commission Seventh Annual Report, p. 80)

In reference to the second class of sales here considered, namely, sales consummated by appellant's out-of-state suppliers to appellant's out-of-state customers, the regulations provide as follows:

"(7) If a taxpayer whose salesman operates from an office located in this state makes a sale to a purchaser in another state in which the taxpayer is not taxable and the property is shipped directly by a third party to the purchaser, the following rules apply:

(A) if the taxpayer is taxable in the state from which the third party ships the property, then the sale is in such state.

(B) if the taxpayer is not taxable in the state from which the property is shipped, then the sale is in this state.

Example: The taxpayer in this state sold merchandise to a purchaser in State A. Taxpayer is not taxable in State A. Upon direction of the taxpayer, the merchandise was shipped directly to the purchaser by the manufacturer in State B. If the taxpayer is taxable in State B, the sale is in State B. If the taxpayer is not taxable in State B, the sale is in this state."

(Multistate Tax Commission Reg. IV. 16. (a) (7), Multistate Tax Commission Seventh Annual Report, pp. 80-81)

V.

POINTS AND AUTHORITIES

1. Receipts from appellant's sales, consummated by delivery by appellant's suppliers from Illinois sources to appellant's customers located in states in which appellant is not subject to tax are properly included in appellant's Illinois numerator of the sales factor of the apportionment formula; or in the alternative are properly excluded from both the numerator and denominator of the sales factor. *Kennecott Copper* v. *State Tax Commission,* 27 Utah 2d 119, 493 P. 2d 632 (1972), appeal dismissed, 409 U.S. 973, rehearing denied, 409 U.S. 1093 (1972); *Hellertown Manufacturing Company* v. *Commonwealth of Pennsylvania,* 358 A. 2d 424 (1976); *The Uniform Division of Income for State Tax Purposes,* 35 Taxes 747 (1957) at pp. 748-749.

2. Receipts from appellant's sales to its out-of-state customers located in states in which appellant is not subject to tax and delivered to such customers by appellant's out-of-state suppliers located in states in which appellant is not subject to tax are properly included in appellant's Illinois numerator of the sales factor of the apportionment formula; or in the alternative, are properly excluded from both the numerator and denominator of the sales factor.

A. *General Rules of Statutory Construction*

73 Am. Jur. 2d, Statutes, §§ 145, 146, 147, 149, 153, 154, 155, 160, 250, 259, 260, 269, 338 and 339;

United States v. *American Trucking Associations,* 310 U.S. 534, 84 L. Ed. 1345, 60 S. Ct. 1049 (1940);

Markham v. *Cabell,* 326 U.S. 404, 9 L. Ed. 165, 66 S. Ct. 193 (1945);

Church of the Holy Trinity v. *United States,* 143 U.S. 457, 36 L. Ed. 226, 12 S. Ct. 511 (1892);

City Bank Farmers Trust Co. v. *New York C. R. Co.,* 253 N.Y. 49, 170 N.E. 489, 69 A. L. R. 940 (1930);

Corn Products Refining Co. v. *Commissioner,* 350 U.S. 46, 100 L. Ed. 29, 76 S. Ct. 20 (1959).

B. The uniform allocation and apportionment regulations adopted by the Multistate Tax Commission on February 21, 1973, are entitled to significant weight in resolving the merits of this controversy.

Skidmore v. *Swift & Co.,* 323 U.S. 143, 89 L. Ed. 124, 65 S. Ct. 161 (1944);

Hewitt-Robbins, Inc. v. *Eastern Freight-Ways, Inc.,* 371 U.S. 84, 9 L. Ed. 2d 142, 83 S. Ct. 157 (1962);

Piedmont Canteen Service, Inc. v. *Johnson,* 256 N. C. 155, 123 S.E. 2d 582, 91 A. L. R. 2d 1127 (1962);

United States v. *Penn. Ind. Chemical Corp.,* 411 U.S. 655, 36 L. Ed. 2d 567, 93 S. Ct. 1804 (1973);

Maritime Board v. *Isbrandtsen Co.,* 356 U.S. 481, 499, 2 L. Ed. 2d 926, 78 S. Ct. 851 (1958).

C. When the language of the Illinois Income Tax is construed as a whole in conformity with applicable rules of statutory construction, it is clear that the Illinois legislature did not intend the result contended for by appellant in reference to sales to appellant's out-of-state customers through appellant's out-of-state suppliers and that the receipts of such sales are properly included in appellant's Illinois numerator of the sales factor or are properly excluded from both the numerator and denominator of the sales factor.

People v. *Schommer,* 392 Ill. 17, 63 N.E. 2d 744, 167 A. L. R. 1347 (1945);

Public Utilities Commission v. *Monarch,* 267 Ill. 528, 108 N.E. 716 (1915);

People v. *Price,* 257 Ill. 587, 101 N.E. 196 (1913);

Uphoff v. *Industrial Board,* 371 Ill. 312, 111 N.E. 128 (1916);

Kennecott Copper Corp. v. *Tax Commission,* 27 Utah 2d 119, 493 P. 2d 632 (1972).

3. The receipts from the sales in question may constitutionally be included in the numerator of the sales factor.

International Harvester Co. v. *Evatt,* 329 U.S. 416, 91 L. Ed. 390, 67 S. Ct. 444 (1967);

Illinois C. R. Co. v. *Minnesota,* 309 U.S. 157, 84 L. Ed. 670, 60 S. Ct. 417 (1940);

Northwestern Portland Cement Co. v. *Minnesota,* 358 U.S. 450, 3 L. Ed. 2d 421, 79 S. Ct. 357, 67 A. L. R. 2d 1292 (1959);

Covington Fabrics Corp. v. *Tax Commission,* 264 S. C. 59, 212 S.E. 2d 574 (1975), appeal dismissed, 423 U.S. 805 (1975).

VI.

THE ARGUMENT

1. Introduction to the Argument.

For proper resolution of the questions at issue, it is essential that the *results* appellant is here contending for be placed in proper focus. It is asking this court to construe the language of UDITPA in a manner to create a vast loophole in the UDITPA apportionment rules by assigning sales factor receipts to states which have no tax jurisdiction or to nowhere leaving it free not to account for a portion of its taxable income to any state. For example, if all of its customers are located in states which do not have jurisdiction to impose a tax on it, appellant contends that one-third of its taxable income should escape taxation as long as the shipments are sent directly from its suppliers to its customers. Appellant does not bother itself with the question of whether or not the goods actually constitute goods it has purchased and thus constitute goods it has located in Illinois prior to the shipment by its suppliers. Furthermore, appellant does not concern itself with the legislative purpose in adopting the apportionment formula as contained in UDITPA in the first instance, namely, the division of its total taxable income among states which have taxing jurisdiction.

As stated by William J. Pierce, the principal author of UDITPA:

> "The Uniform Act, if adopted in every state having a net income tax or a tax measured by net income, would assure that 100 percent of income, and no more or no less, would be taxed.
>
> * * * * *
>
> "As we shall see, the question of allocating and apportioning with reference to the concepts of taxability

> assures that 100 percent of the income of a multistate business theoretically will be taxed by the several states."
>
> (The Uniform Division of Income for State Tax Purposes, 35 Taxes 747 (1957) at pages 748 and 749, respectively.)

It should be further noted that we are here concerned only with proper apportionment of appellant's net income. There is involved no tax on the appellant's sales or its sales activity as such.

The amicus curiae will examine here in the applicable statutory provisions under proper rules of statutory construction to determine whether this inequitable result is required by statute. Furthermore, we will respond to the appellant's claim that the receipts from the sales in question cannot constitutionally be included in the sales factor for apportionment purposes under due process and commerce clauses limitations of the federal constitution.

2. Receipts From Appellant's Sales, Consummated By Delivery By Appellant's Suppliers From Illinois Sources To Appellant's Customers Located In States In Which Appellant Is Not Taxable, Are Properly Included In Appellant's Illinois Numerator Of The Sales Factor Of The Apportionment Formula; Or, In The Alternative, Are Properly Excluded From Both The Numerator And Denominator Of The Sales Factor.

Section 16(b) of UDITPA (§ 3-304(a)(3)(B)(ii) of Illinois Law) expressly provides that sales are in the Illinois numerator of the sales factor if "the property is shipped from an office, store, warehouse, factory, or other place of storage in this state (Illinois in the instant case) and . . . the taxpayer (appellant) is not taxable in the state of

the purchaser." The statute does not require that the shipment be made from appellant's place of business in Illinois. The statutory test is met if the shipment is from any person's place of business in Illinois. This should end the discussion of this question. The argument of appellant (if supported by the record, which it is not) that it has no control over the location from which its suppliers will ship the goods (that is, within or without Illinois) is irrelevant and immaterial. There is nothing in the statutory language or its rationale that has anything to do with the taxpayer's control of the place from which the goods are shipped. The only question is: Were the goods shipped from a point within Illinois to the out-of-state purchaser? If this is the case, the statute language includes the sales in appellant's Illinois numerator.

The authorities relied upon by appellant are irrelevant because we have here express language which includes these sales. Furthermore, there is nothing in the record to indicate that appellant's suppliers are not in fact acting as appellant's agents in delivering the goods to the appellant's out-of-state customers. Also, it is properly assumed that all of the appellant's sales activities in regard to these sales took place in Illinois.

The UDITPA regulations promulgated by the Commission simply repeat in substance the statutory language followed by an example of shipment from the taxpayer's own inventory to a purchaser in a state where the seller is not subject to tax. The regulations (Reg. IV.16(a)(6)) state:

> "If the taxpayer is not taxable in the state of the purchaser, the sale is attributed to this state (the state of the taxpayer-seller) if the property is shipped from an office, store, warehouse, factory, or other place of storage in this state."

ITIB 1974-1, approved and released for publication as of July 15, 1974, provides that the Commission regulations are to be followed unless inconsistent with existing regulations. The Illinois Department of Revenue has thus adopted the interpretation of the UDITPA language contained in the Commission's UDITPA regulations.

It therefore appears beyond question that, by express statutory language and by the Illinois Department's interpretation of the statutory language, that appellant's sales, consummated by delivery from in-state sources of Illinois suppliers, are included in the Illinois numerator of the sales factor. There is absolutely no basis for construing the language of § 3-304(a)(3)(B)(ii) of the Illinois income tax law to create a tax loophole in favor of appellant as to these sales.

Assuming, arguendo, that the language of § 3-304(a)(3)(B)(ii) could be construed *not* to encompass the sales consummated by appellant's suppliers by delivery to appellant's customers, the receipts in question should be eliminated from both the numerator and denominator of the sales factor. As more fully set forth below, this is necessary to carry out the intent of UDITPA and the Illinois legislature in adopting UDITPA to effectuate full and equitable apportionment of appellant's income among the states which have jurisdiction to tax. This results from giving proper effect and significance to the language of section 18 of UDITPA (§ 3-304(e) of the Illinois Law). In no event can the language of § 3-304(a)(3)(B) (ii) coupled with the language of § 3-304(e) grant the exemption appellant contends is applicable to this class of sales. As indicated below, the language of section 18 of UDITPA was construed in *Kennecott Copper* v. *State Tax Commission, supra,* 27 Utah 2d 119, 493 P. 2d 632 (1972) and *Hellertown Manu-*

facturing Co. v. *Commonwealth of Pennsylvania, supra,* 358 A. 2d 424 (1976), to require a fair apportionment of income to the business activities of a taxpayer within the state.

3. Receipts From Appellant's Sales To Its Out-Of-State Customers Located In States In Which Appellant Is Not Subject To Tax And Delivered To Such Customers By Appellant's Out-Of-State Suppliers Located in States In Which Appellant Is Not Subject To Tax Are Properly Included In The Illinois Numerator Of The Appellant's Sales Factor; Or, In The Alternative, Are Properly Excluded From Both The Numerator And Denominator Of The Sales Factor.

We are here concerned with the same statutory language involved with reference to appellant's sales from Illinois sources (origins) of its suppliers. The only difference here is that appellant's suppliers fill the appellant's orders to out-of-state customers from out-of-state locations in which the appellant is not subject to tax. Appellant asserts that the language of section 16(b) of UDITPA and § 3-304(a)(3)(B)(ii) of Illinois law does not cover this factual pattern. Read literally, apart from the general purpose of the statute and apart from other provisions, this language may not include this class of sales in the Illinois numerator of the sales factor. While appellant is not satisfied with a literal reading of the language when applied to sales of its suppliers from Illinois sources, it contends the language should be given literal application here. In both instances, it is necessary to determine whether the language is compatible with the general intent of the legislature considering the statute as a whole.

We will here first consider applicable rules of statutory construction and then focus our attention on other por-

tions of the statute to ascertain legislative intent and give meaning and effect to all parts of the statute.

A. *General Rules of Statutory Construction.*

As heretofore indicated, the appellant is asking this court to construe the language of UDITPA, adopted by twenty-nine states and promulgated by the National Conference of Commissioners on Uniform State Laws, to create a substantial gap and preference in the apportionment of net income of a multistate taxpayer. This is, of course, contrary to the general intent of UDITPA, which is to arrive at a fair and equitable apportionment of the income tax base among those states which have jurisdiction to tax. With this general intent in mind, we turn to some of the applicable rules of statutory construction and some decisions which apply these rules.

Under the general heading, "Aids Generally Applicable To Construction," 73 Am. Jur. 2nd, beginning at page 352, sets forth various rules. In 73 Am. Jur. 2nd Statutes § 147, p. 352, it is stated:

> "The meaning to be ascribed to a statute can only be derived from considered weighing of every relevant aid to construction."

In 73 Am. Jur. 2d Statutes § 149, page 353, it is further noted:

> "The scope or purview of a statute is frequently considered by the courts in the interpretation thereof, since it is a general rule of construction that a statute should be interpreted so as to render it consistent or in conformity with its general scope or purview . . . Indeed, it has even been recognized that the general purview of a statute may control the literal meaning of a particular provision." (Footnotes to case citations omitted.)

The same authority in § 153 at pages 356-357 further note:

> "In construing a law of doubtful meaning or application, the policy which induced its enactment, or which was designed to be promoted thereby, is a proper subject for consideration, where such policy is clearly apparent or can be legitimately ascertained. Indeed, the proper course in all cases is to adopt that sense of the words which promotes in the fullest manner the policy of the legislature in the enactment of the law, and to avoid a construction which would alter or defeat that policy. Even the literal meaning of the terms employed should not be suffered to defeat the manifest policy intended to be promoted . . ." (Footnotes to case citations omitted.)

In 73 Am. Jur. 2d § 154 at pages 358-359, the author states:

> "There are numerous cases involving the interpretation of statutes which make reference to the spirit thereof as an aid to construction . . .
>
> "Where there is a conflict between the spirit of a law and the literal import of the terms employed, the former, at least in connection with other elements, has often been declared to prevail over the latter. Under this rule, that which is within the spirit of the statute though not within its letter is a part of it, and that which is not within the spirit but within the letter is not a part of it . . ." (Footnotes to case citations omitted.)

As stated in 73 Am. Jur. § 155, pages 359-360:

> "In the interpretation of a statute of doubtful meaning, it is proper to take into consideration its purpose or object, or the aim, design, motive, or end in view. The construction of the statute should be made with reference to the purpose of the statute, or in the light thereof, and in harmony and conformity therewith, in

> order to aid, advance, promote, subserve, support, and effectuate such aim, design, motive, end, aspiration, or object. Thus, the general purpose of a statute should be given effect even if it be necessary, in so doing, to restrict somewhat the force of subsidiary provisions that otherwise would conflict with the paramount intent. A construction should be avoided which would operate to impair, pervert, frustrate, thwart, nullify, or defeat the object of the statute . . .'' (Footnotes to citations omitted.)

In a little different vein, 73 Am. Jur. 2d § 160 at page 364 reads:

> ''In the enactment of a statute, it may be presumed that the legislature did not act blindly or arbitrarily, but that it had a reasonable and practicable plan or scheme for the accomplishment of its purpose. Such plan or scheme may be taken into consideration in the interpretation of the statute and its purpose . . .

In speaking of inequitable results, 73 Am. Jur. 2d, § 259 at page 428 states:

> ''The law is presumed to be equitable, and it is a rule of construction to resolve any ambiguity in a statute in favor of an equitable operation of the law . . .''

As otherwise stated in the same authority at § 260 under the heading, ''Injustice or unfairness,'' it is stated at page 429:

> ' ' ' It should not be presumed to have been within the legislative intent to enact a law having an unjust result . . .
>
> ''On the ground that a technicality should not be permitted to override justice, the general intention of the legislature is generally held to control the strict letter of the statute where an adherence to the strict letter would lead to injustice . . .''

Under the heading, "Unequal operation and unsubstantial distinction," 73 Am. Jur. 2d, § 269, pages 430-432 reads:

> "An intent to discriminate unjustly between different cases of the same kind is not to be ascribed to the legislature. Hence, where the legislature has clearly laid down a rule for one class of cases, it is not readily to be supposed that, in the same act, a different rule has been prescribed for another class of cases within the same reason as the first . . . Indeed, nothing but clear and unmistakable language will warrant a court in a construction which will produce the unequal operation of a statute . . ." (Footnotes to cited cases omitted.)

Above all, as stated in 73 Am. Jur. 2d, § 145 at page 351:

> "In the interpretation of statutes, the legislative will is the all-important or controlling factor . . . A construction adopted should not be such as to nullify, destroy, or defeat the intention of the legislature." (Footnotes to case citations omitted.)

The relation of general rules of construction to legislative intent is stated as follows in 73 Am. Jur. 2d, § 146, pages 351-352:

> "In the interpretation of a statute, the intention of the legislature is gathered from the provisions enacted, by the application of sound and well-settled canons of construction. However, since all rules for the interpretation of statutes of doubtful meaning have for their sole object the discovery of the legislative intent, every technical rule as to the construction of a statute must yield to the expression of the paramount will of the legislature. It has even been declared that the intention of the legislature, when discovered, must prevail, any rule of construction declared by previous act to the contrary nothwithstanding."

In reference to the construction of uniform laws, it is stated:

> 1. "A uniform law which is remedial in nature should be liberally construed." (73 Am. Jur. 2d Statutes, § 338, page 480)
>
> 2. "Uniform state laws are to be construed with reference to the objects sought to be obtained . . . The object of uniform state laws is to provide, as far as possible, a uniform law on the subject involved that would be common to all the states adopting it, and this object should be considered in the interpretation of such laws in order to effectuate such purpose . . ." (73 Am. Jur. 2d Statutes, § 339, page 481)

In applying the foregoing rules of construction, at least in part, the Supreme Court in *United States* v. *American Trucking Associations,* 310 U.S. 534, 84 L. Ed. 1345, 60 S. Ct. 1049 (1940), refused to give a literal interpretation to the word "employee" relating the authority granted the Interstate Commerce Commission to establish reasonable requirements with respect to the qualifications and maximum hours of service of employees of motor carriers. In the course of the opinion, the court commented as follows, supported by numerous citations in footnotes, in reference to proper rules of statutory construction:

> ". . . To take a few words from their context and with them thus isolated to attempt to determine their meaning, certainly would not contribute greatly to the discovery of the purpose of the draftsmen of a statute, particularly in a law drawn to meet many needs of a major occupation.
>
> "There is, of course, no more persuasive evidence of the purpose of a statute than the words by which the legislature undertook to give expression to its wishes. Often these words are sufficient in and of themselves to determine the purpose of the legislation. In

such cases we have followed their plain meaning. When that meaning has led to absurd or futile results, however, this court has looked beyond the words to the purpose of the act. Frequently, however, even when the plain meaning did not produce absurd results but merely an unreasonable one 'plainly at variance with the policy of the legislation as a whole' this Court has followed that purpose, rather than the literal words. When aid to construction of the meaning of words, as used in the statute, is available, there certainly can be no 'rule of laws' which forbids its use, however clear the words may appear on 'superficial examination.' The interpretation of the meaning of statutes, as applied to justiciable controversies, is exclusively a judicial function. This duty requires one body of public servants, the judges, to construe the meaning of what another body, the legislators, has said. Obviously there is danger that the courts' conclusion as to legislative purpose will be unconsciously influenced by the judges' own views or by factors not considered by the enacting body. A lively appreciation of the danger is the best assurance of escape from its threat, but hardly justifies an acceptance of a literal interpretation dogma which withholds from the courts available information for reaching a correct conclusion. Emphasis should be laid, too, upon the necessity for appraisal of the purposes as a whole of Congress in analyzing the meaning of clauses or sections of general acts. A few words of general connotation appearing in the text of statutes should not be given a wide meaning, contrary to a settled policy, 'excepting as a different purpose is plainly shown.' " (Footnotes to numerous citations omitted.) (310 U.S. 542-544)

In *Markham* v. *Cabell,* 326 U.S. 404, 90 L. Ed. 165, 66 S. Ct. 193 (1945), the court refused to give literal interpretation to language providing for a statute of limitations as to claims and prescribing the date on which the claims had to exist before they could be recovered from the alien property custodian. It noted:

> "... that the court below refused 'to make a fortress out of the dictionary' and to read § 9(e) strictly and literally. The policy as well as the letter of the law is a guide to decision. Resort to the policy of the law may be had to ameliorate its seeming harshness or to qualify its apparent absolutes as *Church of the Holy Trinity* v. *United States,* 143 U.S. 457 illustrates. The process of interpretation also misses its high function if a strict reading of the law results in the emasculation or deleting of a provision which a less literal reading would preserve." (326 U.S. 409)

Again, in *Church of the Holy Trinity* v. *United States,* 143 U.S. 457, 36 L. Ed. 226, 12 S. Ct. 511 (1892), the Supreme Court refused to give literal application to the words in a statute. The statute under consideration made it unlawful to prepay the transportation, or in any way assist or encourage the importation or migration of any alien or aliens into the United States to perform labor or service of any kind in the United States. The question was whether or not this included a contract entered into by the Church of the Holy Trinity to obtain the services of a rector from England. The Court held that though the language literally applied to such a situation, it was not within the intent of Congress. So holding, the Court stated:

> "While there is great force in this reasoning (that the literal language of the statute was applicable), we cannot think Congress intended to denounce with penalty the transaction like that in the present case. It is a familiar rule that a thing may be within the letter of the statute and yet not within the statute, because not within its spirit nor within the intention of its makers. This has been often asserted, and the reports are full of cases illustrating its application." (143 U.S. 459)

In an opinion written by Chief Judge Cardoza of the Court of Appeals of New York in *City Bank Farmers Trust*

Co. v. *New York Cent. R. Co.,* 253 N.Y. 49, 170 N.E. 489, 69 A. L. R. 940 (1930), the court refused to apply literally the language of a statute to defeat the purpose of the transfer tax on estates. He construed the language "tax imposed by this article" to mean "the tax imposed by this act." In so doing, he stated:

> "In the construction of a statute, adherence to the written word will not be suffered to 'defeat the general purpose and manifest policy intended to be promoted.' (cases cited) The intent, when discovered, will prevail over the letter. (cases cited) (170 N.E. 492).

In the historic income tax case of *Corn Products Refining Co.* v. *Commissioner,* 350 U.S. 46, 100 L. Ed. 29, 76 S. Ct. 20 (1959), the court carved out a judicial exception to the capital assets definition in the Internal Revenue Code by reference to the general intent of Congress in giving special capital gains treatment to certain sales or exchanges of property in the first instance. Under a literal reading of the statute (§ 117(a) of the Internal Revenue Code of 1939) the sale of the commodity futures there involved would have constituted the sale of a capital asset. The court held to the contrary.

In sum, the rules of statutory construction that are here applicable require this court to ascertain the general scope and purpose of the language of UDITPA incorporated into the Income Tax Law of Illinois and give effect to the language of § 3-304(a)(3)(B)(ii) in light of the general intent manifested by the Illinois legislature in adopting a uniform apportionment rule and in light of other applicable provisions of the statute. The mechanical approach to this language suggested by appellant adds little purpose and significance to the judicial function in construing statutory language.

B. *The Uniform Allocation And Apportionment Regulations Adopted By The Multistate Tax Commission On February 21, 1973 Are Entitled to Significant Weight In Resolving The Merits of This Controversy.*

In considering the weight to be given to the Uniform Allocation and Apportionment regulations approved by the Commission on February 21, 1973, this court should be aware of the basic purpose of Illinois and of 28 other states in adopting the language of UDITPA as part of their substantive income tax law. This court may take judicial notice of the fact that the reason Illinois and 28 other states adopted the language of UDITPA was to produce uniformity in the allocation and apportionment of the income of multistate businesses. Furthermore, that the purpose of this uniformity is to protect multistate businesses from over-taxation while requiring multistate businesses to account for their total taxable income to the states which have jurisdiction to tax. Overtaxation or undertaxation would result from each state unilaterally adopting its own allocation and apportionment rules without regard to the rules adopted by other states. In order to prevent overlap or gap in state taxation of multistate businesses, it is also necessary to have uniform interpretation and application of the statutory language. This is, of course, what is intended to be accomplished by the Commission UDITPA regulations and Illinois' adoption of the UDITPA language and its use of the regulations as guides to interpretation.

As stated by the National Conference of Commissioners on Uniform States Laws, in the prefatory note to UDITPA:

"The Uniform Division of Income for Tax Purposes Act is designed for enactment in those states which levy taxes on or measured by net income.

"The need for a uniform method of division of income for tax purposes among the several taxing jurisdictions has been recognized for many years and has long been recommended by the Council of State Governments. There is no other practical means of assuring that a taxpayer is not taxed on more than its net income. At present, the several states have various formulae for determining the amount of income to be taxed, and the differences in the formulae produce inequitable results. The problem has been well analyzed and its historical background outlined in an article appearing in 18 Ohio State Law Journal, page 84.

"The Uniform Division of Income for Tax Purposes Act is the result of conferences with the representatives of the Controller's Institute of America, the Council of State Governments, and various interested individuals."

As heretofore indicated, the states of Arkansas, California, Idaho, Nebraska, New Mexico, North Dakota, Oregon and Utah adopted these regulations, and, while Illinois has not formally adopted the regulations, ITIB 1974-1, issued by the Department of Revenue, states that the proposed regulations are "to be followed as representing department interpretations, positions, and policy to the extent not inconsistent with the presently effective regulations under IITA Article III." Alaska, Indiana, Michigan and Montana and several other states are considering the possibility of adopting these regulations, and Texas is applying the regulations to its franchise tax to the extent possible. It cannot be too strongly emphasized that the basic purpose of Illinois in adopting the UDITPA language as part of its substantive income tax law will be

completely thrwarted if this law is not implemented by uniform regulations and if it is not construed to avoid overtaxation or undertaxation of the income of a multistate taxpayer.

This leads us to a consideration of what effect is to be given uniform interpretation of uniform laws. As heretofore indicated under rules of statutory construction, a uniform law which is remedial in nature should be liberally construed with reference to the object sought to be obtained. Appellant's interpretation of § 304(a)(3)(B)(ii) of the Illinois law thwarts the "full accountability" principle of the UDITPA law; namely, that the income of a multistate corporation should be apportioned and allocated to those states which have jurisdiction to tax. Appellant asks this court to construe the law to create a substantial tax loophole.

In reference to the effect to be given administrative interpretations, the Supreme Court of the United States in *Skidmore* v. *Swift & Co.,* 323 U.S. 143, 89 L. Ed. 124, 65 S. Ct. 161 (1944), stated:

> "We consider that the rulings, interpretations and opinions of the administrator under this act, while not controlling upon the courts by reason of their authority, do constitute a body of experience and informed judgment to which courts and litigants may properly resort for guidance. The weight of such judgment in a particular case will depend upon the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade, if lacking the power to control." (323 U.S. 140)

Cf. *United States* v. *Penn Ind. Chemical Corp.,* 411 U.S. 655, 36 L. Ed. 2d 567, 93 S. Ct. 1804 (1973) and *Maritime Board* v. *Isbrandtsen Co.,* 356 U.S. 481, 499, 2 L. Ed. 2d 926, 78 S. Ct. 851 (1958).

As otherwise stated in 2 Am. Jur. 2d, Administrative Law, § 241, pages 66-67:

> "The formal or informal interpretation or practical construction of an ambiguous or uncertain statute or law by the executive department or other agency charged with its administration or enforcement is entitled to consideration and the highest respect from the courts, and must be accorded appropriate weight in determining the meaning of the law, especially when the construction or interpretation . . . is contemporaneous with the first workings of the statute, . . ."

Courts, while retaining the final authority to expound a statute administered by an administrative agency, should avail themselves of the aid implicit in the agency's superiority in gathering the relevant facts and in marshalling them into a meaningful pattern. *Hewitt-Robbins, Inc.* v. *Eastern Fregiht-Ways, Inc.*, 371 U.S. 84, 9 L. Ed. 2d 142, 83 S. Ct. 157 (1962). Furthermore, an interpretative regulation made by the Commissioner of Revenue will ordinarily be upheld if made pursuant to statutory authority and if not in conflict with the terms and purposes of the act pursuant to which it was made. *Piedmont Canteen Service, Inc.* v. *Johnson,* 256 N.C. 155, 123 S.E. 2d 582, 91 A. L. R. 2d 1127 (1961).

The amicus curiae here are not contending that there is a long history in Illinois or elsewhere concerning the interpretation of UDITPA to the sales transactions in question. They do assert, however, that there has been a well-considered interpretation of the UDITPA language in reference to the sales in question which have seriously been considered by a number of states, including the state of Illinois, which should be given great weight by this court in light of the purpose for the uniform language of UDITPA in the first instance.

C. *When The Language of the Illinois Income Tax Act Is Construed as a Whole in Conformity With Applicable Rules of Statutory Construction, It Is Clear that the Illinois Legislature Did Not Intend the Result Contended For By Appellant In Reference to Appellant's Sales To Its Out-Of-State Customers From Out-Of-State Sources and That the Receipts of Such Sales Are Properly Included in Appellant's Illinois Numerator of the Sales Factor or Are Properly Excluded From Both the Numerator and Denominator of Appellant's Sales Factor.*

Amicus curiae agree with appellant that a literal reading of Chapter 120, § 3-304(a)(3) of the Illinois law, standing alone, does not include the receipts from appellant's sales shipped by its out-of-state suppliers to purchasers in out-of-state destinations in the Illinois numerator of the appellant's sales factor. This follows from the elemental proposition that receipts from such sales are not from the sales of property shipped from an office, store, warehouse, factory or other place of storage in Illinois. However, as indicated above the heading, "General Rules of Statutory Construction" the question of the meaning of § 3-304(a)(3) does not stop here. This language must be fit into the general intent of the legislature of Illinois in adopting the entire provisions of UDITPA which intent was to fairly allocate and apportion all of the taxable income of the appellant to states which have jurisdiction to tax. The statutory construction problem then is to look at the language of UDITPA in its entirety and see what authority would aid the court in upholding this intent.

In *People* v. *Schommer,* 392 Ill. 17, 63 N.E. 2d 774, 167 A. L. R. 1347 (1945), in construing one section of a statute in harmony with the intended purpose and provisions of the whole statute, the court stated:

> "It is a well-settled rule of statutory construction that in construing statutes, the intention of the legislature will control and that the several provisions of the statute should be construed together in the light of the general purpose and object of the act, so as to give effect to the main intent and purpose of the legislature as therein expressed." (292 Ill. 27)

In *Public Utilities Commission* v. *Monarch,* 267 Ill. 528, 108 N.E. 716 (1915) the court refused to give a literal interpretation to the definition of "warehouse" used in the act there considered and after in substance repeating the rules stated in *People* v. *Schommer, supra,* continued:

> "When this intention can be collected from the statute, words may be modified, altered or supplied so as to obviate any repugnancy or inconsistency with such intention, although in doing so particular provisions may not be read or construed according to their literal reading." (cases cited) (267 Ill. 540)

In *People* v. *Price,* 257 Ill. 587, 101 N.E. 196 (1913), the court had before it the application of two sections of an act and construed one section to modify the other section to carry out the purpose of the legislature. The court found it unreasonable to find as a legislative intent that an additive to food as a preservative is injurious and not subject to sale and at the same time to find that the legislature intended the preservative alone could be sold. The court there found that the main purpose of the act was to protect the public health and construed the sections accordingly. In so holding, it stated:

> "It is a primary rule in the interpretation and construction of a statute that the intention of the legislature is to be ascertained and given effect. In ascertaining the legislative intent, each part or section is to be considered in connection with every other part or section, also the evils intended to be remedied by the

> enactment. 'The intent is the vital part, — the essence of the law, — and the primary rule of construction is to ascertain and give effect to that intent.' (Lewis' Sutherland on Stat. Construction, Sec. 363.)." (257 Ill. 593)

As otherwise stated in *Uphoff* v. *Industrial Board,* 371 Ill. 312, 111 N.E. 128 (1916) in construing provisions of the Workmen's Compensation Act:

> "The intention of the law-makers is the law. This intention is to be gathered from the necessity or reason of the enactment and the meaning of the words, enlarged or restricted according to the real intent. In construing a statute the courts are not confined to the literal meaning of the words. A thing within the intention is regarded within the statute though not within the letter. A thing within the letter is not within the statute if not also within the intention. When the intention can be collected from the statute, words may be modified or altered so as to obviate all inconsistency with such intention. (case cited) When great inconvenience or absurd consequences will result from a particular construction, that construction should be avoided, unless the meaning of the legislature be so plain and manifest that avoidance is impossible. (case cited) The courts are bound to presume that absurd consequences leading to great injustice were not contemplated by the legislature, and a construction should be adopted that it may be reasonable to presume it was contemplated. (authorities cited) The statute is passed as a whole, and not in parts or sections; hence, each part or section should be construed in connection with every other part or section. In order to get the real intention of the legislature, attention must not be confined to the one section to be construed. *Warner* v. *King,* 267 Ill. 82, and cases cited." (271 Ill. 315-316)

In applying the specific rules of statutory construction as well as the general rules discussed above under the

heading, "General Rules of Statutory Construction," our task here is to examine the whole statutory pattern of the Illinois income tax law in light of what can be assumed to be the facts and circumstances of this case. We may assume for purposes of this brief that the appellant carried on all its sales activities in the state of Illinois in regard to the class of sales we are here considering. Certainly, there is nothing in the record to prove otherwise. Furthermore, the appellant is contending that the class of sales here in question are not included in the numerator of any since, since the state of the supplier and the state of the purchaser lack jurisdiction to tax the appellant. To adopt the appellant's viewpoint, it is necessary to assume then that the Illinois legislature and the drafters of UDITPA intended to create a large gap or loophole in the sales factor of the apportionment formula.

Our first inquiry is to determine what meaning should be ascribed to § 3-304(a)(3)(B)(ii) of the Illinois law and next to determine whether other provisions of the Illinois law are applicable if § 3-304(a)(3)(B)(ii) does not permit inclusion of the sales in question in the Illinois numerator.

In examining the provisions of § 3-304(a)(3), it is clear that the general rule is for the inclusion of sales receipts on the basis of the location of the purchaser (the destination of the sale as set forth in § 3-304(a)(3)(B)(ii)). The legislature enacted § 3-304(a)(3)(B)(ii) as an exception to the destination test and precluded a sale from being assigned to a destination state in which the taxpayer (seller) was not subject to tax. Section 3-304(a)(3)(B)(ii) was designed to prevent income from being assigned to a state in which the taxpayer did not carry on sufficient activity to uphold taxation by the destination state. Thus, while § 3-304(a)(3)(B)(ii) does not expressly cover out-

of-state shipments to an out-of-state purchaser, the general intent of all the provisions of § 3-304(a)(3) is to assign the sales receipts of the taxpayer/seller to the destination of the sale if the seller is taxable in the state of destination and to the state of origin if the seller is not taxable in another state. Thus, if the manifest legislative intent is to be given effect, the sales in question are to be treated as Illinois sales. Language in § 3-304(a)(3)(B)(ii) can be given this construction by reading the phrase, "The property shipped from an office" to refer to the in-state sales activity of the seller rather than just to the physical shipment of the goods. This construction of the phrase would conform to the general legislative intent and cover the problem of "drop shipments." Such construction has been upheld in numerous cases to give effect to the general legislative intent once that has been ascertained.

On the other hand, it can be argued, as appellant argues in substance, that the legislature failed to take into account shipments of out-of-state suppliers of the seller and thus there exists a gap in the legislation which cannot be closed by judicial construction. However, even if this view is taken of the specific language of § 3-304(a)(3)(B)(ii), the position of the appellant is in error due to other provisions of the Illinois income tax law. Fortunately from the state's viewpoint, the drafters of UDITPA contemplated that there may be circumstances where the prescribed apportionment formula did not arrive at the intended result of a fair apportionment to the states which have jurisdiction to tax.

To cover this situation, the Illinois legislature adopted the following language which is, in substance, section 18 of UDITPA:

"If the allocation and apportionment provisions of subsections (a) through (d) do not fairly represent the extent of a person's business activities in this state, the person may petition, or the director may require, in respect to all or a part of the person's business activity if reasonable:

(1) separate accounting;

(2) the exclusion of one or more factors;

(3) the inclusion of one or more additional factors which will represent the person's business activities in this state; or

(4) the employment of any other method to effectuate an equitable allocation and apportionment of the person's business income."

(§ 3-304(e) of the Illinois Income Tax Law.)

If § 3-304(a)(3)(B)(ii) is construed as contended by appellant to create a gap or loophole in the sales factor, this gap or loophole is expressly covered by subparagraph (4) of § 3-304(e). This provision of the law leaves the director of the Department of Revenue of the State of Illinois free to employ any method of apportionment to effectuate an equitable allocation and apportionment of appellant's business income. Obviously, if the appellant carries on all of its sales activities in the state of Illinois as pertains to the sales in question and is not taxable in the state of the out-of-state supplier or the state of the out-of-state purchaser, a reasonable apportionment of the appellant's business income would require the sales in question to be included in the numerator of the Illinois sales factor of the appellant.

Apart from the language of § 3-304(e), under appellant's construction of § 3-304(a)(3)(B)(ii), all of the appellant's income generated by the sales in question would not be subject to tax by any state. Obviously, if Illinois can-

not include these sales receipts in its numerator of the sales factor and the state of the supplier and the state of the purchaser lacks jurisdiction to tax the appellant, income from these receipts are not subject to tax anywhere. If the language of § 3-304(e) was not intended to cover this situation, it is hard to conceive a situation where the language would be applicable.

Certainly, in light of the language of § 3-304(e), the Illinois law cannot be construed to grant the tax preference appellant contends for here. For example, assume that appellant, an Illinois corporation, has places of business (and thus subject to tax) in States A and B and is not subject to tax in the states of its purchasers and in the states of its out-of-state suppliers. Under these circumstances, States A and B would be entitled in combination to tax only two-thirds of the appellant's income and one-third of its income would escape taxation altogether under appellant's construction of the statute. It takes little imagination to see that, under such circumstances, the apportionment formula does not result in a fair apportionment to States A and B. If this is a result required by the general apportionment rules, the tax administrators of States A and B are entitled under section 18 of UDITPA and § 3-304(e) of the Illinois law to employ any method to effectuate a fair apportionment. To accomplish this purpose, several alternatives are available. The drop shipment sales could be ignored in both the numerator and denominator of the sales factor or as done in the Commission regulations, these sales could be handled as follows:

> "(7) If a taxpayer whose salesman operates from an office located in this state makes a sale to a purchaser in another state in which the taxpayer is not taxable and the property is shipped directly by a third party to the purchaser, the following rules apply:

(A) If the taxpayer is taxable in the state from which the third party ships the property, then the sale is in such state.

(B) If the taxpayer is not taxable in the state from which the property is shipped, then the sale is in this state.

Example: The taxpayer in this state sold merchandise to a purchaser in State A. Taxpayer is not taxable in State A. Upon direction of the taxpayer, the merchandise was shipped directly to the purchaser by the manufacturer in State B. If the taxpayer is taxable in State B, the sale is in State B. If the taxpayer is not taxable in State B, the sale is in this state."

It is respectfully submitted that this is a reasonable application of § 3-304(e) by the Illinois Department of Revenue and should end the controversy on this issue.

The Supreme Court of Utah in *Kennecott Copper Corp., et al.* v. *State Tax Commission of Utah, supra,* 27 Utah 2d 119, 493 P. 2d 632 (1972), construed the effect of the section 18 UDITPA language in relationship to the prescribed apportionment formula. In that case the Utah Supreme Court refused to give a literal application to § 16(b) of UDITPA (§ 3-304(a)(3)(B)(ii) of Illinois Law) in determining what sales were to be included in the Utah numerator of the sales factor. Rather, it applied the language of section 18 of UDITPA. By application of section 18 of UDITPA, the Utah Supreme Court modified the apportionment formula to include in the Utah sales factor sales of minerals from Utah sources, even though sold to purchasers in other states where Kennecott was taxable. The court felt that the sales apportionment factor, standing alone, apart from section 13, did not affect a fair and reasonable apportionment of Kennecott's income to the state of Utah. It noted:

"It is Kennecott's contention that the legislature having adopted a formula for apportionment of business income to the State, the Tax Commission was not authorized to depart from the formula and to make its own allocation. The legislature which adopted the act as a proposed uniform state law also included within the act the provisions of Section 59-13-95 UCA 1953 as amended (the language of § 3-304(e) of Illinois law and section 18 of UDITPA), which authorizes the Tax Commission to employ another method to effectuate an equitable allocation of the taxpayer's income if the apportionment provisions of the act do not fairly represent the extent of the taxpayer's business activity in this state. It should be noted that the provisions of the last mentioned section may be invoked at the instance of the Commission or at the behest of the taxpayer. We do not construe the statute as limiting the Commission to the use of the formula in all cases. The record supports the Commission's conclusion that the use of the formula does not fairly represent the extent of Kennecott's business activity in this state during the years 1967 and 1968. (footnote omitted) (25 Utah 2d 124) (Material within parentheses added.)

In *Hellertown Manufacturing Co.* v. *Commonwealth of Pennsylvania, supra,* 358 A. 2d 424 (1976), the court again relied upon Section 18 of UDITPA to effectuate a fair apportionment of the taxpayer's income. Even though the Pennsylvania legislature had specifically rejected the provisions of UDITPA contained in Illinois Law § 3-304(a)(3)(B)(ii) (the sales "throwback" rule), the court upheld the Secretary of Revenue's determination that sales to states which had no tax jurisdiction over the taxpayer were properly eliminated from the denominator of the sales factor (the "throw-out" rule) under section 18 of UDITPA. In so doing, the court stated:

> "In summary, we hold that where a foreign corporation manufactures all of its products in Pennsylvania, has all of its tangible property in Pennsylvania, pays only a minimum privilege tax to one other state, and is not subject to the taxing jurisdiction of any other state, and files a CNI (Corporate Net Income) tax return showing all of its sales in all states and foreign countries in the denominator of the sales fraction of the three-part formula, upon resettlement the Secretary of Revenue may "throw-out" all sales in foreign jurisdictions where such taxpayer is not subject to any corporate tax and reduce the denominator in the sales fraction accordingly." (Material in parenthesis added)

Also, significantly, the court in *Hellertown* noted that the burden was upon the taxpayer to show that the Section 18 result arrived at by the Secretary of Revenue was an abuse of his discretion under Section 18.

In sum, Section 18 of UDITPA is applicable in the instant case to prevent appellant from obtaining the tax preference it here contends for as a result of a literal reading and interpretation of the language of § 3-304(a)(3)(B)(ii) of the Illinois law. This follows from the elementary proposition that the appellant cannot establish that the apportionment formula, as it would have this court construe it, arrives at a fair apportionment of its income attributable to its Illinois activities. Certainly, the discretion lodged in the Director of the Department of Revenue under section 18 of UDITPA (§ 3-304(e)) has not been abused by its adoption of the language of Regulation IV.16.(a).(7) of the Commission (quoted above) as its interpretive position. The discretion lodged in the Illinois department of revenue director was so lodged to avoid tax inequities such as that urged on this court by the appellant. In no sense can a fair apportionment be achieved for Illinois by including the sales in question in the denominator

of appellant's sales factor and not in the Illinois numerator of appellant's sales factor. They either have to be excluded from both or included in both for a fair apportionment to Illinois.

4. The Receipts From The Sales In Question May Constitutionally Be Included In The Numerator Of The Sales Factor.

We are here concerned with the reasonableness of the result of the Illinois apportionment formula in reaching the income of the appellant properly attributable to Illinois. We do not have here a question of whether or not Illinois could constitutionally impose a sales, or gross receipts tax on the sales receipts in question such as was involved in the *McLeod* v. *Dilworth Co.* case, 322 U.S. 327, 64 S. Ct. 1023, 88 L. Ed. 1034 (1944). In devising an apportionment formula, rough approximation is all that is necessary to uphold its constitutionality. *International Harvester Co.* v. *Evatt,* 329 U.S. 416, 91 L. Ed. 390, 67 S. Ct. 444 (1967); *Illinois C. R. Co.* v. *Minnesota,* 309 U.S. 157, 84 L. Ed. 670, 60 S. Ct. 419 (1940); *Northwestern Portland Cement Co.* v. *Minnesota,* 358 U.S. 450, 3 L. Ed. 2d 421, 79 S. Ct. 357, 67 A. L. R. 2d 1292 (1959).

In *International Harvester Co.* v. *Evatt, supra,* the question before the court was the validity of the apportionment formula of the Ohio corporate franchise tax. The apportionment formula employed a sales factor to determine "business done" in Ohio, which included in the Ohio numerator sales of products manufactured in Ohio and delivered to purchasers out of the state and goods manufactured outside of Ohio and delivered to customers within Ohio. The court held that the apportionment formula did not violate either the due process or commerce clause of the

United States Constitution. As to the due process argument, the court held that Ohio was simply taxing manufacturing and sales in Ohio. As to the interstate commerce argument, the court stated:

> "Plainly Ohio sought to tax only what she was entitled to tax, and there is nothing about the application of the formula in this case that indicates a potentially unfair result under any circumstances . . . Furthermore, this court has long realized a practical impossibility of a state's achieving a perfect apportionment . . . and has declared that 'rough approximation' rather than precision, is sufficient. *Illinois C. R. Co.* v. *Minnesota,* 309 U.S. 157. Unless a palpably disproportionate result comes from an apportionment, the result which makes it patent that the tax is levied upon interstate commerce rather than upon an intrastate privilege, this court has not been willing to nullify honest state efforts to make apportionments . . . A state's tax law is not to be nullified merely because the result is achieved through a formula which includes consideration of interstate and out-of-state transactions in the relationship to the intrastate privilege." (329 U.S. 422-423)

In *Northwestern Portland Cement Co., supra,* the court held that due process and commerce clause restrictions were not violated by a fairly apportioned net income tax on business activities within the taxing state even though the taxpayer carried on only interstate business in the taxing state. After analysis of various cases, the court noted:

> "These cases stand for the doctrine that the entire net income of a corporation, generated by interstate as well as intrastate activities, may be fairly apportioned among the States for tax purposes by formulas utilizing in-state aspects of interstate affairs. In fact, in *Bass, Ratcliff and Gratton,* (266 U.S. 271, 69 L. Ed.

> 282, 45 S. Ct. 82 (1924)) the operations in the taxing state were conducted at a loss, and still the court allowed part of the overall net profit of the corporation to be attributable to the state." (358 U.S. 460)

Specifically as to due process, the court stated:

> "The taxes imposed are levied only on that portion of the taxpayer's net income which arises from its activities within the taxing state. These activities form a sufficient 'nexus' between such a tax and the transactions within a state for which the tax is exacted. '*Wisconsin* v. *J. C. Penney Co., supra* (311 U.S. at 445).' " (358 U.S. 464)

The general tests to be employed to determine whether an apportionment formula is constitutional was before the Supreme Court of South Carolina in *Covington Fabrics Corp.* v. *Tax Commission,* 264 S. C. 59, 212 S.E. 2d 574 (1975), appeal dismissed, 423 U.S. 805 (1975).

The taxpayer was there contending that the provisions of UDITPA that assign sales to the origin state under the sales factor, where the destination state does not have tax jurisdiction, was unconstitutional. The court, in upholding the constitutionality of this feature of UDITPA, noted:

> (1) That there was no constitutional provision that prohibited a state from taxing net income from interstate commerce;
>
> (2) That one who attacks a formula of apportionment carries a distinct burden of showing by clear and cogent evidence that it results in extraterritorial values being taxes;
>
> (3) That exactness in apportionment is not required; and

(4) That there is no authority that supports the argument that the UDITPA three factor apportionment formula unreasonably apportions income and that *Butler Bros.* v. *McColgan,* 315 U.S. 501, 62 S. Ct. 701, 86 L. Ed. 991 ((1941), specifically upheld the validity of a formula employing the factors of property, payroll and sales.

Inasmuch as the appellant has not claimed that the Illinois apportionment formula, with the inclusion of the sales in question in the Illinois numerator, arrives at a palatably disproportionate result, it is clear that the apportionment formula with the inclusion of such sales receipts does not violate either the due process or commerce clauses of the federal constitution. The same is true if the sales in question are excluded from both the denominator and numerator of the sales factor.

VI.

CONCLUSION

The National Conference of Commissioners on Uniform State Laws drafted UDITPA with the general intent of providing a uniform, fair and equitable method of dividing the income tax base among the states which have jurisdiction to tax. This language has been adopted by 29 states. It was incorporated in the language of the Multistate Tax Compact as Article IV to carry out this intended purpose in the Compact member states. Appellant here contends that this purpose must be frustrated because the UDITPA drafters did not specifically take into consideration shipments to purchasers through suppliers of the sellers, the so-called "drop shipments."

This argument of the appellant specifically fails in reference to the shipments by in-state suppliers to out-of-state purchasers of the seller because a literal reading of the language of section 16(b) of UDITPA (§ 3-304(a)(3)(B)(ii) of Illinois Law) expressly covers these types of sales.

This argument of the appellant is defective in reference to appellant's shipments through its out-of-state suppliers to its out-of-state customers because it is directed to a construction of the language of section 16(b) of UDITPA (§ 3-304(a)(3)(B)(ii) of Illinois Law) in conflict with the general legislative intent of the Illinois Income Tax Act apportionment provisions. More particularly, it is in conflict with section 18 of UDITPA (§ 3-304(e) of Illinois Law) which requires the tax administrators to adjust the particular apportionment rules to fairly represent a taxpayer's business activity in the taxing state. To accomplish this objective, section 18(4) of UDITPA specifically authorizes tax administrators to employ any allocation or apportionment method "to effectuate an equitable allo-

cation and apportionment of the taxpayer's business income." In this connection, it cannot be too strongly emphasized that appellant in this case is asking for an unfair apportionment of its business income to Illinois based on the fact that it employs "drop shipments" in filling the orders of its out-of-state customers. The fact that it uses "drop shipments" rather than direct shipments from its own inventories does not change one *iota* the nature and extent of its business activities in the state of Illinois. In fact, as far as the record here is concerned, it might well carry on more significant activity in Illinois in regard to the drop shipments than it would in reference to direct shipments. There are absolutely no facts which would justify the exclusion of appellant's drop shipments just from the Illinois sales factor of the apportionment formula. Furthermore, if the appellant's sales activities in regard to drop shipments be characterized as de minimus and beyond the control of appellant, as it argues in its brief, the logic dictates then under section 18(4) of UDITPA that the "drop shipments" be eliminated from both the Illinois numerator and the denominator of the sales factor. Under no circumstances is a fair and equitable apportionment arrived at by excluding the drop shipment sales from the Illinois numerator and including them in the everywhere denominator of the sales factor.

In short, what the Commission and the amicus curiae states are contending for in this brief is a fair and equitable apportionment of appellant's income to states which have jurisdiction to tax. They do not believe that the language of Illinois apportionment and allocation rules read in conjunction with section 18 of UDITPA (§ 3-304(e) of Illinois Law) which is a part thereof, can reasonably be construed to have the potential effect of exempting one-third of the appellant's income from any state taxation whatsoever.

It is therefore respectfully submitted that this court conclude that the appellant's receipts from the drop shipments in question are includable in the Illinois numerator of the sales factor of the apportionment formula or in the alternative that they are excluded from both the Illinois numerator and the everywhere denominator of the appellant's sales factor. In either event, this court would be according full and equitable apportionment of the appellant's income tax base to the states which have jurisdiction to tax, thus giving effect to the general intent of the drafters of UDITPA and the legislatures of the 29 states which have enacted its provisions to effect a reasonable and fair apportionment of the entire income tax base of Multistate taxpayers.

In so contending, we do not believe that this court is being asked to deviate from the express statutory language. Clearly, § 3-304(a)(3)(B)(ii) covers the first class of sales here considered, namely, drop shipments from in-state suppliers of appellant. If it could be construed to not do so, which we believe is not possible, still § 3-304(e) covers this gap and requires the alternative results we are here contending for, namely, the inclusion of these sales in the Illinois numerator or their elimination from both the Illinois numerator and the everywhere denominator. The same is true in reference to the second class of sales, namely, drop shipments from out-of-state suppliers of appellant. It is admittedly difficult to fit these sales into the specific language of § 3-304(a)(3)(B)(ii). However, proper rules of statutory construction require that, if possible, this language be construed to include these sales as Illinois sales. If this is not possible, § 3-304(e) becomes operative and grants the Illinois Director of the Department of Revenue the administrative power to either include these sales in

the Illinois numerator of appellant's sales factor or to exclude them from both the Illinois numerator and everywhere denominator. In no event can the statute, consistent with the mandate of § 3-304(e) (section 18 of UDITPA) be construed to create the vast loophole and preference here contended for by appellant simply on the basis of its expedient use of drop shipments from its suppliers to fill orders to its customers.

Wherefore, it is respectfully submitted that this court give effect to the intent of the drafters of UDITPA and the 29 enacting states by determining that the drop shipments in question are in the Illinois numerator; or in the alternative, that they are neither in the Illinois numerator or the everywhere denominator of the appellant.

Respectfully submitted,

WILLIAM D. DEXTER,
General Counsel,
Multistate Tax Commission,
Bank of Olympia Building,
Olympia, Washington 98501,

Attorney for Multistate Tax Commission and Named States.

EUGENE F. CORRIGAN,
Executive Director,
Multistate Tax Commission,
1790 30th Street,
Boulder, Colorado 80301,

Of Counsel.