No. 08-1207

In The
Supreme Court of the United States

GEOFFREY, INC.,

Petitioner,

v.

COMMISSIONER OF REVENUE,

Respondent.

On Petition For A Writ Of Certiorari To The Supreme Judicial Court Of Massachusetts

BRIEF OF *AMICUS CURIAE* THE SHERWIN-WILLIAMS COMPANY IN SUPPORT OF PETITIONER

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TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page

CASES

TABLE OF AUTHORITIES – Continued

Page

LEGISLATIVE AND REGULATORY MATERIALS

OTHER AUTHORITIES

TABLE OF AUTHORITIES – Continued

STATEMENT OF INTEREST OF *AMICUS CURIAE*[1]

The Sherwin-Williams Company ("Sherwin-Williams") is an Ohio Corporation in the business of manufacturing and retailing paint and paint-related products. Sherwin-Williams is actively engaged in interstate commerce. As such, Sherwin-Williams relies on this Court's interpretation of the Commerce Clause of the United States Constitution when making business decisions and otherwise conducting itself in the interstate marketplace.

In *Complete Auto Transit v. Brady*, 430 U.S. 274 (1977), this Court held that the Commerce Clause requires that businesses, like Sherwin-Williams, must have substantial nexus with a state for that state to impose its tax on them. Since *Complete Auto*, this Court has only defined substantial nexus once, in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). In *Quill* this Court reaffirmed the long-standing rule that a business must be physically present before a state may impose its tax on them: a state may only tax business that have physical presence within its

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[1] The parties were notified ten days prior to the due date of this brief of the intention to file. The parties have consented to the filing of this brief.

No counsel for a party authored this brief in whole or in part, and no counsel or party made a monetary contribution intended to fund the preparation or submission of this brief. No person other than *amicus curiae*, its members, or its counsel made a monetary contribution to its preparation or submission.

borders.[2] The tax at issue in *Quill* was the sales tax. This Court has only interpreted what substantial nexus means in terms of the sales tax and has never specifically articulated what substantial nexus means in the area of income tax. Yet, it is as critical if not more critical to businesses like Sherwin-Williams for this Court to define substantial nexus in terms of the income tax.

This Court's silence has caused a split among the states. Some states have, rightfully in our view, applied the *Quill* physical presence rule to the income tax. However, many others have interpreted the failure of this Court to articulate a specific income tax nexus rule as license to disregard *Quill* and fashion their own rule called economic presence. Multistate businesses like Sherwin-Williams are left to navigate these uncertain waters.

Most multistate businesses like Sherwin-Williams relied on *Quill* and its ancestors in the absence of a separate ruling from this Court on state income tax nexus. In the states that have abandoned physical presence in favor of the economic presence rule multistate businesses' reliance on *Quill* is much to their detriment as it exposes them to incalculable back taxes, interest and extremely and inappropriately harsh penalties. This climate of uncertainty and potential harshness prevents multistate businesses

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[2] The *Quill* decision involved a state imposition of the duty to collect the sales tax on the business.

like Sherwin-Williams from confidently broadening the scope of their interstate activities. Therefore, not only is it in Sherwin-Williams' interest, but also the free flow of interstate commerce necessitates this Court clarify what substantial nexus means in terms of the state income tax.

SUMMARY OF ARGUMENT

In *Quill*, this Court declared "[u]ndue burdens on interstate commerce may be avoided . . . by the demarcation of a discrete realm of commercial activity that is free from interstate taxation." 504 U.S. at 314-15. Despite this pronouncement, the lack of clear nexus rules for state income taxation resulting from this Court's silence and the corresponding split among the states has unduly burdened interstate commerce. In the absence of a clear income tax nexus rule, as demonstrated by the present case, states are not only imposing their income taxes on businesses with no physical presence but also subjecting these businesses to huge penalties for failure to file income tax returns. To lift this burden and to resolve the split among the states, this Court must articulate what substantial nexus means in terms of state income taxation.

Moreover, a clear nexus rule is even more important for purposes of state income tax than for sales tax. There is no justification for a bright-line physical presence rule only in the context of the sales tax.

Despite what some state courts and academics claim, the reality from the perspective of multistate businesses is that the complexities and compliance demands of income tax laws require greater certainty and a clearer nexus rule than sales and use tax laws demands.

Additionally, dramatic changes in the climate of interstate commerce occurring since the *Quill* decision in 1992 have raised the stakes even higher. Since *Quill* was decided, the nation has experienced several financial accounting scandals and a dramatic rise in attention to corporate financial accountability. Along with Congressional mandates like Sarbannes-Oxley, the Financial Accounting Standards Board ("FASB") has issued rules for corporate accounting increasing the stakes associated with accounting for income taxes on corporate financial statements. FASB Statement No. 109, *Accounting for Income Taxes* and its related interpretation, FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* ("FIN 48"), relate to the recognition of tax benefits and liabilities on a company's financial statement. FIN 48 magnifies the ill effects of the ambiguity surrounding the Commerce Clause as it applies to state income tax nexus.

As *Quill* explains, a bright-line physical presence rule allows corporate taxpayers to precisely determine whether a state may impose a tax on them and if so, to what extent the state may tax them. This principle does not only mandate a bright-line physical presence rule in the case of state sales and use tax.

Because of the complexities of income tax laws, the burdens of compliance, and the high stakes involved, a bright-line physical presence rule is absolutely critical in the case of state income tax nexus.

ARGUMENT

I. The Lack of a Clear and Distinct Income Tax Nexus Ruling from This Court Has Allowed States to Abusively Tax Out-of-State Businesses to the Detriment of Interstate Commerce.

The uncertainty surrounding state income tax nexus has allowed states to abandon long-standing rules and flippantly disregard rules articulated by this Court at the expense of interstate commerce.[3]

[3] The Supreme Court of Appeals of West Virginia for instance wrote:

> It would be nonsense to suggest that [the Framers] could foresee or fathom a time in which a person's telephone call to his or her local credit card company would be routinely answered by a person in Bombay, India or that a consumer could purchase virtually any product on a computer with the click of a mouse without leaving home. This recognition of the staggering evolution in commerce from the Framer's time up through today suggests to this court that in applying the Commerce Clause we much eschew rigid and mechanical legal formulas [like the physical presence rule] in favor of a fresh application of Commerce Clause principles tempered with healthy doses of fairness and common sense.

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Instead, with no holding from this Court dealing specifically with income tax nexus, states have creatively fashioned their own nexus rules that allow them to impose taxes on out-of-state businesses that have not even an iota of physical presence within their borders. The end result is unconstitutional discrimination against interstate commerce.

As this Court noted in *Quill Corp. v. North Dakota*, the law in the area of state tax nexus is in something of a quagmire. 504 U.S. 298, 315 (1992). This is especially true in the context of state income tax nexus. In 1977 in the case *Complete Auto*, this Court articulated a four-part test that a state's imposition of tax must meet under the Commerce Clause. 430 U.S. 247. Under the *Complete Auto* test, a state tax passes Commerce Clause muster only if: 1) the activity taxed has a substantial nexus with the state; 2) the tax is fairly apportioned; 3) the tax does not discriminate against interstate commerce; and 4) the tax is related to the services provided by the state. *Id.*, at 279. Fifteen years later in *Quill*, this Court made its only pronouncement outlining the requirements of the substantial nexus prong of the *Complete Auto* test. In the *Quill* case, the tax at issue was the sales tax. *Quill* reaffirmed the long-standing rule that substantial nexus requires that a business must be physically present before a state may impose

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Tax Comm'r of State v. MBNA America Bank, N.A., 640 S.E.2d 226, 232 (W.Va. 2006).

the burden to collect sales tax on that business. *Quill*, 504 U.S. at 317-18. Since *Complete Auto*, this Court has not heard another substantial nexus case other than *Quill*.

Geoffrey, Inc. v. Comm'r of Rev., 453 N.E.2d 87 (Mass. 2009), reflects the broader trend of states pushing the boundaries of the law in the face of uncertainty. As state budget deficits rise, states are more and more desperate to raise revenue. Common sense dictates how appealing it is for states to tax those who lack political voice allowing them to raise revenue while avoiding the political consequences of tax increases. This Court's silence in the realm of income tax nexus provides the states the perfect opportunity to do just that. Starting with South Carolina, many state courts, legislatures and departments of revenue, leaping a few logical steps and seizing upon dicta in *Quill*, adopted the theory that *Quill* applies only in the context of the sales tax. *See Geoffrey v. SC Tax Comm'n*, 437 S.E.2d 13 (S.C. 1993); *see also, e.g. A&F Trademark, Inc. v. Tolson*, 605 S.E.2d 187 (N.C. 2004); *Geoffrey, Inc. v. Oklahoma Tax Commission*, 132 P.3d 632 (Okla. Civ. App. 2005). This theory allowed these states to impose their income taxes on businesses with absolutely no physical presence within their borders.[4]

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[4] For example, the West Virginia Supreme Court of Appeals recently held:

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The Framers recognized that this type of abuse of power to gain a leg up in the interstate marketplace is in a state's very nature and must be checked. As James Madison wrote:

> . . . the desire of the commercial States to collect in any form, an indirect revenue from their uncommercial neighbours, must appear not less impolitic than it is unfair . . . But the mild voice of reason, pleading the cause of an enlarged and permanent interest, is but too often drowned before public bodies as well as individuals, by the clamours of an impatient avidity for immediate and immoderate gain.

> [T]he Supreme Court appears to have expressly limited *Quill's* scope to sales and use taxes. First, the *Quill* Court noted that "[a]lthough we have not, in our review of other types of taxes, articulated the same physical-presence requirement that *Bellas Hess* established for sales and use taxes, that silence does not imply repudiation of the *Bellas Hess* rule." *Quill*, 504 U.S. at 314, 112 S.Ct. at 1914. Also, the Court commented that "although in our cases subsequent to *Bellas Hess* and concerning other types of taxes we have not adopted a similar bright-line, physical-presence requirement, our reasoning in those cases does not compel that we now reject the rule that *Bellas Hess* established in the area of sales and use taxes." *Id.*, 504 U.S. at 317, 112 S.Ct. at 1916. We believe that a reasonable construction of this language clearly implies that *Quill* applies only to sales and use taxes and not to other types of state taxes.

Tax Comm'r of State v. MBNA America Bank, N.A., 640 S.E.2d 226, 232 (W.Va. 2006).

The Federalist No. 42 at 284 (James Madison). By raising more revenue a state elevates its status in the interstate marketplace. A state's place in the interstate marketplace is raised even further when it attracts more businesses to become physically present within it. Raising taxes and fees on businesses with political voice (i.e. physical presence) within the state is politically difficult if not suicidal.[5] Thus, taxing out-of-state businesses is irresistibly attractive to states and they will continue to do so unless there are clear impediments imposed upon them.

The resulting harm to interstate commerce from this abuse of state power is significant. In the absence of a separate ruling on income tax nexus, the requirements of state income tax nexus under the Commerce Clause remained unclear. The states for their part, split between those states that concluded the physical presence test applies to all state taxes[6] and those that

[5] In fact, most states offer businesses millions of dollars in incentives to stay physically present or become physically present. *See, e.g.* Tom Precious, *Uncertainty Reigns in Development Efforts*, BUFFALO NEWS, Jan. 25, 2009, at P8 (discussing the state's hand-out of $950 million dollars in incentives to businesses to locate in enterprise zones within the state in 2008 alone).

[6] For instance, in 2000, the Tennessee Supreme Court affirmed a lower court decision holding the physical presence rule applies in the context of the income tax. JC Penney Nat'l Bank v. Johnson, Comm'r of Revenue, No. M1998-00497-SC-R11_CV (Tenn. May 8, 2000) (per curiam). The New Jersey Tax Court, in this case, similarly held that the physical presence rule applies in the context of the income tax only to be later reversed

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concluded the physical presence test is isolated to sales and use tax. Until recently, more states held the view that physical presence applied to all taxes and the split among them on the income tax nexus issue was more even. Only recently, have so many states abandoned physical presence.[7] For their part, most multistate businesses like Sherwin-Williams have long relied on *Quill* and its ancestors in the absence of a separate ruling for state income tax nexus. Before a state jumped on the economic nexus bandwagon, businesses without physical presence in that state had no reason to file an income tax return in that state. This fact is of great consequence to these businesses because if a business does not file a return the statute of limitations does not begin to run in most jurisdictions. *See, e.g.* ILCS Chapter 35 § 5/905(c) (2006); N.J. REV. STAT. § 54A:9-4(c)(1)(A) (1976).

As a result and despite these businesses' reasonable reliance on *Quill* and its ancestors, such businesses

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by the state's appellate court, whose decision was later affirmed by New Jersey's highest court. Lanco, Inc. v. Director, Div'n of Tax'n, 21 N.J. Tax 200 (2003).

[7] While South Carolina started the economic presence trend in 1993, most other states did not follow suit until much more recently. *See, e.g.* Kevin Ass'ts, L.L.C. v. Crawford, 865 So. 2d 34 (Sup. Ct. La. 2004); Comptroller v. SYL, 825 A.2d 399 (Ct. of Apps. Md. 2003); Acme Royalty Co. v. Director of Revenue (Mo. Tax Ct. Jan. 3, 2002); KMart Properties, Inc. v. Taxation and Revenue Dept., 40 P.3d 1008 (N.M. 2002); A&F Trademark, Inc. v. Tolson, 605 S.E.2d 187 (N.C. 2004).

may be liable for unquantifiable back taxes and interest attributable to long ago tax years in states in which they have no physical presence whatsoever. Worse still, as the instant case demonstrates, states are eager to assess penalties for failure to file a return and for failure to timely pay income taxes due. These penalties are generally calculated as a percentage of the state-claimed back tax liability. *See e.g.* HAW. REV. STAT. § 231-39 (2007) (imposing a penalty of as much as 25% of the balance due, for the late filing of a corporate income tax return); ME. REV. STAT. ANN. 36 § 187-B(1)(C) (imposing a penalty of as much as 100% of the assessed taxes for the late payment of corporate income taxes).

This is precisely what happened to Geoffrey, Inc. in Massachusetts, even though Massachusetts law requires the abatement of penalties if the taxpayer had reasonable cause for failing to file. MASS. GEN. L. ch. 62C § 33(f). Even if the Commerce Clause does not require physical presence for a state to impose its income tax on a business, the position that it is so required is more than reasonable in the face of *Quill* and this Court's subsequent silence on the substantial nexus issue.[8] The end result is Massachusetts levying its income tax and millions of dollars in penalties on a business with no physical presence or

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[8] The fact that several states have adopted the position that physical presence is necessary for a finding of substantial income tax nexus further supports the reasonableness of Geoffrey's and similar businesses' position.

political voice within the state. Massachusetts' coffers are filled with millions of dollars while suffering virtually no political consequences and interstate commerce bears the heavy burden. This Court can ease this burden by articulating a clear rule of state income tax nexus.

II. The Burdens of Compliance with and the Complexity of State Income Tax Laws and Corporate Accounting Rules Necessitate a Clear and Distinct Income Tax Nexus Ruling from This Court.

Those that argue that the *Quill* physical presence rule is confined to the sales tax and inapplicable to the income tax cite the difference between the sales tax and income tax as justification. However, from our experience as a multistate business the differences between the two taxes actually counsel that the opposite is true: the burdens of complying with the income tax laws themselves as well as with corporate financial accountability rules dictate a bright-line income tax nexus rule is essential for states to fairly levy their income taxes on multistate businesses.

A. The Compliance Burdens Related to Income Tax Laws and Regulations Necessitate a Clear and Distinct Income Tax Nexus Rule.

While the Supreme Judicial Court of Massachusetts maintains that the *Quill* physical presence rule is inapplicable to the analysis of the constitutionality of an imposition of the state's income tax largely because "compliance with specific administrative regulations associated with the collection of sales and use taxes unduly burdened interstate commerce, but that the collection of franchise and income taxes did not appear to cause similar compliance burdens." *Capital OneBank v. Comm'r of Revenue*, 899 N.E.2d 76, ___ (Mass. 2009). From Sherwin-Williams' perspective, this is simply not true. Sherwin-Williams is on the front lines of state tax law compliance, working every day and devoting an entire department of the company to compliance with both sales tax laws and income tax laws, as well as many other types of tax. Sherwin-Williams has first-hand knowledge that complying with state income tax laws is more burdensome than complying with any other type of tax law and income tax laws are far more complex than any other type of tax law, including sales and use tax laws. If anything, the compliance burdens associated with state income tax laws and financial accounting rules dictate that it is even more important to have a bright-line physical presence rule in the case of the income tax than it is to have such a rule in the context of the sales tax.

State courts and academics have focused on the number of returns rather than the complexity of compliance with the respective state laws and generally grossly underestimate the amount of jurisdictions to which multistate companies must file income tax returns. A typical state court justification for concluding that compliance with state income tax laws is less onerous than compliance with state sales tax laws is because "state income tax is usually paid only once a year, to one taxing jurisdiction and at one rate, [but] a sales and use tax can be due periodically to more than one taxing jurisdiction within a state and at varying rates." *A&F Trademark, Inc. v. Tolson*, 605 S.E.2d 187, 194 (N.C. App. 2004); *see also e.g. Tax Comm'r v. MBNA America Bank, N.A.*, 640 S.E.2d 226, 234 (W.Va. 2006); Cory D. Olson, Comment, *Following the Giraffe's Lead – Lanco, Inc. v. Director, Division of Taxation Gets Lost in the Quagmire That Is State Taxation*, 6 MINN. J. L. SCI. & TECH. 789, 813-14 (2005).

This is not the reality for multistate businesses like Sherwin-Williams. In many states, localities are permitted to impose their own income taxes on corporations.[9] Additionally, many income-taxing jurisdictions require multiple income tax filings each year, as well as estimated periodic filings.[10] Also, when a corporate taxpayer needs more time to file a return it generally must file an application for an extension. Sherwin-Williams files returns in approximately 170

[9] Sherwin-Williams' home city of Cleveland, Ohio, for example, imposes an income tax on the company as do over 50 municipalities in the Greater Cleveland area alone. CLEVE. CITY INCOME TAX ORD. § 191.0101 (2004).

[10] Alabama and Idaho are just two of many examples of income-taxing jurisdictions requiring quarterly filing. ALA. ADMIN. CODE R. 810-3-82.02 (1988); IDAHO CODE § 63-3036A (2001).

state and local income tax jurisdictions on behalf of itself and its subsidiaries. As such, over the course of a typical year, the Sherwin-Williams' Tax Department files approximately 1700 income tax returns, estimated periodic payments, or applications for extensions to file returns.

Another typical argument that compliance with sales tax laws is more onerous than compliance with income tax laws is that the differences are less complex between income tax laws across jurisdictions than the differences in sales tax laws across jurisdictions. *See e.g.* John A. Swain, *State Income Tax Jurisdiction: A Jurisdictional and Policy Perspective*, 45 WM. & MARY L. REV. 319, 368 (2003) (arguing "several key features of state corporate income taxes suggest that they are significantly less burdensome" to comply with than state sales tax laws).

From Sherwin-Williams' perspective, this is simply not true. The difference between state sales tax laws generally is limited to exemptions, rates, and the timing and manner of reporting. On the other hand, not only do jurisdictions vary in their income tax rates and timing and manner of income tax reporting, there are also countless other differences adding to the complex web of state and local income tax laws. State and local laws differ, for example, in what items qualify as non-business income, as well as allowable deductions, credits and depreciation methods. The amount of time and resources spent researching and collecting data necessary to claim certain state or local deductions and credits alone can be staggering.[11]

Additionally, some states require combined reporting, a single return for all affiliated corporations, while others permit each corporation to file a separate return. Further complicating matters, some combined reporting states require all domestic and foreign affiliates file a single return, while others only require domestic affiliates file a single return. Also, each state has its own formula for calculating the amount of income allocable to it, known as an apportionment formula. Different states may use a different combination of three factors in their apportionment formulas: sales, payroll, and property. Some states use all three, some states use two, and some one. States also differ in what items are includable in each factor.

As a result of this greater complexity, Sherwin-Williams' Corporate Tax Department devotes significantly more of its resources to state income tax law compliance versus compliance with state sales tax

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[11] One employee in the Sherwin-Williams Tax Department estimates he spent 90 hours annually working to comply with the requirements for claiming the Ohio Refundable Jobs Credit, OHIO REV. CODE ANN. § 122.17 (2006). He spends this time coordinating with other departments within Sherwin-Williams, creating databases of information, sorting through documents, and researching changes to the required form and manner of submission of the information. According to this employee, he spends a similar amount of time working on compliance with the requirements of income tax credits for other states.

laws. Sherwin-Williams' Tax Department employs four accountants who devote their entire time on the job to sales tax law compliance. Comparatively, Sherwin-Williams' Tax Department employs seven accountants who devote their entire time on the job to income tax compliance.[12]

The only reason Sherwin-Williams needs four accountants for sales tax is the volume of returns, since sales tax returns are relatively uniform. Conversely, even though there are fewer returns to prepare, Sherwin-Williams needs seven income tax accountants to handle the complexity of income tax returns. Further illustrating the point, the Sherwin-Williams' income tax accountants are employed at a higher grade level than its sales tax accountants: Sherwin-Williams Tax Department spends 25% of its salary budget on income tax accountant salaries, while spending only 12.5% of its salary budget on sales tax accountant salaries.

Besides accountants, the Sherwin-Williams Tax Department employs five attorneys who spend the vast majority of their time addressing income tax

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[12] The income tax accountants split their time between state and federal income taxes, spending the majority of time working on strictly state issues. It is worth noting that much of the work these accountants do related to federal income taxes is also applicable to state taxes in some way, as many states base at least some of their income tax laws on federal income tax laws. Nebraska, for example, follows the Internal Revenue Code's approach to interest deduction, although with minor modifications. NEB. REV. STAT. § 77-2716 (2007).

issues. The complexity of state income tax law might be best evidenced by the fact that the Sherwin-Williams Tax Department spends a whopping 94% of its state tax litigation budget on litigating income tax issues, while it allocates merely 6% on sales tax issues.

Moreover, many states reimburse businesses a percentage of the sales tax collected from their customers as compensation for the burdens related to complying with sales tax laws. *See e.g.* FLA. STAT. § 212.12(1) (2007) (allowing businesses to retain a percentage of the sales or use tax it collects). Businesses must bear the cost of the burdens related to complying with income tax laws themselves. Additionally, businesses like Sherwin-Williams bear the cost of the income tax out of their own capital, while merely remitting funds they collect from customers to pay the sales or use tax. Accordingly, a corporation's income tax expense is deducted from its overall earnings while amounts remitted as sales and use taxes are not. This is of particular importance to multistate businesses like Sherwin-Williams, because shareholders and other investors generally gauge a corporation's health by how much that corporation earns per share.

Shareholders and investors are concerned about a corporation's state income tax expense because that corporation's effective tax rate, the amount of recognized tax expense related to the income earned in a given year,[13] effects its earnings per share: the more income taxes a corporation is expected to pay per dollar of earnings the lower the earnings per share. Thus, shareholders and investors benefit from a precisely calculated effective tax rate because such gives them confidence in their ability to gauge the health of that corporation.

Besides benefits related to investor confidence, corporations benefit from a precisely calculated effective tax rate because such allows a corporation to know more precisely how much capital it will have available for investment, dividends, pension contributions, and salaries, as well as how its shares are priced on the public market. Lenders rely on this information to determine the corporation's debt-rating.

B. Compliance Burdens Related to Financial Accounting Rules Necessitate a Clear and Distinct Income Tax Nexus Rule.

In today's business climate, more than any other time, a bright-line income tax nexus rule is critical to the free flow of interstate commerce. Now, more than ever, multistate businesses must have the ability to determine their income tax expense as precisely as possible. To address recent financial reporting scandals and to better ensure that corporate financial

[13] The effective tax rate is calculated as the year's recognized tax expense divided by the year's profits before tax.

statements are worthy of investors' reliance,[14] Congress, the SEC, and FASB have increased their regulation and scrutiny of financial reporting. A bright-line physical presence rule would further the aims of Congress, the SEC, and FASB in the area of financial accountability by facilitating a more precise determination of multistate corporations' state income tax expenses and effective tax rates, while the current uncertainty surrounding state income tax nexus thwarts their aims.

Of particular relevance is a recent FASB pronouncement, FIN 48. By way of background, FASB is charged with promulgating corporate accounting rules that are binding on businesses like Sherwin-Williams. One such rule is FASB Statement No. 109 *Accounting for Income Taxes* ("FAS 109"). FAS 109 provides guidelines for reporting the estimated amount of income taxes payable or refundable in a current tax year. In 2006, FASB clarified FAS 109 by issuing FIN 48 to address problems related to accounting for contingent income tax benefits.

FIN 48 limits the income tax benefits a corporation can recognize on its financial statement to those arising from tax positions "more likely than not" to ultimately be sustained. For purposes of FIN 48, an income tax position is more likely than not to be

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[14] Shareholders and other investors rely on a corporation's financial information including its reported income tax expense and effective tax rate to measure the health of that corporation.

sustained if it has a greater than 50% likelihood of being sustained on audit. The more-likely-than-not standard simply determines whether the benefit may be reported on the financial statement at all. If the benefit does not meet the more-likely-than-not threshold the company may not recognize a single dollar of the benefit on its financial statement.

If the benefit meets the more-likely-than-not standard, the company still will likely not be able to report the entire benefit on its financial report. Instead, the company may only include the portion of that benefit that is more likely than not to be sustained on audit. The company determines the reportable portion through the use of a complicated probability analysis and must make detailed disclosures of its analysis. In most cases, the end result is that companies will be able to report only a fraction of the tax benefits they expect during the tax year.

FIN 48 also requires that a corporation report potential penalties related to its tax positions as a tax liability, off-setting the benefit of that position, unless the corporation meets the statutory requirement for waiver of that penalty. In the context of state tax, this sometimes means that all potential penalties must be included on the financial statement as a liability because there is no statutory provision for waiver of that penalty.[15] This is particularly onerous because

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[15] In Alaska, for example, penalties may only be waived in the discretion of the Department of Revenue or the Attorney

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under current conditions, as discussed above, states may potentially impose enormous penalties on corporations with no physical presence within the state.

For these reasons, the ambiguity surrounding the issue of state income tax nexus interferes with corporations' abilities to conduct themselves in the interstate marketplace. The more uncertainty surrounding an income tax position, the less likely it is that a corporation may recognize the benefit from such a position on its financial statement under FIN 48. As a result, the financial statement may reflect lower earnings per share than reality dictates. Combined with the fact that FIN 48 also requires that corporations reserve for potentially enormous penalties resulting from this uncertainty, until the law in this area is clear, corporations will also likely have less available capital for investment. Finally, the potential liability for incalculable back taxes, interest and substantial underpayment penalties, alone, is enough for businesses to think twice before expanding operations interstate.

A clearly articulated physical presence rule for state income tax nexus would go a long way to furthering the ends of FIN 48. Such a rule would reduce uncertainty related to multistate businesses'

General. ALASKA STAT. § 43.05.070 (2006). Therefore, there is no statutory provision for waiver of the penalty and a company must account for all potential Alaska penalties on its financial report.

state income tax positions resulting in a more realistic report of multistate corporations' income tax expense, effective tax rate, and earnings per share.

CONCLUSION

For these reasons, The Sherwin-Williams Company respectfully requests that this Court grant Geoffrey, Inc.'s petition for a writ of certiorari and reverse the decision of the Supreme Judicial Court of Massachusetts.

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