**COMMONWEALTH OF MASSACHUSETTS**

**APPELLATE TAX BOARD**

**BAY STATE GAS COMPANY v. COMMISSIONER OF REVENUE**

**AND AFFILIATES**

Docket No. C332071 Promulgated:

 October 23, 2018

This is an appeal filed under the formal procedure pursuant to G.L. c. 58A, § 7 and G.L. c. 62C, § 39, from the refusal of the Commissioner of Revenue (“Commissioner”) to abate corporate excise, interest, and penalties assessed to Bay State Gas Company and Affiliates (“appellant”) for the tax years ended December 31, 2012 through December 31, 2014 (“tax years at issue”).

Chairman Hammond heard the appellant’s Motion for Summary Judgment and the Commissioner’s Cross Motion for Summary Judgment and was joined by Commissioners Scharaffa, Rose, Chmielinski, and Good in the decision for the Commissioner in part, denying the abatement of corporate excise, and for the appellant in part, granting an abatement of penalties.

These findings of fact and report are made pursuant to requests by both the appellant and the Commissioner under G.L. c. 58A, § 13 and 831 CMR 1.32.

*Richard C. Call*,Esq*.* and *Scott M. Susko*, Esq. for the appellant.

*Brett M. Goldberg*,Esq*.* and *Yuliya Kuzovkova*, Esq. for the Commissioner.

**FINDINGS OF FACT AND REPORT**

This appeal was presented through pleadings and the parties’ Motion and Cross Motion for Summary Judgment with accompanying memoranda and documents. The primary issue was whether the Indiana utility receipts tax (“URT”), imposed pursuant to Ind. Code § 6-2.3-2-1, is disallowed as a deduction for purposes of computing Massachusetts net income under G.L. c. 63, § 30(4)(iii) (“URT Issue”). The Appellate Tax Board (“Board”) also considered the issue of penalties (“Penalties Issue”), specifically whether the Commissioner could propound alternative grounds for penalties under G.L. c. 62C, § 35A and § 35D, as well as the substantive propriety of imposing penalties in this matter. On the basis of the foregoing, the Board made the following findings of fact relevant to the issues in this case.

**I. Procedural History**

 The appellant conducted a natural gas distribution operation in Massachusetts and was subject to the Massachusetts corporate excise during the tax years at issue. The appellant filed a Form 355U: Excise for Taxpayer Subject to Combined Reporting for each of the tax years at issue. The Commissioner issued a Notice of Intent to Assess for the tax years at issue on June 2, 2016 and a Notice of Assessment on August 11, 2016, assessing additional corporate excise, interest, and penalties. The appellant filed a Form ABT: Application for Abatement on October 6, 2016, which the Commissioner denied on December 6, 2016. The appellant timely filed a petition with the Board on February 2, 2017. Based on the foregoing, the Board found and ruled that it had jurisdiction to hear and decide this appeal.

**II. The Board’s Findings**

 Two of the affiliates included in the appellant’s combined group were utility companies that operated in Indiana during the tax years at issue and so they were subject to and paid Indiana adjusted gross income tax pursuant to Ind. Code § 6-3-2-1 as well as the URT pursuant to Ind. Code § 6-2.3-2-1. For retail sales of gas and electricity in Indiana during the tax years at issue, Indiana gross retail tax pursuant to Ind. Code § 6-2.5-2-1 was generally collected by the appellant and this tax was separately stated in bills to customers. The URT was not separately stated in bills to customers during the tax years at issue. The appellant added back the URT to its net income for Indiana tax purposes. For Massachusetts corporate excise purposes, the appellant claimed deductions for the URT, but not for the Indiana adjusted gross income tax.

The URT deductions formed the basis of the Commissioner’s assessments of the tax and penalties at issue in this matter. The Commissioner disallowed the URT deductions under G.L. c. 63, § 30(4)(iii). The Commissioner also assessed penalties pursuant to G.L. c. 62C, § 35A, but then sought to add — by way of a Motion to Amend his answer — G.L. c. 62C, § 35D as an alternative basis for the assessment of penalties.

As discussed further in the Opinion below, the Board found and ruled that though the URT has some characteristics of a transaction-based tax, on balance the URT more strongly resembles “taxes on or measured by income, franchise taxes measured by net income, franchise taxes for the privilege of doing business and capital stock taxes imposed by any state,” the types of tax disallowed as deductions under G.L. c. 63, § 30(4)(iii), and so the appellant was not entitled to an abatement on the URT Issue.

Regarding the Penalties Issue, the Board found that the Commissioner cannot advance G.L. c. 62C, § 35A and § 35D penalties as alternative justifications for a penalty that the Commissioner had already imposed under § 35A. Each section outlines a specific predicate and calculation for the imposition of penalties. The Commissioner cannot decide at the litigation stage of these proceedings that he could have assessed a different penalty than the one he had already assessed. Moreover, the Board found that the penalties assessed under G.L. c. 62C, § 35A were not warranted since the appellant — though ultimately incorrect in its filing position on the URT Issue — had reasonable cause for underpayment of the contested portion of tax. The language of G.L. c. 63, § 30(4)(iii) and the Department of Revenue’s Directives 99-9: Disallowance or “Add-back” of the Deduction for Certain State Taxes to Corporate Net Income (“Directive 99-9”) and 08-7: Gross Receipts-Based Taxes - Disallowance of Both the G.L. c. 62, s. 6(a) Credit and the G.L. c. 63, s. 30.4 Deduction for Taxes Paid to Another Jurisdiction (“Directive 08-7”) do not clearly dictate the resolution of the URT Issue. Notably, the Commissioner evidenced inconsistency and a lack of clarity on the URT Issue, initially maintaining that the URT is an income tax during the audit and abatement stages and then maintaining instead that the URT is a franchise tax during the appeal before the Board.

Accordingly, the Board granted the Commissioner’s Cross Motion for Summary Judgment in part, denying the abatement of corporate excise, and granted the appellant’s Motion for Summary Judgment in part, abating penalties under G.L. c. 62C, § 35A.

**OPINION**

Pursuant to Rule 22 of the Board’s Rules of Practice and Procedure, “[i]ssues sufficient in themselves to determine the decision of the Board or to narrow the scope of the hearing may be separately heard and disposed of in the discretion of the Board.” 831 CMR 1.22. The Board found and ruled that this appeal presented no genuine issue of material fact. Accordingly, the Board ruled that disposition of this appeal by summary judgment was appropriate pursuant to 831 CMR 1.22. *See* ***Correllas v. Viveiros***, 410 Mass. 314, 316 (1991) (“The purpose of summary judgment is to decide cases where there are no issues of material fact without the needless expense and delay of a trial followed by a directed verdict.”).

**I. The URT Issue**

The provisions of G.L. c. 63, § 30(4) state that the term “net income” comprises “gross income less the deductions, but not credits, allowable under the provisions of the Federal Internal Revenue Code.” However, the statute enumerates items for which a deduction is disallowed, including “taxes on or measured by income, franchise taxes measured by net income, franchise taxes for the privilege of doing business and capital stock taxes imposed by any state.” G.L. c. 63, § 30(4)(iii). The primary question in this matter is whether the URT is a tax for which a deduction is disallowed under G.L. c. 63, § 30(4)(iii).

 Pursuant to Ind. Code § 6-2.3-2-1:

An income tax, known as the utility receipts tax, is imposed upon the receipt of:

(1) the entire taxable gross receipts of a taxpayer that is a resident or a domiciliary of Indiana; and

(2) the taxable gross receipts derived from activities or businesses or any other sources within Indiana by a taxpayer that is not a resident or a domiciliary of Indiana.

Ind. Code § 6-2.3-2-1. The term “gross receipts” is defined as “anything of value, including cash or other tangible or intangible property, that a taxpayer receives in consideration for the retail sale of utility services for consumption before deducting any costs incurred in providing the utility services.”

Ind. Code § 6-2.3-1-4. The term “taxable gross receipts” is defined as “the remainder of: (1) all gross receipts that are not exempt from tax under IC 6-2.3-4; less (2) all deductions that are allowed under IC 6-2.3-5.” Ind. Code § 6-2.3-1-9. Utility services include electrical energy, natural gas, water, steam, sewage, and telecommunication services. Ind. Code § 6-2.3-1-14.

In determining whether the URT is disallowed under G.L. c.  63, § 30(4)(iii), the label given to the tax by the Indiana statute is not controlling; rather, the essential query before the Board is whether it is one of the types of tax covered by G.L. c. 63, § 30(4)(iii). *See* ***Liberty Mutual Insurance Co. v. Commissioner of Revenue***, 405 Mass. 352, 356 (1989) (ruling that the reviewing court must “carefully look[] behind the labels of the State statute to determine whether” a tax falls under a statute that covers certain types of tax) (citing ***Commissioner of Revenue v. Massachusetts Mutual Life Insurance Co.***, 384 Mass. 607 (1981)).Directive 99-9 further states that “[t]he legislature has not statutorily identified specific taxes of other states that must be added back. Instead, it has chosen broad language to describe the *types* of state tax that must be added back in calculating Massachusetts corporate net income.” Directive 99-9 provides categories of taxes that are disallowed as deductions, including those that tax “a corporation’s business activity (the privilege of doing business).”

Here, while the URT may have some characteristics of a transaction tax, as contended by the appellant, such as an exemption for occasional sales and an exemption for sales transactions with the U.S. government, *see* Ind. Code § 6-2.3-4-4 and Ind. Code § 6-2.3-4-1, on balance the URT is more akin to “taxes on or measured by income, franchise taxes measured by net income, franchise taxes for the privilege of doing business and capital stock taxes imposed by any state,” the types of tax disallowed by G.L. c. 63, § 30(4)(iii).

The URT is not imposed strictly upon receipts from sales, but also upon legal settlements and judgments pursuant to Ind. Code § 6-2.3-3-3, thus more indicative of a tax measured by income. Indiana has a sales tax pursuant to Ind. Code § 6-2.5-2-1 that is similar to the Massachusetts sales tax statute at G.L. c. 64H, and the appellant collects this Indiana sales tax at 7 percent on utility sales. Ind. Code § 6-2.5-2-2. The particular language of the URT statute (imposed upon the “receipt of” taxable gross receipts rather than “imposed on retail transactions” as in the Indiana sales tax statute) more strongly suggests that the URT uses the receipts on sales as a measurement indicator for the privilege of doing business as a utility company and not as a means of directly taxing individual transactions for a transaction-based tax like the sales tax. Moreover, the URT is paid in minimum quarterly payments of estimated tax liability, similar to the collection of income tax from corporations in Massachusetts, which is also paid in quarterly payments of estimated taxes. Ind. Code § 6-2.3-6-1; G.L. c. 63B, § 3; Form URT-2220: Underpayment of Estimated Utility Receipts Tax (“Form URT-2220”). Underpayments of the quarterly estimated liability for the URT incur a penalty of 10 percent of the total quarterly underpayments. *See* Form URT-2220. Massachusetts also imposes an additional amount on underpayments of estimated taxes. G.L. c. 63B, § 3; G.L. c. 62C, § 32. The method of collection of the URT and the penalty on underpayments is similar to the collection and penalization on underpayments of corporate income tax in Massachusetts.

Further, the Board agreed with the Commissioner’s argument that relevant language in Ind. Code § 6-2.3-8-2, specifically that “the tax imposed by this article is in addition to all other licenses and taxes imposed by law as a condition precedent to engaging in any business, privilege, occupation, or activity that is taxable under such other license or tax,” makes clear that the URT is a tax on the privilege of doing business. The word “other” in this phrase demonstrates that the URT is itself one of the other taxes imposed “as a condition precedent” to the privilege of doing business.

The appellant, on the other hand, interpreted the “all other licenses and taxes” language as being the exclusive “condition precedent,” and interpreted that the URT is not part of that group of “all other licenses and taxes imposed by law as a condition precedent.” Thus, the appellant asserts that the URT is not a “condition precedent” tax, unlike the others. The Board rejected this strained reading of the statutory language.

Statutory language must be “construed according to [its] natural and ordinary meaning” upon a plain reading. ***Chatham Corporation v. State Tax Commission***, 362 Mass. 216, 219 (1972); *see also* ***Bronstein v. Prudential Ins. Co.****,* 390 Mass. 701 (1984). The Supreme Judicial Court also provided that “[a] statute or ordinance should not be construed in a way that produces absurd or unreasonable results when a sensible construction is readily available.” ***Manning v. Boston Redevelopment Authority,*** 400 Mass. 444, 453 (1987). Further, “[t]ax laws ‘should be construed and interpreted as far as possible so as to be susceptible of easy comprehension and not likely to become pitfalls for the unwary.’” ***Assessors of Brookline v. Prudential Ins. Co.***, 310 Mass. 300, 313 (1941) (quoting ***Hemenway v. Milton***, 217 Mass. 230, 233 (1914)). “[I]t is ‘[c]onspicuously important’ to construe the language of a tax law according to its ‘common and ordinary meaning.’” ***County of Middlesex v. Newton***, 13 Mass. App. Ct. 538, 542 (1982) (quoting C. Sands & N. Singer, ***Sutherland Statutory Construction*** 188 (4th ed. 1974)), *further appellate review denied*, 386 Mass. 1104 (1982).

In the present case, the Board determined that the “in addition to all other” language in Ind. Code § 6-2.3-8-2 encompassed the URT based upon a plain language reading of the statute. *See, e.g*., ***White v. Boston***, 428 Mass. 250 (1998). The plain language “the [URT] . . . is in addition to all other licenses and taxes imposed by law as a condition precedent” includes the URT in that group of “licenses and taxes imposed by law as a condition precedent.” Ind. Code § 6-2.3-8-2. The opposite conclusion, advanced by the appellant, that the URT is excluded from this group, would render the word “other” as superfluous.

The appellant also presented several constitutional arguments. It contended that disallowance of the URT deduction would be discriminatory by favoring in-state operations over out-of-state operations. The appellant also contended that G.L. c. 63, § 30(4)(iii) is unconstitutional as applied here because it applies to the transaction taxes of another state but not to the transaction taxes of Massachusetts. The Board determined that both constitutional arguments were without merit.

“A tax measure is presumed valid and is entitled to the benefit of any constitutional doubt, and the burden of proving its invalidity falls on those who challenge the measure.” ***Daley v. State Tax Commission***, 376 Mass. 861, 865–66 (1978). *See* ***Genentech, Inc. v. Commissioner of Revenue***, 476 Mass 258, 272 (2017) (“[W]hat the commerce clause forbids as discriminatory is a State tax measure that ‘tax[es] a transaction or incident more heavily when it crosses state lines than when it occurs entirely within the State.’”). General Laws c. 63, § 30(4)(iii) applies to any tax levied by any state, including Massachusetts, that falls under the types of tax that are disallowed under the statute. Every corporation that takes deductions for Massachusetts corporate excise purposes is treated the same. Further, the Board’s determination that the URT is not a transaction tax renders moot the appellant’s argument that the transaction taxes of Indiana versus Massachusetts are treated differently for purposes of G.L. c. 63, § 30(4)(iii).

Based upon the foregoing, the Board determined that while the URT has some characteristics of a transaction tax, on balance, more factors indicated that the URT is not a transaction tax, but rather a tax encompassing a tax type for which a deduction is disallowed under G.L. c. 63, § 30(4)(iii). Accordingly, the Board granted the Commissioner’s Cross Motion for Summary Judgment in part, and issued a decision in favor of the Commissioner on the URT Issue.

**II. The Penalties Issue**

The Commissioner assessed penalties under G.L. c. 62C, § 35A, but later sought to amend his answer to include G.L. c. 62C, § 35D as an alternative basis for penalties. General Laws c. 62C, § 35A and § 35D are not interchangeable methods of penalization. Each statute sets forth a specific mechanism for the calculation of penalties based upon differing scenarios triggering the penalty. General Laws c. 62C, § 35A is a 20 percent underpayment penalty, whereas G.L. c. 62C, § 35D is an inconsistent position penalty “equal to the amount of tax attributable to the inconsistency.” Notably, the penalty under G.L. c. 62C, § 35D “shall be in addition to all other penalties that may apply,” not in lieu of other penalties. The Commissioner may waive or abate a penalty but he cannot impose a penalty in his answer as an alternative to support the amount already assessed under G.L. c. 62C, § 35A, *i.e.*, the penalty is either imposed at the amount specified by the statute or not at all, not at or up to the amount assessed under another penalty statute.

Additionally, the Commissioner’s own guidance under Administrative Procedure 633 states as follows: “Penalties are not intended as a source of revenue. Rather, penalties are meant to provide taxpayers with an incentive to comply voluntarily with their tax obligations. To promote voluntary compliance, and to foster public confidence in the integrity and effectiveness of the taxation process, penalties must be administered in a fair and consistent manner.” Seeking to impose a penalty under a new section at this stage indicates a defensive, revenue-seeking motive rather than to promote voluntary compliance.

Regardless, the Board determined that the penalty imposed under G.L. c. 62C, § 35A was without merit. Pursuant to G.L. c.  62C, § 35B, “[a] penalty shall not be imposed under section 35A with respect to any portion of an underpayment if it is shown that there was reasonable cause for such portion and that the taxpayer acted in good faith with respect to such portion.” *See* Directive 12-7: Section 35A Penalty for Underpayment of Tax Required to Be Shown on Return; Technical Information Release 06-5: New Penalties Under G.L. c. 62C, §§ 35A-35E.

In this matter, while the Board found and ruled that the URT is a disallowed deduction under G.L. c. 63, § 30(4)(iii), the relevant legal provisions and the Commissioner’s public written statements do not clearly provide for the proper treatment of the URT. Directive 99-9 sets forth an illustrative list of state taxes subject to disallowance but acknowledges that “[t]he legislature has not statutorily identified specific taxes of other states that must be added back. Instead, it has chosen broad language to describe the *types* of state tax that must be added back in calculating Massachusetts corporate net income.” Directive 99-9; *see also* Directive 08-7. The Commissioner himself came to different interpretations, initially contending that the URT is an income tax and later contending that it is a franchise tax. If the answer were so apparent, the Commissioner’s position would have been consistent. Consequently, the Board granted the appellant’s Motion for Summary Judgment in part, granting an abatement on the Penalties Issue.

**CONCLUSION**

Based upon the foregoing, the Board found and ruled that the URT falls within a tax type for which a deduction is disallowed under G.L. c. 63, § 30(4)(iii). The Board also found and ruled that the Commissioner was not allowed to contend that G.L. c. 62C, § 35A and § 35D are alternative methods of penalization, and that imposition of penalties under G.L. c. 62C, § 35A was improper regardless. Accordingly, the Board issued a decision for the Commissioner in part, denying an abatement of corporate excise on the URT Issue, and for the appellant in part, abating penalties on the Penalties Issue.

**THE APPELLATE TAX BOARD**

 **By: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

 **Thomas W. Hammond, Jr., Chairman**

**A true copy,**

**Attest: \_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_\_**

 **Clerk of the Board**