COMMONWEALTH OF MASSACHUSETTS

APPELLATE TAX BOARD

SYNQOR, INC. **v.** **COMMISSIONER OF REVENUE**

Docket No. C331460

Promulgated:
October 2, 2019

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" or "appellee") to grant an abatement of corporate excise tax assessed to SynQor, Inc. ("SynQor" or "appellant") under G.L. c. 63, § 38 in effect for tax year 2011 and tax year 2013 ("tax years at issue").

Commissioner Scharaffa heard this appeal and was joined in the decision for the appellee by Chairman Hammond and Commissioners Rose, Good, and Elliott.

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

Nelson G. Apjohn, Esq., *Nehal Khorraminejed*, Esq., and *Philip S. Olsen*, Esq. for the appellant.

Frances M. Donovan, Esq., *Marikae Grace Toye*, Esq., and *Michael Clifford*, Esq. for the appellee.

FINDINGS OF FACT AND REPORT

Based on the evidence entered into the record, the Appellate Tax Board ("Board") made the following findings of fact.

I. INTRODUCTION AND JURISDICTION

At all times relevant to this appeal, the appellant was a Delaware corporation whose principal place of business was in Boxborough, Massachusetts. The appellant's business consisted of the design, manufacture, and sale of power converters and systems and it was classified as a manufacturing corporation for Massachusetts corporate excise purposes for the tax years at issue.

The appellant owned certain patents that it utilized in connection with its business ("intellectual property"). Prior to the tax years at issue, the appellant brought suit ("Federal litigation") in the United States District Court for the Eastern District of Texas ("Federal District Court") seeking damages for the unauthorized use of the intellectual property. As a result of the Federal litigation, the appellant recovered damages from defendants ("litigation awards") and received settlement payments from certain defendants ("settlement payments"). In addition, the appellant received royalties from customers of certain defendants after an injunction was issued in the Federal litigation ("injunction") prohibiting the defendants from selling products containing the appellant's intellectual property without the appellant's permission ("authorization royalties").

The issue in this appeal is whether G.L. c. 63, § 38(f) and 830 CMR 63.38.1(9)(d)(3)(f) as in effect during the tax years at issue require that the litigation awards, settlement payments, and authorization royalties (collectively "receipts at issue") be attributed to Massachusetts based on the appellant's commercial domicile here as the Commissioner argued or, as the appellant maintained, require that only a percentage of the receipts at issue be apportioned to Massachusetts.

For the tax years at issue, the appellant filed Massachusetts corporate excise tax returns on Form 355. On these returns, the appellant attributed the receipts at issue to Massachusetts by including them in both the numerator and the denominator of its sales factor.[1] Subsequently, the appellant filed with the Commissioner abatement applications for tax years 2011 and 2013 on September 11, 2015 and September 25, 2015, respectively. In each application, the appellant sought a reduction in its tax liability by including only a portion of the receipts at issue in the numerator of its sales factor.

[1] On its tax year 2012 return, the appellant also included the receipts at issue in both the numerator and the denominator of its sales factor. Because the appellant withdrew its appeal of tax year 2012, that year is not before the Board.

By Notices of Abatement Determination dated May 24, 2016, the Commissioner denied the abatement applications for the tax years at issue. On July 15, 2016, the appellant timely filed its petition with the Board. Based on the foregoing facts, the Board found and ruled that it had jurisdiction to hear and decide this appeal for the tax years at issue.

II. FACTUAL BACKGROUND

The evidence in this appeal consisted almost entirely of the parties' Agreed Statement of Facts, exhibits, and the testimony of a single witness, Arthur R. Hofmann, Jr. At the time of the hearing of this appeal, Mr. Hofmann was the Chief Financial Officer, Executive Vice President, and General Counsel of SynQor. During the tax years at issue, he served as Executive Vice President and General Counsel of SynQor.

A. The Appellant's Business

The appellant sold the products it manufactured to customers throughout most of the continental United States and in countries around the world. Its customers included the military, avionics, transportation, medical, industrial, telecommunications, and computing markets. All of the appellant's manufacturing activities were conducted in Massachusetts.

Mr. Hofmann testified that the appellant typically negotiated agreements with its customers and sold products directly to them or their contract manufacturers. During the tax years at issue, the appellant derived all of the income from the operation of its business from product sales. Mr. Hofmann testified that, apart from the activities discussed below that the appellant engaged in as a result of the Federal litigation, it was not engaged in the licensing of its intellectual property to third parties during the tax years at issue.

B. The Federal Litigation

The decision to file the Federal litigation in Texas was made by Mr. Hofmann and the individual whose efforts gave rise to the intellectual property ("inventor"), both of whom normally worked out of the appellant's Massachusetts office. They hired attorneys who were based in Illinois and Texas to represent the appellant in the Federal litigation. The appellant's litigation costs were paid out of the appellant's Massachusetts office. Mr. Hofmann and the inventor traveled to Texas for about one month prior to trial where they continued to make key decisions in connection with the Federal litigation.

Mr. Hofmann testified that most of the appellant's claims were for inducement to infringe its intellectual property rights, although the appellant also brought claims for direct infringement. He testified that the infringement period for damages began on July 4, 2006, when the first patent involved in the Federal litigation was issued, and continued until January 24, 2011, when a permanent injunction was issued by the Federal

District Court (the "Infringement Period"). According to Mr. Hofmann, pre-verdict and post-verdict supplemental damages in the case were measured starting from November 1, 2010, the cutoff for pre-trial discovery.

The defendants in the Federal litigation were commercially domiciled in California, Georgia, Massachusetts, New Jersey, Oregon, Pennsylvania, Texas, Washington, France, Japan, and Taiwan. Mr. Hofmann testified that, because of a protective order issued by the Federal District Court ("protective order"), the defendants were allowed to withhold from the appellant information concerning the defendants' customers who purchased infringing products, including where the defendants' sales took place and where their customers used the infringing products. The protective order was issued in response to a motion by the defendants who, as competitors of the appellant, wanted to protect the identity of the defendants' customers and other business and sales data from disclosure to the appellant.[2]

1. Litigation Awards

The jury awarded an amount for lost profits and, separately, a reasonable royalty for infringement of the intellectual property. According to Mr. Hofmann, lost profits were awarded if

[2] The Board observed that some customers of the defendants became known to the appellant because some of them paid authorization royalties directly to the appellant. Also, Mr. Hofmann testified that some of the defendants' customers were existing customers of the appellant.

the appellant had a comparable product to sell; if not, the jury award was based on a statutory theory providing no more than a reasonable royalty based on 50 percent of lost profits and a minimum award of $12.00. Mr. Hofmann did not cite a statutory basis for these awards.

Additionally, the Federal District Court awarded pre-verdict and enhanced post-verdict supplemental damages, additional damages, civil contempt sanctions, costs, attorneys' fees, and interest. As described in the Federal District Court's final judgment, the supplemental damages were compensation for the defendants' induced and contributory infringement of the appellant's intellectual property. The court also awarded additional damages against one defendant who omitted certain sales from sales data that it provided to the appellant in discovery. In his testimony, Mr. Hofmann stated that other additional damages were awarded for the same reason.

Mr. Hofmann testified that the litigation awards were paid in 2013 after the decision of the Federal District Court was affirmed on appeal and certiorari to the United States Supreme Court was denied. The following table shows the amounts of the litigation awards together with the portion of the awards paid by entities commercially domiciled in Massachusetts.[3]

[3] As described below, one of the appellant's apportionment methods is based on the commercial domiciles of the defendants.

Description	Amount Paid in 2013	Portion Paid by Entity Commercially Domiciled in Massachusetts
Lost profits awarded by the jury	$65,365,498.00	$17,113,179.00
Reasonable royalties awarded by the jury	$6,029,528.00	$817,433.00
Additional damages, and pre-verdict and enhanced post-verdict supplemental damages	$11,802,640.00	$2,681,920.75
Civil contempt sanctions due from one defendant	$500,000.00	0
Attorneys' fees due from one defendant	$60,000.00	0
Pre-judgment interest	$1,051,030.00	$287,256.00
Costs	$338,785.67	$37,642.85
TOTAL LITIGATION AWARDS	**$85,147,481.67**	**$20,937,431.60**

2. Settlement Payments

The appellant reached separate agreements with two of the defendants in the Federal litigation, both of whom agreed to make an additional payment to the appellant within thirty days of a final, non-appealable decision in favor of the appellant in the Federal litigation. One agreement, dated July 20, 2011, concerned additional sales by a Massachusetts-domiciled defendant of products that arguably infringed on one of the appellant's patents. The other agreement, dated April 25, 2012, was based on a failure by a non-Massachusetts defendant to provide sales data that should have been included in discovery. The payments under these agreements, equal to $25,594 and $17,391, respectively, were made to the appellant in 2013.

The appellant also entered into two other agreements: (1) a settlement and license agreement that called for a payment for past damages in the amount of $6,000,000 in 2011 and a royalty payment of $209,978 in 2013 from a defendant commercially domiciled outside of Massachusetts; and (2) a settlement agreement calling for a payment of $4,100,000 from a defendant commercially domiciled in Massachusetts.

Except for the $6,000,000 settlement paid in 2011, all settlement payments were made in 2013. The following table reflects the settlement payments made in 2011 and 2013 based on the parties' Agreed Statement of Facts and the appellant's Exhibit 47.

Description	Amount Paid in 2011	Amount Paid in 2013
Payments pursuant to 7/20/11 agreement with Massachusetts-domiciled defendant	0	$17,391
Payments pursuant to 4/25/12 agreement with a non-Massachusetts defendant	0	$25,594
Payment pursuant to a settlement agreement with a Massachusetts-domiciled defendant		$4,100,000
Payment for past damages pursuant to a settlement and license agreement with a non-Massachusetts defendant	$6,000,000	
Royalty payment pursuant to a settlement and license agreement with a non-Massachusetts defendant	0	$209,978
TOTAL SETTLEMENT PAYMENTS	**$6,000,000**	**$4,352,963**

3. Authorization Royalties

Mr. Hofmann testified that the appellant received a total of $2,059,044 in authorization royalties during tax year 2011 from the defendants' customers who purchased products that incorporated the appellant's intellectual property. The total amount of authorization royalties included $32,688 received from entities commercially domiciled in Massachusetts, or 1.59 percent of the total authorization royalties.

In its abatement application for tax year 2011, the appellant characterized the authorization royalties as proceeds from a litigation award. The appellant changed its argument during the Board proceedings and maintained that the authorization royalties were not a litigation award because they did not derive from the protection and enforcement of legal rights through litigation, arbitration, or settlement of legal disputes or claims, but should instead be treated as fees received from the licensing of intangible assets. The appellant argued that, therefore, only 1.59 percent of these payments, representing the percentage of authorization royalties received from entities that were commercially domiciled in Massachusetts, should be included in the numerator of its Massachusetts sales factor for tax year 2011.

C. The Appellant's Treatment of the Receipts at Issue

As previously noted, the appellant filed its tax returns for the tax years at issue by including the receipts at issue in both the numerator and the denominator of its sales factor. In its abatement application for the tax years at issue, the appellant maintained that the vast majority of these amounts were excludible from the numerator (but not the denominator) of its sales factor or, alternatively, were excludible from both the numerator and the denominator of its sales factor.

During the Board proceedings, the appellant focused on the nature of the rights enforced in the Federal litigation and argued that the receipts at issue were not entirely attributable to Massachusetts. It offered three apportionment methods and asked the Board to choose one.

1. First Apportionment Method

The appellant argued first that only the portion of the receipts at issue that was reflective of its "average Massachusetts sales factor" for the Infringement Period should be included in the numerator of its sale factor for each of the tax years at issue. Mr. Hofmann testified that the appellant reviewed its Massachusetts returns and sales reports for tax years 2006 through 2011 and determined that the average ratio of its Massachusetts sales to total sales for the Infringement Period was 12.443276 percent. Under this approach, the income measure of the appellant's corporate excise would have been $208,007 for tax year 2011 and $1,324,364 for tax year 2013.

2. Second Apportionment Method

As its second proposed apportionment method, the appellant argued that the receipts at issue should be apportioned as gross receipts from the licensing of intangible property. The appellant maintained that, had the defendant's use of the appellant's intellectual property been lawful, the licensing fees paid to the appellant would have been sourced to the commercial domiciles of the defendants in the absence of a showing that the intellectual property was used elsewhere. Since the protective order prevented the appellant and the Commissioner from offering evidence of where the infringing products were actually used, the appellant proposed apportioning the receipts at issue to the commercial domiciles of the defendants, the infringing parties, and including them in the numerator of its sales factor only to the extent that they were paid by entities domiciled in Massachusetts.

Under this second apportionment method, the income measure of the appellant's corporate excise would have been $196,292 for tax year 2011 and $1,992,994 for tax year 2013.

3. Third Apportionment Method

For its third and final apportionment method, the appellant argued that the receipts at issue should be excluded from both the numerator and the denominator of its sales factor, applying the approach taken in the Commissioner's apportionment regulation applicable in years after the tax years at issue. Mr. Hofmann testified that this approach would have resulted in an income measure of the appellant's corporate excise of $217,486 for tax year 2011 and $2,079,517 for tax year 2013.

The following chart shows the abatements calculated by the appellant that would be due under each of its three apportionment methods as set forth in the appellant's Exhibits 54 and 56:

Approach	**Abatement for 2011**	**Abatement for 2013**
Approach One: Applying Average Sales Factor	$76,589	$3,663,291
Approach Two: Based on Payors' Commercial Domicile	$88,304	$3,012,661
Approach Three: Approach taken in Regulation Effective After 2013	$67,110	$2,926,138

The Board observed that all of the amounts shown in the above chart exceeded the requested abatements listed in the appellant's Petition Under Formal Procedure filed with the Board.[4]

III. THE BOARD'S ULTIMATE FINDINGS

The Board found and ruled that the receipts at issue constituted gross receipts from the enforcement of legal rights and were therefore presumed to be attributable to Massachusetts based on the appellant's commercial domicile here in accordance with G.L. c. 63, § 38(f) and 830 CMR 63.38.1(9)(d)(3)(f) as in effect during the tax years at issue. The Board further found and ruled that the appellant failed to overcome this presumption.

The appellant sought to prove that at least one of its three proposed apportionment methods provided an adequate and reliable basis for apportioning an identifiable portion of the receipts at issue to out-of-state sources. The Board concluded that the appellant's first approach to apportionment, relying on its average percentage of total Massachusetts sales to worldwide sales during the Infringement Period, faltered on several grounds. First, the receipts at issue were not attributable solely to lost profits from lost sales. The receipts at issue included a significant amount for supplemental and additional damages, civil

[4] In its Petition, the appellant requested an abatement of $8,767 plus interest for tax year 2011 and an abatement of $2,465,542 plus interest for tax year 2013.

contempt sanctions, costs, attorneys' fees, and settlement payments, none of which were characterized as, or were by their nature, awards for lost profits. The receipts at issue also included reasonable royalties that the appellant provided no sufficient basis for treating as the equivalent of lost profits. In support of its position, the appellant cited non-Massachusetts case law construing a provision of law different from that at issue in this appeal, case law determined by the Board to be inapplicable as detailed in the Opinion below.

Even if the receipts at issue were treated as payments for lost profits, the Board found the appellant's averaging approach to apportionment, based on its stated historic sales data, to be without merit. The jury awarded damages for lost profits on infringing sales made by the defendants to customers of the defendants, most of whom could not be identified due to the protective order. The locations of sales by the defendants to their customers could not reasonably be presumed based on the appellant's historic sales to its own customers during the Infringement Period, and there was no evidence establishing that the defendants' customers had the same locations as the appellant's customers.

The appellant's attempt to apportion the receipts at issue based on the commercial domiciles of the defendants is also without merit. In support of this argument, the appellant asked the Board to indulge in the fiction that, if the defendants had been entitled to use the appellant's intellectual property, they would have paid licensing fees to the appellant for such use. Had such licensing fees been paid, they would have been sourced to the defendants' commercial domiciles, the majority of which were out-of-state, resulting in the out-of-state sourcing of most of the receipts at issue.

This argument is without factual support. The appellant's business during the tax years at issue was the sale of products, not the licensing of intellectual property. The jury award for reasonable royalties comprised only a small portion of the litigation awards and was a "deemed royalty" based on the determination that the appellant did not sell a product comparable to the defendant's infringing product. Further, as detailed in the Opinion below, the appellant again supported its argument by relying on non-Massachusetts case law construing statutes and regulations different from those at issue in this appeal; accordingly, the Board considered them to be inapplicable.

The Board was also not persuaded by the appellant's attempt to rely on an apportionment provision that was not effective until after the tax years at issue in this appeal. For the reasons discussed in the Opinion below, the appellant is not entitled to the retroactive application of a method outlined in a regulation that was not effective during the tax years at issue, and the Commissioner's change of approach for years after those at issue due to a change in the law does not render unreasonable or arbitrary the approach applicable to the present appeal.

Finally, the Board agreed with the Commissioner that the authorization royalties were not derived from the appellant's licensing of intellectual property, but rather arose out of the patent infringement litigation. The appellant was not in the business of licensing its intangible property and its receipt of the authorization royalties was directly related to the injunction issued in the Federal litigation. Accordingly, the Board concluded that the authorization royalties were appropriately treated in the same manner as the litigation awards and settlement payments and were subject to apportionment as such.

The Board therefore found and ruled that, consistent with the position taken by the appellant on its Massachusetts corporate excise tax returns for the tax years at issue, the receipts at issue were properly includible in both the numerator and the denominator of the appellant's Massachusetts sales factor. Accordingly, the Board issued a decision for the appellee in this appeal.

OPINION

As a manufacturing corporation that had income from business activity taxable both within and without Massachusetts, the appellant was required to apportion its taxable net income for the tax years at issue using a single-factor formula, based entirely on its sales, rather than the three-factor formula based upon property, payroll, and sales factors. *See* G.L. c. 63, § 38(1)(2)(v). For each of the tax years at issue, the numerator of the appellant's sales factor was its sales in Massachusetts during the tax year and the denominator was its sales everywhere during the tax year. G.L. c. 63, § 38(f) ("§ 38(f)"). The statute defined sales to mean "all gross receipts" of a corporation, with the exception of certain listed items not relevant to these appeals. ***Id.***

For purposes of determining where a sale took place, §38(f) distinguished between sales of tangible personal property and other sales. It is not disputed that the receipts at issue in this appeal were "gross receipts" from sales "other than sales of tangible personal property" for purposes of § 38(f).

Relevant to this appeal, § 38(f) provided that sales other than sales of tangible personal property were in Massachusetts if:

> 1. the income-producing activity was performed in this commonwealth; or
>
> 2. the income-producing activity was performed both in and outside this commonwealth and a greater proportion of this income-producing activity was performed in this commonwealth than in any other state, based on costs of performance.[5]

[5] For tax years beginning on or after January 1, 2014, § 38(f) provides that a sale other than a sale of tangible personal property is a Massachusetts sale if the corporation's market for the sale is in Massachusetts.

I. THE COMMISSIONER'S APPORTIONMENT REGULATIONS

While § 38(f) was silent as to the meaning of "income-producing activity," the Commissioner promulgated a regulation to "elaborate further the meaning and proper application" of § 38(f) that "fleshe[d] out § 38(f) in several respects." ***Boston Professional Hockey Association v. Commissioner of Revenue,*** 443 Mass. 276, 280-81 (2005) (analyzing receipts from sales other than sales of tangible personal property under the Commissioner's "detailed regulations implementing the corporate excise tax and its apportionment formula").

Under the version of the implementing regulations applicable to the tax years at issue in this appeal ("apportionment regulations"), an "income-producing activity" for sales other than sales of tangible personal property was defined as a "transaction, procedure, or operation directly engaged in by a taxpayer which result[ed] in a separately identifiable item of income." 830 CMR 63.38.1(9)(d)(2). The apportionment regulations went on to "establish specific rules for use in determining when gross receipts arising from different types of 'income-producing activities' (occurring within or outside the Commonwealth) [were] properly apportioned to Massachusetts." ***Boston Professional Hockey Association,*** 443 Mass. at 282.

A. Protection or Enforcement of Legal Rights

The Commissioner maintained that one of those specific rules, 830 CMR 63.38.1(9)(d)(3)(f), governs this appeal by providing that:

> Income-producing activity includes the protection or enforcement of legal rights of a taxpayer through litigation, arbitration, or settlement of legal disputes or claims, including the filing and pursuit of claims under insurance contracts. Gross receipts from the enforcement of legal rights by taxpayers domiciled in Massachusetts are presumed to be attributable to Massachusetts regardless of the forum through which a claim may be pursued, unless the legal dispute or claim relates directly and exclusively to real or tangible personal property of the taxpayer located outside the Commonwealth. . . .

The Commissioner argued that the receipts at issue arose from the appellant's enforcement of legal rights in the Federal litigation and were therefore presumed to be Massachusetts sales under 830 CMR 63.38.1(9)(d)(3)(f). The Board agreed and ruled that the receipts at issue were derived from the Federal litigation and constituted "[g]ross receipts from the enforcement of legal rights" by the appellant. The receipts are therefore "presumed to be attributable to Massachusetts" under 830 CMR 63.38.1(9)(d)(3)(f) because: (1) the appellant was commercially domiciled in Massachusetts during the tax years at issue; and (2) the legal dispute or claim giving rise to the receipts did not relate to real or tangible personal property located outside of Massachusetts.

The appellant argued that this straightforward interpretation of 830 CMR 63.38.1(9)(d)(3)(f) would render it invalid as beyond the scope of § 38(f) because § 38(f) did not treat the enforcement of legal rights as a separate income-producing activity. This argument is without merit. Section 38(f) was silent on the question of what an income-producing activity was or how to determine where income-producing activities took place. The Supreme Judicial Court has recognized that the apportionment regulations "elaborate further the meaning and proper application" of the statute by establishing both a general rule that "fleshes out" the sparse statutory language and "specific rules for use in determining when gross receipts . . . are properly apportioned to Massachusetts." ***Boston Professional Hockey Association,*** 443 Mass. at 281-82. Given the statutory silence, the court and the Board each analyzed the receipts at issue in ***Boston Professional Hockey Association*** - like those in the present appeal - as receipts from sales other than sales of tangible personal property and applied the rules found in the apportionment regulations. ***Id.*** at 286.

The Board found no basis to conclude that the regulation applicable in this appeal was "in conflict with the statutes or exceed[ed] the authority conferred by the statutes" under which the Commissioner operated. *See* ***Duarte v. Commissioner of Revenue,*** 451 Mass. 399, 411 (2008). Rather, the regulation was within the Commissioner's statutory authority to "prescribe regulations . . .

not inconsistent with law, to carry into effect the provisions" of the taxing statutes. G.L. c. 62C, § 3.

B. Effect of the Regulatory Presumption

Given the Board's ruling that the receipts at issue were derived from the Federal litigation and constituted "gross receipts from the enforcement of legal rights" by the appellant, the receipts at issue are therefore "presumed to be attributable to Massachusetts" under 830 CMR 63.38.1(9)(d)(3)(f) for the reasons set forth above. The Commissioner argued that the only way for the appellant to rebut the regulatory presumption was to show that its legal claims related to real or tangible personal property located outside of Massachusetts. That interpretation is inconsistent with the plain words of the regulation and the well-established meaning of the term "presumption."

The operative language of 830 CMR 63.38.1(9)(d)(3)(f) provided that "[g]ross receipts from the enforcement of legal rights by taxpayers domiciled in Massachusetts are presumed to be attributable to Massachusetts . . . unless the legal dispute or claim relates directly and exclusively to real or tangible personal property of the taxpayer located outside the Commonwealth." The clear meaning of this provision is that the presumption at issue arises "unless" the legal dispute relates to real or tangible personal property located outside the Commonwealth. If a legal dispute relates to such property, no presumption arises.

Since, in the present case, the legal dispute did not relate to real or tangible personal property located outside of Massachusetts, the presumption arises. However, the existence of the presumption under 830 CMR 63.38.1(9)(d)(3)(f) is not, standing alone, dispositive in this appeal. In Massachusetts, a presumption is rebuttable upon a showing of evidence sufficient to overcome it. ***Williams v. American Honda Finance Corp.***, 479 Mass. 656, 662 (2018) (holding that "[a] presumption is an evidentiary tool that accepts a certain fact as proven in the absence of contradictory evidence" and "imposes a burden of production on a party as to some fact to be proved"). Even if a presumption is not by its express terms rebuttable, the Supreme Judicial Court has held that it is. ***M & T Charters, Inc. v. Commissioner of Revenue***, 404 Mass. 137 (1989); ***Minchin v. Commissioner of Revenue***, 393 Mass. 1004 (1984) (both dealing with a sales tax statute presuming tangible personal property brought into Massachusetts within six months of purchase to have been purchased for storage, use, or other consumption in Massachusetts).

The Commissioner's own regulations in effect for the tax years at issue also recognized a taxpayer's ability to rebut a regulatory presumption by defining the term "presumption" in the following manner:

> *Presumption*, a conclusion of law or fact that is assumed to apply to a taxpayer unless the Commissioner or the taxpayer affirmatively rebuts the presumption by

> presenting contrary evidence of the actual facts and circumstances applicable to the taxpayer.

830 CMR 63.38.1(2).

The Board concluded, therefore, that 830 CMR 63.38.1(9)(d)(3)(f) afforded the appellant an opportunity to rebut the regulatory presumption. However, the Board also ruled that none of the appellant's three methods of apportionment was supported by evidence sufficient to overcome the presumption, as discussed in the following section.

II. THE APPELLANT'S APPORTIONMENT METHODS

As an initial matter, a taxpayer has the burden of proving its right to an abatement, a burden that is "particularly heavy with respect to challenges to the apportionment of income under G.L. c. 63, § 38." ***Boston Professional Hockey Association,*** 443 Mass. at 285 (quoting ***Gillette Co. v. Commissioner of Revenue***, 425 Mass. 670, 679 (1997)). Further, a rebuttable presumption places the burden of rebuttal squarely on the taxpayer. ***The First Marblehead Corporation v. Commissioner of Revenue***, 470 Mass. 497, 506 (2015).

The Board examined each of the appellant's apportionment methods and ruled that the appellant had not rebutted the regulatory presumption in 830 CMR 63.38.1(9)(d)(3)(f), and had not met its burden of proving its entitlement to an abatement.

A. The Appellant's First Apportionment Method – Average Sales Factor

The appellant first argued that the receipts at issue were appropriately apportionable based on what it determined to be its average Massachusetts sales factor for the Infringement Period. In support of its position, the appellant cited a 2003 decision of the California State Board of Equalization ("California Board") in ***Appellant: Polaroid Corporation***, Case No. 62415, Cal. Tax LEXIS 188 (Cal. St. Bd. Eq., May 28, 2003), and a prior North Carolina case on which the California Board relied, ***Polaroid Corporation v. Offerman***, 349 N.C. 290 (1998). The California Board treated damages awarded by the United States District Court for the District of Massachusetts as a substitute for lost profits from sales and used Polaroid's average California sales factor during the infringement period to determine the amount of those sales that were attributable to California.

Decisions of courts and administrative bodies of other states addressing another state's laws shed little light on the interpretation of a specific and distinct Massachusetts statute and implementing regulations, particularly the Massachusetts corporate excise tax scheme and implementing regulations. ***Raytheon Co. v. Commissioner of Revenue***, 455 Mass. 334, 343 (2009) (citing ***Macy's East, Inc. v. Commissioner of Revenue***, 441 Mass. 797, 807 (2004)); see ***Borofsky's Case***, 411 Mass. 379, 381 (1991)

("Cases from other jurisdictions which tend to favor [a taxpayer] are not helpful because they have been decided under statutes which are dissimilar to ours.").

The issue in the present appeal involves the proper interpretation and application of the Massachusetts apportionment statute and the associated regulations that implemented and fleshed out that statute, including a regulatory rule specifically addressing the sourcing of litigation proceeds. Neither the California Board nor the North Carolina court on which it relied addressed the Massachusetts statute or a regulation similar to the regulation at issue in this appeal. Moreover, the California Board itself determined that its decision had no precedential value, even in California.[6]

Even assuming the decision of the California Board was somehow relevant to the present appeal, this Board found the decision to be clearly distinguishable on its facts. Unlike the damages awarded to Polaroid by the United States District Court for the District of Massachusetts, characterized by the California Board as the equivalent of lost profits from lost sales, the receipts at issue here were not attributable solely to lost profits. The litigation awards included a significant amount for supplemental and additional damages, civil contempt sanctions, costs, and

[6] The California Board's decision bears a notation that the decision is "not to be cited as precedent."

attorneys' fees, none of which were characterized as, or were by their nature, awards for lost profits. In addition, there were settlement payments and a jury award for reasonable royalties.

Further, even assuming that the receipts at issue could be characterized as lost profits, the Board found the appellant's apportionment approach based on its average sales factor to be unsupported. The jury awarded damages for lost profits on infringing sales made to customers of the defendants whose identities were not revealed due to the protective order. There was no showing that the defendants' customers were located in the same jurisdictions as the appellant's customers. Thus, there can be no logical inference that the appellant's average sales factor – based on the location of its own customers – provided a reasonable approximation of where lost profits from sales to the defendants' customers should be sourced.

The Board found and ruled, therefore, that the appellant's first proposed apportionment method did not offer an adequate and reliable basis for apportioning an identifiable portion of the receipts at issue to out-of-state sources.

B. The Appellant's Second Apportionment Method – Licensing Fees

In the alternative, the appellant sought to rebut the regulatory presumption by asserting that the receipts at issue should be apportioned as gross receipts from the licensing of intangible property. The appellant argued that, had the infringing parties' use of the appellant's intellectual property been lawful, they would have paid licensing fees to the appellant sourced to the commercial domiciles of the defendants. As noted above, the identities of the end-users – the defendants' customers – were protected by the protective order, so the locations of the actual use of the intellectual property were unavailable.

As it did to support its first proposed apportionment method, the appellant again cited case law from other jurisdictions to support this method. See ***Getty v. Commissioner***, 913 F.2d 1486, 1490 (9th Cir. 1990) (determining the tax consequences of a litigation award based on the nature of the underlying action); ***Pennzoil Co. v. Department of Revenue***, 332 Ore. 542, 547 (2001) (indicating that courts have determined "the tax consequences of income received through litigation or settlement [by asking]: 'In lieu of what were the damages awarded?'"); ***Milenbach v. Commissioner***, 318 F.3d 924, 932 (9th Cir. 2003) (determining the taxability of a settlement payment based upon the nature and basis of the recipient's claim). The appellant cited no Massachusetts authorities in support of its approach, and the Board found the authorities cited by the appellant to be of no precedential value for the reasons stated above.

Further, as a factual matter, only a small percentage of the receipts at issue were characterized as "reasonable royalties." Moreover, the appellant's second method ignored the uncontroverted evidence establishing that the appellant's business model during the Infringement Period and the tax years at issue involved the sale of its products, not the licensing of its intellectual property. The appellant simply presumed that, had the infringing parties' use of its intellectual property been lawful, the use would have been in the form of the licensing of intangible property, notwithstanding the appellant's actual business model during the Infringement Period.

The Board ruled, therefore, that the appellant's second proposed apportionment method also did not offer an adequate and reliable basis for apportioning an identifiable portion of the receipts at issue to out-of-state sources.

C. The Appellant's Third Apportionment Method – Later Regulatory Treatment

Finally, the Board was equally unpersuaded by the appellant's attempt to overcome the regulatory presumption by applying principles in an apportionment regulation not in effect for the tax years at issue.[7] The Board found that the approach to the apportionment of litigation proceeds taken in the Commissioner's regulation that took effect in 2014 could not inform the interpretation of the Commissioner's long-standing regulation in effect during the tax years at issue. The fact that the Commissioner changed the treatment of litigation proceeds after the tax years at issue due to a change in the law does not mean that the treatment prescribed in the regulation applicable to the tax years at issue was somehow flawed.

D. Characterization of the Authorization Royalties

The Board ruled finally that, like the litigation awards and the settlement proceeds, the authorization royalties were also receipts from the enforcement of legal rights through litigation or settlement. The authorization royalties were not derived from the appellant's licensing of intellectual property, as the appellant maintained, but rather were paid by third-party customers of the defendants in the Federal litigation to enable them to continue to purchase infringing products from the defendants. The authorization royalties would not have been paid

[7] For tax years beginning on or after January 1, 2014, the apportionment regulation promulgated by the Commissioner excludes, from both the numerator and denominator of the sales factor, "[r]eceipts attributable to the protection or enforcement of legal rights of a taxpayer through litigation, arbitration, or settlement of legal disputes or claims." *See* 830 CMR 63.38.1(9)(d)(7)(c) and (14), as in effect for tax years beginning after 2013.

had it not been for the litigation, and the Board found that they arose from the appellant's protection or enforcement of its legal rights through litigation or settlement of legal disputes or claims within the meaning of 830 CMR 63.38.1(9)(d)(3)(f). Therefore, the Board determined that the authorization royalties should be sourced in the same manner as the appellant's litigation awards and settlement payments.

III. CONCLUSION

Accordingly, the Board found and ruled that, pursuant to 830 CMR 63.38.1(9)(d)(3)(f) as in effect for the tax years at issue, the receipts at issue were properly includable in both the numerator and the denominator of the appellant's sales factor for each of tax years 2011 and 2013 because the appellant had not overcome the regulatory presumption sourcing them to Massachusetts. The Board therefore issued a decision for the appellee in this appeal.

THE APPELLATE TAX BOARD

By: ______________________________
Thomas W. Hammond, Jr., Chairman

A true copy,

Attest: ______________________________
Clerk of the Board