

NO. 08-1056

**IN THE
SUPREME COURT OF TEXAS**

**TGS-NOPEC GEOPHYSICAL COMPANY
d/b/a TGS-NOPEC CORPORATION,
*Petitioner,***

VS.

**SUSAN COMBS, SUCCESSOR-IN-INTEREST TO
CAROLE KEETON STRAYHORN, COMPTROLLER OF PUBLIC
ACCOUNTS AND GREG ABBOTT, ATTORNEY GENERAL OF TEXAS,
*Respondents.***

**On Petition from the Court of Appeals
for the Third Judicial District of Texas**

RESPONDENTS' BRIEF ON THE MERITS

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ATTORNEYS FOR RESPONDENTS

TABLE OF CONTENTS

Table of Contents..... i

Table of Authorities.....iii

Statement of Jurisdiction 1

Issues Presented

 The legislature amended the franchise tax statute to specifically include receipts from the use of a license in Texas as “business done in this state” for apportionment purposes. Does this amendment apply to receipts, collected from licensees, in cases where the licensed data is either mailed to a Texas address or billed to a Texas address? 1

 Was it reasonable for the Comptroller to treat the billing or shipping address of TGS’s customers as the location of use for apportionment purposes? 1

Statement of Facts 2

Apportionment Statutes & Rules in Effect for 1998 3

Summary of the Argument 4

Argument 5

I. TGS’s receipts from the issuance of non-exclusive geophysical data license are subject to apportionment as business in Texas, under the Texas Tax Code as amended by the Legislature in 1997 5

 A. Introduction to the franchise tax..... 5

 B. TGS’s arguments that the 1997 amendments do not apply to how geophysical license receipts are apportioned conflicts with the plain language of the statute and the legislative history of the amendments 6

 1. The 1997 amendments clearly evidence a change in standards..... 6

2.	The 1997 amendments apply to TGS’s license receipts	8
3.	TGS’s receipts are receipts from the use of a license	8
4.	The court of appeals did not create or apply a separate test for receipts from the use of a license	11
5.	Application of the Texas sourcing statute to receipts from the use of a license is not dependent on the frequency of payments	14
6.	TGS’s receipts are not “receipts from the sale of an intangible.”	15
II.	The 1997 amendments to the apportionment statutes are a clear and specific statutory departure from the location of payor rule; thus the legislative acceptance doctrine is not applicable.....	17
III.	The court of appeals did not err in holding that it was reasonable for the Comptroller to treat the shipping or billing address of TGS’s customers as the location of use for apportionment purposes.	21
A.	No genuine issue of material fact exists in this case	21
B.	The court of appeals decision does not establish or perpetuate either a “mailing address rule” or any other absolute standard for determining location of use	23
	Prayer	24
	Certificate of Service	25
APPENDIX		TAB
	Act of May 30, 1997, 75th Leg., R.S., ch. 1185, §§ 5-6, 1997 Tex. Gen. Laws 4569, 4569-70	A
	21 Tex. Reg. 11511 (November 26, 1996).....	B

INDEX OF AUTHORITIES

CASES

<i>Humble Oil & Refining Co. v. Calvert</i> , 414 S.W.2d 172 (Tex. 1967)	17, 18, 19
<i>Old Am. County Mut. Fire Ins. Co. v. Sanchez</i> , 149 S.W.3d 111 (Tex. 2004)	19
<i>Nordlinger v. Hahn</i> , 505 U.S. 1 (1992)	8
<i>Railroad Comm’n v. Humble Oil & Refining Co.</i> , 193 S.W.2d 824 (Tex. Civ. App. – Austin, 1946, writ ref’d n.r.e.)	22
<i>City of San Antonio v. City of Boerne</i> , 111 S.W.3d 22 (Tex. 2003).....	19
<i>Sharp v. House of Lloyd, Inc.</i> , 815 S. W.2d 245 (Tex. 1991)	17
<i>Tex. Workers’ Compensation Comm’n v. Garcia</i> , 893 S.W.2d 504 (Tex.1995)	8
<i>TGS-NOPEC Geophysical Co. v. Combs</i> , 268 S.W.3d 637 (Tex. App. – Austin 2008, pet. filed).....	11, 21, 22, 24

LEGISLATION

Act of May 30, 1997, 75th Leg., R.S., ch. 1185, §§ 5-6, 1997 Tex. Gen. Laws 4569, 4569-70	6, 7, 18
--	----------

STATUTES

Tex. Gov’t Code Ann. (West 1998) § 22.001	1
Tex. Tax Code Ann. (West 1998) § 111.008	21
§ 171.002	5
§ 171.101	5
§ 171.103	3, 4, 6, <i>passim</i>
§ 171.1032	3, 4, 6, <i>passim</i>
§ 171.109	23
§ 171.110	5
§ 171.153	5
§ 171.1532	5

Tex. Tax Code Ann. § 111.001 (West 2002)	2
Wis. Stat. § 71.25(9)(dj)	13

RULES

34 Tex. Admin. Code § 3.549(e)(30)(A)(iii) (1996).....	20
34 Tex. Admin. Code § 3.549(e)(30)(A)(iii) (1998).....	3, 8
34 Tex. Admin. Code § 3.557(e)(25)(A)(iii) (1998).....	3, 8
Rule 3.403(e)(11), 13 Tex. Reg. 2971 (June 14, 1988).....	20
21 Tex. Reg. 11511 (November 26, 1996).....	21

TEXAS ADMINISTRATIVE DECISIONS

Hearing No. 43,065, Compr. Publ. Acc'ts (2004), STAR 200409846H	23, 24
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TO THE HONORABLE SUPREME COURT OF TEXAS:

Respondents Susan Combs, Comptroller of Public Accounts of the State of Texas, and Greg Abbott, Attorney General for the State of Texas, (collectively, the Comptroller) respectfully file their Respondents' Brief on the Merits in response to the brief of Petitioner, TGS-NOPEC Geophysical Company d/b/a TGS-NOPEC Corporation (TGS).

STATEMENT OF JURISDICTION

The Court has jurisdiction under Tex. Gov't Code § 22.001 (a)(3) (construction of statutes) and (4) (state revenue). The Court does not have jurisdiction under § 22.001(a)(6) (important error), because the Court of Appeals did not commit any error that requires correction.

ISSUES PRESENTED

1) The legislature amended the franchise tax statute to specifically include receipts from the use of a license in Texas as "business done in this state" for apportionment purposes. Does this amendment apply to receipts, collected from licensees, in cases where the licensed data is either mailed to a Texas address or billed to a Texas address?

2) Was it reasonable for the Comptroller to treat the shipping or billing address of TGS's customers as the location of use for apportionment purposes?

STATEMENT OF FACTS

The Court of Appeals correctly stated the nature of the case. TGS is a Delaware corporation with a principal place of business in Houston, Texas. Clerk's Record (C.R.) 331. TGS performs geophysical seismic studies and licenses Texas and out-of-state exploration and production (E & P) companies to use the data to make prospecting decisions. C.R. 332. TGS is subject to franchise tax. Tex. Tax Code § 171.001(a)(1) (Vernon 2002). The contested gross receipts are revenue received from TGS's licensees in Texas. C.R. 126.

The Comptroller audited TGS and assessed additional franchise tax, penalty, and interest of \$1,757,570.89 for the 1997-2000 and 2001-2003 audit periods.¹ C.R. 129, 140, 310, 408. TGS paid taxes, penalty, and interest under protest, and timely filed this lawsuit. The assessments arose from TGS's failure to correctly apportion receipts from licenses.

TGS produced a summary report listing its Texas customers' shipping or billing addresses. C.R. 126. The Comptroller used the address to which data was mailed or billed to determine the location where it was used. C.R. 127.

¹ The statutory amendment at issue took effect on January 1, 1998, thus the Comptroller's assessment on the "location of use" issue did not include the 1997 tax year.

APPORTIONMENT STATUTES & RULES IN EFFECT FOR 1998

Sections 171.103 and 171.1032 of the Texas Tax Code apportion license receipts and provide, in relevant part:

In apportioning taxable capital, the gross receipts of a corporation from its business done in this state is the sum of the corporation's receipts from: . . . (4) the use of a patent, copyright, trademark, franchise, or license in this state; . . . and (6) other business done in this state. Tex. Tax Code § 171.103(4) and (6) (1998).

. . . [I]n apportioning taxable earned surplus, the gross receipts of a corporation from its business done in this state is the sum of the corporation's receipts from: . . . (4) the use of a patent, copyright, trademark, franchise, or license in this state; . . . and (7) other business done in this state. Tex. Tax Code § 171.1032(a)(4) and (7) (1998).

Rule 3.549 and Rule 3.557 of the Texas Administrative Code implement the apportionment statutes and provide, in relevant part:

(30) Patents, copyrights, and other intangibles. (A) Receipts from the use of intangible rights. . . (iii) For reports due prior to January 1, 1998, revenues received by the owner of a trademark, franchise, and license are apportioned to the location of payor. For reports due on or after January 1, 1998, revenues received by the owner of a trademark, franchise, or license are included in Texas receipts to the extent used in Texas. In regard to the sale/licensing of computer programs, paragraph (7) of this subsection is controlling. 34 Tex. Admin. Code § 3.549(e)(30)(A)(iii) (1998) (Taxable Capital: Apportionment).

(25) Patents, copyrights, and other intangible rights. (A) Revenues from the use of intangibles. . . (iii) Revenues received by the owner of a trademark, franchise, and license are included in Texas receipts to the extent used in Texas; however, in regard to the sale/licensing of computer programs, paragraph (6) of this subsection is controlling. 34 Tex. Admin. Code § 3.557(e)(25)(A)(iii) (1998) (Earned Surplus: Apportionment).

SUMMARY OF THE ARGUMENT

The case turns on whether revenues from licensing non-exclusive geophysical data to licensees located in Texas are Texas receipts, and, if so, whether franchise tax rules distinguishing between licenses and software are constitutional under the equal and uniform taxation requirements of the Texas Constitution. Tex. Tax Code Ann. §§ 171.103, .1032 (Vernon 1998-2003).²

TGS's statutory arguments are predicated on a fundamentally incorrect proposition that the location to which license receipts are apportioned is an open question. To the contrary, the franchise tax statute was expressly amended in 1997 to provide that revenues from licenses used in this state are Texas receipts beginning on January 1, 1998. §§ 171.103, .1032.

TGS's reliance on the legislative acceptance doctrine is misapplied. The 1997 amendments are a clear and affirmative statement of legislative intent to abandon the prior (location of payor) apportionment standard. A plain reading of the statute as amended indicates that revenues received from the use of a license in Texas are Texas receipts for franchise tax apportionment purposes. Comptroller rules and letter rulings based on the statute as it existed prior to the 1997 amendments are superseded by statute. To apply the legislative acceptance doctrine to the facts of this case would turn that principle on its head: defeating a

² Unless otherwise specified, references to the Tax Code will be to the statutes in effect from 1998-2003. Relevant statutes are in the Vernon 2002 volume. References to “§ 171.____” are to the franchise tax statute.

legislative act expressly amending a statutory definition, based solely on the existence of administrative rulings implementing a now repealed statute.

The court of appeals did not commit error in ruling that, *in the absence of other evidence*, Comptroller's use of TGS's customers' shipping or billing addresses for apportionment purposes was reasonable. TGS provided no contradicting evidence as to location of use of the licenses, but instead offers an alternative legal theory as to how the controlling statute should be construed. No genuine issue of material fact exists in this case.

ARGUMENT

I. TGS's receipts from the issuance of non-exclusive geophysical data license are subject to apportionment as business in Texas under the Texas Tax Code as amended by the Legislature in 1997.

A. Introduction to the franchise tax.

A franchise tax is imposed on a corporation's net taxable capital and earned surplus. § 171.002. Taxable capital is essentially net assets, and earned surplus is adjusted federal taxable income. §§ 171.101(a), .110(a).

Franchise taxes are based on Texas business done during the previous accounting year. §§ 171.153, .1532. Both of the tax bases are divided among Texas and other tax jurisdictions by multiplying them by an apportionment factor, the numerator of which is gross receipts from Texas business, and the denominator of which is gross receipts from business everywhere. Taxpayers generate gross

receipts by selling goods and services, receiving dividends and interest, realizing capital gains, and the like. §§ 171.103, .1032.

This case involves the size of the numerator, or how much of TGS's license revenue arises from business done in Texas.

- B. TGS's arguments that the 1997 amendments do not apply to how geophysical license receipts are apportioned conflicts with the plain language of the statute and the legislative history of the amendments.**
 - 1. The 1997 amendments clearly evidence a change in standards.**

Before 1998, license receipts were considered to be revenue from the sale of intangible property, or "other business done in this state. . ." and were apportioned to the location of the licensees' legal domiciles—the states in which they were incorporated. §§ 171.103, .1032; Petition for Review ("Pet.") Tabs 7 & 8. This standard bore no relationship to where licenses were used.

Since 1998, the franchise tax statute has provided that the "use of a patent, copyright, trademark, franchise, or **license in this state**" generates Texas receipts. §§ 171.103, .1032 (emphasis added). Pet. Tabs 9 & 10.

The 1997 amendments were enacted as Senate Bill 861 by the 75th Legislature, when the Comptroller sought legislation that would expressly apportion license, trademark, and franchise revenue to the place they are used, for both taxable capital and earned surplus. Act of May 30, 1997, 75th Leg., R.S.,

ch. 1185, §§ 5-6, 1997 Tex. Gen. Laws 4569, 4569-70 (effective January 1, 1998)(codified at § 171.103 and 171.1032(a)); C.R. 215-218; (Appendix A).³

The Comptroller’s fiscal note analysis for S.B. 861, prepared at the request of the Legislative Budget Board, states:

Current franchise tax law sources the receipts from trademarks, franchises, and licenses used in Texas to the state of legal domicile of the corporation remitting the payments. Patents and copyrights are sourced to Texas if the patent or copyrights are used in Texas. **This bill would equalize treatment among these types of similar intangible assets:** The receipts would be sourced to Texas if the assets were used in Texas. . . . The changes related to sourcing receipts from certain intangible assets would provide a small revenue gain. (emphasis added) Comptroller Fiscal Note Estimate, S.B. 861, 75th Leg., R.S. (1997); C.R. 220-222; Pet. Tab 16.

Thus, the legislature considered that patents, trademarks, copyrights, and licenses are “types of similar intangible assets.” A bill analysis prepared by the Senate Research Center states that S.B. 861 would make substantive changes to “deal with the apportionment of gross receipts from the use of trademarks, franchises, and licenses in Texas; . . .” C.R. 235-237; Pet. Tab 18, ¶ 1. Thus, the information provided to the legislature relating to the effect of S.B. 861 indicates that the legislature acted with an affirmative intent to change the apportionment of license receipts from “location of payor” to “place of use.”

The statute’s plain language and legislative history demonstrate that receipts from licenses, trademarks, and franchises were brought, for the first time, into the same fold as patents and copyrights. TGS may disagree with this policy

³ All references herein to “S.B. 861” or to the “1997 amendments” are references to this Act of the Legislature.

choice, but it was one the legislature had every right to make. *See Nordlinger v. Hahn*, 505 U.S. 1, 12 (1992); *see also, Tex. Workers' Compensation Comm'n v. Garcia*, 893 S.W.2d 504, 520 (Tex. 1995).

2. The 1997 amendments apply to TGS's license receipts.

TGS claims that the 1997 amendments do not encompass geophysical seismic data licenses, but there is no support for this claim because the statute does not qualify or in any way limit the term "license." TGS's contracts are styled as a "Master License Agreement for Geophysical Data," and TGS's customers are designated as "licensees" in the agreements. C.R. 179-181; Pet. Tab 3 (Master License Agreement for Geophysical Data).

TGS licenses the use of data to its licensees. The fees paid to TGS by its licensees are receipts to TGS. A plain reading of § 171.103(4) and § 171.1032(a)(4) indicates that these payments, received by TGS, are gross receipts generated from the use of a license.

3. TGS's receipts are receipts from the use of a license.

TGS argues that the sourcing statute cannot apply because it, TGS, is not the "owner" of the license, but instead its customers own the licenses. This argument attempts to defeat the statute through a misapplication of the Comptroller's sourcing rules. The Comptroller rules apply the sourcing statute to "revenues received by the owner of a ... license." Rules 3.549(e)(30) and 3.557(e)(25). TGS's argument would have the effect of making its customers the taxpayer for the purpose of the statute. However, TGS receives payment from its

customers for the use of intellectual property that it, TGS, owns. This fact brings TGS's receipts under the statute, without the need to determine whether a contractual agreement can be said to be "owned" by either party to the contract. While TGS asserts that its customers "own" the licenses, what the customers truly possess is the right to use TGS's data under the terms and limitations of the license agreement. TGS's brief at 8. C.R. 179-31; Pet. Tab 3 (Master License Agreement).

TGS further attempts to deconstruct the sourcing statute by arguing that neither TGS, nor its customers, really "use" the license and thus the receipts generated by TGS are not subject to the sourcing statute. TGS's brief at 7. TGS carries this argument to the next step by stating that the sourcing statute can only apply in cases where the "asset" being transferred is itself a license (i.e., in the sense of a sublicense). TGS's brief at 10. While it may be trivially true that TGS's customers are not using the license agreements *per se*, they are in fact using the underlying intellectual property. To adopt TGS's theory would eviscerate the statute, which uses the same construction for receipts generated from patents and copyrights as for licenses. § 171.103(4) and § 171.1032(a)(4).⁴ When the owner of a patent permits another party to use the process or formula protected by the patent, the permittee is not using the patent *per se*, but rather using the protected formula or process. Under TGS's theory, receipts from the use of a patent in this

⁴ TGS adopts the convention of referring to both of these provisions collectively as "subsection (4)." TGS's brief at 8. Respondents' brief will use this convention as well.

state would not be sourced by location of use, but rather would be sourced to the location of payor.

The first analogy provided by TGS, on page 11 of its brief, serves to illustrate the above point. TGS's "analogy no. 1," as laid out in its brief, reads as follows:

A owns a patent. B wants to manufacture the patented item. A does not want to convey the patent to B, so A grants B a license to use the patent. When B manufactures the patented item, B uses the patent. Periodic payments from B to A based upon the number of items manufactured using the patent are receipts for the use of a patent.

If B is merely manufacturing the patented item in analogy no. 1 above, it is not using the patent. Instead, B can be said to use the patent when it uses, or sells, the patented item. Further, the frequency of the payments has no bearing on the concept of use in this analogy.

A cleaner analogy, demonstrating the same point as analogy no. 1 is provided below:

A owns a patent to a manufacturing process. B wants to manufacture an item using that process. A does not want to convey the patent to B, so A grants B a license to use the patent. When B utilizes the patented process in its manufacturing operation, B uses the patent. Payments (whether periodic or one-time) from B to A are receipts for the use of a patent.

Eliminating the patent as the mechanism for protecting A's intellectual property and substituting a license, would result in the following:

A possesses data. B wants to manufacture an item using information derived from that data. A does not want to convey to B an unlimited right to use the data, so A grants B a license to use the data. When B

manufactures the item, B uses the license. Payments (whether periodic or one-time) from B to A are receipts for the use of a license.

Thus, a basic inspection of TGS's analogy no. 1 demonstrates that TGS's attempt to conflate the use of license (or patent) with the use of the underlying intellectual property does not provide assistance in construing the sourcing statute. The asset being transferred in the above analogies is the right to use the protected intellectual property. To argue that subsection (4) of the sourcing statute does not apply to receipts from the use of a license is to argue that the statute does not apply to a patent, copyright, or a trademark.

4. The court of appeals did not create or apply a separate test for receipts from the use of a license.

TGS suggests that the court of appeals incorrectly applies the statute by focusing on TGS's "use" of the license as the controlling event. TGS's brief at 15. TGS is correct in stating that it is the location of the customer's use that is controlling for the purpose of the sourcing statute. However, TGS is incorrect in asserting that the court of appeals based its holding on an analysis of TGS's use of the license. The court of appeal clearly and expressly stated that it based its conclusions on the customers' use of the data. "[W]e conclude that payments received by TGS for licensing **its customers to use proprietary seismic data** are gross receipts from the use of a license." *TGS-NOPEC Geophysical Co. v. Combs*, 268 S.W.3d 637, 646 (Tex. App.—Austin 2008, pet. filed) (emphasis added). In rejecting the argument that the customers are the intended taxpayers,

the court did indeed use the phrase “TGS’s use of a license within the meaning of the statutes.” *Id.* at 646. In the text of the opinion cited at page 15 of TGS’s brief, the court focused on receipts, explaining that the customers’ receipts were not subject to the sourcing statute since the customers’ receipts were not generated from the use of the license, but rather from the subsequent sale of tangible property. In contrast, TGS’s receipts **are** subject to subsection (4) of the sourcing statute, since those receipts result directly from the use of a license, or more specifically, from the use of the intellectual property conveyed through the license agreement.

TGS suggests that the court of appeals committed error by focusing on a “license transfer mechanism” test not supported by the statute. TGS’s brief at 22. There is no real basis in the text of the court of appeals’ opinion to support this notion, other than a few quotes taken out of context. In this context it is clear that the court of appeals opinion was focusing on the question of whose receipts were the object of the sourcing statute in determining to which party the sourcing statute applied. TGS fails to show that the court of appeals did not consider the use of the underlying asset when determining how the sourcing statute applied.

In support of the proposition that the Texas statute can only be read to apply in cases where the “asset” being transferred is itself a license, TGS favorably cites to an analogous statute from Wisconsin. TGS’s brief at 22-23. Admittedly, the Wisconsin statute could be considered to be more precise than the Texas statute in that it uses the term “use” in two separate senses: (i) in respect to

the owner's use of a license to protect its intellectual property (i.e., to limit the customer's use) and (ii) in relation to the customer's use or application of the intellectual property in some productive activity. The Wisconsin statute reads:

(dj)1. Except as provided in par. (df) ["df" is a separate rule for computer software], ***gross royalties and other gross receipts received for the use or license of intangible property***, including patents, copyrights, trademarks, trade names, service names, franchises, licenses, plans, specifications, blueprints, processes, techniques, formulas, designs, layouts, patterns, drawings, manuals, technical know-how, contracts, and customer lists, are sales in this state if any of the following applies:

- a. The purchaser or licensee uses the intangible property in the operation of a trade or business at a location in this state. If the purchaser or licensee uses the intangible property in the operation of a trade or business in more than one state, the gross royalties and other gross receipts from the use of the intangible property shall be divided between those states having jurisdiction to impose an income tax on the taxpayer in proportion to the use of the intangible property in those states.
- b. The purchaser or licensee is billed for the purchase or license of the use of the intangible property at a location in this state.
- c. The purchaser or licensee of the use of the intangible property has its commercial domicile in this state.

Wis. Stat. § 71.25(9)(dj) (emphasis added). A close reading of the full text of the Wisconsin statute suggests policy identical to the construction given to Texas Tax Sections 171.103(4) and 171.1032(a)(4). The Wisconsin statute speaks directly to "receipts for" the "use or license of intangible property." This statute applies to intangible property generally, not merely to the situations where the underlying asset is a license. Thus, the apportionment of TGS's receipts would be identical under either the Texas statute or the Wisconsin statute.

5. Application of the Texas sourcing statute to receipts from the use of a license is not dependant on the frequency of payments.

TGS states that both the court of appeals and the Comptroller failed to consider that in order for a receipt to truly be “*from* the use of a license” the amount and/or frequency of the lease payments must be measured by the extent or duration of the licensee’s use. TGS’s brief at 26. Thus, according to TGS, a one-time or sum-certain payment, pursuant to the terms of a license agreement, would not be subject to subsection (4) of the sourcing statute. This contention is not supported anywhere in the statute. Nor does TGS’s dictionary definition of “from” support this contention. TGS relies, instead, on its interpretation of language from the 1959 statute, repealed by the 1997 amendments. TGS’s brief at 26. Even if TGS’s unfounded contention that the prior statute’s use of the term “royalty” was analogous to a royalty on a mineral interest, the term “royalty” has been repealed from the statute. Consequently, any special meaning attributable to that term has also been repealed.

The amount of consideration to be paid under a license, or the method of payment calculation, is purely a matter of contract between the parties and does not affect whether the contract would be properly characterized as a license.

TGS poses an interesting question as to the application of the sourcing statute in a situation where the licensee obtains the right to use intellectual property under a license, but elects not to put that intellectual property to a productive use. Under TGS’s “measured-use” requirement, the payment to the

licensor (“C” in the example on page 29 of TGS’s brief) would not be subject to subsection (4) of the sourcing statute (regardless of use or non use by licensee) because the payment was not, at the outset, measured by the licensee’s amount of use. This demonstrates only that TGS’s theory is internally consistent, not that it is valid. TGS’s analysis ignores the fact that a licensee could use the intellectual property in ways other than by incorporating it into a production line and which had true economic value to the licensee, as with testing and evaluation.

6. TGS’s receipts are not “receipts from the sale of an intangible.”

TGS repeatedly relies on superseded Comptroller policy documents for the proposition that the Comptroller irrevocably decided that receipts from licensees arise from the sale of intangible property and should be apportioned to the location of the payor – the licensees’ legal domicile. In addition to failing to recognize that these policies were superceded by the 1997 amendments, TGS mischaracterizes them.

Before the 1997 amendments expressly included license revenues in the same category as trademarks and similar intangibles, the Comptroller analyzed the essence of the receipts-generating transaction to determine which apportionment rule to apply. Prior to the 1997 amendments, there were three possible categories for license transactions under the apportionment statutes: (i) sales of tangible personal property, (ii) sales of intangible personal property, or (iii) sales of services. Pet. Tab 11 (Taxability Response No. 0851).

In answer to the question “[s]hould gross receipts from the **licensing** of the geophysical ‘proprietary data’ be from sales of tangible personal property, from sales of intangible personal property or from services?” the Comptroller concluded in 1982 that the closest fit was the sale of intangible personal property. Neither of the other two categories fit because the licensing agreements did not represent contracts for the sale of tangible personal property, and performance of a service requires specific customers. *Id.* at ¶ 5. Thus, the only category that fit was the sale of intangible personal property. Accordingly, license receipts were apportioned to licensee’s legal domicile.

Significantly, and contrary to TGS’s attempted characterization of the documents, the Comptroller consistently referred to the license contracts as **licenses**, and the transaction as the **licensing** of geophysical data. Licensing, therefore, was always included in the general category of selling intangible personal property (as it still is), but was also categorized more specifically as licensing. The general and specific categorizations have not changed; but the apportionment of receipts has, under the 1997 amendments.

These long-term consistent characterizations foreclose TGS’s attempt to paint licenses-as-intangible-personal-property as different from the licenses addressed by the 1997 amendments. *See, e.g.*, Pet. Tab 12, Taxability Letter (1990) (superseded) page 1, ¶ 4 (“The gross receipts from these activities are from a **license** to use the geophysical information.”); *id.* at Pet. Tab 12, Taxability Letter (1991), page 1, ¶ 4 (same).

In 1997, when the legislature decided to apportion licenses the same as other transactions involving intangible property, such as trademarks, copyrights, and patents, the Comptroller withdrew the apportionment policies that had been in place before the 1997 amendments. The Comptroller does not, and TGS cannot, rely on superseded policies.

The legislature decided that licenses were more like patents, copyrights, trademarks, and franchises than the sale of other intangibles, and apportioned receipts to the place of use. This clear and unambiguous legislative decision precludes the Comptroller from apportioning license receipts to the location of payor after January 1, 1998. *See Sharp v. House of Lloyd, Inc.*, 815 S.W.2d 245, 249 (Tex. 1991) (Holding that the Comptroller does not have the legal authority to continue to follow a superseded statute, and that no amount of administrative practice inconsistent with the amended statute could change that.).

II. The 1997 amendments to the apportionment statutes are a clear and specific statutory departure from the location of payor rule; thus the legislative acceptance doctrine is not applicable.

TGS argues that the doctrine of legislative acceptance should prohibit the Comptroller from applying the 1997 amendments to the receipts at issue in this case. Specifically, TGS relies on this Court's decision in *Humble Oil*, a case dealing with the predecessor to the statutes at issue in the instant case. TGS accurately recites the parameters of the legislative acceptance doctrine, but misapplies the doctrine to the facts of this case.

TGS asserts that the instant case is strikingly similar to the facts in *Humble Oil*. A closer inspection of *Humble Oil* suggests otherwise. In *Humble Oil*, the statutory change relied upon by the Comptroller was the language added as subsection (d) of Article 2.02. *Humble Oil & Refining Co. v. Calvert*, 414 S.W.2d 172, 177-79 (Tex. 1967). Article 2.02, subsection (d), as added to the franchise tax statute by the 56th Legislature in 1959, provided that gross receipts from the taxpayer's *business done in Texas* shall include "(d) All other business receipts within Texas."⁵ Thus it was a catch-all provision, similar in nature to § 171.103(6) and § 171.1032(a)(7). It was this provision (subsection (d) of the then applicable Article 2.02) that the Court determined was not sufficiently clear to overcome the inherent ambiguity of the phrase "business done in Texas" in the main body of Article 2.02. *Humble Oil*, 414 S.W.2d at 179-80.

In the instant case, the Comptroller relied on an affirmative statutory amendment, expressly adding receipts from "the use of a ... license in this state" to the list of receipts treated as "business done in this state." Act of May 30, 1997, 75th Leg., R.S., ch. 1185, §§ 5-6 (Appendix A). While the ambiguity of the phrase "business done in this state" in the former Article 2.02, as found by the *Humble Oil* court, might still reside in the first sentence of § 171.103 and in § 171.1032(a); a plain reading of the 1997 amendments results in the conclusion

⁵ Subsections (a), (b), and (c) identified numerous categories of receipts which were to be sourced to Texas, but those categories did not cover intangibles in the form of interest and dividends received from foreign domiciled corporations, the transactions at issue in *Humble Oil*.

that “business done in this state” has been specifically defined to include license receipts as of the effective date of the 1997 amendments.

In applying the legislative acceptance doctrine discussed in the *Humble Oil* case, this Court stated that “departmental construction of the ambiguous statute was of such long standing that it should not be changed in the absence of clear statutory authorization.” *Humble Oil*, 414 S.W.2d at 180. In the instant case, the express addition of license receipts to § 171.103 and § 171.1032 serves as that clear statutory authorization.

TGS, however, urges the theory that when the 75th Legislature enacted S.B. 861 it re-enacted the catch-all provisions (§ 171.103(6) and § 171.1032(a)(7)), without change to the text of those specific clauses, and thus “accepted” the prior administrative decisions relating to those provisions. TGS’s brief at 36. This ignores the fact that § 171.103 and § 171.1032 are definitional provisions, statutes that exist for the very purpose of defining what constitutes “business done in this state” for franchise tax purposes. When the 75th Legislature added “use of a ... trademark, franchise, or license in this state” to the list of categories of receipts that constitute “business done in this state,” it effected a substantial (and substantive) change to the verbiage of the statute. *Old Am. County Mut. Fire Ins. Co. v. Sanchez*, 149 S.W.3d 111, 115 (Tex. 2004)(every word of a statute is presumed to have been included or excluded for a reason); *City of San Antonio v. City of Boerne*, 111 S.W.3d 22, 29 (Tex. 2003) (effect must be given to every sentence, clause, and word of a statute so that no part thereof be rendered

superfluous). To adopt TGS's theory would give primacy to the catch-all provisions (and prior administrative decisions relating to those provisions) over the express terms added by the legislature specifically delineating the sources of receipts the legislature had decided to apportion based on location of use, as well as frustrate the legislature's ability to change the express terms of the definition. TGS's interpretation would have the effect of turning the legislative acceptance doctrine on its head: ignoring express terms added by the legislature, in favor of creating an appearance of ambiguity where none exists.

TGS asserts an additional rationale, beyond the legislative acceptance doctrine, arguing that the 75th Legislature adopted the very language of the Comptroller rule, adopted in 1988, which states that receipts from the use of a license in this state are to be sourced to Texas. Rule 3.403(e)(11), 13 Tex. Reg. 2971 (June 14, 1988). TGS reasons that when the legislature affirmatively enacts the text of a rule, the concept of legislative acceptance of the administrative agency's construction of that rule should have even more force than in a traditional legislative acceptance situation. TGS's brief at 39. However, by the time the 75th Legislature enacted S.B. 861, the Comptroller had repealed the 1988 rule (sourcing the license receipts as business done in this state) and replaced it with a rule (relating to taxable capital only) that expressly sourced licensing receipts to the location of payor:

iii. Revenues received by the owner of a trademark, franchise, and license are apportioned to the location of payor. 34 Tex. Admin. Code §3.549(e)(30)(A)(iii) (1996) (Taxable Capital: Apportionment).

Thus, if the extant rules of an administrative agency should have any bearing on the construction of a subsequently enacted statute, a more logical conclusion would be that the 75th Legislature, in enacting S.B. 861, was affirmatively reversing the Comptroller's location of payor rule for licensing receipts and replacing it with a sourcing statute expressly apportioning such receipts to the location of use. 21 Tex. Reg. 11511 (November 26, 1996) (Appendix B).

III. The court of appeals did not err in holding that it was reasonable for the Comptroller to treat the shipping or billing address of TGS's customers as the location of use for apportionment purposes.

A. No genuine issue of material fact exists in this case.

The Tax Code directs the comptroller to “determine the amount of tax to be paid from information contained in the [tax] report **or any other information available to the Comptroller.**” Tax Code § 111.008(a) (emphasis added) (tax deficiency determinations).

The court of appeals ruled that “in the absence of other evidence, we conclude that the Comptroller's use of TGS's customers' shipping or billing addresses to determine location of use was reasonable.” *TGS-NOPEC*, 268 S.W.3d at 649-50. The only documentary evidence available to the Comptroller to determine the location of use (and thus the resultant amount of tax to be paid) is contained in reports identifying TGS's Texas-based customers' shipping or billing addresses. C.R. 126-127, 170, 209. Relative to the facts in this situation, the Comptroller's decision was both reasonable and practical.

A genuine issue of material fact as to where the data was used for the purpose of the franchise tax statute does not exist. TGS urges this Court to accept the premise that it had offered to provide evidence of place of use. TGS's brief at 44 (citing to its Response to Defendant's Motion for Final Summary Judgment). Rather than offering evidence as to location of use in that Response, TGS was instead urging the trial court to adopt its theory that the physical location of the geological formation was a more reasonable standard for sourcing the receipt. C.R. 266. That the Comptroller could have applied another means to determine the location of use does not make the method chosen by the Comptroller unreasonable. *See Railroad Comm'n v. Humble Oil & Refining Co.*, 193 S.W.2d 824, 833 (Tex. Civ. App. – Austin, 1946, writ ref'd n.r.e.).

In response to the Comptroller's discovery, TGS averred that it did not know "each and every location of use" and that "it [TGS] cannot make an accurate determination of where the seismic data may be manipulated or utilized by the purchaser after transfer." C.R. 170, 210. The court of appeals determined that TGS provided "no evidence regarding its proposed method of determining location of use." *TGS-NOPEC*, 268 S.W.3d at 650.

TGS further suggests that generally accepted accounting standards "generally require" exploration and production firms to capitalize the cost of seismic data to the subject property. TGS's brief at 43. TGS does not expressly put forward the cited FASB Statement and Revenue Rules as evidence of location of use; TGS instead appears to put this forward in support of its theory that the

location of the geological formation (i.e., location where the data is shot) is the most logical place of use for franchise tax purposes. While the Comptroller certainly may consider generally accepted accounting principles in determining the taxable earned surplus and taxable capital components of the tax base for the franchise tax (*see* § 171.109(b)), TGS does not explain how these provision relating to capitalization issues would have any direct bearing on the treatment of gross receipts under either § 171.103 or § 171.1032. Furthermore, regardless of accounting principles, TGS's argument again ignores the fact that TGS failed to provide any specific information to the Comptroller on location of use other than the shipping or billing addresses of its customers, which the Comptroller used. The Comptroller's use of the limited information provided by TGS was reasonable under the facts of this case.

B. The court of appeals decision does not establish or perpetuate either a “mailing address rule” or any other absolute standard for determining location of use.

TGS expresses concern that the Comptroller has attempted to establish a presumption that seismic data is used at the customer's headquarters. TGS's brief at 43. TGS expresses further concern that the Comptroller has attempted to create a rule establishing the mailing address of the customer as the *per se* location of use. TGS's brief at 44. While Comptroller's Decision No. 43,065⁶ does indicate that Comptroller staff put forward an argument, at the administrative hearing, that the location of use of the seismic data is the customer's headquarters because “that

⁶ Comptroller hearing decision 43,065 is published as STAR document 200409846H and is available to the public at <http://cpastar2.cpa.state.tx.us/index.html>.

is where the decisions arrived at by use of the Claimant's data are made"; the Comptroller's final decision clearly rejected that theory in the absence of any evidence. The Comptroller's decision in hearing No. 43,065 was based on the fact that the taxpayer did not present any evidence as to the location of use of the data.

More significant to this appeal, the court of appeals did not condone or even suggest the propriety of a *per se* mailing address rule. Indeed, in finding that the Comptroller's use of the mailing addresses to determine location of use was reasonable, the court expressly predicated that determination on the absence of other evidence. *TGS-NOPEC*, 268 S.W.3d at 649-50. This does not suggest the emergence of a *per se* sourcing rule.

PRAYER

The Court should deny the petition for review. Alternatively, if the Court grants review, it should affirm the judgment of the court of appeals.

Respectfully submitted,

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CERTIFICATE OF SERVICE

I do hereby certify that on the ____ of November, 2009, a true and exact copy of the foregoing was mailed via Certified Mail, Return Receipt Requested to counsel of record:

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