



Opinion Summaries March 25, 2022

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TAXES

Franchise Tax

Sirius XM Radio, Inc. v. Hegar, — S.W.3d —, — WL — (Tex. March 25, 2022) [20-0462]

This case concerned a franchise tax dispute over the method of allocating the proportion of services performed in Texas. Sirius XM Radio sells satellite radio services to customers in Texas and elsewhere. The content is largely produced outside of Texas and its transmitted on equipment largely outside of Texas. Customers can access the service by purchasing a radio and paying a subscription fee. A chip set in the radio decrypts the signal. If a customer pays the fee, Sirius sends a signal from out of state that permits the chip set to decrypt the signal.

The Texas franchise tax is based on three steps. First the taxpayer's "margin" is calculated. Second, the "apportioned margin" is calculated as the ratio of the taxpayer's gross receipts from business done in Texas, over the gross receipts from the entire business. Third, permitted deductions are applied to the apportioned margin to yield the "taxable margin" to which the tax rate is applied. This appeal concerned the second step.

The apportioned margin depends on the proportion of the taxpayer's receipts that are "gross receipts from business done in this state," TEX. TAX. CODE § 171.106(a), which in turn depends on receipts from "each service performed in this State," *id.* § 171.103(a)(2). The Comptroller claimed that the relevant service performed in Texas, which it characterized as the "receipt-producing, end-product act," was the service of unscrambling the radio signal. Sirius argued that the relevant receipt-producing acts were the use of equipment and personnel to produce and broadcast the radio content.

Sirius paid the tax under protest and sought a refund. The district court agreed with Sirius as to the correct method for calculating the apportioned margin, and ordered a substantial refund. The court of appeals reversed, agreeing with the

Comptroller that the relevant receipt-producing act was unscrambling the radio signal.

The Supreme Court reversed the court of appeals. The Court held that “service performed in this State” refers here to the production and broadcasting of radio content, which occurs almost entirely outside of Texas. The Court, under a plain-meaning analysis of the statute, concluded that a service is performed in this State if the labor is done in this State. If technology performs the useful act, the location of the equipment is considered. Prior cases have likewise looked to the location of the taxpayer’s personnel and equipment in determining the place where a service is performed. The Court also looked to the economic realities of the service and reasoned that customers are paying for the content Sirius produces and broadcasts, not decryption.

The Court reversed the court of appeals’ judgment and remanded the case to that court for consideration of issues that court had not reached.