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Sirius XM Prevails in Texas Supreme Court on Sourcing of Receipts from Satellite Signal

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In a recently issued taxpayer-favorable opinion, the Texas Supreme Court overturned the court of appeals' decision holding that the state's performance-based sourcing statute for service receipts essentially looks to customer location. The Court, relying on the statute's plain language, then affirmed the taxpayer's methodology, which sourced its receipts to the location where the taxpayer's performance occurred. *Sirius XM Radio, Inc. v. Comptroller*, no. 20-0462 (Tex. Mar. 25, 2022) ("*Sirius* Op.").

The dispute concerned the receipts Sirius XM Radio, Inc. ("Sirius") earned from customer subscription fees to access Sirius' radio programming, which it transmitted using satellites. Sirius produced most of the content broadcast on its satellite radio channels, and its production primarily took place outside of Texas. Similarly, Sirius' "headquarters, transmission equipment, and production studios were located almost exclusively outside of Texas." *Hegar v. Sirius XM Radio Inc.*, 604 S.W.3d 125, 128 (Tex. Ct. App. May 1, 2020). Sirius' satellites, which orbited thousands of miles above the planet, are controlled by Sirius' facilitates also located outside of Texas. Sirius' customers, located in Texas and other states, receive Sirius programming using satellite-enabled radios

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(many of which were located in customers' automobiles).

On audit, the Comptroller took the position that Sirius should have apportioned its customer subscription fee service receipts to the location of a customer's satellite-enabled radio rather than the location where Sirius produces its programs. The basis for the Comptroller's position was its interpretation of the statute at issue, which in this case, it claimed looked to "where the receipt-producing, end-product act is done," which it purported to be the location of a subscriber's radio, where the radio signal was decrypted and enabled for subscriber use. *See Sirius* Op. at 5-6. While the trial court found for Sirius, the court of appeals reversed, and Sirius petitioned for review.

Texas law, similar to the law of some other states, requires taxpayers earning income from the performance of services to apportion the income to Texas if the "service [is] performed in this state" (Tex. Tax Code Ann. § 171.103(a)(2); *see also* 34 Tex. Admin. Code § 3.591(e)(26)(b)). In this case, the statute's plain language was the Court's primary basis for rejecting the Comptroller's "receipt-producing, end-product act test" to determine the location where a service is performed. The Court concluded: "Setting aside the atextual and unhelpful 'receipt-producing, end-product act' test, the most natural reading of 'service performed in this state' supports locating the performance of the service at the place where the taxpayer's personnel or equipment is physically doing useful work for the customer." *Sirius* Op. at 12. Further, the Court noted that its conclusion is supported by past precedent; Texas courts and even the Comptroller itself consistently have interpreted the performance-based statute on an origin, rather than destination, basis. *See id.* at 12-16.

In reaching its conclusion that the service Sirius performed for its customers was its production of radio programs and the transmission of the radio

signal to subscribers' radios, which primarily occurred outside Texas where its employees and equipment were located, the court took a common sense, "economic realities" approach and rejected the Comptroller's hyper-technical approach to characterizing Sirius' service. The court keenly observed: "But the economic reality of Sirius's business is that decryption is not a service performed for the benefit of the customer at all. ... Encryption is a barrier to access imposed by Sirius—an artificial way to manufacture scarcity—in order to extract subscription payments from customers. Those customers want to listen to radio content. They do not want decryption." *Id.* at 17.

Further, the Court clarified that its ruling was in no way based on deference given by the court to an administrative agency's (in this case, the Comptroller's) interpretation of the statute at issue. *See id.* at 8, 16 n.8. The court confirmed that Texas courts have not adopted agency-deference doctrines used by federal courts; rather a Texas court "must always endeavor to decide for itself what the statutory text means so that it can determine whether the agency's construction contradicts the statute's plain language." *Id.* at 8 (citation omitted).

This ruling serves as a significant backstop/warning to taxing agencies that they must act within their authority and not rewrite the law. That is the legislature's job. Moreover, this case is consistent with recent service apportionment rulings in Ohio, Michigan and Washington, where the courts relied on a statute' plain language to resolve the sourcing dispute. *See Defender Security Co. v. McClain*, 165 N.E.3d 1236 (Ohio Sept. 29, 2020); *Honigman Miller Schwartz & Cohn LLP v. City of Detroit*, 505 Mich. 284 (Mich. May 18, 2020); *LendingTree, LLC v. State of Wash., Dep't of Revenue*, 460 P.3d 640 (Wash. Ct. App. Mar. 30, 2020).

Going forward, in Texas, the court's rejection of the Comptroller's "receipt-producing, end-product act"

test at the very least calls into question the validity of the recent amendments to 34 Tex. Admin. Code § 3.591(e)(26) interpreting the performance-based sourcing statute for service receipts in this manner. Outside of Texas, this ruling may be helpful in other jurisdictions where taxpayers and taxing authorities are disputing how to apply apportionment statutes, and the taxing authority's interpretation is inconsistent with the plain language and/or should not be entitled to deference by the court. *See, e.g., Synthes USA HQ, Inc. v. Commonwealth of Penn.*, 236 A.3d 1190 (Pa. Commw. Ct. July 24, 2020) (pending before the Pennsylvania Supreme Court).
