COMMENT

Joyce v. *Finnigan*: Adoption of the "Best" Approach in Hopes of Some Uniformity

I. Introduction

Nowadays, a company is almost certain to conduct business across state lines, which may subject the company to tax in multiple jurisdictions. This, in turn, leads to the issue of state taxation of a multistate corporate taxpayer, where one of the concerns is the apportionment of the taxpayer's income in a way that accurately and fairly reflects the taxpayer's activity within the state.[1] Because of the practical difficulties of determining precisely how much of the tax base corresponds to each state where the taxpayer is subject to tax, state laws provide for formulary apportionment.

Historically, the most common apportionment formula was the equally-weighted, three-factor formula composed of a property factor, payroll factor, and sales factor. The sales factor has proven to be the center of controversy, especially as states continue to weigh it more heavily in their apportionment formulas or, in some cases, rely on it exclusively.

One of the main controversies surrounding the sales factor composition in states that adopt a combined reporting regime is the ongoing *Joyce–Finnigan* debate,[2] which centers around the question of whose sales ought to be included in the sales factor numerator of a group of corporations subject to combined reporting, where some members of the group have nexus[3] with the taxing state and other members do not. California took the lead in this area, first holding in *Joyce* that only sales of taxable members (*i.e.*, those companies that individually have nexus in the state) of the unitary group are included in

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[1] The Commerce Clause and the Due Process Clause limit a state's power to tax a corporation conducting business both within and without the state. *See infra* Part II.A.

[2] *Joyce* and *Finnigan* refer to the two California cases setting the foundation for this issue. *See In re* Joyce, Inc., No. 66-SBE-070, 1966 WL 1411 (Cal. State Bd. of Equalization Nov. 23, 1966), *overruled by In re* Finnigan Corp., No. 88-SBE-022-A, 1990 WL 15164 (Cal. State Bd. of Equalization Jan. 24, 1990), *overruled by In re* Huffy Corp., No. 99-SBE-005, 1999 WL 386938 (Cal. State Bd. of Equalization Apr. 22, 1999); *In re* Finnigan Corp. (*Finnigan I*), No. 88-SBE-022, 1988 WL 152336 (Cal. State Bd. of Equalization Aug. 25, 1988), *aff'd* (*Finnigan II*), No. 88-SBE-022-A, 1990 WL 15164 (Cal. State Bd. of Equalization Jan. 24, 1990), *overruled by In re* Huffy Corp., No. 99-SBE-005, 1999 WL 386938 (Cal. State Bd. of Equalization Apr. 22, 1999).

[3] The term nexus refers to the constitutional requirement that there be a "substantial nexus" (some minimal connection) between the taxed activity and the taxing jurisdiction before a state may impose a tax on a business. *See* Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 279 (1977); Adam B. Thimmesch, *The Illusory Promise of Economic Nexus*, 13 Fla. Tax Rev. 157, 158 (2012) ("Under the Dormant Commerce Clause, a state can only tax a business that has a 'substantial nexus' within it.").

the sales factor numerator.[4] California then switched positions in *Finnigan*, finding that all sales into the taxing state made by members of the group are included in the sales factor numerator so long as any member of the unitary group has nexus within the taxing state, even if the selling entity is not independently taxable in the jurisdiction.[5]

Not surprisingly, there is substantial inconsistency in states' adoption of the *Joyce* or *Finnigan* approach.[6] But, this is not the only area in state taxation of multistate corporations where lack of uniformity is prominent. Rather, nonuniformity exists in a significant number of areas, such as the formulation of apportionment formulas, sourcing of receipts for purposes of computing the sales factor, and classification of business income that should be apportioned as opposed to nonbusiness income that should be allocated, among others. Such nonuniformity has been somewhat lessened by the drafting of two model acts—the Uniform Division of Income for Tax Purposes Act (UDITPA)[7] and the Multistate Tax Compact (Compact)[8]—which have been adopted by a number of states[9] and address many of the mentioned areas of nonuniformity, but neither addresses the *Joyce–Finnigan* issue.

This Comment explores the *Joyce–Finnigan* debate. It argues that *Joyce* is the better rule and should be incorporated in the Compact's apportionment provisions in order to achieve some uniformity on this issue in the area of state taxation of corporations engaged in interstate commerce for states that have adopted the Compact. Part II provides the necessary context for analyzing the *Joyce–Finnigan* debate. It discusses the restraints imposed on states' taxing power by the Constitution, the steps that have been taken to achieve some uniformity in state taxation of multistate corporations, and the unitary business concept of formulary apportionment. Part III traces the origins and development of the *Joyce–Finnigan* debate from California to other jurisdictions. This Comment argues in Part IV.A that while complete uniformity in the area of state taxation of multistate corporations is the ideal solution, it is likely an unrealistic goal. However, a significant area of nonuniformity that leads to problematic results for multistate corporations is the *Joyce–Finnigan* issue. The achievement of consistency in this area would be beneficial in terms of providing for more equitable taxation and reduced complexity. Part IV.B proposes that even though neither the *Joyce* nor *Finnigan* rule is free of flaws, *Joyce* is the better rule primarily because *Finnigan* effectively results in a state taxing income that would otherwise be out of its reach due

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[4] *See Joyce*, 1966 WL 1411, at *4.

[5] *See Finnigan I*, 1988 WL 152336, at *3.

[6] As discussed in Part III.C of this Comment, the *Joyce* rule is currently followed by approximately 15 of the states with combined reporting regimes, while *Finnigan* is followed by about ten of those states.

[7] Unif. Div. of Income for Tax Purposes Act (1957).

[8] Multistate Tax Compact (Multistate Tax Comm'n 1967).

[9] A state is not required to comply with the provisions of the Compact or UDITPA unless the respective state's legislature specifically adopts the model acts in full or in part.

to federal or constitutional limitations. Finally, Part IV.C argues that there are two options for achieving uniformity in the *Joyce–Finnigan* area. One is through Congress; however, given Congress's history of latitude toward the states and general inaction in the area of state taxation of multistate corporations, Congress is unlikely to take any steps imposing on states' taxing powers. Therefore, the most realistic option for settling the *Joyce–Finnigan* debate is for the Multistate Tax Commission to revise its apportionment provisions to adopt the *Joyce* rule.

II. Background

Part II provides the necessary background underlying the *Joyce–Finnigan* debate. Part II.A discusses the federal constitutional constraints imposed on states' power to tax a corporation engaged in interstate commerce with a focus on the requirement that a multistate corporation's tax base be fairly apportioned among the taxing jurisdictions. Part II.B explores the three significant steps that have been taken toward uniformity in the area of state corporate taxation. One of these steps was taken by Congress in enacting Public Law 86-272; the other two are model acts, which have been adopted by a fair number of states imposing a corporate income tax. Finally, Part II.C provides a general overview of three common methods of reporting, focusing on the combined reporting regime for a group of corporations engaged in a unitary business.

A. *Federal Constitutional Constraints on States' Taxing Power*

When a corporation does business solely within one state, there is not a lot of controversy over the fact that the state has the power to tax the corporate profits arising from the entity's in-state activities, assuming the state levies a corporate income tax.[10] However, when a corporation conducts business in several states, it will likely be subject to a corporate income tax in more than one jurisdiction.[11] Federal constitutional provisions, primarily the Commerce

[10] Forty-five jurisdictions, including the District of Columbia, levy a corporate income tax. *See* Walter Hellerstein, State Taxation ¶ 8.11 (3d ed. 2013).

[11] *See, e.g.*, Complete Auto Transit, Inc. v. Brady, 430 U.S. 274, 288 (1977) (citations omitted) ("'It is a truism that the mere act of carrying on business in interstate commerce does not exempt a corporation from state taxation. It was not the purpose of the commerce clause to relieve those engaged in interstate commerce from their just share of state tax burden even though it increases the cost of doing business.'").

Clause[12] and the Due Process Clause,[13] place constraints on a state's power to tax a corporation conducting business both within and without the state.

Under the Commerce Clause, a state tax imposed on an out-of-state corporation engaged in interstate commerce is constitutional when (1) there is a substantial nexus between the taxed activity and the taxing jurisdiction, (2) the tax is *fairly apportioned*, (3) the tax is nondiscriminatory, and (4) the tax "is fairly related to the services provided by the State."[14] The Due Process Clause generally limits the territorial reach of a state's taxing power, requiring "some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax."[15] The Due Process Clause has also been invoked to ensure that the tax base upon which the state tax is imposed includes only the portion of the taxpayer's income or property *fairly apportioned* to the taxpayer's in-state activities.[16]

There is overlap between the restraints imposed by the Commerce and Due Process Clauses, both requiring some minimum nexus and fair apportionment. The Supreme Court has indicated that often, the requirements under these constitutional provisions are substantially similar.[17] For purposes of this Comment, the focus is on the fair apportionment requirement, which basically mandates that a corporation engaged in interstate commerce is entitled to a division of income if it is taxable with respect to that income in more than

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[12] U.S. Const. art. I, § 8, cl. 3 ("The Congress shall have Power . . . [t]o regulate Commerce . . . among the several States . . . ."). The affirmative grant of power provided in the Commerce Clause has long been held to embody implied restraints on permissible state action even if there is no congressional legislation imposing such limits. This concept is referred to as the dormant Commerce Clause. *See* Dep't of Revenue of Ky. v. Davis, 553 U.S. 328, 337-38 (2008) (explaining that even though the text of the Commerce Clause does not explicitly restrain the states, the Court has "sensed a *negative implication* in the provision since the early days").

[13] U.S. Const. amend. XIV, § 1 ("[N]or shall any State deprive any person of life, liberty, or property, without due process of law . . . .").

[14] *Complete Auto*, 430 U.S. at 279; *see* Nw. States Portland Cement Co. v. Minnesota, 358 U.S. 450, 452 (1959).

[15] Miller Bros. v. Maryland, 347 U.S. 340, 344-45 (1954).

[16] *See, e.g.*, Mobil Oil Corp. v. Commissioner of Taxes of Vt., 445 U.S. 425, 436-37 (1980) (citing Moorman Mfg. v. G.D. Bair, 437 U.S. 267, 272-73 (1978)) ("For a state to tax income generated in interstate commerce, the Due Process Clause of the Fourteenth Amendment imposes two requirements: a 'minimal connection' between the interstate activities and the taxing State, and a rational relationship between the income attributed to the State and the intrastate values of the enterprise.").

[17] *See* Ott v. Miss. Valley Barge Line Co., 336 U.S. 169, 174 (1949) (noting that both Commerce Clause and Due Process Clause requirements are satisfied "if the tax is fairly apportioned to the commerce carried on within the State"). For the substantial nexus requirement, the Court has differentiated between the nexus required by the Commerce Clause and the Due Process Clause. *See* Quill Corp. v. North Dakota, 504 U.S. 298, 305 (1992).

one state.[18] The difficulty arises in the application of this requirement—how is a state supposed to ascertain a multistate corporation's tax base precisely attributable to that state? Are taxpayers engaged in business in multiple states supposed to track exactly how much of their income arises within each state?

Given the probably inescapable practical difficulties of ascertaining exactly what a multistate corporation's tax base is within each particular state,[19] the Supreme Court has permitted the states to determine the corporation's tax base attributable to the state by the use of formulary apportionment.[20] The Court has upheld a variety of apportionment methods, declining to mandate a uniform formula for all the states.[21] Although the lack of uniformity in this area might expose taxpaying corporations to a risk of overlapping taxes (or result in nowhere income[22]), the Court has emphasized that it is Congress's job, not the Court's, to require uniformity among states in the area of apportionment.[23] As explained in *Container Corp. of America v. Franchise Tax Board*,

> [E]liminating all overlapping taxation would require this Court to establish . . . a single constitutionally mandated method of taxation . . . . Because that task was thought to be essentially legislative, we declined to undertake it, and held that a fairly apportioned tax would not be found invalid simply because it differed from the prevailing approach adopted by the States.[24]

Not only has the Court declined to impose a uniform method of apportionment, it has also made it relatively difficult for a taxpayer to prevail on a challenge to a state's apportionment formula. In order to successfully challenge a state's tax assessment resulting from the application of its formulary apportionment method, the taxpayer has to prove by "clear and cogent evidence" that the tax base attributable to the state under the formula is "out of all appropriate proportions to the business transacted" in-state or "led to

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[18] *See, e.g.*, Cent. R.R. v. Pennsylvania, 370 U.S. 607, 612 (1962) (citations omitted) (internal quotation marks omitted) (noting that it is "multiple taxation of interstate operations that offends the Commerce Clause"); *see also* HELLERSTEIN, *supra* note 10, ¶ 8.02[1] ("If a taxpayer is taxable in more than one state, denial by either state of the right to a division of the tax base would expose the taxpayer to an unconstitutional risk of multiple taxation.").

[19] *See* Container Corp. of Am. v. Franchise Tax Bd., 463 U.S. 159, 164 (1983) (citations omitted) ("In the case of a more-or-less integrated business enterprise operating in more than one State, however, arriving at precise territorial allocations of 'value' is often an elusive goal, both in theory and in practice.").

[20] *See, e.g.*, *Moorman Mfg.*, 437 U.S. at 273 (upholding Iowa's single-factor apportionment formula and reasoning that, although the use of formulary apportionment leads to a "rough approximation" of the taxpayer's income attributable to the state, the Court has declined "to impose strict constitutional restraints on a State's selection of a particular formula").

[21] *Container Corp. of Am.*, 463 U.S. at 165; *Moorman Mfg.*, 437 U.S. at 273, 280-81.

[22] Nowhere income refers to income that escapes state taxation. *See* Ilya A. Lipin, *Corporate Taxpayers' Sore Arm: Throw-Out Rule Litigation in State and Local Taxation*, 66 TAX LAW. 901, 902-03 (2013).

[23] *See Container Corp. of Am.*, 463 U.S. at 171; *Moorman Mfg.*, 437 U.S. at 278-81.

[24] *Container Corp. of Am.*, 463 U.S. at 171 (citations omitted).

a grossly distorted result."[25] As expected from the formulation of this standard, it is a difficult showing for a corporation to make. In fact, the Court has never held an apportionment formula *facially* unconstitutional, though it has invalidated a state's apportionment formula's *application* to a multistate taxpayer on rare occasions.[26]

With the Court's inaction and hence, apparent blessing, states have devised a variety of apportionment formulas to apportion a multistate taxpayer's tax base among the various taxing jurisdictions.[27] While multistate corporate taxpayers should have their income fairly apportioned among the taxing jurisdictions,[28] apportionment does not necessarily provide a uniform division of their tax base because each state is free to choose its own apportionment formula and sourcing provisions. Congress has yet to act on the Court's invitation in *Container Corp. of America* to impose a uniform method of state apportionment, except for its enactment of Public Law 86-272, discussed in Part II.B. Other organizations have taken more significant steps toward uniformity, with the two leading projects being UDITPA and the Compact, also discussed in Part II.B.

B. *Steps Toward Uniformity: Public Law 86-272, UDITPA, and the Multistate Tax Compact*

Public Law 86-272[29] was enacted in 1959 in response to the Court's decision in *Northwestern States Portland Cement Co. v. Minnesota*.[30] In *Northwestern*,

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[25] *Moorman Mfg.*, 437 U.S. at 274 (internal quotations omitted) (citations omitted); *see* Underwood Typewriter Co. v. Chamberlain, 254 U.S. 113, 121 (1920) (footnote omitted) (in challenging the state's use of a single-factor formula to apportion net income, the taxpayer failed to carry its burden of showing that "the method of apportionment adopted by the state was inherently arbitrary, or that its application to this corporation produced an unreasonable result").

[26] For situations where the Court has held the application of an apportionment formula to an individual taxpayer unconstitutional, see Hans Rees' Sons, Inc. v. North Carolina, 283 U.S. 123, 136 (1931) (invalidating the tax under the Due Process Clause where proof showed that while the state's single-factor property formula produced a tax on 66% to 85% of the taxpayer's income, only 17% of that income was on average actually sourced in state) and Norfolk & W. Ry. v. Mo. State Tax Comm'n, 390 U.S. 317, 326 (1968) (holding that the tax violated the Due Process and Commerce Clauses where the taxpayer successfully bore its "heavy burden" of showing that application of the formula resulted in "gross overreaching, beyond the values represented by the intrastate assets purported to be taxed").

[27] *See Moorman Mfg.*, 437 U.S. at 273 (affirming that a three-factor apportionment formula is not constitutionally required and that a single-factor formula is presumptively valid).

[28] *See Container Corp. of Am.*, 463 U.S. at 169 ("[A] State must then apply a formula apportioning the income of that business within and without the State. Such an apportionment formula must, under both the Due Process and Commerce Clauses, be fair." (citations omitted)).

[29] 15 U.S.C. §§ 381-84 (2012).

[30] *See* Nw. States Portland Cement Co. v. Minnesota, 358 U.S. 450, 465 (1959); Hellerstein, *supra* note 10, ¶ 6.16 (footnote omitted) ("Congress reacted with astonishing speed [to the *Northwestern* case] and, for the first time in its history, adopted an act restricting the states' power to tax interstate businesses."); Michael T. Fatale, *Federalism and State Business Activity Tax Nexus; Revisiting Public Law 86-272*, 21 Va. Tax Rev. 431, 474-79 (2002).

both corporations challenging the constitutionality of the corporate income taxes were engaged in the solicitation of orders within the states through sales persons who maintained offices in the states, but the orders were accepted, filled, and delivered outside of the taxing states.[31] The Court upheld the state taxation of the two companies and for the first time held that a tax on the net income of an out-of-state corporation engaged exclusively in an interstate business within the taxing state is constitutional, provided that the tax is "not discriminatory and is properly apportioned to local activities within the taxing State forming sufficient nexus to support the same."[32]

The *Northwestern* case led to "alarm and protest among businesses" and resulted in Congress adopting, for the first time, a statute that limited the states' power to tax interstate businesses.[33] Under Public Law 86-272, a state cannot impose a tax on the income derived within the state by an out-of-state corporation engaged exclusively in interstate commerce if (1) the corporation's activities within the state are limited to the solicitation of orders[34] for sales of tangible personal property, (2) the orders are processed outside the state, and (3) the orders are filled and delivered from outside the state.[35] Public Law 86-272 is important for purposes of this Comment because, as discussed in Part III, the *Joyce–Finnigan* debate arose, and still typically arises, in the context of attributing the sales made by a member of a group of corporations when that member is not subject to tax in the state in which it is making the sales; one typical reason why an entity is not subject to tax in a state is because its activities are protected under Public Law 86-272.

Aside from Public Law 86-272, Congress has mostly opted for inaction and latitude toward the states in the area of apportionment of multistate taxpayers' income (and state corporate taxation generally). In recent years, efforts by the business community have led to repeated introduction in Congress

[31] *See Northwestern*, 358 U.S. at 454-56.

[32] *See id.* at 452. The significance of the case is highlighted by the precedent that existed prior to *Northwestern*. In an earlier case, the Court had held unconstitutional a state tax measured by net income and imposed on an out-of-state corporation engaged exclusively in interstate business because the state could not impose a tax "on the *privilege of doing business*" despite the tax being nondiscriminatory and fairly apportioned. *See* Spector Motor Serv., Inc. v. O'Connor, 340 U.S. 602, 603 (1951), *overruled by* Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977). After *Northwestern*, states promptly modified their tax regimes to avoid any *Spector* challenges and instead fall within *Northwestern*—states "replac[ed] their franchise taxes on the privilege of doing business by direct net income taxes" although generally, the same rates, apportionment methods, and tax base were used. Hellerstein, *supra* note 10, ¶ 4.11[1].

[33] Hellerstein, *supra* note 10, ¶ 6.16; *see* Mark R. Nethers, *Putting the Nexus Into Public Law 86-272*, 66 Wash. U. L. Rev. 595, 601-02 (1988) (discussing Congress's swift enactment of Public Law 86-272 in response to the business community's "sharp reaction" to *Northwestern*).

[34] Congress did not define the term "solicitation of orders" in the statute, leaving it up to the states to interpret this term. This has led to a variety of interpretations and yet another area of nonconformity in state corporate taxation. *See* Nethers, *supra* note 33, at 603-04.

[35] 15 U.S.C. § 381(a) (2012).

of the Business Activity Tax Simplification Act (BATSA).[36] One of BATSA's main features is the provision of definite and specific standards governing the states' ability to impose a business activity tax.[37] Under BATSA's nexus standards, a state can impose a business activity tax only on those businesses that have a physical presence within the state.[38] Most important for purposes of this Comment, BATSA also provides for use of the *Joyce* rule for certain combined and consolidated returns.[39] Although passage of BATSA would result in a significant amount of simplification and uniformity, commentators are of the opinion that the bill is unlikely to pass mainly because of the bill's taxpayer-friendly nature and resulting opposition from those supporting the states on this issue.[40]

Unlike Congress, other organizations have seen the appeal of and need for uniformity in the area of state taxation of multistate corporations and taken more affirmative steps towards uniformity, leading to the creation of

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[36] BATSA has been introduced in Congress in various forms since 2000. Maria Koklanaris, *U.S. House Subcommittee Hears Conflicting Testimony on BATSA*, 71 St. Tax Notes (TA) 515, 515 (Mar. 3, 2014); *see* H.R. 2992, 113th Cong. (2013); H.R. 1439, 112th Cong. (2011); H.R. 1083, 111th Cong. (2009); H.R. 5267, 110th Cong. (2008); S. 1726, 110th Cong. (2007). The House Judiciary Subcommittee on Regulatory Reform, Commercial and Antitrust Law held hearings on February 26, 2014 on the 2013 bill. *See* Koklanaris, *supra,* at 515; *Congress Holds Hearing on the Business Activity Tax Simplification Act*, PricewaterhouseCoopers, Feb. 27, 2014, http://www.pwc.com/en_US/us/state-local-tax/newsletters/salt-insights/assets/pwc-congress-holds-hearing-business-activity-tax-simplificatio.pdf. *See generally* American Bar Association, *Report of the Task Force on Business Activity Taxes and Nexus of the ABA Section of Taxation State and Local Taxes Committee*, 62 Tax Law. 935, 935 (2009) [hereinafter *ABA Report*] (providing a detailed discussion on business activity taxes and the business activity tax nexus debate).

[37] *See ABA Report*, *supra* note 36, at 981; H.R. 2992, § 3. BATSA also provides for the modernization of Public Law 86-272 so that it applies to all sales and transactions (not only sales of tangible personal property) and to all business activity taxes. H.R. 2992, § 2.

[38] H.R. 2992, § 3.

[39] *See* H.R. 2992, § 4 (emphasis added) ("If, in computing the net income tax or other business activity tax liability of a person for a taxable year, the net income or other economic results of affiliated persons is taken into account, . . . and, if [the state's] generally applicable methodology employs an apportionment formula . . . the numerator or numerators shall include the factors attributable to the state of *only those persons that are themselves subject to taxation by the State* pursuant to the provisions of this Act and subject to all other legal constraints on State taxation of interstate or foreign commerce."); Koklanaris, *supra* note 36, at 515 ("[BATSA would] limit the apportionment of income of a unitary group of affiliated businesses to only that portion of the business activity conducted by physically present businesses.").

[40] *See Federal Legislation — Business Activity Tax Simplification Act of 2013 Introduced*, PricewaterhouseCoopers, Aug. 29, 2013, http://www.pwc.com/en_US/us/state-local-tax/newsletters/mysto/assets/pwc-business-activity-tax-simplification-act-2013-introduced.pdf (noting that "[a]lthough the likelihood of passage as a standalone bill remains questionable, it remains possible that BATSA may be included in a larger package addressing multiple state issues"); *Business Activity Tax Simplification Act of 2011*, WTAS, June 2011, http://www.wtas.com/newsletter/2011/june/simplification.php (discussing the 2011 bill and how "[g]iven the taxpayer friendly nature of The Bill, it likely faces stiff opposition in Congress"). The unlikelihood of BATSA's passage is evidenced by the fact that it has been introduced in Congress repeatedly since the year 2000.

UDITPA[41] and the Multistate Tax Compact.[42] Both of these model acts, none of which has any legal effect unless adopted by the state legislatures, have common objectives: achieve uniformity in state taxation of multistate corporations, establish an equitable apportionment of tax bases, and avoid multiple taxation.[43] UDITPA has been adopted, in whole or in part, by approximately 20 states,[44] and the Compact has the following membership: 17 compact members,[45] 6 sovereignty members,[46] and 25 associate and project members.[47]

The Compact incorporates UDITPA, which provides a model and uniform method for dividing the total tax base of a multistate corporation among the

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[41] Unif. Div. of Income for Tax Purposes Act (1957). UDITPA was adopted by the Commissioners on Uniform State Laws and the American Bar Association in 1957. It is incorporated into Article IV of the Multistate Tax Compact.

[42] Multistate Tax Compact (Multistate Tax Comm'n 1967). The Supreme Court upheld the constitutionality of the Compact in U.S. Steel Corp. v. Multistate Tax Comm'n, 434 U.S. 452, 452 (1978). The Compact was drafted in 1966 by a group of state officials and became effective in 1967. The Compact created the Multistate Tax Commission, *see* Multistate Tax Compact art. VI (Multistate Tax Comm'n 1967), "an intergovernmental state agency working on behalf of states and taxpayers to administer, equitably and efficiently, tax laws that apply to multistate and multinational enterprises." *About the Multistate Tax Commission*, Multistate Tax Comm'n, last accessed Mar. 15, 2014, http://www.mtc.gov/About.aspx?id=40.

[43] *See* M. Bernadette Welch, Annotation, *Construction and Application of Uniform Division of Income for Tax Purposes Act (UDITPA)—Determination of Business Income*, 74 A.L.R. 6th 1 (2012); Multistate Tax Compact art. I (Multistate Tax Comm'n 1967).

[44] As of April 21, 2014, of the states imposing a corporate income tax, 20 (including the District of Columbia) have adopted UDITPA. *See Legislative Fact Sheet - Division of Income for Tax Purposes*, Uniform Law Commission, last accessed Apr. 21, 2014, http://www.uniformlaws.org/LegislativeFactSheet.aspx?title=Division%20of%20Income%20for%20Tax%20Purposes. Despite adoption of UDITPA, a fair number of states have later enacted laws modifying certain UDITPA provisions. *See* R. Gregory Roberts & Rebecca M. Ulich, *To Be or Not to Be: Nonbusiness Income*, Morrison & Foerster News - State + Local Tax Insights, at 2, Summer 2012 (explaining how many of the states that have adopted UDITPA have modified UDITPA's definition of business income).

[45] Compact members are states that have incorporated the Compact into their state law. *Definition of Member States*, Multistate Tax Comm'n, last accessed Apr. 21, 2014, http://www.mtc.gov/About.aspx?id=1818.

[46] Sovereignty members are states that support the Compact by participating in and providing financial support for the general activities of the Multistate Tax Commission. *Definition of Member States*, Multistate Tax Comm'n, last accessed Apr. 21, 2014, http://www.mtc.gov/About.aspx?id=1818.

[47] "Associate members are states that participate in Commission meetings and otherwise consult and cooperate with the Commission and its other member states or, as project members, participate in Commission programs or projects." *Definition of Member States*, Multistate Tax Comm'n, last accessed Apr. 21, 2014, http://www.mtc.gov/About.aspx?id=1818. Although not noted in the Multistate Tax Commission's website regarding Compact membership, there are a number of states that have repealed the Compact from their codes. *See* Amy Hamilton, *Multistate Tax Compact Roundup: Utah Set to Withdraw from Multistate Tax Compact*, 71 St. Tax Notes (TA) 441 (Feb. 24, 2014); Amy Hamilton, *District of Columbia Set to Repeal Multistate Tax Compact*, 69 St. Tax Notes (TA) 264 (Jul. 29, 2013).

states in which it does business.[48] One of the UDITPA features is the provision for the apportionment of "business income" and allocation of "nonbusiness income."[49] For apportionment purposes, UDITPA provides an equally-weighted three-factor formula: "All business income shall be apportioned . . . by multiplying the income by a fraction the numerator of which is the property factor plus the payroll factor plus the sales factor and the denominator of which is three."[50] Each factor is calculated by dividing the taxpayer's property (or payroll or sales) within the state by the taxpayer's property (or payroll or sales) everywhere.[51] Many states still use a multifactor apportionment formula to apportion income;[52] however, there is a trend toward weighing the sales factor more heavily than the other factors[53] or alternatively, switching to a single-factor apportionment formula based on sales.[54]

The apportionment–allocation distinction provided for in UDITPA and reflected in most states' taxation regimes is a consequence of the unitary business requirement explored in Part II.C—finding the existence of a unitary business is a prerequisite to applying an apportionment formula; the business income of that unitary business can be apportioned, while the nonbusiness income has to be allocated.[55]

C. *Methods of Reporting and the Unitary Business Concept*

States employ different methods to compute the tax liability of a corporation that is part of a group of related corporations: separate reporting, consolidated reporting, and combined reporting.[56] Under the separate reporting method, each corporation with nexus with the state files its own corporate

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[48] *See* Multistate Tax Compact art. IV (Multistate Tax Comm'n 1967).

[49] *Id.* The apportionment of business income and allocation of nonbusiness income are explored in more detail in Part III.A.

[50] Unif. Div. of Income for Tax Purposes Act § 9 (1957).

[51] *Id.* §§ 10, 13, 15.

[52] *See* Hellerstein, *supra* note 10, ¶ 9.02 tbl.9–3.

[53] Arizona, District of Columbia, Florida, Maryland, Massachusetts, and Virginia are some of the states providing for the apportionment of income using a three-factor formula based on property, payroll, and double-weighted sales. *See id.*

[54] For example, Colorado, Georgia, Illinois, Indiana, Iowa, Maine, Nebraska, Oregon, South Carolina, and Wisconsin have adopted a single-sales factor apportionment formula. *See id.* New Jersey, for instance, used to have a three-factor formula with double-weighted sales but starting on January 2, 2014, it is on 100% sales apportionment formula. *See* Deloitte, *New Jersey Phases in Single Sales Factor*, Apr. 28, 2011, https://www.deloitte.com/assets/Dcom-United-States/Local%20Assets/Documents/Tax/us_tax_multistate_New%20Jersey_04-29-2011.pdf. Other states, like California, Missouri, and Utah allow corporations to apply the single-sales factor method on an elective basis. *See* Hellerstein, *supra* note 10, ¶ 9.02 tbl. 9-3.

[55] *See* Hellerstein, *supra* note 10, ¶ 9.01 (explaining that "the unitary business principle finds expression in the line that the states have drawn between allocable and apportionable income").

[56] States vary on their requirements on reporting methods; this is just a basic categorization of reporting methods. *See* Timothy C. Kimmel, *An Overview of the Group Reporting Regimes in Use Today*, 2008 St. & Loc. Tax Law. 21, 23 (2008).

tax return, regardless of whether the corporation is part of a group of related corporations.[57] If the group of related corporations qualifies as an affiliated group,[58] it may have the option to elect to file a consolidated state tax return, depending on the provisions of each state.[59] Mostly, whether the state allows a corporation to file a consolidated return turns on whether that corporation was part of a federal consolidated return.[60] If the election is made, the state corporate tax return includes all of the affiliates that are taxable within the state.[61]

The third most common method of reporting employed by states is combined reporting.[62] While a consolidated return depends on the degree of stock ownership within the affiliated group, a combined return depends on the existence of a unitary business.[63] Also, a consolidated return is often confined to those members of a corporate group that have nexus with the state,[64] but a combined return may include entities that are not separately taxable in the state but who are part of the unitary group.[65] For purposes of this Comment, the issue of the *Joyce–Finnigan* debate only arises in those situations where

[57] *Id.*

[58] Generally, an affiliated group is a group of corporations connected through stock ownership and that has a common parent corporation, which directly owns at least 80% of the stock in at least one of the corporations in the group. *See* I.R.C. § 1504(a). At least 80% of the stock of every other corporation in the group must also be owned directly by one or more of the other corporations in the group. § 1504(a).

[59] The meaning of a consolidated return is inconsistent in the state tax context. Kimmel, *supra* note 56, at 43.

[60] Hellerstein, *supra* note 10, ¶ 8.11[1]; *see, e.g.*, Ala. Code § 40–18–39(c)(1) (West, Westlaw through Act 2014-68 of the 2014 Reg. Sess.); Ark. Code Ann. § 26–51–805 (West, Westlaw through 2013 Reg. and 1st Ex. Sess.); Iowa Code Ann. § 422.37 (West, Westlaw through 2013 Reg. Sess.); Ky. Rev. Stat. Ann. § 141.200(9)–(14) (West, Westlaw through 2013 Sess.).

[61] *But see* Ariz. Rev. Stat. Ann. § 43–947(A) (West, Westlaw through the 1st Reg. and 1st Special Sess. of the 51st Leg. (2013)) (providing that the common parent of an affiliated group filing a federal consolidated return is permitted to file an Arizona consolidated return regardless of whether each member of the affiliated group is subject to Arizona tax).

[62] The following states have combined reporting provisions: Alaska, Arizona, California, Colorado, District of Columbia, Hawaii, Idaho, Illinois, Kansas, Maine, Massachusetts, Michigan, Minnesota, Mississippi, Montana, Nebraska, New Hampshire, New Mexico, New York, North Dakota, Oregon, Utah, Vermont, Virginia, West Virginia, and Wisconsin. Hellerstein, *supra* note 10, ¶ 8.11 n.1125.

[63] Hellerstein, *supra* note 10, ¶ 8.11[1]. When the group of related corporations is engaged in a unitary business, combined reporting is often mandatory. *Id.*; *see, e.g.*, Ariz. Admin. Code § 15–2D–401(B) (West, Westlaw through June 2013); Cal. Code Regs. tit. 18, § 25106.5–11(a) (West, Westlaw through Register 2014, No. 33).

[64] Generally, states with consolidated return reporting regimes either follow the federal consolidated affiliated group or allow a nexus-based consolidated return where only those entities in the federal consolidated group with nexus in the state are included in the state consolidated return. *See* William L. Goldman, Kenneth C. Brown & Laura L. Farrell-Legrand, *Income Taxes: Consolidated Returns and Combined Reporting, Detailed Analysis*, 1130-2d Tax Mgmt. Port. (BNA) B-8 (2009).

[65] Hellerstein, *supra* note 10, ¶ 8.11[1]; *see* Kimmel, *supra* note 56, at 31.

the state requires combined reporting for a unitary group. The *Joyce–Finnigan* issue arises when formulary apportionment is permitted, and a unitary business must be present before formulary apportionment can be required.

The unitary business principle provides the "minimum link" required by the Constitution before a state can impose an income tax.[66] If a corporate taxpayer is engaged in separate and discrete activities in different states, then separate accounting can be used to calculate the taxpayer's income within each state, and application of a formula is neither necessary nor appropriate.[67] On the other hand, when the taxpayer is engaged in a unitary business across different states, separate accounting is neither practical nor appropriate.[68]

The unitary combined reporting method looks beyond the legal distinctness of individual entities and treats the group as one business enterprise.[69] The definition of what constitutes a unitary business varies among jurisdictions but generally, it involves a business that has "a high degree of interrelationship and interdependence among the activities of the company or related companies."[70] The Court has come short of providing a precise definition of a unitary business; however, it has given some guidance, although ultimately deferring to the states' judgment of what qualifies as a unitary group.[71] Some of the considerations relevant in determining whether there is a unitary business include unity of ownership,[72] unity of use and management,[73] and unity

[66] *See* Mobil Oil Corp. v. Commissioner of Taxes of Vt., 445 U.S. 425, 439 (1980) ("[T]he linchpin of apportionability in the field of state income taxation is the unitary business principle.").

[67] For a general discussion of separate accounting, see HELLERSTEIN, *supra* note 10, ¶ 8.03. In the early years of the corporate income tax, separate accounting was perceived as the most accurate method of determining the income attributable to each state. *Id.* With the expansion of multistate businesses and increasing complexity of their activities across state lines, separate accounting seemed less and less of a viable and practical option. Today, all states imposing a corporate income tax require apportionment of income from unitary businesses. *Id.*

[68] *See* Container Corp. of Am. v. Franchise Tax Bd., 463 U.S. 159, 165 (1983) ("The unitary business/formula apportionment method . . . rejects geographical or transactional accounting, and instead calculates the local tax base by first defining the scope of the 'unitary business' of which the taxed enterprise's activities in the taxing jurisdiction form one part, and then apportioning the total income of that 'unitary business' between the taxing jurisdiction and the rest of the world on the basis of a formula . . . .").

[69] Kimmel, *supra* note 56, at 32.

[70] *Id.*

[71] *See Container Corp. of Am.*, 463 U.S. at 175.

[72] Butler Bros. v. McColgan, 111 P.2d 334, 341 (Cal. 1941), *aff'd*, 315 U.S. 501 (1942).

[73] *Id.* (finding evidence of unity of use in the entity's "centralized executive force and general system of operation").

of operations.[74] Furthermore, the presence within the group of "functional integration, centralization of management, and economies of scale" has also been emphasized by the Court as evidencing a unitary business.[75] Given the Court's vague and general guidance, the Multistate Tax Commission adopted a definition of unitary business[76] with the goal of providing more precision to this inquiry; however, the relevance of the Multistate Tax Commission's definition is questionable as states continue to diverge on their definition and interpretation of the unitary business concept.[77]

Part II of this Comment has provided the context underlying the *Joyce–Finnigan* debate. States are constrained by federal constitutional provisions in their taxation of corporate taxpayers engaged in interstate commerce, but the Court has repeatedly upheld the use of formulary apportionment for purposes of dividing a multistate taxpayer's income among taxing jurisdictions. Furthermore, the discussion in Part II previewed the many areas where the states diverge and introduced the three main steps that have been taken toward uniformity. Finally, this Part also discussed the concept of a unitary business, which is a prerequisite for a state to apply an apportionment formula. With this context in mind, Part III introduces and analyzes

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[74] Butler Bros. v. McColgan, 315 U.S. 501, 508 (1942) (finding unity of operations as a result of the entity's functional integration and centralized purchasing division). The "three unities" test was articulated by the California Supreme Court in 1941 and became one of the most frequently used definitions of a unitary business. *See Butler Bros.*, 111 P.2d at 341; HELLERSTEIN, *supra* note 10, ¶ 8.09[1]. The California Supreme Court also articulated the "dependency and contribution" test, which provides that there is a unitary business when "the operation of the portion of the business done within the state is dependent upon or contributes to the operation of the business done without the state." Edison Cal. Stores, Inc. v. McColgan, 183 P.2d 16, 21 (Cal. 1947); *accord In re* Nat'l Coop. Refinery Ass'n, 44 P.3d 398, 404 (Kan. 2002); *see* HELLERSTEIN, *supra* note 10, ¶ 8.09[1].

[75] *See* ASARCO Inc. v. Idaho State Tax Comm'n, 458 U.S. 307, 317 (1982) (citing Mobil Oil Corp. v. Commissioner of Taxes of Vt., 445 U.S. 425, 438 (1980)); F.W. Woolworth Co. v. Taxation and Revenue Dep't of N.M., 458 U.S. 354, 364 (1982) (citing *Mobil Oil Corp.*, 445 U.S. at 438). More recently, yet another component of the unitary business inquiry has developed, which highlights the degree of nonconformity and variability on this issue. Under the "operational function" test, there is a unitary business when "the capital transaction serve[s] an operational rather than an investment function," even if there is no "unitary relation between the payor and the payee." Allied-Signal, Inc. v. Director, Div. of Taxation, 504 U.S. 768, 787 (1992) (citations omitted); *see also* MeadWestvaco Corp. *ex. rel.* Mead Corp. v. Ill. Dep't of Revenue, 553 U.S. 16, 29 (2008) (citations omitted) (clarifying that the concept of operational function does not "modify the unitary business principle by adding a new ground for apportionment" but rather "simply recognizes that an asset can be part of a taxpayer's unitary business even if . . . a 'unitary relationship' does not exist between the 'payor and payee.'). *See generally* Stuart R. Harding, *The Scoop on the Unitary Business Principle: How Blue Bell's Corporate Restructuring Increased the Scope of Out-of-State Taxation in* Blue Bell Creameries, LP v. Roberts, 64 TAX. LAW. 989, 992-95 (2011) (discussing the origins and development of the unitary business principle).

[76] MULTISTATE TAX COMM'N REGULATIONS, Reg. IV.1(b)(1).

[77] *See* WILLIAM F. FOX & LEANN LUNA, COMBINED REPORTING WITH THE CORPORATE INCOME TAX: ISSUES FOR STATE LEGISLATURES 12-13 (Nov. 2010) (noting the significant variation in the way states and courts define unitary business).

the *Joyce–Finnigan* debate, its origins in California, and how it has developed in California and other jurisdictions.

III. The *Joyce–Finnigan* Debate

Part III of this Comment explores the *Joyce–Finnigan* debate. First, Part III.A provides an overview of how states generally divide the income of a multistate corporate taxpayer: allocation of nonbusiness income and apportionment of business income through use of a formula. Part III.B discusses how the *Joyce–Finnigan* debate has developed in California, where it originated. Finally, Part III.C explores the *Joyce–Finnigan* debate in other jurisdictions and comments on how its scope has extended beyond the limited context in which it arose in California.

A. *Basics of Division of Income Statutes*

Once the unitary group is identified, the group calculates its tax base and tax liability on a combined basis. Generally, states follow the UDITPA approach and provide for allocation and apportionment to divide the corporation's tax base among the various taxing jurisdictions.[78] Approximately two-thirds of the states, including the District of Columbia, that levy a corporate income tax classify income as business or nonbusiness pursuant to UDITPA.[79] Nonbusiness income—defined as all income other than business income[80]—is allocated to the particular state or states that are considered the source of the income.[81] For instance, rents and capital gains or losses from real property that constitute nonbusiness income are allocated to the state in which the property is located.[82]

On the other hand, when income is apportioned, it is divided among the several states based on an apportionment formula. UDITPA provides for an equally-weighted three-factor formula based on the property, payroll, and sales factors, but the majority of states weigh the sales factor more heavily and some have even transitioned to a single-factor apportionment formula based on sales.[83] There is no doubt that the sales factor, which is the focus of this Comment, is the most controversial of the factors employed to apportion

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[78] Hellerstein, *supra* note 10, ¶ 9.01.

[79] Roy E. Crawford & Russell D. Uzes, *Income Taxes: The Distinction Between Business and Nonbusiness Income*, 1140-2d Tax Mgmt. Port. (BNA) 1140.01 (2014).

[80] Unif Div. of Income for Tax Purposes Act § 1(e) (1957). "'Business income' means income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations." *Id.* § 1(a).

[81] *Id.* § 4.

[82] *Id.* §§ 4-6.

[83] *See supra* notes 52-54 and accompanying text.

income,[84] especially as the states continue to give it greater weight in their apportionment formulas. One controversy is with respect to what exactly goes into the sales factor and not surprisingly, there is variation in how the states define sales (or receipts).[85] In general, the sales factor "covers receipts from services, rentals, royalties, sales of stock, and business operations generally."[86]

Another controversy—the one explored in this Comment—is whether the state follows the *Joyce* or *Finnigan* approach, which governs which members of the unitary group must include their sales in the state's sales factor numerator. An illustration is helpful to exemplify the ongoing *Joyce–Finnigan* debate: A unitary group must file a combined corporate tax return in State X, and the unitary group includes entities that are not taxable in State X (either because of lack of nexus or Public Law 86-272). If the entities that are not separately taxable in State X make sales into the state, are these sales included in the numerator of the unitary group's sales factor? As discussed in Part III.B, California has switched positions on this question several times, first answering "no" in *Joyce* and later taking the opposite position in *Finnigan*.

B. *The* Joyce–Finnigan *Debate in California*

The *Joyce–Finnigan* debate arose in the context of sales of tangible personal property and the application of the throwback rule. When a corporation is engaged in the sale of goods in multiple states, the states with the power to tax the corporation must have a way of assigning each sale made by the corporation to a particular state in order to properly compute the corporation's sales factor. There used to be a host of different tests for attributing these sales,[87] but currently, the vast majority of states follow the destination rule when attributing receipts from sales of tangible personal property for purposes of calculating the sales factor of the apportionment formula;[88] the destination rule is also the approach taken in UDITPA.[89]

Under the destination rule, sales are attributed to the state where the goods are shipped (*i.e.*, the state where the customer is located).[90] Accordingly, receipts from the sale of tangible personal property are included in the numerator of the sales factor of the destination state. One problem is evident: when the corporation whose sales are being attributed to a destination state in which the corporation is not taxable, we have the problem of nowhere

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[84] Hellerstein, *supra* note 10, ¶ 9.18 ("The receipts or sales factor has been the focal point of the major controversies that have arisen over the implementation of the apportionment factors.").

[85] *Id.*

[86] *Id.* UDITPA defines "sales" as "all gross receipts of the taxpayer not allocated." Unif. Div. of Income for Tax Purposes Act § 1(g) (1957).

[87] John S. Warren, *Income Taxes: Principles of Formulary Apportionment*, 1150.07 Tax Mgmt. Port. (BNA) C-1 (1994).

[88] *See* Hellerstein, *supra* note 10, ¶ 9.18[1].

[89] Unif. Div. of Income for Tax Purposes Act § 16 (1957).

[90] *"Nowhere Income" and the Throwback Rule*, Inst. on Tax & Econ. Pol'y, Aug. 2011, http://www.itepnet.org/pdf/pb39throw.pdf.

income—absent some other mechanism, those sales would escape taxation. A corporation may not be taxable in the destination state because it either lacks the minimum connection (nexus) required by the Federal Constitution or is protected from taxation under Public Law 86-272.

The most common mechanism by which states deal with the problem of nowhere income is through application of the throwback rule.[91] Under the throwback rule, when sales of tangible personal property are not taxable in the destination state, the sales are "thrown back" to the state of origin (*i.e.*, the state that is the source of the sale).[92] In the context of combined reporting by a unitary group, application of the throwback rule is complicated by the inconsistency in how states interpret who is a "taxpayer" for purposes of applying the destination state and throwback rules. For example, Corporations X and Y are engaged in a unitary business and are taxable in State A. Corporation X is involved in the sale of tangible personal property shipped from State A (the origin state) to State B (the destination state); Corporation X is not independently taxable in State B, but Corporation Y is and both States A and B have combined reporting regimes for unitary groups. When determining whether the throwback rule is applicable, who is the taxpayer: Corporation X individually or the unitary group as a whole? If only Corporation X is the taxpayer, then the sales to State B must be thrown back to State A (origin state) because Corporation X is not taxable in the destination state, resulting in the problem of nowhere income. However, if both Corporations X and Y are viewed as a unit (*i.e.*, as one taxpayer), then the throwback rule should not apply because Corporation Y is taxable in State B. In a nutshell, the former is the approach taken in *Joyce*, and the latter is the approach taken in *Finnigan*.

1. *Joyce*

In *In re Joyce, Inc.*, Joyce was a California corporation involved in the manufacture and sale of footwear and operated as a member of a unitary group with activities both within and without the state.[93] The company had its principal office in Ohio and manufacturing plants in Ohio and Indiana. The corporation's sole contact in California was the presence in that state of two sale representatives who solicited orders but did not accept them; all orders were accepted and processed in the company's headquarters in Ohio. Joyce's stock was virtually entirely owned by United States Shoe Corporation (U.S. Shoe), whose principal office and manufacturing plants were outside California. Because U.S. Shoe was an Ohio corporation and its activities in California were limited to the solicitation of sales, the company was exempt

[91] There is also a throwout rule, which "excludes from overall sales any sales that are not assigned to any state." *Id.* The throwout rule is currently followed by only two states. *Id.*

[92] *Id.*

[93] *In re* Joyce, Inc., No. 66-SBE-070, 1966 WL 1411 (Cal. State Bd. of Equalization Nov. 23, 1966), *overruled by Finnigan II*, No. 88-SBE-022-A, 1990 WL 15164 (Cal. State Bd. of Equalization Jan. 24, 1990), *overruled by In re* Huffy Corp., No. 99-SBE-005, 1999 WL 386938 (Cal. State Bd. of Equalization Apr. 22, 1999).

from taxation in California under Public Law 86-272.[94] Joyce was not protected by the federal statute because it was incorporated in California, and the protections of Public Law 86-272 do not preclude a state from imposing an income tax on corporations incorporated under the laws of the state.[95]

The California State Board of Equalization (SBE) found that Joyce and U.S. Shoe (along with three other subsidiaries of U.S. Shoe) were engaged in a unitary business.[96] However, unlike the determination issued by the California Franchise Tax Board (FTB), the SBE held that the receipts from the sale of goods shipped to California customers by U.S. Shoe could not be included in the sales factor numerator, unless the corporation itself was subject to an income tax in California, even though a member of the unitary group (Joyce) was taxable in the state.[97]

2. *Finnigan*

In *In re Finnigan Corp.*, the SBE dealt with the throwback rule in the context of two corporations engaged in a unitary business.[98] Finnigan was a California corporation engaged in a unitary business that manufactured and sold scientific instruments in various states through subsidiaries. Disc, one of Finnigan's subsidiaries, was also a California corporation, and it sold goods manufactured in California to customers inside and outside the state. Disc was only taxable in California; however, Finnigan was taxable both in California and in the other states into which Disc's sales were made.

The FTB, relying on *Joyce*, applied the throwback rule to this situation.[99] It concluded that because Disc, a separate legal entity, was not taxable in states other than California, Disc's out-of-state sales were thrown back to California and therefore included in the combined group's sales factor numerator.[100] The FTB interpreted the term taxpayer as used in the throwback rule as referring only to the company that made the sales (Disc).[101] The SBE reversed the FTB's determination and overruled *Joyce*.[102] It held that the term taxpayer referred to the combined unitary group as a whole.[103] Because another member of the unitary group (Finnigan) was taxable in other states besides

[94] *Id.*
[95] *See* 15 U.S.C. § 381(b) (2012).
[96] *Joyce,* 1966 WL 1411, at *3.
[97] *See id.* at *4.
[98] *See* (*Finnigan I*), No. 88-SBE-022, 1988 WL 152336 (Cal. State Bd. of Equalization Aug. 25, 1988), *aff'd* (*Finnigan II*), No. 88-SBE-022-A, 1990 WL 15164 (Cal. State Bd. of Equalization Jan. 24, 1990), *overruled by In re* Huffy Corp., No. 99-SBE-005, 1999 WL 386938 (Cal. State Bd. of Equalization Apr. 22, 1999).
[99] *See id.* at *1.
[100] *See id.*
[101] *See id.*
[102] *See Finnigan II*, 1990 WL 15164, at *3.
[103] *See Finnigan I*, 1988 WL 152336, at *3.

California where Disc made sales, the sales should not be thrown back to California and included in the sales factor numerator.[104]

3. *Present State of the Law in California*

California has been at the forefront of the *Joyce–Finnigan* debate and has switched sides a number of times. After the *Finnigan* decision in 1990, California followed the *Finnigan* approach[105] until 1999 when it decided *In re Huffy Corp.*[106] In *Huffy Corp.*, the SBE was confronted with basically the same fact pattern as in *Joyce* (a member of a unitary group filing a combined return in California made sales into California but the member was protected from taxation under Public Law 86-272) and decided to leave *Finnigan* behind and once again follow the *Joyce* approach.[107] The SBE reasoned that despite the "theoretically good reasons" for the *Finnigan* rule, California should go back to *Joyce* in the interest of uniformity given that nearly all other states at the time continued to follow *Joyce*.[108] Finally, since January 1, 2011, California is back to the *Finnigan* rule, given its amendment to section 25135 of its Revenue and Taxation Code.[109]

Under section 25135, inbound sales of tangible personal property (*i.e.*, California-destination sales) by a member of a unitary group are included in the California sales factor whenever a member of the unitary group is taxable in California, regardless of whether the member making the sale is independently subject to tax in California.[110] For outbound sales of tangible personal property (*i.e.*, where California is the origin state), sales are not thrown back to California even though the member making the sale is not taxable in the

[104] *See id.*

[105] *See In re* NutraSweet Co., No. 87N-1645-PS, 1992 WL 321383 (Cal. State Bd. of Equalization Oct. 29, 1992). In *NutraSweet Co.*, the SBE was presented with the same fact scenario as in *Joyce* but this time, it held, following *Finnigan*, that the California-destination sales of a group member that was not taxable in California under Public Law 86-272 were included in the combined group's sales factor numerator because another member of the group was taxable in California.

[106] *In re* Huffy Corp., No. 99-SBE-005, 1999 WL 386938 (Cal. State Bd. of Equalization Apr. 22, 1999).

[107] *Id.* at *3. However, because taxpayers had relied on the *Finnigan* decision for the past eight years, the SBE's decision to readopt the *Joyce* rule was prospective only. *Id.* at *4.

[108] *Id.* at *3.

[109] *See* Cal. Rev. & Tax. Code § 25135 (West, Westlaw through Ch. 299 of Reg. Sess., Res. Ch. 1 of 2013-2014 2d Ex. Sess.).

[110] *Id.* § 25135(b).

destination state so long as at least one member of the unitary group is taxable in that state.[111]

C. *The* Joyce–Finnigan *Debate Beyond California*

The *Joyce* rule is currently followed by approximately 15 of the states with combined reporting provisions,[112] while *Finnigan* is followed by about ten states.[113] However, in recent years, there has been a trend toward adoption of the *Finnigan* rule, and commentators expect more states to adopt *Finnigan*, primarily for revenue-raising purposes.[114] Furthermore, while the *Joyce–Finnigan* debate originated in a limited context—sales of tangible personal property and the throwback rule—its application today by the states is much broader.

One example of how the *Joyce–Finnigan* debate is no longer limited to application of the throwback rule is *In re Disney Enterprises, Inc. v. Tax Appeals Tribunal of the State*.[115] In *Disney Enterprises, Inc.*, Disney filed a combined tax return in New York.[116] One of Disney's subsidiaries, Buena Vista Home Video (Video), sold movie cassettes to retailers in New York, but Video's receipts from these sales were not included in the combined group's sales factor numerator because Video's New York activities were protected by Public Law 86-272.[117] New York does not have a throwback rule; however, it referred to "the California experience" and applied the *Finnigan* rule.[118] The court held that Video's receipts from the New York-destination sales should be included in the group's sales factor numerator.[119] First, the court reasoned, including Video's receipts in the sales factor numerator was not a tax on Video itself but rather, it was just an attempt to "best measure the combined group's

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[111] *Id.* Even though California now follows *Finnigan* for the treatment of sales of tangible personal property, it is still a *Joyce* state for other purposes. Besides sales of tangible personal property, the *Joyce–Finnigan* issue also affects other tax attributes, like net operating losses and credits. *See* Fox & Luna, *supra* note 77, at 14. States may require one approach for apportionment purposes while applying the other approach for other purposes. *Id.* (providing an example of the application of *Joyce–Finnigan* in the context of NOLs and credits; under *Joyce*, NOLs and credits generated by an entity would be available only to the entity generating the loss or credit, while under *Finnigan*, it would be available to the group as a whole).

[112] Colorado, Hawaii, Idaho, Illinois, Minnesota, Mississippi, Montana, Nebraska, New Hampshire, New Mexico, North Dakota, Oregon, Vermont, Virginia, and West Virginia.

[113] Arizona, California, Indiana, Kansas, Maine, Massachusetts, Michigan, New York, Utah, and Wisconsin. *But see*, *supra* note 111 (regarding California).

[114] *See* Fox & Luna, *supra* note 77, at 14.

[115] *See* Disney Enters., Inc. v. Tax Appeals Tribunal of the State, 888 N.E.2d 1029 (N.Y. 2008).

[116] *Id.* at 1030-31.

[117] *Id.* at 1031-32. Video's only activities in New York were solicitation of sales; it did not take orders, collect money, or accept returned items, and it did not own or rent any property in the state. *Id.* at 1033.

[118] *See id.* at 1038-40.

[119] *See id.* at 1033.

taxable in-state activities" under unitary business principles.[120] Second, the court concluded that Public Law 86-272 did not preclude including Video's receipts in the numerator of the sales factor because the combined group as a whole—rather than Video alone—exceeded the protections of Public Law 86-272.[121] Accordingly, Video's New York-destination sales should be taken into account when computing the unitary group's apportionment percentage, increasing Video's New York tax liability from the minimum of $1,500 to over $1.3 million for the six years at issue (including interest).[122]

One example of how the *Joyce–Finnigan* debate has expanded beyond sales of tangible personal property to include other revenue streams is the recent legislative enactments by Maine,[123] Massachusetts,[124] and Wisconsin.[125] With states like these three switching to combined reporting and adopting the *Finnigan* rule, it is increasingly important for states to achieve some uniformity by at least settling on either *Joyce* or *Finnigan*, as analyzed in Part IV.

Finally, UDITPA, which endorses the destination and throwback rules, does *not* address the problem of whether *Joyce* or *Finnigan* should be followed. The Multistate Tax Commission did embrace the *Joyce* approach but

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[120] *Id.* at 1033-36. The concurring opinion disagreed with this part of the court's reasoning, concluding that "including a company's receipts in the numerator of the apportionment fraction effectively imposes a tax on that company." *Id.* at 1041 (concurring opinion).

[121] *See id.* at 1036-38 (majority opinion). Specifically, Public Law 86-272 provides that no state has the power to impose an income tax on the income derived within the state by any *person* from interstate commerce if the only business activities conducted within the state are protected under the statute. *See* 15 U.S.C. § 381 (2012). In *Disney Enterprises, Inc.*, the court held that the term "person" as used in the statute referred to the Disney unitary group, not Video alone. *See Disney Enters., Inc.*, 888 N.E.2d at 1036. This interpretation of Public Law 86-272 is in accord with Arizona's interpretation of the statute, and Arizona also follows the *Finnigan* approach. *See* Ariz. Dep't of Revenue v. Cent. Newspapers, Inc., 222 Ariz. 626, 633 (Ct. App. 2009); Airborne Navigation Corp. v. Ariz. Dep't of Revenue, No. 395-85-I, 1987 WL 50031, at *2 (Ariz. B.T.A. Feb. 5, 1987) ("It would not be stretching [the definition of "person" in Public Law 86-272] to say that [Airborne] and the other companies in the unitary business group could be considered one 'person' for purposes of this law.").

[122] *See Disney Enters., Inc.*, 888 N.E.2d at 1033.

[123] *See* Me. Rev. Stat. Ann. tit. 36, § 5211(14) (West, Westlaw through Ch. 453 of the 2013 2d Reg. Sess. of the 126th Leg.) (providing that the numerator of the sales factor is the total sales of the taxpayer in Maine and the denominator is the total sales of the taxpayer everywhere, where "total sales of the taxpayer" includes sales of the taxpayer and of any member of its affiliated group with which the taxpayer conducts a unitary business). Maine also exemplifies the recent trend toward adoption of the *Finnigan* rule. Prior to January 1, 2010, Maine followed the *Joyce* approach. *See* Great N. Nekoosa Corp. v. State Tax Assessor, 675 A.2d 963, 964 (Me. 1996) (holding that sales by a Maine taxpayer to a destination state where the taxpayer was not taxable were thrown back to Maine even though an affiliate of the taxpayer was taxable in the destination state); *see also* Mandy Rafool & Todd Haggerty, *State Tax Actions 2010, Appendix E* 60 St. Tax Notes (TA) 795, 808 (June 13, 2011) (noting that Maine's adoption of the *Finnigan* approach results in tax revenue of $3.0 million for fiscal year 2011 and $3.2 million for fiscal year 2012).

[124] Mass. Gen. Laws Ann. ch. 63, § 32B(a) (West, Westlaw through Ch. 43 of the 2014 2d Ann. Sess.).

[125] Wis. Stat. Ann. § 71.255 (West, Westlaw through 2013 Act 135).

only in the context of sales of tangible personal property for purposes of determining whether activities conducted within a state are protected by Public Law 86-272.[126]

IV. Analysis

This Comment argues in Part IV.A that though complete uniformity in the area of state taxation of multistate corporations is likely an unrealistic goal, a significant area of nonuniformity that leads to problematic results is the *Joyce–Finnigan* issue. Achieving consistency in this area would benefit taxpayers and states alike by establishing a more equitable taxation regime and reducing complexity. Part IV.B proposes that even though neither the *Joyce* nor the *Finnigan* rule is free of flaws, *Joyce* is the better rule primarily because *Finnigan* effectively results in a state taxing income that would otherwise be out of its reach under federal or constitutional limitations. Finally, Part IV.C argues that the most realistic and practical option for settling the *Joyce–Finnigan* debate is for the Multistate Tax Commission to revise its apportionment provisions to adopt the *Joyce* rule.

A. *Ideal Solution: Uniformity*

Uniformity is generally desirable in most areas of the law,[127] and state taxation of multistate taxpayers is no exception.[128] However, achieving complete uniformity in this area seems highly unlikely (if not entirely unrealistic) given the significant areas of nonuniformity currently present in state taxation of a combined group of corporations. For example, states differ on what constitutes a unitary business, composition of their apportionment formulas, classification of business and nonbusiness income, the definition of sales, and of course, the adoption of *Joyce* or *Finnigan*. With an increasing number of states adopting combined reporting regimes for a group of corporations engaged in a unitary business,[129] the *Joyce–Finnigan* debate is increasingly important

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[126] *Statement of Information Concerning Practices of Multistate Tax Commission and Signatory States under Public Law 86-272*, Multistate Tax Comm'n, last accessed Mar. 1, 2014, http://www.mtc.gov/uploadedFiles/Multistate_Tax_Commission/Uniformity/Uniformity_Projects/A_-_Z/StatementofInfoPublicLaw86-272.pdf.

[127] For example, in the field of commercial and business law, the Uniform Commercial Code (UCC) plays a crucial role. Unif. Commercial Code, http://www.law.cornell.edu/ucc; *see* Lawrence J. Bugge, *Commercial Law, Federalism, and the Future*, 17 Del. J. Corp. L. 11, 13 (1992) (describing the UCC as "the most spectacular success story in the history of American law").

[128] *See* Kimberley Reeder et al., *The Unitary Group's Identity Crisis: Is There Really an "I" in Unitary?*, 2008 St. & Loc. Tax Law. 83, 113-14 (2008) ("Until states unanimously adopt *Joyce* or *Finnigan*, a unitary group member will continue to suffer from an identity crisis, facing the tax problems inherent in being simultaneously a separate entity and a member of a group.").

[129] *See* Eric L. Stein, *States Look to Combined Reporting to Generate Revenue*, J. St. Tax'n 2011, https://www.ryan.com/Assets/Downloads/Articles/States_Look_to_Combined_Reporting.pdf.

to multistate businesses.[130] Accordingly, achieving uniformity in the *Joyce–Finnigan* area would be a significant step toward uniformity in state taxation.

Uniformity in the *Joyce–Finnigan* area would be desirable in order to achieve more equitable taxation of a unitary group of corporations doing business across state lines.[131] The current inconsistency in states' adoption of *Joyce* or *Finnigan* can lead to two problematic results: double taxation of certain sales or nowhere income.[132] For example, assume Corporations X and Y are engaged in a unitary business and both are taxable in State A. Corporation Y makes sales of goods into State B, but it is protected from taxation in that state under Public Law 86-272; however, Corporation X is taxable in State B and files a combined return in that state, which includes Corporation Y and its other unitary subsidiaries. If State A follows *Joyce* and State B follows *Finnigan*, the end result is double taxation: State A will include Corporation Y's sales to State B in its sales factor numerator under the throwback rule since Corporation Y is not taxable in State B, and State B will also include Corporation Y's sales into the state because another member of its unitary group (Corporation X) is taxable in the state. On the other hand, if State A is a *Finnigan* state and State B is a *Joyce* state, the end result is nowhere income: State A will not include Corporation Y's sales to State B in its sales factor numerator because it believes the sales are properly attributed to State B where other members of the unitary group are taxable; State B will also exclude Corporation Y's sales into the state because under *Joyce*, Corporation Y is not separately taxable in the state.

As discussed in Part II.A, multistate taxpayers have a constitutional right to division of income when they are taxable in more than one state. The Court has acknowledged that the use of apportionment formulas leads to a "rough approximation of a corporation's income" attributable to a state[133] and that a "risk of duplicative taxation exists whenever the [taxing states] do not follow

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[130] *See* Jeffrey A. Friedman & Michele Borens, *A Pinch of SALT: Applying P.L. 86-272 in a Modern Economy*, 57 St. Tax Notes (TA) 49, 51 (July 5, 2010) (noting that with the "recent wave of states that have adopted combined reporting along with the Finnigan method," the complexity and importance of the *Joyce–Finnigan* debate increases along with virtually certain future challenges to the *Finnigan* rule).

[131] Lack of uniformity in corporate tax rules as that created by states' inconsistent apportionment methods leads to inequitable treatment that "undermines the perceived legitimacy of the tax system by arbitrarily discriminating in favor of certain corporations . . . . Returning to a more uniform set of apportionment rules is an important first step in preventing widespread tax avoidance and ensuring that state corporate income taxes are applied fairly." *Corporate Income Tax Apportionment and the Single Sales Factor,* Inst. on Tax & Econ. Pol'y, Aug. 2012, http://itepnet.org/pdf/pb11ssf.pdf.

[132] *See In re* Huffy Corp., No. 99-SBE-005, 1999 WL 386938, at *3 (Cal. State Bd. of Equalization Apr. 22, 1999) (explaining that California should abandon *Finnigan* and go back to the *Joyce* rule because the majority of states still followed *Joyce*, and this nonuniformity resulted in nowhere income or double taxation). For a series of examples illustrating the consequences of the lack of uniformity in states' adoption of *Joyce* or *Finnigan*, see Reeder et al., *supra* note 128, at 108-10.

[133] Moorman Mfg. v. G.D. Bair, 437 U.S. 267, 273 (1978).

identical rules for the division of income."[134] The Court's recognition of this issue does not mean that subjecting corporations doing business in interstate commerce to double taxation is acceptable. Rather, it is a consequence of the use of formulary apportionment, which is the best solution when separate accounting is theoretically and practically impossible. The Court has, likely appropriately, refused to mandate uniform rules of state taxation when it believes that such action is best suited for Congress. Furthermore, counting the same sale receipts in multiple jurisdictions is bad policy and may potentially disadvantage those corporations engaged in a multistate business as compared to their local competitors doing business solely within one state.

On the other hand, nowhere income resulting from nonconformity in states' use of *Joyce* or *Finnigan* is similarly bad policy and provides another reason why uniformity in this area is necessary. States have a right to tax those corporations doing business within their state borders, so long as the minimum link or connection required by the Constitution is present. Businesses engaging in activities within a state enjoy the many benefits accorded to them by state laws.[135] In addition, states have significant revenue needs, and taxing multistate corporations is certainly an important source of tax revenue for the states.[136]

Achieving uniformity with respect to the *Joyce–Finnigan* issue would also lead to less complexity and thus increased efficiency and administrability for taxpayers engaged in business activities in multiple states, especially when the taxpayer is a member of a unitary group. Imagine a multinational corporation doing business across the United States and abroad. Depending on its business activities within each state, it is not difficult to establish the requisite nexus necessary for a state to have taxing jurisdiction; hence, this hypothetical multinational corporation can relatively easily be subject to taxation in a significant number of states, at the federal level, and in other countries. At least having a uniform rule when it comes to the *Joyce–Finnigan* issue would alleviate some of the immense complexity faced by taxpayers and tax practitioners engaged in state tax consulting and compliance for multistate and multinational corporations.

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[134] *Id.* at 278.

[135] *See* Hellerstein, *supra* note 10, ¶ 8.01 (noting that states have competing claims for taxing a multistate taxpayer doing business in several states who obtain "the benefits and protection of the states' markets, their public services, and their legal and other institutions").

[136] *See id.* ¶ 1.02 ("Individual and corporate income taxes . . . combined are currently the leading source of state tax revenue. They produced $153 million, or 8.1 percent of total state tax revenues, in 1932 compared with $329.2 billion, or 40.9 percent of total state tax revenues, in 2012.").

B. *Better Approach:* Joyce *v.* Finnigan

While uniformity in states' adoption of *Joyce* or *Finnigan* is highly desirable, neither approach is without flaws, both having benefits and detriments.[137] That neither can be said to be the best approach is evident from the states' inconsistency in adoption of one of the two approaches. California itself has switched positions several times. Nonetheless, adopting one not entirely perfect approach is better in order to achieve some uniformity among the states.[138] Because *Joyce* respects legal entities and state boundaries and apportions a multistate taxpayer's unitary income while complying with federal and constitutional limitations, it should be uniformly adopted by all states imposing a corporate income tax and a combined reporting regime.

One of the strongest arguments in support of *Finnigan*, and against *Joyce*, is that the *Finnigan* rule is in accord with the unitary business concept, while *Joyce* merely elevates form over substance.[139] Perhaps this argument has some truth to it since entities involved in a multistate unitary business share resources and knowledge and benefit from centralized operations and economies of scale.[140] Although states differ in the definition of a unitary business,

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[137] *See* Charolette Noel & Carolyn Joy Lee, *Would States Adopt a Uniform Model Combined Reporting Statute in a New Wave of Combined Reporting?*, 2008 St. & Loc. Tax Law. 137, 158 (2008) ("The theme thus recurs: Achieving the ideal of uniformity will require significant compromise and changes in policy, with no one approach clearly standing out as the normative 'right' answer.").

[138] California saw the benefit of achieving uniformity in this area and abandoned the *Finnigan* rule in *Huffy Corp.* to go back to *Joyce*, maybe in part because it believed *Joyce* was the better rule, but primarily because most states still followed *Joyce*, making California's approach inconsistent with that of nearly all other states with similar rules. *See In re* Huffy Corp., No. 99-SBE-005, 1999 WL 386938, at *3 (Cal. State Bd. of Equalization Apr. 22, 1999). *But see* Citicorp N. Am., Inc. v. Franchise Tax Bd., 100 Cal. Rptr. 2d 509, 522 (Cal. Ct. App. 2000) (emphasis added) ("[T]he mere fact that other bodies and jurisdictions did not follow the Finnigan rule is not a valid basis for this court to disregard [it]. Adherence to an outmoded rule for the sake of consistency in the face of compelling reasons to change is not a virtue. *Valid principled reasons support the rationale of Joyce* and the rationale of Finnigan. In the absence of legislative direction to the contrary, the SBE is empowered to interpret cases before it in a manner that is consistent with the purposes of the state's tax code.").

[139] *See Finnigan I*, No. 88-SBE-022, 1988 WL 152336, at *3 (Cal. State Bd. of Equalization Aug. 25, 1998) (concluding that "basic unitary theory" supported the *Finnigan* approach); *Finnigan II*, No. 88-SBE-022-A, 1990 WL 15164 at *1 (Cal. State Bd. of Equalization Jan. 24, 1990) ("[T]he [*Joyce*] rule defeats the basic purpose of the sales factor, which is to reflect the markets for the unitary business's goods and services . . . . [B]y focusing on the state's jurisdiction to tax the seller as a separate entity, the [*Joyce*] rule elevates form over substance . . . ."); Hellerstein, *supra* note 10, ¶ 9.18 (arguing that *Finnigan* is correct from a unitary theory standpoint and *Joyce* "permits corporate form to govern economic substance").

[140] For instance, one of the primary reasons why the New York Court of Appeals followed *Finnigan* in *Disney Enterprises, Inc.* was the unitary business concept. The court concluded that the unitary group's tax would be distorted if the court "disregard[ed] the millions of dollars in Video's New York destination sales achieved through the group's cross-promotional activities." *See* Disney Enters., Inc. v. Tax Appeals Tribunal of the State, 888 N.E.2d 1029, 1036 (N.Y. 2008).

all states agree that there is some level of integration and benefits flowing throughout the group. Accordingly, *Finnigan* supporters argue that looking at the group as a whole better reflects unitary business principles. However, a complete disregard of corporate legal entities is not necessarily the correct result simply because a group of corporations is engaged in a unitary business. It is an established principle of corporate law that a corporation is a distinct and individual entity, respected in the eyes of the law as such.[141] Accordingly, the *Joyce* rule's tendency to view the corporation as a distinct taxpayer is in accord with established corporate law principles.

Furthermore, and more importantly, following *Finnigan* effectively results in a state taxing income that would otherwise be exempt from taxation under federal or constitutional limitations.[142] A corporation engaged in interstate commerce may be exempt from taxation in a particular state because its in-state activities are protected under Public Law 86-272, or it lacks the necessary nexus required by the Constitution before a state can impose an income tax. In the case of inbound sales, a *Finnigan* state will include in the sales factor numerator the destination sales made by a member of the unitary group so long as any member of the group is taxable in the state, even if the selling entity is not independently taxable in the jurisdiction. In other words, non-nexus entities that separately would owe no tax to the state are required to include their sales to the state in the sales factor numerator for apportionment purposes, and thus, such entities are being subjected to tax. The *Joyce* approach, on the other hand, respects corporate legal entities and determines which sales are included in the sales factor numerator on the basis of the selling entity's individual nexus to the taxing jurisdiction.

Finnigan supporters would argue that following the *Finnigan* approach is not the same as taxing income that would otherwise not be taxable.[143] For example, in *Disney Enterprises, Inc.*, the New York Court of Appeals was of the view that the inclusion in the sales factor numerator of the New

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[141] For instance, for tax purposes, there is no question that a corporation, even a one-shareholder corporation, is a distinct and separate legal entity provided that the corporation is actually engaged in business activity and has not checked the box electing to be a disregarded entity under Treasury Regulation section 301.7701-1. *See* FLETCHER CYCLOPEDIA OF THE LAW OF CORPORATIONS § 40. Parent corporations and wholly-owned subsidiaries are also generally viewed as distinct and separate entities. *See id.*

[142] *See* Great N. Nekoosa Corp. v. State Tax Assessor, 675 A.2d 963, 966 (Me. 1996) (noting that if the *Joyce* rule was not followed, the state "would inevitably and unconstitutionally tax the entire income of the multistate unitary business"); Reeder, *supra* note 128, at 102 ("[A] state using the [*Finnigan*] method indirectly taxes that which it cannot tax directly . . . . Or . . . one might view [*Finnigan*] as requiring an entity to pay a tax on another's income."). HELLERSTEIN, *supra* note 10, ¶ 9.18 (noting that "there is a serious problem with abandoning [*Joyce*]," namely, "that income of a taxpayer that is not subject to state tax under Public Law 86-272 is being attributed to a group member that is taxable").

[143] *See Disney Enters., Inc.*, 888 N.E.2d at 1039; Citicorp N. Am., Inc., 100 Cal. Rptr. 2d at, 519-20 (concluding that by considering the California-destination sales made by a member of a combined group not separately taxable in California, the state was not taxing that entity but rather apportioning income attributable to California).

York-destination sales of a corporation whose New York activities were protected under Public Law 86-272 was *not* a tax on the selling corporation; rather, it was a way of better measuring the group's in-state activities.[144] This argument is not very persuasive since the larger the sales factor numerator, the larger the apportionment percentage and hence, the larger the tax liability. As Judge Smith pointed out in his concurring opinion in *Disney Enterprises, Inc.*, "including a company's receipts in the numerator of the apportionment fraction effectively imposes a tax on that company."[145]

The recent wave of states adopting combined reporting regimes incorporating the *Finnigan* rule may be due to revenue-raising considerations.[146] While the revenue impact of tax laws is a valid state concern, it should not determine the best approach when a competing one seems more proper from a policy perspective. Furthermore, *Finnigan* does not always result in more revenue to the state and the *Joyce* rule is not always taxpayer-friendly. When the taxing state is the destination state (*i.e.*, in the case of inbound sales), *Finnigan* does result in more revenue because the sales factor numerator will include the sales made by all members of the combined unitary group, regardless of whether each selling member is separately taxable in the state. However, in the case of outbound sales (*i.e.*, when the taxing state is the origin state) of tangible personal property and application of the throwback rule, *Finnigan* does not necessarily result in more revenue because the sales would be included in the destination state's sales factor so long as any member of the group was taxable in that state.[147] On the contrary, if the origin state followed the *Joyce* rule, the sales by a member of the group into a state in which that member was not separately taxable would be thrown back to the origin state, hence leading to a larger apportionment factor and a higher tax liability.[148]

C. *Achieving (Some) Uniformity: Congress or the Multistate Tax Commission*

Having established that uniformity is highly desirable in the area of state taxation of multistate corporations and that one significant step toward uniformity would be for states to settle on the *Joyce* approach, the next issue is how such a goal can be accomplished. The two clearest options are (1) for Congress to finally take a significant step in this area and mandate uniform rules for state apportionment, or (2) for the Multistate Tax Commission to update UDITPA's model apportionment rules and accompanying regulations to address the adoption of the *Joyce* rule for state apportionment purposes based on the assumption that those states that have adopted UDITPA would continue to do so and that other states will also adopt UDITPA.

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[144] *Disney Enters., Inc.*, 888 N.E.2d at 1033.

[145] *Id.* at 1041 (Smith, J., concurring).

[146] *See* Rofool & Haggerty, *supra* note 123.

[147] This was the fact pattern presented in *Finnigan I*.

[148] *See* Great N. Nekoosa Corp. v. State Tax Assessor, 675 A.2d 963 (Me. 1996); Hartmarx Corp. v. Bower, 723 N.E.2.d. 820 (Ill. App. Ct. 1999).

Congress is unlikely to impose uniform tax apportionment rules on the states. As the Court pointed out in *Moorman Manufacturing v. Bair*, "It is clear that the legislative power granted to Congress by the Commerce Clause of the Constitution would amply justify the enactment of legislation requiring all States to adhere to uniform rules for the division of income."[149] Moreover, the Court has repeatedly indicated that it is Congress's job, and not the Court's, to require such uniformity.[150] Despite having the power to do so and the Court's invitation on several occasions to take these steps, Congress has not taken any significant actions in the area of state apportionment. Public Law 86-272 is the only action Congress has taken, and it was in great part due to the reaction of the business community to the Court's decision in *Northwestern*.

Reaffirming the unlikelihood that Congress will take steps toward uniformity in the area of state apportionment is the experience surrounding Public Law 86-272. As mentioned above and discussed in Part II.B, the statute was enacted in large part because of businesses' lobbying for Congress to impose some "minimal jurisdictional standards to limit the states' power to tax the net income of interstate corporations."[151] Congress swiftly enacted Public Law 86-272, which was originally meant to be "a temporary, or stopgap, measure" until further study of the issues involved in state taxation of interstate businesses.[152] Further study actually took place; in fact, a five-year analysis of state taxation of interstate business was conducted by the Willis Committee, resulting in "the most comprehensive analysis ever of the state corporate income tax."[153] The Committee made a series of proposals,[154] which, if adopted, would have led to uniformity in most areas of state taxation of interstate taxpayers.[155] Despite such comprehensive analysis and proposals, Congress did not enact any of them, probably because of states' aversion to the loss of sovereignty that would have resulted from enactment of the proposals, fear that they would lose control over their revenue-raising power, and other opposition to specific proposals.[156] If Congress did not act back when there was significant momentum resulting from the recent enactment

[149] Moorman Mfg. v. Bair, 437 U.S. 267, 280 (1978).

[150] *See* Container Corp. of Am. v. Franchise Tax Bd., 463 U.S. 159, 169-71 (1983); *Moorman Mfg.*, 437 U.S. at 278-80.

[151] Nethers, *supra* note 33, at 602.

[152] Disney Enters., Inc. v. Tax Appeals Tribunal of the State, 888 N.E.2d 1029, 1037 (N.Y. 2008); Nethers, *supra* note 33, at 602.

[153] Charles E. McLure, Jr., *The Difficulty of Getting Serious About State Corporate Tax Reform*, 67 Wash. & Lee L. Rev. 327, 335-37 (2010); *see* Nethers, *supra* note 33, at 602.

[154] *See* H.R. Rep. No. 89-11798 (1966).

[155] McLure, *supra* note 153, at 336 (noting that the Willis Committee made both substantive and administrative proposals that, although not perfect, were better than the current state of affairs because "uniformity would [have] prevail[ed]; the distortions and complexity that result from nonuniformity would not exist").

[156] *See id.* at 337.

of Public Law 86-272 and it had at its disposal a comprehensive set of proposals to increase uniformity in state taxation, there is no reason to think that Congress would act now.[157]

Given the unlikelihood of Congress taking any steps to achieve uniformity in state apportionment rules, the remaining option is action by the Multistate Tax Commission. The Multistate Tax Commission already embraces the *Joyce* approach but only for purposes of determinations under Public Law 86-272 for sales of tangible personal property.[158] The Multistate Tax Commission should update the model apportionment rules in Article IV of the Compact to embrace *Joyce* for all purposes, which would better reflect the developments in state law and provide some uniformity in the area of state apportionment rules.[159] This course of action is not as satisfactory as action by Congress given that the Compact has no legal effect unless adopted by state legislatures; however, because Congress acting on this issue is unlikely, this seems to be the best option.[160]

Additionally, recent efforts by the Multistate Tax Commission with respect to UDITPA's model apportionment provisions suggest that the Multistate Tax Commission is more willing than Congress to act to achieve uniformity. In 2006, the Multistate Tax Commission recommended to the Uniform Law Commission (ULC) that UDITPA should be revised to better reflect the developments that had taken place in the state law apportionment area since UDITPA's original drafting in 1957.[161] Although the ULC followed the Multistate Tax Commission's recommendation and formed a drafting committee to revise UDITPA, the committee was discharged in 2009 and no further work took place.[162] After the ULC abandoned this project, the Multistate Tax Commission decided to take charge, referring the UDITPA revision task

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[157] The current situation with BATSA, *see supra* Part II.B, is evidence of the unlikelihood of Congress taking some action regulating state taxation of multistate taxpayers.

[158] *See supra* note 126.

[159] As discussed in Part III.C, while the *Joyce–Finnigan* debate originated in the context of sale of tangible personal property and application of the throwback rule, its scope has expanded tremendously as states, either judicially or legislatively, have considered this issue outside the context of the throwback rule and for revenue streams other than just sales of tangible personal property.

[160] In addition, the Compact has already been adopted by a fair number of states. *See supra* notes 45-47.

[161] *See Report of the Hearing Officer, Multistate Tax Compact Article IV (UDITPA) Proposed Amendments*, Multistate Tax Comm'n, Oct. 25, 2013, http://www.mtc.gov/uploadedFiles/Multistate_Tax_Commission/Pomp%20final%20final3.pdf; *see also UDITPA Rewrite Necessary, But Will States Listen?*, Leverage Salt LLC, Dec. 5, 2013, http://www.leveragestateandlocaltax.com/2013/12/uditpa-rewrite-necessary-but-will.html (noting that revision of UDITPA "is designed to result not in a perfect solution (which doesn't exist), but in the best rules" and is necessary "because UDITPA is 56 years old and has become outdated").

[162] *Report of the Hearing Officer*, *supra* note 161, at 2; McLure, *supra* note 153, at 337-38 (footnote omitted) (noting that the ULC drafting committee's effort to revise UDITPA was abandoned when representatives of state legislatures "made it clear that it was not welcome and that any revision of the model statute would be widely rejected by the states").

to its Uniformity Committee in 2009; the Committee completed the proposals in March 2012, and public hearing on the revised model was held March 28, 2013.[163]

The proposals made by the Uniformity Committee are: (1) double-weighting of the sales factor in the apportionment formula,[164] (2) amending the equitable apportionment provision,[165] (3) revising the definition of business income,[166] (4) market-based sourcing for receipts from sales of property other than tangible personal property,[167] and (5) limiting the sales factor to receipts from transactions and activities in the ordinary course of business.[168] The proposals, while addressing significant areas of nonuniformity in states' division of income rules, do not address the *Joyce–Finnigan* debate. However, this undertaking by the Multistate Tax Commission illustrates its willingness to work toward uniformity in state taxation of multistate corporations. Accordingly, inclusion by the Multistate Tax Commission in Article IV of a provision adopting the *Joyce* rule for attribution of sales by members in a unitary group seems to be the most practical way of achieving uniformity in this particular area and settling the *Joyce–Finnigan* debate to some extent.

V. Conclusion

Uniformity is a desirable goal in the area of state taxation of corporations engaged in interstate commerce, as it is in many other areas of the law. However, complete uniformity in this area is a fiction, despite the drafting of UDITPA and the Compact, which have been incorporated by a number of states into their law. Nonetheless, some consistency could be achieved if states finally resolved the *Joyce–Finnigan* debate that originated in California in 1966. After decades of controversy, nonuniformity, and inaction by Congress, the Multistate Tax Commission should bring some clarity by incorporating the *Joyce* rule into its apportionment provisions, and hopefully, the states will see that although *Joyce* is not a perfect rule, it is preferable and consistent with the Constitution.

Lisandra Ortiz[169]

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[163] *Report of the Hearing Officer*, *supra* note 161, at 3.

[164] *See Report of the Hearing Officer*, *supra* note 161, at 8-18.

[165] *See Report of the Hearing Officer*, *supra* note 161, at 18-37.

[166] *See Report of the Hearing Officer*, *supra* note 161, at 37-54.

[167] Market-based sourcing essentially mirrors the destination rule for sourcing sales of tangible personal property. *See Report of the Hearing Officer*, *supra* note 161, at 54-96.

[168] *See Report of the Hearing Officer*, *supra* note 161, at 96-113.

[169] Georgetown University Law Center, J.D. 2014. The author thanks her mentor from the ABA Section of Taxation, Brandee A. Tilman, Senior Manager, State Tax Controversies at The Walt Disney Company, for her valuable guidance and feedback. The author also thanks the editorial staff of *The Tax Lawyer* for its editorial contributions.