MULTISTATE TAX COMMISSION

Working Together Since 1967 to Preserve Federalism and Tax Fairness

To: Bruce Fort

From: Elliott Dubin and Parker Armstrong

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Subject: Joyce v. Finnigan

According to the great British author, George Bernard Shaw, "If all the economists were laid end to end, they would never reach a conclusion." In a small instance Shaw was correct – two eminent scholars of the Economics of the Public Sector, William Fox of the University of Tennessee and Charles McLure of Stanford's Hoover Institution came down on opposite sides of the ***GREAT DEBATE***: how should the taxable income of unitary corporations be apportioned among the states – the Joyce Rule or the Finnigan Rule? Fox and his colleagues have come down on the Finnigan side[1] while McLure has tepidly endorsed the Joyce Rule.[2] One reason Fox et. al. endorsed the Finnigan Rule is that adoption of the Joyce Rule prohibits the taxing state from including unitary entities without nexus in that state from the combined report. This allows for transfer pricing manipulation i.e., shifting income to the entity excluded from the combined report.[3] McLure, states that the Joyce Rule, in theory, produces reasonable results, realizes that … "P.L. 86-272 is one of the nuttiest features in the state corporate income tax 'system'"[4] and permits the type of income shifting described by Fox et. al. For what it's worth, Parker and I come down on the side of Finnigan.

Also attached are a table which shows which states have adopted Joyce and which have adopted Finnigan (from Commerce Clearing House), notes on "throwback" vs "throwout" rules, and two tables comparing the revenue impact on a State. Table 1 compares separate entity reporting with combined reporting under Joyce rules (with no throwback or throwout rules) and under Finnigan rules. Table 2 does the same except that it assumes that 25% of this firm's out-of-state sales are in states in which the firm has no nexus. NOTE: I did not use the term "taxpayer" to characterize the firm. It is not a taxpayer; it is a tax conduit.

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[1] William F. Fox, Matthew N. Murray, and LeAnn Luna, "How Should a Subnational Corporate Income Tax be Structured?" ***National Tax Journal***, Volume LVIII, No 1, March 2005, p. 153.

[2] Charles E. McLure, Jr., "The Nuttiness of State and Local Taxes – and the Nuttiness of the Responses Thereto," ***State Tax Notes***, September 16, 2002, page 848.

[3] Fox et. al. ***op. cit***., p147.

[4] Charles E. McLure Jr, "A Comprehensive and Sensible UDITPA," ***State Tax Notes***, September 26, 2005, p. 931.