FISCAL RESEARCH CENTER

COOPERATION OR COMPETITION: THE MULTISTATE TAX COMMISSION AND STATE CORPORATE TAX UNIFORMITY

W. Bartley Hildreth, Matthew N. Murray and David L. Sjoquist

Georgia State University | ANDREW YOUNG SCHOOL OF POLICY STUDIES

COOPERATION OR COMPETITION: THE MULTISTATE TAX COMMISSION AND STATE CORPORATE TAX UNIFORMITY

W. Bartley Hildreth, Matthew N. Murray
and David L. Sjoquist

Fiscal Research Center
Andrew Young School of Policy Studies
Georgia State University
Atlanta, GA

FRC Report No. 110
August 2005

Acknowledgments

We thank Elliott Dubin, Director of Policy Research at the MTC, for providing background material and entertaining our many questions. This paper was presented at the National Tax Association Spring Symposium, May 20, 2005, Washington DC.

Table of Contents

Cooperation or Competition: The Multistate Tax Commission and State Corporate Tax Uniformity

1. Introduction

The Multistate Tax Commission (MTC) was established out of concern over the lack of uniformity in interstate taxation and the fear that in the absence of voluntary uniformity the federal government would dictate the nature of uniformity. This paper first considers why the MTC was formed and what it is and does. In the remainder of the paper we focus on the issue of tax uniformity. We consider what the MTC has accomplished and compare that to what might be expected of a voluntary compact. Finally, we consider alternative ways of achieving uniformity. In the discussion of uniformity we focus on the state corporate income tax since state sales and use taxes are the subject of the paper by Swain and Hellerstein (2005). We want to make it clear that this paper is not an expose or an evaluation of the MTC. Rather, it is a discussion of the MTC and its role in achieving interstate tax uniformity of state corporate income tax systems.

The rest of the paper proceeds as follows. In the next two sections we discuss the MTC, how it came to be and what it does. We also present a brief history of efforts to achieve uniformity of state corporate income taxes. In section 4 we discuss the case for interstate uniformity. We then turn to a discussion of what might be expected of an interstate compact, focusing on both “theory” and evidence from other compacts. In section 7 we present information about the degree of uniformity of state corporate income taxes that has been achieved since the formation of the MTC. In section 8, we discuss the advantages and disadvantages of alternative approaches to achieving uniformity, namely voluntary compacts versus federal mandates. Section 9 contains some concluding remarks.

2. Precursors and Pressures

The roots of MTC formation lay in the lack of uniformity of state tax systems. We begin our inquiry near the close of the 19th century. Tax nonconformity motivated seven states to send representatives to a conference in 1892 that culminated with the formation of the National Conference of Commissioners for Uniform State Laws (NCCUSL). By 1912, all of the states had appointed commissioners to NCCUSL. Tax policy analysts are most familiar with the Uniform Division of Income for Tax Purposes Act (UDITPA) which was promulgated by NCCUSL in the late 1950s. In practice the uniformity focus of NCCUSL has long encompassed more than just tax policy.[1] But the organization has had an undeniable impact on the tax policies of the states.

The Introduction of State Income Taxes

Nonconformity of state tax systems became a major issue following the widespread adoption of personal and corporate income taxes in the early 20th century,[2] a period that coincided with an expanding multistate presence on the part of corporate taxpayers. Wisconsin implemented its income tax in 1911, two years prior to the ratification of the 16th Amendment, which enabled the federal income tax. Corporate income was initially apportioned in Wisconsin on the basis of "business transactions" and property (Hellerstein and Hellerstein, 1988). Sixteen states had adopted a corporate income tax by 1930 (Pomp and Oldman, 2001).

Early commentators bemoaned this evolving structure of corporate taxation. Mudge notes in 1934 that "...the tax methods are almost as numerous as the taxing jurisdictions" (p.532). Hunter and Allen similarly note in 1940 "There is lack of

[1] See: www.nccusl.org.

[2] Concerns were also voiced regarding nonconformity of inheritance and estate taxes and the subsequent threat of multiple taxation. By 1929, 45 states had some form of inheritance/estate tax. Seligman (1925) among others criticizes these systems and discusses possible remedies, including federal intervention and federal assumption of inheritance/estate taxes. Cooperative interstate agreements are dismissed by Seligman because of the different interests of the states.

uniformity not only in the method by which corporations in general are taxed, but also in the taxation of specific types of corporations" (p.358).[3]

State practice certainly showed wide variation in this early era of corporate income taxation. While some states used the familiar three-factor formula[4] for the apportionment of corporate income, others used single- or two-factor formulas, including sales-only factors and property-only factors. There were also disparities in the way in which sales (i.e. *receipts*), property and payroll were measured and implemented in the various apportionment formulas. For example, there was differential treatment of receipts from the sale of tangible goods, intangibles (like securities) and services, and similar incongruities in the treatment of real, personal and intangible property. The three-factor formula was challenged in Pennsylvania in 1936 on the basis that different factors meant different tax burdens for firms with similar income in a given state (Hellerstein and Hellerstein, 1988). The U.S. Supreme Court not only upheld the three-factor formula but also ruled that uniformity does not preclude classification systems that allow different apportionment systems for different industries.[5]

The National Tax Association (NTA) weighed in early on the issue of state taxation of multistate entities to address "…the conflicting claims of independent taxing authorities" (Hunter and Allen, 1940, pp. 599). In the early 20th Century working committees of the NTA were focused on the lack of tax policy uniformity across the states but they could not reach agreement on possible remedies. Agreement was reached by the time the 26th annual conference was held in Phoenix in 1933. A model tax system was proposed by the NTA that included a single

[3]Hellerstein and Hellerstein (1988) comment on the disarray of business taxes that prevailed across the states in the pre-income tax era.
[4]A multistate corporation's tax base is apportioned based on that portion of net income attributable to a particular state using a formula. The use of the three-factor formula requires multiplication of net multistate income by a fraction representing the arithmetic average of the ratios of property, sales and payroll factors – with each of the three factor expressed as a fraction with the numerator representing the dollar value within the state and the denominator representing the dollar value elsewhere.
[5]Wheeling Steel Corp. v. Fox (1936).

business tax on corporate income and the use of the three-factor formula to apportion income. At the time, 4 states were in fact utilizing the three-factor formula. But the NTA recognized that agreement and cooperation between the states would be difficult if not impossible to realize in practice (Hunter and Allen, 1940).

The States Push the Envelope

Through the 1950s the states pushed the limits of apportionment, including more and more income that had previously been subject to allocation.[6] This meant shifting tax burdens for firms and shifting corporate revenue streams for the states. Uncertainties arose regarding state nexus standards and the right to tax corporate income, as well as what income would be apportioned and allocated, and to where this income would be distributed. UDITPA was adopted by NCCUSL in 1957 in an effort to encourage greater uniformity in taxation across the states. While UDITPA offered a common basis for the interstate distribution of corporate income, it did not address other quarrelsome issues like nexus.[7]

The nexus issue reared its ugly head in 1959 with the decision rendered by the U.S. Supreme Court in *Northwestern Portland Cement v. Minnesota*.[8] The Court ruled that the solicitation of sales was a sufficient basis to enable the state's right to tax corporate income. The business community was outraged and thus engaged Congress, which ultimately passed Public Law 86-272. This law was seen as a temporary measure and offered nexus protection to corporations for which the sole activity in a state was the solicitation of sales of tangible goods.[9] PL 86-272 was "temporary" in the sense that it was accompanied by a mandate for Congress to study

[6]Following UDITPA, apportionable income is that which is derived from the regular course of business and trade, while allocable income is all other income. Allocable income typically includes income from intangibles and is generally assigned for tax purposes on a residency basis to the state of corporate domicile.
[7]The corporate income tax was not the only point of contention between businesses and the states. There were also concerns regarding the sales tax, including the failure of some states to grant credits under the use tax for sales tax paid in other states and uncertainty regarding state nexus standards (Kinnear, 1971).
[8]See Peters (1997) and Pomp and Oldman (2001) for a broader discussion of this case.
[9]There remains some question today regarding the applicability of 86-272 to firms selling *intangible* services. The MTC deems certain repair services as exceeding the solicitation of orders standard established by 86-272 (Hellerstein and Hellerstein, 1988).

the state taxation of business and make recommendations to promote uniformity. The Willis Commission was established to study the issue and its report was released in 1965. Pressures mounted for a state response.

Congress reacted to the Willis Commission Report (1965) by proposing a legislated remedy in the form of H.R. 11798.[10] The bill included a physical nexus standard, a two-factor property/payroll apportionment formula, full apportionment of *all* corporate income and federal oversight of state corporate income taxation through the Secretary of the Treasury. The states felt threatened by the proposed Congressional action, generally fearing the loss of sovereignty to the federal government. Market states were disappointed that there was no sales factor in the apportionment formula. Through full apportionment some states would have lost revenue previously derived from allocable income, in particular dividend income. And the states wanted the flexibility to pursue their own policy objectives, especially the promotion of economic development through the corporate income tax. Uniformity, particularly uniformity of the federal variety, was not what the states wanted. Some members of the business community objected as well to the proposed federal legislation. One specific concern was the potential apportionment of foreign-source income and dividends.

The MTC is Established

As these events transpired the challenge became one of balance. The horizontal sovereignty of the states in a federalist system had to be weighed against the vertical constraints of the Constitution and the preferences of a Congress that was heavily lobbied by the business community. The states reacted quickly. In 1966, at the impetus of the Council of State Governments and with the participation of the National Association of Tax Administrators, the concept of a Multistate Tax Compact was hatched. The Compact would come into play when 7 states adopted its provisions; the Compact included UDITPA as the basis for distributing corporate income. On August 4, 1967 the Compact and its executive body, the MTC was

[10]The following discussion draws heavily from Peters (1997) and Sharpe (1975), as well as Brunori's (1999) interview with Eugene Corrigan, the first Executive Director of MTC.

enabled.[11] The Compact was not Congressionally-sanctioned as a formal compact with binding regulatory authority. In fact, the states objected to S. 3333 which would have granted such expansive regulatory authority.[12] The states clearly wanted the freedom to pursue their own policy agendas.

In the early days of the MTC there were some cooperative efforts with the business community.[13] But disputes over the treatment of dividends and foreign-source income could not be resolved to the satisfaction of both parties. Friction soon arose in response to MTC's interstate (joint) audit practices which relied on world-wide combined reporting methods and a broad approach to income apportionment (see below). World-wide reporting was not consistent either with reporting under the federal corporate income tax nor with the practice in the international community.

The business community stiffened its back and sought remedy through Congressional action, state action, and litigation. The Committee on State Taxation, originally linked to the Council of State Chambers of Commerce, was formed to represent and lobby on behalf of large multistate taxpayers. None of the bills submitted to Congress passed as they all included elements opposed by the respective parties.[14] Pressure from the business community was effective in causing Florida, Illinois and Indiana to withdraw from the Compact.

Litigation culminated with *United States Steel Corp et al. v. Multistate Tax Commission*, a class-action law suit started in 1972 ultimately representing 16 large

[11] Johnson (2001) provides a history of the MTC.
[12] S. 3333 was an ad hoc bill introduced in 1972, 92nd Congress, 2nd Session. Kinnear (1971) notes the absence of MTC support for the bill. The 1971/72 MTC *Annual Report* states that some state tax administrators thought the bill would exempt too much corporate income from tax.
[13] Bucks (2000) provides a list of more recent cooperative efforts between the MTC and the business community.
[14] Cahoon and Brown (1973) call for "uniform federal rules" and discuss the Ribicoff-Mathias Bill, S. 1245, which was introduced in Congress in 1973. For the state corporate income tax the bill would have required a physical presence rule for nexus, allowed for variations in the nature of formulary apportionment, precluded apportionment and allocation of foreign-source income and required allocation of dividend income. Sales would have been assigned on destination basis and throwback rules would not have been allowed. A federal court of claims would have been used to settle disputes.

corporations, with funding support provided by COST (Oveson, 2002). The plaintiffs had several concerns, including the constitutionality of the Compact and the legitimacy of multijurisdictional audits. In focusing on the Compact Clause of the U.S. Constitution, the Court examined whether the Compact increased the political power of the states vis-a-vis the federal government. The Court ruled against the plaintiffs in 1978 and sustained the Multistate Tax Compact.[15]

Also sustained was the conflict between the MTC and the business community. Joint audits have remained a contentious issue, as discussed below. And, a storm of controversy was created by the issuance of Nexus Program Bulletin 95-1 in 1995, which in the eyes of the MTC was intended to clarify nexus standards for the computer industry. In response, California almost withdrew from the Compact. Efforts to promote uniformity have encountered staunch opposition from businesses and COST, which is no longer affiliated with the U.S. Chamber of Commerce. (As Peters [1997] notes, not even COST can agree on uniformity measures because of the different interests of different members of the business community.) Incentives like sales-weighted apportionment, which deviate from UDITPA, are illustrative of the pressures created by the self interest of the states and corporations.

[15]See section 6 for a discussion of this case.

3. Multistate Tax Compact and Commission

The Multistate Tax Compact is a model tax law that may be adopted by the states through discretionary legislative action. The Multistate Tax Commission was enabled and its broad parameters for operation defined through creation of the Compact. The intent of the Compact is to:

- ensure the "equitable apportionment of tax bases and settlement of apportionment disputes,"
- "promote uniformity or compatibility in significant components of tax systems,"
- support "taxpayer convenience and compliance" and
- "avoid duplicative taxation" (mtc.gov/compact/html).

The preservation of state sovereignty is not mentioned explicitly in the Compact itself. However, this goal does appear in statements made by Commission members and in Commission publications (e.g. *Multistate Tax Commission Review*, September 2001).

The most salient features of the Compact include Articles IV (UDITPA), VII (uniform regulations and forms), VIII (interstate audits) and IX (arbitration for dispute resolution). The Compact also details the general *powers* and the committee structure of the Commission, as well as the required financial contributions of member states. The Commission is charged with developing bylaws to govern its operations. There is no explicit mechanism in the Compact or in the Commission bylaws to change the language of the Compact. The bylaws may be changed through Commission action.

Neither the Compact nor the positions taken by the Commission are binding on member states. While full members (see below) are required to adopt the Compact, including UDITPA, they are not bound to any uniformity provisions or policies, and have no legal responsibility other than payment of dues. In practice member states have deviated from UDITPA, a good example being the adoption of sales-weighted corporate income apportionment formulas rather than UDITPA's recommended three-factor formula.[16] States may formally withdraw from membership by repealing the Compact, inclusive of UDITPA. The voluntary nature of Compact and Commission policy adoption on the part of the states reflects the desire to preserve state sovereignty over tax policy and tax administration. An important practical consequence, however, is the inability to achieve one of the core objectives of the Compact, the uniformity of state tax systems. The MTC itself notes in a discussion of uniformity that "…it would be inappropriate to suggest any or all variations in individual state laws should or could be eliminated" (MTC *Annual Report*, 1971/72, p. 2).

Interestingly, in the process to create another interstate compact--the Streamlined Sales and Use Tax Agreement--the 'flaws' of the MTC related to the pursuit of uniformity are highlighted:

> A caution: Although a Governing Board is provided for, the [Streamlined Sales and Use Tax] Agreement does not arm it with disciplinary powers. If member states want to bend or break a rule or two, there appears to be no formal mechanism for forcing compliance with the Agreement once a state is accepted as a member. [State of Washington adopted a version of the Agreement that does not accept the Agreement's transaction sourcing rules.] This is the same flaw present in the Multistate Tax Compact (governing the allocation and apportionment of income among states). Almost every member of the

[16]From a review of MTC annual reports, it appears that Minnesota was the first full-member state to deviate from UDITPA's uniform three-factor formula for income apportionment as it adopted a 70 percent sales factor in 1987. Florida was a compact member in 1971 when it implemented its corporate income tax, but it deleted UDITPA (1971/72 MTC *Annual Report*) and later withdrew from the Compact. There is no bright-line test on how far a state can stray from the Compact and no mechanism to sanction a member state for any deviations from UDITPA. In the context of UDITPA, Pomp and Oldman (2001, pp. 10-12) note that "Nonsubstantial deviations are permitted." Nonmember states that have adopted UDITPA don't necessarily adopt all of its provisions. For example, West Virginia adopted UDITPA but used a sales-only factor in 1971 (MTC *Annual Report*, 1971/72). MTC notes that the "optional feature" of UDITPA adoption in the context of multistate taxpayers who may benefit from deviations from the three-factor formula. States can choose to offer unique formulas, but they can also make "…uniformity available to taxpayers where and when desired" (MTC *Annual Report*, 1969/70, p. 3).

> Multistate Tax Compact (including New Mexico) violates the Compact's requirement that income be apportioned based on equally-weighted property, payroll and sales factors. Other than wringing its collective hands, the Compact's board has done nothing to stop members from adopting numerous variations.[17]

The current Commission bylaws (not the Compact) provide for four different membership categories, which reflect a differential scope of participation in the organization. The presumed intent is to engage a broader set of states in a dialogue with the Commission. There are currently 21 full *Compact* members, the same number of full members as in 1971, although the mix of states has changed. Compact members are afforded complete voting and committee participation rights within the MTC. *Sovereignty* members, of which there are 5, pay the same dues as Compact members and are entitled to participate in meetings and serve on committees other than the Executive Committee; Sovereignty members do not hold voting rights. *Associate* and *Project* members pay on a fee-for-service basis for programs and activities and may be charged rates higher than those imposed on Compact and Sovereignty members; Associate members may serve on committees but they do not hold voting rights. States holding these other membership positions need not adopt UDITPA. Only four states have chosen to have no membership linkage with the MTC. Member-state representatives are required to be those who serve as heads of state revenue agencies that oversee the taxes that fall under the scope of the MTC.[18] They are appointed by state governors and must be approved by the state senate.

Table 1 shows membership status by fiscal year, drawn from available MTC *Annual Reports*. In the initial years of the MTC the bylaws only enabled Compact members and Associate members. In 1967/68 there were 13 Compact members and

[17] O'Neill (undated, p.3).

[18] See Article VI. The Compact additionally states that "Each party state shall provide by law for the selection of representatives from its subdivisions affected by this compact to consult with the Commission member from that State." *Multistate Tax Compact*, Article 6 (b). This provision provides some assurance the substate jurisdictions at least have an indirect voice at the table.

Table 1: MTC Membership Trends

Fiscal Year

	67/68	68/69	69/70	70/71	71/72	72/73	73/74	74/75	75/76	76/77	77/78	78/79	79/80	80/81	81/82	82/83	83/84	84/85	85/86	86/87	87/88	88/89-92/93	93/94	94/95-96/97	97/98	98/99	99/00	00/01-03/04	04/05
AL	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A		M		M	M	M		M
AK	A	A	N	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
AZ	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A		A		A	A	A		A
AR	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
CA	A	A	A	A	A	A	A	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
CO	N	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
CT	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		A		A	A	A		A
DE	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		N		N	N	N		N
DC	N	N	N	N	N	N	N	N	N	N	N	N	N	M	M	M	M	M	M	M	M		M		M	M	M		M
FL	M	M	M	M	M	M	M	M	N	N	N	N	N	N	N	N	N	N	N	N	N		P		S	S	S		S
GA	N	N	N	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A		A		A	A	A		A
HI	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
ID	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
IL	M	M	M	M	M	M	M	N	N	N	N	N	N	N	N	N	N	N	N	N	N		N		A	A	A		A
IN	A	A	A	N	M	M	M	M	M	N	N	N	N	N	N	N	N	N	N	N	N		N		N	N	N		N
IA	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		P		P	P	P		P
KS	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
KY	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		P		A	A	A		S
LA	N	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A		A		A	A	A		S
ME	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		A		M	M	M		M
MD	N	N	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A		A		A	A	A		A
MA	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A		A		A	A	A		A
MI	A	N	N	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
MN	N	N	N	A	A	A	A	A	A	A	A	A	A	A	A	M	M	M	M	M	M		M		M	M	M		M
MS	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		N		N	A	A		A
MO	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
MT	A	N	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
NE	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	N	N	N	N		P		P	P	P		P
NV	M	M	M	M	M	M	M	M	M	M	M	M	M	N	N	N	N	N	N	N	N		N		N	N	N		N
NH	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		A		A	A	A		A
NJ	N	N	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A		A		A	A	A		S
NM	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
NY	N	A	A	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		N		N	N	N		A
NC	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		N		A	A	N		A
ND	A	N	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
OH	N	N	N	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A		A		A	A	A		A
OK	N	N	N	N	N	N	A	A	A	N	N	N	N	N	N	N	N	N	N	N	N		N		A	A	A		A
OR	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
PA	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A		A		A	A	A		A
RI	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		N		P	P	P		P
SC	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		P		P	A	A		A
SD	N	A	A	A	A	A	A	A	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
TN	N	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A	A		A		A	A	A		A
TX	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
UT	A	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
VT	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		N		N	N	N		A
VA	N	A	A	A	A	A	A	A	N	N	N	N	N	N	N	N	N	N	N	N	N		N		N	N	N		N
WA	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M	M		M		M	M	M		M
WV	A	A	A	A	A	A	A	A	A	A	A	A	A	M	M	N	M	N	N	N	N		A		A	A	A		A
WI	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N	N		A		A	A	A		A
WY	N	M	M	M	M	M	M	M	M	N	N	N	N	N	N	N	N	N	N	N	N		N		N	N	N		S

NOTE: M=Compact Members; S=Sovereignty Members; A=Associate Members; P=Project Members; N=Non-Members

12 Associate members.[19] By 1993/94 Project member status had been adopted and by 1997/98 Sovereignty members had been enabled by the MTC. Many states have chosen to jump directly to full Compact membership status, others have moved through the ranks of membership status and some have been stable members of some form. There are numerous instances of members withdrawing from the MTC, including Florida, Illinois, Indiana, Nebraska, Nevada, New York, North Carolina, Virginia, West Virginia and Wyoming.[20] In some cases states have subsequently re-joined the MTC. The broadened scope of membership categories seems to have been quite effective in drawing a larger number of states into the MTC.

Both the Commission bylaws and the Compact speak to voting procedures. A quorum is represented by a majority of Commission members. The Compact (Article 6, paragraph (c)) notes that "...no action shall be *binding* unless approved by a majority of the total number of members."[21] The bylaws go one step further by requiring not only a majority of states, but also a majority of the population of the member states.

As the only committee entity created by the Compact, the Executive Committee has seven members, including a chair, vice chair, treasurer and four other members elected by the Commission at large. The Executive Committee is governed by the bylaws of the MTC. The bylaws state that members serve single year terms; a quorum is represented by four or more members. An Executive Director position was also established by the bylaws to oversee the administrative affairs of the Commission. The formation of other committees is also enabled by the bylaws.

The Compact delineates the budgeting process and financial structure of the Commission. The Commission develops a budget for its activities which is then submitted to the member states for approval. Membership dues in support of the general activities of the Commission are set by formula, with 10 percent split equally

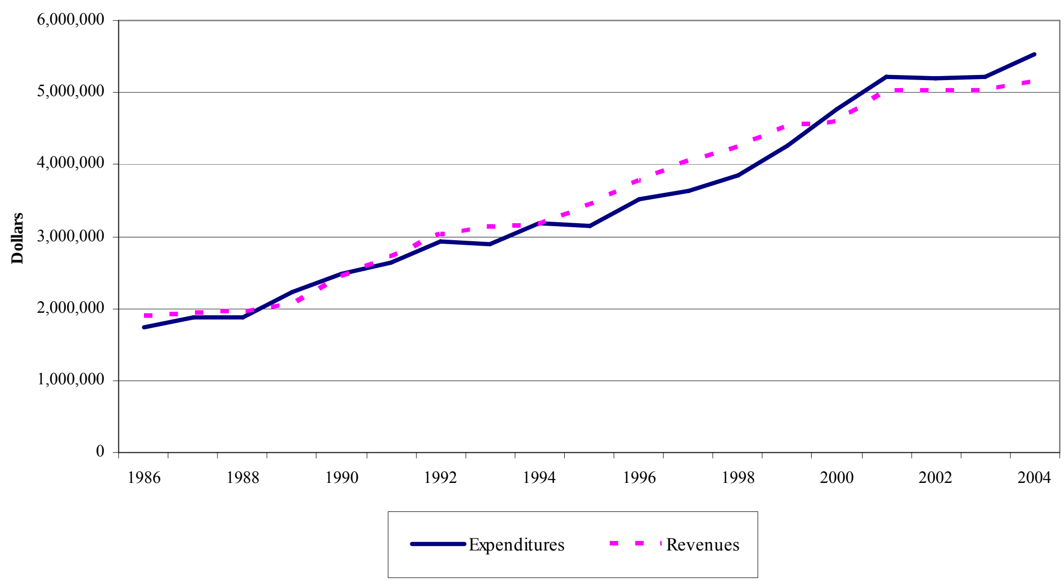
---

[19]To the extent possible the data in Table 1 are based on membership during the relevant fiscal year. In some instances this has not proven possible. For example, in 1967/68 the *Annual Report* show full membership status by date, while there is only a listing of associate members with no indication of when the states joined MTC.
[20]Maine recently voted to drop its membership.
[21]Emphasis added. It is interesting that the word *binding* is used when states cannot in fact be bound by the policies of the Compact and the Commission.

across member states and 90 percent based on each member's share of state and local revenue derived from income, capital stock, gross receipts and sales/use taxes. Therefore, the MTC budget does not increase with larger state and local tax collections in a particular state; only its share of the MTC formula is subject to change. Some specific activities, notably interstate audits (discussed below), are provided by the MTC on a fee-for-service basis.

As reported in its first *Annual Report* (1967/68), revenues totaled $197,000. Revenue and expenditure data for the period 1985/86 through 2003/04 are shown in Figure 1. These data include total revenues and spending for unappropriated, appropriated and restricted funds. Together the data reflect all activities of the MTC, including the interstate audit program and the NEXUS program. Revenues totaled nearly $1.9 million in 1985/86 and rose to $5.2 million in 2003/04, reflecting a compound annual growth rate of 5.7 percent.

FIGURE 1. REVENUES AND EXPENDITURES OF THE MTC, 1986-2004



Note: Includes revenues and expenditures from unappropriated funds, appropriated funds and restricted funds.

Source: MTC, direct correspondence.

Commission Activities

Commission powers are specified in the Compact and include studying state and local tax systems and taxes, developing uniformity or compatibility proposals and providing information to facilitate compliance with state and local tax laws. The Compact specifically spells out the general parameters for development of uniformity provisions, the conduct of interstate audits, and dispute resolution through arbitration. In practice the range of Commission activities is rather extensive and goes well beyond the parameters of the Compact. It has been engaged in visible multistate activities like the Streamlined Sales Tax Program (SSTP), written amicus curiae briefs on behalf of both states and taxpayers,[22] offered training programs and seminars, issued studies and reports,[23] implemented initiatives like the *national nexus program*,[24] and passed policy resolutions.[25] The Commission is also actively engaged in communication with other interstate bodies both formally and informally. *TaxExchange*, for example, is an electronic-based system for dialogue between the MTC and the Federation of Tax Administrators. Finally, in a cooperative effort with COST the MTC developed an *Alternative Dispute Resolution Program* (ADR) that was adopted by the Commission in 1995. A primary purpose of the ADR was to use discussion and dialogue to cooperatively resolve disputes between multistate taxpayers and the states and avoid costly and uncertain litigation.

[22]In 2004 the MTC and COST each filed an amicus brief in support of a taxpayer (AT&T), the first time they have done so. The annual reports of MTC devote considerable space to the discussion of litigation activities. http://www.statetax.org/Template.cfm? Section=Briefs_ Filed&Template=/ContentManagement/ContentDisplay.cfm&ContentID=5085. For recently filed briefs see http://www.mtc.gov/amicus%20briefs.htm.

[23]A good example is *Federalism at Risk*, published in 2003. The Commission also publishes the *Multistate Tax Commission Review* on an irregular basis. The *Review* offers information on Commission activities and special reports on timely policy issues.

[24]This is a voluntary multistate disclosure program that allows firms to resolve sales, income and franchise tax liability uncertainties with states that have chosen to participate in the nexus program. The service is provided at no cost to taxpayers.

[25]The policy resolutions include both honorary/congratulatory and substantive positions (commonly on uniformity) taken by the Commission. See http://www.mtc.gov/POLICY/ 2004res.htm. Some resolutions percolate up through the MTC committee structure while others are initiated at the Commission level.

Joint Audit Program

The Joint Audit Program began in 1969 with the completion of three pilot audits, two covering the corporate income tax and one covering the sales tax. With the hiring of an audit coordinator in 1969, MTC notes that "There is the real possibility that constructive results of [audit] activities may soon overshadow all other Commission activities in furthering the causes of equity, uniformity and tax administration efficiency among the states" (MTC *Annual Report*, 1969/70, p. 11). By 1971, field offices for corporate income tax auditing had been established in New York and Chicago, with 3 auditors in each office. The Audit Program was described as MTC's most prominent activity in its 1977/78 *MTC Annual Report*.

The Audit Program turned out to be a contentious issue with taxpayers in the early years of the Commission. Some firms balked at requests for information and data that were to support the audit. Subpoenas ultimately were issued by the states to secure information from taxpayers who resisted MTC's actions. There was a backlash in 1972 when legal action was taken by U.S. Steel in response to an MTC audit. U.S. Steel took the position that MTC was an unconstitutional construct (see Krol, 1975). Other taxpayers, as well as COST, soon joined the case on behalf of U.S. Steel. This case preoccupied MTC until February of 1978 when the Supreme Court ruled 7 to 2 against the plaintiffs. In the intervening years MTC had won a series of favorable lawsuits regarding the viability of its audit program in state courts, as discussed in their *Annual Reports*.

The business community's more specific objections to the audit program were numerous (Krol, 1975). Perhaps most prominent was the concern over the use of the combined reporting system as the basis for information gathering to support the MTC audits. MTC auditors used combined reporting over the unitary business entity at the request of the states, not at its own initiative. In practice this meant collection of information from "…all affiliates wherein more than 50 percent common ownership is involved" (Cappetta, 1974, p. 55).

The Audit Program had many stated objectives, including enhanced efficiency for both states and taxpayers who could avoid multiplicative audits. MTC also notes that it may spare corporate taxpayers from multiple taxation and reveal to the states some of the consequences of nonuniformity in tax structure. According to the first executive director:

> These audits help provide uniform interpretations through the decisions of a single auditor acting on behalf of many states with respect to the same taxpayer. The auditor can demonstrate to the states the effects of varying interpretations. Because variations by the states often are inadvertent, the auditor's mere exposure of variations often will result in a return to the norm by the states. (Corrigan, 1976, p. 437)

The audit selection process begins when a state recommends to MTC's Audit Committee that a firm be selected for examination. The Audit Committee then contacts other states to determine their interest in pursuing the case. Based upon the response from the states a recommendation is made on whether the examination should go forward. Taxpayers may also request that an MTC audit be undertaken. MTC staff auditors conduct the examination and make recommendations to the individual states regarding refunds or assessments; states are not bound by the outcome of the audit. Individual states pay for the audits on a fee-for-service basis. In fiscal year 1993/94 MTC completed 13 sales tax audits and 9 income tax audits entailing 229 contacts with the states; total audit fees were nearly $1.7 million, or $77,193 per audit.

The number of audits conducted in any given year has never been particularly large. Through the decade of the 1990s a peak of 12 completed income tax audits took place in 1993 and encompassed 132 state contracts. Between 1983/84 and 1993/94 assessments plus collections for the income and sales taxes totaled $290 million, benefiting 24 states. Audit productivity has shown considerable variation. In 1984/85 there was $29 in assessments for every dollar spent on auditing; a low of 7:1 was recorded in 1973/74.

Uniformity

MTC has a formal system in place for the development of uniformity recommendations.[26] Generally the recommendations work their way up through the Uniformity and Executive Committees. The Uniformity Committee is comprised of revenue agency personnel who have been appointed by their respective Commission member. Upon request the Uniformity Committee drafts a study for internal review. If the proposal receives Committee approval, public input is sought through *public participation working groups*, which include as members various affected parties, notably the states and representatives of the business community. The working group drafts its version of the proposal for consideration by the Uniformity and Executive Committees. The Executive Committee then takes action, including tabling the initiative or moving it forward for public hearing. Based on input from the public hearing, member states are polled to see whether a majority would adopt the proposal as a Commission policy; they need not agree to adopt the proposal as part of their own tax system. If a majority is in favor of the initiative (both a majority of states and a majority of state population represented by MTC members) a formal vote is held. Upon passage the states are informed of the recommended policy.

[26]See: http://www.mtc.gov/UNIFORM/9STEPS.HTM.

4. Is There a Need For State Corporate Income Tax Coordination?

As noted above, the MTC performs many functions. But in the remainder of this paper we focus on tax uniformity, in part because that was the principal purpose for establishing the MTC. Because Swain and Hellerstein (2005) focus on the sales tax, we limit our discussion to state corporate income tax. As noted above and discussed in section 7, it is the case that there is a lack of interstate uniformity in state corporate income taxes.

Concern over the lack of uniformity has a long history. As far back as 1916, the National Tax Association focused on the lack of uniformity in the distribution of income to the various states, and for many years had a standing committee that considered the issue of state corporate income tax uniformity.[27] But the Willis Commission conducted perhaps the most extensive study of interstate taxation. The Willis Commission concluded:

> It has been found that the present system of State taxation as it affects interstate commerce works badly for both business and the States. It has also been found that the major problems encountered are not those of any one of the taxes studied but rather are common to all of them. This is not surprising in that all of these problems reflect the pervasive conflict between the approach of the taxation of interstate companies as it appears in State and local law, and the practical difficulties of realistic compliance expectations and effective enforcement. Increasingly the States, reinforced by judicial sanction, have broadened the spread of tax obligations of multistate sellers. As the principle of taxation by the State of the market has been accepted, the law has prescribed substantially nationwide responsibility for more and more companies. The expanding spread of tax obligations has not, however, been accompanied by the development of an approach by the States which would allow these companies to take a

[27]For a history of the NTA's involvement see the Willis Commission Report, pp. 128-133.

national view of their tax obligations. The result is a pattern of State and local taxation which cannot be made to operate efficiently and equitable when applied to those companies who activities bring them into contact with many States.

First, it was found that the system is characterized by widespread noncompliance. …

A second defect of the current system is its tendency to give rise to overtaxation and undertaxation. …

A third defect of the present system is the existence of provisions which are advantageous to locally based companies relative to competitors based elsewhere.

…

A fourth defect of the present system is the attitude which it has generated among taxpayers, especially small and moderate-sized companies. The diversities and complexities in legal rules, the prevalence of returns in which the cost of compliance exceed the tax, … and other aspects of the present system have produced widespread resistance to the assumption of taxpayer responsibility. …

The problems found in this system as it operates today are sufficiently troublesome to require that something must be done. Even more disquieting, however, are the prospects for the future. …

A prescribed system as widely disregarded as the present one cannot be said to be one which the interests of the States demand be preserved intact at all costs. At the same time the interests of the nation in a free flow of commerce, unhampered by needless interference, clearly call for a change. The recommendations which

> follow present a program designed to establish a system that will work better for both business and the States (pp.1127-1128).

Many students of tax uniformity have noted, sometimes in rather strong terms, the condition of state corporate income tax uniformity. In 1981, McLure wrote, "Though substantial progress has been made toward uniformity since the landmark *Northwestern Portland Cement v Minnesota* case was decided in 1959, states taxation of the income of multistate/multinational corporations **remains a mess** (emphasis added)." (McLure, 1986, p. 131). Similarly, Henderson (1990) wrote, "This multitude of tax systems amounts to a drag on interstate trade almost as debilitating as the border restrictions our federal system was originally designed to prevent" (p. 1352). In 2003, McLure (2003) did not have a more positive view of state corporation income tax. In addressing a group in California, he stated, "The sales tax system, in particular, is a 'Great Swamp,' but the state income tax system is not much better—a Lesser Bog" (p. 127). He goes on to state that state corporate income taxes badly need rationalization to provide greater uniformity.

There are several problems that arise because of a lack of uniformity in the taxation of interstate income. McLure and Hellerstein (2004) list three general problems: adverse economic effects, excessive compliance costs, and revenue loss from increased opportunity for tax planning. In addition, the existence of multiple state tax systems can lead to more litigation, and more legislative time devoted to tax law changes (Shaviro, 1993). In the remainder of this section we consider the evidence on the three problems listed by Hellerstein and McLure.

Economic Inefficiency

The lack of uniformity can result in economic inefficiency. Differences across states in corporate income tax systems lead to interstate differences in effective tax rates on the return to capital. In equilibrium capital is expected to yield the same after tax rate of return in all states, thus in states with higher effective tax rates the before tax rate of return will be higher than in states with lower effective tax rates. It follows that a revenue neutral (in the aggregate) tax reform that equalized effective marginal tax rates across states would be welfare enhancing. (It is assumed that the aggregate capital stock does not change as result of the reform.) In addition, the interstate differences in state corporate tax systems can also result in differences in effective marginal tax rates by industry and perhaps by type of firm. This adds to the welfare loss.

Shaviro (1993) largely bases his case for uniformity in interstate taxation on the problem of location distortions that are caused by interstate differences in tax rates. He argues that interstate tax disparities have the same effect as an outright tariff, something prohibited by the Constitution.

To the best of our knowledge, no one has attempted to estimate the magnitude of this welfare loss. However, Sørensen (2001) has estimated the welfare loss from differences in effective corporate tax rates across countries in the European Union. He employed a computable general equilibrium (CGE) model to analyze a revenue neutral (within each country) tax reform that eliminated differences across countries in the effective corporate income tax rate and replaced them by a uniform rate throughout the EU, namely the population weighted current marginal tax rates. He finds that such uniformity would increase welfare by 0.16 to 0.35 percent of GDP, an amount he notes to be "disappointingly small."

Given that effective marginal tax rates within the EU are much larger than those for U.S. state corporation income taxes, and that differences in tax rates across the EU are likely to be larger than interstate differences within the U.S., the welfare gain from such a reform in the U.S. would likely be even smaller than what Sørensen estimates for the EU.[28]

A second economic effect from the lack of coordination of state corporate income taxes is tax competition. Wilson (1999), Wildasin and Wilson (2001), Oates (2001), and Zodrow (2003) provide reviews of this literature. As Zodrow points out, the implications of the tax competition literature are mixed, and thus "it is difficult to draw unambiguous conclusions regarding their implications for corporate tax coordination…" (p. 660). The implications of the basic tax competition model, for

[28]This conclusion needs to be tempered since the use of an apportionment formula complicates the effect of corporate taxes on the return to capital and other factors. See McLure (1981).

example, Oates (1972), is that tax competition leads to a "race to the bottom" in terms of tax rates on capital. Thus, in the absence of tax harmonization public services would be underprovided. This result is driven by the assumption that the stock of capital is fixed. Other tax competition models yield contrary implications.

These two economic welfare effects of tax harmonization depend on equalizing effective marginal tax rates across states. But the uniformity that has generally been sought in the U.S. focuses on features of state corporate income taxes other than the tax rates. If states are free to set their own tax rates, or even to provide subsidies to businesses outside the state corporate income tax structure, then any potential welfare improvement from uniformity is likely to be very small.

Compliance Costs

A second major concern regarding the lack of uniformity is the cost of tax compliance. The differences in state corporate tax systems lead to the need to keep duplicative records, to know about a host of different rules and interpret their application, to file multiple tax returns, and to be subject to multiple audits. It is generally assumed that the lack of conformity leads to unreasonable compliance costs. Yet we were able to identify only two studies of the effect of the lack of uniformity on compliance costs.

The first study, conducted by the Willis Commission, was an extensive investigation of corporate income tax compliance costs, as well as sales tax compliance cost. Table 2 shows the distribution of compliance cost as a share of total firm receipts for the corporate income tax. There is a wide range of cost, but for 75 percent of the 100 firms in their sample the range of compliance cost was from 0.01 percent to 0.2 percent of receipts (p. 356).

The Willis Commission noted that individual firm estimates of compliance costs are consistent with the estimates from the Willis Commission's cost study. The report goes on to say that compliance costs are high for some firms but those cases seem to be rare. The report concludes that compliance costs, when compared to gross receipts "do not appear to be very significant for most companies" (p. 383). And the Commission goes on to state, "Indeed, there has been some business

TABLE 2. COMPLIANCE COSTS

Costs/Receipts	Number of Firms
----	5
1/1000 of 1% or less	2
2/1000 of 1%	2
5/1000 of 1%	10
1/100 of 1%	12
2/100 of 1%	14
5/100 of 1%	26
1/10 of 1%	13
2/10 of 1%	9
½ of 1%	3
1% of more	4
Total	100

Source: Willis Commission Report, p. 356

acknowledgement that the present operation of the income tax system is not too expensive" (p. 383).

More recent estimates of the cost of complying with state corporate income taxes are provided by Gupta and Mills (2003). For their sample, the average cost of complying with state corporate income taxes is $258,000 in 1991 dollars.[29] For the 251 firms that report both compliance cost and state income tax liabilities, compliance cost is 2.9 percent of taxes and 0.022 percent of sales. Gupta and Mills use these values to estimate that the aggregate compliance cost for the state corporate income tax for the largest 1000 firms in the Compustat database is $334 million for 1995.

Gupta and Mills note that the compliance cost for the federal corporate income tax is 1.4 percent of tax liability, or less than half the percentage for state corporate income taxes. They state that this provides "prima facie evidence of the impact of disconformity in state tax rules" (p. 363). Gupta and Mills also estimate the effect on compliance cost of the number of returns filed and find that a one percent increase in the number of returns increases compliance cost by 0.04 percent. At the 25th percentile of all variables, the effect of adding one more return is to increase compliance cost by $8,000.

[29]Gupta and Mills (2003) use the data from Slemrod and Blumenthal (1993) and Slemrod (1997).

As a share of receipts, the estimates from the Willis Commission are much larger than those reported by Gupta and Mills. We do not necessarily believe that it would be appropriate to conclude that this implies that compliance costs have decreased. While advances in technology has no doubt lead to a reduction in the cost of maintaining records, etc., differences in the methodologies by which compliance costs were measured may account for the differences.

Over- and Under-Apportionment

Finally, many authors have suggested that differences in state corporate income tax systems can lead to inequities in tax payments in the sense that corporations could be taxed on more or less than their total profits. The focus of this over- or under-apportionment is on the non-uniformity of apportionment formulas across states. There are two studies of this issue that we are aware of.

Sheffrin and Fulcher (1984) calculated state taxable profits using three formulas that differed by the weight of the payroll and sales factors. The three formulas used were: a 100 percent sales factor; a 100 percent payroll factor; and a formula with weights of $2/3^{rd}$ for the payroll factor and $1/3^{rd}$ for the sales factor. The authors did not have property value, so they double weighted payroll in the third formula to account for that.

Clearly, if all states used the same formula, then 100 percent of corporate profits would be taxed. Sheffrin and Fulcher assumed that each state adopted the formula that produced the maximum tax revenue and calculated the amount of corporate profit that would be taxed by the states, and then compared this to the actual total profit for 1980. They found that taxed profit was 6.14 percent higher than actual profit. The same experiment for 1977 yielded an over-apportionment of 4.5 percent.

This overstates the likely over-apportionment since all states do not adopt a formula that maximizes revenue. (Moreover, federal PL 86-272 affords nexus protection to firms for which the only contact with a state is the solicitation of sales.) If each state adopted the revenue maximization formula in 1977 and had that same formula in 1980, Sheffrin and Fulcher find that over-apportionment in 1980 would be only 3.6 percent. They conclude that over-apportionment is not a major issue, and note that this result is consistent with the Willis Commission's finding that the choice of formula is not an issue involving a lot of money.

Sheffrin and Fulcher conducted a further experiment in which they allowed a state to choose a different formula for each industry (defined mainly as two-digit SIC industries) in the state that maximizes the tax revenue from that industry. In this case they find that over-apportionment amounts to 17.1 percent for 1980 and 15.3 percent for 1977. Over-apportionment does differ by industry, with over-apportionment being high for natural resource and manufacturing industries and low for other industries. For example, they calculate that for oil and gas extraction the over-apportionment would be 51.0 percent (which is toward the upper end) and for the paper industry it would be 17.6 percent (which is at the lower end for manufacturing), while for communication it would be 8.8 percent (which is about the median for other industries). Since states do not adopt separate formulas for each industry, the results of the exercise clearly over state the degree of over-apportionment.

The exercise by Sheffrin and Fulcher assumes that each state takes the firm's total profit (for example federal taxable income) and apportions it. But states adopt unique provisions that alter federal taxable income in converting it to state taxable income. These changes could result in larger or smaller over-apportionment. In practice the pressures of interjurisdictional competition probably biases policy toward smaller over-apportionment if not under-apportionment.

Lopez and Martinez-Vazquez (1997) estimated the degree of over- and under-apportionment of corporate profits for different business sectors resulting from heterogeneous apportionment formulas. Their procedure is to simulate each state's actual apportionment formula for 20 2-digit manufacturing industries for the years 1972 to 1987. The time period allows them to account for changes in the value of the factors and in the formula. They find that the profits of these industries were under-apportioned by an average of 4.5 percent over the period. With the exception of tobacco and textile mills, all industries were under-apportioned. Tobacco was over-apportioned by an average of 1.45 percent, while textile mills were over-apportioned by an average of 0.8 percent. The results hold for sub-periods. When they added throwback rules, the results change marginally, but are qualitatively the same.

These two studies suggest that over-apportionment may not be an important issue empirically. But is there an equity issue in principle? Is it unfair for a corporation to be taxed on more than 100 percent of its profits? We can think of fairness in this case as treating two identical corporations the same, i.e., one can apply the principle of horizontal equity. In any case, do differences in apportionment formula violate the principal of horizontal equity? We do not think it would be considered unfair that a firm doing all of its business in one state pays more in state corporate income taxes than a firm with the same profit but located in another state with a higher tax rate. Furthermore, we do not think it would be considered unfair if all states used the same apportionment formula but had different tax rates, and as a result a multistate corporation that did business in the high-tax state paid more taxes than an equivalent corporation doing business in a low-tax state.

Now suppose that there are two states with the same tax rate but different apportionment formulas. Suppose there are two equivalent corporations engaged in the two states and they pay the same total tax, although the tax rates may apply to more than 100 percent of the profits. Now suppose one of the states adopts the same formula as the other state but changes it tax rate so that the two firms continue to pay the same total tax as before. The taxes paid in the later case are no different than the former case when the states had different apportionment formulas. But we suggested above that the later case would be considered fair, so the former case must also be fair. If there are corporations with the same profit but engage in business in a different way in the two states, the corporations are not equivalent, so the principle of horizontal equity does not apply. Thus, we don't think that the issue of over-apportionment is an equity issue. But the resulting differences in effective tax rates may have implications for efficiency.

In summary, it appears that the common view is that the lack of uniformity is a serious problem. This conclusion is based on 1) the writings on state corporate income tax that make this claim, 2) that the concern over uniformity is long standing, and 3) that great effort has been made over a long period to achieve uniformity.

Certainly uniformity of state corporate income taxes would be preferred to non-uniformity. But the evidence that exists does not seem to suggest that the system is "debilitating," as Henderson (1990) suggests. The empirical evidence is sparse and not comprehensive, but it does suggest that the rhetoric may need to be toned down and that more research needs to be conducted.

5. Is Cooperation Feasible? A Theoretical Framework

Analysis of a voluntary tax compact and its effectiveness begs the question of whether states would cooperate with respect to the design of a corporate tax system. This section presents a simple framework in which to consider whether states will mutually agree on some proposed tax provision. The results are not encouraging. For simplicity, assume that a state will either adopt, denoted A, or not adopt, denoted NA, a proposed provision and it does so based on the net benefits from adopting relative to not adopting the provision. Not adopting a proposed provision means the state will maintain the status quo. Consider a state j and let k represent the other state (or all other states). We consider whether the states will mutually agree on the tax provision by framing the decision in a 2 x 2 payoff matrix. Figure 2 is the payoff matrix for state j, where B represents the net payoff for state j and the subscripts represent the decisions of j and k respectively. We assume that states follow Nash behavior, that is, each state acts on the assumption that what the other state has done is given.

FIGURE 2: PAYOFF MATRIX

		State k	
		A	NA
State j	A	$B_{A,A}$	$B_{A,NA}$
	NA	$B_{NA,A}$	$B_{NA,NA}$

There are four cases of the relationships between net benefits that should be considered. For Case 1, $B_{NA,A} > B_{A,A} > B_{NA,NA}$. If this condition holds for both states, then we have a classic prisoner's dilemma game, and if each state follows Nash behavior, equilibrium will be for no state to adopt the proposed provision.

For Case 2, $B_{A,A} > B_{A,NA} \geq B_{NA,NA}$. In this case benefits are higher if both states adopt the provision then if either or both do not adopt. However, if just state j adopts the provision, the net benefit to state j will be smaller, but not less than if neither state adopts the provision. If this condition holds for both states, we expect that states should be willing to agree to adopt the provision. And, if $B_{A,NA}$ is strictly greater than $B_{NA,NA}$ for both states, then the adoption of the proposed policy is the dominant strategy for both states.

For Case 3, $B_{NA,A} = B_{A,A}$, the state is indifferent between adopting and not adopting the provision. Case 4 is the situation for which $B_{A,A} < B_{NA,A} \leq B_{NA,NA}$. In this case not adopting the proposed provision would be the preferred option. While the expected outcome for Cases 1 and 4 are the same, Case 4 is not a prisoner's dilemma game.

If the ranking of benefits is the same for both states, then only for Cases 2 and 3 will both states agree to adopt the provision. In the other two cases, neither state will adopt if they act independently. However, in Case 1 mutual cooperation could yield adoption by both. If the ranking of benefits differ between the states, then both states will adopt only if Case 2 represents the ordering of benefits for one state and Case 3 represents the ordering for the other state. A state represented by Case 2 or Case 3 will adopt regardless of the decision of the other state. A state represented by Case 1 or Case 4 will not adopt the provision regardless of the decision of the other state.

The benefits to a state from adopting a provision as opposed to maintaining the status quo may consist of changes in tax revenue, in state tax administrative expense, in compliance cost for firms, or in the employment level. These might be appropriately labeled as economic benefits.

In addition to these economic benefits, there are more political or psychic factors that may affect the decision of whether to adopt. It is possible that a state views changing its regulations or policies as undesirable, for example the bureaucracy may not want to be bothered with having to change procedures required by the proposed provision. The state might put a relatively high value on maintaining its autonomy and thus does not want to agree to conform. Of course, in that case the state could adopt the provision while maintaining the freedom to modify or discard the provision in the future. The state may have a strong preference for its current provision and thus does not want to change. For example, perhaps the current provision is associated with an important official who has a personal or emotional attachment to it. The current, adopted provision presumably was the result of some political process in which the proposed provision could have been adopted. Thus, generally to change from the current provision to the proposed provision will entail some political cost, although the cost will depend on the nature and magnitude of the change.

Finally, it is not clear how the state will aggregate the different benefits. For example, while states should prefer lower compliance cost for firms, *ceteris paribus*, it is not clear that the state would weight this benefit the same as, say, increased revenue. The weight the state places on a particular benefit no doubt depends on the political pressure interstate and intrastate businesses bring to bear on the subject. For example, a state may adopt an apportionment formula with a heavier weighted sales factor even if tax revenue decreases as a result if the change reduces the tax liability of important firms located in the state and they exert political pressure on the state to adopt the change. A similar case would be a proposal to apportion certain income, for example, royalty income, that is opposed by firms that have allocated such income to states with low or non-existent taxes on such income.

The net benefits will depend on the nature of the tax provision, and in particular whether the proposed provision involves tax policy or tax regulations. An example of the former would be a proposal for a specific apportionment formula, while an example of the later would be a proposal for a common sales tax reporting form. We expect tax policy proposals to involve larger net benefits (either positive or negative) and larger political pressure than tax regulation proposals.

Consider a proposal to adopt a common apportionment formula, say, the 3-factor formula and that initially all states agree to that. Suppose that state j determines that it could increase its tax revenue by shifting to a different formula, say a single factor sales formula. This suggests that the situation is described by Case 1 or Case 4. Such an increase in revenue might occur if the state is a “market region.” But it is not feasible for all states to be “market regions” and thus to benefit from shifting to the same formula. Assuming there are two formulas, then state k must be reflected by Case 2. Thus, state k would retain the 3-factor formula, while state j would switch to the single factor formula.

But the switch to another formula may instead be driven by economic development consideration. Edmiston (2002) studied the effects of shifting to a formula that weights sales more heavily. He finds that it is advantageous in terms of the level of economic activity for a state to independently adopt a double-weighted sales factor formula, but when all states adopt a more heavily weighted sales formula there are winners and losers. In other words, he finds Case 1, i.e., a prisoner's dilemma.

Proposed regulations as opposed to proposed policies are unlikely to have much effect on revenue, but could make compliance easier for firms or might reduce the state's administrative burden. Such proposals probably fall into Case 2, where there is significant benefit if all states adopt the proposal. Thus, it seems that obtaining uniformity on tax regulation issues will be much easier than on tax policy.

There is a substantial literature on the theory of cooperation within a game-theoretic framework. While a discussion of this literature is beyond the focus of this paper, we present some ideas or concepts from that literature that we believe are relevant to the issue of cooperation among states on MTC proposed provisions.

Suppose that for a proposed provision one state falls into Case 1 or Case 4, while the other state falls into Case 2 or Case 3. In this case there is no common policy adopted if states act non-cooperatively. There are two possible approaches to reaching agreement in this situation. One is to compensate the state whose benefit of adopting the proposed provision is negative. This would seem to be difficult to carry out, particularly if the compensation would have to be paid every year that the state agreed to the proposal. A second approach is to bundle provisions, some of which yield positive benefits sufficient to offset the negative benefits from other proposals. This form of logrolling would work only if the adoption of the bundled proposal was all or nothing. But it would be relatively easy for a state to adopt some parts of the bundled proposal but not others.

The more difficult situation is when both states are represented by Case 1. Axelrod has written extensively on game theory, including cooperation. In *The Evolution of Cooperation*, Alexrod (1984) addresses the question, under what conditions will cooperation emerge when the payoffs are represented by Case 1?

Certainly for a prisoner's dilemma game that is played one time by selfish individuals not cooperating is the dominant strategy. Axelrod argues that cooperation can occur if the players in such a game might meet again, that is, if the game is played repeatedly. In such iterated prisoner's dilemma games experiments have shown that cooperative behavior is possible. For example, a Tit for Tat strategy yields cooperative behavior.

In an iterated prisoner's dilemma game there is a series of payoffs, but future payoffs are worth less than current payoffs. Key to a cooperative outcome is that the weights players assign to future outcomes are large enough. Axelrod illustrates this with two examples. Consider two firms that do business with one another. The willingness of the supplier to provide credit to the buyer would fall if there was a high probably that the buyer would go into bankruptcy, which means that the weight on future payoffs is low. Likewise the willingness of two legislators to cooperate would be affected if one of them was unlikely to be re-elected.

What does this suggest about how cooperation among states might be increased? Since cooperation is premised on reciprocity, it would be important for the players to have frequent interactions, even outside the "game." The problem here in the context of the MTC is that there is not a "player" from each state. Rather, the decision of whether to adopt a proposed policy provision is made by the state's elected representatives, most of whom do not participate in interactions with representatives from other states within the context of the MTC. In making a decision, a representative considers the political cost of the decision relative to the gain from cooperation. While the threat of retaliation by other states will reduce the benefits to the state, voters are unlikely to blame the representative.

For cooperation to result in an iterative prisoner's dilemma game, the threat of retaliation, i.e., of defecting, must be effective. With a Tit for Tat strategy if one player defects, then the other player will also defect, resulting in lower payoffs for both players. The first player "learns" that cooperation is better. But with 50 states the threat of retaliation is not likely to be very effective. Suppose that one state does not adopt a proposed policy. To have real retaliation, the other 49 states would have to defect. If only one state defects, the benefits to the other 49 states from maintaining cooperation may fall as a result, but the benefits may be much higher than if they all defect. Thus, this situation is not like the traditional prisoner's dilemma game in which the payoff to the person who does not defect is much lower than if they both defect.

The threat could also come from an external force. In particular, if the federal government threatened some action if states did not cooperate, and if the effect of the action was sufficiently large, then the payoff matrix could change in such a way that not adopting a proposed policy is no longer a dominant strategy. However, if the federal government would not take the action if a few states did not adopt the proposed policy, then some states might decide they could free-ride and thus not adopt the policy.

Of course, it is possible that players do not behave as selfish utility maximizers. For example, players may be altruistic, or engage in what Ernst Fehr and Armin Falk (2002) refer to as "reciprocal fairness". Fehr and Falk show that participants in experiments do show evidence of reciprocal fairness and that cooperation is possible within a prisoner's dilemma game.

What is implied by the above discussion is that cooperation is difficult to achieve for most of the major tax policy proposals, and that significant non-uniformity in state corporate tax systems exists should not be a surprise. The problem is not that all proposed provisions are represented by a prisoner's dilemma. Rather, for many proposed policies some states would benefit from adoption while others would not, that is, some states are represented by Case 2 or Case 3, while others are represented by Case 4. In those situations there will be conformity among some, but not all states.

6. Expectations of Compacts

Helping to explain why interstate cooperation is difficult to achieve is the fact that state governments in America guard their independence, from the competitive behavior of other states and from the intrusive power of the federal government. The ease of labor and capital movement fosters competition among states for economic growth and development. Despite these pressures (and the points made in section 5), joint state action is possible. Compacts offer a means for dealing with problems that are beyond the "jurisdictional reach of any one state" (Zimmerman & Wendell, 1951, p. 5).

Federalism also embraces tension between the national government and the states. There is a risk to the federal structure, however, if a group of states can organize in a way that diminishes the national government's powers. Accordingly, the Compact Clause (Article I, Section 10) of the United States Constitution declares that "…no State shall, without the consent of Congress…enter into any agreement or compact with another State…." A similar provision was included in the earlier Articles of Confederation, with the first compact consummated between two states without Congressional approval two years before the U.S. Constitution was drafted.

From this auspicious start, interstate compacts and agreements are now a staple of interstate cooperation. There are an estimated 192 interstate compacts covering a variety of national and regional matters (Bowman, 2004). Depending on the compact's scope and purpose, it can be administered informally through the actions of the respective states or more formally by an active administrative body or commission with powers delegated to it by the member states. The first compact with its own administrative body is the regional compact termed the Port Authority of New York and New Jersey – officially the Port of New York Authority Compact – that facilitates commerce and development within 25 miles of the Statue of Liberty (Zimmerman, 2002). Created in 1921 with Congressional consent, the Port Authority, among other things, operates port and rail facilities and runs the three major international airports in the area, and it was the owner of the twin towers of the World Trade Center. An example of a national compact in which most states participate, but without a specially created administrative body, is the Interstate

Compact for the Supervision of Parolees and Probationers (Zimmerman, 2002). In this case, compact administration is left up to each state's parole and probation agencies, not a separate interstate commission agency. Thus, there are compacts with and those without administrative commissions. The Multistate Tax Compact created an administrative entity.

Read literally, the Compact Clause would require the states to obtain congressional approval before entering into any agreement with themselves. This interpretation was rejected by the U.S. Supreme Court in *Virginia v. Tennessee* (1893, p. 519) in ruling that the "application of the Compact Clause is limited to agreements that are directed to the formation of any combination tending to the increase of political power in the States, which may encroach upon or interfere with the just supremacy of the United States."

In 1978, the Court faced the same question when corporate taxpayers challenged the constitutionality of the Multistate Tax Compact which was entered into by certain states without congressional approval. The Court, in *U.S. Steel Corp et al. v. Multistate Tax Commission* stated that it was "reluctant … to circumscribe modes of interstate cooperation that do not enhance state power to the detriment of federal supremacy" (p. 460). Despite any enhanced political influence afforded by the "strength in numbers and organization" (p. 479), the Court judged that the states were not organized in a way that encroached upon or interfered with national supremacy. Although the Court recognized that states could gain "some incremental increase in the bargaining power" against corporations and that "…. [g]roup action in itself may be more influential than independent actions by the States….[t]his pact does not purport to authorize the member States to exercise any powers they could not exercise in its absence." Moreover, the Court dismissed claims by taxpayers that the Compact sanctioned a "campaign of harassment" against taxpayers by inducing member states to issue "burdensome requests" for documents and issuing "arbitrary assessments" against taxpayers who refused to comply. As the Court pointed out, only the individual states, not the Multistate Tax Commission, could issue a tax assessment, and, besides, such issues were irrelevant to the facial validity of the Compact. For these and other reasons, the Court upheld the constitutionally of the

Multistate Tax Compact despite the lack of Congressional approval. Thus, within the meaning of the Compact Clause, the Multistate Tax Compact is not an "agreement or compact."

Assessing Compacts in General

Compacts, in general, and the MTC, in particular, face challenges as an "instrumentality of state policy" (Leach and Sugg, 1959). The literature on compacts mainly centers on legal, administrative, and political perspectives. There are case studies of particular compacts and general discussions of interstate cooperation. Weissert and Hill (1994, p. 29) find compacts as the "quintessential intergovernmental solution." Dimock and Benson, in their 1937 pamphlet *Can Interstate Compacts Succeed?* conclude generally in the affirmative because compacts are "an important part of the machinery of American federalism." From the extant literature on compacts, four key concerns persist.

States cede power. The U.S. Supreme Court rejected the contention that states lose power through the Multistate Tax Compact because states retain all their sovereign powers and responsibilities. Ridgeway (1971, p. 298) contents that this "strict legal view…ignores the political side of the matter" by tying one state to the actions of others. In addition, the MTC permits states to select from a smorgasbord of services – a form of pick-and-chose tax approach to tax policy and tax administration. One would not think this is the *modus operandi* of a controlling entity over state behavior.

Lack of oversight. A criticism of compacts is the lack of periodic review by the member states or Congress (Ridgeway, 1971). Dixon (1965) even calls interstate compacts "headless" because they are partially insulated from both legislative and executive branches. States fund the MTC through yearly assessments that may be buried in the budgets of revenue departments and accepted as a matter of course by budget reviewers (both executive and legislative). In one sense, this constitutes yearly acceptance by the state of the role of the MTC since a state could withhold its payment. The other Compact members, however, could have legal standing under contract impairment theory (Hardy, 1982) to contest this action, but the results of such state-against-state litigation could harm future MTC interactions. Barton (1965, p. 169) concludes that compact commissions have "no power to tax and thus are dependent upon the states for annual appropriations [which] renders them responsive to the states rather than to any regional constituency." This dependence theory protects the states. In fact, states have formal and informal controls over the Compact and Commission activities in particular.[30] Formal controls include but are not limited to gubernatorial control over the state's representative, continued state funding, and, ultimately, repeal of the Compact itself. Informal controls include, in part, the Compact's requirement for annual reports, audited financial statements, public participation, and the overall need for Commission solvency. While a state can formally exit the Compact only by repealing its original legislation authorizing the Compact, it can avoid adopting legislation or policy that might be necessary to implement particular MTC policy preferences. Few states engage in any form of periodic, systematic evaluation of their participation in interstate compacts (Florestano, 1994). In contrast, an organized group of taxpayers (i.e., COST) continues to demonstrate a willingness and ability to monitor and aggressively mount challenges to MTC activities that are perceived to be injurious to taxpayer interests. This form of market monitoring has been successful in limiting MTC's actions, such as in the recent efforts by COST to keep MTC from having an administrative role regarding the proposed compact known as the Streamlined Sales and Use Tax Agreement.

Goal succession. Upon meeting its original goal, an organization can expand its coverage in order to perpetuate itself. To the Supreme Court in *U.S. Steel Corp. et al. v. Multistate Tax Commission* (1978), the MTC is a means "to facilitate uniformity of taxation by member states of the income of interstate businesses and to avoid duplicative taxation." Armed with such a broad goal, MTC's wide range of programs confirm the dynamic nature of the original goal, negating the need for goal

[30]Based on the ideas outlined in Dixon (1965, footnote 106).

succession.[31] The MTC's "*Federalism at Risk*" program highlights the range of activities that fall under the ambit of the MTC's goal.

The few control the many. The concern is that a few people, such as the full-time staff administering a compact, could seek to skew the work beyond the confines of the original agreement among the member states. To Leach and Sugg (1959), a successful compact requires the services of "a small group of dedicated" staff and member representatives. Given that state revenue secretaries are the state representatives to the MTC, and they come and go with gubernatorial whims and elections, the growth of MTC participating states over time provides an indication that member states are relatively satisfied with the MTC and its direction. Another indicator of dedication is the long length of service of the two MTC executive directors -- Gene Corrigan from 1969 to 1988 (Brunori, 1999) and Dan Bucks from 1988 to 2005 (Brunori, 2000). While steady leadership at the helm of an organization like the Multistate Tax Commission provides continuity, the coming and going of numerous individuals who have populated the voting slots at the Commission have made the MTC, in essence, a succession of 'different' organizations over the MTC's nearly 38 years of existence. Still, the Compact's purpose of "promoting uniformity" has provided a never changing goal.

Evaluating Interstate Compact 'Commissions'

In a political science dissertation, Hill (1992) conducts the only known systematic study of the effectiveness of interstate compact *commissions*. As such, the study excluded compacts that did not have a central administrative entity, or commission. Hill's study, in particular, focuses on water compact commissions. First, Hill posits a theoretical evaluation framework for compact commissions based upon the organizational effectiveness literature. This theory allows Hill to identify 'effective' interstate water compact commissions based upon a survey of compact

[31]The MTC audited financial statements for June 30, 2003 and 2002 indicate the following projects and activities: cooperative auditing; automation plan; enterprise automation project; national nexus program; nexus activities; nexus education; 4R project; deregulation program; and, TaxNet.

directors and commissioners. Hill then validates those theory-driven results against what the literature characterizes as an effective compact.

Hill frames his work in the organizational effectiveness literature, but finds no single way to measure compact commission effectiveness. Instead, he adopts multiple criteria based on three organizational approaches: the goal model; the system-resource model; and, the strategic constituencies model.

First, the goal model assumes an organization is "deliberate, rational, [and] goal-seeking" so the focus is on the "accomplishment of ends rather than the means of attaining them" (p. 100). Compacts, in particular, "have a finite number of legally defined goals in the compact instrument developed by a consensus among the compacting states … so there is an historical basis for assessing how well the compact commissions have performed their statutory goals" (p. 100). The MTC, in particular, faces competing goals of state sovereignty and multistate tax uniformity.

Hill's system-resource model addresses the means, not the ends, of a compact. Specifically, this model recognizes that goals cannot be attained without sufficient funding of the compact commission. "State support of a compact is also a good indicator of the compacting states' assessments of the commission's effectiveness in terms of doing what the states cannot do for themselves" (p. 101). As demonstrated in Figure 1 discussed above, the MTC's budget (and, by extension, other income-producing activities) have grown over the years. It remains to be seen if the resources devoted are sufficient or efficiently deployed.

A constituency model represents Hill's third theoretical framework for compact commission effectiveness. This model rests on the power of external interests with their own goals in influencing an organization. External influence is especially relevant for a compact commission given that it operates in the political arena. For the MTC, the constituency test fits if for no other reason than the variation in formal state participation and the active monitoring by COST.

Hill uses these three theoretical models to develop variables measurable by survey results that permit him to characterize water compact commissions' effectiveness. Hill isolates two goal model variables—overall effectiveness and goal impact—as assessed by the compact commission executive director. Two systems-resource model variables—funding adequacy and state burden sharing—are also based on the executive director's assessment. Four strategic constituencies model variables, all based on responses from commission members, focused on overall effectiveness, goal impact, specific state actions, and goal consensus. Based upon these results, Hill generated a list of 'effective' and 'not effective' water compact commissions.

Hill sought to validate his theory-derived listing of effective water compact commissions against seven characteristics of effective compacts – he calls them hypotheses – drawn from the general literature on interstate compacts and on water compacts in particular. According to Hill (1992, pp. 114-115), the literature suggests that an effective interstate compact commission must have:

- "coercive authority to force compliance with compact goals"
- "origins…traced to either a federal initiative or a crises that precipitated the development of a compact"
- "formal participation of the federal government"
- no "one state veto voting power"
- "a high degree of communication among its member states"
- "elite constituencies"
- "flexibility."

These seven literature-based criteria for an effective interstate compact commission can serve as one way to assess the MTC's effectiveness.

Being able to force compliance with the goals of the compact is Hill's first element of an effective interstate compact. (As made clear in section 5 above, voluntary cooperation is difficult to achieve, suggesting that forced compliance may be necessary to obtain agreement among all states.) Even in the context of interstate water compacts in which Hill formulated his hypotheses, however, results were at variance with this expectation. As he pointed out, coercive power may not be needed when compact activities are of high quality, where there is a close working relationship and respect among members, and where persuasion and education can foster acceptance of compact recommendations (Hill, 1992, pp. 153-156). Hill relies on Leach and Sugg (1959) for the high quality of work concept. To Leach and Sugg

(1959, p. 213), an effective compact clearly defines the terms of its commission and that body stays focused and does not try to "do too much."

The MTC cannot force compliance with the goals of the Compact. As Hardy (1982) notes, an interstate compact is both a statute and a contract. Therefore, the terms of this relationship means that a member state could seek redress against the actions of another member(s) for any contract impairment. Hill concludes that effective compacts have no post-compact litigation among its members. We know of no state-against-state legal action pertaining to MTC activities. This is despite the fact that states are heterogeneous with notable differences in political culture, economy, and the domicile of multistate taxpayers.

Instead, the compact was challenged by major taxpayers as an unconstitutional agreement among the states given that the Compact did not have Congressional approval as specified by the Compact Clause of the U.S. Constitution. In *U.S. Steel Corp. et al. v. Multistate Tax Commission* (1978), the U.S. Supreme Court upheld the MTC as not enhancing state power at the expense of federal supremacy.

Hill's second criterion is that a federal initiative or a crisis must precipitate creation of the compact for it to be effective. In fact, events that propelled the creation of the MTC included the U.S. Supreme Court's 1959 decision in *Northwestern Portland Cement v. Minnesota*, the enactment later that year of Public Law 86-272, and subsequent Congressional inquiry and legislative proposals. The 1959 law called for a study commission (the Willis Commission) that released its report in 1965, which prompted additional legislative proposals to preempt state tax options. In response, several associations of state officials coalesced around the formation of a multistate tax compact. Although Hill found no support in his study of interstate water compacts for this hypothesis, it does fit the origins of the MTC.

Hill's third hypothesis of an effective compact is the formal participation of the federal government. This bias for federal participation emerges specifically from the geographic setting of water compacts, the subject of Hill's study.

> The rationale for this argument is that compacts draw strength from federal infusions of authority, federal resources (expertise, policy

> information, or finances become available to the commission), and the federal government becomes morally committed to carry out its water resources program in accordance with the compact plan. In the case of federal-interstate compacts…federal involvement creates strong moral and political claims on all future Congresses, even [if] they are not judicially enforceable. (pp. 159-160, citations deleted)

With respect to the MTC, the formal participation of the federal government was trumped by state concerns over sovereignty. State sovereignty, in turn, trumped spillovers given the divergent interests of the states. (See the discussion of sovereignty in section 9.) There is no participation of the federal government in the MTC. In fact, the MTC takes policy positions on federal issues that are perceived to be a threat to state tax sovereignty. For the MTC "to be viable," Sharpe (1975, p. 273) states that "the MTC must be independent of the federal government and respected by business and the states." Therefore, the MTC fails on Hill's federal participation criterion. MTC advocates are likely to find failure here very acceptable.

Criterion number four is the voting structure of the compact with a unanimous vote requirement indicative of an ineffective compact. Article VI of the Multistate Tax Compact specifies that the Commission is "composed of one 'member' from each party State who shall be the head of the State agency charged with administration of the types of taxes to which this compact applies." There is one vote per state. Moreover, Article VI states that the Commission must have a majority of the members present, and that it takes a majority votes for an action to be binding. In 1971, the MTC adopted a bylaw that requires not only a majority of states but a majority of the population represented by the voting members before MTC can approve a proposal. As Sharpe (1975, footnote 211) notes, this provision was adopted only after much concern expressed by California and Pennsylvania interests. Thus, this provision ensures that voting states with small populations cannot coalesce against the larger states. Accordingly, the MTC is an effective compact by Hill's fourth standard.

Hill finds that a high degree of communications among its members is the fifth basis for an effective compact commission. The amount of public information issued annually and the frequency of contact was used by Hill to assess interstate water compacts. Hill found that communication was neither a necessary nor a sufficient condition for compact commission effectiveness. Hill's study was before the Internet and its tremendous opportunities for the provision of public information. The MTC exploits this opportunity with extensive information on the Web, even if it is disjointed in places. Just based upon the types of information posted on the Web (newsletters, annual reports, resolutions, etc.), there are frequent communications with participating states. In terms of frequency of meetings, the Web site conveys numerous meetings, including ones on specialized topics, with the opportunity for participation by teleconference. MTC member states have many opportunities for close communication on relevant tax matters such as meetings of the Federation of Tax Administrators, the National Tax Association, and other groups of state officials.

A high degree of "elite constituency" and participation opportunities is Hill's sixth basis for an effective organization. To Hill (1992, pp. 165-166), an elite constituency means a group with the political ability to influence the achievement of the compact commission's goals. Relevant constituencies would include those that can provide external validity and public/political support. Under the Compact, the formal representatives are the respective state tax commissioners. But, as pointed out in the theory of cooperation (the prior section) there is a need for frequent interactions among the 'players' from each state. It is not the state tax commissioner who has final authority in a state over whether or not to adopt a proposed MTC policy. Rather, it is that state's elected representatives who have the definitive vote in each state, and they are not formal participants in MTC activities. These elected officials may be generally supportive, absent a major controversy. Other supportive constituencies include groups such as the Federation of Tax Administrators.

For a particular business, its only direct contact with MTC may be during a joint tax audit – not the most inviting opportunity for a sharing of constructive ideas. Yet, businesses do interact and monitor the MTC through joint action. What is now known as COST was originally the Committee on State Taxation of the Council of

State Chambers of Commerce. As would be expected, COST is very active in protecting the interests of business taxpayers. Over the years, members of this 'elite constituency' have been very persuasive in getting states to repeal the Multistate Tax Compact or not join in the first place (Peters, 1997). A former chair of COST confirms the reality of this constituency: "The interstate business community has the power and influence to create or destroy" (Peters, 1998). Based upon Hill's sixth criterion, the MTC may be an effective interstate compact commission due to the role of COST. This finding is sure to please COST.

More challenging for MTC is how it is perceived by key constituencies. Sharpe (1975, p. 280) challenged MTC to "pursue policies that will gain and cement the support of the business and state communities before attempting to formulate tax solutions which, though ultimately the most rational and equitable, would be unacceptable to those still suspicious of its motives." While it is hard to know if businesses and states are "still suspicious of its motives," the MTC is not free of distracters.

Another aspect of the same hypothesis is the provision of public participation. Hill found formal methods for interest group participation an indication of an effective compact commission (pp. 165-166). Achieving uniformity among states on a tax matter requires the MTC to engage a wide variety of interested parties in the drafting and vetting of ideas. Therefore, there are public participation working groups that have an active role in reviewing proposed provisions. While such proposals may not be adopted by the MTC, this form of public participation goes beyond mere information sharing events. On the Internet, MTC (2005) provides the following statement regarding public participation with MTC:

> Generally, meetings of the Commission and its Committees are public. Persons attending public sessions need not identify themselves. However, some of the listed meetings may not be entirely public. Under the Commission's *Public Participation Policy*, closed meetings may be held in matters involving certain personnel issues and the acquisition/disposition of real estate, matters required by law to be confidential, including discussion of certain taxpayer

> information, and some discussions with counsel over pending litigation. For your convenience, you may choose to contact [the]… Deputy Director, at [phone number], for an indication of which of the listed meetings may not be entirely public. Your contact, which may be on an anonymous basis, also permits the Commission to provide adequate seating. For more information concerning any meetings or events listed in this Calendar, please contact [the]… MTC Administrative Officer, at the Commission's Washington, DC headquarters office [phone number]. Please note that there are no registration fees associated with attendance at meetings of the Multistate Tax Commission or its committees; however, registration fees are charged for the Annual Meeting Seminar (and associated social events) and the Fall Business-Government Dialogue on State Tax Uniformity.[32]

More specifically, MTC's cited public participation policy provides:

> The Multistate Tax Commission exists to aid in the conduct of the people's business. To this end the Commission declares that its proceedings be conducted openly so that the public may remain informed. In adopting this policy the Multistate Tax Commission finds and declares that it is the intent of this policy that actions of the Multistate Tax Commission be taken openly and that its deliberations be conducted openly.[33]

There is an interesting history to MTC's public participation policy. Public debate among California's State Board of Equalization members on the need for public participation predated MTC's adoption of its public participation provisions.[34] Later, California's other tax agency, the Franchise Tax Board (1999), called for the

[32]MTC (2005).
[33]MTC (2003a).
[34]California Taxpayers' Association (1996).

MTC to amend its public participation policy to incorporate similar open meeting requirements to that required in California. California's legislature premised its continued support for that state's payments to the MTC on this and other accommodations.[35]

Hill's last hypothesis focuses on a compact's flexibility, including its ability to include all affected members in a geographically defined compact. The first part of this flexibility hypothesis relates to the proper geographical coverage of a compact. While it is sensible to include all affected parties within a narrowly defined geographic space such as a water basin, it becomes a little more problematic for a national compact like the MTC. As discussed earlier, the MTC has an inclusive public participation process.

The second part of the flexibility hypothesis is the compact's ability to adapt to changing circumstances in order to avoid becoming ineffective. Hardy (1982) reports that a weakness of interstate compacts is that they are "too inflexible to be effective." This concern relates to the purposes of the compact and the ease of members to make a change.

The MTC encompasses broad purposes. As specified earlier, the Compact's specific purposes are liberal. Even broader, the MTC presents itself as "a joint agency of state governments established to (1) improve the fairness, efficiency and effectiveness of state tax systems as they apply to interstate and international commerce, and (2) preserve state tax sovereignty."[36]

Along with a flexible mission that can meet changing circumstances, an effective compact must offer members an opportunity to terminate their membership if state concerns and that of the compact diverge. The Multistate Tax Compact is not subject to change unilaterally by a state. In fact, a state must repeal its enabling legislation if it wants to exit the Compact. The Commission is endowed with fairly general and broad powers to implement the Compact through changed by laws,

---

[35]California Franchise Tax Board (1999). See Sharpe (1975, footnote 211) on California conditioning earlier support on a voting rule change.
[36]MTC (2003b).

policies and programs. In fact, the bylaws expanded the Compact to allow other forms of membership, as noted above. The expanded scope of membership represents the most significant difference between the bylaws and the Compact itself. Short of formally withdrawing from the Compact, a state can simply not adopt a particular MTC policy. States have a variety of ways to participate in the affairs of the MTC. In fact, a variety of programs and services[37] involve different groups of states (compact members, sovereign members, and other participating members). According to the flexibility hypothesis, the MTC meets this test of an effective compact commission.

In summary, the MTC fits the effective interstate compact commission tests specified by Hill better than the interstate water compacts that he studied. It is not clear, however, that the MTC has been particularly effective in achieving its specific compact objectives since state sovereignty and tax uniformity are conflicting goals.

Economic Criteria for Evaluating a Tax Compact

What are the underlying economic benefits of a compact? There is no known economic analysis of interstate compacts in general or a tax compact in particular. This lack of attention to a tax compact may arise from the fact that the MTC is specified as the only tax-related compact in the most recent comprehensive compact listing (Voit & Nitting, 1999). A framework can be offered to structure an understanding of the economic benefits of a tax compact such as the MTC. The criteria presented here parallel the concerns over nonconformity raised by McLure and Hellerstein (2004) and discussed above.[38]

From an efficiency perspective, a compact should seek to minimize tax administration and tax compliance costs. In *U.S. Steel Corp. et al. v. Multistate Tax Commission* (1978, p. 691-692), the U.S. Supreme Court confirmed this point in saying that the Multistate Tax Compact "symbolized the recognition that, as applied

[37]The MTC audited financial statements for June 30, 2003 and 2002 indicate the following projects and activities: cooperative auditing; automation plan; enterprise automation project; national nexus program; nexus activities; nexus education; 4R project; deregulation program; and, TaxNet.

[38]We ignore the issue of state sovereignty as it does not lend itself to economic assessment.

to multistate business, traditional state tax administration was inefficient and costly to both State and taxpayer." Earlier the Willis Commission Report (1965) called the situation "a picture of a system which calls upon tax administrators to enforce the unenforceable, and the taxpayers to comply with the uncompliable" (Sharpe 1975, footnote 32). Uniformity is an important means of minimizing tax compliance costs. Uniformity and interstate cooperation in administration (including examination and enforcement) may also produce lower costs of administration.

A second dimension of efficiency relates to standard economic distortions. Differences in corporate tax structure are a source of distortion, and these efficiency losses can be reduced through uniformity of state tax systems. A third and rather unique efficiency issue relates to the free-rider problem. Being a compact member of MTC allows the state to vote on Commission matters. But most of the other benefits provided by the MTC can be enjoyed with a "lesser" membership status. In other words, states can nearly free ride. In fact, in an analysis in 1999 of a bill that would repeal the Multistate Tax Compact in California made essentially that argument.[39] Fee-for-service activities like the joint audit program do not lend themselves to free riding.

Because revenue is the objective when a state imposes a tax, a tax-related compact has as an underlying rationale the collection of money due under imposition of the levy. An incentive for non-domicile states to form the Compact was to gain revenue, just as the joint audit program remains one of the most successful programs preserving state involvement in the MTC. The tax burden on business activity can be inequitable through effective tax planning practices. The MTC provides a means of dealing with the planning problem in a number of ways, including uniformity provisions that may reduce multistate avoidance opportunities and through the joint audit program. All of this begs the question of whether or not a compact should be created merely to increase revenue collections. Perhaps this is an issue that will be

[39]California Franchise Tax Board (1999).

addressed more directly by the paper on the proposed sales and use tax collection compact – better known as the Streamlined Sales Tax Program.

7. Has the MTC Led to Greater Uniformity?

It is beyond the scope of this paper to determine the precise economic effects attributable to the Compact and the MTC. As section 3 points out, the MTC engages in a substantial number of activities, and we make no attempt to evaluate those activities with the exception of uniformity. However, it is possible to look qualitatively at trends in uniformity as uniformity can lead to lower efficiency losses associated with the tax system. A primary goal of the Compact is the uniformity of state tax systems and the MTC has actively pursued this goal since inception. There is good evidence that state corporate tax systems have moved toward greater uniformity in the last 40 years.[40] At the same time significant differences remain across the states.

There are at least six major ways that state corporate income tax systems may differ:

- Apportionment formula. While most states use the three factor formula for most industries, many states double weight the sales factor or use just a sales factor. While the level of variation in the factors and their weights that existed at the time of the Willis Commission has decreased, differences still exist, and the formulas used for certain industries, such as airlines, differ substantially across states.
- Definition of the factors used in the formula. There are substantial differences in how states measure property, sales, and payroll. For example, while most states use cost for the property factor, some states use net book value, and states exempt different types of property. For the sales factor, some states include receipts from franchise fees while others do not and there are differences in the treatment of services. States also differ in what is included in payroll; for example some include tax-deferred compensation while others do not. Finally, some states have throwback rules while most do not.

[40]Slemrod (2005) has investigated the complexity of state income taxes and finds that complexity increases with duration, although that effect is not found when he control for more political factors.

- Allocable income. Many states have adopted UDIPTA, but there are substantial differences across states in legislative language defining certain features of the corporate tax, in particular non-business (allocable) income.
- Definition of the taxable firm. Some states require combined reporting for the unitary business but most do not; some states allow combined reporting while others do not.
- Tax base. While most states start with federal corporate taxable income, states make numerous and different adjustments to arrive at state taxable income.
- Administrative procedures. Different states follow different administrative practices, using different forms, examination procedures, and so on. Even with the same corporate tax structure, differences in administrative procedures can lead to higher costs of compliance.

Because of its broad scope—encompassing many elements of the six features noted above—UDITPA represents the most important uniformity initiative a state may adopt. While compact members are expected to adopt UDITPA, other states have adopted UDITPA but have chosen not to be a member of the MTC. By 1963, which is 6 years after the introduction of UDIPTA and prior to the formation of the MTC, only 3 of the 38 states with a corporate income tax had adopted the model tax law. This increased to 29 out of the 45 states with the tax by 1975 and to 31 out of 45 states in 1989 (ACIR, 1990). For 2004, Healy and Schadewald (2004) reported that 24 out of the 46 states with a corporate income tax had adopted UDIPTA, but of the 24, only 9 adopted it without modification. The implied decrease between 1989 and 2004 is probably due to how the various authors categorized partial adoptions of UDIPTA and not actual changes in adoptions.

Another measure of the increase in uniformity is the change in the number of states that have adopted the three-factor apportionment formula, although not necessarily with equally-weighted factors. Weiner (1999) provides such information (see Table 3). In 1929, only two of the 16 states with a corporate income tax used the three factor formula. By 1963 that increased to 26 of the 38 states (68 percent), and

TABLE 3. APPORTIONMENT FORMULAE IN USE, VARIOUS YEARS

	------------Number of states using each formula-------------					
	1929	1948	1953	1963	1977	1989
Three factors[1]						
Property-payroll-sales	2	15	16	26	41	44
Property-manufacturing cost-sales	1	5	3	-	-	-
Two factors[1]						
Property-sales	1	4	3	1	1	-
Property-business	1	2	1	-	-	-
Property-manufacturing cost	-	3	-	-	-	-
Property-payroll	1	-	1	1	1	-
One factor						
Property	4	-	-	-	-	-
Manufacturing cost	1	1	-	-	-	-
Sales	2	3	4	2	2	1
Other	3	n.a.	5	5	-	1
No formula	3[3]	-	-	-	-	-
Number of taxing states[2]	17	34	35	38	46	46

Note: If the state uses multiple formulas, the formula is given for manufacturing companies. Some states may be listed more than once. Since alternative formulas may be available. Manufacturing costs include labor, raw materials and other manufacturing costs.
n. a. = not applicable
[1] Not all states weight each factor equally.
[2] Including Hawaii (tax adopted in 1901), the District of Columbia (1947), and Alaska (1949), Michigan, which taxes on value added instead of income, uses an apportionment formula for purposes of the state corporate value-added tax.
[3] Montana required separate accounting in 1929. Georgia and Oregon had recently adopted the state income tax and had not yet specified the formula.

Source: Adapted from Table 9C.1 in Annex 2c, "Tax Coordination and Competition in the United States of America, "in *The Ruding Report* (1992), p. 433.

by 1977, to 41 out of 46 states (89 percent); in 1989, 44 of the 46 states (96 percent) used the formula. In 1993, 43 states used a three factor formula, with 24 states equally weighting the factors and 19 double weighting the sales factor. Of the other three states, two used just sales. In 2005, 14 states used equally weighted factors and 23 states used double weighed sales; of the other 9 states, 4 used only sales, while the other 5 states more than doubled the weight on the sales factor.[41] The share of states

[41]See Federation of Tax Administrators (2005).

using the three-factor formula stood at only 30 percent in 2005, falling precipitously from its peak of 96 percent in 1989. This illustrates the way in which other state policy objectives—notably economic development—can interfere with achieving the goal of uniformity. While there has been deviation from the three-factor formula specified by UDITPA there is now greater uniformity around sales-weighted apportionment.

Uniformity trends for several dimensions of corporate tax structure are reported in Table 4 for those states with a corporate tax. The first panel of the table emphasizes trends in state conformity with the federal corporate income tax between 1967 and 2005. In all but one instance—the adoption of federal bonus depreciation—there is clear evidence of greater uniformity across states. While most states no longer adhere to federal bonus depreciation provisions, there remains considerable uniformity but now in terms of nonadherence.

TABLE 4. STATE ADOPTION OF CORPORATE INCOME TAX PROVISIONS: PERCENT OF CORPORATE INCOME TAX STATES

Corporate Tax Provision	Percent in 1967	Percent in 2005
Loss Carryover	56.1	100
Federal Tax Deductible	31.7	10.9
Federal Income as Base	56.1	93.4
Federal Depletion Allowance	58.5	93.1
Federal Bonus Depreciation	78.0	28.3
Corporate Tax Provision	**Percent in 1994**	**Percent in 2005**
Original Cost, Property Factor	84.8	86.0
Officer's Comp. in Payroll Factor	80.4	76.3
401(k) Earnings in Payroll Factor	54.3	63.0
Throwback Rule for Sales Factor	56.5	54.3
UDITPA for Nonbus. Income	56.5	54.3
Combined Reporting	65.2	50.0

Note: For apportionment factors, applies only to those states that use the respective factor.
Source: 2005 State Tax Handbook, CCH Inc.; State Tax Handbook, December 31, 1994, CCH Inc.; and State Tax Handbook, 1967, CCH Inc.

Movement toward uniformity is not so apparent in the lower panel of Table 4 where the focus falls on state-specific tax provisions for a more recent time period. In only two cases have the states become more uniform: the use of original cost in defining the property factor and the inclusion of 401(k) earnings in the payroll factor.

Notably there has been slight movement away from UDITPA in defining allocable non-business income.

Table 5 is an MTC summary of adoption of model regulations, statutes and guidelines. It clearly shows that member states are far more willing to pass uniformity recommendations at the Commission level than legislatively adopt them at the state level. Most (full) compact members have adopted uniformity guidelines regarding income allocation and apportionment. But for the vast majority of other initiatives—including apportionment of income for special industries—only a small number of member states have adopted the MTC policy. In fact in one instance (collection of taxes on fundraising transactions, a relatively new guideline) there is no evidence that a single state has adopted the uniformity recommendation. Not shown in the table is adoption of the uniform sales tax exemption form which now is used by 38 states.

Over time there is some tendency toward increased adoption of model guidelines. MTC reports in its 1985/86 *Annual Report* that 20 states had formally or informally adopted its guidelines on apportionment and allocation, while the number was 25 states in 2002. For airline apportionment there were 7 adopting states in 1985/86 versus 11 in 2002; for railroads there were 7 states in 1985/86 and 12 in 2002; for contractors there was no change over this time period (10 states in both years).

There is certainly greater uniformity in the structure of the corporate income tax today than there was when UDITPA was promulgated by NCCUSL and at the time of the Willis Commission. MTC deserves at least some credit for this change in tax structure, but just how much will never be known. While progress has been made, total uniformity will likely never be realized absent federal intervention given the self interest of the states. Options for achieving greater uniformity are discussed next.

Table 5: Adoption of Multistate Tax Commission Model Regulations, Statutes and Guidelines
As of October 18, 2002

State	Allocation & Apportionment of Net Income	Apportionment of Income for Special Industries: Airlines	Construction Contractor	Railroads	Trucking	PL 86-272 Guidelines	Television and Radio Broadcasting	Publishing	Financial Institutions	ABA Model S Corporation Income Tax Act with Six Proposed Modifications "MOSCITA"	Model Direct Pay Permit Regulation	Funeral Trust	Collection of Taxes on Fundraising Transactions	Uniform Protest Statute	Model Recordkeeping & Retention Statute	Uniform Principles Governing State Transactional Taxation of Telecommunications: Vendor Version	Vendee Version	Applicability of Sales and/or Use Tax of Sales of Computer Software
Alabama *	Yes	Yes	Yes	Yes	Yes	Phase II<1>	Yes	Yes<1>	Yes<1>	Yes<1>	No		No	No	Yes	No	No	No
Alaska *	Yes<1>	Yes<2>	Yes<1>	No	Yes<1>	Yes<1>	No	No	Yes<1>	No	No		No	No	No	No	No	No
Arizona	Yes	No	No	No	No	No	Yes	No	No	No								
Arkansas	Yes<1>	No	No	Yes<1>	No	Phase II	No	No	Yes	No								
California *	Yes	No	Yes	Yes	Yes<1>	Phase II<1>	Yes<1>	Yes<1>	Yes	No	No		No	No	No	No	No	No
Colorado	Yes	Yes<1>	Yes	Yes	Yes	Phase II	Yes<1>	No	Yes	No								
Connecticut*	No	No	No	No	No	Phase II<1>	No	No	No	<3>					Yes			
Delaware	No	No	No	No	No	No	No	No	No	No								
District of Columbia	Yes<1>	No	No	No	No	Phase I	No	No	No	No								
Florida *	<2>	No	No	No	No	Phase I	No	No	No	No	No		No	No	Yes<1>	No	No	No
Georgia*	No	No	No	No	No	No	No	No	No	N/D	No		No	No	No	No	No	No
Hawaii *	Yes	No	No	No	No	Phase II	Yes	No	Yes	Yes<1>	No		No	No	No	No	No	No
Idaho *	Yes	Yes	Yes	Yes	Yes	Phase II	Yes	Yes<1>	Yes	N/D	No	Yes	No	No	No	No	No	No
Illinois *	Yes<1>	No	No	No	No	Phase I	No	No	No	No	No		No	No	No	No	No	No
Indiana	<2>	No	No	No	No	No	No	No	No	N/D								
Iowa *	No	No	No	No	No	No	No	No	No	N/D	No		No	No	No	No	No	No
Kansas *	Yes	Yes	No	No	No	Phase I<1>	No	No	Yes	N/D	No		No	No	No	No	No	No
Kentucky*	Yes<2>	No	No	Yes	No	(informally)	No	No	Yes	No	No	No	No	Yes	No	No	No	Yes
Louisiana	No	No	No	No	No	Phase II	No	No	No	No								
Maine*	No	No	No	No	No	Phase II<1>	No	No	Substantial	No								
Maryland	No	No	No	No	No	No	No	No	Substantial	No								
Massachusetts*	No	No	No	No	No	No	No	No	Substantial	No								
Michigan (Single Business Tax)	No	No	No	No	No	No	No	No	Yes	No								
Minnesota*	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No	No
Mississippi*	No	No	No	No	No	No	No	No	Yes	N/D	No	No	No	No	No	No	No	No
Missouri *	Yes	Yes	Yes	Yes	Yes	Phase I	No	No	No	No	No		No	No	No	No	No	No
Montana *	Yes	Yes	Yes	Yes	Yes	Phase II	Under rev.	Under rev.	No	No	No	NR	No	No	No	No	No	No
Nebraska *	Yes<1>	Yes<1>	No	No	Yes<1>	No	No	No	No	No	No		No	No	No	No	No	No
Nevada	No corporate income tax																	
New Hampshire	No	No	No	No	No	No	Yes	No	Yes	<3>								
New Jersey	No	No	No	No	No	No	No	No	No	No								
New Mexico	Yes	Yes	Yes	Yes	Yes	Phase II	No	No	Yes	No								
New York	No	No	No	No	No	No	No	No	No	No								
North Carolina*	Yes<1>	Sales Facto	No	Sales Factor	Sales Factor	No	No	No	No	No	No	NR	No	No	No	No	No	No
North Dakota *	Yes	Yes	No	Yes	Yes	Phase II	Yes	Yes	Yes	No	Yes	NR	No	No	Yes	No	No	Yes<1>
Ohio*	No<1>	No	No	No	No	Substantially	No	No	Yes	No	Yes<1>	No	No	No	No	No	No	Yes<1>
Oklahoma *	<2>	No	No	No	No	No	No	No	No	N/D	No	NR	No	No	No	No	No	No
Oregon *	Yes	Yes	Yes	Yes	Yes	Phase II<1>	No	No	Yes	No	No		No	No	Yes	No	No	No
Pennsylvania*	<2>	No	No	No	No	No	No	No	No	No	No		No	No	No	No	No	No
Rhode Island*	No	No	No	No	No	Phase II<1>	No	No	Yes	No	No		No	No	No	No	No	No
South Carolina *	No	No	No	No	No	Yes<1>	No	No	No	N/D	No		No	No	Yes	No	No	No
South Dakota*	No corporate income tax										Yes				Yes			
Tennessee*	No	No	No	No	No	Phase I	No	No	No	<3>				Yes<1>	Yes<1>			
Texas *	No corporate income tax								No	<3>	No		No			Yes<1>	Yes<1>	Yes<1>
Utah *	Yes	No	Yes	Yes	Yes	Phase II<1>	No	No	Yes	N/D	No		No	No	Yes	No	No	No
Vermont	No	No	No	No	No	No	No	No	No	No								
Virginia	No	No	No	No	No	No	No	No	No	No								
Washington (Business & Occupatio	No	No	No	No	No	No	No	No	Yes	N/D	No		No	No	No	No	No	No
West Virginia*	No	No	No	No	No	No	No	No	No	N/D	No		No	No	No	No	No	No
Wisconsin *	<2>	No	No	No	No	No	No	No	No	No	No		No	No	No	No	No	No
Wyoming *	No corporate income tax										No		No	No	No	No	No	No
Total of Responding States: 35	25	11	10	12	12	25	8	4	22	2	3	1	0	1	8	1	1	2

* Responded to MTC Survey.
<1> With exceptions or additions.
<2> No formal adoption, but formula is similar to UDITPA; Multistate Tax Commission regulations adopted on modified basis.
<3> Does not recognize S Corporations.
N/D Not Determined.
NR No response.
Sources: Research Institute of America; Commerce Clearing House; and 2000 Multistate Corporate Tax Guide, Aspen Publishers Inc.

8. Options for Achieving Uniformity

The alternative approaches to achieving uniformity lie along a continuum. At one extreme is complete state autonomy (including the absence of organizations such as the MTC that promote uniformity), while the other extreme is complete federalization of the state corporate tax (for example, an add-on to the federal corporate tax with the revenues distributed to states on a formula basis). Between these extremes are a voluntary compact (i.e., the MTC model) and a federal mandate (e.g., the Willis Commission approach) which lies short of complete federal take over of the state corporate income taxes. The trade-off along this continuum is between the degree of uniformity achieved (or more appropriately the reduction in the costs and inefficiency generated by non-uniformity) and the loss of state autonomy. In this section, we consider these two approaches and discuss the nature of the trade-off.

It is most unlikely that all states will agree on a uniform corporate income tax structure. This point was made in section 5 from a more theoretical perspective, while section 7 presented evidence of the change in the level of uniformity. But this same conclusion has been reached by several authors.

The Willis Commission Report (1965) concluded:

> Fifty years ago, as the first of the States adopted the income tax, forward-looking men warned of the dangers of each state taxing interstate commerce in its own way. For 50 years State tax administrators have been discussing ways of achieving simplicity and uniformity. One proposal after another has been formulated, discussed, revised, and in spite of the expenditure of enormous effort, discarded. And, today, the States appear to be as far from a solution as they have ever been. In short, history of 50 years of state income taxation leaves no room for optimism that the States will be any more successful in the future than they have in the past.
>
> The problems found in this system as it operates today are sufficiently troublesome to require that something must be done. Even more

> disquieting, however, are the prospects for the future. There is every reason to believe that, without congressional action, the worst features of the present system will continue to multiply (p. 599).

Henderson (1990), former chairman of the Tax Section of the New York State Bar Association, in an address to the National Association of State Sections, made the following statement, "One of our goals for the 1990s should be to encourage the states and cities—through federal action under the commerce clause of the Constitution if necessary—to adopt a single model income tax, so that only the rates will differ between jurisdictions" (pp. 1351-1352).

While Shaviro (1993) notes that the level of "interstate cooperation is in some respects impressive" (p. 72), he goes on to state, "Yet the history of Supreme Court commerce clause litigation richly testifies to the incompleteness of interstate cooperation. The important question is not whether existing cooperation is impressive and substantial but whether it is sufficient. The practical evidence of non-cooperation from litigated cases—which presumably would be even greater if states did not anticipate commerce clause challenges—accords with powerful theoretical reasons for expecting cooperation to fall well short of the optimum" (p. 78).

The history of uniformity since the adoption of state corporate income taxes suggests that the states are not going to voluntarily achieve complete uniformity. In the 50 some years since the Willis Commission and the 40 some years that the MTC has been in existence states have not reached agreement on uniformity (see section 7).

Nor is it clear that either states or interstate businesses will press for uniformity, a point made by Lindholm (1991). Interstate businesses are interested in minimizing the sum of tax payments and compliance costs, not just compliance cost. To minimize taxes interstate businesses take advantage of interstate differences in state corporate tax structures. Thus, businesses are not likely to lobby intensively for complete uniformity, a point made by Shaviro (1993). This is in part reflected in the positions of business groups such as COST, which have been critics of the MTC.

Many states have not been supporters of the MTC and it regulations, as reflected by the number of states that are not MTC members, the number that have not adopted UDIPTA in full and the incomplete adoption of other uniformity provisions. Some of these states regard the MTC as an equal threat to their sovereignty (Sharpe 1975), and this is one reason that some states, for example, New York and Arizona, have either withdrawn from or not joined the MTC. (New York is not a member, while Arizona adopted UDIPTA but is only an associate member.) A second reason why states have not agreed on uniformity is that adoption of the proposed provision may lead to a reduction in a state's tax revenue or to less economic development.

If substantially greater uniformity is desired but not achievable by voluntary state action, then federal action is required. The scope of a federal mandate could range from the extreme of converting the state corporate income tax into a federal add on with revenue allocated back to the state, to mandating uniformity of everything but the tax rate, to mandates over selected features of the tax, e.g., the apportionment formula.[42] Certainly the Federal government has the power through the Commerce Clause to impose controls on state taxation, and has at times done so. In particular, the Supreme Court has stated that the Commerce Clause provides sufficient justification for the federal government to require states to use uniform rules for apportioning or allocating income (see *Moorman Manufacturing v. Bair,* 1978). And, the Federal government has taken action to limit the taxing authority of states, for example, the Railroad Revitalization and Regulatory Reform Act of 1975 (the so called 4 R Act which limits the ability of states to impose differential property taxes on railroads), the Internet Tax Freedom Act, the Telecommunications Act of 1996, the Mobile Telecommunications Sourcing Act, and of course Public Law 86-272.

Is there federal interest at stake? The dissent in the definitive case of *U.S. Steel Corp. et al. v. Multistate Tax Commission* (1978, p. 489) found ample federal interest given the "Willis Report, the Willis Bills, the successor bills, and the dozen shelvings of compact ratification bills."

[42]Since the Willis Commission there have been several pieces of legislation introduced to increase uniformity of state corporate income taxes or at least to limit state discretion. In the early years of the MTC, the various *Annual Reports* spend considerable time discussing various Congressional proposals regarding state taxation.

Might the Federal Government act? While the Commerce Clause gives the federal government the authority to impose restrictions on interstate taxation, this is not a reason or cause for exercising such authority. Rather, such action is likely to be the result of political pressure. If states or interstate businesses lobbied the federal government for uniformity, then Congress may well act; for example, public Law 82-272 was enacted because of an outcry from businesses resulting from the Northwestern case. As history suggests, Congress is not likely to act in response to the pleadings of academic tax policy experts. But as we suggest, states oppose federal intervention since it would result in a loss of state sovereignty. And, as long as the state corporate income tax system is not too outrageous, interstate businesses are not likely to demand complete uniformity, although they might push for further controls on state taxing authority. This suggests that we should not look to the federal government to impose uniformity, particularly if this expands the state power to tax. If that is true, we should seek ways of making the MTC more effective.

Should the Federal Government act? The principal argument against federal action is that the power to tax is seen as essential to the existence of state sovereignty (McLure and Hellerstein, 2004). They argue that there are at least three reasons why it would be insufficient for states to have the power to spend, but with the federal government having the power to tax and distributes revenue to the states: 1) the federal government is likely to impose constraints on how states spend the revenue; 2) the ability of the state to shape its public sector would be substantially limited; and 3) state spending of federal funding is likely to be "bloated and wasteful." Hellerstein has stated, "Absent some pressing need for federal intervention…the states should be free to go their own way" (cited in footnote 5 of Shaviro, 1993).

There are many arguments advanced in support of autonomy for state and local governments. Some of the arguments are based on the economic efficiency inherent in providing the appropriate level and mix of public services at the right scale and which match inter-jurisdictional differences in tastes. The basis for this argument are that smaller governments are more responsive to the preferences of voters and that more jurisdictional choice leads to inter-government competition that drives government to be efficient and to keep taxes low. Support for a more decentralized governmental structure is also found in the Madisonian view that by dividing political authority the potential to do great harm is reduced.

These arguments are relevant to federal control over both tax base and rate, but they do not seem to be as relevant to a federally mandated uniform corporate tax base. Furthermore, given that corporate income tax revenue is a small and declining share of state tax revenue, a federal mandate that did not restrict the tax rate that could be imposed would seem to have little consequence on the ability of the state to provide the appropriate level and mix of public services. But if uniformity meant an expanded capacity to tax multistate businesses, the federal government may be loath to act.

There are other arguments in favor of state autonomy on tax matters. First, autonomy on tax matters would allow state governments to exploit and develop the resources they already posses. Second, autonomy promotes experimentation with different kinds of tax rules or tax policy. Shaviro (1993) argues that while these points have some validity they have "limited consequences" (p. 78).

The first point implies that state governments should be allowed to exploit its unique or monopoly-like positions to the benefit of its citizens, for example, by imposing heavy taxes on natural resources or on tourists/conventioneers. For the corporate income tax, this would allow the state to design its apportionment formula to take advantage of the nature of the state's economic structure, in essence allowing the state to use it competitive advantage to "export" part of its corporate tax. But the state's ability to tailor its corporate income tax also allows the state to react to differential elasticities of capital mobility. While tax credits are one way of reducing taxes to mobile capital, states might shift their apportionment formula to a single sales factor formula or adopt special tax provisions in order to reduce the tax burden on more mobile capital.

The second argument, i.e., state experimentation, is a traditional one. But Shaviro suggests that when one considers the wide range of diversity in tax matters, and that many of the experiments are adopted as ways of exporting taxes "it is hard to remain confident that the 'laboratory' is yielding an acceptable ratio of benefits to costs." (p. 94)

After considering these arguments for federalism, Shaviro (1993) concludes, "while state and local governments serve a number of important purposes, the case for preserving their discretion in deciding what to tax (as opposed to how much to tax) seems weak. …This seems particularly true for relatively narrow and esoteric tax issues, such as the design details for a particular tax base" (p. 94).

In terms of specific Federal action, mandating a system that included specifying the tax rate would seem to be extreme. However, Rivlin (1991) proposed a common shared tax with the proceeds allocated to states on a formula basis. While such a scheme could be adopted by interstate compact, she thought it was more realistic that the federal government would have to enact the tax and collect the tax on behalf of the states.[43]

While such a mandate is not the same as general revenue sharing, it has many of the same features. But the U.S. experiment with general revenue sharing did not last very long. This leads to the obvious concern that if the federal government were to assume responsibility for collecting state corporate income tax and distributing the revenues back to the states via a formula, the federal government would at some point decide to usurp all or part of the revenue.

An argument for not having the federal government dictate the tax base is that such a step may start us on a slippery slope. The federal government has already taken steps to restrict state taxation, in what might be considered relatively minor ways. Specifying everything about the state corporate income tax other than the tax rate would be a much bigger step. Sharpe (1975), for example, points out that, "The danger of the Willis Bill stemmed, not from the extent to which it restricted the states' sovereignty in this particular instance, but from its critical precedential value in extending federal control over state systems of taxation" (p. 243). Concern over recent federal government's actions regarding state sovereignty has lead the National

[43]The proposed tax was part of a larger proposal for a reconsideration of the current state of federalism, and in particular for the states to take a larger role in providing services such as health care. The call for a common tax was driven by the concerns that states compete with each other and that states have unequal resources.

Conference of State Legislatures to launch *Preemption Monitor* to track pending federal legislation and Supreme Court cases.

A similar point was made in an MTC report on federalism, "Over time, however, states' ability to raise their own revenue through their tax systems has come under intense pressure from the federal government, especially where state and local taxation affects interstate commerce." (Multistate Tax Commission 2003c, p. 29) Thus, the issue is not just federal mandates for the structure of the corporate income tax, but the fear of broader federal intervention in state and local tax issues.

A more practical issue with a federally-mandated state corporate income tax base is whether such a mandate could be enforced. Would such a mandate encompass a levy like the Michigan single business tax? Would states simply adopt yet another tax on corporations or adopt programs that target financial benefits to selected corporations in place of tax benefits? The answer is likely to be yes.

One can also point to the experience of local governments and the control imposed by state governments on taxing authority. While the Dillon Rule is not the same as the Commerce Clause, it provides similar authority, and states have certainly used the power to restrict local taxes, e.g., by imposing property tax limitations and expanding tax exemptions. State governments frequently treat local governments as just one more special interest group rather than a partner. If the federal government were to treat states the way some states treat local governments, states do have justification for being concerned.

In 2001, the MTC sponsored a series of public seminars on state taxation and federalism. As might be expected, the report of those seminars (Multistate Tax Commission, 2003c) supported state control over state taxes. "The authority to tax is a key element of state sovereignty and is critical to the ability of states to serve the needs of their citizens and interstate commerce effectively" (p. 6). However, while the MTC argues for state sovereignty in the aggregate in tax matters, it calls for states to give up their individual sovereignty by agreeing to common tax provisions. The report goes on to suggest that, "The tensions surrounding state taxation of interstate commerce can be resolved through greater uniformity and coordination among states in their tax policies and administrative practices affecting interstate commerce. To preserve state sovereign authority and create a productive partnership with Congress on issues of taxation, the Commission recommends…." (p. 6). The report's recommendations include action to strengthen interstate coalitions, enhance cooperation between the states and the federal government, work cooperatively with Congress to enact legislation that supports equitable state taxation, and "coordinate federal and state tax bases in a manner that facilitates federal fiscal policy while minimizing adverse effects on states and localities" (pp. 6-7).

Sharpe (1975) argued that, "UDITPA and the Willis Commission represent polar extremes, volunteerism and coercion. Neither offered the delicate uniformity needed to restore a balance among sovereignty, fairness, and federalism" (p. 243). What is that balance? The level of uniformity achieved through a voluntary compact will be imperfect. Federal mandate will achieve uniformity and lower efficiency costs, but at the cost of a lost of state control, i.e., a federalism issue. In both situations, states lose individual sovereignty. Clearly, there is a difference between voluntarily giving up sovereignty and having the federal government mandate it, even if the resulting corporate tax structure is the same in both cases. So, the basic issue is whether the cost imposed by the current level of non-uniformity is sufficiently high to warrant the lost of control to the federal government. Federal imposition of identical tax rates would be extreme, i.e., would not justify the reduction in state sovereignty. But, since empirical evidence is so limited, it is not clear if the benefit from increased uniformity exceeds the increased cost from reduced state sovereignty.

There are options for seeking state corporate income tax uniformity that lie between a voluntary compact and a federal mandate. For example, suppose that states were to agree on a uniform tax structure (e.g., tax legislation like UDIPTA), but with rates set by the states, where agreement would require approval of, say, half of the states (with a corporate income tax) comprising at least 60 percent of the U.S. population. The federal government could then mandate that each state follow this structure, or provide incentives to the states to adopt the structure, for example, tie some grant programs to the states' adoption of the structure. The MTC could be given the responsibility to issue regulations and to propose changes to the law, with approval of some supermajority of the states. The federal government would yield its authority to the MTC in the sense that the federal government would not change the law without MTC agreement, although it is not clear how this could be accomplished. In practice, such a plan is not likely to surface, especially in light of the states' opposition to a binding compact.

In summary, voluntary cooperation will not yield complete uniformity, or even substantial uniformity on state corporate income tax policy issues. But it is not clear that states and interstate businesses, and perhaps even the MTC, really desire near uniformity. If uniformity is to be substantially increased, federal intervention will be required, which involves a trade off between the benefits of increased uniformity and the cost of the reduction in state sovereignty.

9. Concluding Remarks

If the basic question is "Can the Multistate Tax Compact succeed?"[44] a simple answer is 'yes' given that it became effect in August 1967 and remains a viable organization almost 38 years later in helping states administer their particular corporate income taxes. In essence, that is all the U.S. Supreme Court affirmed in 1978 (in *U.S. Steel Corp. et al. v. Multistate Tax Commission*) as to the validity of the Multistate Tax Compact – that the Compact merely helps states do what they could do otherwise and neither diminishes federal power nor increases the states' power.

The next question is to succeed at *what*? While the MTC has engaged in many worthwhile activities, the goal that is examined in this paper, as stated in the Compact's Purpose (Article I), is to "promote uniformity." The MTC falls short of achieving uniformity, but, then again, one can "promote" without having to show any results. Clearly, a goal of "no state left behind" has not been achieved. Then again, it is quite presumptuous to have assumed, or to continue to assume, that the MTC is all that it takes to achieve tax uniformity given the pronounced (and desirable) competitive nature of states in a federal system. In 1978, even the Court was less than confident that the goal would be achieved when it said "to the extent that the Commission succeeds in promoting uniformity…" (p. 474). To the credit of the member states united by the Compact, the MTC has faithfully pushed the need for uniformity and cooperation against the competitive nature of states and the forceful challenge of corporate taxpayers. Of course, this has been achieved by redefining success – as in finding a way to get as many states as possible at the discussion table even if it takes expanding the terms of participation to include different member classifications. Fundamentally, the conflicting goals of sovereignty and uniformity clash. However, while the MTC argues for state sovereignty in the aggregate in tax matters, it calls for states to give up their individual sovereignty by agreeing to common tax provisions.

Game theory suggests that it should not be a surprise that cooperation and uniformity are hard to achieve. Cooperation is possible, but not always. Moreover,

[44] Based on the title of Dimock and Benson (1937) book: "Can Interstate Compacts Succeed?"

the experience of interstate compacts and their administrative entities – the compact commission – confirms that trying to define the success of these organizations is illusive.

There are alternatives to the current situation of non-uniformity of corporate taxation. The federal government could assert its rights under interstate commerce to clean up what McLure (1986, p. 131) termed “a mess,” either by state invitation or federal fiat. Voluntarily giving up state sovereignty is unlikely to provoke a positive response from states absent a tangible carrot – the assurance of money (either preventing the loss of the existing level of collections or, better yet, capturing an increase). The cost of non-conformity for elected officials and corporate taxpayers, in particular, and the economy, in general, remains unanswered.

References

Advisory Commission on Intergovernmental Relations. 1990. *Significant Features of Fiscal Federalism, Volume 1: Budget Processes and Tax Systems*. Washington DC: ACIR.

Alexrod, Robert. 1984. *The Evolution of Cooperation*. New York: Basic Books, Inc.

Barton, Weldon V. 1965. *Interstate Compacts in the Political Process*. Chapel Hill, NC: University of North Carolina Press.

Bowman, Ann O'M. 2004. "Horizontal Federalism: Exploring Interstate Interactions." *Journal of Public Administration Research and Theory* 14(4): 535-546.

Brunori, David. 1999. "Interview: Gene Corrigan, A 'Proud Parent' of the MTC." *State Tax Notes* 17: 1295-1301.

Brunori, David. 2000. "Interview: Dan Bucks of the Multistate Tax Commission." *State Tax Notes* 19:303-308.

Bucks, Dan. 2000. "Dan Bucks of the Multistate Tax Commission." *State Tax Notes* 19:303-311.

Cahoon, C.R. and William R. Brown. 1973. "The Interstate Tax Dilemma — A Proposed Solution." *National Tax Journal* XXVI:187-97.

California Franchise Tax Board. 1999. "Analysis of Original Bill [AB 753, to repeal the Multistate Tax Compact]." March 31.

California Taxpayers' Association. 1996. "BOE Adopts Clarifications to Computer Software Property Tax Exemption Regulation." *CaltaxLetter*, July 29, 1996. Available at: http://caltax.org/member/taxletter/vol9-28.htm.

Cappetta, Fredrick P. 1974. "The Joint Audit Program of the Multistate Tax Commission." *Annual Report of the Multistate Tax Commission, 1973/1974*.

Corrigan, Eugene F. 1976. "Interstate Corporate Income Taxation – Recent Revolutions and a Modern Response." *Vanderbilt Law Review* 29:423-442.

Dimock, Marshall Edward and George C.S. Benson. 1937. *Can Interstate Compacts Succeed: The Uses and Limitations of Interstate Agreements?* Chicago: Public Policy Pamphlet No. 22, The University of Chicago Press.

Dixon, Jr., Robert G. 1965. "Constitutional Bases for Regionalism: Centralization; Interstate Compacts; Federal Regional Taxation." *The George Washington Law Review* 33:47-88.

Edmiston, Kelly. 2002. "Strategic Apportionment of the State Corporate Income Tax." *National Tax Journal* 55(2):239-262.

Federation of Tax Administrators. 2005. "State Apportionment of Corporate Income." Available at: http://www.taxadmin.gov/fta/rate/corp_app.html.

Fehr, Ernst and Falk, Armin. 2002. "Reciprocal Fairness, Cooperation and Limits to Competition." In E. Fullbrook (ed.), *Intersubjectivity in Economics*. New York: Routledge.

Florestano, Patricia S. 1994. "Past and Present Utilization of Interstate Compacts in the United States." *Publius* 24:13-24.

Gupta, Sanjay and Lillian F. Mills. 2003. "Does Disconformity in State Corporate Income Tax Systems Affect Compliance Cost Burdens?" *National Tax Journal* 56(2):355-372.

Hardy, Paul T. 1982. *Interstate Compacts: The Ties That Bind*. Athens GA: Institute of Government, University of Georgia.

Healy, John C. and Michael S. Schadewald. 2004. *2004 Multistate Corporate Tax Guide*. New York: Aspen Publishers.

Hellerstein, Jerome R. and Walter Hellerstein. 1988. *State and Local Taxation: Cases and Materials*. 5th edition. St. Paul: West Publishing Company.

Henderson, Gordon D. 1990. "What Can We Do about What's Wrong with the Tax Law." *Tax Notes* 49:1349-1353.

Hill, James Perry. "Managing the Nation's Waters Without Washington: The Interstate Compact Experience." Unpublished Ph.D dissertation, Department of Political Science, Michigan State University.

Hunter, Merlin Howard and Harry Kenneth Allen. 1940. *Principles of Public Finance*. New York: Harper and Brothers Publishers.

Johnson, R. Bruce. 2001. "The Multistate Tax Commission – Its History and Its Future." *The State and Local Tax Lawyer* 6:45-55.

Kinnear, George. 1971. "The Multistate Tax Commission: A New Experiment in Intergovernmental Relations." *Canadian Tax Journal* XIX(2):136-143.

Krol, Richard J. 1975. "Taxpayers Balking at Submitting to Audits of the Multistate Tax Commission." *The Journal of Taxation* 43(1):364-367.

Leach, Richard H. and Redding S. Sugg, Jr. 1959. *The Administration of Interstate Compacts*. Baton Rouge LA: Louisiana State University Press.

Lindholm, Doug. 1991. "State Tax Uniformity Debated at Multistate Tax Commission Dialogue." *State Tax Notes* 236:236.

Lopez Salvador and Jorge Martinez-Vazquez. 1998. "State Corporate Income Taxation: An Evaluation of the Formula Apportionment System." *National Tax Association, Proceedings of the Ninth Annual Conference*, pp. 155-62.

McLure, Jr. Charles E. 2003. "Reducing the Nuttiness of State Taxes and Draining the Swamp: What California Should Do." *State Tax Notes* 27:127-30.

_____. 1986. "Toward Uniformity in Interstate Taxation: A Further Analysis." In C.E. McLure, Jr. (ed), *Economic Perspectives on State Taxation of Multijurisdictional Corporations*. Arlington VA: Tax Analyst.

_____. 1981. "The Elusive Incidence of the Corporate Income Tax: The State Case." *Public Finance Quarterly* 9(4):395-413.

McLure, Jr., Charles E. and Walter Hellerstein. 2004. "Congressional Intervention in State Taxation: A Normative Analysis of Three Proposals." *State Tax Notes* 31:721-735.

Moorman Manufacturing v. Bair, 437 U.S. 267, 280 (1978).

Multistate Tax Commission. 2003a. "Public Participation Policy." Adopted November 21, 1996, amended August 1, 2003. Available at: http://www.mtc.gov/PUBLCPAR/Ppp0803.htm.

Multistate Tax Commission. 2003b. "About the Multistate Tax Commission." Available at: http://www.mtc.gov/ABOUT MTC/About MTC05_03.htm.

Multistate Tax Commission. 2003c. *Federalism at Risk: A Report by the Multistate Tax Commission*. Washington DC: MTC.

Multistate Tax Commission. 2005. "Statement Regarding Public Participation." Available at: http://www.mtc.gov/MEETINGS/calendar.htm.

Multistate Tax Commission. Various Years. *Annual Report*. Washington DC: MTC.

Mudge, F.W. 1934. "The Taxation of Business Corporations." In Elmer D. Fagan and C. Ward Macy (eds), *Public Finance: Selected Readings*. London: Longmans, Green and Company.

Northwestern Portland Cement v. Minnesota, 358 U.S. 450 (1959).

O'Neill, James P (New Mexico Tax Research Institute). Undated. "The Streamlined Sales and Use Tax Agreement and New Mexico's Gross Receipts and Compensating Taxes." Available: http://legis.state.nm.us/lcs/bluetaxdocs/Steamlined.pdf.

Oates, Wallace E. 2001. "Fiscal Competition and European Union: Contrasting Perspectives." *Regional Science and Urban Economics* 31:133-145.

_____. 1972. *Fiscal Federalism*. New York: Harcourt Brace Jovanovich.

Oveson, Val. 2002. "Lessons in State Tax Simplification." *State Tax Notes* 23:283-287.

Peters, James H. 1997. "Why the Multistate Tax Compact?" *State Tax Notes* 12:1607-1612.

_____. 1998. "What Kind of Interstate Tax System Do You Want? A Challenge to the Interstate Business Community." *State Tax Notes* 14:765-768.

Pomp, Rick and Oliver Oldman. 2001. *State and Local Taxation*, 4th edition. Harford CT: R.D. Pomp.

Ridgeway, Marian E. 1971. *Interstate Compacts: A Question of Federalism*. Carbondale IL: Southern Illinois University Press.

Rivlin, Alice M. 1991. "Distinguished Lecture on Economics in Government: Strengthening the Economy by Rethinking the Role of Federal and State Governments." *Journal of Economic Perspectives* 5(2):3-14.

Seligman, Edwin R. A. 1925. *Essays in Economics*. New York: Macmillan.

Sharpe, Jerry. 1975. "State Taxation of Interstate Businesses and the Multistate Tax Compact: The Search for a Delicate Uniformity." *Columbia Journal of Law and Social Problems* 11(2):231-280.

Shaviro, Daniel. 1993. *Federalism in Taxation: The Case for Greater Uniformity*. Washington DC: AEI Press.

Sheffrin, Steven M. and Jack Fulcher. 1984. "Alternative Divisions of the Tax Base: How Much is at Stake?" In C.E. McLure, Jr. (ed.), *The State Corporate Income Tax: Issues in Worldwide Unitary Combination*. Stanford CA: Hoover Institute Press, pp. 192-213.

Slemrod, Joel. 2005. "The Etiology of Tax Complexity: Evidence from U.S. State Income Tax Systems." *Public Finance Quarterly* 33(3):279-299.

_____. 1997. "Measuring Taxpayer Burden and Attitudes for Large Corporations: 1996 and 1992 Survey Results." *Office of Tax Policy Research Working Paper No. 97-1*. Ann Arbor: University of Michigan.

Slemrod Joel, and Marsha Blumenthal. 1993. "The Compliance Cost of Big Business." Washington DC: The Tax Foundation.

Sørensen, Peter Birch. 2001. "Tax Coordination in the European Union: What Are the Issues." *Swedish Economic Policy Review* 8:143-195.

Swain, John and Walter Hellerstein. 2005. "The Political Economy of the Streamlined Sales and Use Tax Agreement." Paper presented at the National Tax Association Spring Symposium, Washington DC, May 20.

U.S. Steel Corp. et al. v. Multistate Tax Commission, 434 U.S. 452 (1978).

Virginia v. Tennessee, 148 U.S. 503 (1893).

Voit, William and Gary Nitting. 1999. *Interstate Compacts and Agencies, 1998*. Lexington KY: Council of State Governments.

Weiner, Joann M. 1999. "Using the Experience in the U.S. States to Evaluate Issues in Implementing Formula Apportionment the International Level." *OTA Paper 83*. Washington DC: Office of Tax Analysis, U.S. Department of the Treasury.

Weissert, Carol S. and Jeffrey S. Hill. 1994. "Low-Level Radioactive Waste Compacts: Lessons Learned from Theory and Practice." *Publius* 24:27-43.

Welch, Susan and Cal Clark. 1993. "Interstate Compacts and National Integration: An Empirical Assessment of Some Trends." The Western Political Quarterly 26(3):475-84.

Wheeling Steel Corp. v. Fox, 298 U.S. 193 (1936).

Wildasin, David E. and John D. Wilson. 2001. "Tax Competition: Bane or Boon?" University of Kentucky.

Willis Commission Report. 1965. Special Subcommittee on State Taxation of Interstate Commerce of the Committee on the Judiciary. H.R. Rep. No. 89-952 (1965); H.R. Rep. No. 89-565 (1965); H.R. Rep. No. 88-1489 (1964). Washington DC: U.S. Government Printing Office.

Wilson, John D. 1999. "Theories of Tax Competition." National Tax Journal 52:269-304.

Zimmerman, Frederick L. and Mitchell Wendell. 1951. *The Interstate Compact Since 1925*. Chicago: The Council of State Governments.

Zimmerman, Joseph F. 2002. *Interstate Cooperation: Compacts and Administrative Agreements*. Westport CT: Praeger Publishers.

Zodrow, George R. 2003. "Tax Competition and Tax Coordination in the European Union." *International Tax and Public Finance* 10:651-671.

About the Authors

W. Bartley Hildreth is the Regents Distinguished Professor of Public Finance at Wichita State University, with joint tenured appointments on the faculty of public administration in the Hugo Wall School of Urban and Public Affairs and the finance faculty of the W. Frank Barton School of Business. Additionally, he serves as Director of the Kansas Public Finance Center. His research interests include tax policy, public budgeting and financial management, and municipal securities. Dr. Hildreth received his Doctorate in Public Administration from the University of Georgia.

Matthew N. Murray is Professor of Economics and Associate Director of the Center for Business and Economic Research at the University of Tennessee, Knoxville. His recent research focuses on sales taxation, tax evasion and avoidance, regional economic development, and state corporate income tax. Dr. Murray holds a Ph.D. from Syracuse University.

David L. Sjoquist is Professor of Economics, holder of the Dan E. Sweat Distinguished Scholar Chair in Educational and Community Policy, and Director in the Fiscal Research Center of the Andrew Young School of Policy Studies at Georgia State University. He has published widely on topics related to state and local public finance and urban economics. He holds a Ph.D from the University of Minnesota.

About The Fiscal Research Center

The Fiscal Research Center provides nonpartisan research, technical assistance, and education in the evaluation and design of state and local fiscal and economic policy, including both tax and expenditure issues. The Center's mission is to promote development of sound public policy and public understanding of issues of concern to state and local governments.

The Fiscal Research Center (FRC) was established in 1995 in order to provide a stronger research foundation for setting fiscal policy for state and local governments and for better-informed decision making. The FRC, one of several prominent policy research centers and academic departments housed in the School of Policy Studies, has a full-time staff and affiliated faculty from throughout Georgia State University and elsewhere who lead the research efforts in many organized projects.

The FRC maintains a position of neutrality on public policy issues in order to safeguard the academic freedom of authors. Thus, interpretations or conclusions in FRC publications should be understood to be solely those of the author.

FISCAL RESEARCH CENTER STAFF

David L. Sjoquist, Director and Professor of Economics
Peter Bluestone, Research Associate
Margo Doers, Administrative Coordinator
Kenneth J. Heaghney, State Fiscal Economist
John W. Matthews, Research Associate
Lakshmi Pandey, Senior Research Associate
William J. Smith, Senior Research Associate
Dorie Taylor, Assistant Director
Arthur D. Turner, Microcomputer Software Technical Specialist
Sally Wallace, Associate Director and Associate Professor of Economics
Laura A. Wheeler, Senior Research Associate
Tumika Williams, Staff Assistant

ASSOCIATED GSU FACULTY
James Alm, Chair and Professor of Economics
Roy W. Bahl, Dean and Professor of Economics
Carolyn Bourdeaux, Assistant Professor of Public Administration and Urban Studies
Robert Eger, Assistant Professor of Public Administration and Urban Studies
Martin F. Grace, Professor of Risk Management and Insurance
Shiferaw Gurmu, Associate Professor of Economics
Amy Helling, Associate Professor of Public Administration and Urban Studies
Gregory B. Lewis, Professor of Public Administration and Urban Studies
Jorge L. Martinez-Vazquez, Professor of Economics
Theodore H. Poister, Professor of Public Administration and Urban Studies
David P. Richardson, Professor of Risk Management and Insurance
Michael J. Rushton, Associate Professor of Public Administration and Urban Studies
Bruce A. Seaman, Associate Professor of Economics
Geoffrey K. Turnbull, Professor of Economics
Mary Beth Walker, Associate Professor of Economics
Katherine G. Willoughby, Professor of Public Administration and Urban Studies

PRINCIPAL ASSOCIATES
David Boldt, State University of West Georgia
Gary Cornia, Brigham Young University
Kelly D. Edmiston, Federal Reserve Bank of Kansas City
Alan Essig, Georgia Budget and Policy Institute
Dagney G. Faulk, Indiana University Southeast
Catherine Freeman, U.S. Department of Education
Richard R. Hawkins, University of West Florida
Julie Hotchkiss, Atlanta Federal Reserve Bank
Mary Mathewes Kassis, State University of West Georgia
Julia E. Melkers, University of Illinois-Chicago
Jack Morton, Morton Consulting Group
Ross H. Rubenstein, Syracuse University
Benjamin P. Scafidi, Georgia College and State University
Jeanie J. Thomas, Senior Research Associate
Kathleen Thomas, Mississippi State University
Thomas L. Weyandt, Atlanta Regional Commission

GRADUATE RESEARCH ASSISTANT
Kailou Wang

RECENT PUBLICATIONS

(All publications listed are available at http://frc.aysps.gsu.edu or call the Fiscal Research Center at 404/651-2782, or fax us at 404/651-2737.)

Cooperation on Competition: The Multistate Tax Commission and State Corporate Tax Uniformity **(W. Bartley Hildreth, Matthew N. Murray and David L. Sjoquist)**. This report explores how interstate uniformity of state corporate income taxes has varied over time, the role played by the MTC, and how likely it is that uniformity will be achieved. FRC Report 110 (August 2005)

Tax Revenue Volatility and a State-Wide Education Sales Tax **(John Matthews)**. This brief examines issues of revenue source stability raised by proposals to shift K-12 education costs from local property taxes to a state-wide sales tax. FRC Brief 109 (June 2005)

Accountability for Economic Development Incentives in Georgia **(Jeanie Thomas)**. This report identifies Georgia's major economic development incentives and other forms of public finance support and calls for a comprehensive evaluation of public expenditures in this area. FRC Report/Brief 108 (July 2005)

Teen Childbearing and Public Assistance in Georgia **(Lakshmi Pandey, Erdal Tekin and Sally Wallace)**. This brief examines the link between teen births and welfare. FRC Brief 107 (May 2005)

The Link Between Teen Childbearing and Employment in Georgia **(Lakshmi Pandy, Erdal Tekin and Sally Wallace)**. This brief analyzes teen births and employment of teen mothers. FRC Brief 106 (May 2005)

What Georgians Are Thinking About Taxes III **(Peter Bluestone)**. This brief is the third of three briefs reporting on telephone surveys of Georgians. FRC Brief 105 (April 2005)

What Georgians Are Thinking About Taxes II **(Peter Bluestone)**. This brief is the second of three briefs reporting on telephone surveys of Georgians. FRC Brief 104 (April 2005)

Fiscal Capacity of Counties in Georgia **(John Matthews)**. This brief examines the fiscal strength of Georgia's counties. FRC Brief 103 (April 2005)

Status of Health and Pension Benefits for Employees of the State of Georgia in 2004 **(David P. Richardson)**

This report analyzes the Health and Retirement Package offer to employees of the State of Georgia. FRC Report/Brief 102 (April 2005)

What Georgian's are Thinking About Taxes I **(Peter Bluestone and Sally Wallace)**

This brief is the first of three briefs reporting on telephone surveys of Georgians. FRC Brief 101 (March 2005)

A Historical Perspective of Georgia's Economy **(Mary Mathewes Kassis and David Boldt)**

This report chronicles the history of Georgia's economy from the 1950s to the present and provides an outlook for the future growth areas in Georgia. FRC Report/Brief 100 (February 2005)

How Different are Sales Tax Rates Along Georgia's Border? **(Lakshmi Pandey and David L. Sjoquist)**

This brief provides a comparison of sales tax rates in counties on Georgia's borders. FRC Brief 99 (January 2005)

An Initial Evaluation of a Proposed Statewide Education Sales Tax **(David L. Sjoquist, John W. Matthews and William J. Smith)**

This report provides a preliminary analysis of a proposal to replace education property taxes with a statewide sales tax. FRC Report 98 (December 2004)

Financing Georgia's Future **(Peter Bluestone, David L. Sjoquist, William J. Smith and Sally Wallace)**

This report explores how Georgia finances its expenditures through various revenue sources and compares Georgia's taxes across states and over time on multiple dimensions. FRC Report 97 (December 2004)

The Advantage of Accessibility to Goods and People: Transportation and Georgia's Economic Development **(Amy Helling)**

This report describes how transportation affects Georgia's economic development at present and what is likely in the future, and makes a set of recommendations for the direction of state transportation policy. FRC Report/Brief 96 (November 2004)

Distribution of Per Capita Income in Georgia: 1969-2000 **(Robert L. Collins and William J. Smith)**

This paper examines major changes in the county-level distribution of per capita income between 1969 and 2000. The analysis focuses on income convergence and geographic shifts in per capita income over the 31-year period. FRC Report/Brief 95 (September 2004)

(All publications listed are available at http://frc.aysps.gsu.edu or call the Fiscal Research Center at 404/651-2782, or fax us at 404/651-2737.)

Cooperation on Competition: The Multistate Tax Commission and State Corporate Tax Uniformity

Publisher(s): Fiscal Research Center of the Andrew Young School of Policy Studies

Author(s): W. Bartley Hildreth; Matthew N. Murray; David L. Sjoquist

Date Published: 2005-08-01

Subject(s): Community and Economic Development; Government Reform