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by Karl A. Frieden and Douglas L. Lindholm

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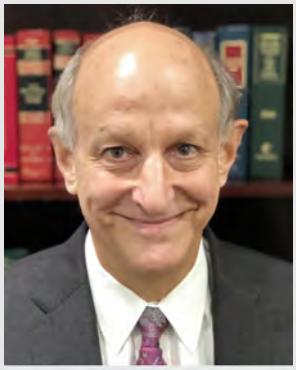

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In this article, Frieden and Lindholm explore why it is so important to view proposals to expand foreign-source income inclusion in state corporate income tax bases not in isolation, but as part of the larger fabric of state and local taxation of businesses.

The inclusion of foreign-source income (FSI)[1] in the state corporate income tax (CIT) base consistently ranks as one of the most controversial and hotly debated state tax issues. Over the years, FSI treatment has surfaced numerous times in virtually every state legislature, and parties as diverse as the U.S. Supreme Court, state supreme courts, a U.S. presidential commission, and key foreign trading partners have all weighed in on different elements of the subject.[2] It is our view, however (and the topic of this article), that most legislative examinations of the FSI issue, and particularly those considered after passage of the federal Tax Cuts and Jobs Act in 2017, have failed to consider state taxation of FSI within a broader tax policy context and its impact on state and national economic competitiveness. That failure is creating negative consequences in the state tax arena — ramifications that state policymakers should not ignore.

There's an ancient Buddhist parable called "The Blind Men and the Elephant" that is instructive here. The parable describes the experiences and impressions of four blind men examining an elephant for the first time. One feels the trunk, another a tusk, another the elephant's leg, and the fourth latches on to an ear. Upon later comparison, their subjective interpretations, each undoubtedly correct, differ so greatly that the men come to blows after accusing each other of dishonesty. One of the lessons of the parable, of course, is that unless we examine the entire animal, our selective interpretations of its characteristics are necessarily incomplete.

In considering the merits of FSI inclusion, it is imperative that state legislators and policymakers consider the broader context of state business taxes. Most significant FSI legislative proposals in the last few years have been stand-alone bills with

[1] FSI is taxed by states under many different methods and theories, and may include foreign dividends, income of controlled foreign corporations and 80-20 companies, subpart F income, income from foreign partnerships, income of "tax haven" subsidiaries, global intangible low-taxed income, and implementation of mandatory worldwide combined reporting. All are manifested by inclusion of FSI in a state's (domestic) CIT base.

[2] *See generally* Department of Treasury, "The Final Report of the Worldwide Unitary Taxation Working Group: Chairman's Report and Supplemental View" (Aug. 1984); *Container Corp. v. Franchise Tax Board*, 463 U.S. 159 (1983); *Barclays Bank PLC v. Franchise Tax Board*, 512 U.S. 298 (1994).

legislative deliberations undertaken in isolation from other state tax policy issues.[3] To rectify this glaring imbalance, any debate over inclusion of FSI in the state CIT base should encompass:

- the recent rapid growth of state CIT revenue without further FSI base inclusion;
- the impact of transformational global tax reform that for the first time is systematically addressing (and reducing) low-taxed FSI through the adoption of a global minimum tax (GMT);
- the need to match increased CIT base inclusion of FSI with a commensurate CIT apportionment formula that requires foreign factor representation; and
- consideration of the design flaws in other state and local taxes that disfavor businesses far more than the CIT design purportedly favors businesses.

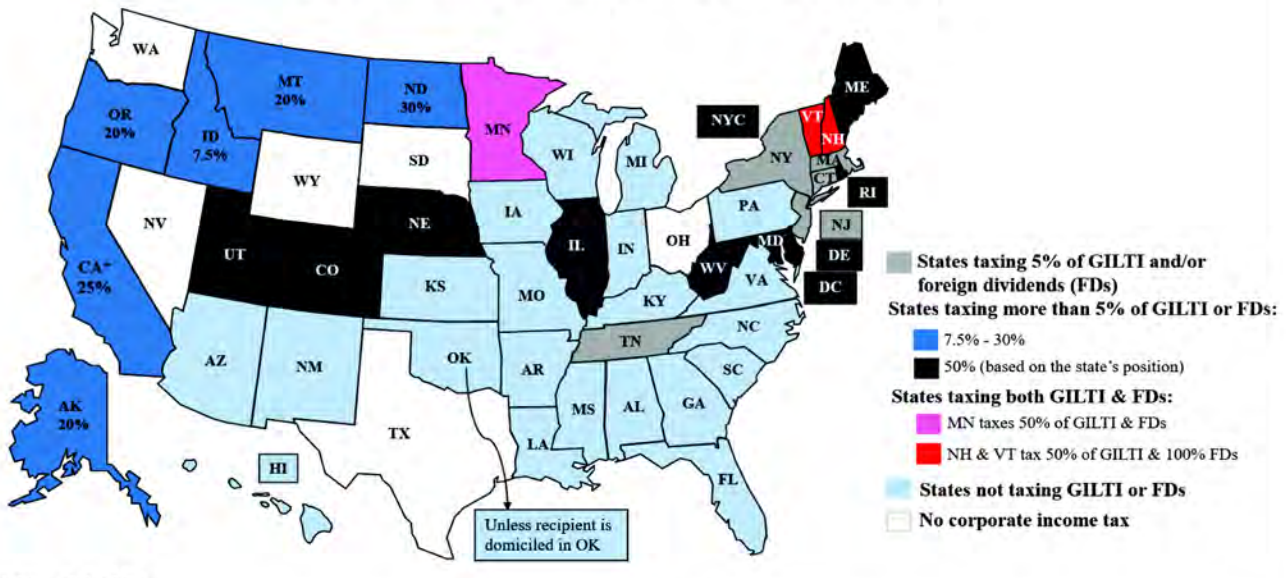
The Recent History of FSI Legislation

Over the last 40 years, state legislative outcomes on FSI were relatively stable, as most states, especially the most populous ones, generally avoided including FSI in the CIT base.[4] A substantial minority of states, however, included some portion of FSI in the CIT base through a combination of categories encompassing foreign dividends, subpart F income, tax haven subsidiary income, and global intangible low-taxed income. During that time frame, the one significant CIT change was that states that previously included a portion of foreign dividends in the CIT base have switched to include a portion of GILTI in the CIT base (see Figure 1).

[3]For examples of stand-alone worldwide combined reporting bills, see Connecticut H.B. 5968 (2025); Hawaii H.B. 116 (2025); Maryland S.B. 766 (2024); Minnesota H.F. 1938 (2023); Nebraska L.B. 40 (2024); New Hampshire H.B. 121 (2024); Oregon S.B. 419 (2025); and COST, "Letter in Opposition to Vermont's Efforts to Impose Mandatory Worldwide Combined Reporting" (Feb. 28, 2024).

[4]States may only include income in the CIT base that has substantial nexus with the state, does not discriminate against interstate commerce, is fairly apportioned, and is fairly related to the services provided by the state to the taxpayer. Further, such inclusion must not create a substantial risk of international multiple taxation, nor prevent the federal government from speaking with one voice when regulating commercial relations with foreign governments. *See Complete Auto Transit Inc. v. Brady*, 430 U.S. 274 (1977); *Japan Line Ltd. v. County of Los Angeles*, 441 U.S. 434 (1979). Inclusion of FSI in the state CIT base is frequently challenged for violating one or more of these prongs, generating significant litigation.

Figure 1.
State Taxation of GILTI and Foreign Dividends



** CA taxes 25% of FDs.*
Disclaimer: This map is based on the best available information, but several states do not have clear guidance on GILTI. Therefore, this information should be used for general guidance and not relied upon for compliance.
Source: Council On State Taxation (June 2025).

Despite the relative stability of long-term outcomes, in recent years a rising tide of state legislative proposals have sought to expand state CIT bases to encompass more FSI. While most proposed legislation includes a portion of GILTI in the state CIT base, for the first time in decades, multiple jurisdictions have introduced mandatory worldwide combined reporting (MWWCR) bills, including Connecticut, the District of Columbia, Hawaii, Maryland, Minnesota (almost enacted), Nebraska, New Hampshire, Oregon, Tennessee, and Vermont.[5] Momentum for state-level inclusion of FSI has grown largely because of the extensive publicity surrounding international profit shifting and the enactment of new federal and global measures to address the problem. The primary national solutions include U.S. federal inclusion of a portion of current (GILTI) rather than deferred (foreign dividends) FSI in the CIT base, and the transformational OECD/G20 pillar 2 GMT.

For proponents of MWWCR or inclusion of GILTI in state CIT bases, the justification is twofold: (1) the composition of state CIT bases without FSI inclusion is flawed because it does not adequately address international profit shifting, and (2) states are losing significant CIT revenue (and multinational businesses are not paying their fair share) unless states remedy this structural defect either by adoption of MWWCR or the inclusion of GILTI.[6]

What is largely missing, however, from proponents' justification and advocacy for current MWWCR/GILTI legislative proposals is consideration of state CIT reform in a broader tax policy context. Too often, proponents focus with tunnel vision on this one element of SALT design, divorced from other interconnecting fiscal and tax considerations. To that end, advocates wear their "white hats" and loudly proclaim that the design of state CIT statutes that don't include all or most FSI in the tax base is indicative of state tax laws that unduly favor businesses.[7]

This article explores why it is so important to view proposals to expand FSI inclusion in state CIT bases not in isolation, but as part of the larger fabric of state and local taxation of businesses. First, we look at the robust growth of state CIT revenue in the five years following the passage of the federal TCJA. This state-level revenue spike has resulted in state CIT revenues reaching their highest level in 20 years, relative to both total state and local taxes on businesses, and to GDP. The rapid state CIT revenue growth is often overlooked because of the large shadow cast by the TCJA's substantial federal CIT cuts.

Second, we review the unprecedented global tax reform tackling international profit shifting at a national and not a subnational (state) level. The OECD/G20's pillar 2 GMT in conjunction with the new U.S. GILTI regime is fundamentally altering the treatment of low-taxed income around the world and doing so in a way that is rendering state taxation of FSI both less necessary and potentially harmful to U.S. multinational enterprises.

Third, we examine the tendency of states that include FSI in the CIT base to deny MNEs matching foreign factor representation in the apportionment formula. For the last 40 years, only a small minority of states that tax FSI — either by CIT base inclusion of a portion of foreign dividends or a portion of GILTI — provide full foreign factor representation. The rest provide either no foreign factor representation or only the fraction of it as measured by the net foreign income base inclusion. This method is unfair and potentially unconstitutional. Moreover, it is another example of how FSI is treated in isolation, as if traditional apportionment rules that match base inclusion with factor representation do not apply.

Fourth, we examine the two largest categories of state and local taxes imposed on businesses — the tax on business property and the sales and use tax on business inputs — that together make up nearly three-fifths of all state and local taxes on

[5] *See* Connecticut H.B. 5968 (2025); D.C. "Tax Administration Modernization and Simplification Act of 2022"; Hawaii H.B. 116 (2025); Maryland S.B. 766 (2024); Minnesota H.F. 1938 (2023); Nebraska L.B. 40 (2024); New Hampshire H.B. 121 (2024); Oregon S.B. 419 (2025); Tennessee H.B. 2043 (2024); and COST letter, *supra* note 3.

[6] *See generally* Michael Mazerov, "States Can Fight Corporate Tax Avoidance by Requiring Worldwide Combined Reporting," *Tax Notes State*, July 22, 2024, p. 227; Bruce J. Fort, "State Taxation of MNEs Under the TCJA: It's Time for a Policy Reassessment," *Tax Notes State*, June 17, 2024, p. 845.

[7] For background on whether businesses are paying a fair share of state and local taxes, see Karl A. Frieden, "Wearing Blinders in the Debate Over Business's 'Fair Share' of State Taxes," *Tax Notes State*, Apr. 8, 2024, p. 91; and Frieden, "The Boomerang Effect of the Business 'Fair Share' Tax Debate," *Tax Notes State*, Feb. 10, 2025, p. 405.

businesses. We show how the designs of these taxes significantly disfavor businesses, resulting in several hundred billion dollars more in taxes than businesses would pay under more optimal or neutral designs. And yet the business-unfriendly designs of the largest state and local business taxes are generally ignored during legislative deliberations over the smaller-dollar-value state CIT redesign, skewing the debate away from an informed and balanced approach.

State Taxation of FSI Should Consider Other State CIT Developments

State CITs typically fluctuate from year to year, but over the last five years state CIT revenues have increased faster — both in absolute terms and relative to other state and local business taxes — than at any time during the last 20 years (see Figure 2).[8] State and local CIT collections increased from $65.9 billion in fiscal 2018 to $130.5 billion in fiscal 2023 or by about 63 percent after inflation. This significant CIT increase caused the CIT share of all taxes paid by business to increase from 8.5 percent in fiscal 2018 to 12 percent in fiscal 2023.[9] Over the same five years, state CIT revenues also outpaced GDP growth by more than 50 percent.[10]

This recent, rapid state CIT revenue growth, however, has received scant attention because of its juxtaposition with the well-publicized relative decline of federal CIT revenue following TCJA enactment in 2017 (effective for 2018). One of the centerpieces of the TCJA was the reduction of the federal CIT rate from 35 percent to 21 percent — a 40 percent drop. To partially offset the loss of federal CIT revenue, the corporate tax rate cut was combined with a number of base broadeners (and some base narrowers). The net impact was to reduce baseline federal CIT revenue by about 10 percent over 10 years.[11]

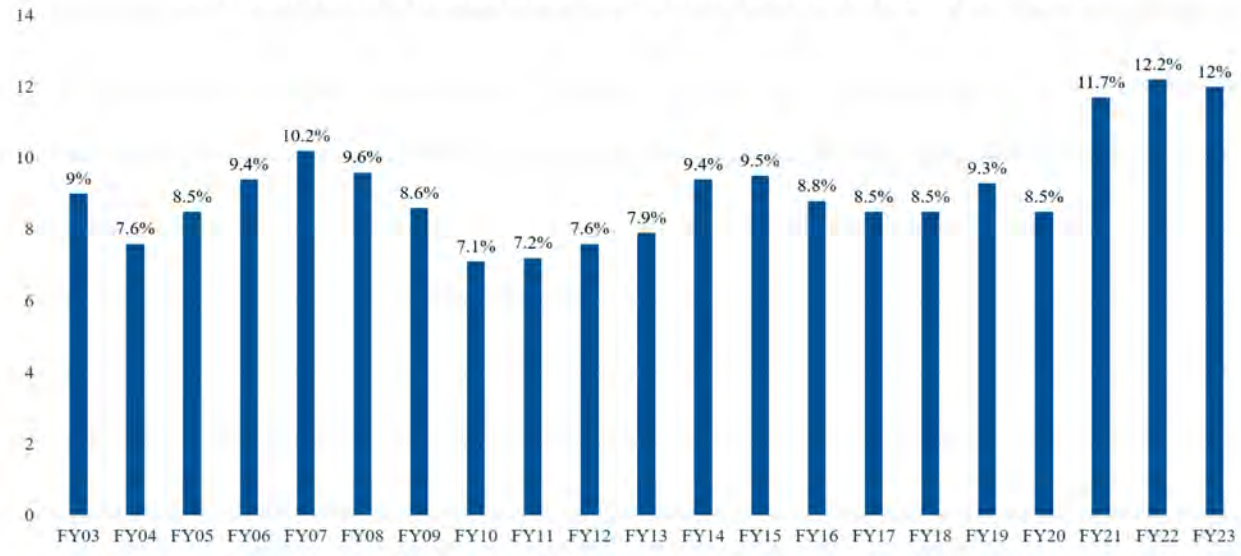
[8] For the 20-year trend, see Figure 2, derived from annual studies: EY, State Tax Research Institute (STRI), and COST, "Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2002-2023."

[9] EY, STRI, and COST, "Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2023" (Dec. 2024). EY, STRI, and COST, "Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2018" (Oct. 2019).

[10] *See* EY, STRI, and COST, "Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2023," at 21 (Figure 8).

[11] *See* Joint Committee on Taxation, "Estimated Budget Effects of the Conference Agreement for H.R. 1, The Tax Cuts and Jobs Act," JCX-67-17 (Dec. 18, 2017).

Figure 2.
Share of CIT in Total State and Local Business Taxes, FY02-FY23



Source: "Total State and Local Business Taxes: State-by-State Estimates," COST/STRI/EY (updated annually).

What was less recognized at the time was that the TCJA had the opposite impact on state CIT revenue. State conformity with TCJA provisions varied significantly; however, no state conformed with the large TCJA federal CIT cut, since states maintain their own CIT rates. Only a small number of states conformed to federal CIT base narrowers (and revenue losers), including accelerated depreciation and the expensing of capital investment. Conversely, most states conformed with some of the largest federal CIT base broadeners (and revenue raisers), including interest deduction limitations (IRC section 163(j)) and the amortization of research and experimentation expenditures.[12]

While state CIT conformity with the federal TCJA provisions was a substantial contributing factor, it was not the most significant one animating the five-year surge of state CIT revenue. Other factors also substantially accelerated state CIT revenue collections, including strong economic growth and corporate profits. For most states, however, conformity with TCJA base broadeners jump-started the surge in CIT revenue with estimated state CIT baseline revenue growth of 12 percent or more.[13]

Moreover, the TCJA-related revenue growth was largely fortuitous. Most states, when given the opportunity, could not turn down the substantial revenue increases derived simply by conforming to federal CIT base broadeners. While few of these states entered 2018 with the legislative resolve to raise state CIT revenue, they could simply do so by conforming to the IRC as they had in the past without designing any new statutory provisions.

The recent upward trajectory of state CIT revenue, however, is almost entirely absent from the analysis of proponents favoring more FSI inclusion in state CIT tax bases. In a June 2024 *Tax Notes State* article, Bruce Fort, senior counsel with the Multistate Tax Commission, encouraged states to reassess state taxation of FSI and to include GILTI in the state CIT base. Fort suggested that federal GILTI revenues were "too big to ignore."[14] The overall impression left by Fort's analysis was that U.S. corporations, especially U.S. MNEs, received more favorable state CIT treatment after the enactment of the TCJA.[15]

However, while advocating for expansion of state CIT bases because of "missing" revenue, Fort almost completely ignores the largely inadvertent "windfall" of state CIT revenue growth attributable to state conformity with TCJA base broadeners. According to the Joint Committee on Taxation, revenue growth (over 10 years) from just two of the largest TCJA base broadeners that most states conformed to (the net interest expense limitations and the amortization of research and experimentation costs) raised about three times as much revenue as federal adoption of the GILTI provision (net of the section 250 deduction).[16]

Similarly, Michael Mazerov, a consultant with the progressive Center on Budget and Policy Priorities, ignored the surge in state CIT revenue in a July 2024 *Tax Notes State* article on MWWCR. Mazerov claimed that states could gain an additional $10 billion to $15 billion in CIT revenue annually if they all adopted MWWCR.[17] In the course of his passionate advocacy for MWWCR, he never once considered whether the timing is appropriate for raising state CIT revenue following so closely the unprecedented — and at least for the TCJA-related portion — unintended surge of state CIT revenue over the last five years.[18]

State CIT revenues fluctuate year-to-year and state-to-state based on both political and economic factors. At a minimum, however, when total state CIT revenues reach their highest levels in the last 20 years both in relation to GDP and

[12] *See generally* Andrew Phillips and Steven Wlodychak, "The Impact of Federal Tax Reform on State Corporate Income Taxes," prepared for STRI by EY, at ii (Mar. 2018); Frieden and Stephanie T. Do, "State Tax Conformity to Key Taxpayer-Favorable Provisions in the CARES Act," *Tax Notes State*, Apr. 20, 2020, p. 303.

[13] Phillips and Wlodychak, *supra* note 12. The EY study estimate was based on historic patterns of state CIT conformity to federal tax base provisions. *Id.*

[14] Fort, *supra* note 6, at 857.

[15] Fort cautioned that "it is time for the states to reassess whether their tax structures should be modernized to ensure parity in tax burdens among those engaged in domestic and foreign commerce." *Id.* at 845.

[16] *See* JCT, *supra* note 11; and Phillips and Wlodychak, *supra* note 12, at 4-5.

[17] Mazerov, *supra* note 6, at 236.

[18] *Id.*

relative to other state and local business taxes, debates over new proposals to increase state CIT revenue (through adoption of GILTI or MWWCR) should proceed with caution and heightened scrutiny. This is especially true in a state that experienced a large CIT revenue increase from TCJA conformity intended (at the federal level) to produce the opposite result.[19]

State CIT Base Inclusion of FSI Should Not Be Considered in Isolation From Global and National FSI Solutions

Legislative proposals to redesign the state CIT base to include more FSI should not proceed in isolation from global and national solutions addressing the same issue. The primary justification of advocates for state MWWCR adoption or GILTI inclusion is that some MNEs are engaged in global profit shifting facilitated by moving assets to low-tax nations. In evaluating how to address international profit shifting, however, proponents focus almost exclusively on state-level remedies and largely ignore the more impactful national and global solutions transforming the international tax landscape.

To understand the importance of the global approach it is helpful to review the 11-year history of the OECD base erosion and profit-shifting project. The BEPS project began in 2013 with a primary focus on two challenges to national income tax systems: global profit shifting and the digital economy. In 2015 the OECD issued a 2,000-page report that focused on 15 different "action plans" to address these problems. Some of the proposed solutions were implemented by countries in subsequent years.[20]

After passage of the TCJA, however, the OECD project turned in a different direction, adopting a new approach to low-taxed FSI centered on the implementation of a GMT. The "pillar 2" approach, as it became known, includes a 15 percent minimum tax on the income of large MNEs in every country in which they operate. The GMT, implemented through global anti-base erosion (GLOBE) rules, imposes a rate of at least 15 percent on a multinational group's constituent entities — parents, subsidiaries, branches, or permanent establishments — in every country with a rate below 15 percent by "topping up" the country rate so that the entities' effective tax rate is at least 15 percent.[21]

The right to impose a top-up tax is first granted to the source country — typically either a low-tax-rate country or a higher-tax-rate country with significant tax credits and incentives that bring the ETR below 15 percent (known as the qualified domestic minimum top-up tax). If the source country does not impose the tax, the home country of the parent company can collect the tax by increasing the taxable income of the parent subject to tax (known as the income inclusion rule). Finally, the GMT imposes an undertaxed profit rule that specifies that if neither the source country nor the parent country chooses to impose the top-up tax, the countries in which the MNE's affiliates operate can choose to share the top-up tax that could have been levied in the source country.[22]

GLOBE rules apply only to large MNEs — those corporate groups with revenue exceeding €750 million (approximately $850 million) in two

[19] Fort and Mazerov both make an ancillary argument in support of state taxation of FSI — that the current CIT design favors larger multinational businesses over smaller domestic businesses. Fort, *supra* note 6, at 845; Mazerov, *supra* note 6, at 227. For a critique of their positions, see Frieden, "The Boomerang Effect of the Business 'Fair Share' Tax Debate," *supra* note 7, at 411-413. Available studies suggest that larger businesses are generally not favored by the SALT system compared with smaller or domestic-only businesses. It is common knowledge in the tax community and among tax scholars that most small, medium-size, and even many large businesses do not pay CITs at all but are taxed under more favorable personal income tax passthrough entity (PTE) laws. A PwC study in 2017 found that PTEs comprise about 95 percent of all business entities and generally earn about three-fifths of all business revenue. The study was the first ever to quantify the differences in state effective tax rates on business income earned by C corporations compared with PTEs. The study (based on 2013 data) concluded that the aggregate state-level effective business income tax rate for C corporations (6.1 percent) was 30 percent higher than the aggregate rate for passthrough businesses (4.7 percent). *See* PwC, "Corporate and Pass-Through Business State Income Tax Burdens: Comparing State-Level Income and Effective Tax Rates," prepared for the STRI (Oct. 2017). The rate differential was attributable both to generally lower personal income tax rates for PTEs (than CIT rates for C corporations) and the single level of tax on PTEs. *Id.* A similar federal-level study in 2024 (based on 2021 data) by William G. Gale and Kyle Pomerleau found that the average federal ETR of C corporations exceeds the rate of passthrough businesses by more than 20 percent. The federal-level study found PTEs have had a sizable ETR advantage over C corporations continuously for the last four decades. *See* Gale and Pomerleau, "Efficient and Equitable Income Taxation of the Affluent," *Tax Notes Federal*, Nov. 19, 2024, p. 1409.

[20] OECD, "BEPS Project Explanatory Statement" (2015).

[21] *See* Felix Hugger et al., "The Global Minimum Tax and the Taxation of MNE Profit," OECD Taxation Working Papers (Jan. 2024).

[22] Congressional Research Service, "The Pillar 2 Global Minimum Tax: Implications for U.S. Tax Policy" (Sept. 2023).

of the previous four years. Pillar 2 does not directly impose a minimum tax rate upon countries that impose a low rate. Under pillar 2, jurisdictions are still free to determine their own tax systems, including whether they have a CIT and the level of their tax rates. However, the operation of the IIR and UTPR allow the home country or the location of affiliates to collect a minimum tax if the source country chooses not to. This, of course, creates an incentive for the source country to impose a tax rate at least as high as the minimum tax under the GLOBE rules.[23]

The pillar 2 provisions thus fundamentally foster tax parity among countries by creating a global framework under which countries can impose additional tax on the low-taxed foreign income of MNEs. In 2021 the pillar 2 GMT approach was approved in principle by 140 nations, including virtually all leading economies in the world.[24] Pillar 2 adoption is not through a multilateral agreement but by individual country adoption. In 2024, the first year of planned GMT implementation, adoption of the provisions of pillar 2 was widespread. To date, about 60 countries have adopted some of the key provisions of pillar 2 or declared their intentions to do so (see Figure 3).[25] Pillar 2 adoption has occurred in both larger high-tax nations such as the members of the European Union; and also in smaller low-tax countries, many of which have operated for years as tax havens, including the Bahamas, Bahrain, Barbados, Bulgaria, Curaçao, Cyprus, Gibraltar, Guernsey, Hong Kong, Ireland, Isle of Man, Jersey, Liechtenstein, Luxembourg, the Netherlands, Singapore, and Switzerland (see Figure 3).[26]

[23] *See* Hugger et al., *supra* note 21. *See also* OECD, "Cover Statement by the Inclusive Framework on the Reports on the Blueprints of Pillar One and Pillar Two," OECD/G20 Inclusive Framework on BEPS (Oct. 2020).

[24] CRS, *supra* note 22.

[25] PwC's Pillar 2 Country Tracker.

[26] *Id.* OECD researchers have estimated that about half of global profit shifting is attributable to high-tax-rate countries offering credits and incentives that bring the ETR below 15 percent. *See* Hugger, Ana Gonzalez Cabral, and Pierce O'Reilly, "Effective Tax Rates of MNEs: New Evidence on Global Low-Taxed Profit," OECD Taxation Working Paper No. 67 (Nov. 21, 2023).

Figure 3.
The Nations That Have Adopted or Announced Adoption of Some or All the Provisions of the OECD's Pillar 2 Global Minimum Tax

Low-Tax Nations
Bahamas
Bahrain
Barbados
Bulgaria
Curaçao
Cyprus
Gibraltar
Guernsey
Hong Kong
Ireland
Isle of Man
Jersey
Liechtenstein
Luxembourg
The Netherlands
Singapore
Switzerland

Other Nations		
Australia	Indonesia	Romania
Austria	Israel	Slovakia
Belgium	Italy	Slovenia
Brazil	Japan	South Africa
Canada	Kenya	South Korea
Croatia	Kuwait	Spain
Czech Republic	Malaysia	Sweden
Denmark	New Zealand	Thailand
Finland	North Macedonia	Türkiye
France	Norway	United Arab Emirates
Germany	Oman	United Kingdom
Greece	Poland	Vietnam
Hungary	Portugal	Zimbabwe
Iceland	Qatar	

Source: PwC's Pillar Two Country Tracker

The significance of international receptivity to the GMT cannot be overstated. Twelve years after the BEPS project started, the promise of transformative international tax reform has transitioned from hypothetical to real. The adoption of the GMT by many OECD/G20 inclusive framework nations is likely to significantly reduce the incidence and revenue impact of global profit shifting. According to an internal OECD study released in January 2024, because the GMT significantly lessens the incentives to shift profits, it will reduce global profit shifting by nearly 50 percent.[27] More importantly, the percentage of profits in low-tax jurisdictions (those with tax rates below 15 percent) is expected to fall by two-thirds, with a concomitant increase in global CIT revenue of nearly $200 billion.[28] Given the minimum dollar threshold levels for the application of the GLOBE rules, the additional revenue-raising will solely affect large MNEs.

Nor has the U.S. federal government been left behind in the wave of international tax reform that seeks to curtail or eliminate low-taxed global income. To date, the United States has not adopted the pillar 2 GMT, and the Trump administration has announced it has no intention of doing so.[29] Nonetheless, the U.S. government's adoption of GILTI — a form of a GMT — has accelerated international tax reform from a series of BEPS 1.0 solutions with mixed adoption records to a global juggernaut that represents the most massive tax reform over the last century. For most U.S. MNEs, GILTI has an ETR of 13.125 percent (when factoring in the 10.5 percent rate and 80 percent foreign tax credit). But in 2026 the ETR is scheduled to increase to 16.406 percent (when the section 250 deduction is reduced from 50 percent to 37.5 percent).[30]

Given the enormity of the unprecedented global tax reform and the GMT's rapid adoption, do the potential sharp reductions in low-taxed FSI alter the perspective of the proponents of MWWCR or state GILTI inclusion? Not very much. For instance, Mazerov, in his July 2024 *Tax Notes State* article advocating for all states to adopt MWWCR, never once mentions the OECD's pillar 2 GMT and its potentially game-changing reduction of global profit shifting.[31] This omission is particularly surprising since the key rationale behind his passionate advocacy for MWWCR is to reduce international profit shifting.[32]

Moreover, Mazerov wrote his latest MWWCR article in the middle of the very year (2024) that GMT adoption was occurring in dozens of countries around the world (and before the outcome of the U.S. presidential election was known). The pillar 2 GMT is not some futuristic solution that is a pipe dream or on some government wish list. Rather, the GMT is effectively structured to be virtually self-propelling without a broad multilateral agreement.

In his article, Mazerov quotes studies of profit shifting, tax havens, and MNEs' behavior and acts as if these fact patterns are frozen in time, unaffected by changes occurring in the national and global tax arenas.[33] He compares MWWCR favorably to other state-level remedies but completely ignores the much greater potential impact of national- and global-level solutions. It seems implausible to have a current discussion on international profit shifting without factoring in the transformative effort of nations around the

[27] *See* Hugger et al., *supra* note 21.

[28] *Id.* at 52. The incidence and revenue impact of pillar 2 could change if the GMT provisions are altered based on continuing dialogue between adopting and non-adopting nations.

[29] The White House, "The Organization for Economic Co-operation and Development (OECD) Global Tax Deal (Global Tax Deal)" (Jan. 20, 2025).

[30] Frieden and Barbara M. Angus, "Convergence and Divergence of Global and U.S. Tax Policies," *Tax Notes State*, Aug. 30, 2021, p. 955. Under the TCJA, there is a scheduled reduction of the section 250 deduction from 50 percent to 37.5 percent in 2026. This reduction may not occur, however, if 2025 tax legislation under consideration by Congress delays or modifies the change in the section 250 deduction. *See* H.R. 1, One Big Beautiful Bill Act.

[31] Mazerov, *supra* note 6.

[32] *Id.* Mazerov states: "While several alternative approaches to addressing international profit shifting have been adopted or proposed, worldwide combined reporting is a more comprehensive solution, and its legality (unlike some of the alternatives) has been fully established." *Id.* at 228. For a comprehensive critique of MWWCR, see Douglas L. Lindholm and Marilyn A. Wethekam, "Mandatory Worldwide Combined Reporting: Elegant in Theory but Harmful in Implementation," COST/STRI (Mar. 2024).

[33] Lindholm and Wethekam, *supra* note 32.

world to address the problem. With the OECD's study concluding that the GMT will be quite effective in reducing low-taxed FSI, this omission highlights the complete divorce of the proponents of MWWCR and state taxation of GILTI from the broader realities of national and global taxation.[34]

Potential Competitive Disadvantage for U.S. MNEs

The omission in Mazerov's article of any reference to pillar 2's GMT and the anticipated reduction in global profit shifting is perplexing, but it may be intentional. While the proponents of MWWCR rest their advocacy on the need to combat international profit shifting by U.S. MNEs, nothing in the MWWCR formulation addresses profit shifting or low-tax foreign jurisdictions. In fact, the opposite is true, as the MWWCR and state GILTI methods generally apply the same way, whether low-taxed foreign income is reduced by 25 percent, 50 percent, or 75 percent.

The key differentiator between the MWWCR/state GILTI provisions and pillar 2 GMT/federal GILTI provisions is that the former do not provide a credit for taxes paid to other jurisdictions. The global GMT and federal GILTI provisions both operate in effect as top-up taxes, imposing an additional tax only if the current tax burden on MNEs does not reach a prescribed minimum tax. For the GMT the minimum tax is 15 percent; for the federal GILTI provisions the minimum tax is generally 13.125 percent (potentially increased to 16.406 percent in 2026).

By contrast, the MWWCR/state GILTI methods provide no credit for taxes paid to other foreign jurisdictions. For instance, if a low-tax nation increases the tax on a U.S. MNE from 5 percent to 15 percent, this will generally eliminate any GMT (because the "source" country will now impose a 15 percent tax rate) and any federal GILTI (because the higher FTC will offset the federal tax on FSI). The MWWCR/state GILTI tax calculations, however, may not change at all as they are based on formulary apportionment and do not provide an FTC. Accordingly, if there is an increase in the amount of foreign tax imposed on a U.S. MNE but no change in the sales or other foreign apportionment factors that contribute to the generation of the FSI, there is no reduction in the state income tax paid based on the MWWCR/state GILTI formulas.[35]

This may help explain why Mazerov is not alone in his omission of any reference to the game-changing impact of the GMT in reducing international profit shifting. The same applies to the updated 2025 Institute on Taxation and Economic Policy analysis of state revenue increases from MWWCR.[36] The initial 2019 ITEP study[37] is used by virtually all key MWWCR proponents as the basis for their estimates of state tax revenue increases from MWWCR. Yet the new and revised ITEP study released in February 2025, which concludes that MWWCR will produce somewhat higher state CIT increases than its earlier study, similarly makes no reference to the GMT or its potential impact in significantly reducing international profit shifting.[38]

Neither Mazerov's 2024 article nor the 2025 ITEP study explains why they fail to analyze the impact of transformative global reforms aimed at reducing low-taxed foreign income. Nonetheless, a plausible answer is that the unilateral enactment of MWWCR/state GILTI in individual states does not have a material impact on global profit shifting, nor is it intended to. Rather, it is a way for states to increase CIT revenue even if low-taxed FSI is significantly reduced on a global basis.

Over the last decade, a global consensus has developed that international profit shifting by MNEs is a serious problem assignable to structural deficiencies in national CITs. This consensus is the driving force behind the widespread adoption of pillar 2's GMT. However, the global accord applies to harmonized central government solutions, not

[34]Similarly, Fort authored his 2024 article advocating for states to expand the CIT base to include GILTI without any mention or analysis of the pillar 2 solutions. In doing so, Fort surveyed only state remedies to address international profit shifting and not national and international solutions. Fort, *supra* note 6.

[35]Joseph X. Donovan et al., "State Taxation of GILTI: Policy and Constitutional Ramifications," *State Tax Notes*, Oct. 22, 2018, p. 315, at 330-334. The problem is generally worse under state GILTI provisions (compared with MWWCR) because most states that tax a portion of GILTI do not provide full foreign factor representation. *See* Figure 4.

[36]Carl Davis, Matt Gardner, and Mazerov, "A Revenue Analysis of Worldwide Combined Reporting in the States," ITEP (Feb. 2025).

[37]Richard Phillips and Nathan Proctor, "A Simple Fix for a $17 Billion Loophole: How States Can Reclaim Revenue Lost to Tax Havens," ITEP (2019).

[38]Davis, Gardner, and Mazerov, *supra* note 36.

to unilateral subnational (state) solutions. In previous years no large industrialized nations (other than the United States) have attempted to tax FSI at the state or provincial level.[39] The GMT similarly reflects this pattern, with adoption occurring (outside the United States) only at the national level.[40]

The GMT is structured as a minimum tax floor, not a ceiling. Nonetheless, MNEs headquartered in the United States compete for customers and resources on a global basis. The disharmony of our 50-state subnational tax system already imposes significant compliance and resource burdens on businesses greater than those imposed in countries without subnational taxation of corporate income. The GMT and federal GILTI provisions strike a balance between a higher minimum tax on FSI and relative parity among nations in the rate of the tax. The additional imposition of a subnational CIT on FSI can destabilize this balance.

U.S. national/subnational divergence from the GMT model of a 15 percent top-up tax could create a competitive disadvantage for U.S. MNEs. Foreign MNEs are potentially subject to the 15 percent GMT on their FSI but not to any subnational income tax in their own country.[41] U.S. MNEs are potentially subject to the 15 percent GMT and/or the federal GILTI provisions in addition to any state subnational income tax imposed on FSI.[42] Thus, each state that includes FSI in the CIT base either through an additional GILTI inclusion or by adopting MWWCR may exacerbate the rate differential between U.S. and foreign MNEs. Indeed, the more successful the GMT and federal GILTI are at imposing a minimum tax on MNEs' FSI and reducing profit shifting, the more the threat that MWWCR or state GILTI will result in double taxation of U.S. MNEs.

Granted, the federal and global measures to counteract international profit shifting are still in development and will undoubtedly require significant fine-tuning over time. The GMT establishes a tax floor but by itself doesn't eliminate all profit shifting. The future of the UTPR component of the GMT is still uncertain, given the level of opposition to that part of the plan. Substantive differences between the U.S. GILTI provision and the pillar 2 GMT are problematic to achieving a harmonized global solution. The changes in MNE behavior caused by the new global tax regime are still evolving.[43]

Furthermore, the Trump administration's tax and tariff policies and their impact on FSI remain unclear. On the one hand, the Trump administration has announced it is no longer a participant in pillar 2 and has threatened retaliation if other countries treat U.S. MNEs unfairly. The U.S. House of Representatives recently included in its version of the 2025 budget and tax legislation a retaliatory tax that could be used against other countries. On the other hand, a central part of Trump's "America First" platform is bringing jobs and investment back to the United States, which would also reduce global profit shifting by U.S. MNEs. Finally, a future Democratic administration might reverse course again and follow the lead of the Biden administration in providing support for the pillar 2 GMT.[44]

[39]PwC, "Survey of Subnational Corporate Income Taxes in Major World Economies: Treatment of Foreign Source Income," prepared for STRI (Nov. 2019). Subnational taxation of corporate income is common in the United States but is not the norm in the other 48 industrialized nations in the OECD, which represent (together with the United States) nearly 90 percent of global GDP. And it is rarer still to identify a country with subnational taxation of corporate income that includes FSI in the subnational tax base. Indeed, of these 48 countries, only eight impose a subnational CIT, and only one of those eight (South Korea) subjects active FSI to subnational taxation (at a low 2.5 percent rate) in one large metropolitan area. In the other seven countries, FSI is either not subject to tax or is 95 percent exempt from taxation at the subnational level. *Id.*

[40]PwC's Pillar 2 Country Tracker, *supra* note 25.

[41]A foreign-headquartered MNE could be subject to MWWCR but not to GILTI, which applies only to U.S. MNEs. However, the foreign-headquartered MNE would be subject to WWCR only on the apportioned share of its U.S. income, not on its FSI earned in other countries.

[42]As noted below, the imposition of the pillar 2 provisions on U.S. MNEs is still in flux given current Trump administration opposition to discriminatory extraterritorial taxes. But even if U.S. MNEs are exempted from the UTPR provision, they could still be subject to the 15 percent qualified domestic minimum top-up tax in the source country.

[43]One possible outcome of the change in global tax rules is that U.S. MNEs will move some foreign operations back to the United States. If this occurs, however, the development also lessens the need for states to tax more FSI, since the state CIT base will expand under current state CIT rules.

[44]The White House, *supra* note 29. A new provision in the House of Representatives 2025 tax legislation would allow retaliation against foreign countries that impose discriminatory taxes on U.S. MNEs. See the new IRC section 899 retaliatory tax plan in H.R. 1, One Big Beautiful Bill Act. Conversely, the other OECD inclusive framework participants have indicated they plan to proceed with the pillar 2 GMT. Keven Pinner, "Work to Continue on OECD Tax Plan Despite U.S. Pullback," *Law360*, Apr. 11, 2025; Sophie Petitjean, "EU Shows Openness but Steadfastness on Pillar 2," *Tax Notes Int'l*, May 14, 2025, p. 1015.

At a minimum, however, before enacting any major change to a state's CIT base (including a switch to MWWCR or a large percentage inclusion of GILTI), a state should take notice that international profit shifting and creation of a level playing field between U.S. and foreign MNEs is already being addressed at the global and national levels. A unilateral state-level solution is unlikely to alter profit shifting and could hinder progress toward a rational global solution, especially given the likely volatility of global tax and trade policy over the next few years. Finally, there is a distinct possibility that any state-level solution could create a competitive disadvantage for U.S. MNEs at a time of significant economic uncertainty.

State Taxation of FSI Should Match CIT Base Inclusion With Foreign Factor Representation

Another significant contextual issue frequently disregarded in the debate over state CIT inclusion of FSI is the requirement to match any CIT base expansion with commensurate foreign factor representation. The litmus test of a well-designed apportionment method is that if a state incorporates new sources of income into the tax base, it should also include the factors that contribute to generating that income in the apportionment formula. As stated in the treatise *State Taxation*, "the factors that are employed to apportion income among the states should reflect the factors that produce the income being apportioned. This virtually axiomatic proposition is also a principle of constitutional law."[45] This principle was enunciated by the Supreme Court in *Container Corp.*: "The factor or factors used in the apportionment formula must actually reflect a reasonable sense of how income is generated."[46]

The key to this principle is the use of factors of production — initially property, payroll, and sales, but in recent years, increasingly just sales — to apportion income. In terms of the sales factor, this entails including the gross receipts that contribute to income production in the apportionment ratio.

Unfortunately, states have a long history of doing exactly the opposite — adding FSI into the CIT tax base without matching the base expansion with the foreign apportionment factors that helped generate the income. This history dates back to the pre-TCJA years when a significant minority of states taxed a portion of foreign dividends.[47]

Currently, most of the states that tax a portion of GILTI or foreign dividends include only in the sales factor denominator the net GILTI or net foreign dividends amount, and not the total foreign gross receipts contributing to the generation of that income. A small number of states (New Hampshire, Utah, and Vermont) include in the denominator of the sales factor the total foreign gross receipts relating to the FSI (see Figure 4).[48]

The omission of foreign factor representation from state apportionment formulas has recently become more overt and punitive. In three widely publicized FSI legislative proposals — one seriously considered in California and two enacted in Minnesota and Illinois — the statutory language entirely precludes foreign factor representation. In the past, states that provided zero foreign factor representation typically included only a small percentage of FSI in the tax base. For example, Connecticut, Massachusetts, and Tennessee provide no foreign factor representation but include only 5 percent of GILTI and/or foreign dividends in the state CIT base (see Figure 4).[49] However, neither California's proposed legislation nor the enacted legislation in Minnesota and Illinois provides foreign factor representation even though they include about half of MNEs' FSI in the tax base.[50]

[45] Jerome Hellerstein, Walter Hellerstein, and Andrew Appleby, *State Taxation*, ch. 9C, para. 9.15(1) (2022).

[46] *Container Corp.*, 463 U.S. at 169.

[47] Philips and Wlodychak, *supra* note 12, at 13 (Figure 7).

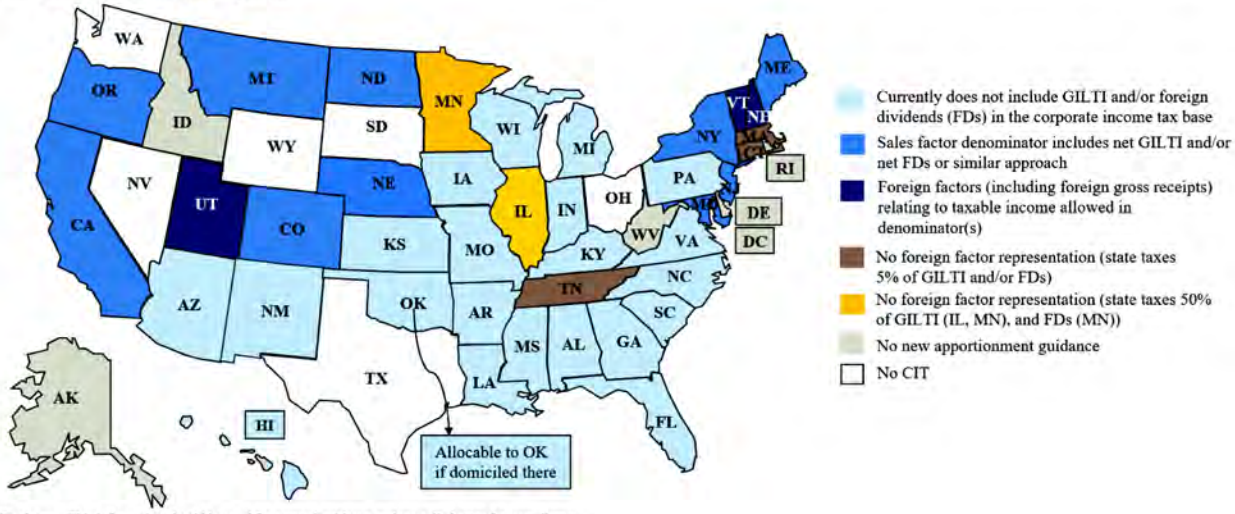
[48] Internal research by COST. *See* Frieden and Fredrick J. Nicely, "Minnesota's New Approach to Taxing Foreign Income Is Unfair and Unwise," *Tax Notes State*, Aug. 21, 2023, p. 583.

[49] *Id.*

[50] On proposed California A.B. 71, see Frieden and Erica S. Kenney, "Eureka Not! California CIT Reform Is Ill-Conceived, Punitive, and Mistimed," *Tax Notes State*, May 24, 2021, p. 795. On Minnesota's enacted legislation (H.F. 1938), see Frieden and Nicely, *supra* note 48. Before the enactment of H.F. 1938, Minnesota provided no foreign factor representation but taxed only 20 percent of foreign dividends and subpart F income. *Id.*

Figure 4.
GILTI and Foreign Dividends State Factor Representation

Based generally on 80% or more direct corporate ownership of foreign corporations. Other rules may apply for smaller percentage ownership or personal income tax purposes.



Disclaimer: This information should be used for general guidance and not relied upon for compliance.
Source: COST (June 2025).

The California legislation, A.B. 71, was introduced in the California State Assembly in December 2020. A.B. 71 would have drastically expanded the California inclusion of FSI in the water's-edge combined filer's tax base. First, on a one-time basis, the proposed legislation would require a taxpayer making a water's-edge election to retroactively include 40 percent of its undistributed foreign dividend income from 1986 to 2017 in the tax base (compared with the 25 percent historically included in the California CIT base). At the same time, the legislation prohibited the taxpayer from including in its apportionment formula denominator any of the foreign sales that contributed to the generation of the repatriated income over the 40-year period. Second, on a current basis, A.B. 71 required a taxpayer that makes a water's-edge election to include in the CIT tax base 50 percent of GILTI. Once again, the proposed bill prohibited the taxpayer from including in its apportionment formula any of the foreign sales that contributed to the generation of GILTI earnings.[51] The bill passed several assembly committees before it was rejected by the full assembly because the super majority required for tax increases in California could not be obtained.[52]

In 2023 Minnesota adopted a new statutory approach to taxing FSI that vastly expands the amount of that income in the CIT base. Before the legislation, Minnesota included 20 percent of foreign dividends and subpart F income in its CIT base.[53] Under the new legislation, Minnesota includes (for the first time) 50 percent of GILTI in the CIT base and increases the inclusion of foreign dividends and subpart F income to 50 percent. The significant expansion of FSI in the CIT base was done without providing any factor representation in the apportionment formula for the foreign sales that produced the foreign-source income. Minnesota, the first state to include 50 percent of FSI in the state CIT base with zero factor representation,[54] has now been joined by Illinois.

[51] Frieden and Kenney, *supra* note 50.

[52] *Id.*

[53] Subpart F income is a category of foreign-source income historically taxed on a current, not deferred, basis under IRC sections 951 and 952. For controlled foreign corporations, subpart F income is generally a small portion of foreign-source income and typically includes "movable"- or "passive investment"-type income. *See* IRS, "Subpart F Overview" (Sept. 3, 2014).

[54] Frieden and Kenney, *supra* note 50.

On May 31, 2025, the Illinois Assembly, in its recently enacted tax omnibus bill (H.B. 2755) included 50 percent of GILTI in the Illinois CIT base. Similar to Minnesota, and different than any other state that includes a substantial portion of FSI in the CIT tax base, Illinois fails to provide any factor representation in the apportionment formula for the foreign sales that produced the foreign-source income.[55]

This new approach to taxing foreign-source income makes Minnesota and Illinois not only anomalies among states, but also outliers compared with the federal income tax scheme under the TCJA. As noted above, the federal government allows taxpayers a credit for 80 percent of foreign taxes paid on GILTI. For federal purposes, the FTC is crucial to avoiding double taxation of FSI. According to a study using IRS Statistics of Income division data, in 2018 — the first year GILTI was in the federal income tax base — the use of the FTC reduced the federal tax on GILTI by approximately 57 percent.[56] Similarly, pillar 2's GMT is a 15 percent top-up tax, which effectively allows a 100 percent FTC by reducing the income subject to tax based on the percent of tax applied in the foreign jurisdiction.[57]

Despite the sharp deviation from the normative apportionment of domestic income, the advocates of FSI base inclusion stoutly defend the zero factor representation as rational tax policy. Their theory is grounded in the notion that up to 50 percent of FSI is not foreign income at all but "displaced domestic income" and therefore requires no additional factor representation.[58]

Whatever one thinks of the debate over international profit shifting and how to address it, this view of FSI is without factual basis and is increasingly obsolete. The purpose of matching base inclusion with factor representation is to allow the apportionment formula to provide a proxy for allocating income to a jurisdiction.[59] The notion that you can somehow arbitrarily determine how much income is domestic and how much is foreign is akin to a "separate accounting" method that the proponents of FSI inclusion typically disparage.[60] The state FSI advocates refuse to acknowledge the obvious — that the allowance of zero or limited foreign factor representation is related to maximizing state CIT revenue, not to providing a fair or constitutionally valid apportionment of in-state income. Indeed, the recent ITEP study on the state revenue impact of MWWCR illustrates this point with its conclusion that Minnesota raises 80 percent more revenue by taxing 50 percent of GILTI with no foreign factor representation than it would with a MWWCR statute that includes 100 percent of FSI in the CIT base with full foreign factor representation.[61]

Moreover, in the context of the widespread adoption of the GMT, this "no foreign factor representation" approach is hopelessly outdated. It operates as if the taxation of FSI is static and no other tax base or rate changes occur elsewhere. By contrast, the pillar 2 GMT and federal GILTI approaches both make allowances for increases in foreign taxes paid on FSI by providing an offset against the GMT rate or a credit against the tax on GILTI.

To be sure, states generally do not use credits for CITs paid to other jurisdictions. But that is the purpose of apportionment formulas — to operate as a proxy for tax credit calculations. When FSI proponents impose their subjective judgment (without factual basis) on what constitutes domestic or foreign income without the aid of traditional apportionment formulas, the outcome is patently unfair, likely unconstitutional, and

[55] Illinois H.B. 2755. The Illinois General Assembly in late May 2025 passed H.B. 2755, which includes 50 percent of GILTI in the CIT base (at 601).

[56] Andrew P. Duxbury, Morgan Whaley, and Irana J. Scott, "Have the TCJA International Provisions Met Revenue Estimates?" *Tax Notes Int'l*, July 31, 2023, p. 541.

[57] CRS, *supra* note 22.

[58] *See* Dan R. Bucks et al., "Weak Corporate Tax Reform Critiques Suggest Serious Debate Isn't Intended," *Tax Notes State*, Oct. 23, 2023, p. 287. The MTC's Bruce Fort adopts a different perspective than some of the other advocates of including more FSI in the CIT base: He endorses foreign factor representation. Fort, *supra* note 6, at 854-855.

[59] For instance, the MTC has a long-standing position that applies full foreign factor representation to FSI. The MTC model combined reporting statute addresses several discrete categories of foreign-source income, including subpart F income earned by foreign subsidiaries, income from so-called 80-20 corporations (with 20 percent or more of their factors in the United States), and income from foreign subsidiaries with income in designated "tax haven" countries. Whenever it requires foreign income inclusion, the MTC model statute requires inclusion in the taxpayer's apportionment calculation of "the apportionment factors related to that income." *See* MTC, "Proposed Model Statute for Combined Reporting," section 5A (as amended by the MTC on July 29, 2011).

[60] *See* Mazerov, *supra* note 6.

[61] Davis, Gardner, and Mazerov, *supra* note 36, at 24 (Figure 5).

puts all of the newly raised CIT revenues at risk in future litigation.[62]

'Fair Share' Arguments for State Taxation of FSI Should Not Be Isolated From a Broader Discussion

The debate over whether business pays a "fair share" of state and local taxes is a fourth sphere in which expanding the CIT base to include more FSI is divorced from the overall fabric of SALT. This disconnect is best illustrated by a critique made by co-author Frieden of the views of a group of leading progressives who, over the last five years, in quarterly roundtables in *Tax Notes State*, have regularly advocated for redesigning the state CIT to include more FSI: Dan Bucks, Peter Enrich, Mazerov, and Darien Shanske (BEMS). BEMS's advocacy is supported by dual principles. First, that business does not pay its fair share of state and local taxes, with a particular emphasis on the CIT as a microcosm of the whole. Second, that this "underpayment" of state and local taxes is the result of flaws in the design of tax statutes that favor businesses.[63]

To rebut the BEMS thesis, Frieden, in an April 2024 *Tax Notes State* article titled "Wearing Blinders in the Debate Over Business's 'Fair Share' of State Taxes" (the Blinders article), asked the following questions: (1) Does the structural design explanation for the business "underpayment" of CIT apply equally to other key state and local taxes imposed on business? (2) If not, is there a quantifiable business "overpayment" of other state and local taxes compared with what businesses would pay with a more optimal or neutral tax design?[64]

The answer, backed by extensive data, is that the designs of the largest state and local taxes disfavor businesses far more than they favor businesses.[65] *First, the tax on business property is the largest of all state and local taxes imposed on businesses, accounting for over one-third of all state and local taxes on businesses.* The property tax design in most jurisdictions significantly favors residential homeowners and disfavors businesses.[66]

Most state property tax laws have statutory exemptions that favor homeowners. These include homestead exemptions, property tax credits, assessment limits, and "circuit breakers" — almost all designed to provide property tax relief for homeowners but not businesses. About half the states impose dual (or split-roll) tax rate classifications that favor homeowners and disfavor businesses. In addition, most states have enacted personal property tax base provisions that disfavor businesses. In sum, property taxes in most states deviate from a neutral tax design, with the average ETRs of the largest categories of business property far exceeding the ETRs on homeowner property.[67]

The sales tax on business inputs is the second largest of all state and local taxes imposed on businesses, accounting for over one-fifth of all state and local taxes on businesses. Sales tax experts widely agree that a well-designed retail sales tax should exempt all or most business inputs to avoid sales tax pyramiding.[68]

The sales tax (in all states where it is levied) deviates significantly from an optimal sales tax model, relying heavily on the inclusion of business inputs in the sales tax base. The extensive taxation of business inputs culminates in a business share of total sales tax collections of about 42 percent. The Blinders article focuses on (and quantifies for the first time) the most clear-cut deviation from an optimally designed sales tax — the pyramided portion of taxable business inputs. Sales tax pyramiding or cascading — when sales tax is imposed more than once on a

[62] *See* Frieden and Donovan, "Where in the World Is Factor Representation for Foreign-Source Income?" *State Tax Notes*, Apr. 15, 2019, p. 199.

[63] Frieden, "Wearing Blinders in the Debate Over Business's 'Fair Share' of State Taxes," *supra* note 7. In keeping with their "fair share" focus, Enrich, Mazerov, and Shanske named their "Model Statute for Worldwide Combined Reporting" the "Fair Share For Billionaire Corporations Act."

[64] Frieden, "Wearing Blinders in the Debate Over Business's 'Fair Share' of State Taxes," *supra* note 7.

[65] *Id. See also* Frieden, "The Boomerang Effect of the Business 'Fair Share' Tax Debate," *supra* note 7. State and local taxes on business property (38 percent), sales tax on business inputs (21.9 percent), and CIT (12 percent) make up 70 percent of total state and local taxes on businesses. EY, COST, and STRI, *supra* note 9, at 5.

[66] Frieden, "Wearing Blinders in the Debate Over Business's 'Fair Share' of State Taxes," *supra* note 7, at 106-112.

[67] *Id.*

[68] *Id.* at 99-106.

related series of transactions — accounts for about half of the dollar value of transactions involving taxable business inputs.[69]

In 2024 EY, in its annual study of "total state and local business taxes" commissioned by the Council On State Taxation/State Tax Research Institute (STRI), added a new section that estimates "excess tax" paid by businesses based on deviations from neutral tax designs.[70] First, regarding property taxes paid by businesses, EY concludes that businesses paid $142.8 billion more in property taxes in fiscal 2023 than they would have if they paid using the average ETR and the personal property tax base that applies to homeowners (see Figure 5).[71] The EY study found that the average ETR on business real property is about 50 percent higher than the average ETR on homeowner real property.[72] The estimate of excess business property taxes constitutes over one-third of the total property taxes paid by business in fiscal 2023.[73]

Regarding the sales tax on business inputs, EY's business taxes study estimates that 49 percent of all sales tax on business inputs represents "pyramided" sales taxes — when taxes are imposed more than once on the same supply chain of goods and services. Based on EY's fiscal 2023 estimate of $240.4 billion of sales taxes paid by businesses on purchases of business inputs, this amounts to $118.1 billion of pyramided taxes (see Figure 5).[74]

[69] *Id.*

[70] *See* EY, COST, and STRI, *supra* note 9, at 26-27 (EY has produced the business taxes study (on behalf of COST/STRI) on an annual basis since fiscal 2002); and COST, COST/STRI Studies, Articles and Reports. EY's estimates are based on expanded data sources and a more comprehensive method than used in the "Blinders" article but derive similar results.

[71] EY, COST, and STRI, *supra* note 9, at 26-27.

[72] *Id.*

[73] *Id.*

[74] *Id.* (The EY estimate of the pyramided share of the sales tax on business inputs is slightly lower than the Blinders article estimate, which was based not on U.S. data but on data from Canada's experience with a national goods and services tax (basically a VAT) and provincial sales and use taxes.); Frieden, "Wearing Blinders in the Debate Over Business's 'Fair Share' of State Taxes," *supra* note 7, at 102).

Figure 5.
Estimated 'Excess' Business Property Taxes and Pyramided Sales Taxes on Business Inputs FY23

Amount the Largest State and Local Business Taxes Exceed Taxes Based on Neutral Tax Designs, FY23 ($ billions)

	Estimated Business Tax Paid (EY)	Estimated Tax if Business Property Is Taxed at Homeowner ETR/ Tax Base; and SUT on Non-Pyramided Business Inputs	Excess Tax Based on Neutral Tax Design
Property Tax on Business Property	$394.3	$251.5	$142.8
Sales Tax on Business Inputs	$240.4	$122.3	$118.1
Total Selected Taxes	$634.7	$373.8	$260.9

Source: "Total State and Local Business Taxes: State-by-State Estimates for FY23," prepared by EY for COST and STRI (Dec. 2024). EY estimates based on data from the Bureau of Economic Analysis, the U.S. Census Bureau Annual Survey of State and Local Government Finances, and the Lincoln Institute of Land Policy/Minnesota Center for Fiscal Excellence 50-state property tax comparison study.

The EY analysis of the two largest state and local taxes paid by business (property taxes and sales taxes on business inputs comprise about three-fifths of all state and local business taxes) concludes that businesses paid about $261 billion more in fiscal 2023 than they would have under neutral tax designs (see Figure 5). This finding, while slightly different in the particulars, is consistent with the Blinders article's conclusion that excess property taxes on business property and pyramided sales tax on business inputs attributable to design flaws that disfavor businesses are far greater than BEMS's claims of business underpayments of CIT arising from design flaws that favor businesses.[75]

In response, Enrich asserts that the strategy of the Blinders article is to divert attention and say: "Stop worrying about the CIT and trying to fix that because businesses are already paying way more than their fair share in other categories."[76] He is half right. We have shown clearly that businesses, using BEMS's own criteria of determining fair share based on deviation from an optimal or neutral tax design, are paying more than their fair share in the largest state and local business tax categories.[77]

But the point here is not that states should ignore the CIT or stop worrying about its design. BEMS raise relevant questions about state CIT design, highlighting a long-standing debate over combined reporting and the inclusion of FSI in the CIT base. However, if BEMS want to push for significant increases in CIT or other business taxes justified by design and fair share arguments, they must expect the business community to insist that the designs of all state and local business taxes are evaluated on a broader basis to determine if they favor or disfavor business.

Conclusion

Currently, advocates of increasing state CIT revenue by including more foreign-source income in the CIT base typically make their case completely divorced from other fiscal, tax, or state and local tax design considerations. Every state has different mixes of budgetary needs, tax composition, and tax designs. Ultimately, state tax policy must focus on state-specific budget and tax considerations. State CIT base expansion legislation should not be considered in isolation from other relevant factors, including:

- other contemporaneous (and very large) increases in state CIT revenue;
- GMT and federal GILTI measures that significantly reduce the impact of international profit shifting and provide relative parity in the treatment of MNEs;
- fair and constitutionally permissible apportionment formulas that provide symmetry between foreign-source income base inclusion and foreign factor representation; and
- other state and local business tax designs that disfavor businesses far more than CIT designs purportedly favor businesses. ■

[75] Frieden, "Wearing Blinders in the Debate Over Business's 'Fair Share' of State Taxes," *supra* note 7, at at 112-114. BEMS allege businesses are underpaying as much as $17 billion in CIT as the result of the absence of MWWCR in all states (*id.* at 98). An updated ITEP study (relied on by BEMS) estimates that state CIT losses due to the absence of MWWCR are $18.7 billion. *See* Davis, Gardner, and Mazerov, *supra* note 36.

[76] Bucks et al., "Incidence Is Not Incidental: A First Response to COST's Flawed Critique," *Tax Notes State*, Oct. 21, 2024, p. 173, at 174-175.

[77] BEMS's primary critique of Frieden's "fair share" argument is that the burden of state and local taxes when the "legal" incidence of the tax falls on business is not fully on businesses because some or most of the "economic" incidence of the taxes is passed on to consumers and workers. *See* Bucks et al., *supra* note 76. For Frieden's detailed rebuttal of BEMS's economic incidence theory, see Frieden, "The Boomerang Effect of the Business 'Fair Share' Tax Debate," *supra* note 7.