Barclays Bank PLC v. Franchise Tax Board of California: Does the Application of Worldwide Unitary Taxation to Non-U.S. Parent Corporate Groups Violate the Commerce Clause?

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Barclays Bank PLC v. Franchise Tax Board of California: Does the Application of Worldwide Unitary Taxation to Non-U.S. Parent Corporate Groups Violate the Commerce Clause?

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Abstract

This Comment examines whether the Supreme Court in Barclays v. Franchise Tax Board, correctly decided that the application of worldwide unitary taxation to non-U.S. parent groups does not violate the Commerce Clause.
COMMENTS

BARCLAYS BANK PLC v. FRANCHISE TAX BOARD OF CALIFORNIA: DOES THE APPLICATION OF WORLDWIDE UNITARY TAXATION TO NON-U.S. PARENT CORPORATE GROUPS VIOLATE THE COMMERCE CLAUSE?

Zain E. Husain*

INTRODUCTION

In 1983 multinational corporations1 ("MNCs") suffered a major setback in their legal campaign to invalidate worldwide unitary taxation2 (or "WWCR") when the U.S. Supreme Court

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1. See Lewis B. Kaden, State Taxation of Multinational Corporations, 32 CATH. U. L. Rev. 829 (1983) for a description of multinational corporations ("MNCs"). The modern MNC is a far-flung enterprise, active in markets scattered throughout the world. *Id.* at 831. MNC activities are usually directed from a central headquarters where strategic decisions are made and communicated to units around the world. *Id.* The typical MNC considers its diverse components part of a single global system whose overall success, rather than that of the individual component, is considered critical. *Id.* Decisions on the location of separate units are commonly based on a complex set of factors, including financing, government relations, regulation, labor conditions, and marketing opportunities. *Id.; see also* Note, Multinational Corporations and Income Allocation Under Section 482 of the Internal Revenue Code, 89 HARV. L. REV. 1202, 1205 (1976) (stating that MNC is "cluster of corporations of diverse nationality joined together by ties of common ownership and responsive to a common management").

Under worldwide unitary taxation, a MNC's income tax base is established by assessing the income of all affiliated corporations, including the income of non-U.S. entities operating solely in non-U.S. jurisdictions. Marlis Carson & Douglas W. Briggs, Jr., U.S. Supreme Court Backs California in Barclays Dispute Over Unitary Method, 8 TAX NOTES INT'L 1687 (June 27, 1994). The worldwide unitary taxation method assumes that a MNC receives a pro rata share of the worldwide income generated by all business within the corporate family. *Id.* A corporation's income tax base is the amount of the corporation's income subject to apportionment. Jerome Hellerstein & Walter Hellerstein, State and Local Taxation, ¶¶ 7.02, 7.03, at 7-3 to 7-6 (2d ed. 1991). The U.S. Supreme Court has defined worldwide unitary taxation in the following manner:

[Worldwide unitary taxation] calculates the local tax base by first defining the scope of the "unitary business" of which the taxed enterprise's activities in the
("Supreme Court" or "Court") held in *Container Corp. of America v. Franchise Tax Board* that California's WWCR-based franchise tax scheme did not violate the Commerce Clause. For those states using worldwide unitary taxation, *Container* was less than an absolute constitutional endorsement because the decision did not complete the analysis of WWCR-based taxation under the Commerce Clause. The Supreme Court in *Container* resolved solely those Commerce Clause questions arising from the application of worldwide unitary taxation to U.S. parent MNCs. The Supreme Court in *Container* declined to decide whether the application of worldwide unitary taxation to non-U.S. parent MNCs would survive Commerce Clause review.

Following the *Container* decisions non-U.S. parent MNCs ini-

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4. Id. at 184-97. The Commerce Clause grants Congress the power "[t]o regulate commerce with foreign nations, and among the several states." U.S. CONST. art. I, § 8, cl. 3.


6. Id. at 189 n.26. The Supreme Court stated that "[w]e have no need to address in this opinion the constitutionality of combined apportionment with respect to state taxation of domestic corporations with foreign parents or foreign corporations with either foreign parents or foreign subsidiaries." *Id.* The Supreme Court similarly noted later in its opinion that "[w]e recognize that the fact that the legal incidence of a tax falls on a corporation whose formal corporate domicile is domestic might be less significant in the case of a domestic corporation that was owned by foreign interests. We need not decide here whether such a case would require us to alter our analysis." *Id.* at 195 n.32. The possible constitutional analysis of this reserved question has been the subject of several commentaries. See, e.g., Elizabeth Harris, Note, *Desperate for Revenue: The States' Unconstitutional Use of the Unitary Method to Apportion the Taxable Income of Foreign Parent Corporations*, 19 HASTINGS CONST. L.Q. 1077 (1992) (concluding that use of unitary taxation method to apportion state income tax liabilities of non-U.S. parent corporations with U.S. subsidiaries would violate Commerce Clause); Kevin M. Kohls, Note, *State Unitary Taxes Imposed on Foreign Based Multinational Groups: A Post Container Analysis*, 31 WAYNE L. REV. 219 (1984) (concluding that Supreme Court would strike down state worldwide unitary tax imposed on non-U.S. parent MNCs); Kirsten Schlenger, Note, *State Worldwide Unitary Taxation: The Foreign Parent Case*, 23 COLUM. J. TRANSNAT'L L. 445 (1985) (arguing that policy considerations as well as case law prohibits application of worldwide unitary taxation to non-U.S. parent MNCs); Douglas M. Ventura, Note, *State Unitary Business: Are Multinational Corporations Being Subjected to an Unconstitutional Tax*, 21 SAN DIEGO L. REV. 879 (1984) (concluding that worldwide unitary taxation when applied to non-U.S. parent MNCs violates the negative implications of the Commerce Clause).
tiated litigation in federal court challenging worldwide unitary taxation and also began a concerted political campaign at the state and federal levels to force a resolution of the worldwide unitary taxation dispute. The MNCs' legal efforts were initially unsuccessful because of procedural obstacles, which prevented them from gaining standing in federal court. The reserved issue on worldwide unitary taxation was finally presented for adjudication on the merits before the Supreme Court when review was granted in Barclays Bank PLC v. Franchise Tax Board of Califor-

7. See, e.g., Shell Petroleum, N.V. v. Graves, 709 F.2d 593 (9th Cir.), cert. denied, 464 U.S. 1012 (1983); EMi Ltd. v. Bennet, 738 F.2d 994 (9th Cir.), cert. denied, 469 U.S. 1073 (1984). In Shell Petroleum, the Ninth Circuit addressed whether Shell Petroleum, an Anglo-Dutch MNC involved in the petroleum business, had standing to bring a shareholder derivative suit on behalf of its California subsidiaries challenging California's WWCRA-based franchise tax scheme. Shell, 709 F.2d at 596. The Ninth Circuit decided that Shell could not maintain a shareholder derivative suit because it had failed to demonstrate a personal and direct injury, and was thus precluded from challenging the California tax. Id. In EMI Ltd., the Second Circuit used substantially the same reasoning to also dismiss on standing grounds a non-U.S. parent MNC suit challenging California's worldwide unitary taxation scheme. EMI, 738 F.2d at 997.

The Seventh Circuit, however, declined to follow the Ninth and Second Circuits in Alcan Aluminum Ltd. v. Franchise Tax Bd., 860 F.2d 688 (7th Cir.), rev'd, 493 U.S. 331 (1988). In Alcan, the Seventh Circuit analyzed whether a non-U.S. parent MNC had standing to bring suit in federal court for an injunction and declaratory judgment to invalidate under the Commerce Clause the apportionment of the income of its California subsidiaries under a California worldwide unitary tax scheme. Id. at 690-91. The Seventh Circuit concluded that the shareholder-standing rule did not operate as a procedural restriction barring Alcan's claim because the subsidiary was an instrumentality of Alcan's multinational business activities. Id. at 697. Since the California tax restricted the parent's ability to control the conduct of international business by its California subsidiaries, it suffered a distinct and personal injury. Id.

On appeal, the Supreme Court decided that Alcan's suit fell within the constitutional parameters of an Article III "case or controversy" because the California method "threaten[ed] to cause actual financial injury to Alcan... under Article III by illegally reducing the return on [its] investment." Alcan, 493 U.S. at 336. Nevertheless the Supreme Court reversed the Seventh Circuit and considered it unnecessary to reach the question of whether non-U.S. parent MNCs could meet the prudential requirements of the standing doctrine because the claim was infirm under the Tax Injunction Act. The Tax Injunction Act provides that "the district courts shall not enjoin, suspend or restrain the assessment, levy or collection of any tax under State law where a plain, speedy and efficient remedy may be had in the courts of the state." Id. (quoting Tax Injunction Act, 28 U.S.C. § 1341 (1982)). For a discussion of the standing issue see, Note, Standing Under Commercial Treaties: Foreign Holding Companies and the Unitary Tax, 97 Harv. L. Rev. 1894 (1984) (arguing that federal courts should grant non-U.S. parent MNCs standing to challenge unitary taxation); Diane M. Parker, Note, Unitary Tax Litigation After Alcan: What Options Remain for Foreign Parent Companies, 26 Tex. Int'l L.J. 125 (1991) (arguing that federal courts have correctly concluded that non-U.S. parent MNCs lack standing to challenge state unitary taxation schemes).
nia.\textsuperscript{8} The Barclays case was before the Supreme Court on appeal from a lawsuit challenging WWCR-based taxation initiated in California state court.\textsuperscript{9} The Supreme Court handed down its decision in Barclays on June 20, 1994.\textsuperscript{10} The Supreme Court held in Barclays that the application of worldwide unitary taxation to non-U.S. parent MNCs was constitutionally indistinguishable from its application to U.S. parent MNCs and thus did not transgress Commerce Clause principles.\textsuperscript{11} In contrast to their unsuccessful legal campaign,\textsuperscript{12} the MNCs' political effort to force a resolution of the worldwide unitary taxation dispute was largely successful and forced WWCR states to modify their corporate income tax schemes in ways that mitigated the controversial aspects of WWCR-based taxation.\textsuperscript{13}

The final political resolution of the reserved WWCR issue has significant domestic and international implications. First, Barclays resolves questions regarding several billion dollars in tax revenues and thus has important budgetary consequences for the states.\textsuperscript{14} Second, the result in the Barclays case implicates

\textsuperscript{8} 114 S. Ct. 379 (1993). The following entities filed amicus briefs in the Barclays Supreme Court litigation: State of New Mexico; State of North Dakota; State of Alaska; Banque Nationale de Paris; California Legislature; California Tax Reform Association; Citizens for Tax Justice; Committee on State Taxation; Confederation of British Industry; Congressman Don Edwards; Council of State Governments; European Community Members; Federation of German Industry; Japan Tax Association; Keidanren (Japan Federation); Member States of the European Community; Multi-State Tax Commission; Organization for International Investment, Inc.; Reuters Limited; Senator Byron L. Dorgan; United Kingdom (on petition for \textit{certiorari}); United Kingdom (on the merits); United States; Washington Legal Foundation. John Turro, \textit{U.S. Supreme Court a Hard Sell for Barclays/Colgate Unitary Cases}, 8 \textit{TAX NOTES INT'L} 903, 905-06 (Apr. 4, 1994).


\textsuperscript{10} 114 S. Ct. 2268 (1994).

\textsuperscript{11} \textit{Id.} at 2276.

\textsuperscript{12} McArthur & Houghton, \textit{supra} note 2, at 179.

\textsuperscript{13} \textit{Id.}

\textsuperscript{14} See \textit{Unitary Taxes: Clinton Meets California Tax Board Chairman on “Barclays” Unitary Tax Case}, Daily Tax Rep. (BNA) No. 95, at D-19 (May 19, 1993). Brad Sherman, the Chairman of the California Equalization Board, estimated that California could lose up to US$4 billion in revenues if the U.S. Supreme Court found worldwide unitary taxation unconstitutional. \textit{Id.} California's revenue losses from an adverse decision in Barclays for the 1994 and 1995 tax years were expected to exceed US$2 billion. \textit{Unitary}
issues relating to future commercial relations between the United States and its international trading and investment partners. Finally, the Barclays decision modifies the framework for future judicial review of state taxation under the Commerce Clause.

This Comment examines whether the Supreme Court in Barclays correctly decided that the application of worldwide unitary taxation to non-U.S. parent groups does not violate the Commerce Clause. Part I describes the worldwide unitary taxation method, and separate accounting, the primary alternative available to states imposing corporate income taxes. Next, Part I analyzes the worldwide unitary taxation controversy and sets forth the Commerce Clause limitations on state taxation. Finally, Part I discusses the Container decision in which the Supreme Court upheld the application of worldwide unitary taxation to U.S. parent corporate groups. Part II describes the decisions of the California state courts and the U.S. Supreme Court in Barclays. Part III argues that the Supreme Court correctly decided the non-U.S. parent MNC issue in Barclays. Part III also


15. See, e.g., John Turro, \textit{German Finance Committee Warns White House Against Supporting California's Unitary Tax Method}, 7 Tax Notes Int'l 165 (July 19, 1993). A July 1, 1993 resolution of the Finance Committee of the German Bundestag called on the Clinton administration to oppose California's use of worldwide unitary taxation. \textit{Id.} The Committee's intent was to put pressure on the Clinton administration not to support California in the Barclays case. \textit{Id.} The Committee resolution added that the retention by California of worldwide unitary taxation would seriously prejudice economic relations between the Germany and the United States. \textit{Id.; see also} Michael I. Goodbee, \textit{The British Threat to Retaliate Against the Unitary Method of Taxation}, 7 Tax Notes Int'l 538, 538 (Aug. 23, 1993). On May 13, 1993 the U.K. Chancellor of the Exchequer threatened that if a satisfactory resolution to the worldwide unitary taxation dispute was not reached, the United Kingdom would have to take retaliatory action. \textit{Id.} The threatened U.K.'s retaliatory actions included the withdrawal of tax refunds from U.S. corporations of under the U.S.-U.K. income tax treaty. \textit{Id.} at 540. In May 1993, Christiane Scrivener, European Community Tax Commissioner, stated that U.S. corporations doing business in the European Union would be subject to retaliatory taxation if the U.S. Supreme Court upheld California's use of worldwide unitary taxation. EC Tax Commissioner Warns of Retaliation if California Unitary Tax System is Upheld, DAILY TAX REP. (BNA) No. 90, at G-1 (May 12, 1993).

argues that after Barclays, taxpayers face a heightened burden in demonstrating that state taxes violate the Commerce Clause and that the states are unlikely to embrace worldwide unitary taxation even though the Commerce Clause no longer constitutes an obstacle. This Comment concludes that with Barclays, the Supreme Court has completed the constitutional analysis of worldwide unitary taxation under the Commerce Clause.

I. WORLDWIDE UNITARY TAXATION AND COMMERCE CLAUSE LIMITATIONS ON STATE TAX POWER

Dividing the income of a corporation engaging in interstate or international business between taxing jurisdictions is a highly controversial and complex aspect of state tax administration. The sophistication of modern business has contributed to the complexity of the apportionment process. While historically, the states of the United States used the separate accounting method for division of income purposes, because of the perceived shortcomings of separate accounting, the states adopted the unitary taxation method beginning in the 1930's. Later in the 1970's several states adopted a particular variation of unitary taxation called worldwide unitary taxation. Few controversies concerning U.S. tax policy have generated as much controversy as worldwide unitary taxation. From the late 1970's onwards MNCs engaged in a sustained legal campaign to invalidate world-
wide unitary taxation, predicated on the Commerce Clause of the U.S. Constitution.24 Although MNC Commerce Clause arguments failed in 1983 in Container, the Supreme Court left open the possibility that the application of worldwide unitary taxation to non-U.S parent MNCs with U.S. subsidiaries might not pass Commerce Clause scrutiny.25

A. Apportioning Multijurisdictional Corporate Income: Separate Accounting, Unitary Taxation, and the Worldwide Unitary Taxation Controversy

When a state seeks to tax the net income of a corporation operating across tax frontiers, as a threshold matter it must devise a taxation mechanism that identifies a portion of net income attributable to the corporation's activities conducted within the state.26 Two primary alternatives are available for apportioning multijurisdictional corporate income: separate accounting and unitary taxation.27 Worldwide unitary taxation is a

24. See supra note 2 (citing cases where MNCs have brought Commerce Clause challenges to worldwide unitary taxation).
26. HARTMAN, supra note 17, § 9:16, at 521. Net income is the "end product of the numerous intermingled transactions and operating events conducted by a taxpayer within an arbitrary time period called a taxable year." Dexter, supra note 18, at 313. For tax purposes, net income is classified as an intangible, giving multiple jurisdictions the legal right to tax the same income. HARTMAN, supra note 17, § 9:2, at 462. State corporate income taxes or income-based taxes can broadly be divided into two categories: (1) excise taxes imposed for doing business within the state or for holding a license for doing business within the state, and (2) taxes on net income that originates in the state. STATE AND LOCAL TAXATION, supra note 2, ¶ 7.01, at 7-1 to 7-2. Excise taxes are commonly referred to as "franchise" taxes. Id. Taxes on net income are commonly referred to as "direct net income" taxes. Id.

Income and income-based taxes were first used by the states in the 1840's when Pennsylvania, Maryland, Virginia, Alabama, Florida, and North Carolina, adopted income based fiscal measures as a source of revenue. David M. Hudson & Daniel C. Turner, International and Interstate Approaches to Taxing Business Income, 6 NW. J. INT'L L. & BUS. 562, 582 (1984). Under the financial pressures of the Civil War (1860-65) six other states also turned to corporate income taxes, including Georgia, Missouri, Texas, Louisiana, West Virginia, and Kentucky. Id. at 582-83. Wisconsin imposed the first modern income tax in 1911 with graduated rates on personal and corporate income. Id. at 584. Wisconsin was soon followed by other states so that by the 1930's a majority of states were using corporate income taxes, either as direct taxes on income or as indirect excise taxes measured by income. Id.

27. HARTMAN, supra note 17, § 9:16, at 521-24. A third method, specific allocation, is also used to apportion corporate net income for tax purposes. Id. Under the specific allocation method, business income is identified with a specific geographic source and confers on the source state the right to tax that income. STATE AND LOCAL TAXATION,
refinement of the unitary taxation method,\textsuperscript{28} which although only used by a minority of states,\textsuperscript{29} has generated intense opposition from both U.S and non-U.S. parent MNCs.\textsuperscript{30}

1. Separate Accounting

Historically, the separate accounting method was used by the states to apportion the income of both multi-state and multinational businesses.\textsuperscript{31} Under separate accounting, the in-state activities of an MNC are separated from its overall business activities and then the net income attributable to those in-state activities are established.\textsuperscript{32} Because the taxed entity is considered separate from its affiliates and subsidiaries, attributable income is established without reference to the financial performance of the taxpayer's businesses operating in other jurisdictions.\textsuperscript{33} The value and profits of an entity’s in-state activities are determined by reference to its own accounting records, and the taxing jurisdiction may tax only the income reflected by those separate accounts.\textsuperscript{34} To ensure that multi-entity businesses operating across tax boundaries do not use the transfer pricing mechanism to shift income into low tax jurisdictions,\textsuperscript{35} under the separate ac-
counting method transactions between affiliated entities are deemed to occur at “arm’s length” prices.36

2. Unitary Taxation

An alternate method available to the states for apportioning multi-state or multinational income is unitary taxation,37 first used over a century ago by the states to tax interstate utilities,38 and presently used by all states imposing corporate income taxes.39 Unlike the separate accounting method, unitary taxation does not purport to identify the exact geographical source of an enterprise’s profits.40 The premise of unitary taxation is

36. Id. at 182. “Arm’s length” prices are prices equal to those charged unrelated firms. Id.
37. STATE AND LOCAL TAXATION, supra note 2, ¶ 8.05, at 8-36.
38. Id. ¶ 8.05, at 8-36. The states developed unitary taxation at the turn of the century as an ad valorem property tax for interstate utility systems and railroads. Id. Under the “unit rule,” the value of a railroad or utility was treated as a function of the interstate system as a whole. Id. Therefore, a formula was applied to apportion the income of the entire railway or utility as a unit between the jurisdictions in which it operated. Id.

The U.S. Supreme Court upheld the states’ application of the “unit rule” in Adams Express Co. v. Ohio State Auditor, 165 U.S. 194 (1897). In Adams Express the Supreme Court agreed with the states that a tax purely on the tangible property of a railroad used within its borders did not represent the true value of a utility’s activities within any particular state:

No more reason is perceived for limiting the valuation of the property of express companies to horses, wagons and furniture, than that of railroad, telegraph and sleeping car companies, to roadbeds, rails and ties; poles and wires; or cars. The unit is a unit of use and management, and the horses, wagons, safes, pouches and furniture; the contracts for transportation facilities; the capital necessary to carry on the business, whether represented in tangible or intangible property... [possess] a value in combination and from use in connection with the property and capital elsewhere, which [can] as rightfully be recognized in the assessment for taxation in the instance of these companies as the others.

We repeat that while the unity which exists may not be a physical unity, it is something more than a mere unity of ownership. It is a unity of use, not simply for the convenience or pecuniary profit of the owner, but existing in the very necessity of the case - resulting from the very nature of the business. Id. at 221-22. The unit rule is the theoretical progenitor for modern unitary taxation. STATE AND LOCAL TAXATION, supra note 2, ¶ 8.05, at 8-38.
40. HARTMAN, supra note 17, 9:18, at 523.
that the total income of an enterprise results from certain income producing factors. The assumption continues that income produced by the combination of those factors has its source where those income producing factors are located.

In order to compute the income tax base, unitary taxation first defines the unitary business of which the taxed entity forms a part. The most common definition of a unitary business states that a unitary business includes all affiliated enterprises that share common ownership, common management, and common operations. Next unitary taxation requires the taxpayer to combine the net income of the entire group of related enterprises and to submit a single consolidated net income report, which represents the taxpayer’s apportionable tax base. Finally, the income of the unitary business is apportioned by applying a formula that allocates a fair share of the unitary business’ consolidated income to the taxing jurisdiction. Most states using unitary taxation employ a standard three-factor formula based on a unitary business’ interest in state property, payroll, and sales as compared to its total property, payroll, and sales. Generally, each factor within an apportionment formula is

41. Id.
42. Id.
43. Id.
44. State and Local Taxation, supra note 2, ¶ 8.11, at 8-76.
46. Pearson, supra note 22, at 96.
47. Hartman, supra note 17, § 9:18, at 523.
48. Id. § 9:18, at 523-24. For example, assume first that the total multinational income of Corporation X’s unitary business is US$100,000 and the percentage of property, payroll, and sales represented by Subsidiary XY, Corporation X’s subsidiary in unitary tax State Y, is 27.5%, 15%, and 2.5% respectively. In this case the average State Y percentage of Corporation X’s total property, payroll, and sales is 15%. Fifteen percent of US$100,000, or US$15,000, will be the figure on which State Y’s taxing authority will assess Subsidiary XY’s corporate income tax.
equally weighted.\textsuperscript{49}

Under worldwide unitary taxation, which is a variation of the unitary taxation method, a taxpayer is required to consolidate the income of all enterprises throughout the world that comprise a part of its unitary business.\textsuperscript{50} Thus, U.S.-parent MNCs can be required to include in the apportionable tax base the non-U.S. income of non-U.S. affiliates that are part of its unitary business.\textsuperscript{51} Similarly, the U.S. subsidiary of a non-U.S. parent MNC can be required to include the non-U.S. income of its

\textsuperscript{49} Pearson, supra note 22, at 112. Some states, however, assign a 50% weight to the sales factor and 25% weight to both the property and payroll factors. \textit{Id.} By changing the relative weight of each factor within the apportionment formula a state effectively lowers income taxes for local businesses that export products and increases taxes for out-of-state businesses that produce goods that are sold in the taxing state. \textit{Id.} By increasing the weight of the sales factor, states provide an incentive for out-of-state businesses to relocate in the taxing state. \textit{Id.}

Much of the prevailing non-uniformity between state apportionment formulae can be ascribed to the pursuit of economic self-interest by the states. See \textit{Special Subcomm. on State Taxation of Interstate Commerce of the House Comm. on the Judiciary, State Taxation on Interstate Commerce, H.R. No. 1480, 88th Cong., 2d Sess. 123 (1964)} (stating that "[t]he formulae presently employed by the various states were enacted by state legislatures for revenue purposes only, and without thought to uniformity with the laws of other states" and that "[f]actors of formulae, and the components thereof have been weighted to meet local interests peculiar to the state, and with no interstate cooperation in view [which] has resulted in many inequities, some of gross proportions").

\textsuperscript{50} Pearson, supra note 22, at 112. Worldwide unitary taxation is also referred to as "Worldwide Combined Reporting" or "Total Worldwide Combination." A.W. Grumwell et al., \textit{Worldwide Unitary Tax: Is it Invalid Under the Treaties of Friendship, Commerce and Navigation}, 18 \textit{Law & Pol'y Int'l Bus.} 695, 705 (1986). Certain other variations on the scope of income reporting are employed by states using unitary taxation. \textit{Id.} Under "Domestic Worldwide Combined Reporting" or "Domestic Worldwide Combination," subsidiaries and parent corporations located outside the U.S. which are not involved in any U.S. business are automatically excluded from the reporting requirement. \textit{Id.} A third form of unitary taxation reporting known as "Domestic Combined Accounting" includes in the apportionable tax base only the income of U.S. businesses. \textit{Id.} at 707. This method effectively limits includible income to profits only of U.S. affiliates. \textit{Id.} This restricted form of income combination falls within the parameters of the "water's edge" unitary taxation method. \textit{Id.}


\textsuperscript{51} Pearson supra note 22, at 112.
non-U.S. parent and affiliates.\textsuperscript{52} Worldwide unitary taxation constitutes the most expansive assertion by the states of the unitary taxation method.\textsuperscript{53}

3. The Worldwide Unitary Taxation Controversy

The use of worldwide unitary taxation to determine and distribute the net income of an MNC operating among several taxing jurisdictions has generated opposition from MNC taxpayers because they argue it grossly distorts income allocation.\textsuperscript{54} MNCs argue that to the extent that income overallocated to one jurisdiction is also taxed by another jurisdiction, they are systematically subjected to international multiple taxation.\textsuperscript{55} Non-U.S. MNCs additionally argue that worldwide unitary taxation requires making adjustments to international accounting records to comply with U.S. accounting principles, including aggregating the income of international subsidiaries, translating data from other languages, and converting non-U.S. financial statements into U.S. dollars.\textsuperscript{56} In their view, meeting the costs of these adjustments unfairly burdens non-U.S. businesses and specifically provides a competitive advantage to U.S. parent MNCs that maintain their accounting records in WWCR-compatible format.\textsuperscript{57}

States that use worldwide unitary taxation respond that WWCR-based taxation is fairer and more efficient method by which to apportion multijurisdictional corporate income.\textsuperscript{58} Specifically, separate accounting, the primary alternative to unitary taxation, allows MNCs to evade income tax liabilities by distorting prices of intra-corporate transfers to shift income into low tax jurisdictions.\textsuperscript{59} Establishing “arm’s length” prices for intra-corporate transfers does not mitigate the problem of tax evasion in their view.\textsuperscript{60} In most cases there are no uncontrolled

\footnotesize{\textsuperscript{52} Id. \\
\textsuperscript{53} Grumwell et al., supra note 50, at 705. \\
\textsuperscript{54} Pearson, supra, at 123-24. \\
\textsuperscript{55} Id. \\
\textsuperscript{56} Id. \\
\textsuperscript{57} Id. \\
\textsuperscript{58} STATE AND LOCAL TAXATION, supra note 2, at \S 8.03, at 8-29-32; see supra notes 35-36 (describing transfer pricing mechanism). \\
\textsuperscript{59} Id. \\
\textsuperscript{60} STATE AND LOCAL TAXATION, supra note 2, \S 8.03, at 8-29-31.}
sales within a corporate group against which to compare particular transfers. It thus becomes necessary to construct "arm's length" prices by comparing equivalent transactions in the open market or by estimating the costs of the goods or services in question and adding a reasonable profit. Usually, however, there exists no comparable market data. Similarly, attempting to establish "arm's length" prices by adding a reasonable profit to the manufacturing price is often impracticable because it is difficult to estimate manufacturing costs and reasonable profit margins. Second, maintaining separate accounting records for taxpayers in a format that provides adequate data to establish its separate tax liabilities is prohibitively expensive. Finally, the unitary tax states argue that separate accounting bears little connection to the realities of modern business activity because it fails to recognize that MNCs are operationally centralized and net income is the outcome of integrated economic activity.

B. Commerce Clause Limitations on State Taxation

State discretion to devise corporate tax schemes taxing income earned in interstate or international commerce, while recognized as extensive, is limited in important respects by the Commerce Clause of the U.S Constitution. Commerce Clause measures adopted by the federal government override any state measures with which they conflict under the Supremacy

61. Id.
62. Id.
63. Id.
64. Id.
65. Id.
66. Id.
67. Id. Professors Jerome Hellerstein and Walter Hellerstein state that: [Separate accounting] operates in a universe of pretense; as in Alice in Wonderland, it turns reality into fancy, and pretends that it's in the real world. For the essence of the separate accounting technique of dividing the income of a unitary business is to ignore the interdependence and integration of the business operations ... and treat them, instead, as if they were separate, interdependent, and non-integrated. The difference between ... separate businesses and the national and multinational unitary businesses that dominate our economy are crucial. Indeed, and to considerable extent the wealth, power, and profits of gargantuan enterprises are attributable to the very fact that they are integrated, unitary businesses.

Id. ¶ 8.03, at 8-31 to 8-32.
68. HARTMAN, supra note 17, ¶ 1:1, at 1-2.
69. Id. ¶ 2:2, at 14-19.
Clause.\textsuperscript{70} Given the absence generally of congressional regulation limiting state taxation, however,\textsuperscript{71} the restrictions issuing from the "dormant" Commerce Clause have operated more extensively to restrict state taxation.\textsuperscript{72} Under the "dormant" Commerce Clause doctrine the Supreme Court has established standards for reviewing state tax schemes to ensure that they do not unduly burden interstate and international commerce.\textsuperscript{73} In \textit{Container} the Supreme Court reviewed worldwide unitary taxation under the "dormant" Interstate and Foreign Commerce Clause tests but found that WWCR-based taxation was not unconstitutional.\textsuperscript{74}

1. The Commerce Clause

The U.S. states generally have extensive discretion in exercising their taxation power under the U.S. federal system.\textsuperscript{75} The U.S. Constitution, however, places important restrictions on state taxation.\textsuperscript{76} Primary among them are the Commerce Clause

\textsuperscript{70} Id.
\textsuperscript{71} \textit{Id.} ¶ 13:1, at 677-78.
\textsuperscript{72} Id. ¶ 2:2, at 17-18.
\textsuperscript{74} Container Corp. v. Franchise Tax Bd., 463 U.S. 159 (1983).
\textsuperscript{75} HARTMAN, supra note 17, 1:1, at 1-2; see Wisconsin v. J.C. Penny Co., 311 U.S. 435, 444 (1940). In \textit{J.C. Penny} the Supreme Court stated that: The Constitution is not a formulary. It does not demand of states strict observance of rigid categories nor precision of technical phrasing in their exercise of the most basic power of government, that of taxation. . . . A state is free to pursue its own fiscal policies, unembarrassed by the Constitution, if by the practical operation of a tax the state has exerted its power in relation to opportunities which it has given, to protection which it has afforded, to benefits which it has conferred by the fact of being an orderly civilized society.
\textsuperscript{76} HARTMAN, supra note 17, ¶ 1:1, at 6. The Due Process Clause of the Fourteenth Amendment has figured as prominently in worldwide unitary tax litigation as the Commerce Clause. \textit{Id.} The Due Process Clause states that "nor shall any state deprive any person of life, liberty, or property, without due process of law." U.S. Const. amend. XIV, cl. 1.
The Due Process Clause restricts the incidence of state taxation of interstate or international commerce to the benefits the state has conferred on the taxpayer. \textit{See}, e.g., \textit{J.C. Penny Co.}, 311 U.S. at 444 ("The test is whether property was taken without due process of law, or . . . whether the taxing power exerted by the state bears fiscal relations to protection, opportunities, and benefits given by the state. The simple but controlling question is whether the state has given anything for which it can ask some-
limitations placed on the states' power to tax interstate or international commerce.\footnote{77. U.S. CONST. art. I, § 8, cl. 3. The Commerce Clause grants Congress the power, "[t]o regulate commerce with foreign nations, and among the several states." \textit{Id.}}

First, the Commerce Clause restricts state taxes that conflict
with any federal measure regulating interstate or international commerce. Preemption occurs in cases of conflict because the Commerce Clause of the U.S. Constitution affirmatively grants Congress the authority to regulate interstate and international commerce. Under the Supremacy Clause, when Congress acts within the scope of its expressly delegated commerce authority, any conflicting state fiscal measure is preempted by the federal measure.

The Commerce Clause also operates to restrict state taxation on interstate or international commerce under the "dormant" Commerce Clause doctrine. The U.S. Constitution, subject to one narrow exception under the Import-Export Clause, provides no overt textual limitations on the state tax power. Moreover, with few exceptions, Congress has declined to exercise its authority under the Commerce Clause to limit state taxation. Recognizing that myopic state tax policies can have detri-

78. HARTMAN, supra note 17, ¶ 2:2, at 14-19.
79. Id.
80. U.S. CONST. art. VI, § 2. The Supremacy Clause states that "the Laws of the United States . . . shall be the supreme Law of the Land." Id.; see JOHN E. NOWAK & RONALD D. ROTUNDA, CONSTITUTIONAL LAW § 8.1, at 274 (3d ed. 1991) (stating that "when a state regulation conflicts with federal legislation enacted under the commerce clause, the federal statute controls pursuant to the supremacy clause."); LAURENCE H. TRIBE, AMERICAN CONSTITUTIONAL LAW § 6-25, at 479 (2d ed. 1988) (stating that "so long as Congress acts within an area delegated to it, the preemption of conflicting state or local action . . . flow directly from the substantive source of power of the congressional action coupled with the supremacy clause article IV"); STATE AND LOCAL TAXATION, supra note 2, ¶ 4.15, at 4-111 (stating that "[u]nder the Supremacy Clause of the Constitution, State action that conflicts with a valid exercise of Congressional power must give way and consequently, State taxes on interstate or foreign commerce that conflict with Federal legislation, enacted pursuant to the grant to Congress of the power to regulate the commerce, are invalid").
81. HARTMAN, supra note 17, ¶ 2:2, at 17-18.
82. U.S. CONST. art. I, § 10, cl. 2. State power to tax foreign commerce is limited by the Import-Export Clause, which states that "[n]o state shall, without the consent of the Congress, apply any Imposts or Duties on Imports or Exports, except what may be absolutely necessary for executing its inspection Laws." Id. The Export-Import Clause could potentially have served as an important limitation on state taxes on interstate commerce. Walter Hellerstein, State Taxation of Interstate Business: Perspectives on Two Centuries of Constitutional Adjudication, 41 TAX L. 37, 39 (1987) [hereinafter Two Centuries]. Since the late 19th century, however, the Import-Export Clause has been interpreted by the Supreme Court as having no application to commerce among the states. Id. (citing Woodruff v. Parnham, 75 U.S. (8 Wall.) 129 (1868)).
83. NOWAK & ROTUNDA, supra note 80, § 8.1, at 274; TRIBE, supra note 80, § 6.2, at 403.
84. HARTMAN, supra note 17, § 13.1, at 677-78. Before 1959 Congress had declined to exercise its powers under the Commerce Clause to legislate in the state tax field.
mental economic consequences for the states and ultimately the nation as a whole, the U.S. Supreme Court for over a century has interpreted the Commerce Clause as limiting by its own force state taxes that threaten interstate or international commerce. The judicial branch has thus assumed the role of policing state fiscal conduct to protect the larger commercial interests of the United States under the "dormant" Commerce Clause doctrine.


85. *See Hartman, supra* note 17, § 1:1, at 2 (stating that "[t]he existence of myopic state tax policies can be destructive of harmonious coordination of political power between the Nation and state governments at home, plus the impairment of uniform federal policy in the commercial and political relations abroad [and] additionally, such harmful state policies could curtail optimum national economic development").

86. *See Two Centuries, supra* note 82, at 43-44; *see also* Wardair Canada v. Florida Dept. of Rev., 477 U.S. 1, 7-8 (1986). In *Wardair* the Supreme Court stated that:

[W]e have acknowledged the self-executing nature of the Commerce Clause and held on countless occasions that, even in the absence of specific action taken by the Federal Government to disapprove of state regulation that is contrary to the constitutional principle in ensuring that the conduct of individual States does not work to the detriment of the Nation as a whole, and thus ultimately to all of the States, may be invalid under the unexercised Commerce Clause.

*Id. at* 7-8.

87. *See, e.g., Wardair, 477 U.S. at* 7 (stating that "[i]n cases involving the so-called dormant Commerce Clause, both interstate and foreign, [where] [sic] the Federal Government has not affirmatively acted, and [sic] it is the responsibility of the judiciary to determine whether actions taken by state or local government unduly threatens the values the Commerce Clause was intended to serve").

Judicial branch decisions invalidating state measures under the "dormant" Commerce Clause are subject to a logical doctrinal caveat: since the Supreme Court is exercising Congressional power, Congress may respond to a Supreme Court decision invali-
2. Interstate Commerce Clause Review of State Taxation

The Interstate Commerce Clause promotes national economic integration among the states and curtails destructive interstate trade practices. The modern Interstate Commerce Clause framework was established by the Supreme Court in 1977 in Complete Auto Transit, Inc. v. Brady. In Complete Auto, a motor carrier engaged in the interstate transportation of automobiles challenged a Mississippi tax imposed on taxpayers for the privilege of engaging in the transportation business within the state. The Mississippi tax was measured by a business' gross receipts from such services. In analyzing whether the Mississippi tax violated the Commerce Clause, the Supreme Court, in a unanimous decision delivered by Justice Harry Blackmun, established that a state or local tax on exclusively interstate business

dating or allowing a state measure by subsequent legislation overturning the judicial determination. See NOWAK & ROTUNDA, supra note 80, § 8.1, at 274-75 (stating that "a necessary corollary to the right of the Court to interpret the sounds of silence . . . is the acknowledgment that Congress can respond to the Court's decision with subsequent legislation 'overturning' the effect of the Court's prior determination"); TRIBE, supra note 80, § 6.2, at 403-04 (stating that "[g]iven their origin as negative judicial inferences from a constitutional grant of power to Congress, the Supreme Court's doctrinal limitations on state interference are always subject to congressional revision").

88. See, e.g., Wardair, 477 U.S. at 7 (quoting Hughes v. Oklahoma, 441 U.S. 322, 325-26 (1979)). In Hughes the Supreme Court underscored the historical importance of the Commerce Clause in creating an integrated national economy:

The few simple words of the Commerce Clause . . . reflected a central concern of the Framers that was an immediate reason for calling the Constitutional Convention: the conviction that in order to succeed, the new Union would have to avoid the tendencies toward economic Balkanization that had plagued the relations among the Colonies and later among the states under the Articles of Confederation.

Id.; see also HARTMAN, supra note 17, § 2.1, at 14 (stating that "[t]he purpose of [the Commerce Clause] is to maintain and advance the idea of a national . . . economy, with the concomitant idea that state legislation, taxing as well as regulatory measures, runs afoul of the commerce clause, if the legislation creates an undue impediment to the operation of the economy"); NOWAK & ROTUNDA, supra note 80, § 8.1, at 275 (stating that "the rational of the Commerce Clause was to create and foster the development of a common market among the states, eradicating internal trade barriers, and prohibiting the economic Balkanization of the Union."); TRIBE, supra note 80, § 6.3, at 404 (stating that "[t]he Articles of Confederation had failed in large part because the states had waged destructive trade wars against one another . . . . Madison's prescription for economic matters affecting more than one state was to shift legislative authority over [commerce] to Congress").

90. Id. at 276.
91. Id. (citing Miss.Code Ann., § 10105 (1972 Supp.))
92. Id. (citing Miss.Code Ann., § 10109(2) (1972 Supp.))
was permissible provided it complied with four requirements. First, the tax applied to an activity with a substantial nexus to the taxing state. Second, the tax was fairly apportioned. Third, the tax did not discriminate against interstate commerce. Finally, the tax was fairly related to the services provided by the State. Finding that the challenged tax did not violate any of these four requirements, the Supreme Court dismissed Complete Auto’s Commerce Clause challenge. The Supreme Court has held that the Complete Auto test is implicated where a state tax threatens not only interstate commerce but international commerce as well.

3. Foreign Commerce Clause Review of State Taxation

At the international level, the Commerce Clause limits state taxes that threaten U.S. international commercial interests.

93. Complete Auto, 430 U.S. at 279.
94. Id.
95. Id.
96. Id. at 279. Under the first two Complete Auto requirements, a state tax affecting interstate commerce will not be sustained unless there is a: (1) a factual connection between the taxing state and the taxpayer's interstate activities, and (2) the measure of the tax fairly reflects the taxpayer's activities in the state.

Under the third Complete Auto requirement, states may not employ fiscal measures that impose a greater burden on out-of-state goods, activities, or enterprises than on competing in-state goods, activities, or enterprises. See, e.g., Northwestern States Portland Cement Co. v. Minn., 358 U.S. 450, 457 (1959) (stating that "no State, consistent with the commerce clause, may impose a tax which discriminates against interstate commerce . . . by providing a direct commercial advantage to local business"). State taxes may be invalidated under this anti-discrimination principle even if discrimination is unintentional. See, e.g., Halliburton Oil Well Cementing Co. v. Reily, 373 U.S. 64, 72 (1963) (deciding that even though "inequality in question [was] an accident of statutory drafting" Louisiana use tax violated anti-discrimination principle of interstate commerce clause).

The fourth and final requirement of the Complete Auto test has not been subject to much litigation, but it appears to be satisfied upon the provision of basic in-state services. See, e.g., Commonwealth Edison Co. v. Mont., 453 U.S. 609, 624 (1981) (requirement fulfilled when state provide taxpayer with "police and fire protection, the benefits of a trained workforce, and the advantages of a civilized society").

97. Complete Auto, 430 U.S. at 289.
99. Id. at 446-50. The U.S. Supreme Court has articulated the view that the scope of Congress's powers in the international commerce context exceed its interstate commerce powers, requiring a more extended judicial review of state measures touching upon the U.S.’s external commerce. See, e.g., Atlantic Cleaners & Dyers, Inc. v. United States, 286 U.S. 427, 434 (1932) (stating that "[i]n the Constitution, the power to regulate commerce is conferred by the same words of the commerce clause with respect both to foreign commerce and interstate commerce [and] yet the power when exer-
Review of state tax schemes burdening international commerce occurs under the Foreign Commerce Clause review of state taxation schemes established in 1979 in Japan Line, Ltd. v. County of Los Angeles. In Japan Line, the Supreme Court analyzed whether an ad valorem property tax imposed by the County of Los Angeles on containers, which were used exclusively in the transport of cargo in foreign commerce, violated the Commerce Clause. The containers were based in, registered, and subject to a property tax on their full value without apportionment by Japan. The Los Angeles tax was assessed by reference to the value of the containers on the tax lien date and their “average
Speaking for the majority, Justice Harry Blackmun indicated that state fiscal measures touching upon international commerce raised two concerns in addition to those addressed by the Complete Auto Interstate Commerce Clause test. First, the majority noted that in the international context, in contradistinction to the interstate context, no authoritative tribunal existed that could guarantee that cumulative tax burdens were fairly apportioned between competing tax jurisdictions where one of those jurisdictions was a sovereign state. Corporations subject to multiple taxation were, therefore, without any judicial remedy. Second, the Supreme Court pointed out that state taxation schemes could potentially interfere with and damage U.S. international commercial interests. Where state taxation policies deviated from parallel federal policies U.S. trading partners disadvantaged by a state tax might retaliate against U.S. corporations operating in their jurisdictions. In addition, state tax

103. Id. at 437.
104. Japan Line, 441 U.S. at 446 (citing Complete Auto Transit, Inc. v. Brady, 430 U.S. 274 (1977); see supra notes 88-99 and accompanying text (discussing Complete Auto Interstate Commerce Clause test)). Initially, the Supreme Court noted that had the containers been instrumentalities of purely interstate commerce, the Complete Auto test would apply and be satisfied and the Commerce Clause analysis would be at an end. Japan Line, 441 U.S. at 445. Because the containers were instrumentalities of foreign commerce, however "a more extensive constitutional inquiry [was] required." Id. at 446.
105. Japan Line, 441 U.S. at 447. The Supreme Court stated that:

[N]either this Court nor this nation can ensure full apportionment when one of the taxing entities is a foreign sovereign. If an instrumentality of commerce is domiciled abroad, the country of domicile may have the right, consistently with the custom of nations, to impose a tax on its full value. If a State should seek to tax the same instrumentality on an apportioned basis, multiple taxation inevitably results. Hence, whereas the fact of apportionment in interstate commerce means that "multiple burdens logically cannot occur," the same conclusion as to foreign commerce, logically cannot be drawn. Due to the absence of an authoritative tribunal capable of ensuring that the aggregation of taxes is computed on no more than one full value, a state tax, even through fairly apportioned to reflect an instrumentality's presence within the State, may subject foreign commerce to the risk of a double tax burden to which domestic commerce is not exposed, and which the commerce clause forbids.

106. Id.
107. Id. at 448.
108. Japan Line, 441 U.S. at 450. The Supreme Court stated that "[i]f a novel state
schemes having negative international consequences could also potentially interfere with the federal government's conduct of international commercial policy by preventing the federal government from dealing uniformly with other nations.109

The Supreme Court sought to protect these international concerns by prohibiting state taxes that, first, created an enhanced risk of multiple taxation110 and, second, prevented the federal government from speaking with "one voice" when regulating commerce with other countries.111 Thus, after Japan Line, a state tax implicating international commerce had to meet all four elements of the Complete Auto test as well as the additional two elements established in Japan Line to satisfy Commerce Clause requirements.112

The Supreme Court held that the Los Angeles tax violated both parts of the newly created Foreign Commerce Clause test.113 First, the tax not only created an enhanced risk of multiple taxation but resulted in multiple taxation in fact.114 Because the containers at issue were subject to property taxes to their full value in Japan, any additional taxation by Los Angeles would result in multiple taxation.115 Second, the Court decided that the Los Angeles tax violated the Japan Line "one voice" standard prohibition because it conflicted with the federal government's established tax policy with respect to containers used in international trade.116 The United States and Japan as signatory coun-

tax creates an asymmetry in the international tax structure, foreign nations disadvantaged by the levy may retaliate against American-owned instrumentalities present in their jurisdictions." Id. at 448. The Supreme Court stated that "(f)oreign commerce is pre-eminently a matter of national concern. In international relations and with respect to foreign intercourse and trade the people act through a single government with unified and adequate national power." Id. (citing Board of Trustees v. United States, 289 U.S. 48, 59 (1933)).

109. Id. at 448.
110. Id. at 446.
111. Id. at 448-49. The Supreme Court stated that "a court must . . . inquire, first, whether the tax . . . creates a substantial risk of international multiple taxation, and, second, whether the tax prevents the Federal Government from speaking with one voice when regulating commercial relations with foreign governments. If a state tax contravenes either of these precepts, it is unconstitutional under the Commerce Clause." Id. at 451.
112. Japan Line, 441 U.S. at 451; see also Hartman, supra note 17, § 2:17, at 88.
114. Id. at 451-52.
115. Id.
116. Id. at 452-53.
tries to the Customs Convention on Containers had agreed not to impose taxes or duties on containers temporarily present in their jurisdiction. The Los Angeles tax both conflicted with and frustrated this congressional policy and created an international asymmetry to Japan’s disadvantage.

C. Container Corporation of America v. Franchise Tax Board: *The Constitutionality of Worldwide Unitary Taxation in the U.S.-Parent MNC Case*

The *Japan Line* decision left open important questions relating to the scope of Foreign Commerce Clause doctrine. First, because the Supreme Court had invalidated the Los Angeles tax in *Japan Line* based on the existence of actual multiple taxation, it remained unclear whether the mere risk of multiple taxation also constituted sufficient grounds to invalidate state tax measures. Second, it also remained unclear whether Foreign Commerce Clause review extended beyond property taxation schemes such as those at issue in *Japan Line* to include other fiscal schemes such as state corporate income taxes.

In *Container Corporation of America v. Franchise Tax Board* the U.S. Supreme Court reviewed for the first time the constitutionality of worldwide unitary taxation under the Commerce Clause and addressed some of the questions left open in *Japan Line*. In *Container*, a U.S.-parent MNC incorporated in Delaware, headquartered in Illinois, and engaged in the business of manufacturing custom ordered paper-board packaging, brought a tax refund suit against the Franchise Tax Board of California ("FTBC") for the refund of additional franchise tax


119. HARTMAN, *supra* note 17, § 2:17, at 100.
120. *Id.*
121. *Id.* § 2:17, at 101.
123. *Container*, 463 U.S. at 163.
124. *Id.*
125. *Id.* at 171.
assessments levied against it for the 1963-1965 tax years. The Commerce Clause questions in Container’s challenge arose from the FTBC’s definition of Container’s unitary business to include its Latin American and European subsidiaries under California’s WWCR-based franchise tax scheme. Container contended that this inclusive characterization of its unitary business resulted in a violation of the Foreign Commerce Clause. By combining non-U.S. income in the state apportionable tax base, California’s tax scheme created a heightened risk of multiple taxation not present when combined apportionment was limited to the domestic context.

When addressing this first Japan Line inquiry, Justice William Brennan, speaking for the majority, reaffirmed the Supreme Court’s Japan Line position that multiple taxation in the international context implicated sensitive questions of international relations and sovereignty. The Supreme Court also reiterated its concern that taxpayers, who were subjected to international multiple taxation, had no recourse to judicial relief.

The Supreme Court, however, decided that judicial review of state taxes under the Japan Line multiple taxation framework needed to account for first, the context in which multiple taxation took place and second, other taxation schemes reasonably available to a taxing state. Applying this “context” and “op-

126. Id. at 174.
127. Id.
128. Id. at 185.
129. Id. at 189.
130. See supra notes 105-07 and accompanying text (discussing Japan Line multiple taxation test).
131. Container, 463 U.S. at 189. The Supreme Court reiterated its previous position that “[e]ven a slight overlapping of tax-a problem that might be deemed de minimis in a domestic context-assumes importance when sensitive matters of foreign relations and national sovereignty are concerned.” Id. (citing Japan Line, Ltd. v. County of Los Angeles, 441 U.S. 454, 456 (1979)).
132. Id. at 186. Justice Brennan stated:
Due to the absence of an authoritative tribunal capable of ensuring that the aggregation of taxes is computed on no more that one full value, a state tax, even when fairly apportioned to reflect an instrumentality’s presence within the State, may subject foreign commerce to the risk of double tax burden to which [domestic] commerce is not exposed and which the commerce clause forbids.

Id.
133. Id. at 189.
tions" overlay to the multiple taxation analysis, the Supreme Court, while conceding that California's franchise tax actually resulted in international multiple taxation, 134 held that because the tax was directed at net income the risk of multiple taxation could not be entirely eliminated under a separate accounting method, even if California were to adopt such a scheme. 135 The Supreme Court noted, however, that if a state taxation scheme inevitably led to multiple taxation, then grounds might exist to invalidate it under the Foreign Commerce Clause. 136

In addressing the second Japan Line requirement, 137 the Supreme Court stated that the "one voice" test required an examination of whether California's taxation scheme, first, implicated external policy issues that must be left to the federal government or, second, violated a clear federal policy. 138 The Court failed to find any especially harmful international implications of WWCR that might offend U.S. trading partners and lead them to retaliate. 139 Rather, the Supreme Court concluded that Cali-

134. Id. at 187.
135. Id. at 191. The U.S. Supreme Court, focusing on the general imprecision of any method for apportioning multijurisdictional income, noted that "[a]llocating income among the various taxing jurisdictions bears some resemblance . . . to slicing a shadow." Id. at 192. The Supreme Court further noted that:

"[E]ven though most nations have adopted the arm's-length approach in its general outlines, the precise rules under which they reallocate income among affiliated corporations often differ substantially, and whenever that difference exists, the possibility of double taxation also exists. Thus, even if California were to adopt some version of the arm's-length approach, it could not eliminate the risk of double taxation of corporations subject to its franchise tax, and might in some cases end up subjecting those corporations to more serious double taxation than would occur under formula apportionment."

Id. at 191. Because multiple taxation was as likely under WWCR as it was under the separate accounting method, the Court was unwilling to mandate "one allocation method that sometimes results in double taxation in favor of another allocation method that also sometimes results in double taxation." Id. at 193. Justice Brennan further stated that "[i]n the absence of a central coordinating authority, absolute consistency, even among taxing authorities whose basic approach to the task is quite similar, may just be too much to ask." Id. at 192.

137. Id. at 193-94.
138. Id. at 194.
139. Id. at 194-96. When analyzing whether California's WWCR based franchise might lead to retaliation by the U.S.'s trading partners, the Supreme Court stated:

"In considering this issue . . . we are faced with a distinct problem. This Court has little competence in determining precisely when foreign nations will be offended by particular acts, and even less competence in deciding how to balance a particular risk of retaliation against the sovereign right of the
fornia’s WWCR-based franchise tax merely had non-significant international resonances, and that as such it survived scrutiny under the one voice standard.\textsuperscript{40} In reaching its conclusion, the Court noted that the Executive Branch had failed to submit an \textit{amicus} brief in opposition to California’s franchise tax.\textsuperscript{41} The absence of such a submission reinforced the Supreme Court’s view that the external policy of the United States was not seriously threatened by California’s use of WWCR.\textsuperscript{42} The Court also failed to find any explicit federal policy prohibiting worldwide unitary taxation.\textsuperscript{43} Finally, the Court rejected Container’s argument that Congress was opposed to WWCR and had preempted states from using WWCR-based taxation. The Court found that the application of WWCR to domestic-parent MNCs was not fatally inconsistent with any federal policy.\textsuperscript{44} In upholding California’s worldwide unitary taxation scheme, the Supreme Court subjected its holding to one significant qualification. The Supreme Court declined to decide whether the application of worldwide unitary taxation to non-U.S. parent MNCs would sur-

\begin{enumerate}
\item United States as a whole to let the States tax as they please. The best that we can do, in the absence of explicit action by Congress, is to attempt to develop objective standards that reflect very general observations about the imperatives of international trade and international relations.

\textit{Id.} at 194. The Supreme Court concluded that three factors made it doubtful that international retaliation would be forthcoming: (1) an “automatic asymmetry” in international taxation was not the result of California’s franchise tax; (2) the incidence of the tax was ultimately borne by a domestic rather than a non-U.S. corporation; and (3) while other nations had a legitimate interest in reducing the tax burden of a domestic corporation, the petitioner-taxpayer was clearly amenable to state taxation, and the amount of that tax was more a function of California’s tax rate rather than its allocation method. \textit{Id.} at 194-95.

\item \textit{Container,} 463 U.S. at 194.

\item \textit{Id.} at 195.

\item \textit{Id.} at 196.

\item \textit{Id.} at 197. Thus, the Supreme Court, in reviewing the California tax scheme under one voice test, employed an explicit federal directive standards as well as a “more relaxed standard which [took] into account . . . [the Court’s] residual concerns about the foreign policy implications of California’s tax.” \textit{Id.}

\item \textit{Id.} at 197. In the Supreme Court’s view, the absence of prohibitory congressional intent was clear for three reasons: (1) U.S. bilateral income tax treaties, while requiring the federal government to use the “arm’s length” method to tax the U.S. income of non-U.S. parent MNCs, generally waive that requirement with respect to U.S. parent MNCs; (2) the federal tax statutes did not prohibit California from using worldwide unitary taxation; (3) the U.S. Senate, in considering a proposed tax treaty attached a reservation declining to give its consent to a provision that would have prohibited the use of worldwide unitary taxation by the states. \textit{Id.} at 196.
vive Foreign Commerce Clause review.\textsuperscript{145}

D. Wardair Canada, Inc. v. Florida Department of Revenue: Federal Acquiescence Preemption to State Taxation

Under “dormant” Commerce Clause doctrine federal government silence triggers judicial review of state tax schemes to determine whether they impermissibly burden commerce.\textsuperscript{146} Not all instances of federal government silence trigger “dormant” Commerce Clause analysis, however. Courts in certain circumstances have interpreted congressional inaction as intentional, and have read that inaction as acquiescence to a state tax scheme.\textsuperscript{147} In \textit{Wardair Canada, Inc. v. Florida Department of Revenue},\textsuperscript{148} the Supreme Court analyzed whether federal government silence on the issue of state taxation of aviation fuel constituted federal acquiescence to such taxation altogether precluding Foreign Commerce Clause analysis.\textsuperscript{149}

In \textit{Wardair}, Wardair Canada, a Canadian air carrier engaged exclusively in international travel, challenged a Florida sales tax on aviation fuel.\textsuperscript{150} Wardair Canada contended that the federal

\textsuperscript{145} \textit{Container}, 463 U.S. at 189 n.26. The Supreme Court stated that “[w]e have no need to address in this opinion the constitutionality of combined apportionment with respect to state taxation of domestic corporations with foreign parents or foreign corporations with either foreign parents or foreign subsidiaries.” \textit{Id.} The Supreme Court similarly noted later in its opinion that “[w]e recognize that the fact that the legal incidence of a tax falls on a corporation whose formal corporate domicile is domestic might be less significant in the case of a domestic corporation that was owned by foreign interests. We need not decide here whether such a case would require us to alter our analysis.” \textit{Id.} at 195 n.32.

\textsuperscript{146} See supra notes 81-87 and accompanying text (discussing operation of “dormant” Commerce Clause).


\textsuperscript{148} 477 U.S. 1 (1986).

\textsuperscript{149} Id. at 6 (citing \textit{Pacific Gas & Elec. Co. v. State Energy Resources Conservation and Dev. Comm’n}, 461 U.S. 190 (1983)). Under the preemption doctrine, if Congress has adopted a federal policy that occupies a field and expressly displaces a state law or, absent a conflict between state and federal policy, if Congress intends to preempt the specific field covered by a state law, then the state measure must be invalidated by the Supreme Court under the Supremacy Clause. \textit{Id.}; see supra notes 78-80 (discussing Supremacy Clause).

\textsuperscript{150} \textit{Wardair}, 477 U.S. at 3-4. Under a 1983 statute, Florida imposed a flat rate five percent fuel tax on a deemed price of US$1.148 per gallon on aviation fuel. \textit{Id.}
government had long-standing agreements with Canada\(^{151}\) and more than seventy other countries\(^{152}\) under which the signatories had agreed not to subject each other’s air carriers to excise taxes on aviation fuel.\(^{153}\) Florida’s actions, in Wardair Canada’s view, violated the Japan Line one voice standard by frustrating the operation of this federal taxation policy.\(^{154}\) None of the international agreements referred to by Wardair Canada, however, addressed the issue of state taxation of aviation fuel.\(^{155}\)

Justice William Brennan, speaking for the Supreme Court, rejected Wardair Canada’s argument that federal policy prohibited the imposition of state aviation fuel taxes.\(^{156}\) Rather, the Supreme Court concluded that the federal government’s failure to address the issue of subnational taxes on aviation fuel in its international aviation agreements constituted an affirmation of the states’ power to impose the tax.\(^{157}\) Thus, the Supreme Court concluded that the federal government, by remaining silent on the issue of state taxation of aviation fuel, had in practice affirmatively acquiesced to such taxation, making unnecessary a Foreign Commerce Clause analysis.\(^{158}\) The Supreme Court noted:

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\(^{152}\) Id. at 10.

\(^{153}\) Id. at 9-10.

\(^{154}\) Wardair, 477 U.S. at 9. Wardair Canada recognized that there was no threat of multiple taxation in its case since the fuel tax was imposed only upon the sale of fuel, a discrete transaction that occurred only within one jurisdiction. Id.

\(^{155}\) Id. at 11.

\(^{156}\) Id. at 9.

\(^{157}\) Id. at 12. The U.S. Supreme Court examined the international aviation agreements specified by Wardair Canada and noted that they contained notable omissions on the state aviation tax issue, and thus supported an inference of affirmative congressional acquiescence to such taxation: for example (1) the Federal Aviation Act, while regulating aviation extensively, nevertheless expressly permitted states to impose the type of taxation in question, id. at 7 (noting that § 1513(b) of Federal Aviation Act, 49 U.S.C. app. § 1513 (addressing issue of “State Taxation of Air Commerce” expressly permits “state or use taxes on the sale of goods and services”); (2) the US-Canada international aviation agreement did not deny the states the power to tax purchases of aviation fuel, id. at 6-7; and (3) the federal government had enacted more than 70 international aviation agreements, none of which contained provisions limiting taxation of aviation fuel by state and local governments, id. at 11.

\(^{158}\) Wardair, 477 U.S. at 12. The Supreme Court stated:

What all of this makes abundantly clear is that the Federal Government has not remained silent with regard to the question whether States should have the power to impose taxes on aviation fuel used by foreign carriers in international travel. By negative implication . . . the United States has at least acquiesced in state taxation of fuel used by foreign carriers in international
that while the federal government held an aspiration to eliminate impediments to international air travel, the law as it stood did not prohibit the taxation of aviation fuel by the states.  

II. BARCLAYS BANK PLC v. FRANCHISE TAX BOARD OF CALIFORNIA

In Barclays Bank PLC v. Franchise Tax Board of California, the Supreme Court analyzed the reserved issue it had declined to answer eleven years earlier in Container regarding worldwide unitary taxation. The issue before the Supreme Court in Barclays was whether California's use of WWCR-based taxation to calculate state franchise tax liabilities of non-U.S. parent MNCs with in-state subsidiaries violated the Interstate and Foreign Commerce Clauses. The Supreme Court concluded, first, that California's use of worldwide unitary taxation did not constitutionally discriminate against non-U.S. parent MNCs and thus did not violate the Interstate Commerce Clause. The Supreme Court concluded, second, that the California's use of WWCR-based taxation did not violate Foreign Commerce Clause prohibitions against multiple taxation or interfere with the federal government's conduct of international commerce.

A. The Factual Background in Barclays

In Barclays, Barclays Bank PLC ("Barclays") brought a tax refund suit in California state court to recover additional travel... It would turn dormant Commerce Clause analysis entirely upside down... to apply it in such a way as to reverse the policy that the Federal Government has elected to follow. For the dormant Commerce Clause, in both its interstate and foreign incarnations, only operates where the Federal Government has not spoken to ensure that the essential attributes of nationhood will not be jeopardized by States acting as independent economic actors.

Id. at 10.

159. Id. at 10.
161. Id. at 2271; see supra notes 132-47 (discussing Container reservation by Supreme Court as to constitutionality of applying worldwide unitary taxation to non-U.S. parent MNCs).
162. Id. at 2272.
163. Id. at 2276-77.
164. Id. at 2281, 2285.
165. Barclays IV, 114 S. Ct. at 2274. The tax refund suits were initially brought in California state court by Barclays Bank of California ("Barcal") and Barclays Bank International ("BBI"). Id. at 2274. In 1977, Barcal was a California banking corporation
franchise tax\textsuperscript{166} assessments levied against it by the Franchise Tax Board of California ("FTBC") for the 1977 tax year.\textsuperscript{167} The refund suit arose from the FTBC's rejection of Barclays' characterization of unitary business to include only its California operations.\textsuperscript{168} The FTBC, after determining that under the California WWC\textsuperscript{R}-based franchise tax statute\textsuperscript{169} Barclays' California subsidiaries, together with its U.K.-based parent, Barclays Bank Limited,\textsuperscript{170} and related worldwide affiliates, was part of a single unitary business, the Barclays Group,\textsuperscript{171} applied California's three

wholly owned by Barclays Bank International. Barclays Bank Int'l Ltd. v. Franchise Tax Bd., 275 Cal. Rptr. 626, 639 (Ct. App. 1990), \textit{rev'd}, 829 P.2d 279 (Cal. 1992), \textit{cert. denied}, 113 S. Ct. 202 (1992) [hereinafter \textit{Barclays I}]. The California Supreme Court remanded the Barclays matter to the California Court of Appeal for further consideration. Barclays Bank Int'l Ltd. v. Franchise Tax Bd., 14 Cal. Rptr. 2d 537 (Ct. App. 1992), \textit{aff'd}, Barclays Bank PLC v. Franchise Tax Bd., 114 S. Ct. 2278 (1994). BBI in 1977 was a U.K. corporation doing business directly or through subsidiaries in approximately 55 countries. \textit{Barclays I}, 275 Cal. Rptr. at 639. BBI had an interest for California unitary group purposes in more than 70 subsidiaries operating in approximately 34 countries outside the United Kingdom. \textit{Id}. The petitioner-taxpayer in the U.S. Supreme Court litigation was Barclays Bank PLC ["Barclays"], the U.K.-based successor-in-interest to the tax refund claims of Barcal and BBI, the plaintiffs in the California state court litigation. \textit{Barclays IV}, 114 S. Ct. at 2275 n.7. This Comment refers to the plaintiff-taxpayers throughout its discussion of the Barclays cases, both in state and federal court, as "Barclays.”

\textit{Barclays IV}, 114 S. Ct. at 2274-75.

\textit{Barclays IV}, 114 S. Ct. at 2274. In computing its California franchise taxes for the 1977 income year, Barcal reported only the income from its own operations in California. \textit{Id}. BBI reported income based on the assumption that it was part of a unitary business composed of itself and its subsidiaries, but not its parent corporation and the other subsidiaries of its parent corporation. \textit{Id}.

\textit{Barclays I}, 275 Cal. Rptr. at 626 (citing \textit{CAL. REV. & TAX. CODE}, § 25101 (West 1977)). In 1977 California’s worldwide unitary taxation statute provided in pertinent part:

When the income of a taxpayer subject to the tax imposed under this part is derived from or attributable to sources both within and without the state the tax shall be measured by the net income derived from or attributable to sources within this state in accordance with the provisions of Article 2.

\textit{Id}.


\textit{Barclays IV}, 114 S. Ct. at 2274. Altogether the Barclays Group comprised more than 220 separate entities engaged in business activities in approximately 60 countries. \textit{Barclays I}, 275 Cal. Rptr. at 640. In 1977 approximately 1.5% of the income of the Barclays Group worldwide was generated in California. \textit{Id}.

Thus, over 98% of the Barclays Group’s income in 1977 had its source outside the United States. \textit{Id}.
factor apportionment formula to establish Barclays' in-state income tax base.\textsuperscript{172} Based on these calculations the FTBC assessed additional taxes amounting to US$154,098.\textsuperscript{173} Barclays' primary claim was that the application of California's franchise tax to non-U.S. parent MNCs violated the Foreign Commerce Clause.\textsuperscript{174} Additionally, Barclays claimed that WWCR imposed inordinate compliance costs on specifically non-U.S. parent MNCs, and thereby violated the anti-discrimination prohibition of the Interstate Commerce Clause.\textsuperscript{175} Barclays prevailed on both its Interstate and Foreign Commerce Clause arguments in California Superior Court, thus invalidating California's use of worldwide unitary taxation for determining franchise tax liabilities of non-U.S. parent MNCs.\textsuperscript{176}

B. The California Court of Appeal Decision

In reviewing the California Superior Court's decision, the California Court of Appeal for the Third District ("Court of Appeal") addressed the FTBC's threshold argument that dormant Commerce Clause analysis was preempted by the existence of a federal policy allowing WWCR based taxation.\textsuperscript{177} The FTBC pointed to several examples of federal conduct on the WWCR issue that demonstrated an affirmative federal policy to allow WWCR-based taxation.\textsuperscript{178} The Court of Appeal rejected this ar-

\textsuperscript{172} Barclays IV, 114 S. Ct. at 2273.
\textsuperscript{173} Id.
\textsuperscript{174} Id. at 2279. Barclays conceded from the outset of the litigation that together with its U.K. parent and affiliates it constituted a unitary business. Id. at 2274-75.
\textsuperscript{175} Barclays IV, 114 S. Ct. at 2277.
\textsuperscript{177} Barclays I, 275 Cal. Rptr. at 634.
\textsuperscript{178} Id. The FTBC pointed to five factors that supported its argument that Congress had affirmatively acquiesced to the states' use of WWCR: (1) the failure of U.S. bilateral income tax treaties to consider state taxes except in nondiscrimination clauses; (2) the absence of specific requirements in U.S. Friendship, Commerce, and Navigation Treaties ("FCN" Treaties) that the states use a particular method of tax accounting; (3) actions by the Executive Branch, including the adoption of a Model Income Tax Treaty and the reservation of its position in the Organization of Economic Cooperation and Development's Model Convention with respect to subnational taxes; (4) the absence of Congressional legislation prohibiting or restricting the use of WWCR to non-
argument on the grounds that the specified federal actions demonstrated only a general policy by the federal government of non-interference in state taxation and a desire to preserve the principle of state sovereignty.179

Having overcome the preemption hurdle, the Court of Appeal next addressed whether the application of WWCR to non-

U.S. parent MNCs; and (5) the U.S. Senate's removal of Article 9(4) in the Convention Between United States and United Kingdom for Avoidance of Double Taxation, Dec. 31, 1975, 31 U.S.T. 5670, 5677, T.I.A.S. No. 9682 [hereinafter U.S.-U.K. Tax Treaty], which would have prohibited the states' application of WWCR to U.K.-based corporate groups. Id.

179. Id. The California Court of Appeal ["Court of Appeal"] reasoned that the first three factors pointed to by the FTBC did not sufficiently translate into an affirmation of a particular type of taxation for three reasons: (1) since most U.S. bilateral income tax treaties antedated the WWCR methodology, Congress could not have been aware of the WWCR methodology when it ratified those treaties and, therefore, could not by "negative implication" have acquiesced to its use; (2) non-discrimination clauses in U.S bilateral income tax treaties, like those in FCN treaties, simply reflected a general principle that a state cannot tax a non-U.S. business more than it taxes domestic businesses and did not sufficiently translate into an affirmation of a particular type of taxation; and (3), none of the U.S. bilateral income tax treaties, with the exception of the US-U.K Tax Treaty specifically dealt with the issue of unitary taxation or the use of WWCR by subnational units. Id. at 634-36. The Court of Appeal concluded that:

The [FTBC's] approach is simply too general and ignores the historical context in essentially arguing that when a treaty is limited to national taxes or fails to discuss a particular taxation method, a conscious decision has been made to allow states to tax in any manner they please. Common sense charts a different course while respecting the broad power of a state to tax.

Id. The Court of Appeal rejected the FTBC's more concrete argument that the U.S. Senate's removal of Article 9(4) in the U.S.-U.K. Tax Treaty constituted an affirmative federal policy to allow WWCR because such a conclusion would be "reading too much into too little." Id. The Court of Appeal reasoned that the U.S.-U.K. Tax Treaty with the prohibitory provision included had the support of the Senate majority since it failed to receive the requisite two-third majority by only five votes. Id. at 636-37.

The Court of Appeal also compared the treaty analysis in Wardair with the arguments put forward by the FTBC. Id. at 635; see supra notes 158-61 (discussing Supreme Court's treaty analysis in Wardair). In contrast to its general treatment of WWCR by the federal government, the Court of Appeals highlighted the specific and concrete treatment of aviation fuel taxation by the federal government. Id. The Court of Appeal pointed out that the state aviation fuel taxes at issue in Wardair had been discussed in the Chicago Convention on International Civil Aviation, Dec. 7, 1944, 15 U.N.T.S. 295, T.I.A.S. No. 1591, and a Nov. 14, 1966 Resolution of the International Civil Aviation Organization, well before the more than 70 international aviation agreements which the United States had entered into were negotiated. Id. Therefore "[t]he American government and the international community were . . . negotiating these agreements with a keen awareness of the tax involved in Wardair." Id. The Court of Appeal concluded its pre-emption analysis by noting that "in trying to assign a specific reason to legislative inaction, we must enter the realm of pure speculation" and "find[ing] meaning in legislative silence [was] about as difficult as hearing sound in a vacuum." Id. at 636.
U.S. parent MNCs violated the Foreign Commerce Clause. The Court of Appeal decided that because multiple taxation in the non-U.S. parent context was not the inevitable outcome of WWCR and resorting to the separate accounting method would not entirely eliminate double taxation, California's tax did not violate the first requirement. The Court of Appeal concluded, however, that the application of WWCR to non U.S.-parent MNCs posed a significant threat to U.S. international commercial interests and violated the one voice test. Examining the international ramifications of WWCR, the Court of Appeal found that worldwide unitary taxation had offended U.S. trading partners and had created a danger of retaliation against U.S. businesses overseas. The Court

180. Barclays I, 275 Cal. Rptr. at 645.
181. Id. at 687.
182. Id. The Court of Appeal stated that there was no "constitutionally significant differences between domestic-based and foreign-based multinational corporations concerning the enhanced risk of multiple taxation: in neither case is double taxation inevitable." Id.; see supra notes 120-47 and accompanying text (discussing Supreme Court's Container decision).
183. Id.  id.
184. Id.
185. Barclays I, 275 Cal. Rptr. at 637-38. The Court of Appeal pointed to the significant number of protests the United States had received from its trading partners regarding the states' use of worldwide unitary taxation. Id. at 638. In addition, the Court of Appeal noted that in 1985 the United Kingdom had initiated retaliatory legislation designed to withdraw tax advantaged for any U.S. businesses operating in the U.K. and based in a WWCR state. Id. The Court of Appeal also concluded that retaliation against the United States was likely under the three factors identified in Container for analyzing the likelihood of international countermeasures. Id.; see supra note 141 (discussing three factors specified in Container for determining likelihood of international retaliation against state fiscal measure). First, the application of WWCR to non-U.S. parent MNCs created an automatic asymmetry in international taxation operating to the non-U.S. parent MNC's disadvantage. Barclays I, 275 Cal. Rptr. at 638. An international asymmetry existed for two reasons: (1) because no other country in the world used WWCR, domestic-parent MNCs did not face the taxation method abroad; and (2) the compliance burden imposed on non-U.S. parent MNCs doing business in states using WWCR disproportionately affected non-U.S. businesses. Id. Second, the Court of Appeal determined that the legal incidence of California's WWCR-based franchise tax was borne by a non-U.S. rather than a domestic parent MNC. Id. at 638-39. Finally, the Court of Appeal found that it was the application of unitary taxation, not the unitary tax rate itself, that imposed the compliance burden on non-U.S. corporate groups. Id. at 639. The Court of Appeal noted that non-U.S. parent MNCs incurred a significantly greater burden than domestic corporations in complying with California's WWCR
of Appeal also found that California’s application of WWCR to non U.S.-parent MNCs violated a federal directive barring the states from using WWCR as pronounced by the executive branch.\(^\text{186}\) While noting that no explicit congressional policy existed on this issue, in the Court of Appeal’s view, consistent Executive Branch opposition to the application of worldwide unitary taxation to non-U.S.-parent MNCs provided the necessary federal directive.\(^\text{187}\)

scheme because non-U.S. multinationals often did not keep their records in English, U.S. currency, or in accord with U.S. accounting principles. Id. In addition, non-U.S. parent MNCs often incurred substantial costs in obtaining the necessary financial information and translating it into WWCR-compatible format. Id. Citing testimony from the trial record, the Court of Appeal noted that it would cost Barclays between US$6.4-7.7 million to establish an accounting system that satisfied California’s WWCR requirements, and between US$2-3.8 million a year to maintain the system. Id. The Court of Appeal finally concluded that:

> In contrast to Container then, we do not have to speculate on whether the taxation method at issue may offend our foreign trading partners and lead them to retaliate against the nation as a whole. They are offended; they have retaliated. And the three general factors identified in Container that might justifiably lead to significant retaliation . . . are all present in this case.

Id. at 640-41.

186. Barclays I, 275 Cal. Rptr. at 641-42. The Court of Appeal relied on Justice Jackson’s tripartite framework established in Youngstown Sheet & Tube Co. v. Sawyer, 343 U.S. 579 (1952), to overcome the constitutional problem inherent in establishing the existence of a federal policy by reference to Executive Branch pronouncements. Id. at 642-43. While noting that the U.S. Constitution explicitly granted Congress the foreign commerce power, under the Youngstown framework, "[w]hen the President acts in absence of either a congressional grant or denial of authority, he can only rely upon his own independent powers, but there is a zone of twilight in which he and Congress may have concurrent authority." Id. at 643 (citing Youngstown, 343 U.S. at 636-38). The Court of Appeal further noted that "congressional inertia, indifference or quiescence may sometimes . . . enable, if not invite, measures on independent presidential responsibility," and "[i]n this area, any actual test of power is likely to depend on the impertives of events and contemporary imponderables rather than on abstract theories of law." Id. The Court of Appeal determined that the Executive Branch’s actions on the WWCR controversy aligned themselves with this second category of Justice Jackson’s framework. Id. Given the historic recognition in American constitutional jurisprudence that the executive branch possessed extensive power in the foreign relations field, combined with the need for "swift and effectual national power" in this era of changing economic conditions, the Court of Appeal concluded that the Executive Branch’s position on WWCR was entitled to the full weight of a federal policy. Id. at 643-44.

187. Id. at 642. The Court of Appeal pointed to a number of actions by the Executive Branch supporting its conclusion that the federal government opposed the states’ use of WWCR in the international context: (1) the Treasury Department, the executive organ that formulated federal tax policy, had undertaken several studies in which it had concluded that WWCR should not be applied to non-U.S. parent corporate groups; (2) Executive Branch opposition to the application of WWCR had remained constant...
C. The California Supreme Court Decision

On appeal to the California Supreme Court, Justice Arabian, in a unanimous decision, reversed the Court of Appeal and resurrected California's worldwide unitary taxation scheme. After reviewing the U.S. Supreme Court's principal Foreign Commerce Clause cases, the California Supreme Court concluded that during the 1980's the scope of this doctrine had been significantly narrowed by the Court. This more restricted application of the Foreign Commerce Clause doctrine, the California Supreme Court opined, was primarily the result of the U.S. Supreme Court's Wardair decision and reflected the Court's heightened sensitivity to congressional pronouncements on external policy issues.

Following the Wardair precedent, the California Supreme Court decision stated that:


190. Id. at 290. The California Supreme Court stated that:

The fact is... that dormant foreign commerce clause... jurisprudence has evolved in the nine years since Container was decided, an evolution that, as we parse the cases, has reoriented the doctrine. That development has reduced the scope for a dormant analysis and makes its invocation here particularly inappropriate.

191. Id. at 293. The California Supreme Court stated that:

We are confident that the overarching significance of Wardair lies in its explicit limitation on when a dormant foreign commerce clause analysis is appropriate, its affirmation that the analysis "only operates where the Federal Government has not spoken," and its statement that the court has "never suggested that the Foreign Commerce Clause insists that the Federal Government speak with any particular voice."

192. Barclays II, 829 P.2d at 290-293. The California Supreme Court decided that the scope of dormant Foreign Commerce Clause doctrine was curtailed in Wardair because the interpretive framework established in that case for adducing from congressional pronouncements the existence of the kind of governmental silences foreclosing
Court examined congressional actions on the worldwide unitary taxation issue. First, the California Supreme Court noted that the U.S. Senate in 1978 had rejected the U.K.-U.S. Tax Treaty, whose centerpiece, Article 9(4), prohibited the states from using worldwide unitary taxation to calculate the income tax liabilities of U.K. MNCs. Only after Article 9(4) was removed by amendment, the California Supreme Court emphasized, was the requisite two-thirds majority necessary to ratify the U.S.-U.K. Tax Treaty obtainable. Second, the California Supreme Court pointed out that over twenty U.S. House and Senate bills had been introduced into Congress during a twenty-year period to curtail the states' use of worldwide unitary taxation, none of which had been enacted into law. Finally, the California Supreme Court highlighted that while U.S. bilateral income tax treaties generally required the federal government to use the separate accounting method in its tax treatment of domestic dormant analysis reflected a "heightened judicial attentiveness to expressions of congressional foreign policy." 

193. Id. at 295 (quoting Convention Between United States and United Kingdom for Avoidance of Double Taxation, Dec. 31, 1975, 31 U.S.T. 5670, 5677, T.I.A.S. No. 9682, at 10). Prior to its amendment, Article 9(4) of the U.S.-U.K. Tax Treaty stated that:

Except as specifically provided in this Article, in determining the tax liability of an enterprise doing business in a Contracting State, or in a political subdivision or local authority of a Contracting State, such Contracting State, political subdivision or local authority shall not take into account the income, deductions, receipts, or outgoings of a related enterprise of the other Contracting State or of an enterprise of any third State related to an enterprise of the other Contracting State.

Id. (quoting art. 9(4), 31 U.S.T. at 5677, T.I.A.S. No. 9682, at 10).

194. Id. at 295 (quoting 124 Cong. Rec. 18,416 (1978)). The congressional debate stated that "the provisions of paragraph (4) of Article 9... shall not apply to any political subdivision or local authority of the United States." Id. The California Supreme Court rejected the Court of Appeal's argument that an affirmative congressional intent to preserve worldwide unitary taxation could not be inferred from the U.S. Senate's rejection of the U.S.-U.K. Tax Treaty without the reservation, because it failed by only five votes to garner the necessary two-thirds majority. Id. at 296; see supra note 181 (discussing Court of Appeal reasoning as to U.S.-U.K. Tax Treaty). In the California Supreme Court's view:

Preliminary voting tallies lack meaning precisely because they are not definitive, may be cast for any number of tactical parliamentary reasons, and thus do not reliably reflect legislative policy. The sole constitutional mechanism for congressional consideration of executive-negotiated treaties is Senate ratification by a two-thirds majority...; to that defining vote, institutional significance sensibly can and should be ascribed.

Barclays II, 829 P.2d at 296.

195. Id.
branches of non-U.S. businesses, the same requirement did not apply to taxation methods used by political subdivisions.\textsuperscript{196} Many of these same tax treaties also contained non-discrimination provisions that were explicitly binding on subnational organs.\textsuperscript{197} By negative implication the California Supreme Court surmised that a limited ban of some aspects of taxation combined with inclusion as to other aspects of tax treatment demonstrated that Congress had adopted a policy of curtailing only some aspects of state fiscal power while implicitly preserving others.\textsuperscript{198} In light of this congressional conduct the California Supreme Court concluded that Congress by negative implication had affirmatively allowed the states to use WWCR-based taxation, fully precluding a Commerce Clause analysis.\textsuperscript{199}

\begin{itemize}
\item \textsuperscript{196} Id. at 298.
\item \textsuperscript{197} Id.
\item \textsuperscript{198} Barclays II, 829 P.2d at 295-98. The California Supreme Court rejected the Court of Appeal's conclusion that U.S. bilateral income tax treaties did not demonstrate congressional acquiescence to the state's use of WWCR. Id. at 297. In the California Supreme Court's view, the Court of Appeal had erroneously concluded that such income tax treaties could not, by negative implication, demonstrate congressional affirmation of WWCR because when they were adopted, diplomatic and international circles were not aware of the WWCR methodology. Id. According to the California Supreme Court, international financial and diplomatic circles were fully cognizant of WWCR from at least the mid-1950's, well before the multinational corporate boom and the surge in unitary tax litigation of the 1970's. Id. This conclusion was evident from the number of unitary taxation cases adjudicated in the 1950's, a 1956 federal tax statute authorizing the use of unitary taxation in the international context, and explicit references in U.S. bilateral income tax treaties entered into in the 1940's. Id.
\item \textsuperscript{199} Id. at 294. The California Supreme Court concluded its opinion by stating that:

\begin{quote}
It is clear that federal limitations on the states' use of worldwide formula apportionment is a controversial political and economic issue of which Congress has long been aware. In light of the history, we cannot turn away from the substantial evidence of Congress's repeated refusal to intervene in the regulation of state division of income methods for tax purposes, even one that provokes continuing international complaint. Under the compulsions of established constitutional doctrine, the courts sometimes are required to divine what foreign commerce policy Congress would pursue in the absence of any indication that it has thought about the subject; it is a quite different matter, however, for a court to ignore a pattern of congressional action that evidences both an awareness of an issue and a refusal to adopt the remedy urged upon it by executive officials and resisted by its state constituencies. The latter, we believe, viewed in context alongside additional treaty materials, is a governmental silence that is eloquent.

In light of Congress's awareness of antagonistic state taxation and international business interests, the path taken by the high court in [Wardair] seems the constitutionally correct one here. To invest a paper trail of executive aspiration with the dignity of a clear federal directive would . . . "turn dormant
The California Supreme Court remanded the case to the Court of Appeal for further proceedings on Barclays' additional constitutional challenges predicated on the Interstate Commerce Clause. On remand the California Court of Appeal found that the application of WWCR-based taxes to non-U.S. parent MNCs did not violate the Interstate Commerce Clause. The Court of Appeal thus upheld California's use of worldwide unitary taxation in the non-U.S. parent context.

D. The United States Supreme Court Decision

On June 20, 1994, the U.S. Supreme Court delivered its decision in Barclays Bank PLC v. Franchise Tax Board of California. The Supreme Court, in a seven-to-two decision written by Justice Ruth Bader Ginsburg, held that the application of WWCR to non-U.S. parent MNCs did not violate either the Interstate or the Foreign Commerce Clauses. California's use of WWCR to calculate franchise tax liabilities for non-U.S. parent corporations was therefore found to be constitutional. Justices Harry Blackmun and Antonin Scalia filed concurring opinions. Justices Blackmun and Scalia's concurrence criticized the court's approach, stating: "Taking our lead from the high court, we decline to adjudicate on dormant foreign commerce clause grounds a debate between the political branches of the federal government over what is...a sharply contested issue of national tax policy that has been repeatedly aired before Congress. We adhere to the central meaning of the high court's opinion in Wardair in holding that Congress's refusal to legislate restrictions on state use of worldwide formula apportionment is not the sort of governmental silence that triggers a dormant foreign commerce clause analysis." (Id. at 300 (quoting Wardair Canada, Inc. v. Florida Dept. of Rev., 477 U.S. 1, 12 (1986))).

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200. Id. at 300.
202. Id.
203. U.S. __, 114 S. Ct. 2268 (1994). The case went before the U.S. Supreme Court on a writ of certiorari to the California Court of Appeal, __ U.S. __, 114 S. Ct. 379 (1993). A companion case, Colgate-Palmolive Co. v. Franchise Tax Bd., __ U.S. __, 114 S. Ct. 2268 (1994), which also involved constitutional challenges against California's use of WWCR by a U.S.-parent MNC, was consolidated and heard jointly with the Barclays IV petition. Id. at 2275. This Comment does not discuss the Colgate litigation in the U.S. Supreme Court.

204. See supra note 145 and accompanying text (discussing reservation by Supreme Court as to constitutionality of WWCR when applied to non-U.S. parent MNCs in Container).
205. Barclays IV, 114 S. Ct. at 2272, 2285.
206. Id. at 2286-87.
practice Sandra Day O'Connor, joined by Justice Clarence Thomas, filed an opinion concurring in part and dissenting in part.207

1. The Majority Opinion

Barclays first claimed that the application of worldwide unitary taxation to non-U.S. parent MNCs violated the non-discrimination principle of the Interstate Commerce Clause.208 Barclays argued that in complying with California's WWCR-based franchise tax scheme, non-U.S. parent MNCs were subjected to a prohibitive burden209 converting non-U.S. financial and accounting records for their international operations into U.S. language, currency, and accounting principles.210 U.S. taxpayers, who already maintained their records in WWCR-compatible format, did not bear an analogous hardship.211 This unequal compliance burden operated in substance as economic protection for U.S.-owned corporations in contravention of the anti-discrimination principle of the Interstate Commerce Clause.212

While reaffirming the principle that state-imposed compliance burdens falling disproportionately on out-of-state and non-U.S. entities violated the Interstate Commerce Clause,213 the majority found that the factual predicates of the Barclays' claim did not establish a constitutional violation.214 The Supreme Court reasoned that while California's franchise tax reporting requirements could potentially discriminate against non-U.S parent corporations,215 actual compliance costs were mitigated by Califor-
nia's provision for the use of "reasonable approximations" where the required data could not be developed from standard financial records. Because Barclays had computed its worldwide income based on such "reasonable approximations," the large compliance costs of which it complained were avoided. As Barclays had not in fact suffered an inordinate burden in complying with California's WWCR system, the Supreme Court held that no unconstitutional discrimination had occurred.

The Supreme Court next proceeded to Barclays' Foreign Commerce Clause arguments. The Foreign Commerce

profit and loss statement... for each foreign branch or corporation;" (2) the "consolidated profit and loss statement prepared for the related corporations of the which the unitary business is a member which is prepared for filing with the Securities and Exchange Commission;" or (3) "the consolidated profit and loss statement of the prepared for reporting to shareholders and subject to review by an independent auditor." Id. at 2278 n.12.

216. Id. at 2278. California regulations implementing the state's WWCR scheme provided that the Franchise Tax Board "shall consider the effort and expenses required to obtain the necessary information," and in "appropriate cases, such as when the necessary data cannot be developed from the financial records maintained in the regular course of business," may accept "reasonable approximations." Id. (citing CAL.CODE REGS. tit. 18, § 25137-6(e)(1)).

217. Id.

218. Id. (citing Barclays III, 14 Cal. Rptr. 2d at 548 n.9). The Court of Appeal found that Barclays' actual compliance costs were on average between US$900 and US$1250 per annum for the years immediately preceding the 1977 tax-year. Id. at 2278 n.15 (citing Barclays III, 14 Cal. Rptr. 2d at 548 n.9).

219. Barclays IV, 114 S. Ct. at 2278. Barclays additionally argued that even if the allowance of "reasonable approximations" mitigated the discriminatory operation of California's reporting requirements, the "reasonable approximations" method was unconstitutional. Id. Specifically, since no substantive criteria were specified for determining which approximations would be accepted by the FTBC, the grant of standardless discretion violated Due Process. Id. (citing Brief for Barclays Bank PLC, at 49, Barclays IV (No. 92-1384)). The majority rejected this argument on the grounds that California tax officials did not in fact exercise arbitrary authority: because (1) California courts had construed the California law to limit the discretion of the FTBC by requiring the FTBC to "consider regularly-maintained or other readily-accessible[e] corporate documents in deciding whether the cost and effort of producing [worldwide combined reporting] information justifie[d] submission of reasonable approximations," id. (quoting Barclays III, 14 Cal. Rptr. 2d at 549; (2) Barclays had the opportunity to resort to administrative procedures by which "to clarify the meaning of the regulation[s] by its own inquiry, or by resort to an administrative process," id. (quoting Hoffman Estates v. Flipside, Hoffman Estates, Inc., 445 U.S. 489, 498 (1982)); and (3) taxpayers could seek under the California regulations a determination in advance as to the tax consequences of a proposed course of action, id. at 2279 (citing CAL.CODE OF REGS., tit. 18, § 25137(e)(2) (1985)).

220. Id. at 2279; see supra notes 100-19 and accompanying text (discussing Foreign Commerce Clause).
Clause required the Supreme Court to determine, first, whether the application of California's franchise tax to non-U.S. parent MNCs created an enhanced risk of multiple taxation.\footnote{Barclays IV, 114 S. Ct. at 2279.} Barclays sought to distinguish its case as a non-U.S. parent MNC from that of U.S. parent MNCs with respect to the multiple taxation issue.\footnote{Id.} Barclays argued that non-U.S parent MNCs typically had a larger percentage of their operations and affiliates outside the United States when compared to U.S.-parent MNCs,\footnote{Id. at 2279.} and consequently, a larger proportion of a non-U.S. parent MNC's income was subject to taxation in other countries.\footnote{Id. (citing Brief for Barclays Bank PLC, at 33, Barclays IV (No. 92-1384)).} Thus, in Barclays' view, by forcing non-U.S. parent MNCs to include their worldwide income under its franchise tax reporting requirements, California's tax exposed non-U.S. parent MNC's to a more aggravated risk of multiple taxation than U.S. parent MNCs.\footnote{Id. (citing Brief for Barclays Bank PLC, at 92-93, Barclays IV (No. 92-1384)).} Barclays additionally argued that because California wage rates, property values, and sales prices were on average higher than corresponding values in other countries where it conducted business, California's apportionment formula operated to allocate a higher proportion of income to the state, which resulted in multiple taxation.\footnote{Barclays IV, 114 S. Ct. at 2279.}

In analyzing the multiple taxation issue, the Supreme Court affirmed the analytical framework for analyzing multiple taxation issues it had developed earlier in Container.\footnote{Id. at 2280 n.18. The Court recognized that its decision in Container, "effectively modified, for purposes of income taxation, the Commerce Clause multiple taxation inquiry described in Japan Line." Id.; see supra notes 121-38 and accompanying text (discussing Container decision and its analysis of the double taxation issue).} The Court rejected Barclays' arguments that the application of worldwide unitary taxation to non-U.S. parent MNCs led to unconstitutional multiple taxation on the grounds WWCRR did not inevitably result in multiple taxation,\footnote{Barclay IV, 114 S. Ct. at 2280.} and because no alternatives reasonably available to California existed that dispositively lessened the risk of multiple taxation.\footnote{Id. The majority opinion stated: \[Container's\] holding on multiple taxation relied on two considerations: first, that multiple taxation was not the inevitable result of the California
The Supreme Court next addressed the federal preemption issue and the "one voice" inquiry.\textsuperscript{230} The majority, unable to discern any specific indications of congressional intent barring WWCR,\textsuperscript{231} concluded that Congress had not preempted California's worldwide unitary taxation scheme.\textsuperscript{232} First, the Court noted that in the eleven years since its \textit{Container} decision, Congress could have, but did not, enact legislation barring the states' use of WWCR.\textsuperscript{233} Second, Congress, aware that other nations were displeased with worldwide unitary taxation, had on several occasions studied the WWCR problem, but had repeatedly failed to enact legislation prohibiting its use.\textsuperscript{234} Finally, the Supreme Court pointed out that the U.S. Senate's failure to pass the U.S.-U.K. Tax Convention with a prohibition on the states' use of WWCR indicated that Congress condoned its use.\textsuperscript{235}

In reviewing whether California's franchise tax prevented the federal government from speaking with "one voice," the Supreme Court opined that Congress could more passively indi-
cate that certain state tax schemes did not interfere with U.S. international commerce.\textsuperscript{236} Congress, the Court noted, did not need to convey its intent to permit certain state practices with the same unmistakable clarity required to permit state regulations that discriminated against interstate commerce or otherwise did not meet the requirements of the \textit{Complete Auto} test.\textsuperscript{237} Drawing negative inferences from the same congressional actions on WWCR, highlighted when analyzing the preemption question earlier in its opinion, the Court reasoned that Congress's implicit approval\textsuperscript{238} of WWCR also demonstrated that California's franchise tax scheme did not interfere with the federal regulation of international commerce.\textsuperscript{239}

Finally, the majority rejected the argument that Executive Branch opposition to the states' use of WWCR prohibited its use.\textsuperscript{240} The Supreme Court emphasized that the Constitution expressly granted to Congress, and not the President, the foreign commerce power, and Congress had implicitly allowed WWCR.\textsuperscript{241} Thus, although the Executive Branch was opposed to WWCR, its position was not determinative to a resolution of the "one voice" issue.\textsuperscript{242} The majority concluded its opinion by em-

\textsuperscript{236} Id. at 2282-83.
\textsuperscript{237} Id. at 2282-83. The majority stated:

In both \textit{Wardair} and \textit{[Container]}, the Court considered the one voice argument only after determining that the challenged state action was otherwise constitutional. An important premise underlying both decisions is this: Congress may more passively indicate that certain state practices do not impair federal uniformity in an area where federal uniformity is essential; it need not convey its intent with the unmistakable clarity required to permit state regulation that discriminates against interstate commerce or otherwise falls short under \textit{Complete Auto} inspection.


\textsuperscript{238} \textit{Barclays IV}, 114 S. Ct. at 2284.
\textsuperscript{239} Id. at 2284. The majority stated:

Given these indicia of Congress' willingness to tolerate States' worldwide combined reporting mandates, even when those mandates are applied to foreign corporations and domestic corporations with foreign parents, we cannot conclude that the foreign policy of the United States . . . is [so] seriously threatened by California's practice as to warrant our intervention.

\textit{Id.} (citing \textit{Container Corp. v. Franchise Tax Bd.}, 463 U.S. 159, 196 (1983)).

\textsuperscript{240} Id. at 2285.
\textsuperscript{241} Id.

\textsuperscript{242} \textit{Barclays IV}, 114 S. Ct. at 2285. The Supreme Court stated that "Executive Branch actions - press releases, letters, and amicus briefs - . . . are merely precatory" and
phasizing the Supreme Court's lack of competence to resolve the primarily political question of balancing the sovereign right of the states to exercise their tax power against the federal government's conduct of international commerce.\textsuperscript{243}

2. Minority Opinions

In a separate concurring opinion, Justice Blackmun stated that the majority, in analyzing the "one voice" issue, should not have inferred congressional acquiescence to worldwide unitary taxation from Congress's failure to prohibit it.\textsuperscript{244} Justice Blackmun concluded, however, that because Barclays was controlled by the Supreme Court's earlier Container decision, and because California's franchise tax did not impose an administrative burden on non-U.S. parent MNCs, the tax did not violate the one voice standard.\textsuperscript{245}

Justice Scalia, in an opinion concurring in judgment, also agreed that California's franchise tax did not violate the Com-

\textsuperscript{243}Id. at 2284-85. The majority opinion stated:

This Court has no constitutional authority to make the policy judgments essential to regulating foreign commerce and conducting foreign affairs. Matters relating to the conduct of foreign relations... are so exclusively entrusted to the political branches of government as to be largely immune from judicial inquiry or interference. For this reason, Barclays'... argument that California's worldwide combined reporting requirement is unconstitutional because it is likely to provoke retaliatory action by foreign governments is directed to the wrong forum. The judiciary is not vested with power to decide how to balance a particular risk of retaliation against the sovereign right of the United States as a whole to let the States tax as they please.

\textsuperscript{244} Barclays IV, 114 S. Ct. at 2286.

\textsuperscript{245} Id. at 2287.
merce Clause.\textsuperscript{246} In Justice Scalia's view, dormant Commerce Clause analysis was appropriate in only two circumstances: first, where a state law facially discriminated against interstate or foreign commerce or, second, if the state law was indistinguishable from a type of law previously invalidated by the Supreme Court.\textsuperscript{247} Because neither of those circumstances were implicated by California's franchise tax, Justice Scalia concluded there was no Commerce Clause violation.\textsuperscript{248}

In an opinion concurring in judgment in part and dissenting in part, Justice O'Connor, joined by Justice Thomas,\textsuperscript{249} concluded that the application of California's franchise tax to Barclays violated the Foreign Commerce Clause prohibition against multiple taxation.\textsuperscript{250} Justice O'Connor began by drawing a sharp distinction between the application of WWCR-based tax schemes to non-U.S. parent MNCs with U.S.-parent MNCs.\textsuperscript{251} In the U.S.-parent case, when the income of international affiliates was subjected to multiple taxation, the incidence of multiple taxation was ultimately borne by the U.S.-parent corporation.\textsuperscript{252} Multiple taxation in this context was not unlawful because U.S.-parent corporations are subject to full taxation regardless of whether income is domestically or internationally generated.\textsuperscript{253} In contrast, when a WWCR-based tax was imposed on a non-U.S. parent MNC, with both U.S. and non-U.S. affiliates, the incidence of the resulting multiple taxation of non-U.S. source income\textsuperscript{254} was ultimately borne by a non-U.S. corporation, even though the federal government and the states were entitled to tax only income earned domestically.\textsuperscript{255} Because no judicial forum existed in the international context that could ensure that non-U.S. parent MNCs were not subjected to multiple taxation, Justice O'Connor reasoned that state taxes that led to multiple taxation should on principle be invalidated under the Foreign

\textsuperscript{246}Id. (citing Itel Containers v. Huddleston, 113 S. Ct. 1095, 1106-07 (1993) (Scalia, J., concurring in part and concurring in judgment)).
\textsuperscript{247}Id.
\textsuperscript{248}Id.
\textsuperscript{249}Id. at 2287.
\textsuperscript{250}Barclays IV, 114 S. Ct. at 2287-88.
\textsuperscript{251}Id.
\textsuperscript{252}Id. at 2289.
\textsuperscript{253}Id.
\textsuperscript{254}Id.
\textsuperscript{255}Id.
In Barclays' case Justice O'Connor highlighted that ninety-eight percent of its business was conducted outside the United States. In addition Justice O'Connor pointed out that the trial court had made a finding that Barclays was subject to actual multiple taxation. Justice O'Connor, therefore, concluded that because Barclays was a non-U.S. parent MNC the application of California's WWCR-based franchise tax violated the Foreign Commerce Clause prohibition against multiple taxation.

Justice O'Connor noted that although prohibiting WWCR only in the non-U.S. parent MNC case would leave states free to discriminate unfairly against U.S. parent MNCs, such a situation was not unfair because U.S. MNCs had access to the political process to seek redress from discriminatory state taxation.

In contrast a corresponding remedy did not exist for non-U.S. parent MNCs, thus justifying enhanced judicial protection.

III. THE SUPREME COURT CORRECTLY CONCLUDED THAT THE COMMERCE CLAUSE DOES NOT PROHIBIT THE STATES FROM APPLYING WORLDWIDE UNITARY TAXATION TO NON-U.S. PARENT MULTINATIONAL CORPORATIONS

The Barclays decision, while leaving the Interstate Commerce Clause framework intact, narrows the Foreign Commerce Clause framework for reviewing state taxation schemes. This deference to state discretion to devise their fiscal schemes reflects the Supreme Court's unwillingness to impose judicial solutions to what are ultimately issues that must be resolved in the political arena. Such deference on the issue of worldwide unitary taxation is fully apposite since worldwide unitary taxation implicates uniquely political questions of international affairs and federalism which must be resolved by the political branches.

A. Impact on Commerce Clause Review of State Taxation

The substance of the Supreme Court's Interstate Commerce Clause framework for reviewing state taxation schemes estab-
lished in *Complete Auto* remains unchanged after the *Barclays* opinion. However, the Supreme Court's application of Foreign Commerce Clause principles, established in *Japan Line* and narrowed in *Container*, is further restricted in *Barclays*. First, the Supreme Court's application of the multiple taxation test indicates that in the future a state tax on corporate income will only be struck down if multiple taxation is inevitable and can also be avoided under an existing alternative taxation scheme. Second, the Supreme Court appears to have established a "one voice" standard under which state taxation will only be struck down where Congress clearly manifests that a state tax measure interferes with its commerce powers. What precise factors the Supreme Court will examine or consider significant in evaluating whether the federal commerce authority is threatened, however, is not made clear in the *Barclays* opinion. It appears that although *Japan Line* and *Container* regarded the threat of retaliation by U.S. trading partners as a factor indicating a state tax infringed on the federal government's ability to speak with "one voice" in international commerce, after *Barclays* the Supreme Court will no longer examine such factors. The Supreme Court made clear in *Barclays* that such issues are properly directed towards Congress, the body best able to resolve these uniquely political questions. In addition, the Supreme Court has also made clear that the Executive Branch has no constitutional authority to pronounce federal commerce policy, and demonstrates a heightened sensitivity to Congressional pronouncements on issues of international commerce.

The refinement of the Foreign Commerce Clause standards

261. See supra notes 88-99, 210-24 and accompanying text (discussing *Complete Auto* Interstate Commerce Clause review of state taxation and Supreme Court application in *Barclays*).
262. See supra notes 99-118 and accompanying text (discussing *Japan Line* Foreign Commerce Clause review of state taxation).
263. See supra notes 119-45 and accompanying text (discussing *Container* decision).
264. See supra notes 220-29 and accompanying text (discussing the Supreme Courts application of multiple taxation test in *Barclays*).
265. See supra notes 230-39 and accompanying text (discussing Supreme Court's analysis of the "one voice" issue in *Barclays*).
266. Id.
267. See supra note 243 and accompanying text (discussing Supreme Court's view that it lacks authority to resolve external policy issues).
268. See supra notes 240-43 and accompanying text (discussing Executive Branch authority to establish federal commerce policy).
in *Barclays* creates a much higher burden for taxpayers to sustain. The Court in *Barclays* has held that an income tax that resulted in international multiple taxation of foreign-source income received by a non-U.S. parent MNC was acceptable because the problem was not caused by California, and Congress chose not to prohibit it. This holding demonstrates a very high level of tolerance for state tax schemes.

**B. Future Use of Worldwide Unitary Taxation by the States**

In contradistinction to *Container*, which produced an immediate reaction by many states that viewed WWCR as a cure for their financial problems, *Barclays* is unlikely to lead to widespread adoption of worldwide unitary taxation. The 1983 *Container* decision galvanized the business community into united action against WWCR and led it to mount a concerted political campaign against WWCR.\(^{269}\) Under this concerted pressure the WWCR states modified their unitary tax schemes to mitigate the controversial aspects of its operation, most commonly through the adoption of "water's edge" legislation.\(^{270}\) California modified its worldwide unitary tax statute in 1986.\(^{271}\)

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270. *State and Local Taxation, supra* note 2, ¶ 8.16, at 8-185. Florida which had adopted worldwide unitary taxation in 1983 in the wake of the *Container* decision repealed it in 1984. *Id.* Arizona amended its corporate income tax statute in 1985 to limit apportionment to U.S. water's edge income. *Id.* Oregon abandoned worldwide unitary taxation in 1985 also. *Id.* By 1987 the majority of states which used worldwide unitary taxation, including Idaho, Indiana, Montana, New Hampshire, North Dakota, and Utah had abandoned it. *Id.*
271. Eric J. Coffill, *A Kinder Gentler “Water’s Edge” Election: California Wards Off Threat of U.K. Retaliation as Part of Comprehensive Business Incentive Tax Package*, 7 *Tax Notes Int’l* 1049 (Oct. 25, 1993). In 1986, California passed legislation which provided that “qualified taxpayers” subject to state franchise taxes are allowed to establish the state income tax base pursuant to a “water’s edge” election that takes into account only the income of certain related entities. *Cal. Rev. & Tax. Code* § 25110(a) (West 1995). Only certain “qualified taxpayers” can make a “water’s edge” election. *Id.* § 25110(a). A “qualified taxpayer” is a bank or corporation that consents to the Franchise Tax Board taking depositions from key corporate personnel, the taking of *duces tectum*, the reasonable production of documents, and agrees that any “functionally related dividends” received by the electing taxpayer will be treated as apportionable business income. *Id.* § 25110(b)(2). A “qualified taxpayer” must agree to pay an annual election fee equivalent to thirty-thousandths of 1% (or 0.0003) of the sum of the taxpayer’s California property, payroll, and sales. *Id.* § 25115(b). Taxpayers making a “water’s edge” election are required to file with the Franchise Tax Board a “domestic disclosure spreadsheet,” which describes the state tax reporting methods of the taxpayer and its affiliates that are doing business in the United States. *Id.*
Following criticism from governments and non-U.S. MNCs that California's "water's edge" legislation did not proceed far enough to address their concerns, the state again modified its worldwide unitary tax statute in 1993. The adoption of "water's edge" legislation was driven by a number of factors including the recognition by the states that an aggressive assertion of the right to use WWCR-based taxation was detrimental for the local economy, as well as state attempts to forestall possible federal legislation limiting unitary taxation associated with determined pressure exerted by the Executive Branch.

§ 25401d(a). Finally the Franchise Tax Board is empowered to disregard a taxpayer's election if the taxpayer fails to file a domestic disclosure spreadsheet or information that was requested at an audit. Id. § 25401(b)(d). California's "water's edge" statute of 1986 in actual operation excluded from the worldwide unitary group only out-of-state corporations having less that 20% of their operations in the United States. Ruurd G. Leegstra et al., The California Water's-Edge Election, 14 Int'l Tax J. 101, 102 (1987); Robert K. Wiederstein, Comment, California and Unitary Taxation: The Continuing Saga, 9 Ind. Int'l & Comp. L. Rev. 135 (1992).

272. Coffill, supra note 269, at 1052-53. In 1993, in response to several domestic and international developments, California modified its "water's edge" legislation. First, the U.S. Supreme Court asked the U.S. Solicitor General's office to file an amicus brief in the Barclays case then pending before it. Id. at 1052. Faced with the possibilities of either supporting California on worldwide unitary taxation, and probably provoking an international trade/tax war with other countries, or reneging on a campaign promise to support California in the Barclays' litigation by opposing worldwide unitary taxation, the request for the amicus brief placed the Clinton administration in an acute political dilemma. Id. Second, in May 1993 the British Chancellor of the Exchequer threatened that the United Kingdom would take retaliatory measures against U.S. companies operating in the United Kingdom if the unitary taxation problem was not solved. Id. California's changes to its "water's edge" election were designed to avert the threat of impending British retaliation and to resolve the Clinton administration's political problems. Id. These changes became effective on January 1, 1994. Id. at 1055. The major changes made to the "water's edge" scheme included, first, the elimination of election fees. Cal. Rev. & Tax. Code § 25111(a) (West 1995). Second, a taxpayer making an election no longer has to file a domestic disclosure spreadsheet. Id. Third, the election is for an initial term of seven years. Id. Finally, the Franchise Tax Board lacks the power to disregard a "water's edge" election. Id. § 25111(c).

273. See, e.g., State and Local Taxation, supra note 2, ¶ 8.16, at 8-186. For example Oregon, in the face of intense pressure by Japanese businesses in particular, amended its worldwide unitary tax statutes to comply with the "water's edge" restriction. Id. Japanese businesses declared that they would not make new investments or expand existing plants in the state if worldwide unitary taxation was applied to them. Id. at ¶ 8.16, at 8-186 (citing The Oregonian, Sept. 20, 1984).

274. See State and Local Taxation, supra note 2, ¶ 8.16, at 8-185. Following the Container decision, the Reagan administration established the Worldwide Unitary Taxation Working Group headed by Donald Regan, then Secretary of the Treasury, to review worldwide apportionment. Id. The 1984 Working Group Report recommended that the states adopt water's edge legislation for both U.S. and non-U.S. parent MNCs. Id. More forcefully, the Working Group Report recommended that in the event that
Similarly, after 1994 the states are faced with few legal impediments to adopting worldwide unitary taxation. Barclays, however, will likely not be embraced by the states with the same enthusiasm as was Container. The probable reigniting of hostilities by the business community against any attempt to restore WWCR-based taxation will restrict the states’ readoption of WWCR.

C. The Supreme Court Correctly Resolved the Worldwide Unitary Taxation Problem

The Barclays decision reconfirms the Supreme Court’s general unwillingness to impose judicially crafted solutions to the commerce clause aspects of the worldwide unitary taxation dispute earlier demonstrated in Container. Such judicial restraint is appropriate because the division of income disputes with respect to non-U.S. parent MNCs was a uniquely political issue that brought into conflict the extensive fiscal authority vested in the states against the federal government’s enumerated powers to regulate international commerce. The Supreme Court early on correctly recognized that any durable solution to the problem necessarily had to come from the political arena. Developments since the Container decision have borne out the validity of this general stance and support the ultimate holding in Barclays. Worldwide unitary taxation was a political problem. As such it was rightly resolved in the political arena.

CONCLUSION

After 1983 the one remaining avenue open under the Commerce Clause for MNCs to challenge worldwide unitary taxation was the reserved issue in Container — the possible unconstitutionality of applying WWCR-based taxation to non-U.S. parent MNCs. By deciding in Barclays that the application of WWCR to such legislation was not adopted, federal legislation requiring such limitations should be enacted. Id.

275. See supra note 139 (setting forth Supreme Court’s view expressed in Container that it has no authority to decide sensitive issues of international relations).

276. See supra note 139 (setting forth Supreme Court’s view expressed in Container that it has no authority to decide sensitive issues of international relations).

277. See supra notes 269-74 and accompanying text (discussing political pressure placed on states to modify worldwide unitary taxation legislation and adoption of “water’s edge” legislation).
non-U.S. parent MNCs does not violate the Commerce Clause the Court has completed the constitutional analysis applicable to worldwide unitary taxation. The Court has also removed the last Commerce Clause hurdle to the states' use of WWCR-based taxation, but because political and economic imperatives are aligned against worldwide unitary taxation it is unlikely that the states will implement such taxation laws in the wake of Barclays.