School of Law
UNIVERSITY OF GEORGIA

Digital Commons @ University of Georgia School of Law

Scholarly Works | Faculty Scholarship

1-1-2020

Distortion of Income in a Single-Factor Sales Formula World

Walter Hellerstein
Distinguished Research Professor & Francis Shackelford Distinguished Professor in Taxation Law Emeritus *University of Georgia School of Law*, wallyh@uga.edu

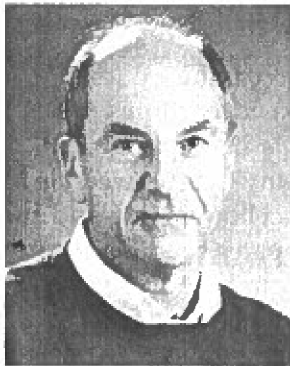
Repository Citation

Walter Hellerstein, *Distortion of Income in a Single-Factor Sales Formula World* , 96 Tax Notes State 729 (2020),
Available at: https://digitalcommons.law.uga.edu/fac_artchop/1540

This Article is brought to you for free and open access by the Faculty Scholarship at Digital Commons @ University of Georgia School of Law. It has been accepted for inclusion in Scholarly Works by an authorized administrator of Digital Commons @ University of Georgia School of Law. Please share how you have benefited from this access
For more information, please contact tstriepe@uga.edu.

Distortion of Income in a Single-Factor Sales Formula World

by Walter Hellerstein



Walter Hellerstein

Walter Hellerstein is the Distinguished Research Professor Emeritus and the Francis Shackelford Professor of Taxation Emeritus at the University of Georgia Law School, a visiting professor at the Vienna University of Economics and Business, and chair of the *Tax Notes State* advisory board.

In this article, Hellerstein describes the framework governing constitutional challenges to state income tax apportionment formulas in light of the widespread adoption of single-factor sales formulas and speculates as to whether a recent Michigan court decision invalidating the application of such a formula on constitutional grounds might be a harbinger of things to come.

Taxpayers have been singularly unsuccessful in challenging formulary apportionment of income on the ground that the application of the formula creates unconstitutional distortion in attributing the taxpayer's income to the state.[1] Indeed, it has been nearly a century since the U.S. Supreme Court invalidated the application of a state income tax apportionment formula on this ground.[2]

The explanation for this fact lies principally in the forgiving standards that the Court has articulated for determining whether the application of an apportionment formula results in unconstitutional distortion of the taxpayer's income. However, the explanation may also lie in part in the states' widespread embrace during the second half of the 20th century of three-factor apportionment formulas of property, payroll, and sales[3] that were less vulnerable to attack in theory and in practice than the single-factor formulas that prevailed during the earlier era of state corporate income taxation.

But times have changed in the world of state income tax apportionment. Today more than half of the states with income taxes use single-sales-factor formulas to apportion net income — with many others attributing double weight to the sales factor.[4] These developments may have made state income tax formulas more vulnerable to attack as a theoretical and practical matter. After exploring the constitutional framework within which these issues arise, this article discusses a recent Michigan decision that could be a harbinger of things to come.

Historical Overview of Constitutional Restraints on Distortion of Income Attributable to Formulary Apportionment: The *Reader's Digest* Version

From the very beginning, the Supreme Court adopted a forbearing standard for evaluating claims of unconstitutional distortion

[1] *See generally* Jerome R. Hellerstein, Walter Hellerstein, and John A. Swain, *State Taxation*, para. 8.16 (2020 rev.) (hereinafter Hellerstein, *State Taxation*) from which this article freely draws.

[2] *Hans Rees' Sons Inc. v. North Carolina ex rel. Maxwell*, 283 U.S. 123 (1931). The Court did, however, more recently invalidate the application of a state property tax apportionment formula on this ground. *Norfolk & W. Ry. v. Missouri State Tax Comm'n*, 390 U.S. 317 (1968).

[3] Indeed, in 1978 43 of the 45 states with income taxes (as well as the District of Columbia) employed an equally weighted three-factor formula for apportioning net income. *Moorman Mfg. Co. v. Bair*, 437 U.S. 267, 283 (1978) (Powell, J., dissenting). Iowa employed a single-factor sales formula and West Virginia employed a two-factor formula of property and payroll. *Id.* at 283 n.1.

[4] Walter Hellerstein, "The Transformation of the State Corporate Income Tax Into a Market-Based Levy," 130(5) *J. Tax'n* 4 (2019).

resulting from states' attribution of income under apportionment formulas.[5]

The Court's 1920 decision in *Underwood Typewriter Co. v. Chamberlain*[6] was the first case in which it considered the constitutionality of the application of an apportionment formula to attribute a taxpayer's income to a state. Underwood was a Delaware corporation that did all its manufacturing in Connecticut, had its main office in New York, and maintained branch offices across the country through which it sold, leased, and repaired typewriters, accessories, and supplies. Under Connecticut's single-factor property formula, 47 percent of Underwood's income was attributed to the state. Underwood contended that the tax violated the due process clause, because "it is imposed on income arising from business conducted beyond the boundaries of the state,"[7] an objection, the Court observed, that "rests solely upon the showing that of its net profits $1,293,643.95 was received in other states and $42,942.18 in Connecticut."[8] The Court continued:

> But this showing wholly fails to sustain the objection. The profits of the corporation were largely earned by a series of transactions beginning with manufacture in Connecticut and ending with sale in other states. . . . The Legislature, in attempting to put upon this business its fair share of the burden of taxation, was faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders. It, therefore, adopted a method of apportionment which, for all that appears in this record, reached, and was meant to reach, only the profits earned within the state. "The plaintiff's argument on this branch of the case . . . carries the burden of showing that 47 per cent of its net income is not reasonably attributable, for purposes of taxation, to the manufacture of products from the sale of which 80 per cent of its gross earnings was derived after paying manufacturing costs." The corporation has not even attempted to show this . . . . There is, consequently, nothing in this record to show that the method of apportionment adopted by the state was inherently arbitrary, or that its application to this corporation produced an unreasonable result.[9]

Four years after *Underwood*, the Court reaffirmed the decision's basic teachings in *Bass, Ratcliff & Gretton Ltd. v. State Tax Commission*.[10] Bass was an English company that brewed ale in England and sold its product both in England and the United States. The company's federal income tax return showed a loss from U.S. operations, although the business as a whole operated at a profit. Under New York's single-factor property formula, the state apportioned a share of the company's global income to New York. The company asserted that the state's tax thereby violated the commerce and due process clauses by attributing income earned outside the United States to New York. The Court, quoting the passage set forth in the preceding paragraph and observing that "the constitutionality of this tax as applied in the present case is controlled . . . by the decision in *Underwood*,"[11] declared:

> So in the present case we are of opinion that, as the Company carried on the unitary business of manufacturing and selling ale, in which its profits were earned by a series of transactions beginning with the manufacture in England and ending in sales in New York and other places — the process of manufacturing resulting in no profits until it ends in sales — the State was justified in attributing to New York a just proportion of the profits earned by the Company from such unitary business.[12]

---

[5] The ensuing summary of the constitutional restraints on distortion of income attributable to formulary apportionment draws freely from Hellerstein, *State Taxation*, *supra* note 1, paras. 8.13-8.16, where the unabridged version of this discussion may be found.

[6] 254 U.S. 113 (1920).

[7] *Id.* at 120.

[8] *Id.*

[9] *Id.* at 120-121.

[10] 266 U.S. 271 (1924).

[11] *Id.* at 280.

[12] *Id.* at 282.

The only case in which the U.S. Supreme Court has struck down the application of an income apportionment formula on constitutional grounds was handed down in the decade following its decisions in *Underwood* and *Bass*. In *Hans Rees' Sons Inc. v. North Carolina ex rel. Maxwell*,[13] the taxpayer was a New York corporation engaged in tanning and manufacturing leather with its tannery and manufacturing plant, which were in North Carolina. The state used a single-factor property formula to apportion the taxpayer's net income to the state, resulting in an average apportionment of roughly 80 percent for the years at issue. The taxpayer contended that the attribution of income to North Carolina was unconstitutional based on evidence that its income derived from three sources: buying profit, manufacturing profit, and selling profit — only 17 percent of which was properly attributable to North Carolina. The trial court, however, struck this evidence from the record on the ground that the taxpayer was conducting a unitary business and it therefore "was not permissible to lop off certain elements of the business constituting a single unit, in order to place the income beyond the taxing jurisdiction of the State."[14] The Supreme Court of North Carolina sustained the trial court's decision. The U.S. Supreme Court reversed, declaring:

> We are unable to agree with this view. Evidence which was found to be lacking in the *Underwood* and *Bass* cases is present here. . . .
>
> Undoubtedly the enterprise of a corporation which manufactures and sells its manufactured product is ordinarily a unitary business, and all the factors in that enterprise are essential to the realization of profits. The difficulty of making an exact apportionment is apparent, and hence, when the state has adopted a method not intrinsically arbitrary, it will be sustained until proof is offered of an unreasonable and arbitrary application in particular cases. But . . . evidence may always be received which tends to show that a state has applied a method, which, albeit fair on its face, operates so as to reach profits which are in no just sense attributable to transactions within its jurisdiction. . . .
>
> For the present purpose, . . . it is sufficient to say that, in any aspect of the evidence, . . . the statutory method, as applied to the appellant's business for the years in question operated unreasonably and arbitrarily, in attributing to North Carolina a percentage of income out of all appropriate proportion to the business transacted by the appellant in that state.[15]

The Court's post-*Hans Rees* decisions addressing taxpayers' claims of unconstitutional distortion attributable to formulary apportionment of their income have consistently rejected such claims and reaffirmed the Court's underlying approach in *Underwood* and *Bass*. Thus, in *Butler Brothers v. McColgan*,[16] the Court rejected such a claim when the formula attributed $93,500 to California but the taxpayer's books and records revealed a loss of $83,000.[17] In so holding, the Court observed that it did not need to "impeach the integrity" of the taxpayer's accounting system in concluding that this did not prove the taxpayer's assertion that "extraterritorial values are being taxed," because:

> A particular accounting system . . . may not fit the different requirements when a State seeks to tax values created by business within its borders. That may be due to the fact, as stated by Mr. Justice Brandeis in *Underwood Typewriter Co. v. Chamberlain*, . . . that a State in attempting to place upon a business extending into several States "its fair share of the burden of taxation" is "faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders." Furthermore, the

---

[13] 283 U.S. 123 (1931).

[14] *Id.* at 131-132.

[15] *Id.* at 132-136 (citations omitted).

[16] 315 U.S. 501 (1942).

[17] The loss was determined by subtracting direct and indirect expenses associated with sales into California from the gross receipts from those sales.

> particular system used may not reveal the facts basic to the State's determination. *Bass, Ratcliff & Gretton Ltd. v. Tax Commission.*[18]

In *Moorman Manufacturing Co. v. Bair,*[19] the Court dismissed the taxpayer's claim of unconstitutional distortion, noting that despite the opportunity "to demonstrate that the . . . formula produced an arbitrary result," the record "contains no such showing and therefore . . . is not subject to challenge under the Due Process Clause."[20] In *Exxon Corp. v. Wisconsin Department of Revenue,*[21] the Court summarily disposed of the taxpayer's claim of distortion, noting that "this is hardly a case where the State has used a formula 'out of all appropriate proportion to the business transacted . . . in that State.'"[22]

In *Container Corp. of America v. Franchise Tax Board,*[23] the Court reiterated the relaxed standard of review it applied to constitutional challenges to formulary apportionment of income; it reaffirmed its long-standing position that separate accounting evidence, standing alone, did not impeach apportionment by formula; and it concluded, in any event, that the alleged distortion at issue (14 percent) lacked what might be characterized as "constitutional dignity" — to wit, "a far cry from the more than 250 [percent] difference that led us to strike down the state tax in *Hans Rees* . . . and a figure certainly within the substantial margin of error inherent in any method of attributing income among the components of a unitary business."[24]

Finally, in *Trinova Corp. v. Michigan Department of Treasury,*[25] the Court dismissed an analogous unconstitutional distortion claim in rejecting a challenge to the fair apportionment of Michigan's single business tax (SBT)[26] by an Ohio-based manufacturer of window glass and other automobile products. Trinova's fair apportionment argument rested on its claim that its SBT base, composed largely of compensation and depreciation, was located in Ohio and that the effect of the application of the three-factor formula that Michigan used to apportion the SBT — with its sales factor largely reflecting its substantial Michigan sales — was to assign Ohio compensation and depreciation to Michigan. In rejecting Trinova's claim that the formula effectively "taxed profits not attributable to activities within the State" during the tax year, the Court declared:

> Trinova gives no basis for distinguishing the same arguments that were pressed, and rejected, with regard to the apportionment of income. We could not accept Trinova's argument that the sales factor distorts Michigan's apportionment formula without rejecting our precedents which approve the use of the same formula to apportion income.[27]

The Court's Recognition of the Virtues of the 3-Factor Formula of Property, Payroll, and Sales for Apportioning Income

If the preceding discussion has accomplished nothing else, it has demonstrated the difficulty that taxpayers have confronted in challenging formulary apportionment of their income under a constitutional standard that requires a taxpayer to prove "by 'clear and cogent evidence' that the income attributed to the State is in fact 'out of all appropriate proportion to the business transacted . . . in that State,' or 'has led to a grossly distorted result.'"[28] However, there is one additional feature

---

[18] *Butler Bros.*, 315 U.S. at 507–508 (citations omitted).

[19] 437 U.S. 267 (1978)

[20] *Id.* at 275. As explained below, the taxpayer's failure in this regard is attributable to the fact that it thought the Iowa statute was vulnerable to attack on its face. See text accompanying notes 37-38 *infra*.

[21] 447 U.S. 207 (1980).

[22] *Id.* at 227 (quoting *Hans Rees*). The Court also cited *Moorman*, *Butler Bros.*, *Bass*, and *Underwood* in support of its conclusion. *Id.*

[23] 463 U.S. 159 (1983).

[24] *Id.* at 184.

[25] 498 U.S. 358 (1991).

[26] Before the SBT's repeal effective 2008, Michigan was unique among American states in having as its principal form of business tax an exaction on "value added" — the Michigan SBT. In contrast to the typical corporate net income tax, which is measured by a corporation's profits during the taxable year, the SBT was measured roughly by the increase in the value of goods and services attributable to the taxpayer's business activity during the taxable year. The essential components of the SBT were the values added by the contributions of labor, capital, and entrepreneurial skill that the taxpayer made in producing its goods or services.

[27] *Trinova*, 498 U.S. at 383.

[28] *Moorman*, 437 U.S. at 274 (quoting *Hans Rees*, 283 U.S. at 135, and *Norfolk & W. Ry.*, 390 U.S. at 326).

of the Court's opinions addressed to formulary apportionment that warrants consideration in surveying the contemporary constitutional landscape in this domain.

In several of the Court's more recent opinions involving claims of distortion in the application of apportionment formulas, it has recognized the virtues of the once-prevailing "standard" three-factor formula as a fair way of apportioning income. Thus, in *General Motors Corp. v. District of Columbia*,[29] the Court stated: "The standard three-factor formula can be justified as a rough, practical approximation of the distribution of either a corporation's sources of income or the social costs which it generates."[30] In *Container*, the Court reaffirmed its endorsement of the three-factor formula for apportioning income, observing that "not only has the three-factor formula met our approval, but it has become . . . something of a benchmark against which other apportionment formulas are judged."[31] The Court further noted that:

> The three-factor formula . . . has gained wide approval precisely because payroll, property, and sales appear in combination to reflect a very large share of the activities by which value is generated.[32]

In *Trinova*, the Court reiterated and elaborated upon these sentiments, declaring:

> The Michigan SBT uses the same three-factor apportionment formula we first approved for apportionment of income in *Butler Brothers v. McColgan*. . . . This standard has become "something of a benchmark against which other apportionment formulas are judged." Although the one-third weight given to each of the three factors — payroll, property, and sales — is not a precise apportionment for every case, the formula "has gained wide approval precisely because payroll, property, and sales appear in combination to reflect a very large share of the activities *by which value is generated*." *Container Corp*. . . .(emphasis added). The three-factor formula is widely used, and is included in the Uniform Division of Income for Tax Purposes Act . . . (approved in 1957 by the National Conference of Commissioners on Uniform State Laws and the American Bar Association).[33]

To be sure, in *Moorman*, in sustaining the constitutionality of the application of Iowa's single-sales-factor formula to the taxpayer's income, the Court distanced itself from any suggestion that its kind words about the three-factor formula in *General Motors* — in which it had invalidated the application of the District of Columbia's single-factor formula on statutory grounds — should be read as suggesting that the three-factor formula was constitutionally required. Thus, in *Moorman*, the Court described its decision in *General Motors* in the following terms:

> In that case the Court held that a regulation prescribing a single-factor sales formula was not authorized by the District of Columbia Code. It concluded that the formula violated the statutory requirement that the net income of a corporation doing business both inside and outside the District must be deemed to arise from "sources" both inside and outside the District. But that statutory requirement has no counterpart in the Constitution, and the Court in *General Motors* made clear that it did "not mean to take any position on the constitutionality of a state income tax based on the sales factor alone."[34]

The Court nevertheless observed that "it is true" that "the Court . . . expressed doubts about the wisdom of the economic assumptions underlying the challenged formula and noted that its use in the context of the more prevalent three-factor formula would not advance the policies underlying the Commerce Clause."[35]

Indeed, one of the ironies of the *Moorman* case is that the taxpayer never made a serious effort to

[29] 380 U.S. 553 (1965).

[30] *Id.* at 561.

[31] *Container*, 463 U.S. at 170.

[32] *Id.* at 183.

[33] *Trinova*, 498 U.S. at 380-381.

[34] *Moorman*, 437 U.S. at 275 (citation omitted).

[35] *Id.* at 275 n.8.

demonstrate that Iowa's single-factor formula, *as applied*, resulted in unconstitutional distortion. As we have already observed,[36] the Court in *Moorman* dismissed the taxpayer's claim of unconstitutional distortion, noting that despite the opportunity "to demonstrate that the . . . formula produced an arbitrary result," the record "contains no such showing and therefore . . . is not subject to challenge under the Due Process Clause."[37] The explanation for this failure is apparent. The taxpayer thought the constitutional "handwriting was on the wall" for the last rites of Iowa's single-sales-factor formula under the commerce clause after the Court struck down the District's single-sales-factor formula in *General Motors* and declared:

> The conclusion which we reach by analysis of the plain language of the statute also finds support in the consequences which a contrary view would have for the overall pattern of taxation of income derived from interstate commerce. The great majority of States imposing corporate income taxes apportion the total income of a corporation by application of a three-factor formula which gives equal weight to the geographical distribution of plant, payroll, and sales. The use of an apportionment formula based wholly on the sales factor, in the context of general use of the three-factor approach, will ordinarily result in multiple taxation of corporate net income; for the States in which the property and payroll of the corporation are located will allocate to themselves 67 [percent] of the corporation's income, whereas the jurisdictions in which the sales are made will allocate 100 [percent] of the income to themselves. Conversely, in some cases enterprises will have their payroll and plant located in the sales-factor jurisdictions and make their sales in the three-factor jurisdictions so that only 33 [percent] of their incomes will be subject to state taxation. In any case, the sheer inconsistency of the District formula with that generally prevailing may tend to result in the unhealthy fragmentation of enterprise and an uneconomic pattern of plant location, and so presents an added reason why this Court must give proper meaning to the relevant provisions of the District Code.[38]

This raises the tantalizing question of what might have happened in *Moorman* if the taxpayer had in fact mounted a serious "as applied" challenge to Iowa's single sales factor in light of the Court's recognition that "payroll, property, and sales appear in combination to reflect a very large share of the activities *by which value is generated*"[39] and its "doubts about the wisdom of the economic assumptions underlying"[40] the single-sales-factor formula. In effect, that is the question that taxpayers face today in challenging the constitutionality of the application of single-sales-factor formulas, and it is the focus of the final section of this article.

The Michigan Court of Appeals Decision in *Vectren*

In *Vectren Infrastructure Services Corp. v. Department of Treasury*,[41] Minnesota Ltd. Inc. (MLI), an S corporation headquartered in Minnesota, was engaged in the business of constructing, maintaining, and repairing oil and gas pipelines, as well as providing responses to hazardous materials incidents. MLI employed over 600 employees during the peak season for its work, serving a 24-state territory, primarily in the northern Midwest, including Michigan. MLI provided its services to its customers on a contract-by-contract basis, so that its project locations were different every year. At no time did MLI maintain a permanent business location in Michigan or retain permanent employees in the state.

For many years, MLI was owned equally by two siblings. When one of the siblings began

[36] *See* text accompanying notes 19-20 *supra*.

[37] *Moorman*, 437 U.S. at 275.

[38] *General Motors*, 380 U.S. at 559-560 (footnote omitted).

[39] *See* text accompanying note 33 *supra*.

[40] *See* text accompanying note 35 *supra*.

[41] No. 345462, 2020 WL 1223417 (Mich. Ct. App. Mar. 12, 2020).

experiencing health issues around 2010, the owners agreed to sell the business. During the period that MLI was seeking a buyer, MLI was hired to assist in the cleanup of a severe oil pipeline spill in Kalamazoo, Michigan. In 2011, while the cleanup was ongoing, MLI's owners sold its stock, which they elected to treat as an asset sale by MLI (including MLI's intangible assets of receivables, cash, and goodwill) under IRC section 338(h)(10).[42] The purchase price was $80 million.

The Michigan business tax, which was measured both by business income and gross receipts,[43] used a single-sales-factor formula to apportion the tax base. Although the gain from the deemed asset sale was included in MLI's apportionable tax base, there was a dispute over the question whether the receipts from the sale should be included in the sales factor. MLI contended that those receipts should be included, resulting in a Michigan apportionment percentage of roughly 15 percent — whereas the Department of Treasury took the opposite position, resulting in a Michigan apportionment percentage of roughly 70 percent. MLI contended, among other things, that exclusion of the receipts resulted in unconstitutional distortion. The court noted that "we do not necessarily disagree" with the department's "basic position on how to calculate the tax under the statutory formula," because:

> Its position is reasonable in light of the differing definitions of "business activity," "business income," and "sales" and how those terms are employed in calculating the tax base and applying the sales factor to apportion the sales to Michigan.[44]

The Michigan Court of Appeals determined, however, that it did need to address these issues because "we find one to be dispositive in plaintiff's favor. . . . To apply the statutory formula, as defendant did, to the circumstances of this case would result in the imposition of a tax in violation of the Commerce Clause."[45]

After a careful review of the case law that we have described earlier, the court concluded that "this is an exceptional case where the taxpayer has met its burden of providing clear and cogent evidence that the business activity attributed to it 'is out of all appropriate proportion to the actual business activity transacted in this state and leads to a grossly distorted result.'"[46] While recognizing that "some of MLI's value can undoubtedly — and should undoubtedly — be attributed to its business activity in Michigan,"[47] the court pointed out that historically MLI's Michigan sales averaged only about 7 percent of its total sales and that most of MLI's value "stemmed, not from its activity in Michigan during the Short Year or even over the years, but from intangible assets built-up in multiple other states over time."[48]

Consequently, in the court's view, by looking only to the activity during the short year and imposing a tax on 70 percent of the gain on the sale when, at least as matter of history, only 7 percent of MLI's activities occurred in Michigan, the application of the statute created "unconstitutional distortion."[49]

The court elaborated on its constitutional analysis, observing that "application of the statutory formula in this case runs afoul of the Due Process and Commerce Clauses . . . because it does not fairly determine the portion of income from the Sale that is reasonably attributed to in-state activities."[50] Quoting *Container*, the court continued that "fairness . . . requires that 'choice of factors used in the apportionment formula must actually reflect a reasonable sense of how [the business activity] is generated'"[51] and "looking only at the Short Year does not actually and reasonably reflect how the income from the

---

[42] *See* Hellerstein, *State Taxation*, *supra* note 1, para. 7.14 (discussing states' conformity to IRC section 338(h)(10)).

[43] See *id.* para. 7.12[8] (describing the Michigan business tax). The tax was in force from 2008-2011 and was replaced effective 2012 by a conventional corporate income tax.

[44] *Vectren*, 2020 WL 1223417, at *3.

[45] *Id.*

[46] *Id.* at *6 (quoting Mich. Comp. Stat. Ann. section 208.1309).

[47] *Id.*

[48] *Id.*

[49] *Id.*

[50] *Id.*

[51] *Id.* (quoting *Container*, 463 U.S. at 169; brackets added by Michigan court).

Sale was generated."[52] Thus, "as in *Hans Rees' Sons*, the statutory formula when applied in this case operates 'so as to reach profits which are in no just sense attributable to transactions within its jurisdiction.'"[53]

Finally, and addressing the fundamental question raised by this article, in response to the contention that *Trinova*[54] supported the state's position, the court declared:

> But *Trinova* involved the [Single Business Tax Act's][55] three-factor apportionment formula. The Court effectively held that showing a distortion as to a single factor after the ratios are averaged did not impeach the basic premise of the three-factor formula, given that the business was to be viewed as a whole and that the *averaged* ratios actually reflected a reasonable sense of how the taxpayer's business activity was generated. *Trinova* is not helpful to the Department's position; that the Court accepted an actual distortion of up to 1000 times greater than actual is immaterial to this case where the three-factor apportionment formula is not at issue. Rather, the [Michigan business tax] uses a single factor, sales. And, unlike the three-factor formula in *Trinova*, MLI's Michigan sales alone do not reasonably reflect how the gain on the Sale was generated. *Trinova* is inapposite.[56]

It is plainly premature at this juncture, based solely on the Michigan Court of Appeals decision in *Vectren*, to provide a definitive answer to the basic question raised by this article — namely, whether courts are likely to be more receptive to claims of unconstitutional distortion under single-factor sales formulas than they generally have been in the past in adjudicating claims of unconstitutional distortion under income apportionment formulas. In short, whether the Michigan Court of Appeals decision in *Vectren* is a harbinger of things to come for states with single-factor sales formulas remains to be seen. It does raise the possibility, however, that the states incur enhanced constitutional risks in adopting such formulas and ignoring entirely the Court's century-old declaration that "income may be defined as the gain derived from capital, from labor, or from both combined"[57] as well as the Court's more recent observations that "the three-factor formula . . . has gained wide approval precisely because payroll, property, and sales appear in combination to reflect a very large share of the activities by which value is generated"[58] and "can be justified as a rough, practical approximation of the distribution of either a corporation's sources of income or the social costs which it generates."[59] ■

[52] *Id.*

[53] *Id.* (citing *Hans Rees*, 283 U.S. at 134).

[54] *See* text accompanying notes 25-27 *supra*.

[55] The reference is to the former Michigan SBT described in note 26 *supra*, in connection with our discussion of the *Trinova* case.

[56] *Vectren*, 2020 WL 1223417, at *6 (emphasis in original).

[57] *Eisner v. Macomber*, 252 U.S. 189, 207 (1920) (quoting *Stratton's Independence Ltd. v. Howbert*, 231 U.S. 399, 415 (1913), and *Doyle v. Mitchell Bros.*, 247 U.S. 179 (1918)).

[58] *Container*, 463 U.S. at 183.

[59] *General Motors*, 380 U.S. at 561.