ASSOCIATED INDUSTRIES OF VERMONT
REPRESENTING THE VERMONT INDUSTRIAL AND BUSINESS COMMUNITY SINCE 1920

Follow Up Comment and Recommendations on Corporate Tax Reform

House Ways and Means Committee

February 19, 2020

AIV appreciates the ongoing discussion in this Committee regarding corporate tax reform focused on the goal of supporting, retaining, and attracting employers that keep and grow employment and investment, including property, in Vermont. We would like to offer further comments and recommendations in the context of this overarching goal on three of the topics being discussed: single sales apportionment, the throwback rule, and the 80/20 rule.

Single Sales

Moving toward single sales apportionment can be seen as a more rational approach to tax policy, but it is also an important means toward the goal of retaining and attracting high value employment and investment in Vermont.

- It focuses on the most direct analog to income, sales, as opposed to property and payroll, which are not direct analogs to income.
- It focuses on income earned in the state, as opposed to income earned in other states, which both fairly allocates Vermont's share of a company's income and encourages manufacturing and other companies that export goods and services, which provide high value for the economy.
- It would still create a competitive advantage over other states that have not adopted it, but with more states adopting single sales there is a risk of falling further behind if we delay unnecessarily.

We would recommend moving forward toward single sales apportionment. Modest initial steps phasing it in are reasonable, but a clear schedule is important to stay focused and signal serious intent to employers making longer term plans for Vermont. In addition, a concrete first step is important so that we have real world experience to study. We would recommend a three year process, starting with a move to triple weighting sales and ending with full single sales apportionment, with monitoring and reporting on impacts along the way. Whether to include a second step between the initial triple weighting and single sales apportionment is something that could be further considered.

Throwback

Retaining the throwback rule is not only arbitrary tax policy, but it also runs exactly counter to the intent and effect of moving toward a single sales factor as a means toward retaining and attracting high value employment and investment in Vermont

- Identical companies can be taxed differently simply because they have different sales patterns or footprints in other states.
- Companies with the same Vermont income year over year could have different taxable income simply because of different sales patterns in other states.

- Another arbitrary aspect of throwback is that it is only triggered if there is no taxable nexus in another state, not by what the tax rate is in other states (and possibly does not apply to states without income taxes).

- Taxing income in other states is directly counter to the principle and practical intent of moving toward a single sales factor.

- Because throwback only distorts the sales factor, the negative impacts only get more significant as a state moves toward single sales apportionment.

- Most states with a single sales factor do not have a throwback rule.

Like moving toward a single sales factor, eliminating the throwback rule up front would be ideal, but phasing it out can also be reasonable. If it is not eliminated in the first year of the three year process recommended above, we would recommend reducing it by 50% in the first year and eliminating it in the second year, or simply eliminating it in the second year. Alternatively, we could also switch to the throwout rule for tangible goods during the transition period to single sales. But in any case, we should move to reduce the negative and counter productive impact of the throwback rule as we move toward single sales.

80/20 Rule

Getting rid of the 80/20 rule can make rational sense, but there could be concerns about practical effects, especially in the context of how we tax "overseas business organizations" and other companies with foreign footprints and income overall.

- The fact that Vermont aggressively taxes foreign dividends and other related tax policies could mean that these companies might already be paying more in taxes in Vermont than in states without an 80/20 rule but with much lower taxes on foreign income, which raises potential competitiveness issues.

- Without a better understanding of what kinds of companies are utilizing the 80/20 rule, it is also difficult to know what kind of initial "sticker shock" could be created by its repeal on top of longer term competitiveness concerns noted above.

We would recommend delaying the elimination of the 80/20 rule for at least one year to allow time to study and better understand its use in Vermont but also to understand the larger context of how Vermont taxes companies with foreign footprints and income, so that we could make more comprehensive changes overall to both fairly tax these companies while also avoiding creating serious competitive disadvantages. This could include making adjustments to multiple related tax policies, either up front or phased in as well.

Summary

In summary, then, we would recommend a three year process:

- Move to triple weighted sales in the first year, with single sales apportionment in the third year and reports on impacts along the way. An interim step in the second year could also be included.

- Eliminate the throwback by the second year of this process, in one or two steps.

- Further study the use and impact of the 80/20 rule in Vermont along with other policies taxing companies with foreign footprints and income, with recommendations for the second or third year of this process.

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