

Corporate Income Tax Overview - Update

House Committee on Ways and Means

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How does Vermont tax businesses?

- Vermont – like the Federal Government – treats taxes on net income/profit depending on how a business is structured
- Two Characterizations
 1. Corporations
 - Subject to the Corporate Tax.
 2. Pass-Through Businesses
 - Profits are divided amongst shareholders depending on shares of business.
 - Owners of the business pay taxes through the Personal Income Tax Code.
 - Increasing the corporate tax rate would not affect business income owners receive from pass-throughs.



Corporate Income Taxes

- Vermont currently applies an 8.5% marginal tax rate on net corporate income above \$25,000.
- Corporate income of a unitary group includes, the total net income of a parent corporation and all subsidiaries.
- Income is determined by an apportionment formula:
 - Pre-2023: a three-factor formula used share of payroll, property and sales in Vermont relative to national payroll, property and sales.
 - Beginning January 2023: single factor sales apportionment
 - Tax rates apply to the net income apportioned to Vermont
- Firms with zero taxable income (roughly 70% of returns) pay the minimum tax, which ranges from \$100 to \$100,000



Corporate Income Taxes

Marginal Tax Rates		
Income Allocable to Vermont		Tax Rate
\$0	\$10,000	6.0%
\$10,000	\$25,000	7.0%
\$25,000	and up	8.5%

Minimum Annual Tax		
Vermont Gross Receipts		Minimum Tax
\$0	\$500,000	\$100
\$500,000	\$1,000,000	\$500
\$1,000,000	\$5,000,000	\$2,000
\$5,000,000	\$300,000,000	\$6,000
\$300,000,000	and up	\$100,000

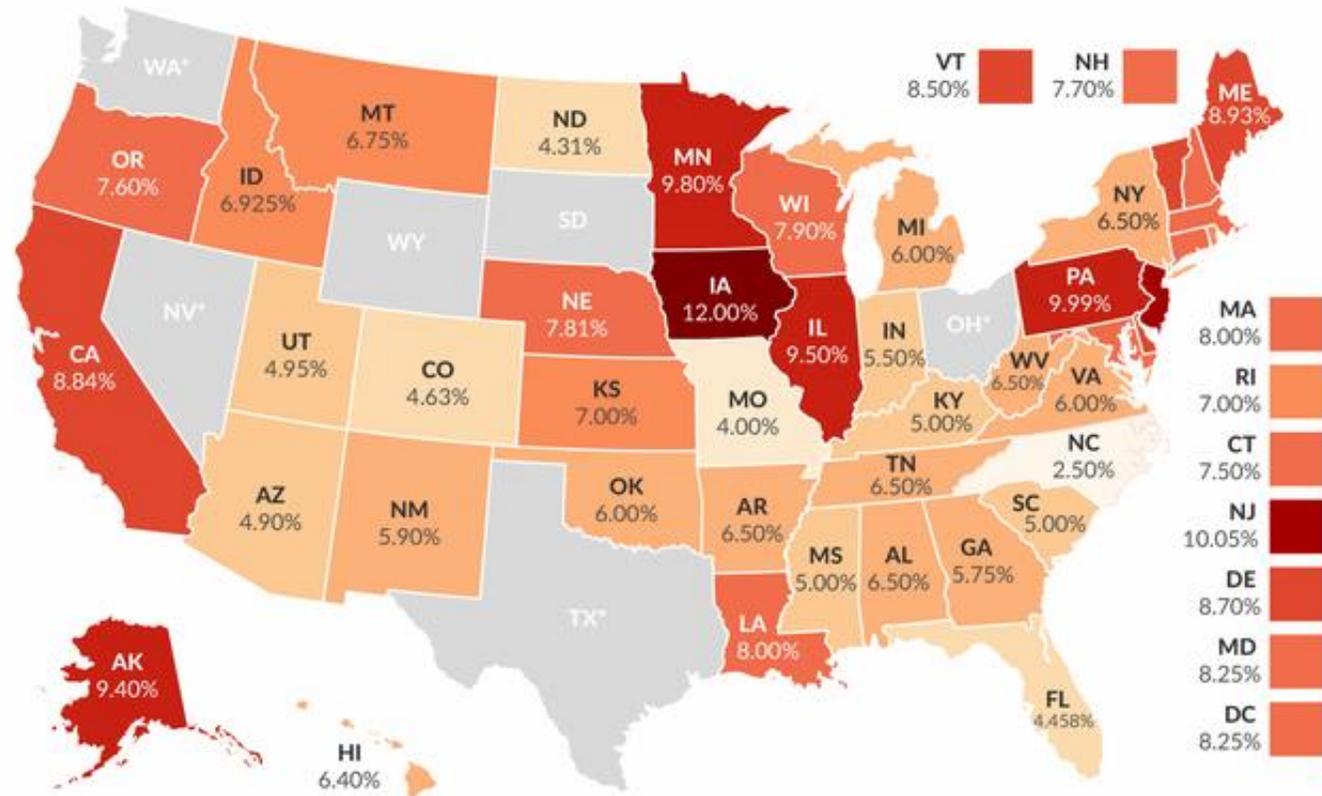


Corporate income tax in other states

- 44 states have a corporate income tax.
- 15 of these states (including Vermont) have different rates that apply to different income brackets.
- The remainder levy a single tax rate on all levels of corporate income.
- Note that apportionment factors and determination of net income across states differs so looking at the rate is only part of the story.
- Vermont's current 8.5% top corporate income tax rate starts at \$25,000 of net income.
 - At \$25,000 California (8.84%), Delaware (8.7%), Illinois (9.5%), Minnesota (9.8%), and Pennsylvania (8.9%) have higher tax rates at that level.
- <https://taxfoundation.org/data/all/state/state-corporate-income-tax-rates-brackets-2023/>



Top Marginal Corporate Income Tax Rates as of January 1, 2020



Note: (*) Nevada, Ohio, Texas, and Washington do not have a corporate income tax but do have a gross receipts tax with rates not strictly comparable to corporate income tax rates. Delaware and Oregon have gross receipts taxes in addition to corporate income taxes, as do several states like Pennsylvania, Virginia, and West Virginia, which permit gross receipts taxes at the local (but not state) level. Florida's corporate income tax rate will return to 5.5% for tax years beginning on or after Jan. 1, 2022. Georgia's corporate income tax rate will revert to 6% on January 1, 2026. The state could see a drop to 5.5% in 2020, pending legislative approval. Illinois' rate includes two separate corporate income taxes, one at a 7% rate and one at a 2.5% rate. Indiana's rate will change to 5.25% on July 1, 2020. The rate is scheduled to decrease to 4.9% by 2022. Mississippi continues to phase out the 3 percent bracket by increasing the exemption by \$1,000 a year. This year, the exemption is \$3,000. By the start of 2022, the 3 percent bracket will be fully eliminated. New Hampshire's rate is 7.9% for tax periods ending before Dec. 31, 2019. In New Jersey, the rates indicated apply to a corporation's entire net income rather than just income over the threshold. A temporary surcharge is in effect, bringing the rate to 10.5 percent for businesses with income over \$1 million. In addition to regular income taxes, many states impose other taxes on corporations such as gross receipts taxes and franchise taxes. Some states also impose an alternative minimum tax and special rates on financial institutions.

Sources: Tax Foundation; state tax statutes, forms, and instructions; Bloomberg Tax



Corporate Income Tax Forecast Overview

- The January 2024 consensus forecast estimates corporate income tax revenue will generate \$241.5 million in revenue in FY2024. This equates to approximately 11.3% of total forecasted General Fund revenue in FY24.
- This represents a downgrade of approximately \$1.2 million or 0.5% from the July 2023 consensus forecast.
- CI tax revenue was approximately \$281.4 million in FY23. The January 2024 forecast represents a decrease of \$39.9 million or 14.2% from the prior year.



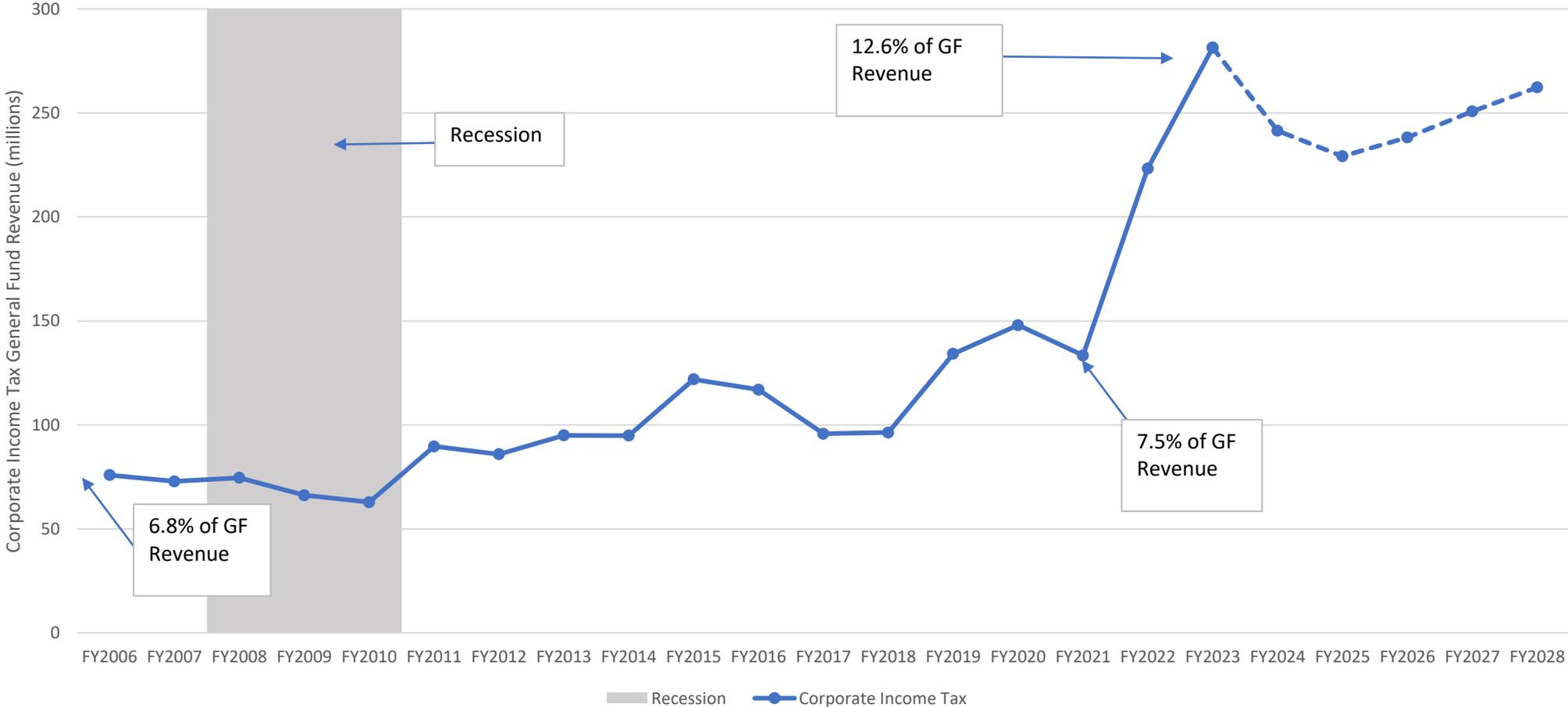
Corporate Income Tax Overview

- In the first six months of the FY24 corporate income revenue was below the July consensus forecast by approximately \$7.7 million or -7.3%.
- The consensus forecast notes that corporate income tax receipts will face growing headwinds as the economy is expected to continue to slow in the next year.
- After an initial decrease in CI revenue in FY24 and FY25 the forecast estimates revenues will start growing steadily in the years after.
- CI revenue is projected to remain about 11% of total General Fund revenue going forward.



Corporate Income Tax Collections since FY2006

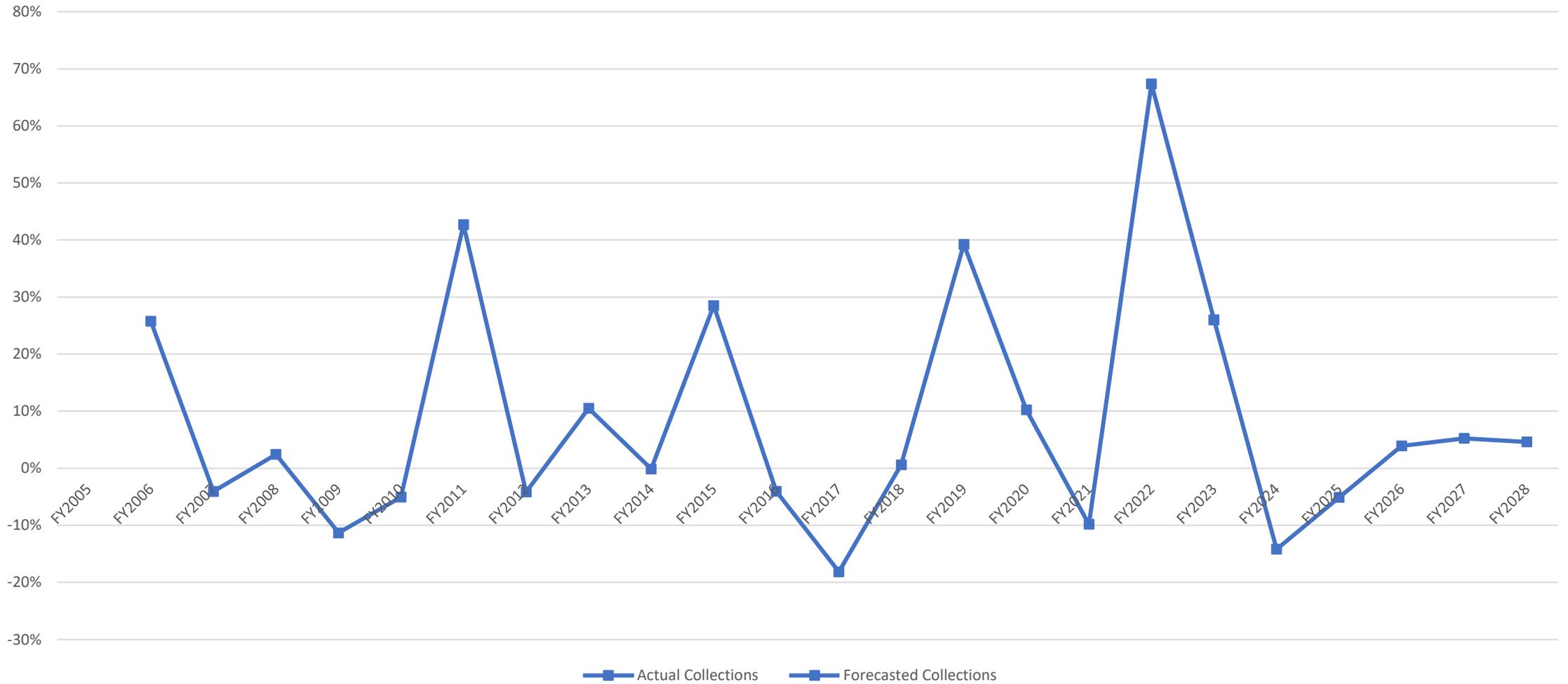
(Not Adjusted for Inflation)



Source: January 2024 Consensus Revenue Forecast



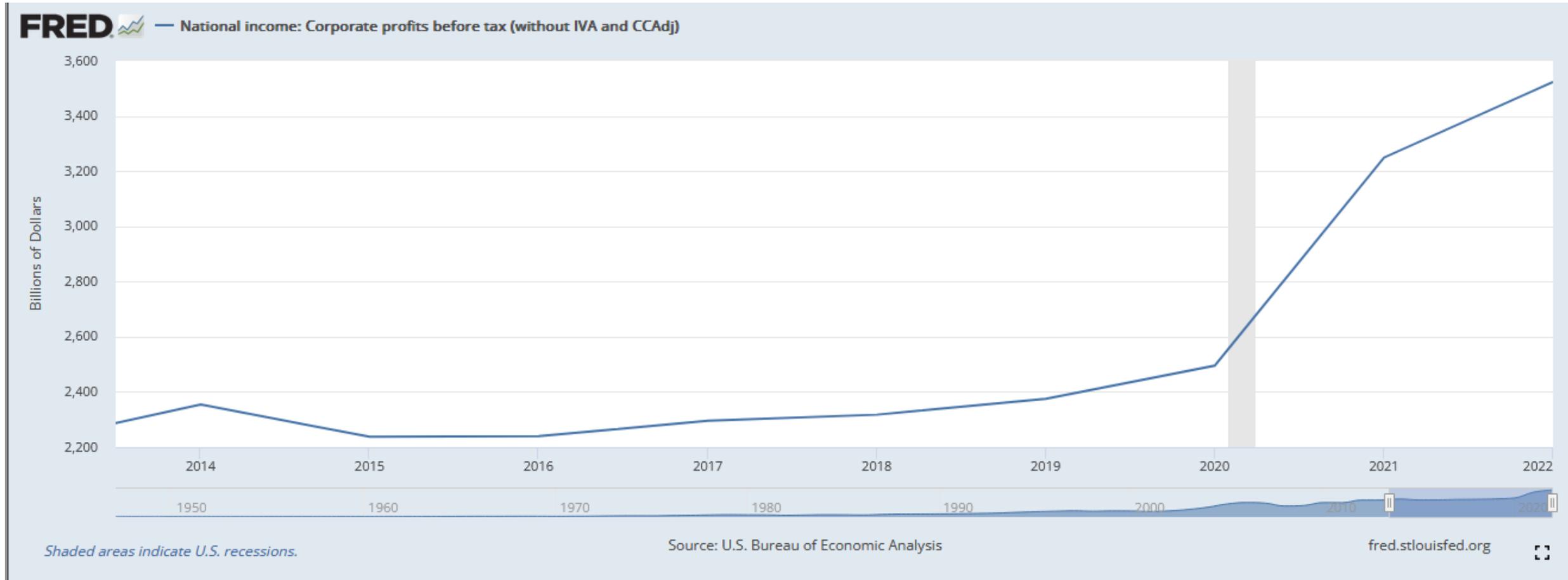
Percent Change in Corporate Income Tax Collections



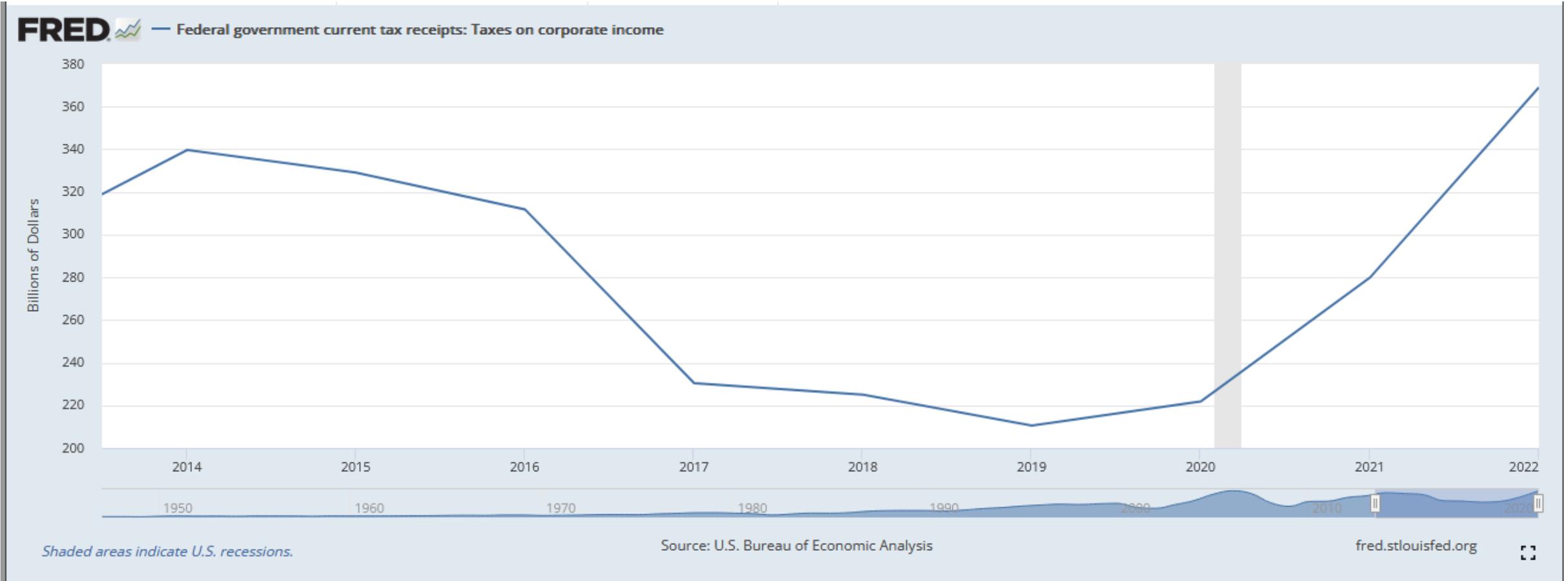
Source: January 2024 Consensus Revenue Forecast



Corporate Profits - Nationally



Federal Corporate Tax Collections



Recent Corporate Tax Law Changes

- Repeal of 80/20 language
- Single sales factor
- Joyce to Finnigan Methodology
- Throwback rule repeal
- Minimum Corporate Taxes



Recent Corporate Tax Law Changes

- The structure of the corporate tax changes effective for tax year 2023 is largely expected to be revenue neutral. Many of the changes represented a modernization of the VT corporate tax code.
- More and better information on the effects of these changes will be available towards the end of this year.
- More details can be found in the fiscal note: https://ljfo.vermont.gov/assets/Publications/As-Passed-by-the-General-Assembly/bc8de0f4f0/GENERAL-361032-v5-S_53_Fiscal_Note_2022_Session.pdf

Table 1: Fiscal Impacts of S.53, Committee of Conference (in millions)				
Section	Description	FY2023	FY2024	FY2025
1	Repeal of 80/20 Language	\$0.83	\$2.28	\$2.29
2	Corporate Minimum Tax Changes	\$0.83	\$2.33	\$2.33
3	Change to Single Sales Apportionment Factor	-\$4.01	-\$11.00	-\$11.05
3	Throwback Rule Repeal	-\$0.30	-\$0.85	-\$0.85
5	Joyce to Finnigan Methodology	\$2.65	\$7.27	\$7.30
Overall Fiscal Impact (General Fund)		\$0.00	\$0.02	\$0.02



Worldwide Reporting Overview



Will corporations end up paying more or less?

- The relative profitability of a unified group's foreign and domestic subsidiaries largely determine if they end up paying more.
- Reminder: A corporation's net income that is taxable in Vermont is determined by their sales factor.
- Adding foreign income will increase the net income portion of the equation, but at the same time decrease the sales factor.
 - Whether a firm pays more under WWCR is ultimately determined by the relative profitability of foreign and domestic subsidiaries.
 - However, multinationals that shift income to foreign subsidiaries that hold intellectual property are likely to pay more under WWCR.



Will corporations end up paying more or less?

Same Profitability			
Geography	Sales	Profitability	Profits
Domestic	10,000	10%	1,000
Foreign	10,000	10%	1,000
Reporting Type	Water's Edge	Worldwide	
Profits	1,000	2,000	
Sales Factor	100%	50%	
Taxable Income	1,000	1,000	



Will corporations end up paying more or less?

More Profitable Domestically			
Geography	Sales	Profitability	Profits
Domestic	10,000	15%	1,500
Foreign	10,000	5%	500
Reporting Type	Water's Edge	Worldwide	
Profits	1,500	2,000	
Sales Factor	100%	50%	
Taxable Income	1,500	1,000	



Will corporations end up paying more or less?

Less Profitable Domestically			
Geography	Sales	Profitability	Profits
Domestic	10,000	5%	500
Foreign	10,000	15%	1,500
Reporting Type	Water's Edge	Worldwide	
Profits	500	2,000	
Sales Factor	100%	50%	
Taxable Income	500	1,000	



Estimated Revenue Impact of WWCR

- The most difficult factor to pinpoint in estimating the revenue impact on Vermont is what the value of foreign net income that would be pulled in under WWCR.
 - There is a significant range in recent estimates of net income that would be captured by WWCR from a variety of sources that include academic researchers and the Congressional Budget Office.
- Recent estimates range from \$142 billion to \$558 billion in net income that would be pulled in under WWCR.



Estimated Revenue Impact of WWCR

- Remember: more net income does not necessarily mean that revenue will increase. The share that is allocable to Vermont has to be determined.
- Recent example: Minnesota estimated the revenue impact of a shift to WWCR last year following a methodology presented by ITEP and using actual corporate returns to apportion income to the state.
 - <https://itep.org/a-simple-fix-for-a-17-billion-loophole/>
 - <https://www.revenue.state.mn.us/sites/default/files/2023-04/hf2883-combined-worldwide-reporting.pdf>
 - ITEP estimated in 2019 that Vermont would gain \$31 million if it shifted to WWCR.



Estimated Revenue Impact of WWCR

- JFO is assuming a net income base increase of \$432 billion, in line with recent academic research.
 - <https://www.nber.org/papers/w30086>
- We can make some assumptions about the portion of that income attributable to Vermont and therefore taxable.
- JFO's preliminary annualized estimate of the revenue impact of shifting to WWCR is an increase between \$20 million and \$60 million.
 - This range will be further refined pending updated data on Vermont apportionment.

