

CORPORATE INCOME TAX

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House Ways and Means - January 19, 2024

Corporate Income Tax (CIT)

Today's focus:

- ▶ Unitary Returns
- ▶ Allocation and Apportionment

CIT Structure

- **Tax Base:** Vermont net income
 - 32 V.S.A. § 5811(18)
- **Tax Rates:**
 - progressive brackets, marginal tax rates
 - minimum tax based on Vermont gross receipts
 - 32 V.S.A. § 5832
- **Tax Liability:** allocation and apportionment
 - 32 V.S.A. § 5833

Current Law: Who Pays?

- ONLY U.S. resident C Corporations
- Individuals and “pass-through” businesses do NOT pay corporate income tax

Current Law: Who Pays?

- U.S. resident C Corporations
 - Incorporated entities (ending in names like: Inc., Corp., etc.)
 - Creation of separate legal person, which provides shareholders protection from personal liability.
 - “C” corporation” refers to the subchapter of the Internal Revenue Code.
 - Corporate income tax is imposed on the entity; not on individual shareholders.
 - Shareholders then pay personal income taxes on dividends and capital gains on the appreciation of shares.
 - Advantage: ability to raise money on public markets.

CIT: Who Does NOT pay?

Individuals, “pass-through” businesses, and foreign entities do not pay corporate income tax.

- Foreign controlled corps. pay a limited amount, which passes through from the federal return
- Business structure: partnerships, limited liability companies, S Corporations, sole proprietors.
- Income tax is generally not imposed on pass-throughs at the entity level.
 - Instead, income passes through directly to the members (or partners, owners, sole proprietor, etc.), who are then taxed under the personal income tax.

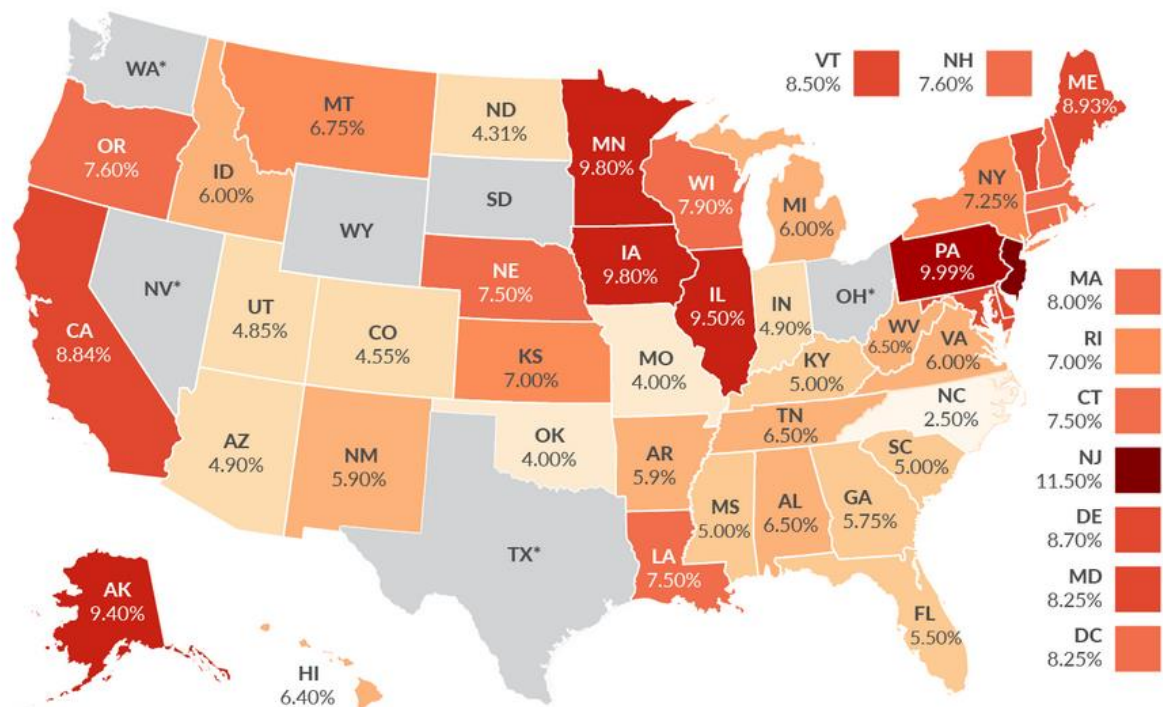
CIT Definitions: Vermont Net Income

- Vermont taxes C corporations' "net income"
- "Net income" starts with federal taxable income, plus and minus certain items of income.
 - No deductions allowed for bonus depreciation, non-VT bond interest, or federal operating losses.
 - Deductions allowed for certain income added at the federal level related to foreign credits and job-creating credits. Cannabis establishments may now deduct business expenses in Vermont.

CIT Definitions: Federal Taxable Income

- Federal taxable income is a corporation's receipts minus allowable deductions, including:
 - cost of goods sold, wages and other employee compensation expenses, interest, nonfederal taxes, depreciation, and advertising.

Top State Marginal Corporate Income Tax Rates as of July 1, 2022



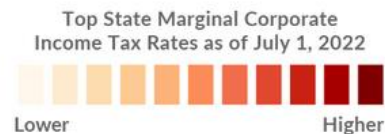
Note: In addition to regular income taxes, many states impose other taxes on corporations such as gross receipts taxes and franchise taxes. Some states also impose an alternative minimum tax and special rates on financial institutions.

*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.

Connecticut charges a 10% surtax on a business's tax liability if it has gross proceeds of \$100 million or more, or if it files as part of a combined unitary group. This surtax was recently extended and is scheduled to expire on January 1, 2023.

Illinois' rate includes two separate corporate income taxes, one at a 7% rate and one at a 2.5% rate. In New Jersey, the rates indicated apply to a corporation's entire net income rather than just income over the threshold. A temporary and retroactive surcharge is in effect from 2020 to 2023, bringing the rate to 11.5% for businesses with income over \$1 million.

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



CIT Minimum Tax

- A minimum tax applies to all active corporations (including LLCs electing to be taxed as C corporation).
- The minimum tax is based on the amount of the corporation's Vermont gross receipts.

Vermont gross receipts	Min. tax amount
\$0-100,000	\$250
\$100,001-\$1 million	\$500
Over \$1 million to \$5 million	\$2,000
Over \$5 million to \$300 million	\$6,000
Over \$300 million	\$100,000

Identifying Corporate Income

- What is the income of the taxpayer?
 - Unitary combined reporting v. separate reporting
- How is income is apportioned to the State?
 - Apportionment Factors

Identifying Corporate Income

- Most multistate corporations have complex organizational structures composed of a “parent” corporation and a number of “subsidiary” corporations owned by the parent.
- There are generally two approaches to reporting income: separate or combined reporting.

Identifying Corporate Income

- **Separate reporting** treats transactions between affiliated companies as though they were unrelated entities, so each entity files its own return. As a result, intercompany transactions may be deductible expenses (e.g., as cost of goods sold). This enables corporations to shift income between affiliated companies to reduce tax liability.
- **Combined reporting** treats affiliated companies that are part of a “unitary group” as one entity for tax purposes, so the group only files one return.

Unitary Combined Reporting

- “Unitary business” means one or more related business organizations engaged in business both within and outside the State among which there exists a **unity** of ownership, operation, and use; or an **interdependence** in their functions. 32 V.S.A. § 5811(23); Vt. Reg. § 1.5862(d) – 6.
- “Affiliated group” means a group of two or more corporations in which more than 50 percent of the voting stock of each member corporation is directly or indirectly owned by a common owner or owners, either corporate or noncorporate, or by one or more of the member corporations, but shall exclude corporations taxable under 8 V.S.A. § 6014 [captive insurance companies]. 32 V.S.A. § 5811(22); Vt. Reg. § 1.5862(d) – 4.

Unitary Combined Reporting

- Unitary combined reporting applies to:
 - Multi-state businesses that are part of a unitary group; and
 - the portion of the unitary business that occurs both within and outside (as of 2023) the U.S. borders.
- Unitary combined reporting does not apply to:
 - S corporations; or
 - Captive insurance companies.

CIT Allocation and Apportionment

- Multistate corporations typically have different member entities that operate in and receive income from different taxing jurisdictions.
 - When a C Corp's income is derived entirely from within Vermont, all the C Corp's Vermont net income is allocated to Vermont.
 - When a C Corp's income is derived from both within and outside Vermont, Vermont law apportions a corporation's income that is allocated to the State based on a statutory formula. 32 V.S.A. § 5833(a).

CIT Apportionment

- Historically, apportionment formulas looked at property, payroll, and sales, but the recent trend has been to increase the importance of the sales factor.
 - Many states counted the sales factor twice or more (double or triple weighting).
 - When Vermont enacted unitary combined reporting in 2004 (effective TY 2006), its apportionment factors were also changed from 3 equally weighted factors to a double-weighted sales factor.
 - More recently, many states, including Vermont as of 2023, have moved to a “single sales factor,” where sales is the only factor used in apportioning net income to the state.

STATE APPORTIONMENT OF CORPORATE INCOME

(Formulas for tax year 2022 -- as of January 1, 2022)

ALABAMA *	Sales	MONTANA *	Double wtd Sales
ALASKA*	3 Factor	NEBRASKA	Sales
ARIZONA *	Sales/Double wtd Sales	NEVADA	No State Income Tax
ARKANSAS *	Sales	NEW HAMPSHIRE (3)	Double wtd Sales
CALIFORNIA *	Sales	NEW JERSEY	Sales
COLORADO *	Sales	NEW MEXICO *	3 Factor/Sales
CONNECTICUT	Sales	NEW YORK	Sales
DELAWARE	Sales	NORTH CAROLINA *	Sales
FLORIDA	Double wtd Sales	NORTH DAKOTA *	3 Factor/Sales
GEORGIA	Sales	OHIO	N/A (2)
HAWAII *	3 Factor	OKLAHOMA	3 Factor
IDAHO *	Double wtd Sales	OREGON	Sales
ILLINOIS *	Sales	PENNSYLVANIA	Sales
INDIANA	Sales	RHODE ISLAND	Sales
IOWA	Sales	SOUTH CAROLINA	Sales
KANSAS *	3 Factor	SOUTH DAKOTA	No State Income Tax
KENTUCKY *	Sales	TENNESSEE	Triple wtd Sales
LOUISIANA	Sales	TEXAS	Sales
MAINE *	Sales	UTAH	Sales
MARYLAND	Sales	VERMONT	Double wtd Sales
MASSACHUSETTS	Sales/Double wtd Sales	VIRGINIA	Double wtd Sales/Sales
MICHIGAN	Sales	WASHINGTON	No State Income Tax
MIDNESOTA	Sales	WEST VIRGINIA *	Sales
MISSISSIPPI	Sales/Other (1)	WISCONSIN *	Sales
MISSOURI *	Sales	WYOMING	No State Income Tax
		DIST. OF COLUMBIA	Sales

Source: Compiled by FTA from state sources.

Notes:

The formulas listed are for general manufacturing businesses. Some industries have a special formula different from the one shown.

* State has adopted substantial portions of the UDITPA (Uniform Division of Income Tax Purposes Act).

Slash (/) separating two formulas indicates taxpayer option or specified by state rules.

3 Factor = sales, property, and payroll equally weighted.

Double wtd Sales = 3 factors with sales double-weighted

Sales = single sales factor

(1) Mississippi provides different apportionment formulas based on specific type of business. A single sales factor formula is required if no specific business formula is specified.

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(2) Ohio Tax Department publishes specific rules for situs of receipts under the CAT tax.

(3) New Hampshire will use a Single Sales Factor for tax years ending on or after 12/31/22.

Act 148 of 2022 changed Vermont to a single sales factor state as of 2023

Source: [Federation of Tax Administrators](#)

CIT: Determining Jurisdiction (Joyce v. Finnigan)

- “Joyce” and “Finnigan” are methods to determine state jurisdiction over a corporation’s income for apportionment purposes. The names refer to several California tax court cases.
 - *Joyce* method looks at each entity in a unitary group as a separate taxpayer and determines whether each entity has nexus in the state.
 - Only income from entities with nexus will be included in the apportionment formula.
 - *Finnigan* method considers the “taxpayer” to include all members of a unitary group.
 - Once one entity in a unitary group has nexus in the state, then the entire group has nexus and income from all entities is included in the apportionment formula.

CIT: Recent Federal Changes, TCJA 2017

Federal Tax Cuts and Jobs Act, enacted Dec. 22, 2017

- Move from a modified worldwide system to a territorial system, with simultaneous repatriation of profits, and decrease in corporate income tax rates.
 - Federal corporate tax rate is a flat 21%, lowered by TCJA from top rate of 35%.
 - TCJA eliminated tiered corporate income tax rates and 20% corporate alternative minimum tax.

Vermont's response

- *Rates*: No response, because Vermont's income tax rates are already decoupled from the federal rates.
- *Income*: Vermont's existing definition of corporate income was sufficient to capture one-time federal revenue changes such as the repatriation of certain deferred foreign profits.

CIT Recent VT Changes: Act 148 of 2022

Beginning Jan. 1, 2023:

- Only apportionment factor is sales (“single sales factor”)
- VT given jurisdiction over all corps in unitary group when 1 corp in group has nexus with VT (*Finnigan* method)
- 80/20 rule repealed, which excluded overseas corps from apportionment factors
- “Throwback” rule repealed, which added back income from corps in a unitary group that was not taxable in another state
- New minimum tax brackets and amounts