

HJR 177/SJR 101 - Joint Subcommittee studying Benefits of Adopting a Single Sales Factor for Corporate Income Tax Purposes

(<http://dls.state.va.us/ssf.htm>)

August 27, 2008

Organization and Opening Remarks

During its first meeting, which was held in Richmond, the joint subcommittee studying the benefits of adopting a single sales factor for corporate income tax purposes elected Delegate Kathy Byron and Senator Walter Stosch as co-chairmen. Then they discussed the purpose of the study which is to decide whether the current double-weighted sales factor formula used to calculate a corporation's Virginia taxable income should be changed to a single sales factor formula in order to attract new manufacturers to the Commonwealth as well as encourage those already here to expand. Following these comments, the other members of the joint subcommittee introduced themselves and provided some background about themselves. In addition to the co-chairs, the members of the joint subcommittee are Senators Charles J. Colgan, and Mary Margaret Whipple; Delegates Christopher K. Peace, Jimmie P. Massie, III, Adam P. Ebbin, and Albert C. Pollard, Jr.; Tax Commissioner Janie Bowen; Mr. Brad Gilks, Mr. Charles H. Majors, and Mr. William (Sandy) Rowe.

Presentations by the Staff

Next on the meeting agenda were presentations by the subcommittee staff. The first presentation outlined the history of Virginia's corporate income tax from its beginnings as a license tax in the early 1840's to the current system based on a corporation's net earnings. The Virginia corporate income tax applies to all domestic (incorporated in Virginia) and foreign (incorporated outside Virginia) corporations doing business in the state, with a few exceptions. Virginia's six percent corporate income tax applies to a corporation's Virginia taxable income, which is computed by using federal taxable income as the base. Most states (39 of the 45 states that impose a corporate income tax) conform their corporate tax, in general, to the federal system for much the same reason most states conform their individual income tax. For Virginia tax returns, modifications are made to federal taxable income in order to determine Virginia taxable income.

Virginia permits corporations engaged in multistate activities that have income taxable by Virginia and out-of-state political subdivisions to apportion

their Virginia taxable income through the following three-factor formula, so that different states do not impose a tax on the same income:

1. A Property Factor (25 percent): A ratio of the average real and tangible personal property value of the firm in Virginia to the firm's total average real and tangible personal property value.

2. A Payroll Factor (25 percent): A ratio of the payroll in Virginia to the firm's total payroll.

3. A Sales Factor (50 percent): A ratio of the sales in Virginia to the firm's total sales.

These ratios are added together with the sales factor doubled and divided by a denominator of four to determine the portion of total taxable income subject to the Virginia corporate income tax. Because the sales factor is doubled, this is referred to as the double-weighted sales factor formula. However, if there is no sales factor, then the denominator will be the number of existing factors and where there is a sales factor but no payroll or property factor, the denominator will be the existing factors plus one. Also, a corporation can petition the Tax Commissioner to use a different allocation formula if the three-factor formula is inherently unfair to the particular corporation.

The second staff presentation provided a comparison of other states that have an apportionment formula that includes a sales factor for computing the corporate income tax. There are 20 states that currently use the single sales factor or offer it as an option for businesses to use in calculating their corporate income tax liability. Those neighboring states of Virginia that use the single sales factor formula or offer it as an option are Kentucky, Georgia, Maryland, and South Carolina. A sales factor that is at least double weighted is utilized by 16 states, including Virginia, while 11 states impose an equally weighted payroll, property, and sales factor formula. Finally, between 2000 and 2007, seventeen states increased the weighting of the sales factor but no state decreased it.

Other Business

The co-chairmen opened the floor to comments and two individuals took the opportunity to speak. One was the executive director from Net Choice, an IT company in the Washington, DC area and the other was the executive director of the Commonwealth Institute. The Net Choice speaker asked the joint subcommittee members to consider not only the single sales factor for manufacturers but to also examine the method used by service providers (cost of performance) in calculating their taxable income. He suggested that using a customer base/where the service is delivered rather than where the service originates is a better method for service providers such as Net Choice and other technology companies.

The Commonwealth Institute spokesperson urged the members to examine what happened to manufacturing in Virginia when the state adopted the double weighted sales factor formula in the first part of this decade. Has the number of manufacturing jobs grown since then? Also, do not forget the property and payroll factors and why they are important to the process. Finally, he suggested that if the single sales factor is adopted in Virginia it should be performance based in order to measure job growth or loss among manufacturers following its enactment.

Finally, members asked questions the answers to which will be provided during the next meeting of the joint subcommittee. There being no further business, the meeting was adjourned.

Future Meetings

The joint subcommittee may meet up to three more times and must complete their work by November 30, 2008, with an executive summary of their findings and recommendations due no later than January 14, the first day of the 2009 General Assembly session. Currently, meetings are scheduled for September 30 and October 21 at 10:00 a.m. The September 30th meeting will be held in Richmond in Senate Room B. The meeting agenda will be posted on the study's website (<http://dls.state.va.us/ssf.htm>) at least one week prior to that meeting.