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)

September 30, 2008

Opening Remarks

The joint subcommittee studying the benefits of adopting a single sales factor for corporate income tax purposes held its second meeting in Richmond. Co-chair Walter Stosch welcomed everyone after calling the meeting to order. Following his comments, the members of the joint subcommittee who were absent from the August meeting introduced themselves. Then the presentations began.

Legislative and Tax Department staff presentations

Mark Vucci, staff to the joint subcommittee, provided and reviewed a list of the states that have adopted the single sales factor formula and the year of adoption, beginning with those prior to 2001 (Illinois, Iowa, Massachusetts, Missouri, Nebraska, and Texas) and ending with the 2009 tax year (Colorado). There are 23 states that have adopted the single sales factor formula for implementation immediately or over a set number of years.

Next on the agenda from the Department of Taxation were Mark Haskins, Director of the Policy Development Division, and John Josephs, Senior Lead Tax Policy Analyst in the Policy Development Division. Mr. Haskins provided the joint subcommittee members with a table showing a variety of tax incentives/benefits that are available to the manufacturing industry. These benefits are found in sales and use tax exemptions, local tax preferences (machinery and tools tax, intangible personal property tax, tangible personal property tax, BPOL tax), and conformity with the federal Internal Revenue Code. Mr. Haskins also distributed a chart showing the corporate income tax revenue collections for 1997 through 2007. The outstanding feature was the volatility of the tax with a 35.7% decrease in revenues for 2001 and a 44.9% increase in 2005. Finally, the apportionment of income from sales of services and intangibles by the cost of performance formula was discussed by Mr. Haskins. In Virginia, the formula is a single factor based on costs of performance in the state over costs of performance everywhere the company sells services. Virginia's apportionment method for sales of services and intangibles seems to be the way the majority of states calculate such sales.

Mr. Josephs gave an in depth look at Virginia's apportionment formula, which is currently in the mainstream with other states. Changing it to a mandatory single sales factor formula will increase the tax liability for some corporations, decrease it for others and have little, if any, impact for most. Corporations having significant operations in Virginia that produce more than they sell in the state would see their corporate income taxes reduced. However, corporations with minor operations in Virginia that sell more than they produce here would owe more corporate income taxes. Those corporations with mostly equal operations and sales in Virginia would experience very little change in their taxes. If the single sales factor formula is enacted in Virginia for all corporations, there would be a significant corporate income tax revenue loss, according to the Tax Department. Based on 2006 tax returns, if all corporations used the single sales factor, the estimated loss would equal $47.4 million and if it were optional, it would rise to $122.7 million. There would be 136 winners, 132 losers, and 29 with no change in taxes owed. If only manufacturers were allowed to use the single sales factor, the estimated loss would equal $33.9 million and if it were optional, it would increase to $64.7 million. In this case, there would be more losers (40) than winners (37) and only 4 would have no change in taxes owed, if manufacturers were required to use the single sales factor apportionment formula.

Commonwealth Institute for Fiscal Analysis

Mr. Michael Cassidy, Executive Director of the Commonwealth Institute for Fiscal Analysis, in his presentation labeled the single sales factor as "an economic development tool that isn't." His main points were:

1. The single sales factor does not have a positive record as an effective economic development tool.
2. The single sales factor is unfair tax policy for Virginia businesses with few or no out-of-state sales.
3. The single sales factor is a no-strings-attached tax giveaway.
4. Virginia already ranks at the top as a business-friendly state.
5. If Virginia's manufacturer's are paying less, her residents will end up paying more.
6. The real cost of the single sales factor is unclear.

The Commonwealth Institute for Fiscal Analysis is an independent, non-partisan, nonprofit that provides information and analyses of state public policies.

Virginia Economic Development Partnership (VEDP)

Workforce development is the number one priority of VEDP, according to its Director of Research, Mr. Rob McClintock. However, it is also important to keep businesses in Virginia and VEDP is always developing innovative methods to do that. When companies consider Virginia as a place to do business they consider several factors -- workforce, markets, buildings and infrastructure, quality of life, and business climate. Virginia's business climate has been highly rated by a number of organizations including Forbes.com, CNBC, Pollina, and Tax Foundation.

In considering a tax policy change, such as the single sales factor, Mr. McClintock suggested a need for in-depth analysis of the change, do no harm, promote fairness, and improve the business climate. What will do the most good for the most businesses? All agreed that maintaining Virginia's competitive business environment is of utmost importance.

Virginia Society of Certified Public Accountants (VSCPA)

The final presentation came from four representatives of VSCPA -- Emily Walker, Art Auerbach, Damon DeSue, and Teresa Jordan. The VSCPA strongly supported the legislation that created the joint subcommittee study to examine the single sales factor formula. They recommended as part of the study methodology asking to whom should this apply? How would it be implemented? And what are additional changes that should be considered in this process?

As far as the single sales factor, VSCPA's position is neutral. They do think it is important to look at the impact of adopting the single sales factor and to be well balanced in this examination. In examining economic development incentives, the impact on investment and on employment should be considered. As far as fiscal impacts on tax collections, net losses and gains need to be determined and the shift of tax collections from corporate to individual income tax, sales and use taxes and other taxes should be analyzed.

Other questions to consider are:

1. Will the single sales factor formula apply to all industries or only targeted industries?

2. Will it be phased in over several years or implemented immediately?

3. Will its application be optional or mandatory?

Finally, it should be determined who are the winners and who are the losers before the single sales factor formula is enacted in order to make an informed decision. In conclusion, the VSCPA representatives offered their continued assistance with the study.

There being no further business, the meeting was adjourned.

Next Meeting

The third meeting of the joint subcommittee is scheduled for October 21 at 10:00 a.m. At that meeting, the Virginia Manufacturer's Association will make a presentation and staff will review two studies that were done with regard to New York's and Georgia's single sales factor experience. The meeting agenda will be posted on the study's website *(http://dls.state.va.us/ssf.htm)* prior to that meeting.