



The Single Sales Factor for Corporate Income Taxes

Is it Really a Good Deal for Florida?

Some representatives of the business community are urging the Florida Legislature to change the “apportionment formula” that is used to determine a multistate corporation’s nationwide profit that is subject to Florida’s corporate income tax. Instead of calculating Florida’s corporate income tax on the portion of the multi-state corporation’s sales, property and payroll (a three-factor formula) as a percentage of the total, they advocate for a substantial change that would base a corporation’s tax on only the portion of sales in our state – a single sales factor. It is argued that this approach will stimulate job creation and investment by producing/manufacturing businesses. However, there is little evidence that would actually happen. Rather, the lost tax revenue that will result from changing the apportionment formula may impair the ability of Florida to provide vital and critical services needed.

Florida’s current apportionment formula considers sales (50%), property (25%) and payroll (25%). Companies that have relatively large shares of their jobs and facilities in Florida, but primarily sell their products outside of Florida argue that Florida’s current apportionment formula penalizes them for investing more capital in our state to expand their production facilities and increase jobs. Hence, corporate interests with a corporate model such as this would have a substantial tax decrease in Florida corporate income tax under a single sales factor for apportionment. In the extreme, a manufacturing company that produced its entire product in Florida but sold it all outside of Florida would pay no corporate income tax to Florida!

In contrast, companies with a relatively small share of property and payroll in Florida, but a significant share of their total sales in our state, would experience an increase in their corporate income tax. In other words, if Florida were to change to a single sales factor some corporations would receive tax cuts and others would experience a tax increase.

The three-factor formula recognizes that a state provides a range of services to a corporation’s property and workers and provides a market for the products of the company, and therefore the corporate income tax levied against that company should consider all three factors.

Corporations benefit from a wide range of governmental services that specifically relate to the extent of property and payroll in a state. Under the single sales-only formula, only the portion

of the corporation's sales in the state are considered even if 90% of its employees and property are within the state. Therefore, a single sales factor apportionment formula is inconsistent with the fundamental principle behind the corporate income tax - that a corporation should pay taxes to a state as compensation for the benefits it receives from state services (environmental impact, police protection, transportation infrastructure, educated workforce, etc.) and the ability to market its products in the state. The change from a property-payroll-sales formula to a sales-only formula substantially reduces the corporate tax burden of businesses that arguably are benefiting the most from public services in a state and unfairly shifts the tax burden to out-of-state businesses (or in-state businesses that have a high sales factor) that benefit from state services to a lesser extent.

If all states adopted a single sales factor (SSF) apportionment approach there would be no competitive advantage to multistate corporations. However, with the current patchwork of apportionment formulae and different tax rates, an out-of-state corporation that would pay higher corporate taxes if Florida changes to a sales-only formula would have an incentive to remove all of its property and employees from our state to eliminate its tax liability. These companies would argue that a lack of physical presence means there is no "nexus" and therefore they cannot be taxed at all no matter how much of their product they sell in Florida. Therefore, switching to a single sales factor may cause some companies with significant sales outside of Florida to expand their operations in our state (as proponents argue) but it may also lead some companies to pull out of the state (unintended consequence) leading to both job gains and losses.

The Center examined the relationship between job trends in the manufacturing sector and the nature of each state's apportionment formula. If the single sales factor formula is an incentive for job growth, it would be expected that those states with such a formula would lead the country in job growth in manufacturing. Table 1 illustrates that the only trend that exists is that there is no direct relationship. Of the 18 states with a single sales factor (either implemented or approved for implementation), nine are above and nine are below the median percentage of employment change in manufacturing for the period December 2001 to December 2007.ⁱ

Notwithstanding the benefits and costs associated with changing Florida's corporate income tax apportionment formula to attract manufacturers to Florida, it should be noted that in total, manufacturing is a declining sector of the national economy. Between 2001 and March 2009, manufacturing jobs in the U.S. have decreased from 16,441,000 to 12,310,000.ⁱⁱ Clearly, Florida and the nation's economic future are not in manufacturing.

It is also important to examine what happens to a state's corporate income tax revenue when it changes to a single sales factor. For example, the state of California enacted a Single Sales Factor tax apportionment during the 2009 Assembly session (effective tax year 2011). As noted in the California Senate bill analysis, the fiscal impact will exceed \$1.45 billion by FY 2012-13 (approximately 15% of the total corporate income tax revenues), "...with additional and

growing losses in subsequent years.”ⁱⁱⁱ Earlier research found that a similar trend in revenue reduction was probable in states adopting a single sales factor apportionment formula.^{iv}

These findings strongly suggest that changing Florida’s corporate income tax apportionment formula to a single sales factor would not be a good deal for our state. Harm from adoption of such a change would be even greater if the state did not first make other reforms to its corporate income tax policy. As further support for this admonition, the Senate Select Committee for Florida’s Economy Florida was advised by the Haas Center (its contractor for economic advice and recommendations) that any consideration of the single sales factor should also implement the following in order to avoid “jurisdiction shopping:”

- A broad and inclusive economic nexus standard to keep the taxable base broad;
- Combined reporting to reduce incentives to declare costs in one place and profits in another;
- Business level tax on LLC’s to avoid inequity between C corporations and LLC’s; and
- A throwback rule to capture “nowhere income.”^v

Florida already has one of the lowest corporate income tax rates in the country at 5.5%. As the Center already recommended (<http://www.fcfe.org/Documents/CloserLookTaxProposal.pdf>), we believe the best deal for Florida and its business partners is to make the corporate income tax fairer by closing corporate loopholes and eliminating the advantage certain businesses have due to a particular legal structure, and ultimately, reducing the corporate income tax rate to attract **all types of businesses** to Florida, not just manufacturers.

Table 1 - Selected State Corporate Income Tax (CIT) Characteristics

State	CIT Apportionment Formula Type	Maximum Corporate Income Tax Rate	Manufacturing Employment Change December 2001 - December 2007
Alabama	Equal 3F	6.50%	-6.7%
Alaska	Equal 3F	9.40%	13.3%
Arizona	>50% SF	6.97%	-5.8%
Arkansas	2xSF	6.50%	-15.0%
California	SSF (effective 2011)	8.84%	-14.0%
Colorado	Equal 3F or 2F	4.63%	-14.3%
Connecticut	SSF *	7.50%	-13.0%
Delaware	Equal 3F	8.70%	-10.4%
Florida	2xSF	5.50%	-11.2%
Georgia	SSF	6.00%	-12.1%
Hawaii	Equal 3F	6.40%	-5.0%

Idaho	2xSF	7.60%	-0.5%
Illinois	SSF	7.30%	-13.3%
Indiana	SSF (effective2011)	8.50%	-7.6%
Iowa	SSF	12.00%	-0.3%
Kansas	Equal 3F	4.00%	-2.4%
Kentucky	2xSF	6.00%	-11.0%
Louisiana	SSF *	8.00%	-3.1%
Maine	SSF	8.93%	-16.6%
Maryland	SSF *	8.30%	-19.0%
Massachusetts	SSF *	9.50%	-20.2%
Michigan	SSF	4.95%	n/a
Minnesota	SSF (effective2014)	9.80%	-7.4%
Mississippi	2xSF	5.00%	-12.4%
Missouri	SSF	6.25%	-11.1%
Montana	Equal 3F	6.75%	-1.4%
Nebraska	SSF	7.81%	-5.7%
Nevada	none	n/a	n/a
New Hampshire	2xSF	8.50%	-12.6%
New Jersey	2xSF	9.00%	-18.9%
New Mexico	Equal 3F or 2xSF	7.60%	-7.2%
New York	SSF	7.50%	-19.4%
North Carolina	2xSF	6.90%	-19.8%
North Dakota	Equal 3F	6.50%	9.3%
Ohio	>50% SF	8.50%	-15.8%
Oklahoma	Equal 3F	6.00%	-8.8%
Oregon	SSF	6.60%	-1.0%
Pennsylvania	>50% SF	9.99%	-17.2%
Rhode Island	Equal 3F *	9.00%	-23.1%
South Carolina	SSF *	5.00%	-17.0%
South Dakota	none	n/a	n/a
Tennessee	2xSF	6.50%	-13.9%
Texas	none	n/a	n/a
Utah	Equal 3F or 2xSF	5.00%	10.2%
Vermont	2xSF	8.50%	-17.8%
Virginia	2xSF	6.00%	-16.9%
Washington	none	n/a	n/a
West Virginia	2xSF	8.50%	-17.0%
Wisconsin	SSF	7.90%	-7.9%
Wyoming	none	n/a	n/a

* Includes variations to apportionment method

Source: “The “Single Sales Factor” Formula for State Corporate Taxes – A Boon to Economic Development or a Costly Giveaway”, Michael Mazerov, Center for Budget and Policy Priorities, September 2005 as updated.

ⁱ “The “Single Sales Factor” Formula for State Corporate Taxes – A Boon to Economic Development or a Costly Giveaway”, Michael Mazerov, Center for Budget and Policy Priorities, September 2005.

ⁱⁱ U.S. Bureau of Labor Statistics: <ftp://ftp.bls.gov/pub/supl/empsit.ceseeb1.txt>

ⁱⁱⁱ Bill analysis AB 15 X3 as amended February 14, 2009, the California Senate.

^{iv} The “Single Sales Factor” Formula for State Corporate Taxes – A Boon to Economic Development or a Costly Giveaway”, Michael Mazerov, Center for Budget and Policy Priorities, September 2005.

^v Select Committee on Florida’s Economy, Florida Senate, Meeting Packet, April 15, 2009.