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Fiscal Note

May 19, 2022 Graham Campbell, Senior Fiscal Analyst

S.53: An act relating to change to Vermont corporate income tax and conformity to federal tax laws

As Passed by the General Assembly

https://legislature.vermont.gov/Documents/2022/Docs/BILLS/S-0053/S-0053%20As%20Passed%20by%20Both%20House%20and%20Senate%20Official.pdf

Bill Summary

This bill makes numerous changes to Vermont corporate income tax laws. Changes include:

- Requiring corporations with subsidiaries with significant overseas operations to include that income as part of the total income for the corporation's sales apportionment (repeals 80/20 language).
- Changing the current corporate minimum tax structure, lowering the minimum tax for small corporations but raising it for larger ones
- Changing the state's apportionment factor to sales-only, from a three-factor apportionment formula.
- Repealing the rule that requires the throwback of sales to Vermont when a firm makes sales into a state where it is not taxed.
- Making changes to the determination of nexus for unitary taxpayers with subsidiaries (Joyce to Finnigan methodology).

The bill also links Vermont's income tax codes to the Federal income tax codes as written as of December 31, 2021.

Fiscal Impact

JFO estimates that this bill is net revenue neutral for the General Fund in FY2023 and will increase revenues by $20,000 in FY 2024. The individual sections in the bill raise and lower revenues for the State, but the aggregate impact is revenue neutral. See Table 1 for the fiscal impacts of S.53:

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**

Explanation/Detail

The following sections would have a fiscal impact.

Section 1: Repeal of 80/20 Language for Overseas Businesses

Under current law, if a corporation has a subsidiary whose primary source of sales comes from overseas sales (defined as 80% of total sales or more), it is excluded from the sales of the parent corporation for the purposes of determining their sales factor.[1]

This bill would change current law, to repeal that language so that any subsidiary operating in Vermont, even if 20% or less of its operations are based in the United States, would be counted as a member of a unitary group's sales for sales apportionment.

JFO estimates that this change will raise $830,000 in General Fund revenue in FY 2023 and $2.28 million in FY 2024. The change from FY2023 to FY2024 reflects a full tax year of implementation for corporations.

Section 2: Changes to the Corporate Minimum Tax

Under current law, if a corporation has zero or negative taxable income, it is subject to Vermont's corporate minimum tax. The current minimum tax (CMT) is as follows:

- For corporations with Vermont gross receipts less than $2 million, the CMT is $300
- For corporations with Vermont gross receipts greater than $2 million but less than $5 million, the CMT is $500.
- For corporations with Vermont gross receipts greater than $5 million, the CMT is $750.

This section of the bill creates a new CMT structure based upon Vermont gross receipts as follows:

VT Gross Receipts	S. 53 CoC Proposed
Less than $500K	$100
$500K-$1 million	$500
$1million to $5 million	$2000
$5 million to $300 million	$6000
Over $300 million	$100,000

Each year, there are roughly 12,000 to 13,000 corporate tax returns. Of these returns, about 10,000 pay the

[1] Under current law, the portion of a corporation's net income attributable to Vermont is determined using a three-factor formula that takes into account of Vermont payroll, property, and sales relative to its nationwide payroll, property, and sales.

corporate minimum tax. It is estimated that about 85-88% of these corporate minimum taxpayers have Vermont gross receipts of less than $500,000. This group would receive a reduction in their minimum tax paid, from $300 to $100. The remaining firms would see an increase in their CMT. The top bracket of $300 million and over in Vermont gross receipts is expected to impact around 10 corporations per year.

This section of the bill is estimated to increase General Fund revenues by $830,000 in FY2023, growing to $2.33 million per year thereafter as all corporations are expected to be subject to this change by mid-year 2023.

Section 3: Single Sales Apportionment and Repeal of the Throwback Rule

This section makes a significant change to the way Vermont calculates a corporation's presence in Vermont for the purposes of taxation. Under current law, the portion of any given corporation's net income attributable to Vermont is determined using a three-factor formula that takes into account Vermont payroll, property, and sales relative to its nationwide payroll, property, and sales.

This section of the bill proposes changing that apportionment to sales-only. That is, a company's net income attributable to Vermont would only be determined by the ratio of their Vermont sales to the nationwide sales.

Changing Vermont's apportionment formula to sales-only is expected to reduce General Fund revenues by $4.01 million in FY2023, growing to approximately $11 million per year thereafter. This represents roughly 5-6% of total corporate tax revenues once fully implemented. The change from FY2023 to FY2024 reflects a full tax year of implementation for corporations.

The above revenue estimate reflects the net tax change across all corporate taxpayers. On an individual level, the change could either reduce or increase a corporation's tax liability depending upon its structure. In general, this change is expected to benefit corporations in sectors of the economy with large payroll and property presences in Vermont that also export most of their sales, such as the manufacturing sector. JFO and the Department of Taxes estimate that much of the tax benefit of this change will accrue to the top 100 tax filers. This corresponds with general trends in business taxation, in which a large portion of the State revenues come from a small number of filers. Many of these top 100 filers tend to have significant payroll and property presences in Vermont while selling most of their goods or services elsewhere.

This being said, there are a number of corporate taxpayers who will end up paying more under this apportionment formula, particularly those without significant physical presence in Vermont. Based upon Department of Taxes modeling, firms in industries such as information technology, finance and insurance, and professional services are expected to in aggregate pay more corporate income tax as a result of the change.

Corporate taxpayers without taxable income, which make up approximately 70 to 80% of total corporate tax returns, will see no impact from this change.

This section also repeals the Throwback Rule for corporations. Under current law, if a corporation sells into a state in which it has no nexus (and therefore, no taxability), Vermont requires the corporation to count those sales as Vermont sales for the purposes of determining their sales apportionment factor. This proposal would repeal that rule. **This is expected to reduce General Fund revenues by $220,000 in FY2023 and $850,000 each fiscal year thereafter.** The change from FY2023 to FY2024 reflects a full tax year of implementation for corporations.

Section 5: Joyce to Finnigan Methodology

This section of the bill addresses how corporations with many subsidiaries determine their presence in Vermont. Under current law (Joyce methodology), a corporation's nexus in Vermont is limited to only the group of subsidiaries that have nexus in Vermont. Under this proposal, if one subsidiary has nexus, the entirety of the group of subsidiaries is considered to have nexus in Vermont. This change impacts the apportionment formula for corporations.

This section of the bill is expected to increase General Fund revenues by $2.65 million in FY2023 and $7.27 million in FY2024, growing slowly thereafter. The change from FY2023 to FY2024 reflects a full tax year of implementation in FY2024.

Appendix: Resources

- Vermont Department of Taxes corporate income tax data and modeling.
- Throwback rule repeal:
  - Oregon 2020 Tax Expenditure Report estimate for throwback repeal.
  - Department of Taxes analysis of corporate tax returns with throwback sales.
- Joyce to Finnegan change:
  - Comptroller of Maryland reports from tax years 2006 and 2007 on the impact of switching from Joyce to Finnigan methodology.
  - Estimates from Rhode Island and Colorado
- Single sales factor revenue estimates
  - Department of Taxes modeling of corporate taxpayers for tax years 2016 through 2020.
  - Fiscal estimates of switching to single sales factors in the following states: Rhode Island, Pennsylvania, Georgia, Minnesota, Delaware, Oregon, North Carolina, Connecticut, Maine, Illinois, Maryland, Wisconsin, Kentucky, New York, and Massachusetts.
- Repeal of 80/20 language:
  - Information provided to the Department of Taxes and JFO from the Minnesota Department of Revenue.
  - Fiscal estimates from the Colorado Legislative Council