Testimony on Combined Reporting
House Finance Committee
June 29, 2023
Matthew Knittel, Director, Independent Fiscal Office

Good morning, Chairmen Samuelson and Greiner and members of the committee, thank you for the opportunity to testify on the filing method known as combined reporting. For my brief remarks, I will review the figure and three tables that are attached.

Under mandatory combined reporting, multi-state firms that form a unitary group are required to file a combined return as if the related entities were a single corporation. The combined return reflects the net income or loss associated with the business operations of all members of the unitary group, and income is apportioned to the state based on the activity of the combined group within the state. Advocates assert that the filing method reduces a firm's ability to shift profits to low or no tax states through related-party transactions and is subject to less manipulation by firms.

The **figure and first table** show states that use combined reporting and the highest corporate net income tax (CNIT) rate levied for 2023 by that state.

- 44 states levy a CNIT, and 27 states use the combined reporting filing method.
- Over the past decade, 5 states enacted combined reporting, most recently New Mexico (2020).
- In 2021 and 2022, legislation was introduced in Virginia and Maryland.

The **second table** displays recent published revenue estimates for states that enacted or proposed combined reporting:

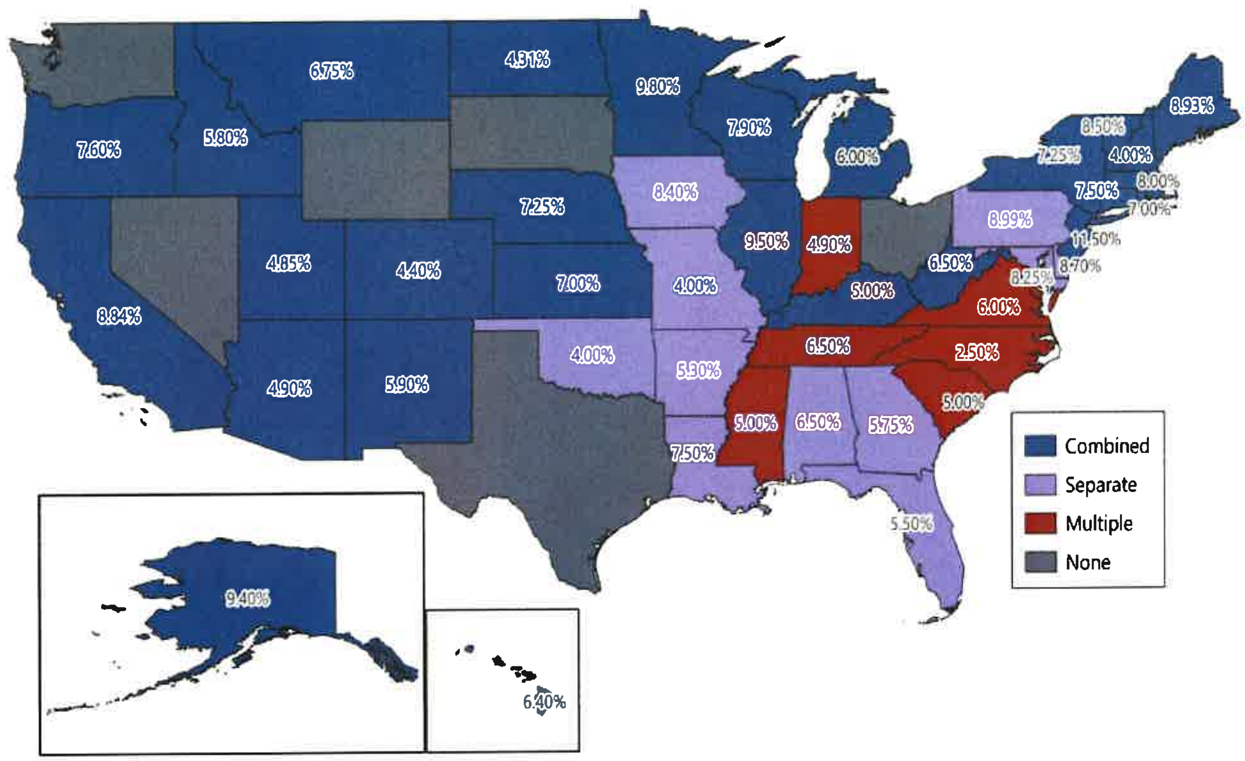
- Across these states, there appears to be a consensus that combined reporting would increase tax revenues by roughly 8% to 12%.
- Some states did not issue a revenue impact estimate due to the high degree of uncertainty (Kentucky, New Mexico).
- It should be noted that the revenue impact could vary considerably across states due to the size and industry composition of corporations in each state.

The **third table** displays the impact if combined reporting enhances revenues by 6%, 9% and 12%.

- Currently, corporate profits are unusually high, and these projections assume a partial reversion to more normal levels.
- The estimates reflect the lower CNIT rate and other recent policy changes.
- Previously, the IFO had assumed that combined reporting would increase revenues by 12% per annum. Given recent policy changes, we believe the relative revenue gain would be smaller but have not yet revised our previous analysis.

Thank you. I would be happy to address any questions you may have.

States with Corporate Net Income Tax by Reporting Method (2023)



Note: States designated as "multiple" generally require separate reporting, but either allow taxpayers to elect another form of reporting, or may require combined reporting based on audits. Tax rate reflects top rate in states that have a graduated corporate income tax structure.

Source: CCH State Tax SmartCharts (June 2023) and the Tax Foundation.

Corporate Net Income Tax States by Reporting Method (2023)

State	Rate	Method	State	Rate	Method
New Jersey	11.5%	Combined	Michigan	6.0%	Combined
Minnesota	9.8%	Combined	Virginia	6.0%	Multiple
Illinois	9.5%	Combined	New Mexico	5.9%	Combined
Alaska	9.4%	Combined	Idaho	5.8%	Combined
Pennsylvania	**9.0%**	**Separate**	Georgia	5.8%	Separate
Maine	8.9%	Combined	Florida	5.5%	Separate
California	8.8%	Combined	Arkansas	5.3%	Separate
Delaware	8.7%	Separate	Kentucky	5.0%	Combined
Vermont	8.5%	Combined	Mississippi	5.0%	Multiple
Iowa	8.4%	Separate	South Carolina	5.0%	Multiple
Maryland	8.3%	Separate	Arizona	4.9%	Combined
Massachusetts	8.0%	Combined	Indiana	4.9%	Multiple
Wisconsin	7.9%	Combined	Utah	4.9%	Combined
Oregon	7.6%	Combined	Colorado	4.4%	Combined
Connecticut	7.5%	Combined	North Dakota	4.3%	Combined
Louisiana	7.5%	Separate	Missouri	4.0%	Separate
Nebraska	7.3%	Combined	New Hampshire	4.0%	Combined
New York	7.3%	Combined	Oklahoma	4.0%	Separate
Kansas	7.0%	Combined	North Carolina	2.5%	Multiple
Rhode Island	7.0%	Combined	Nevada	--	n.a.
Montana	6.8%	Combined	Ohio	--	n.a.
Alabama	6.5%	Separate	South Dakota	--	n.a.
Tennessee	6.5%	Multiple	Texas	--	n.a.
West Virginia	6.5%	Combined	Washington	--	n.a.
Hawaii	6.4%	Combined	Wyoming	--	n.a.

Notes: States designated as "multiple" generally require separate reporting, but either allow taxpayers to elect another form of reporting, or may require combined reporting based on audits. Tax rate reflects top rate in states that have a graduated corporate income tax structure.

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Combined Reporting Base Expansion Estimates in Other States

State	Tax Year CR Effective	Year Est. Prepared	Est. Impact ($ Millions)	Est. Base Expansion
Maryland	--	2022	$160	8%
Virginia	--	2021	$60-$80	6-8%
New Mexico	2020	2019	--	--
New Jersey	2018	2016	$115-$280	5-10%
Kentucky	2018	2018	--	--
Connecticut	2016	2015	$39	5%
Rhode Island	2015	2018	$38	28%
West Virginia	2009	2007	$24-$28	8-10%
Massachusetts	2008	2007	$188	9%
Wisconsin	2008	2007	$76	11%
New York	2007	2008	$315-$420	6-8%

Note: Base expansion and dollar impact estimates relate to the first full fiscal year of tax impact, except for Rhode Island, which reflects full tax year impact. The base expansion estimate relates to the impact of combined reporting only and does not incorporate the impact of other simultaneous tax law changes. Vermont and Michigan adopted combined reporting after 2006 but were not included in this table because detailed revenue impact analyses could not be located. Texas also adopted mandatory combined reporting for its Margin Tax during this period, but this state is not included because it does not collect a traditional corporate income tax.

Source: Other state estimates come from a survey of select states by the National Conference of State Legislatures, various state fiscal notes, analyses and reports.

Potential Revenue Impact from Combined Reporting

- A filing method that effectively expands the tax base.
- Most states have assumed the filing method would increase revenues by 8% to 12%.
- IFO had previously assumed a 12% base expansion (2020).
- Changes have been enacted that suggest a reduced revenue impact prospectively.
- These include rate reduction, which reduces incentives to shift profits to other states, the codification of economic nexus and market sourcing, which expand the tax base.
- Impacts assume that legacy NOLs cannot be shared among unitary group members.

Base Expansion	Impact
6% Base Expansion	$300 to $350 million per annum, full phase-in
9% Base Expansion	$450 to $500 million
12% Base Expansion	$600 to $650 million

COMBINED REPORTING TESTIMONY

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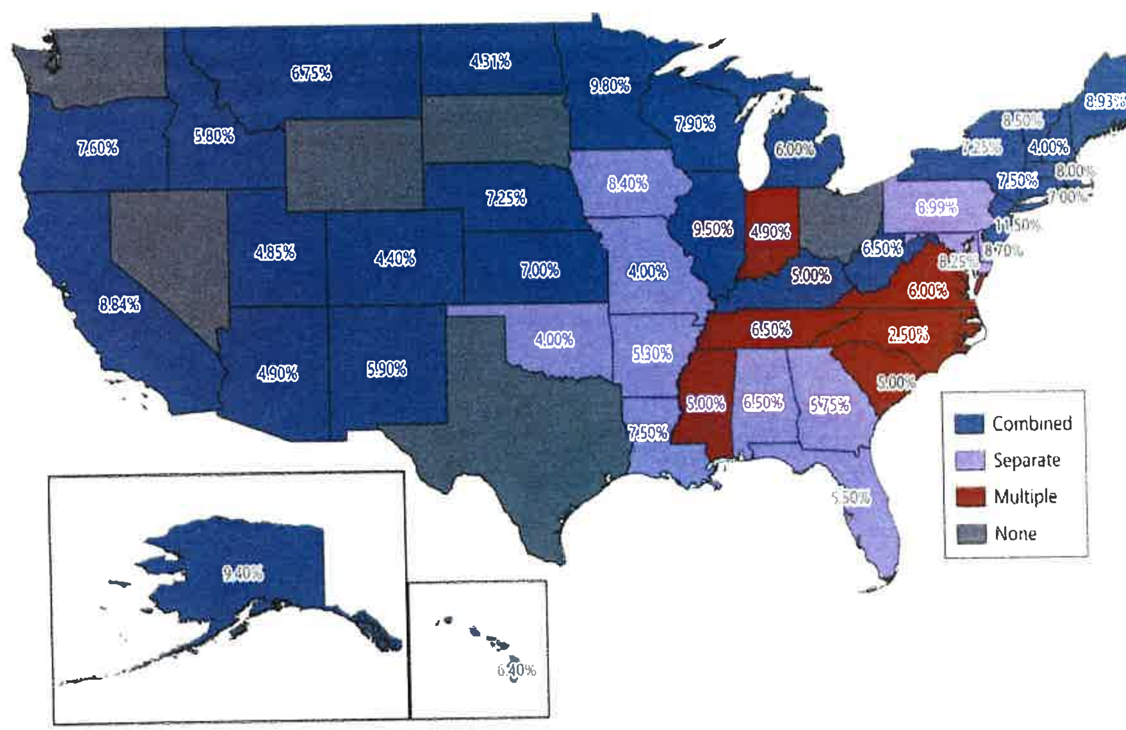

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