CORPORATE FRANCHISE TAX
Phase In of 100% Sales Weighting

March 8, 2004

	Yes	No
Separate Official Fiscal Note Requested		
Fiscal Impact		
DOR Administrative Costs/Savings		

Department of Revenue
Analysis of H.F. 2432 (Lenczewski) / S.F. 2540 (Rest)

	Revenue Gain or (Loss)			
	F.Y. 2004	**F.Y. 2005**	**F.Y. 2006**	**F.Y. 2007**
		(000's)		
General Fund	($2,900)	($12,700)	($23,500)	($33,100)

Effective for tax years beginning after December 31, 2003, and fully phased in for tax years beginning after December 31, 2007.

EXPLANATION OF THE BIL

Current Law: The total income of a corporation is apportioned to Minnesota based on the weighting of percentages from a three-factor formula. The three factors are based on the percentages of a corporation's total payroll, property, and sales that are attributable to Minnesota. The sales factor receives a 75% weight versus a 12.5% weight each for the payroll and property factors. The result of summing the weighted percentages is the apportionment percentage. A corporation's apportioned income is the product of its total income multiplied by the apportionment percentage.

Mail order businesses with 99% of their property and payroll in Minnesota are allowed to apportion income based on a single factor of sales.

Proposed Law: Effective for tax years beginning after December 31, 2003, the weighting for the property and payroll factors would decrease and the weight on the sales factor would increase (see table 1). In tax years beginning after December 31, 2007, the ratio of Minnesota sales to total sales would be the apportionment percentage. This 100% weighting is referred to as single sales factor weighting.

Table 1. Weights of Property, Payroll and Sales Factors under H.F. 2432

Time Period	Property	Payroll	Sales
Tax year beginning after 12/31/2003	10.0%	10.0%	80%
Tax year beginning after 12/31/2004	7.5%	7.5%	85%
Tax year beginning after 12/31/2005	5.0%	5.0%	90%
Tax year beginning after 12/31/2006	2.5%	2.5%	95%
Tax year beginning after 12/31/2007	0.0%	0.0%	100%

REVENUE ANALYSIS DETAIL

- The revenue estimate is based on data from returns received by the Department of Revenue in calendar year 2001. The model was adjusted to reflect changes in tax law made by the 2003 legislature.
- A program was run against corporate data to calculate the revenue effect from changing the current law weighting to the series of weightings shown in table 1.
- No change in revenue is assumed from corporations that have 100% of their economic activity in Minnesota.
- Growth in overall corporate tax collections as projected by the Department of Finance in the February 2004 forecast is used to project future revenue losses.
- Tax year revenue estimates are allocated to fiscal years using a 30% / 70% ratio.
- This law change also affects the apportionment of income generated by entities other than C corporations, mainly S corporations. The estimate was adjusted to include these other businesses.

Number of Taxpayer Affected: This proposal has an overall effect of changing the tax liability, including both increases and decreases, on about 11,000 corporations. Every year approximately 50,000 corporate tax returns are filed with the Department of Revenue.

When the proposal is fully phased in during tax year 2008, approximately 210 corporations will have tax changes greater than $100,000 (this includes both tax increases and decreases.) These corporations account for over 65% of the revenue change associated with the proposal. The average tax decrease in this group of taxpayers is $500,000 and the average tax increase is $200,000.

Effect of H.F. 2432 / S.F. 2540 on
Minnesota and Non-Minnesota Corporations
($000's)

Fiscal Year	Minnesota Corporations	Non-Minnesota Corporations	Net Effect
2004	($4,300)	$1,400	($2,900)
2005	($18,200)	$5,500	($12,700)
2006	($33,800)	$10,300	($23,500)
2007	($49,500)	$16,400	($33,100)

Source: Minnesota Department of Revenue
Tax Research Division
http://www.taxes.state.mn.us/taxes/legal_policy

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