



Setting THE record straight

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Combined reporting is not the answer for economic growth, job creation

As Pennsylvania continues to slowly recover from the recession, fostering a competitive business climate is more important now than ever before.

In his recent budget address, Gov. Ed Rendell proposed a number of business tax reforms long supported by the business community – including the elimination of the restrictive cap on net operating losses; movement toward basing the Corporate Net Income tax solely on sales; and reducing the CNI tax rate, the second-highest in the nation. Unfortunately, the governor wants these improvements tied to combined reporting, a complex tax reporting system that would have far-reaching, harmful effects on large and small employers. The certain result would be lost investment and lost jobs in the Commonwealth.

Combined reporting treats affiliated taxpayers (parents and subsidiaries) engaged in a unitary business as a single entity for the purpose of determining taxable income. Proponents say it is necessary in order to close so-called “tax loopholes” – an increasingly popular term used by supporters to negatively characterize legitimate and legal tax planning policies with regard to some corporations’ use of passive investment (Delaware holding) companies in other states.

Combined reporting is not a remedy

There are a number of factors that should give lawmakers pause in deciding whether or not to implement combined reporting in Pennsylvania, particularly at a time when job creation and economic growth should be priority No. 1.

In many cases, combined reporting is a solution looking for a problem, as it would impact businesses that do not have passive investment companies. As such, combined reporting is akin to using a missile to kill a mosquito. It’s not necessary, especially since the state Department of Revenue already has sufficient authority to address any activities designed solely to avoid tax.

There is also no guarantee that combined reporting would bring in additional revenue for the state because it merely creates winners and losers within the tax system. Some industries might see their tax burden lowered under combined reporting, while other businesses and industries would pay significantly more taxes. There is no statistical evidence that states enforcing combined reporting collect more tax revenues than states that employ separate accounting, given the other characteristics of the tax structure and the state’s economy. Yet its adoption would certainly raise a red flag for companies considering locating in the Commonwealth.

In addition, substantial details remain unclear as to how combined reporting would be instituted. For example, the concept of a “unitary business” is often poorly defined and prone to litigation. California, the first state to impose combined reporting, should have had all the wrinkles in its system ironed out by now. However, California currently has unresolved taxpayer disputes that are literally decades old. The additional compliance and administrative costs associated with combined reporting, as well as revenue uncertainties resulting from possible litigation, should be included in a balanced evaluation of the benefits and costs of its adoption.

The truth about combined reporting, businesses and taxes

An issue of this complexity and with so many negative implications for the state deserves an honest debate. It is disingenuous for combined reporting proponents to continuously repeat the claim that a majority of Pennsylvania corporations subject to the CNI tax do not pay taxes without fully explaining that many of these companies have either lost money or broke even and therefore, have no tax liability. Even the Rendell administration previously testified that under combined reporting, more than half of businesses would still legitimately not pay the CNI tax. In fact, when compared to other states, including states that have enacted combined reporting, Pennsylvania’s proportion of corporations that do not pay the CNI is typical.

It is also disingenuous to fail to mention the host of other taxes businesses pay, somehow implying that they are getting a free ride. Approximately 42 percent of state and local taxes is paid by business. If Pennsylvania was a nation, its overall corporate tax rate of 41.5 percent (federal plus state, accounting for state-local deduction) would be the highest in the world!

Job creation should be priority No. 1

The governor admitted more needs to be done to bring jobs to Pennsylvania and create a more prosperous economic future. Combined reporting would head the Commonwealth in the wrong direction. All Pennsylvanians, residents and businesses alike, would be much better off if the administration and like-minded lawmakers chose to follow the positive steps other states have taken to improve their overall business climate and economic competitiveness.

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The Pennsylvania Chamber of Business and Industry is the state's largest broad-based business association, with its membership representing nearly 50 percent of the private workforce. More information is available on the Chamber's website at www.pachamber.org

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