MONTANA LEGISLATIVE BRANCH

Legislative Fiscal Division

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Director
AMY CARLSON

DATE: March 13, 2018

TO: Joint Subcommittee on the Changing Economy and Impacts to the Long-Term Viability of Montana's Tax Structure

FROM: Sam Schaefer

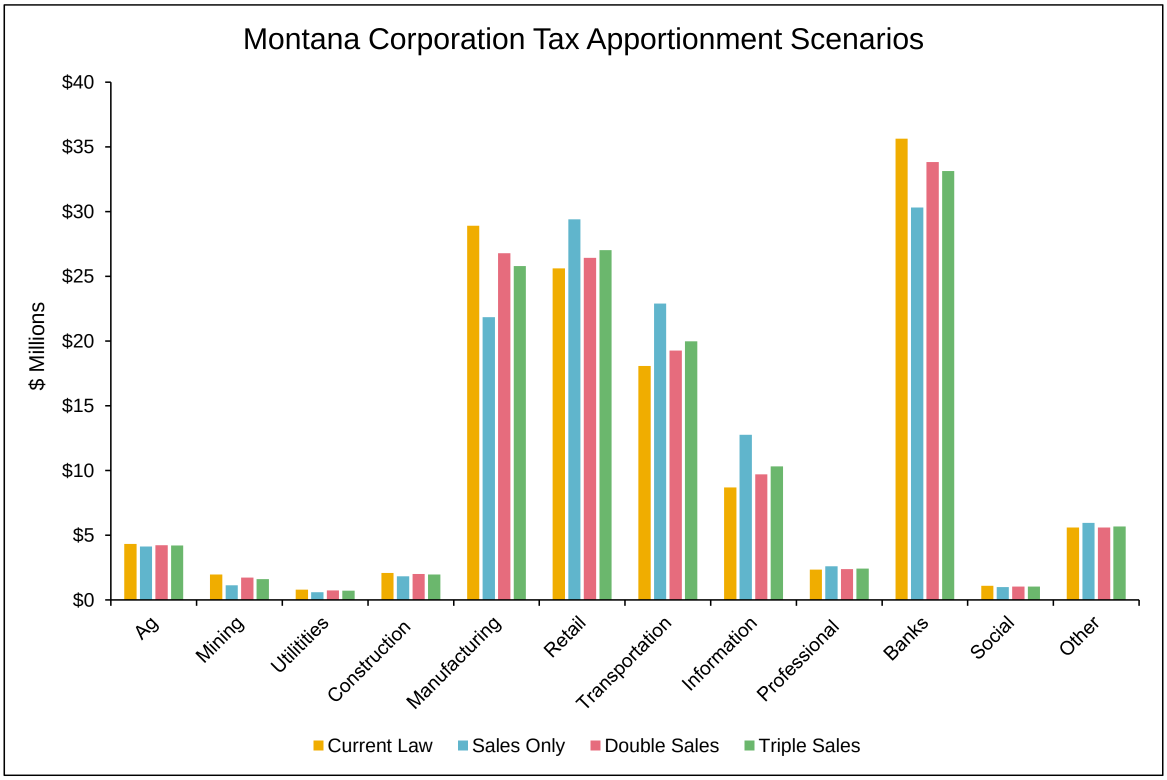
RE: Implications of Changing Montana's Corporation Apportionment Formula

The Legislative Fiscal Division (LFD) was asked to perform an analysis on the implications of changing Montana's apportionment factor, by putting more emphasis on in-state sales. It was determined that increasing the sales weight would have an extremely small impact on corporation income tax revenues. For practical purposes, the concept of apportionment is demonstrated in the example below.

If a corporation does business only in Montana, then a tax of 6.75% is levied on its net taxable income. However, for those corporations doing business both inside and outside of Montana, the net taxable income must be apportioned to each state. Currently, Montana uses a three-factor apportionment formula to determine its share of a multi-state corporation's net taxable income. The three factors used are a corporation's proportion of payroll, property, and sales that are present in Montana. All three factors are then equally weighted to produce a final apportionment factor.

Montana Apportionment Formula Example		
Payroll in Montana	**Total Payroll**	**Payroll Factor**
$1,500,000	$10,000,000	0.15
Property in Montana	**Total Property**	**Property Factor**
$2,000,000	$20,000,000	0.10
Sales in Montana	**Total Sales**	**Sales Factor**
$5,000,000	$25,000,000	0.2
Montana Apportionment Factor (Average)		0.15

Not all states use the same three-factor apportionment formula. Many states place a larger emphasis on the sales factor in comparison to the property and payroll factors. Two common practices are to place twice the weight on the sales factor as the other two (double-weighted sales) or to only use the sales factor. For this analysis these two practices were calculated for 2015 Montana calendar-year corporation tax data as well as the practice where the sales factor is given three times the weight as the other two (triple-weighted sales). Results are shown in the chart on the next page for all three methods on a sector-by-sector basis.



As the results show, increased revenue would occur in the retail, transportation, and information sectors as a result of switching to a sales dominated formula. However, revenue would decrease in both the manufacturing and financial sectors. Any changes across the remaining sectors would be quite small. Furthermore, combined collections are nearly identical in all scenarios, ranging from $133.8 million for the double-weighted sales model to $135.2 million under current law.