Kathleen Kittrick
Director, State Tax Policy
Public Affairs, Policy & Communications
1300 I Street, N.W. Suite 400
Washington, DC 20005
Office: 202-515-2482
Kathleen.kittrick@verizon.com

Written Statement in Opposition to Bill No. 6628
Kathleen Kittrick
Director, State Tax Policy, Verizon

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Verizon appreciates the opportunity to submit a written statement in opposition to Bill No. 6628. Verizon is opposed to legislation that would mandate unitary combined reporting in Connecticut. There has been a lot of rhetoric in recent years regarding corporations in Connecticut not paying their fair share of taxes. This rhetoric makes for great sound bites in a tough economy when hard budget choices must be made, but these sound bites are not factual.

Those that portray mandatory unitary combined reporting as a solution to close the corporate tax "loopholes" that have allowed corporations to shelter income and avoid paying their full and fair share of taxes, reflect a misunderstanding of what combined reporting is and its potential negative impact on tax revenue. One of the major concerns surrounding combined reporting is that a state could be arbitrarily assigned more income than is justified by the level of a corporation's real economic activity in the state. In addition, combined reporting can result in an a dramatic increase or decrease in revenues from corporate income taxes. As a result, the overall revenue impact of adopting combined reporting cannot be predicted reliably because of its complexity.

Mandatory unitary combined reporting reduces the link between income tax liabilities and where income is actually earned because it assumes all corporations in an affiliated unitary group have the same level of profitability, which is not consistent with either economic theory or business experience.

Combined reporting is complex and increases administrative burdens for both the taxpayer and the tax administrator:

- There is little agreement among the states as to what specifically constitutes a unitary group and the concept of a "unitary business" is uniquely factual and universally poorly-defined.
- Determining the scope of the unitary group is a complicated, subjective and costly process that is not required in separate filing states and often results in expensive, time consuming litigation.
- In addition, due to the factual nature of the inquiry, unitary combined return audits take much longer than separate company return audits and often require more state personnel to effectively complete.
- Combined reporting does not create a level playing field, particularly for small businesses with limited compliance resources.

While Verizon does not support a move to mandatory unitary combined reporting for Connecticut, if the Commission does plan to move forward with that recommendation, we request that the Commission also include the following:

FAS-109 Relief - Without it, Companies Will Be Hit Twice By Combined Reporting

- Companies book assets for financial reporting purposes under Generally Accepted Accounting Principles (GAAP) rules. However, Internal Revenue Service rules for recording and depreciating the same assets are different.
- The move to combined reporting is a significant tax law change that will require companies to analyze the differences between the financial book basis of assets they own versus the income tax basis of those same assets. The cumulative effect of those differences will likely require most companies to record an <u>additional</u> deferred tax liability expense under Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" (FAS 109).
- One of the most significant differences recognized by many companies occurs as a result of accelerated <u>tax</u> depreciation taken on depreciable assets under I.R.S. rules versus the amount that is deducted for financial <u>book</u> purposes.
- Since depreciable assets create one of the largest differences required to be accounted for under FAS 109, it is likely that this requirement to reflect the additional expense resulting

from the state's proposed changes would hit capital intensive companies much harder than other companies.

- The FAS 109 ramifications of the move to combined reporting must be addressed to avoid companies being detrimentally impacted twice by combined reporting changes. Not only will they experience an increase in their income tax liability as a result of these major changes, but they will also have the added financial strain of recognizing additional tax expense for financial reporting purposes. This financial statement impact generally is recorded upfront on adoption of MUCR.
- By providing for a reasonable schedule to allow the future deduction of the additional expenses triggered from any book/tax differences, Connecticut will negate any financial reporting detriment that may have been required under FAS 109.

Ability to Use the Federal Consolidated Filing

If mandatory unitary combined reporting were to be adopted in Connecticut, companies should be provided with the right to elect to file a Connecticut consolidated return which includes the federal consolidated group members. Alternatively, the Connecticut combined group should include only members of the federal consolidated group. This simplifies things in the following ways:

- For federal purposes, taxpayers that constitute an affiliated group (generally ownership of 80% or more) file a consolidated return. Permitting a consolidated return would avoid the question of whether the corporations are part of a "unitary" group. Conversely, including corporations that are not consolidated members will add complexity and additional administrative cost.
- Including only corporations that are part of a consolidated federal return is more appropriate and equitable than including corporations that are more than 50% owned. The mere fact that a corporation is more than 50% owned does not mean the corporation is "controlled" by the majority owner. Generally, consent is required from the minority owner on significant issues. In addition, the broader the group, the more likely that distortions are created (tax liability should be linked to where income is earned; expanding the group/base further erodes this linkage).
- Auditing a consolidated state return which uses the consolidated federal group and consolidated federal taxable income as the starting point will be much easier for the state.

- The broader the group the less predictable the effect on revenue. Consolidated or combined groups are permitted to offset losses of one corporation against income of other corporations. This can result in less revenue for a state particularly in bad times.
- While some taxpayers may attempt to shift income among 80% or more owned companies to minimize separate state income tax liabilities, it is very unlikely that taxpayers will shift income to more than 50% but less than 80% owned companies. As a result, a more than 50% ownership threshold for combined filing is unnecessary and as discussed above is not appropriate.

Thank you for the opportunity to present these items for discussion. To reiterate, Verizon does not support the move to combined reporting in Connecticut. However, if you choose make that dramatic income tax change, we believe you must include FAS 109 relief and the ability to elect federal consolidated group filing.

State policymakers need to be especially careful to create tax policies that encourage infrastructure investments that provide network benefits to the broad economy. Bill No. 6628 would likely increase Verizon's tax burden and diminish investments that benefit the entire Connecticut economy. Verizon respectively requests that Bill No. 6628 not be advanced from this committee.