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CORPORATION TAX INCOME APPORTIONMENT FORMULAS

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You asked what types of corporation tax income apportionment formulas states use and how many states have "throwout" and "throwback" rules.

SUMMARY

The 46 states that impose state corporation taxes (all states except Nevada, South Dakota, Washington, and Wyoming – see Table 1) require companies subject to those taxes to use state-specified apportionment formulas to determine income subject to tax in a taxing state. Apportionment formulas are designed to allocate to a taxing state, for tax purposes, a share of a company's income that corresponds to its business activity in the state. State formulas use one or more factors to determine each company's overall income apportionment percentage. Most states require all corporations to use the same apportionment formula, but 10 states have more than one formula and require or allow different types of businesses to use different formulas.

The common apportionment factor used by all 46 states is one that compares a company's sales in the taxing state to its total sales. Some states use sales as their single apportionment factor, but most (33 states) use formulas that also include factors comparing each company's property and payroll in the taxing state to its total property and payroll. But even if they use three factors, most states emphasize sales in

apportioning income. Of the states with three-factor formulas, 22 give extra weight to the sales factor in calculating the overall apportionment percentage.

The importance of the sales factor in apportioning corporate income subject to state taxes has led many states to boost the relative share of the in-state sales in a company's sales factor through the use of throwout or throwback rules. Such rules require companies to either count otherwise untaxed sales as sales in the taxing state (throwback) or exclude untaxed sales from a company's total sales (throwout). Of the states that have the rules, 25 use throwback and two use throwout.

INCOME APPORTIONMENT FORMULAS

All states with corporation taxes use at least one of the following corporation tax income apportionment formulas.

- ***Three-Factor Formula*** – This formula uses three fractions representing the ratios of a company's property, payroll, and sales within a taxing state to its total property, payroll, and sales. The three ratios are multiplied together to produce the percentage of the company's total taxable income to be allocated to the taxing state. In the classic version of this formula, each of the factors has equal weight in the calculation. Twelve states use an equal-weighted, three-factor apportionment formula.

- ***Three-Factor Formula With an Extra Weighting for Sales*** – A variation of the three-factor formula uses the same three factors, but gives extra weight to sales when the three are multiplied together. The most common variation double-weights the sales factor so that, instead of property, payroll, and sales each counting as one third of the apportionment percentage, the sales factor counts as 60% and the others as 20% each. Of the 22 states that use this type of apportionment formula, 17 double-weight the sales factor; five give it a weight of 70% or more; and one uses the double-weighted formula as its default while allowing certain companies to use a formula that gives an 80% weighting to sales.

- ***Single-Factor Formula*** – This formula apportions income for tax purposes using only the ratio of a company's in-state to its total sales. The single-factor formula dispenses entirely with the payroll and property factors. Eighteen states use a single-factor formula for some or all types of companies.

For companies that sell in national and global markets, formulas that emphasize sales apportion income away from the taxing state, thereby reducing tax liability in that state. Compared to an equally weighted three-factor formula, single-factor or extra-sales-weight apportionment formulas benefit companies that sell most of their products outside the taxing state, especially when they have significant property and numbers of employees in a taxing state.

"THROWOUT" AND "THROWBACK"

States use throwout and throwback rules to offset the effects of apportionment formulas based mostly on relative sales. The sales factor in an apportionment formula requires a company to compare its sales in the taxing state to its total sales. For companies operating in multiple states, apportionment formulas that rely completely or mostly on sales can shift income away from taxing states, even when the companies have significant operations in those states. But, a state can recoup some taxable income by changing the treatment of so-called "nowhere sales" in the sales factor. Nowhere sales are sales that are not apportioned to, or taxed in, any state because they are made to (1) the federal government or (2) purchasers in states where a company is not taxed because either it has no taxable nexus there or the state has no corporation tax.

States capture income from nowhere sales by requiring companies either to (1) subtract, or throwout, nowhere sales from total sales or (2) add, or throwback, nowhere sales to in-state sales. Either method increases the relative weight of in-state sales in the sales factor, thus increasing the income apportioned to the taxing state.

Of the 46 states with corporation taxes, 27 have throwout or throwback rules.

STATE-BY-STATE INFORMATION

Table 1 shows state apportionment formulas for the 2012 tax year. It also shows states that have throwout or throwback rules in their sales factors calculations. Unless otherwise noted, the throwback or throwout rules noted below apply to sales to both the U.S. government and into states where the company is not subject to tax.

TABLE 1: STATE CORPORATION TAX APPORTIONMENT FORMULAS AND THROWOUT/THROWBACK RULES

STATE	***APPORTIONMENT FORMULA(S)***	***THROWOUT/THROWBACK RULE***
Alabama	Three-factors, double-weighted sales	Throwback
Alaska	Three factors, equal weight	Throwback
Arizona	• Three factors, double-weighted sales • Three factors, 80% sales weight, if company agrees to disclose its name to the Joint Legislative Budget Committee and participate in an economic impact analysis	None
Arkansas	Three-factors, double-weighted sales	Throwback
California	• Three-factors, double-weighted sales • Companies can chose single factor starting in 2011 tax year	Throwback
Colorado	Single factor	Throwback, if: • the sale is into a state where the company is not taxable and • the company is domiciled in Colorado and its patents and copyrights are used in a state where it is not taxable
Connecticut	• Single factor for income derived from other than manufacturing, sale, or use of tangible personal property. Also applies to broadcasters and manufacturers in Sectors 31, 32, or 33 of the North American Industrial Classification System (except see below) • Three factors with double-weighted sales for income derived from manufacturing, sale, or use of tangible personal property. Manufacturers that derive 75% or more of their income from sales to the U.S. government may elect to use this formula. • Special formulas must be used by other types of businesses, such as air carriers, securities brokers, and financial services companies	None
Delaware	Three factors, equal weight	None
Florida	Three-factors, double-weighted sales	None
Georgia	Single factor	None
Hawaii	Three factors, equal weight	Throwback
Idaho	Three-factors, double-weighted sales	Throwback
Illinois	Single factor	Throwback
Indiana	Single factor	Throwback
Iowa	Single factor	None
Kansas	Three factors, equal weight	Throwback
Kentucky	Three-factors double-weighted sales	Throwback

Table 1 (continued)

STATE	***APPORTIONMENT FORMULA(S)***	***THROWOUT/THROWBACK RULE***
Louisiana	Three factors, equal weight unless another formula is specified	None
Maine	Single factor	• Throwout, except, for companies that are members of a unitary group, rule excludes sales into a state where an affiliate is taxable • Throwback applies to sales to U.S. government
Maryland	• Three-factors, double-weighted sales • Single factor for manufacturers	None
Massachusetts	Three-factors, double-weighted sales	Throwback applies to sales if property is: • sold into a state where company is not taxable and • not sold by a company's agent chiefly connected with, or situated at, the company's business premises outside Massachusetts
Michigan	Single factor	None
Minnesota	Three-factors, 93% weight for sales	None
Mississippi	Single factor for companies not required to use specified formula based on the type of business	Throwback
Missouri	• Three factors, equal weight • Companies other than certain public utilities and transportation companies can choose single-factor formula	Throwback
Montana	Three factors, equal weight	Throwback
Nebraska	Single factor	None
New Hampshire	Three-factors, double-weighted sales	Throwback
New Jersey	Three-factors, 70% weight for sales	None, for periods beginning on or after July 1, 2010
New Mexico	Three factors, equal weight	Throwback
New York	Single factor	None
North Carolina	Three-factors, double-weighted sales	No statutory throwout or throwback rule, but a company apportioning income must count as sales in North Carolina, sales into any state where it is not required to file a tax return. This rule is essentially throwback for those sales.
North Dakota	Three factors, equal weight	Throwback
Ohio	• Three-factors, triple-weighted sales for corporate franchise tax • Various apportionment formulas for commercial activity tax	None
Oklahoma	• Three factors, equal weight • Companies meeting investment criteria may double-weight the sales factor	Throwback
Oregon	Single factor	Throwback
Pennsylvania	Three-factors, 95% weight for sales	None
Rhode Island	Three factors, equal weight	Throwback for sales into a state where company is not taxed

Table 1 (continued)

STATE	*APPORTIONMENT FORMULA(S)*	*THROWOUT/THROWBACK RULE*
South Carolina	Single factor	None
Tennessee	Three-factors, double-weighted sales	Throwback for sales to U.S. government
Texas	Single factor	None, for periods after 2007
Utah	• Three factors, equal weight • Companies may elect double-weighted sales factor	Throwback
Vermont	Three-factors, double-weighted sales	Throwback
Virginia	Three-factors, double-weighted sales	None
West Virginia	Three-factors, double-weighted sales	Throwout for sales into any state where company is not taxed
Wisconsin	Single factor	Throwback

Source: CCH, *State Tax Guide*.

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