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MOST LARGE NORTH CAROLINA MANUFACTURERS ARE ALREADY SUBJECT TO "COMBINED REPORTING" IN OTHER STATES

Fears of Job Loss from Reducing Corporate Tax Avoidance Are Unwarranted

By Michael Mazerov

For the past seven years, there has been serious discussion in North Carolina of adopting an important reform in the state corporate income tax known as mandatory "combined reporting." Some North Carolina businesses and their lobbying organizations have opposed this change, claiming that it would result in some companies leaving the state or shunning North Carolina for new investment. However, the vast majority of the largest manufacturers in the state — the type of businesses that in theory are most likely to avoid states adopting tax policies they view as unfavorable — quite willingly subject themselves to mandatory combined reporting in other states. At least 60 of the 75 largest North Carolina manufacturers maintain a facility in at least one state that mandates combined reporting and therefore are subject to income taxes that implement this policy.

Most large corporations consist of a parent corporation and its subsidiaries. Combined reporting effectively treats the parent and most or all of its subsidiaries as a single corporation for state income tax purposes. In doing so, combined reporting nullifies a wide array of tax-avoidance strategies large multistate corporations have devised to artificially move profits out of the states in which they are earned and onto the books of subsidiaries located in states that will tax the income at a lower rate — or not at all.[1] North Carolina has been greatly victimized by these strategies. It was forced to litigate a case all the way to the U.S. Supreme Court to shut down an abusive tax shelter put in place by The Limited, and it currently is embroiled in similar litigation with Wal-Mart. If combined reporting had been mandatory, these costly court cases would have been unnecessary.

KEY FINDINGS

Former Governor Easley and tax policy study groups in North Carolina have periodically called for the enactment of "combined reporting" (CR), a corporate income tax reform aimed at nullifying tax shelters used by large multistate corporations. Some current legislators may be concerned that this could lead companies to leave the state or shun it for new investments. However, an investigation of the location decisions of the 75 largest North Carolina manufacturers demonstrates that such concerns are unwarranted:

- 60 of the 75 have chosen to maintain facilities in at least one combined reporting state.
- Almost half have facilities in 5 or more CR states, 17 have facilities in 10 or more, and 1 has facilities in *every one* of the CR states.
- 18 have long-maintained their *headquarters* in CR states, including Cisco Systems, Freightliner, and Georgia-Pacific.
- Several opponents of CR have facilities in numerous CR states, including Smithfield and Baxter Healthcare.

Some 16 states have mandated the use of combined reporting for at least two decades; six more have put it into effect in the last five years. The adoption of combined reporting was recommended in 2002 by the Governor's Commission to Modernize State Finances,[2] in 2007 by the Income Tax Subcommittee of the State and Local Fiscal Modernization Commission,[3] and in 2007 by the legislature's Revenue Laws Study Committee.[4] Former Governor Easley recommended the adoption of mandatory combined reporting as part of his FY08-FY09 budget package.[5]

Representatives of some major multistate corporations doing business in North Carolina have expressed opposition to combined reporting, claiming that it will subject them to difficult and costly tax compliance burdens and possibly lead to job losses as major employers leave North Carolina or reject the state for future investments.[6] Despite the growing number of states adopting this policy and previous endorsements of combined reporting by key policymakers in North Carolina, some current members of the General Assembly may be reluctant to mandate the use of combined reporting out of concern that it will adversely affect the state's economy.

This study presents compelling evidence that such concerns are unwarranted. It summarizes the results of a careful examination of the states in which the 75 largest North Carolina manufacturers have physical facilities and therefore are subject to the state's corporate income tax. Manufacturers were chosen as the focus of the research because, in theory, they have a greater ability than do retailers and service businesses to locate in states far away from their customers to take advantage of what they view as more favorable state tax policies. As documented in Figure 1, the study finds that:

- At least 60 of the 75 largest North Carolina manufacturers examined maintain facilities in at least one combined reporting state or are a member of a corporate group that has a facility in at least one combined reporting state. The "compliance burdens" and tax liabilities arising from combined reporting cannot be that great if these manufacturers — or the parent corporation that controls their decision-making — have willingly maintained a facility in one or more combined reporting states.

- Many of the corporations examined maintain facilities in *multiple* combined reporting states. Almost half — 36 out of 75 — have facilities in five or more combined reporting states, 17 have facilities in 10 or more such states, and 10 companies have facilities in 15 or more CR states.

- One company, Eaton Corporation, has facilities in *all 20* combined reporting states. (Two states that implemented combined reporting just as of January 1, 2009 are not included in the study.)

- Fully 18 of the companies have long-maintained their *headquarters* in combined reporting states, including Freightliner, Cisco Systems, Caterpillar, Georgia-Pacific, Sara Lee, and John Deere.

Taken together, these facts provide compelling evidence that North Carolina's adoption of combined reporting would not lead these companies to remove facilities or shun the state as a location for future investments. The data presented in Figure 1 also suggest the following observations:

FIGURE 1

Most Large North Carolina Manufacturers Are Already Subject to Combined Reporting in Other States

North Carolina Manufacturer [parent corp.] (In order of size)	Long-Time Combined Reporting (CR) States																New CR States				# of CR States	HQ
	AK	AZ	CA	CO	HI	ID	IL	KS	ME	MN	MT	NE	NH	ND	OR	UT	MI	NY	TX	VT		
International Business Machines																					9	NY
Smithfield Packing Co Inc																					9	
Hanesbrands, Inc																					15	
GlaxoSmithKline																					1	
Perdue Products Incorporated																					0	
Tyson Farms Inc																					8	
Goodyear Tire and Rubber Inc																					13	
Cisco Systems Inc																					17	CA
RJ Reynolds Tobacco Company																					0	
Tyco Electronics Corp																					19	
Montaire Farms of NC Inc																					0	
Freightliner of Cleveland LLC [Daimler AG]																					5	OR
House of Raeford Inc																					1	
Pilgrim's Pride Corporation																					3	TX
Carolina Turkeys [Goldsboro Milling Co]																					0	
Cutler Hammer Inc [Eaton Corporation]																					20	
Nortel Networks Inc																					10	
UNIFI Manufacturing Inc																					0	
Philip Morris USA Inc [Altria Group]																					8	NY
Baxter Healthcare Corp																					9	IL
HDM Furniture Industries Inc [Furn. Brands Intl]																					2	
General Electric Corp																					19	
Weyerhaeuser Company																					16	
RF Micro Devices Inc																					4	
Commscope Inc																					3	
Talecris Biotherapeutics																					10	
Caterpillar, Inc																					10	IL
Bridgestone/Firestone North America																					6	
Klaussner Furniture Industries Inc																					1	
Hickory Spring MFG. Co																					1	
Lorillard Tobacco Company																					0	
Corning Cable Systems LLC																					6	NY
Lenovo (United States) Inc																					0	
Revlon Consumer Products Corp																					1	NY
Thomas Built Buses, Inc [Daimler AG]																					5	OR
Solectron USA Inc [Flextronics Intl Ltd]																					6	
Thomasville Furniture [Furn. Brands Intl]																					1	
Alliance One International Inc																					0	

FIGURE 1 Continued

Most Large North Carolina Manufacturers Are Already Subject to Combined Reporting in Other States

North Carolina Manufacturer [parent corp.] (In order of size)	Long-Time Combined Reporting (CR) States																New CR States				# of CR States	HQ
	AK	AZ	CA	CO	HI	ID	IL	KS	ME	MN	MT	NE	NH	ND	OR	UT	MI	NY	TX	VT		
International Paper Company		■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■	■		18	
Consolidated Diesel Co [Cummins Inc]										■								■			2	
Bernhardt Furniture Company																					0	
American & Efird Inc [Ruddick Corp]																					0	
Moen Incorporated [Fortune Brands]			■				■								■						3	
American Cyanamid Co [Wyeth]			■				■	■										■		■	5	
Wix Filtration Corp LLC [Affinia Group]			■				■					■			■		■		■		6	MI
Cree Research Inc																					0	
Volvo Group North America Inc																					0	
Hatteras Yachts [Brunswick]			■				■			■					■		■	■	■		7	IL
PPG Industries Inc		■	■	■		■	■	■		■					■	■	■	■	■		12	
Guilford Mills Inc																	■				1	
Townsends Inc																					0	
Georgia-Pacific Corp [Koch Industries]	■	■	■	■			■	■		■	■	■	■	■	■		■	■	■		15	KS
A W North Carolina Inc [Aisin AW Co Ltd]																	■				1	
Sara Lee Corp		■	■	■		■	■	■	■	■		■	■	■	■	■	■	■	■		16	IL
Pharr Yarns Inc			■																		1	
Ingersoll Rand Financial Services	■	■	■	■	■	■	■	■		■		■	■		■	■	■	■	■		16	
Corning Incorporated		■							■				■				■	■	■		6	NY
VF Jeanswear LP [V.F. Corp]		■	■	■		■	■	■	■	■		■			■	■	■	■	■		14	
Charlotte Pipe & Foundry Company																■			■		2	
Ethan Allen Operations Inc			■						■											■	3	
Mohawk ESV Inc		■	■			■	■	■		■					■	■	■		■		10	
GKN Automotive Components Inc			■				■										■		■		4	
Broyhill Furn Ind Inc [Furn. Brands Intl]			■																		1	
John Deeer Shared Services Inc			■				■	■		■				■					■		6	IL
Rock Tenn Services Inc							■			■							■	■	■	■	6	
ATI Allvac [Allegheny Technologies Inc]															■	■	■	■	■		5	
The Timken Company		■	■				■	■					■			■					6	
Blue Ridge Paper Products Inc																					0	
Kayser-Roth Corporation																		■			1	
Freightliner of Mt Holly LLC [Daimler AG]							■								■	■	■	■			5	OR
Leggett & Platt Inc			■				■												■		3	
Century Furniture LLC																					0	
Lance Mfg LLC																			■		1	
NACCO Materials Handling Group Inc							■							■	■				■		4	
IAC Old Fort LLC [Intl Automotive Comp. Grp]													■				■		■		3	MI

- As noted above, several of the companies that have gone on record in opposition to North Carolina's adoption of combined reporting maintain facilities in numerous CR states. Smithfield Packing and Baxter Healthcare both have facilities in 9, for example. Baxter is actually headquartered in Illinois, a long-time combined reporting state.

- Six companies (two of which have a common parent) have what appears to be a single facility in a single, long-time combined reporting state; none of those facilities appears to be the corporate headquarters.[7] If combined reporting were truly sufficiently onerous to induce a company to abandon a state, it would seem that these facilities would have been prime candidates for such action. The fact that they are maintained is further evidence that a state's adoption of combined reporting is unlikely to affect corporate location decisions.

- There are six states that have implemented combined reporting only since 2004. The two that implemented combined reporting only as of January 1, 2009 (Massachusetts and West Virginia) are excluded from this study entirely. But for the other four recent adopters it might be argued that the presence of facilities in those states cannot be cited as evidence that combined reporting does not affect corporate location because companies have not had enough time to react to the change by moving their plants. In fact, as shown in Figure 1 (where these four states are isolated in the right-most columns), 54 of the 60 companies with a facility in at least one CR state have a facility in one of the CR states that enacted this policy *prior to 1985*.

It would take considerable effort to determine *when* the facilities identified in this report were sited in combined reporting states, and such an investigation is beyond the scope of the study. However, given that 16 states have mandated the use of combined reporting for 20 years or longer, it seems reasonable to assume that many of these manufacturers sited their facilities in CR states *after* the state adopted combined reporting. It also seems reasonable to assume that many of these same plants have been expanded and/or modernized since the initial siting decision was made. In other words, not only have 60 of the 75 companies chosen not to abandon CR states, it seems likely that many or most of them have chosen to locate or expand in CR states fully cognizant of the fact that the state had implemented this policy. If this is true, it provides further evidence that North Carolina would not be harming its economic prospects by enacting this important corporate income tax reform.

Combined Reporting and State Economic Development: Additional Evidence

There is no denying the fact that some large multistate corporations oppose combined reporting. Combined reporting is likely to result in increased corporate income tax payments for corporations that have put aggressive tax shelters in place. Its enactment also sharply limits the ability of large corporations to avoid a state's income tax going forward.

The question, however, is whether the dislike that some multistate corporations harbor toward combined reporting will actually result in harm to the economy of a state that adopts it. Would its adoption by North Carolina cause existing corporations to leave the state or reject it as a location for future investments? Would corporations not presently doing business in North Carolina be dissuaded from doing so by combined reporting?

Table 1: Manufacturing Job Change, 1990-2007 7 of 8 States with Net Job Gains Had Combined Reporting (CR) in Effect	
North Dakota (CR)	**66.7%**
Idaho (CR)	**26.0**
Utah (CR)	**23.3**
Iowa	4.8
Montana (CR)	**4.6**
Kansas (CR)	4.5
Nebraska (CR)	**4.1**
Arizona (CR)	**2.9**
Oregon (CR)	**0.0**
Minnesota (CR)	**-0.1**
Texas	-1.4
New Mexico	-2.4
Oklahoma	-3.5
Wisconsin	-4.3
Kentucky	-6.2
Alaska (CR)	**-7.1**
Indiana	-9.2
Louisiana	-10.5
Arkansas	-13.7
Colorado (CR)	**-14.0**
Vermont	-15.7
Georgia	-17.6
Alabama (Median State)	-18.4
New Hampshire (CR)	**-20.9**
Florida	-21.8
Tennessee	-23.4
Missouri	-23.6
California (CR)	**-25.5**
Mississippi	-26.1
Illinois (CR)	**-26.1**
Hawaii (CR)	**-26.2**
Ohio	-27.1
Delaware	-27.1
Virginia	-28.0
West Virginia	-28.0
South Carolina	-28.1
Pennsylvania	-30.7
Maryland	-33.5
North Carolina	-34.6
Connecticut	-36.4
Maine (CR)	**-36.5**
Massachusetts	-38.5
New Jersey	-40.9
New York	-43.7
Rhode Island	-46.6

The data on the facility location decisions of major North Carolina manufacturers discussed above provide significant evidence that the answer to both questions is “no.” This conclusion is supported by the job-creation track record of the combined reporting states and by academic studies as well.

Combined reporting states are well-represented among the most economically-successful states in the country. Between 1990 and 2007, for example, only eight states that levy corporate income taxes managed to achieve net positive growth in manufacturing employment. Seven of those eight states — Arizona, Idaho, Kansas, Montana, Nebraska, North Dakota, and Utah — had combined reporting in effect throughout the 1990-2007 period.[8] California is the state that has used combined reporting the longest and enforces it most aggressively, yet it was able to give birth to Silicon Valley in the 1990s. The presence of combined reporting has not been a barrier to Intel Corporation’s maintenance of its headquarters in California and its decision to place the bulk of its expensive chip fabrication plants in Oregon, Arizona, and Colorado — all combined reporting states.

It may seem illogical to acknowledge that some multistate corporations oppose combined reporting yet argue that it has no measurable impact on where they choose to locate. The apparent contradiction can be easily reconciled, however. All state and local taxes paid by corporations represent less than two and one-half percent of their total expenses on average, and the state corporate income tax represents on average less than 10 percent of that amount — or less than one-quarter of one percent of total costs.[9] A state’s decision to adopt combined reporting increases that small corporate tax load only slightly.[10] The potential influence on corporate location decisions of state corporate tax policies is simply overwhelmed in most cases by interstate differences in labor, energy, and transportation costs, which comprise a much greater share of corporate costs than state corporate income taxes do and often vary more among the states than effective rates of corporate taxation. It comes as no surprise, then, that a recent study by economists Robert Tannenwald and George Plesko, which measured interstate differences in *overall* state and local tax costs for corporations in a particularly rigorous way, found that there was not a statistically-significant (inverse) correlation between those costs and state success in attracting business investment.[11] In other words, higher state and local business taxes did not impede business investment.

Helping Small Businesses

Opponents of combined reporting also ignore potential *benefits* of this policy. Small (often family-owned) corporations doing most or all of their business in the state in which they are located generally do not have the resources to set up “Delaware Holding Companies,” “captive REITs,” and other tax shelters that exploit the absence of combined reporting in the state.[12] But their large, multistate corporate competitors do. By nullifying the corporate tax savings from aggressive tax-avoidance, combined reporting could benefit North Carolina’s economy by preventing large out-of-state corporations from under-pricing the state’s small businesses or attracting investment capital at a lower cost — thereby letting economic efficiency and not tax planning determine which businesses succeed in the marketplace. Perhaps this phenomenon explains in part why a recent study financed by the federal Small Business Administration found that: "States with more aggressive corporate income taxes, specifically including combined reporting . . . tend to have higher entrepreneurship rates.”[13]

Maintaining Services Businesses Need

Finally, the enactment of combined reporting could benefit North Carolina’s economy by preserving the long-term viability of the corporate income tax. This revenue source makes an important contribution to the ability of the state to finance education, transportation infrastructure, public safety, health care, and other vital services. Businesses need these services to provide a productive, well-trained workforce, to protect their facilities, and to ensure that they can obtain their supplies and transport their products to their customers expeditiously. Numerous economic studies confirm that the quality of these services in particular locations has a significant impact on where businesses choose to invest.[14] Failing to mandate combined reporting could harm the state’s economy by allowing the erosion of the state’s corporate tax base to continue, squeezing the ability of the state to furnish services that the private sector needs.

Conclusion

Combined reporting is a key tax policy choice needed to ensure that multistate corporations pay their fair share of the North Carolina corporate income tax, just as small North Carolina businesses must do. North Carolina’s Secretary of Revenue has the authority to require combined reporting by a particular corporation if he/she can demonstrate that it is necessary to nullify a particular instance of abusive tax avoidance. But applying combined reporting on a case-by-case basis is inefficient and is likely to be challenged in court as unwarranted; indeed, that is the basis of the current litigation with Wal-Mart mentioned above. Other approaches to nullifying income-shifting, such as asserting taxing jurisdiction over the out-of-state corporation receiving the income or disallowing deductions for royalties paid to out-of-state companies (one method of income-shifting) are controversial and also remain vulnerable to legal challenge because they have never been upheld by the U.S. Supreme Court. In contrast, the legality and fairness of combined reporting have twice been upheld by the Court.

This report has presented compelling, North Carolina-specific evidence refuting the key objection to mandatory combined reporting — that its enactment will harm the state’s economic prospects. However much they may object rhetorically to combined reporting, the vast majority of the state’s major manufacturers have willingly submitted and adapted to combined reporting-based income taxes in other states, often in *numerous* other states. North Carolina policymakers can confidently join those in a growing number of states that are enacting this critical corporate income tax reform without worry about negative impacts on the state economy.

Appendix: Data Sources

The manufacturing corporations whose facility locations were investigated for this report were identified by the Employment Security Commission of North Carolina as the 75 largest in the state (measured by the number of employees) as of the first quarter of 2008.[15] All of the manufacturers in that list were included in the study. As noted above, only manufacturers were studied because they are generally considered to be the type of enterprise that is potentially the most mobile in reaction to what are perceived as unfavorable state tax policies and practices. In contrast, a company like Wal-Mart (North Carolina's largest for-profit employer) obviously could not continue to serve its North Carolina customers at its current scale if it removed its retail stores from the state. It would therefore bias the conclusions of this study to cite Wal-Mart and similar businesses with retail facilities in their customers' states as evidence that combined reporting does not have a significant impact on where corporations choose to locate.

The two principal sources of information used to identify the states in which the manufacturers have facilities were the annual "10-K" reports filed by publicly-traded corporations with the Securities and Exchange Commission and the company's own Web sites. Every Form 10-K has a section titled "Properties" in which the corporation describes its major facilities. Although this section sometimes contains a generic description, in the majority of cases specific states are named.

Form 10-K information was supplemented by an examination of company Web sites. Many companies have a section of their Web sites listing their locations, often in connection with a description of their "good corporate citizen" activities. For those companies that did not have such a page, it was sometimes possible to use the Web pages aimed at assisting prospective employees find job openings. Companies often list *all* of their locations on the job vacancy sections of their Web sites; where they did not, states were included in Figure 1 only if there was a job listing for that state. (Job listings for sales jobs were disregarded, however, because the presence of a corporation's sales personnel in a state does not automatically establish corporate income tax liability for the company under federal Public Law 86-272.)

The data presented in this report on the number of states in which North Carolina manufacturers and their parent companies maintain facilities should be viewed as the minimum number of combined reporting states in which they are taxable. States were counted only if it was possible to gather written evidence authored by the company itself that it had a facility in a specific combined reporting state. It is quite possible that the information obtained was incomplete. For example, the annual report of Lorillard, a major cigarette manufacturer in North Carolina, states that "Lorillard leases sales offices in major cities throughout the United States. . . and warehousing space in 20 public distributing warehouses located throughout the United States." It seems likely that a number of those facilities are located in combined reporting states; indeed, it is quite possible that Lorillard has facilities in the large majority of combined reporting states. Nonetheless, because no hard documentation was obtainable from any source identifying the location of those facilities, Lorillard is listed in this report as a company that does not have facilities in any combined reporting state.

Notes

[1] See: Michael Mazerov, "State Corporate Tax Shelters and the Need for 'Combined Reporting'," Center on Budget and Policy Priorities, October 26, 2007, www.cbpp.org/10-26-07sfp.pdf.

[2] Governors' Commission to Modernize State Finance, *Final Report*, December 2002, p. 10; available at www.osbm.state.nc.us/files/pdf_files/final_rpt_gov_comm.pdf.

[3] State and Local Fiscal Modernization Commission, "Subcommittee Recommendations," undated 2007, available at www.ncleg.net/DocumentSites/committees/FiscalModernization/Comission%20Meetings/April%2016/Subcommittee%20Recommendations.pdf.

[4] Revenue Laws Study Committee, *Report to the 2007 General Assembly of North Carolina 2007 Session*, January 2007, pp. 25-33; available at www.ncleg.net/DocumentSites/committees/revenuelaws/Revenue%20Laws%20Reports%20to%20the%20General%20Assembly/Report%20to%20the%202007%20General%20Assembly%20(2007%20Session).pdf.

[5] Section 20.6, House Bill 708, 2007 legislative session.

[6] See, for example, a white paper in opposition to SB244/HB462 in the 2007 legislative session signed by several local chambers of commerce and individual corporations, available at www.ncleg.net/DocumentSites/committees/revenuelaws/2007-2008/Meeting%20Documents/Meetings%20for%20Report%20to%202009%20Session/19%20November%202008/NC%20Chamber%20Position%20on%20Combined%20Reporting.pdf.

[7] The companies are GlaxoSmithKline, Klaussner Furniture Industries, Hickory Spring Manufacturing, Thomasville/Broyhill/Furniture Brands International, and Pharr Yarns.

[8] Table 1 also indicates that the ninth and tenth best-performing states in manufacturing job growth were both combined reporting states. Oregon had a small net gain of manufacturing jobs in the 1990-2007 period that rounded down to zero. Minnesota had a small net loss of manufacturing jobs. Table 1 also shows that there were 11 combined reporting states that had better manufacturing job performance than the median state, Alabama, and only 5 combined reporting states that had steeper manufacturing job declines than Alabama.

[9] According to 2005 data published by the Internal Revenue Service (the most recent available), corporations deducted $473 billion in federal, state, and local taxes on their 2005 federal tax returns. This amount represented 2.0 percent of total expense deductions of $23.6 trillion. (The data are available at www.irs.gov/pub/irs-soi/05sb1ai.xls.) Since corporations have a strong financial incentive to deduct from their otherwise taxable profit every state and local tax payment for which they are liable, IRS statistics arguably are the most accurate source of information concerning state and local taxes incurred by corporations.

The Council on State Taxation (COST), an organization representing major multistate corporations on state tax matters, has taken issue with using IRS data to evaluate the relative importance of state and local tax costs in influencing corporate location decisions. (See: Joseph R. Crosby, "Just How 'Big' Are State and Local Business Taxes?" *State Tax Notes*, June 20, 2005, pp. 933-935.) Crosby correctly notes that the line-item for taxes deducted on federal returns omits a major category of state and local taxes paid by businesses — sales taxes paid on equipment and supply purchases. (Such taxes are hidden in other expense line-items in the IRS data.) However, as noted above, the line-item also includes a number of *federal* taxes paid by corporations that are deductible on federal returns — such as the federal telecommunications excise tax and unemployment compensation taxes for some corporate employees. If one were to add a reasonable estimate of the omitted state and local sales taxes and subtract a reasonable estimate of the inappropriately-included federal taxes, the resulting estimate for total state and local taxes incurred by corporations might not differ significantly from the $473 billion IRS figure for total deducted taxes.

In fact, COST has commissioned its own estimate of the total amount of state and local taxes paid by businesses. The figure for state fiscal year 2006 is $553.7 billion. (See: Robert Cline, Tom Neubig, and Andrew Phillips (Ernst & Young LLP), "Total State and Local Business Taxes, 50-State Estimates for Fiscal Year 2006," February 2007; available at www.statetax.org/WorkArea/DownloadAsset.aspx?id=67460.) This figure represents the estimated taxes paid by all businesses, not just corporations. But even if one assumed that all of these costs were incurred by corporations and substituted this figure for the IRS data for taxes deducted, it still results in an estimate that state and local taxes represent 2.3 percent of total corporate expenses (of $23.6 trillion) — not significantly different from the 2.0 percent figure arrived at using only the IRS data.

More importantly, COST also takes issue with the use of the $23.6 trillion IRS figure for total corporate expenses used in the denominator. COST argues that the relevant analysis is an examination of the share of total final economic output produced by private businesses that is absorbed by state and local taxes paid by such businesses. COST asserts that using the $23.6 trillion of corporate expenses is inappropriate because that figure includes multiple sales of the same item from (for example) a manufacturer to a wholesaler and then from the wholesaler to a retailer. In contrast, using total U.S. gross state product produced in the private sector (otherwise known as private sector "value-added") measures the value only of final production.

COST's preferred denominator of gross state product produced by private businesses might be appropriate for evaluating the total "burden" of state and local business taxes on final production in the economy. It is inferior, however, in evaluating the issue under discussion here — the role played by state and local corporate tax costs in influencing corporate location decisions as compared to the role played by other corporate expenses for labor, energy, and transportation. For each actor in the supply chain described above (manufacturer, wholesaler, retailer), the influence of state and local tax expenses on its location decisions is determined in relation to the other expenses incurred in its business that also vary among locations. How many times its inputs may have been resold prior to its purchase of them and how many times its outputs may be resold prior to reaching their final purchasers is irrelevant in influencing its location decisions. What is true for the individual economic actors is true for the supply chain as a whole. Thus, the relative importance of state and local taxes in influencing corporate location decisions in the overall economy is best illustrated by looking at those expenses as a share of total corporate expenses, not the total value of final corporate production or value-added.

In sum, it is entirely reasonable to argue that state and local taxes have a relatively minor impact on corporate location decisions because they constitute only 2.3 percent or less of total corporate expenses and their potential influence is overwhelmed by interstate differences in labor, energy, transportation, and other costs of production that account for almost 98 percent of total corporate production expenses.

[10] To the author's knowledge, no official estimate has ever been made by an executive or legislative agency in North Carolina of the revenue impact of mandating combined reporting. In Iowa, however — to take a typical example — the adoption of combined reporting was estimated to boost corporate tax receipts by $75 million in FY09. That would have represented an 18 percent increase over the contemporaneously-forecasted FY09 corporate income tax baseline of $416.5 million.

[11] George A. Plesko and Robert Tannenwald, "Measuring the Incentive Effects of State Tax Policies Toward Capital Investment," Federal Reserve Bank of Boston Working Paper 01-4, December 3, 2001.

[12] For a detailed description of some of the tax-avoidance strategies to which non-combined reporting states are most vulnerable, see the source cited in Note 1.

[13] Donald Bruce and John Deskins, "State Tax Policy and Entrepreneurial Activity," November 2006. Available at www.sba.gov/advo/research/rs284tot.pdf.

[14] For a recent summary of these studies in the context of Massachusetts' debate on combined reporting, see: Robert G. Lynch, William Schweke, Nicholas W. Jenny, and Noah Berger, "Building a Strong Economy: The Evidence on Combined Reporting, Public Investments, and Economic Growth," 2007. Published by the Economic Policy Institute and the Massachusetts Budget and Policy Center, June 2007. Available at www.massbudget.org/BuildingStrongEconomyJune07.pdf.

[15] The list is available at www.ncesc.com/lmi/industry/Manufacturing_Employers_Only.pdf.