

An Analysis of State Corporate Tax Revenue Growth: Does the Use of Combined Reporting Make a Difference?

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Strong U.S. economic growth is creating a tax-revenue boom for the states (Edwards, 2006). State tax revenues jumped 8.7 percent in 2004 and about 8 percent in 2005. To put this in perspective, total state taxes grew by the annual average of 5.4 percent since 1988. Similarly, state income taxes grew by 6.1 percent over this period and sales taxes grew by just more than 5 percent. While state corporate income tax (SCIT) revenue grew by more than 28 percent in 2005, the overall average growth rate since 1988 has been only 3.4 percent. By way of contrast, federal corporate income taxes grew by an average annual rate of 6.2 percent over this same period.

The decline of the state corporate income tax has been the subject of numerous recent studies. Moreover, a number of recent studies have identified reasons for the decline in SCIT revenues. Of all the reasons advanced for the decline in state corporate taxes, the most often cited is the failure of states to adopt and implement the combined reporting tax collection system. Accordingly, a number of states are contemplating or have already implemented combined reporting. The explicit assumption made by advocates of combined reporting is that it will force companies to report and pay larger amounts of state corporate tax. This in turn would lead to higher rates of corporate tax collection for states that use combined reporting compared with those that do not.

The primary objective of this paper is to examine whether the use of combined reporting tends to stabilize and improve the rate of state corporate tax revenue collection. The tax buoyancy methodology (cite) is employed to compare the rate of corporate tax revenue collections in states that use combined reporting with those that use other tax collection systems. This study also examines whether a state's implementation of combined reporting leads to an increase in the rate of corporate tax revenue collection.

Surprisingly, the data examined here does not support the idea that combined reporting provides more stable corporate tax revenues for states that use combined reporting *vis-à-vis* those that do not. This question was also examined by comparing the growth of state corporate tax revenue as a percentage of state GDP before and after the adoption of combined reporting. These results support the same conclusion; combined reporting does not lead to more stable corporate tax revenue collections for states that adopt this tax reporting method. Policymakers should factor these results into their proposed solutions for increasing the rates of state corporate tax revenue collection.