

Iowa Corporate Income Tax

Where Did All the Money Come From
and When Will It Stop?

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Background

In 1934, Iowa implemented a tax on corporate net income at a flat rate of 2 percent. Through 1965 the corporate tax rate was changed four times rising to 4 percent. The flat rate was replaced by a graduated rate structure in 1967 that ranged from 4 percent to 8 percent. The existing four rate brackets, which range from 6 percent on net income up to \$25,000 to 12 percent on net income over \$250,000, was adopted in 1981.

Since the tax's inception C-corporations doing business both in Iowa and outside the State have been allowed to apportion income based only on sales. Also, C-corporations are allowed to file returns either separately or on a state combined basis when multiple entities of a single corporate parent do business in Iowa.

Iowa Corporate Tax Base

For tax year 2005 over 37,500 C-corporations filed tax returns in Iowa. For analysis purposes corporate taxpayers are divided into five groups taking into consideration whether or not they report positive net income for tax purposes, residency, and geographic scope of operations. Corporations with positive net income are divided among the following categories:

- Iowa based corporations with only Iowa sales,
- Non-Iowa corporations with only Iowa sales,
- Iowa based corporations with sales both in and outside Iowa, and
- Non-Iowa based corporations with sales both in and outside Iowa.

The last category contains those corporations that report losses for the tax year.

The number, net income, and average income for each of the five groups are summarized in Table 1.

Home State	Apportionment	Number	Net Income (\$Million)	Average Income
Iowa	All Iowa	20,963	\$328.7	\$15,679
Other	All Iowa	1,918	\$1,996.8	\$1,041,084
Iowa	Apportioned	2,299	\$29,243.2	\$12,719,965
Other	Apportioned	9,043	\$415,881.3	\$45,989,302
Other	Reports Loss	3,313	-\$142,272.5	-\$42,943,692
Totals		37,536	\$305,277.5	\$8,132,526

The majority of Iowa corporate taxpayers (55.8%) are Iowa-based with sales only inside the State. These corporations are generally small and for 2005 had average income of only around \$16,000. At the other end of the spectrum are the 9,043 (24.1%) regional and national corporations based outside Iowa with average 2005 income equal to almost \$46 million. Those corporations that indicated losses for the year, 8.8 percent of filers, were also generally large regional and national companies based outside Iowa.

The total number of C-corporations required to file Iowa income tax returns has remained relatively stable over the past decade. However, as shown in Table 2 changes within the five categories have been considerable. Some reasons for the changes include:

- A law change enacted in 1996 that allowed S-corporations with multi-state sales to apportion income in the same manner as C-corporations,
- The acquisition of a number of Iowa corporations by non-Iowa based companies,
- More aggressive tax planning by C-corporations, and
- The growth of business tax credit programs.

Home State	Apportionment	Number 1995	Number 2005	Change	% Change
Iowa	All Iowa	24,998	20,963	-4,035	-16.14%
Other	All Iowa	1,758	1,918	160	9.10%
Iowa	Apportioned	2,428	2,299	-129	-5.31%
Other	Apportioned	5,719	9,043	3,324	58.12%
Other	Reports Loss	2,099	3,313	1,214	57.84%
Totals		37,002	37,536	534	1.44%

This table shows percentage changes of over 50 percent for both non-Iowa based corporations that apportion income and for those corporations that report losses.

Of more interest from a budget perspective is what has happened to net income and tax liability. Table 3 shows how these two measures have changed over the period from 1995 through 2005 for each of the five categories of corporate filers. Prior to the last recession net income (as reported on the company's federal tax returns) peaked at \$73.2 billion in tax year 1996, dropped to -\$80.3 billion in tax year 2001, and then recovered to \$305.2 billion in tax year 2005. Looking at just corporations with positive net income, year-to-year changes varied from a low of \$1.2 billion between tax years 2000 and 2001 to a high of \$173.5 billion between tax years 2004 and 2005. Similarly, corporations that reported losses experienced the greatest increase in aggregate losses between tax years 2000 and 2001 and experienced the largest decrease in losses between tax years 2004 and 2005. Thus, corporate net income reported on Iowa tax returns clearly exhibits a relationship to national economic fluctuations.

Table 3: Net Income of C-Corporations by Tax Year, 1995-2005

Part 1: Net Income of C-Corporation Taxpayers (\$ Million)												
Home State	Allocates Income	Tax Year										
		1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Iowa	Allowa	\$ 372.12	\$ 385.90	\$ 440.10	\$ 251.27	\$ 300.17	\$ 216.17	\$ 107.39	\$ 81.07	\$ 160.34	\$ 266.75	\$ 328.68
Other	Allowa	629.45	569.68	2,792.26	1,293.02	986.63	475.19	426.05	1,849.01	726.75	1,010.69	1,996.80
	Allowa	1,001.57	955.58	3,232.36	1,544.29	1,286.80	691.36	533.45	1,930.08	887.09	1,277.45	2,325.49
Iowa	Allocates	\$ 2,353.74	\$ 2,692.99	\$ 3,517.36	\$ 3,801.86	\$ 3,333.62	\$ 3,481.90	\$ -1,632.79	\$ 974.21	\$ 1,139.33	\$ 7,573.31	\$ 29,243.20
Other	Allocates	92,808.04	112,220.25	113,964.73	118,816.03	135,861.97	142,405.64	148,873.85	152,767.85	200,071.18	265,144.42	415,881.26
	Allocates	95,161.78	114,913.23	117,482.09	122,617.90	139,195.59	145,887.55	147,241.06	153,742.07	201,210.51	272,717.73	445,124.45
	Positive Income	96,163.35	115,868.82	120,714.45	124,162.18	140,482.39	146,578.91	147,774.50	155,672.15	202,097.60	273,995.18	447,449.94
Other	Reports Loss	-41,883.50	-43,526.15	-63,588.89	-100,332.72	-142,832.36	-172,773.16	-228,119.97	-222,717.38	-212,612.00	-187,257.36	-142,272.45
	T total	54,279.85	72,342.67	57,125.55	23,829.47	-2,349.96	-26,194.26	-80,345.47	-67,045.23	-105,144.40	86,737.81	305,177.49
Part 2: Change from Prior Year Net Income of C-Corporation Taxpayers (\$ Million)												
Home State	Allocates Income	Tax Year										
		1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Iowa	Allowa	\$ 13.77	\$ 54.20	\$ -188.84	\$ 48.90	\$ -84.00	\$ -108.78	\$ -26.32	\$ 79.27	\$ 106.41	\$ 61.93	
Other	Allowa	-59.76	2,222.57	-1,499.24	-306.39	-511.44	-49.14	1,422.96	-1,122.26	283.94	968.11	
	Allowa	-45.99	2,276.78	-1,688.07	-257.48	-595.44	-157.91	1,396.64	-1,042.99	390.36	1,048.04	
Iowa	Allocates	\$ 339.25	\$ 824.37	\$ 284.50	\$ -468.24	\$ 148.29	\$ -5,114.70	\$ 2,607.01	\$ 165.12	\$ 6,433.97	\$ 21,669.89	
Other	Allocates	19,412.21	1,744.48	4,851.31	17,045.94	6,543.67	6,468.21	3,894.00	47,303.33	65,073.24	150,736.84	
	Allocates	19,751.46	2,568.85	5,135.81	16,577.70	6,691.95	1,353.51	6,501.01	47,468.45	71,507.22	172,406.73	
	Positive Income		19,705.47	4,845.63	3,447.74	16,320.21	6,096.51	1,195.60	7,897.64	46,425.45	71,897.58	173,454.77
Other	Reports Loss	-1,642.65	-20,062.75	-36,743.82	-42,499.64	-29,940.80	-55,346.81	5,402.60	10,105.37	25,354.64	44,984.91	
	T total	18,062.82	-15,217.12	-33,296.09	-26,179.43	-23,844.29	-54,151.21	13,300.24	56,530.83	97,252.22	218,439.68	
Part 3: Percent Change from Prior Year Net Income of C-Corporation Taxpayers												
Home State	Allocates Income	Tax Year										
		1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Iowa	Allowa		3.70	14.05	-42.91	19.46	-27.98	-50.32	-24.51	97.77	66.37	23.22
Other	Allowa		-9.49	390.14	-53.69	-23.70	-51.84	-10.34	333.99	-60.70	39.07	97.57
	Allowa		-4.59	238.26	-52.22	-16.67	-46.27	-22.84	261.81	-54.04	44.00	82.04
Iowa	Allocates		14.41	30.61	8.09	-12.32	4.45	-146.89	-159.67	16.95	564.71	286.14
Other	Allocates		20.92	1.55	4.26	14.35	4.82	4.54	2.62	30.96	32.53	58.85
	Allocates		20.76	2.24	4.37	13.52	4.81	0.93	4.42	30.88	35.54	63.22
	Positive Income		20.49	4.18	2.86	13.14	4.34	0.82	5.34	29.82	35.58	63.31
Other	Reports Loss		3.92	46.09	57.78	42.36	20.96	32.03	-2.37	-4.54	-11.93	-24.02
	T total		33.28	-21.03	-58.29	-109.86	1014.67	206.73	-16.55	-84.32	-924.94	251.84
Notes:												
(1) Corporations that have sales both inside and outside Iowa may allocate their income between Iowa and the remainder of the nation for Iowa corporate income tax purposes.												
(2) Unlike most other states which allow income allocation for tax purposes based on a three factor formula including sales, employment and property, Iowa considers only sales.												
(3) Reports losses includes non-Iowa firms that report a net loss of greater than \$100,000.												
(4) Tax year includes returns whose tax years begin on or after the first day of the calendar year.												

Aggregate Iowa corporate income tax liability exhibits comparable cyclical fluctuations. Prior to the last recession net corporate taxes reached a high of \$300.6 million in tax year 1997. Then in tax year 2001 corporate liability dropped to \$132.6 million, but by 2005 corporate income tax liability recovered and reached a new high of \$327.6 million.

Table 4: Tax Liability of C-Corporations by Tax Year, 1995-2005

Part 1: Tax Liability of C-Corporation Taxpayers (\$ Million)												
Home State	Allocates Income	1995	1996	1997	1998	1999	Tax Year 2000	2001	2002	2003	2004	2005
Iowa	All Iowa	\$ 39.36	\$ 42.88	\$ 49.05	\$ 38.22	\$ 42.75	\$ 40.43	\$ 30.43	\$ 28.87	\$ 31.42	\$ 33.27	\$ 40.73
Other	All Iowa	9.59	14.41	111.88	4.59	5.25	3.75	2.79	4.45	8.25	7.31	44.45
	All Iowa	48.95	57.29	160.93	42.81	48.00	44.19	33.21	33.32	39.67	40.58	85.18
Iowa	Allocates	\$ 20.69	\$ 23.73	\$ 38.17	\$ 31.18	\$ 21.42	\$ 14.21	\$ 27.22	\$ 33.80	\$ 26.22	\$ 47.84	\$ 70.97
Other	Allocates	85.73	91.21	102.42	98.38	112.74	99.03	74.89	75.51	95.91	120.70	177.25
	Allocates	106.42	114.95	140.59	129.56	134.17	113.23	102.11	109.31	122.12	168.53	248.22
	Positive Income	155.37	172.23	301.52	172.38	182.17	157.42	135.32	142.63	161.80	209.11	333.40
Other	Reports Loss	2.38	1.96	-0.92	-0.19	-0.38	-8.79	-2.69	-4.09	-6.79	-4.05	-5.81
	Total	157.75	174.19	300.61	172.18	181.79	148.62	132.63	138.54	155.01	205.07	327.59
Part 2: Change from Prior Year Tax Liability of C-Corporation Taxpayers (\$ Million)												
Home State	Allocates Income	1995	1996	1997	1998	1999	Tax Year 2000	2001	2002	2003	2004	2005
Iowa	All Iowa	\$ 3.52	\$ 6.16	\$ -10.82	\$ 4.53	\$ -2.32	\$ -10.01	\$ -1.56	\$ 2.56	\$ 1.85	\$ 7.46	
Other	All Iowa	4.82	97.48	-107.29	0.66	-1.50	-0.96	1.67	3.80	-0.94	37.14	
	All Iowa	8.34	103.64	-118.11	5.19	-3.82	-10.97	0.11	6.35	0.91	44.60	
Iowa	Allocates	\$ 3.04	\$ 14.44	\$ -6.99	\$ -9.76	\$ -7.22	\$ 13.01	\$ 6.58	\$ -7.58	\$ 21.62	\$ 23.14	
Other	Allocates	5.48	11.21	-4.04	14.36	-13.72	-24.14	0.62	20.39	24.79	56.55	
	Allocates	8.52	25.65	-11.03	4.61	-20.94	-11.13	7.20	12.81	46.41	79.69	
	Positive Income	16.87	129.29	-129.15	9.79	-24.75	-22.10	7.31	19.17	47.32	124.29	
Other	Reports Loss	-0.43	-2.87	0.72	-0.18	-8.42	6.11	-1.40	-2.70	2.74	-1.76	
	Total	16.44	126.42	-128.42	9.61	-33.17	-15.99	5.91	16.47	50.06	122.53	
Part 3: Percent Change from Prior Year Tax Liability of C-Corporation Taxpayers												
Home State	Allocates Income	1995	1996	1997	1998	1999	Tax Year 2000	2001	2002	2003	2004	2005
Iowa	All Iowa		8.96	14.37	-22.07	11.85	-5.42	-24.75	-5.13	8.86	5.87	22.42
Other	All Iowa		50.26	676.63	-95.90	14.34	-28.56	-25.71	59.83	85.21	-11.36	507.96
	All Iowa		17.05	180.91	-73.40	12.11	-7.95	-24.83	0.32	19.06	2.29	109.91
Iowa	Allocates		14.69	60.82	-18.31	-31.29	-33.69	91.58	24.18	-22.43	82.47	48.36
Other	Allocates		6.40	12.29	-3.95	14.60	-12.17	-24.37	0.83	27.01	25.85	46.85
	Allocates		8.01	22.31	-7.85	3.55	-15.61	-9.83	7.05	11.72	38.00	47.28
	Positive Income		10.86	75.07	-42.83	5.68	-13.59	-14.04	5.40	13.44	29.25	59.44
Other	Reports Loss		-17.93	-146.79	-78.77	93.67	2236.33	-69.44	52.23	65.98	-40.41	43.51
	Total		10.42	72.57	-42.72	5.58	-18.25	-10.76	4.45	11.89	32.30	59.75

Notes:
(1) Corporations that have sales both inside and outside Iowa may allocate their income between Iowa and the remainder of the nation for Iowa corporate income tax purposes.
(2) Unlike most other states which allow income allocation for tax purposes based on a three factor formula including sales, employment and property, Iowa considers only sales.
(3) Reports losses includes non-Iowa firms that report a net loss of greater than \$100,000.
(4) Tax year includes returns whose tax years begin on or after the first day of the calendar year.

Some clues to the sources of year-to-year variation in corporate tax liability may be obtained by looking at the composition of the tax base by type of business. Although it was not possible to classify all corporate taxpayers,

Table 5: Tax Liability of C-Corporations by Sector and Tax Year, 1995-2005

Part 1: Tax Liability of C-Corporation Taxpayers by NAICS Classification (\$ Million)

NAICS Classification	Tax Year										
	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Ms Classified	\$ 12.68	\$ 30.02	\$ 36.17	\$ 32.71	\$ 31.49	\$ 26.58	\$ 17.26	\$ 22.86	\$ 31.30	\$ 37.30	\$ 40.71
Agriculture	8.08	10.13	9.37	4.68	6.41	10.88	7.53	5.59	9.07	6.57	7.88
Mining	1.00	1.23	1.81	2.41	1.60	1.14	0.78	1.16	0.68	1.87	3.19
Utilities	0.33	3.58	1.91	0.64	0.43	10.21	2.41	4.37	2.72	1.55	1.56
Construction	8.85	9.23	8.19	9.21	9.42	6.54	6.64	5.68	5.28	5.16	5.77
Non Durable Manufacturing	7.86	12.16	9.82	10.49	13.76	8.30	16.43	16.14	21.06	20.06	19.74
Durable Manufacturing	35.54	33.19	134.96	22.80	28.29	5.72	-2.61	-4.24	-6.01	-3.36	21.42
Wholesale Trade	11.68	13.21	12.79	13.84	11.48	9.65	10.25	11.36	14.25	18.39	25.25
Retail Trade	18.23	14.39	30.24	32.42	29.60	18.45	31.19	20.71	37.06	46.47	40.46
Transportation and Warehousing	9.84	5.54	7.75	6.53	4.96	4.92	4.58	4.22	3.22	5.39	7.84
Information	8.30	10.59	8.08	8.25	18.24	21.39	6.05	5.40	6.94	16.70	12.75
Finance	10.41	5.39	7.52	10.08	6.49	5.80	3.61	5.66	6.22	11.88	9.06
Real Estate	12.78	13.85	16.61	9.71	6.45	8.16	5.35	13.56	7.74	12.72	11.06
Professional and Technical Services	6.76	7.08	6.99	7.69	7.89	4.90	4.27	3.40	3.33	4.77	7.16
Management	-0.09	-0.01	-1.49	0.73	0.76	0.27	9.67	1.96	2.38	4.60	8.06
Administrative Services	0.01	0.02	0.03	0.17	0.56	0.62	0.84	1.35	0.92	0.78	1.05
Education	0.03	0.02	0.02	0.04	0.01	0.02	0.02	0.16	0.12	0.09	0.85
Health Care	1.99	1.57	6.50	1.28	0.82	1.32	1.84	2.36	2.16	2.24	9.91
Entertainment	1.09	1.01	0.95	0.14	0.31	0.22	0.23	0.19	0.90	0.41	0.27
Accommodation and Food Service	1.01	0.96	1.01	1.38	1.25	0.99	0.84	1.44	2.62	2.73	4.62
Other Services	1.13	1.01	1.04	1.16	1.11	1.22	1.18	1.26	1.75	1.28	1.03
Total	157.53	174.15	300.26	176.37	181.35	147.29	128.37	124.60	153.72	197.59	239.65

Part 2: Change from Prior Year Tax Liability of C-Corporation Taxpayers by Sector

NAICS Classification	Tax Year										
	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Ms Classified	\$ 17.33	\$ 6.16	-\$ 3.46	-\$ 1.22	-\$ 4.92	-\$ 9.32	\$ 5.60	\$ 8.44	\$ 6.00	\$ 3.41	
Agriculture	2.05	-0.76	-4.69	1.74	4.46	-3.34	-1.95	3.48	-2.50	1.31	
Mining	0.22	0.58	0.60	-0.81	-0.46	-0.36	0.38	-0.49	1.20	1.32	
Utilities	3.24	-1.67	-1.27	-0.21	9.78	-7.80	1.96	-1.66	-1.17	0.01	
Construction	0.38	-1.04	1.02	0.20	-2.88	0.11	-0.96	-0.40	-0.13	0.62	
Non Durable Manufacturing	4.29	-2.34	0.67	3.28	-5.47	8.13	-0.29	4.92	-1.00	-0.32	
Durable Manufacturing	-2.35	101.78	-112.16	5.48	-22.57	-8.33	-1.63	-1.77	2.65	24.78	
Wholesale Trade	1.53	-0.42	1.05	-2.36	-1.83	0.60	1.11	2.89	4.15	6.86	
Retail Trade	-3.84	15.85	2.18	-2.82	-11.15	12.75	-10.48	16.35	9.41	-6.01	
Transportation and Warehousing	-4.31	2.21	-1.21	-1.58	-0.04	-0.34	-0.36	-1.00	2.17	2.45	
Information	2.29	-2.52	0.18	9.98	3.15	-15.34	-0.66	1.54	9.76	-3.94	
Finance	-5.02	2.13	2.57	-3.59	-0.69	-2.20	2.05	0.56	5.66	-2.82	
Real Estate	1.07	2.76	-6.90	-3.27	1.71	-2.81	8.21	-5.83	4.98	-1.66	
Professional and Technical Services	0.32	-0.10	0.70	0.21	-2.99	-0.63	-0.87	-0.07	1.44	2.39	
Management	0.08	-1.49	2.22	0.04	-0.50	9.41	-7.72	0.42	2.22	3.46	
Administrative Services	0.01	0.01	0.14	0.39	0.06	0.22	0.51	-0.43	-0.15	0.27	
Education	-0.01	0.00	0.02	-0.02	0.01	0.00	0.14	-0.03	-0.03	0.76	
Health Care	-0.43	4.94	-5.22	-0.46	0.50	0.52	0.52	-0.20	0.07	7.68	
Entertainment	-0.08	-0.06	-0.81	0.16	-0.09	0.01	-0.04	0.70	-0.48	-0.14	
Accommodation and Food Service	-0.04	0.05	0.37	-0.13	-0.26	-0.16	0.61	1.18	0.11	1.89	
Other Services	-0.12	0.03	0.12	-0.04	0.11	-0.04	0.08	0.49	-0.48	-0.25	
Total	16.62	126.11	-123.89	4.98	-34.06	-18.92	-3.77	29.11	43.88	42.06	

Part 3: Percent Change from Prior Year Tax Liability of C-Corporation Taxpayers by Sector

NAICS Classification	Tax Year										
	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005
Ms Classified	136.7%	20.5%	-9.6%	-3.7%	-15.6%	-35.1%	32.4%	36.9%	19.2%	9.1%	
Agriculture	25.3%	-7.5%	-50.1%	37.1%	69.6%	-30.7%	-25.8%	62.3%	-27.5%	19.9%	
Mining	22.1%	47.7%	33.3%	-33.8%	-28.6%	-31.5%	48.9%	-41.8%	176.6%	70.4%	
Utilities	971.9%	-46.6%	-66.5%	-32.2%	2249.3%	-76.4%	81.2%	-37.9%	-43.1%	0.9%	
Construction	4.3%	-11.2%	12.5%	2.2%	-30.6%	1.7%	-14.4%	-7.0%	-2.4%	12.0%	
Non Durable Manufacturing	54.6%	-19.3%	6.8%	31.3%	-39.7%	98.0%	-1.7%	30.5%	-4.7%	-1.6%	
Durable Manufacturing	-6.6%	306.7%	-83.1%	24.1%	-79.8%	-145.6%	62.5%	41.8%	-44.0%	-737.2%	
Wholesale Trade	13.1%	-3.2%	8.2%	-17.0%	-15.9%	6.2%	10.8%	25.4%	29.1%	37.3%	
Retail Trade	-21.1%	110.1%	7.2%	-8.7%	-37.7%	69.1%	-33.6%	79.0%	25.4%	-12.9%	
Transportation and Warehousing	-43.8%	39.9%	-15.7%	-24.1%	-0.8%	-6.9%	-7.8%	-23.6%	67.2%	45.5%	
Information	27.6%	-23.7%	2.2%	120.9%	17.3%	-71.7%	-10.9%	28.6%	140.6%	-23.6%	
Finance	-48.3%	39.6%	34.1%	-35.6%	-10.6%	-37.9%	56.9%	9.9%	91.1%	-23.7%	
Real Estate	8.4%	19.9%	-41.5%	-33.6%	26.5%	-34.4%	153.5%	-43.0%	64.4%	-13.0%	
Professional and Technical Services	4.8%	-1.4%	10.0%	2.7%	-37.9%	-12.9%	-20.3%	-2.1%	43.2%	50.0%	
Management	-93.8%	27441.0%	-148.8%	5.0%	-64.8%	3496.5%	-79.8%	21.7%	93.2%	75.2%	
Administrative Services	49.7%	50.9%	538.9%	235.4%	11.1%	35.3%	60.7%	-31.6%	-15.9%	35.2%	
Education	-37.3%	23.8%	95.1%	-61.9%	42.8%	-15.5%	757.8%	-20.8%	-27.2%	850.3%	
Health Care	-21.3%	314.9%	-80.3%	-36.1%	61.0%	39.3%	28.5%	-8.3%	3.5%	343.1%	
Entertainment	-7.4%	-6.1%	-85.0%	114.8%	-29.7%	6.8%	-15.6%	360.6%	-53.6%	-34.4%	
Accommodation and Food Service	-4.1%	4.9%	36.6%	-9.2%	-20.8%	-15.8%	72.6%	81.6%	4.2%	69.0%	
Other Services	-10.7%	2.9%	11.6%	-3.7%	9.6%	-3.3%	6.8%	39.1%	-27.3%	-19.5%	
Total	10.6%	72.4%	-41.3%	2.8%	-18.8%	-12.8%	-2.9%	23.4%	28.5%	21.3%	

Note: Tax year includes returns whose tax years begin on or after the first day of the calendar year

Table 5 does show that in most years the lowa corporate tax base is dominated by the manufacturing, trade, information services, finance, and real estate

sectors. When looking at year-to-year variations in tax liability the durable goods manufacturing sector dominates all others. The treatment of depreciation for tax purposes is likely one explanation for the significant variation in tax liability for this sector. Other contributing factors include Iowa's treatment of net operating losses, which allows both carry-backs and carry-forwards, and modifications to and the expansion of business tax incentive programs that in Iowa tend to favor manufacturers over businesses in other sectors.

Importance of Corporate Taxes

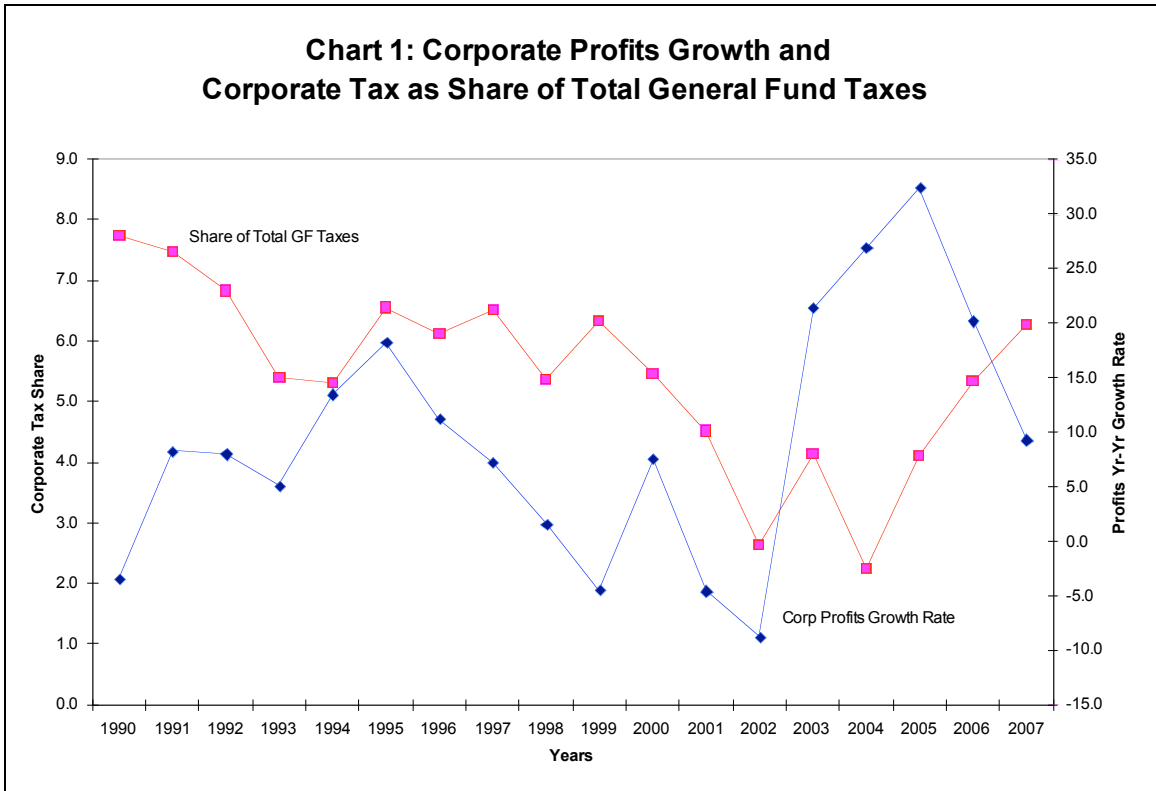
To some the statistics presented in the above tables imply fluctuations in corporate tax liability depend largely on the economy. However, there exists considerable anecdotal evidence that law changes and aggressive "tax planning" by corporations have contributed to a long-term downward trend in the importance of this revenue source in state budgets. This can be seen by comparing corporate tax receipts on a cash basis to total General Fund tax receipts. In Iowa, during FY1990 the ratio of corporate to total tax receipts equaled 7.7 percent. Even with the strong recovery in corporate profits over the past several years the share of General Fund tax revenues paid by corporations has only risen back to 6.3 percent. (See Table 6 and Chart 1.)

Case studies reinforce this perception. A case study of the television broadcasting industry in Iowa revealed considerable differences between profits reported for tax purposes and profits reported in regulatory filings and on financial statements in stockholders reports. At the time of the study 10 VHF and

**Table 6: Iowa Corporate Income Tax
and Total General Fund Tax Receipts and Refunds**

Fiscal Year	Corporate Income Tax (\$ Mil)					All General Fund Taxes (\$ Mil)			Share of Total Taxes (%)	% Change Corp Profits
	Estimates	Returns	Gross	Refunds	Net	Gross	Refunds	Net		
1990	154.104	76.594	230.698	31.139	199.559	2,795.155	218.865	2,576.290	7.7	-3.5
1991	161.995	77.446	239.441	37.510	201.931	2,936.202	232.287	2,703.915	7.5	8.3
1992	175.646	61.602	237.248	44.445	192.803	3,060.686	236.468	2,824.218	6.8	8.0
1993	157.135	67.023	224.158	57.112	167.046	3,399.740	307.904	3,091.836	5.4	5.1
1994	163.553	57.216	220.769	46.484	174.285	3,626.230	341.529	3,284.701	5.3	13.5
1995	212.669	56.030	268.699	40.175	228.524	3,818.956	329.885	3,489.071	6.5	18.2
1996	238.637	38.996	277.633	53.160	224.473	4,039.342	371.253	3,668.089	6.1	11.2
1997	275.528	43.232	318.760	66.036	252.724	4,267.062	387.544	3,879.518	6.5	7.2
1998	250.845	39.862	290.707	75.893	214.814	4,462.532	455.653	4,006.879	5.4	1.6
1999	281.220	40.599	321.819	67.938	253.881	4,526.988	510.558	4,016.430	6.3	-4.5
2000	279.860	46.289	326.149	95.440	230.709	4,744.808	523.936	4,220.872	5.5	7.6
2001	237.886	46.944	284.830	94.025	190.805	4,776.004	547.712	4,228.292	4.5	-4.5
2002	171.166	50.084	221.250	115.968	105.282	4,661.729	654.898	4,006.831	2.6	-8.8
2003	200.656	36.385	237.041	68.200	168.841	4,735.304	646.120	4,089.185	4.1	21.4
2004	200.368	34.419	234.787	140.042	94.745	4,925.951	703.564	4,222.387	2.2	26.9
2005	255.452	25.422	280.874	94.514	186.360	5,230.838	703.257	4,527.581	4.1	32.4
2006	306.556	42.071	348.627	90.707	257.920	5,427.178	593.783	4,833.395	5.3	20.2
2007	331.299	93.317	424.616	98.550	326.066	5,784.501	590.340	5,194.161	6.3	9.3

**Chart 1: Corporate Profits Growth and
Corporate Tax as Share of Total General Fund Taxes**



13 UHF stations served Iowa. The study found that the VHF stations tended to be owned by large national broadcasting companies and that their State tax returns were generally filed by mid-level subsidiaries. On the other hand, the

UHF stations tended to be owned by partnerships or S-corporations, and thus did not file Iowa corporate income tax returns.

The findings of this study that reveal most about how the broadcast companies organized as C-corporations managed their Iowa tax liabilities are the following:

- Some of the companies only reported income from local advertisers although regional and national ads were broadcast in Iowa markets.
- In some cases the corporate parents made large loans to the subsidiaries filing the Iowa returns for no apparent business purpose other than to increase the Iowa companies' interest expenses.
- Some companies ran dividend income through their Iowa stations in order to reduce the Iowa apportionment factor.
- Several of the companies consistently reported losses for the entity filing the Iowa tax return.

Findings from this study are presented only for illustrative purposes.

Different techniques are used by other types of corporations to minimize their Iowa tax liabilities. One feature of Iowa's law that makes the State susceptible to some of the most aggressive tax management techniques used by corporations is the fact that tax returns do not have to be filed on a nationwide combined basis.

Estimated Impacts of Requiring Combined Reporting

The past two legislative sessions bills have been introduced that would require nationwide combined report for C-corporations. However, neither bill made it out of committee. Part of the explanation for the inaction on this issue is the lack of good information on the impact of such a law change. In order to fill this information void the Iowa Department of Revenue undertook a study of the overall fiscal implications and the likely distributive impacts if C-corporations were

required to file Iowa tax returns on a nationwide combined basis.

Trying to estimate the fiscal impact of requiring nationwide combined reporting presented a number of challenges. Primary among these challenges was the inability to obtain federal tax information for all C-corporations filing Iowa returns. In addition, even when the federal return was included with the Iowa filing it was not always possible to determine exactly how intra-corporate transactions should be adjusted to obtain a revised net income amount.

In Iowa C-corporations may elect one of three filing statuses. These are:

- Filing status 1 – Each business entity files separate Iowa and federal tax returns,
- Filing status 2 – For corporations with two or more business entities operating in the State each business entity operating in Iowa files a separate State tax return but the corporation files a combined federal tax return, and
- Filing status 3 – Corporations file a single combined State tax return for all business entities operating in Iowa and file combined federal tax returns.

Corporations that currently file separate State and federal tax returns for each business entity (Filing Status 1) would not be impacted by a State combined reporting requirement. In most cases these are companies that operate single business entities within the State. For each of the four years of the analysis between 94 percent and 95 percent of corporate taxpayers were Filing status 1 filers.

Table 7 shows the overall results of the fiscal impact analysis for Filing Status 2 and 3 corporations. The analysis included tax returns filed for tax years 2000 through 2003. As is often experienced with corporate income tax the State impact of implementing a nationwide combined reporting requirement varies considerably from year to year. Also, some of the variation may be attributed to

limitations of the study. One of these limitations was the lack of complete information on net operating losses for prior tax years that could affect future State tax liabilities under a combined reporting regime.

Filing Basis	Tax Year Iowa Liability (\$ million)				
	2000	2001	2002	2003	Average
Filing Status 2					
Number of Returns	1,584	1,699	2,068	2,016	1,842
Tax Liability under Combined Reporting	\$39.2	\$56.2	\$108.2	\$79.5	\$70.8
Tax Liability under Separate Reporting	\$20.1	\$13.9	\$46.4	\$47.8	\$32.0
Difference	\$19.2	\$42.2	\$61.8	\$31.7	\$38.7
Filing Status 3					
Number of Returns	933	897	962	869	915
Tax Liability under Combined Reporting	\$194.6	\$315.6	\$74.0	\$65.1	\$162.3
Tax Liability under Separate Reporting	\$34.3	\$35.4	\$36.3	\$35.2	\$35.3
Difference	\$160.3	\$280.2	\$37.7	\$29.9	\$127.0
Both Filing Statuses					
Number of Returns	2,517	2,596	3,030	2,885	2,757
Tax Liability under Combined Reporting	\$233.8	\$371.8	\$182.1	\$144.6	\$233.1
Tax Liability under Separate Reporting	\$54.3	\$49.3	\$82.7	\$83.0	\$67.3
Difference	\$179.5	\$322.5	\$99.5	\$61.7	\$165.8
Total Tax Liability Under Current Law	\$148.6	\$132.6	\$138.5	\$155.0	\$143.7
Percent Change	120.8%	243.1%	71.8%	39.8%	115.4%
Notes:					
(1) Filing status 2 means C-corporations file as separate business entities in Iowa, but file federal returns on a combined basis. Filing status 3 means C-corporations with more than one business entity operating in Iowa file a single combined return for those entities in Iowa and file federal returns on a nationwide combined basis.					

Averaging over the four years, the estimated fiscal impact equals \$165.8 million, which equals a 115.4 percent increase in corporate income tax liability. However, since the tax year 2000 and 2001 impact estimates may have been unusually affected by the national recession and the treatment of net operating

losses in the analysis, a more reasonable impact estimate may be obtained by averaging the estimates for just tax years 2002 and 2003. This average impact equals \$80.6 million, or a 54.9 percent increase in tax liability.

From a political perspective, one key issue that arises with the introduction of combine reporting legislation is how businesses based in the State will be impacted versus those based out-of-state. Table 8 presents the results of the fiscal impact analysis by whether corporations are domiciled in Iowa or outside the State for Filing Status 2 filers.

Table 8: Distributional Impact of Combined Reporting for Filing Status 2 Corporations					
	Tax Year Iowa Liability (\$ million)				Average
	2000	2001	2002	2003	
Iowa Domiciled Corporations					
Number of Returns	200	215	194	142	188
Tax Liability under Combined Reporting	\$2.6	-\$4.5	\$8.5	\$7.8	\$3.6
Tax Liability under Separate Reporting	\$1.3	-\$3.9	\$7.1	\$7.5	\$3.0
Difference	\$1.3	-\$0.6	\$1.3	\$0.4	\$0.6
Non-Iowa Domiciled Corporations					
Number of Returns	1,384	1,484	1,874	1,874	1,654
Tax Liability under Combined Reporting	\$36.6	\$60.6	\$99.7	\$71.7	\$67.2
Tax Liability under Separate Reporting	\$18.8	\$17.8	\$39.2	\$40.3	\$29.0
Difference	\$17.9	\$42.8	\$60.5	\$31.3	\$38.1
All Filing Status 2 Corporations					
Number of Returns	1,584	1,699	2,068	2,016	1,842
Tax Liability under Combined Reporting	\$39.2	\$56.2	\$108.2	\$79.5	\$70.8
Tax Liability under Separate Reporting	\$20.1	\$13.9	\$46.4	\$47.8	\$32.0
Difference	\$19.2	\$42.2	\$61.8	\$31.7	\$38.7
Notes:					
(1) Filing status 2 means C-corporations file as separate business entities in Iowa, but file federal returns on a combined basis.					

This analysis shows the impact on Iowa domiciled corporations would be relatively small, but for corporations domiciled outside Iowa the impact would

average about \$23,000 per year in additional tax, which equals a 131.7 percent increase in tax liability.

Table 9 presents a similar distributional analysis for Filing Status 3 corporations. This table shows that on average Iowa domiciled corporations that currently file combined returns for their Iowa operating entities would experience a 56.1 percent decrease in their State tax liabilities. On the other hand, corporations domiciled outside Iowa would experience an average annual tax increase of about \$112,000, or 217.5 percent.

Table 9: Distributional Impact of Combined Reporting for Filing Status 3 Corporations					
	Tax Year Iowa Liability (\$ million)				Average
	2000	2001	2002	2003	
Iowa Domiciled Corporations					
Number of Returns	519	476	474	444	478
Tax Liability under Combined Reporting	\$3.6	\$7.9	\$1.2	\$7.4	\$5.0
Tax Liability under Separate Reporting	\$10.3	\$13.0	\$11.9	\$10.5	\$11.4
Difference	-\$6.7	-\$5.1	-\$10.7	-\$3.1	-\$6.4
Non-Iowa Domiciled Corporations					
Number of Returns	438	440	501	438	454
Tax Liability under Combined Reporting	\$82.1	\$84.8	\$72.8	\$57.8	\$74.4
Tax Liability under Separate Reporting	\$25.3	\$19.5	\$24.4	\$24.5	\$23.4
Difference	\$56.8	\$65.3	\$48.4	\$33.3	\$50.9
All Filing Status 3 Corporations					
Number of Returns	957	916	975	882	932
Tax Liability under Combined Reporting	\$85.6	\$92.6	\$74.0	\$65.3	\$79.4
Tax Liability under Separate Reporting	\$35.6	\$32.5	\$36.3	\$35.1	\$34.9
Difference	\$50.0	\$60.2	\$37.7	\$30.2	\$44.5
Notes:					
(1) Filing status 3 means C-corporations with more than one business entity operating in Iowa file a single combined return for those entities in Iowa and file federal returns on a nationwide combined basis.					
(2) Summary does not include corporations for which returns are under audit review.					

Concluding Comments

It is unknown at this time whether combined reporting will be on the coming year's legislative agenda in Iowa. The recent rise on corporate tax payments has reduced some of the pressure to make any changes in current law. Nevertheless, the need for change does remain. As in many states Iowa's corporate income tax was designed for a different era. In 1934 most corporations doing business in Iowa only did business in Iowa or at most in a few surrounding states. This meant that allowing corporations to allocate income only based on sales did not provide much of an opportunity for corporations to move income out of the State. Today large regional and national corporations dominate Iowa's economy. Not requiring these corporations to report income on a nationwide combined basis has resulted in considerable inequity in the effective rates at which large and small corporations are taxed. Combined report would fix part of the problem, but only part. Even in those states that require combined reporting many corporations pay little or no corporate income tax. Obviously other factors allow corporations that report large profits to shareholders and creditors to report minimal profits on their tax returns. Understanding why the difference exists remains a challenge for state revenue agencies.