D.C. Tax Revision Commission Policy Options

Policy Option #33: Adopt Single-Sales Factor Formula

MEMORANDUM

Proposal: Only use sales to apportion business income to D.C. for tax purposes
Tax Type: Business
Origin: Norton Francis
Commission Goal: Broaden tax base

Current Law

D.C. uses a three-factor formula (sales, property and payroll) to apportion income of a multi-state business to D.C. for taxation purposes. In 2011, D.C. decided to double-weight the sales factor in its formula. As a result, a company's sales in D.C. have a larger effect on its apportionment of income than its property or payroll.

Proposed Change

Shift entirely to sales to apportion business income to D.C. for taxation. Thus, if a multi-state business has 10% of its sales in D.C., it must apportion 10% of its income to D.C. The change would only affect multi-state companies.

Reason for Change

Many multi-state companies sell to D.C. customers but relatively few companies locate in D.C. (or have property or payroll in the city). Using a single-sales factor formula would make D.C. more attractive to firms looking to locate in the region. Also, for many multi-state companies, a single-sales factor would apportion more taxable income to D.C.

The single-sales factor is also increasingly popular for states with business income taxes. For example, Virginia is currently phasing in a single-sales factor formula for retail businesses. Maryland still uses a double-weighted sales formula.

Pros

- Could encourage companies to locate in D.C. since their investments in D.C. property and payroll would no longer affect their tax bill.
- Could increase the share of income from multi-state firms that would be taxable in D.C., which would increase tax revenue.

Cons

- The single-sales factor apportionment may not correspond to the benefits an out-of-state business receives from D.C. In many instances, companies would use fewer government services to support a marketplace than the services they would use with more physical property and payroll located in the city.
- Companies may reduce their sales to D.C. to mitigate their tax liability.

Revenue Impact

The Office of Revenue Analysis estimates that in its first year of implementation adopting a single-sales factor formula would raise $20,000,000 in new tax revenue.