



ALLEGHENY INSTITUTE

FOR PUBLIC POLICY

June 22, 2023

Policy Brief: Volume 23, Number 23

Is Pennsylvania's Corporate Net Income Tax cut going to speed up?

Summary: A 2022 *Policy Brief* (Vol. 22, No. 31) detailed changes to Pennsylvania's Corporate Net Income Tax (CNIT). Act 53 of 2022 reduces the CNIT rate by five percentage points over the course of nine years. The first reduction, a 1 percentage point drop from 9.99 percent to 8.99 percent, occurred Jan. 1, 2023. A new legislative proposal would speed up the current schedule on which the tax is to be reduced by five years.

According to the state's Tax Compendium, the CNIT is "the tax paid by all domestic and foreign corporations for the privilege of doing business, carrying on activities, or employing or owning capital or property in Pennsylvania."

Pennsylvania's current CNIT rate is 8.99 percent. When the rate dropped at the beginning of 2023, it was the first reduction since 1995. For the first 11 months of the current fiscal year (FY) 2022-23, the state Independent Fiscal Office (IFO) reported that collections were \$5.1 billion, which was greater than the \$4.4 billion collected over the same period in FY 2021-22.

Prior to the reduction, from January through May 2022, \$1.98 billion was collected. From January through May 2023, after the reduction to 8.99 percent, \$2.46 billion was collected, an increase in collections of \$480 million.

In its official revenue estimate for FY 2023-24 the IFO placed CNIT collections at \$5.7 billion. This is a decrease from the revised \$6.2 billion that IFO estimated for FY 2022-23.

How does PA compare?

According to the Tax Foundation, 44 states currently levy a corporate income tax, four (Nevada, Ohio, Texas, and Washington) levy gross receipts taxes in lieu of a corporate income tax, and two (South Dakota and Wyoming) levy neither. Of the states that tax corporate income, 29 levy the tax at a single rate while 15 have a marginal corporate income tax rate, which levies a different percentage tax based on the income brackets of separate corporations.

Despite its recent reduction, Pennsylvania still possesses the third-highest corporate income tax compared to other single-rate states, with Minnesota and Illinois ranking higher. Pennsylvania also ranks third-highest measured against those states with a marginal rate, behind New Jersey's and Alaska's top marginal rate. This demonstrates slight improvement from last year when Pennsylvania was the highest tax among single rate states and the second-highest compared to marginal rate states.

When contrasted with other states that are in the same geographic area, it can be seen that the reduction has brought Pennsylvania to a comparable corporate income tax level with several of them, unfortunately still on the high end. Both Delaware and Maryland are close, with tax rates at 8.7 percent and 8.25 percent, respectively. New York and West Virginia are slightly lower with rates of 7.25 percent and 6.5 percent each. New Jersey measures substantially higher, boasting a top marginal tax rate of 11.5 percent, the highest in the country.

Although Pennsylvania cut its rate, so, too, did six other states: Iowa; Arkansas; Nebraska; Idaho; Colorado and New Hampshire. Of these, on a percentage point basis, Pennsylvania had the second-largest decrease behind Iowa, and the largest decrease of the four single-rate tax states.

Act 53's next CNIT reduction calls for a 0.5 percentage point drop to 8.49 percent in January 2024. Assuming all 43 other states with a corporate income tax maintain their current corporate income tax rates, Pennsylvania would rank 5th highest behind Delaware for single rate states and would also be ranked 5th highest behind Vermont for states with a marginal rate.

Legislative proposal

As noted in last year's *Brief*, candidates running for the governor's office, as well as members of the General Assembly, expressed support for a more rapid decrease in the tax rate. Legislation introduced in the Senate last month would amend Act 53's reduction schedule by arriving at the 4.99 percent rate by the beginning of 2026. It would accomplish this by reducing the rate by 1 percentage point per year rather than the current half percentage point schedule.

CNIT Rates under Act 53 and New Proposal

Year	Act 53	New Proposal
2022	9.99%	9.99%
2023	8.99%	7.99%
2024	8.49%	6.99%
2025	7.99%	5.99%
2026	7.49%	4.99%
2027	6.99%	4.99%
2028	6.49%	4.99%
2029	5.99%	4.99%
2030	5.49%	4.99%
2031	4.99%	4.99%

Possible effects

A benefit of Pennsylvania pursuing the abbreviated reduction period of the CNIT is that it could incentivize individuals and corporations to migrate to the state. This is a trend that has not been going in the right direction and needs to be reversed. According to the IFO, which used IRS migration data from 2020-2021, Pennsylvania recorded a net migration loss of 14,376 residents. This represented a 0.11 percent decrease in Pennsylvania's population. By age-range, the combined negative net migration of ages 26-54 was 4,684 (33 percent of total) in this period.

The six states Pennsylvanians were most likely to move to were Texas; Georgia; South Carolina; Delaware; North Carolina and Florida. These states, by and large, are comparatively more business-friendly, with all but Delaware being Right-to-Work states.

This more aggressive schedule should be a boost to Pennsylvania, which is lagging behind other states in terms of post-pandemic job recovery. According to the Bureau of Labor Statistics (BLS), average monthly nonfarm employment in the U.S. for 2019, prior to the lockdowns and pandemic of the following year, were 150.9 million. By 2022, this number had increased, with the average climbing to 152.6 million, a 1.1 percent increase.

These numbers are in stark contrast to Pennsylvania's statistics. In 2019, Pennsylvania had a monthly average of 6.07 million nonfarm jobs. However, in 2022, this count had decreased to 5.98 million, a drop of 1.3 percent.

Additionally, the 2023-24 Executive Budget presented in March budgets CNIT revenue for FY 2023-24 at \$5.3 billion. As the gradual reduction of the CNIT continues, the Executive Budget estimates that by FY 2027-28, when the CNIT drops to 6.49 percent during the fiscal year in accordance with the current reduction schedule, CNIT revenue will have dropped to \$4.2 billion, a 21 percent reduction.

In order to come up with spending reductions to offset revenue losses from the lower CNIT rates, policymakers should look first to the economic development subsidies and

incentives it grants to targeted businesses. After all, any business that would be subject to paying the CNIT will be paying the same reduced rate as others, thus leveling the playing field and reducing the need to grant subsidies to certain select businesses.

The recent proposal can be seen as a benefit to Pennsylvania. Not only would it offer a reprieve from the high tax rate encumbering existing corporations in the commonwealth but it could also serve as a beacon, incentivizing both other corporations and individuals to migrate to Pennsylvania.

Eric Montarti, Research Director

Scott T. Cross, Research Assistant

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Allegheny Institute for Public Policy
305 Mt. Lebanon Blvd.* Suite 208* Pittsburgh PA 15234
Phone (412) 440-0079
E-mail: aipp@alleghenyinstitute.org
Website: www.alleghenyinstitute.org
Twitter: [AlleghenyInsti1](https://twitter.com/AlleghenyInsti1)