Delaware: Dow Chemical and DuPont merge causing Delaware to change its tax code

David M. Kall | Friday, March 4, 2016

Last December, Dow Chemical Co. and DuPont Co., headquartered in Auburn Hills, Michigan and Wilmington, Delaware, respectively, **announced** that they would combine in a game-changing, all-stock merger of equals.

The new firm, DowDuPont, with a combined market capitalization of approximately $130 billion, intends to separate into three independent, publicly traded companies through tax-free spin-offs within the 18-24 months after the merger is closed. These businesses would be the following:

1. An agricultural concern, uniting the seed and crop protection businesses;
2. A material science entity, purposed in creating high-growth, high-value industry segments in packaging, transportation, and infrastructure solutions; and
3. A specialty products enterprise that will center on unique businesses that share similar investment characteristics and specialty market focus, and which will include DuPont's Nutrition & Health, Industrial Biosciences, Safety & Protection and Electronics & Communications, as well as the Dow Electronic Materials business.

In a February 19, 2016, **joint press release**, the companies stated that they expect to achieve $1.3 billion in "synergies." Prior to the separation into three parts, there will be dual headquarters in both states. After, the agricultural concern and specialty products will both be in Wilmington, while material science will be in Midland, Michigan. Additionally, global business centers will be located in Indiana, Iowa, and elsewhere in the United States and around the world.

To make sure that Delaware retains as much of the operations as possible, lawmakers **agreed** to modify the state's tax code. The reforms, which do not impact the fiscal year 2017 budget projections, include these:

1. Modification of the state's research and development tax credit to lift the yearly $5 million expenditure caps and make the credit refundable;
2. Reintroduction of a modernized version of Delaware's "New Economy Jobs Tax Credit," intended to attract corporate headquarters jobs to Delaware; and
3. Implementation of a Strategic Fund grant, which the Delaware Economic Development Office will present to the Council on Development Finance. This could be worth a total of $9.6 million over five years, mostly in the form of matching funds capital expenditure assistance. The Fund would help DowDuPont and related spinoffs upgrade research facilities in Delaware, contingent upon spending at least $200 million in the state over the five-year time frame.

Beyond these, Delaware Governor Markell signed the **Delaware Competes Act** at the end of January. According to the **synopsis** of the original bill, its overarching purpose is to encourage job creation and investment in The First State. More specifically, it changes how income is apportioned – the process by which multi-state firms determine what share of their total income is assigned to Delaware – for purposes of the corporate income tax.

As it currently stands, Delaware uses three equally weighted factors to apportion income: a) property; b) payroll; and c) sales.

These factors are expressed as a fraction with Delaware's share in the numerator and the total amount in the denominator, which are then averaged to arrive at the ultimate Delaware apportionment percentage.

Many corporations criticize the use of property and payroll in this calculation, because when they add employment or facilities in Delaware, their Delaware apportionment often rises, creating higher Delaware corporate income taxes.

Delaware Competes revises the calculations to eliminate investment disincentives. It also simplifies tax compliance for smaller businesses by reducing tax payment and filing burdens. These measures include:

- Doubling the thresholds at which businesses must make monthly gross receipts tax and withholding filings, enabling hundreds of Delaware businesses to file quarterly instead;
- Indexing filing thresholds and tax calculations for inflation, which locks in the simplification and efficiency gains for future taxpayers;
- Allowing firms with receipts under $20 million to utilize a simpler, evenly-weighted schedule. Now, all corporations must pay 50 percent of their estimated tax liability for the first quarter of their taxable year, followed by payments of 20 percent, 20 percent and 10 percent in each of their second through fourth quarters, but under the new schedule, they can pay 25 percent per quarter.
- Updating the calculation for the penalty for underpayment of estimated tax, which has not changed in more than 30 years.

The **fiscal note** reveals that the costs for fiscal year 2017, 2018, and 2019 are $8,200,000, $17,600,000, and $22,900,000, respectively.

BloombergBusiness pointed out that DowDuPont Co. plans to reduce the total 63,000 person workforce by 10 percent, and reduce costs by $700 million. In Delaware, it will cut about 28 percent, or 1,700 out of 6,100 employee, in early 2016. This, even though it does not expect to have received shareholder and federal government approvals until the end of 2016.

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