MDCEP
MARYLAND CENTER ON ECONOMIC POLICY
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Closing Corporate Tax Loopholes Would Enable Maryland to Invest in our Future

Position Statement in Support of House Bill 473

Given before the House Ways and Means Committee

House Bill 473 would close a loophole that allows large, multistate corporations to artificially lower their tax responsibilities in Maryland. Allowing these special tax breaks makes it harder to invest in the pillars of Maryland's economy, such as health care and education. It also puts small, Maryland-based businesses at a disadvantage. The Maryland Center on Economic Policy supports House Bill 473 because it would improve provisions of our tax system that shield corporate profits from taxation.

When a company does business in multiple states, the states must determine how its income should be divided when calculating the company's tax responsibility. Like most states, Maryland does this using a formula intended to measure the portion of a corporation's business activities that occur in Maryland. This system helps to prevent multiple states from taxing each dollar of a business's profits. However, due to a federal law passed in the 1950s, when a company located in Maryland makes sales into another state, this income is sometimes not subject to taxation by any state. It becomes "nowhere income."

House Bill 473 would ensure that each dollar of corporate income in Maryland is subject to taxation by a single state, without double taxation or nowhere income. Specifically, when a Maryland corporation sells goods into states that do not have jurisdiction to tax those sales, the bill would assign the resulting income to Maryland for the purpose of calculating the company's tax bill. This practice is often called the throwback rule, because profits are "thrown back" to the state where a business is located. Adopting the throwback rule would put small companies that primarily do business inside Maryland on more equal footing with large corporations that sell into other states.

Nowhere income is a tax break corporations get that similarly situated individuals can't access. If you live in one state and work in another, you pay income tax on your total income in your state of residence. You can claim a credit for taxes paid to another state, but by default your state of residence get it. House Bill 473 would essentially apply the same rule to corporations as individuals already follow.

Passing House Bill 473 would put Maryland in good company. Most states that levy a corporate income tax already use either the throwback rule or a similar "throw out" rule that achieves the same end using a different formula. Because it is so common, most large corporations that would be subject to these provisions already have significant experience complying with it elsewhere.

Legislative analysts estimate that House Bill 473 would increase state revenues by about $50 million per year once fully implemented, enabling the state to invest more in education and other essential services that will strengthen our economy in the long run.[i] Cleaning up our tax code by removing special interest tax breaks is the best way to raise the resources Maryland needs to build world-class public schools, a healthy population, and modern transportation infrastructure.

Maryland has a lot to offer as a place to do business, and will retain these advantages with corporate tax reforms that support increased investments in the foundation of our economy. We have the highest median household income among the 50 states.[ii] Our workforce is highly educated, with the second-highest share of advanced degree holders. College graduates have moved into Maryland at higher rates in recent years than into most other states.[iii] We have the more millionaires per capita than all but three states.[iv] And our mix of taxes and services is among the most favorable to businesses, according to the accounting and consulting firm Ernst and Young.[v]

House Bill 473 represents an important step forward for Maryland's revenue system. If enacted, it would help us make the investments needed to build Maryland's future prosperity.

For these reasons, the Maryland Center on Economic Policy respectfully requests that the House Ways and Means Committee make a favorable report on House Bill 473.

Equity Impact Analysis: House Bill 473

Bill summary

House Bill 473 closes a loophole that currently allows large, multistate corporations to reduce their tax responsibility in Maryland.

Enacting the throwback rule would require Maryland-based corporations to attribute to Maryland any profits from sales into states where they are not taxable because of a lack of legal nexus. This would ensure that each dollar in profits is attributed to exactly one state for tax purposes, eliminating so-called "nowhere income."

Background

The throwback rule is well established across the country.

- Most states that levy a corporate income tax already use either the throwback rule or a similar "throw out" rule that achieves the same end using a different formula, ranging from nearby West Virginia to economic powerhouse California.

Equity Implications

- Corporate tax loopholes primarily benefit the small number of wealthy households that hold the bulk of corporate stock and other financial assets. Multiple intersecting areas of historical and continuing racist policy have made household wealth in the United States heavily lopsided. The wealthiest 10 percent of white households nationwide (about 6 percent of all households) control nearly two-thirds of all built-up wealth.[vi] Closing corporate tax loopholes would ensure that our tax code does not place greater responsibilities on people who derive their income from work than on those whose income comes from wealth, and thereby lower one barrier that holds back many Marylanders of color.
- Closing corporate tax loopholes would generate revenues that could be invested in things like world-class

schools, sufficient child care assistance, and reliable transit. Investing in these basics strengthens our economy and can dismantle the economic barriers that too often hold back Marylanders of color.

Impact

House Bill 473 would likely **improve racial and economic equity** in Maryland.

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[i] Heather MacDonagh, "Fiscal and Policy Note: House Bill 473," Department of Legislative Services, 2020, http://mgaleg.maryland.gov/2020RS/fnotes/bil_0003/hb0473.pdf.

[ii] 2017 American Community Survey one-year estimates.

[iii] Quoctrung Bui, "The States That College Graduates Are Most Likely to Leave," *The New York Times*, Nov. 22, 2016, https://www.nytimes.com/2016/11/22/upshot/the-states-that-college-graduates-are-most-likely-to-leave.html

[iv] Jeff Clabaugh, "Maryland Loses No. 1 Spot for Millionaires; DC Is No. 2," *WTOP*, January 30, 2019, https://wtop.com/business-finance/2019/01/maryland-loses-no-1-spot-for-millionaires-dc-is-no-2/

[v] "Total State and Local Business Taxes: State-by-State Estimates for Fiscal Year 2016," Ernst & Young LLP, 2017, https://www.ey.com/Publication/vwLUAssets/ey-total-state-and-local-business-taxes-2016/$File/ey-total-state-and-local-business-taxes-2016.pdf

[vi] 2016 Survey of Consumer Finances.