# MSEA_zwerling_fav_SB24

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Position: FAV

msea maryland state education association

EDUCATORS TOGETHER

140 Main Street
Annapolis, MD 21401-2003
marylandeducators.org

# Testimony in Support of Senate Bill 24
# Small Business Fairness Act

## Senate Budget and Taxation Committee
## January 9, 2020
## 1:00 PM

## Samantha Zwerling
## Government Relations

The Maryland State Education Association supports SB 24 proposing to require specific corporations to compute Maryland taxable income using the method of combined reporting.

MSEA represents 74,000 educators and school employees who work in Maryland's public schools, teaching and preparing our 893,689 students for career jobs of the future. MSEA also represents 39 local affiliates in every county across the state of Maryland, and our parent affiliate is the 3 million-member National Education Association (NEA).

MSEA supports passage of an adequate, sustainable, predictable revenue stream that will adequately fund both the operating and construction costs of our public schools. Public education, as with many other worthy services provided by government, is a common good and needs to be supported with revenue sources that are broad based, reliable, and stable. Providing adequate funding for education is an investment that promotes families, communities, economic development, and public safety. Investing in education provides an educated workforce that pays income taxes based upon higher salaries, pays sales taxes based upon greater consumer demand, and pays property taxes through expanded home purchasing power. Today's investment in education is tomorrow's increased government revenues.

A great public school for every child means our students have updated technology, small manageable classes, safe and modern schools, proper healthcare and nutrition, and have highly qualified and highly effective educators. The work of the Commission on Innovation and Excellence in Education (Kirwan Commission) further recommends improvements to access to Pre-K and Career Technology Education, as well as expansion of the educator workforce and increased salaries to help deliver individualized instruction and recruit and retain the best workforce in the country.

The Kirwan Commission has determined that Maryland will need to put substantially more resources into education if our state is to help our citizens become truly successful in the very competitive national and global economies. This is the time to be locating and allocating more resources to education, and combined reporting is part of that funding solution.

**We urge the committee to issue a Favorable Report on Senate Bill 24.**

# COST Testimony in Opposition to S 24 (MUCR)
Uploaded by: Duckman, Ashley
Position: UNF

**Patrick J. Reynolds**
*Senior Tax Counsel*
(202) 484-5218
preynolds@cost.org

January 9, 2020

Senate Budget and Taxation Committee
Maryland General Assembly

**Re: In Opposition to Senate Bill 24, Mandatory Unitary Combined Reporting**

Dear Chair Guzzone, Vice Chair Rosapepe, and Members of the Committee,

Thank you for the opportunity to submit testimony on behalf of the Council On State Taxation (COST) in opposition to Senate Bill 24, the Small Business Fairness Act, which would impose mandatory unitary combined reporting (MUCR) on retail trade and food and beverage establishments. MUCR arbitrarily assigns income to a state, negatively impacts the real economy, has an unpredictable effect on state revenue, and imposes significant administrative burdens on both the taxpayer and the state. Further, the Maryland Economic Development and Business Climate Commission, established at the request of the General Assembly's leadership, has expressed that Maryland should not adopt MUCR because it: (1) creates revenue volatility, (2) picks winners and losers among taxpayers, and (3) leads to additional litigation and administrative costs.

## About COST

COST is a nonprofit trade association based in Washington, DC. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce and today has an independent membership of approximately 550 major corporations engaged in interstate and international business. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities.

## COST's Position on Mandatory Unitary Combined Reporting

The COST Board of Directors has adopted a formal policy statement on MUCR. COST's policy position is:

*Mandatory unitary combined reporting ("MUCR") is not a panacea for the problem of how to accurately determine multistate business income attributable to economic activity in a State. For business taxpayers, there is a significant risk that MUCR will arbitrarily attribute more income to a State than is justified by the level of a corporation's real economic activity in the State. A switch to MUCR may have significant and unintended impacts on both taxpayers and States. Further, MUCR is an unpredictable and burdensome tax system. COST opposes MUCR.*

One of the most controversial business tax policy issues currently debated by state legislators, tax administrators, and business taxpayers is how a state should determine the corporate income tax base. The first approach, "separate entity reporting," treats each corporation as a separate taxpayer. This is the method Maryland currently uses; it is also used by Maryland's regional competitor-states, including Delaware, Pennsylvania, and Virginia. The second approach, MUCR, treats affiliated corporations (parents and subsidiaries) engaged in a "unitary business" as a single group for purposes of determining taxable income.[1] MUCR has several serious flaws.

- **Reduces Jobs –** Proponents of MUCR have focused on the benefits in terms of reducing tax planning opportunities, but they fail to acknowledge the evidence that adopting MUCR hinders investment and job creation. Even if MUCR results in only a relatively small increase in net corporate tax revenue, there will be significant increases and decreases in tax liabilities for specific businesses. Depending on the industry distribution of winners and losers, adopting MUCR may have a negative impact on a state's overall economy. Moreover, economic theory suggests that any tax increase resulting from adopting MUCR will ultimately be borne by labor in the state through fewer jobs (or lower wages over time) or by in-state consumers through higher prices for goods and services.

  States that use separate entity reporting have experienced higher job growth than have states with MUCR. From 1982-2006, job growth was 6% higher in states without MUCR than in states with it (after adjusting for population changes).[2] Furthermore, MUCR has been found to reduce economic growth, especially when the tax rate exceeds 8%[3] (Maryland's rate is 8.25%).

- **Uncertain Revenue –** Implementing MUCR would have an unpredictable and uncertain effect on Maryland's revenue. The corporate income tax is the most volatile tax in every state in which it is levied, regardless of whether MUCR is employed. A study conducted by the University of Tennessee found no evidence that states with MUCR collect more revenue, and then in a later study found that MUCR may or may not increase revenue.[4] Maryland's own commission found similar uncertainty and volatility, with MUCR increasing revenue in some years and reducing it in others; after examining five years of pro forma tax returns, MUCR may have resulted in less revenue than the State's current corporate income tax structure in two or three of those years.[5] The Indiana Legislative Services Agency conducted a study in 2016 finding that any potential positive revenue

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[1] The concept of a "unitary business" is a constitutional requirement that limits the states' authority to determine the income of a multistate enterprise taxable in a state. Due to varying state definitions and case law decisions, the entities included in a unitary group are likely to vary significantly from state to state.
[2] Robert Cline, "Combined Reporting: Understanding the Revenue and Competitive Effects of Combined Reporting," Ernst & Young, May 30, 2008, p. 16.
[3] William F. Fox, LeAnn Luna, Rebekah McCarty, Ann Boyd Davis and Zhou Yang, "An Evaluation of Combined Reporting in the Tennessee Corporate Franchise and Excise Taxes," University of Tennessee, Center for Business and Economic Research, October 30, 2009, p. 39. Another study by the two lead authors commissioned by the National Conference of State Legislatures reached similar conclusions.
[4] *Ibid*. 3, p. 34.
[5] Andrew Schaufele, Director, MD Bureau of Revenue and Estimates, Report on Combined Reporting to Governor, President and Speaker Report on Combined Reporting to Governor, President and Speaker, March 1, 2013.

impact from adopting MUCR would be only short-term and would likely decline to zero in the long-term.[6]

- **Regional Outlier –** Most of the states that utilize MUCR are west of the Mississippi River or in the Northeast. Apart from the District of Columbia and West Virginia, none of Maryland's neighboring competitor states currently utilizes MUCR, not Virginia, North Carolina, Delaware, or Pennsylvania.

- **Administrative Complexity –** MUCR is, by definition, complex, requiring extensive fact-finding to determine the composition of the "unitary group" and to calculate combined income. This complexity results in unnecessary and significant compliance costs for both taxpayers and the State. Further, the bill inappropriately delegates many details of the administration of the tax that should be codified in Maryland's law. The bill does not clearly specify how the tax should be administered; instead, it gives the Comptroller broad authority to adopt regulations to enforce the collection of the tax using MUCR.

    - *Determining the Unitary Group*: The concept of a "unitary business" is uniquely factual and universally poorly-defined. It is a constitutional (Due Process) concept that looks at the business as a whole rather than individual separate entities or separate geographic locations. In order to evaluate the taxpayer's determination of a unitary relationship, state auditors must look beyond accounting and tax return information. Auditors must annually determine how a taxpayer and its affiliates operate at a fairly detailed level to determine which affiliates are unitary. Auditors must interact with a corporation's operational and tax staff to gather this operational information. In practice, however, auditors routinely refuse to make a determination regarding a unitary relationship on operational information and instead wait to determine unitary relationships until after they have performed tax computations. In other words, the tax result of the finding that a unitary relationship exists (or does not exist) often significantly influences, or in fact controls the auditor's finding. Determining the scope of the unitary group is a complicated, subjective, and costly process that is not required in separate filing states and often results in expensive, time-consuming litigation.

    - *Calculating Combined Income*: Calculating combined income is considerably more complicated than simply basing the calculations on consolidated federal taxable income. In most MUCR states, the group of corporations included in a federal consolidated return differs from the members of the unitary group. In addition to variations in apportionment formulas among the states that apply to all corporate taxpayers, further compliance costs related to MUCR result from variations across states in the methods used to calculate the apportionment factors. From a financial reporting perspective, adopting MUCR is a significant change that requires states to consider ways to mitigate the immediate and negative impact those tax changes have on a company's financial reporting.[7]

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[6] A Study of Practices Relating to and the Potential Impact of Combined Reporting, Office of Fiscal and Management Analysis, Indiana Legislative Services Agency, October 1, 2016.
[7] ASC 740 (formally FAS 109) requires a recordation of tax expense under certain circumstances that can negatively impact a company's stock price and value.

- **Arbitrary –** Although proponents of MUCR argue that it helps to overcome distortions in the reporting of income among related companies in separate filing systems, the mechanics used under MUCR create new distortions in assigning income to different states. The MUCR assumption that all corporations in an affiliated unitary group have the same level of profitability is not consistent with either economic theory or business experience. Consequently, MUCR may reduce the link between income tax liabilities and where income is actually earned. Many corporate taxpayers may conclude that there is a significant risk that MUCR will arbitrarily attribute more income to a state than is justified by the level of a corporation's real economic activity in the state.

## Conclusion

The General Assembly's own commission tasked with studying how to improve the State's economy stated that MUCR should be expressly rejected because its continued consideration discourages business investment in the State.[8] MUCR will not help Maryland attract jobs or investment and should not be adopted. This is especially true for an arbitrary imposition of MUCR on retail and food service businesses.

COST urges members of the committee to please vote "no" on Senate Bill 24.

Respectfully,

Patrick J. Reynolds

cc: COST Board of Directors
Douglas L. Lindholm, COST President & Executive Director

[8] Report of the Maryland Economic Development and Business Climate Commission, Phase II: Taxes, published January 19, 2016, p. 39.

**SB 24 _ Small Business Fairness Act**
Uploaded by: Duckman, Ashley
Position: UNF

MARYLAND
Chamber of Commerce

**LEGISLATIVE POSITION:**
**Unfavorable**
**Senate Bill 24**
**Small Business Fairness Act**
**Senate Budget and Taxation Committee**

**Thursday, January 9, 2020**

Dear Chairman Guzzone and Members of the Committee:

Senate Bill 24 would require businesses in retail and food services to compute their taxes using the combined reporting method—a highly complex system of determining taxable income among all states in which a company does business.

Over the last decade, combined reporting has been exhaustively researched and debated among policymakers in Annapolis and across the state. The prevailing sentiment remains that combined reporting is not an appropriate or accurate method of computing state taxable income or attributing multistate business income to economic activity in Maryland. In fact, a combined reporting system would result in significant and unintended negative consequences for business taxpayers, including competitive disadvantage, undue complexity and administrative burden, all while resulting in no guaranteed increase to state revenue.

Combined reporting will not increase state tax revenue. Proponents of combined reporting contend that it will raise millions in additional tax revenue, but there is no data to support that argument. In fact, under the previous administration, Maryland's own Business Tax Reform Commission found that instituting combined reporting "would result in a shift of the tax burden, substantial in some cases, among industries and among taxpayers, resulting in winners and losers." The Commission explained further that the reasons cited in support of combined reporting have each been addressed through other legislative vehicles adopted by the General Assembly and tougher audit methods now utilized by the Comptroller's Office.

Since 2004, the Comptroller's Office has utilized two provisions of the State's Tax Statute to correct perceived abuses of intercompany/interstate transactions. The first is the "add-back" provision that disallows deductions for certain expenses paid to related corporations in other states. The second are provisions granting the Comptroller discretionary powers to adjust amounts of income and expenses between related corporations.

Combined reporting would have a negative impact on Maryland's economy since its adoption may, in practice, increase effective corporate income tax rates. For example, even if its proponents were correct in arguing that combined reporting would result in an increase in net corporate tax revenue, there will be significant increases and decreases in tax liabilities for specific businesses, thereby resulting in winners and losers. What is more, any resulting tax increase will ultimately be felt most by in-state consumers, who will contend with higher prices for goods and services, and by labor through fewer jobs and/or lower wages over time.

Combined reporting presents a real competitive disadvantage for Marylanders. Within the region, many of our neighboring states—including Virginia, Pennsylvania and Delaware—do not utilize the mandatory combined reporting method. As a result, it would be detrimental for Maryland to employ a new taxation system that will harm the attraction and retention of businesses, and cost Marylanders access to more jobs and economic opportunities.

For these reasons, the Maryland Chamber of Commerce respectfully requests an **unfavorable report** on **SB 24**.

# GBCFry_Oppose_SB24
Uploaded by: Fry, Donald
Position: UNF

# gbc POSITION STATEMENT

**TESTIMONY PRESENTED TO THE SENATE BUDGET AND TAXATION COMMITTEE**

**SENATE BILL 24 -- SMALL BUSINESS FAIRNESS ACT**

**January 9, 2020**

**DONALD C. FRY**
**PRESIDENT & CEO**
**GREATER BALTIMORE COMMITTEE**

**Position: Oppose**

The Greater Baltimore Committee (GBC) opposes Senate Bill 24, which requires retail trade and food services corporations to compute Maryland taxable income using combined reporting. At issue is competitiveness, which has long been at the forefront of debate and discussion with regard to Maryland's business climate. While Maryland has numerous competitive strengths, including a highly-skilled workforce, excellent access to health care, top-ranked universities and a good quality of life, in many annual reviews Maryland consistently ranks near the bottom on a number of key business metrics. Additionally, when compared to neighboring states, Maryland's tax structure as it relates to business growth and job creation is often viewed unfavorably.

Combined reporting has been considered and defeated for many years. In 2010, the Maryland Business Tax Reform Commission (MBTRC) evaluated the effects of implementing combined reporting. The MBTRC recommended that the Maryland General Assembly reject this policy for a number of reasons, including that many of the tax avoidance measures that combined reporting is intended to prevent had already been addressed in previous policies enacted by the legislature. In 2014 while opposing a similar bill that would have required combined reporting, the Council on State Taxation wrote that combined reporting reduces jobs, increases the administrative burden on businesses and would have an "unpredictable and uncertain effect on Maryland's revenue."

In 2015, the Maryland Economic Development and Business Climate Commission, also known as the Augustine Commission, issued a report recommending that combined reporting not be adopted in Maryland and emphasized that this intent should be clearly communicated. The report said combined reporting "…can create revenue volatility and winners and losers among corporate taxpayers." It further added, "Combined reporting can also lead to additional litigation from taxpayers and create additional administrative costs for both taxpayers and the state."

Aside from creating additional difficulties on businesses, combined reporting would also adversely affect Maryland's competitiveness as many states do not require this method of computing taxable income. In the Mid-Atlantic region, very few states require the combined reporting method.

If Maryland strives to be competitive in the 21st century economy, policies must reflect an understanding of the challenges faced by our State's businesses and a willingness of government to partner with the business community. Senate Bill 24 would put additional administrative burdens on businesses, which is not reflective of a state that strives to be competitive and welcoming to business growth and job creation.

Furthermore, one of the criticisms of combined reporting is complexity on Maryland companies. In Senate Bill 24, only select industries are required to use the combined reporting method. This would make Maryland's tax structure unnecessarily complicated.

This bill is inconsistent with two of the key tenets in *Gaining the Competitive Edge: Keys to Economic Growth and Job Creation in Maryland,* a report published by the GBC that identifies eight core pillars for a competitive business environment and job growth:

> **Competitive costs of doing business.** Public policies must reflect a government predisposition to nurture business growth and to avoid arbitrarily or disproportionately imposing additional overhead upon the business sector.
>
> **Tax structure that is fair and competitive.** Maryland's tax policy must be perceived by business as being competitive and devoid of elements that unreasonably target specific businesses or business sectors.

Finally, the Greater Baltimore Committee's 2020 Legislative Priorities state that a key priority is building a competitive, predictable and fair tax system. The 2020 Legislative Priorities specifically cites this proposed legislation, stating that the Maryland legislators should "Oppose the passage of destabilizing business taxation proposals that would create uncertainty, negatively affect the corporate tax structure or diminish the economic vitality of our State."

**For these reasons, the Greater Baltimore Committee urges an unfavorable report on Senate Bill 24.**

*The Greater Baltimore Committee (GBC) is a non-partisan, independent, regional business advocacy organization comprised of hundreds of businesses -- large, medium and small -- educational institutions, nonprofit organizations and foundations located in Anne Arundel, Baltimore, Carroll, Harford, and Howard counties as well as Baltimore City. The GBC is a 65-year-old, private-sector membership organization with a rich legacy of working with government to find solutions to problems that negatively affect our competitiveness and viability.*

**RestaurantAssociation_MelvinThompson_Oppose_SB24**
Uploaded by: Thompson, Melvin
Position: UNF

**SENATE BILL 24**

**Small Business Fairness Act**

**January 9, 2020**

**Position: Oppose**

Mr. Chairman and Members of the Budget and Taxation Committee:

The *Restaurant Association of Maryland* opposes Senate Bill 24, which would require certain affiliated foodservice corporations with multiple locations to compute Maryland taxable income using a combined reporting method.

This legislation targets the foodservice industry. The proposed formula would create an additional tax burden on some members of our industry, potentially increasing their Maryland tax liability through a computation method that includes income from non-Maryland locations. There is no basis for crossing state lines for tax purposes on income not related to Maryland transactions.

Passage of this legislation would also discourage some restaurant groups from expanding into Maryland, especially given that new restaurants typically operate at a loss for the first couple of years as they pay off opening costs and find operational efficiencies.

For these reasons, we oppose this legislation and request an unfavorable report.

Sincerely,

Melvin R. Thompson
Senior Vice President
Government Affairs and Public Policy