SB123 - FAV - MSEA Zwerling.pdf

Uploaded by: Zwerling, Samantha
Position: FAV

MARYLAND STATE EDUCATION ASSOCIATION

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Testimony SUPPORT of Senate Bill 123
Small Business Fairness Act

Senate Budget and Taxation Committee
January 21, 2021

Samantha Zwerling
Government Relations

The Maryland State Education Association supports SB 123, which would require specific corporations to compute Maryland taxable income using the method of combined reporting.

MSEA represents 75,000 educators and school employees who work in Maryland's public schools, teaching and preparing our 896,837 students for careers and 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. 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 Blueprint for Maryland's Future outlines 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.

Implementing the Kirwan Commission's recommendations and making up for the learning loss and socio-emotional effects of the pandemic will take considerable resources. Senate Bill 123 can be part of that funding solution.

MSEA urges a favorable report of Senate Bill 123.

SB_123_Combined_Reporting_2021.pdf
Uploaded by: Celentano, Matthew
Position: UNF

ACLI
Financial Security...for Life.

The League of Life and Health Insurers of Maryland

January 21, 2021

The Honorable Chair Guy Guzzone
Senate Budget & Taxation Committee
3 West
Miller Senate Office Building
Annapolis, MD 21401

RE: Senate Bill 123 – Small Business Fairness Act

Unfavorable

Dear Chair Guzzone:

We are writing on behalf of the American Council of Life Insurers ("ACLI") and the League of Life and Health Insurers of Maryland ("League"). ACLI and the League's member companies together provide over 95% of the life, disability, long term care insurance and annuities in Maryland and nationally. We ask for your opposition to unitary/combined reporting, or in the alternative, we ask for an exemption for insurance companies from unitary/combined reporting.

The enactment of unitary/combined reporting will subject insurers to income tax **in addition to** premium taxes, which they currently pay.

Insurers should be excluded because they are currently taxed under a completely different system than non-insurers. Insurers are taxed on gross premiums received rather than net income. **Premium taxes are paid whether the business is profitable or not.** Premium taxes are also paid by both Maryland domestic and foreign (domiciled in a state other than Maryland) insurers. Because of the heavy burden posed by the upfront premium tax, insurers are exempt from corporate income tax.

The benefits to the state of Maryland of the current state insurance company premium tax system are:

1. Stable source of revenue
2. Predictable source of revenue
3. Administrative ease and legal certainty
4. Credit certainty

Life insurers paid approximately $111,000,000 in premium taxes in 2015. Obviously, health insurers and property casualty insurers paid millions of additional dollars in 2015. If life insurers had paid taxes based upon the regular business tax, they would have paid $75 million in 2015 or $36 million less than what was paid through premium taxes.

American Council of Life Insurers
101 Constitution Avenue, NW, Washington, DC 20001-2133
www.acli.com

The League of Life and Health Insurers of Maryland
15 School Street, Annapolis, MD 21401

Any attempt to combine income tax with a premium tax system presents numerous problems. Probably the most critical of these problems is the impact on the national retaliatory tax system which is unique to the insurance industry. That system exists because the federal McCarran-Ferguson Act, 15 U.S.C. Sec. 1011 et seq. excludes the business of insurance from Commerce Clause applicability. Moreover, insurers have a different accounting system (statutory vs. GAAP) than non-insurers.

The forced combination of insurance companies with affiliated non-insurance companies would, for both the insurance industry and the state raise critical tax policy concerns, add tax burdens and uncertainties, create myriad administrative and substantive issues, and almost certainly lead to litigation.

For these reasons ACLI and the League respectfully request an unfavorable report on the provisions concerning unitary combined reporting or that insurers be expressly excluded from the application of combined/unitary reporting.

Respectfully submitted,

Matthew Celentano
American Council of Life Insurers
The League of Life and Health Insurers of Maryland

cc: Members, Senate Budget & Taxation Committee

012121 COST Testimony in Opposition to S 123 (MUCR
Uploaded by: Do, Stephanie
Position: UNF

Stephanie T. Do
Senior Tax Counsel
(202) 484-5228
sdo@cost.org

January 19, 2021

Senate Budget and Taxation Committee
Maryland General Assembly

Re: In Opposition to Senate Bill 123, 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 123, 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 would: (1) create revenue volatility, (2) pick winners and losers among taxpayers, and (3) lead to additional litigation and administrative costs.

These harmful impacts will be forced upon some of the industries struggling the most by the economic volatility caused by the COVID-19 pandemic. Now is not the time to target retailers and food service establishments.

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 over 500 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. Many COST members engaged in retail and food service businesses have operations in Maryland that would be negatively impacted by this legislation.

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 the breadth of a state's 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 MUCR have experienced lower job growth than have states that use separate entity reporting. From 1982-2006, job growth was 6% lower in states with MUCR than states without 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 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

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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.

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 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; *i.e.*, it is <u>not</u> used in 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

[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.
[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.

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]

- **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—magnified by the negative economic consequences of the COVID-19 pandemic on these businesses.

COST urges members of the committee to please vote "no" on Senate Bill 123.

Respectfully,

Stephanie T. Do

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

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

SB 123 MACPA Written Testimony - UNFAVORABLE.pdf
Uploaded by: Halpern, MB
Position: UNF

January 19, 2021

The Honorable Guy Guzzone, Chair
Budget and Taxation Committee
Miller Senate Office Building
Annapolis, MD 21401

SB 123 Small Business Fairness Act - UNFAVORABLE

Dear Chair Guzzone and members of the Committee:

The Maryland Association of CPAs represents nearly 9,000 Certified Public Accountants throughout the state. These CPAs are in public practice, private industry, government, non-profit, and education.

A change to a combined reporting system would positively impact some businesses while negatively impacting others, as was demonstrated in data collected by the Office of the Comptroller. As CPAs, we represent businesses in both categories and, as such, do not take a position to support or oppose the adoption of combined reporting into Maryland law. Our focus is to ensure that any legislation enacted on this topic is both enforceable and unambiguous in order for our members to effectively compute this tax for clients.

Beyond interpreting the legislation, significant work is required of the Comptroller's office, and by taxpayers and tax preparers. The Comptroller's office must prepare draft regulations, allow for the required public comment period, and finalize the regulations. They must train their auditors and taxpayer-assistance staff, and develop administrative protocols such as forms, instructions, and computer programming changes, in order to accommodate the new filing method. Other states can be used as models, but these processes must still be made specific to Maryland.

Taxpayers and tax practitioners will need to become educated about the new statute and regulations and forms. Many will have to modify or acquire new tax preparation software. They will have to study the detailed operations of each and every corporation in order to make the fact-driven and interpretive determinations of which corporations are properly includable in a "unitary" combined reporting group, and they will have to collect data they never had to prepare before, for correct preparation of the income tax return.

Organizations such as MACPA will need to actively publicize the new requirements and provide educational programs to its members and their clients to help prepare for these new processes.

Maryland and many nearby states have always been separate entity states, so combined reporting is a new concept to many Maryland taxpayers and tax practitioners. Combined reporting will have implications for all corporate groups no matter the size of their businesses, and it is the small and medium sized corporations, of whom there are many with operations in Maryland, that will find the new administrative requirements most burdensome. Providing sufficient time for educating them would make for a better transition to the new law.

An implementation date applying to all taxable years beginning after December 31, 2021 as proposed in SB 123 is an inadequate timeframe to properly address all of these issues. A proper implementation timeline would allow at least two years of preparation time, i.e. tax years after December 31, 2023.

Combined reporting is a complex change for taxpayers, tax preparers, and the Comptroller's office. Without opposing or supporting the adoption of combined reporting, we respectfully observe that SB 123 does not provide the required time to effectively deal with the complex technical issues related to implementation We therefore recommend an unfavorable report for SB 123.

Thank you very much for the opportunity to offer these comments for your consideration.

Sincerely,

J. Thomas Hood, III, CPA CEO & Executive Director
cc: Nick Manis, Manis Canning & Associates

RestaurantAssociation_MelvinThompson_Oppose_SB123.

Uploaded by: Thompson, Melvin

Position: UNF

SENATE BILL 123

Small Business Fairness Act

January 21, 2021

Position: Oppose

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

The *Restaurant Association of Maryland* opposes Senate Bill 123, 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

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

Restaurant Association of Maryland 6301 Hillside Ct Columbia, MD 21046 410.290.6800 FAX 410.290.6882