SB361_CarriedInterest_FAV.pdf
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Position: FAV

A sustainable, just, and prosperous economic future for all Marylanders

Testimony in Support of SB 361
Income Tax - Carried Interest - Additional Tax
Senate Budget and Taxation Committee

FAVORABLE

February 9, 2022

Dear Chairman Guzzone and Members of the Budget and Taxation Committee:

On behalf of Strong Future Maryland, we write in support of SB 361. Strong Future Maryland works to advance bold, progressive policy changes to address systemic inequality and promote a sustainable, just and prosperous economic future for all Marylanders. SFM supports fixing our tax system to ensure that large corporations and wealthy individuals are paying their fair share for the public services we all rely on.

SB 361 will close the carried interest loophole that allows wealthy investment fund managers to pay a special, low tax rate on their income.

Like thousands of other Maryland workers, from restaurant servers to salespeople, private equity and hedge fund managers are paid partly on the basis of their performance. Unlike other workers, wealthy fund managers pay a special, low tax rate on this income — the capital gains rate, rather the standard income tax rate. This special treatment violates core principles of effective tax policy by taxing similar activities at different rates and shifting tax responsibility away from those who can best afford to pay.

SB 361 would offset this special tax break that powerful special interests convinced Congress to enact and ask wealthy fund managers to pay their fair share in Maryland. It would also increase revenue by more than $40 million annually. This is new revenue that could significantly contribute to the needs of families and small businesses recovering from the pandemic and support core public services in the long term.

For a strong recovery from COVID-19 and to support long-term investments that allow all Maryland families and communities to thrive, it's time to reform Maryland's tax code to make it more effective and more equitable. **<u>Therefore, we urge a favorable report on SB 361.</u>**

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SB0361_Carried_Interest_MLC_FAV.pdf
Uploaded by: Cecilia Plante
Position: FAV

MARYLAND LEGISLATIVE COALITION

TESTIMONY FOR SB0361
INCOME TAX – CARRIED INTEREST – ADDITIONAL TAX

Bill Sponsor: Senator Pinsky
Committee: Budget and Tax
Organization Submitting: Maryland Legislative Coalition
Person Submitting: Cecilia Plante, co-chair
Position: FAVORABLE

I am submitting this testimony in favor of SB0361 on behalf of the Maryland Legislative Coalition. The Maryland Legislative Coalition is an association of individuals and grassroots groups with members in every district in the state with well over 30,000 members.

We pay people to manage our money. They need to make a living – we understand that. But everyone should pay their fair share of taxes. Why should hedge fund and private equity managers pay less taxes than everyone else?

Everyone should pay their fair share. Everyone. We need to get rid of the loopholes for the rich.

We support this bill and recommend a **FAVORABLE** report in committee.

SB 361 Carrie Interest --AFSCME.pdf
Uploaded by: Cindy Smalls
Position: FAV

AFSCME 3
190 West Ostend St., #201
Baltimore, MD 21230
Phone: 410.547.1515
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Patrick Moran - President

Testimony
SB 361 Income Tax – Carried Interested – Additional Tax
Budget &Taxation Committee
February 9, 2022
Support

AFSCME Council 3 which representing 30,000 state and Higher Education employees supports SB 361.

Senate Bill 361 closes a tax loophole that currently allows investment fund managers to pay the lower capital gains tax rate on the portion of their compensation that is based on the success of the funds that they manage. This is the only industry that receives such tax benefits for its employees. Senate Bill 361 would close this loophole by allowing the state to collect revenue from Maryland taxpayers that would go to the federal government if it accurately classified carried interest as ordinary income.

The historical reasoning behind the lower capital gains tax rate was that individuals making investments in a new business, a new building, or the stock market are putting their own money at risk. Managers of private equity and hedge funds aren't putting their own money at risk. They are simply paid a larger or smaller amount for their work, depending on how well the fund performs.

There are many other types of industries where someone's pay is based at least in part on their performance, such as restaurant servers, sales people working on commission, and even other types of finance professionals. Those in all other industries pay the regular personal income tax rate on their salaries, bonuses, and commission.

Closing the carried interest loophole would generate about $40 million in revenue per year that could support new investments in state agencies, Maryland schools or other community priorities. Such spending would create jobs and boost consumer demand today, as well as lay the groundwork for a strong economy in the long run.

The carried interest loophole allows wealthy investment managers to pay a lower tax rate on their income than the majority of workers, weakening the economy and costing billions of dollars in revenue nationwide each year. If we ask state and Higher Education employees pay their fair share in tax for earned work. It's time to ask fund managers to pay their fair share by passing Senate Bill 361

For these reasons, we urge you to a favorable report on Senate Bill 361.

SB 361 Carried Interest.pdf
Uploaded by: Denise Riley
Position: FAV

A Union of Professionals
AFT-Maryland

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Marietta English
PRESIDENT

Kenya Campbell
SECRETARY-TREASURER

Written Testimony before the Maryland Senate Budget & Taxation Committee
SB 361 - Income Tax - Carried Interest - Additional Tax
February 9, 2022

SUPPORT

Chair Guzzone and members of the Committee. On behalf of AFT-Maryland's more than 20,000 state, municipal, and public education workers, we ask for a favorable report on SB 361.

As the statewide organization for the Baltimore Teachers Union (BTU), as well as unions representing thousands of state employees, AFT-Maryland supports bills that will help bring badly needed revenues into the state. With the increased funds, our state will in a better position to compete economically, provide a world-class public education system and meet the needs of our residents who rely on state services.

The proposed public school reform policies introduced by the Kirwan Commission and in the Blueprint for Maryland's Future, found that significant new resources must be committed to education to build our state's economy.

In order to accomplish this, all citizens and businesses must be willing to pay their fair share of taxes. Currently, the burden lays heavily on the middle class and lower income residents who pay higher taxes per capita than the wealthy. It is time for capital gains to be taxed fairly so the wealthy and businesses begin to pay their fair share.

It is for these reasons that we ask the committee for a favorable report to SB 361. Thank you.

Kenya Campbell
President

SB 361 - Carried Interest - Additional Tax.pdf
Uploaded by: Donna Edwards
Position: FAV

MARYLAND STATE & D.C. AFL-CIO

AFFILIATED WITH NATIONAL AFL-CIO

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Secretary-Treasurer
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SB 361 – Income Tax – Carried Interest – Additional Tax
Senate Budget and Taxation Committee
February 9, 2022

SUPPORT

Donna S. Edwards
President
Maryland State and DC AFL-CIO

Chairman and members of the Committee, thank you for the opportunity to provide testimony in support of SB 361 – Income Tax – Carried Interest – Additional Tax. My name is Donna S. Edwards, and I am the President of the Maryland State and DC AFL-CIO. On behalf of the 340,000 union members in the state of Maryland, I offer the following comments.

Hedge fund and investment managers pay a lower tax rate than restaurant servers, state and county workers, nurses, bus operators, teachers, and everyone else in Maryland that works for a living. Carried interest income is taxed much lower than income derived from wages. This special treatment for those who make money by investing the income of others undermines the value of all our labor.

SB 361 corrects this inequality by applying a 17% state income surtax on the pass-through income that is attributable to investment management services provided in Maryland. Last year it was estimated that the State would gain an additional $44.8 million per year in revenue, providing much needed resources to help fund priorities for our children, families, and communities.

Our tax laws reflect our values. The dignity of all workers should be honored and valued. Investment fund managers need to pay their fair share.

We urge a favorable report on SB 361.

Erica Payne MD carried interest testimony 2022.pdf
Uploaded by: Erica Payne
Position: FAV

Dear Chair Guzzone and other members of the Budget and Taxation Committee,

My name is Erica Payne. I am the founder and president of the Patriotic Millionaires, a nationwide network of high net worth Americans - including several in Maryland - who share a profound concern about economic inequality in our country, which has reached historic and destabilizing levels.

As their representative and a Maryland resident myself with an MBA from the Wharton Business School, I am here today to support SB361, a critical piece of legislation that would close the carried interest loophole on a state level, and in the process would raise tens of millions of dollars a year in much-needed revenue for the state of Maryland without costing 99.9% of taxpayers a dime.

The carried interest loophole is a loophole in the federal tax code that allows private equity fund managers, some of the wealthiest people in the world who often earn millions of dollars a year, to incorrectly classify their earnings as capital gains rather than ordinary income.

In the process they cut their tax bill nearly in half, paying the capital gains rate, just 20%, rather than the top income tax rate of 37%. This leaves them paying a lower tax rate than their secretaries or the janitors who clean their offices, and in fact a lower top tax rate than anyone making more than $40,000 a year in income.

This special tax break is entirely undeserved. The income that's classified as carried interest is just a fee that fund managers earn from their investors in exchange for managing their money. In any other industry this type of income would be taxed as normal income, but thanks to this loophole it's taxed at the lower capital gains rate.

The federal capital gains tax rate is lower than the income tax rate because the government believes that by incentivizing investment and risk-taking, it will spur growth. But fund managers invest no money of their own and take on no risks, they just manage other people's investments. Their earnings meet none of the standard criteria to be classified as capital gains, and should not be taxed as such.

Private equity managers claim that while they might not invest money, they invest their time and expertise through something they call "sweat equity," which should qualify their earnings as capital gains. But the investment of time and expertise in exchange for payment is quite literally the definition of employment. Every person who has ever worked a day in their life has traded their time and expertise in exchange for money.

This argument is clearly nonsense, yet it's the basis for the entire premise of giving carried interest special treatment.

This loophole is so ridiculous that even Donald Trump famously declared that people using the carried interest loophole were "getting away with murder." But when it came time for Republicans to rewrite the federal tax code when they passed the Tax Cuts and Jobs Act in 2017, they almost completely ignored the carried interest loophole. By closing this loophole on a state level, Maryland has a chance here to show the nation, and legislators in the nearly dozen other states that are considering similar legislation, that better things are possible.

And don't worry about whether or not millionaires are going to leave the state when you tax them - study after study shows that rich people don't actually move to avoid taxes. In fact, New York significantly raised taxes on millionaires a few years ago, but today the number of millionaires in the state is higher than it's ever been.

This should be a no-brainer. If we can raise tens of millions of dollars for housing, healthcare, education, or public safety by requiring a few hundred millionaires and billionaires to pay the tax rate they should have been paying all along, then we should do it.

Hi, my name is Erica Payne. I am the founder and president of the Patriotic Millionaires, a nationwide network of high net worth Americans - including several in Maryland - who share a profound concern about economic inequality in our country, which has reached historic and destabilizing levels.

As their representative and a Maryland resident myself with an MBA from Wharton Business School, I am here today to support HB439, a critical piece of legislation that would close the carried interest loophole on a state level, and in the process would raise as much as $45 million a year in revenue for the state of Maryland.

The carried interest loophole is a loophole in the federal tax code that allows private equity fund managers, some of the wealthiest people in the world who often earn millions of dollars a year, to incorrectly classify their earnings as capital gains rather than income.

In the process they cut their tax bill nearly in half, paying the capital gains rate, just 20%, rather than the top income tax rate of 37%. This leaves them paying a lower tax rate than their secretaries or the janitors who clean their offices, and in fact a lower top tax rate than anyone making more than $40,000 a year in income.

This special tax break is entirely undeserved. The basic way a private equity fund works is that a group of people give their money to the managers of a fund, the fund managers manage that money for their investors, then investors pay the managers a fee that's a percentage of the total value of the fund and a percentage of the fund's profits. That percentage of the fund's profits is called carried interest, and despite it being a fee for a service, which is taxed as income in virtually every other industry, it's instead taxed under the lower capital gains rate.

The federal capital gains tax rate is lower than the income tax rate because the government believes that by incentivizing investment and risk-taking, it will spur growth. But fund managers invest no money of their own and take on no risks, they just manage other people's investments. Their earnings meet none of the standard criteria to be classified as capital gains, and should not be taxed as such.

Private equity managers claim that while they might not invest money, they invest their time and expertise through something they call "sweat equity," which should qualify their earnings as capital gains. But the investment of time and expertise in exchange for payment is quite literally the definition of employment. Every person who has ever worked a day in their life, from the most brilliant scientist all the way down to a teenager mowing lawns, has traded their time and expertise in exchange for money. This argument is clearly nonsense, yet it’s the basis for the entire premise of giving carried interest special treatment.

This loophole is so ridiculous that even Donald Trump famously declared that people using the carried interest loophole were “getting away with murder.” But when it came time for Republicans to rewrite the federal tax code when they passed the Tax Cuts and Jobs Act in 2017, they almost completely ignored the carried interest loophole.

By closing this loophole on a state level, Maryland has a chance here to show the nation that better things are possible. Legislators in nearly a dozen other states are considering similar legislation, but none have pulled the trigger yet. By closing this loophole - passing a piece of legislation that on a very basic level simply corrects a mischaracterization of income at the federal level – we could kick off a nationwide trend, and in the process generate as much as $45 million a year in revenue.

And don’t worry about whether or not millionaires are going to leave the state when you tax them - study after study shows that rich people don’t actually move to avoid taxes. In fact, New York significantly raised taxes on millionaires a few years ago, but today the number of millionaires in the state is higher than it’s ever been.

This should be a no-brainer. If we can raise $45 million dollars for housing, healthcare, education, or public safety by requiring a few hundred millionaires and billionaires to pay the tax rate they should have been paying all along, then we should do it.

SB 361 to B&T Support --- Carried Interest .pdf

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Position: FAV

MARYLAND NONPROFITS
marylandnonprofits.org

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February 9, 2022

Testimony on Senate Bill 361
Income Tax - Carried Interest - Additional Tax
Senate Budget and Taxation Committee

Position: Favorable

Maryland Nonprofits is a statewide association of more than 1300 nonprofit organizations and institutions. As a member of the Fair Funding Coalition we strongly urge you to support Senate Bill 361 to make our system of business taxation more equitable.

The Maryland Fair Funding Coalition supports proposals that eliminate loopholes and tax breaks that benefit special interests and fix our upside-down tax code, which allows the wealthiest individuals to pay the smallest share of their income in state and local taxes. Fixing our tax system will ensure that large corporations and wealthy individuals are paying their fair share for the public services we all rely on.

Senate Bill 361 will close the 'carried interest' loophole that allows wealthy investment fund managers to pay a special, low tax rate on their income. Like thousands of other Maryland workers, from restaurant servers to salespeople, private equity and hedge fund managers are paid partly on the basis of their performance. Unlike other workers, wealthy fund managers pay a special, low tax rate on this income — **the capital gains rate**, rather the standard income tax rate. This special treatment violates core principles of effective tax policy by taxing similar activities at different rates and shifting tax responsibility away from those who can best afford to pay.

SB 361 would offset this special tax break that powerful special interests convinced Congress to enact and ask wealthy fund managers to pay their fair share in Maryland. It would also increase revenue by more than $40 million annually. This is new revenue that could significantly contribute to the needs of families and small businesses recovering from the pandemic and support core public services in the long term.

For a strong recovery from COVID-19 and to support long-term investments that allow all Maryland families and communities to thrive, it's time to reform Maryland's tax code to make it more effective and more equitable. Therefore, we urge a favorable report on SB 361.

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SB361_MD Center on Economic Policy_FAV.pdf
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Position: FAV

It’s Time for Wealthy Investment Managers to Pay their Fair Share

Position Statement Supporting Senate Bill 361

Given before the Senate Budget and Taxation Committee

Like thousands of other Maryland workers, from authors to restaurant servers, private equity and hedge fund managers are paid partly on the basis of their performance. Unlike other workers, wealthy fund managers pay a special, low tax rate on this income. This special treatment violates core principles of effective tax policy by taxing similar activities at different rates, shifting tax responsibility away from those who can best afford to pay, and eliminating revenue that could be used to support vital investments in public health, schools, and other priorities. The Maryland Center on Economic Policy supports Senate Bill 361, which would close this loophole and ask wealthy fund managers to pay their fair share.

Investors in private equity and hedge funds see better returns when the funds perform well and worse returns when the funds perform poorly. The managers of these funds do too, thanks to carried interest – the share of profits they receive as performance pay. Unlike investors, though, fund managers do not put their own money at risk. They are simply paid a larger or smaller amount for their work, depending on how well the fund performs.

However, the federal government taxes carried interest at the capital gains rate, which is ordinarily reserved for investors who risk their own money. This allows many highly paid investment managers to pay much less in taxes than other workers.[i] With a historically high share of income going to those at the very top, it does not make sense to give special tax breaks to wealthy finance professionals. Senate Bill 361 would close this loophole by allowing the state to collect revenue from Maryland taxpayers that would go to the federal government if it accurately classified carried interest as ordinary income.

The special treatment given to private equity and hedge fund managers weakens the economy by creating an inflated incentive to work in these industries. We do not give special tax breaks to doctors, engineers, or other highly skilled professionals, despite the essential work they do. Even other finance professionals pay ordinary income tax rates on bonuses and other types of performance pay, not the lower capital gains rate. This is why experts across the political spectrum have recommended closing the carried interest loophole.[ii]

Closing this loophole would also bring in needed revenue, strengthening the state’s ability to make much-needed improvements in priorities like public health, schools, and child care. Based on past estimates by the Department of Legislative Services, Senate Bill 361 would likely raise $40 million or more each year. Taxing wealthy investment managers accurately would mean more money for public health, Maryland schools, and health care. It is also likely to increase economic activity in Maryland, as money invested in public services immediately flows back into the economy. Wealthy fund managers, on the other hand, are more likely to sit on extra income that they have few uses for.[iii]

While many beneficiaries of the carried interest loophole are opposed to closing it, the arguments they offer do not hold water:

- Fund managers are not unique in receiving pay that varies over time and therefore carries risk. Restaurant servers who work for tips, authors who earn royalties, and even other finance professionals who are paid bonuses all pay income taxes on their performance pay – not a special capital gains rate.
- Funds cannot easily pass taxes on to investors by charging higher fees. As the high fees associated with alternative investments have come under increasing scrutiny in recent years, the large institutional investors that dominate the market have become less willing to pay large sums without a clear benefit.[iv]
- There is no reason to expect funds' performance to suffer because investment managers are taxed accurately. Managers will still be paid largely on the basis of performance, and market competition will still direct business to the highest-performing funds.
- Senate Bill 361 includes a provision that would allow the legislature to cancel the corrective tax it creates if the federal government closes the loophole, so there is no risk of taxing financial services twice in the future.
- While some investment managers would likely look for ways to avoid paying the corrective tax, this is a good reason to ensure the law is enforced appropriately – not a reason to exempt them from their responsibility to pay taxes.

The carried interest loophole allows wealthy investment managers to pay a lower tax rate on their income than the majority of workers, weakening the economy and costing billions of dollars in revenue nationwide each year. It's time to ask fund managers to pay their fair share by passing Senate Bill 361.

For these reasons, the Maryland Center on Economic Policy respectfully asks that the Senate Budget and Taxation Committee make a favorable report on Senate Bill 361.

Equity Impact Analysis: Senate Bill 361

Bill summary

Senate Bill 361 closes a tax loophole that currently allows investment fund managers to pay the special, lower capital gains tax rate on the portion of their compensation that is based on the success of the funds that they manage. This is the only industry that receives such tax benefits for its employees. Senate Bill 361 would close this loophole by allowing the state to collect revenue from Maryland taxpayers that would go to the federal government if it accurately classified carried interest as ordinary income.

Background

The historical reasoning behind the lower capital gains tax rate was that individuals making investments in a new business, a new building, or the stock market are putting their own money at risk. Managers of private equity and hedge funds are not putting their own money at risk. They are simply paid a larger or smaller amount for their work, depending on how well the fund performs.

There are many other types of industries where someone's pay is based at least in part on their performance, such as restaurant servers (who, analogously to fund managers, are often paid based on a "$3.63 and 20%" rule), sales people working on commission, and even other types of finance professionals. Those in all other industries pay the regular personal income tax rate on their salaries, bonuses, and commission.

Closing the carried interest loophole could generate about $40 million in revenue per year that could support new investments in Maryland schools or other community priorities. Such spending would create jobs and boost consumer demand today, as well as lay the groundwork for a strong economy in the long run.

Equity Implications

- More than 60 percent of capital gains income in Maryland goes to the wealthiest 1 percent of tax filers, a group in which private equity and hedge fund managers are significantly overrepresented.[v] Providing special tax treatment for their income will predominately benefit the small minority of white families who hold nearly two-thirds of all household wealth nationwide.
- Closing the carried interest loophole would generate public resources that could be invested in things like public health, world-class schools, and sufficient child care assistance. Investing in these basics strengthens our economy and can dismantle the economic barriers that too often hold back Marylanders of color.

Impact

Senate Bill 361 would likely **improve racial and economic equity** in Maryland.

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[i] For example, Mitt Romney, a private equity financier, famously paid only 14 percent of his $22 million income in federal taxes in 2010. Lori Montgomery, Jia Lynn Yang, and Philip Rucker, "Mitt Romney Releases Tax Returns," *The Washington Post*, January 24, 2012, https://www.washingtonpost.com/politics/2012/01/23/gIQAj5bUMQ_story.html?utm_term=.6e61ef350161.

[ii] For example, conservative economist Greg Mankiw has written against the carried interest loophole. N. Gregory Mankiw, "The Taxation of Carried Interest," *Greg Mankiw's Blog*, 2007, http://gregmankiw.blogspot.com/2007/07/taxation-of-carried-interest.html.

[iii] During a recession, the households with the most built-up assets spend only one-tenth as much of each additional dollar of income as families living paycheck to paycheck, according to research out of Johns Hopkins University.
Christopher Carroll, Jiri Slacalek, Kiichi Tokuoka, and Matthew White, "The Distribution of Wealth and the Marginal Propensity to Consume," *Quantitative Economics 8*, 2017, https://onlinelibrary.wiley.com/doi/epdf/10.3982/QE694

[iv] Suzanne Barlyn and Svea Herbst-Bayliss, "Mismanagement Cost NY Pension $3.8 Billion over Eight Years: Regulator," *Reuters*, October 17, 2016, http://www.reuters.com/article/us-new-york-pensions-idUSKBN12H210.

[v] While the small number of people in this group limits the precision of survey-based estimates, data from the 2013–2017 indicate that as many as one in eight Maryland financial managers in investment industries are in the state's wealthiest 1 percent of households and nearly one in four are in the wealthiest 1 percent nationwide.

SB361_MD Fair Funding Coalition_FAV.pdf
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Position: FAV

MARYLAND
FAIR FUNDING
COALITION

February 9, 2022

Testimony in Support of Senate Bill 361
Senate Budget and Taxation Committee

Income Tax - Carried Interest - Additional Tax

The Maryland Fair Funding Coalition is a coalition of more than 30 organizations across the state that are committed to policies that make our tax system more equitable and allow the state to raise sufficient revenue to sustain the essential public services Maryland families and communities need to thrive.

The coalition supports proposals that eliminate loopholes and tax breaks that benefit special interests and fix our upside-down tax code, which allows the wealthiest individuals to pay the smallest share of their income in state and local taxes. Fixing our tax system will ensure that large corporations and wealthy individuals are paying their fair share for the public services we all rely on.

Our coalition supports SB 361, **which will close the carried interest loophole that allows wealthy investment fund managers to pay a special, low tax rate on their income.**

Like thousands of other Maryland workers, from restaurant servers to salespeople, private equity and hedge fund managers are paid partly on the basis of their performance. Unlike other workers, wealthy fund managers pay a special, low tax rate on this income — the capital gains rate, rather the standard income tax rate. This special treatment violates core principles of effective tax policy by taxing similar activities at different rates and shifting tax responsibility away from those who can best afford to pay.

SB 361 would offset this special tax break that powerful special interests convinced Congress to enact and ask wealthy fund managers to pay their fair share in Maryland. It would also increase revenue by more than $40 million annually. This is new revenue that could significantly contribute to the needs of families and small businesses recovering from the pandemic and support core public services in the long term.

For a strong recovery from COVID-19 and to support long-term investments that allow all Maryland families and communities to thrive, it's time to reform Maryland's tax code to make it more effective and more equitable. **Therefore, we urge a favorable report on SB 361.**

SB361_MSEA_Zwerling_FAV.pdf
Uploaded by: Samantha Zwerling
Position: FAV

MARYLAND STATE
EDUCATION
ASSOCIATION

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Testimony in SUPPORT of Senate Bill 361
Income Tax – Carried Interest – Additional Tax

Senate Budget and Taxation Committee
February 9, 2022

Samantha Zwerling
Government Relations

The Maryland State Education Association supports Senate Bill 361, which closes a tax loophole for hedge fund managers.

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 Blueprint for Maryland's Future with fidelity and making up for the learning loss, and social-emotional and behavioral health impacts of the COVID-19 pandemic will take considerable resources. Thanks to the tough decisions this committee has made in the past, the Blueprint's state contributions are funded into FY27. The estimated $50 million per year generated from the implementation of this bill could help fund the Blueprint in the out-years and ensure Maryland's public schools meet our expectations. SB 361 is part of that funding solution.

MSEA urges a Favorable Report on Senate Bill 361.

SB 361_MDCC_Income Tax-Carried Interest-Additional

Uploaded by: Andrew Griffin

Position: UNF

MARYLAND
Chamber of Commerce

LEGISLATIVE POSITION:
Unfavorable
Senate Bill 361
Income Tax—Carried Interest—Additional Tax
Senate Budget & Taxation Committee

Wednesday, February 9, 2022

Dear Chairman Guzzone and Members of the Committee:

Founded in 1968, the Maryland Chamber of Commerce is the leading voice for business in Maryland. We are a statewide coalition of more than 5,500 members and federated partners, and we work to develop and promote strong public policy that ensures sustained economic recovery and subsequent growth for Maryland businesses, employees, and families. Part of that work includes evaluating, promoting, and maintaining the best approaches for tax policy for the state.

What has come to be known as the "carried interest" issue is a U.S. federal income tax matter, not a Maryland state tax matter. All types of income are taxed at the same tax rate in Maryland and imposing an additional State tax to make up for a federal tax difference between the capital gains tax rate versus other income tax rate will result in more than tripling the Maryland tax on this income. This is poor state tax policy.

Carried interest is a financial term for the profit certain partners and limited liability company (LLC) members receive as a product of their invested capital or for the interest in the partnership or LLC received by these partners or members in connection with investment management activities they perform. As such, it is treated under the Internal Revenue Code as an investment taxable under the capital gains tax, and under Maryland's tax statute as taxable income.

The federal tax code taxes capital gains separately because they are not salary. Rather, they are investments that can make or lose money. Because of that risk, they are taxed differently, including at a different tax rate. The way in which the tax is currently structured provides an incentive for individuals to invest. This investment helps to start businesses, advance technology and innovation and create the tools needed to help economic development overall.

Importantly, this income is already subject to full income tax in Maryland with respect to residents and nonresident members of pass-through entities. The issue is not one involving Maryland income tax, but one involving the difference in tax rates for U.S. income tax, i.e. the rates for "ordinary income" versus "capital gain." The bill's proposed additional tax rate is even obvious in its derivation from the federal tax rates—rates in existence prior to recent federal tax changes. Ordinary income was taxed at a high of 39.6% and capital gains at 20%. There is no such different tax rate structure in Maryland—both ordinary income and capital gains are taxed at the same rate.

If passed, this bill would impose an exorbitant increase in tax, a 17% surtax, on income that is already taxed at Maryland's full state-plus-local tax rate. Maryland's income tax rates are already among the highest in the nation. "Carried interest" is a federal issue that is best addressed by the United States Congress under the Internal Revenue Code. It is not a Maryland tax issue.

Finally, businesses continue to weather an anemic economic recovery. COVID-19 has had a tremendous, detrimental impact on Maryland's economy and there is plenty of reason to remain cautious and concerned about its lasting implications. Maryland businesses continue to struggle, and a period of economic turbulance and future uncertainty is not the time to implement tax measures that stand to negatively impact Maryland job creators.

For these reasons, the Maryland Chamber of Commerce respectfully requests an **unfavorable report** on **SB 360.**

SB0361 -- Income Tax - Carried Interest - Addition
Uploaded by: Brian Levine
Position: UNF

Senate Bill 361 -- *Income Tax - Carried Interest - Additional Tax*
Senate Budget and Taxation Committee
February 9, 2022
Oppose

The Montgomery County Chamber of Commerce (MCCC), the voice of business in Metro Maryland, opposes Senate Bill 361 -- *Income Tax - Carried Interest - Additional Tax.* Senate Bill 361 imposes a 17% State income tax on the distributive share or pro-rata share of a pass-through entity's taxable income that is attributable to investment management services provided in Maryland.

This legislation represents a discriminatory tax increase that will drive segments of the financial services industry out of Maryland. This legislation creates a punitive tax that puts private equity funds, venture capital funds, hedge funds, and other investors in Maryland at a competitive disadvantage with those in other states. MCCC is concerned that creating a unique tax structure for carried interest will harm Maryland's business climate and harm an industry important to the State's economy.

MCCC asserts that Senate Bill 361 seeks to remedy a tax issue that should be the exclusive purview of the U.S. Congress. Maryland should not institute its own system of taxing carried interest, but instead push for action on the federal level. Federal action will ensure that Maryland is on a level playing field with surrounding and competitor states.

Additionally, during the COVID-19 pandemic, segments of Maryland's economy continue to struggle, and potential employment and economic volatility remains high. Significant tax policy changes have the potential to cause economic disruption that the State of Maryland cannot afford during this volatile period. Policymakers must ensure they take a cautious approach with Maryland's economy and labor market.

MCCC continues to support the creation of a commission to analyze and make recommendations as to how to make Maryland's tax structure more fair, equitable, and economically competitive. This more comprehensive and strategic approach should be adopted, rather than a piecemeal approach to tax policy.

For these reasons, the Montgomery County Chamber of Commerce opposes Senate Bill 361 and respectfully requests an unfavorable report.

The Montgomery County Chamber of Commerce, on behalf of our nearly 500 members, advocates for growth in business opportunities, strategic investment in infrastructure, and balanced tax reform to advance Metro Maryland as a regional, national, and global location for business success. Established in 1959, MCCC is an independent non-profit membership organization and a proud Montgomery County Green Certified Business.

Brian Levine / Vice President of Government Affairs
Montgomery County Chamber of Commerce
51 Monroe Street / Suite 1800
Rockville, Maryland 20850
301-738-0015 / www.mcccmd.com

SIFMA SB 361 Comment Carried Interest.pdf
Uploaded by: Chris DiPietro
Position: UNF

sifma®

Invested in America

February 7, 2022

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

RE: SB 361 – Income Tax – Carried Interest – Additional Tax – Unfavorable

Dear Chair Guzzone and Members of the Senate Budget and Taxation Committee:

The Securities Industry and Financial Markets Association ("SIFMA")[1] is a national trade association which brings together the shared interests of hundreds of broker-dealers, banks and asset managers. We appreciate the opportunity to provide comments on SB 361, legislation which would impose an additional 17% tax on "Maryland taxable income that is attributable to investment management services."

It is our understanding that this bill is intended to close a perceived tax gap related to the taxable income of certain investment fund managers at the federal level, known as "carried interest." While we have reservations about the policy of attempting to remedy perceived gaps in federal tax law at the state level, our primary concern is that the bill, in its current form, is far broader than necessary to achieve its intended purpose, and it would harm a broad class of employees of financial services firms who do not receive carried interest or benefit from preferential rates.

As you carry out discussions over this bill, we respectfully request that you consider the following adverse consequences of SB 361:

- Extends beyond private equity funds to employees who receive company stock as part of their compensation.

  The 17% surtax appears to apply to individual employees who have an equity interest in a business, including a partnership, an S corporation, or any other entities that are providing investment, acquisition or financing advice. This broad definition appears to fit many broker-dealer, asset manager and investor advisor employees who receive company stock as part of an employee compensation plan. Employees in many industries receive company stock. It seems unnecessarily punitive to penalize financial services employees with an unprecedented 17% surtax when employees in other industries that receive company stock remain eligible for retirement incentives that often include lower rates on long term capital gains.

[1] SIFMA is the leading trade association for broker-dealers, investment banks and asset managers operating in the U.S. and global capital markets. On behalf of our industry's nearly 1 million employees, we advocate for legislation, regulation and business policy, affecting retail and institutional investors, equity and fixed income markets and related products and services. We serve as an industry coordinating body to promote fair and orderly markets, informed regulatory compliance, and efficient market operations and resiliency. We also provide a forum for industry policy and professional development. SIFMA, with offices in New York and Washington, D.C., is the U.S. regional member of the Global Financial Markets Association (GFMA). For more information, visit http://www.sifma.org.

Moreover, the surtax seems to apply even when such employees pay ordinary income rates, such as when an employee sells company stock held for less than one year or receives non-qualified dividends. The bill should, at the very least, contain an exclusion for interests held in a public company, and an exclusion for employees of a publicly traded company. In addition, we think you should consider a *de minimis* threshold of ownership and you should exempt ownership interests held through a qualified plan, such as a 401(k) plan, so that employees who own small equity interests in a much larger company are not subject to punitive taxation on their retirement assets.

- Applies to a broad class of employees who support investment managers.

  SB 361 broadly defines investment services to include "any activity in support of" any investment management service. We are concerned that this language could be interpreted to include not only highly paid investment managers but their assistants and many other categories of employees, such as human resources personnel, who indirectly support an investment manager and who own a small stake in a financial services company as part of an employee stock compensation plan. So interpreted, the bill would unfairly prevent these employees from benefiting from the retirement incentives that employees in every other industry enjoy. Maryland investment management companies would also lose an important means to align the incentives of their employees and shareholders.

- Improperly extends to proprietary trading firms, family offices and other businesses.

  The definition of "investment management services" would also seem to apply to proprietary trading firms, family offices and other businesses that are investing and managing assets using only the capital provided by their owners. This goes far beyond perceived gaps in federal tax law. Employees of these businesses should be exempt.

- Fails to consider that not all taxable income from carried interest is taxed at a preferential rate at the federal level.

  Similarly, SB 361 would, in some instances, result in over-taxation. The legislation does not draw a distinction between long-term capital gains and other types of income that are taxed at ordinary rates. This could result in individuals paying the higher federal tax rate and also paying the 17% surtax. The legislation should be modified to make clear that any additional tax is imposed only when the taxpayer's income qualifies as long-term capital for U.S. federal income tax purposes.

- Discourages investment management firms from locating in Maryland.

  The 17% surtax is likely to discourage investment management firms from locating in Maryland. Those that remain in the State would likely have a harder time attracting and retaining employees. This runs counter to the State's interest in promoting economic development and job growth.

- Make it harder for Maryland residents and institutional investors to invest.

  The additional tax on investment management services could also make it more difficult for Maryland pension funds and other businesses to find local asset managers. At a minimum, the increased costs of investing resulting from the surtax is likely to be shared at least in part by the business' clients.

In short, we believe that SB 361 is an overly broad "fix" for a narrow concern that would impose a significant burden on Maryland residents and the firms that employ them. We would encourage you to not move forward with the legislation.

We appreciate your willingness to consider our concerns. Please do not hesitate to contact me at 212-313-1233 or nlancia@sifma.org with any questions.

Sincerely,

Nancy Lancia

Managing Director
State Government Affairs
SIFMA

MD_TechNet_Carried Interest SB 361_2.9.22.pdf
Uploaded by: Christopher Gilrein
Position: UNF

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www.technet.org | @TechNetNE

February 9, 2022

The Honorable Senator Guy Guzzone, Chair
Senate Budget and Taxation Committee
Maryland General Assembly
Annapolis, Maryland 21401

Re: TechNet Opposition to SB 361 – Carried Interest Additional Tax

Dear Char Guzzone and members of the Committee:

I write to respectfully express TechNet's strong opposition to SB 361, which would levy an additional 17 percent surtax on any income realized by Maryland-based venture capital (VCs) on startup investment in the State of Maryland.

TechNet is the national, bipartisan network of technology CEOs and senior executives that promotes the growth of the innovation economy by advocating a targeted policy agenda at the federal and 50-state level. TechNet's diverse membership includes dynamic American businesses ranging from startups to the most iconic companies on the planet and represents over four million employees and countless customers in the fields of information technology, e-commerce, the sharing and gig economies, advanced energy, cybersecurity, venture capital, and finance. TechNet has offices in Austin, Boston, Chicago, Denver, Olympia, Sacramento, San Francisco, Silicon Valley, and Washington, D.C.

Despite the pandemic, Maryland saw a staggering 32% increase in new business applications – the largest number of startup applications in the state since the government began tracking the data. During the same time period, VC investment in Maryland companies shattered records, surpassing the $1.26 billion raised in all of 2020 in just three quarters of 2021. This is not coincidental. Venture capital is the catalyst that helps to turn great ideas into innovative new companies.

It is important to note that the tax applied under SB 361 would be in addition to all other state and local taxes VCs already pay, including the tax on capital gains, which includes carried interest. This is particularly punitive as the existing capital gains rate is the same as the corporate interest rate. If SB 361 were to be enacted, VC activity would be taxed at a rate 400 percent higher than other income in the state.

Such a major tax burden would depress the appetite for the long-term and high-risk investment that is necessary to fuel new company formation. With the anticipated reduction in venture fund formation, investment, and new company registration, such a tax may likely be a net loss for the state in terms of revenue, and would undoubtably be a severe hit to the state's leadership position in the startup economy.

We ask that the Committee not advance this legislation. SB 361 would represent a significant self-inflicted wound to a part of the Maryland economy that is thriving and providing new opportunities in every part of the state.

Thank you for your consideration, and please do not hesitate to contact me if I can provide any additional information or assistance.

Sincerely,

Christopher Gilrein
Executive Director, Northeast
TechNet
cgilrein@technet.org

Maryland SB 361 Written Testimony in Opposition_Ma

Uploaded by: Joseph Schwartz

Position: UNF

Managed Funds Association
The Voice of the Global Alternative Investment Industry
Washington, D.C. | New York

February 9, 2022

Via Electronic Submission

The Honorable Guy Guzzone
Chair, Budget and Taxation Committee
Maryland State Senate
Miller Senate Office Building
11 Bladen St., Annapolis, MD 21401

The Honorable Jim Rosapepe
Chair, Budget and Taxation Committee
Maryland State Senate
Miller Senate Office Building
11 Bladen St., Annapolis, MD 21401

Re: Written Testimony in OPPOSITION to SENATE BILL 361 ("Income Tax – Carried Interest – Additional Tax")

Dear Chairman Guzzone, Vice Chairman Rosapepe, and Members of the Budget and Taxation Committee,

Managed Funds Association[1] ("**MFA**") appreciates the opportunity to provide written testimony to the Budget and Taxation Committee (the "**Committee**") in opposition to Senate Bill 361,[2] entitled "Income Tax – Carried Interest – Additional Tax," which would impose an additional 17% state tax on both a pass-through entity's nonresident taxable income (paid on behalf of nonresident partners) and a corporation's or individual's Maryland taxable income attributable to "investment management services." **If enacted, the legislation would result in combined federal, state, and local marginal tax rates up to 66.75%, and Maryland would stand alone as imposing the most punitive state tax on the investment management community. Senate Bill 361 will drive business and investments out of the state.**

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1 MFA represents the global alternative investment industry and its investors by advocating for regulatory, tax and other public policies that foster efficient, transparent, and fair capital markets. MFA's more than 150 members collectively manage nearly $1.6 trillion across a diverse group of investment strategies. Member firms help pension plans, university endowments, charitable foundations, and other institutional investors to diversify their investments, manage risk, and generate attractive returns over time. MFA has a global presence and is active in Washington, London, Brussels, and Asia.

In Maryland, the alternative investment industry delivers for retirement security, college education, and the important work done by nonprofits and charities through $30.67 Billion in investments. Institutional investors – like pensions, university endowments, and nonprofits – use alternative investments to meet financial obligations, diversify their investment portfolios, and manage risk.

The Maryland State Retirement and Pension System invests approximately $4.3 Billion to help provide secure retirements for its more than 187,430 plan participants. Johns Hopkins University Office of Investment Management invests approximately $2.7 Billion to help fund education opportunities for its more than 27,000 students. Howard Hughes Medical Institute invests approximately $4.5 Billion to help fund its support of biomedical scientists and educators. Investing in Opportunity, Maryland: Hedge Funds Deliver for Maryland Retirees, Students, and Nonprofits (June 17, 2021), at https://investinginopportunity.org/wp-content/uploads/2021/06/Maryland-State-Sheet-MFA-6.17.21.pdf.

2 S.B. 361, 2022 Leg., 444th Sess. (Md. 2022).

Specifically, the additional state tax is calculated by reference to the performance of the investment portfolio funds, and not from the investment itself, and is not imposed on fees calculated by reference to the total assets under management of a pass-through entity engaged in investment management services. Notably, the exclusion for management fee income follows the rationale that "[t]he management fee…is subject to ordinary federal and State income tax rates…and the federal self-employment tax."[3]

Of principal concern, the same exclusion and rationale is not afforded to performance allocations and performance fees included in income as short-term capital gain or ordinary income which are similarly taxed at the graduated ordinary income rates.[4] As a result, Senate Bill 361 creates disproportionately high, and uneconomical, marginal rates on Maryland residents and nonresidents engaged in investment management services as described below.

<u>PERFORMANCE ALLOCATION INCOME (ASSETS HELD LESS THAN 3 YEARS)</u>[5]

<u>Federal tax rates</u>

Short-term capital gains or ordinary income – 37%

Net investment income tax – 3.8%

<u>Maryland tax rates</u>

State individual income tax rate – 5.75%

Local income tax – 3.2%[6]

---

3 Dep't of Leg. Svcs., S.B. 361 (2022) Fiscal and Policy Note 2 (Feb. 4, 2022) (on file with committee).

4 For example, a taxpayer's net long-term capital gain with respect to an "applicable partnership interest," as defined by 26 U.S.C. § 1061(c), will be recharacterized as short-term capital gain to the extent such gain is from the sale or exchange of a capital asset held for not more than 3 years. *See* 26 U.S.C. § 1061(a). Alternatively, the taxpayer may structure this performance element as a fee or make an election under 26 U.S.C. § 475(f), in which cases any income or gain, respectively, will be treated as ordinary income.

5 *See* 26 U.S.C. § 1061(a).

6 Please note that local income taxes vary by jurisdiction; minimum taxes are at least 1% of Maryland taxable income, and no more than 3.2%. Nonresidents are subject to a 2.25% tax in addition to state income tax. Nonresidents may further be subject to a retaliatory local tax, up to 3.2% instead of 2.25%, if the nonresident resides in a local jurisdiction that imposes local income tax on Maryland residents. *See* Md. Code Ann., Tax-Gen. §§ 10-106(a)(1)(iii), 10-106.1; Comptroller of Maryland, Tax Information for Individual Income Tax (Feb. 7, 2022), at https://www.marylandtaxes.gov/individual/income/tax-info/index.php.

<u>Proposed Maryland State surcharge – 17%</u>

Combined Federal, State, and Local Marginal Tax Rate –66.75%

<u>PERFORMANCE FEE INCOME</u>

<u>Federal tax rates</u>

Ordinary income – 37%

Medicare taxes – 3.8%

<u>Maryland tax rates</u>

State individual income tax rate – 5.75%

Local income tax – 3.2%

<u>Proposed Maryland State surcharge – 17%</u>

Combined Federal, State, and Local Marginal Tax Rate –66.75%

If enacted, Maryland would stand alone as imposing the most punitive state tax on the investment management community. The effective date of Senate Bill 361 is not contingent on the adoption of similar legislation in neighboring states and is likely to result in flight from Maryland and rapid secular decline of the investment management community in Maryland. Taking into account taxpayers' likely behavioral responses to the proposed additional state tax, we believe the fiscal impact is overstated.[7] For these reasons, we respectfully request an unfavorable report on Senate Bill 361.

*   *   *

We appreciate the opportunity to provide our written testimony to the Committee regarding Senate Bill 361, and we would be pleased to meet with the Committee or its staff to discuss our

---

[7] The Department of Legislative Services ("DLS") has indicated that,

> It is likely that State revenues will increase by less than estimated, as it does not take into consideration individuals altering behavior on the state level to avoid the tax. DLS anticipates a significant number of taxpayers altering their behavior to avoid the tax, but the extent to which this occurs cannot be quantified.

Dep't of Leg. Svcs., S.B. 361 (2022) Fiscal and Policy Note 4 (Feb. 4, 2022) (on file with committee). Importantly, geographical proximity to other jurisdictions which provide for a lesser overall tax burden on investment management services is the basis on which we expect responsive behavior to be prevalent.

testimony. If the Committee or its staff have questions or comments, please do not hesitate to contact the undersigned at (202) 730-2600.

Respectfully submitted,

/s/ Joseph E. Schwartz

Joseph E. Schwartz
Director & Counsel, Regulatory Affairs
Managed Funds Association
1301 Pennsylvania Ave. N.W., Suite 350
Washington, D.C. 20004

2022 IMC Testimony SB361 - Oppose.pdf
Uploaded by: Michael Johansen
Position: UNF

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TESTIMONY

TO: Honorable Guy Guzzone, Chairman
Senate Budget & Taxation Committee

FROM: Mike Johansen, RWL on behalf of
INVEST IN MARYLAND COALITION

DATE: February 9, 2022

RE: OPPOSITION to SB 361- "Income Tax – Carried Interest – Additional Tax"

The Invest in Maryland Coalition is comprised of many segments of the Maryland financial advisory services industry. It was formed to advocate on legislative matters affecting the delivery of professional financial advisory services to Maryland businesses and individuals – those who rely on professionals to plan for retirement, grow their savings, maximize the value of their businesses and holdings, invest in new ventures, and generally protect their assets.

The Invest in Maryland Coalition opposes legislation that would place new burdens on Maryland individuals, businesses, and the financial services industry – especially when those burdens are limited to the State of Maryland. ***State tax policy should incentivize, not discourage, growth and investment within state borders.***

SB 361 imposes an additional tax on 'carried interest.' The bill imposes a 17% tax on certain income derived from investment management services – on top of the existing state income tax of up to 5.5%. Further, the bill is applicable to tax year 2022 -- meaning the new tax applies to activity occurring prior to the bill's July 1, 2022 effective date.

SB 361 would hinder investment in Maryland. The new tax burden would have one of two effects, or both – first, investors would avoid Maryland and focus their activities in other states where the tax does not apply; and second, the value of Maryland businesses and start-ups would fall. Relocation out of Maryland could occur – as the new tax arguably applies to Maryland based investment management companies even if their investments are out of state.

The proposed legislation also has a retroactive effect. Not only does the new tax apply to income generated in TY 2022 prior to the effective date, the bill would levy the new 17% tax on investment decisions made many years ago (at a time when the value of the deal was not subject to this unique tax treatment). This is an inherent unfairness that should be avoided when creating new tax policy.

The negative impacts of this legislation will be felt far beyond the financial services industry. Maryland will lose jobs, innovation, and even tax revenue as firms respond by de-investing in the State.

For all these reasons, we urge an unfavorable report on SB 361.

For more information contact Mike Johansen or John "JR" Reith at 410-269-5066.

IMD - Oppose SB 361.pdf
Uploaded by: Michael Johansen
Position: UNF

Alan M. Rifkin
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TESTIMONY

TO: Honorable Guy Guzzone, Chairman
Senate Budget & Taxation Committee

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INVEST IN MARYLAND COALITION

DATE: February 9, 2022

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The negative impacts of this legislation will be felt far beyond the financial services industry. Maryland will lose jobs, innovation, and even tax revenue as firms respond by de-investing in the State.

For all these reasons, we urge an unfavorable report on SB 361.

For more information contact Mike Johansen or John "JR" Reith at 410-269-5066.

Oppose SB 361 - Brown Advisory.pdf

Uploaded by: Michael Johansen
Position: UNF

Michael D. Hankin
President and Chief Executive Officer

February 7, 2021

The Honorable Guy J. Guzzone, Chair
Senate Budget and Taxation Committee
Miller Senate Office Building
3 West Wing
11 Bladen Street
Annapolis, MD 21401

Oppose: SB 361- Carried Interest – Additional Tax

Dear Senator Guzzone and Members of the Committee:

I am writing in opposition to SB 361 – Carried Interest Additional Tax.

Brown Advisory is a private, global, independent investment and strategic advisory firm. Our mission is to make a material and positive difference for our clients by delivering a combination of first-class investment performance, strategic advice and the highest level of service. We serve individual, family, government, and institutional clients in 50 states and 37 countries, overseeing nearly $140 billion in client assets.

Brown Advisory is headquartered in Baltimore City, Maryland. Of our nearly 850 employees globally, more than 350 are employed in our Baltimore office and 70 more are employed in Montgomery County. Brown Advisory has 13 offices outside of Maryland.

Brown Advisory is structured as a partnership and every one of our employees is an owner of our firm. SB 361 would impose a 17% surtax on income derived from any "*investment management services*" conducted in Maryland and would further subject our employees and outside shareholders who are Maryland taxpayers to a 17% surtax on the growth of our partnership. This creates a strong incentive to move operations and client activity away from Maryland and additionally incentivizes individual taxpayer relocation away from Maryland.

Brown Advisory has steadfastly committed to Maryland as we have grown across the United States and globally. Our firm and employees are involved, generous, faithful members of our community. Much of what our firm does for clients could be performed from our rapidly growing offices in Austin, Texas or another lower tax jurisdiction with relative ease. In an environment where work is more mobile than ever, we believe this legislation would have intensely negative policy impact.

For these reasons, I respectfully request an unfavorable report on SB 361.

Sincerely,

Mike

BROWN ADVISORY
901 South Bond Street, Suite 400, Baltimore, MD 21231
410-537-5400 800-645-3923

www.brownadvisory.com

SB - 361 - Carried Interest - NAIOP Testimony B&T.
Uploaded by: Tom Ballentine
Position: UNF

NAIOP
MARYLAND CHAPTERS
THE ASSOCIATION FOR COMMERCIAL REAL ESTATE

February 9, 2022

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

Oppose: SB 361 – Carried Interest – Additional Tax

Dear Senator, Guzzone and Committee Members:

The NAIOP Maryland Chapters represent more than 700 companies involved in all aspects of commercial, industrial and mixed-use real estate. On behalf of our member companies, I am writing in opposition to SB 361 – Carried Interest Additional Tax.

Carried interest is a term that dates to the Renaissance merchants of Genoa, Pisa, Florence, and Venice. Ship captains sent to carry goods around the world were provided an interest in the value of the cargo, a *"carried interest."*

Although the concept of *carried interests* are often associated with stock investors, much of the real estate development that takes place today is within partnership entities. According to the IRS, real estate partnerships represent nearly 50 percent of the 3.7 million partnerships in the United States.

In real estate partnerships a *carried interest* is given by the limited partners to the general partner in return for the risks taken, pursuit costs and liabilities borne by that partner during the project. A general partner will often personally guarantee, development design and permit approvals, construction of the project, as well as payment of all debts. In addition, the general partner is at risk for all partnership liabilities such as environmental compliance, and any lawsuits.

SB 361 refers to, *carried interests* but the legislation would simply impose a 17% surtax on the income derived from "*investment management services"* conducted in Maryland. For example, if a real estate management company were to work on acquisitions, dispositions financing and property management, the members' share of the income would be subject to an additional 17% surtax. The bill would increase the tax burden on real estate activities that already pay a repeated series of sales, property, excise, transfer, recordation, and income taxes.

Real estate development, unlike some investments from industries that are the intended focus of the bill, results in the creation of a tangible, capital asset: a mixed-use community, an office building, a housing project, or a distribution warehouse. The investment in the underlying real estate asset gives rise to jobs, results in an increased state and local tax revenue and provides other community benefits through economic multiplier effects.

Applying SB 361's tax surcharge to real estate would have negative policy implications:

+ Increasing fixed development costs and frontloading those costs rather than deferring them by taking them out of capital gains after the project is stabilized would pressure partnerships to take on more debt to finance development operating costs.

U.S. Mail: P.O. Box 16280, Baltimore, Maryland 21210 **Phone:** 410.977.2053 **Email:** tom.ballentine@naiop-md.org

+ Willingness to take development risk is reduced by a tax surcharge. A 2013 study by Douglas Holtz-Eakin, former director of the nonpartisan Congressional Budget Office, found that *carried interest* legislation could result in reduced construction activity and decreased wages in the real estate industry.

+ Reducing the flow of investment capital to real estate projects would be felt hardest by already difficult to finance projects such as urban redevelopment, affordable housing, or property with environmental contamination.

+ The tax surcharge would apply to the distributions of partnership agreements drafted years, perhaps decades, earlier. This penalizes the patient, long-term build and hold business model most of our members follow.

Under current federal law, for investments held less than three years, capital appreciation is taxed as ordinary income; for investments held longer than 3-years it is taxed as long-term capital gain for all partners. SB 361 makes no distinction about the holding period and would impose the 17% tax on passthrough income that is federally taxed at the ordinary income rate.

Federal tax treatment of real estate related income and capital gains may significantly change under the Build Back Better legislation now under consideration in Congress. An increase in the long-term capital gains rate could increase the effective tax rate in Maryland to 37.55%. Adding the 17% surtax in SB 361 would increase the top rate to 54.55%. Because the concepts in federal *carried interest* legislation are not the same as SB 361, we question the value of the abrogation provision and its ability to prevent stacking of taxes.

Because real estate assets are often owned and managed by separate entities within the same real estate enterprise structure, the exemption in the bill based on the percentage of assets in real estate would be insufficient.

For these reasons, NAIOP respectfully recommends your unfavorable report on SB 361.

Sincerely;

T.M. Ballentine

Tom Ballentine, Vice President for Policy
NAIOP Maryland Chapters -*The Association for Commercial Real Estate*

cc: Senate Budget and Taxation Committee Members
Nick Manis – Manis, Canning Assoc.

U.S. Mail: P.O. Box 16280, Baltimore, Maryland 21210 **Direct:** 410.977.2053 **Email:** tom.ballentine@naiop-md.org