



THE MARYLAND HOUSE OF DELEGATES
ANNAPOLIS, MARYLAND 21401

HOUSE BILL 457
THROWBACK RULE AND COMBINED REPORTING

January 28, 2021

SUPPORT

Madam Chair, Mr. Vice Chair and Members of the Ways and Means Committee,

I am here today to ask your favorable consideration of HB 457. Enacting House Bill 457, throwback rule and combined reporting of corporate income changes how corporate income tax is calculated, and in doing so provides a more accurate accounting of the profits that multi-state corporations earn from their activities in Maryland.

Corporations that produce and sell goods in multiple states are required to pay state corporate income taxes based on the portion of their profits that can be attributed to the states in which they operate. Simply selling goods in a state does not alone subject a corporation to that state's corporate income tax. Under federal law, states can only tax corporations with a sufficient "nexus" to the state, which generally means a physical presence. As a result, many multi-state corporations have "nowhere" income that cannot be taxed in any state.

Nowhere income creates an opportunity for multistate corporations to avoid paying a state's income taxes. For example, if a Maryland-based company only makes 10% of its sales in Maryland, then the remaining 90% will be nowhere income that is not taxed anywhere. And yet that company takes full advantage of Maryland's infrastructure and talented workforce. This loophole hurts Maryland's small businesses because they usually pay state income tax on 100% of their profits, yet must compete with larger rivals who pay much less.

Combined reporting recognizes a multi-state parent company and its subsidiaries as one corporation for state income tax purposes. It establishes that multi-state corporations report to the state income based on the amount of Maryland business they conduct. Additionally, the

throwback rule states that if a corporation with facilities in Maryland has income that is not taxed by any state, that income is “thrown back” into Maryland, and taxed here. These strategies prevent the multi-state company from reducing its taxable profits through a range of legal accounting tactics.

IMPACT

- First and foremost, this is a fairness issue. Combined reporting helps to put larger multi-state companies on more equal tax footing with those businesses whose enterprises are in Maryland only. Main Street businesses cannot afford these complicated tax avoidance structures. In that way, large multi-state competitors gain an unfair advantage.
- Multi-state corporations and their employees consume Maryland resources and services. They use roadways and bridges and ride our mass transit. Their kids attend our public schools.
- Many local businesses in each of our own districts are struggling or have failed because of COVID-19. At the same time, many large corporations have done a very well and profits have grown.
- Combined reporting is well-established around the country - Combined reporting requirements and the throwback rule are currently in effect in 28 states each as well as the District of Columbia.
- If passed this year, HB 457 could provide at least \$175-\$180 million per year in additional revenue once fully phased in. Additionally, HB 457 would have no effect on local or small business.
- This bill will fund important improvements in our schools and is ever more urgent in the face of the pandemic and structural deficit our state is expected to face for years to come.
- In 2020, Delegate Stewart’s throwback rule and combined reporting bill passed through the House and I urge this committee to pass it again this year.

COMBAT COUNTER CLAIMS REGARDING THROWBACK

The bill’s opponents will argue that the throwback rule amounts to a large tax increase on Maryland’s businesses and will cause job losses. But these apocalyptic warnings are contrary to all available academic research on this topic. There have been three rigorous studies of the impact of throwback rules on a state’s economy. In 2007, a group of researchers at the University of Tennessee found throwback rules to be insignificant as a predictor of Gross State Product. In a similar study, Professor Teresa Lightner at Oklahoma State University found that

throwback rules were not significant predictors of economic growth. Professor Robert Tannenwald at Brandeis University focused specifically on manufacturing, and found that a state's business tax climate, including its adoption of a throwback rule, has "only a small, highly uncertain effect on manufacturer's capital spending." He added that "states may be more likely to stimulate their economy by enhancing public services valued by businesses." All of this research was confirmed mostly recently in 2014 by Reed College's Professor Kimberly Clausing, who found that throwback rules have no significant impact on employment or investment. Our own Department of Legislative Services has found that the bill will have minimal effect on small businesses.

The catastrophic predictions from the bill's opponents about job losses to the manufacturing and warehouse industries have not materialized in other states. In fact, many of the best states for manufacturing in the country--including California, Oregon, Kansas, Wisconsin, Alabama, and Louisiana--have throwback rules. When Indiana repealed its throwback rule in 2016, it was ranked by the Site Selection Group as the fifth best state for manufacturing; by last year, it had dropped to tenth in the same ranking. The opponents might also cite warehouse and distribution as a sector that will be devastated by this bill. But many of the states most aggressively targeted for Amazon's new distribution centers--including Illinois and Massachusetts--have throwback rules.

In closing, thank you for your consideration and I respectfully request a favorable report.

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