COST

COUNCIL ON STATE TAXATION

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

February 2, 2022

Delegate Vanessa E. Atterbeary, Chair
Delegate Alonzo T. Washington, Vice Chair
House Ways and Means Committee
Maryland General Assembly

Re: In Support of H.B. 321, Relief for Detrimental Financial Statement Effects of Single Sales Factor

Dear Chair Atterbeary, Vice Chair Washington, and Members of the Committee:

Thank you for the opportunity to provide testimony today on behalf of the Council On State Taxation (COST) in support of House Bill 321 (H.B. 321), a measure to provide taxpayer relief for adverse financial reporting impacts of transitioning to single sales factor apportionment. Significant tax law changes such as this can inadvertently have immediate and negative impacts on taxpayers' financial reporting, creating new financial statement expenses in addition to changing a company's actual tax liability. Providing a deduction over time for detrimental effects on deferred tax assets and liabilities can help mitigate inadvertent detrimental financial statement impacts of such tax changes.

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 have operations in Maryland.

COST's Position on Consequences of Significant Tax Law Changes on Financial Reporting

The COST Board of Directors has adopted a formal policy statement on consequences for financial reporting resulting from significant tax law changes. COST's policy position is:

When enacting significant corporate tax law changes, states must mitigate the immediate and negative impact of those changes on a company's financial reporting. While it is evident that companies may experience a change in their actual tax liability as a result of some tax law changes, the financial impact of having to immediately recognize additional tax expense for financial reporting purposes is not always evident.

State Mitigation of Unintended Financial Reporting Effects of Tax Policy Choices

The Internal Revenue Code and associated state rules for recording income and expenses are often different from the Generally Accepted Accounting Principles (GAAP) publicly traded companies follow for recording income and expenses. The difference between the GAAP and tax accounting methods typically result in the creation of deferred tax assets and tax liabilities on the financial statement balance sheets of companies. Significant tax law changes, such as a transition to single sales factor apportionment, typically require companies to re-compute the value of tax assets or liabilities they had previously recorded, and the cumulative effect of that re-computation often requires companies to immediately record additional tax expenses under the relevant financial accounting rules. The recognition of these expenses, in turn, may result in an immediate market adjustment of the company's stock price and value.

States should ensure that such ramifications are addressed to avoid detrimentally impacting companies twice—once through actual tax payments and a second time by a reduction in market value—by tax law changes enacted by their legislatures. States can mitigate these detrimental effects by allowing a deduction to be claimed in the future that can be spread equally over a specified period of time. By providing a reasonable schedule to allow the future deduction of the additional expenses triggered from any book/tax differences, a state can eliminate any financial reporting impact that may be required under financial accounting rules.

H.B. 321 would further sound tax policy in Maryland by providing those taxpayers experiencing detrimental financial statement impacts from the enactment of single sales factor apportionment during the 2018 legislative session a deduction, spaced out over ten years, to mitigate the loss of deferred tax assets and creation of deferred tax liabilities that were not intended by the General Assembly's tax policy decision.

Conclusion

For the reasons set forth above, we encourage you to vote in support of H.B. 321.

Respectfully,

Stephanie T. Do

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