MARYLAND
Chamber of Commerce

LEGISLATIVE POSITION:
UNFAVORABLE
Senate Bill 576
Corporate Income Tax – Combined Reporting
Senate Budget & Taxation Committee

Tuesday, March 7, 2023

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 6,400 members and federated partners working to develop and promote strong public policy that ensures sustained economic recovery and growth for Maryland businesses, employees, and families.

Senate Bill 576 would mandate that certain corporations compute their Maryland income tax using the combined reporting method -- a highly complex system of determining taxable income among all states in which a company does business.

Requiring combined reporting would be a bad tax policy choice for Maryland.

- Data collected by the Maryland Comptroller's Office showed that the revenue impact of mandatory combined reporting would be volatile, including revenue losses in some years.
- The data collected by the Comptroller's Office showed that some corporations would see a *reduction* of their Maryland corporate income tax liability, while other corporations would experience an increase in their tax; i.e., there are both winners and losers. **<u>See an example below showing how the arithmetic of combined reporting can reduce a company's tax.</u>**
- Experiences in other states have shown that after adoption of combined reporting the revenue increase expected did not materialize.
- In 2004, the Maryland General Assembly enacted provisions into the state's tax law that addressed the perceived abuses of "shipping profits outside the state" via intercompany transactions. Additionally, the Comptroller's aggressive audits have resulted in huge additional tax assessments from companies that had utilized intercompany transactions in reducing their Maryland income tax for both pre and post 2004 years.
- Combined reporting is a complex methodology that involves US Constitutional constraints that have been addressed by the US Supreme Court and in dozens of state court cases; it is much more than just adding all related corporations' data together, but rather requires detailed factual analysis to determine which corporations form the "unitary business group."
- The complexity of the combined reporting system would require significant training of the Comptroller's personnel and would likely require add additional staff. There would also be a need for educational outreach to Maryland taxpayers and tax practitioners.

- The complexity of the combined reporting system will further add to the cost of compliance by Maryland's businesses and add to the costs of the State's administration of the income tax.
- Our close competitor states of Virginia, Pennsylvania and Delaware do not require combined reporting.

Example of combined reporting, this one results in less Maryland tax to be paid:

Corporation	Net Income	Apportionment factors: in MD / Everywhere
Parent	$20,000,000	30,000,000/100,000,000
Subsidiary A	30,000,000	10,000,000/500,000,000
Subsidiary B	10,000,000	Zero / 400,000,000
Total group	$60,000,000	40,000,000/ 1,000,000,000

Maryland Tax Calculation – Separate returns:

Parent	$20,000,000 x 30M/100M x 8.25% =	$495,000
Subsidiary A	$30,000,000 x 10M/500M x 8.25% =	$ 49,500
Subsidiary B	Zero apportionment	0
Total		$544,500

Maryland Tax Calculation – Combined reporting:

Total group	$60,000,000 x 40M/1,000M x 8.25% =	$198,000

Group pays **less** Maryland income tax, i.e.,
Maryland's revenue **loss** from combined reporting = $346,500

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

Combined reporting is not a guarantee for increased state tax revenue. Proponents of combined reporting contend that it will raise millions in additional tax revenue without data to support that argument. In fact, Maryland's own Business Tax Reform Commission found that instituting combined reporting "would result in a shift of the tax burden, substantial in some cases, among industries and among taxpayers, resulting in winners and losers." The Commission explained further that the reasons cited in support of combined reporting have each been addressed through other legislative vehicles adopted by the General Assembly and tougher audit methods now utilized by the Comptroller's Office.

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

Combined reporting presents a real competitive disadvantage for Marylanders. Within the region, many of our neighboring states—including Virginia, Pennsylvania, and Delaware—do not utilize the combined reporting method. **In fact, during their 2021 legislative interim, the Virginia General Assembly's Combined Reporting Workgroup determined that combined reporting was not a more efficient system of deterring abusive tax planning beyond their existing tax policy requiring add-backs of certain intercompany transactions – the exact same policy and authority already granted to Maryland's Comptroller.** They further found that combined reporting would not cause a sea change in tax revenue collected, with their results showing 13% of taxpayers would pay more in tax under combined reporting, 14% would pay less, and 73% would pay roughly the same in tax, thus further reinforcing the understanding that combined reporting simply shifts the tax burden among certain industries, creating winners and losers. It would be detrimental for Maryland to employ a new taxation system that will harm the attraction and retention of businesses, and cost Marylander's access to new jobs and economic opportunities, all while increasing the complexity and costs of administering Maryland tax law.

Furthermore, the State's switch to single sales-factor only became fully phased in last year and this committee has heard legislation in the past to provide deferred tax relief to those businesses that experienced detrimental impacts as a result of the shifting tax burden created by that policy. We are only now in a position to fully understand what the impacts of that policy are on revenue collections, now is not the time to implement yet another change in State tax policy.

Maryland businesses are continuing to struggle with extreme workforce shortages and persistently high inflation. According to the New York Federal Reserve there is a 53.8% probability the United States will enter a meaningful economic recession by January 2024.[1] Implementing new income tax schemes that have proven unreliable for revenue collection would clearly have a negative impact on Maryland's job creators and the state budget.

For these reasons, the Maryland Chamber of Commerce respectfully requests an **unfavorable report** on **HB 46**.

[1] https://www.reuters.com/markets/us/two-fed-measures-see-notable-recession-risk-despite-strong-data-2023-02-24/