

TESTIMONY OF PROGRESSIVE MARYLAND BEFORE THE HOUSE WAYS & MEANS COMMITTEE ON HB 1037 and HB 1206

February 25, 2004

My name is Sean Dobson. I'm deputy director of Progressive Maryland, an alliance of 10,000 individuals along with organizational affiliates, including some of the biggest labor unions, faith congregations, and civil rights groups in the state. Progressive Maryland defends the interests of working families.

As such, we are alarmed that over the past year, Gov. Bob Ehrlich has led the way in cutting \$900 million – nearly 10% of state discretionary spending – to balance the FY04 budget. His approach balanced the budget entirely on the backs of hardworking families. Ehrlich's FY05 budget, submitted this session, is a repeat performance, further cutting state programs, cutting local aid, and resorting to creative bookkeeping. Ehrlich also raised what he calls "user fees" – including *de facto* regressive taxes on working families, such as the "flush tax" and "granny tax".

Can Ehrlich's chicanery and chainsaw keep on closing future deficits projected at roughly \$1 billion per year for the foreseeable future? He has run out of accounting gimmicks. As for cuts, Maryland has always been a low-tax, small-government state. Maryland ranks 38th out of 50 states in terms of the amount of total income claimed by state and local governments. Because our government is revenue-starved, we underinvest in our future. Measured as a percent of total income, Maryland ranks 44th in spending on schools and libraries and 47th in spending on health and social services. Government revenues actually declined by 7 percent between 1979 and 1999, when adjusted for inflation – one of the only states that experienced a decline in revenue. Maryland's anemic level of investment has dropped even further over the past year thanks to nearly \$1 billion in cuts. *If the state is broke, it is not as a result of past profligacy, but instead because the state government does not take in enough revenue.*

So more cuts would slice muscle, not fat, from a budget that was lean to begin with. Marylanders agree: 78% oppose further cuts to the state budget, according to an August 2003 Gonzales opinion poll (that poll is in your folder).

Thus, to close future deficits, lawmakers should find more revenue, not impose more cuts. Are slots the answer? Regardless of whether a slots bill passes, gambling revenue would not flow into the Treasury for at least two years. And it would not offer enough money to fully fund pressing public investment needs.

A penny sales tax? If dedicated entirely to public schools, such a proposal is acceptable, despite its regressivity. But the \$600 million it would bring in would also not cover all of Maryland's investment needs.

Maryland needs more revenue than that. Many of the bills you are considering today not only bring in vital revenue, they also would make Maryland's unfair tax code a bit fairer. When testifying on a specific bill, I will spell out precisely how, over the years, Maryland's tax code has become increasingly unfair to small business and regular individual taxpayers.

HB 1037

Madame Chairwoman, thank you for sponsoring last year HB 753, which aimed to close down the three corporate tax loopholes that are almost now household names: the Delaware Holding Company loophole, the Non-Business Income loophole; and the Nowhere Income loophole. Your bill this year to close loopholes, HB 1037, goes in the right direction, but contains two flaws, which I will discuss in a minute.

Corporations in Maryland can well afford to comply with the law and stop cheating on their taxes. That's because Maryland is a corporate tax paradise. Don't take my word for it. Just read the report by the Council on State Taxation -- a conservative, corporate-funded think-tank -- which just last month issued a report comparing business taxes in all 50 states. The report finds that businesses contribute less to state and local taxes in Maryland, in percentage terms, than in any other state in the country (report and *Baltimore Sun* article attached). **Maryland ranks last out of 50 states when it comes to imposing taxes on businesses.** The report is in your folder -- just take a look at Table 3.

Thanks to increasing use of loopholes, corporations dodge an ever greater share of the total tax load in our state. The Multistate Tax Commission -- the national, bipartisan association of state comptrollers -- says that corporate tax-shirking robs Maryland of 42% of the corporate taxes we should be collecting each year. No wonder that the corporate share of taxation has fallen by nearly half in Maryland, to 7.6 percent of total tax revenue in 2002, down from 13 percent in 1980, according to Maryland Deputy Comptroller Stephen M. Cordi.

And let's be clear about the culprits. Locally owned businesses rarely can hire the fancy accountants who dream up these scams. Small-business owners in Maryland play by the rules. The tax cheaters are the big multistate corporations like Burger King and Victoria's Secret. They get all the benefits of doing business in Maryland's lucrative market, but they don't pull their weight when it comes to financing schools that train their workers, the roads by which customers come to their stores, the cops that protect them from thieves, and the firefighters who safeguard their buildings.

Considering these facts, considering the widespread consensus in Maryland that corporate tax loopholes should be closed, and considering the wide margin by which HB 753 passed on the floor last year, we were disappointed to read in the February 5th *Gazette* that you have stripped out of this year's loophole bill – HB 1037 -- the “throwback provision” that would finally close down the notorious Nowhere Income tax loophole.

A corporation based in Maryland gets innumerable benefits from making our state its home base: a world-class workforce educated in Maryland schools; a high quality of life for employees stemming largely from Maryland's vibrant public sector; good roads and transit links; good communications infrastructure; proximity to national and international political leaders and media elites; a geographic location on I-95 between North and South. All these public assets put these corporations in a good position to earn big profits worldwide – including in jurisdictions where said corporation perhaps has no “nexus”. Maryland provides enormous assets to these corporations; our state has the right to tax their profits regardless of where the profits are earned.

Closing this loophole would make perfect sense even in the best of times to restore some fairness to the tax code. That's because corporations are dodging more and more of the state's tax burden, as I mentioned a minute ago. But this year there is an especially compelling reason to implement a throwback rule: our state is in a severe fiscal crisis. Funds for schools, health care, and the environment are being cut. Given these stark alternatives, why allow continued corporate tax cheating? Especially considering how easily HB 753 passed last year, why retreat now? As you know, our schools, hospitals, colleges, and universities need that revenue.

In just one year, \$1 billion has been cut from a budget that was lean to begin with. Everybody should tighten their belts so that Maryland can balance its budget – including big corporations. These same multistate firms can well afford to do so. A recent report by the Council on State Taxation – a pro-business, corporate-funded think-tank --- just released a report showing that businesses contribute less to state and local taxes in Maryland, in percentage terms, than in any other state in the country (report and *Baltimore Sun* article attached). **Maryland ranks last out of 50 states when it comes to imposing taxes on businesses.** Maryland is a tax-avoidance paradise. So what is MedImmune whining about?

MedImmune, the company leading the charge against the throwback, can well afford to pay its taxes. Like all drug companies, it receives tremendous research subsidies from our federal taxes. That industry just received a \$139 billion subsidy from the federal “reform” of Medicare. MedImmune in particular also received a 100% tax break on the construction impact tax in Montgomery County, so it will contribute nothing to pay for the roads its employees will use to get to work. The fact that it describes itself in its annual report as a “Delaware

corporation headquartered in Gaithersburg, Maryland” strongly suggests that it also uses the *illegal* Delaware PIC loophole. And by taking advantage of tax break after tax break, MedImmune has built itself into the 476th-largest corporation in the world, larger than telecom giant Sprint, with 2003 gross income of \$10.5 billion and net income of \$183.2 million. In 2003, it boasts to potential investors about its record profits. So why can’t MedImmune afford to pay its taxes? And how can we tell seniors and low-income families they have to pay their taxes, but a \$10 billion corporation doesn’t?

When lobbying lawmakers, MedImmune threatens to “move to Virginia” if Maryland dares to institute a throwback. Not likely: the Council on State Taxation report referenced above points out that business’ share of state and local taxes was 37 percent last year in Virginia, much higher than Maryland’s 32 percent (the least of any state in the country). And both Gov. Warner and Senate presiding officer Chichester intend to close the throwback loophole in Virginia, which will raise their percentage even further. On this issue, you shouldn’t be to the right of Republicans in Virginia.

Finally, we attach a table prepared by the Center on Budget and Policy Priorities. As you can see, there is absolutely no correlation between a state’s imposition of a throwback and economic growth. Indeed, many of the states with a throwback have flourishing manufacturing and high tech sectors, notably California.

Most of you on this committee support revenue for vital programs. This information should be good news for you – you have the data you need to tell the special-interest lobbyists that there is no reason in the world why they can’t pay their taxes, just like all other good honest Marylanders.

Finally, I would like to note one problem with this bill. Inexplicably, it privileges biotechs as the only type of company that may continue to abuse the Delaware Holding Company tax dodge. As we all know by now, the Delaware loophole is a travesty: how can a company charge itself money to use its own name? No company should be allowed to use this scam. And super-profitable “biotechs” (many of which are ordinary drug companies) need this giveaway a lot less than smaller, less profitable firms.

In summary, Progressive Maryland urges you to put the throwback back into HB 1037, remove the exemption for biotechs regarding the Delaware Holding Company loophole, and then give this bill a favorable report.

HB 1206

Big corporations like Burger King hide taxable income earned in Maryland in dummy firms in Delaware and Nevada. President Miller's loophole bill (SB 156) shuts down this practice. But President Miller's bill does not stop corporations from hiding taxable income in *offshore* locations such as the Cayman Islands.

That's why we support Del. Ross's bill, HB 1206, which would bring Maryland into line with 16 states that require "combined reporting". Under combined reporting, a firm and its subsidiaries are considered a single taxable entity. Under combined reporting, firms cannot hide taxable income in dummy firms.

Montana has applied combined reporting to foreign subsidiaries of U.S. corporations as well. This bill follows the Montana model. If enacted, it would bring in \$90 million each year, which big corporations currently stash in places like the Cayman Islands to avoid Maryland taxes they owe, according to the Multistate Tax Commission (see the report in your folder).

Mr. Chairman, HB 1206 is not a "tax hike", but instead tax enforcement. Nobody – even Gov. Ehrlich -- should object to tax enforcement.

Attachments:

- Gonzales August 2003 poll question on further cuts to the budget
- Report by the Council on State Taxation
- Summary of COST report by the Baltimore Sun
- Report by the Multistate Tax Commission (bipartisan association of state comptrollers)
- Report by Institute on Taxation and Economic Policy
- Gonzales December 2003 poll on Millionaires Tax
- Table on throwback prepared by Center on Budget and Policy Priorities