

## Fact Sheet On Combined Reporting

Revenues from Maryland's corporate income tax – which is supposed to equal 7 percent of corporate profits – have not nearly kept pace with robust corporate profits. This spring, the Comptroller's office revealed that half of the biggest corporations in our state – most of which report big profits to Wall St. – no longer pay any Maryland income tax whatsoever. In an earlier analysis, the Comptroller's office also found that the corporate share of Maryland income taxes fell by nearly half from 1980 to 2002. Corporate underpayment of income taxes stems mostly from proliferating tax loopholes invented by corporate accountants. In particular, multistate corporations move profits out of the states in which they are earned and into states in which they will be taxed at lower rates — or not at all. They do this by creating subsidiaries – often just a mail slot with no employees -- in “tax haven” states like Delaware and then shifting funds to them in the form of fake royalties, fake rent, and sham transactions.

The Multistate Tax Commission -- a national, bipartisan association of state comptrollers and revenue departments – estimates that corporate tax evasion of this kind deprives Maryland of up to 34 percent of the corporate income taxes we should collect each year.

Due in large part to these loopholes, Maryland now has the lowest business taxes of any state in the country when business taxes are measured as a share of all taxes, according to the conservative Council on State Taxation.

In 2004, Maryland took a step in the right direction when it closed the infamous Delaware Holding Company loophole. But corporate accountants continue the DHC's basic ploy of creating fake subsidiaries in no-tax jurisdictions to siphon off income earned in Maryland before the Comptroller can tax it. That is exactly what accountants did when they invented the "captive REIT" loophole, which instead of siphoning off income in the form of fake royalties instead siphons it off in the form of fake rent. As long as Maryland tries to close one loophole at a time, accountants will keep inventing new ones using this basic ploy.

### **Combined Reporting: A Proven, Comprehensive Solution to Loopholes**

Combined reporting embodies a simple, mainstream value: a corporation should not be allowed stash profits in multiple (often phony) subsidiaries in an effort to beat taxes while simultaneously declaring all these same profits to Wall Street in an effort to boost its stock. Combined reporting requires a corporation to have a single set of books and

therefore report to the Comptroller all its profits, regardless of where they are deposited. And it prevents a corporation from getting tax breaks for loaning itself money, among other dubious practices. Thus, combined reporting treats corporations like real persons, who may not create fictitious subsidiaries of themselves in order to hide income from the Comptroller or engage in sham transactions.

Combined reporting has other virtues in that it:

- Would recoup at least \$100 million annually in lost corporate tax revenue for Maryland. The DLS estimate of \$25 million is far, far too low. Our \$100+ million estimate is based on numbers from the Multistate Tax Commission.
- Only affects multistate corporations that resort to multiple subsidiaries and dubious accounting. By contrast, Maryland-based, unistate corporations are, by definition, unaffected by combined reporting. Thus, combined reporting restores a level playing field to Maryland-based companies vis-à-vis giant multistate competitors.
- Enjoys the overwhelming support of Marylanders, who immediately understand its basic fairness. A 2007 poll finds that 87% of Marylanders support combined reporting. Check out the poll at [www.AllianceForTaxFairness.org](http://www.AllianceForTaxFairness.org)
- Is already law in 21 states, which together comprise more than half of the U.S. economy, making this a proven reform.
- Is straightforward to implement. Maryland can rely on years of experience of the 21 combined reporting states in administering this law. The Multistate Tax Commission offers model regulations and training on how to implement and administer combined reporting.
- Correlates with economic growth:
  - Many of the 21 state economies where combined reporting is law rank among the most dynamic in the country, including California, New York, Illinois, and New Hampshire.
  - Since 1990, only 10 out of 50 states have shown positive manufacturing job growth. Of these 10 states, nine have combined reporting.

On pure fairness grounds, Maryland should adopt combined reporting. But the state's \$1.7 billion budget deficit makes combined reporting a necessity. If Maryland is going to ask regular folks to pay more taxes with a hike in the sales tax and ask mom-and-pop Maryland businesses to pay more with a hike in the corporate income tax rate, we should also ask giant, multistate corporations to stop inventing loopholes and pay their fair share.