MARYLAND BUSINESS TAX REFORM COMMISSION

Raymond S. Wacks, Chairman

Maryland Business Tax Reform Commission

May 4, 2010
Minutes of Meeting

A meeting of the Maryland Business Tax Reform Commission was held in the Louis L. Goldstein Treasury Building on Tuesday, May 4, 2010 at 2:00 p.m.

Those present were:

Raymond Wacks, Chairman

Steven J. Banks, Greater Baltimore Committee
Michael Ettlinger, Public Member
Secretary T. Eloise Foster, Department of Budget and Management
Delegate Sheila Hixson
Senator Verna Jones
James Kercheval, Maryland Association of Counties
Senator Nancy J. King
Martin Lobel, Public Member
Senator Richard S. Madaleno, Jr.
Dominick Murray, Department of Business and Economic Development
Paul Nolan, Manufacturers Alliance of Maryland
Karen Syrylo, Maryland Chamber of Commerce
Linda Tanton, Deputy Comptroller

David Roose, Bureau of Revenue Estimates
Marc Nicole, Department of Budget and Management

Speakers present were:

Matt Power, Deputy Secretary Maryland Department of Planning
Michael Day, Chief, Office of Preservation Services
Robert Lynch, Ph.D., Washington College

The meeting was open to the public and members of the local government, state government, media, as well as others, were in attendance.

Chairman Raymond Wacks opened the meeting at 2:00 p.m. Chairman Wacks asked the commission to save time at the end of the meeting to discuss their work plan based on the passed legislation requiring the commission to have their report ready this December rather than December 2011.

Maryland Heritage Structure Rehabilitation Tax Credit Program and the Sustainable Communities Act of 2010 – HB 475

Matt Power: We were originally scheduled to meet with you back in February during legislative session but the meeting was postponed due to the snow storm. I will try to give you the history of our program, the tax credit itself, the legislation that we introduced this past session which was successfully passed.

Please refer to our website; http://btrc.maryland.gov/archive.asp *May 4, 2010.*

Raymond Wacks: Is the program limited to $10 million a year or does the Governor have the discretion to increase or decrease?

Matt Power: The Governor has the discretion to increase or decrease; the only requirement is there is an appropriation and in theory that could be $1.00 appropriation. There is no set dollar amount.

Michael Ettlinger: I had a conversation with a federal government official and one thing he said that I had not thought of before; if you do it as an appropriated grant program, you have to go through this whole contract process with the recipient that the federal government takes several months creating a delay whereas if they did it through the tax code it was much more streamlined. I wonder if that is an issue in Maryland.

Matt Power: Generally we would agree with that. The roll on basis by which a tax credit allows us to accept applications at any part during the year, for one thing, limits them to be spread out throughout the course of the year and there isn't an annual competition as far as scoring and ranking; every single project is against one another and having only this amount of fund the top projects. With a true tax credit, if you meet the criteria you would be eligible and have certainly that you would get it.

Michael Ettlinger: You also mentioned you have a cap on the tax credit so then there has to be some judgments.

Matt Power: Correct. If you have a capped authorized program, essentially if we had a $10 million authorized program, it could come down to a one day sort of competition.

Michael Day: There isn't a contract per say; we have an application that locks someone into it and if they don't carry out the project/ application which we approve then they don't get the credit. Ultimately, if they don't get the credit if they change the project or they haven't come back to us to revise it and get approval for that then that money goes away; it comes completely out of the system. An authorization would only change one thing in that, it would allow the money to go back into the system to be reprocessed to another project that is worthy. We do have a one time of the year competition for the money that we were appropriated for the program.

The feds have another program; rehabilitation tax credit program which started in 1976 and we monitor as well. That has always remained an open ended tax credit as well with the same kind of agreement.

Martin Lobel: Is there any provision or analysis as to whether the program is continuing to be worth the cost to the taxpayers?

Matt Power: I think we regularly have an economic analysis done although not on an annual basis because at some point you start getting the same results back on each of them.

I would argue with our program one of the greatest returns you can see is revitalization of an entire community. I don’t think there are many tax credits that can compete with that.

Steven Banks: I wonder if you could make the study that you are referring to available to the commission.

Matt Power: Absolutely.

Steven Banks: Is this the first year it has become a refundable credit?

Matt Power: No, it was a refundable credit before. It was initially a nonrefundable credit, in the early 2000 it became a refundable credit and has remained.

Steven Banks: Calculation of the credit remains the same whether you are a non profit or tax paying?

Matt Power: Yes**;** 20% of the eligible costs.

James Kercheval: You listed the number of buildings you had done under the program; do you have a breakdown between the numbers of buildings that you did versus the tax credit information?

Matt Power: Yes, we certainly do. It would look a lot like the funding chart.

James Kercheval: Well that really wouldn’t show the properties that were done when they ran out of tax credit monies; your study didn’t track say if a client came in and completed a building, didn’t qualify for the tax credit?

Matt Power: If they didn’t receive funding, it would not be included in our study.

<u>Impact of State Tax Policy on Economic Growth</u>

Raymond Wacks: Introduced Dr. Robert G. Lynch.

Professor Robert Lynch: I am a Professor of Economics at Washington College where I have been since 1998. I have been studying effectiveness of tax policy, tax incentives and public services on state on local governments for over 25 years.

Good Afternoon, I am delighted to be here and share with you my findings on research on the economic effects of tax policy, in general, and business tax incentives.

This is, of course, a particularly important subject right now that we are in the midst of a significant economic downturn and the State of Maryland is grappling with projects of multi-billion dollar budget deficits in the years to come. Please refer to our website http://btrc.maryland.gov/articles/documents/Impact_of_State_Tax_Policy.pdf for Dr. Lynch's presentation.

Raymond Wacks: Chairman asked if any members had questions for Dr. Lynch.

Senator Madaleno: How do we get into the dynamic that we are representing a different county and how do you focus on competition in Northern Virginia? Fairfax County seems to have a model of key factors lower by constantly pushing growth and having a variety of policies designed to push growth as a way to pay. How do you compare that with your statement to # 2; Customer Services per business growth.

Professor Lynch: One of the interesting things that is happening in Northern Virginia; the business community has been asking the Governor of their state to raise taxes as we way to improve infrastructure, roads and bridges.

Senator Madaleno: The same dynamic happens here; across the board business groups have been hopeful in wanting to increase transportation taxes.

Professor Lynch: Right, and in general often the business community is very supportive of taxes when they are used to promote investments in infrastructure, other programs that improve the quality of life which will reduce their cost of doing business in an area.

One of the things that happen too; Northrop Grumman decided to locate to Virginia and the Governor of Virginia talked about the fact that the incentives had been successful and worked, but actually it's sort of the opposite; Northrop Grumman announced more than a year and a half ago that they were going to move to the Washington D.C. area; that had nothing to do with any incentives they were offered. They made it very clear they were coming here because their largest client, the Pentagon, was here and after they made the announcement, and after they terminated their leases, contracts in Los Angeles, they then told the Virginia, D.C. and Maryland: We are coming to your area, what can you do for us? Then there was this bidding war that happened and it turns out that Virginia offered apparently $12 – $14 million in incentives. I don't know what Maryland may have offered but the Washington Post reports that Washington D.C. offered more than twice that amount in incentives. They were not going to locate in Washington D.C.; it was either going to be Northern Virginia or Maryland; had a lot to do with the proximity of their clients, housing need, office building cost, etc.

What we know is that when we look at what firms actually do in response to tax incentives, we actually measure the movement of businesses and job creation. We find it has very little effect of these tax incentives.

Senator Madaleno: Moving away from the idea of tax incentives, and with regards to tax policy, there are some differences between the states on choices. Is there an impact to the differences between our personal income tax in Maryland than in Delaware; are there corporate income taxes and what are the differences, etc?

Professor Lynch: What I can tell you is that certain tax systems are more effective and some are less effective. There are several basic principles:

- Tax system must be efficient;
- Don't want tax system to tax investment, you want the tax system to tax the outcome of investment;
- Tax system to raise the amount of revenue needed to provide public assistance; healthcare, public schools, etc.;
- Simplicity, transparent as possible;
- Maintain fairness.

States that have distribution of state and local taxes which are more technical tend to do better than ones that are less technical; Maryland tends to be somewhat better than most other states in that respect. Data shows for the bottom, 60% of equal distribution in Maryland, state and local taxes take approximately 10% of their income versus at the top, 1% Maryland state income tax takes approximately 6% of their income. That is actually quite a bit better than other states.

When you have the above principles working together, states tend to do better.

Michael Ettlinger: When I look at your findings and studies are aggregate in general. I assume you are not saying that no business has ever made a decision based on a different tax liability.

Professor Lynch: You are absolutely correct. There are so many different tax incentive policies that have been offered. All of them have different effects and some clearly are more effective and some clearly less effective and I am talking about the general effects overall and so I would not advocate that we should eliminate every single business tax incentive policy but what I would argue is that I wish there was the degree of scrutiny of these policies that we typically have for many other programs and we look at it much more carefully and try to calculate to see which of the policies really are effective in creating jobs and which ones are not effective. If we eliminate the ineffective ones that is revenues we could either use as general tax cuts written down or to improve public services; infrastructure, education, healthcare, etc.

So, your point is absolutely well taken; this is a general comment, on tax incentives as a whole, nationwide.

It seems to be that those taxes incentives which are promoting investment tend to do better than those that simply reward certain activities like Enterprise Zone and things like that. But this is something that for the State of Maryland; I don't know the specifics on the programs, I think the state itself should be doing its own internal analysis as to the effectiveness of these programs. I wouldn't want to comment on that.

Michael Ettlinger: Some of these studies were really looking at tax levels overall; could you clarify for us the distinction you are making between tax incentives and tax breaks.

Professor Lynch: Tax incentives typically come in different forms.

- Provide tax breaks for businesses that undertake activities in a particular area like Enterprise Zone;
- Provide tax breaks provided to a specific firm like Northup Grumman, 12 – 14 million in tax incentives that are not available to anyone else;
- Provide tax breaks that are named for a specific activity like a Job Creation Tax Credit.

That is different from the general across the board tax approach which would benefit everyone, for example, increase or decrease in corporate tax break would be different than a tax incentive.

Evidence of the effectiveness on these programs is that the firm's specific tax breaks, do not have a lot of evidence to support them although there are exceptions, there are specific examples and specific circumstances where they do seem to be somewhat more effective.

Steven Banks: I do agree with one of the comments that you made; state taxes in of themselves are not significant in term of the total expenses of an organization but they are one expense that every company considers in relocation or expansion of their environment.

Recently we had some analysis of the Maryland tax structure versus Pennsylvania and Virginia, unfortunately to your comment about these aggregate studies; we are not competing with Arkansas; we are competing with Virginia, Pennsylvania and Delaware. I would suggest that Northrup Grumman did not go to Virginia for 14 million dollars, if you look at the total package; individual tax rate package, no estate tax in Virginia, corporate tax rate, sales tax rate; all of those things combined, you start talking about meaningful numbers.

The other comment I would make is it's not surprising when you talk about these studies and the fact that business people not coming out and saying, "We did this because of the state tax incentives" because in all likelihood there were twenty other reasons as well. Companies do consider all costs; standard of living, education, etc.

Professor Lynch: I agree with your general comments but I would point out; when also asked to look at lessons of the opportunity costs; if that money wasn't spent in that way, how would it have been spent? If Virginia hadn't spent that 12 - 14 million, what would they have been spent it on, would they have spent it on improving roads?

Steven Banks: But your assumption is bringing Northrup Grumman isn't going to create more than 12 – 14 million dollars of revenues to the state that would offset. I don't think states would put that money out without hope for a return.

Professor Lynch: I would have to argue that Northup Grumman came to this area not for the tax incentives; they made the decision to relocate before they were offered the incentives.

Karen Syrylo: Yes, and then they chose between Virginia and Maryland. Most businesses make a decision that they are going to go to this area and then they go through the process. How do you take your analysis and compare Maryland and Virginia?

Senator Jones: I was intrigued by what you said about states specifically looking at whether or not their incentives are truly incentives and what is opportunity and what is the impact if those incentives were here versus not here.

In Maryland, I have specifically introduced legislation to try and capture that information and the businesses have been very reluctant to give up such information that would help us to make those kinds of decisions. So what experiences do you have as far as what states have been doing as far as capturing that information to look at return on investment and the real impacts of those incentives?

Professor Lynch: It's actually been very even in a sense that some states do little or nothing to try account for their return on investment. A few states have been making significant effort to try to quantify just how much they are giving away in tax incentives; we don't even know that for most states. That is the very important first step; just to collect the data, how much was granted in tax incentives, what was the overall cost. If you have some baseline you know what the cost is, you can then look at the economic activity that has occurred in the area and you can start doing some analysis on how effective it was or how beneficial.

It is very difficult to get the information; some people in the business community are very reluctant to give up that information, some cases probably for legitimate reasons and for other times having to do with it not being very effective. New York and Massachusetts have been improving their data collection but other states we haven't a clue in how much they are given away in tax incentives. Economists have been forced to examine what actually happens to immigration/migration firms; this is their happiest point when a change of law has been made where incentives have been offered. Has it actually increased jobs or not. What firms actually do in response to these tax incentives.

Senator Jones: New York and Massachusetts are model states you would suggest looking at?

Professor Lynch: Yes, there are actually others too. I will contact you and let you know who they are.

Dominick Murray: *Mr. Murray is the Deputy Secretary for Department of Business and Economic Development sitting in for the Secretary, Christian Johansson.* As someone who was very intimately involved with the decision involving Northrup Grumman relocation decision, I would like to confirm what Dr. Lynch mentioned. We were advised, and I have no reason to doubt, that Northrup Grumman's decision eventually came down to buildings they were looking at; two in Virginia and one in Maryland and they liked one of the buildings in Virginia. They did assure us and the CEO himself had multiple conversations with both Governors' in both states who were in final competition that the tax policies and incentives accounted not enough in the noise level to make up the decision. I have no reason to doubt what there #2 person told me. It just confirms everything that you were talking about in terms of cost of doing business and what it represented.

Karen Syrylo: The business community still worries about the ever growing list of people who have decided on the Virginia side and not the Maryland side.

My question for Professor Lynch; I have taken two different messages out of what you said, one is the negative data about the benefits of incentives, actual tax reductions that are going through for a variety of reasons that you listed versus your statement that tax increases are actually the job creators. You listed a couple of studies by name and I am familiar with others and I am interested in what you feel about their research; Rutgers University said that New Jersey lost 27,000 jobs after their massive 2002 tax increases; New Jersey lost $10 billion worth of taxable income from people as well as businesses moving out of New Jersey, Boston College studies talk about high income individuals many of whom are business decision makers are migrating out of the high tax states, the fact that Maryland setting aside the millionaires tax issue which we don't know what part of it was economic driven versus tax driven but Maryland aside from that looses a net 20,000 people every year.

What does your research do with those other types of studies that say something different from what you said to us today?

Professor Lynch: First of all my argument is not that increasing taxes is good for growth; context of the deficit and how are you going to close the deficit; by cutting spending or by raising taxes or by some combination of the two. My argument is generally it's less damaging to the state economy to reduce that deficit by raising taxes than it would be by cutting spending. So it's in the context of the deficit.

I am not familiar with the Rutgers study you mentioned.

The Boston study I think frankly was not very good study, effective study. I think we need to be careful with some of the analysis that people put out there; sometimes they do it very carefully and sometimes not so carefully.

Again, I'm not arguing that the state should be raising taxes; I'm arguing in context of this budget deficit, their better off to cut deficit by raising revenues than reducing public spending.

It is the responsibility of the state government to look at all the public service they are offering and go through with a fine tooth comb into many of those tax incentive programs which are waste to the taxpayer's dollars and get rid of them. That I believe you will find will there's a lot more waste in the tax incentives program than the public service programs.

Karen Syrylo: Has any of your research done a complete list of the 50 states and have you done your own ranking of the states that you think are better at overall tax policy? Have you looked at a state by state comparison and have you rated them on your own scale?

Professor Lynch: No, I have not but I have looked at other research that has done that. Interestingly enough, many of the states that are defined as the high tax states are also the ones with the highest personal income, highest standard of living and the states with the most tax burdens are often the lowest standards as well.

Karen Syrylo: We are here as the "Business Tax Reform Commission" we are looking at how Maryland's business tax structure impacts businesses. The other piece that I have not heard talked about in terms of the services that your describing is there are studies out there that show the amount of taxes that businesses are paying compared to the value of the services that the business community gets from the services that you describe. Most of the states show that businesses are paying more in taxes than the services they are receiving.

Professor Lynch: Very few of those studies I think for the most part are not high quality studies.

Martin Lobel: I am assuming from an economic standpoint that when you talk about tax incentives you are really talking about tax expenditures; money that is not being collected, being spent by the state for a particular purpose that the general taxpayer is paying for. Is that a correct assumption?

Professor Lynch: Yes.

Martin Lobel: If we are talking about cutting expenditures, why are we not talking about cutting tax expenditures? Isn't that the same economic impact?

Oklahoma sunsets all tax expenditures and requires a cost benefit analysis before it's enacted. Would that help solve the problem?

Isn't it true that lifestyle, the services provided by the state is far more important in terms of attracting businesses?

Professor Lynch: At minimum we ought to be carefully analyzing the effectiveness of the tax credit policies within the state; periodically review them to make sure they are achieving the goals set out and that they are cost effective and when they are, we should be giving them money and stop wasting taxpayers money. Likewise, clearly when we look at the things that make a state a great place to invest in are the same things that make it a great place to live in; high quality schools, high quality amenities, public services; they tend to improve the chances of firms coming in and investing in an area and creating jobs.

Paul Nolan: In terms of your research that you have done; have you ever done individual interviews, or any sort of more anecdotally routed evidence to talk to executives or businesses or economic individuals involved in these decision making processes?

Professor Lynch: Yes in two ways; the study I did in New York State on Industrial Development Agency; I contacted all 3,000 firms and got their tax incentives and spoke personally to several hundred executives to get their feedback.

Professor Lynch gave additional examples of studies he did.

Paul Nolan: You're positing in effect the incremental decision about a dollar; that it should go to the public sector rather than the private sector because the public sector job is effectively better and yield more services. When you've done studies on this, are you studying the long term effects of this? The long term effects of the incremental cost effectiveness?

Professor Lynch: Yes these studies are going on 30 years.

Paul Nolan: Is there a point of declining marginal return on that decision?

Professor Lynch: I am not sure I understand your question.

Paul Nolan: Meaning the point at which the incremental benefits on each extra dollar begin to decline. You are saying that you're making a decision (in favor of public investment over private investment) just because it's the right decision on the increment, but it may not be the right decision at all increments. Otherwise, all investment should be public and there would be no private sector and that would be socialism. *Laughter.*

Paul Nolan: Where I sit with a Maryland company that has been here since 1889, we are keenly aware of costs. We have increased productivity in the state. We've invested $250 million in capital improvements in this state in the last five years. Every new dollar that's about to be invested has to make sense commercially: all cost are analyzed. But the assumption shouldn't be made just because a company like us is here today; that it means we will be here tomorrow under a different set of circumstances and that is not a threat to say that we move, that's to say that we face global competition everyday and we could lose due to high costs. All of those cost come in everyday so if there's a dramatic shift in the tax structure and a dramatic change, that will have an impact on us.

Audio becomes intelligible due to background noise during Professor Lynch's response.

Professor Lynch: If you provide say $100 million in tax breaks to businesses in Maryland, the state loses that $100 million in revenue, the business does not gain, those taxes are deductible on a federal level, so if they are paying a 35% rate, $35 million of that immediately goes to the federal government, so you have the state loosing $100 million, private sector business gaining $65 million, huge differential. What they will do with that money; many different things, hopefully reinvest in the state creating jobs, hopefully, there's no guarantee that will be the case. Even more so depending on the nature of that business, if you are a multi-state or multi-national firm you may very well be taking that $65 million and using for investments in out of state or out of the country all together versus states spends that $100 million, the first round likely be spent entirely in the state.

Paul Nolan: I understand what you are saying but I'm not an economist. From my perspective I understand that point and after the increment of the decision but I think over time that the $100 invested in the private firm, that will generate more significant activity in the state.

There are ways to for the legislature perspectives to put controls around the incentive issues. We have not applied for certain Department of Business and Economic Development incentives in the past because we were not in a position to make the guarantees that they require not because of anything involved with that project but because we knew of other potential developments and with integrity we just couldn't and would not make the quarantees.

James Kercheval: With regards to the Enterprise Zone Tax incentive, you don't always have enterprise zones to attract a job to your state or community. Sometimes it's just to get a business to locate in an area.

Raymond Wacks: Thanked Professor Lynch for his presentation and requested a copy of his testimony. *Professor Lynch presentation document has been posted to Maryland Business Tax Reform Commission website.*

Using Tax Return Data to Measure the Effectiveness of Tax Credits

David Roose: Just some introductory comments first; It is the case in Maryland many tax credits and I think when we are talking about tax incentives, at least in Maryland, we're generally talking about tax credits or one or two other provisions that act that way. The Enterprise Zone was the first tax credit that was specifically enacted as a tax incentive and that was early 1980's; sometime back. For some period of time after that, there was very little activity on the tax credit front. About 10 – 15 years ago a number of tax credits were enacted and at that time most of the new tax credits have been enacted since then and do in fact have sunsets on them. Many of them do require studies either from the Comptroller's Office or a handful of other state agencies that administer the tax credits. I can't speak to the reception that those studies get but there is some effort made by the state to look at some of these issues. Some of these questions are very difficult to get even very simple answers to.

The Comptroller's Office has for quite a number of years now provided tax credit data specifically to the Department of Legislative Services and also to anyone who calls and asks for information. It is generally the case that the only specific information that can be known with certainty from the tax returns is the aggregate cost to the state of all the tax credits together. We cannot know things such as even the dollar amount that the state has spent on one specific tax credit. We also cannot tell from tax return data, for example, how many employees have been hired for the Work Opportunity Tax Credit or a number of the other tax credits even though we ask for data on tax forms to give us some detail as to the activity that underlies the tax credits.

I think the view of the Comptroller's Office, that in many of these instances where these credits are administered or certified by other state agencies, those agencies are much better positioned to measure the effectiveness of those credits; how people are being hired, how many jobs are being created. Those agencies are in much better position to asses how well these are working than the Comptroller's Office is. Why is that?

Business tax credits are claimed on the 500 CR. This form is eight pages, asking for information about the 18 or 20 business tax credits that are available. The data from that form is not captured automatically as the data from the main corporate income tax form or the individual income tax form is captured by the tax processing system. We actually have to spend about six weeks every year manually determining which tax returns have that form attached to them, entering by hand the data from those returns, giving quite a bit of review to that data as rendering it to try to make some sense of it, clean up where taxpayers may not have gotten things exactly correct and then try to make sense of it in light of what is on the remainder of their tax return. There are issues that come up such as; if a taxpayer has no taxable income for the tax year, they may not enter on the form 500 CR for the corporate income tax they received business tax credits because those credits will have no effect on their tax liability.

The way the tax processing system is currently structured if there is nothing on that line then we don't know that the form has a 500 CR attached and cannot go to get it, can't get the system to tell us here is this form, go get the data from it. It may be the case that if the taxpayer has no tax liability in that year regardless of the credits may not give us the 500 CR even if they've done something that earns a credit in that year that they can carry forward to the following year.

We have discussed in prior meetings; if a taxpayer for whatever reason does not file a tax return and claim the credit, the Comptroller's Office has no idea that the incentive provided by the credit has actually been enacted upon and somebody has done that activity. As odd as it may sound, there are examples of taxpayers who have been certified for tax credits, sometimes pretty substantial tax credits, and a tax return never comes in the door that claims that credit as far as we know. Many of these credits can be claimed against the insurance premium tax, or the franchise tax. Those are administered by the Insurance Administration and the Department of Assessment and Taxation; the Comptroller's Office obviously has no information about those credits. But in those cases where the activity has been undertaken but there has been no income tax form filed, it may be the case for many of these credits which are certified or administered by other agencies that those agencies do know that this activity has occurred.

When we're talking about tax returns, some very mundane issues like the timing of filing of returns can complicate trying to make sense of some very simple questions. Until a tax return is filed, we have no idea what any taxpayer has done. It is the case for many corporate taxpayers that there tax year doesn't start on January 1st like it does for most individuals.

- 70% of corporations don't start on January 1st
- 30% of other corporations have a tax year that starts later in the year
- 6% start of corporate taxpayers have a tax year July 1
- 5% start on September 1

What the means is for us to get a consistent twelve month period of data, we have to wait almost two full years after the end of the calendar year in question before we know that we have something that is consistent. You can't use the tax data to say, "I want to know all of the activity that has occurred between January and December of this tax year, this calendar year or any other twelve month period." The only way we can get what is a comprehensive look at twelve months of activity is again, waiting for almost two full years after a calendar year.

Again, not all of these credits are certified or administered by other agencies, but for those credits which are, it is quite possible in many instances those agencies have a handle on what is occurring both in real time and during consistent periods of time because tax years can stretch almost over two full years. Obviously economic circumstances can change and we may not even as best as we can look at consistent full year of activity doesn't reflect the same sort of economic activity throughout that period.

On a related note with respect to tax administration; amended returns can affect how we look at tax credits that have actually been claimed. Returns for can be amended for net operating loss, carrybacks, audits and it a return can be filed one year claiming a tax credits, amended two years later with net operating loss carrybacks that wipes out all of the taxable income for that tax year and effectively removes the credits from being claimed in that tax year, then they can be carried forward claimed in another year; all of these issues really complicate interpreting the data from the tax returns trying to make sense of what incentive these credits are actually having.

Credits in Maryland state law are not prioritized. If you were to claim two credits in one year, and those credits exceed your tax liability, we have to make an assumption as to whether all of one credit, and a portion of the other or the credits were two thirds claimed with the remaining third carried forward to the next year; issue which complicates interpretation both for this year and for any year in which credits are carried forward. A carried forward credit and a credit earned in the carried forward year, we don’t know which dollar claimed as a tax credit on the tax form applies to which credit.

Several of these issues can be addressed through legislation.

I mentioned credit carried forwards; the way the tax forms and the tax processing system are now, if your credit exceeds tax liability for many of these credits, the excess credit can be carried forward to a future year and applied to reduce liability in that year. When that happens, we lose track of the identity of that credit. It would take an awful lot of manual research putting together tax returns for every taxpayer from one year to the next to identify that the $500 that shows up on the 500 CR, Part U- Excess Credit Carryover Calculation, we would have to look at prior year tax returns to identify what kind of credit that was.

One of the greatest complicating factors and the most difficult to resolve is deals with Pass Through Entities; Non C corporations, LLC’s, Partnerships, other type of non corporate entities income of which is reported on the individual income tax returns of each of the owners. Many of these entities can have dozens or even hundreds of owners meaning that the $3,000 tax credit can be spread across fifty individual income tax returns. That has several complicating issues; the current system right now has no way to tie together all of the members of one pass through entity. We cannot take the tax data and say, this $3,000 is one credit, in a related fashion, if this credit is showing up on all the fifty owners, we are going to count if we can identify this credit, that credit as showing up on fifty returns and being fifty credits. We don’t know it’s really on one piece of action that has resulted in that credit. Again, the agencies that have certified the credit are in a much better situation to make those judgments.

Raymond Wacks: So what is the most significant thing that this commission could recommend or that the legislature can implement that would make it easier for us to judge the effectiveness of tax credits?

David Roose: I think there are several things; as many of you know we are in midst of implementing a new tax processing system which by itself may mitigate the effect some of these issues although I think to fully address all of them would really take a tremendous amount of resources in terms of programming time.

We have attached in your packet how we report the credits that have been earned for business tax credits. There are several points about that table; these are non-necessarily the cost to the state because these credits may have exceeded taxpayer liability that amount would be carried forward. These do in a sense reflect the liability the state would ultimately have for these credits.

Martin Lobel: How much does business have to pay their accountant and lawyers to complete all these forms?

Karen Syrylo: As you can see the small number of business using these credits.

Discussion of Revised 2010 Schedule

Raymond Wacks: Is this the best day to hold our meetings? Any days of the weeks that is better.

- Move meetings to Thursday instead of Tuesday
- Issues about staff furloughs along with November elections and holidays;

Chairman Wacks asked commissioner members to e-mail David Roose with concerns on the schedule.

May 18th speakers are already lined up to speak at the meeting.

Raymond Wacks: Consider this is your potential work schedule and give us your comments on how you think this can go forward. We have a lot of work to do now that the report is due December 15th. We should try and do most of our work this summer and move forward.

We will try and finalize the schedule at the May 18th meeting.

James Kercheval: So if I understand this schedule correctly, the subcommittees are not going to meet at all and the two next dates we are actually going to give direction to the reporters on what the report is going to be.

David Roose: Our thought is the subcommittees will get back together to discuss the pros and cons of the various issues and approaches. The subcommittees themselves won't be making any recommendations. The subcommittees will then report to the full commission in mid June.

James Kercheval: We are basically giving the final information on what we want and the pros and cons.

David Roose: essentially to start developing the report and start putting the issues on the table and making things more concrete.

Karen Syrylo: What do we do if there are items that were recommended for the commission to look at by a member but at our prior meetings we hadn't gotten to those items or had not fully discussed those items? Are we limited to what has been discussed so far or can one of the items of the subcommittee be a recommendation they want to add something to the list of studies?

David Roose: Depending how extensive it is, that certainly could be. We have asked all of the members for any particular options in terms of changes to tax policy that they would like investigated for discussion in late May, and early June. Nothing needs to be final until we get to October, November. I think the commission agreed, public hearings and discussion throughout the summer of all the issues. If there are anymore issues that need to be brought to the table, discussed in more detail, there's no reason that can't be worked in.

Michael Ettlinger: Are the subcommittee's going to make the recommendations to the full commission or are we just teeing up the questions?

Raymond Wacks: I think we are pretty much teeing up the questions for the full commission and trying to list the pros and cons. They maybe hold some public hearings and then this fall try to finalize our recommendations.

Karen Syrylo: Since the May 18th meeting is a discussion on more items about combined reporting, may I refresh the minutes please with a request that I made at one of our prior meetings about having staff show us a chart of the collective data about combined reporting in a slightly different format. What I'd ask for is having the numbers be based on two categories:

- In state payroll
- In state property

The chart now is broken shows by size of company based on gross receipts. I think it would be helpful on which companies are already paying significant salary dollars.

David Roose: We will have that available for the meeting on May 27th.

Paul Nolan: So we will be reporting the subcommittee reporters at the next meeting?

David Roose: It would be helpful if the commission decided how exactly to approach; getting here to a final report on December 15th. Again this is our thoughts on how we could get there.

Raymond Wacks: We can discuss this more on the May 18th meeting. We will try to finalize our dates, work schedule and processes. If you have any comments, please send them to us.

Next meeting: May 18, 2010

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