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Beyond loopholes: BHI study suggests simplifying and lowering all business taxes to 5.3%

BOSTON – Massachusetts business tax laws are a hodgepodge of poorly-conceived measures that violate the most fundamental principles of tax equity and efficiency. By taxing all business entities similarly and adopting unitary reporting, single-sales-factor apportionment, along with other proposed reforms, the Commonwealth could cut the corporate tax rate to 5.3% and achieve approximate revenue neutrality. The Beacon Hill Institute details these reforms in its new study, Business Taxes in Massachusetts: Toward Fundamental Reform, released today.

BHI’s proposed reform would provide a stimulus to the state economy. The Institute predicts that its proposal would create about 4,000 new private sector jobs and $120 million in new investment upon implementation. The state would lose $86 million in revenue or about 0.41% of state tax revenue. David G. Tuerck, Executive Director of the Institute and a co-author said that “this tiny loss in revenue is well worth the economic stimulus and the tax simplification that the proposal would make possible.”

At 9.5%, Massachusetts currently levies the fourth highest statutory state corporate income tax rate in the United States. By reducing the tax rate and broadening the tax base, the BHI proposal would send a signal to the business world that Massachusetts is now a destination for adding plant and payrolls. The problem of corporate loopholes would disappear as firms found it in their interest to report income in Massachusetts rather than other states.

“Massachusetts should strive for a predictable and competitive business tax policy that serves firms, investors, workers and government in the most optimal manner,” said James Angelini, PhD, Director of the Master of Science in Taxation program in the Sawyer School of Business at Suffolk University and the lead author of the study. “A uniform rate covering a broader base would provide a stable source of revenue and promote economic growth.”

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Specifically, the Institute proposes that the Commonwealth:

- set the tax rate at 5.3%, the same rate as for individuals;
- eliminate the $2.60 per thousand tax on tangible personal property or net worth, applicable to C and S-corporations only;
- eliminate the conduit concept by taxing entities at the rate of 5.3% at the entity level;
- eliminate the double taxation of C-corporation earnings (and large S-corporations) by taxing business entities (domiciled in MA or with nexus) by 5.3% at the entity level (as apportioned if multi-state) and eliminating the tax on corporate dividends to C-corporation shareholders or flow-through income from conduits;
- eliminate the $456 minimum tax on C- and S-corporations;
- adopt combined reporting and unitary tax principles, without a “waters edge” election. (This will apply to all types of entities, not just corporations)
- adopt single-sales-factor apportionment for all entities and industries, not just some;
- allow net operating loss carryover deductions by sole proprietors, corporate trusts and partnerships;
- eliminate all tax incentives; and
- allow a 100% dividends-received deduction for dividends received by corporations, regardless of the percentage owned.

Against the tide of corporate tax avoidance strategies, the Commonwealth could strike a competitive blow by lowering rates rather than simply raising more revenue. “If they are expected to become viable sources of revenue in a volatile economy, business taxes must be reformed in a manner that promotes revenue stability, economic growth as well as equity, simplicity and transparency,” added Angelini.