Doc 2008-13184 (21 pgs)

Business Taxes in Massachusetts: Toward Fundamental Reform

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The authors would like to acknowledge the assistance of Suffolk University students James A. Nolet and Michael Head, as well as interns Ashley Mowatt of Simmons College and Ian Finn of Boston College.

Editor's note: Most of this report was written before enactment of the corporate tax revision bill. See note 2 on p. 381. For news coverage of Democratic Massachusetts Gov. Deval Patrick's signing into law the corporate tax bill, see State Tax Notes, *July 14, 2008, p. 75,* Doc 2008-14981, *or* 2008 STT 132-9. *For a viewpoint by Joseph X. Donovan and Sarah Wellings, with the Boston-based law firm of Sullivan & Worcester, about the new combined reporting law see* State Tax Notes, *July 21, 2008, p. 193,* Doc 2008-15443, *or* 2008 STT 141-5.

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I. Introduction

Massachusetts has a history of trying to placate two competing interests: corporations that are among its largest employers and that seek relief from the high corporate tax rates imposed by the state, and the ever-needful state government that seeks to close loopholes and otherwise capture more money for state programs. The result is the worst of all worlds -- a reputation as a state with high business taxes and steady frustration over an inability to collect enough (as some would see it) in business tax revenue.

We propose a comprehensive business tax reform that would, if implemented, bring sense to that broken tax system. Our proposal would broaden the base, lower the rate, and make Massachusetts a competitive destination for businesses. It would attract business and bring workers into the state, while creating a level playing field for all types of business. It would help reverse the perception that Massachusetts is a high-cost, high-tax state and play to the strengths of the Massachusetts economy. With our reform plan, small businesses could expect predictability, and larger businesses could expect a new opportunity to source their income, payrolls, and property to Massachusetts rather than to other states.

Massachusetts has many economic advantages over other states, including access to a highly educated workforce and an open, diverse economy that brings the resources of its financial enterprises to its many technology start-ups. According to the Beacon Hill Institute's 2007 "State Competitiveness Report," Massachusetts ranks second among all states in its ability to sustain a high level of income for its citizens. However, even with that high ranking, Massachusetts has to improve dramatically its substandard state and fiscal policy performance. One way to improve the prospects for the state's long-term economic health is to expand the business tax base while cutting the statutory tax rate on corporations.

Sound tax policy requires that any tax should meet the test of horizontal equity -- that is, the application of a tax to two equal individuals or entities treats them equally. Sound policy likewise requires a tax to meet the test of vertical equity, in which the concept of ability to pay is applied to individuals and firms with different incomes. Other objectives are simplicity, transparency, stability, neutrality, and economic growth. The current tax system and recent proposals fail to meet any of those tests of sound tax policy.

Because the taxation of legal business entities varies considerably from business to business, Massachusetts taxes do not achieve horizontal equity. Firms with similar business income face different tax burdens, depending on the legal business forms they may have chosen. Table 1 (next page) compares income tax rates on the various entities allowable in Massachusetts and their owners, as well as property and other taxes. The table makes clear the wide disparity in taxation. Some businesses are subject to double taxation, taxes on tangible property, taxes on net worth, minimum taxes, or annual report fees, or some combination of the above.

Table 1. Comparison of Tax Rates on Massachusetts Business

	C Corp	**S Corp ‹$6 million**	**S Corp ›$6 - ‹$9 million**	**S Corp ›$9 million**	**Partnership**	**Sole Proprietor**	**Corporate Trust**
Entity Tax Rate	9.5%	0.0%	3.0%	4.5%	0.0%	0.0%	5.3%
Owner Tax Rate (Individual)	5.3%	5.3%	5.3%	5.3%	5.3%	5.3%	0.0%
Total Tax Rate*	14.8%	5.3%	8.3%	9.8%	5.3%	5.3%	5.3%
Minimum Tax	$456	$456	$456	$456	None	None	None
Annual Report Fee	$125	$125	$125	$125	$500 (LLC)	None	$75
Tax on Tangibles or Net Worth	$2.60/M	$2.60/M	$2.60/M	$2.60/M	None	None	None

*Assumes that there is no federal tax effect and that dividend distributions are unaffected by state corporate taxes.

Massachusetts tax law also violates the principle of vertical equity, because large multistate corporations (often with greater tax law expertise) have more opportunity than smaller firms to shift income to lower-tax states. That inequity distorts business decisions, driving smaller firms and their employees out of the state. It also diminishes the amount of revenue generated by other taxes, including the individual income tax, the sales tax, the meals tax, and property taxes.[1]

Part II summarizes business tax law in Massachusetts and describes the tax treatment of corporate income. Part III compares Massachusetts business tax law with that of competitor states. Part IV presents a set of reform proposals, and Part V examines the revenue and economic consequences of those proposals. Part VI includes a summary and the conclusion.

II. Business Tax Law in Massachusetts

Businesses in Massachusetts can choose to organize as C corporations, S corporations, partnerships, limited liability companies, limited liability partnerships, sole proprietorships, or corporate trusts (also called trusts with transferable shares). An option to establish regular trusts is also available in Massachusetts, but it is rarely used because most businesses do not operate as trusts. Each form has unique characteristics that include tax and nontax factors. The taxation of those forms in Massachusetts is the result partly of federal tax policy and partly of the state's tax treatment.

Federal tax law, which has its own inequities, often dictates the form of entity, because federal taxes are usually larger than state taxes. However, Massachusetts has a long tradition of steadfastly resisting the imposition of federal tax policy on state tax law -- often adopting some, but not all, portions of the Internal Revenue Code. Therefore, Massachusetts tax law can still be driven by tax policies that benefit the state, regardless of the choice of entity for federal tax purposes. We next explore the tax differences between state and federal business forms.

In Massachusetts, business entities are either taxpaying entities, conduit entities, or a combination of both. A conduit entity passes all its income (or losses) through to owners. The entity itself does not usually pay taxes. Choice of entity is one of several important tax planning decisions a business must make, and mistakes are costly. Often the decision is influenced more by federal taxes than by state taxes; however, there is no good policy reason why a business's state form must be the same as its federal form. Businesses should have the ability to choose which entity, at each level of government, is appropriate for tax and other purposes. In Massachusetts, businesses that pay tax at the entity level include C corporations, larger S corporations, sole proprietorships, LLCs (if taxes are paid at the federal level), and corporate trusts. S corporations, partnerships, LLCs (if conduits at the federal level), and LLPs are conduit entities.

A. C Corporations (Form 355)

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[1] Tax Foundation, *State Business Tax Climate Index*, 2003-2008, October 10, 2007. This index indicates that in 2008 Massachusetts's overall business taxes rank 34th in the nation, which is a decrease from 26th in 2003. Massachusetts ranks 46th for corporate taxes alone.

C corporations pay taxes on net taxable income at the rate of 9.5 percent, which is the fourth-highest state corporate tax rate in the country.[2] If the corporation has a loss or very low taxes, it pays a minimum tax of $456. C corporations also must pay a $125 fee to the secretary of state for filing their annual report. In addition to the corporate income tax, C corporations pay a significant tax on tangible personal property located in Massachusetts (other than property that is taxed locally by a city or town). If they do not have sufficient personal property, they pay a tax on net worth. The rate is $2.60 per $1,000 for both. The tangible property tax includes all property the company owns, including machinery and equipment, trucks and automobiles, furniture and fixtures, leasehold improvements, construction in progress, inventory, and supplies. If any of those assets is taxed by a city or a town, it is exempt from the tangible property tax. The tangible property or net worth tax and the minimum tax are regressive because they are not based on income; companies with losses still have to pay those taxes. The burden is especially heavy on companies with inventory, which usually increases during times of decreased sales. There is little incentive to store inventory or supplies in Massachusetts.

Massachusetts C corporations are subject to double taxation. If a portion of corporate profits is distributed as a dividend, the distribution generally is taxed to the shareholder. Corporate profits are thus taxed once to the corporation and again to the shareholder when they are distributed as dividends (assuming the corporation has adequate earnings and profits per IRC sections 301, 312, and 316). A Massachusetts corporation that receives dividend income from another corporation is allowed to deduct 95 percent of the dividends received if it owns more than 15 percent of the corporation paying the dividend. Dividends from Massachusetts corporate trusts are not eligible for that deduction. The purpose of the dividends received deduction is to prevent possible triple taxation. However, that goal is not met for dividends from corporations with less than 15 percent ownership.

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[2] On July 2, 2008, Massachusetts adopted new legislation that will lower the business C corporation excise tax from 9.5 percent to 8.75 percent in 2010, 8.25 percent in 2011 and 8 percent in 2012. S corporations with total receipts in excess of $9 million will pay tax at the same rate as business C corporations, less the personal income tax rate on ordinary income (currently 5.3 percent). S corporations with total receipts between $6 million and $9 million will pay two-thirds of this rate. Massachusetts has also adopted unitary taxation starting in 2009, but on a water's-edge basis unless the corporation elects otherwise. Furthermore, Massachusetts will conform to federal law regarding business entity classification ("check-the-box" rules). While these reforms are a step in the right direction they fall far short of the substantive reforms we recommend here. When fully phased in, the 8 percent corporate tax rate is still one of the highest in the nation and does not! eliminate double taxation. The changes to S corporation tax rates do not eliminate the double taxation of S corporation earnings, which is rare, but do lower the rates slightly. The adoption of unitary taxation is in agreement with one of our proposals, but requiring a water's edge calculation significantly weakens the tax avoidance goal. Furthermore, unitary taxation is required only for Massachusetts corporations that still allow tax avoidance for large partnerships and LLCs.

As an example of corporate double taxation consider the following: John owns 100 percent of the stock in XYZ Inc. (a C corporation). XYZ Inc. had Massachusetts net taxable income for the current year of $100,000 and paid dividends to John totaling $100,000. What is the Massachusetts tax treatment of XYZ's earnings?

- XYZ Inc. pays Massachusetts corporate tax on the net earnings of $100,000. At 9.5 percent, that would equal $9,500.
- Also, John pays income tax at a rate of 5.3 percent on the $100,000 of dividends that he receives, or $5,300. Therefore, the $100,000 is taxed twice for a total corporate and individual tax of $14,800, a combined rate of 14.8 percent.[3]

C corporations also pay twice on liquidation. At the point of liquidation, C corporations pay tax at the corporate level on the gain on any appreciated assets, and the shareholders pay tax again when they receive the liquidating dividend. That means that C corporations are induced not to hold real estate, which tends to appreciate, because the appreciation will be double-taxed if the corporation liquidates (liquidation is common in an asset sale, which is preferred by buyers). Shareholders have an incentive to own the real estate separately or in a realty trust, in which there is no possibility of double taxation.

There are various methods of avoiding the double tax on C corporation earnings and those methods are used in Massachusetts as well as at the federal level (although a single method may not work for both federal and Massachusetts taxes). The following advice applies to a business entity that aims to minimize its tax liability:

- **Elect to be taxed as an S corporation if Massachusetts gross receipts are less than $6 million.** Massachusetts S corporations do not pay tax at the corporate level if their gross receipts are less than $6 million. A corporation must choose S status in the first 75 days of its tax year for the S status to be applicable for that year. If it misses that deadline, it is a C corporation for that year (it can ask the IRS for a late election, but there is no guarantee that the IRS will grant it). If there is appreciated property in the corporation, and if the corporation does not elect S status in the first year, it will have to wait 10 years to liquidate its assets to avoid a corporate-level tax even though it is an S corporation. That is called a built-in gains tax, which prevents C corporations that want to liquidate from electing S status just before the liquidation to avoid the corporate-level tax. Another benefit of electing S status in the first year of the corporation's life is that losses, which are likely in the first year, will flow through to, and potentially be deductible by, the shareholders. If a filing corporation misses the deadline and elects S status in the second year, the first-year losses will be stuck in the C corporation until the corporation liquidates, which may not be for many years. The shareholders will not be able to deduct the S corporation losses on their Massachusetts personal income tax returns.
- **Don't pay out dividends, because they are taxed twice.** Although the IRS has the accumulated earnings tax, widely seen as a weapon against that strategy,

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[3] That assumes no federal tax effect and that dividend distributions are unaffected by state corporate taxes.

there is no such penalty tax in Massachusetts. Accumulating income in a C corporation is encouraged in Massachusetts.

- **Pay the dividend as a deductible salary to shareholders who are also employees instead of paying nondeductible dividends.** However, all deductions have to be reasonable in amount. So, for example, the salary must be reasonable for the duties performed by the shareholder-employee. That is not workable if the shareholder is not an employee. The Department of Revenue will attack "unreasonable" compensation and claim that part of it is disguised dividends and therefore not deductible.
- **Pay deductible rent instead of nondeductible dividends if the shareholder leases property to the corporation (another reason why real estate should not be in a C corporation).** Deciding which assets should be transferred to the corporation and which should be retained by the shareholders and leased to the corporation is one of the important decisions a corporation must make early on. Also, the rental of real estate will generate depreciation deductions that do not require a cash outlay.
- **Pay deductible interest instead of nondeductible dividends to shareholders who are also creditors.** Another decision to make when forming the corporation is how it will be capitalized. The shareholders can put the assets into the corporation in exchange for stock (equity) or stock and some debt (a note owed to them). Interest expense paid by the C corporation to the shareholder-creditor is deductible if not usurious. Also, repayment of the principal is tax free. However, on corporate formation, if the shareholders are transferring appreciated assets into the corporation, the receipt of debt will trigger a gain to the shareholder (section 351).

These examples show how the law creates an incentive for businesses to use their resources on tax avoidance efforts rather than business investment. Those tax avoidance strategies, which are more applicable to smaller business, permit some C corporations to avoid paying the double tax.

B. S Corporations (Form 355S)

Massachusetts S corporations are hybrid entities. They are both taxpaying and conduit entities. The corporation pays no tax when gross income is less than $6 million.

S corporations pay a tax of 3 percent on net taxable income when gross receipts are between $6 million and $9 million, and 4.5 percent on net income when gross receipts are above $9 million. That treatment is not mirrored at the federal level, at which there is usually no entity tax. Note that the determination of the tax rate is based on *gross* receipts or sales, before deductions, and not on *net* income. The tax, however, is based on net taxable income. Therefore, a Massachusetts S corporation could pay income tax even though net taxable income is far less than $6 million. That treatment is inequitable because it favors companies with low sales and high profit margins compared with companies with high sales and low profit margins.

Income or loss is passed through to S shareholders. At the federal level, an S corporation's income is not taxed twice, as it is with a C corporation. However, without a special rule, a C corporation faced with double taxation of earnings or liquidation could easily avoid the double tax by simply electing to become an S corporation. To prevent that, federal law may impose a double tax on S corporations that switch to S status after their initial year as C corporations. Those special S corporation double taxes are called built-in-gains taxes or passive income taxes. In Massachusetts the corporation usually does not pay tax below the $6 million gross receipts level, unless it was once a C corporation and converted to S status after the first year of its life. In that case the Massachusetts S corporation could pay income tax on built-in gains or passive income, even if receipts are less than $6 million. The S corporation also pays a tax on tangible property or net worth, the $456 minimum tax, and the $125 annual filing fee, similar to C corporations. Therefore, S corporations in Massachusetts are subject to double taxation when gross income is above $6 million and possibly under $6 million if they were once C corporations.

C. Partnerships (Form 3), LLCs, and LLPs

A Massachusetts partnership never pays taxes. Therefore, there is no double taxation, as there is for C or some S corporations. They also do not pay the $456 minimum tax, nor do they pay the $125 annual report filing fee.

Massachusetts LLCs are taxed in the same manner as they are for federal taxes, if they have at least two owners. At the federal level, a business can check the box on Form 8832, which allows it to be taxed as a C or S corporation or as a partnership. Single-member LLCs (allowed in Massachusetts) cannot be taxed as partnerships but are taxed as sole proprietorships, or as a branch or division of the owner. Therefore, the tax form chosen at the federal level must be used for Massachusetts tax purposes.

Massachusetts LLPs are not subject to the same restriction. They are always taxed as partnerships, regardless of how they are treated at the federal level. However, there is no policy justification for requiring conformity to federal treatment for LLCs but permitting nonconformity for LLPs. Both LLCs and LLPs pay a $500 annual report fee to the secretary of state, which is four times the fee paid by corporations. Regular partnerships pay no annual fee. There is no justification for those huge fee disparities based on the entities' legal form; doing so violates horizontal equity.

An important distinction in the tax treatment of conduits is that the income (or loss) of the partnership or the S corporation flows through and is taxable to the partners or shareholders regardless of how much they have taken out as draw (partnerships) or dividends (S corporations) during the year. The income is taxable to the owners regardless of whether they actually get it. If partnership taxable income is $100,000, the partners will be taxed on $100,000 on their personal returns, even if they did not receive any money from the partnership in draw. And they are taxed only on $100,000 even if they took a draw of $150,000. The same is true for S corporations. Therefore, it is the flow of income, not cash, that is taxed. The cash paid out as draw or dividends is not taxable and is ignored, with rare exceptions.

That is not true for C corporations. For C corporations, if a shareholder receives dividends, he pays tax. Otherwise he pays no tax. Any guaranteed payments paid to partners, and salaries paid to shareholders who are also employees, are deductible by the partnership or corporation and taxable to the partner or shareholder. Those types of payments are not ignored and they reduce the amount that flows through. Guaranteed payments to a partner are like a salary to an employee, but technically, they are not a salary, because a partner can never be an employee of the partnership.

When there are losses in a partnership or S corporation, those also flow through and are potentially deductible. Again, those losses flow through to owners regardless of how much cash they have taken during the year as partner draw or employee salary to the S shareholder. That treatment can create cash flow problems for minority shareholders or partners. For example, a minority (50 percent) shareholder in an S corporation is taxed on her share of the income and has no power to force management to pay a dividend. In effect, the shareholder pays the corporation's income tax. However, when there are losses, those are potentially deductible by the S shareholder or partner, unless restricted by the passive loss rules or lack of basis.

Example. Judy owns 10 percent of the stock in XYZ Corp., an electing S corporation. After deducting Judy's wages of $10,000 for various services to the corporation, the corporation earned a net taxable profit of $50,000 for the current year and made cash dividend distributions to the shareholders of $30,000.

- Judy includes in her income the wages of $10,000 and her share of the corporate income of $5,000 (10 percent of $50,000). The $10,000 is deductible to the corporation. The $5,000 increases her basis in her corporate stock.
- Judy receives 10 percent of the dividend distribution, or $3,000. That distribution is tax free, unless it exceeds her basis in her stock.

Therefore, the tax treatment of Massachusetts conduits varies dramatically from that of C corporations and is solely due to the legal form chosen, rather than to sound policy considerations.

For both the S corporation and the partnership there is the potential for nonreporting of the passthrough income to nonresidents. Forms SK-1 and 3K-1, indicating each owner's share of the entities net income, is sent to all owners. The nonresident shareholder or partner has the responsibility to file a nonresident Massachusetts income tax return (Form 1-NR/PY) to report that income. Whether the nonresident actually does file is another matter. An out-of-state owner may not file, making it difficult to collect the tax he owes.

D. Sole Proprietorship (Schedule C and Form 1)

Massachusetts sole proprietorships are firms owned by one individual. A sole proprietorship is not a separate legal entity and the owner has unlimited liability; that is, his personal assets are at risk. The income or loss is calculated on Massachusetts Schedule C and included on the owner's individual income tax return (Form 1). There is no double tax, minimum tax, or annual report fee due.

E. Corporate Trusts (Form 3F)

A Massachusetts corporate trust (also called a trust with transferable shares) is any partnership, association, or trust for which ownership is represented by transferable shares. Corporate trusts are taxed in the same manner as sole proprietorships, although many IRC provisions that apply to corporations also apply to corporate trusts. For federal purposes corporate trusts could be C or S corporations. They do not pay the $456 minimum tax but they do pay a $75 annual filing fee.

F. Apportionment and Unitary Tax Issues

An important question for Massachusetts, or any state, is whether it has the ability to tax corporations incorporated in other states or countries (foreign corporations) when they do business in Massachusetts. The U.S. Supreme Court addressed this issue as it affects the commerce clause of the U.S. Constitution, stating that a state has the right to tax a foreign corporation when:

- the foreign corporation has sufficient nexus with the taxing state;
- the tax is fairly apportioned;
- the tax does not discriminate against interstate commerce; and
- the tax bears a relationship to the services provided by the state.[4]

For our purposes, the first two prongs of that test are the most important.[5] The legal right to tax a foreign corporation in Massachusetts depends on whether there is sufficient nexus between the corporation and Massachusetts. Adequate nexus includes physical presence, such as ownership or the leasing of property, offices, employment, and other tests, within Massachusetts. The existence of nexus (and hence the ability to tax a non-Massachusetts business) has been frequently litigated by the states.[6]

When a business entity has income both from business activity or ownership of any property in Massachusetts and in another state, and the other state levies an income or franchise tax, the entity must determine the amount of income that is taxable in Massachusetts by apportioning income on the basis of sales, tangible property, and payroll located within Massachusetts. For a partnership, there must also be one or more corporate or nonresident individual partners.

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[4] *See Complete Auto Transit v. Brady*, 430 U.S. 274 (1977).

[5] The U.S. Supreme Court has not defined what constitutes discrimination in interstate commerce, but it has provided some guidelines. A state may not tax a transaction more simply because it is multistate rather than an entirely in-state transaction. Interstate tax discrimination should not interfere with the economic decision of where to site one's business. The last test requiring the tax to bear a fair relationship to the services provided requires only that the tax is reasonably related to the amount of business the foreign business conducts in the state.

[6] P.L. 86-272, 15 USC 381-385 applies to state taxes based on net income and helps define when there is sufficient nexus. For example, the mere solicitation of sales orders of tangible personal property (but not real or intangible property), in which the orders are sent out of state for fulfillment, does not constitute nexus. There are several questions not addressed by that law, and there are many activities that will cause the loss of protection, and thus create nexus.

The goal of fair apportionment is to prevent multiple taxation of the same income by the states where a company does business.[7] A similar goal exists at the federal level for multinational companies except that the approach is different. Federal law taxes all of the income of U.S. companies doing business in several countries and, to reduce or eliminate the potential for multiple taxation, allows a deduction or credit for taxes paid to other countries. Foreign companies doing business in the United States are taxed only on income effectively connected in some way with the United States. States do not prevent multiple taxation by taxing all the income of a foreign corporation and allowing deductions or credits for taxes paid to other states. Rather, they apportion income using various formulas to approximate the economic activity in each state.

The Massachusetts apportionment formulas vary according to the type of industry or the type of legal entity. Only business income is apportioned. Massachusetts follows the rule whereby interest, nonbusiness rents, royalties, and some capital gains are not apportioned but are attributed 100 percent to the state where the property is sited.

The general formula for apportionment is to divide Massachusetts tangible property, payroll, and sales by worldwide property, payroll, and sales to yield percentages. The sales percentage is multiplied by two and added to the percentage for property and payroll. That total is then divided by four. The resulting apportionment percentage is multiplied by modified federal taxable income to determine Massachusetts taxable income. Oddly, partnerships use a single-weighted sales factor and divide by three. Manufacturers and some mutual fund companies use only sales to determine their apportionment percentage (single-sales-factor apportionment).

The multitude of apportionment formulas used by the states creates inefficiencies and inequities in income apportionment. Only 10 states use a three-factor formula, and 20 states double-weight the sales factor. In 2008 Illinois, Nebraska, Iowa, Oregon, Texas, Georgia, Wisconsin, and New York are starting to use single-factor-sales apportionment for all entities. Other states are contemplating or moving toward single-sales-factor apportionment. Some states allow the business to choose among several formulas.

Single-sales-factor apportionment benefits companies that are headquartered in the single-sales-factor apportionment state, because they usually have large investments in property and large payrolls that would receive no weight in the formula. That apportionment method likewise forces companies with high sales but small investment and small payrolls in the state to allocate more of their income to the state.

Under single-sales-factor apportionment, non-Massachusetts companies doing business in Massachusetts would allocate more of their income to Massachusetts than they do under the three-factor formula, because they usually have little property and only small payrolls in the state. Using a single sales factor would induce the same companies to site more of their property and payrolls in Massachusetts. Massachusetts

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[7] The Uniform Division of Income for Tax Purposes Act is a model law providing a standardized set of rules for the taxation of multistate corporations. Some states have adopted it as is and others have partly adopted it or modeled their own laws after it.

uses a throwback rule that does not allow a Massachusetts business to apportion income to a state that will not tax the income because of a lack of nexus or other reasons.

The potential for tax avoidance by businesses comprising many different business entities is a major problem for states. Significant tax avoidance opportunities exist to shift income to subsidiaries or related companies located in low-tax states or low-tax countries. For example, a corporation in a low-corporate-tax state such as Texas can form a Massachusetts-related corporation and charge the Massachusetts company royalties for use of the company name or for other intangible assets. The royalties paid are an expense that is deductible by the Massachusetts company and not taxable to the corporation in Texas. Similar tax avoidance can be accomplished with the payment of interest on loans to related entities.[8]

The states approach that issue in various ways. Some states use separate entity reporting, in which each legal entity is required to file a return and is taxed, *if* there is nexus. Some states allow the filing of a single consolidated income tax return if the entities are related and each has taxable income in the state. For the latter method, there are two approaches to apportionment of the income. Either the income is apportioned for each member of the group separately and the taxable income is combined, or the apportionment formula is applied to the data of the combined group using a single formula.

Massachusetts allows corporations, if they are filing a consolidated return for federal purposes, to elect to be taxed as separate entities or to file a consolidated return. Apportionment is applied to each corporation separately.

Another option is to allow combined reporting for a unitary business. The crucial difference between a consolidated return and a combined return for a unitary business is that under the unitary concept, the income from all affiliated businesses is included in the apportionment calculation, even if a member of the unitary group does not have nexus in the state. Therefore, the income (or loss) of a company without nexus in the unitary group is included in the apportionment, and a portion is allocated to a state even though the corporation does not operate in that state. The member of the unitary group that has nexus reports its share of income based on an apportionment formula that includes the factors of the *entire* unitary group rather than just those with nexus. That approach is constitutional and can include foreign subsidiaries of a U.S. multinational or a foreign multinational with U.S. subsidiaries.[9]

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[8] *See Geoffrey, Inc. v. South Carolina Tax Commission*, 114 S. Ct. 550 (1993) and *Kmart Properties, Inc. v. Taxation and Revenue Department* (Docket No. 21,140, New Mexico Ct. App., Nov. 28, 2001). Those cases held that the licensing of intangible assets that are used in-state create sufficient nexus to tax the parent or related company. (For the decision in *Geoffrey*, see *93 STN 133-12*; for the decision in *Kmart*, see *Doc 2001-29956* or *2001 STT 233-18*.)

[9] *Container Corp. of America v. Franchise Tax Bd.*, 463 U.S. 159, 103 S. Ct. 2933 (1983); *Barclays Bank PLC v. Franchise Tax Bd.*, 512 U.S. 298 (1994). Some states

Of course, the important question is determining which entities are members of the unitary group; that is much like determining nexus. Under a unitary approach, legal entities are ignored, and the rules apply to partnerships as well as to corporations. The determination of which entities are included in the unitary group is difficult because there is no standard definition. The courts have applied various tests, including common ownership, common operations, centralized management, functional integration, interdependence among entities, and other factors.[10] The objective of combined unitary reporting is to eliminate the tax avoidance potential of intercompany transactions. That is the same objective as for consolidated returns, except that the unitary approach is more effective. Massachusetts has not adopted that approach.[11]

III. Massachusetts Business Tax Laws Compared With Competitor States' Laws

In Table 2 we present a comparison of the Bay State's business tax laws with business tax laws of competitor states.[12] We compare tax rates, double taxation, tangible property or net worth taxes, minimum taxes, unitary taxation, apportionment formulas, and C corporation dividends received deductions for C corporations, S corporations, partnerships, and sole proprietors.

The analysis indicates that Massachusetts has the second-highest C corporation tax rate and is one of the few states that taxes S corporations at the entity level. Massachusetts is one of 14 states out of 18 we surveyed that double-tax C corporation income, but is 1 of only 2 states that also double-taxes S corporation income. Massachusetts is one of only two states with a tax on tangible property or net worth in addition to the income tax. Massachusetts is not alone in imposing minimum taxes on corporations (C or S). Eleven states of the aforementioned states impose that tax, and four states impose a minimum tax on other entities, such as partnerships or LLCs; Massachusetts does not. Ten of the 18 states have adopted unitary tax principles; Massachusetts is not one of them.[13] Massachusetts has three different apportionment formulas, which apply to different industries and businesses; that is more different formulas than any other state has. Except for one, all states that tax corporate business income permit a deduction for dividends received from other corporations.

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allow a taxpayer to make a water's-edge election, which limits apportionment to only those entities within the United States.

[10] For example, see *Butler Bros. V. McColgan*, 315 U.S. 501 (1942) and *Mobil Oil Corp. v. Commissioner of Taxes of Vermont*, 445 U.S. 425 (1980).

[11] *Supra* note 2.

[12] Compiled by authors from examination of tax forms and laws and based on states included in Beacon Hill Institute "State Competitiveness Reports 2001-2007" and Massachusetts Technology Collaborative as enumerated in *The Index of Innovation Economy, 2006*.

[13] Massachusetts has adopted a "water's edge" unitary law as of January 1, 2009. The water's edge requirement significantly weakens the tax avoidance purpose of unitary taxation.

We conclude from that comparison that Massachusetts significantly lags behind other states in competitiveness regarding tax rates, S corporation entity taxation, tangible property and net worth taxation, and unitary taxation. Whether Massachusetts is competitive in apportionment formulas is difficult to say. However, applying different formulas to different businesses clearly violates horizontal equity principles. Massachusetts is competitive regarding sole proprietor tax rates and the double taxation of C corporations (but not S corporations), and is somewhat competitive regarding minimum taxes (11 of the 18 states impose lower or no minimum taxes).

IV. Reform Proposals

In some quarters, Massachusetts has an image problem that may be hindering investment decisions. According to one report, Massachusetts ranks 46th out of all states for corporate taxes and 34th when other taxes, such as unemployment taxes and property taxes, are included.[14] Other reports maintain that overall business taxes in Massachusetts are low when compared with personal income.[15] That view, however, does not address the possibility that the state's poor record in creating new jobs may be attributable to its corporate taxes.

Clearly, other states have been competing more effectively than Massachusetts in lowering their business taxes. Not surprisingly, the growth of Massachusetts's economy from 2003 to 2006 was almost the slowest in the nation.[16] To prevent further erosion of the tax base, including personal income, property, sales, and meals taxes, Massachusetts should consider lowering the nominal business tax rate.

State governments are not alone when facing the problem of complex, inefficient tax codes. A parallel can be seen at the federal level. The United States has the second-highest effective corporate tax rate in the developed world.[17] Not long ago, the United States could boast of having one of the lowest corporate tax rates. But that has changed. Other countries are aggressively competing by lowering their corporate tax burdens. Declining corporate tax revenue, combined with a slowing economy and decline in the value of the dollar, are related to the nation's lack of international tax competitiveness.

Table 2. Comparison of Tax Characteristics of Competitor States

	C-corp	S corp	Sole Proprietor	Double

[14] Tax Foundation, "State Business Tax Climate Index," 2008.

[15] Massachusetts Budget and Policy Center, "Business Taxation: Isolated Statistics Versus a More Complete Picture," *MassBudget Brief*, Jan. 10, 2008, *available at* http://www.massbudget.org/BizTaxBrief.pdf.

[16] Based on Beacon Hill Institute calculations, Massachusetts ranked 48th, ahead of Ohio and Michigan. Data are available on request.

[17] Tax Foundation, "New Ranking: Major U.S. Trading Partners Cut Corporate Tax Rates While U.S. Stands Pat With Second-Highest Rate," July 27, 2007. *Available at* http://www.taxfoundation.org/news/show/22504.html.

State	Tax Rate (%)	Tax Rate (%)	Partnership Tax?	Tax Rate (%)	Taxation (entity)
California	8.84	1.50	No[d]	1.0 - 9.3	Yes (C & S)
Colorado	4.63	0.0	No	4.63	Yes (C)
Connecticut	7.50	0.0	No	3.0 - 5.0	Yes (C)
Delaware	8.7[a]	0.0	No	0.0 - 5.95	Yes (C)
Florida	5.50	0.0	No	None	No
Maine	3.5-8.93	0.0	No	2.0 - 8.5	Yes (C)
Maryland	7.00	0.0	No	2.0 - 4.75[e]	Yes (C)
Massachusetts	**9.50**	**0.0, 3.0, 4.5**	**No**	**5.30**	**Yes (C & S)**
Minnesota	9.80	0.0	No[d]	5.35 - 7.85	Yes (C)
New Hampshire	8.5 - 9.25	8.5 - 9.25	8.5 - 9.25	8.5 - 9.25	No
New Jersey	6.5 - 9.00	0.0	No	1.4 - 8.97	Yes (C)
New York	7.10	0.0	No	4 - 6.85[e]	Yes (C)
North Carolina	6.90	0.0	No	6 - 7.75	Yes (C)
Rhode Island	9.00	0.0	No	3.75 - 9.9[f]	Yes (C)
Texas	0.50 - 1.00[b]	Same as C	Same as C	None	No
Utah	5.00	0.0	No	2.3 - 6.98	Yes (C)
Vermont	6.00 - 8.50	0.0	No[d]	3.6 - 9.5	Yes (C)
Washington	.015 - 0.484[c]	Same as C	Same as C	Same as C	No

Table 2 *(Continued)*

State	Tangible Property or Net Worth Tax	Minimum Tax ($/entity)	Unitary Taxation	Apportionment Formula[a]	Dividends Received Deduction[j]
California	None	800 (C, S, P, LLC)	Yes	SSPP	Yes (V)
Colorado	None	None	Yes	SPP, SP	Yes (F)
Connecticut	Yes	250 (C, S, LLC)	Yes	SSF, SSPP	Yes (V)
Delaware	None	35 - 165,000	No	SPP	Yes (F)
Florida	None	None	No	SSPP	Yes (F)
Maine	None	None	Yes	SSF	Yes (F)
Maryland	None	None	No	SSPP, SSF	Yes (F)
Massachusetts	Yes (C, S)	456 (C, S)	No	SSF, SSPP, SPP	Yes if >15% owned
Minnesota	None	0 - 5,000 (C, S, P)	Yes	SPP[i]	Yes (V)
New Hampshire	None	None	Yes	SSPP	No
New Jersey	None	500 - 2000 (C, S)	No	SSPP	Yes (V)
New York	None	800 (C, S)	Yes	SSF	Yes (V)
North Carolina	None	$1.50[g] (C, S)	No	SSPP	Yes (F)
Rhode Island	None	500[h] (C, S)	No	SPP	Yes (F)
Texas	None	None	Yes	SSF	Yes
Utah	None	100	Yes	SPP, SSPP	Yes (V)
Vermont	None	250 (C, S, P, LLC)	Yes	SSPP	Yes (F)
Washington	None	None	N/A	N/A	N/A

Note: SSF = single sales factor;
SSPP = double weighted sales, property and payroll;
SPP = single-weighted sales, property, payroll;
SP = Sales and property.
All factors evenly weighted unless otherwise noted.

[a]Plus .576 on gross receipts;

[b]X Gross revenue - (CGS or comp.);

[c]on gross receipts;
[d]minimum tax applies;
[e]plus local taxes;
[f]or 7 flat rate;
[g]per $1,000 of stock;
[h]or $2.50 per $10,000 of stock;
[i]SSF in 2013;
[j]V=varies by % owned, F = same as federal.

Our reform proposals seek to meet the following objectives:

- broaden the tax base by increasing the number of businesses that are taxed;
- increase horizontal and vertical equity;
- eliminate double taxation;
- increase compliance by nonresident entities and owners;
- decrease tax avoidance;
- attract business to Massachusetts; and
- increase tax revenues of all types in the long term while maintaining current business tax revenue.

Specifically we propose the following:

Set the statutory business tax rate on all entities at 5.3 percent, the same rate as for individuals. C corporations now pay 9.5 percent. S corporations pay nothing if gross receipts are less than $6 million, 3 percent of taxable income if gross receipts are greater than $6 million but less than $9 million, and 4.5 percent if gross receipts are over $9 million. Partnerships pay no tax; corporate trusts and sole proprietors pay 5.3 percent. The varying tax rates violate horizontal equity, in that two business taxpayers with the same income will pay very different income taxes (see Table 1).

Eliminate the tax of $2.60 per $1,000 on tangible personal property or net worth, applicable only to C and S corporations. That tax is regressive and not uniformly applied to all businesses. Partnerships, sole proprietors, and corporate trusts do not pay this tax. Because the tax bears no relationship to the ability of the business to pay, it is regressive. In fact, it often increases when a business is doing poorly and when inventories, which are included in the tax base, are growing. The tax does not make Massachusetts an attractive place to invest capital.

Eliminate the conduit concept by taxing all entities at the rate of 5.3 percent at the entity level. All entities, regardless of the legal form, would pay tax at the entity level. That proposal would tax businesses organized as partnerships or S corporations under $6 million in gross receipts, which currently are not taxed. The major benefit of that proposal would be to increase compliance by nonresident partners and shareholders, who often fail to file nonresident personal income tax returns for the flow-through income from those entities. That would also eliminate the need to adopt check-the-box rules. If tax considerations are removed, Massachusetts should allow any choice of entity that the taxpayer desires, and the choice could be different from the form chosen at the federal level. Taxpayers should be allowed to choose the form in which they wish to conduct business to accomplish business goals, other than tax avoidance.

Eliminate the double taxation of C corporation earnings (and the earnings of large S corporations) by taxing all business entities (domiciled in Massachusetts or with nexus) at 5.3 percent at the entity level (as apportioned if multistate) and eliminating the tax on corporate dividends to C corporation shareholders or flow-through income from conduits. Dividends from Massachusetts corporations would not be taxable to resident or nonresident shareholders. Dividends to Massachusetts residents from corporations not subject to Massachusetts taxation would continue to be taxable. Flow-through income to partners or S shareholders would not be taxable if from entities taxable in Massachusetts. Dividends would continue to be nondeductible by the corporation. That eliminates the problem of collecting tax on nonresident owners. It also eliminates double taxation on liquidation and discourages the use of debt versus equity capital structures, excessive compensation, and rent as double-tax avoidance schemes. Of course, taxpayers may still use those techniques to avoid federal tax, which would affect Massachusetts, and compliance could still be a problem in the reporting of compensation, interest income, and rental income by nonresident shareholders, as it is now. The solution to that problem is to deny the corporation a deduction for wages, interest, or rents paid to nonresident shareholders. Also, we propose elimination of the 9.5 percent built-in gains and passive income taxes of S corporations that were once C corporations.

Eliminate the $456 minimum tax on C and S corporations. That tax is regressive and horizontally inequitable. The minimum tax is not assessed on partnerships, sole proprietors, or corporate trusts and has no bearing on the ability to pay tax. The largest multinational corporation with a loss and the smallest new corporation with few assets pay the same tax. It impedes business formation in Massachusetts and discourages businesses from choosing the corporate form. It has been justified as a fee for the privilege of using the corporate form and the benefits it confers, such as limited liability; however, corporations already pay $125 ($500 for LLCs) to the secretary of state when filing their annual report. The minimum tax is exorbitant and without merit. Further, LLCs enjoy limited liability yet do not pay the minimum tax if they choose to be taxed as a partnership.

Table 3. Static Revenue Estimates, 2009-2013
($ millions)

	2009	2010	2011	2012	2013
C Corporate Income Tax Changes					
Rate Reduction to 5.3%	(323.13)	(328.92)	(334.96)	(341.28)	(347.88)
Minimum Tax Elimination	(21.55)	(21.93)	(22.34)	(22.76)	(23.20)
Combined Reporting and Unitary Tax Principles	182.24	185.50	188.91	192.47	196.19
Incentive Tax Credits	135.80	138.23	140.77	143.42	146.20
Subtotal	(26.65)	(27.13)	(27.62)	(28.15)	(28.69)
S Corporation Tax Changes					
S Corp Tax Collections Expansion	47.16	48.01	48.89	49.81	50.78
Minimum Tax Elimination	(39.55)	(40.26)	(41.00)	(41.77)	(42.58)
Combined Reporting and Unitary Tax Principles	94.33	96.02	97.78	99.62	101.55

Incentive Tax Credits	76.90	78.27	79.71	81.22	82.79
Subtotal	178.84	182.04	185.39	188.88	192.54
Business Property Tax Change	(264.45)	(268.99)	(273.62)	(278.32)	(283.10)
Total Net Change	(112.26)	(114.08)	(115.85)	(117.58)	(119.25)

Adopt combined reporting and unitary tax principles, without a water's-edge election, for all business entities. That will apply to all types of entities, not just corporations. Massachusetts does not use unitary or combined reporting.[18] Doing so would capture some of the income -- including income in other countries -- of affiliated (unitary) out-of-state corporations, without direct nexus in Massachusetts that now escape taxation. That income escapes taxation via a number of tax avoidance schemes, such as using transfer pricing; establishing nexus in low-tax states and shifting income out of state; avoiding the Massachusetts business property tax by investing in low-tax states; and intercompany transactions such as management fees, interest, and royalties. The state should also eliminate throwback rules, which seek to assert Massachusetts tax on income, properly allocable to another state, if the other state imposes no tax. The throwback rule cannot be defended on equity grounds and is simply a revenue raiser.

Adopt single-sales-factor apportionment for all entities and industries, not just some. Why discourage payroll and property investments in Massachusetts by including those factors in the formula? Single-sales-factor apportionment would make Massachusetts more competitive and attract more business to the state. The apportionment factors used in Massachusetts depend on the industry the taxpayer is in, which is not horizontally equitable. Single-sales-factor apportionment would also simplify apportionment calculations under combined reporting.

Allow net operating loss carryover deductions by sole proprietors, corporate trusts, and partnerships. Only corporations are now allowed to carry over their losses to future years. Allowing only some businesses to take those loss deductions violates horizontal equity. It also punishes the taxpayer whose earnings vary considerably from year to year and rewards those with steady earnings. This is consistent with the proposal to tax all businesses at the entity level.

Eliminate all tax incentives. Those include:

- the 3 percent investment tax credit;
- the economic opportunity area credit;
- the vanpool credit;
- the research credit;
- the harbor maintenance tax credit;
- the full employment credit;
- the brownfields credit;
- the low-income housing credit;
- the historic rehabilitation credit;
- the home energy efficiency credit;
- the solar heat credit;

[18] *Supra* notes 2 and 13.

- the film incentive credit; and
- the medical device credit.

Those credits decrease the tax base and reward targeted industries and taxpayers, and therefore are not horizontally equitable.

Table 4. Dynamic Tax Revenue Changes, 2009-2013
($ millions)

Tax	2009	2010	2011	2012	2013
Sales and use tax	4.16	4.25	4.33	4.42	4.51
Motor fuel taxes	0.19	0.19	0.19	0.19	0.19
Motor vehicle fees	0.10	0.10	0.10	0.10	0.10
Corporations excise tax	(106.48)	(106.53)	(106.58)	(106.63)	(106.68)
Personal income tax	4.38	4.39	4.39	4.39	4.39
Cigarette and tobacco taxes	0.25	0.26	0.27	0.27	0.28
Other taxes, fees, and revenue	11.09	11.24	11.39	11.55	11.70
Unemployment insurance tax	0.42	0.42	0.42	0.42	0.42
State dynamic revenue change	***(85.89)***	**(85.69)**	**(85.49)**	**(85.29)**	**(85.09)**
Residential property	0.02	0.02	0.02	0.02	0.02
Business property	6.76	6.76	6.76	6.77	6.77
Local dynamic revenue change	*6.78*	*6.78*	*6.78*	*6.79*	*6.79*
Net dynamic revenue change	**(79.11)**	**(78.91)**	**(78.71)**	**(78.51)**	**(78.30)**

Allow a 100 percent dividends received deduction for dividends received by corporations, regardless of the percentage owned. Currently, only corporations that own more than 15 percent of the dividend paying corporation are allowed this deduction. There is no equitable rationale for that arbitrary percentage cutoff. That change will eliminate double or triple taxation of dividends.

Under our proposal, although first-year tax revenue would decrease because of the lowering of the rate, elimination of double taxation and minimum taxes, we expect that the decrease would be largely offset by revenue increases because of the following:

- Single-sales-factor apportionment will decrease taxes on businesses that have payroll and property in Massachusetts but increase taxes on non-Massachusetts businesses with little payroll or property in Massachusetts.
- Taxing all entities, including partnerships and small S corporations, will decrease loss of revenue due to noncompliance of out-of-state partners and S corporation shareholders.
- Unitary or combined reporting without a water's edge election will increase revenue because of elimination of many of the tax avoidance schemes now used by multistate corporations. That will broaden the tax base by capturing income from entities in low-tax states or countries without nexus in Massachusetts.
- The elimination of all targeted tax credits will increase revenue.
- There will be an increase in the first-year tax base because of new business formation in Massachusetts created by improvements in equity and the lowering of tax rates and elimination of double taxation.

V. Estimated First-Year and Long-Term Revenue Effects

We provide both "static" and "dynamic" revenue estimates. Static estimates assume that there is no change in underlying economic activity in response to a change in tax law. For example, under a static estimate, a decrease in the corporate income tax rate from 9.5 percent to 5.3 percent would be predicted to cause corporate tax revenue to fall by 44.2 percent (= (9.5-5.3)/9.5).

The evidence shows that state- and local-level tax changes have significant effects on state economic activity.[19] A dynamic estimate shows a smaller drop in revenue, because it captures the positive effect on the tax base of the reduction in the corporate income tax.

To analyze the sweeping changes in how business entities are taxed in Massachusetts, the Beacon Hill Institute (BHI) built a computable general equilibrium (CGE) model of the Massachusetts economy, called Massachusetts-STAMP (for state tax analysis modeling program). The purpose of the model is to answer questions about what would happen to the Massachusetts economy under a variety of hypothetical tax changes.[20]

Table 3 (previous page) presents our estimates of the static revenue effects in the first year from adoption of these tax proposals.[21] Here we assume that our proposals are adopted, effective January 1, 2009.[22]

Table 5. The Plan's Economic Effects, 2009-2013

	2009	2010	2011	2012	2013
Employment					
Private Jobs	4117	4217	4259	4300	4342
Government Jobs	(92)	(93)	(94)	(95)	(96)

[19] T. Bartik, "Who Benefits From State and Local Economic Development Policies?" (Kalamazoo, MI: Upjohn Institute, 1991).

[20] Detailed information about the Massachusetts CGE STAMP 07 model can be obtained by sending an e-mail to fconte@beaconhill.org or by visiting www.beaconhill.org.

[21] All data are 2004 Massachusetts Department of Revenue data. The estimate for combined reporting and the estimate for unitary tax principles were obtained from the Massachusetts "Study Commission on Corporate Taxation, Final Report," Dec. 28, 2007, p. 120. The estimates were inflated to 2009-2013 levels using the following method: We first calculated the ratio of the change in revenue due to the individual reform proposal to the total revenue collections for the appropriate tax (corporate, personal, and business property) in 2004. That ratio was applied to the Beacon Hill Institute projections of total revenue collections for corporate income, personal income, and business property taxes in fiscal 2009 through fiscal 2014. That provided the basis for our calendar-year estimates in Table 3.

[22] We could not obtain static revenue estimates for all of our proposals. It is our judgment that the revenue gains not captured by our estimates roughly offset the revenue losses.

Total Jobs	4025	4124	4165	4205	4246
Investment					
$ millions	119.73	126.38	133.39	140.79	148.61
Real disposable income					
$ millions	255.31	252.57	249.86	247.19	244.54

In 2009 the state loses $323.13 million from lowering the C corporation tax rate from 9.5 percent to 5.3 percent, and $21.55 million from eliminating the minimum corporate tax payment. However, the state gains $182.24 million from adopting combined reporting and unitary tax principles and $135.8 million from the elimination of incentive tax credits. The state would lose a net of $26.65 million from the reforms to the taxation of the businesses registered as C corporations.

The corporate tax reforms' effects on firms incorporated as S corporations also affect state tax collections. The expansion of the S corporation collections would produce an additional $47.16 million in tax revenue. The adoption of the unitary tax principles and the elimination of incentive tax credits would increase tax collections by $171.23 million. Those gains are offset by the elimination of the minimum tax collection, which would reduce collections by $39.55 million. On a net basis, reforming the corporate tax laws that apply to S corporations would increase state coffers by $178.84 million in 2009.

The state would also lose $264.45 million in 2009 from the elimination of the tax on tangible property and net worth levied on both C and S corporations. On a net static basis, the state would lose a total of $112.26 million under the reforms outlined above. However, as stated above, those static estimates fail to account for the economic and behavioral effects of the reforms solutions; thus, we need to estimate the dynamic revenues.

Table 4 presents dynamic tax revenue estimates. As expected, the tax changes would affect the revenue collection of state and local taxes. Under the plan, combined state and local tax revenues would decline by $79.11 million in 2009. The decrease would be caused primarily by the $106.48 million reduction in corporate excise tax collections. However, the economic stimulus created by the reforms would boost revenue collections for the sales and income taxes by $4.16 million and $4.38 million, respectively, and other revenue and fees by almost $11.09 million. The remaining state taxes would undergo gains of almost $1 million combined. Those estimates imply a difference of $26.37 million between the static and dynamic state revenue estimate, with the static estimate overstating the decrease in revenue collections.

Local government would see an increase of $6.78 million in their property taxes as businesses choose to locate more capital and labor in the state.

The dynamic tax revenue estimates are predictably smaller than the static estimates. In 2009, total tax revenue collections, including state and local government, would decrease by $79.11 million, $33.15 million less than the static estimate.

The above analysis shows how the push and pull of economic activity affect the revenue collections of the different taxes in place. We now consider the effects of the proposed tax changes on seven different economic indicators. Those effects are presented in Table 5 (previous page).

The first economic indicator we consider is employment. The number of private-sector jobs that otherwise would have been in place would increase, while the public sector would lose jobs. The decrease in the public-sector jobs would result from the decrease in the total revenue collected by the state government. With less revenue, the state would have to reduce expenditures. Under the reform, we estimate that in 2009 that would lead to the elimination of 92 government jobs in Massachusetts. However, the private sector would gain jobs as a result of the reduction in the tax rate on C and S corps and business property taxes. We estimate that the private sector would employ 4,117 more people in 2009 under our plan. The employment gains would lead to an increase of $255.31 million in total real disposable income in the state in 2009.

Investment would increase by $119.73 million in 2009 under the plan because the reduction in corporate taxation and the preferential treatment of capital goods would increase the funds available for investment within the state and attract more investment to Massachusetts from outside the state.

VI. Summary and Conclusions

The Massachusetts business tax code cries out for reform. If they are expected to be viable sources of revenue, business taxes must be reformed in a manner that promotes stability, economic growth, equity, simplicity, and transparency.

Massachusetts should strive for a predictable and competitive business tax policy that serves firms, investors, workers, and government in the most optimal manner. A uniform rate covering a broader base would provide a stable source of revenue and promote economic growth. All businesses would be treated with consistent, equitable tax policies that recognize that the investments those companies make in Massachusetts are catalysts for economic and job growth.

Adopting a business income tax rate of 5.3 percent, applied to all forms of business, would represent the kind of bold move that would attract new businesses and thus benefit all Massachusetts taxpayers.