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January 17, 2023

Honorable Laurie Sanborn, Chair
Honorable John Janigian, Vice-Chair
Ways and Means Committee
House of Representatives
Concord, NH 03301

Via E-mail

Re: COST's Opposition to H.B. 121, "Relative to Worldwide Combined Reporting for Unitary Businesses Under the Business Profits Tax"

Dear Chair Sanborn, Vice-Chair Janigian, and Members of the Committee:

On behalf of the Council On State Taxation (COST), we are writing in opposition to H.B. 121, legislation that would repeal the "water's-edge" combined reporting provision in New Hampshire's business profits tax and replace it with a mandatory worldwide combined reporting requirement. No other state in the United States or country in the world currently utilizes mandatory worldwide combined reporting to calculate corporate income taxes without alternative filing elections (*e.g.*, water's-edge reporting), and New Hampshire should reject this approach as well.

Moreover, this bill is premature as it would circumvent the State's commission studying worldwide combined reporting, which has not issued a final report yet.

About COST

COST is a nonprofit trade association based in Washington, DC. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce and today has an independent membership of over 500 major corporations engaged in interstate and international business. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities. Many COST members have operations in New Hampshire that would be negatively impacted by this legislation.

Shift to Mandatory Worldwide Combined Reporting Would Further Make New Hampshire an Outlier

Over the last three decades, the number of states adopting combined reporting

statutes has increased significantly, but none have chosen to utilize the mandatory worldwide combined reporting approach. All have adopted some form of water's-edge combined reporting (mandatory or elective). Generally, water's-edge combined reporting limits the determination of income subject to apportionment in a state to the income and apportionment factors of a group of unitary companies operating within the "water's-edge" of the United States. No state currently uses mandatory worldwide combined reporting that includes the income and apportionment factors of all domestic and foreign corporations in the state corporate income tax base (*e.g.,* New Hampshire's business profits tax) without also providing alternative filing elections.[1] Even the Multistate Tax Commission's model combined reporting statute includes a water's-edge election.

States have rejected worldwide combined reporting to avoid being out-of-step with other jurisdictions and to steer clear of the inequities and imbedded complexities of that approach. These include the potential for double taxation of foreign source income; the complexities of determining which foreign entities—sometimes numbering in the hundreds—are "unitary" with their domestic affiliates; and the accounting difficulties resulting from different exchange rates, foreign accounting methodologies and technology platforms utilized by foreign affiliates.

New Hampshire is already an outlier among the states in taxing a portion of foreign source income. New Hampshire is one of only a handful of states that taxes both 100 percent of foreign dividends (when repatriated to the U.S. parent corporations), and 50 percent of GILTI. While these deviations from the water's-edge combined reporting methodology are unfortunate policy choices, they stop short of discarding the water's-edge limitation and replacing it with mandatory worldwide combined reporting that would include all foreign source income in the business profits tax base.

Global Profit Shifting and State Corporate Tax Revenues

Over the last twenty years, many countries lowered their corporate income tax rates to incentivize businesses to locate and expand there. As the disparity between corporate tax rates imposed by various countries grew, policy makers at the international level became concerned with the increased use of global profit shifting – the artificial shifting of income and activity from high-tax jurisdictions to low-tax jurisdictions. Efforts to combat global profit-shifting have been underway at the Organization for Economic Cooperation and Development (OECD) for many years, culminating in its 2015 BEPS Project Reports recommending methods to address international "base erosion and profit shifting." During their deliberations, the OECD BEPS project considered, and rejected, the use of mandatory worldwide combined filing. Similarly, the current OECD Pillar 1 and 2 proposals for reforming international taxation steer clear of any consideration of mandatory worldwide combined filing.[2] Finally, the United States government, which adopted sweeping tax reform with the passage of the Tax Cuts and Jobs Act (TCJA) in 2017, moved away from its prior worldwide tax filing regime to a quasi-territorial tax system that includes a more limited taxation of foreign source income principally through the inclusion in the corporate tax base of 50 percent of global intangible low-taxed income (GILTI).

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[1] Alaska is the only state that mandates worldwide combined reporting, but only for oil companies.

[2] At the subnational level, only one country other than the U.S. among the world's 49 largest economies imposes a corporate income tax on any portion of foreign source operating income. *See* "Survey of Subnational Corporate Income Taxes in Major World Economies: Treatment of Foreign Source Income," prepared by PricewaterhouseCoopers LLP for the State Tax Research Institute, November 2019.

Many economic papers in recent years have contributed to these international tax reform efforts by attempting to quantify the global impact of profit shifting. Not surprisingly, the results of these studies vary dramatically, and each study contains disclaimers regarding the complexity, difficulty, and uncertainty of its conclusions.

Nevertheless, a recent report by a partisan think tank seized on the high point of these studies and extrapolated that number to individual states through a series of assumptions and estimates. It then presented those numbers to the states as "money left on the table" that is there for the taking if the state would only enact mandatory worldwide combined reporting. These estimates (and the report) should be viewed with great skepticism. Not only does the Institute on Taxation and Economic Policy (ITEP) report rely on highly generalized and problematic global tax data, but it makes no effort to customize its estimate to the laws of particular states.[3] Thus, in the case of New Hampshire, the study does not address the fact that the State already includes significant amounts of foreign source income in its business profits tax base through its taxation of 100 percent of foreign dividends (when repatriated to U.S. parent corporations), and 50 percent of GILTI through the State's conformity to the TCJA.

Finally, the ITEP report focuses solely on the New Hampshire business profits tax and does not reflect the level of or increases in other state and local taxes that businesses pay in New Hampshire, such as the business enterprise tax, the property tax, and miscellaneous other excises and taxes. For instance, in FY21, the latest year for which information is available, the business share of total state and local taxes in New Hampshire equaled 47.9%, compared to the national average of 43.6%. The business share of state taxes in New Hampshire totaled 62.7%, compared to the national average of 37.8%.[4]

House Bill 121 Is Premature

House Bill 121 also inappropriately circumvents the General Court's wishes to study worldwide combined reporting further, rather than hastily adopt worldwide combined reporting. On April 2022, H.B. 102 was enacted. House Bill 102 established a commission to study the worldwide combined reporting method. The commission will issue a final report of its findings and any recommendations for proposed legislation on or before November 1, 2023, and the commission has yet to issue its final report. House Bill 121, however, inappropriately sidesteps the commission and the process established by H.B. 102.

Conclusion

Mandatory worldwide combined filing is contrary to the approach to taxing corporate profits currently employed by all other states and nations with corporate income taxes. Its adoption would place New Hampshire at a competitive disadvantage among states and send a warning flag to multinational businesses that the State is a hostile environment for business expansion and relocation. New Hampshire's current water's-edge provision also serves not only as a practical limitation on combined reporting that reduces the incidence of double taxation and economic

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[3]Institute on Taxation and Economic Policy and U.S. PIRG, "A Simple Fix for a $17 Billion Loophole: How States Can Reclaim Revenues Lost to Tax Havens," Jan. 17, 2019, pp 17-18.
[4] "Total State and Local Business Taxes: State-By-State Estimates for FY21," prepared by Ernst & Young for the State Tax Research Institute (Dec. 2022).

distortion, but it also keeps the State within the conventional norms of business taxation. House Bill 121 is also premature considering the commission, established by enacted H.B. 102, is studying this issue. For the reasons stated above, COST respectfully opposes H.B. 121 and urges the members of the committee to reject it.

Respectfully,

Stephanie T. Do

cc: COST Board of Directors
Douglas L. Lindholm, COST President & Executive Director