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Chair James Eldridge
Joint Committee on Revenue

Via Email

Re: COST Opposes S.2041—Creation of a State "Tax Haven" Blacklist

Dear Chair Eldridge and Members of the Joint Committee on Revenue:

On behalf of the Council On State Taxation (COST), I respectfully submit this testimony in opposition to S.2041, a bill that would create a list of foreign jurisdictions in which a corporation is presumptively incorporated for purposes of avoiding Massachusetts's corporate excise tax. S.2041 would require corporate taxpayers to include affiliates incorporated in these jurisdictions ("tax havens") in their combined group income. COST has a long-standing policy position in opposition to state "tax haven" legislation. The "tax haven" blacklist approach is arbitrary, misleading, and fraught with constitutional infirmities. The approach is also completely out of step with the fundamental international tax reform addressing low-tax rate competition.

About COST

COST is a non-profit 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 approximately 500 major corporations engaged in interstate and international business, many of which directly do business in Massachusetts. COST's objective is to preserve and promote the equitable and non-discriminatory state and local taxation of multijurisdictional business entities.

State "Tax Havens": Misguided Tax Policy

The COST Board of Directors has approved a policy position opposed to all state "tax haven" provisions which provides in part:

> *State "tax haven" designations are arbitrary and overly broad, reflect a discarded "worldwide" approach to state taxation, and are inappropriate to address income shifting or other tax avoidance concerns. Punitive treatment of multinational businesses with affiliates in countries designated by states as "tax havens" interferes with the U.S. Government's ability to "speak with one voice" on foreign affairs and is constitutionally suspect. States should limit their income tax base to the domestic "water's-edge" and not tax foreign income with little or no connection with the United States.*[1]

[1] COST's policy position on this issue is available at: https://cost.org/globalassets/cost/state-tax-resources-pdf-pages/cost-policy-positions/cost-state-tax-haven-policy-statement-final-4-16-15.pdf.

In addition to the COST policy position, the State Tax Research Institute (STRI), an IRC 501(c)(3) research organization founded by COST, undertook a significant research project relating to state "tax haven" legislation. In 2016, STRI published its report entitled "State Tax Haven Legislation: A Misguided Approach to a Global Issue" that provides a detailed analysis of why states should not adopt "tax haven" legislation.[2]

State "Tax Havens": Detrimental Impact on a State's Economy

The blacklisting of foreign countries as "tax havens" and inclusion in the Massachusetts's tax base of income from businesses operating in these listed countries contravenes the approach taken by virtually all other U.S. states and nations in the world. Branding foreign nations as "tax havens" has been widely rejected as an arbitrary and illegitimate means for dealing with tax avoidance. The U.S. federal government has never adopted the "tax haven" approach as a means for defining its income tax base. More importantly, a "tax haven" provision will deter international businesses from locating or expanding their operations in Massachusetts, undermining the Commonwealth's ability to attract jobs and capital investment that would improve Massachusetts's overall economy.

State "Tax Havens": Arbitrary and Overly Broad Approach

Branding foreign nations as "tax havens" has been widely rejected as a legitimate means for dealing with tax avoidance. The "tax haven" lists are derived largely from a list created over 15 years ago by the Organization for Economic Cooperation and Development (OECD) to encourage countries to adopt greater transparency and information sharing about tax issues. It was not done to broaden the tax base of member countries. Presently, no countries remain on the OECD's list of uncooperative tax jurisdictions. Moreover, no country, including the United States, has ever adopted the "tax haven" approach as a means for defining their income tax base. Rather than providing a viable solution to the issue of foreign income sourcing, the adoption of a "tax haven" blacklist creates new problems by arbitrarily targeting sovereign nations.

More importantly, this legislation does not consider the significant progress made over the past decade by the OECD and G20 nations (including the United States) to implement fundamental international tax reform to address low-tax rate competition. The OECD/G20 project, commonly referred to as the base erosion and profit-shifting project or BEPS, is one of the most ambitious international tax projects ever undertaken. BEPS was initiated in 2013 to address concerns over profit shifting and to limit the capacity of large multinational companies to move intangible assets around the world to take advantage of more-favorable income tax rates and rules in low-tax jurisdictions. Most recently, 137 of the 141 countries and jurisdictions participating in BEPS, including the United States, agreed to implement a global minimum tax of 15% with the goal of eliminating or drastically reducing profit shifting and global low-tax rate competition.[3]

State "Tax Havens": Foreign Commerce Clause Concerns

Given the recent progress to reform the international corporate tax system and the United States' participation in that process, state "tax haven" legislation warrants heightened scrutiny for violation of the Foreign Commerce Clause. The constitutional standard set forth in *Japan Line, LTD v. County of Los Angeles*, 441 U.S. 434 (1979), is clear: state tax measures may not impose a risk of multiple taxation at

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[2] Karl Frieden and Ferdinand Hogroian, State Tax Haven Legislation: A Misguided Approach to a Global Issue, State Tax Research Inst. (Feb. 2016), https://www.cost.org/globalassets/cost/state-tax-resources-pdf-pages/coststudies-articles-reports/state-tax-haven-legislation--a-misguided-approach-to-a-global-issue.pdf.
[3] OECD, *International Collaboration to End Tax Avoidance*, https://www.oecd.org/tax/beps/.

the international level and may not prevent the federal government from "speaking with one voice" on international policy matters.

Many of the jurisdictions targeted by the S.2041 "tax haven" legislation have already adopted the 15% global minimum tax[4]. By requiring the income of affiliates incorporated in those jurisdictions to be included in a Massachusetts combined group's taxable income, this bill potentially subjects those taxpayers to multiple taxation in violation of the Foreign Commerce Clause. In effect, by penalizing taxpayers for conducting business in specific countries, Massachusetts risks running afoul of constitutional limits on state taxation of foreign commerce.

Conclusion

COST respectfully urges you to veto S.2041, which would create a "tax haven" blacklist, that would significantly worsen Massachusetts's business climate and will certainly have the opposite effect of raising revenues by potentially involving the Commonwealth in costly litigation.

Sincerely,

Leonore F. Heavey

cc: COST Board of Directors
Patrick J. Reynolds, COST President & Executive Director

[4] https://www.oecd.org/en/topics/sub-issues/global-minimum-tax/central-record-of-legislation-with-transitional-qualified-status.html#qdmtt-rules-safe-harbours