Testimony of Jeff McLynch,
Executive Director, New Hampshire Fiscal Policy Institute,
Before the House Finance Committee
Regarding the FY 2016-2017 Budget
March 5, 2015

Chairman Kurk, Members of the Committee, thank you for the opportunity to appear before you today.

For the record, my name is Jeff McLynch and I am the Executive Director of the New Hampshire Fiscal Policy Institute. NHFPI is an independent, nonpartisan, nonprofit organization dedicated to exploring, developing, and promoting public policies that foster economic opportunity and prosperity for all New Hampshire residents, with an emphasis on low- and moderate-income families and individuals.

I am here this afternoon to express NHFPI's support for two key elements of Governor Hassan's FY 2016-2017 budget proposal.

First, NHFPI commends the Governor for acknowledging the chief source of New Hampshire's fiscal challenges – the failure of its revenue system to recover from the last recession – and for offering multiple recommendations to begin to address it. In so doing, her budget proposal is better able to preserve valuable investments in higher education and other areas critical to the state's economic future.

To expand on this point, at the close of FY 2014, General and Education Fund revenue amounted to \$2.17 billion. After adjusting for inflation, that sum is approximately 12 percent or roughly \$290 million less than what the state collected from the same sources in FY 2008. Key sources of tax revenue have seen even steeper declines in recent years. For instance, between FY 2008 and FY 2014, New Hampshire's twin business taxes – the business profits tax and the business enterprise tax – have dropped almost 20 percent or just over \$136 million. Over the same span, the interest and dividend tax has fallen by \$52 million or roughly 39 percent on an inflation adjusted basis.

Moreover, in the absence of policy changes, it seems unlikely that this trend will soon be reversed. Both the baseline revenue estimates for FY 2016-2017 included in the Governor's budget and those affirmed by the House of Representatives in the form of HR 12 would leave General and Education Fund revenue below FY 2008 levels on an inflation-adjusted basis.

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This failure to rebound stems both from recent changes in tax policy that have drained millions of dollars out of the state budget and from long-standing flaws in New Hampshire's tax system that perpetuate the state's fiscal woes. Governor Hassan's budget proposal attempts to respond to both sources. With regard to the former, her budget proposal would largely undo changes, enacted in 2011, relating to the reasonable compensation deduction under the business profits tax (BPT); such changes appear to have led to a roughly 18 percent increase in the size of that deduction between tax years 2010 and 2011 and a significant loss of revenue for the state.

In the case of the latter, her budget proposal includes provisions designed to limit New Hampshire's current vulnerability to international tax planning by instituting a common-sense reform now in place in several states. Such provisions would require companies subject to the BPT to report the income they realize in roughly 30 nations recognized as international tax havens, such as the Bahamas and the Cayman Islands, and to include such income in determining the amount of tax they owe.

Recent research by the US Public Interest Research Group (PIRG) finds that the aggregate revenue loss states are experiencing due to such vulnerabilities is substantial, draining away as much as $1 billion annually in just the 22 states and District of Columbia that, like New Hampshire, use combined reporting as part of their corporate income taxes.[i]

Likewise, a May 2014 analysis conducted by Citizens for Tax Justice (CTJ) of the 10-K filings Fortune 500 companies have submitted to the US Securities and Exchange Commission reveals that 300 of those entities have disclosed holding some of their income as "permanently reinvested" offshore profits. As of 2013, those reinvested profits totaled $1.95 trillion. More to the point, CTJ's analysis finds that, while 243 Fortune 500 companies declined to disclose the US tax rate they would pay on such income, at least 28, including Hertz, Bank of America, and Wells Fargo, have likely shifted profits to tax havens.[ii]

Such findings are in keeping with research conducted by Jane Gravelle of the Congressional Research Service. In a January 2015 study, she writes that "ample evidence of a significant amount of profit shifting exists" and calculates the profits US companies reported in various countries as a percentage of those countries' gross domestic product (GDP) in 2010. As one might expect, those percentages are quite low in large industrialized nations such as France or Germany. In some smaller countries generally considered tax havens, however, US companies' foreign profits amounted to several multiples of GDP. For example, US companies' foreign profits equaled 2066 percent of GDP in the Cayman Islands and 1614 percent of GDP in Bermuda that year.[iii]

In considering the potential impact of these provisions, it is important to note that they would not subject businesses operating in New Hampshire to a new tax, nor would they increase the number of businesses subject to the BPT. Rather, they simply take a step toward ensuring that those companies now subject to BPT that have operations overseas cannot use those operations to artificially reduce their New Hampshire tax liability. As a result, these provisions would create a more level playing field between small, locally-owned businesses that have neither the capacity nor the desire to avail themselves of such tax planning techniques and those large multinational corporations that currently employ them to their advantage.

Second, the Governor's budget proposal would extend the New Hampshire Health Protection Program beyond its currently scheduled termination date of 2016, providing greater certainty for Granite State workers, health care providers, and others, while maintaining fiscal protections originally included in the legislation creating the program.

As the Committee knows well, the Health Protection Program allows New Hampshire to access federal funds to provide affordable health insurance coverage to thousands of low-income Granite Staters. More than 35,000 people have already enrolled in the program, which, in turn, will bring more than $200 million in federal funds into the New Hampshire economy in the current fiscal year alone. Information recently presented by the Department of Health and Human Services to the Finance Committee suggests that the flow of federal funds will swell to more than $400 million annually or in excess of $800 million in the FY2016-17 biennium.

Data released earlier this week by the New Hampshire Hospital Association suggest that the Health Protection Program is already yielding real benefits. More specifically, a survey of the Association's membership reveals that, while overall inpatient admissions, emergency room visits, and outpatient services have been roughly stable between 2013 and 2014, there have been substantial declines in these areas among the uninsured, thus reducing the amount of uncompensated care local hospitals have had to provide. Moreover, extensive research demonstrates that affordable health insurance coverage, such as that available through the Health Protection Program, improves not just physical and mental health, but also enhances financial security and workplace productivity over the longer term.

Of note, while the Governor's budget proposal would ensure that the Health Protection Program would continue beyond 2016, it nevertheless keeps in place statutory provisions that would repeal the program in the event that federal matching percentages (which will range between 95 and 90 percent over the next several years) should fall below the levels currently stipulated in law.

Finally, as the members of the Committee are no doubt aware, a great deal of attention has already been paid this year to efforts to reduce the rates of the business profits tax and the business enterprise tax. In fact, the other body, earlier today, voted on two measures that, taken together, would ultimately reduce state revenues by more than $40 million per year. However, the Governor's budget proposal demonstrates quite clearly that New Hampshire simply cannot afford costly and ineffective business tax cuts at a time when revenues remain insufficient to address critical needs. Consequently, I urge the Committee to reject any attempt to use the FY 2016-2017 budget to lower business taxes, either now or in the future.

Again, I thank you for the opportunity to testify this afternoon and would be happy to try to answer any questions you may have.

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[i] Baxandall, Phineas, et. al., *Closing the Billion Dollar Loophole: How States Are Reclaiming Revenue Lost to Offshore Tax Havens*, U.S. Public Interest Research Group, Winter 2014.
[ii] Citizens for Tax Justice, *Dozens of Companies Admit Using Tax Havens: Hundreds More Likely Do the Same, Avoiding $550 Billion in U.S. Taxes*, May 19, 2014.
[iii] Gravelle, Jane, *Tax Havens: International Tax Avoidance and Evasion*, Congressional Research Service, January 15, 2015.