February 18, 2021

Re: H.F. 991, Governor's tax bill

Chair Marquart and members of the House Tax Committee,

Thank you for the opportunity to testify today on Governor Walz's tax proposal. I am submitting written comments in addition to my verbal testimony today on behalf of the Minnesota Chamber of Commerce. The Minnesota Chamber is a statewide organization representing more than 6,300 businesses – and more than half a million employees – throughout Minnesota. The majority of our members are small and mid-sized businesses.

First, the message we carry on behalf of our members this session is clear: Minnesota's economic recovery from the COVID-19 pandemic must be the top priority for the 2021 Legislative Session. Re-opening the economy and managing the continued economic fallout due to the pandemic is one of the top concerns of Minnesota businesses. A "do no harm" approach is critically important so that additional cost burdens and mandates are not placed on employers who are doing their best to keep their doors open and people employed.

We strongly oppose Governor Walz's $1.6 billion in new taxes impacting private sector employers of all sizes while they continue to grapple with the impacts of the COVID19 pandemic. Many of these taxes are regressive, extremely volatile and will greatly harm Minnesota's business climate and economic growth by undermining investment, entrepreneurship, talent recruitment and retention. Minnesota is already known as a high cost state and this will worsen our competitiveness. We oppose the following proposals:

- The corporate tax rate increase to 11.25% would bring Minnesota's rate to ***highest in nation*** with a 15% increase in corporate taxes impacting over 34,000 corporate tax filers including many small businesses. New Jersey, which is currently highest nationally, has a temporary surcharge on their corporate rate. As soon as that temporary rate is discontinued, Minnesota would take the top ranking. The corporate tax has been found in numerous economic studies to negatively impact investment, entrepreneurship and economic growth. Ultimately it harms Minnesota consumers and employees, per the Minnesota Department of Revenue study, which says the long-run incidence impact of a change in Minnesota business taxes would tend to fall less on nonresidents, less on Minnesota owners of capital, and more on Minnesota consumers and workers.

- The new 5th tier rate of 10.85% would bring Minnesota's tax rates to the ***third highest in the nation*** just behind California and Hawaii. This tax increase would hit many pass-through business entities of all sizes. The vast majority - 92% of Minnesota's businesses - are pass-through entities, including its smallest and newest companies. These businesses "pass through" business income to the owner's personal income tax return making the personal income tax just as important to Minnesota's business climate as the corporate tax. Pass-through income is taxed even if it is retained within the business for reinvestment. Studies have found that high marginal income tax rates detrimentally impact business investment decisions, entrepreneurial activities, and recruitment of talent – the very items needed for economic growth.

- A capital gains surcharge of 1.5% and 4% bringing Minnesota's rate to the ***highest in the nation*** at 14.85%. This would negatively impact investment and attraction of capital to Minnesota. It would harm many small businesses, farmers and individuals that may have a one-time sale of an asset. Many times the capital gains is illusory as the gain is from inflation that would now be penalized with a hefty tax. The average and median top capital gains rates in the 40 states that tax capital gains is about 6%.

- The taxation of foreign income would impact Minnesota-based headquarter companies and put them at a competitive disadvantage with their foreign competitors. Minnesota's success relies greatly on the ability of our businesses to compete in the international marketplace, both through the ability of our businesses to sell abroad and to attract investment into Minnesota. It is important for Minnesota to <u>not</u> be a tax outlier for international taxation. This retroactive tax raises serious constitutional concerns as well as brings into question the stability and reliability of Minnesota's tax laws.

- The sales tax change for qualified data centers undermines the state's integrity by going back on an economic development incentive that businesses had in good faith relied on when deciding to invest in data centers in Minnesota. Companies were certified by Minnesota Department of Employment and Economic Development, invested hundreds of millions of dollars in building these facilities in reliance on the economic development tax incentives that were promised.

- Estate tax law change moving back to a $2.7 million threshold will make Minnesota's estate even more of an outlier. Most states do not impose this tax. This tax hits many family businesses and farms that may have a high value but also have assets that are not liquid, so paying taxes can become a serious problem. The estate tax, plus the high individual income tax, creates an unfortunate incentive for more affluent Minnesotans to change their permanent residences or not move to our state resulting in a loss to our communities, our tax base and our economy.

The Governor's bill would add great uncertainty and instability to state's budget by relying on the most volatile revenue sources for permanent spending increases – corporate taxes, capital gains and the new 5th tier. According to a 2015 presentation by Minnesota's state economist, the corporate income tax is the most volatile of the revenue sources, extremely sensitive to economic cycles and thus subject to great uncertainty. The volatility of corporate tax is almost 2 ½ times greater than individual income tax and 5 times greater than sales tax. Capital gains, with a volatility measure of 44.2 percent, is the most volatile tax base component. Capital gains by their very nature are very volatile as it is up to the taxpayers to determine when they sell.

We also have concerns with the increased cigarette tax as Minnesota's tax is already much higher than all surrounding states and this has resulted in increased smuggling and harmed retailers legally selling these products. We do support the angel tax credit and additional business grants contained in the Governor's budget. But, we were deeply disappointed the Governor did not include any federal tax conformity including PPP loan program which will result in a tax hit in Minnesota for this federal lifeline provided to small businesses to help retain employees during the great uncertainty and losses caused by the COVID-19 pandemic.

We look forward to working with you to advance a pro-growth tax and budget proposal that will focus on Minnesota's economic recovery and not undermine Minnesota's competitiveness and private sector employers.

Sincerely,
Beth Kadoun, Vice President, Tax and Fiscal Policy
Minnesota Chamber of Commerce