

New tax law draws fresh fire from pharma

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State and national industry organizations are pushing to change a tax law that has ensnared foreign life sciences companies operating in Massachusetts. The so-called “combined reporting” tax law requires corporations to file a combined report to Massachusetts tax authorities, forcing many to include income generated outside the state.

The law’s goal is to discourage companies from locating part of their businesses in low-tax states, such as Delaware, to avoid paying Massachusetts taxes. But the law also applies to companies with both foreign and domestic operations.

All of the other approximately 20 states that have enacted similar laws also have included a “water’s edge” provision, which means that overseas companies would be excluded.

But the Massachusetts law is vague and the **Department of Revenue** has interpreted it in the broadest possible sense, critics say. DOR representatives declined to be interviewed for this article but issued a statement saying, “the general purpose of this provision in the statute is to prevent the income of a U.S. combined group from being reduced by royalty or interest payments to overseas affiliates.”

The law was enacted in January and regulations were just finalized in June. Foreign companies just began feeling the pain — or at least the administrative nuisance — when they filed their second quarter estimated tax payments.

All industries are affected by the law, but backers of the state’s life sciences industry are particularly concerned that it could undermine the state’s heavily promoted efforts to recruit companies. Internationally headquartered pharmaceutical companies, including U.K.-based **Shire PLC**, France-based Sanofi Aventis, Switzerland-based **Novartis**, U.K.-based **AstraZeneca** and EMD Serono, the U.S. arm of Switzerland-based **Merck Serono SA**, have operations in Massachusetts. So do medical-device companies such as Ireland-based **Covidien** and U.K.-based Smith and Nephew PLC.

“We keep saying that life sciences is going to be the savior of the state and then we slap them any chance we get,” said Eileen McAnneny, senior vice president at the **Associated Industries of Massachusetts**. She said the new tax law is the latest in a long list of government actions, including the enactment of the gift ban restricting big pharma’s relationships with doctors, that sharply raise the “hassle-factor” of doing business in Massachusetts.

McAnneny and other industry insiders say that while no companies have so far threatened to leave, the full impact of the bill hasn’t been felt yet.

McAnneny said that’s why it needs to be changed by year’s end, when companies will reconcile their estimated and actual tax liabilities. AIM and others have been working on

an amendment, House Bill 2694, that would exempt foreign companies from the law. The bill is currently waiting for action by the Joint Committee on Revenue before it can be voted on by the full Legislature.

The local effort to amend the law is being aided by the national lobby group the **Organization for International Investment**. The national outfit estimates that over 173,000 Massachusetts residents work for foreign companies across all industries.

“When a state unilaterally enacts a law that goes in the opposite direction of international tax norms it doesn’t just close the window on future international investment, it pulls down the shades and closes the shutters,” said Nancy McLernon, president of the Organization for International Investment.

Lawmakers won’t be taking up legislation in earnest until the middle of September, but advocates of the bill hope it can move forward soon after that. While there’s strong momentum behind the amendment, it could face some push back.

“We’re in a climate where anything that has revenue implications is difficult to change,” said Joe Donovan, a lawyer for Sullivan and Worcester. Donovan testified before the Joint Revenue Committee on behalf of the **Massachusetts Biotechnology Council** last month in support of the amendment to the combined reporting law. But Donovan said that the DOR’s decision to interpret the law broadly to capture more tax revenue might not bear fruit. One reason: If the Massachusetts portion of the company is profitable, but an overseas part is not, it could actually lower the Massachusetts tax liability.

Democratic state Rep. Ronald Mariano said that many lawmakers, himself included, did not fully appreciate the impact the 77-pages of regulations would have on foreign companies with operations in Massachusetts. He was first made aware of the problem by EMD Serono while working with the drug company on a separate issue. The problem was further driven home as he and other local lawmakers began recruiting **Stop & Shop** to locate its headquarters in Quincy. Stop & Shop is owned by Netherlands-based Ahold.

“We have to deal with this. It’s so easy these days for companies to pick up and move. We don’t want to give them any reason to do that,” Mariano said.