

**Senate Finance Committee Hearing
Testimony for Mike Cortez
Vice President and General Counsel
Sheetz, Inc.
May 26, 2010**

Good morning Chairman Browne, Chairman Ferlo, and esteemed members of the Senate Finance Committee. My name is Mike Cortez, and I am Vice President and General Counsel for Sheetz Inc. Joining me today is Gene Barr, Vice President of Government and Public Relations for the PA Chamber of Business and Industry.

Headquartered in Altoona, PA, Sheetz, Inc. is a family owned business with more than 13,000 employees operating 371 convenience stores in 6 different states. In this Commonwealth alone, we have more than 201 stores, a large distribution center, an industrial kitchen and our corporate headquarters. One of the things we're most proud of is that we employ nearly 8000 of our fellow Pennsylvanians.

Most of you are probably aware that Sheetz's top legislative priority is to change Pennsylvania's antiquated liquor code laws to allow us to sell beer in our convenience stores, as is permitted in nearly every state in the nation, including the other five states in which we actually sell beer in our stores. Setting aside my encouragement for this legislative body to consider consumer-friendly SB 1300, today I'm here to talk about another issue of importance to Sheetz, as well as the business community in general – combined reporting.

In 2004, I served as the Chamber's representative to Governor Rendell's Tax Reform Commission. Created by Executive Order number 2004-3, the purpose of the Tax Reform Commission was to "evaluate the current business tax structure in this Commonwealth and recommend changes in the Commonwealth's business tax structure that will broaden those tax bases, thereby allowing rates to be reduced, leveling the playing field, and creating a fairer business tax climate." Not only did the Order limit the scope of our work and establish a predetermined direction for our deliberations, but it also required that the Commission's recommendations "ensure revenue neutrality." In essence, the Executive Order charged the Commission to develop recommendations that merely shift tax liability among businesses without truly improving Pennsylvania economic competitiveness.

It was under these guidelines that the Tax Reform Commission met over several months, heard testimony from dozens of interested parties, analyzed numerous studies, reports and data and engaged in countless corporate tax-related discussions. In the end, the Commission made a comprehensive set of proposals that were to be considered as a total package and not as individual recommendations. The package the Commission recommended included the following components:

- Lower the corporate net income tax (CNIT) rate to between 6 and 7 percent (although I argued and maintain that the rate should be below 6%, specifically to help offset the negative implications of combined reporting);

- Implement mandatory unitary combined reporting;
- Establish a single sales factor for CNIT apportionment purposes;
- Utilize market-based sourcing for the sale of services (i.e. sources the sales of services in the same manner as sales of tangible property);
- Prospectively remove the cap on net operating losses;
- Impose a net 1% entity level tax on pass through businesses, raising their tax liability from 3.07% to 4.07% of federally reported net income;
- Continue the scheduled phase-out of the capital stock and franchise tax (CSFT);
- Reform Pennsylvania's tax appeals process.

Over the last several years, I have been frustrated by the characterization from others that combined reporting was recommended by the Governor's Tax Reform Commission and therefore should be implemented in Pennsylvania. As pointed out, combined reporting was one of a series of recommendations that are part of a delicately balanced package. I can tell you that there was significant discussion and agreement by the Commission members to this end, and in fact, the final report clearly states, "The Commission endorses the tax recommendation contained in this plan as a package; it does not endorse any of the recommendations individually except the recommendations on the improvements to the tax appeals process."

To further emphasize my point, on combined reporting itself, the report specifically says, "The Commissioners believe that an acceptable solution would be combined reporting, provided that it is enacted together with the other reforms discussed herein." Again, any and all references pertaining to the Commission's recommendations as a reason or excuse to support combined reporting are not only erroneous, but they represent an affront and disservice to the fourteen extraordinarily capable individuals who volunteered their time and effort to this Commonwealth.

With that said, I admit to being one of several vocal detractors on the Commission throughout the countless discussions we had on combined reporting. As I stated in my commentary under Tab 24 of the Commission's Final Report, I believe combined reporting is unfriendly to business and could drive investment away from the Commonwealth.

As you have heard and will hear from others today, there are a number of legitimate institutional, administrative and substantive concerns pertaining to the adoption of a combined reporting system. We know from the testimony and Commission deliberations that it is such a complex system that combined reporting continues to pose challenges and shortcomings in states that have decades of experience with it. We also know that combined reporting would be costly for Department of Revenue to implement, it would lead to a significant upturn in litigation for the Commonwealth, and, its adoption would actually lead to a LOSS in revenue for the first two or three years of implementation. While I defer to the other experts who are here today to discuss substantive concerns more specifically, I can tell you that combined reporting is NOT the panacea of corporate tax systems as proponents would have you believe.

The last thing I will mention before opening up to questions for Gene and me, is that one of the most glaring shortcomings during the Commission's deliberations was the reliance on static modeling and the lack of dynamic modeling as we evaluated various tax policy changes. Dynamic modeling, while somewhat subjective, could have provided the Commission critical insight into the potential impact that the various policy changes under consideration would have had on other aspects of the economy. For example, certain tax policies might stimulate economic growth (i.e. additional jobs, income, consumer activity, etc.) while others might hinder the economy. The effect of such changes might increase or decrease corporate tax revenues or tax revenue from other sources (i.e. PIT, Sales). Absent this type of data and insight, it was impossible for the Commission to make full-informed decisions as we developed our recommendation.

To conclude, I want to be clear that the Tax Reform Commission did not and would not support the adoption of combined reporting without the adoption of the other provisions contained in the final report. Even with the other provisions, several of us on the Commission maintained reservations over such a system of corporate tax reporting and believe that the corresponding CNIT rate reduction was not significant enough to offset combined reporting. We were, however, significantly limited by the scope of the Executive Order and the lack of time and opportunities to further explore other tax policy issues and the dynamic affects of the various policy changes. In fact, I would argue that combined reporting as a Commission recommendation was driven by the Commission's limited parameters – That is, the Executive Order's dictate to look at only the CNIT and the CSFT, the requirement of revenue neutrality, the relatively short time frame to fully consider all tax policy issues and the lack of dynamic economic modeling to determine long-term impact of policy changes.

With that, I thank you for the opportunity to testify and I welcome any questions you might have.