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Three Progressive Tax Policies to Help Small Businesses in Massachusetts

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Our Commonwealth celebrates small businesses as a way for ordinary working people to build wealth and pursue a productive life more independent from the large corporations that dominate our economy and society.

Proposals for corporate tax cuts often claim their aim is to help small businesses, even when most of the benefit would go to large corporations. For instance, after decades of paying contribution rates to the Commonwealth's unemployment trust fund that were below federal standards, many big business groups have lobbied to use public funds to relieve this debt in the name of "helping small business." Many small businesses, however, are sole proprietorships that rarely have employees for whom they pay unemployment taxes. Although there are many small businesses that do have employees, 96 percent of Massachusetts payroll is in companies with annual revenue over $1 million.[1]

Key Takeaways

- Tax policy proposals often claim to be for helping small business, even when most of the benefit would go to large corporations.
- Tax policies to help small businesses should be narrowly targeted to those that are truly small-scale. Policies should avoid reducing public revenues which support investments that small businesses need to thrive.
- Municipalities can enact the *small commercial entity exemption,* which reduces property taxes for the smallest companies. The difference is paid by companies with higher property valuation.
- Massachusetts can expand the payroll tax wage base used to calculate unemployment taxes. Companies with lower wage workers—generally in smaller companies and in lower-income communities—won't pay taxes on a disproportionately greater share of their employees' wages than do bigger corporations.
- The minimum corporate income tax should be tiered to have a similar impact on large companies as on small ones.

All businesses in the Commonwealth depend on public investment in programs and infrastructure that ensure a well-educated workforce, reliable and far-reaching transportation networks, public health, dependable court systems, and other public functions. These systems may be especially important for smaller businesses, which can't create their own distribution networks, training programs, childcare centers, etc. State policies such as those in the Black Mass Coalition Blueprint for a New World are examples of investments well-targeted to help BIPOC entrepreneurs.

Tax policies that aim to help small businesses should substantially raise revenue from the highest income taxpayers, such as the Fair Share Amendment, or be narrowly targeted to small businesses while avoiding reduction of overall public revenues. This paper explores three examples of how policymakers can increase the share of business taxes paid by larger corporations in order to reduce the share paid by small companies and to provide more of the public investment that small businesses need to thrive. Examples are from local property tax policy, employer payroll taxation, and corporate income taxation.

Every year, each city and town government chooses how to configure their property taxes. Each municipality annually chooses whether or not to offer the **small commercial entity property tax exemption** or whether to deny the option. The policy exempts from taxation up to 10 percent of a commercial/industrial property that is valued at $1 million or less with average employment of no more than ten persons.

This policy might typically assist small businesses like a shop, gallery, small farm, landscaper, or local gas station. According to the Commonwealth's Division of Local Services, "the option shifts the tax responsibility from parcels occupied by small businesses to those occupied by other commercial and industrial taxpayers" in that city or town.

Despite overwhelming support voiced for small "mom and pop" businesses, only 14 of Massachusetts' 351 municipalities chose this option in Fiscal Year 2021.[2] If municipalities want to encourage small businesses, they can choose this option with little appreciable impact on large business and no reduction of revenue. Business owners of color are more likely to have smaller businesses, so the policy can also promote racial equity through wealth building over time. The Legislature could also further encourage municipalities by updating the law to allow cities and towns to set the threshhold at a higher maximum amount.

Likewise, smaller companies and those in less affluent communities would generally be helped by **expanding the wage base on which employers pay unemployment insurance taxes**. For years, Massachusetts employers have contributed payroll taxes by applying the tax rate only to the first $15,000 of each worker's wages. The size of the wage base doesn't affect how much total unemployment taxes are collected, but it does affect how they are distributed among businesses. In order to raise sufficient revenue for the state unemployment insurance system on a narrower tax base, a higher tax rate must then be applied to the base. As a result, smaller businesses and those in poor communities, which tend to pay lower wages, end up paying unemployment insurance taxes on a larger percent of their employees' wages. Larger

The Low $15,000 Wage Base for Unemployment Insurance Tends to Disadvantage Smaller Businesses

Consider a company with workers who are paid an average of $30,000. This most likely smaller company would pay unemployment insurance taxes on the first $15,000 of each employee. Taxes are thus applied to *half* ($15,000/$30,000) of wages. Compare this to another likely-larger company that pays employees an average of $150,000. They also pays taxes on the first $15,000 of each employee's wages. The tax is only applied to *10 percent* ($15,000/$150,000) of their employees' wages. The tax has a relatively larger impact on the smaller company.

corporations, which tend to pay higher wages, pay taxes on a smaller share of their employees' wages and are indirectly subsidized by the current system. Massachusetts could raise the base amount and adjust it annually for inflation, as 16 other states do. Washington state's taxable wage base is $52,700 and four other states set theirs above $40,000. The Commonwealth could alternately eliminate the taxable wage base altogether and apply a far lower tax rate on workers' full wages. Any of these changes would spread payroll collections across a wider base and thereby decrease the rates paid on those wages, while making it easier to restore long-term solvency to the state's unemployment insurance trust fund.

There are other ways to increase public revenues from larger corporations without increasing taxes on small businesses. One way is to **create a tiered structure for the corporate minimum tax**. For decades, all businesses have paid a $456 minimum corporate income tax, a backstop that ensures every business pays some taxes. Roughly three-quarters of all businesses pay this amount. For a truly small business, this backstop may represent a small but consequential amount. But many multi-billion dollar corporations also pay this tiny sum. For them, the tax may be no more than a rounding error on their weekly catering expenses. The lack of scaling up this minimum creates an unlevel playing field because this minimum tax impacts business decisions only for the smallest businesses. Massachusetts should follow several other states in adding tiers for a more meaningful minimum rate on larger corporations. The Massachusetts House passed such a policy in 2020 as part of a transportation financing bill that was not voted on by the Senate.

Public revenue is crucial both to sustain public infrastructure and programs like roads, courts, schools, and childcare that help small businesses thrive, and for more targeted help for communities with obstacles to small business success. For instance, a state bank could provide targeted loans that help small businesses, such as those owned by people of color, to obtain easier access to capital.

Policies can best help small business when they are very clear about closely targeting benefits to companies that truly are small-scale, by ensuring that public revenues that support the whole economy are not diminished, and by focusing on areas like childcare, worker training, access to public procurement contracts, and access to financing which are especially difficult areas for the smallest businesses.

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Endnotes

[1] According to the U.S. Census' American Business Survey, a national survey of all majority owners of any business with annual receipts of $1,000 or more. See U.S. Census, 2019 Annual Business Survey (ABS) for the 2018 reference year.

[2] Division of Local Services, Commonwealth of Massachusetts, "Splitting the Difference: Reviewing Tax Rate Shifts," *City and Town*, August 2021, p.4.