SB 248

Department of Legislative Services

Maryland General Assembly
2012 Session

FISCAL AND POLICY NOTE

Senate Bill 248 (Senators Jones-Rodwell and Montgomery)
Budget and Taxation

Taxation of Corporations - Alternative Minimum Assessment

This bill imposes an alternative minimum assessment for certain corporations. The alternative minimum assessment is based on the gross receipts or gross profits of a corporation. Corporations are required to pay an alternative minimum assessment in the amount by which the assessment exceeds the corporate income tax liability for the taxable year. The bill provides that corporations that are subject to the assessment can claim these liabilities against future corporate income taxes under specified circumstances.

The bill takes effect July 1, 2012, and applies to tax year 2012 and beyond.

Fiscal Summary

State Effect: General fund revenues increase beginning in FY 2013 due to additional revenues from the alternative minimum assessment. Transportation Trust Fund (TTF) revenues and Higher Education Investment Fund (HEIF) revenues increase beginning in FY 2013. General fund expenditures increase by $220,000 in FY 2013 due to administrative expenses at the Comptroller's Office.

Local Effect: Local highway user revenues distributed from the corporate income tax will increase beginning in FY 2013. Local expenditures are not affected.

Small Business Effect: Minimal.

Analysis

Bill Summary: Beginning in tax year 2012, corporations are subject to an alternative minimum assessment (AMA). This assessment is based on two methods, either a gross receipts method or a gross profits method. Corporate taxpayers are required to select either the gross receipts or gross profits assessment method. Once the election has been made, the corporation must use this method to calculate the AMA in the next four tax years. After the first five years, a corporation may elect to switch methods. After any switch, however, the corporation must use the method for five successive tax years.

For any taxable year, if the calculation using either the gross receipts method or gross profits method results in an AMA that exceeds the State income tax, then an AMA must be paid. The AMA is equal to the amount by which the AMA exceeds the State income tax for the taxable year. The AMA for a corporation may not exceed $5.0 million, or $20.0 million if five or more corporations are members of an affiliated group.

The bill provides that if the State income tax for a corporation in any tax year exceeds the AMA for that tax year, a corporation may claim a credit equal to the amount of the AMA tax imposed in any previous taxable year. This credit can be carried forward indefinitely until the full amount of the credit is used. In any tax year, however, the amount of the credit cannot exceed the lesser of (1) the amount by which the State income tax exceeds the AMA; or (2) 50% of the State income tax.

Current Law/Background: A corporate income tax rate of 8.25% is applied to a corporation's Maryland taxable income. In general, the Maryland corporate income tax is computed using federal provisions to determine income and deductions.

Every Maryland corporation and every corporation that conducts business within Maryland, including public service companies and financial institutions, are required to pay the corporate income tax. The tax base is the portion of federal taxable income, as determined for federal income tax purposes and adjusted for certain Maryland addition and subtraction modifications, that is allocable to Maryland. Federal taxable income for this purpose is the difference between total federal income and total federal deductions (including any special deductions). The next step is to calculate a corporation's Maryland taxable income. The Maryland taxable income of a corporation that operates wholly within the State is equal to its Maryland modified income. Corporations engaged in multistate operations are required to determine the portion of their modified income attributable to Maryland, based on the amount of their trade or business carried out in Maryland. Corporations are generally required to use either a three-factor apportionment formula of payroll, property, and sales, with sales double weighted or, in the case of a manufacturing corporation, a single sales factor formula. The apportionment factor is then multiplied by the corporation's modified income to determine Maryland taxable income. The Maryland tax liability of a corporation equals the Maryland taxable income multiplied by the tax rate, less any tax credits.

Maryland is a "unitary business" state, in that a corporation is required to allocate all of its Maryland income (that portion that is "derived from or reasonably attributable to its trade or business in the State") attributable to the corporation's "unitary business." Essentially, a unitary business exists when the operations of the business in various locations or divisions or through related members of a corporate group are interrelated to and interdependent on each other to such an extent that it is reasonable to treat the business as a single business for tax purposes and it is not practicable to accurately reflect the income of the various locations, divisions, or related members of a corporate group by separate accounting.

Under Maryland law, however, the application of the unitary business principle is limited in the case of affiliated groups of related corporations because of the requirement that each separate corporation must file a separate income tax return and determine its own taxable income on a separate basis. For a multi-corporate group, the unitary business principle is restricted to consider only the isolated income and business activities of each separate legal entity. Even though the activities of related corporations may constitute a single unitary business, the affiliated corporations that lack nexus with the State (or are protected from taxation by federal law) are not subject to the corporate income tax and neither the net income nor the apportionment factors of those affiliated corporations are taken into account on the corporate income tax return of any related corporation that is subject to the tax.

State Revenues: Beginning in tax year 2012, corporations are subject to AMA. As a result, general fund revenues may increase significantly beginning in fiscal 2013. TTF revenues and HEIF revenues may also increase significantly beginning in fiscal 2013. The amount of the increase depends on a corporation's income tax liability, gross receipts, and gross profits and cannot be reliably estimated at this time.

The Comptroller's Office advises that data on the gross profits of corporations is not currently available. In examining tax year 2007 data, it estimated that if all corporations elected to use the gross receipts AMA, corporate income tax revenues would have increased by a maximum of $466 million. The Comptroller's Office advises that this amount substantially overstates the impact of the bill since it does not take into account that corporations may elect the gross profits method in determining the AMA. In addition, the bill allows corporations to claim the amount of the AMA paid against future corporate income tax revenues to the extent the corporate income tax exceeds the AMA in these tax years. In examining the 15,878 entities with Maryland nexus, the Comptroller's Office estimates that a little more than one-half would owe no corporate income tax or AMA.

State Expenditures: The Comptroller's Office reports that it will incur a one-time expenditure increase of $220,000 in fiscal 2013 for income tax form change expenses. This includes data processing changes to the SMART income tax return processing and imaging systems and system testing.

Additional Information

Prior Introductions: SB 979 of 2011 received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Similar legislation was introduced in the 2007 special session and 2005 session. SB 22 of the 2007 special session was referred to the Senate Budget and Taxation Committee, but no further action was taken. HB 1135 of 2005 received a hearing in the House Ways and Means Committee, but no further action was taken. Its cross file, SB 748, received a hearing in the Senate Budget and Taxation Committee, but no further action was taken.

Cross File: None.

Information Source(s): Comptroller's Office, Department of Legislative Services

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