Department of Legislative Services
Maryland General Assembly
2018 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 538 (Senator Pinsky)
Budget and Taxation

Corporate Income Tax - Throwback Rule

This bill applies a "throwback" rule in determining whether sales are considered in the State for purposes of the State's corporate income tax apportionment formula. **The bill takes effect July 1, 2018, and applies to all taxable years beginning after December 31, 2017.**

Fiscal Summary

State Effect: General fund revenues increase by $56.8 million in FY 2019 from additional corporate income tax revenues. Transportation Trust Fund (TTF) revenues increase by $10.4 million and Higher Education Investment Fund (HEIF) revenues increase by $4.3 million in FY 2019. Future year revenue estimates reflect the timing of tax payments and inflation. The Comptroller's Office can implement the bill with existing resources.

($ in millions)	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
GF Revenue	$56.8	$47.2	$43.9	$44.8	$45.7
SF Revenue	$14.7	$12.2	$11.4	$11.6	$11.9
Expenditure	0	0	0	0	0
Net Effect	$71.5	$59.4	$55.3	$56.5	$57.6

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate increase; (-) = indeterminate decrease

Local Effect: Local highway user revenues distributed from the corporate income tax increase by $1.0 million in FY 2019 and by $0.8 million in FY 2023. Local expenditures are not affected.

Small Business Effect: Minimal.

Analysis

Bill Summary: Sales of tangible personal property must be included in the numerator of the sales factor used for determining the Maryland taxable income of a multistate corporation if (1) the property is delivered or shipped to a purchaser within the State, regardless of the point from where it is shipped or other conditions of the sale or (2) the property is shipped from an office, store, warehouse, factory, or other place of storage in the State and the corporation is not taxable in the state of the purchaser. The bill provides that a corporation is considered taxable in a state if (1) in that state the corporation is subject to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business, or a corporate stock tax or (2) that state has jurisdiction to subject the taxpayer to a net income tax, regardless of whether, in fact, the state imposes a tax.

Current Law: Under existing Maryland apportionment of income rules, the sales factor of the apportionment fraction is generally determined by including in the denominator all sales of the corporation and by including in the numerator only those sales of property delivered or shipped to a purchaser within the State, regardless of point of shipment or other conditions of sale, making Maryland a "destination" state. However, federal law essentially prevents other states from imposing corporate taxes on sales by Maryland corporations, even though they make sales in those states, if the corporation limits its activities in the other states to specified permissible activities. The interaction of Maryland's corporate taxation rules and the federal restriction therefore results in "nowhere income" – income that is apportioned nowhere for state income tax purposes. Under the bill, in calculating the sales factor of the apportionment fraction, sales of goods to a purchaser located in another state where the seller is not taxable are included (or "thrown back") in the numerator if the property is shipped from Maryland.

Background: The Comptroller's Office issued its most recent analysis of the revenue impact of adopting the throwback rule in March 2013 on corporate income tax returns filed in tax year 2010. The Comptroller's Office estimated that under a throwback rule, 144 entities would have had $4.6 billion of income from sales made into states in which they did not have nexus thrown back to Maryland in tax year 2010. After apportioning that income and accounting for losses, corporate income tax revenues would have increased by $15.7 million, with 94 of the entities paying additional taxes. If sales to the federal government were also thrown back to Maryland, which is not required by the bill, corporate income taxes would have increased by an additional $28.1 million. In tax years 2006, 2007, 2008, and 2009, adoption of a throwback rule that did not include government sales was estimated to have increased corporate income tax revenues by $44.3 million, $31.3 million, $32.8 million, and $96.5 million, respectively.

The Comptroller's Office states that the actual revenue gain from the throwback rule in each tax year would have been greater as single-entity corporations and noncorporate entities were exempt from the reporting requirements.

As **Exhibit 1** shows, 28 states and the District of Columbia currently have some type of throwback rule.

Exhibit 1
States with Throwback Rules

Alabama	Kansas	North Dakota
Alaska	Kentucky	Oklahoma
Arkansas	Louisiana	Oregon
California	Maine	Rhode Island
Colorado	Massachusetts	Tennessee
Connecticut	Mississippi	Utah
District of Columbia	Missouri	Vermont
Hawaii	Montana	West Virginia
Idaho	New Hampshire	Wisconsin
Illinois	New Mexico	

Source: CCH Intelliconnect

State Revenues: The bill requires the adoption of a throwback rule under the corporate income tax beginning in tax year 2018. Fiscal 2019 revenues will increase by most of the increase attributable to tax year 2018 and a little less than 30% of the tax year 2019 increase. As a result, general fund revenues increase by $56.8 million, TTF revenues increase by $10.4 million, and HEIF revenues increase by $4.3 million in fiscal 2019. **Exhibit 2** shows the impact of the bill in fiscal 2019 through 2023. This estimate is based on the Comptroller's estimate of the tax year 2006 through 2010 impacts of the adoption of a throwback rule.

Exhibit 2
Effect of Throwback Rule
Fiscal 2019-2023
($ in Millions)

	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
General Fund	$56.8	$47.2	$43.9	$44.8	$45.7
HEIF	4.3	3.6	3.3	3.4	3.5
TTF	10.4	8.7	8.1	8.2	8.4
State	*9.4*	*7.8*	*7.3*	*7.4*	*7.6*
Local	*1.0*	*0.8*	*0.8*	*0.8*	*0.8*
Total	**$71.5**	**$59.4**	**$55.3**	**$56.5**	**$57.6**

HEIF: Higher Education Investment Fund
TTF: Transportation Trust Fund

In addition, the fiscal estimates of the Comptroller's Office for tax years 2006 through 2010 were limited only to those corporations that are members of a corporate group and were required to provide informational returns. It is likely that additional significant revenue gains will be realized from other corporations that were not required to file these returns.

Additional Information

Prior Introductions: SB 833 of 2017 received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Its cross file, HB 639, received a hearing in the House Ways and Means Committee, but no further action was taken. Additionally, a similar bill, SB 800 of 2011, received an unfavorable report from the Senate Budget and Taxation Committee.

Cross File: None designated; however, HB 1051 (Delegate P. Young, *et al.* – Ways and Means) is identical.

Information Source(s): Comptroller's Office; State Department of Assessments and Taxation; CCH Intelliconnect; Department of Legislative Services

Fiscal Note History: First Reader - February 23, 2018
md/hlb

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