

SENATE BILL 523

Q3

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By: **Senators Guzzone, Hester, Beidle, Carozza, Edwards, Elfreth, Feldman, Griffith, Kagan, King, Kramer, Peters, Serafini, West, and Zucker**

Introduced and read first time: January 30, 2020

Assigned to: Budget and Taxation

A BILL ENTITLED

1 AN ACT concerning

2 **Income Tax – Pass-Through Entities – Imposition of Tax**

3 FOR the purpose of altering the State income tax imposed on certain pass-through entities;
4 requiring each pass-through entity to pay the tax imposed with respect to certain
5 shares of certain nonresident and nonresident entity members of the pass-through
6 entity; authorizing a pass-through entity to pay the tax imposed with respect to
7 certain shares of all members of the pass-through entity; providing for the
8 calculation of the tax; prohibiting the tax required to be paid for any taxable year
9 from exceeding a certain amount; allowing each member to claim a credit against the
10 State income tax and county income tax for the member's proportionate share of the
11 tax paid by the pass-through entity; defining certain terms; making certain stylistic
12 and conforming changes; providing for the application of this Act; and generally
13 relating to the State income tax and pass-through entities.

14 BY repealing and reenacting, with amendments,
15 Article – Tax – General
16 Section 10–102.1, 10–701.1, and 10–706
17 Annotated Code of Maryland
18 (2016 Replacement Volume and 2019 Supplement)

19 SECTION 1. BE IT ENACTED BY THE GENERAL ASSEMBLY OF MARYLAND,
20 That the Laws of Maryland read as follows:

21 **Article – Tax – General**

22 10–102.1.

23 (a) (1) In this section the following words have the meanings indicated.

24 (2) “Distributable cash flow” means taxable income reportable by a

EXPLANATION: CAPITALS INDICATE MATTER ADDED TO EXISTING LAW.

[Brackets] indicate matter deleted from existing law.



1 pass-through entity on its federal income tax return for the taxable year:

2 (i) adjusted, in the case of an entity using the accrual method of
3 accounting to report federal taxable income, to reflect the amount of taxable income that
4 would have been reported under the cash method of accounting;

5 (ii) increased by the sum of:

6 1. cash receipts for the taxable year that are not includable
7 in the gross income of the entity, including capital contributions and loan proceeds;

8 2. amounts allowable to the entity for the taxable year as
9 deductions for depreciation, amortization, and depletion; and

10 3. the decrease, if any, in the entity's liability reserve as of
11 the end of the taxable year; and

12 (iii) decreased by the sum of:

13 1. cash expenditures for the taxable year that are not
14 deductible in computing the taxable income of the entity, not including distributions to
15 shareholders, partners, or members; and

16 2. the increase, if any, in the entity's liability reserve as of
17 the end of the taxable year.

18 (3) "Liability reserve" means accrued unpaid liabilities that are not
19 deductible in computing taxable income.

20 (4) "Member" means:

21 (i) a shareholder of an S corporation;

22 (ii) a general or limited partner of a partnership, limited
23 partnership, or limited liability partnership;

24 (iii) a member of a limited liability company; or

25 (iv) a beneficiary of a business trust or statutory trust.

26 (5) "Nonresident entity" means an entity that is not formed under the laws
27 of the State and is not qualified by or registered with the Department of Assessments and
28 Taxation to do business in the State.

29 (6) "Nonresident taxable income" means any income described in §
30 10-210(b)(1) through (4) of this title.

1 (7) “Pass-through entity” means:

2 (i) an S corporation;

3 (ii) a partnership;

4 (iii) a limited liability company that is not taxed as a corporation
5 under this title; or

6 (iv) a business trust or statutory trust that is not taxed as a
7 corporation under this title.

8 (8) “PASS-THROUGH ENTITY’S TAXABLE INCOME” MEANS THE
9 PORTION OF A PASS-THROUGH ENTITY’S INCOME UNDER THE FEDERAL INTERNAL
10 REVENUE CODE THAT IS DERIVED FROM OR REASONABLY ATTRIBUTABLE TO THE
11 TRADE OR BUSINESS OF THE PASS-THROUGH ENTITY IN THIS STATE.

12 (b) (1) [In] SUBJECT TO PARAGRAPH (2) OF THIS SUBSECTION, IN addition
13 to any other tax imposed under this title, a tax is imposed on each pass-through entity
14 [that has:

15 (1) any member who is a nonresident of the State or is a nonresident entity;
16 and

17 (2) any nonresident taxable income for the taxable year].

18 (2) EACH PASS-THROUGH ENTITY:

19 (I) SHALL PAY THE TAX IMPOSED UNDER PARAGRAPH (1) OF
20 THIS SUBSECTION WITH RESPECT TO THE DISTRIBUTIVE SHARES OR PRO RATA
21 SHARES OF THE NONRESIDENT AND NONRESIDENT ENTITY MEMBERS OF THE
22 PASS-THROUGH ENTITY; OR

23 (II) MAY ELECT TO PAY THE TAX IMPOSED UNDER PARAGRAPH
24 (1) OF THIS SUBSECTION WITH RESPECT TO THE DISTRIBUTIVE SHARES OR PRO
25 RATA SHARES OF RESIDENT MEMBERS OF THE PASS-THROUGH ENTITY.

26 (c) (1) [The] WITH RESPECT TO A PASS-THROUGH ENTITY THAT PAYS
27 THE TAX IMPOSED UNDER SUBSECTION (B)(1) OF THIS SECTION IN ACCORDANCE
28 WITH SUBSECTION (B)(2)(I) OF THIS SECTION, THE tax [imposed under subsection (b)
29 of this section] shall be treated as a tax imposed on the nonresident or nonresident entity
30 members that is paid on behalf of the nonresidents or nonresident entities by the
31 pass-through entity.

32 (2) The Comptroller shall provide by regulation for the treatment of the tax

1 imposed under subsection (b) of this section that is paid on behalf of a nonresident entity
2 member that is itself a pass-through entity.

3 (d) (1) [Except as provided in paragraph (2) of this subsection, the] **WITH**
4 **RESPECT TO A PASS-THROUGH ENTITY THAT PAYS THE TAX IMPOSED UNDER**
5 **SUBSECTION (B)(1) OF THIS SECTION IN ACCORDANCE WITH SUBSECTION (B)(2)(I)**
6 **OF THIS SECTION, THE** tax imposed [under subsection (b) of this section] is the sum of:

7 (i) a rate equal to the sum of the rate of the tax imposed under §
8 10-106.1 of this subtitle and the top marginal State tax rate for individuals under §
9 10-105(a) of this subtitle applied to the sum of each nonresident individual member's
10 distributive share or [pro-rata] **PRO RATA** share of [a] **THE** pass-through entity's
11 nonresident taxable income; and

12 (ii) the rate of the tax for a corporation under § 10-105(b) of this
13 subtitle applied to the sum of each nonresident entity member's distributive share or
14 [pro-rata] **PRO RATA** share of [a] **THE** pass-through entity's nonresident taxable income.

15 **(2) WITH RESPECT TO A PASS-THROUGH ENTITY THAT PAYS THE TAX**
16 **IMPOSED UNDER SUBSECTION (B)(1) OF THIS SECTION IN ACCORDANCE WITH**
17 **SUBSECTION (B)(2)(II) OF THIS SECTION, THE TAX IMPOSED IS THE SUM OF:**

18 **(I) A RATE EQUAL TO THE SUM OF THE RATE OF THE TAX**
19 **IMPOSED UNDER § 10-106.1 OF THIS SUBTITLE AND THE TOP MARGINAL STATE TAX**
20 **RATE FOR INDIVIDUALS UNDER § 10-105(A) OF THIS SUBTITLE APPLIED TO THE SUM**
21 **OF EACH INDIVIDUAL MEMBER'S DISTRIBUTIVE SHARE OR PRO RATA SHARE OF THE**
22 **PASS-THROUGH ENTITY'S TAXABLE INCOME; AND**

23 **(II) THE RATE OF THE TAX FOR A CORPORATION UNDER §**
24 **10-105(B) OF THIS SUBTITLE APPLIED TO THE SUM OF EACH ENTITY MEMBER'S**
25 **DISTRIBUTIVE SHARE OR PRO RATA SHARE OF THE PASS-THROUGH ENTITY'S**
26 **TAXABLE INCOME.**

27 **[(2)] (3)** The tax required to be paid for any taxable year [on behalf of
28 nonresident or nonresident entity members] by a pass-through entity may not exceed:

29 **(I) WITH RESPECT TO A PASS-THROUGH ENTITY THAT PAYS**
30 **THE TAX IMPOSED UNDER SUBSECTION (B)(1) OF THIS SECTION IN ACCORDANCE**
31 **WITH SUBSECTION (B)(2)(I) OF THIS SECTION,** the sum of all of the nonresident and
32 nonresident entity members' shares of the pass-through entity's distributable cash flow;
33 **AND**

34 **(II) WITH RESPECT TO A PASS-THROUGH ENTITY THAT PAYS**
35 **THE TAX IMPOSED UNDER SUBSECTION (B)(1) OF THIS SECTION IN ACCORDANCE**

1 WITH SUBSECTION (B)(2)(II) OF THIS SECTION, THE SUM OF ALL OF THE MEMBERS'
2 SHARES OF THE PASS-THROUGH ENTITY'S DISTRIBUTABLE CASH FLOW.

3 (E) IN ACCORDANCE WITH § 10-701.1 OF THIS TITLE, EACH MEMBER MAY
4 CLAIM A CREDIT AGAINST THE TAX IMPOSED ON THE MEMBER FOR THE MEMBER'S
5 PROPORTIONATE SHARE OF THE TAX PAID BY THE PASS-THROUGH ENTITY UNDER
6 SUBSECTION (B) OF THIS SECTION.

7 [(e)] (F) (1) (i) The tax imposed under subsection (b) of this section does
8 not apply with respect to the distributive share or [pro-rata] PRO RATA share of a member
9 that is itself a pass-through entity formed under the laws of the State or qualified by or
10 registered with the Department of Assessments and Taxation to do business in the State.

11 (ii) A member of a pass-through entity that is itself a pass-through
12 entity as described in subparagraph (i) of this paragraph shall ITSELF comply with the
13 provisions of this section [with respect to any of its members that are nonresidents or
14 nonresident entities].

15 (2) The tax imposed under subsection (b) of this section does not apply with
16 respect to the direct or indirect distributive share or pro rata share of a member that is:

17 (I) a real estate investment trust as defined by § 856 of the Internal
18 Revenue Code; OR

19 (II) AN ENTITY THAT IS EXEMPT FROM TAXATION UNDER § 501
20 OF THE INTERNAL REVENUE CODE.

21 [(f)] (G) The Comptroller may provide by regulation for:

22 (1) the filing of composite returns by a pass-through entity on behalf of its
23 nonresident and nonresident entity members; and

24 (2) application of or exemption from the tax imposed under subsection (b)
25 of this section for a pass-through entity:

26 (i) that files a composite return on behalf of nonresident and
27 nonresident entity members; or

28 (ii) the [nonresident or nonresident] entity members of which are
29 tax exempt.

30 [(g)] (H) (1) Subject to paragraph (2) of this subsection, if a partnership fails
31 to pay the tax when due the tax may be collected from the partners under the law applicable
32 to debts of the partnership, with the partnership and partners having rights of contribution
33 against any [nonresident] partner on whose behalf the tax is paid.

1 (2) Unless it is established by the Comptroller that the partner
2 participated in a pattern of distributions to one or more partners with the intention of
3 defeating the partnership liability for the tax imposed under subsection (b) of this section,
4 any partner otherwise liable under paragraph (1) of this subsection shall be liable for the
5 tax imposed on the partnership only to the extent of distributions from the partnership to
6 that partner after the tax was due to be paid by the partnership.

7 **[(h)] (I)** Except as provided in § 10–701.1 of this title, nothing in this section
8 limits or affects in any way the liability of an individual nonresident member or a
9 nonresident entity member for the tax imposed on the individual nonresident or
10 nonresident entity under § 10–102 of this subtitle.

11 **[(i)] (J)** The tax imposed under subsection (b) of this section does not apply to a
12 publicly traded pass-through entity that has agreed to file with the Comptroller an annual
13 information return reporting the name, address, taxpayer identification number, and other
14 information requested by the Comptroller of each nonresident or nonresident entity
15 member whose distributive share or **[pro-rata] PRO RATA** share of the pass-through
16 entity's nonresident taxable income for the taxable year exceeds \$500.

17 10–701.1.

18 An individual or a corporation may claim a credit against the State income tax **AND**
19 **COUNTY INCOME TAX** for a taxable year in the amount of tax paid by a pass-through
20 entity under § 10–102.1 of this title that is attributable to the individual's or corporation's
21 share of the pass-through entity's **[nonresident]** taxable income, as defined in **[(§**
22 **10–102.1(a)(6)] § 10–102.1(A)(8)** of this title.

23 10–706.

24 (a) Except as otherwise provided in this section, a credit allowed under this
25 subtitle is allowed against the State income tax only.

26 (b) A credit under § 10–701 **OR § 10–701.1** of this subtitle is allowed against the
27 total county and State income taxes.

28 (c) (1) A credit allowed under § 10–704(a)(1) or § 10–709(b)(1) of this subtitle
29 is allowed against the State income tax only.

30 (2) A credit allowed under § 10–704(a)(2) or § 10–709(b)(2) of this subtitle
31 is allowed against the county income tax only.

32 **SECTION 2. AND BE IT FURTHER ENACTED,** That this Act shall take effect July
33 1, 2020, and shall be applicable to all taxable years beginning after December 31, 2019.