SB 694

Department of Legislative Services

Maryland General Assembly
2020 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 694 (Senator Guzzone)
Budget and Taxation

Corporate Income Tax - Single Sales Factor Apportionment Exemption - Worldwide Headquartered Company Election

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This bill alters the number of employees that a worldwide headquartered company must have for purposes of the single sales apportionment exemption. If the parent corporation is a franchisor, it must employ at least 400 full-time employees at the parent corporation's principal executive office that is located within the State, among other requirements, to be considered a worldwide headquartered corporation. **The bill takes effect July 1, 2020, and applies to tax year 2020 and beyond.**

Fiscal Summary

State Effect: General fund, Transportation Trust Fund (TTF), and Higher Education Investment Fund (HEIF) revenues and TTF expenditures may decrease beginning in FY 2021.

Local Effect: Local highway user revenues may decrease beginning in FY 2021. Local expenditures are not affected.

Small Business Effect: None.

Analysis

Current Law: Prior to tax year 2018, corporations were 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 one-factor formula based on sales, referred to as a single sales factor formula. The apportionment factor is then multiplied by the corporation's modified income to determine Maryland taxable income.

Chapters 341 and 342 of 2018 phase in a requirement that all corporations subject to the corporate income tax, with an exception for specified worldwide headquartered companies, use a single sales factor formula to apportion income to the State. In general, sales represent 60% of the final apportionment factor in tax year 2018, 66.67% of the final apportionment factor in tax year 2019, 71.42% of the final apportionment factor in tax year 2020, 75% of the final apportionment factor in tax year 2021, and 100% of the final apportionment factor in tax year 2022 and beyond. Corporations engaged primarily in manufacturing activities must use a single sales apportionment factor.

A corporation may elect annually to use a three-factor formula that incorporates property, payroll, and a double-weighted sales factor if the corporation included in a group of corporations, including a parent corporation, is a worldwide headquartered company that filed a federal corporate income tax return for the taxable year, filed a specified form with the Securities and Exchange Commission, has its principal executive office in the State, and employs at least 500 full-time employees during a specified period.

To determine the Maryland modified income of a corporation or group of corporations that is a worldwide headquartered company that filed a federal corporate income tax return for the taxable year, gross income from intangible investments, including dividends, interest, royalties, and capital gains from the sale of intangible property, must be included in the calculation of the numerator based on the average of the property and payroll factors.

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, as described above.

The Maryland tax liability of a corporation equals the Maryland taxable income multiplied by the tax rate, less any tax credits.

The majority of corporate income tax revenues are distributed to the general fund with 6% of corporate income tax revenues distributed to HEIF. A portion of corporate income tax revenues are also distributed to TTF, of which 13.5% of TTF revenues are used to provide capital transportation grants to local governments (9.6% beginning in fiscal 2025).

State Revenues: Approximately a dozen or fewer corporations will be able to elect to be exempt from the single sales apportionment requirement under the bill. These companies may elect annually to use a three-factor formula that incorporates property, payroll, and a double-weighted sales factor. Thus, general fund, TTF, and HEIF revenues may decrease beginning in fiscal 2021 to the extent that these companies elect to use the double-weighted sales factor apportionment formula. The Comptroller's Office advises that they are not able to disclose the fiscal impact of the bill due to taxpayer confidentiality; however, they do not expect the bill to have a significant fiscal effect and the revenue loss, if any, is likely to be less than $5.0 million annually.

State Expenditures: A portion of TTF revenues are used to provide capital transportation grants to local governments. To the extent that TTF revenues decrease as a result of taxpayers altering their apportionment method on the corporate income tax, TTF expenditures decrease by 13.5% of the TTF revenue decrease beginning in fiscal 2021 (9.6% beginning in fiscal 2025). TTF revenues also fund the State capital program; thus, a decrease in TTF revenues decreases expenditures for the State capital program.

Local Revenues: Local governments receive a portion of corporate income tax revenues as local highway user revenues through capital transportation grants. Thus, local highway user revenues may decrease beginning in fiscal 2021 to the extent that corporate income tax revenues decrease.

Additional Information

Prior Introductions: SB 1022 of 2019 received a favorable report from the Senate Budget and Taxation Committee, but no further action was taken.

Designated Cross File: None.

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

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