Department of Legislative Services

Maryland General Assembly
2024 Session

FISCAL AND POLICY NOTE
First Reader - Revised

House Bill 1007 (Delegate Palakovich Carr, *et al.*)
Ways and Means

Fair Share for Maryland Act of 2024

This bill (1) decreases the exclusion amount under the Maryland estate tax from $5.0 million to $2.0 million; (2) institutes a sales factor "throwback" rule for purposes of Maryland corporate income apportionment; (3) establishes an additional tax rate of 8.25% on specified pass-through entity (PTE) income; (4) alters individual income tax rates and brackets; (5) imposes an additional 1% income tax rate on specified net capital gains income; (6) alters the State's earned income credit for individuals without a qualifying child; (7) enhances and expands eligibility for the State's child tax credit; and (8) requires affiliated corporations to compute Maryland taxable income using worldwide combined reporting. **The bill generally takes effect July 1, 2024. Provisions relating to the individual income tax and taxation of specified PTE income take effect July 1, 2027, and apply to tax year 2027 and beyond. Provisions relating to corporate combined reporting take effect July 1, 2027, and apply to tax year 2028 and beyond.**

Fiscal Summary

State Effect: No impact in FY 2025. In FY 2026, general and special fund revenues increase by an estimated $101.3 million and $5.9 million, respectively, and special fund expenditures for local highway user revenue grants increase by an estimated $0.9 million. Future quantified revenues reflect the phase-in of the bill's provisions, current revenue forecasts, and annualization. General fund expenditures increase by an estimated $3.8 million in FY 2027; future years reflect ongoing expenses and elimination of one-time costs.

($ in millions)	FY 2025	FY 2026	FY 2027	FY 2028	FY 2029
GF Revenue	$0	$101.3	$355.6	$181.8	$312.3
SF Revenue	$0	$5.9	$20.3	$34.9	$71.5
GF Expenditure	$0	$0	$3.8	$0.5	$0.2
SF Expenditure	$0	$0.9	$3.1	$4.0	$8.2
Net Effect	$0.0	$106.3	$369.0	$212.2	$375.4

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

Local Effect: No impact in FY 2025. Local highway user revenues increase by an estimated $0.9 million in FY 2026 and $8.2 million in FY 2029, as discussed below. Montgomery County expenditures for its earned income credit supplement program may increase beginning in FY 2028.

Small Business Effect: Minimal.

Analysis

Current Law/Bill Summary:

Estate Tax

The State imposes a tax on property that passes at or after the death of an individual through an estate tax and an inheritance tax. Estates may generally claim a credit against the estate tax for the amount of inheritance taxes paid.

A Maryland estate tax return is required for every estate with a federal gross estate, plus specified adjustments, that equals or exceeds the Maryland estate tax exclusion amount for the decedent's date of death. An estate with a value that exceeds this exclusion amount must file a return if the decedent, at the date of death, was a Maryland resident or the decedent was a nonresident who owned real or tangible personal property having a taxable situs in Maryland.

The federal Tax Cuts and Jobs Act of 2017 (TCJA) decreased federal estate taxes by doubling the federal exclusion amount for decedents dying in calendar 2018 through 2025. The Act's estate tax provisions terminate for decedents dying beginning in calendar 2026. Chapters 15 and 21 of 2018 decoupled the Maryland estate tax from the increased federal exclusion amount enacted by the federal Act. Beginning January 1, 2019, the State exclusion amount equals $5.0 million. Special rules apply under the Maryland estate tax for qualified agricultural land. *Under the bill*, the State exclusion amount decreases to $2.0 million for a decedent dying on or after January 1, 2025.

Chapters 15 and 21 also established "portability" under the State estate tax by allowing, under specified circumstances, the estate of a married taxpayer to pass along the unused part of the estate tax exclusion amount to the surviving spouse. A surviving spouse may subsequently elect to claim the unused portion of the estate tax exclusion amount of the predeceased spouse.

In addition, unless the federal estate tax credit used to calculate the Maryland estate tax is in effect at the time of a decedent's death, the federal credit used to determine the State estate tax may not exceed 16% of the amount by which a decedent's taxable estate exceeds the applicable exclusion amount.

Corporate Income Tax

Under Maryland's corporate income tax, a tax rate of 8.25% is applied to a corporation's Maryland taxable income. Maryland taxable income is federal taxable income (federal gross income minus allowable federal deductions) adjusted for Maryland addition and subtraction modifications (Maryland modified income) and allocated to the State based on the applicable apportionment factor.

Unitary Business Principle

Maryland is a unitary business state; in other words, under Maryland's corporate income tax, a corporation operating a unitary business within and outside the State must allocate to the State income derived from or reasonably attributable to trade or business carried on in the State.

In Maryland, however, the application of the unitary business principle is limited in the case of affiliated groups of corporations. State law requires that each member of an affiliated group of corporations file a separate income tax return and compute separate taxable income. Thus, although the activities of an affiliated group of corporations may constitute a unitary business, the members that lack nexus with the State are not subject to Maryland corporate income tax, and neither the net income nor apportionment factors of such members are reflected on the corporate income tax return of any affiliated corporation that is subject to the tax.

Under the bill, beginning in tax year 2028, specified corporations engaged in a "unitary business" must submit a combined income tax return, reporting and paying tax on worldwide taxable income as a combined group, reflecting the aggregate income tax liability of all members of the combined group. "Unitary business" is defined as a single economic enterprise that is made either of separate parts of a single business entity or of a commonly controlled group of business entities that are sufficiently interdependent, integrated, and interrelated through their activities so as to provide mutual benefit that produces a sharing or exchange of value among them and a significant flow of value to the separate parts. The term must be construed to the broadest extent allowed under the U.S. Constitution. The taxable income of a corporation required to file a combined return is equal to the combined group's Maryland modified income as adjusted under the bill.

The Comptroller must adopt regulations to carry out the bill's combined reporting provisions. The regulations must be consistent with principles adopted by the Multistate Tax Commission for determining the existence of a unitary business.

Apportionment of Income to Maryland

Pursuant to Chapters 341 and 342 of 2018, beginning in tax year 2022, corporations operating as unitary businesses within and outside the State (with the exception of specified worldwide headquartered companies) must use a single-factor apportionment formula based on sales (single sales factor formula) to determine Maryland taxable income. With respect to sales factor sourcing rules, Maryland is considered a "destination" state in that gross receipts from sales of tangible personal property are included in the numerator of the apportionment fraction only if the property is delivered or shipped to a purchaser within the State, regardless of the point of shipment or other conditions of sale.

Under the bill, beginning in tax year 2026, sales of tangible personal property must be included in the numerator of the sales factor ("thrown back") if (1) the property is delivered or shipped to a purchaser within the State, regardless of the point of shipment or other conditions of sale, or (2) the property is shipped from an office, a store, a warehouse, a factory, or any other place of storage in the State and the corporation is not taxable in the state of the purchaser. A corporation is considered taxable in a state if (1) in that state the corporation is subject to a net income tax, franchise tax measured by net income, franchise tax for the privilege of doing business, or 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. For tax year 2026, the Comptroller must assess interest and penalties if a corporation pays estimated income tax in an amount less than 90% of the tax required to be shown on the corporation's income tax return for the tax year.

Individual Income Tax

Exhibit 1 shows Maryland's individual income tax rates and income brackets under current law and under the bill.

Exhibit 1
Maryland Individual Income Tax Rates
Current Law vs. the Bill

Under Current Law

Single, Dependent, Married Filing Separately		Joint, Surviving Spouse, Head of Household	
Rate	**Maryland Taxable Income**	**Rate**	**Maryland Taxable Income**
2.00%	$1-$1,000	2.00%	$1-$1,000
3.00%	$1,001-$2,000	3.00%	$1,001-$2,000
4.00%	$2,001-$3,000	4.00%	$2,001-$3,000
4.75%	$3,001-$100,000	4.75%	$3,001-$150,000
5.00%	$100,001-$125,000	5.00%	$150,001-$175,000
5.25%	$125,001-$150,000	5.25%	$175,001-$225,000
5.50%	$150,001-$250,000	5.50%	$225,001-$300,000
5.75%	Excess of $250,000	5.75%	Excess of $300,000

Under the Bill

Single, Dependent, Married Filing Separately		Joint, Surviving Spouse, Head of Household	
Rate	**Maryland Taxable Income**	**Rate**	**Maryland Taxable Income**
2.00%	$1-$1,000	2.00%	$1-$1,000
3.00%	$1,001-$2,000	3.00%	$1,001-$2,000
4.00%	$2,001-$3,000	4.00%	$2,001-$3,000
4.75%	$3,001-$100,000	4.75%	$3,001-$150,000
5.00%	$100,001-$125,000	5.00%	$150,001-$175,000
5.25%	$125,001-$150,000	5.25%	$175,001-$225,000
5.50%	$150,001-$250,000	5.50%	$225,001-$300,000
6.00%	$250,001-$500,000	6.00%	$300,001-$600,000
6.50%	$500,001-$1,000,000	6.50%	$600,001-$1,200,000
7.00%	Excess of $1,000,000	7.00%	Excess of $1,200,000

Source: Comptroller's Office; Department of Legislative Services

State Income Tax Treatment of Capital Gains

Maryland conforms to the federal income tax treatment of capital gains, as discussed below. However, under current State law, and unlike the treatment of capital gains income under the federal income tax, net capital gains are taxed at the same State income tax rates as other income.

Under the bill, net capital gains included in Maryland taxable income are subject to an additional 1% State income tax rate. The additional tax rate does not apply to any amount of capital gain from the sale or exchange of (1) a specified residential dwelling sold for less than $1,500,000 that is the individual's primary residence; (2) specified assets held in a 401(k), 403(b), or 457(b) plan, an individual retirement account or annuity (IRA), a Roth IRA, or a defined contribution plan, defined benefit plan, or similar retirement savings plan; (3) cattle, horses, or breeding livestock held for more than 12 months, as specified; (4) land that is subject to or will be subject to a conservation, agricultural, or forest preservation easement; (5) property used in a trade or business, the cost of which is deductible under § 179 of the Internal Revenue Code (IRC); or (6) affordable housing owned by a nonprofit organization.

Federal Income Tax Treatment of Capital Gains

For purposes of federal income tax, long-term capital gains and losses are distinguished from short-term capital gains and losses. A gain or loss from the disposition of a capital asset held for more than one year is treated as a long-term capital gain or loss; a gain or loss from the disposition of a capital asset that is held for one year or less is treated as a short-term capital gain or loss.

Net capital gain (net long-term capital gain minus net short-term capital loss) is generally taxed at a lower federal income tax rate (0%, 15%, or 20%, depending on the taxpayer's filing status and taxable income) than ordinary income. Net short-term capital gain is taxed as ordinary income with a top marginal rate of 37%.

An individual or other noncorporate taxpayer may deduct up to $3,000 in net capital losses each year; any unused amount of losses may be carried forward indefinitely. For corporate taxpayers, capital losses may only offset capital gains. Any unused net capital loss may be carried forward to future tax years until fully used.

Special rules apply to the sale of collectibles, investment real estate, principal residences, and to taxpayers who make qualifying investments within federal opportunity zones.

Pass-through Entities

A PTE must pay the nonresident PTE tax on the distributive or *pro rata* shares of its nonresident and nonresident entity members at a rate equal to the sum of the top marginal

State individual income tax rate and the special nonresident tax rate or, in the case of a nonresident entity member, the State corporate income tax rate.

In response to a provision of the TCJA that limited the allowable state and local tax deduction (SALT deduction) for individuals to $10,000 ($5,000 if married filing separately) in tax years 2018 through 2025, Maryland, like a number of other states, enacted legislation authorizing PTEs to elect to be taxed at the entity level for State income tax purposes. In Notice 2020-75, the Internal Revenue Service clarified that specified income tax payments made by a partnership or S corporation would not be taken into account in the application of the SALT deduction limitation for its individual members.

Under the bill, an additional tax rate of 8.25% is imposed on the distributive or *pro rata* share of income distributed to a member of a PTE from the PTE's taxable income that exceeds $1.0 million. The additional tax rate does not apply to the income of sole proprietorships.

Earned Income Tax Credit

Maryland's earned income credit offers both refundable and nonrefundable credits against the State income tax and a nonrefundable credit against the local income tax for low- to moderate-income resident taxpayers. The State nonrefundable credit is generally equal to 50% of the amount of an eligible taxpayer's federal earned income credit for the taxable year. A taxpayer for whom the State nonrefundable credit is less than the taxpayer's State income tax liability may also be eligible to claim the State and local poverty level credits.

Individuals Without Qualifying Children

Legislation enacted in the 2018, 2021, and 2023 sessions expanded the State's earned income credit for individuals without qualifying children. Specifically:

- Chapters 611 and 612 of 2018 allowed individuals without qualifying children to claim the State and local earned income credits without regard to the federal minimum age requirement for childless claimants;
- for tax years 2020 through 2022, Chapter 39 of 2021 increased the value of the State refundable credit for individuals without qualifying children to 100% of the individual's federal earned income credit (minus any pre-credit State income tax liability), up to a maximum of $530;
- for tax years 2020 through 2022, Chapter 40 of 2021 generally expanded eligibility for Maryland's earned income credit to taxpayers who would be eligible for the federal earned income credit but for specified identification requirements; and
- Chapters 3 and 4 of 2023 permanently extended beyond tax year 2022 the temporary expansions to the earned income credit enacted in 2021 and eliminated the

$530 limit on the value of the State refundable credit for individuals without qualifying children.

Thus, for tax year 2023 and beyond, an eligible individual without a qualifying child may claim a fully refundable State earned income credit in an amount equal to the allowable federal earned income credit, without limitation. The federal earned income credit for individuals without qualifying children is equal to 7.65% of an eligible taxpayer's earned income up to the "earned income amount" ($8,260 for tax year 2024), minus 7.65% of the taxpayer's earned income in excess of the "phaseout amount" ($10,330 for tax year 2024). The maximum value of the federal earned income credit for individuals without qualifying children is $632 for tax year 2024.

Under the bill, the State's earned income credit for individuals without qualifying children is further enhanced through an increase in the income threshold at which the credit begins to phase out. Specifically, beginning in tax year 2027, the value of the credit is calculated by substituting $19,160 (as adjusted for inflation beginning in tax year 2027, as specified) for the federal phaseout amount. (See the Additional Comments section of this fiscal and policy note.)

Child Tax Credit

In addition to expanding eligibility for the Maryland earned income credit, Chapter 40 established, for tax years 2020 through 2022 only, a refundable credit against the State income tax for low-income taxpayers with qualifying children (child tax credit). Under the Act, taxpayers with federal adjusted gross income of up to $6,000 were eligible to claim a credit equal to $500 per qualified child (which was defined as a dependent under § 152 of the IRC who is younger than age 17 and has a disability, as defined under § 8-401 of the Education Article), minus the amount of any federal child tax credit claimed with respect to the qualified child.

Chapters 3 and 4 permanently extend the child tax credit beyond tax year 2022. The Acts also (1) expand eligibility to taxpayers with federal adjusted gross income of up to $15,000, and limit eligibility to residents of the State; (2) expand the definition of a "qualified child" for purposes of the credit to include qualified dependents younger than age six, regardless of disability status; and (3) eliminate the requirement that the amount of the credit be reduced by the amount of any federal child tax credit claimed.

Under the bill, the child tax credit is further enhanced beginning in tax year 2027. Specifically, (1) the definition of a qualified child for purposes of the credit is expanded to include qualified dependents younger than 18, regardless of disability status; (2) the value of the credit for a qualified child younger than age six is increased to $750, and both values of the credit are adjusted for inflation beginning in tax year 2027, as specified; and (3) the existing income eligibility threshold is repealed. The bill further specifies that the amount of the credit for a qualified child must be reduced by $50 for each $1,000, or fraction thereof, by which the taxpayer's federal adjusted gross income exceeds $45,000 ($65,000 for joint filers, surviving spouses, and heads of households and $32,500 for married individuals filing separately).

State Revenues: **Exhibit 2** displays the bill's quantified effect on State revenues by provision and fund type. As shown in the exhibit, the bill's net quantified effect on State revenues totals $107.1 million in fiscal 2026, including $101.3 million in net general fund revenues. Future years reflect the phasing in of the bill's various provisions, current revenue forecasts, and annualization.

Exhibit 2
Quantifiable State Revenue Effects
($ in Millions)

	FY 2025	FY 2026	FY 2027	FY 2028	FY 2029
By Provision					
Estate Tax Alterations	$0	$83.3	$86.0	$88.9	$91.8
Throwback Rule	0	23.9	82.2	86.7	86.7
PIT Rate/Bracket Alterations	0	0.0	207.7	423.2	439.2
EITC Alterations	0	0.0	0.0	(108.5)	(112.8)
CTC Alterations	0	0.0	0.0	(338.8)	(345.6)
Combined Reporting	0	0.0	0.0	65.3	224.6
By Fund					
General Fund	$0	$101.3	$355.6	$181.8	$312.3
HEIF	0	1.4	4.9	9.1	18.7
TTF	0	4.5	15.3	25.8	52.8
Net State Revenue Effect	**$0**	**$107.1**	**$375.9**	**$216.7**	**$383.8**

CTC: child tax credit
EITC: earned income tax credit
HEIF: Higher Education Investment Fund
PIT: personal income tax
TTF: Transportation Trust Fund

Note: Numbers may not sum to total due to rounding.

Source: Comptroller's Office; Department of Legislative Services

The Department of Legislative Services cautions that actual revenues under the bill's quantified provisions may differ significantly from the above estimate. Estimated revenue effects relating to the bill's adoption of a throwback rule and combined reporting for affiliated corporations are based on a previous study conducted by the Comptroller's Office based on data collected from taxpayers in tax years 2006 through 2010, adjusted for subsequent changes in the economy and corporate income tax revenues. The study's examination of the potential impacts of combined reporting contemplated a water's edge election; with the exception of Alaska, which requires worldwide combined reporting for oil and gas companies, no state currently requires worldwide combined reporting as provided by the bill. In its study of the potential State revenue effects of combined reporting, the Comptroller's Office concluded that, while combined reporting would likely increase corporate income tax revenues *on average*, it would also increase the volatility of those revenues; thus, the effect of the proposed change on corporate income tax revenues may be positive or negative in any given year.

Other provisions of the bill not quantified – specifically, the additional 1% tax rate on specified capital gains income and the additional 8.25% tax rate on specified PTE income – result in potentially significant increases in general fund revenues beginning in fiscal 2027; however, such revenues cannot be reliably estimated due to data limitations, the volatility of these income sources, and uncertainty regarding the response of affected PTEs to the bill's provisions and the expiration of the TCJA's limitation on SALT deductions after tax year 2025.

State Expenditures:

Comptroller's Office

General fund expenditures for the Comptroller's Office increase by an estimated $3.8 million in fiscal 2027 in order to implement the bill's corporate combined reporting provisions. This estimate reflects the cost of (1) hiring two full-time regular senior tax attorneys, as well as four legal consultants for a period of 18 months; (2) one-time information technology (IT) development to accommodate corporate combined reporting; and (3) Multistate Tax Commission (MTC) training for Comptroller staff. It includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Regular Positions	2
Contractual Positions	4
Regular Salaries and Fringe Benefits	$202,422
Contractual Salaries and Fringe Benefits	539,454
One-time IT Development	3,000,000
MTC Training	12,500
Other Operating Expenses	45,286
Total FY 2027 Comptroller Expenditures	**$3,799,662**

Future year expenditures reflect full salaries with annual increases and employee turnover, annual increases in ongoing operating expenses, and termination of the contractual positions in fiscal 2028. This estimate does not include any health insurance costs that could be incurred for specified contractual employees under the State's implementation of the federal Patient Protection and Affordable Care Act.

To the extent that the Comptroller's Office requires further support to process increased tax credit claims or otherwise implement the bill's provisions, general fund expenditures increase further.

Transportation Trust Fund

Transportation Trust Fund expenditures for local highway user revenue grants may increase by an estimated $0.9 million in fiscal 2026, $3.1 million in fiscal 2027, $4.0 million in fiscal 2028, and $8.2 million in fiscal 2029.

Local Fiscal Effect: Local highway user revenues may increase by an estimated $0.9 million in fiscal 2026, $3.1 million in fiscal 2027, $4.0 million in fiscal 2028, and $8.2 million in fiscal 2029.

Montgomery County expenditures for the Working Families Income Supplement Program, which provides a match to county residents based on the amount of the State earned income credit, may increase beginning in fiscal 2028.

Additional Comments: The bill specifies that (1) beginning in tax year 2027, the amount of the State earned income credit for individuals without qualifying children must be calculated by substituting $7,840 for the applicable federal earned income amount (consistent with the applicable earned income amount for tax year 2023) and $19,160 for the applicable federal phaseout amount and (2) beginning in tax year 2027, the Comptroller must increase these amounts in accordance with the cost-of-living adjustment (COLA) specified under the IRC (on which the federal COLAs to the federal earned income and phaseout amounts are based) by substituting "calendar year 2026" for "calendar year 2016" in IRC § 1(f)(3)(B).

As written, due to the bill's reference to IRC § 1(f)(3)(B) and substitution of "calendar year 2026" for "calendar year 2016" in its application, the alterations to the earned income and phaseout amounts differ from the bill's intent. For purposes of this analysis, it is assumed that the bill applies as intended, which would be achieved by amending the IRC reference to be § 1(f)(3)(A) and substituting "calendar year 2022" for "calendar year 2016" in its application.

Additional Information

Recent Prior Introductions: Similar legislation has not been introduced within the last three years.

Designated Cross File: SB 766 (Senator Hettleman, *et al.*) - Budget and Taxation.

Information Source(s): Comptroller's Office; Judiciary (Administrative Office of the Courts); Register of Wills; Internal Revenue Service; Department of Legislative Services

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