Letter of Information – House Bill 337 Income Tax – Capital Gains, Dividends, and Foreign-Derived Intangible Income - Alterations (Investing in Marylanders Act of 2023)
Ways and Means Committee
February 9, 2023

House Bill 337 would require the Comptroller to make significant modifications to individual, corporate, pass-through entity, and fiduciary income tax forms, tax processing programs, business rules, and image and data collection systems in order to administer the complex provisions of the bill that includes the following:

- creating a new, additional State individual income tax rate on the net capital gains of individuals;
- expanding the addback provisions currently applicable to captive real estate investment trusts (REITs) to all REITs claiming a federal dividends paid deduction;
- creating a new addition modification for amounts deducted on a federal return for foreign-derived intangible income;
- creating a new addition modification for amounts deducted on a federal return for dividends received from a foreign corporation;
- modifying an existing addition modifications for certain corporate interest expenses and intangible expenses; and
- modifying an existing subtraction modification for certain dividends received from a foreign corporation.

These changes relate to some of the most complex areas of the federal and State income tax laws to administer and audit. Extensive research into the intersection of the various areas of the code would be required to make a reasoned estimation of the fiscal impact on the State, especially regarding the addbacks that, at the Maryland level, counter the federal regimes established to encourage U.S. multinational corporations to increase their investments in the U.S.

The operational impact on the agency to administer these provisions, instruct the programming to implement these changes, train staff, and update existing regulations and other guidance for staff, taxpayers and the practitioner community will require significant expenditures in the form of additional staffing resources with expertise in complex tax transactions, programming, and audit. We estimate that concurrent changes of this magnitude to four separate income tax types in both the agency's legacy and integrated tax processing systems will require approximately two years planning, development, testing, and training to implement. Given other existing significant initiatives (e.g., taxation of adult-use cannabis, implementation of bracketed local income tax) the Comptroller's Office would face extraordinary challenges if required to complete the work to implement these changes applicable to tax years beginning after December 31, 2022, and core agency functions would suffer. Even in a subsequent tax year, the scope of the changes in this bill would substantially impact core agency operations and would also require delaying other ongoing projects, including the tax modernization project, in order to complete this work within a single tax year.

Additionally, the Comptroller objects to the proposed language in Tax-General Article §10-306.1(c) which seeks to apply a "clear and convincing evidence" standard to review of an interest expense or intangible expense to determine whether the transaction giving rise to the payment or expense had a principal purpose of tax avoidance. Application of a judicial standard of review is not aligned with the Comptroller's obligation to administer the tax laws under a voluntary system of tax reporting subject to audit.

As always, the Comptroller's Office is willing and available to discuss these concerns or any questions you may have at your convenience. Please contact Justin Hayes, Legislative Director at jhayes@marylandtaxes.gov or 410-260-7696.