



Corporate Income Tax Reform in Maryland--What Next?

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Maryland's Corporate Income Tax

- Separate reporting state
- Generally, three-factor apportionment with double-weighted sales
 - Single sales factor for manufacturers
 - Several other calculations for smaller industries
- Several industries made fully subject to corporate income tax over past eight years



MD's Corporate Income Tax (con't)

- 24% of revenues distributed to the TTF; remainder is general fund revenue
- Revenue Trends
 - 1968 - 1980 corporate income tax averaged 5.5% of general fund revenue
 - 1981 - 1994 (before major changes), 2.5%
 - 1995 - 2003 (with rough adjustment for additions to tax base), 3.1%



MD's Corporate Income Tax (con't)

- Corporate income tax not of particular interest over past 15 years or so
 - Only 2% - 4% of general fund revenues
 - Ranks well below individual income and sales taxes and lottery as general fund revenue source
 - May soon be rivaled by tobacco tax and insurance premium tax



Two paths to reform

- Driven initially by Comptroller's Office over the Delaware holding company issue
- Fiscal concerns have led General Assembly to take an interest in far-reaching reform



Comptroller's Office

- In mid-1990s, Comptroller's Office began auditing for Delaware holding companies
- Several dozen corporations with holding companies were uncovered
- Assessments for period in question (generally four to eight tax years, ending in late 1990s) totaled about \$40 million



Comptroller's Office (con't)

- Assessments were levied against both the parent and the subsidiary corporations
- Assessments were challenged at every step-
-internally, at the Tax Court, and at the district court level
- Auditing caseload was backing up; stopped auditing for this issue in late 1990s



Comptroller's Office (con't)

- Court of Appeals (Maryland's highest court) heard the appeals of Crown Cork & Seal, Syms, and MCI in November 2000
- No decision appeared to be forthcoming
- Fast forward *two years...*



Legislative Approach

- As fiscal crisis developed, the General Assembly became interested in corporate income tax issues
- Several bills introduced in 2003 Session
 - Combined reporting, holding companies, §482 authority (SB 398/HB 776)
 - Throwback rule (SB 392/HB 776)
 - Nonoperational income (SB 397/HB 776)



Legislative Approach (con't)

- Business community countered, proposing in lieu of those reforms
 - Bill providing §482 authority
 - Increase in corporate filing fees from \$100 to \$300, and application of fees to noncorporate business entities, which paid no filing fees
 - Three-year 10% income tax surcharge



Legislative Approach (con't)

- Consideration of the bills was hampered by lack of information, particularly the fiscal impact
- Very little information is requested on/captured from our corporate income tax returns
 - Federal taxable income, a variety of Maryland additions and subtractions, apportionment factor, credits, payments and tax due/refund
 - First four pages of federal return are attached and scanned, but not captured
 - No Corporate SOI



Legislative Approach (con't)

- Only information the Comptroller's Office could provide was from Delaware holding company audits
 - How representative of universe of taxpayers?
 - No information on combined reporting, throwback/throwout, nonoperational income



Legislative Approach (con't)

- The House of Delegates passed HB 753
 - Took business community's proposed filing fee increase and 10% income tax surcharge...
 - And entire package of reforms
 - Included in bill was the application of the 2% insurance premium tax to HMO premiums
- The Senate amended the bill to exempt biotechnology companies from the Delaware holding company provision



Legislative Approach (con't)

- Governor Ehrlich vetoed the bill, claiming the imposition of the premium tax on HMO fees was excessive in times of rising health care costs and recession
- Meanwhile...



Comptroller's Office (*redux*)

- In June 2003, over 30 months after the cases were heard, the Court of Appeals issued its decision on the holding company cases
 - Syms and Crown Cork & Seal holding companies were found to be without economic substance; MCI decision has not been issued due to bankruptcy
 - Cases remanded to Tax Court



Comptroller's Office (con't)

- Both parties (Syms and Crown Cork & Seal) have indicated they will appeal to the U.S. Supreme Court
- Several settlements have been offered, but none satisfactory to the Comptroller
- Comptroller's staff feel relatively confident, but no revenue will be forthcoming for the foreseeable future



What Next?

- “[Senate President] Miller said he plans to pass a new corporate tax package even larger than last year's \$135 million proposal....But he said in order to make his plan more politically palatable, he would not include a tax on HMO premiums, and added that he does not think he has the votes to override the governor's veto. Ehrlich, giving himself plenty of wiggle room, declined to comment on Miller's plan.”

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