

Department of Legislative Services
 Maryland General Assembly
 2019 Session

FISCAL AND POLICY NOTE
 First Reader

House Bill 922 (Delegate Mangione, *et al.*)
 Ways and Means

Corporate Income Tax - Rate Reduction

This bill reduces the corporate income tax rate from 8.25% to 8.0% for tax year 2020, 7.75% for tax year 2021, 7.50% for tax year 2022, 7.25% for tax year 2023, 7.00% for tax year 2024, 6.75% for tax year 2025, 6.50% for tax year 2026, 6.25% for tax year 2027, and 6.00% for tax year 2028 and beyond. **The bill takes effect July 1, 2019.**

Fiscal Summary

State Effect: General fund revenues decrease by \$9.6 million, Transportation Trust Fund (TTF) revenues decrease by \$1.8 million, and Higher Education Investment Fund (HEIF) revenues decrease by \$0.7 million in FY 2020. Future year revenue losses reflect the current revenue forecast and applicable tax rate. TTF expenditures decrease by \$0.2 million in FY 2020 and by \$4.2 million in FY 2024.

(\$ in millions)	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024
GF Revenue	(\$9.6)	(\$44.0)	(\$84.6)	(\$127.1)	(\$169.4)
SF Revenue	(\$2.5)	(\$11.4)	(\$21.9)	(\$33.0)	(\$43.9)
SF Expenditure	(\$0.2)	(\$1.1)	(\$2.1)	(\$3.2)	(\$4.2)
Net Effect	(\$11.8)	(\$54.3)	(\$104.4)	(\$156.9)	(\$209.1)

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

Local Effect: Local highway user revenues decrease by \$0.2 million in FY 2020 and by \$4.2 million in FY 2024. Expenditures are not affected.

Small Business Effect: Minimal.

Analysis

Current Law/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.

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 single sales factor formula. The apportionment factor is then multiplied by the corporation's modified income to determine Maryland taxable income. Chapter 342 of 2018 altered the apportionment formula so that by tax year 2022, all corporations subject to the corporate income tax, with an exception for specified worldwide headquartered companies, that carry on a trade or business in and out of State must allocate to the State the part of the corporation's Maryland modified income derived from or attributed to being carried on in the State using an apportionment formula in which Maryland modified income is multiplied by 100% of the sales factor. 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.

Net corporate income tax revenues are projected to total just over \$1.2 billion in fiscal 2020. Of this amount, \$965.3 million is general fund revenues, \$177.4 million is TTF revenues, and \$72.9 million is HEIF revenues. Corporate income tax revenues comprise about 5.2% of all general fund revenues. According to data from the Comptroller's Office, of the over 60,000 State corporate income tax returns filed in tax year 2015, about 40% were taxable.

Exhibit 1 shows the corporate income tax rates in Maryland and surrounding states, including the District of Columbia.

Exhibit 1
Corporate Income Tax Rates
Maryland and Surrounding States
Tax Year 2019

Delaware	8.7%
District of Columbia	8.25%
Maryland	8.25%
Pennsylvania	9.99%
Virginia	6.0%
West Virginia	6.5%

Source: CCH Intelliconnect

The Department of Legislative Services issued a [report](#) in October 2013 that estimates the economic impacts of reducing the corporate income tax rate from 8.25% to 7.25%.

The federal Tax Cuts and Jobs Act of 2017 altered the federal corporate income tax rates. For tax years beginning after December 31, 2017, the graduated corporate tax rate structure is eliminated and corporate taxable income is taxed at a 21% flat rate.

State Revenues: The bill reduces the corporate income tax rate to 8% in tax year 2020 and to 6% by tax year 2028. Fiscal 2020 revenues will decrease by approximately 30% of the tax year 2020 decrease. As a result, general fund revenues decrease by \$9.6 million in fiscal 2020. TTF revenues decrease by \$1.8 million, and HEIF revenues decrease by \$0.7 million in fiscal 2020. **Exhibit 2** shows the impact of the bill in fiscal 2020 through 2024.

Exhibit 2
Fiscal Impact
Fiscal 2020-2024
(\$ in Millions)

<u>Revenues</u>	<u>FY 2020</u>	<u>FY 2021</u>	<u>FY 2022</u>	<u>FY 2023</u>	<u>FY 2024</u>
General Fund	(\$9.6)	(\$44.0)	(\$84.6)	(\$127.1)	(\$169.4)
HEIF	(0.7)	(3.3)	(6.4)	(9.6)	(12.8)
TTF	(1.8)	(8.1)	(15.5)	(23.4)	(31.1)
Total Revenues	(\$12.0)	(\$55.4)	(\$106.5)	(\$160.0)	(\$213.3)
TTF Expenditures	(\$0.2)	(\$1.1)	(\$2.1)	(\$3.2)	(\$4.2)

HEIF: Higher Education Investment Fund
TTF: Transportation Trust Fund

This estimate is based on the current Board of Revenue Estimates corporate income tax forecast, adjusted for the estimated correlation between tax year and fiscal year revenues.

State Expenditures: A portion of TTF revenues are used to provide capital transportation grants to local governments. Thus, any decrease in TTF revenues from corporate tax revenues results in a 13.5% decrease in TTF expenditures to local governments. Accordingly, TTF expenditures decrease by \$0.2 million in fiscal 2020 and by \$4.2 million in fiscal 2024 as shown in Exhibit 2. TTF revenues also fund the State capital program; thus, a decrease in TTF revenues decreases expenditures for the State capital program.

Processing changes to the Comptroller’s tax system can be handled with existing resources.

Local Revenues: Local governments receive a portion of corporate income tax revenues as local highway user revenues through capital transportation grants. Under this bill, local highway user revenues decrease by \$0.2 million in fiscal 2020 and by \$4.2 million in fiscal 2024.

Additional Comments: State law specifies that the corporate income tax revenue distributed to TTF is pledged to the payment of the principal of and interest on consolidated transportation bonds as they become due and payable. No part of the tax or other funds applicable to debt service on the bonds may be repealed, diminished, or applied to any other purpose until the bonds and the interest on them have become due and fully paid or adequate and complete provision for payment of debt service has been made. Thus, an amendment to the bill is needed to provide for adequate payment of principal of and interest

on the Department of Transportation's consolidated transportation bonds that were issued before July 1, 2019.

Additional Information

Prior Introductions: HB 818 of 2018 received a hearing in the House Ways and Means Committee, but no further action was taken.

Cross File: SB 190 (Senator West, *et al.*) - Budget and Taxation.

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

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