COMPTROLLER of MARYLAND
Serving the People

Peter Franchot
Comptroller

David Roose
Director
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March 1, 2012

Honorable Martin O'Malley
Governor of Maryland
State House
Annapolis, Maryland 21404

Honorable Thomas V. "Mike" Miller, Jr.
President of the Senate
State House
Annapolis, Maryland 21404

Honorable Michael E. Busch
Speaker of the House
State House
Annapolis, Maryland 21404

Dear Governor, President and Speaker:

As required by Maryland Tax-General Article Section 10-402, I am submitting this report on the impact of the change in the apportionment of income of manufacturing corporations from a three-factor formula of property, payroll and double-weighted sales to a single-factor formula consisting solely of sales. The change to the single-factor apportionment formula for manufacturers was adopted under Chapter 633, Acts of 2001, applicable to tax years beginning on or after January 1, 2001.

Our analysis finds that tax year 2009 corporate income tax revenues for corporations that were required to file the information report were about $5.9 million lower with the single factor apportionment than they would have been under the three-factor apportionment. In 2008, revenues were about $12.6 million lower. This loss in tax year 2009 equates to a reduction of about 4.5% of the $130.7 million tax year liability of all manufacturers and agricultural corporations (excluding refiners, who are exempt from using a single-sales apportionment), and about 0.7% of the total corporate income tax liability.

It should be noted that a small number of corporations greatly affect the net difference of $5.9 million due to higher Maryland modified income. The top ten companies with the greatest liability decrease under the single-sales calculation account for $19.3 million of the loss of revenue. On the other hand, the 10 companies with the greatest liability increase account for $17.1 million of the offsetting revenue gain for the State. Without the changes associated with these 20 corporations, the net impact of the single-factor apportionment for manufacturers for tax year 2009 would have been a revenue loss of approximately $3.7 million.

This report represents information gathered from those corporations who returned Form 500MC through February 2012. The 500MC is used to gather tax information for multistate manufacturing corporations with more than 25 employees in order to help determine the effect of single sales and three-factor apportionment on these companies. Information from corporate income tax returns is based on returns processed through December 6, 2011, for tax year 2009. Because the 2010 tax return filing deadline for corporations that file on a fiscal year basis has not yet been reached, the tax return data from tax year 2010 is not yet complete. For this reason, the tax year 2010 analysis will be included in the 2013 report.

I hope you find this report informative. If you should have any questions or concerns regarding this report, please do not hesitate to contact me at 410-260-7450.

Sincerely,

David F. Roose

Attachment

cc. Comptroller Peter Franchot
Len Foxwell
Linda Tanton

SINGLE SALES FACTOR APPORTIONMENT FOR MANUFACTURING CORPORATIONS TAX YEAR 2009

Chapter 633, Acts of 2001 (Maryland Tax-General Article Section 10-402), altered the determination of how income of a manufacturing corporation that does business in Maryland and other states is allocated to Maryland for purposes of income taxation. Prior to enactment of the law, income was apportioned based on how much property, payroll and sales (double-weighted) were in Maryland relative to the whole. Under the new law, manufacturers' income is apportioned to Maryland based solely on the ratio of sales in Maryland to total sales. The change to a single-factor formula of sales reduces income tax liability for corporations with a relatively large presence in the State. Tax liability decreases when the average of the property and payroll factors is greater than the sales factor, and increases when the average is less than the sales factor.

Corporations with North American Industry Classification System (NAICS) codes 11 and 31 through 33 are required to attach a 500 MC to their return. Industries in NAICS code 11 are Agriculture, Forestry, Fishing and Hunting; the following manufacturing industries are included in codes 31 through 33:

- 311 Food
- 312 Beverage and Tobacco Products
- 313 Textile Mills
- 314 Textile Product Mills
- 315 Apparel
- 316 Leather and Allied Products
- 321 Wood Products
- 322 Paper
- 323 Printing and Related Support Activities
- 324 Petroleum and Coal Products
- 325 Chemicals
- 326 Plastics and Rubber Products
- 327 Nonmetallic Mineral Products
- 331 Primary Metals
- 332 Fabricated Metal Products
- 333 Machinery
- 334 Computer and Electronic Products
- 335 Electrical Equip., Appliances, & Components
- 336 Transportation Equipment
- 337 Furniture and Related Products
- 339 Miscellaneous

A total of 1,468 corporations, with relevant NAICS codes, filled out a 500MC in tax year 2009, 58 fewer than in tax year 2008. Based on information reported on 2009 corporate income tax returns, federal taxable income reported on all 5,110 non-refiner manufacturing and agricultural returns totaled $1.5 billion; excluding negative values, total federal taxable income for those corporations was $126.5 billion. After statutory addition and subtraction modifications, positive Maryland modified income apportioned to Maryland using the single-factor formula totaled $1.6 billion. For 2009, the total tax liability on all 2009 returns of manufacturing (excluding refiners) and agricultural corporations as they were filed and processed was $130.7 million. Of the 5,110 returns filed by manufacturing corporations, 3,425 – or 67.0% – were unaffected by the change to the single-factor apportionment formula because they were not multi-state (1,618), or had no positive Maryland modified income (1,807).

For the 1,468 corporations that returned the information report, Form 500MC, tax liability increased by more than $10 under the single-sales formula for 380 corporations at an average of $69,461. For 239 corporations, tax liability declined by more than $10 by an average of $135,063. The remaining 849 corporations saw no significant change in tax liability between the two apportionment calculations.

Based on the information reported by the corporations who returned Form 500MC, the change from the three-factor method of apportionment to a single-factor method resulted in a revenue loss of $5.9 million for the State for tax year 2009, compared with a loss of nearly $12.6 million for the for tax year 2008. This represents a decrease of 4.5% in the total 2009 tax liability of the non-refiner manufacturing and agricultural sectors, and about 0.7% of the total corporate income tax liability for tax year 2009.

The attached tables provide the revenue impact of the law change by three-digit NAICS code. Several industry codes were combined to avoid the disclosure of confidential tax information. The majority of the manufacturing industries saw an increase in tax liability under the single-sales calculation. The largest net decrease (approximately $6.7 million) occurred within industry codes 110-115 & 339: Agriculture, Forestry and Logging, Fishing, Hunting & Trapping, Support Activities for Agriculture and Forestry, and Misc. Manufacturing. This is most likely due to the fact that the companies in these industries have a greater share of property, plant and equipment in Maryland than other manufacturing industries and that they were among the more profitable sectors. This group also makes up a large majority of the firms that filed a 500MC at approximately 18.5% of the total. The industry grouping with the largest net *increase* in tax liability under the single-sales formula was industry codes 311-316, Food, Beverage & Tobacco, Textile Mills, Textile Product Mills, Apparel, Leather & Allied Products. The net increase was just over $7.4 million; this group makes up 10.8% of the companies that reported[1].

In addition to requesting tax and other financial data, Form 500MC also included two questions. For the first, which asked if the corporation was headquartered in Maryland, 134 corporations responded in the affirmative, and reported that their tax liability was $13.4 million lower under the single-sales regime. The second question asked “at any time after 2000, was Maryland sales transferred from the manufacturing company to a non-Maryland sales/distribution company?” To that question, 27 corporations answered affirmatively, reporting a reduction in tax liability of about $274,557 for tax year 2009.

It should be noted that the $5.9 million revenue loss provided in this report is not the actual impact of single-sales apportionment for manufacturing corporations since those corporations with fewer than 25 employees are not required to file the information report. For the tax year 2001 and 2002 reports, the information needed to calculate the impact for all corporations was required to be reported on page two of the corporations’ Maryland tax returns and the reported revenue loss estimates included all of those corporations. It should also be noted that the change from a three- to a single-factor formula not only affects the apportionment of income by corporations, but also affects the apportionment of income by multi-state subchapter-S corporations with one or more nonresident shareholders, partners or members. While certain data is captured from returns of pass-through entities, the return is primarily for informational purposes and is not tied in an automated manner to the returns of its shareholders, partners or members where the calculation of tax liability is made. For this reason, the revenue impact from the change in apportionment formulas for this group cannot be determined.

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[1] These groups have been combined for disclosure purposes and to maintain similar grouping in this and prior reports. The majority of the revenue decrease results from firms in industry 339, Miscellaneous Manufacturing. The majority of the revenue increase results from firms in industry code 331, Food Manufacturing.

NAICS Group		Total Positive Taxable Income			Change in Tax Liability					
			Maryland Using:		Increase		Decrease		No change	Net Change
		# Returns	Single-Factor	3-factor	#	$	#	$	#	$
311-316	Food, Beverage & Tobacco, Textile Mills, Textile Product Mills, Apparel, Leather & Allied Products	159	344,705,261	254,727,223	58	9,843,147	31	(2,419,960)	70	7,423,187
321-322 &337	Wood Products, Paper, Furniture Produ	92	22,700,667	21,139,264	23	691,824	11	(562,993)	58	128,831
323-324	Printing & Related Support Activities, Pe	53	29,144,145	30,887,625	8	306,533	12	(450,372)	33	(143,838)
325	Chemicals	172	143,435,503	128,275,247	39	4,511,139	31	(3,260,422)	102	1,250,717
326	Plastics & Rubber Products	39	5,897,273	9,578,002	10	149,896	8	(453,557)	21	(303,661)
327	Nonmetallic Mineral Products	56	7,770,255	7,379,611	12	137,550	11	(105,322)	33	32,228
331	Primary Metals	36	6,190,873	39,871,255	7	201,533	10	(2,980,165)	19	(2,778,632)
332	Fabricated Metal Products	122	18,406,073	27,652,392	30	271,812	16	(1,034,632)	76	(762,820)
333	Machinery	149	20,923,903	21,089,141	41	437,958	18	(451,588)	90	(13,630)
334	Computer & Electronic Products	150	89,891,055	110,615,158	32	1,384,981	18	(3,094,714)	100	(1,709,733)
335	Electrical Equip., Appliances, & Compor	90	15,013,273	38,209,937	27	357,668	16	(2,271,394)	47	(1,913,725)
336	Transportation Equipment	78	230,660,909	234,909,074	14	5,684,186	16	(6,034,663)	48	(350,477)
110-115 & 339	Agriculture, Forestry and Logging, Fishing, Hunting & Trapping, Support Activities for Agriculture and Forestry, Misc. Manufacturing	272	137,215,733	218,955,399	79	2,416,825	41	(9,160,348)	152	(6,743,523)
Total		**1,468**	**1,071,954,921**	**1,143,289,330**	**380**	**26,395,052**	**239**	**(32,280,131)**	**849**	**(5,885,079)**