



Maryland State Bar Association, Inc.

July 14, 2008

*Via electronic (droose@comp.state.md.us)
and First Class Mail*

David F. Roose
Director, Bureau of Revenue Estimates
Comptroller of Maryland
80 Calvert Street
Annapolis, Maryland 21401

Dear Mr. Roose,

Thank you for providing the draft regulations for Tax General §§ 10-402, 10-804 and 10.804.1, Maryland's new corporate reporting requirements, to the Section of Taxation of the Maryland State Bar Association ("the Section"). I am writing on behalf of the Section to provide comments. Please note that due to time constraints, the comments provided herein may be incomplete. To the extent necessary, the Section may submit additional comments during the regulation approval process. The following comments are the views of the Section of Taxation, but do not necessarily represent the position of the Maryland State Bar Association.

As an initial observation, the Section has significant concerns regarding the State's authority to impose such onerous reporting requirements on Maryland corporations, much less those corporate entities that do not have nexus with the State. While the Section understands that it is not the Comptroller's responsibility to challenge the constitutionality of legislation, the Section believes it is important to raise this issue for further discussion.

In addition, Tax Gen. § 10-402 applies only to those manufacturing corporations that have 25 or more employees and, as noted in Tax Gen. § 10-804, are required by law to file Maryland income tax or estimated income tax returns.¹ Tax Gen. § 10-804.1 imposes the new reporting requirements on all corporations that are part of a corporate group and subject to Maryland income tax. It would be helpful if the regulations explain the relationship between these sections, both of which were amended by House Bill 664.

¹ Newly amended Tax Gen. § 10-804 provides that, "[e]ach person *required under this subtitle to file an income tax return or estimated income tax declaration or return* shall . . . attach to an income tax return or otherwise file with the Comptroller any records or statements that the Comptroller requires . . ." Tax-Gen. § 10-804 (emphasis supplied).

With respect to the specific language of the draft regulations, § 02.B provides, "Every corporate group shall file with the Comptroller the following reports..." Section 01.B(2) of the draft regulations define "corporate group" by reference to Tax Gen. § 10-804.1(a)(1), which provides:

(1) "corporate group" means:

(i) an affiliated group or controlled group under § 1504 or § 1563 of the Internal Revenue Code; or

(ii) an affiliated group of corporations:

1. that is engaged in a unitary business; and

2. more than 50% of the voting stock of each member of which is directly or indirectly owned by a common owner or common owners, either corporate or noncorporate, or by one or more members of the group; and

As a preliminary matter, the reference in § 01.B(2) of the draft regulations should be to Tax Gen. § 10-804.1(a)(1) *and* (a)(2), which provides an express limitation on the definition of a "corporate group":

(2) "corporate group" does not include:

(i) any corporation that, for any reason, is not subject to United States federal income tax;

(ii) an insurer as defined in § 1-101 of the Insurance Article; or

(iii) a regulated investment company, as defined in § 851(a) of the Internal Revenue Code.

Moreover, there is no limitation in the definition of "corporate group" to only those corporations subject to Maryland income tax. Thus, the draft regulations appear to impose the reporting requirements on "all" corporations, rather than just those required to file a Maryland income tax return. Because such a result creates an unauthorized expansion of the reach of the law and would certainly violate due process, the Section recommends amending the language of §

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02.B of the draft regulations to: "Every corporate group that includes a corporation required to file a Maryland income tax return shall file with the Comptroller the following reports..." And because a "corporate group" includes affiliates that are not necessarily part of a unitary business (*see* Tax Gen. § 10-804.1(a)(1)(ii)), the Section further recommends that § 02.B of the draft regulations be revised by inserting the phrase, "with respect to the members thereof engaged in a unitary business" after "reports" and before the colon.

The extensive reporting requirements set forth in the draft regulations are not contemplated by House Bill 664. The proposed reporting requirements are unduly burdensome and onerous, particularly for corporations with numerous subsidiaries. Moreover, we suspect that the calculations required to satisfy the reporting requirements will be far too complex and confusing for smaller corporate groups and many return preparers. The Section recommends simplifying the information requested and calculations required. For example, the Comptroller could select one method of reporting, either a Joyce or Finnigan combination, and providing detailed examples of the chosen method to better assist those taxpayers and preparers who attempt in good faith to comply with the reporting requirements.

In addition, the Section recommends modifying the definition of "Finnigan" or "Full Unitary Combination" in § 01.B(5)(b)(ii) of the draft regulations by adding the following language at the end of the definition: "where at least one of the corporations is required to file a Maryland corporate income tax return."

An area of significant concern is the penalty section of the draft regulations. While the Comptroller has been directed to develop and implement an oversight and penalty system to ensure that corporations provide the required disclosure statements in a timely and accurate manner, the amount and nature of the penalties proposed go well beyond deterrence and instead, border on extreme retribution.

The existing penalty regime set forth in Subtitle 7 of Title 13 of the Tax General Article does not use *per diem* penalties. Because Tax Gen. § 10-804.1 imposes a reporting requirement for purposes of evaluating a change to combined reporting, and has nothing to do with a taxpayer's actual compliance and tax liabilities, a one-time fixed penalty, with a one-time increase for failure to comply after notice from the Comptroller, is more reasonable and appropriate. Moreover, a *per diem* penalty is certain to raise far more administrative issues and burdens, including challenged computations and waiver requests, than a fixed penalty.

The Section recommends a one-time fixed penalty for failure to comply with the reporting requirements. The amount of penalty should take into account the size of the company involved. In addition, § 03.A should expressly provide that no penalty will be imposed where the failure to comply is due to reasonable cause. Based on the foregoing, the Section proposes the following revision to § 03.A of the draft regulations:

03.A. Failure to file required reports.

(1) In the case of failure to file the reports required under this chapter, unless it is shown that such failure is due to reasonable cause and not due to willful neglect, the Comptroller shall assess the penalties set forth herein.

(2) The penalty to be assessed shall initially equal \$1,500 for companies with gross Maryland revenue less than \$2,500,000; \$3,000 for companies with gross Maryland revenue equal to or in excess of \$2,500,000 to less than \$10,000,000; and \$5,000 for companies with gross Maryland revenue equal to or in excess of \$10,000,000. If a company does not comply within sixty (60) days after receiving written notice from the Comptroller of failure to file appropriate reports, the penalty shall increase to \$5,000 for companies with gross Maryland revenue less than \$2,500,000; \$10,000 for companies with gross Maryland revenue equal to or in excess of \$2,500,000 to less than \$10,000,000; and \$35,000 for companies with gross Maryland revenue equal to or in excess of \$10,000,000.

In addition, the time for correcting inaccurate reports should be extended beyond 20 days. As such time period runs from the date of the notice, more response time is needed to account for the potential of time passage until the notice is actually mailed, the period of time in the mail, and the potential for intervening weekends and holidays. The Section recommends a minimum 60-day correction period running from the date the Comptroller issues written notice to the corporate group, particularly in light of the complexities of the calculations required. The draft regulations should provide that all such notices must be sent to each member of the corporate group that would be subject to penalties for failure to comply with the reporting requirements.

With respect to imposition and collection of any penalties imposed, the Section recommends revision of § 03.C to account for the fact that Maryland does

not have jurisdiction over the members of a corporate group that do not have nexus with the State. In addition, the language should be amended to provide that the penalties imposed are "joint and several" and not cumulative, and to the extent the Comptroller collects a penalty, or portion thereof, from one member of the corporate group, the Comptroller is required to provide prompt written notice of that payment to the other members of the corporate group and to adjust their accounts accordingly. Based on the foregoing, the Section recommends that § 03.C of the draft regulations be amended as follows:

C.(1) With respect to any penalties assessed under this chapter, all members of the corporate group that are required to file a Maryland income tax return or that are engaged in a unitary business will be jointly and severally liable for the penalties assessed.

(2) To the extent a member of a corporate group pays all or a portion of a penalty assessed under this chapter, the Comptroller is required to send written notice of such payment, and any remaining balance due as of the date of the notice, to all members of the corporate group assessed with the penalty at issue.

Under Tax Gen. § 10-804.1(c)(3), the Comptroller is required to publish the name of, and penalty imposed on, any corporation failing to file a statement required under this section or filing an inaccurate statement. The draft regulations should provide that the Comptroller will issue written notice of its intent to publish such information to each member of the corporate group and provide the corporate group with an opportunity to come into compliance. In addition, because the draft regulations specifically provide for an opportunity to correct an inaccurate report, the draft regulations should further provide that no publication pursuant to Tax Gen. § 10-804.1(c)(3) will occur until a corporate group is given notice of any deficiency and a reasonable (i.e., 45 days) opportunity to cure.

Finally, the penalty appeal rights under the draft regulations are unclear. Under § 03.D of the draft regulations, a taxpayer can appeal a penalty assessed by seeking revision pursuant to Tax Gen. § 13-508. The draft regulations further provide that, "[a]ll statutes and regulations applicable to the informal hearing procedures set forth in § 13-508 shall apply.... [and] [a]fter the Comptroller's hearing officer issues a notice of final determination, the provisions of Maryland law regarding administrative and judicial review shall apply." Regs. § 03.D(1) and (2). However, § 03.E of the draft regulations, without citation to statute, provides that the Comptroller's refusal to waive a penalty, or decision to waive a

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part, but not the full amount of, a penalty, assessed under the regulation "shall be final and not subject to appeal." It is unclear whether the purpose of § 03.E of the draft regulations is to allow for consideration of "reasonable cause" or to provide for correction of erroneous assessments as contemplated by Tax Gen. § 13-509.

Assuming that § 03.A(1) of the draft regulations is amended as suggested herein by adding the "reasonable cause" language, the Section recommends the removal of § 03.E. A taxpayer's right to appeal is clearly provided in § 03.D of the draft regulations and the authority of the Comptroller to address late appeals is already provided by Tax Gen. § 13-509. Alternatively, the Section recommends amending § 03.E of the draft regulations to provide:

E. To the extent the imposition of a penalty has been upheld following a taxpayer's appeal as contemplated in § 03.D, or if no timely appeal was filed, the Comptroller may issue an order abating or decreasing the penalty assessed to correct an erroneous assessment as contemplated in Tax Gen. § 13-509.

The Section appreciates the Comptroller's invitation to participate in this process. Should you have any questions regarding the Section's comments, or if the Section can provide additional assistance, please contact:

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You may also contact me at (410) 547-7852 or cciraolo@rosenbergmartin.com. Thank you again for this opportunity to comment on the draft regulations.

Very truly yours,



Caroline D. Ciralo
Chair, Section of Taxation