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This Week in State Tax (TWIST)

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Massachusetts: Tax Conference Agreement Includes Corporate Tax Changes

After weeks of negotiations, the Massachusetts House and Senate agreed to a tax compromise plan that includes components of earlier House and Senate tax proposals. The legislation, H. 4104, was quickly passed by both chambers and as of Monday, October 2, 2023, was awaiting action by Governor Healey.

The final agreement incorporates changes to the corporate excise tax law that were included in the earlier House tax bill and reduces the tax rate on short-term capital gains. The legislation also includes many provisions aimed at providing tax relief for individuals, including but not limited to, an expanded tax credit for children, disabled adults, and seniors, an expanded estate tax exemption, and tax breaks for renters and senior citizens.

General Corporation Apportionment Changes: Under current law, the income of a corporation is apportioned to the Commonwealth by multiplying net income by a fraction, the numerator of which is the property factor plus the payroll factor plus twice the sales factor, and the denominator of which is four. Certain entities- manufacturing corporations, mutual fund service providers, and defense corporations- use single sales factor apportionment. Effective January 1, 2025, all corporations will apportion net income to the Commonwealth by use of the sales factor only. Oddly, the effective date does not address the specific "tax years" to which the move to single-sales factor apportionment applies.

The bill also makes changes to reflect that all corporations will now be using single sales factor apportionment.

Financial Institution Apportionment Changes: Currently, financial institutions apportion receipts to Massachusetts using an evenly weighted three factor property, payroll, and receipts factor formula. Effective January 1, 2025, financial institutions will apportion net income to the Commonwealth using the receipts factor only. The bill also revises the provisions addressing how financial institutions source interest, dividends, net gains and other income from investment assets and activities and from trading assets and activities under Mass. G.L. c. 63 § 2A(d)(xii). Currently, this amount is determined by multiplying various categories of income from such assets and activities by a fraction, the numerator of which is the average value of the assets assigned to a regular place of business of the taxpayer within the Commonwealth and the denominator of which is the average value of all such assets of the institution.

Effective January 1, 2025, the amount of such receipts included in the Massachusetts numerator will be determined by multiplying all income from such assets and activities by a fraction. The numerator of the fraction is the total receipts included in the numerator pursuant to Mass. G.L. c. 63 § 2A(d)(i) through (x), which are the statutory sourcing rules for various types of income of a financial institution, and paragraph (xii). The denominator of the fraction is all total receipts of the taxpayer included in the denominator other than interest, dividends, net gains, but not less than zero, and other income from investment assets and activities and trading assets and activities. While the intent of the law appears to be to source interest, dividends, net gains, and other income from investment assets and activities and from trading assets and activities based on a financial institution's other Massachusetts receipts, the reference to including receipts from paragraph (xii) in the numerator is somewhat circular; paragraph (xii) informs a financial institution how such receipts should be attributed to the Commonwealth.

The bill strikes language in the statute that addresses the computation of the property and payroll factors for a financial institution.

Individual Tax Changes: Currently, individuals are taxed on their short-term capital gains at a rate of 12 percent. H. 4101 reduces the rate on the gain from the sale or exchange of capital assets held for one year or less to 8.5 percent effective for tax years beginning on or after January 1, 2023. In addition, the individual income tax code has been revised to require married persons to file a joint tax return if they file a joint federal tax return. The purpose of this change is to ensure that married couples cannot avoid the new so-called Millionaire's Tax, which was approved by voters last November. Under the revised law, effective for tax years beginning on or after January 1, 2023, the flat individual income tax rate was increased from 5 percent to 9 percent on income above $1 million. It should be noted that a working draft TIR was recently issued in Massachusetts that indicates a nonresident's income would be subject to the 4 percent surtax on income over $1 million if the nonresident's Massachusetts source income exceeded the threshold. This provides clarity as there was concern that a proportional amount of Massachusetts income might be subject to the surtax if the nonresident's federal income exceeded $1 million.

Another change affecting individuals involves the so-called "Chapter 62F refunds." Under Massachusetts law, when tax revenues exceed a certain amount in a given fiscal year, the excess revenue is refunded to individual taxpayers. Historically, a taxpayer's refund was based on a percentage of their personal income tax liability for the given year. Effective for tax years beginning on or after January 1, 2023, the refund will be provided based on the number of personal income taxpayers filing an income tax return in the previous taxable year. In other words, each personal income taxpayer will receive the same refund amount, regardless of their personal income tax liability. Persons that are married filing jointly count as two taxpayers. Please contact George Burns or Jamie Posterro with questions on H. 4101.