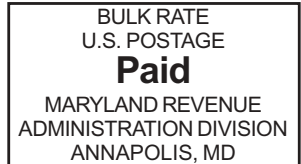



Forwarding Service Requested



- 
- Remove the label and attach it to the return you are filing.
 - If someone else prepares the return, ask the preparer to use the label.
 - If any information on the label is incorrect, please do not use the label.

2001

Maryland Tax Forms for Pass-Through Entities

**Forms and instructions for filing pass-through entity income tax returns
for calendar year or any other tax year or period beginning in 2001.**

This booklet includes:

- Form 510 - Pass-Through Entity Income Tax Return
- Form 510E - Application for Extension of Time to File Pass-Through Entity Income Tax Return
- Form 510D - Declaration of Estimated Pass-Through Entity Nonresident Tax

Important reminders:

- Read the instructions in this booklet.
- Use the above label on Form 510.
- Enter the Federal Employer Identification Number (FEIN) and taxable year beginning and ending dates on all forms and payments.
- Sign and date the return and use the appropriate envelope provided in this booklet.

New businesses can
register online &
set up tax accounts
when visiting our
website at
www.marylandtaxes.com
See the back of this
booklet for more
details.



William Donald Schaefer

Maryland Pass-Through Entity Taxpayers

This booklet contains the forms and instructions necessary for a pass-through entity to file a 2001 Maryland tax return. Please read the instructions and forms carefully.

Form 510 and its related forms are to be used by partnerships, S corporations, limited liability companies (LLC) and business trusts.

Manufacturing corporations are subject to a special single factor formula of receipts. The rules for calculating this single factor can be found in Maryland Regulation 03.04.03.10. A manufacturing corporation that has more than 25 employees and apports its income, must complete all three (3) factors on page 2 of Form 510.

A business trust shall be classified as a corporation, a partnership, a trust or otherwise, as shall be determined under the United States Internal Revenue Code.

The pass-through entity return is generally an information return. The entity's income or loss is passed through to the individual partners, shareholders or members for taxation purposes.

Pass-through entities are required to pay the personal income tax on behalf of nonresidents at a tax rate of 4.80% of the nonresident partner's, shareholder's or member's distributive or pro rata share of income allocable to Maryland. The amount of tax payable by the pass-through entity may be limited based on the distributable cash flow. For additional information, see the instructions for pass-through entity nonresident tax.

Nonresident partners and shareholders must file a nonresident return, Form 505. Credit may be claimed on the nonresident return for any tax paid on behalf of the nonresident by the pass-through entity. Taxpayers may elect to file a composite return on behalf of qualified nonresident partners, shareholders and members under which the entity would be the agent to receive any refund or to pay any tax due. See Administrative Release #6 for more information. You can obtain Release #6 from any Maryland taxpayer service office or from our website at www.marylandtaxes.com or request it from our Forms-by-Fax service by calling 410-974-FAXX (3299).

Certain investment partnerships are not subject to the nonresident tax. See the Specific Instructions for line 4.

Form 500CR

Form 500CR is used by individuals and businesses to claim allowable business tax credits, as listed below. You can obtain Form 500CR from any Maryland taxpayer service office or our web site at www.marylandtaxes.com, or by calling our Forms-by-Fax service at 410-974-FAXX (3299).

Businesses That Create New Jobs Tax Credit

* Clean Energy Incentive Act

* Commuter Tax Credit

Electric and Gas Utility Credits

Employer Provided Long-term Care Insurance Credit

Employment of Individuals with Disabilities

Employment Opportunity Tax Credit

* Enterprise Zone Tax Credit

Heritage Area Mortgage Credit

Job Creation Tax Credit

Maryland Disability Employment Tax Credit

Maryland-mined Coal Tax Credit

Neighborhood Partnership Program

One Maryland Economic Development Tax Credit

* Research and Development Tax Credit

Telecommunications Property Tax Credit

Water Quality Improvement Credit

Work-based Learning Program Credit

* These credits were modified for tax year 2001, see Form 500CR.

Businesses that claim a credit for the rehabilitation of a heritage structure must complete Form 502H for the Heritage Area Tax Credit.

Forms and help

For online business registration, tax forms, instructions, publications, and Maryland Tax

Regulations, visit our website at:

www.marylandtaxes.com

To obtain forms by fax:

410-974-FAXX (3299)

E-mail your tax questions to us at:
taxhelp@comp.state.md.us

For assistance, call:

410-260-7980

in Central Maryland or

1-800-MD TAXES (638-2937)
from elsewhere

PASS-THROUGH ENTITY INCOME TAX RETURN

GENERAL INSTRUCTIONS

FILING FORM 510

Purpose of Form Form 510 is used by a pass-through entity to file an information income tax return for a specific tax year or period. The term pass-through entity includes partnerships as defined in Internal Revenue Code Section 761, S corporations as defined in Internal Revenue Code Sections 1361 and 1362, limited liability companies as defined in Maryland Corporation & Associations Article Section 4A-101 and Business Trusts in Maryland Corporation and Association, Article Section 12-101.

An LLC is treated as a partnership for Maryland income tax purposes, unless it is treated as a corporation for federal income tax purposes.

A business trust shall be classified as a corporation, a partnership, a trust or otherwise, as shall be determined under the United States Internal Revenue Code.

NOTE: If you are an unincorporated pass-through entity please follow the rules for partnerships and partners throughout these instructions. If you are an incorporated pass-through entity please follow the rules for S corporations and shareholders.

Generally, Maryland will follow the same rules for the "check-the-box" regulations as those promulgated by the IRS in the treatment of entities which are affected by the regulations.

Taxpayers Required to File Every Maryland pass-through entity must file a return on Form 510, even if it has no income or the entity is inactive. Every other pass-through entity which is subject to Maryland income tax law must also file on Form 510.

A multistate pass-through entity which operates in Maryland but is not subject to the Maryland income tax law is not required to file, although a return reflecting no income allocable to Maryland may be filed for record purposes. Letters in lieu of filing will not be accepted.

Qualified Sub-S Subsidiaries are treated as divisions under the Internal Revenue Code and are not considered as separate entities for Maryland purposes. These divisions will be included on the parent company's annual Maryland return.

When and Where to File File Form 510 by the 15th day of the 4th month following the close of the taxable year or period if a partnership or by the 15th day of the 3rd month if an S corporation. The return must be filed with the Comptroller of Maryland, Revenue Administration Division, Annapolis, Maryland 21411-0001.

Signatures Required Form 510 must be signed by a duly authorized official of the pass-through entity. Preparers, other than pass-through entity employees, must also sign the return.

GENERAL INFORMATION FOR FORM 510

Accounting Periods The taxable year or period used for the federal return must be used for the Maryland return. Accordingly, calendar tax years, fiscal tax years, and short tax periods may be necessary for Maryland filing purposes.

If a federal return is filed or required, a corre-

sponding Maryland return must be filed. The form used for filing must reflect the preprinted tax year in which the pass-through entity's tax year begins.

Use of Federal Figures In preparing Form 510, all items that are reported for federal purposes must be reported on the Maryland return in the same manner. The character of an item cannot be changed from that required or elected for federal purposes.

Taxability Form 510 is generally an information return and payment of income tax is not required. The items of income or loss are passed through to the individual partner or shareholder and taxed at that level. Each partner or shareholder must file a personal income tax return on Form 502 (Form 505 for nonresidents).

If there are nonresident partners or shareholders the **pass-through entity nonresident tax** applies. Pass-through entities are required to pay the personal income tax on behalf of nonresidents; the tax is 4.80% of the nonresident partners' or shareholders' distributive or pro rata share of income allocable to Maryland. When the tax is expected to exceed \$1,000, the pass-through entity must make quarterly estimated payments. See Form 510D for instructions.

NOTE: The terms nonresident partner and shareholder do not include a partner or shareholder which is: 1) a corporation, including an S corporation; 2) a partnership; 3) an organization which is exempt under IRS code; 4) an estate; or 5) a trust.

The distributive share for partnerships is the net amount of lines 1 through 7 of the federal Form 1065-Schedule K. The pro rata share for S corporations is the net amount of lines 1 through 6 of the federal Form 1120S-Schedule K.

The amount of tax payable by the pass-through entity may be limited based on the distributable cash flow. For additional information see the instructions for distributable cash flow limitation.

Nonresident partners and shareholders must file a personal nonresident return, Form 505. Nonresident partners and shareholders must report their distributive or pro rata share of income received from a partnership or S corporation attributable to business conducted in Maryland. Such income must be reported in the partner's or shareholder's taxable year in which the partnership's or S corporation's taxable year ends. Credit for taxes paid by the partnership or S corporation must be claimed on the same return on which the nonresident reports the income which is subject to that tax.

A partnership or S corporation may elect to file a composite return on behalf of qualified nonresident partners and shareholders. All partners and shareholders who qualify and elect to be included on the composite return must agree that the partnership or S corporation is their agent for the receipt of any refund or for payment of any tax due.

If there is S corporation **income subject to federal corporate income tax**, such as excess net passive income, built-in gains or LIFO recapture, that income is also subject to Maryland corporate income tax. If the corporation is subject to the federal corporation income tax, use Form 500 – Corporation Income Tax Return to calculate the amount of Maryland corporate income tax.

On the Form 500: (1) Enter the corporate name, Federal Employer Identification Number and taxable year. (2) Enter the total taxable income on line 1, check the applicable box labeled "Other" and enter "1120S". (3) Report addition and subtraction modifications to the extent applicable to the income subject to federal income tax. (4) Complete all other lines as necessary to calculate the amount due (including the lines for modification to income, apportionment of income and payments and credits, if applicable). Attach payment of the balance due to the front of Form 500.

In addition to filing Form 500 to calculate and pay the corporate income tax, file Form 510 – Pass-Through Entity Income Tax Return for information purposes.

OTHER MATTERS

Extension of Time to File If unable to file Form 510 by the due date, the pass-through entity must submit Form 510E – Application for Extension of Time to File Pass-through Entity Income Tax Return.

The request for extension of time to file will be automatically granted and will not be acknowledged, provided that:

- 1) the application is properly filed and submitted by the 15th day of the 4th month following close of the tax year or period for partnerships or by the 15th day of the 3rd month for S corporations.
- 2) an application for extension of time has been filed with the Internal Revenue Service or an acceptable reason has been provided with the Maryland application.

Properly and timely filed requests for extension of time will be automatically granted for three months for partnerships and six months for S corporations.

Audits and Appeals All items reported on Form 510 are subject to audit, verification and revision. Returns and amendments are subject to audit and adjustment for a period of 3 years from the date the return was due (including extensions) or the date the return was filed, whichever is later.

In the event of revision, the Maryland Revenue Administration Division will notify the pass-through entity.

Amended Returns To correct an error in a previously filed return, complete and submit a revised Form 510 checking the box for "AMENDED RETURN" on page 1. A separate page should be attached containing a detailed explanation of the changes being made, and if the federal return has been amended, a copy of the federal amended form must be attached to Form 510. If additional tax was paid with the filing of the original return, include the amount paid on line 10b of Form 510. A Form 502X – Amended Maryland Tax Return must also be submitted for each partner's or shareholder's income tax return (Form 502 or 505).

Statements to Partners or Shareholders The federal Form K-1 provided by the pass-through entity must be modified to include: the share of Maryland addition and subtraction modifications, the share of credits from Forms 500CR and 502H (see front inside cover) and, in the case of nonresident individuals, the amount of income attrib-

utable to Maryland sources and the amount of tax paid on behalf of the partner or shareholder receiving the Form K-1.

Internal Revenue Service Adjustments If the items on the federal return are adjusted by the Internal Revenue Service (IRS), a copy of the final IRS adjustment report must be submitted within 90 days. Copies of the IRS adjustment report must be submitted for each partner's or shareholder's personal income tax return (Form 502 or 505).

Taxpayer Identification Required for Returns and Other Documents All returns, correspondence, payments or other documents must indicate the pass-through entity name, Federal Employer Identification Number, type of tax and tax year(s) to which the document relates.

All pass-through entities are required to secure a Federal Employer Identification Number from the Internal Revenue Service (IRS). The Federal Employer Identification Number is the only number used by the IRS for processing purposes and is also the primary number used by the Maryland Revenue Administration Division. For returns filed without the federal number a temporary number will be assigned for processing purposes until the actual number is provided.

The type of tax and tax year(s) are necessary to identify the subject of the document and the intention of payments. This information ensures that documents are directed to the correct area and that payments are applied to the correct account.

Use of Paid Preparers The pass-through entity is responsible for the timely filing of returns, payment of tax, responding to requests and all other requirements, even though a paid preparer is used.

Substitute Forms Maryland income tax returns may be reproduced and filed on computer-prepared or computer-generated substitute forms provided that they are approved in advance by the Maryland Revenue Administration Division. Reproductions or substitutes of forms in which machine-readable taxpayer information has been preprinted by the Revenue Administration Division may not be used.

For additional information, see Administrative Release No. 26, Procedures for Computer-Printed Substitute Forms, which can be obtained from any office of the Maryland Revenue Administration Division. (See back cover of packet for address and phone number for substitute forms information.)

Employer Withholding of Income Tax Employers that make payments to individuals of salaries, wages or compensation for personal services must withhold an income tax as prescribed in published tables and remit the withholdings to the Maryland Revenue Administration Division.

The tax withheld must be remitted with Form MW506 – Employer's Return of Income Tax Withheld on a monthly basis if the quarterly withholding is \$700 or more. If the quarterly withholding is less than \$700, the tax withheld is to be remitted quarterly. Employers may not change from monthly to quarterly without approval of the Revenue Administration Division.

An annual reconciliation is required to be filed on Form MW508 – Annual Employer Withholding Reconciliation Report and submitted with the state copy of the wage and tax statements issued to employees. If the employer is required to submit wage and tax statement information on magnetic media for federal reporting purposes, it is required to submit magnetic media for state reporting purposes.

For additional information regarding employer

withholding tax, contact the Maryland Revenue Administration Division. (See back cover of packet for address and phone number.)

Privacy Notice The Maryland Revenue Administration Division requests tax return information to administer the income tax laws of Maryland, including the determination and collection of the correct taxes and other amounts. Failure to provide all or part of the requested information may result in the disallowance of claimed amounts and an increased tax liability. In addition, the law makes provision for securing information from taxpayers that fail to supply required information, and a penalty may apply.

Taxpayers have a right to access their tax records maintained by the Revenue Administration Division, and may inspect, amend or otherwise correct them. To obtain a copy of such tax records, submit a written request containing the pass-through entity name, address and identification numbers and specifying the information needed. The request must be signed by an authorized partner or shareholder.

As authorized by law, information furnished to the Revenue Administration Division may be given to the Internal Revenue Service, a proper official of any state that exchanges tax information with Maryland, and to an officer of this State having a right to the information in that officer's capacity. Also, the information may be obtained in accordance with a proper judicial or legislative order.

SPECIFIC INSTRUCTIONS

SPECIAL NOTE: Complete the federal income tax return first and use it in preparation of the Maryland return. Use a minus sign (-) in front of the number to indicate a negative amount.

Name, Address and Other Information IMPORTANT — IF A LABEL HAS BEEN PROVIDED, PLEASE ATTACH IT TO THE DESIGNATED AREA ON THE FORM 510. IF SOMEONE ELSE IS PREPARING THE RETURN, GIVE THE PREPARER THE LABEL SO THAT IT MAY BE USED. If any of the information on the label is incorrect, **DO NOT USE THE LABEL.**

If you do not have a label, type or print the required information in the designated area. Enter the exact pass-through entity name and continue with any "Trading As" (T/A) name if applicable.

Enter the Federal Employer Identification Number (FEIN). If a FEIN has not been secured, enter "APPLIED FOR" followed by the date of application. If a FEIN has not been applied for, do so immediately.

Enter the date of incorporation and the Federal Business Activity Code. The date of incorporation must be expressed numerically, using two digits each for the month, the day and the year. This code number is a six-digit number available from the federal return which identifies the principal business activity.

Be sure to check the applicable box to indicate the type of pass-through entity: partnership, S corporation, limited liability company or business trust.

Check the applicable box if: (1) the name or address has changed; (2) this is the first filing of the pass-through entity; (3) this is an inactive pass-through entity (in Maryland and elsewhere); (4) this is the final return of a pass-through entity which has dissolved, liquidated or withdrawn from Maryland; or (5) this is a manufacturing entity. Do not check the box for inactive or final if the pass-through entity is inactive in Maryland but active elsewhere. If Form 510 is being amended, check the "AMENDED RETURN" box.

Taxable Year or Period THE TAXABLE YEAR IS SHOWN AT THE TOP OF FORM 510. The

form used for filing must reflect the preprinted tax year in which the pass-through entity's tax year **begins**. The same taxable year or period used for the federal return must be used for Form 510.

If the tax year of the pass-through entity is other than a calendar year, enter the beginning and ending dates of the fiscal year in the space provided at the top of Form 510.

Line 1 - Number of partners, shareholders, or members Enter the number of partners, shareholders, or members that are residents of Maryland, the number that are nonresidents of Maryland, the number of other entities, and the total number of all partners, shareholders or members.

Line 2 - Total distributive or pro rata income per federal return Enter the distributive or pro rata income from the federal pass-through entity return. Distributive or pro rata share is defined for this purpose as the net amount of income/loss for the partnership or S corporation, less interest from federal obligations.

The distributive share for partnerships is the net amount of lines 1 through 7 of federal Form 1065 - Schedule K. The pro rata share for S corporations is the net amount of lines 1 through 6 of federal Form 1120S - Schedule K.

ALLOCATION OF INCOME

For unistate pass-through entities, all income is allocable to Maryland. If the entity is unistate, meaning that business is conducted only in Maryland, do not complete this area.

Multistate pass-through entities, those conducting business in more than one state, must allocate income if there are one or more nonresident partners or shareholders. If there are no nonresident partners or shareholders do not complete this area.

Line 3a - Non-Maryland income Multistate partnerships with one or more nonresident partners may use separate accounting to allocate income. Multistate S corporations with one or more nonresident shareholders may use separate accounting if the activity of the corporation within Maryland is nonunitary. If using separate accounting, enter the amount of income or loss allocable to other states and attach a worksheet detailing the allocation between or among the states.

Line 3b - Maryland apportionment factor Multistate partnerships with one or more nonresident partners may elect the apportionment method of allocation. Multistate S corporations with one or more nonresident shareholders must use the apportionment method unless the activity of the corporation within Maryland is nonunitary. If using the apportionment method, see the instructions for computation of apportionment factor on page 3 and enter the apportionment factor as calculated on Page 2 of Form 510.

Line 4 - Distributive or pro rata share allocable to Maryland For unistate pass-through entities or multistate pass-through entities **without** nonresident partners or shareholders, enter the amount shown on line 2.

For multistate pass-through entities using **separate accounting**, subtract line 3a from line 2 and enter the difference. For multistate pass-through entities using the **apportionment method** of allocation, multiply line 2 by the factor on line 3b and enter the result.

NOTE: Do not complete lines 5 through 9 if:

1. The pass-through entity has no partners or shareholders that are nonresidents of Maryland.

2. The pass-through entity is a partnership whose activities and assets are limited to in-

vestment in stocks, bonds, futures, options or debt obligations other than debt instruments directly secured by real or tangible personal property. It is not subject to the partnership tax merely because the investment decisions, trading orders, research and the like are conducted by a general partner from a Maryland location.

Partnerships, however, such as brokerage firms which deal with the general public, are not exempt if the business is conducted within Maryland and should complete lines 5-9.

Line 5 - Percentage of ownership by individual nonresident partners or shareholders Enter the total percentage of ownership by individual nonresident partners or shareholders. If the profit/loss percentage is different from the ownership percentage, use the profit/loss percentage to complete this line.

Line 6 - Distributive or pro rata share for nonresident partners, shareholders or members Multiply line 4 by the percentage on line 5 and enter the result.

Line 7 - Nonresident tax Multiply the amount on line 6 by 4.80%.

Line 8 - Distributable cash flow limitation Pass-through entities may elect to use the distributable cash flow method to limit the nonresident partner or shareholder tax which must be paid by the entity. If the distributable cash flow is less than the nonresident tax, the required payment is limited to the amount determined by the distributable cash flow method.

utable cash flow method.

Election of the distributable cash flow limitation will not reduce the tax liability of the nonresident partners, or shareholders.

If the distributable cash flow limitation is used, check the box and enter the result on line 8. If less than zero, enter zero. If the distributable cash flow limitation is not used, do not complete this line.

Line 9 - Nonresident partner or shareholder tax due If the distributable cash flow limitation is not used, enter the amount shown on line 7. If the distributable cash flow method is used, enter the lesser of the amount on line 7 or line 8.

Line 10 - Payments

10a. Enter the total of amounts paid during the taxable year with Form 510D-Declaration of Estimated Pass-through Entity Nonresident Tax Return.

10b. Enter any amount paid with Form 510E-Application for Extension of Time to File Pass-through Entity Income Tax Return.

10c. Add the amounts on lines 10a and 10b and enter the total.

Line 11 - Balance of Tax Due If the amount on line 9 is greater than the amount on line 10c subtract line 10c from line 9 and enter the result.

Line 12 - Interest and/or Penalty Calculate the amount of interest and/or penalty due as a result of the underpayment of estimated tax and as a result of late filing of Form 510 and payment of the tax. Enter the total. (Use Form 500UP.)

Line 13 - Total Balance Due Add the amounts

on lines 11 and 12 and enter the result. The total amount due must be paid with Form 510.

NOTE: Overpayments will not be refunded or applied to next year's estimated tax.

Partners', Shareholders' or Members' Information Enter all information requested in this area. Enter the name, address and social security number of all partners, shareholders or members. Also check the applicable box to identify the partner, shareholder or member as a resident or nonresident of Maryland.

For each partner or member, the distributive share of income is a portion of the amount on line 2, page 1 of Form 510. For each shareholder, the pro rata share of income is a portion of the amount on line 2, page 1 of Form 510. Enter the amount of tax paid on behalf of each nonresident individual from line 10c.

Additional Information Required Enter all information requested in these areas on Page 2.

Signature and Verification An authorized officer of the pass-through entity must sign and date Form 510 and enter his or her corporate title. If a paid preparer is used, the preparer must also sign and date the return and enter the firm name and address.

Mailing Instructions Use the envelope provided in the tax package. Also, be sure to read and follow the reminders listed on the back of the envelope.

DISTRIBUTABLE CASH FLOW LIMITATION WORKSHEET

(Complete this worksheet only if using the distributable cash flow limitation.)

- A. Total distributive or pro rata share (adjusted, in the case of an entity using the accrual method of accounting to report federal taxable income, to reflect the amount of taxable income that would have been reported under the cash method of accounting) .. _____
- B. Cash receipts for the taxable year that are not includable in the gross income of the entity including capital contributions and loan proceeds
- C. Amounts allowable to the entity for the tax year as deductions for depreciation, amortization and depletion
- D. The decrease, if any, in the entity's liability reserve as of the end of the taxable year
- E. Total (Add lines A through D)
- F. Cash expenditures for the taxable year that are not deductible in computing the taxable income of the entity, not including distributions to partners or shareholders
- G. The increase, if any, in the entity's liability reserve as of the end of the taxable year
- H. Total distributable cash flow (Add lines F and G, and subtract the total from line E)
- I. Total percentage of ownership (or profit/loss sharing if applicable) by nonresident partners or shareholders
- J. Distributable cash flow (Multiply line H by line I)
- K. Nonresident tax previously paid
- L. Distributable cash flow limitation (Subtract line K from line J. If less than 0, enter 0)

WORKSHEET INSTRUCTIONS

Line A - Enter amount from Form 510, line 2.

Line B - Enter any cash receipts received by the entity that were not included in gross income including capital contributions and loan proceeds.

Line C - Enter the allowable depreciation, amortization and/or depletion used as a deduction from federal taxable income.

Line D - If the entity has established a liability reserve, enter the amount that represents the decrease, if any, in this reserve account. Liability reserve means accrued unpaid liabilities that are not deductible in computing taxable income.

Line E - Add lines A through D and enter total.

Line F - Enter any cash expenditures that are not deducted when computing taxable income for the entity. Items such as distributions to partners or shareholders are not included in this amount.

Line G - If the entity has established a liability reserve, enter the amount that represents the increase, if any, in this reserve account. Liability reserve means accrued unpaid liabilities that are not deductible in computing taxable income.

Line H - Add lines F and G and subtract the total from line E. This is the total distributable

cash flow for the year.

Line I - Enter the amount from Form 510, line 5.

Line J - Multiply line H by line I. This is the portion of distributable cash flow for individual nonresidents.

Line K - Enter all individual nonresident estimated tax paid with Forms 510D or 510E.

Line L - Subtract line K from line J. This is the distributable cash flow limitation for the entity. If this amount is less than 0, enter 0.

INSTRUCTIONS FOR COMPUTATION OF APPORTIONMENT FACTOR - 2001

Pass-through entities that conduct business in more than one state must allocate income if one or more of the partners or shareholders are nonresidents of Maryland. Partnerships may use separate accounting or the apportionment method of allocation. S corporations must use the apportionment method unless the activity in Maryland is nonunitary. If the activity within Maryland is nonunitary, S corporations may use separate accounting.

APPORTIONMENT FORMULA

All factors of the apportionment formula are developed as fractions, the numerator of which is the total of Maryland items and the denominator is the total of items everywhere during the tax year. Each factor is calculated to six decimal places and used to arrive at the final apportionment factor. The items of both numerator and denominator should reconcile to the items as categorized and reported on the federal income tax return.

THREE-FACTOR FORMULA

Multistate pass-through entities using the apportionment method of allocation are generally required to use a three-factor formula of property, payroll and double-weighted receipts. The sum of the property factor, payroll factor and twice the receipts factor is divided by four to arrive at the final apportionment formula. Specific requirements regarding each factor are set forth below:

Receipts Factor The receipts factor includes the amount of income reported during the taxable year as gross receipts or sales (less returns and allowances), dividends, interest, gross rents, royalties, capital gains and other income on the federal return.

Gross receipts from sales of tangible personal property are included in the numerator if the property is delivered or shipped to a purchaser which takes possession in Maryland, regardless of f.o.b. point or other conditions of sale. Sales of tangible personal property to an out-of-state purchaser are also included in the numerator if the purchaser takes possession in Maryland. Sales of property in transit which are destined to Maryland are included in the numerator.

Gross receipts from service-related activities are included in the numerator if the receipts are derived from customers within this State. There are specific rules to determine "Customers Within this State". To review these rules see Maryland Regulation 03.04.03.08 D.

Gross income from intangible items such as dividends, interest, royalties and capital gains from the sale of intangible property are included in the numerator based upon the average of the property and payroll factors.

Gross receipts from the rental, leasing or licensing of real or tangible personal property

are included in the numerator if the property is located within Maryland. If tangible personal property is located in this State for a portion of the tax year, only the income received for that portion is included in the numerator.

Capital gains from the sale of real and tangible personal property are included in the numerator if the property is located within Maryland. Ordinary net gain or loss derived from the sale of depreciable assets is excluded from the factor.

Other income items are included in accordance with the provisions previously stated depending upon the nature and type of each item.

Property Factor The property factor includes owned as well as rented tangible personal property used in the trade or business during the taxable year. Such properties are inventory, machinery and equipment, buildings and land, and other tangible assets. Property is included in the numerator if it has a situs within Maryland.

Property owned by the pass-through entity is valued at its original cost and is reflected in the factor at the average of the tax year beginning and ending amounts. If there are material changes during the tax year and the yearly average is not a fair representation, the average must be calculated on a monthly or daily basis.

Property in transit is considered to be at its destination for purposes of the factor. Property under construction during the tax year is excluded from the factor until actually placed in service.

Property leased or rented by the pass-through entity is included in the factor at a capitalized value. To arrive at the capitalized value, expenses associated with the privilege of occupying or using the property, including such items as fixed rent, percentage rent, real estate taxes, insurance and maintenance, are multiplied by eight. Expenses for gas, electricity, oil, water or other items normally consumed are excluded.

Lease or rental expense below the market rate must be adjusted to reflect a reasonable market rate and then capitalized. Sublease income cannot be used to arrive at the capitalized value of leased or rented property, but must be included in the receipts factor.

Improvements to the leased or rented property (which revert to the owner at expiration of the lease or rental term) are amortized and not capitalized. The actual cost of the improvements is divided by the number of years remaining for the lease or rental term and the result is included in the factor for each tax year.

Property that has remained idle and has not produced any revenue for a period of five or more years is not included in the factor.

Payroll Factor All compensation is to be included in the numerator, both when the individual's service is performed entirely within Maryland, and when the individual's service is performed both within and without Maryland but the service performed outside Maryland is incidental to the individual's service within.

Compensation is also included in the numerator if some part of the service is performed within Maryland and the base of operations or place from which the service is controlled is in Maryland. If the base of operations or place from which the service is controlled is not in any state where the service is performed but the individual's residence is in Maryland, the compensation is also included in the numerator.

OTHER APPORTIONMENT FORMULAS

NOTE: Double-weighted receipts factor provisions are not applicable for pass-through entities subject to the following apportionment formulas.

Pass-through entities engaged in leasing or rental operations are required to use an equally weighted two-factor formula of receipts and property. The receipts and property factors are calculated in accordance with the provisions for those factors of the three-factor formula, except that receipts from intangible items are excluded.

Pass-through entities engaged primarily in certain types of transportation operations are required to use a one-factor formula as follows:

- Trucking operations (motor freight carriers) must use total road mileage traveled in Maryland divided by total road mileage traveled everywhere.
- Railroad operations must use total track mileage traveled in Maryland divided by total track mileage traveled everywhere.
- Shipping operations must use total voyage days in Maryland divided by total voyage days everywhere. Voyage days are the number of days which ships spend in ports and on waterways.
- Airline operations should see Administrative Release No. 22 for instructions.

Banks and similar institutions are subject to special apportionment rules. To review these rules, see Maryland Regulation 03.04.08 or contact the Maryland Revenue Administration Division for instructions. (See back cover of packet for address and phone number.)

Manufacturing corporations are subject to a special single-factor formula of receipts. A manufacturing corporation that has more than 25 employees and apportions its income must complete all three (3) factors on page 2 of Form 510. The rules for calculating the single factor can be found in Maryland Regulation 03.04.03.10 or contact the Maryland Revenue Administration Division for forms and instructions. (See back cover of booklet for address and phone number.)

SPECIAL RULES

If the apportionment formula does not fairly represent the extent of the pass-through entity's activity within Maryland, the Maryland Revenue Administration Division may alter the formula or components accordingly.

The pass-through entity's share of receipts, property and wages of a partnership or joint venture is included in the entity's receipts, property and wage factors as if they were the direct receipts, property and wages of the entity. The partnership share is included only to the extent of the factors required for the pass-through entity.

MARYLAND BUSINESS REGISTRATION & TAXATION

COMPTROLLER OF MARYLAND REGISTRATION & TAXES

Registration and Licensing All new businesses (corporations, S corporations, partnerships, limited liability companies, and sole proprietorships) can file a single application with the Central Registration Unit of the Revenue Administration Division of the Comptroller's Office to establish accounts for employer income tax withholding, sales and use tax, admissions and amusement tax, tire recycling fee, motor fuel tax, alcohol and tobacco tax and unemployment insurance. The Revenue Administration Division offers assistance for filing applications and establishing accounts.

The Central Registration Unit assigns a single state identification number for the taxes listed above.

Corporation Income Tax The corporation income tax applies to every Maryland corporation and every other corporation which has a nexus with Maryland. Nexus is the term used to indicate a taxable connection between a corporation and a taxing authority. If a corporation conducts business activity within Maryland and exceeds the provisions of U.S.C.A. Title 15, Section 381 of the Interstate Commerce Act (P.L. 86-272) it has a nexus and must file an income tax return.

The tax is based on federal taxable income after state modifications. Corporations engaged in multistate operations must allocate income using an apportionment formula, generally consisting of receipts, property and payroll factors. The tax is imposed at a flat rate of 7% of Maryland taxable income.

Employer Withholding of Income Tax Employers making payments to individuals of salaries, wages or compensation for personal services must withhold income tax and remit the withholding to the Maryland Revenue Administration Division. The amount of tax to be withheld is prescribed in published tables which are based on the individual income tax rates. See the General Instructions for Form 500 for additional information on employer withholding requirements.

Sales and Use Tax This tax applies to businesses selling in Maryland or purchasing out of state for Maryland use.

The general Maryland sales and use tax rate is 5% (1¢ tax on each 20¢ or fraction of price). A special 8% rate is imposed on rental trucks, and a special rate of 11½% is charged on rentals of passenger cars and recreational vehicles. Most sales of food by substantial grocery or market businesses are not subject to tax. Specific prepared foods purchased in grocery stores are subject to tax. Other exemptions include all sales solely for resale, medicine, energy for residential use, manufacturing machinery and equipment, and certain agricultural equipment and supplies.

Motor Fuel Tax Generally, this tax applies to businesses selling or using motor fuel in Maryland.

The Maryland motor fuel tax rate is currently 23½¢ per gallon of gasoline and 24¼¢ per gallon of diesel fuel. There are other requirements for motor carriers, dealers, special fuel users, sellers, and service station operators.

Maryland implemented the International Fuel Tax Agreement (IFTA) for motor carriers on January 1, 1996.

Alcohol and Tobacco Tax These taxes apply to businesses manufacturing, selling, distributing or storing alcoholic beverages or selling and/or distributing cigarettes in Maryland.

The Maryland excise tax rates on alcoholic beverages are \$1.50 per gallon of distilled spirits, 40¢ per gallon of wine, and 9¢ per gallon of beer. The tobacco tax rate is 66¢ per pack of 20 cigarettes.

Admissions & Amusement Tax This tax is imposed on a variety of activities, such as admission to any place, including motion pictures, athletic events, races, shows or exhibits. Also subject to this tax are receipts from athletic equipment rentals, bingo, coin-operated amusement devices, boat rides and excursions, amusement rides, golf green fees, golf cart rentals, skating, bowling shoe rentals, lift tickets, riding academies, horse rentals, and merchandise, refreshments, or a service sold or served in connection with entertainment.

The admissions and amusement tax is a local tax collected by the Comptroller's Office for Maryland's counties, Baltimore City, other incorporated cities and towns. The tax is set by the localities at rates varying from one-half of 1% to 10% of the admissions and amusement receipts.

Tire Recycling Fee This fee applies to tire wholesalers or a tire retailer who buys tires from out-of-state sources. Registration and payment of the fee is handled by the Revenue Administration Division.

Utility Surcharge This surcharge is collected from electric companies generating electricity in Maryland for deposit in the Environmental Trust Fund, and from telephone companies doing business in Maryland for deposit in the 911 Emergency Telephone System and Telephone Access of Maryland Funds.

The utility surcharges are collected by the Comptroller's Compliance Division.

OTHER REGISTRATIONS & TAXES

New Corporations In addition to registering with the Central Registration Unit of the Comptroller's Office, all corporations doing business in Maryland must register with the Department of Assessments and Taxation. This is also the office to contact to form a new corporation.

Financial Institution Franchise Tax The franchise tax on commercial banks was replaced with the corporate income tax for the tax years beginning after 12/31/97.

Public Service Company Franchise Tax In addition to corporation income tax, public service companies are also subject to the Department of Assessments & Taxation franchise tax on gross receipts.

Insurance Company Premium Tax Insurance companies are exempt from the corporation income tax and subject to the Department of

Licensing and Regulation premium tax.

Unemployment Insurance Employers are subject to the Department of Labor, Licensing and Regulation unemployment insurance requirements and must file a combined registration application to establish an account.

Workers' Compensation Employers in Maryland must provide workers' compensation insurance for all employees. Employers may obtain coverage from a private insurance company by becoming self-insured or by contacting the State Injured Workers' Insurance Fund. Employers believing they are not required to obtain this insurance may contact the Workers' Compensation Commission for certification of compliance.

Business Licenses Licenses are required for certain businesses to operate in Maryland. To determine if a license is necessary, contact the clerk of the circuit court in the county (or Baltimore City) where the business operates. A circuit court is located in each Maryland county and Baltimore City.

OTHER REQUIREMENTS

Bulk Sales When an existing business is bought, the purchaser must pay a 5% bulk sales and use tax on the price of tangible personal property, such as furniture and fixtures, that is part of the business. This tax is collected by the Comptroller of Maryland; Compliance Division.

Dissolution of Corporation An application for termination must be filed with the Department of Assessments and Taxation for the dissolution of a corporation. As of October 1, 1999, a tax clearance certificate is no longer required for the dissolution of a corporation.

Unclaimed Property Unclaimed funds such as wages, insurance benefits, bank accounts or security deposits must be reported if they remain unclaimed for five years. This property must be reported to the Comptroller of Maryland - Compliance Division.

NOTE: The information provided above is a brief summary of the various Maryland business requirements and is based on the law in effect as of 1/1/2001. For additional information, see the reverse side for the addresses and phone numbers of the Maryland agencies most frequently contacted by businesses.

MARYLAND STATE AGENCIES

(MOST FREQUENTLY CONTACTED BY BUSINESSES)

COMPTROLLER OF MARYLAND
www.marylandtaxes.com

Online business registration
www.marylandtaxes.com

New businesses can register online and set up tax accounts any time 24 hours a day.

For other new business information, visit the Business License Information System at www.blis.state.md.us.

Alcohol & Tobacco Tax Unit 410-260-7314
Goldstein Treasury Building — Room 310 or 888-784-0145
Annapolis, MD 21404-2999

Compliance Division
301 W. Preston Street
Baltimore, MD 21201-2383

Bulk sales 410-767-1579
or 800-492-1791

Business tax collections 410-649-0633
or 888-614-6337

Sales & use, admissions & amusement tax and tire fee refunds 410-767-1538

State License Bureau 410-260-6244

Unclaimed property 410-767-1700
or 800-782-7383

Utility surcharges

911 Telephone System Trust Fund 410-585-3015

Environmental Surcharge 410-767-8025

Universal Service Fee 410-767-4204

Universal Electricity Deregulation Surcharge 410-767-7285

General Accounting Division
Goldstein Treasury Building — Room 200
Annapolis, MD 21404-0746

Tax clearances 410-260-7813

Motor Fuel Tax Unit
Goldstein Treasury Building — Room 315
Annapolis, MD 21404-1751

Motor Fuel Licensing & Registration 410-260-7126
Room 317 or 888-784-0142

Motor Carrier & IFTA Licensing 410-260-7215
Room 317 or 888-784-0141

Revenue Administration Division
Revenue Administration Center
Annapolis, MD 21411-0001

Employer withholding tax 410-260-7980
or 800-638-2937

Facsimile transmittal 410-974-2967

Forms (all income tax and employer withholding) 410-260-7951

Substitute/computer-generated 410-260-7424

Income tax information (corporation, individual, fiduciary, pass-through entity) 410-260-7980
or 800-638-2937

Income tax refund inquiries 410-260-7701
or 800-218-8160

Tax-exempt organization registration 410-260-7980
or 800-638-2937

Baltimore area office 410-767-1300
301 W. Preston Street — Room 206 or 800-492-1751
Baltimore, MD 21201-2383

Admissions and amusement tax

Central registration

Sales and use tax information

Sales tax exemptions

Tire recycling fee

OTHER AGENCIES

Department of Agriculture 410-841-5700
50 Harry S. Truman Parkway or 800-492-5590
Annapolis, MD 21401

Conservation tillage equipment certification 410-841-5863
www.mda.state.md.us

Department of Assessments & Taxation
301 W. Preston Street — Room 806
Baltimore, MD 21201-2395

Charter/incorporation information 410-767-1350

Financial institution & public service company franchise tax 410-767-1940

New corporation information 410-767-1350

Resident agent information 410-767-1330

Personal property tax assessments 410-767-1170
or 888-246-5941

Property tax credits 410-767-4433
www.dat.state.md.us or 800-944-7403

Office of Business and Economic Research . . . 410-767-6435
217 E. Redwood Street — 23rd Floor or 800-541-8549
Baltimore, MD 21202

Office of Regional Response 410-767-0523

Enterprise Zones — Economically disadvantaged employee certification 410-767-6438
www.dbed.state.md.us

Department of Labor, Licensing & Regulation 410-767-2000
1100 N. Eutaw Street — Room 214
Baltimore, MD 21201

Unemployment insurance 410-767-2000
or 800-492-5524

Job services 410-767-2148
www.dllr.state.md.us

Department of the Environment 410-631-3000
2500 Broening Highway — or 800-633-6101
Building 30A (1st Floor)
Baltimore, MD 21224

Air management and radiation (oil furnace conversion) 410-631-3265

Asbestos 410-631-3801
www.mde.state.md.us

Injured Workers' Insurance Fund 410-494-2000
8722 Loch Raven Boulevard or 800-264-4943
Towson, MD 21286-2235
www.iwif.state.md.us

Maryland Insurance Administration
525 St. Paul Place
Baltimore, MD 21202

Insurance company premium tax 410-468-2000
www.gacc.com/mia or 800-492-6116

Department of Natural Resources
Tawes State Office Building — 580 Taylor Avenue
Annapolis, MD 21401-2397

Reforestation & timber stand improvement information 410-260-8531
www.dnr.state.md.us

Workers' Compensation Commission 410-864-5100
6 N. Liberty Street — Room 940 or 800-492-0479
Baltimore, MD 21201-3785
www.charm.net/~wcc