



Commonwealth of Massachusetts

Department of Revenue

Annual Report

Fiscal Year 2006

To the Honorable Deval L. Patrick, Governor of the Commonwealth, and the Honorable Members of the General Court of Massachusetts:

I am pleased to present you with the Department of Revenue's Fiscal Year 2006 Annual Report. FY06 was an exciting and innovative year on all fronts — tax administration, child support enforcement and local services. DOR continues to enhance its operations while providing quality and courteous customer service to all taxpayers.

There were a number of significant processing accomplishments. For the first time in history, DOR collected over \$18.4 billion — 80% of which was electronically accepted. More than half of the 3.1 million income tax returns were e-filed, and DOR electronically received and processed almost 60,000 corporate returns. This was excellent timing as legislation reduced the number of days to process timely filed refunds from 120 to 45 days. Overall, DOR reduced timely income and fiduciary tax refund processing by 76 days.

Utilizing data warehouse technology, DOR led an interstate clearinghouse program allowing states to combine resources to more efficiently discover nonfilers and discrepancies in credits claimed in their respective states. The overwhelming success of the pilot program is resulting in a multi-state data sharing initiative. There is a great spirit of cooperation, and I look forward to reporting even better results from this project next year.

It was also a record year for DOR's Child Support Enforcement Division as they collected more than a half-billion dollars. DOR expanded electronic delivery of child support payments via direct deposit and debit card, and as a result, nearly 95% of disbursements were made electronically. DOR continued its success of the License Suspension Program by collecting more than \$25.5 million in past-due child support by suspending drivers' and professional licenses and vehicle registrations of delinquent noncustodial parents.

In an effort to work proactively with cities and towns, DOR's Division of Local Services enhanced its online services. Local Services published online local aid estimates by city, town and regional school districts at each juncture of the state budget process and included narrative links to accurately describe the critical milestones for each program. New online tools were also rolled out to assist cities and towns with their budgeting and forecasting analysis.

I hope that you find this report informative. I look forward to working with you and the Commonwealth's taxpayers — and I thank my predecessor, Alan LeBovidge, for the fine work he directed in fiscal 2006.

Sincerely,

A handwritten signature in black ink, appearing to read 'H. Dormitzer', with a stylized flourish at the end.

Henry Dormitzer
Commissioner of Revenue

Year In Review FY 2006

Introduction

Fiscal Year 2006 was a very successful year for the Department of Revenue in many areas of taxpayer service, revenue collections and electronic programs. The following sections underscore DOR's achievements in its three primary areas of business: tax administration, child support enforcement and local services.

Tax Administration

For the first time in the Commonwealth's history, revenue collections topped \$18 billion, an increase of 8.2 percent over FY05. These collections exceeded benchmark estimates by \$329 million. Fiscal year 2006 also was a record-breaking year for audit assessments, surpassing \$1.5 billion in assessments. DOR's new retained revenue hires far exceeded the \$71 million target set by the Legislature by assessing more than \$115 million.

One of the Department's key objectives is to employ the latest technology to make filing returns and making payments as easy as possible. As seen in previous years, e-filing continued to gain in popularity with both personal income and business taxpayers. More than half of the 3.1 million 2006 income tax returns were filed electronically. DOR also electronically processed 60,000 corporate returns, 40,000 corporate extensions and 8,000 fiduciary returns. The increase in e-filed returns helped DOR process returns more quickly, efficiently and accurately than in previous years.

DOR's investments in technology have also been used to reach out to other state tax agencies to share data in order to locate non-filers and under-reporters. The pilot Clearinghouse project netted more than \$300,000 owed to Massachusetts by reviewing personal income tax data provided by the state of Connecticut. The success of the pilot helped DOR secure support for a multi-state data sharing initiative. At present 10 tax agencies in the northeast have signed on to use the program to help them locate individuals not paying taxes to their respective states.

In addition, DOR auditors were provided with sophisticated new tools for conducting audits in FY06. The new Web-based application, Audit Workbench, is an electronic audit file containing taxpayer records, auditor workpapers and DOR notices and was designed to promote better accountability at the auditor level. The program was being tested at the end of FY06 and was scheduled for complete roll-out at the close of the calendar year.

The Department made great strides in reimbursing underground storage tank (UST) owners and operators for clean-up costs associated with leaking UST systems and disbursing grants to communities for removing and replacing underground fuel storage tanks. In FY06, \$77.5 million in revenues was collected from annual fees and 21 grants were approved resulting in \$421,000 in reimbursements to cities and towns.

Child Support Enforcement

The Department's Child Support Enforcement Division provides important services to families by assisting parents in establishing paternity and child support orders, collecting child support and asking courts to adjust support orders when circumstances change. FY06 was a noteworthy year for CSE in many of its key functions, particularly in establishing paternity and collecting child support: CSE established paternity for more than 20,000 children and collected over a half-billion dollars in child support.

CSE's license suspension program has proven to be an effective method of collecting past-due child support. In FY06, CSE collected \$25.5 million by suspending the drivers' and professional licenses and vehicle registrations of delinquent noncustodial parents. Since its inception in 2002, the program has brought in approximately \$73 million.

In FY06, more families than ever before received their payments through either direct deposit or the child support debit card, which make the funds far more readily available and easily accessible. With the expansion of these options, nearly 95 percent of child support payments are made electronically, up from 25 percent in FY05.

CSE also made progress in improving customer service over the previous fiscal year. The number of new child support orders increased by 14 percent over FY05 and CSE closed 26 percent more preobligated cases and 30 percent more obligated cases in FY06, compared to FY05. In addition, CSE reduced the average time to answer a call to its customer service bureau from 20 minutes to just 50 seconds; reduced the call abandonment rate from 32 percent to 2 percent; and increased the percentage of calls answered from 68 percent to 98 percent.

Local Services

The Department's Division of Local Services (DLS) has oversight of property taxation and municipal finance for the Commonwealth's 351 cities and towns. The Division of Local Services exists to help the Commonwealth's municipalities achieve fair and equitable property taxation and efficient fiscal management.

In FY06, DLS made numerous enhancements to its website to provide cities and towns with vital tools designed to assist them with budgeting and forecasting analysis. The Division introduced a new online application, which allows municipalities to forecast revenues and expenditures on a multi-year basis, and also made financial data available online to report collective bargaining data.

The Division also published, on its website, full local aid estimates by city, town and regional school district at each juncture of the state budget process to assist local officials in the budgeting process by providing the most current information available on local aid.

The Division successfully implemented these programs while continuing to fulfill its annually recurring duties, such as certifying tax rates, certifying free cash and distributing cherry sheet and local aid to cities and towns. DLS timely issued \$4.8 billion in electronic cherry sheet aid and distributed \$4.5 billion in local aid through the quarterly distribution process.

Legislative Review FY 2006

Corporate Excise

Net Worth Calculations for REITS

Recent legislation has revised the statutory net worth formula of the corporate excise for qualified Real Estate Investment Trusts (REITs) that are intangible property corporations. St. 2005, c. 163, § 22, codified at G.L. c. 63, § 30(9). A qualified REIT is a domestic or foreign corporation that both qualifies as a REIT under section 856 of the Internal Revenue Code (as the Code is defined at G.L. c. 63, § 30(16)), and that is required to file with the Securities and Exchange Commission annual and other reports as specified in Section 13 or Section 15(d) of the Securities Exchange Act of 1934, as amended. The net worth of a qualified REIT, whether a domestic business corporation taxable under G.L. c. 63, § 32(a)(1), or a foreign business corporation taxable under G.L. c. 63, § 39(a)(1), is measured by multiplying the book value of the REIT's total assets minus its liabilities on the last day of its taxable year by a fraction, the numerator of which is the book value of the REIT's tangible assets situated in Massachusetts on the last day of its taxable year that are not subject to local taxation plus the amount of its intangible assets on the last day of its taxable year allocable to Massachusetts, and the denominator of which is the book value of the total assets of the REIT on that same date. The further definition of intangible assets allocable to Massachusetts and other applicable rules and definitions are set out in G.L. c. 63, § 30(9). The legislation is effective for tax years ending on or after August 9, 2004. St. 2005, c. 163, § 66. *See* TIR 06-6.

Unrelated Business Income of Nonprofit Corporations

Statutory changes contained in St. 2005, c. 163 affect the taxation of corporations exempt from taxation under Internal Revenue Code (IRC) section 501. Pursuant to amendments to G.L. c. 63, corporations exempt from taxation under IRC § 501 will be subject to tax on their unrelated business taxable income as defined under IRC § 512. The amendments are effective for tax years beginning on or after January 1, 2006.

Under federal law, charitable or non-profit organizations are generally exempt from taxation on their income under IRC § 501. One exception is the tax imposed by section 511 of the Code on unrelated business taxable income as defined in IRC § 512. Generally, unrelated business taxable income does not include certain investment income, such as interest and dividends. Prior to the recent statutory amendments to G.L. c. 63, corporations exempt from taxation under IRC § 501 were excluded from the definitions of "domestic corporation" and "foreign corporation" in G.L. c. 63, §§ 30.1 and 30.2. As such, exempt corporations were not subject to the Massachusetts corporate excise.

The new legislation subjects exempt corporations to taxation on their unrelated business taxable income. St. 2005, c. 163, §§ 19, 20, 21, 28, and 59. The Act amended G.L. c. 63, § 30 to expand the definitions of "domestic corporation" and "foreign corporation" to include a corporation which is exempt from federal taxation under IRC § 501. The Act further amended § 30 to define the net income of a corporation exempt from taxation under IRC § 501 as its unrelated business taxable income as defined in IRC § 512.

In addition, the Act amended chapter 63 to add new section 38T, which provides that exempt corporations are not subject to the non-income measure of the corporate excise or the minimum tax. Newly added § 38T also allows an exempt corporation with unrelated business taxable income taxable in Massachusetts and elsewhere to apportion its income pursuant to G.L. c. 63, § 38. The apportionment factors must be determined by reference only to the unrelated business activity of the exempt corporation. The credits allowed to corporations under G.L. c. 63 are also allowed to exempt corporations. However, the corporate excise on unrelated business taxable income can only be offset by credits generated from unrelated business activity. *See* TIR 06-7.

Modification of DOR's Role in Reviewing Certified Projects

Pursuant to recent amendments to G.L. c. 63, § 38N, set forth in section 62 of chapter 123 of the Acts of 2006, effective June 24, 2006, the Commissioner of Revenue (Commissioner) is no longer directed to certify applications for the economic opportunity area (EOA) credit before a corporation may take the credit or to periodically review certified projects to determine continued compliance with certain requirements. Corporations seeking to take the credit are no longer required to file the EOA credit application with the Commissioner for certification thereof. *See* TIR 06-23.

General Laws chapter 63, section 38N authorizes a credit against the tax imposed by chapter 63 for corporations that participate in a certified project in an economic opportunity area. The credit allowed is an amount equal to five percent of the cost of eligible property. The credit is a component of the Economic Development Incentive Program administered by the Economic Assistance Coordinating Council (EACC) within the Massachusetts Office of Business Development pursuant to G.L. c. 23A.

Effective June 24, 2006, G.L. c. 63, § 38N, now provides in relevant part:

A credit allowed under section 38N may be taken only after the taxpayer completes a report signed by an authorized representative of the corporation, and files the report with the EACC within two years after the initial project certification by the EACC and annually thereafter.

The EACC shall certify that property eligible for the credit is a certified project within an economic opportunity area, as defined in section 3E of said chapter 23A, and wholly within an area designated as an economic target area pursuant to section 3D of chapter 23A, and also that the certified project reasonably satisfies the employment projections specified in the original project proposal.

The EACC shall determine whether the certified project is in compliance with the definition of certified project set forth in section 38N and whether the project has a reasonable chance of increasing employment opportunities as advanced in the initial proposal as certified by the EACC.

If the EACC determines that the certified project is no longer in compliance, then the EACC shall revoke certification of the project as provided in section 3F of chapter 23A and notification of decertification shall be given to the Commissioner who shall disallow any future credits to the project under section 38N.

If a project is considered decertified for reasons of fraud or material misrepresentation, as determined by the EACC and the Commissioner, the Commissioner shall have a cause of action against the controlling business of the project for the value of any economic benefits received, including, but not limited to, the amount of the tax credit allowed under section 38N.

Nothing in section 38N shall limit the authority of the Commissioner to make adjustments to a corporation's liability upon audit.

Sales Tax

Sales Tax Holiday

On July 22, 2005, a statute was enacted that provided for a Massachusetts "sales tax holiday weekend," *i.e.*, two consecutive days during which most purchases made by individuals for personal use were not subject to Massachusetts sales or use taxes. St. 2005, c. 52, §§ 1–5, ("the Act"). The Act provided that the sales tax holiday would occur on August 13 and 14, 2005 and on those days, non-business sales at retail of single items of tangible personal property costing \$2,500 or less were exempt from sales and use taxes, subject to certain exclusions. The following did not qualify for the sales tax holiday exemption and remained subject to tax: all motor vehicles, motorboats, meals, telecommunications services, gas, steam, electricity, tobacco products and any single item whose price is in excess of \$2,500. The Act charges the Commissioner of Revenue

with issuing instructions or forms and rules and regulations necessary to carry out the purposes of the Act. Two changes from the sales tax holiday of 2004 were the *exclusion* of tobacco products from the holiday and the *inclusion* of non-motorized boats such as canoes, kayaks and rowboats costing \$2,500 or less. See TIR 05-9.

Transfers of Prewritten Computer Software

On December 8, 2005, legislation was passed concerning sales of standardized computer software ("prewritten software"). As a result of this change, prewritten software sold to a customer in Massachusetts or purchased for use in Massachusetts is deemed a transfer of tangible personal property subject to the sales or use tax regardless of the method of delivery, including transfers by electronic means such as the Internet or "load and leave." This change is effective April 1, 2006. Prior to this statutory change, sales or use tax was imposed on sales of prewritten software delivered in tangible form such as a disk, but not on prewritten software delivered electronically or by "load and leave." See 830 CMR 64H.1.3, DD 01-3 and LR 00-14 and TIR 05-15.

The legislation also provides that the development and sale of prewritten software is considered a manufacturing activity for purposes of certain corporate excise provisions, regardless of the method of the delivery of the software. This may result in the applicability of single sales factor apportionment and eligibility for potential local property tax benefits, investment tax credits, and certain sales tax exemptions. These changes are effective for taxable years beginning on or after January 1, 2006.

The recent legislation amends the definition of "tangible personal property" in the sales tax statute, G.L. c. 64H, § 1, to add the following: "A transfer of standardized computer software, including but not limited to electronic, telephonic, or similar transfer, shall also be considered a transfer of tangible personal property. The commissioner may, by regulation, provide rules for apportioning tax in those instances in which software is transferred for use in more than one state."

The legislation also amends provisions in the corporate excise statute at G.L. c. 63, §§ 38C and 42B to provide that for purposes of those sections and G.L. c. 63, § 38, "the development and sale of standardized computer software shall be considered a manufacturing activity, without regard to the manner of delivery of the software to the customer."

Qualifying Small Business Exemption

On December 8, 2005, the Massachusetts Legislature amended the sales tax exemption in G.L. c. 64H, § 6 (qq) ("the small business exemption"), which exempts sales of gas, steam, electricity or heating fuel for use by qualifying small businesses. See St. 2005, c. 163, s. 36, effective April 1, 2006; See also TIR 06-2. Under prior law, the small business exemption exempted sales of gas, steam, electricity or heating fuel to a business having five or fewer employees. Chapter 64H, § 6(qq), as recently amended, exempts "[s]ales of gas, steam, electricity or heating fuel for use by any business that has five or fewer employees and that had gross income of less than \$1,000,000 for the preceding calendar year, and that reasonably expects gross income of less than \$1,000,000 for the current calendar year."

The revised statute retains the "5 or fewer employees" requirement, but adds two significant restrictions. First, the energy must be purchased for use by a qualifying small business itself. Purchasers, such as management companies, having five or fewer employees and meeting the income requirements above may claim exemption for energy purchased solely for their own consumption, but cannot claim the exemption if any portion of the energy purchased is provided to or for the benefit of other entities, such as tenants. Second, the purchaser must meet the gross income limitations above. Businesses that may not have had gross income during the preceding calendar year, *e.g.*, newly-formed businesses, may be eligible for the exemption if they reasonably expect to have gross income of less than \$1,000,000 for the current calendar year. For purposes of determining its gross income for the pre-

vious year, a business should refer to the applicable income tax return containing this information.

Personal Income Tax

Heating Energy Assistance and Tax

On November 22, 2005, the Legislature signed "An Act Relative to Heating Energy Assistance and Tax Relief" ("the Act") under which certain taxpayers subject to the personal income tax imposed by G.L. c. 62 are eligible for a deduction for certain expenses for home heating, and for a credit for energy-efficient heating items installed in residential property located in Massachusetts. Eligible taxpayers may claim a home heating fuel deduction up to a maximum of \$800. The Act requires that "[t]he deductions may be used only for the cost of home heating oil, natural gas and propane purchased between November 1, 2005 and March 31, 2006." *See* St. 2005, c. 140, § 14(a). A taxpayer who qualifies for the deduction may apply the deduction in taxable year 2005 for purchases made between November 1, 2005 and December 31, 2005. If the taxpayer does not take the full \$800 deduction in taxable year 2005, the taxpayer may take the remainder in taxable year 2006 for purchases made in 2006 through March 31, 2006. *See* St. 2005, c. 140 and TIR 05-18.

Subject to certain limitations, a person or entity subject to taxation under G.L. c. 62 or G.L. c. 63 that is the owner of residential property located in Massachusetts may claim a credit in the amount of the net expenditure for energy-efficient heating items "purchased on or after November 1, 2005, but not later than March 31, 2006, for installation in said property." St. 2005, c. 140, §§ 15 and 16.

Also under the Act, taxpayers subject to the corporate excise imposed by G.L. c. 63 may be eligible for a credit under c. 63, § 38T for the purchase and installation of a solar water heating system in a commercial building between November 1, 2005 and March 31, 2006 may be applied to the taxable year 2006. A taxpayer may use the credit against the corporate excise beginning with the tax year of the qualifying pur-

chase. The taxpayer may carry over and apply, in taxable year 2007, the portion of the credit that exceeds the tax for taxable year 2006.

A taxpayer cannot claim multiple credits with respect to the same property. A deduction under G.L. c. 63, § 38H is allowed with respect to the installation of any solar or wind-powered climate control unit or water heating unit. The deduction is in lieu of any other credit or deduction for the same property for the taxable year or years of installation or conversion. *See* G.L. c. 63, § 38H(b)(1). Thus, a taxpayer cannot use the same expenses to claim both the credit at section 38T and the deduction at section 38H. A taxpayer may not sell or transfer the energy-efficiency heating credit to another taxpayer. The credit cannot reduce the excise below the greater of the minimum excise or 50 percent of the excise before credits. G.L. c. 63, §§ 32(b), 32C, 39(b).

Lower Capital Gains Tax Rates for 2002

On December 8, 2005, the Legislature passed "An Act Relative to Tax Laws" ("the Act") St. 2005, c. 163. The Act delays the effective date of the 2002 capital gains tax rate increase in a manner that complies with the *Peterson II* decision by the Supreme Judicial Court. *See* TIR 05-20. Pursuant to the Act, the rate increase will now be effective for tax years beginning on or after January 1, 2003. As a result of the Act, a taxpayer with capital gains transactions in the portion of the 2002 tax year ending April 30, 2002 will not owe tax at the increased rate. Also, under the Act, certain taxpayers with capital gains transactions in the portion of the 2002 tax year after April 30, 2002 may be entitled to refunds.

The Act provides that the capital gains tax rate increase to 5.3 percent, generally applicable to long-term capital gains (with holding periods exceeding one year), will be effective for tax years beginning on or after January 1, 2003.

The Act reinstitutes the lower capital gains tax rates that initially existed during the portion of the 2002 tax year ending April 30, 2002 (5 percent ranging down to 0

percent depending on the holding period) and provides that such rates shall be applicable to the entire 2002 tax year, *i.e.*, a tax year beginning on or after January 1, 2002 and prior to January 1, 2003. With certain exceptions, the capital gains law in effect for tax year 2002 is explained in the Department's regulation at 830 CMR 62.4.1, *Capital Gains and Losses*.

Claim of Right Deduction

On December 8, 2005, new legislation was signed that provides a deduction, available for tax years beginning on or after January 1, 2005, to taxpayers who have paid Massachusetts personal income taxes in a prior year on income attributed to them under a "claim of right" to deduct the amount of that income from their gross income if it later develops that they were not in fact entitled to the income, and have repaid the amounts in question. *See* new G.L. c. 62, § 3(B)(a)(14). The deduction is allowed in the year of repayment, provided that the repayment is not otherwise deductible in determining Massachusetts income taxable under G.L. c. 62. *See* TIR 06-4.

Under the federal "claim of right" doctrine, a taxpayer receiving income under a claim of right and without restrictions on its use or disposition is taxed on that income in the year of receipt, even though the right to retain the income is not yet fixed or the taxpayer may later be required to return it. *See, e.g., United States v. Skelly Oil Co.*, 394 U.S. 678, 680 81 (1969); *Healy v. Commissioner of Internal Revenue*, 345 U.S. 278, 281 82 (1952); *North American Oil Consolidated v. Commissioner of Internal Revenue*, 286 U.S. 417, 424 (1932). Since, pursuant to G.L. c. 62, § 2, Massachusetts gross income for a taxable year is federal gross income for the same period with certain modifications, it follows that any amount included in a taxpayer's federal gross income for the taxable year under a claim of right must also be included in the taxpayer's Massachusetts gross income for the same taxable year.

Prior to the enactment of this statute, a taxpayer was not entitled to adjust his or her Massachusetts gross income for an

earlier year based on a subsequent repayment of amounts held under a claim of right by filing an amended return for that year. This situation has been changed by amending G.L. c. 62, § 3(B)(a), which now allows a deduction for: (14) The amount as is described in section 1341(a)(2) of the Code, to the extent, if any, that that amount (i) was previously included in Massachusetts taxable income and (ii) is not otherwise deductible under section 2(d)(1) of this chapter.

Adoption of the Updated Internal Revenue Code ("Code Update")

Massachusetts gross income includes all items included in federal gross income as defined in the Internal Revenue Code (the "Code") as amended and in effect as of a specific date, unless there exists a specific modification in the Massachusetts General Laws which includes a federally excluded item or excludes a federally included item from Massachusetts gross income. G.L. c. 62, § 2. As time passes and the Code changes, federal provisions are added, deleted or changed, thereby creating differences between the federal and Massachusetts personal income tax provisions. Periodically, the Massachusetts Legislature adopts a more recent version of the Code ("Code Update"), resulting in many changes to the Massachusetts personal income tax provisions.

On December 8, 2005, the Massachusetts Legislature enacted Code Update which incorporated into Massachusetts personal income tax law the Code as amended and in effect on January 1, 2005. Massachusetts previously used the Code as amended and in effect on January 1, 1998. As a result of Code Update, Massachusetts will now adopt many of the federal tax law changes that have been enacted by Congress in the past seven years, including the *American Jobs Creation Act of 2004*, the *Medicare Prescription Drug, Improvement, and Modernization Act of 2003* and the *Job Creation and Worker Assistance Act of 2002*. TIR 05-16 explains the changes and effect of Code Update on the Massachusetts personal income tax provisions.

Tax Administration

New Penalties under G.L. c. 62C, 35A-E

On December 8, 2005, the Governor signed into law chapter 163 of the Acts of 2005 (the "Act"). Sections 12 and 14 of the Act add sections 35A through 35E to chapter 62C of the General Laws. These new sections impose penalties that apply in the following circumstances:

1. A taxpayer substantially understates a tax liability or underpays taxes due to negligence or disregard of Massachusetts laws, including public written statements of the Commissioner;
2. A preparer with respect to a tax return or claim for abatement or refund knows or reasonably should know that the return or claim reflects a position or positions unsupported by Massachusetts law, and the position was not disclosed or was frivolous; or a preparer willfully attempts to understate tax liability or demonstrates a careless, reckless or intentional disregard of Massachusetts tax laws or written public statements issued by the Commissioner;
3. A taxpayer takes a tax return reporting position on an issue in Massachusetts that is inconsistent with a position taken in another state and the governing law relating to that issue is the same in all material respects in Massachusetts and the other state, and;
4. A person organizes, assists in the organization of, or sells (or assists in the sale of) any plan or arrangement, and makes or furnishes, or causes another person to make or furnish, a false, fraudulent or deliberately misleading statement with respect to the allowability of any deduction or credit, the excludability of any income, or the securing of any other tax benefit, including the avoidance of a filing requirement.

These penalty provisions were in substantial part derived from provisions of the federal Internal Revenue Code imposing like penalties with respect to federal returns, and DOR intends to apply and interpret the new penalties in a manner generally consistent with such provisions of the Code and the Treasury Regulations promulgated

thereunder, to the extent that such federal law provides pertinent authority. See TIR 06-5.

Payments in Error

Recent legislation, St. 2005, c. 163, § 15, adds a new paragraph to G.L. c. 62C, § 36A. If the Department has made a "payment in error," has demanded return of that payment, and the full amount has not been repaid within 30 days, the amount demanded is considered a tax assessed under G.L. c. 62C. The term "payment in error" includes a refund in excess of the amount properly due or a payment where no refund is due, *i.e.*, an erroneous refund. Thus, an erroneous refund may now be collected like a tax, and the failure to repay an erroneous refund after demand for repayment may now result in the imposition of interest and penalties. The provisions in St. 2005, c. 163, § 15 are effective December 8, 2005, and apply to all failures to repay erroneous refunds or other payments in error after demand for repayment occurring on or after that date. DOR Directive 94-7 is superseded to the extent that it is inconsistent with TIR 06-11.

Miscellaneous

Vehicle Rental Surcharge in Revere

On September 22, 2005, legislation was enacted that authorized the city of Revere to impose a surcharge of not more than \$10 upon each vehicular rental transaction contract in the City of Revere. St. 2005, c. 92, § 1. Pursuant to the provisions of this statute, Revere has enacted an Ordinance providing for a \$10.00 surcharge. See REVERE ORDINANCES, Title 3, c. 3.02, § 3.02.020(B)(2005). Funds derived from the surcharge will be used to construct and equip a new public safety facility for the City of Revere. Vendors entering into vehicular rental transaction contracts in Revere on or after October 1, 2005 that fail to collect and remit the surcharge are subject to assessment and collection by the Department of Revenue.

The \$10 surcharge is imposed upon each vehicular rental transaction contract in Revere. The term "vehicular rental transaction

contract” includes any written agreement setting forth the terms and conditions governing the use of a vehicle provided by a rental company for 30 continuous days or less, except as provided in TIR 05-14. *See also, generally*, G.L. c. 90, § 32E½. A written agreement may be executed upon tangible media or electronically, such as through the Internet.

The \$10 surcharge on a vehicle rental contract in Revere is imposed separately and in addition to the existing 5 percent sales tax imposed under G.L. c. 64H, § 2. The \$10 surcharge on a vehicle rental contract in Revere is not part of the sales price subject to Massachusetts sales tax. For billing purposes, the \$10 surcharge must be stated separately from the sales price and the sales tax. *See* Letter Ruling 99-6.

Film Industry Incentive

The Massachusetts Legislature recently enacted personal income tax and corporate excise credits and sales tax exemptions that provide incentives to the motion picture industry (the “Act”). *See* St. 2005, c. 158; amended by St. 2005, c. 167. In particular, these credits and exemptions

apply to a qualifying motion picture production company and the sales tax exemption also applies to a qualifying film school student. For taxable years beginning on or after January 1, 2006 and before January 1, 2013, the Act provides two tax credits that can be taken by a motion picture production company against either its personal income tax or corporate excise liabilities. G.L. c. 62, § 6(l) and c. 63, § 38T. Each credit has its own qualification requirements and a taxpayer is allowed to qualify for and claim both credits; however, the total amount of tax credits allowed to any one motion picture shall not exceed \$7,000,000. *See* TIR 06-1.

The credits may be used or transferred by any taxpayer within the meaning of chapter 63, including financial institutions, utility corporations and insurance companies, and by corporations that are exempt from taxation under Internal Revenue Code (“Code”) § 501. Insurance companies may apply the credit against the insurance premiums tax. *See* G.L. c. 63, § 20 et. seq. Corporations that are exempt from tax under Code § 501 may apply the credit

against the tax on unrelated business income. *See* G.L. c. 63, § 38T. Flow-through entities may pass the film credits through to partners, members or owners in proportion to their sharing of other tax or economic attributes of the entity.

Economic Incentive Legislation

On June 24, 2006, the Legislature enacted St. 2006, c. 123, “An Act Relative to Economic Investments in the Commonwealth to Promote Job Creation, Economic Stability, and Competitiveness in the Massachusetts Economy” (the “Act”). The Act includes provisions that expand the jobs incentive payment program, change the sales and use tax filing requirements for certain vendors that are materialmen, extend the Brownfields tax credit to nonprofit organizations, allow the transfer of Brownfields tax credits, extend the time period and the amount of the historic rehabilitation tax credit, and clarify that single-sales-factor apportionment applies for certain manufacturers of value-added agricultural products. *See* TIR 06-16 for explanations of the effect of these changes on Massachusetts tax law.

The Taxes FY 2006

TYPE OF TAX	MEASURE	RATE ¹	RETURN DUE
Personal income and fiduciary income	Net capital gains ²	5.3–12%	On or before April 15 for calendar year filings.
	Dividends, interest, wages, other income	5.3%	The 15th day of the 4th month for fiscal year filings.
Nonresident	Massachusetts source income	5.3%	
Estimated tax	Liability in excess of \$400		Due quarterly on or before the 15th day of April; June, September and January.
Withholding	Wages	5.3%	Varies depending on amount of tax withheld in calendar year. If annual withholding: up to \$100 — annual filing; \$101–1,200 — quarterly filings; \$1,201–25,000 — monthly filings; over \$25,000 — quarterly filings, weekly payments.
Estate	Federal taxable estate	0.8%–16% ³	Within 9 months after date of decedent's death.
Nonresident	Massachusetts real and tangible property ³		Within 9 months after date of decedent's death.
Alcoholic beverages	Malt (31-gal. bbl.)	\$3.30	Monthly, on or before the 20th day of the month.
	Cider 3%–6% (wine gal.)	\$.03	
	Still wine 3%–6% (wine gal.)	\$.55	
	Sparkling wine (wine gal.)	\$.70	
	Alcoholic beverages 15% or less (wine gal.)	\$1.10	
	Alcoholic beverages more than 15%–50% (wine gal.)	\$4.05	
	Alcoholic beverages more than 50% or alcohol (proof gal.)	\$4.05	
Cigarettes	20-count package	\$1.51	Monthly, on or before the 20th day of the month. Unclassified acquirers must file upon importation or acquisition.
	Smokeless tobacco (percentage of price paid by licensee)	90%	Quarterly, on or before the 20th day following the close of the tax period.
	Cigars and smoking tobacco (percentage of price paid by licensee)	30%	
Marijuana and controlled substances tax	Weight of marijuana	\$3.50 per gram	Payment due immediately upon acquisition or possession in Massachusetts by dealer. Payment evidenced by stamps purchased from the Commissioner.
	Weight of controlled substance	\$200 per gram	
	Dosage unit of controlled substance	\$2,000 per 50 dosage units	
Deeds	Sales price (less mortgage assumed) of real estate	\$2.28 ⁴ per \$500	Monthly, on or before the 10th day of the month (filed by Registers of Deeds).
Motor fuels	Gasoline and diesel fuel per gallon	\$.21	Monthly, on or before the 20th day of the month.
	Propane, liquified gas, etc. (no minimum)	19.1%	
	Aviation (10¢ minimum)	7.5%	
	Jet fuel at local option (5¢ minimum)	5%	
Room occupancy	Transient room occupancy	5.7%	Monthly, on or before the 20th day following the close of the tax period.
	At local option, up to	4.0%	
	Convention Center Financing Fee	2.75%	
	(Boston, Cambridge, Springfield, Worcester, Chicopee and West Springfield)		

¹ Tax rates as of August 1, 2004.

² Gains from the sale or exchange of capital assets (except collectibles) held for more than one year are taxed at 5.3%. Short-term capital gains, as well as long-term capital gains arising from the sale of collectibles (with a 50% deduction) are taxed at 12%.

³ Resident rate is equal to federal credit for state death taxes based on December 31, 2000 IRC. Nonresident rate is equal to Massachusetts proportionate share of federal credit for state death taxes.

⁴ In Barnstable County, the rate is \$5.70 per \$1,000.

TYPE OF TAX	MEASURE	RATE	RETURN DUE
Club alcoholic beverages	Gross receipts	0.57%	On or before April 15.
Sales and use tax	Sale, rental or use of tangible personal property, including cigarettes, telecommunication services and certain fuel.	5%	On or before the 20th day following the close of the tax period. If annual liability: up to \$100 — annual filing; \$101–1,200 — quarterly filings; over \$1,200 — monthly filings
Sales tax on meals, prepared food and all beverages	All “restaurant” food and on-premises consumption of any beverages in any amount.	5%	Monthly, on or before the 20th day following the close of the tax period.
Business and manufacturing corporations	Net income Tangible property or net worth Minimum	9.5% ⁵ \$2.60 per \$1,000 \$456	On or before the 15th day of third month after close of taxable year.
Estimated tax	Liability in excess of \$1,000		Due quarterly as follows: 15th day of 3rd (40%), 6th (25%), 9th (25%) and 12th (10%) months of taxable year. ⁶
Security corporation			
Non-bank holding co.	Gross income	1.32%	Same as business corporations.
Bank holding company	Gross income	0.33%	
	Minimum	\$456	
Financial institutions	Net income Minimum	10.50% \$456	Same as business corporations.
Public utilities	Net income	6.5%	Same as business corporations.
Ship excise tax	Value (equity interest) of the corporation’s interest in a ship or vessel engaged in interstate or foreign trade.	0.379%	Same as business corporations.
Insurance company			
Domestic life	Premiums	2.0%	On or before March 15.
	Massachusetts net investment income	4.8%–14.0%	
Foreign life	Premiums	2.0%	
Domestic casualty	Premiums	2.28%	On or before May 15.
	Gross investment income	0.2%–1.0%	
Foreign casualty	Premiums	2.28%	
Ocean marine	Underwriting profit	5.7%	
Preferred provider arrangements	Premiums	2.28%	
Motor vehicle garaged outside Massachusetts	90% to 10% of manufacturer’s list price	\$25 per \$1,000	On or before 30 days from issuance of tax bill.
Boston sightseeing tour	Ticket purchase price of any water- or land-based sightseeing tourist venue or entertainment cruise or trolley tour originating or located in Massachusetts and conducted partly or entirely in Boston.	5%	Quarterly, on or before the 20th day following the close of the tax period.
Boston vehicular rental transaction surcharge	Each vehicular rental transaction contract executed in Boston.	\$10	Quarterly, on or before the 20th day following the close of the tax period.
Parking facilities surcharge in Boston, Springfield and/or Worcester	Parking facilities built in conjunction with or as part of a project authorized by the Convention Center Financing Act in Boston, Springfield or Worcester.	\$2 per vehicle per day	Quarterly, on or before the 20th day following the close of the tax period.

⁵S corporations: 4.5% if total receipts \$9 million or more; 3% if total receipts are \$6 million or more but less than \$9 million.

⁶30%, 25%, 25% and 20% for corporations with fewer than 10 employees in their first full tax year.

Revenue Collections FY 2006

In thousands	FY02	FY03	FY04	FY05	FY06	FY05-06 % change
STATE TAXES COLLECTED BY DOR						
Tax on personal income						
TOTAL	\$ 7,912,934	\$ 8,026,148	\$ 8,830,334	\$ 9,690,270	\$10,483,437	8.2
Taxes on business						
Corporations	\$ 586,743	\$ 799,450	\$ 997,602	\$ 1,062,722	\$ 1,390,684	30.9
Insurance companies	347,645	344,626	373,721	372,823	396,683	6.4
Public utilities	88,486	40,621	64,733	71,136	118,492	66.6
Commercial banks ¹	134,431	347,833	238,740	198,937	349,932	75.9
Savings institutions ¹	2,597	(3,293)	00	0	0	—
TOTAL	\$ 1,159,902	\$ 1,529,237	\$ 1,674,796	\$ 1,705,618	\$ 2,255,791	32.3
Taxes on commodities sold						
Motor fuels	\$ 666,751	\$ 676,426	\$ 684,912	\$ 685,537	\$ 671,844	(2.0)
Cigarettes	274,997	451,044	425,421	423,637	435,336	2.8
Alcoholic beverages	65,356	66,298	67,902	68,630	68,854	0.3
Sales and use ²	3,194,989	3,196,044	3,211,197	3,331,830	3,421,166	2.7
Sales on meals	500,885	512,025	532,014	559,115	588,205	5.2
TOTAL	\$ 4,702,978	\$ 4,901,837	\$ 4,921,446	\$ 5,068,749	\$ 5,185,405	2.3
Other taxes						
Estate & inheritance	\$ 200,547	\$ 181,295	\$ 194,706	\$ 255,127	\$ 196,260	(23.1)
Room occupancy excise	123,306	119,991	120,178	133,487	144,808	8.5
Deeds excise ³	97,782	105,091	132,625	156,501	149,283	(4.6)
Club alcoholic beverage excise	571	657	621	621	672	8.2
Motor vehicle excise	86	72	51	70	76	8.6
Controlled substances	0	0	0	0	0	—
Convention Center surcharge	10,502	9,934	9,804	10,390	11,039	6.2
Community preservation trust	42,451	53,503	50,520	37,406	36,088	(3.5)
TOTAL	\$ 475,245	\$ 470,543	\$ 508,505	\$ 593,602	\$ 538,226	(9.3)
Total state taxes collected by DOR	\$14,251,059	\$14,927,765	\$15,935,081	\$17,058,239	\$18,462,859	8.2

¹All bank tax transactions (both savings and commercial) appear in the Commercial Bank Excise category.

²Include sales and use tax on motor vehicles.

³Due to different accounting methods, amounts reported for the deeds excise differ from those amounts reported by the comptroller.

Because of rounding, detail may not add to Totals.

The figures contained herewith are DOR figures pending the Comptroller's Fiscal Year 2006 Statutory Basis Annual Financial Report.

In thousands	FY02	FY03	FY04	FY05	FY06	FY05-06 % change
LOCAL TAXES COLLECTED BY DOR ON BEHALF OF COMMUNITIES						
Urban redevelopment	\$ 46,824	\$ 47,083	\$ 48,729	\$ 49,874	\$ 50,681	1.6
Local option airplane jet fuel	12,914	12,846	12,541	16,269	20,228	24.3
Local option room occupancy	70,953	69,617	68,484	75,490	81,590	8.1
Local rental vehicle (Convention Center 10%)	1,028	962	945	1,023	1,086	6.2
Embarkation fees	—	—	72	1,293	1,290	(0.2)
Total local taxes collected by DOR on behalf of communities	\$ 131,719	\$ 130,508	\$ 130,771	\$ 143,949	\$ 154,875	7.6
OTHER REVENUE						
Utility and insurance assessments	\$ 0	\$ 0	\$ 0	\$ 0	\$ 0	—
Department fees, licenses, etc.	6,475	7,166	8,043	10,924	20,021	83.3
County Correction Fund — deeds	6,121	6,605	8,343	9,902	9,413	(4.9)
County recording fees		17,954	60,384	45,662	43,103	(5.6)
Abandoned deposits — bottle	37,109	36,205	36,422	36,817	39,009	6.0
Total other revenue	\$ 49,705	\$ 67,930	\$ 113,192	\$ 103,305	\$ 111,546	8.0
STATE TAXES COLLECTED BY OTHER AGENCIES						
Horse and dog racing	\$ 6,856	\$ 6,547	\$ 5,697	\$ 4,677	\$ 4,181	(10.6)
Beano and boxing	3,066	2,793	2,591	2,146	1,964	(8.5)
Raffles/bazaars	846	889	965	1,038	1,121	8.0
Special insurance brokers	13,030	21,805	26,042	29,480	30,377	3.0
UI surcharge	22,198	21,394	20,451	21,135	21,400	1.3
Deeds, Secretary of State	39,721	42,704	54,418	63,831	60,860	(4.7)
Total state taxes collected by other agencies	\$ 85,717	\$ 96,132	\$ 110,164	\$ 122,307	\$ 119,903	(2.0)
TAXES ON PROPERTY COLLECTED BY LOCAL GOVERNMENT						
Real estate	\$ 7,651,814	\$ 8,126,933	\$ 8,607,527	\$ 9,105,150	\$ 9,602,983	5.5
Personal property	352,104	367,088	407,845	378,305	380,155	0.5
Motor vehicles	597,915	645,160	605,090	683,168	694,259	1.6
Total taxes on property collected by local government	\$ 8,601,833	\$ 9,139,181	\$ 9,652,061	\$10,166,623	\$10,677,397	5.0
TOTAL ALL TAXES	\$23,120,033	\$24,361,516	\$25,941,269	\$27,594,423	\$29,526,580	7.0

Because of rounding, detail may not add to Totals.

The figures contained herewith are DOR figures pending the Comptroller's Fiscal Year 2006 Statutory Basis Annual Financial Report.

Offers in Final Settlement FY 2006

Under M.G.L. c. 62C, sec. 37A, the Commissioner of Revenue has the authority, under specific conditions, to accept less than full payment as a final settlement for a state tax liability. The statutory condition for such settlement is "serious doubt" as to collectibility of the tax due or the taxpayer's liability for it. The Commissioner must also determine that the taxpayer or responsible person has acted without intent to defraud. The settlement must be recommended to the Commissioner by at least two deputy commissioners.

The written agreement, signed by all parties and including the reasons for settlement, is a public record. In cases where the liability is reduced by more than half, or by \$20,000 or more, the Attorney General of the Commonwealth must review the settlement and has the authority to object to it.

The law requires that a listing of all settlements entered into during the fiscal year be included in the Commissioner's annual report. In Fiscal Year 2006, 41 settlements were made. All 41 were reviewed by the Attorney General.

The cases approved were as follows:

NAME	TOTAL TAX, INTEREST & PENALTIES	AMOUNT PAID IN SETTLEMENT	AMOUNT ABATED
Towle, Harry P.	\$ 49,791.54	\$ 4,290.00	\$ 45,501.54
The Borrowed Butler, Inc.	61,240.00	32,500.00	28,740.00
Caswell and Company, LTD	338,383.57	108,000.00	230,383.57
Wiksten, Harold & Jeanne	12,938.71	10,600.00	2,338.71
Lookin' Good Babe, Inc.	21,827.11	10,000.00	11,827.11
Zanotti, Lee	24,357.46	8,200.00	16,157.46
Block, Adam T.	39,681.03	1,000.00	38,681.03
Guitar Academy & Showroom, Inc.	194,290.09	74,521.00	119,769.09
Video To Go, Inc.	90,878.97	40,000.00	50,878.97
Gulino, Salvatore R.	36,172.68	13,400.00	22,772.68
Lafountain, Robert	15,375.47	3,240.00	12,135.47
Chlebus, Mercy A. d/b/a	14,023.61	10,000.00	4,023.61
Gamalian, Patricia	9,136.91	550.00	8,586.91
Beldena, Inc.	233,600.28	36,000.36	197,599.92
Raikkonen, John O.	333,097.15	50,000.00	283,097.15
Joe's Pub & Grub, Inc.	145,223.93	20,000.00	125,223.93
Hagopian, Kris	72,702.14	35,000.00	37,702.14
Rapps Deli, Inc.	19,301.33	7,700.00	11,601.33
Taylor III, William C.	28,077.92	12,000.00	16,077.92
Punchline Entertainment of the Cape, Inc.	25,597.02	3,900.00	21,697.02
Stewart, Zoila R.	15,153.83	5,000.00	10,153.83
Kelliher, Amy A.	13,568.16	5,000.00	8,568.16
Celebration at the Close of the Millenium Inc.	17,234.47	7,500.00	9,734.47
Bettencourt, Clifford	17,653.99	3,300.00	14,353.99
New England Personnel Inc.	23,196.60	7,500.00	15,696.60
D & S Auto Repair, Inc.	159,758.12	25,000.00	134,758.12
Kelley, Gail d/b/a	21,325.51	2,063.00	19,262.51
Cabana, David	23,994.99	8,000.00	15,994.99
Asfour, Maher (RP)	76,626.17	20,000.00	56,626.17
Roccanti, Robert d/b/a	97,379.81	39,930.00	57,449.81
Metalwoods Workshop Inc.	26,345.86	16,500.00	9,845.86
Maurer, David	1,899.70	600.00	1,299.70
Le Foi Corporation	76,549.49	13,500.00	63,049.49
Spensjak Corporation, The	94,929.72	38,000.00	56,929.72
Anderson, Eugene	67,094.39	12,700.00	54,394.39
Rackliffe, Eric W. (RP)	19,177.88	6,000.00	13,177.88
Gotham Networks Inc	126,533.96	15,000.00	111,533.96
Sapir, Arthur D. d/b/a	217,560.39	73,000.00	144,560.39
Boutilier, Henry and Lorraine	4,138.70	817.00	3,321.70
White, William	36,427.08	7,200.00	29,227.08
Day, Kenneth	11,742.15	1,500.00	10,242.15
TOTAL	\$2,913,987.89	\$789,011.36	\$2,124,976.53

Because of rounding, detail may not add to Totals.

The figures contained herewith are DOR figures pending the comptroller's Comprehensive Annual Financial Report.

Collection Agencies FY 2006

Chapter 209 of the Acts of 1988 permits the Commissioner of Revenue to use private collection agencies to collect unpaid state taxes. The Commissioner is required to notify all taxpayers whose accounts are to be assigned to a collection agency at least 30 days beforehand.

The law requires that the Commissioner list all agencies with whom collection agreements exist, the amount of taxes collected and the amount of compensation paid in the Department's annual report. They are as follows:

CONTRACTOR	TOTAL COLLECTED	FEES PAID	NET TO DOR
GCS	\$2,273,810	\$356,035	\$1,917,775
OSI	2,493,119	342,217	2,150,902
Walker Associates	2,635,935	349,217	2,286,718
TOTAL	\$7,402,863	\$1,047,469	\$6,355,394

Because of rounding, detail may not add to Totals.

The figures contained herewith are DOR figures pending the comptroller's Comprehensive Annual Financial Report.