

Department of Legislative Services
Maryland General Assembly
2009 Session

FISCAL AND POLICY NOTE

Senate Bill 321
Budget and Taxation

(Senator Brochin)

Estimated Income Tax Deficiencies - Interest

This bill alters the calculation of the annual interest rate that the Comptroller sets for tax deficiencies related to the underpayment of estimated income taxes. The interest rate assessed for these unpaid amounts is equal to the applicable interest rate charged by the Internal Revenue Service (IRS) for underpayment of federal income taxes.

The bill takes effect July 1, 2009.

Fiscal Summary

State Effect: General fund revenues decrease by \$11.4 million in FY 2010 due to estimated change in personal income and corporate income interest rates set by the Comptroller. Transportation Trust Fund (TTF) revenues decrease by \$0.9 million due to estimated change in corporate income tax interest rates. Future year revenues reflect estimated amounts of interest collected and forecasted interest rates. Expenditures are not affected.

(\$ in millions)	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
GF Revenue	(\$11.4)	(\$10.6)	(\$8.1)	(\$8.5)	(\$9.0)
SF Revenue	(\$.9)	(\$.8)	(\$.6)	(\$.6)	(\$.6)
Expenditure	0	0	0	0	0
Net Effect	(\$12.3)	(\$11.4)	(\$8.7)	(\$9.1)	(\$9.6)

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: Local income tax revenues decrease by \$5.1 million in FY 2010 and by \$4.1 million in FY 2014. Local highway user revenues decrease by \$261,000 in FY 2010 and by \$188,000 in FY 2014. Expenditures are not affected.

Small Business Effect: Minimal.

Analysis

Current Law: By October 1 of each year, the Comptroller's Office must set the annual interest rate for tax refunds and monies owed to the State for the next calendar year at a rate equal to the greater of 13% or three percentage points above the average prime rate of interest in the previous fiscal year, based on information from the Federal Reserve Bank. This interest rate applies to all unpaid income tax liabilities.

Background: Exhibit 1 compares the average penalty interest rates assessed by the Comptroller's Office and the IRS in calendar 2004 through 2008.

Exhibit 1 Average Annual Interest Rates Assessed Calendar 2004-2008

<u>Calendar Year</u>	<u>Comptroller's Office</u>	<u>IRS</u>	<u>IRS-Large Corporations</u>
2004	13%	4.50%	6.50%
2005	13%	6.00%	8.00%
2006	13%	7.50%	9.50%
2007	13%	8.00%	10.00%
2008	13%	6.00%	8.00%

Source: Department of Legislative Services

In addition to charging a higher interest rate for underpayments than the IRS, the Comptroller's Office will typically pay a higher interest rate for overpayments relative to the IRS. In the first quarter of 2009 the IRS will apply a 5% interest rate to overpayments by individuals, 4% for corporate overpayments, and 2.5% for corporate payments in excess of \$10,000. The Comptroller's Office will apply a 13% interest rate to overpayments during this time.

Of the 44 states that impose an income tax, the typical penalty interest rate assessed in 2008 was 8.8%. Compared to the interest rate assessed by the IRS on individuals, 37 states assessed a higher rate, six assessed about the same, and one assessed a lower rate. The average penalty interest rates in surrounding jurisdictions in 2008 were: New Jersey (9% - 10.5%), District of Columbia (10%), West Virginia (9.5%), Virginia (8%), Pennsylvania (7%), and Delaware (6%).

State Fiscal Effect: The bill limits the State interest rate assessed for the underpayment of estimated taxes. Based on the amount of current interest collected on the underpayment of estimated taxes and projected interest rates, general fund revenues will decrease by \$11.4 million in fiscal 2010 and by \$9.0 million in fiscal 2014. TTF revenues will decrease by \$869,000 in fiscal 2010 and by \$628,000 in fiscal 2014. **Exhibit 2** lists the estimated change in State revenues and local revenues in fiscal 2010 through 2014.

Local Fiscal Effect: Local income tax revenues and local highway user revenues would decrease beginning in fiscal 2010 as shown in Exhibit 2.

Exhibit 2
Revenues Losses from Interest Rate Changes
Interest on Estimated Payment Deficiencies
(\$ in Millions)

	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>	<u>FY 2013</u>	<u>FY 2014</u>
Personal Income Tax (General Funds)	\$8.0	\$7.5	\$5.9	\$6.2	\$6.5
Corporate Income Tax	4.3	3.9	2.8	2.9	3.1
General Fund	3.4	3.1	2.2	2.3	2.5
Transportation Trust Fund	0.9	0.8	0.6	0.6	0.6
State	0.6	0.6	0.4	0.4	0.4
Local	0.3	0.2	0.2	0.2	0.2
Local Income Tax	5.1	4.7	3.7	3.9	4.1

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Comptroller's Office, Internal Revenue Service, Moody's Investors Service, Department of Legislative Services

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