Department of Legislative Services

Maryland General Assembly
2009 Session

FISCAL AND POLICY NOTE

House Bill 465 (Delegate Ross)
Ways and Means

Income Tax - Payments - Sale of Real Property by Nonresidents

This bill alters the amount of withholding required for nonresident real estate sale payments.

The bill takes effect July 1, 2009.

Fiscal Summary

State Effect: General fund revenues increase by $2.8 million in FY 2011 as a result of increased nonresident realty withholdings. This one-time increase in withholdings will eventually be refunded once a nonresident files a Maryland income tax return. Any increase in revenue is due to a timing issue and is not due to a net increase in revenue collections. Expenditures are not affected.

($ in millions)	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
GF Revenue	$0	$2.8	$0	$0	$0
Expenditure	0	0	0	0	0
Net Effect	$.0	$2.8	$.0	$.0	$.0

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

Local Effect: None.

Small Business Effect: Minimal.

Analysis

Current Law/Background: In most cases, a real estate sale by a nonresident involves property that is not the individual's primary residence, meaning the sale may trigger a capital gain that is taxable under Maryland income tax. A nonresident may not elect to file a Maryland return and the federal return would not necessarily indicate Maryland taxable income. In the absence of withholding, it could be difficult to collect Maryland taxes owed from these transactions.

Chapter 203 of 2003 – Budget Reconciliation and Financing Act of 2003 (BRFA of 2003) – required that, except under specified circumstances, certain payments be made to either the clerk of the circuit court or the Department of Assessments and Taxation in order to record a change of ownership in a sale or exchange of real property by a nonresident or nonresident entity. The payment must be transferred to the Comptroller's Office within 30 business days as a withholding for income taxes due on the sale of the property. Chapter 203 required that the payment equal 4.75% of the total payment to a nonresident or 7% of the total payment to a nonresident entity.

Total payment is defined as the net proceeds of a sale paid to a nonresident, including the fair market value of any property transferred. Net proceeds are equal to the total sales price paid to the nonresident less: (1) debts of the nonresident secured by a mortgage or other lien on the property being transferred that are being paid upon the property sale or exchange; and (2) other expenses of the nonresident arising from the property sale or exchange and disclosed at settlement, not including adjustments in favor of the transferee. Net proceeds do not include adjustments in favor of the transfers that are disclosed at settlement.

Chapter 444 of 2005 (BRFA of 2005) altered the rate of withholding for nonresidents to be equal to the sum of the top marginal State income tax rate imposed plus the special nonresident tax imposed on nonresidents not subject to the local income tax. The special nonresident tax is equal to the lowest county income tax rate imposed in the tax year, which is currently 1.25%. Chapter 3 of the 2007 special session increased the corporate income tax rate to 8.25% and altered the withholding provision for nonresident entities to be equal to the current corporate income tax rate. Chapter 3 of 2007 also increased the top marginal income tax rate under the State personal income tax to 5.5% which Chapter 10 of 2008 subsequently increased, for tax years 2008 through 2010, to 6.25%.

In fiscal 2008, a total of $41.8 million was withheld from nonresident realty sales and virtually all of this was withheld from nonresident individuals. This is roughly the same amount that was withheld in 2004, which reflects a decrease in real estate sales and prices and an increase in the rate of withholding (for nonresidents the rate increased from 4.75% to 7.5% for nonresidents and 7% to 8.25% for nonresident entities). If a nonresident files a Maryland income tax return the individual is able to "claim" the amount of taxes withheld in determining final tax liability. In most cases, the amount withheld from a sale will be more than the final State income tax liability. As a result, if a nonresident files a Maryland tax return, the final tax payment in most instances will be less than the amount withheld and the individual will receive a refund. Nonresidents can also generally claim a credit against the income tax in the state in which he/she resides for the amount of income tax paid to Maryland.

State Effect: The bill would alter the State withholding tax rate on nonresident real estate sales beginning July 1, 2009. Under current law, the top marginal tax rate under the personal income tax decreases from 6.25% to 5.5% beginning with tax year 2011 – the amount withheld under current law will decrease from 7.5% to 6.75%. The bill requires nonresident withholdings to remain at 7.5% for all tax years. As a result, general fund revenues will increase by $2.8 million in fiscal 2011, which reflects increased nonresident realty sales withholdings during one-half of tax year 2011. It is assumed that nonresidents will file a tax return and receive a refund in fiscal 2012 due to the additional amount withheld as a result of the bill. Future years will not be impacted as increased withholding during the fiscal year is assumed to be offset by refunds filed on tax returns. To the extent that additional withholdings reflect additional tax liabilities for a nonresident, general fund revenues could increase in fiscal 2012 and beyond but any increase is expected to be minimal. Revenue gains in fiscal 2011 will be less if the lowest county income tax rate imposed is increased from 1.25%.

The bill's provision altering the amount withheld from a nonresident entity will not impact revenues under current law.

Additional Information

Prior Introductions: None.

Cross File: SB 453 (Senator Peters, *et al.*) - Budget and Taxation.

Information Source(s): Comptroller's Office, Judiciary (Administrative Office of the Courts), Department of Legislative Services

Fiscal Note History: First Reader - February 16, 2009
ncs/hlb

Analysis by: Robert J. Rehrmann

Direct Inquiries to:
(410) 946-5510
(301) 970-5510