HB 112

Department of Legislative Services

Maryland General Assembly
2017 Session

FISCAL AND POLICY NOTE
Enrolled

House Bill 112 (Delegate Fraser-Hidalgo, *et al.*)
Ways and Means Budget and Taxation

Interest Rate on Tax Deficiencies and Refunds - Rounding

This bill repeals the requirement that the Comptroller, when setting the annual interest rate for tax refunds and monies owed to the State, round the interest rate to the nearest whole number.

The bill takes effect July 1, 2017.

Fiscal Summary

State Effect: General fund revenues decrease by $1.0 million in FY 2018 due to the decrease in interest income revenues from not rounding the interest rate. Transportation Trust Fund (TTF) revenues decrease by $18,000 and Higher Education Investment Fund (HEIF) revenues decrease by $7,400 in FY 2018. Future year estimates reflect projected interest revenues and rates. No effect on expenditures.

(in dollars)	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022
GF Revenue	($1,035,300)	($1,035,300)	($1,035,300)	($1,035,300)	($1,035,300)
SF Revenue	($25,500)	($25,500)	($25,500)	($25,500)	($25,500)
Expenditure	0	0	0	0	0
Net Effect	($1,060,800)	($1,060,800)	($1,060,800)	($1,060,800)	($1,060,800)

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

Local Effect: Local income tax revenues decrease by $702,000 in FY 2019, FY 2021, and FY 2023. Local highway user revenues decrease by $3,400 in FY 2019, FY 2021, and FY 2023. No effect on local expenditures.

Small Business Effect: Potential meaningful. Small businesses could realize reduced interest charges in calendar years 2018, 2020, and 2022.

Analysis

Current Law: Chapter 322 of 2016 altered the calculation of the annual interest rate that the Comptroller sets for tax deficiencies and refunds. 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, rounded to the nearest whole number, equal to the greater of three percentage points above the average prime rate of interest in the previous fiscal year, based on information from the Federal Reserve Bank, or:

- 13% for calendar 2016;
- 12% for calendar 2017;
- 11.5% for calendar 2018;
- 11% for calendar 2019;
- 10.5% for calendar 2020;
- 10% for calendar 2021;
- 9.5% for calendar 2022; and
- 9% for calendar 2023 and each year thereafter.

Thus, the interest rate will be rounded up to 12% for calendar 2018, 11% for calendar 2020, and 10% for calendar 2022, assuming these rates are higher than three percentage points above the average prime rate of interest in the previous fiscal year.

Background: Of the states that impose an income tax, the interest penalty rate currently imposed on overpayments typically ranges from 3% to 8%. Of those states, only Oklahoma (15%) has a higher rate than Maryland, and Georgia and North Dakota have a rate equal to Maryland in calendar 2017. The current interest penalty rates in surrounding jurisdictions are Delaware (6%), District of Columbia (1% above the primary credit discount rate for the Richmond Federal Reserve Bank, rounded to the nearest whole number, not to exceed 6%), Pennsylvania (4%), Virginia (6%, adjusted quarterly), and West Virginia (6.5% for the first half of 2017).

In fiscal 2014, the Comptroller's Office collected the following amounts of interest: $34.2 million from the individual income tax and fiduciary returns; $4.3 million from the corporate income tax; $2.1 million from income tax withholding; and $2.6 million from sales tax returns. A further amount was collected from interest ($2.2 million) from pass through entities on sales tax assessments. The Comptroller's Office typically pays out less than $1.0 million in interest annually, depending on the year, for the various taxes.

State Fiscal Effect: By eliminating the requirement to round the interest rate to the nearest whole number, the bill alters the State interest rate for late payment of taxes and tax refunds by setting the rate at the greater of 11.5% for calendar 2018 (instead of 12%), 10.5% for calendar 2020 (instead of 11%), and 9.5% for calendar 2022 (instead of 10%) or three percentage points above the average prime rate of interest in the previous fiscal year. Based on the amount of current interest collected on late taxes, interest paid on tax refunds, and projected interest rates, general fund revenues will decrease by $1.0 million, TTF revenues will decrease by $18,000, and HEIF revenues will decrease by $7,400 in fiscal 2018, which represent approximately one-half of the estimated annual revenue decrease for calendar 2018.

The estimated changes in interest payments shown in **Exhibit 1** are based on the difference in interest rates that would be applied by the Comptroller's Office under the bill compared to the estimated effective interest rates under current law in each tax year. For purposes of this estimate, the average of interest payments received and paid over a six-year period (fiscal 2009 through 2014) was used to estimate future year changes due to annual fluctuations in the amount of payments received. This amount was then adjusted to account for increased tax compliance efforts instituted over the past several years. Future year payments are estimated to remain constant.

Exhibit 1
State and Local Revenue Impacts
Fiscal 2018-2022

	FY 2018	FY 2019	FY 2020	FY 2021	FY 2022
General Fund	($1,035,300)	($1,035,300)	($1,035,300)	($1,035,300)	($1,035,300)
HEIF	(7,400)	(7,400)	(7,400)	(7,400)	(7,400)
TTF-MDOT	(18,000)	(18,000)	(18,000)	(18,000)	(18,000)
Total	**($1,060,800)**	**($1,060,800)**	**($1,060,800)**	**($1,060,800)**	**($1,060,800)**
Local Revenues					
TTF-LHUR	$0	($3,400)	$0	($3,400)	$0
Income Tax	0	(702,000)	0	(702,000)	0
Total	**$0**	**($705,400)**	**$0**	**($705,400)**	**$0**

HEIF: Higher Education Investment Fund
TTF: Transportation Trust Fund
MDOT: Maryland Department of Transportation
LHUR: local highway user revenues

Local Fiscal Effect: Local revenues will decrease as a result of a decrease in local highway user revenues distributed from the corporate income tax and from local income tax revenues. Local governments receive a portion of personal income tax interest penalty revenues. These distributions are made biannually, with the first distribution made in the first month of a fiscal year based on interest collections from the second half of the preceding fiscal year. The second distribution is made in January and is attributable to interest received in the first half of that fiscal year. Thus, as a result of the interest rate changes in calendar 2018, 2020, and 2022, local governments will receive distributions in the following fiscal year, so total local revenues will decrease by $705,400 in fiscal 2019, 2021, and 2023.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Comptroller’s Office; Department of Legislative Services

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