

Department of Legislative Services
Maryland General Assembly
2018 Session

FISCAL AND POLICY NOTE
Third Reader

House Bill 686

(Delegate Luedtke, *et al.*)

Ways and Means

Budget and Taxation

Income Tax - Wynne Case - Local Government Repayments to the Local Reserve
Account

This bill delays by two years the time period in which local jurisdictions must reimburse the local income tax reserve account pursuant to specified refunds resulting from the final decision under *Maryland State Comptroller of the Treasury v. Brian Wynne, et ux.*, 431 Md. 147 (2013) (Wynne case).

Fiscal Summary

State Effect: The Comptroller's Office can implement the bill's requirements with existing resources. No effect on revenues.

Local Effect: Local income tax revenues for local jurisdictions impacted by the Wynne case increase by approximately \$100.0 million in FY 2019 through 2021 and decrease by a corresponding amount in FY 2024 through 2026. Local expenditures are not affected.

Small Business Effect: None.

Analysis

Current Law: The Budget Reconciliation and Financing Act of 2015 (Chapter 489) requires the Comptroller to (1) pay certain interest and refunds for prior tax years from the Wynne case from the local income tax reserve account and (2) if a local government does not reimburse the account in a timely manner, withhold the affected local government's quarterly income tax distributions in nine equal installments beginning in the first quarter of fiscal 2017, until the amount is fully reimbursed by the local government for its share of related refunds and interest. Under Chapter 489, the Comptroller would have withheld

quarterly income distributions for affected local governments over three fiscal years – fiscal 2017 through 2019.

Chapter 24 of 2016 delayed and lengthened the time period for reimbursing the local income tax reserve account, if a local government does not reimburse the account in a timely fashion, by requiring the Comptroller to withhold from the affected local government's quarterly distributions in 20 equal installments beginning in the fourth quarter of fiscal 2019. As a result, the Comptroller will withhold quarterly income distributions for affected local governments over six fiscal years – fiscal 2019 through 2024.

Local Income Tax Reserve Account

The local income tax reserve account is used by the Comptroller's Office to manage the cash flow of personal income tax payments and distributions to local governments. The account is also used to meet the State's liability for local income taxes according to generally accepted accounting principles. A portion of personal income tax net receipts is put into the account each month, representing an estimate of local income tax payments. In all but two months, a distribution of local income tax revenues is made from the account to local governments.

The Comptroller's Office distributes to each municipality, special taxing district, and county its pro rata share of income tax revenue based on the income tax collected in each local jurisdiction. After making specified distributions, the Comptroller's Office distributes to each special taxing district and municipality, based on the certification as to the State income tax and county income tax liability of its residents, the greater of 17% of the county income tax liability or 0.37% of the Maryland taxable income of the residents. After making distributions to municipalities and special taxing districts, the Comptroller's Office distributes to each county the remaining revenue attributable to the county income tax.

Background: In the Wynne case, the Maryland Court of Appeals upheld a ruling of the Howard County Circuit Court that the failure of the State to allow a credit with respect to the county income tax for out-of-state income taxes paid to other states on pass-through income earned in those states discriminates against interstate commerce and violates the Commerce Clause of the U.S. Constitution. The State appealed the decision to the U.S. Supreme Court, which affirmed the judgment of the Maryland Court of Appeals on May 18, 2015.

As of December 2017, the Comptroller's Office has issued a total of \$244.9 million in refunds for tax years 2006 through 2014. Local governments have repaid \$1.8 million of this amount. In tax year 2015, the first year in which taxpayers could claim the local tax

credit from the beginning of the tax year, taxpayers claimed a total of \$52 million in out-of-state income taxes paid to other states against the local income tax.

Local Fiscal Effect: The bill delays by two years the time period in which the local reserve account must be reimbursed. The Comptroller must withhold the amount owed from the affected local jurisdiction’s quarterly income tax distributions in 20 equal installments beginning with the fourth quarter of fiscal 2021. **Exhibit 1** shows the estimated net impact of altering the repayment schedule for local jurisdictions impacted by the Wynne case.

Exhibit 1
Net Revenue Impact on Local Jurisdictions
Wynne Case
Fiscal 2019-2026
(\$ in Millions)

| | <u>2019</u> | <u>2020</u> | <u>2021</u> | <u>2022</u> | <u>2023</u> | <u>2024</u> | <u>2025</u> | <u>2026</u> |
|-------------------|---------------|---------------|---------------|-------------|-------------|-----------------|-----------------|-----------------|
| Current Law | \$25.0 | \$50.0 | \$50.0 | \$50.0 | \$50.0 | \$25.0 | \$0.0 | \$0.0 |
| Proposed | 0.0 | 0.0 | 25.0 | 50.0 | 50.0 | 50.0 | 50.0 | 25.0 |
| Net Impact | \$25.0 | \$50.0 | \$25.0 | \$0 | \$0 | (\$25.0) | (\$50.0) | (\$25.0) |

Additional Information

Prior Introductions: None.

Cross File: SB 742 (Senator Madaleno, *et al.*) - Budget and Taxation.

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

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