HB 664

Department of Fiscal Services

Maryland General Assembly

FISCAL NOTE

House Bill 664 (Delegate Finifter, *et al.*)
Ways and Means

Recordation and Transfer Taxes - Estate Planning Exemption

This bill exempts the transfer of property to a corporation, partnership, or limited liability company from recordation and transfer taxes if the transfer is for estate planning purposes. The bill also imposes recordation and transfer taxes on any transfers of ownership interest in an estate planning entity unless the transfer of the entity's assets to the recipient would be otherwise exempt.

The bill is effective July 1, 1997.

Fiscal Summary

State Effect: Indeterminate effect on revenues and expenditures beginning in FY 1998 as discussed below.

Local Effect: Indeterminate decrease in local recordation and transfer tax revenues beginning in FY 1998 as discussed below.

Small Business Effect: Minimal impact on small businesses as discussed below.

Fiscal Analysis

Background: Under certain circumstances, current law exempts portions of direct transfers of real property between family members from recordation and transfer taxation. However, if a direct transfer is executed for estate planning purposes and gift taxes are to be avoided, the transfer could significantly complicate management of the property. On the other hand, if such a transfer is executed through the intermediary of a wholly owned partnership, corporation, or limited liability company, recordation and transfer taxes will be imposed when the property is transferred to the intermediate entity.

This bill is primarily designed to allow parents to transfer portions of real property to their children each year through the use of a partnership, corporation, or limited liability company while maintaining management control over the property and avoiding recordation and transfer taxes.

Bill Summary: This bill exempts the transfer of property to a corporation, partnership, or limited liability company from recordation and State and local transfer taxes if:

- each of the individuals with ownership interest in the property maintains ownership interest in the estate planning entity after the transfer;
- no other individuals have an ownership interest in the estate planning entity;
- an ownership interest in the estate planning entity is the only consideration payable for the transfer; and
- the transferor signs a statement under oath that the transfer is primarily for estate planning purposes.

The bill also imposes recordation and transfer taxes on any subsequent transfers of ownership interest in the estate planning entity unless the transfer of the entity's assets to the recipient would otherwise be exempt. The bill contains a number of reporting requirements for the implementation of this provision:

- Upon receiving an exemption for estate planning purposes, the estate planning entity must file a certificate with the Department of Assessments and Taxation that sets forth: (1) all the owners of the real property who initially transferred it to the estate planning entity; (2) all the owners of an entity that initially transferred the real property to the estate planning entity; and (3) all of the owners of any interest in the estate planning entity to which the real property is transferred. A filing fee of $500 is assessed for this certificate.
- Upon receiving an exemption for estate planning purposes, and every five years thereafter, an owner of an estate planning entity must file an affidavit, accompanied by a $250 filing fee, affirming that either (1) the entity is owned entirely by individuals who are not subject to recordation tax; or (2) the recordation and transfer taxes have been paid for an ownership interest held by an individual who is subject to the recordation and transfer taxes. In each filing after the first, the affidavit must also identify any transferees who are subject to the recordation and transfer taxes.

- The estate planning entity must also file with the department a report of any transfer of interest in the estate planning entity within 30 days of the transfer. The report must include the consideration payable for the transfer, the amount allocable to the assets of the estate planning entity other than real property located in the State, and any exemption from recordation and transfer taxes. The report must be accompanied by payment of a $250 filing fee as well as any recordation and transfer taxes, penalties, or interest due on the transfer. If the taxes are not paid within 30 days of the transfer, interest on the unpaid amount accrues at 1% per month and a penalty of 10% of the unpaid amount is assessed.

State Revenues: The State transfer tax rate is currently 0.5%. State transfer tax revenues could decrease depending upon the number of transfers of real property to estate planning entities. This revenue loss could be somewhat offset in later years by subsequent transfers of ownership interest in estate planning entities, depending upon how many transfers would be exempt. Since data is not available on the number or magnitude of transfers qualifying for an exemption, any decrease in revenues cannot be reliably estimated at this time.

Portions of State transfer tax revenues are distributed to Program Open Space, the Agricultural Land Preservation Fund, and the Heritage Conservation Fund. Any decrease in transfer tax revenues would result in a funding decrease for these programs.

The bill requires the Department of Assessments and Taxation to charge a $500 filing fee for an initial certificate outlining the owners of the real property who initially transferred property into an estate planning entity and the owners of any interest in the estate planning entity to which the real property is transferred. The department is also required to charge a fee of $250 for update filings to be submitted at least every five years and a $250 report fee for any estate planning entity that has a transfer of interest in an entity. These fees would increase general fund revenues depending upon the number of new filings and update filings. The Department of Assessments and Taxation estimates that there could be approximately 1,000 new transfer certificates ($500 per transfer) each year starting in fiscal 1998 and an estimated 800 update transfers per year ($250 per transfer) beginning in fiscal 2002. Based on these estimates, general fund revenues from these transfers could increase by $500,000 per year through fiscal 2001 and by $700,000 in fiscal 2002. However, the Department of Fiscal Services advises that sufficient data does not exist to determine the number of transfers that may occur. Without this data, any increase in revenues cannot be reliably estimated. It also cannot be reliably estimated as to how many transfers of interest for estate planning entities may occur in any given fiscal year.

This bill requires the department to pay any recordation taxes it collects from these property transfers to the appropriate clerks of the circuit courts, increasing State general fund revenues as discussed below.

To the extent that enactment of this bill provides an incentive for more individuals to use this type of estate planning, the State could also realize a loss in estate and inheritance tax revenues in the long term.

State Expenditures: To track transfers of ownership interests in estate planning entities and collect the appropriate taxes, the Department of Assessments and Taxation may need additional staff. The department advises that it would need to hire one Charter Specialist and one Office Secretary at a cost of $98,600 in fiscal 1998. However, the Department of Fiscal Services advises that the need for these additional positions depends upon the number of transfers that would be reported, which cannot be reliably determined at this time.

Local Revenues: Local recordation and transfer tax revenues could decrease depending upon the number of transfers of real property to estate planning entities and the respective local tax rates. This revenue loss could be slightly offset in later years by subsequent transfers of ownership interest in the estate planning entities; this is dependent upon how many of those transfers would be exempt. Because data is not available on the number or magnitude of transfers qualifying for the exemption, any decrease in revenues cannot be reliably estimated at this time.

The Department of Assessments and Taxation currently pays the recordation taxes that it collects directly to the counties. This bill requires the department to pay any recordation taxes it collects from these property transfers to the appropriate clerks of the circuit courts, who retain commissions from recordation taxes of anywhere from 2.5% to 5% of all collections received. Since clerks of the courts are part of the Judiciary and the commissions retained by the clerks are general fund revenues, State revenues would increase while county finances would be negatively affected. Any specific impact is indeterminate.

Small Business Effect: This bill could positively impact small businesses that provide estate planning services since an incentive is provided for the creation of estate planning entities. The bill would create costs for estate planning entities due to reporting requirements and the payment of certain filing fees to the Department of Assessments and Taxation. Any specific impact cannot be reliably estimated at this time.

Information Sources: Judiciary (Administrative Office of the Courts), Department of Assessments and Taxation, Garrett County, Prince George's County, Montgomery County, Department of Fiscal Services

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