SB 310

Department of Legislative Services
Maryland General Assembly

FISCAL NOTE
Revised

Senate Bill 310 (Senator Hoffman, *et al.*)
Budget and Taxation

Qualified Capital Gains - Maximum Tax

This bill creates a tax credit, against both State and local income taxes, of the amount by which the State income tax exceeds the sum of $65,000 and the tax on Maryland taxable income less "qualified capital gains". Qualified capital gains are defined as long-term capital gains less short-term capital losses which would not be taxed if the taxpayer were a non-resident.

This bill is effective July 1, 1998 and applies to all taxable years beginning after December 31, 1997.

Fiscal Summary

State Effect: Potential indeterminate general fund revenue loss in FY 1999 and beyond. Expenditures would not be affected.

Local Effect: Local revenues could decline from 30% to 60% of any general fund revenue loss. Expenditures would not be affected.

Small Business Effect: Potential meaningful effect.

Fiscal Analysis

Background: The credit created by this bill affects those taxpayers with qualified capital gains (long-term capital gains less short-term capital losses which would not be taxed if the taxpayer were a non-resident) of $1,313,131 or more. The credit has the effect of capping the gains subject to tax at this amount in tax year 1998. As the top tax rate declines through 2002, the cap will increase to $1,368,421. **Exhibit 1** demonstrates several examples of how the credit operates.

Exhibit 1
Examples of Effect of SB 310 in Tax Year 1998

	Taxpayer A	Taxpayer B	Taxpayer C	Taxpayer D
Total Taxable Income	$1,500,000	$1,500,000	$2,000,000	$2,000,000
Qualified Capital Gains	1,000,000	1,400,000	1,400,000	1,800,000
Other Taxable Income	500,000	100,000	600,000	200,000
State Taxes	74,192	74,192	98,942	98,942
$65,000+Tax on Other Taxable Income	89,692	69,892	94,642	74,842
Amount of Credit	0	4,300	4,300	24,100
Net Taxes Paid	74,192	69,892	94,642	74,842
Value of Credit in Terms of Taxable Income	0	86,869	86,869	486,869

Taxpayer A does not receive a tax credit, because qualified taxable gains are less than $1.3 million. Taxpayers B and C receive the same credit, $4,300. This credit equates to exempting $86,869 of income from tax, which is the amount by which their qualified capital gains exceed $1,313,131. Taxpayer D, with the same total taxable income as taxpayer C, receives a $24,100 credit. This equates to exempting $486,869 of income from tax, which again is the amount by which qualified capital gains exceed $1,313,131.

State Revenues: This bill would result in an indeterminate general fund revenue loss. There will be an estimated 705 returns with tax liability greater than $65,000 in tax year 1998. On average, State tax liability is estimated at $107,175, while the average State tax liability without capital gains is estimated at $73,127, implying average capital gains of $687,840. Thus, the average taxpayer with State tax liability greater than $65,000 would not receive the credit provided by this bill. However, it is anticipated that some unknown but very small number of individuals would have qualified capital gains over $1,313,131. The general fund revenue loss would be 4.95% of the total qualified capital gains over $1,313,131 for each taxpayer. If, for example, five taxpayers have $2 million of qualified capital gains each, the revenue loss would be $170,000.

State Expenditures: The Office of the Comptroller advises that $45,000 of expenditures would be incurred for programming changes to the tax processing system and $2,700 of expenditures would be incurred for form and instruction changes in fiscal 1999. The Department of Legislative Services advises that economies of scale regarding computer programming changes could be realized, since there will be changes to the income tax processing system due to the 1997 income tax reduction which is phased in through 2002. Additionally, since forms and instructions are updated annually, these costs could be incurred within existing budgeted resources.

Local Revenues: Since this credit serves to reduce both State and local income taxes, piggyback taxes would be reduced. Since this credit would be claimed by very few taxpayers, however, the actual piggyback loss could range from 30% to 60% of the State loss (based on a $1,200 personal exemption and a 5% top tax rate), depending on the counties of residence of taxpayers claiming this credit.

Small Business Effect: Small businesses filing individual income tax returns with capital gains over $1,313,131, if any, could realize a substantial reduction in State and local income taxes.

Information Source(s): Office of the Comptroller (Bureau of Revenue Estimates), Department of Legislative Services

Fiscal Note History:	First Reader - February 20, 1998
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