

Department of Legislative Services
Maryland General Assembly

FISCAL NOTE

Senate Bill 602 (Senator Neall. *et al.*)

Budget and Taxation

Income Tax Reduction

This bill reduces the top marginal State income tax rate from 4.95% to 4.9% for tax year 1998; from 4.9% to 4.8% for tax year 1999; from 4.85% to 4.7% for tax year 2000; from 4.8% to 4.6% for tax year 2001; and from 4.75% to 4.5% for tax year 2002. The two-income subtraction modification is adjusted to account for the effect of the lower top rates.

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

Fiscal Summary

State Effect: General fund revenues would decline by an estimated \$67.7 million in FY 1999, increasing to \$190.9 million in FY 2003, when this tax reduction would be fully phased-in. Expenditures would not be affected since tax rates are already changing through 2002.

(in millions)	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
GF Revenues	(\$67.7)	(\$87.4)	(\$125.8)	(\$166.0)	(\$190.9)
GF Expenditures	0.0	0.0	0.0	0.0	0.0
Net Effect	(\$67.7)	(\$87.4)	(\$125.8)	(\$166.0)	(\$190.9)

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

Local Effect: None.

Small Business Effect: Meaningful.

Fiscal Analysis

State Revenues: Based on 1996 income tax collections and current revenue forecasts, general fund revenues would decline by an estimated \$67.7 million in fiscal 1999; \$87.4 million in fiscal 2000; \$125.8 million in fiscal 2001; \$166.0 million in fiscal 2002; and \$190.9 million in fiscal 2003. This rate reduction would result in a revenue reduction of approximately 14.3% in tax year 2002 when compared to tax law prior to the 1997 Tax Reduction Act (a \$1,200 personal exemption and a 5% top rate).

The Governor's proposed fiscal 1999 budget is based on revenue reductions resulting from the 1997 Tax Reduction Act. The proposed budget also provides a \$100 million allowance to the Rainy Day Fund to fund the 1997 tax reduction in future years.

Small Business Effect: Many different forms of businesses pay the individual income tax rather than the corporate income tax, including sole proprietorships, partnerships, limited liability companies, and subchapter S corporations. Most, but not all, businesses of these types are small businesses. The total number of these types of businesses, as well as the number which are small businesses, is unknown.

A reduction in the top income tax rate will benefit these small businesses as it will all other taxpayers by allowing such businesses to retain a greater share of taxable income. These small businesses will save up to 5% of their State tax liability.

Additional Comments: Exhibit 1 shows the savings in 1998 and 2002 (when the bill would be fully implemented) for single individuals earning \$25,000 and \$60,000 (with the standard deduction and \$8,000 of itemized deductions), and for families of four earning \$40,000 and \$100,000 (with the standard deduction and \$10,000 of itemized deductions, two-income subtraction). The table also shows the increased federal income tax liability for those who itemize deductions. Of the total reduction in State taxes paid by Maryland taxpayers, about 15% would be paid in higher federal income taxes by those who itemize.

**Exhibit 1
Examples of Tax Savings**

	<u>Single Individual</u>		<u>Family of Four</u>	
	\$25,000	\$60,000	\$40,000	\$100,000
Gross Income				
1998 State Savings	9	24	13	40
Federal Tax Increase	0	7	0	11
Net Savings	9	17	13	29
2002 State Savings	44	117	56	191
Federal Tax Increase	0	33	0	53
Net Savings	44	84	56	135

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

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