HB 910

Department of Legislative Services

Maryland General Assembly
2003 Session

FISCAL AND POLICY NOTE
Revised

House Bill 910 (Delegate C. Davis)
Ways and Means

Balancing Budget Act of 2003

This bill increases the highest income tax bracket by 0.05% to 4.8% and lowers the exemption for taxpayers and their dependents to $2,100 for tax years 2003 and 2004 only. The bill also increases the motor fuel tax by 5 cents a gallon and the sales tax by 1% for fiscal 2004 and 2005 only.

The bill takes effect June 1, 2003, with the effective dates of the various tax provisions noted above.

Fiscal Summary

State Effect: General fund revenues could increase by approximately $704.6 million in FY 2004 and $619.7 million in FY 2005. Transportation Trust Fund (TTF) revenues (and other minor special fund revenues) could increase by $141.5 million in FY 2004 and $143.0 million in FY 2005. The Comptroller's Office would experience administrative expenditures in FY 2003 and 2005.

($ in millions)	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
GF Revenue	$0	$704.6	$619.7	$0	$0
SF Revenue	0	141.5	143.0	0	0
GF Expenditure	.1	0	.2	0	0
Net Effect	($.1)	$846.1	$762.5	$0	$0

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

Local Effect: Transportation revenues distributed to local governments via TTF revenue sharing would increase by approximately $45 million in FY 2004 and by approximately $46 million in FY 2005.

Local government revenues would increase by approximately $60.7 million in FY 2004 and $20.4 million in FY 2005 as a result of lowering personal exemption amounts.

Small Business Effect: Meaningful. To the extent that the additional sales tax rate encourages consumers to shift purchases to out-of-state or remote sellers and away from Maryland retailers that are small businesses, these small businesses could experience a meaningful negative impact. Small businesses may also experience minimal additional costs due to reprogramming their cash registers.

Analysis

Current Law: See discussion below.

Background: The sales tax rates for neighboring states are as follows: District of Columbia (5.75%), West Virginia (6%), Pennsylvania (6%, plus 1% local sales tax in certain jurisdictions; no sales tax on clothing), Delaware (none, but a gross receipts tax on retailers), and Virginia (4.5%, including 1% universal local sales tax).

State Revenues: The estimated revenue impact of these provisions are illustrated below:

Exhibit 1
Summary of Fiscal Impact
($ in Millions)

Estimated Additional Revenues	Revenue Distribution	FY 2004	FY 2005
4.8% tax bracket	General fund	69.2	24.0
$2,100 exemption	General fund	101.5	34.1
1% sales tax	General fund	530.6	558.2
5 cent motor fuel tax			
Total TTF	Special fund	140.6	142.1
MDOT share		97.2	98.2
Local highway user revenues		43.5	43.9
Waterway Improvement and Fisheries and Dev.	Special fund	0.9	0.9
Chesapeake Bay programs	General fund	3.3	3.5
Total motor fuel tax		144.8	146.3
Total impact – HB 910		**846.1**	**762.6**

Increase Top Marginal Rate to 4.8%

General fund revenues would increase by approximately $45.2 million in tax year 2003 and $47.9 million in tax year 2004. Because the top rate is increased beginning with tax year 2003, it is assumed that most taxpayers will not adjust their estimated payments to reflect the increased top marginal rate prior to July 1, 2003. Consequently, general fund revenues are estimated to increase by $69.2 million in fiscal 2004, reflecting the impact of one and one-half tax years, and by $24.0 million in fiscal 2005, which reflects the impact of one-half of tax year 2004. The estimate is based on the following facts and assumptions:

- in tax year 2001 there were 2,111,370 taxable returns filed with net taxable income over $3,000;

- Maryland taxable income was approximately $93.9 billion in tax year 2001; and

- tax year 2001 taxable income is increased according to Bureau of Revenue Estimates official forecast.

Lower Personal Exemption Amount to $2,100

General fund revenues would increase by approximately $67.4 million in tax year 2003 and $68.1 million in tax year 2004. Because the personal exemption amount is reduced beginning with tax year 2003, it is assumed that most taxpayers will not adjust their estimated payments to reflect the new personal exemption amount prior to July 1, 2003. Consequently, general fund revenues are estimated to increase by $101.5 million in fiscal 2004, reflecting the impact of one and one-half tax years, and by $34.1 million in fiscal 2005, which reflects the impact of one-half of tax year 2004. The estimate is based on the following facts and assumptions:

- in tax year 2000, there were 4,543,990 exemptions claimed for taxpayers and their dependents;

- the number of exemptions increase by approximately 1% annually; thus, it is estimated that 4,681,677 exemptions will be claimed in tax year 2003 and 4,728,494 will be claimed in tax year 2004; and

- top marginal tax rate is 4.80% for tax years 2003 and 2004.

Motor Fuel Tax

A 5 cent increase in the tax (except for aviation and turbine fuels, which represent a negligible portion of motor fuel sales) would result in a revenue increase of about $144.8 million in fiscal 2004 and $146.3 million in fiscal 2005. The estimated distribution of these additional revenues is illustrated in **Exhibit 1**. This estimate assumes a 0.6% decline in total consumption associated with fuel price elasticity.

Increased Sales Tax

State sales tax revenues (general funds) could increase by $530.6 million in fiscal 2004, increasing in fiscal 2005 based on projected sales tax growth, and incorporating a projected 1% decline in taxable sales, as illustrated below in **Exhibit 2**.

Exhibit 2
Projected Increase in Sales and Use Tax Revenues
($ in Millions)

	FY 2004	FY 2005
Current GF Estimate	2,850.8	2,999.4
Less Rental Vehicle Revenues	2,822.1	2,969.2
Implied Taxable Sales @ 5%	56,442.1	59,383.8
Implied Taxable Sales with 1% Decline	55,877.6	58,789.9
Total Revenues @ 6%	3,352.7	3,527.4
Net GF Revenue Increase	530.6	558.2

The 1% decline reflects an assumption about foregone taxable sales based on one of three causes: (1) the sale does not take place at all because the marginal cost dissuades the purchaser (minimal); (2) the sale is diverted to a neighboring state where the sales tax is lower; or (3) the sale is diverted to a remote seller, such as an Internet or mail order retailer. The amount of such sales decline cannot be precisely estimated; the 1% projection reflects assumptions about the marginal revenue loss attributable to these factors. To the extent that sales decline further than projected, then sales tax revenues would decline correspondingly.

State Expenditures: Changing the highest marginal tax rate and lowering the exemption would require the Comptroller to issue revised withholding schedules in fiscal 2003 and again in fiscal 2005. Printing and mailing new withholding booklets would cost approximately $138,959 in fiscal 2003 and $159,650 in fiscal 2005.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Comptroller's Office, Department of Legislative Services

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