

Department of Legislative Services
 Maryland General Assembly
 2003 Session

FISCAL AND POLICY NOTE

House Bill 936 (The Minority Leader)
 (By Request – Administration)
 Ways and Means

Tax Compliance Act of 2003

This Administration bill imposes various tax compliance requirements.

The bill takes effect July 1, 2003. The provision changing the schedule for remitting withheld payroll taxes is delayed until January 1, 2004.

Fiscal Summary

State Effect: State general fund revenues could increase by approximately \$50.5 million in FY 2004 and by approximately \$62.5 million in FY 2005. To the extent that any of these revenues from compliance efforts reflect corporate income taxes, 24% of these revenues would go to the Transportation Trust Fund (TTF). Future year growth reflects annualization and forecasted growth in the underlying tax revenues, offset by projected diminished returns of some of the compliance efforts. The Comptroller’s administrative expenditures would increase by approximately \$185,000 in FY 2004, decreasing to \$125,000 in FY 2005 and thereafter.

(\$ in millions)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
GF Revenue	\$50.5	\$62.5	\$58.5	\$54.7	\$55.8
GF Expenditure	.2	.1	.1	.1	.1
Net Effect	\$50.3	\$62.4	\$58.4	\$54.5	\$55.7

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

Local Effect: To the extent that State individual income tax collections increase under the compliance provisions, particularly related to license clearance, then local “piggy-back” income taxes would also increase. To the extent that TTF revenues increase, local governments would receive additional revenue sharing for transportation.

Small Business Effect: The Administration has determined that this bill has minimal or no impact on small business (attached). Legislative Services concurs with this assessment.

Analysis

Bill Summary: See discussion under State Revenues.

Current Law: See discussion under State Revenues.

Background: The Commission on Maryland’s Fiscal Structure (Puddester Commission) pointed out several options for increasing tax compliance, including the provisions below related to accelerating withholding payments, permitting direct salary attachment for all tax liabilities, expanding the requirement for tax clearance for licenses, and streamlining the bank attachment process. These options were discussed before the commission when the Comptroller’s Office discussed issues of State tax compliance.

State Revenues: The impact on State revenues from imposing tax compliance requirements is discussed below and illustrated in **Exhibit 1**.

Exhibit 1 Tax Compliance Items

<u>Tax Compliance Items</u>	<u>FY 2004</u>	<u>FY 2005</u>	<u>FY 2006</u>	<u>FY 2007</u>	<u>FY2008</u>
Withhold from proceeds of real estate sales by nonresidents	20.0	20.0	20.0	20.0	20.0
Require remittance of payroll taxes on more frequent schedule	6.5	21.0	22.1	23.2	24.3
Streamline bank attachment process	12.5	10.0	5.0	5.0	5.0
Tax clearance for licenses: expanded scope, requirement for agency verification	10.0	10.0	10.0	5.0	5.0
Permit direct salary attachment for taxes other than income tax	1.5	1.5	1.5	1.5	1.5
Total	50.5	62.5	58.6	54.7	55.8

Require Withholding from Proceeds of Real Estate Sales By Nonresidents

In most cases, a real estate sale by a nonresident involves property that is not the individual's primary residence, meaning the sale may trigger a taxable capital gain that is taxable under Maryland income tax. No Maryland income taxes, however, are currently withheld against this tax liability. Given that the nonresident may not file a Maryland return, and the federal return would not necessarily indicate Maryland taxable income, it is difficult to collect Maryland taxes owed from these transactions. The proposed change requires the purchaser of property owned by a nonresident seller to withhold and transmit to the Comptroller 3% of the total payment. This withholding would be offset against any Maryland taxes owed by the nonresident.

At least three other states – Vermont, Rhode Island, California – currently require withholding of taxes on such sales. Based roughly on their experience, it is estimated that this provision would increase tax collections by approximately \$20 million annually. Local income tax revenues are not affected because nonresidents do not pay local income tax.

Require Withholding Taxes to Be Remitted on More Frequent Schedule

Employers are currently required to remit State withholding tax collections by the fifteenth of the following month, except for quarter-end months, when the due date is the last day of the following month. The federal requirement for remittance of federal income tax withholdings are the same as above for those with less than \$50,000 of annual liability. For those with more than \$50,000 of annual liability (which covers most employers), the due date is semi-weekly (either the Wednesday or Friday following payday). For those with more than \$100,000 of accumulated liability (monthly or semiweekly), the due date is the first banking day after the \$100,000 threshold is reached.

This bill requires Maryland tax withholding by an employer to be remitted within three business days after payroll once \$700 of liability is reached, if total withholding for the prior calendar year was \$15,000 or more. This provision takes effect January 1, 2004. Because \$15,000 of withholding for a calendar year equates to approximately \$250,000 of wages, most businesses will be required to withhold more frequently than under current law. While on average, withholding is currently remitted 35 calendar days after payday, under this provision most employers will be required to remit within three business days after payroll, which for most employers is every two weeks. This more closely approximates the federal schedule and the Comptroller advises that it expects most employers to remit biweekly.

Based on approximately 30 fewer days of employer “float,” an overnight interest rate of 2%, and a State withholding of \$7.9 billion annually, it is estimated that additional interest earnings to the State would be approximately \$13 million annually. Based on the January 1, 2004 effective date of this provision, fiscal 2004 revenues are estimated at \$6.5 million. Reflecting a full year of withholding and assuming that withholding grows by 6.5% and overnight rates increase to 3%, fiscal 2005 revenues are estimated at approximately \$21 million. Future year revenues are projected to grow at 5%; however, actual out-year revenues would depend both on withholding growth and overnight interest rates.

Streamline Bank Attachment Process

This provision streamlines the process by which the Comptroller attaches funds in bank accounts of taxpayers subject to a tax lien. Current law requires a multi-step, individualized condemnation process that requires significant time and expense by the Comptroller. The Comptroller advises that under the proposed streamlining, it would be able to process attachments of tax liens in bulk, thereby increasing the number of such attachments. This process would be similar to that currently employed for child support collections.

The additional revenues from such an increase in attachments cannot be precisely estimated at this time, but is estimated to be approximately \$12.5 million in fiscal 2004 (reflecting the current backlog of attachments). Future year revenues would decline as the backlog of accounts of tax delinquents declines.

Expansion of License Clearance and Requirement for Agency Verification of Tax Clearance

The bill requires that before various licenses or permits may be renewed, the issuing authority must verify through the Comptroller’s Office that the applicant has paid all undisputed taxes and unemployment insurance contributions or that the applicant has provided for payment in a manner satisfactory to the unit responsible for collection. Covered licenses and permits include those governing business occupations and professions, regulated industries, natural resources and environment, health occupations, other licenses granted by the Comptroller, and certain motor vehicle licenses and permits (but not motor vehicle registrations or drivers’ licenses).

This provision extends to individuals who obtain business and professional licenses the requirements currently in place for alcoholic beverage and private investigator licenses, and would strengthen current requirements for those licenses issued by the Department of Labor, Licensing, and Regulation (DLLR). Approximately 170,000 licenses issued by

DLLR are subject to minimal clearance requirements and an additional 30,000 licenses with no current clearance requirements would be affected. The additional revenues from such an increase in attachments cannot be precisely estimated at this time but based on the experience with current clearance programs, it is expected that adding approximately 200,000 or more individuals to the clearance process will result in additional revenue of approximately \$10 million or more annually. This increase could flatten or decline in the out-years, after all licensees have cycled through one renewal. To the extent that additional income taxes are paid, local revenues could also increase.

Permit Direct Salary Attachment for Other Taxes

The Comptroller currently has the authority to directly attach salaries for the individual income tax. This provision would extend that authority to directly attach salaries and wages for all other taxes collected by the Comptroller, such as the sales tax, the admissions and amusement tax, etc. Additional revenues from this action are estimated at \$1.5 million annually.

State Expenditures: The Comptroller's Office will incur one-time and ongoing administrative costs to implement the bill, particularly those provisions related to the accelerated withholding schedule and the license clearance program. The agency will incur approximately \$60,000 in one-time costs for computer reprogramming and communications costs associated with the license clearance program, in order to process the lists of licensees from the various agencies. The Comptroller's Office advises that the accelerated withholding schedule will result in approximately twice as many remittance transactions per year related to the mailing of coupon books and contractor services to process the returned coupons and checks, increasing administrative expenses by approximately \$200,000 per year. Legislative Services notes that this amount should decline over time as more employers remit their withholdings electronically.

Several of the agencies and boards that would be required to coordinate with the Comptroller's Office to ensure tax clearance for the granting of their respective licenses or permits have indicated they would incur significant one-time and ongoing costs to comply with the bill's requirements. For instance, the Motor Vehicle Administration advises that it would incur approximately \$135,000 in one-time programming costs and \$75,000 in additional annual costs to coordinate its license data with the Comptroller's Office. The Department of Health and Mental Hygiene's division of health boards advises that it could incur approximately \$131,000 in annual ongoing costs. The Department of Labor, Licensing, and Regulation, the agency likely to be the most affected by the requirement, advises that it will incur a one-time cost of \$50,000.

Legislative Services advises that the licensing agencies may incur some one-time costs in providing data to the Comptroller's Office in a transferable format, and may also incur some ongoing costs in notifying license and permit applicants that their applications have been denied due to tax delinquency. Legislative Services believes, however, that such additional costs could be absorbed within the agencies' existing budgeted resources.

Additional Information

Prior Introductions: None.

Cross File: SB 656 (The President) (By Request – Administration) – Budget and Taxation.

Information Source(s): Comptroller's Office; Maryland Department of Transportation (Motor Vehicle Administration); Department of Health and Mental Hygiene; Department of Labor, Licensing, and Regulation; Department of Legislative Services

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lc/jr

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