Department of Legislative Services
Maryland General Assembly
2003 Session

FISCAL AND POLICY NOTE

House Bill 19 (Delegate Healey, *et al.*)
Ways and Means

Recordation and Transfer Taxes - Transfers of Controlling Interests

This bill imposes recordation and transfer taxes on the transfer of real property, with a value of $500,000 or more, when the transfer is achieved through the sale of a "controlling" interest in a specified corporation, partnership, limited liability company, limited liability partnership, or other form of unincorporated business. "Controlling" interest is defined as more than 80% of total value of the stock or the interest in capital and profits.

The bill is effective January 1, 2004.

Fiscal Summary

State Effect: Special fund revenues could increase by $4.8 million in FY 2004, reflecting the bill's January 1, 2004 effective date, and general fund expenditures could increase by $50,000. Future year estimates reflect stable tax collections and inflation.

($ in thousands)	FY 2004	FY 2005	FY 2006	FY 2007	FY 2008
SF Revenue	$4,760	$9,465	$9,470	$9,475	$9,485
GF Expenditure	50	84	89	96	102
Net Effect	$4,710	$9,381	$9,381	$9,379	$9,383

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

Local Effect: Local government revenues could increase by $16 million in FY 2004, reflecting the bill's January 1, 2004 effective date. Expenditures would not be affected.

Small Business Effect: Potential meaningful impact.

Analysis

Bill Summary: The bill specifies: (1) that it applies to transfers of controlling interests by entities which have tangible assets of which at least 80% are comprised of real property in Maryland that has an aggregate value of at least $500,000; (2) that certain transfers (e.g., mergers and dissolutions) will be exempt; and (3) a report be filed with the Department of Assessments and Taxation upon the transfer of a controlling interest within 30 days of the final transfer.

The tax is to be imposed on the consideration payable for the transfer of controlling interest in the real property entity reduced by the amount allocable to assets other than the real property. Consideration includes any mortgage, deed of trust, or other lien on the real property directly or beneficially owned by the real property entity and any other debt or encumbrance of the real property entity. The entity has the burden of establishing the consideration related to the real property and if it fails to do so the tax is imposed on the most recent assessed value of the property.

Current Law: Real property can be transferred without payment of transfer and recordation taxes by transferring controlling interest or ownership of the entity if the property is owned by a corporation, limited liability company, or partnership.

The counties and Baltimore City are authorized by law to impose locally established recordation tax rates on any business or person: (1) conveying title to real property; or (2) creating or giving notice of a security interest (i.e., a lien or encumbrance) in real or personal property, by means of an instrument of writing.

The State transfer tax rate is 0.5% of the consideration payable for an instrument of writing conveying title to, or a leasehold interest in, real property (0.25% for first-time Maryland home buyers). A local property transfer tax may be imposed on instruments transferring title to real property. A distinction is made in the local codes between instruments transferring title such as a deed and certain leaseholds and instruments securing real property such as a mortgage. Except in Prince George's County, mortgages are not subject to the tax.

Background: Numerous other jurisdictions in the country currently tax the transfer of the controlling interest in an entity owning real property: California, Connecticut, Delaware, District of Columbia, Illinois, New York, New York City, Pennsylvania, Philadelphia, and Washington.

State transfer tax revenues are special fund revenues dedicated for specific programs and are distributed as follows: 3% of total revenues are earmarked to defray administrative costs and $1 million to cover debt service expenses. The remaining revenues are approximately dedicated to the following: Program Open Space (76%), Agricultural Land Preservation Fund (17%), Heritage Conservation Fund (2%), and Rural Legacy Program (5%). Approximately 50% of Program Open Space revenues are distributed to local Program Open Space programs.

State Revenues: There were 634 sales of single-parcel commercial or industrial property in fiscal 2002 where more than $500,000 was paid that were subject to recordation and transfer taxes. The total consideration for those sales was $1.6 billion. Based on a fiscal 1992 review of transfers of controlling interest, it is estimated that this bill would generate an additional $4.8 million in transfer tax revenues in fiscal 2004 and $9.5 million annually thereafter. The fiscal 2004 estimate reflects the bill's January 1, 2004 effective date.

The Department of Assessments and Taxation recently identified 23 transactions in fiscal 2002 that would have resulted in the following recordation and transfer tax collections if this bill were effective:

Recordation Tax	$2,751,305
State Transfer Tax	$2,736,595
County Transfer Tax	$5,398,915

Out-year revenues would fluctuate depending on the real estate market and the number of transfers. Additionally, the imposition of taxes on these transactions may reduce the number that occurs. The actual increase in revenues depends on the number of transfers of controlling interest in real property entities and the consideration attributable to the real property.

State Expenditures: General fund expenditures by the Department of Assessments and Taxation could increase by approximately $49,728 in fiscal 2004 and by $84,222 in fiscal 2005 for the costs of hiring one charter specialist and one office secretary to assist in the collection of additional recordation and transfer taxes.

Local Revenues: It is estimated that this bill would generate approximately $16 million in fiscal 2004 in additional recordation and transfer taxes and $31.5 million in future years. The estimate for fiscal 2004 reflects the bill's January 1, 2004 effective date.

Small Business Effect: This bill could increase the costs of small businesses purchasing or selling real property through a sale of the controlling interest in a corporation, partnership, limited liability company, or another form of unincorporated business by imposing transfer and recordation taxes on these purchases. The 1998 Survey of U.S.

Business by the U.S. Census Bureau indicated that 92.9% of the firms in Maryland had less than 50 employees.

Additional Information

Prior Introductions: HB 557 of 2002, a nearly identical bill, passed the House but received an unfavorable report from the Senate Budget and Taxation Committee. This bill was introduced as HB 1100 in 1998 which was withdrawn and was also introduced as HB 1069 in 1997 which was not reported on by the Ways and Means Committee.

Cross File: SB 120 (Senator Miller, *et al.*) – Budget and Taxation.

Information Source(s): Department of Assessments and Taxation, Maryland Chamber of Commerce, Montgomery County, Baltimore County, Anne Arundel County, Maryland Association of Counties, Department of Legislative Services

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Analysis by: Karen S. Benton

Direct Inquiries to:
(410) 946-5510
(301) 970-5510