

Department of Legislative Services
Maryland General Assembly
2005 Session

FISCAL AND POLICY NOTE

Senate Bill 724

(Senator Pinsky)

Budget and Taxation

Income Tax Revenues - Distributions to Municipal Corporations

This bill provides that a municipal corporation can meet with the county in which it is located to request that the county distribute additional local income tax revenues to the municipal corporation in the next fiscal year. The bill provides for factors that should be considered in whether or not additional distributions should be made and specifies a process that must be followed in order to alter local income tax revenue distributions. A county cannot increase distributions to a municipality unless the municipality's request is done under the process specified by the bill.

Fiscal Summary

State Effect: To the extent that a municipal corporation and county reach an agreement to increase income tax revenue distributions to a municipal corporation, general fund expenditures would increase by approximately \$15,500 due to computer programming changes at the Comptroller's Office. No effect on revenues.

Local Effect: To the extent an agreement is reached, revenues to a municipal corporation would increase and revenues to the county in which these municipal corporations are located would decrease by a corresponding amount. No effect on expenditures.

Small Business Effect: None.

Analysis

Current Law: After the Comptroller distributes individual income tax revenue to the refund and administrative cost accounts, the Comptroller allocates a certain amount of revenue to an unallocated income tax revenue account. After these distributions are made, the Comptroller distributes income tax revenues to each special taxing district that received a distribution in fiscal 1977 and each municipal corporation based on the State and county income tax liability of the residents of the district or municipal corporation. The distribution is equal to the greater of 17% of the county income tax liability or 0.37% of the State income tax liability of the district or municipal corporation residents. If the county in which the district or corporation is located imposes an income tax rate of less than 2.6%, the amount of the distribution determined previously is multiplied by a numerator which is 2.6% and a denominator which is the county income tax rate. The Comptroller adjusts the distributions to districts and municipal corporations based on the proportionate amount of the prior year's refund and interest payments made after the distribution to a district or municipal corporation for that year.

Background: The income tax is the third largest revenue source for most county governments, accounting for 16.5% of total revenues in fiscal 2003. The reliance on income tax revenues ranges from about 6.5% in Baltimore City and Worcester County to almost 23% in Montgomery County. In Montgomery County, the income tax is the second largest revenue source after property taxes.

Local governments collected \$2.9 billion in local income tax revenues in fiscal 2003. **Exhibit 1** shows the amount of income tax revenue collected by each type of local government.

Exhibit 1 Local Income Tax Revenues Fiscal 2003

	Local Income Tax Revenues	Percent of Total
Counties – With Municipalities	\$2,086,782,549	71.4%
Counties – Without Municipalities	596,849,795	20.4%
Baltimore City	<u>173,466,278</u>	<u>5.9%</u>
Subtotal – Counties and Baltimore City	\$2,857,098,622	97.8%
Municipal Corporations	<u>63,668,950</u>	<u>2.2%</u>
Total	\$2,920,767,572	100.0%

Structure of Local Governments

Counties are the primary unit of local government in Maryland, responsible for most basic services such as police, fire, sanitation, highways, health, libraries, and parks and recreation. In addition, unlike most states, local school systems in Maryland are fiscally dependent on the county government for funding. For most purposes under State law, Baltimore City is considered a county.

Municipalities in Maryland provide a more limited array of public services. Public works and public safety are the two largest functions of municipal governments, comprising 65% of municipal expenditures. There are 156 municipalities in Maryland. Based on 2003 population estimates, approximately 15% of Maryland's population resides within municipalities (excluding Baltimore City). Municipalities in Maryland are relatively small, with 62%, or 97 municipalities, having fewer than 2,500 residents and 5%, or eight municipalities, having more than 25,000 residents. The City of Gaithersburg (Montgomery County) with 57,365 residents is Maryland's largest municipality, followed by the City of Frederick (Frederick County) with 56,128 residents. The Town of Port Tobacco (Charles County) is the smallest with 17 residents.

Local Funding for Public Services

Approximately 96% of local expenditures take place at the county level, with municipalities accounting for only 4% of local expenditures. **Exhibit 2** illustrates the nature and amount of local government expenditures by level of government. Public works activities account for 44% of municipal expenditures, the largest function for most municipalities. A portion of these expenditures, such as water and sewer services, are financed through service charges. Service charges are the largest revenue source for most municipalities, accounting for 31% of municipal revenues. For counties, funding for public schools comprise the largest share of county expenditures, approximately 50% on a statewide basis. Unlike public works activities, public schools cannot be funded through service charges. County governments rely primarily on the property and income taxes to fund the local share of public school costs.

Exhibit 2
Local Government Expenditures
Fiscal 2003
(\$ in Millions)

	<u>Expenditures</u>	<u>Percent of Total</u>
County Level	\$18,264.6	95.8%
Municipal Level	\$792.1	4.2%
Total	\$19,056.7	100.0%

<u>County Level</u>	<u>Expenditures</u>	<u>Percent of Total</u>
Public Schools	\$8,575.5	49.8%
Libraries	202.5	1.2%
Community Colleges	749.7	4.4%
Health Departments	569.8	3.3%
County Governments	<u>7,131.7</u>	<u>41.4%</u>
Subtotal	\$17,229.2	100.0%
Debt Service	<u>1,035.5</u>	
Total	\$18,264.6	

State Expenditures: The Comptroller's Office reports that should an agreement be reached that alters distributions between a county and municipal corporation, it would incur a one-time expense of \$15,500 in programming expenses in order to allow local income tax revenue distributions to vary by municipal corporations.

Additional Information

Prior Introductions: None.

Cross File: None.

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

Fiscal Note History: First Reader - March 13, 2005
ncs/hlb

Analysis by: Robert J. Rehrmann

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