Department of Legislative Services
Maryland General Assembly
2005 Session

FISCAL AND POLICY NOTE

Senate Bill 5 (Senator Green)
Budget and Taxation

Prince George's County - Sales Tax for School Construction and Operating Costs

This bill authorizes the Prince George's County Council to impose a 1% local sales tax in addition to the State's 5% sales tax. Net revenues collected from the local sales tax must be used to provide operating funding for the Prince George's County Board of Education and capital funding for the construction, renovation, and upgrading of public schools, including funding of debt service on bonds. To take effect, the sales tax must first be submitted to a referendum of Prince George's County voters at the November 2006 election.

The bill takes effect July 1, 2005 for the purpose of holding the referendum; if the tax is approved, it would take effect January 1, 2007.

Fiscal Summary

State Effect: If the referendum is approved, and if the local sales tax encourages residents of Prince George' County to make purchases outside the State, sales tax revenues could decrease by approximately $2.1 million in FY 2007 and $4.4 million beginning in FY 2008. Future year revenue decreases reflect growth in taxable sales.

(in dollars)	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
GF Revenue	$0	($2,076,300)	($4,364,300)	($4,586,900)	($4,820,800)
Expenditure	$0	$0	$0	$0	$0
Net Effect	$0	($2,076,300)	($4,364,300)	($4,586,900)	($4,820,800)

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

Local Effect: Assuming approval of the mandated referendum, Prince George's County revenues could increase by an estimated $40.1 million in FY 2007 based on the January 1, 2007 effective date, increasing to $84.3 million in FY 2008. Future year revenues reflect estimated growth in taxable sales.

Small Business Effect: Meaningful impact on small businesses in Prince George's County.

Analysis

Bill Summary: Vendors must file returns with the county on the twenty-first day of each month and shall remit the taxes collected with the return. Vendors are allowed a deduction of 1.5% of the tax collected.

Current Law: State law prohibits local governments from imposing any general retail sales or use taxes, with certain exceptions. These exceptions include taxes that existed before January 1, 1971; sales or use taxes on fuels, utilities, space rentals, and certain controlled dangerous substances; and certain sales or use taxes on food and beverages. The latter permits the Town of Ocean City to levy a 1% sales tax on food and beverages.

The sales and use tax is the State's second largest source of general fund revenues accounting for approximately $3.2 billion in fiscal 2006. The Maryland sales and use tax rate is currently set at 5.0%.

Background: The State currently participates in the Streamlined Sales Tax Project, a multistate effort to harmonize state sales tax structures and thereby overcome the administrative and legal hurdles of collecting sales taxes on remote transactions, such as sales from catalogs and the Internet. One significant obstacle to the harmonization effort has been local sales taxes. As noted above, Maryland has relatively few local sales taxes, while some other states have extensive local sales tax structures.

State Revenues: To the extent that Prince George's County residents make out-of-state purchases to avoid the local sales tax, then State sales tax revenue will also decline. If 1% of county sales are diverted out-of-state, State sales tax revenues could decline by $2.1 million in fiscal 2007 (reflecting the January 1, 2007 effective date) and $4.4 million annually beginning in fiscal 2008, as shown in **Exhibit 1**.

Local Revenues: Prince George's County revenues could increase by $40.1 million in fiscal 2007 as a result of imposing a 1% county sales tax. This estimate reflects projected sales tax growth and a 2% decline in taxable sales due to the higher sales tax. **Exhibit 1** shows increased sales tax revenues for fiscal 2007 through 2011. The estimate is based on the following:

- estimation of reported State sales tax collections attributable to Prince George's County of $353.8 million in fiscal 2004;

- adjustment for the State sales tax vendor credit;
- projection of sales tax growth from 2006 to 2011 based on statewide estimates by the Bureau of Revenue Estimates; and
- assumption that 1% of sales in the county will be diverted to other Maryland counties and that an additional 1% of county sales will be diverted out of the State altogether due to the higher tax rate.

Exhibit 1
Estimated County and State Revenue Effect of SB 5
($ in Millions)

	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
Estimated Net Sales Tax Collections	$415.3	$436.4	$458.7	$482.1	$506.7
Implied Taxable Sales	8,305.00	8,728.56	9,173.71	9,641.57	10,133.29
Implied Taxable Sales with 1% Decline	8,221.95	8,641.27	9,081.98	9,545.16	10,031.96
State Sales Tax Revenues at 5%	411.10	432.06	454.10	477.26	501.60
Potential State Revenue Decrease	**($2.1)**	**($4.4)**	**($4.6)**	**($4.8)**	**($5.1)**
Prince George's County Impact					
Implied Taxable Sales with 2% Decline	$8,138.90	$8,553.99	$8,990.24	$9,448.74	$9,930.63
County Sales Tax Revenues at 1%	40.7	85.5	89.9	94.5	99.3
County Net Revenues after Vendor Credit	**$40.1**	**$84.3**	**$88.6**	**$93.1**	**$97.8**

The 2% decline in taxable sales (1% county and 1% State) used in the estimate reflects sales that no longer are subject to the State or local sales tax for three reasons: (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 or county where the sales tax rate is lower; or (3) the sale is diverted to a remote seller, such as an Internet or mail order retailer. To the extent that sales decline more or less than projected as a result of the tax increase, sales tax revenues would change correspondingly.

Due to the method by which the Comptroller apportions sales tax revenues to the counties, the county's actual collections could differ significantly from the estimate above. Legislative Services advises, however, that there is no alternative, more accurate measure of retail sales taking place in the county. Also, to the extent that avoidance of the additional sales tax is greater than estimated, particularly for "big ticket" purchases, then realized revenues may be lower than estimated.

Small Business Effect: For retail establishments in Prince George's County, there will be additional initial costs associated with reprogramming cash registers and ongoing administrative costs from remitting the tax collections. In most cases, these costs will be offset by the vendor commission. For retail establishments that lose sales to other jurisdictions because of the tax, the vendor commission may not offset the lost revenue.

Additional Information

Prior Introductions: This bill was introduced as SB 38 in the 2003 session. No action was taken by the Senate Budget and Taxation Committee. Similar bills were introduced at the 2001 and 2002 sessions. SB 120 of 2001 received an unfavorable report from the Senate Budget and Taxation Committee. SB 777 of 2002 was not reported from the Senate Budget and Taxation Committee.

Cross File: None.

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

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mp/hlb

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