SB 56

Department of Legislative Services

Maryland General Assembly
2005 Session

FISCAL AND POLICY NOTE

Senate Bill 56 (Senator Currie)
Budget and Taxation

Income Tax - Nonresidents - Withholding from Payments and Taxation of Pass-Through Income

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This bill: (1) increases withholding tax rates by including the lowest county income tax imposed on nonresident income derived from real estate sales and gambling winnings; the rate increases from 4.75% to 6%; and (2) increases the pass-through entity (PTE) tax imposed on nonresident partnerships, Limited Liability Corporations (LLCs), and S corporations by including the lowest county income tax rate imposed, increasing the tax from 4.75% to 6%.

The bill takes effect July 1, 2005 and applies to tax year 2005 and beyond.

Fiscal Summary

State Effect: General fund revenues could increase by approximately $14.2 million in FY 2006, due to increased PTE taxes and withholdings on nonresident income derived from real estate sales and gambling winnings. Future years reflect estimated amount of tax compliance from increased withholdings and estimated increase in PTE taxes.

($ in millions)	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
GF Revenue	$14.2	$5.6	$5.8	$6.0	$6.2
Expenditure	$0	$0	$0	$0	$0
Net Effect	$14.2	$5.6	$5.8	$6.0	$6.2

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

Local Effect: None.

Small Business Effect: Minimal.

Analysis

Current Law:

Withholding Tax Rates

Withholding tax rates are: (1) 4.75% for nonresident income derived from real estate sales and gambling winnings. Nonresident entity income derived from real estate sales is withheld at 7%.

Pass-through Entity (PTE) Tax on Nonresidents

A tax of 4.75% is applied to the sum of each nonresident's share of income of a partnership, LLC, and S Corporation. The tax is assessed on the proportion of income attributable to: (1) a partnership's and LLC's nonresident distributive share; and (2) an S corporation's nonresident shareholder pro rata share.

The lowest county income tax rate currently imposed is 1.25% (Worcester County).

State Revenues: The bill increases specified withholdings beginning on July 1, 2005 and increases the nonresident PTE tax beginning with tax year 2005. As a result, general fund revenues would increase by approximately $14.2 million in fiscal 2006 and $5.6 million in fiscal 2007 and increase by approximately 4% annually thereafter. The fiscal impact of each of the provisions of the bill is discussed separately below.

Increase Withholding on Nonresident Real Estate Sales

Increase in General Fund Revenues
($ in Millions)

FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
$7.5	$3.3	$3.5	$3.7	$3.9

This estimate is based on the following facts and assumptions: (1) in calendar 2004, approximately $41.7 million was collected in withholdings from nonresident realty sales; (2) the value of nonresident real estate sales increases by 5% annually from 2004 through 2010; and (3) 25% of affected individuals do not file a tax return and represent additional income to the State. Fiscal 2006 revenue increases reflect the additional impact of six months of withholding for tax year 2006 and increased tax compliance from one-half of tax year 2005 and one-half of tax year 2006. Future year revenues reflect estimated increase in revenues due to tax compliance. Legislative Services advises that the estimated compliance rate is based on limited data available for amounts withheld in tax year 2003.

Increasing the PTE Tax on Nonresidents

Increase in General Fund Revenues
($ in Millions)

FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
$6.2	$2.1	$2.2	$2.2	$2.3

General fund revenues would increase by $6.2 million in fiscal 2006, which represents the impact of one and one-half tax years. Future fiscal years reflect the impact of one-half of prior tax year and one-half of current tax year. This estimate is based on the following facts and assumptions: (1) PTE tax revenues totaled approximately $38 million in tax year 2003; (2) the amount is estimated to increase 2% annually from 2004 through 2010; and (3) 20% of the amount paid is not otherwise filed for on a Maryland tax return.

Increase Withholding of Nonresident Gambling Winnings

Increase in General Fund Revenues

FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
$521,500	$87,300	$89,900	$92,500	$95,300

State revenues would increase by $520,000 in fiscal 2006 due to increased withholdings on nonresident wagering winnings. Fiscal 2006 increases reflect the additional impact of six months of withholding for taxes in 2006 that are not refunded until the following fiscal year and the estimated revenue gain from individuals who will not file Maryland taxes in one-half of tax year 2005 and one-half of tax year 2006. This estimate is based on the following facts and assumptions: (1) according to the State Lottery Agency, $18.4 million was withheld from all State Lottery winnings in fiscal 2004; (2) according to the Comptroller's Office, approximately $400,000 was withheld in fiscal 2004 from all horseracing winnings; (3) nonresidents comprise 17% of all individuals affected; (4) the amount of horseracing winnings remains constant and lottery winnings increase by 3% annually; and (5) 10% of the money withheld from nonresidents is not filed on a tax return.

Additional Information

Prior Introductions: None.

Cross File: HB 202 (Delegate Hixson, *et al.*) – Ways and Means.

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

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