

Department of Legislative Services
Maryland General Assembly
2006 Session

FISCAL AND POLICY NOTE

Senate Bill 576 (Senator Ruben, *et al.*)
Budget and Taxation

**Alcoholic Beverage Tax - Special Fund for Geographic Cost of Education Index
Adjustment**

This bill increases the State tax rates for alcoholic beverages from \$1.50 to \$4.50 per gallon for distilled spirits (from 39.63 cents to \$1.19 for each liter), from 40 cents to \$1.20 per gallon for wine (from 10.57 cents to 31.71 cents for each liter), and from 9 cents to 27 cents per gallon for beer (from 2.3778 cents to 7.1334 cents for each liter). For distilled spirits that contain alcohol greater than 100 proof, the additional tax is raised from 1.5 cents to 4.5 cents per gallon for each proof over 100 proof.

The bill requires that 100% of the additional alcoholic beverage taxes resulting from the tax increase be distributed to a special fund for the purpose of funding the Geographic Cost of Education Index (GCEI).

The bill takes effect July 1, 2006.

Fiscal Summary

State Effect: Special fund revenues could increase by approximately \$53.0 million in FY 2007, and special fund expenditures would increase by a corresponding amount to provide funding for the GCEI. Future year revenues and expenditures increase by 1.78% annually.

(\$ in millions)	FY 2007	FY 2008	FY 2009	FY 2010	FY 2011
SF Revenue	\$53.0	\$54.0	\$54.9	\$55.9	\$56.9
SF Expenditure	53.0	54.0	54.9	55.9	56.9
Net Effect	\$0	\$0	\$0	\$0	\$0

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

Local Effect: State aid to 13 local school systems would increase by an estimated \$53.0 million in FY 2007. Future year funding reflects increased alcoholic beverage tax collections.

Small Business Effect: Potential meaningful.

Analysis

Current Law: State tax rates for alcoholic beverages in Maryland are \$1.50 per gallon for distilled spirits, 40 cents per gallon for wine, and 9 cents per gallon for beer.

Background: Compared to other states, Maryland has relatively low tax rates on alcoholic beverages, and these rates have not changed in recent years. The tax on distilled spirits has not increased since 1955, and the tax on beer and wine was last increased in 1972. **Exhibit 1** shows alcoholic beverage tax rates in all 50 states and the District of Columbia, as of January 1, 2006.

Exhibit 1 Alcoholic Beverage Taxes by State, as of January 2006

<u>State</u>	<u>Distilled Spirits¹</u> <u>(\$ per Gallon)</u>	<u>Wine²</u> <u>(\$ per Gallon)</u>	<u>Beer³</u> <u>(\$ per Gallon)</u>
Alabama	*	\$1.70	\$.53
Alaska	\$12.80	2.50	1.07
Arizona	3.00	.84	.16
Arkansas	2.50	.75	.23
California	3.30	.20	.20
Colorado	2.28	.32	.08
Connecticut	4.50	.60	.19
Delaware	5.46	.97	.16
Florida	6.50	2.25	.48
Georgia	3.79	1.51	.48
Hawaii	5.98	1.38	.93
Idaho	*	.45	.15
Illinois	4.50	.73	.185
Indiana	2.68	.47	.115
Iowa	*	1.75	.19
Kansas	2.50	.30	.18
Kentucky	1.92	.50	.08
Louisiana	2.50	.11	.32
Maine	*	.60	.35
Maryland	1.50	.40	.09

<u>State</u>	<u>Distilled Spirits¹</u> <u>(\$ per Gallon)</u>	<u>Wine²</u> <u>(\$ per Gallon)</u>	<u>Beer³</u> <u>(\$ per Gallon)</u>
Massachusetts	4.05	.55	.11
Michigan	*	.51	.20
Minnesota	5.03	.30	.15
Mississippi	*	.35	.43
Missouri	2.00	.30	.06
Montana	*	1.06	.14
Nebraska	3.75	.95	.31
Nevada	3.60	.70	.16
New Hampshire	*	**	.30
New Jersey	4.40	.70	.12
New Mexico	6.06	1.70	.41
New York	6.44	.19	.11
North Carolina	*	.79	.53
North Dakota	2.50	.50	.16
Ohio	*	.30	.18
Oklahoma	5.56	.72	.40
Oregon	*	.67	.08
Pennsylvania	*	**	.08
Rhode Island	3.75	.60	.10
South Carolina	2.72	.90	.77
South Dakota	3.93	.93	.28
Tennessee	4.40	1.21	.14
Texas	2.40	.20	.19
Utah	*	**	.41
Vermont	*	.55	.265
Virginia	*	1.51	.26
Washington	*	.87	.261
West Virginia	*	1.00	.18
Wisconsin	3.25	.25	.06
Wyoming	*	**	.02
District of Columbia	1.50	.30	.09
U.S. Median	3.75	.69	\$.188

¹22 states and DC have different rates for products with certain percentages of alcohol and/or other sales/excise taxes.

²37 states have different rates for products with certain percentages of alcohol and/or other sales/excise taxes.

³23 states have different rates for products with certain percentages of alcohol and/or other sales/excise taxes.

*In 18 states, the government directly controls the sales of distilled spirits. Revenue in these states is generated from various taxes, fees, and net liquor sales.

**All wine sales are through state stores. Revenue in these states are generated from various taxes, fees, and net profits.

Source: Federation of Tax Administrators

Geographic Cost of Education Index

One of the recommendations of the Commission on Education Finance, Equity, and Excellence (Thornton Commission) was to adjust State aid to reflect regional differences in the cost of education that are outside the control of local jurisdictions. The Thornton Commission defined adequate funding as revenues sufficient to acquire the resources needed to reasonably expect that students can meet the State's academic performance standards. Because the cost of these resources may vary by jurisdiction, the Thornton Commission recommended that State aid be adjusted to account for the variations. However, the commission did not believe that an acceptable GCEI existed at the time it was completing its work. The commission recommended that the Maryland State Department of Education (MSDE) contract with a private consultant to develop a Maryland-specific index to be used to adjust State aid beginning in fiscal 2005. This recommendation was codified in the Bridge to Excellence in Public Schools Act of 2002.

The consultants hired by MSDE submitted a final report entitled *Adjusting for Regional Differences in the Cost of Educational Provision in Maryland* on December 31, 2003. The report includes a GCEI with index values that range from 0.948 in Garrett County to 1.048 in Prince George's County. **Exhibit 2** shows the index that appears in the report. The index was used to establish a discretionary GCEI adjustment formula that was set in statute in 2004. The formula increases aid for counties with above average costs (*i.e.*, GCEI values greater than 1.0) but does not reduce aid for counties that have below average costs (*i.e.*, GCEI values less than 1.0). Funding for the GCEI formula was not provided in fiscal 2006 and is not included in the proposed fiscal 2007 State budget.

Exhibit 2
Geographic Cost of Education Index

<u>School System</u>	<u>GCEI Value</u>	<u>School System</u>	<u>GCEI Value</u>
Allegany	0.959	Harford	0.992
Anne Arundel	1.018	Howard	1.015
Baltimore City	1.042	Kent	1.010
Baltimore	1.008	Montgomery	1.034
Calvert	1.021	Prince George's	1.048
Caroline	1.000	Queen Anne's	1.011
Carroll	1.014	St. Mary's	1.002
Cecil	0.989	Somerset	0.973
Charles	1.020	Talbot	0.991
Dorchester	0.978	Washington	0.974
Frederick	1.024	Wicomico	0.971
Garrett	0.948	Worcester	0.959

Source: *Adjusting for Regional Differences in the Cost of Educational Provision in Maryland*

State Revenues: As a result of the tax increases on alcoholic beverages, special fund revenues would increase by approximately \$53.0 million in fiscal 2007 based on the following facts and assumptions:

- 105.6 million gallons of beer are projected to be purchased in Maryland in fiscal 2007; due to the tax increase, sales could decrease by 0.76%.
- 12.5 million gallons of wine are projected to be purchased in Maryland in fiscal 2007; due to the tax increase, sales could decrease by 1.6%.
- 9.1 million gallons of distilled spirits are projected to be purchased in Maryland in fiscal 2007, including distilled spirits of over 100 proof; due to the tax increase, sales could decrease by 7.2%.

Future year revenues are expected to increase by approximately 1.78% annually, per the forecast of the Board of Revenue Estimates.

To the extent that the tax increases proposed by the bill result in a higher incidence of cross-border sales activity than is accounted for in the estimate, revenues would in turn

be lower than estimated. This would most likely apply to the sale of distilled spirits, since it is the most price sensitive.

State Expenditures: The bill requires the revenue generated from the tax increase to be used to provide funding for the GCEI. **Exhibit 3** shows the funding formula for the GCEI. The funding would be distributed to local school systems in accordance with the GCEI formula, which provides additional education aid to 13 of the 24 local school systems.

Exhibit 3
GCEI Formula Funding
Fiscal 2007 to 2011
(\$ in Thousands)

<u>School System</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>	<u>FY 2011</u>
Phase-in Percent	62%	74%	86%	100%	100%
Anne Arundel	\$4,770	\$6,226	\$7,386	\$8,776	\$8,980
Baltimore City	12,918	16,574	19,324	22,418	22,378
Baltimore	3,028	3,941	4,668	5,522	5,627
Calvert	1,311	1,751	2,103	2,513	2,579
Carroll	1,474	1,931	2,306	2,743	2,807
Charles	1,872	2,486	2,993	3,605	3,727
Frederick	3,420	4,539	5,481	6,587	6,816
Howard	2,630	3,465	4,170	4,985	5,115
Kent	84	108	124	142	141
Montgomery	16,992	22,320	26,725	31,909	32,901
Prince George's	22,461	29,441	35,060	41,351	42,003
Queen Anne's	298	391	473	570	588
St. Mary's	<u>116</u>	<u>153</u>	<u>184</u>	<u>220</u>	<u>228</u>
Total	\$71,374	\$93,327	\$110,997	\$131,341	\$133,891

However, because the amount of revenue generated by the alcoholic beverage tax increase is less than required by the formula, the formula was recalculated to show the distribution of revenues resulting from the alcoholic beverage tax increase, as shown in **Exhibit 4**.

Exhibit 4
GCEI Formula Funding from Alcoholic Beverage Tax Increase
Fiscal 2007 to 2011

<u>School System</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>	<u>FY 2011</u>
Anne Arundel	\$3,543,665	\$3,600,574	\$3,655,458	\$3,735,773	\$3,816,547
Baltimore City	9,597,470	9,584,840	9,563,097	9,542,835	9,510,534
Baltimore	2,249,415	2,279,025	2,310,036	2,350,543	2,391,472
Calvert	973,822	1,012,422	1,040,546	1,069,533	1,095,917
Carroll	1,094,886	1,116,846	1,141,209	1,167,524	1,193,044
Charles	1,391,048	1,437,819	1,481,029	1,534,429	1,583,910
Frederick	2,540,607	2,625,106	2,712,420	2,804,064	2,897,000
Howard	1,953,926	2,003,961	2,063,889	2,122,110	2,174,023
Kent	62,778	62,426	61,468	60,341	60,016
Montgomery	12,623,854	12,907,538	13,225,840	13,582,856	13,983,231
Prince George's	16,687,097	17,025,556	17,351,011	17,602,470	17,851,594
Queen Anne's	221,575	226,020	233,967	242,688	249,918
St. Mary's	<u>86,477</u>	<u>88,362</u>	<u>91,201</u>	<u>93,779</u>	<u>96,917</u>
Total	\$53,026,622	\$53,970,496	\$54,931,170	\$55,908,945	\$56,904,124

Any expenditure associated with printing new tax forms and postage is assumed to be minimal and could be absorbed within existing budgeted resources.

Local Revenues: State aid to 13 local school systems would increase by an estimated \$53.0 million in fiscal 2007. Future year funding reflects increased alcoholic beverage tax collections as shown in Exhibit 4.

Small Business Effect: The alcoholic beverage tax increase will result in a decline in sales for all retailers and wholesalers of alcoholic beverages. Those businesses located near the State's borders, particularly those in Montgomery and Prince George's counties, could be more adversely affected as customers in those areas could cross the border with the District of Columbia to purchase alcoholic beverages, where the taxes will be considerably lower. Also, small businesses that import beer into the State would be required to prepay the tax.

Additional Information

Prior Introductions: Similar bills that increased the tax on alcoholic beverages were introduced as SB 557 in 2005, SB 527 in 2004, and SB 384 in 2003. No action was taken by the Senate Budget and Taxation Committee on any of the bills.

Cross File: None.

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

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