Department of Legislative Services

Maryland General Assembly
2007 Special Session

FISCAL AND POLICY NOTE

Senate Bill 14 (Senator Rosapepe)
Budget and Taxation

Reduction of Tax Evasion

This bill imposes various tax compliance requirements.

The bill takes effect January 1, 2008.

Fiscal Summary

State Effect: General fund revenues could increase by approximately $45.1 million in FY 2008. Future years reflect annualization and estimated revenue gains from tax changes and compliance measures. Transportation Trust Fund revenues could increase by $6.2 million in FY 2009 and by $4.9 million annually beginning in FY 2010.

($ in millions)	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
GF Revenue	$45.1	$113.9	$107.7	$105.7	$103.3
SF Revenue	0	6.2	4.9	4.9	4.8
Expenditure	$0	$0	$0	$0	$0
Net Effect	$45.1	$120.1	$112.6	$110.6	$108.1

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

Local Effect: Local highway user revenues could increase by $1.9 million in FY 2009 and by $1.5 million annually beginning in FY 2010. Local income tax revenues could increase beginning in FY 2009 due to the increased tax compliance measures in the bill. Expenditures would not be affected.

Small Business Effect: Minimal.

Analysis

Bill Summary: See discussion under State Revenues.

State Revenues: The impact on State revenues from imposing tax compliance requirements is discussed below and illustrated in **Exhibit 1**.

Exhibit 1
Tax Compliance Items
($ in Millions)

Tax Compliance Items	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
Banks – DHC addback	$0.0	$25.8	$20.5	$20.5	$20.0
Withhold from proceeds of real estate sales by residents	18.0	37.0	37.0	37.0	37.0
Repeal sales tax on cigarettes/ Increase cigarette tax	24.2	45.3	43.1	41.1	39.1
Mandated use tax return	0.0	1.0	1.0	1.0	1.0
Federal vendor offset	0.4	1.0	1.0	1.0	1.0
Tax clearance – vehicle registration	2.5	10.0	10.0	10.0	10.0
Tax clearance – bar admission	*	*	*	*	*
Total	**$45.1**	**$120.1**	**$112.6**	**$110.6**	**$108.1**

*Revenue assumed to be minimal.
Source: Comptroller's Office, Department of Legislative Services

Include Banks in Delaware Holding Company Addback

The bill repeals an exception for banks from income tax provisions requiring corporations to add back to federal taxable income any otherwise deductible interest expense or intangible expense paid directly or indirectly to one or more related members, except under certain circumstances.

The current addition modification for holding companies has generated about $45 million in net tax revenue for both tax years 2004 and 2005. Of the revenues received from the 2004 holding company settlement, the majority was from retailers, although revenue was received from manufacturers, service companies and others.

An analysis of the relative growth in intangible assets in Delaware and Maryland commercial banks indicates that over $330 million of income from Maryland operations could be sheltered in Delaware. Therefore the addback would generate approximately roughly $20 million annually.

Require Withholding from Proceeds of Real Estate Sales by Residents

The bill requires a resident to pay an amount equal to 4.75% of the amount by which the total payment in the sale or exchange of real property and associated tangible personal property exceeds $250,000 (or $500,000 for married couples filing a joint income tax return) before the deed or other instrument of writing may be recorded.

A similar requirement is imposed on the sale of property by nonresidents. Based on an estimate provided by the Comptroller's Office, this provision is expected to increase general fund revenues by approximately $37.0 million annually.

Repeal Sales and Use Tax on Sale of Cigarettes and Increase Cigarette Tax

The bill provides that the sales and use tax does not apply to the sale of cigarettes on which the tobacco tax is paid. The bill increases the tax on cigarettes from $1.00 per pack to $1.44 per pack (20 or more cigarettes). The net effect will be the increased revenue from the tobacco tax increase, minus the loss in sales tax, plus any revenue increase from additional compliance. General fund revenues would increase by $24.2 million in fiscal 2008 and $45.3 million in fiscal 2009. Revenue increases would decrease slightly thereafter.

The estimated increase in tobacco tax revenues is based on the estimated price elasticity of tax-paid cigarettes in the State. The estimated gain in compliance is based on the Minnesota Department of Revenue's estimated compliance revenue after that state eliminated the retail sales tax on cigarettes and imposed a wholesale level tax, adjusted for the relative sales tax rate and cigarette sales in Maryland.

Mandated Use Tax Return

The bill requires an employer who is required to file an annual income tax withholding return to file a sales and use tax return at least annually, even if the employer is not a licensed vendor under the sales and use tax.

The sales tax return has a line for use taxes owed, but many businesses that may owe use tax are not required to file a sales tax return. Adding a use tax requirement for employers who do not have a sales tax license would result in some revenues from voluntary compliance and would give the Comptroller the authority to levy an assessment if a return is not filed. It is expected that general fund revenues would increase by $1 million annually with this requirement.

Federal Vendor Offset

The bill adds salaries, wages, and pension income to provisions authorizing the Comptroller to enter into reciprocal agreements with the federal government for interception of tax refunds and vendor payments for collection of delinquent liabilities.

The federal vendor offset program permits reciprocal offsets between Maryland and the federal government. Including State employees salaries and pensions to be offset would allow federal salaries and pensions to be run through the federal offset for Maryland liabilities, increasing general fund revenues by an estimated $1 million annually.

Tax Clearance – Vehicle Registration

The bill adds motor vehicle registrations to the various licenses or permits that are subject to "tax clearance" verification through the Comptroller's Office prior to renewal. Covered licenses and permits under current law include those governing business occupations and professions, regulated industries, natural resources and environment, health occupations, other licenses granted by the Comptroller, and certain motor vehicle licenses and permits.

Adding motor vehicle registrations to the tax clearance program would bring many more taxpayers under the existing program and could provide a substantial increase in revenues. Based on an estimate provided by the Comptroller's Office, it is estimated that revenues would increase by as much as $10 million annually. Assuming a 25% start-up delay due to the bill's January 1, 2008 effective date would result in $2.5 million increase in fiscal 2008.

Tax Clearance – Admission to the Bar

The bill adds admission to the bar to the various licenses or permits that are subject to "tax clearance" verification through the Comptroller's Office prior to renewal.

Attorneys are one of the last occupations regulated by the State that are not included under the tax clearance program. The bill requires the clearance before admission to the bar, however, which is at a time when many individuals may not have substantial outstanding liability with the State. In addition, revenues collected from these individuals might have been collected from an existing State compliance measure, or the other compliance measures contained in this bill. The revenue increase from this provision is therefore expected to be minimal.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Comptroller's Office; Department of Labor, Licensing, and Regulation; Department of Legislative Services

Fiscal Note History: First Reader - November 1, 2007
mll/hlb

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