

Department of Legislative Services
 Maryland General Assembly
 2012 Session

FISCAL AND POLICY NOTE

House Bill 836
 Ways and Means

(Delegate Healey, *et al.*)

Income Tax - Repeal of the 1997 Tax Reduction

This bill increases specified State income tax rates by 0.25% and specified State income tax withholding rates. The bill also increases from 3.2% to 3.325%, the maximum local income tax rate a county is authorized to impose.

The bill takes effect July 1, 2012, and applies to tax year 2012 and beyond.

Fiscal Summary

State Effect: General fund revenues increase by \$527.7 million due to the income tax rates specified by the bill, reflecting revenues from one and one-half tax years. Future year estimates reflect annualization and the current income tax revenue forecast. Minimal general fund expenditure increase in FY 2013 due to implementation costs at the Comptroller’s Office.

(\$ in millions)	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
GF Revenue	\$527.7	\$375.0	\$393.5	\$413.5	\$432.9
GF Expenditure	-	\$0	\$0	\$0	\$0
Net Effect	\$527.7	\$375.0	\$393.5	\$413.5	\$432.9

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

Local Effect: Potential increase in local income tax revenues beginning in FY 2013 for counties that opt to impose additional local income taxes.

Small Business Effect: Meaningful.

Analysis

Current Law/Bill Summary:

State Income Tax

Exhibit 1 and **Exhibit 2** show the State income tax rates under current law and as proposed by the bill.

Exhibit 1 Maryland State Income Tax Rates Current Law

Single, Dependent Filer, Married Filing Separate		Joint, Head of Household, Widower	
<u>Rate</u>	<u>Maryland Taxable Income</u>	<u>Rate</u>	<u>Maryland Taxable Income</u>
2.00%	\$1-\$1,000	2.00%	\$1-\$1,000
3.00%	\$1,001-\$2,000	3.00%	\$1,001-\$2,000
4.00%	\$2,001-\$3,000	4.00%	\$2,001-\$3,000
4.75%	\$3,001-\$150,000	4.75%	\$3,001-\$200,000
5.00%	\$150,001-\$300,000	5.00%	\$200,001-\$350,000
5.25%	\$300,001-\$500,000	5.25%	\$350,001-\$500,000
5.50%	Excess of \$500,000	5.50%	Excess of \$500,000

Exhibit 2 Maryland State Income Tax Rates Proposed

Single, Dependent Filer, Married Filing Separate		Joint, Head of Household, Widower	
<u>Rate</u>	<u>Maryland Taxable Income</u>	<u>Rate</u>	<u>Maryland Taxable Income</u>
2.00%	\$1-\$1,000	2.00%	\$1-\$1,000
3.00%	\$1,001-\$2,000	3.00%	\$1,001-\$2,000
4.00%	\$2,001-\$3,000	4.00%	\$2,001-\$3,000
5.00%	\$3,001-\$150,000	5.00%	\$3,001-\$200,000
5.25%	\$150,001-\$300,000	5.25%	\$200,001-\$350,000
5.50%	\$300,001-\$500,000	5.50%	\$350,001-\$500,000
5.75%	Excess of \$500,000	5.75%	Excess of \$500,000

County Income Tax

The counties and Baltimore City are required to levy a local income tax on their residents. The tax is assessed as a percentage of the taxpayer's Maryland taxable income. Counties are authorized to set a local income tax rate of at least 1% but not more than 3.2%. The tax rate is a flat rate, as counties are not authorized to impose the tax at different tax rates. Generally, each incorporated municipality shares in its county's income taxes by receiving a portion of the county income taxes paid by the municipality's residents.

A county may not increase its income tax rate by an act, ordinance, or resolution above 2.6% until the county has held a public hearing. If a county alters its county income tax rate, the county must (1) alter the tax rate in increments of one-hundredth of a percentage point, effective January 1 of the year the county designates; and (2) provide notice of the change by July 1 prior to its effective date.

The Comptroller's expenses that are necessary to administer the income tax are paid by distributions from State and local income tax revenues. These costs include the amount necessary to administer the local income tax.

Background:

State Income Tax

Chapter 4 of 1997 (the 1997 Tax Reduction Act) was designed to provide a 10% reduction in State income taxes. This reduction began in tax year 1998 and was originally to be phased in over five years. Better than anticipated revenue growth enabled the General Assembly to enact Chapter 4 of 1998, which accelerated the income tax reduction for tax years 1998 and 1999. The Acts reduced the top marginal State income tax rate from 5.0% to 4.75% and increased the regular personal exemption from \$1,200 to \$2,400, as illustrated in **Exhibit 3**.

Exhibit 3 **Phased-in Personal Income Tax Reduction** **as Enacted by Chapter 4 of 1997 and Chapter 4 of 1998**

	<u>Previous</u> <u>Law</u>	<u>1998</u>	<u>1999</u>	<u>2000</u>	<u>2001</u>	<u>2002 and</u> <u>Beyond</u>
Top marginal income tax rate	5.0%	4.875%	4.85%	4.85%	4.80%	4.75%
Regular personal exemption	\$1,200	\$1,750	\$1,850	\$1,850	\$2,100	\$2,400

Source: Department of Legislative Services

Chapter 3 of the 2007 special session (1) established new State income tax rate brackets of up to 5.5%; and (2) increased the regular personal exemption to \$3,200 for single filers with FAGI of \$100,000 or less (\$150,000 or less for joint filers), but gradually reduced the value of the exemption to \$600. Chapter 10 of 2008 established an income tax rate of 6.25% on net taxable income in excess of \$1 million for tax years 2008 through 2010.

County Income Tax

During the 1999 session, the General Assembly passed legislation (Chapter 493) that altered the method of calculating local income taxes from a percentage of State tax liability to a flat county income tax rate applied to net taxable income. The legislation specified each county’s local income tax rate for calendar 1999 through 2002; however, the county tax rate after calendar 1999 could be altered by a county through an ordinance or resolution. Pursuant to the legislation, county income tax rates may range between 1% and 3.2%.

Over the last five years, local income tax rates have remained relatively stable. Five local jurisdictions – Baltimore City and Howard, Montgomery, Prince George’s, and Queen Anne’s counties – are imposing the maximum income tax rate of 3.2% in tax year 2012. Worcester County has the lowest local income tax rate at 1.25%. The typical local income tax rate imposed for tax year 2012 is 2.9%.

State Revenues: The bill increases specified income tax rates beginning in tax year 2012, with general fund revenues increasing by \$352.0 million in tax year 2012 and by \$365.6 million in tax year 2013. As a result, fiscal 2013 revenues increase by \$527.7 million, reflecting the change in tax year 2012 and a little less than one-half of the change in tax year 2013. **Exhibit 4** shows the fiscal impact of the bill in fiscal 2013 through 2017.

Exhibit 4
HB 836 Fiscal Impact
(\$ in Millions)

<u>FY 2013</u>	<u>FY 2014</u>	<u>FY 2015</u>	<u>FY 2016</u>	<u>FY 2017</u>
\$527.7	\$375.0	\$393.5	\$413.5	\$432.9

Local Revenues: Local income tax revenues will increase beginning in fiscal 2013 in counties that opt to impose additional local income taxes as authorized by the bill. **Exhibit 5** shows the potential additional revenue yield from imposing a 3.325% county income tax rate (over the amount of revenues generated from the current county income tax rate).

Small Business Effect: Small businesses that are partnerships, S corporations, limited liability companies, and sole proprietorships would be meaningfully impacted by the bill. Any of these small businesses with higher amounts of taxable income would be negatively impacted through increased income tax liabilities. An unknown number of impacted businesses would be small businesses.

Additional Information

Prior Introductions: None.

Cross File: None.

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

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ncs/jrb

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Exhibit 5
Additional Local Revenue Yield from Imposing a 3.325% County Income Tax Rate
Fiscal 2012 – Projected Revenues

County	Population	County Income Tax Revenues	County Income Tax Rate	Potential Rate Increase	Additional Revenue Yield	Per Capita Amount
Allegany	75,087	\$23,000,000	3.05%	0.28%	\$2,073,800	\$27.62
Anne Arundel	537,656	366,588,200	2.49%	0.84%	122,932,200	228.64
Baltimore City	620,961	243,612,000	3.20%	0.13%	9,516,100	15.32
Baltimore	805,029	508,547,194	2.83%	0.50%	88,950,800	110.49
Calvert	88,737	61,517,634	2.80%	0.53%	11,534,600	129.99
Caroline	33,066	10,300,000	2.63%	0.70%	2,721,900	82.32
Carroll	167,134	120,000,000	3.05%	0.28%	10,819,700	64.74
Cecil	101,108	44,836,172	2.80%	0.53%	8,406,800	83.15
Charles	146,551	88,744,000	2.90%	0.43%	13,005,600	88.74
Dorchester	32,618	8,600,000	2.62%	0.71%	2,314,100	70.95
Frederick	233,385	155,843,000	2.96%	0.37%	19,217,100	82.34
Garrett	30,097	9,300,000	2.65%	0.68%	2,368,900	78.71
Harford	244,826	161,600,000	3.06%	0.27%	13,994,800	57.16
Howard	287,085	325,465,000	3.20%	0.13%	12,713,500	44.28
Kent	20,197	8,040,000	2.85%	0.48%	1,340,000	66.35
Montgomery	971,777	1,117,243,000	3.20%	0.13%	43,642,300	44.91
Prince George's	863,420	443,234,000	3.20%	0.13%	17,313,800	20.05
Queen Anne's	47,798	31,100,000	3.20%	0.13%	1,214,800	25.42
St. Mary's	105,151	65,500,000	3.00%	0.33%	7,095,800	67.48
Somerset	26,470	6,027,684	3.15%	0.18%	334,900	12.65
Talbot	37,782	19,000,000	2.25%	1.08%	9,077,800	240.27
Washington	147,430	59,380,000	2.80%	0.53%	11,133,800	75.52
Wicomico	98,733	34,376,000	3.10%	0.23%	2,495,000	25.27
Worcester	51,454	9,200,000	1.25%	2.08%	15,272,000	296.81
Total	5,773,552	\$3,921,053,884			\$429,490,100	\$74.39

Source: Department of Legislative Services