HB 429

Department of Legislative Services

Maryland General Assembly
2012 Session

FISCAL AND POLICY NOTE

House Bill 429 (Delegate Schuh, *et al.*)
Ways and Means

Sales and Corporate Income Tax Relief (Better Maryland - Tax Relief)

This bill reduces the State corporate income tax rate from 8.25% to 7.25% beginning in fiscal 2013 and reduces the State sales and use tax rate from 6% to 5.5% in fiscal 2013 and to 5% beginning in fiscal 2014.

The bill takes effect July 1, 2012.

Fiscal Summary

State Effect: General fund revenues decrease by $428.3 million in FY 2013 and special fund revenues decrease by $17.8 million. Future year revenue losses reflect the full phase-in of the sales tax rate reduction and the current sales and use tax and corporate income tax revenue forecasts. General fund expenditures increase by $124,300 in FY 2013 for computer programming and notification costs.

($ in millions)	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
GF Revenue	($428.3)	($765.7)	($803.8)	($834.5)	($878.5)
SF Revenue	($17.8)	($24.9)	($26.7)	($27.2)	($26.1)
GF Expenditure	$.1	$0	$0	$0	$0
Net Effect	($446.2)	($790.6)	($830.5)	($861.7)	($904.6)

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

Local Effect: Local highway user revenues will decrease by $982,000 in FY 2013 and by $1.8 million in FY 2017. Expenditures are not effected.

Small Business Effect: Potential meaningful.

Analysis

Current Law: The State sales and use tax rate is 6%, except for the sale of alcoholic beverages, which are taxed at a rate of 9%. The State corporate income tax rate is 8.25%.

Background: The sales and use tax is the State's second largest source of general fund revenue, accounting for approximately $4.0 billion in both fiscal 2012 and 2013, according to the December 2011 revenue forecast. **Exhibit 1** shows the sales and use tax rates in surrounding states and the District of Columbia.

Exhibit 1
Sales and Use Tax Rates in Maryland and Surrounding States

Delaware	0%
District of Columbia	6%
Maryland	6% 9% for alcoholic beverages
Pennsylvania	6% plus 1% in certain local jurisdictions 0% sales tax on clothing
Virginia	5%; 2.5% for food, both rates include 1% for local jurisdictions
West Virginia	6%; 2% for food

A corporate income tax rate of 8.25% is applied to a corporation's Maryland taxable income. In general, the Maryland corporate income tax is computed using federal provisions to determine income and deductions.

Every Maryland corporation and every corporation that conducts business within Maryland, including public service companies and financial institutions, are required to pay the corporate income tax. The tax base is the portion of federal taxable income, as determined for federal income tax purposes and adjusted for certain Maryland addition and subtraction modifications, that is allocable to Maryland. Federal taxable income for this purpose is the difference between total federal income and total federal deductions (including any special deductions). The next step is to calculate a corporation's Maryland taxable income. The Maryland taxable income of a corporation that operates wholly within the State is equal to its Maryland modified income. Corporations engaged in multistate operations are required to determine the portion of their modified income attributable to Maryland, based on the amount of their trade or business carried out in

Maryland. Corporations are generally required to use either a three-factor apportioned formula of payroll, property, and sales, with sales double weighted or, in the case of a manufacturing corporation, a single sales factor formula. The apportionment factor is then multiplied by a corporation's modified income to determine Maryland taxable income. The Maryland tax liability of a corporation equals the Maryland taxable income multiplied by the tax rate, less any tax credits.

Chapter 3 of the 2007 special session increased the corporate income tax rate from 7% to 8.25%. Chapter 3 also created the Higher Education Investment Fund (HEIF), and distributed a portion of corporate income tax revenues to that fund. Net corporate income tax revenues are projected to total $822.3 million in fiscal 2013. Of this amount, $706.7 million is general fund revenues, $66.3 million is TTF revenues, and $49.3 million is HEIF revenues.

State Revenues: Total revenues will decrease by $446.1 million in fiscal 2013 and by $904.6 million in fiscal 2017, based on the current sales tax and corporate income tax revenue forecasts.

Reducing the sales and use tax rate to 5.5% in fiscal 2013 and to 5% beginning in fiscal 2014 will reduce general fund revenues by approximately $319.2 million in fiscal 2013 and by approximately $778.1 million in fiscal 2017. The estimate assumes a 0.47% increase in taxable sales resulting from the sales tax rate reduction.

Reducing the corporate income tax rate to 7.25% beginning in fiscal 2013 will reduce general fund revenues by approximately $109.1 million and special fund (TTF and HEIF) revenues by approximately $17.8 million in fiscal 2013.

Exhibit 2 shows the estimated decrease in general fund, TTF, and HEIF revenues resulting from the bill.

Exhibit 2
Effect of HB 429 on State Revenues

	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
General Fund	($428,254,000)	($765,662,000)	($803,758,000)	($834,521,000)	($878,549,000)
HEIF	(7,614,000)	(6,637,000)	(7,118,000)	(7,241,000)	(7,590,000)
TTF	(10,229,000)	(18,302,000)	(19,629,000)	(19,968,000)	(18,463,000)
State	(9,247,000)	(16,545,000)	(17,744,000)	(18,051,000)	(16,690,000)
Local	(982,000)	(1,757,000)	(1,884,000)	(1,917,000)	(1,772,000)
Total	**($446,097,000)**	**($790,601,000)**	**($830,505,000)**	**($861,730,000)**	**($904,602,000)**

State Expenditures: The Comptroller's Office will incur a variety of one-time expenditures to administer the sales tax rate decrease, including notification costs relating to mailing and postage and minimal computer programming modifications. As a result, general fund expenditures increase by $124,300 in fiscal 2013. The estimate is based on computer programming costs of $12,000 and notifying 130,000 sales tax account holders and 62,000 corporate income tax filers of the changes under the bill at an average cost of $0.585 per account.

Local Revenues: Local highway user revenues will decrease as a result of the reduction of the corporate income tax rate. Local highway user revenues will decrease by $982,000 in fiscal 2013 and by $1.8 million in fiscal 2017, as shown in Exhibit 2.

Small Business Effect: To the extent that small retail businesses located in Maryland have been adversely affected due to lost sales resulting from increasing the sales and use tax rate to 6% beginning in January 2008, reducing the tax rate would presumably help mitigate any negative effects. The fiscal and policy note for Chapter 6 of the 2007 special session assumed a 0.95% reduction in sales due to the tax rate increase. As a point of reference, this would result in approximately $9,500 in recouped sales for a business with $1 million in gross sales after the rate is reduced to 5%. However, the actual effect would vary from business to business.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): State Department of Assessments and Taxation, Comptroller's Office, Maryland Association of Counties, Maryland Municipal League, Department of Legislative Services

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Analysis by: Michael Sanelli

Direct Inquiries to:
(410) 946-5510
(301) 970-5510