SB 732

Department of Legislative Services

Maryland General Assembly
2014 Session

FISCAL AND POLICY NOTE

Senate Bill 732 (Senator Manno)
Budget and Taxation

Income and Sales Tax Incentives - Emergency Preparedness Equipment

This bill establishes an annual six-day sales tax-free period in calendar 2014 through 2018 for the purchase of emergency preparedness equipment costing $60 or less. The tax-free period is from May 19 through May 24. The Comptroller must, by January 1, 2015, publish a list of emergency preparedness equipment that is exempt during the tax-free period on the Comptroller's website. The Comptroller is authorized to amend the list of exempt items for subsequent sales tax-free periods. Emergency preparedness equipment is any equipment necessary or convenient during an emergency, not including portable generators.

The bill also allows a qualified nursing home to claim a refundable credit against the State income tax for the amount of any sales tax paid during the taxable year on the purchase of a backup generator for the nursing home.

The bill generally takes effect July 1, 2014, and applies to taxable years beginning after December 31, 2013, but before January 1, 2019. The income tax provisions of the bill terminate June 30, 2019.

Fiscal Summary

State Effect: General fund and special fund revenues decrease by a significant amount from FY 2015 through 2019. The amount of the decrease depends on the types of equipment identified by the Comptroller as qualifying for the sales tax exemption, the amount of emergency preparedness equipment purchased, the cost of each exempt item, as well as the number and amount of income tax credits claimed by qualified nursing homes. Under various assumptions the sales tax holiday may reduce revenues by at least $1.0 million annually and the income tax credit may reduce revenues by an additional $270,300 on an annual basis. General fund expenditures increase by $79,000 in FY 2015 for one-time tax form changes and computer programming modifications at the Comptroller's Office.

Local Effect: Potential decrease in local highway user revenues in FY 2015 though 2019. Expenditures are not affected.

Small Business Effect: Minimal.

Analysis

Current Law/Background: There are two sales tax-free periods each year in Maryland. The purchase of any item of clothing or footwear, excluding accessories, if the taxable price of the item of clothing or footwear is $100 or less is exempt from the State sales tax during the seven-day period beginning the second Sunday in August through the following Saturday. The purchase of specified Energy Star products or solar hot water heaters made on the Saturday immediately preceding the third Monday in February through the third Monday in February is also exempt from the State sales tax.

The two current sales tax-free periods are estimated to reduce general fund revenues by a total of $6.7 million in fiscal 2014 and by $6.9 million in fiscal 2015.

The sales and use tax is the State's second largest source of general fund revenue, accounting for approximately $4.2 billion in fiscal 2014 and $4.4 billion in fiscal 2015, according to the December 2013 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	5.75%
Maryland	6% 9% for alcoholic beverages
Pennsylvania	6% plus 1% or 2% in certain local jurisdictions
Virginia*	5.3%; 2.5% for food, both rates include 1% for local jurisdictions
West Virginia	6%; 1% for food

*An additional State tax of 0.7% is imposed on sales in localities in Northern Virginia and the Hampton Roads region.

Task Force to Study Tax Benefits for Emergency Preparedness Equipment

Chapter 481 of 2013 established the Task Force to Study Tax Benefits for Emergency Preparedness Equipment to study and make recommendations regarding an income tax credit for purchasing electric generators and a sales tax-free period for emergency preparedness equipment. The task force was required to report its findings and recommendations to the Governor and General Assembly by December 1, 2013.

The task force met during the 2013 interim and issued its report on January 24, 2014. The task force issued the following recommendations:

- After careful consideration of the budget outlook for the State and ensuring that the policy not prove detrimental to other important budget priorities, the General Assembly should consider enacting a refundable tax credit for backup power generators purchased by assisted living facilities with 49 beds or less.

- The tax credit for assisted living facilities should be limited to 50% of the cost of the generator without a cap.

- The length of the period of the tax credit should not exceed five years to allow for adequate participation in the program.

- After careful consideration of the budget outlook for the State and ensuring that the policy not prove detrimental to the other important budget priorities, the General Assembly should consider enacting a tax holiday for emergency preparedness products and supplies with a selling price of $60 or less for a period of one week prior to the official start of Hurricane Season (June 1). The tax holiday should expire five years from the passage of the legislation.

A copy of the task force report to the Governor and General Assembly can be found at:
http://msa.maryland.gov/megafile/msa/speccol/sc5300/sc5339/000113/018000/018944/unrestricted/20140017e.pdf

Major Outage Events

Several major power outage events have occurred in the State in recent years. For example, several violent thunderstorms hit the Pepco service territory on July 25, August 5, and August 12, 2010, causing power outages to 297,000, 75,000, and 98,000 customers, respectively. The Public Service Commission (PSC) received many complaints about the outages. On January 26, 2011, a winter storm caused 126,000 peak customer outages in the Baltimore Gas and Electric (BGE) service territory and 190,000 peak customer outages in the Pepco service territory.

On June 29, 2012, a "derecho" storm severely impacted electrical service to a large portion of the State, especially in the BGE and Pepco service territories. High sustained wind speeds with gusts in excess of 65 miles per hour (mph) resulted in downed trees, broken telephone poles, and damaged electric distribution infrastructure. Based on the definition of "major outage event," most electric companies in the State were required to file a written report on the outage and subsequent repair services. The reports indicate that BGE and Pepco each experienced over 750,000 total customer outages, with maximum concurrent interruptions of over 400,000 customers each – significantly higher than for any other recent major outage event. **Exhibit 2** contains information related to customer outages and service restoration for each electric company that filed a report. Full copies of each of the reports can be found on PSC's website under Case No. 9298.

Exhibit 2
Summary Statistics – Utility Major Outage Event Reports
June 29, 2012 Derecho Storm

	Total Maryland Customers	Total Customer Outages	Maximum Concurrent Interruptions	Customer Interruption Hours	Average Duration per Customer (Hours)	Duration of Major Outage Event
BGE	1,240,173	762,781	429,841	28,643,177	37.6	8 Days,15 Hours
Delmarva	194,945	50,476	28,059	436,823	8.7	3 Days, 19 Hours
Pepco	534,601	786,766	410,679	20,465,930	26.0	8 Days, 6 Hours
SMECO	151,800	83,250	56,424	1,203,860	14.5	3 Days, 19 Hours

SMECO: Southern Maryland Electric Cooperative
Source: Major Outage Reports Filed in PSC Case No. 9298

Finally, Hurricane Sandy made landfall near Atlantic City, New Jersey, on October 28, 2012. Much of Maryland experienced sustained wind speeds in excess of 35 mph, with gusts ranging from 55 to 65 mph. Many areas in the State experienced between four and six inches of rain, and some areas on the Eastern Shore experienced double that, while some areas in Western Maryland received approximately two feet of snow. Despite these totals, customer outages were fewer and of shorter duration, on average, than those related to the June derecho storm. Customer outages in each service territory were approximately:

- 350,000 in BGE;
- 110,600 in Potomac Edison;

- 83,600 in Delmarva;
- 81,400 in Pepco; and
- 35,800 in SMECO.

Additional outage information for each electric company can be found in the major storm reports posted on PSC's website under Case No. 9308.

Other States

Alabama, Florida, Louisiana, and Virginia have or have had annual sales tax holidays for hurricane preparedness equipment. These sales tax holidays are typically held in May, prior to the start of hurricane season. Florida has proposed a two-week holiday for 2014, beginning June 1. Items eligible for the sales tax exemption in these states as well as any price limits are specifically stated.

State Revenues: General fund revenues and special fund revenues will decrease by a significant amount in fiscal 2015 through 2019 as a result of the annual sales tax-free period for emergency preparedness equipment as well as for the income tax credit for qualified nursing homes.

Sales Tax Exemption

The amount of the decrease attributable to the sales tax exemption for emergency preparedness equipment depends on the types of emergency preparedness equipment identified by the Comptroller as qualifying for the exemption, the amount of emergency preparedness equipment purchased during the tax-free period, and the cost of each exempt item, none of which can be reliably estimated; the list of exempt items is not required to be defined until January 1, 2015. Depending on the types of equipment identified by the Comptroller and the cost of this equipment, the effect on general fund revenues from the sales tax-free period specified by the bill is likely to be significant.

As a point of reference, the following hurricane preparedness items are exempt during Virginia's hurricane preparedness sales tax holiday (May 25 through May 31, 2014), if the tax price of the item is $60 or less: artificial ice, blue ice, ice packs, and reusable ice; batteries (excluding automobile or boat batteries), including AAA cell, AA cell, C cell, D cell, 6 volt, 9 volt, and cell phone batteries; any portable self-powered light sources including flashlights, lanterns, and glow sticks; any tarpaulins, plastic sheeting, plastic drop cloths, and other flexible waterproof sheeting; bungee cords, rope, ground anchor systems or tie down kits; ratchet straps; duct tape; carbon monoxide detectors; smoke detectors; fire extinguishers; gas or diesel fuel tanks or containers; water storage containers; nonelectric food storage coolers; bottled water; manual can openers; portable self-powered radios (including self-powered radios with electrical power capability);

two-way radios; weather radios; storm shutter devices; cell phone chargers; and first aid kits. Virginia also provides a sales tax exemption for portable generators and inverters, if the taxable price is $1,000 or less, as well as for gas-powered chainsaws ($350 or less) and accessories ($60 or less).

The Comptroller's Office reports that the sales tax holiday in Virginia has reduced that state's revenues by approximately $2.5 million annually since the holiday went into effect in fiscal 2008. After making adjustments to take into account generator sales included in the sales tax holiday, it is estimated that Virginia residents spent, on average, $2.82 during each of the state's sales tax holidays on a per capita basis.

If, *for illustrative purposes only*, it is assumed that the Comptroller specifies a similar list of tax-exempt emergency preparedness items as in Virginia, and that Maryland residents will spend a commensurate amount on these items as those in Virginia, and taking into account Maryland's population, it is estimated that general fund revenues would decrease by at least $1.0 million each year during the sales tax holiday proposed by the bill.

Income Tax Credit

The task force report indicates that most assisted living facilities in the State are required to have some form of backup generation for emergency situations. However, there are 1,335 assisted living facilities in the State with 49 or fewer beds that are exempt from this requirement. The task force report states that the cost of a backup generator for these facilities will likely range from $15,000 to $30,000 depending on the size of the facility. The amount of revenue loss depends on the number of qualifying nursing homes that purchase a backup generator in a given year and cannot be reliably estimated.

However, *for illustrative purposes only*, if it is assumed that 75% of assisted living facilities with 49 or fewer beds purchase a backup generator over the five-year life of the tax credit, general fund revenues will decrease by approximately $1.4 million over the five-year period. The estimate assumes an average generator price of $22,500 and that approximately 200 facilities will purchase a backup generator each year between fiscal 2015 and 2019 and claim the credit against the personal income tax. Under this scenario the annual revenue loss is estimated to total approximately $270,300.

To the extent credits are claimed against the corporate income tax, Transportation Trust Fund (TTF) and Higher Education Investment Fund revenues will decrease. Local governments receive a portion of TTF revenues in the form of local highway user revenues for the purpose of constructing and maintaining local roads. Accordingly, local highway user revenues will decrease as a result of any credits claimed against the corporate income tax.

State Expenditures: The Comptroller's Office reports that it will incur a one-time expenditure increase of $79,000 in fiscal 2015 to add the credit to the personal and corporate income tax forms. This amount includes data processing changes to the SMART income tax return processing and imaging systems and systems testing.

Local Revenues: Local governments receive a portion of corporate income tax revenues to support the construction and maintenance of local roads and other transportation facilities. As a result, local highway user revenues may decrease beginning in fiscal 2015 from income tax credits being claimed against the corporate income tax.

Additional Information

Prior Introductions: None.

Cross File: HB 784 (Delegate A. Miller, *et al.*) - Ways and Means.

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

Fiscal Note History: First Reader - February 24, 2014
mc/jrb

Analysis by: Michael Sanelli

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