**HB 267**

# Department of Legislative Services
Maryland General Assembly
2016 Session

## FISCAL AND POLICY NOTE
**First Reader**

House Bill 267 (Delegates Grammer and Metzgar)
Ways and Means

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**Sales and Use Tax - Exemption - Sales by Out-of-State Vendors**

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This bill exempts from the State sales and use tax the sale of tangible personal property or a taxable service if the sale is made by an out-of-state vendor whose only connection to the State is having an employee operating in the State for the purposes of delivering, selling, or taking orders for tangible personal property or a taxable service and the out-of-state vendor has 10 or less employees operating in the State.

The bill takes effect July 1, 2016.

## Fiscal Summary

**State Effect:** General fund revenues decrease by a potentially significant amount beginning in FY 2017. The amount of the revenue decrease depends on the number of qualifying vendors and the amount of sales those vendors make in Maryland. General fund expenditures for administrative costs in the Comptroller's Office increase by $81,300 in FY 2017.

**Local Effect:** None.

**Small Business Effect:** Minimal.

## Analysis

**Current Law:** Engaging in the business of an out-of-state vendor means to sell or deliver tangible personal property or a taxable service for use in the State. This includes (1) permanently or temporarily maintaining, occupying, or using any office, sales or sample room, or distribution, storage, warehouse, or other place for the sale of tangible personal property or a taxable service directly or indirectly through an agent or subsidiary; (2) having an agent, canvasser, representative, salesman, or solicitor operating in the State for the purpose of delivering, selling, or taking orders for tangible personal property or a taxable service; or (3) entering the State on a regular basis to provide service or repair for tangible personal property.

The general sales and use tax is imposed on a bracket basis approximating 6%. Numerous exemptions from the sales and use tax are provided under Maryland law.

**Background:** The sales and use tax is the State's second largest source of general fund revenue, accounting for approximately $4.5 billion in fiscal 2016 and $4.7 billion in fiscal 2017, according to the December 2015 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**

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| Delaware | 0% |
| District of Columbia | 5.75%; 10% for liquor sold for off-the-premises consumption and restaurant meals, liquor for consumption on the premises, and rental vehicles |
| Maryland | 6%<br>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%; plus 0.5% or 1% in certain municipalities |

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

*Sales Tax Nexus*

Pursuant to a 1992 U.S. Supreme Court ruling (*Quill Corp. v. North Dakota*), Internet and mail-order retailers are only required to collect sales and use tax from out-of-state customers if the retailer maintains a physical presence (*e.g.*, a store, office, or warehouse) in the customer's home state. In an effort to ensure parity with bricks-and-mortar sellers, New York passed a law in 2008 providing that affiliate sellers (*e.g.*, independent websites that link to an online retailer's products in return for a commission) were included within the definition of "physical presence," thus requiring out-of-state web retailers to collect sales taxes from buyers in the state if the retailers have New York-based representatives referring businesses to them.

A number of other states, including Arkansas, California, Connecticut, Georgia, Illinois, Minnesota, Missouri, North Carolina, and Rhode Island, have passed legislation similar to the legislation passed in New York. As a result, Amazon.com and Overstock.com, generally the largest companies affected, ended their relationships with affiliates in some of those states in order to avoid a determination that nexus exists.

Beginning October 1, 2014, Amazon.com began collecting sales taxes on sales made to Maryland residents as a result of opening a distribution center in Baltimore City. The Comptroller's Office estimated that Amazon.com will collect approximately $55.0 million in sales taxes in fiscal 2016.

The Comptroller's Office advises that 38 of the 50 largest online retailers in the United States currently have nexus in the State.

**State Fiscal Effect:** General fund revenues will decrease by a potentially significant amount beginning in fiscal 2017. The amount of the decrease depends on the number of out-of-state vendors with 10 or fewer employees doing business in the State and the amount of sales taxes currently being collected by these businesses, neither of which can be reliably estimated.

The Comptroller's Office advises that the bill may create an incentive for some businesses near the 10 employee threshold specified in the bill to reduce their employment in order to qualify for the exemption. In addition, businesses located in Maryland with 10 or fewer employees may find it cost effective to restructure and register out of state while maintaining sales in Maryland.

As a point of reference, and *for illustrative purposes only*, if 0.5% of current sales tax revenues are collected by out-of-state vendors who would qualify for the exemption under the bill, general fund revenues would decrease by approximately $23 million annually beginning in fiscal 2017.

The Comptroller's Office would incur a one-time expenditure increase of $81,300 in fiscal 2017 to notify the approximately 130,000 sales and use tax account holders of the sales tax change.

## Additional Information

**Prior Introductions:** None.

**Cross File:** None.

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

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