

Department of Legislative Services  
 Maryland General Assembly  
 2018 Session

FISCAL AND POLICY NOTE  
 Third Reader - Revised

Senate Bill 565

(Senator Serafini)

Budget and Taxation

Ways and Means

Interest Rate on Tax Deficiencies and Refunds

This bill alters the calculation of the annual interest rate that the Comptroller sets for tax deficiencies and refunds by setting the interest rate at three percentage points above the average prime rate of interest quoted by commercial banks to large businesses during the State’s previous fiscal year. **The bill takes effect July 1, 2018.**

Fiscal Summary

**State Effect:** General fund revenues decrease by \$8.8 million in FY 2019. Transportation Trust Fund (TTF) revenues decrease by \$148,800 and Higher Education Investment Fund (HEIF) revenues decrease by \$67,700 in FY 2019. Future year estimates reflect projected interest revenues and rates. No effect on expenditures.

(\$ in millions)	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
GF Revenue	(\$8.8)	(\$8.4)	(\$4.5)	(\$2.5)	(\$0.4)
SF Revenue	(\$0.2)	(\$0.2)	(\$0.1)	(\$0.1)	\$0.0
Expenditure	0	0	0	0	0
Net Effect	(\$9.0)	(\$8.6)	(\$4.6)	(\$2.5)	(\$0.4)

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

**Local Effect:** Local income tax revenues decrease by \$2.1 million in FY 2019 and by \$87,600 in FY 2023. Local highway user revenues decrease by \$15,800 in FY 2019 and by \$600 in FY 2023. No effect on local expenditures.

**Small Business Effect:** Potential meaningful. Small businesses could realize reduced interest charges in FY 2019 through 2023.

## Analysis

**Current Law:** Chapter 322 of 2016 altered the calculation of the annual interest rate that the Comptroller sets for tax deficiencies and refunds. By October 1 of each year, the Comptroller's Office must set the annual interest rate for tax refunds and monies owed to the State for the next calendar year at a rate, rounded to the nearest whole number, equal to the greater of three percentage points above the average prime rate of interest in the previous fiscal year, based on information from the Federal Reserve Bank, or:

- 13% for calendar 2016;
- 12% for calendar 2017;
- 11.5% for calendar 2018;
- 11% for calendar 2019;
- 10.5% for calendar 2020;
- 10% for calendar 2021;
- 9.5% for calendar 2022; and
- 9% for calendar 2023 and each year thereafter.

Chapter 506 of 2017 repealed the requirement that the Comptroller, when setting the annual interest rate for tax refunds and monies owed to the State, round the interest rate to the nearest whole number.

**Background:** Of the states that impose an income tax, the interest penalty rate currently imposed on overpayments typically ranges from 3% to 8%. Of those states, only Oklahoma (15%) and North Dakota (12%) have a higher rate than Maryland in calendar 2018. The current interest penalty rates in surrounding jurisdictions are Delaware (6%), District of Columbia (1% above the primary credit discount rate for the Richmond Federal Reserve Bank, rounded to the nearest whole number, not to exceed 6%), Pennsylvania (4%), Virginia (6%, adjusted quarterly), and West Virginia (7.25%, adjusted quarterly).

In fiscal 2014, the Comptroller's Office collected the following amounts of interest: \$34.2 million from the individual income tax and fiduciary returns; \$4.3 million from the corporate income tax; \$2.1 million from income tax withholding; and \$2.6 million from sales tax returns. A further amount was collected from interest (\$2.2 million) from pass through entities on sales tax assessments. The Comptroller's Office typically pays out less than \$1.0 million in interest annually, depending on the year, for the various taxes.

**State Fiscal Effect:** The bill sets the State rate of interest for late payment of taxes and tax refunds at three percentage points above the average prime rate of interest quoted by commercial banks to large businesses during the State's previous fiscal year. **Exhibit 1** shows the estimated new interest rates for fiscal 2019 through 2023.

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**Exhibit 1**  
**Estimated Interest Rates Under the Bill**  
**Fiscal 2019-2023**

FY 2019	8.6%
FY 2020	9.5%
FY 2021	9.6%
FY 2022	9.4%
FY 2023	9.2%

Source: Department of Legislative Services

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Based on the amount of current interest collected on late taxes, interest paid on tax refunds, and projected interest rates, general fund revenues will decrease by \$8.8 million, TTF revenues will decrease by \$148,800, and HEIF revenues will decrease by \$67,700 in fiscal 2019, which represent approximately one-half of the estimated annual revenue decrease for calendar 2019.

The estimated changes in interest payments shown in **Exhibit 2** are based on the difference in interest rates that would be applied by the Comptroller's Office under the bill compared to the estimated effective interest rates under current law in each tax year. For purposes of this estimate, the average of interest payments received and paid over a six-year period (fiscal 2009 through 2014) was used to estimate future year changes due to annual fluctuations in the amount of payments received. This amount was then adjusted to account for increased tax compliance efforts instituted over the past several years. Future year payments are estimated to increase by 2% each year.

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**Exhibit 2**  
**State and Local Revenue Impacts**  
**Fiscal 2019-2023**

	<u><b>FY 2019</b></u>	<u><b>FY 2020</b></u>	<u><b>FY 2021</b></u>	<u><b>FY 2022</b></u>	<u><b>FY 2023</b></u>
General Fund	(\$8,767,500)	(\$8,436,700)	(\$4,474,800)	(\$2,457,700)	(\$358,100)
HEIF	(67,700)	(65,100)	(34,500)	(19,000)	(2,800)
TTF-MDOT	(148,800)	(143,200)	(75,900)	(41,700)	(6,100)
<b>Total</b>	<b>(\$8,983,900)</b>	<b>(\$8,644,900)</b>	<b>(\$4,585,300)</b>	<b>(\$2,518,400)</b>	<b>(\$367,000)</b>
 <b>Local Revenues</b>					
TTF-LHUR	(\$15,800)	(\$15,200)	(\$8,100)	(\$4,400)	(\$600)
Income Tax	(2,145,200)	(2,064,300)	(601,300)	(601,300)	(87,600)
<b>Total</b>	<b>(\$2,161,000)</b>	<b>(\$2,079,500)</b>	<b>(\$609,400)</b>	<b>(\$605,800)</b>	<b>(\$88,300)</b>

HEIF: Higher Education Investment Fund  
LHUR: local highway user revenues  
MDOT: Maryland Department of Transportation  
TTF: Transportation Trust Fund

Source: Comptroller's Office; Department of Legislative Services

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**Local Fiscal Effect:** Local revenues will decrease as a result of a decrease in local highway user revenues distributed from the corporate income tax and from local income tax revenues. Local governments receive a portion of personal income tax interest penalty revenues. These distributions are made biannually, with the first distribution made in the first month of a fiscal year based on interest collections from the second half of the preceding fiscal year. The second distribution is made in January and is attributable to interest received in the first half of that fiscal year. Total local revenues will decrease by \$2.2 million in fiscal 2019 and by \$88,300 in fiscal 2023, as shown in Exhibit 2.

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**Additional Information**

**Prior Introductions:** None.

**Cross File:** None.

**Information Source(s):** Comptroller's Office; CCH Intelliconnect; Department of Legislative Services

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