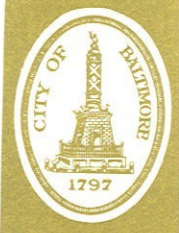


Andrew Klein

<b>FROM</b>	NAME & TITLE	Andrew W. Kleine, Chief
	AGENCY NAME & ADDRESS	Bureau of the Budget and Management Research Room 469, City Hall (396-4941)
	SUBJECT	City Council Bill # 11-0640 –Hotel Penalty

CITY of  
BALTIMORE  
**MEMO**

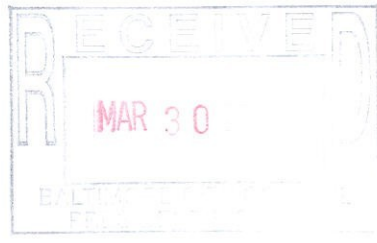


**TO** The Honorable President and

DATE: March 28, 2011

Members of the City Council  
C/O Karen Randle  
Room 409, City Hall

Attention: Karen Randle



**Synopsis of Proposed City Council Bill**

CCB 11-0640 changes the current 100% penalty to a 10% penalty for late hotel tax payments.

**Analysis**

- Tax evasion has been shown to be a function of the probability of being caught and the penalty associated with being caught. The higher the penalty, the less likely a tax payer is to evade taxes.
- Hotel Taxes are self reported.
- Enforcement is dependent on audits by the Comptroller’s Office.
- An audit is a very expensive enforcement measure and can often cost more than the taxes recovered.
- A lower penalty will increase tax evasion.
- These funds are City funds and are not for used by hotels for internal financing. These funds become City funds at the point of sale, as opposed to the point of payment to City.

**Fiscal Impact**

The City could expect a reduction in paid hotel taxes if the penalty is reduced. Utilizing the Allingham-Sandmo Model of tax evasion, the City could expect a 4.5% increase in tax evasion if the rate were lowered from 100% to 10%. The Allingham-Sandmo model<sup>1</sup> calculates the expected benefits of evasion under the premise that a higher penalty and higher probability of getting caught result in lower evasion. With the annual hotel tax of \$25M, the estimated cost to the City could be \$1.1M.

<sup>1</sup> Sandmo, Agnar, (2005), “The Theory of Tax Evasion: A Retrospective View”, *National Tax Journal*, 58(4), p.643.

**Recommendation**

The Finance Department opposes this bill.

Cc: Edward J. Gallagher  
Angela Gibson  
William Voorhees

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