SB 263

Department of Legislative Services

Maryland General Assembly
2020 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 263 (Senator Rosapepe)
Budget and Taxation

Opportunity Zone Tax Deduction Reform Act of 2020

This bill requires a person to add back to Maryland adjusted gross income or Maryland modified income the amount of capital gains deferred or excluded under the federal Qualified Opportunity Zones Program. **The bill takes effect July 1, 2020, and applies to tax year 2020 and beyond.**

Fiscal Summary

State Effect: General fund revenues increase by $13.5 million in FY 2021 as a result of income being added back to the corporate and personal income tax. Transportation Trust Fund (TTF) revenues increase by $2.0 million and Higher Education Investment Fund (HEIF) revenues increase by $0.8 million in FY 2021. Future year revenue estimates reflect projected income added back in each year. TTF expenditures increase by $0.3 million in FY 2021 and by $0.2 million in FY 2025 due to an increase in local highway user revenue grants.

($ in millions)	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
GF Revenue	$13.5	$12.6	$11.8	$11.2	$10.8
SF Revenue	$2.9	$2.7	$2.5	$2.4	$2.3
SF Expenditure	$0.3	$0.3	$0.2	$0.2	$0.2
Net Effect	$16.1	$15.1	$14.1	$13.4	$13.0

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

Local Effect: Local highway user revenues distributed from the corporate income tax increase by $0.3 million in FY 2021 and by $0.2 million in FY 2025. Local income tax revenues increase by $1.5 million in FY 2021 and by $1.2 million in FY 2025 due to taxpayers adding back income to the personal income tax. Local expenditures are not affected.

Small Business Effect: Potential meaningful.

Analysis

Current Law: The Federal Tax Cuts and Jobs Act of 2017 established the Qualified Opportunity Zones Program to incentivize private investment in certain communities. Under the Act, states may nominate up to 25% of specified low-income census tracts for designation by the U.S. Treasury as opportunity zones.

The program offers three federal tax incentives related to capital gains: (1) a temporary tax deferral for capital gains reinvested in an Opportunity Fund; (2) a step up in basis for capital gains reinvested in an Opportunity Fund, which excludes up to 15% of the original capital gain from taxation; and (3) a permanent exclusion from taxable income of capital gains from the sale or exchange of an investment in an Opportunity Fund, if the investment is held for at least 10 years. Investors and investments must also meet numerous other requirements.

Qualifying investments may only be made through calendar 2026. The opportunity zone designations expire on December 31, 2028, but the tax benefits for existing investments may be claimed through at least calendar 2047.

Maryland generally conforms to federal tax law, so any capital gain deferred or excluded under the program is also deferred or excluded under the Maryland income tax.

Background: The U.S. Treasury has designated a total of 8,769 zones, of which 149 are located in Maryland. The U.S. Joint Committee on Taxation estimates the program will reduce federal revenues by about $3.4 billion annually throughout the next five federal fiscal years.

In addition to federal and state tax benefits, Chapter 211 of 2019 established the Opportunity Zone Enhancement Program. Administered by the Department of Commerce, the program provides enhanced incentives for qualifying businesses within an opportunity zone. Qualifying businesses within an opportunity zone may qualify for enhanced incentives under the following tax credit programs (1) job creation; (2) One Maryland; (3) enterprise zone; (4) biotechnology investment incentive; (5) cybersecurity investment incentive; and (6) More Jobs for Marylanders.

State Fiscal Effect: Under current law, Maryland conforms to the federal tax treatment of capital gains eligible for special treatment under the federal Qualified Opportunity Zones Program. The bill requires a person to add back the amount of capital gains that are deferred or excluded under the program, thereby making these gains taxable for State income tax purposes. As a result, general fund revenues will increase by $13.5 million in fiscal 2021. TTF revenues will increase by $2.0 million, and HEIF revenues will increase by

$0.8 million in fiscal 2021. **Exhibit 1** shows the estimated State fiscal impacts resulting from the bill.

Exhibit 1
Fiscal Impact
($ in Millions)

	FY 2021	FY 2022	FY 2023	FY 2024	FY 2025
General Fund	$13.5	$12.6	$11.8	$11.2	$10.8
HEIF	0.8	0.8	0.7	0.7	0.7
TTF	2.0	1.9	1.8	1.7	1.6
Total	**$16.3**	**$15.3**	**$14.3**	**$13.6**	**$13.1**
TTF Expenditures	**$0.3**	**$0.3**	**$0.2**	**$0.2**	**$0.2**

HEIF: Higher Education Investment Fund
TTF: Transportation Trust Fund

Source: Department of Legislative Services

This estimate is based on the U.S. Joint Committee on Taxation's forecast of the federal revenue impact of the opportunity zone program, adjusted for Maryland. The estimate also reflects a change in investor behavior in response to the bill and a modest decrease in revenue losses under the State Opportunity Zone Enhancement Program.

A portion of TTF revenues are used to provide capital transportation grants to local governments. An increase in TTF revenues from corporate income tax revenues will result in a 13.5% increase in TTF expenditures to local governments (9.6% beginning in fiscal 2025). Accordingly, TTF expenditures increase by $0.3 million in fiscal 2021 and by $0.2 million in fiscal 2025, as shown in Exhibit 1.

Local Revenues: Local governments receive a portion of corporate income tax revenues as local highway user revenues through capital transportation grants. Local highway user revenues increase by approximately $0.3 million in fiscal 2021 and by $0.2 million in fiscal 2025 as a result of income being added back to the corporation income tax. Local income tax revenues will increase by $1.5 million in fiscal 2021 and by $1.2 million in fiscal 2025 due to the bill's add-back requirement.

Small Business Effect: Small businesses that receive investments through the program or small business qualified investment funds may be negatively impacted by the loss of State and local tax benefits.

Additional Information

Prior Introductions: None.

Designated Cross File: HB 224 (Delegate Palakovich Carr, *et al.*) - Ways and Means.

Information Source(s): U.S. Joint Committee on Taxation, Department of Legislative Services

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