HB 1111

Department of Legislative Services

Maryland General Assembly
2021 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 1111 (Delegate Wivell)
Ways and Means

Income Tax - Itemized Deductions

This bill allows an individual to itemize deductions for State income tax purposes without regard to whether or not the individual itemizes for federal income tax purposes. For an individual who itemizes on their State but not federal income tax return, the value of the itemized deductions is calculated as if the individual itemized on their federal income tax return. **The bill takes effect July 1, 2021, and applies to tax year 2021 and beyond.**

Fiscal Summary

State Effect: Allowing a taxpayer the option of itemizing for State income tax purposes will decrease general fund revenues by at least $159.5 million in FY 2022, reflecting the impact from about one and one-half tax years. Future year estimates reflect annualization and projected growth in eligible expenses. General fund expenditures increase beginning in FY 2022 due to implementation costs at the Comptroller's Office.

($ in millions)	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026
GF Revenue	($159.5)	($115.4)	($118.8)	($122.8)	($126.9)
GF Expenditure	-	-	-	-	-
Net Effect	($159.5)	($115.4)	($118.8)	($122.8)	($126.9)

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

Local Effect: Local revenues decrease by at least $103.3 million in FY 2022 and by $82.2 million in FY 2026. Local expenditures are not affected.

Small Business Effect: Small businesses that are partnerships, S corporations, limited liability companies, and sole proprietorships may be meaningfully impacted by the bill. Any of these small businesses with lower amounts of taxable income would be positively impacted through decreased income tax liabilities.

Analysis

Current Law:

Federal Law

To determine federal taxable income, a taxpayer may generally reduce their federal adjusted gross income by either claiming the standard deduction or itemizing allowable deductions.

The federal standard deduction in tax year 2019 increases to $12,200 for an individual taxpayer ($24,400, if married filing jointly, and $18,350 for a head of household). These values are indexed in future years for inflation.

The expenses that may be itemized include eligible home mortgage interest, charitable contributions, investment interest, medical expenses, casualty and theft losses attributable to federally declared disasters, and up to $10,000 in State and local taxes.

State Income Tax

An individual is allowed to itemize deductions for State income tax purposes only if the individual itemizes for federal income tax purposes. In addition, a taxpayer can itemize an expense for State income tax purposes only if the expense can be claimed as a federal itemized deduction. Taxpayers generally may only deduct expenses that qualify for the federal itemized deduction. An individual who itemizes for State income tax purposes is required to reduce the sum of the individual's federal itemized deductions by any amount:

- required by Internal Revenue Code (IRC);
- deducted under Section 170 of IRC for contributions of a preservation or conservation easement for which a State credit is claimed; and
- claimed as taxes on income paid to a state or political subdivision of a state, after subtracting a *pro rata* portion of the reduction to itemized deductions required under Section 68 of IRC.

The value of the standard deduction is equal to 15% of Maryland adjusted gross income, subject to minimum and maximum values depending on filing status as shown in **Exhibit 1**.

Exhibit 1
State Income Tax Standard Deduction
Current Law – Tax Year 2019

Single, Dependent Filer, Married Filing Separately		Joint, Head of Household, Widower	
MAGI	**Deduction**	**MAGI**	**Deduction**
Under $10,000	$1,500	Under $20,333	$3,050
$10,000-$14,999	15%	$20,333-$30,322	15%
$15,000 and Over	$2,250	$30,333 and Over	$4,550

MAGI: Maryland adjusted gross income

Note: Estimated values based on projected cost-of-living index.

State Revenues: The bill allows an individual to itemize deductions for State income tax purposes without regard to whether or not the individual itemizes for federal income tax purposes, beginning with tax year 2021. As a result, general fund revenues decrease by at least $159.5 million in fiscal 2022, which reflects the impact of tax year 2021 and about one-half of tax year 2022. **Exhibit 2** shows the projected State and local revenue loss from the bill.

Exhibit 2
Projected State and Local Revenue Impact
($ in Millions)

	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026
State	($159.5)	($115.4)	($118.8)	($122.8)	($126.9)
Local	(103.3)	(74.7)	(77.0)	(79.5)	(82.2)
Total	**($262.8)**	**($190.1)**	**($195.8)**	**($202.3)**	**($209.0)**

The estimated revenue loss shown in Exhibit 2, which is consistent with estimates produced for similar legislation introduced in previous sessions, reflects only the impact of allowing taxpayers to itemize deductions allowable under current federal income tax law. It does not reflect any revenue loss from allowing taxpayers to itemize deduction amounts that are currently limited or eliminated by the federal Tax Cuts and Jobs Act of 2017. By comparison, the Bureau of Revenue Estimates recently examined State income tax returns and estimated that $374.4 million in tax year 2021 State and local income tax revenue is attributable to taxpayers who switched from itemizing deductions to claiming the standard deduction in response to all of the changes enacted by the federal Tax Cuts and Jobs Act.

Most of the federal Act's personal income tax provisions expire after tax year 2025. The revenue impact of the bill will be substantially less beginning in fiscal 2027.

State Expenditures: The Comptroller's Office may incur additional costs beginning in fiscal 2022 as a result of hiring additional revenue examiners and incurring programming expenses.

Local Revenues: Local income tax revenues decrease by about 3% of the net increase in deductions claimed. Local revenues will decrease by at least $103.3 million in fiscal 2022 and by $82.2 million in fiscal 2026, as shown in Exhibit 2.

Additional Information

Prior Introductions: SB 486 of 2020 received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Its cross file, HB 788, received a hearing in the House Ways and Means Committee, but no further action was taken. HB 327 of 2019 received a hearing in the House Ways and Means Committee, but no further action was taken. HB 450 of 2019, a similar bill, received a hearing in the House Ways and Means Committee, but no further action was taken. SB 191 of 2018, a similar bill, received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Its cross file, HB 589, received a hearing in the House Ways and Means Committee, but no further action was taken. HB 1039 of 2018 received a hearing in the House Ways and Means Committee, but no further action was taken.

Designated Cross File: None.

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

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