Department of Legislative Services
Maryland General Assembly
2024 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 908 (Senator Augustine)
Budget and Taxation

Income Tax - Addition Modification - Interest for and Depreciation of Residential Rental Property

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This bill requires an addition modification under the personal and corporate income tax for amounts deducted under § 163 (interest expense deduction) and § 167 (depreciation) of the Internal Revenue Code (IRC) by a disqualified single-family property owner (defined as a taxpayer who owns, directly or indirectly, at least 25 single-family residential rental properties in the State) with respect to specified single-family residential rental property, unless the property is sold to (1) an individual for use as the individual's principal residence or (2) a qualified nonprofit organization. **The bill takes effect July 1, 2024, and applies to tax year 2024 and beyond.**

Fiscal Summary

State Effect: General fund, Transportation Trust Fund (TTF), and Higher Education Investment Fund (HEIF) revenues increase by an indeterminate amount beginning in FY 2025, as discussed below. TTF expenditures for local highway user revenue grants increase by an indeterminate amount beginning in FY 2025. Expenditures are not otherwise affected.

Local Effect: Local income tax revenues and local highway user revenues increase by an indeterminate amount beginning in FY 2025, as discussed below. Local expenditures are not affected.

Small Business Effect: Minimal.

Analysis

Bill Summary: The bill is modeled on proposed federal legislation to disallow interest and depreciation deductions for certain disqualified single-family property owners. "Single-family residential rental property" means residential rental property (any building or structure if 80% or more of the gross rental income from such building or structure for the tax year is rental income from dwelling units) that contains four or fewer dwelling units and improvements to real property directly related to the dwelling units located on the site of those dwelling units. It does not include residential real property (1) with respect to which a credit is allowed under § 42 (low-income housing credit) of the IRC for the tax year; (2) that was constructed by the taxpayer; or (3) that was acquired by the taxpayer after the residential rental property's construction but before the first date on which any dwelling unit in the property was acquired by a resident.

"Qualified nonprofit organization" means an organization that is not organized for profit and has as its principal purpose the creation, development, or preservation of affordable housing. It includes a community development corporation; a community housing development organization; a qualified community-based development organization; a land bank; a resident-owned cooperative or community land trust; and a subsidiary of a public housing agency.

Current Law: Section 163 of the IRC allows a deduction for interest paid or accrued on debt within the tax year, subject to various special rules and limitations. For noncorporate taxpayers, the deduction for investment interest expenses is limited to the amount of net investment income for the tax year; any excess may be carried forward to future years. Maryland generally conforms to the federal interest expense deduction except for interest expenses directly or indirectly paid or accrued by a corporation to a related member, as defined under State law.

Section 167 of the IRC allows as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear, or obsolescence of a capitalized asset. Property is depreciable if it is used in business or held for the production of income and has a determinable useful life of more than one year. Most business and investment property placed in service after 1986, including residential rental property, is depreciated using the Modified Accelerated Cost Recovery System. Maryland generally conforms to federal depreciation rules, with the exception of the § 168(k) bonus depreciation allowance and any increase in § 179 expensing after 2002, which are allowed for State income tax purposes only with respect to property placed in service by a manufacturing entity after 2018.

State Revenues: General fund, TTF, and HEIF revenues increase beginning in fiscal 2025 to the extent the bill results in additional personal and corporate income tax liability.

However, the precise impact cannot be reliably estimated at this time due to data limitations and uncertainty regarding the response of affected taxpayers to the bill's provisions.

State Expenditures: To the extent the bill results in additional corporate income tax revenues, TTF expenditures for local highway user revenue grants increase beginning in fiscal 2025. However, the precise impact cannot be reliably estimated, as discussed above.

Local Revenues: Local income tax revenues and local highway user revenues increase beginning in fiscal 2025 to the extent the bill results in additional personal and corporate income tax liability, respectively. However, the precise impact cannot be reliably estimated.

Additional Information

Recent Prior Introductions: Similar legislation has not been introduced within the last three years.

Designated Cross File: None.

Information Source(s): Comptroller's Office; Internal Revenue Service; Library of Congress; CCH AnswerConnect; Department of Legislative Services

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