

Department of Legislative Services
 Maryland General Assembly
 2004 Session

FISCAL AND POLICY NOTE

House Bill 1489 (Delegate Parrott)
 Ways and Means

**Income Tax - Subtraction for Health Insurance Costs of Individuals Receiving
 Federal Health Coverage Tax Credit**

This bill provides a subtraction modification for individuals who claim the federal health coverage tax credit. The subtraction modification equals the amount by which qualified health care coverage expenses paid by the individual exceeds the amount of the federal health coverage tax credit. Any health care coverage expenses that are paid using a distribution from an Archer Medical Savings Account (MSA) or otherwise are reimbursed are not eligible for the subtraction modification.

The bill takes effect July 1, 2004 and applies to tax year 2004 and beyond.

Fiscal Summary

State Effect: General fund revenues would decline by approximately \$228,600 in FY 2005. Future year estimates reflect estimated use of the subtraction.

(in dollars)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
GF Revenue	(\$228,600)	(\$236,700)	(\$244,200)	(\$252,400)	(\$259,700)
Expenditure	\$0	\$0	\$0	\$0	\$0
Net Effect	(\$228,600)	(\$236,700)	(\$244,200)	(\$252,400)	(\$259,700)

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

Local Effect: Local revenues would decrease by approximately \$139,539 in FY 2005, increasing to \$158,527 by FY 2009. Expenditures would not be affected.

Small Business Effect: None.

Analysis

Current Law: An individual may not deduct health care expenses for State purposes if the individual claims the federal health care coverage tax credit. Individuals who do not claim the credit may, for federal tax purposes, deduct qualifying health care expenditures if the expenses exceed 7.5% of the individual's gross income. This deduction flows through for State income purposes.

Background: The federal Trade Adjustment Assistance Reform Act of 2002 provides that certain displaced workers and eligible Pension Benefit Guaranty Corporation (PBGC) pension recipients, can receive assistance in covering the cost of health insurance coverage. An "eligible PBGC pension recipient" is defined as an individual who is 55 years of age or older and is receiving a pension benefit paid in whole or part by PBGC. The tax credit is equal to 65% of the amount paid by an eligible individual for coverage of the individual and certain family members under qualified health insurance coverage.

Chapter 2 of 2003 made individuals eligible for the federal health care coverage tax credit eligible for the State Maryland Health Insurance Program (MHIP). This change is estimated to cost the State \$12.8 million in fiscal 2005.

Exhibit 1 lists the effects of the enactment of the federal health care coverage tax credit. Before the federal tax credit, if an individual was able to deduct health care expenditures for federal purposes the deduction would flow through for State income tax purposes. If the individual claims the federal tax credit, the individual is not currently able to deduct any of these health care expenditures for State income purposes.

Exhibit 1 Federal and State Tax Treatment of Health Care Expenses Due to the Enactment of Federal Tax Credit

	<u>Qualifying Health Care Expenses</u>	<u>Federal Tax Savings</u>	<u>State Tax Savings</u>	<u>Total Tax Benefits</u>
Without federal credit	\$10,000	\$1,500	\$475	\$1,975
With federal credit	10,000	6,500	0	6,500

State Revenues: General fund revenues would decrease by approximately \$228,555 in fiscal 2005, based on the following facts and assumptions:

- Data are not available for the amount of federal credits claimed. The Joint Committee on Taxation's estimate for total credits claimed by displaced workers and PBGC recipients for fiscal 2005 to 2009 is utilized.
- It is estimated that 3.3% of individuals in PBGC and 1% of displaced workers are from Maryland.
- The amount of estimated credits claimed is adjusted by 3.3% and 1% respectively to calculate the number of credits that will be claimed in Maryland.
- It is assumed that individuals who claim the credit will itemize the other 35% of eligible health care costs as provided under the bill.

Local Revenues: Local revenues would decrease by approximately 2.8% of the State subtraction taken in tax year 2005. In fiscal 2005 the decrease would be approximately \$139,539. Future year revenues decrease as the amount of the total State subtraction increases, totaling approximately \$144,505 in fiscal 2006, \$149,111 in fiscal 2007, \$154,077 in fiscal 2008, and \$158,527 in fiscal 2009.

Additional Information

Prior Introductions: None.

Cross File: None.

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

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