

Department of Legislative Services
 Maryland General Assembly
 2007 Session

FISCAL AND POLICY NOTE

House Bill 410 (Delegate Kaiser, *et al.*)
 Ways and Means

Income Tax - Deduction for Qualified Tuition and Related Expenses

This bill provides an individual with additional State income tax deductions for qualified tuition and related expenses by conforming State law to the federal qualified tuition and related expenses deduction under Section 222 of the Internal Revenue Code (IRC).

The bill takes effect July 1, 2007 and applies to tax year 2007 and beyond.

Fiscal Summary

State Effect: General fund revenues would decrease by \$10.5 million in FY 2008 due to allowable subtractions for qualified tuition and related expenses. Revenues would not be affected in FY 2009 as the federal deduction is scheduled to expire after tax year 2007. Legislative Services advises, however, that the federal deduction has been extended each time it was previously scheduled to expire, meaning that revenues could decrease similarly in FY 2009 and beyond. Expenditures would not be affected.

(\$ in millions)	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
GF Revenue	(\$10.5)	\$0	\$0	\$0	\$0
Expenditure	\$0	\$0	\$0	\$0	\$0
Net Effect	(\$10.5)	\$0	\$0	\$0	\$0

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

Local Effect: Local income tax revenues would decrease by \$6.6 million in FY 2008. Expenditures would not be affected.

Small Business Effect: None.

Analysis

Current Law: The State is “decoupled” from the federal deduction for qualified tuition and related expenses. Taxpayers who claim the federal deduction are required to add back the amount deducted when calculating Maryland adjusted gross income (MAGI).

Background: For federal tax purposes, an above-the-line deduction for qualified tuition and related expenses is available for taxpayers in tax years 2002 through 2007 under Section 222 of the IRC. Qualified tuition and related expenses include tuition and fees required for the enrollment or attendance of the taxpayer, taxpayer’s spouse, or dependent, at an eligible institution of higher education. The amount of the deduction is limited depending on the taxpayer’s federal adjusted gross income and the tax year in which the deduction is claimed.

Specifically, in 2002 and 2003, the deduction is limited to \$3,000, and is only available to taxpayers with adjusted gross income not exceeding \$65,000 (\$130,000 for joint filers). Beginning in 2004, the maximum amount deductible increased to \$4,000 for taxpayers with adjusted gross income not exceeding \$65,000 (\$130,000 for joint filers). Taxpayers whose income exceeds that limit but does not exceed \$80,000 (\$160,000 for joint filers) may deduct up to \$2,000 in qualified expenses. Married individuals filing separately are not allowed to take the deduction. No deduction is allowed for any expense for which a deduction is otherwise allowed or with respect to an individual for whom a Hope credit or Lifetime Learning credit is claimed. The federal Tax Relief and Health Care Act of 2006 extended the deduction through tax year 2007.

The federal above-the-line deduction is available to a taxpayer regardless of whether the taxpayer itemizes. This deduction reduces federal adjusted gross income, which in turn reduces State taxes by flowing through to MAGI. The Budget Reconciliation and Financing Act of 2002 (Chapter 440) decoupled the State from the federal deduction.

State Revenues: Taxpayers would no longer be required to add back the amount of federal deduction claimed beginning in tax year 2007. As a result, general fund revenues could decrease by \$10.5 million in fiscal 2008.

This estimate is based on the total number of deductions claimed by federal taxpayers in 2002 through 2004 and on the estimated cost of the recent extension by the federal Joint Committee on Taxation. It is also based on the following facts and assumptions:

- 27.2% of Americans had at least a college degree in 2005 compared with 34.5% of Marylanders. Based on this, it is estimated that 2.4% of all federal returns claiming the deduction are from Maryland;

- based on the 2006 Maryland Higher Education Commission Data Book, it is assumed that the number of individuals claiming the deduction increases by 6.5% annually; and
- all taxpayers who claim the federal deduction have more MAGI than the amount of the federal deduction claimed.

Additional Information

Prior Introductions: HB 987 of 2005 and 2006, identical bills, received unfavorable reports from the House Ways and Means Committee.

Cross File: None.

Information Source(s): Maryland Higher Education Commission, Joint Committee on Taxation, Internal Revenue Service, U.S. Census Bureau, Department of Legislative Services

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