

Department of Legislative Services  
 Maryland General Assembly  
 2009 Session

FISCAL AND POLICY NOTE

House Bill 158 (Delegate Krebs, *et al.*)  
 Ways and Means

Fairness in Taxation for Retirees Act

This bill expands the existing State pension exclusion subtraction modification by allowing income from the following plans to be included within the subtraction modification allowed for retirement income: Individual Retirement Accounts and annuities under Section 408 of the Internal Revenue Code; Roth Individual Retirement Accounts under Section 408(a) of the IRC; Simplified Employee Pension under Section 408(K) of the IRC; and an ineligible deferred compensation plan under Section 457(F) of the IRC.

The bill takes effect July 1, 2009 and applies to tax year 2009 and beyond.

Fiscal Summary

**State Effect:** General fund revenues decrease by at least \$17.6 million in FY 2010, which represents the impact of one and one-half tax years. Future year revenues reflect annualization, the estimated number of eligible taxpayers, and additional amounts of income subtracted as provided by the bill. Expenditures are not affected.

(\$ in millions)	FY 2010	FY 2011	FY 2012	FY 2013	FY 2014
GF Revenue	(\$17.6)	(\$12.3)	(\$12.8)	(\$13.3)	(\$13.9)
Expenditure	0	0	0	0	0
Net Effect	(\$17.6)	(\$12.3)	(\$12.8)	(\$13.3)	(\$13.9)

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

**Local Effect:** Local income tax revenues decrease by \$11.1 million in FY 2010 and by \$8.8 million in FY 2014. Expenditures are not affected.

**Small Business Effect:** None.

## Analysis

**Current Law:** Maryland income tax law currently provides a pension exclusion subtraction modification for individuals who are at least 65 years old or who are totally disabled. Under this subtraction modification, up to a specified maximum annual amount of taxable pension income (\$24,000 for 2008) may be exempt from tax. The maximum exclusion allowed is indexed to the maximum annual benefit payable under the Social Security Act and is reduced by the amount of any Social Security payments received; this is known as the “Social Security offset.”

Given that Social Security benefits are exempt from Maryland income tax, even though they are partly taxable for federal income tax purposes, the Social Security offset works to equalize the tax treatment of individuals who receive their retirement benefits from different sources by reducing the amount of the allowable exclusion by the amount of Social Security benefits received.

Social Security benefits and benefits received under the Railroad Retirement Act are totally exempt from the Maryland income tax, even though they may be partly taxable for federal income tax purposes. In addition to the special treatment of Social Security and other retirement income, other income tax relief is provided to senior citizens regardless of the source of their income. Each individual age 65 and older is allowed a \$1,000 personal exemption in addition to the regular personal exemption allowed for all individuals; and can earn more income without being required to file taxes.

**State Fiscal Effect:** Additional amounts of income could be subtracted as provided by the bill beginning in tax year 2009. It is assumed that most taxpayers will adjust withholdings and estimated payments. As a result, fiscal 2010 revenues will decrease by both the change in tax year 2009 revenues and also by one-half of tax year 2010, resulting in a decrease of approximately \$17.6 million in fiscal 2010. This estimate is based on the following facts and assumptions:

- In tax year 2005, approximately 24,000 taxable returns filed by individuals over 65 years old had taxable distributions from an IRA/SEP but no pension income. The average distribution was \$18,000.
- The average pension exclusion in tax year 2005 was \$10,750.
- Based on an analysis of the March 2007 Current Population Survey, individuals with annuities would increase the total cost of the bill by about 2%.
- The average amount of 2005 distributions was decreased to reflect recent negative stock market returns.

This estimate does not include revenue losses from distributions from Section 457(F) deferred compensation plans, disabled individuals, and individuals who already receive a pension and would be able to subtract even more income under the pension exclusion due to additional types of qualifying retirement income provided by the bill. This additional revenue loss is likely to be significant. Revenue losses from Roth Individual Retirement Accounts would be minimal, as qualified distributions are not taxable for federal and State income tax purposes.

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### **Additional Information**

**Prior Introductions:** HB 999 of 2008 was not reported from the House Ways and Means Committee. In addition, HB 1162 of 2007 and HB 151 of 2005 were not reported from the House Ways and Means Committee.

**Cross File:** None.

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

**Fiscal Note History:** First Reader - February 3, 2009  
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