SB 400

Department of Legislative Services
2012 Session

FISCAL AND POLICY NOTE

Senate Bill 400 (Senator Pugh)
Budget and Taxation

Income Tax - Subtraction Modification - Health Improvement and Cost Savings Act of 2012

This bill creates a subtraction modification against the State income tax for qualified expenses related to fitness activities, tobacco cessation, and weight loss programs. The amount of the subtraction modification cannot exceed $1,500 ($750 for married couples filing separately). The Comptroller, in cooperation with the Department of Health and Mental Hygiene (DHMH), must administer the subtraction modification and adopt regulations that specify expenses eligible for the subtraction modification. The Comptroller and DHMH must report to the General Assembly by September 1, 2012, on the implementation of the bill.

The bill takes effect July 1, 2012, and applies to tax year 2013 and beyond.

Fiscal Summary

State Effect: General fund revenues will decrease significantly beginning in FY 2014 due to subtraction modifications claimed against the personal income tax. If 10% of taxpayers claim the maximum subtraction modification, State revenues will decrease by $15.7 million annually. Revenue losses could be significantly more. General fund expenditures increase by $22,000 in FY 2013 for one-time tax form changes and computer programming modifications at the Comptroller's Office.

Local Effect: Local revenues will decrease significantly beginning in FY 2014. Assuming that 10% of taxpayers claim the maximum subtraction modification, local revenues will decrease by $9.8 million annually. Expenditures are not affected.

Small Business Effect: Minimal.

Analysis

Bill Summary: The bill creates a subtraction modification against the State income tax for specified wellness-related expenses incurred by a taxpayer. Expenses that qualify include (1) qualified fitness expenses for the taxpayer, taxpayer's spouse, or adult dependent; (2) participation by the taxpayer, taxpayer's spouse, or dependent in a qualified tobacco cessation program or weight loss program; or (3) participation by a dependent child in a qualified physical activity program. The Comptroller, in cooperation with DHMH, must administer the subtraction modification and adopt regulations that specify the expenses eligible for the subtraction modification. The Comptroller and DHMH must report to the General Assembly by September 1, 2012, on the implementation of the bill.

The amount of the subtraction modification is limited to $500 for each type of qualifying expense incurred by the taxpayer, taxpayer's spouse, or taxpayer's dependent. This limit is increased to $750 if the qualified individual is at least 65 years old. The total value of the subtraction modification may not exceed $1,500 ($750 for a married individual filing a separate return).

Current Law: Maryland conforms to federal tax law regarding medical expenses. As discussed below, certain medical-related expenses can be deducted for federal income tax purposes, which typically results in a lower federal, State, and local income tax liability.

Background: Medical expenses under the Internal Revenue Code are defined as the costs of diagnosis, cure, mitigation, treatment, or prevention of disease, and the costs for treatments affecting any part or function of the body. They include the costs of equipment, supplies, and diagnostic devices needed for these purposes. Medical expenses must be primarily to alleviate or prevent a physical or mental defect or illness. Expenses that are beneficial to general health, such as vitamins or a vacation, do not qualify. Qualifying medical expenses may be deducted if an individual itemizes and is equal to the amount of medical expenses in excess of 7.5% of federal adjusted gross income. The cost of tobacco cessation programs may qualify for the deduction; the cost of weight-loss programs may also qualify for a deduction if it is a treatment for a specific disease diagnosed by a physician. In addition to the medical expenses deduction, individuals may opt to pay for certain medical expenses out of a health savings account or other tax-favored health plans.

According to the Centers for Disease Control and Prevention, chronic diseases – such as heart disease, stroke, cancer, diabetes, and arthritis – are among the most common, costly, and preventable of all health problems in the United States. Four modifiable health risk behaviors – lack of physical activity, poor nutrition, tobacco use, and excessive alcohol consumption – are responsible for much of the illness and early death related to chronic diseases. Research has identified the benefits of preventative care and behavior modification in reducing chronic disease incidence. Some employers and health care companies have instituted programs providing for the payment or reimbursement of costs associated with employee/member participation in healthy behavior and wellness programs.

State Revenues: Subtraction modifications may be claimed beginning in tax year 2013. Accordingly, general fund revenues will decrease significantly beginning in fiscal 2014. However, the amount of the revenue loss cannot be reliably estimated and depends on the type of expenses that qualify for the subtraction modification and the amount of individuals claiming the benefit. The U.S. Bureau of Labor and Statistics' Consumer Expenditure Survey provides information on consumer expenditures by class of expenditure but does not include enough detail to estimate the expenditures that will qualify under the bill. **Exhibit 1** shows the annual decrease in State and local revenues if a certain percentage of taxpayers claim the maximum subtraction modification in each tax year.

Exhibit 1
Potential Annual State and Local Revenue Decreases
($ in Millions)

Percent of Taxpayers	State	Local	Total
5%	$7.8	$4.9	$12.7
10%	15.7	9.8	25.5
25%	39.1	24.5	63.6

State Expenditures: The Comptroller's Office reports that it will incur a one-time expenditure increase of $22,000 in fiscal 2013 to add the subtraction modification to the personal income tax return. This includes data processing changes to the SMART income tax return processing and imaging systems and system testing.

Local Revenues: Local income tax revenues may decrease by about 3% of the total net subtraction modification claimed. Exhibit 1 illustrates the loss of local revenues depending on how many individuals claim the maximum subtraction modification.

Additional Information

Prior Introductions: SB 566 of 2011 received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Its cross file, HB 229, received a hearing in the House Ways and Means Committee, but no further action was taken. SB 1003 of 2010 received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Its cross file, HB 1105, received a hearing in the House Ways and Means Committee, but no further action was taken. HB 711 of 2009 received a hearing in the House Ways and Means Committee, but no further action was taken.

Cross File: None.

Information Source(s): U.S. Bureau of Labor Statistics, Comptroller's Office, Department of Legislative Services

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mc/jrb

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