SB 752

Department of Legislative Services

2012 Session

FISCAL AND POLICY NOTE

Senate Bill 752 (Senator Young, *et al.*)
Budget and Taxation

Income Tax - Subtraction Modification - Retirement Income

This bill expands the existing State pension exclusion subtraction modification for taxpayers who are at least 70 years of age or who qualify for the exclusion under current law due to a disability.

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

Fiscal Summary

State Effect: General fund revenues may decrease significantly beginning in FY 2013 due to additional pension income being exempted. Expenditures are not affected.

Local Effect: Local income tax revenues may decrease significantly beginning in FY 2013. Expenditures are not affected.

Small Business Effect: None.

Analysis

Bill Summary: The bill expands the existing State pension exclusion subtraction modification for taxpayers who are at least 70 years of age or who qualify for the exclusion under current law because of a disability.

It is assumed that the intent of the bill is to increase the maximum pension exclusion for qualifying individuals to (1) $33,000 in tax year 2012; (2) $40,000 in tax year 2013; (3) $47,000 in tax year 2014; (4) $54,000 in tax year 2015; (5) $61,000 in tax year 2016; (6) $68,000 in tax year 2017; and (7) $75,000 beginning in tax year 2018. The maximum exclusion amount is reduced by the amount of Social Security payments received as provided under current law.

Current Law\Background: Maryland law provides a pension exclusion (in the form of a 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 amount of taxable pension income ($26,300 for 2011) 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 (Social Security offset).

The "Social Security offset" is the reduction in the maximum pension exclusion allowed under current law for an individual. The Social Security offset was established at the same time as the pension exclusion. Given that Social Security benefits are exempt from Maryland income tax, the 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 any Social Security benefits received.

One significant feature of the current pension exclusion is that it is limited to income received from an "employee retirement system." Eligible employee retirement systems are retirement plans established and maintained by an employer for the benefit of its employees and qualified under sections 401(a), 403, or 457(b) of the IRC. These include defined benefit and defined contribution pension plans, 401(k) plans, 403(b) plans, and 457(b) plans. However, individual retirement arrangements (IRAs), Keogh plans, and simplified employee pension plans are not considered employee retirement systems.

In addition to the special treatment of Social Security and other retirement income, additional 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 also earn more income without being required to file taxes.

State Revenues: The bill expands the existing State pension exclusion subtraction modification beginning in tax year 2012 for taxpayers who are at least 70 years of age or who qualify for the exclusion under current law because of a disability. Accordingly, general fund revenues may decrease significantly beginning in fiscal 2013. However, the amount of the revenue loss cannot be reliably estimated and depends on the amount of additional pension income that would be exempted by qualified individuals.

Local Revenues: Local revenues decrease by approximately 3% of the total net State subtraction modification claimed.

Additional Information

Prior Introductions: None.

Cross File: None.

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

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