

Department of Legislative Services  
 Maryland General Assembly  
 2017 Session

FISCAL AND POLICY NOTE  
 Third Reader

House Bill 873  
 Ways and Means

(Delegates Carey and Lisanti)

Budget and Taxation

**Income Tax Credit - Security Clearances - Employer Costs - Extension**

This bill extends the termination date of the employer security clearance costs tax credit through tax year 2021.

The bill takes effect July 1, 2017.

**Fiscal Summary**

**State Effect:** General fund revenues decrease by \$1.6 million annually in FY 2019 through 2023 as a result of tax credits being claimed against the corporate and personal income tax. Transportation Trust Fund (TTF) revenues decrease by \$0.2 million annually and Higher Education Investment Fund (HEIF) revenues decrease by \$0.1 million annually in FY 2019 through 2023. Expenditures are not affected.

| (\$ in millions) | FY 2018 | FY 2019 | FY 2020 | FY 2021 | FY 2022 |
|------------------|---------|---------|---------|---------|---------|
| GF Revenue       | \$0     | (\$1.6) | (\$1.6) | (\$1.6) | (\$1.6) |
| SF Revenue       | \$0     | (\$0.3) | (\$0.3) | (\$0.3) | (\$0.3) |
| Expenditure      | 0       | 0       | 0       | 0       | 0       |
| Net Effect       | \$0.0   | (\$1.9) | (\$1.9) | (\$1.9) | (\$1.9) |

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

**Local Effect:** Local highway user revenues distributed from the corporate income tax decrease by \$19,300 annually in FY 2019 through 2023. Local income tax revenues increase by \$700 annually in FY 2019 through 2023 due to taxpayers adding back the amount of credits claimed against the personal income tax. Local expenditures are not affected.

**Small Business Effect:** Potential meaningful. Any small business that incurs eligible expenses will be positively impacted by the program's extension.

## Analysis

**Current Law/Background:** Chapter 478 of 2012 established the Employer Security Clearance Costs Tax Credit program. The program allows a tax credit against the State income tax for certain security clearance administrative expenses and for the construction and equipment costs to construct or renovate a sensitive compartmented information facility (SCIF) located in the State. To qualify, the security clearance administrative expenses must be incurred with regard to an employee in the State and include (1) processing application requests for clearances; (2) maintaining, upgrading, or installing computer systems in the State that are required for obtaining federal security clearances; and (3) training employees to administer the application process.

Chapter 482 of 2013 expanded the credit by specifying that expenses incurred for rental payments owed during the first year of a rental agreement for spaces leased in the State qualify for the credit, if the company qualifies as a small business and performs security-based contracting. A small business is a firm that (1) is independently owned and operated; (2) is not a subsidiary of another firm; (3) is not dominant in its field of operation; and (4) did not employ more than 25 individuals in its most recent fiscal year. Chapter 482 of 2013 also generally doubled the maximum value of the credit.

The amount of expenses that qualify for the credit are equal to (1) 100% of eligible security clearance administrative expenses, not to exceed \$200,000; (2) 100% of eligible rental payments, not to exceed \$200,000; and (3) 50% of eligible costs incurred to construct or renovate each SCIF, not to exceed \$200,000. If a company constructs and/or renovates multiple SCIFs, the total amount of aggregate expenditures that qualify for the credit is limited to \$500,000. If the total amount of the credit exceeds the tax liability imposed in the year, the excess can be carried forward to future tax years until the full amount of the excess is used. Businesses claiming the credit are required to add back to Maryland adjusted gross income or Maryland modified income the amount of expenses claimed under the credit.

The Department of Commerce is authorized to award a maximum of \$2.0 million in total credits each year, and credits may be claimed in tax years 2013 through 2016. If the amount of credits claimed in each year exceeds the maximum aggregate limit, the value of the credit is reduced based on the total amount of excess credits claimed. In tax year 2013, the Department of Commerce awarded credits to 40 businesses. The median credit awarded was \$33,734. Five companies received a credit of \$100,000 or greater, with these companies receiving about 40% of all credits. In tax year 2014, the Department of Commerce awarded \$2.0 million in credits to 48 businesses that claimed \$8.25 million in employer security clearance costs. The median credit awarded was \$22,638. Six companies received a credit of \$100,000 or greater, with these companies receiving almost 50% of all credits.

**State Revenues:** The bill extends the termination date of the employer security clearance costs tax credit through tax year 2021. The Department of Commerce can award a maximum of \$2.0 million in credits annually in tax years 2017 through 2021. As a result, general fund revenues decrease by \$1.6 million annually in fiscal 2019 through 2023. TTF revenues decrease by \$200,900 annually, of which \$181,600 goes to the State, and HEIF revenues decrease by \$82,600 annually in fiscal 2019 through 2023.

Before claiming the tax credit, the Department of Commerce must certify the amount of expenses incurred by the business. These expenses are certified on December 15 of the calendar year following the end of the taxable year in which the qualifying expenses occurred. A business must then file an amended return to claim the credit – it is assumed that this could be done beginning in fiscal 2019 and that companies do not adjust estimated payments.

The estimated revenue loss due to the expansion is based on the following facts and assumptions:

- the maximum amount of credits will be awarded in each tax year;
- 75% of credits are claimed against the corporate income tax, with the remaining amount claimed against the personal income tax;
- businesses have enough tax liability to claim the full credit; and
- any credit claimed is added back to Maryland adjusted gross income or Maryland modified income.

**Local Revenues:** Local highway user revenues distributed from the corporate income tax decrease by \$19,300 annually in fiscal 2019 through 2023. Local income tax revenues increase by \$700 in fiscal 2019 through 2023 due to taxpayers adding back the amount of credits claimed against the personal income tax.

**Small Business Impact:** Any small business that incurs eligible expenses could be positively impacted by the program's extension. In 2013, an estimated one-third of companies that were awarded the credit were small businesses. The credit received by these businesses ranged from \$5,100 to \$56,900.

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### **Additional Information**

**Prior Introductions:** A similar bill, SB 246 of 2016, received a hearing in the Senate Budget and Taxation Committee, but no further action was taken.

**Cross File:** SB 138 (Senators Manno and Miller) - Budget and Taxation.

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

**Fiscal Note History:** First Reader - February 10, 2017  
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