SB 650

Department of Legislative Services

Maryland General Assembly
2018 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 650 (Senator King, *et al.*)
Budget and Taxation

Income Tax Subtraction Modification - College Savings Plan Accounts - Contributions (College Savings Tax Enhancement Act)

This bill expands the existing college savings plan income tax subtraction modification by increasing from $2,500 to $5,000 the maximum value of the subtraction modification. In order to qualify for the increased subtraction modification, the taxpayer must have a federal adjusted gross income of $225,000 or less ($150,000 if single or married filing separately). **The bill takes effect July 1, 2018, and applies to tax year 2018 and beyond.**

Fiscal Summary

State Effect: General fund revenues decrease by $2.9 million annually beginning in FY 2019 as a result of additional subtraction modifications claimed against the personal income tax. Expenditures are not affected.

($ in millions)	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
GF Revenue	($2.9)	($2.9)	($2.9)	($2.9)	($2.9)
Expenditure	0	0	0	0	0
Net Effect	($2.9)	($2.9)	($2.9)	($2.9)	($2.9)

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

Local Effect: Local revenues decrease by $1.9 million annually beginning in FY 2019. Local expenditures are not affected.

Small Business Effect: None.

Analysis

Current Law:

Maryland 529 Plans

Qualified tuition plans, also known as 529 plans, are state programs that allow an individual to either prepay or contribute to an account established for paying a student's qualified education expenses at an eligible educational institution. The College Savings Plans of Maryland Board currently operates two qualified tuition plans: the Maryland Prepaid College Trust and the Maryland College Investment Plan. Chapter 548 of 2008 authorized the board to establish a third plan, the Maryland Broker-Dealer College Investment Plan, but the board has yet to do so.

State Subtraction Modification

A person may claim a subtraction modification for the advanced amount of tuition payments made to the Maryland Prepaid College Trust or amount contributed to the Maryland College Investment Plan. The subtraction modification claimed by a taxpayer may not exceed $2,500 for each contract purchased (Maryland Prepaid College Trust) or $2,500 per beneficiary (Maryland College Investment Plan). This limitation is increased to $5,000 for married individuals who file jointly.

Any unused amount of the subtraction modification can be carried forward to future tax years until the full amount of the excess is used under the Maryland Prepaid College Trust and up to 10 tax years for contributions to the Maryland College Investment Plan.

Exhibit 1 shows the number of resident tax returns that claimed the subtraction modification in tax year 2014 by federal adjusted gross income, the percentage of all returns that claimed the subtraction modification, and the average deduction claimed.

Exhibit 1
College Savings Plans Subtraction Modification
Tax Year 2014

		Claimed Either Benefit		
FAGI	**Total Tax Returns**	**Number**	**% of All Returns**	**Average Claim**
Less than $25,000	1,032,398	598	0.1%	$2,893
$25,001-$100,000	1,400,308	8,376	0.6%	2,780
$100,001-$200,000	500,515	26,124	5.2%	3,743
$200,001-$500,000	157,246	20,064	12.8%	5,636
Over $500,000	34,077	4,277	12.6%	8,053
Total	**3,124,544**	**59,439**	**1.9%**	**$4,499**

FAGI: federal adjusted gross income

Note: Tax returns (total and those claiming the subtraction modification) reflect resident tax returns only.

Source: Comptroller's Office; Department of Legislative Services

An investment account holder is not eligible for the subtraction modification for contributions to an investment account in any year in which the account holder receives funds under the State Contribution Program described below.

State Contribution Program

The College Affordability Act of 2016 (Chapters 689 and 690) established a State matching contribution of $250 per beneficiary for new Maryland College Investment Plan accounts. For investment accounts established under the plan after December 31, 2016, a State matching contribution may be made to an investment account if:

- the qualified beneficiary of the investment account is a Maryland resident;
- the account holder submits an application to the board or its designee between January 1 and June 1 of each year; and
- the account holder has Maryland taxable income or $112,500 or less ($175,000 for a married couple filing a joint return).

A minimum contribution is necessary to receive a State matching contribution and ranges from $25 to $250, depending on the taxpayer's Maryland taxable income.

Background:

Federal Tax Benefits and 529 Plans

The U.S. Congress enacted legislation in 1996 and 2001 establishing federal tax advantages for qualified education savings accounts. Contributions are not deductible for federal tax purposes; however, amounts deposited in the account grow tax free and distributions are not subject to federal or state taxes if the distributions are used for qualified education expenses. These tax advantages are similar to the federal tax treatment of Roth IRAs. Account withdrawals could be used to pay for eligible expenses at institutions of higher education.

Recent federal tax legislation altered 529 plans by allowing an account holder to withdrawal up to $10,000 for enrollment or attendance of the designated beneficiary at a public, private, or religious elementary or secondary school. This limitation applies to each child rather than a per account basis.

State Revenues: The bill expands the existing college savings plan income tax subtraction modification by increasing from $2,500 to $5,000 the maximum value of the subtraction modification for a taxpayer who has a federal adjusted gross income of $225,000 or less ($150,000 if individual or married filing separately). As a result, general fund revenues may decrease by $2.9 million annually beginning in fiscal 2019.

This estimate is based on the following facts and assumptions:

- in tax year 2014, 9,500 tax returns that claimed the maximum subtraction modification of $2,500 met the bill's income requirements;
- these returns claimed approximately 20,800 subtraction modifications;
- each of these tax returns will be able to subtract on average an additional $2,250 of the maximum additional $2,500;
- taxpayers who claim the maximum subtraction modification currently carry forward and claim 3% of the excess in each tax year following the year in which the eligible contribution is made;
- future year contributions increase by 2% annually; and
- taxpayers elect to claim the increased subtraction modification in lieu of receiving a State matching contribution.

In addition, revenue losses in each year are increased to account for recent federal legislation that expands 529 eligibility to certain K-12 schools.

Local Revenues: Local income tax revenues will decrease as a result of additional subtraction modifications claimed against the personal income tax. Local revenues will decrease by $1.9 million annually beginning in fiscal 2019.

Additional Information

Prior Introductions: None.

Cross File: Although designated as a cross file, HB 131 (Delegate Korman – Ways and Means) is not identical.

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

Fiscal Note History: First Reader - February 25, 2018
mm/hlb

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