

Department of Legislative Services
 Maryland General Assembly
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FISCAL AND POLICY NOTE
 First Reader

House Bill 1711 (Delegate Kipke)

Ways and Means and Health and
 Government Operations

**Income Tax - Subtraction Modification for Higher Education Expenses and
 ABLE Account Contributions - Annual Limitation**

This bill expands the existing college savings plan and ABLE account income tax subtraction modifications by increasing from \$2,500 to \$4,000 the maximum value of the subtraction modification. **The bill takes effect July 1, 2018, and applies to tax year 2018 and beyond.**

Fiscal Summary

State Effect: General fund revenues decrease by \$3.5 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	(\$3.5)	(\$3.5)	(\$3.5)	(\$3.5)	(\$3.5)
Expenditure	0	0	0	0	0
Net Effect	(\$3.5)	(\$3.5)	(\$3.5)	(\$3.5)	(\$3.5)

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

Local Effect: Local revenues decrease by \$2.2 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 Maryland 529 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.

The Stephen Beck, Jr., Achieving a Better Life Experience Act of 2014 established a new § 529A of the Internal Revenue Code that permits a state (or a state agency or instrumentality) to establish and maintain a new type of tax-advantaged savings program, a qualified ABLE program, under which contributions may be made to an account that is established for the purpose of meeting the qualified disability expenses of the designated beneficiary of the account.

Eligibility is limited to individuals with significant disabilities for whom the onset of the disability occurred prior to age 26. Total annual contributions are generally limited to the amount allowed for tax-free gifts, and assets over \$100,000 in an account count toward eligibility for Social Security supplemental income.

Chapter 39 of 2016 required the Maryland 529 Board, in consultation with the Maryland Department of Disabilities, to establish, administer, manage, and promote the Maryland ABLE Program. The Act implemented recommendations of a State task force established in 2015. The program began accepting applicants in late November 2017, and as of January 19, 2018, had 216 accounts with a combined \$1.2 million in assets (\$5,379 on average).

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 or ABLE account. 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 or ABLE account). 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 or ABLE account.

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

<u>FAGI</u>	<u>Total Tax</u>	Claimed Either Benefit		
	<u>Returns</u>	<u>Number</u>	<u>% of All</u>	<u>Returns</u>
				<u>Average</u>
				<u>Claim</u>
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 of \$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 and ABLE account income tax subtraction modifications by increasing from \$2,500 to \$4,000 the maximum value of the subtraction modification. As a result, general fund revenues may decrease by \$3.5 million annually beginning in fiscal 2019.

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 \$2.2 million annually beginning in fiscal 2019.

Additional Information

Prior Introductions: None.

Cross File: None.

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

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