HB 463

Department of Legislative Services

Maryland General Assembly
2018 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 463 (Delegate Morales, *et al.*)
Ways and Means

Income Tax - Subtraction Modification - First-Time Homebuyer Savings Accounts

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This bill allows a taxpayer to designate an account with a financial institution as a first-time homebuyer savings account. An eligible account holder may claim a subtraction modification for (1) the amount contributed, up to $5,000, during the taxable year to a designated account and (2) the earnings, including interest and other income on the principal, from the designated account during the tax year. The subtraction modification may be claimed for up to 10 years and for a maximum earnings amount of $50,000 during the 10-year period. **The bill takes effect July 1, 2018, and applies to tax year 2018 and beyond.**

Fiscal Summary

State Effect: General fund revenues decrease beginning in FY 2019 due to eligible contributions and earnings being claimed against the State income tax. Based on similar programs in other states, general fund revenues may decrease by $50,000 in FY 2019 and by $200,000 in FY 2023. General fund expenditures increase by $169,200 in FY 2019 due to implementation costs at the Comptroller's Office.

(in dollars)	FY 2019	FY 2020	FY 2021	FY 2022	FY 2023
GF Revenue	($50,000)	($75,000)	($125,000)	($150,000)	($200,000)
GF Expenditure	$169,200	$71,300	$73,500	$76,100	$78,900
Net Effect	($219,200)	($146,300)	($198,500)	($226,100)	($278,900)

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

Local Effect: Local revenues decrease by $32,000 in FY 2019 and by $126,000 in FY 2023. Local expenditures are not affected.

Small Business Effect: Minimal.

Analysis

Bill Summary: The bill allows a taxpayer to designate an account with a financial institution as a first-time homebuyer savings account (designated account). The taxpayer may make this designation for the sole purpose of paying or reimbursing eligible costs for the purchase of a home in the State by a qualified beneficiary. A qualified beneficiary is an individual, including an account holder, who purchases a single-family home as a principal residence in the State and (1) has not owned or purchased, either individually or jointly, a home in the State in the last seven years and (2) is designated as the beneficiary of a first-time homebuyer savings account. An account holder is an individual who establishes, individually or jointly with other individuals, a designated account. Eligible costs include the down payment and eligible closing costs for the purchase of a single-family home by a qualified beneficiary.

An account holder may claim a subtraction modification for (1) the amount contributed, up to $5,000, during the tax year to a designated account and (2) the earnings, including interest and other income on the principal, from the designated account during the tax year. The subtraction modification may be claimed for up to 10 years and for a maximum earnings amount of $50,000 during this 10-year period.

In order to continue to qualify for the subtraction modification, the principal and earnings must remain in a designated account until the beneficiary purchases an eligible home, unless the earnings and principal are rolled over into another designated account. A person other than an account holder who transfers money into the designated account may not claim the subtraction modification. The account holder is required to use the funds in the designated account within 15 years following the date on which the account was established. At the end of the 15-year period, the remaining funds are subject to taxation as ordinary income under certain circumstances.

If the account holder withdraws any funds from the account for an ineligible purpose, the funds are taxed as ordinary income and the account holder is subject to a 10% penalty unless the account holder has filed for bankruptcy protection. A financial institution may not be held responsible for the use or application of funds deposited in or withdrawn from the account and may use designated account funds to pay administrative costs.

A taxpayer claiming the subtraction modification must submit specified information to the Comptroller. The Comptroller must adopt regulations to implement the bill.

Current Law/Background: No similar State income tax subtraction modification exists.

Federal income tax law provides several benefits to promote home ownership. These include itemized deductions for eligible real estate taxes paid and qualified home mortgage interest and mortgage insurance premiums paid.

To pay for a house down payment, homebuyers may withdraw up to $10,000 from a Roth Individual Retirement Account (IRA) or standard IRA if certain conditions are met. Withdrawals from a Roth IRA account are not subject to taxation. Homeowners can also withdraw money from a 401(K), subject to a potential 10% penalty, or borrow against the value of the account.

Numerous federal, State, and local programs provide home down payment assistance. These include federal reduced down payment loan programs through the U.S. Federal Housing Administration, U.S. Department of Veterans Affairs, and the U.S. Department of Agriculture. State programs include the Down Payment Assistance and Partner Match Programs. Local programs include Montgomery County's Moderately Priced Dwelling Unit Program.

Colorado, Iowa, Minnesota, Mississippi, Montana, and Virginia have established similar first-time homebuyer savings account programs. New York recently enacted legislation establishing a program, but its implementation has been delayed by the governor in order to conduct a detailed analysis of the program's fiscal and economic impacts.

State Revenues: Subtraction modifications can be claimed beginning in tax year 2018. As a result, general fund revenues will decrease beginning in fiscal 2019. The amount of the revenue loss depends on the number of designated accounts established, the amount contributed to each account, and the eligible earnings that can be exempted from the State income tax. Contributions and earnings will generally be subject to federal taxation.

Based on the estimated amounts contributed to similar programs in other states and adjusted for differences in population and housing, general fund revenues may decrease by $50,000 in fiscal 2019. Revenue losses will increase as additional individuals participate and deduct eligible earnings and may total $200,000 by fiscal 2023. State revenue losses will continue to increase as the number of participants grows over time. In addition, the Department of Legislative Services notes that revenue losses could be significantly greater than estimated. State law provides tax benefits for the eligible contributions made to a college savings plan – it is estimated these tax benefits reduce State revenues by $16.0 million annually.

State Expenditures: The Comptroller's Office advises that it will incur additional costs beginning in fiscal 2019 as a result of hiring one revenue examiner and incurring programming expenses. As a result, general fund expenditures increase by $169,200 in fiscal 2019, which reflects a January 1, 2019 hiring date. It includes a salary, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Position	1
Salary and Fringe Benefits	$35,950
Operating Expenses	5,203
Programming Expenditures	128,000
Total FY 2019 Expenditures	**$169,153**

Future year expenditures reflect a full salary with annual increases and employee turnover as well as ongoing operating expenses.

Local Revenues: Local income tax revenues decrease by about 3% of the total net State subtraction modifications claimed in each taxable year. Under the assumptions above, local income tax revenues may decrease by $32,000 in fiscal 2019, $47,000 in fiscal 2020, $79,000 in fiscal 2021, $95,000 in fiscal 2022, and by $126,000 in fiscal 2023.

Additional Information

Prior Introductions: HB 230 of 2017 received a hearing in the House Ways and Means Committee, but no further action was taken. SB 372 of 2015 received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Its cross file, HB 953, received a hearing in the House Ways and Means Committee, but no further action was taken.

Cross File: SB 972 (Senator Manno, *et al.*) - Budget and Taxation.

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

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Analysis by: Robert J. Rehrmann

Direct Inquiries to:
(410) 946-5510
(301) 970-5510