

Department of Legislative Services
 Maryland General Assembly
 2019 Session

FISCAL AND POLICY NOTE
 First Reader

House Bill 104 (Delegate Malone)
 Ways and Means and Appropriations

**Income Tax - Subtraction Modification for Qualified Higher Education Expenses
 - Annual Limitation**

This bill expands the existing Maryland Prepaid College Trust income tax subtraction modification by increasing from \$2,500 to \$5,000 the maximum value of the subtraction modification. **The bill takes effect July 1, 2019, and applies to tax year 2019 and beyond.**

Fiscal Summary

State Effect: General fund revenues decrease by \$4.6 million in FY 2020 as a result of additional subtraction modifications claimed against the personal income tax. Future year revenues reflect the estimated amount of eligible contributions. Expenditures are not affected.

(\$ in millions)	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024
GF Revenue	(\$4.6)	(\$4.7)	(\$4.9)	(\$5.0)	(\$5.2)
Expenditure	0	0	0	0	0
Net Effect	(\$4.6)	(\$4.7)	(\$4.9)	(\$5.0)	(\$5.2)

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

Local Effect: Local revenues decrease by \$2.9 million in FY 2020 and by \$3.2 million in FY 2024. 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

FAGI	Total Tax Returns	<u>Claimed Either Benefit</u>		
		<u>Number</u>	<u>% of All Returns</u>	<u>Average 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 plan 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.

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. The Maryland Prepaid College Trust currently operates plans for 12 institutions under the University System of Maryland, Morgan State University, and St. Mary's College of Maryland.

State Revenues: The bill expands the existing Maryland Prepaid College Trust income tax subtraction modification by increasing from \$2,500 to \$5,000 the maximum value of the subtraction modification. As a result, general fund revenues may decrease by an estimated \$4.6 million in fiscal 2020. **Exhibit 2** shows the projected State and local revenue loss from increasing the maximum value of the subtraction modification.

Exhibit 2
Projected State and Local Revenue Loss
(\$ in Millions)

	<u>FY 2020</u>	<u>FY 2021</u>	<u>FY 2022</u>	<u>FY 2023</u>	<u>FY 2024</u>
State	(\$4.6)	(\$4.7)	(\$4.9)	(\$5.0)	(\$5.2)
Local	(2.9)	(3.0)	(3.0)	(3.1)	(3.2)
Total Revenues	(\$7.5)	(\$7.7)	(\$7.9)	(\$8.2)	(\$8.4)

Local Revenues: Local income tax revenues decrease by about 3% of the total net State subtraction modifications claimed. Local revenues will decrease by \$2.9 million in fiscal 2020 and by \$3.2 million in fiscal 2024, as shown in Exhibit 2.

Additional Information

Prior Introductions: HB 1663 of 2018 received a hearing in the House Ways and Means Committee, but no further action was taken.

Cross File: SB 108 (Senator Reilly) - Budget and Taxation.

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

Fiscal Note History: First Reader - February 5, 2019
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