Department of Legislative Services

Maryland General Assembly
2021 Session

FISCAL AND POLICY NOTE
Third Reader

Senate Bill 779 (Senator Elfreth, *et al.*)

Budget and Taxation Appropriations

Maryland 529 Program – Board Authority and State Contribution – Alterations

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This bill modifies and adds requirements for receiving a State contribution within the Maryland Senator Edward J. Kasemeyer College Investment Plan. Specifically, the bill requires an account holder under the State Contribution Program to be a resident of Maryland and file income taxes on or before July 15 of each year. The bill also alters the income measurement of account holders for program eligibility from Maryland *taxable* income to Maryland *adjusted gross* income. A qualified beneficiary must be younger than age 26 in the calendar year before the account holder submits an application to receive a State contribution. The bill also establishes a $9,000 cap on the State contribution amount received over the lifetime of an account holder. Finally, the bill authorizes the Maryland 529 Board to aggregate and distribute administrative fees across all Maryland 529 programs. **The bill takes effect July 1, 2021.**

Fiscal Summary

State Effect: General fund expenditures likely decrease beginning in FY 2023; however, the reduction depends on the extent to which program eligibility restricts total State contributions as discussed below. State agencies can implement the bill's changes with existing resources. Maryland 529 fee revenues decrease to the extent fewer account holders and beneficiaries are eligible for the contribution program.

Local Effect: None.

Small Business Effect: None.

Analysis

Current Law: The Maryland 529 Board currently operates two qualified tuition plans: a prepaid plan and an investment plan. State income tax deductions are available independently for both plans, generally for up to $2,500 per year. Investment accounts established after December 31, 2016, are also eligible for a State matching contribution under specified conditions, as described below. An investment account holder may not claim an income tax deduction in the same year that a State match is received.

Generally, funds in the plans may only be used for qualified education expenses, which historically meant certain expenses related to higher education. However, under the federal Tax Cuts and Jobs Act of 2017, the investment plan may be used to pay for tuition expenses at K-12 public, private, and parochial schools.

State Matching Contributions

For 529 investment accounts established after December 31, 2016, a State contribution of $250 or $500, depending on income, may be made to an investment account if:

- the *qualified beneficiary* of the investment account is a Maryland resident;
- the account holder (for example, a parent) submits an application to the 529 Board or its designee between January 1 and June 1 of each year; and
- the account holder has Maryland *taxable* income in the previous taxable year no greater than $112,500 for an individual or $175,000 for a married couple filing a joint return.

A minimum amount of funds must be deposited into the investment account by the account holder in order to receive a State match, which is received by the end of the calendar year. Minimum contributions increase with income as the State match decreases. Chapter 538 of 2020 limited a qualified beneficiary to two State matching contributions per year beginning for application periods after December 31, 2020.

The Governor must provide at least $3.0 million each fiscal year for matching contributions. If the amount of funding is insufficient to fully fund all contributions, the 529 Board must prioritize awards based on the order in which the applications are received and for account holders who did not receive a contribution in any prior year.

State Expenditures: Since fiscal 2019, the cost to fund eligible applications has exceeded the $3.0 million mandated appropriation for State matching contributions. For fiscal 2021, a total of $12.5 million (including a $2.4 million deficiency appropriation) is budgeted to fully fund eligible applications. The Governor's proposed fiscal 2022 budget includes

$10.1 million. Although not required, since the program began (in fiscal 2018), it has provided a match for all eligible applicants and, if demand exceeded appropriated funding in a fiscal year, a deficiency appropriation was provided.

The bill's changes to residency requirements and age restrictions will reduce the number of accounts eligible for State contributions. The income requirement change from Maryland taxable income to Maryland adjusted gross income would, in many cases, also restrict eligibility. The total amount of Maryland adjusted gross income is often greater than the total amount of Maryland taxable income for taxpayers at the margins of eligibility (*i.e.,* an individual with taxable income less than $112,000, but adjusted gross income greater than $112,000). The more individuals who fall out of eligibility because of these restrictions, the greater the potential expenditure reduction. Finally, to the extent individuals would receive more than $9,000 in total State matching contributions, expenditures decrease by the difference between potential matching contributions and the $9,000 cap across however many account holders would exceed that cap.

The total impact on State general fund expenditures cannot be reliably estimated, but it is likely a significant decrease in expenditures above the mandated appropriation level beginning in fiscal 2023. Although the bill has a July 1, 2021 effective date, it is assumed that the changes do not apply to 2021 applications, which are due between January 1 and July 1, and that the changes would apply beginning with applications *received after December 31, 2021*.

Additional Information

Prior Introductions: None.

Designated Cross File: HB 1238 (Delegate Forbes) - Appropriations.

Information Source(s): Comptroller's Office; College Savings Plans of Maryland; Department of Legislative Services

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