

Department of Legislative Services
 Maryland General Assembly
 2023 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 1290 (Delegate Forbes)
 Appropriations

Higher Education - Maryland 529 Program - Reform

This emergency bill transfers administration of the Maryland 529 Program from the Maryland 529 Board to the State Treasurer, abolishes the Maryland 529 Board effective June 1, 2023, and makes conforming changes to specify that the State Treasurer must perform all duties previously performed by the board. The bill also phases out the Maryland Senator Edward J. Kasemeyer Prepaid College Trust (MPCT) by establishing that, beginning June 1, 2023, no new MPCT accounts may be created, either directly or via rollover. Finally, the bill establishes the Workgroup on the Maryland 529 Prepaid College Trust Program, with an associated report due to the Governor and the General Assembly by June 1, 2024.

Fiscal Summary

State Effect: Beginning in FY 2023, nonbudgeted revenues and expenditures associated with program operations shift to the State Treasurer’s Office (STO), with a likely reduction in revenues and expenditures due to the phase out of MPCT. Likewise, related general fund expenditures shift to STO. STO general fund expenditures also increase by \$336,100 in FY 2024 and \$146,900 in FY 2025 for contractual staff to help phase out MPCT; additional expenditures to enhance program administration are likely incurred. The requirement for interest payments to accounts rolled over, as specified, may increase State general fund expenditures. Additional other, likely minimal, impacts are also discussed below.

(in dollars)	FY 2023	FY 2024	FY 2025	FY 2026	FY 2027
NonBud Rev.	(-)	(-)	(-)	(-)	(-)
GF Expenditure	-	\$336,100	\$146,900	-	-
NonBud Exp.	(-)	(-)	(-)	(-)	(-)
Net Effect	(-)	(-)	(-)	(-)	(-)

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

Local Effect: Local revenues may minimally increase from foregone income tax deductions for contributions to MPCT accounts, as discussed below. Expenditures are unaffected.

Small Business Effect: None.

Analysis

Bill Summary:

Maryland 529 Program Transfer

The bill transfers the Maryland 529 Program, including all administrative facets of MPCT, the Maryland Senator Edward J. Kasemeyer College Investment Plan (MCIP) and related State matching contributions, the Maryland Achieving a Better Life Experience (ABLE) Program, and the statutorily authorized but unestablished Maryland Broker-Dealer College Investment Plan from the Maryland 529 Board to the State Treasurer.

On June 1, 2023, the Maryland 529 Board is abolished, and the State Treasurer – as the successor of the board – assumes fiduciary duties and responsibility for administering the Maryland 529 Program. Additionally, all appropriations, including State and federal funds held by agencies and units of the State to carry out the functions, programs, and services transferred under the bill are transferred to STO. The transfer includes all employees, functions, powers, duties, books and records, real and personal property, equipment, fixtures, assets, liabilities, obligations, credits, rights, and privileges of Maryland 529. All employees transferred to STO must be transferred without diminution of their rights, benefits, employment, or retirement status. Any transaction affected by the transition remains valid after the transition.

All existing laws, regulations, and other mandates or responsibilities continue in effect and are legally binding on the State Treasurer until otherwise ended. Any regulations adopted by the Maryland 529 Board prior to June 1, 2023, continue to be in force and effect unless otherwise altered by the State Treasurer.

The bill also gives the State Treasurer additional responsibilities beyond the responsibilities of the board under current law. Specifically, the bill authorizes the State Treasurer to administer oaths, take testimony, and subpoena witnesses and books, records, and other documents in administering Maryland 529. Part of the bill's transfer includes the responsibility for producing an annual audit report, for which the bill also removes the discretion to submit the annual audit report in combination with any other audit or report for the same fiscal year required by the General Assembly. The bill further enumerates

additional responsibilities beyond those of the Maryland 529 Board under current law related specifically to the wind down of MPCT, as described below.

Phase-out of the Maryland Senator Edward J. Kasemeyer Prepaid College Trust

Beginning June 1, 2023, the State Treasurer may not establish prepaid contracts under MPCT nor may any account holder enter into new prepaid contracts under MPCT. Also beginning June 1, 2023, the State Treasurer may not allow the transfer of funds from any other qualified State tuition program into an MPCT account.

Although no new MPCT accounts may be opened on or after June 1, 2023, the State Treasurer must still allow accounts to be rolled over from MPCT and transferred to any other qualified tuition program if done by December 31, 2024. Accordingly, the State Treasurer may not allow the transfer of funds from MPCT to any other qualified State tuition program beginning January 1, 2025. As part of the rollover process, the State Treasurer must grant an interest payment to an account holder who rolls their account over into MCIP (and adopt regulations to determine the interest rate). The balance of an MPCT account following this distribution must be an accurate allocation of the principal and earnings of that account and may not be considered a contribution to the account for the purposes of State income taxes.

Workgroup on the Maryland 529 Prepaid College Trust

The bill establishes the Workgroup on the Maryland 529 Prepaid College Trust Program to identify policies, procedures, and practices that led to issues relating to the earnings calculation formula and Maryland 529 account holders' inability to access their prepaid college trust benefits to pay for college expenses. The workgroup must also develop and make recommendations for improvement of Maryland 529 in specified areas. STO must staff the workgroup. A member of the workgroup may not receive compensation but is entitled to reimbursement for expenses under standard State travel regulations. The workgroup must report its findings and recommendations to the Governor and the General Assembly by June 1, 2024.

Financial Education and Capability Commission

The bill alters the membership of the Financial Education and Capability Commission to require the Executive Director of Maryland 529, rather than a Maryland 529 Board member to serve on the commission.

Conforming Changes

The bill requires that the publisher of the Annotated Code of Maryland, in consultation with and subject to the approval of the Department of Legislative Services (DLS), correct, with no further action required by the General Assembly, cross-references and terminology rendered incorrect by the bill. Any corrections made must be adequately described in an editor's note following the affected section.

Current Law:

Maryland 529

The Maryland 529 Board consists of 11 members, 6 of whom serve by virtue of the State office they hold: the State Treasurer; the State Comptroller; the Secretary of Higher Education; the State Superintendent of Schools; the Chancellor of the University System of Maryland; and the Secretary of Disabilities. The other 5 members are appointed by the Governor.

Maryland 529 currently offers three savings plans: one savings plan for individuals with disabilities; and two savings plans for higher education expenses. The savings plan for individuals with disabilities is the Maryland ABLE Program, which allows certain individuals with disabilities to save for qualified disability expenses. Of the two savings plans for higher education, one is a defined benefit plan called MPCT, and the other is an investment plan called MCIP. 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. Both higher education savings plans (MPCT and MCIP) are also known as 529 plans after the section in the Internal Revenue Code that allows an individual to either prepay or contribute to an account established for paying a student's qualified education expenses at an eligible educational institution.

As of fiscal 2022, MPCT had 27,683 total accounts with 1,152 new enrollments that fiscal year, representing a total of \$1.1 billion in investment holdings by MPCT. As of fiscal 2022, MCIP had 270,482 total beneficiaries with 37,567 new accounts opened that fiscal year for a total of \$7.8 billion in investment holdings. As of fiscal 2022, Maryland ABLE had 4,937 total beneficiaries with total assets under management of \$50.5 million.

State income tax deductions are available independently for both qualified tuition plans (MPCT and MCIP) and ABLE accounts, generally for up to \$2,500 per year. MCIP 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.

Maryland Senator Edward J. Kasemeyer Prepaid College Trust

MPCT allows interested persons, on behalf of a child, to prepay the cost of higher education tuition and mandatory fees by purchasing a contract based on the current weighted average tuition and mandatory fees at Maryland public institutions of higher education, the selected payment plan, the number of years until the child enters college, and other factors.

Each account holder enters into a contract with the trust for prepayment of tuition and mandatory fees for a specified number of years of community college and/or semesters or years of university tuition. Payments may be made in single, monthly, or annual installments. For a child enrolled in a Maryland public institution of higher education, the trust will pay the full in-state tuition and mandatory fees. If a child attends an eligible private or out-of-state institution of higher education, the trust will pay up to the calculated weighted average tuition of the tuition plan selected or the calculated minimum benefit, whichever is greater. Calculated minimum benefits are generally the amount paid into the account, less any operating fees plus a certain rate of return.

Maryland Senator Edward J. Kasemeyer College Investment Program

MCIP allows contributions to an investment account established to provide for tuition, fees, books, supplies, equipment, and room and board for a designated beneficiary. Under the plan, participants accept a level of investment based on their selected investment option. Account values in the investment plan are based solely on contributions and investment performance and are not guaranteed by the State.

The plan began in December 2001 and is open to children or adults of any age. Enrollment is open year-round, and investors may choose how much and how often they wish to contribute. Contributions and investment earnings are available for eligible higher education expenses, including tuition, fees, room and board, and other expenses as defined by Section 529 of the Internal Revenue Code. In 2017, the U.S. Congress passed a new tax reform measure that expanded eligible costs for 529 plans to distributions of up to \$10,000 per beneficiary per year for tuition at elementary or secondary public, private, or religious schools; trade/technical schools; or certified apprenticeship programs.

Maryland College Investment Plan 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 younger than age 26 in the calendar year before the account holder submits an application;
- the account holder is at least 18 years old for applications filed on or after January 1, 2022;
- the account holder (for example, a parent) is also a resident of Maryland and files income taxes on or before July 15 of each year;
- the account holder submits an application to the Maryland 529 Board or its designee between January 1 and June 1 of each year; and
- the account holder has Maryland adjusted gross 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. Chapters 435 and 436 of 2021 established a \$9,000 cap on the State contribution amount received over the lifetime of an account holder.

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 Maryland 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.

Maryland Achieving a Better Life Experience Program

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 another 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. 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. State programs must adhere to minimum federal guidelines to be considered qualified ABLE programs under federal law. Individuals with disabilities for whom the onset of the disability occurred prior to age 26 are considered “eligible individuals” under Internal Revenue Service (IRS) regulations. Eligible individuals who establish an ABLE account and are the owner of such account are “designated beneficiaries” under IRS regulations.

Maryland Broker-Dealer College Investment Plan

In 2008, the Maryland 529 Board was given the authority to establish a Maryland Broker-Dealer College Investment Plan, which would allow Maryland families who invest through private investment advisors to participate in a Maryland college savings plan; however, the Maryland 529 Board has not implemented a broker-dealer plan.

Financial Education and Capability Commission

Chapters 519 and 520 of 2012 created the Financial Education and Capability Commission to (1) monitor the implementation of public and private initiatives to improve the financial education and capability of residents of the State and (2) make recommendations on the coordination of financial education and capability efforts across State agencies. The commission is required to annually report to the Governor and the General Assembly, by December 1, on its recommendations and the status of the State's efforts to improve the financial education and capability of residents of the State. The Maryland Creating Assets, Savings, and Hope Campaign provides staff for the commission.

State Fiscal Effect:

Maryland 529 Program Transition

This analysis assumes that, consistent with the bill's uncodified language, the transfer of Maryland 529 Program responsibilities and the repeal of the Maryland 529 Board occur on June 1, 2023. To the extent provisions of the bill relating to the transfer of responsibility for the Maryland 529 Program take effect earlier than that, upon enactment consistent with the bill's emergency status, significant additional expenditures are required to expedite the program transfer. The initial year of fiscal impact remains fiscal 2023 under either set of assumptions.

Maryland 529 Board nonbudgeted revenues and expenditures decrease and STO nonbudgeted revenues and expenditures correspondingly increase beginning in fiscal 2023 to reflect the transfer of the program and its associated operating costs. In addition, general funds budgeted to the Maryland Higher Education Commission (MHEC) to support administration of the ABLE Program are likewise transferred to STO as early as fiscal 2023. The exact amount of nonbudgeted and general funds related to the administration of Maryland 529 (including the ABLE Program) to be transferred (on June 1, 2023, or before) is unknown; however, the total fiscal 2023 appropriation reflects \$6.3 million in nonbudgeted operating expenditures to administer MPCT and MCIP and \$453,539 in partially nonbudgeted (\$109,392), partially State general fund expenditures (\$344,157) for the Maryland ABLE Program. Along with the funds, 15 regular full-time

employees and 2.24 full-time equivalent contractual employees of Maryland 529 employed as of fiscal 2023 are transferred to STO.

This analysis assumes that, for fiscal 2024 and beyond, the general fund support budgeted for the Maryland ABLÉ Program (\$300,000 for fiscal 2024) and nonbudgeted revenues from fees assessed account holders (estimated at \$5.5 million for fiscal 2024) continue to support the operating expenditures for Maryland 529 administration once it is transferred to STO. This estimate assumes that the physical offices for Maryland 529 remain in their current location. To the extent that staff are moved to be physically co-located at STO, one-time costs are incurred. In addition, additional costs for STO are likely incurred to improve administration of the programs following the transfer, discussed in further detail below.

Additional State Treasurer's Office Expenses

STO advises its general fund expenditures increase significantly beyond the transfer of existing Maryland 529 administrative expenses beginning in fiscal 2023. Specifically, STO advises it needs additional funding to bolster its legacy information technology (IT) system and retain additional staffing for IT, customer service, contract management, legal services, and marketing. STO further advises it may require additional staff, and potentially attorneys from the Office of the Attorney General, to appropriately develop regulations and implement the interest payment requirement established in the bill. DLS advises that only some of these costs are directly a result of the requirements of the bill and most of them have not been quantified at this time and are not accounted for in this estimate.

Regardless, at least one full-time contractual attorney and three full-time contractual consumer service staff are needed in fiscal 2024 and 2025 to develop the regulations to determine the interest rate for payments to an account and to assist account holders with rolling over or closing their existing MPCT accounts. Thus, general fund expenditures increase by \$336,064 in fiscal 2024 and \$146,863 in fiscal 2025. This estimate reflects a hire date of July 1, 2023, and a termination date of January 1, 2025, for the employees. It includes four full-time salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Contractual Positions	4.0
Salaries and Fringe Benefits	\$305,368
Other Operating Expenses	<u>30,696</u>
Additional Minimal FY 2024 State Expenditures	\$336,064

Future year expenditures reflect (1) salaries with annual increases and employee turnover; (2) annual increases in ongoing operating expenses; and (3) termination of the contractual employees in mid-fiscal 2025 since rollovers must be completed before January 1, 2025.

This estimate does not include any health insurance costs that could be incurred for specified contractual employees under the State's implementation of the federal Patient Protection and Affordable Care Act.

Other Effects of Phasing Out the Maryland Senator Edward J. Kasemeyer Prepaid College Trust

Nonbudgeted revenues from account fees and expenditures associated with administering MPCT decrease beginning in fiscal 2023 as the bill prohibits any new accounts from being opened on or after June 1, 2023. The impact is likely minimal as this analysis assumes most current MPCT account holders will rollover to an MCIP account and prospective college savers may likewise choose an MCIP account instead of an MPCT contract. Therefore, the decrease is likely offset, to some extent, by administrative costs and associated fees on new MCIP accounts. To the extent individuals do not elect to rollover an MPCT contract into another 529 account, nonbudgeted revenues and expenditures for MPCT continue at an increasingly lower level for a couple of decades as the terms of contracts individuals have already entered into come to term.

State Matching Contributions

To the extent that the winding down of MPCT and new rollovers to MCIP cause additional individuals to make contributions to MCIP accounts that are eligible for matching contributions and apply for such matching contributions from the State, expenditures for matching contributions increase. Any increase is capped at \$9,000 per new rollover account that receives a match as Chapters 435 and 436 established a \$9,000 cap on the State contribution amount received over the lifetime of an account holder.

The exact timing of the increase depends on when individuals choose to rollover MPCT accounts but likely begins in fiscal 2025, reflecting the requirement that, to receive a match for contributions in a given year, the individual must submit an application between January 1 and June 1 of each year and payments for applications received during that timeframe are paid out in December of the same year.

MHEC currently administers the State matching fund, the Save4College Plan. Under the bill, the Save4College Plan is also moved to STO. General fund expenditures, therefore, decrease for MHEC and increase by an offsetting amount for STO with transfer of administration of State matching contributions for MCIP. The fiscal 2023 budget and

fiscal 2024 budget as introduced both include an appropriation of approximately \$11.0 million for State matching contributions.

Account Funds

The above estimate does not include non-operating revenues and expenditures (the assets/contract payments of account holders) as this analysis assumes those would remain in funds managed by third-party vendors/investors under contract with Maryland 529. Specifically, T. Rowe Price is the program manager for MCIP and Intuition College Savings Solutions, LLC is the program manager for MPCT. For the Maryland ABLE Program, Vestwell State Savings, LLC is the program manager and provides administrative and recordkeeping services to the program under the direction of the Maryland 529 Board.

In fiscal 2022, MCIP received \$883 million in contributions from and disbursed \$624.6 million in distributions to account holders. The total value of investments held in MCIP totaled \$7.8 billion. MPCT received \$36.7 million in contributions from contract holders and honored its contract obligations by paying approximately \$73.6 million in tuition benefits. As of fiscal 2022, MPCT consisted of \$1.1 billion in trust investments. For fiscal 2022, contributions by Maryland ABLE account holders totaled \$23.2 million, and Maryland ABLE account holders received over \$6.1 million in distributions.

The ABLE Program received \$642,600 in general funds in fiscal 2017 for start-up costs. Currently, the Maryland 529 Board plans to reimburse the State for these expenditures. To the extent Maryland 529, in becoming part of STO, no longer repays the initial start-up appropriation, State general fund revenues may decrease.

Interest Payment for Rollover Accounts

The bill does not specify the amount of any interest payments made to accounts that rollover from MPCT into MCIP and requires the State Treasurer to adopt regulations specifying the interest rate determinations. Therefore, the exact cost of interest payments is unknown and will depend on regulations ultimately adopted by the State Treasurer. While it is unclear how an interest rate determination would be made for rollovers from prepaid contracts, this analysis assumes that any such interest payments would likely be paid using MPCT funds, not State general funds. This analysis further assumes that the interest rate will be calculated in such a way to allow existing MPCT funds to cover the cost of any interest payment without the need for additional State funds. To the extent trust funds are not able to be used to cover the cost of interest payments or such payments would cause MPCT to become insolvent, significant additional State general fund expenditures may be necessary to cover the interest paid to rollover accounts. In the event the specified interest payments to rollover accounts cause the fund to become insolvent, contract terms

for individuals remaining in MPCT may need to be adjusted or additional State general funding may be needed to cover the shortfall.

Effect of Income Tax Deductions for 529 Accounts

The net effect of ending MPCT on State revenues from income tax deductions claimed by individuals for contributions to 529 accounts is likely minimal. Even with the wind down of MPCT, most individuals currently saving for college via an MPCT account do not likely cease saving for college with the closure of MPCT to new accounts. Instead, this analysis assumes that most will save for college using another similarly tax-advantaged savings plan (likely MCIP, given the requirement for an interest payment to accounts that complete such a rollover). Accordingly, the wind down of MPCT has limited overall effect on the income tax deductions claimed for contributions to 529 accounts. Additionally, MPCT is a relatively small 529 program with only 1,152 new enrollments in fiscal 2022. The Office of the Comptroller advises that, for electronic filers only in tax year 2021, approximately 13,400 individuals claimed income tax deductions for contributions to 529 accounts for a total sum of approximately \$100.5 million. Nevertheless, to the extent the wind down has an effect, general fund revenues increase minimally.

There are no additional income tax effects from interest distributions since the bill also specifies that interest distributions to accounts that rollover into an MCIP account do not count as contributions for the purposes of law governing State income tax.

Workgroup

The State Treasurer advises that, depending on the nature of the work actually undertaken by the workgroup, additional support staff may be required to complete the required tasks. However, DLS advises that the scope of the workgroup is likely such that STO can staff the workgroup with existing resources.

Local Revenues: As described above, the bill may influence the number of individuals claiming income tax deductions for contributions to 529 accounts as the bill phases out MPCT; however, any such effect is likely minimal.

Additional Information

Prior Introductions: Similar legislation has not been introduced within the last three years.

Designated Cross File: SB 959 (Senator Benson, *et al.*) - Budget and Taxation and Education, Energy, and the Environment.

Information Source(s): Comptroller's Office; Maryland State Treasurer's Office; Maryland Higher Education Commission; University System of Maryland; Maryland 529; Maryland Department of Disabilities; Department of Legislative Services

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