

Department of Legislative Services
 Maryland General Assembly
 2023 Session

FISCAL AND POLICY NOTE
Third Reader - Revised

Senate Bill 721

(Chair, Budget and Taxation Committee)(By Request -
 Departmental - Commerce)

Budget and Taxation

Ways and Means

Income Tax - Credit for Federal Security Clearance Costs - Alterations

This departmental bill reauthorizes the employer security clearance costs tax credit from tax year 2023 through tax year 2027 for an individual or corporation with up to 500 employees. **The bill takes effect July 1, 2023, and applies to tax year 2023 and beyond.**

Fiscal Summary

State Effect: General fund revenues decrease by \$1.5 million annually from FY 2025 through 2028. Transportation Trust Fund (TTF) revenues decrease by \$0.2 million to \$0.3 million annually and Higher Education Investment Fund (HEIF) revenues decrease by \$0.1 million annually from FY 2025 through 2028. There is a similar revenue effect in FY 2029. General fund expenditures for the Comptroller’s Office increase by \$50,000 in FY 2024 only.

(\$ in millions)	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028
GF Revenue	\$0	(\$1.5)	(\$1.5)	(\$1.5)	(\$1.5)
SF Revenue	\$0	(\$0.3)	(\$0.3)	(\$0.3)	(\$0.3)
GF Expenditure	\$0.1	\$0	\$0	\$0	\$0
SF Expenditure	\$0	\$0.0	(\$0.1)	(\$0.1)	\$0.0
Net Effect	(\$0.1)	(\$1.8)	(\$1.8)	(\$1.8)	(\$1.8)

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

Local Effect: Local highway user revenues decrease by \$36,400 to \$51,400 annually from FY 2025 through 2028. Local income tax revenues increase minimally from FY 2025 through 2028 due to taxpayers adding back the amount of credits claimed against the personal income tax. Local expenditures are not affected.

Small Business Effect: The Department of Commerce has determined that this bill has a meaningful impact on small business (attached). The Department of Legislative Services concurs with this assessment. (The attached assessment does not reflect amendments to the bill.)

Analysis

Current Law/Background: Chapter 478 of 2012 established the Employer Security Clearance Costs Tax Credit program. The program allows a tax credit against the State income tax for certain security clearance administrative expenses and for the construction and equipment costs to construct or renovate a sensitive compartmented information facility (SCIF) located in the State. The program originally applied to tax years 2013 through 2016. Chapter 240 of 2017 extended the program duration through tax year 2021.

Commerce is authorized to award a maximum of \$2.0 million in total credits each year. If the amount of credits claimed in each year exceeds the maximum aggregate limit, the value of the credit is reduced based on the total amount of excess credits claimed.

The amount of expenses that qualify for the credit are equal to (1) 100% of eligible security clearance administrative expenses, not to exceed \$200,000; (2) if the individual or corporation is a small business, 100% of eligible rental payments, not to exceed \$200,000; and (3) 50% of eligible costs incurred to construct or renovate each SCIF, not to exceed \$200,000. If a company constructs and/or renovates multiple SCIFs, the total amount of aggregate expenditures that qualify for the credit is limited to \$500,000. If the total amount of the credit exceeds the tax liability imposed in the year, the excess can be carried forward to future tax years until the full amount of the excess is used.

An individual or corporation may either file an amended income tax return for the taxable year in which the costs were incurred or claim the credit in any subsequent taxable year. Businesses claiming the credit are required to add back to Maryland adjusted gross income or Maryland modified income the amount of expenses claimed under the credit.

The credit has been oversubscribed in recent years: the percentage of qualified costs that received the tax credit was 54% in tax year 2018 (64 recipients) and 46% in tax year 2019 (81 recipients). Just over half of the credits were awarded to businesses with fewer than 50 employees in both years. Most of the credit amounts provided each year cover eligible security clearance administrative expenses.

State Fiscal Effect: The bill reauthorizes the employer security clearance costs tax credit from tax year 2023 through tax year 2027 for an individual or corporation that employs up to 500 employees. Commerce can award a maximum of \$2.0 million in credits annually in

those years. Before claiming the tax credit, Commerce must certify the amount of expenses incurred by the business. These expenses are certified by December 15 of the calendar year following the end of the taxable year in which the qualifying expenses occurred. A business may then either file an amended return to claim the credit for the taxable year in which the costs were incurred or claim the credit for a subsequent taxable year.

As a result, State revenues decrease by \$1.8 million to \$1.9 million annually from fiscal 2025 through 2028, as shown in **Exhibit 1**. Most revenue losses each year are general funds. Revenues decrease by similar amounts in fiscal 2029 as well, prior to the tax credit expiring.

Exhibit 1
Projected Effect on State Revenues
Fiscal 2025-2028
(\$ in Millions)

	<u>FY 2025</u>	<u>FY 2026</u>	<u>FY 2027</u>	<u>FY 2028</u>
State Revenues				
General Fund	(\$1.5)	(\$1.5)	(\$1.5)	(\$1.5)
HEIF	(0.1)	(0.1)	(0.1)	(0.1)
TTF	(0.2)	(0.3)	(0.3)	(0.2)
Total	(\$1.8)	(\$1.9)	(\$1.9)	(\$1.8)

HEIF: Higher Education Investment Fund

TTF: Transportation Trust Fund

Source: Department of Legislative Services

The estimated revenue loss due to the extension of the credit is based on the following facts and assumptions:

- the maximum amount of credits will be awarded in each tax year, even with the limitation on business size in the bill;
- 75% of credits are claimed against the corporate income tax, with the remaining amount claimed against the personal income tax;
- businesses have enough tax liability to claim the full credit;
- credits are applied to the taxable year in which the costs were incurred; and

- any credit claimed is added back to Maryland adjusted gross income or Maryland modified income.

It is estimated that general fund expenditures for the Comptroller's Office increase by \$50,000 in fiscal 2024 for one-time changes to the Comptroller's tax systems.

Additional Information

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

Designated Cross File: None.

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

Fiscal Note History: First Reader - March 3, 2023
km/jrb Third Reader - March 22, 2023
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ANALYSIS OF ECONOMIC IMPACT ON SMALL BUSINESSES

TITLE OF BILL: Income Tax - Credit for Federal Security Clearance Costs - Alterations

BILL NUMBER: SB 721

PREPARED BY: Michael Siers

PART A. ECONOMIC IMPACT RATING

This agency estimates that the proposed bill:

WILL HAVE MINIMAL OR NO ECONOMIC IMPACT ON MARYLAND SMALL BUSINESS

OR

WILL HAVE MEANINGFUL ECONOMIC IMPACT ON MARYLAND SMALL BUSINESSES

PART B. ECONOMIC IMPACT ANALYSIS

The proposed legislation will extend the Maryland Employer Security Clearance Costs Tax Credit from tax year ending 2022 through 2027. This tax credit provides three ways for companies to receive a credit:

1. A credit towards administrative expenses related to obtaining and maintaining employee security clearances,
2. A credit towards the cost of constructing or renovating a SCIF (sensitive compartmented information facility), and
3. A credit towards the first-year leasing costs for small businesses doing security-based contract work.

Currently, the program provides companies with \$2 million annually in tax credits spread across the three programs. Most of the assistance is provided to cover administrative expenses related to obtaining and maintaining employee security clearances.

The majority of the assistance is provided to small businesses within Maryland. In tax year 2019, the most recent tax year for which data is available, a total of 81 companies received assistance through this tax credit. Of these 81 companies, 57% had fewer than 50 employees and 79% had fewer than 100 employees. In tax year 2018, 53% of companies who received assistance had fewer than 50 employees and 81% had fewer than 100 employees. If the tax credit is extended for another five years, it is likely that most of this assistance will continue to benefit small businesses in Maryland.