

Department of Legislative Services
 Maryland General Assembly
 2023 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 1106 (Delegate Alston)
 Ways and Means and Appropriations

Maryland College Investment Plan – Subtraction Modification Amounts and Eligibility and Establishment of Accounts

This bill alters the Maryland personal income tax subtraction modification for contributions to an investment account under the Maryland College Investment Plan by limiting the number of investment accounts with respect to which an individual contributor may claim the subtraction modification and increasing the maximum annual subtraction per beneficiary from \$2,500 to \$16,000 by tax year 2032. In addition, the bill requires the Maryland 529 Board to establish a maximum contribution amount of \$750,000 with respect to the Maryland College Investment Plan. Finally, the bill requires the State to establish an investment account under the Maryland College Investment Plan for each ward of the State, as defined under the bill, and make an annual contribution of \$500 during the period of time that the child remains a ward of the State. **The bill takes effect July 1, 2023. The income tax provisions apply to tax year 2023 and beyond.**

Fiscal Summary

State Effect: General fund revenues decrease by an estimated \$5.4 million in FY 2024; future years reflect phased increases in the value of the income tax subtraction modification for specified Maryland 529 account contributions and projected growth in eligible contributions. General fund expenditures increase by *at least* \$3.2 million annually beginning in FY 2024, as discussed below.

(\$ in millions)	FY 2024	FY 2025	FY 2026	FY 2027	FY 2028
GF Revenue	(\$5.4)	(\$10.2)	(\$14.4)	(\$18.1)	(\$21.5)
GF Expenditure	\$3.2	\$3.2	\$3.2	\$3.2	\$3.2
Net Effect	(\$8.6)	(\$13.4)	(\$17.6)	(\$21.3)	(\$24.7)

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

Local Effect: Local income tax revenues decrease by an estimated \$3.5 million in FY 2024 and \$13.8 million in FY 2028, as discussed below. Local expenditures are not affected.

Small Business Effect: None.

Analysis

Current Law/Bill Summary:

Qualified Tuition Plans

Qualified tuition plans, as authorized under § 529 of the Internal Revenue Code (IRC), are programs established and maintained by a state, state agency or instrumentality, or eligible education institution under which a person may (1) purchase tuition credits or certificates on behalf of a designated beneficiary or (2) make contributions to an account established for the purpose of meeting the qualified higher education expenses of the designated beneficiary.

Among other requirements, a program may not be treated as a qualified tuition program unless it provides adequate safeguards to prevent contributions on behalf of a designated beneficiary in excess of those necessary to provide for the qualified higher education expenses of the beneficiary. Under the federal Tax Cuts and Jobs Act of 2017, qualified higher education expenses may include up to \$10,000 in expenses for tuition in connection with enrollment or attendance at an elementary or secondary public, private, or religious school.

Maryland 529 currently operates two qualified tuition plans: the Maryland Prepaid College Trust and Maryland College Investment Plan.

Maryland College Investment Plan

The Maryland College Investment Plan allows contributions to investment accounts established for the purpose of meeting the qualified higher education expenses of qualified designated beneficiaries. Contributions to the plan on behalf of a beneficiary may not exceed the maximum amount determined by the Maryland 529 Board to be in accordance with § 529 of the IRC.

Under the bill, the board must establish a maximum contribution amount of \$750,000. In addition, the bill requires the State to establish an investment account under the Maryland College Investment Plan for each ward of the State. “Ward of the State” is defined as a child younger than age 18 for whom a State or county agency or official has been appointed

legal guardian, or who has been committed by a court of competent jurisdiction to the legal custody of a State or county agency or official; this includes a child younger than age 18 who has been adjudicated as delinquent. The State must annually contribute \$500 to each such investment account during the period of time that the child remains a ward of the State. If the qualified beneficiary does not use the account balance for qualified higher education expenses by age 26, the balance of the investment account, including interest earnings, must revert to the State general fund.

The bill authorizes the Maryland 529 Board to adopt any regulations necessary to carry out the bill's provisions with respect to required investment plans for wards of the State. The bill further specifies that the balance of or distribution from an investment account may not be used in determining eligibility for State benefits.

Income Tax Subtraction Modifications

An individual may claim a subtraction modification against the Maryland personal income tax for payments made to an investment account under the Maryland College Investment Plan. The subtraction may not exceed \$2,500 per contributor per beneficiary in any taxable year. (For purposes of the limitation, each spouse on a joint return is treated separately.) Any amount in excess of this limitation may be carried forward for up to 10 tax years until fully used. The subtraction may not be claimed if the account holder received funds under the State Contribution Program during the tax year.

An individual may similarly claim a subtraction modification against the personal income tax for the amount of advance tuition payments made to the Maryland Prepaid College Trust. The subtraction may not exceed \$2,500 per prepaid contract in any taxable year. Any amount in excess of this limitation may be carried forward to future tax years until fully used.

Under the bill, the maximum annual subtraction modification for contributions to an investment account under the Maryland College Investment Plan is increased to \$16,000 per contributor per beneficiary by tax year 2032. The subtraction modification for tuition payments made to the Maryland Prepaid College Trust is unchanged. Specifically, the dollar amount limit increases to:

- \$3,850 for tax year 2023;
- \$5,200 for tax year 2024;
- \$6,550 for tax year 2025;
- \$7,900 for tax year 2026;
- \$9,250 for tax year 2027;
- \$10,600 for tax year 2028;

- \$11,950 for tax year 2029;
- \$13,300 for tax year 2030;
- \$14,650 for tax year 2031; and
- \$16,000 for tax year 2032.

In tax years after tax year 2032, the limit is increased by the lesser of (1) the percentage increase in the Consumer Price Index for All Urban Consumers for the Washington Metropolitan Area, or any successor index, for the immediately preceding 12-month period or (2) 5%.

In addition, the bill specifies that a contributor who is an individual may claim the subtraction modification only for contributions made to up to four investment accounts during the taxable year. The bill further specifies that if a contributor is a person other than an individual, the subtraction may be claimed only if the person has at least one employee covered under the State workers’ compensation laws.

State/Local Revenues: State and local income tax revenues decrease beginning in fiscal 2024 due to the bill’s phased increases in the value of the Maryland income tax subtraction modification for contributions to investment accounts under the Maryland College Investment Plan.

Exhibit 1 shows the bill’s estimated effect on State general fund revenues and local income tax revenues in fiscal 2024 through 2028. As shown in the exhibit, in fiscal 2024, State general fund revenues decrease by an estimated \$5.4 million, and local income tax revenues decrease by an estimated \$3.5 million. Future years reflect annual phased increases in the value of the subtraction modification and projected increases in eligible contributions. This estimate is based on tax year 2021 claims for the existing subtraction modification.

Exhibit 1
Projected State and Local Revenue Effect
Fiscal 2024-2028
(\$ in Millions)

	<u>FY 2024</u>	<u>FY 2025</u>	<u>FY 2026</u>	<u>FY 2027</u>	<u>FY 2028</u>
State	(\$5.4)	(\$10.2)	(\$14.4)	(\$18.1)	(\$21.5)
Local	(3.5)	(6.6)	(9.3)	(11.7)	(13.8)
Total	(\$8.8)	(\$16.7)	(\$23.6)	(\$29.8)	(\$35.3)

Note: Numbers may not sum to total due to rounding.

As noted above, the bill specifies that an individual contributor may claim the subtraction modification only for contributions made to up to four investment accounts during the taxable year. Due to data limitations, it is unknown how many taxpayers claim the existing subtraction modification with respect to contributions to more than four accounts. To the extent that the bill's restriction limits the amount of allowable subtraction modifications claimed by taxpayers, the revenue decreases may be partially offset by some indeterminate amount.

In addition, as discussed further below, the bill requires the State to make certain contributions to investment accounts under the Maryland College Investment Plan for wards of the State and specifies that unused funds revert to the general fund under specified circumstances. Thus, general fund reductions may be further offset to the extent that account balances are not used for qualified education expenses and subsequently revert to the general fund.

State Expenditures: As discussed above, the bill requires the State to open an investment account under the Maryland College Investment Plan for each ward of the State, as defined under the bill, and contribute \$500 annually to each such account while the child remains a ward of the State. It is assumed, for purposes of this analysis, that general funds are used to make the required contributions.

It is not readily known how many children are potentially affected by the bill's requirement. However, based on the number of children in out-of-home placements in fiscal 2022, it is estimated that general fund expenditures increase by *at least* \$3.2 million annually beginning in fiscal 2024 for required contributions to investment accounts. The bill does not further contemplate how provisions relating to investment accounts for wards of the State would be implemented by relevant State and/or local agencies; thus, this fiscal and policy note does not account for any other potential implementation costs resulting from these provisions.

General fund expenditures increase further to the extent the Comptroller's Office incurs implementation costs related to the bill's income tax provisions. However, sufficient information was not provided in time to fully analyze the bill's effect on the operations of the Comptroller's Office.

Additional Comments: As noted above, a program may not be treated as a qualified tuition program under § 529 of the IRC unless it provides adequate safeguards to prevent contributions on behalf of a designated beneficiary in excess of those necessary to provide for the qualified higher education expenses of the beneficiary. The bill requires the

Maryland 529 Board to establish a contribution limit of \$750,000 for Maryland College Investment Plan accounts.

According to Maryland 529, the Maryland 529 Board most recently voted to raise the maximum aggregate account balance from \$350,000 to \$500,000 at its October 2018 meeting, based on a review of actuarial projections of higher education expenses. Maryland 529 advises that increasing the aggregate account balance limit under the Maryland College Investment Plan to \$750,000 would make the program an outlier among qualified tuition programs and would require further study to ensure compliance with federal requirements. However, this fiscal and policy note does not account for any potential impacts of the bill on the Maryland College Investment Plan's status as a qualified tuition program.

Additional Information

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

Designated Cross File: None.

Information Source(s): Comptroller's Office; Maryland 529; Moody's Analytics; Department of Legislative Services

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