

Department of Legislative Services
 Maryland General Assembly
 2026 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 801 (Delegate Embry)
 Ways and Means

**Income Tax - Addition Modifications - Business Stock Gains, Fines, Penalties,
 and Bonus Depreciation**

This bill repeals the exemption for qualified manufacturers from the income tax decoupling modifications relating to the § 168(k) bonus depreciation allowance and enhancements to the § 179 expensing allowance. The bill also requires addition modifications for (1) any qualified small business stock (QSBS) gain excluded from income under § 1202 of the Internal Revenue Code (IRC) and (2) any amount in excess of \$50,000 paid or incurred during the tax year for restitution that is deducted as a trade or business expense under IRC § 162. **The bill takes effect July 1, 2026, and applies to tax year 2026 and beyond.**

Fiscal Summary

State Effect: In FY 2027, general fund revenues increase by an estimated \$32.6 million; Higher Education Investment Fund revenues increase by an estimated \$0.8 million; Transportation Trust Fund (TTF) revenues increase by an estimated \$3.9 million; and TTF expenditures for local highway user revenue grants increase by an estimated \$0.5 million. Future years reflect the projected net effect of delayed deductions, as discussed below. General fund expenditures for the Comptroller’s Office increase by an estimated \$0.2 million in FY 2027 only.

(\$ in millions)	FY 2027	FY 2028	FY 2029	FY 2030	FY 2031
GF Revenue	\$32.6	\$32.0	\$29.8	\$29.9	\$31.1
SF Revenue	\$4.7	\$4.2	\$3.5	\$3.3	\$3.2
GF Expenditure	\$0.2	\$0	\$0	\$0	\$0
SF Expenditure	\$0.5	\$0.3	\$0.2	\$0.1	\$0.1
Net Effect	\$36.7	\$35.9	\$33.1	\$33.1	\$34.2

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

Local Effect: Local revenues increase by an estimated \$11.4 million in FY 2027 and by similar amounts thereafter, as discussed below.

Small Business Effect: Minimal.

Analysis

Current Law:

Sections 179 and 168(k) Expensing Allowances

IRC §§ 179 (election to expense certain depreciable business assets) and 168(k) (first-year additional depreciation allowance, or “bonus depreciation”) allow businesses to expense certain depreciable business property placed in service during the tax year. The two expensing allowances apply to many of the same types of assets and are each enhanced under the federal One Big Beautiful Bill Act (OBBBA) of 2025. As discussed below, the Maryland income tax is permanently decoupled from the § 168(k) bonus depreciation allowance and enhancements to the § 179 expensing allowance enacted after 2002. However, pursuant to the More Jobs for Marylanders Act of 2017 (Chapter 149), Maryland income tax conforms to the current § 168(k) and § 179 allowances as they apply to property placed in service by a qualified manufacturing entity after 2018.

Section 179 Expensing Allowance: A taxpayer may elect to expense the cost of any section 179 property (as defined), subject to a certain dollar amount limitation that phases out dollar-for-dollar by the amount by which aggregate investment in section 179 property placed in service during the tax year exceeds a certain phaseout threshold. The allowance is also subject to an income limitation – specifically, the allowance may not exceed the taxpayer’s aggregate taxable income from the active conduct of all trades or businesses of the taxpayer during the tax year. “Section 179 property” includes tangible property eligible for depreciation under the Modified Accelerated Cost Recovery System (MACRS) (e.g., machinery and equipment), certain depreciable computer software, and certain qualified improvements to nonresidential real property.

OBBBA increases the § 179 dollar amount limitation and investment threshold for property placed in service after December 31, 2024. Specifically, for tax year 2025, the dollar amount limitation increases from \$1.25 million to \$2.5 million, and the investment threshold at which the allowance begins to phase out increases from \$3.13 million to \$4.0 million. Consistent with prior law, the enhanced dollar amount limitation and investment threshold are indexed to inflation for tax years after 2025.

The Budget Reconciliation and Financing Act (BRFA) of 2004 (Chapter 430) and subsequent legislation decoupled Maryland income tax from enhancements to the § 179 expensing allowance enacted under the federal Jobs and Growth Tax Relief Reconciliation Act of 2003 and subsequent federal legislation for tax years after 2002. Thus, for Maryland income tax purposes, the expensing allowance is limited to \$25,000 reduced dollar-for-dollar by the amount by which the aggregate investment in section 179 property placed in service during the tax year exceeds \$200,000. As discussed above, the More Jobs for Marylanders Act exempted manufacturing entities from the related decoupling modification for property placed in service after 2018; thus, Maryland income tax conforms to the current § 179 expensing allowance as it applies to such property.

Section 168(k) Bonus Depreciation Allowance: A taxpayer may claim an additional first-year depreciation deduction (“bonus depreciation”) for qualified property acquired for use in the active conduct of a trade or business and that is placed in service by the taxpayer during the tax year. Qualified property includes any MACRS property with a recovery period of 20 years or less (*e.g.*, machinery, equipment, and certain qualified improvements to nonresidential real property); depreciable computer software; water utility property; and certain film, television, theatrical, and sound recording productions.

The federal § 168(k) bonus depreciation allowance was first enacted under the federal Job Creation and Worker Assistance Act of 2002 as a 30% additional first-year depreciation deduction for qualified property placed in service after September 10, 2001, and before September 11, 2004. The BRFA of 2002 (Chapter 440) permanently decoupled the Maryland income tax from this federal tax change.

The federal bonus depreciation allowance has since been enhanced, reinstated, extended, and otherwise modified several times and was most recently amended by the Tax Cuts and Jobs Act (TCJA) of 2017 and OBBBA. TCJA allowed a 100% bonus depreciation deduction for qualified property placed in service after September 27, 2017, and before January 1, 2023; the Act gradually phased down the bonus depreciation percentage for tax years after 2022 (80% for 2023; 60% for 2024; 40% for 2025; and 20% for 2026) and fully phased out the allowance for tax year 2027 and beyond. OBBBA permanently restores 100% bonus depreciation for property placed in service after January 19, 2025.

As discussed above, the More Jobs for Marylanders Act allowed qualified manufacturing entities to claim the federal § 168(k) bonus depreciation deduction against Maryland taxable income for qualified property placed in service after 2018. Maryland has otherwise remained decoupled from § 168(k).

Qualified Small Business Stock Gain Exclusion

Per IRC § 1202, noncorporate taxpayers may exclude from gross income certain gain from the sale or exchange of QSBS (generally, stock in a qualified small business that is acquired by the taxpayer at its original issue). “Qualified small business” is generally defined as a domestic C corporation that meets a certain aggregate gross assets test. Prior to amendment by OBBBA, the exclusion was available only with respect to QSBS held for more than five years. For QSBS acquired before July 4, 2025, the gain exclusion percentage is 50% (75% for QSBS acquired after February 17, 2009, and before September 28, 2010, and 100% for QSBS acquired after September 27, 2010). The exclusion is subject to an aggregate per-issuer limitation on a taxpayer’s eligible gain.

OBBBA creates a tiered exclusion for QSBS held for at least three years. Specifically, for QSBS acquired after July 4, 2025, the gain exclusion percentage is 50% for QSBS held for at least three years, 75% for QSBS held for at least four years, and 100% for QSBS held for at least five years. OBBBA also increases the (1) aggregate gross assets threshold for qualified small businesses from \$50 million to \$75 million and (2) the per-issuer limitation on a taxpayer’s excludable gain from \$10 million to \$15 million. Each of these enhanced limitations are indexed to inflation for tax years after 2026.

Maryland Net Capital Gain Surtax

The BRFA of 2025 (Chapter 604) imposes a 2% surtax for taxpayers with federal adjusted gross income (AGI) in excess of \$350,000 on certain net capital gain included in Maryland AGI. The surtax does not apply to gain from the sale or exchange of a primary residential dwelling sold for less than \$1.5 million; assets held in specified retirement savings plans; cattle, horses, or breeding livestock held for more than 12 months; certain land subject to a conservation, agricultural, or forest preservation easement; section 179 property; or affordable housing owned by a nonprofit organization. The Comptroller must distribute 37.5% of the proceeds from the surtax to TTF.

Restitution

IRC § 162(f) disallows ordinary and necessary deductions for fines or penalties paid to a government or governmental entity for violations of law. However, exceptions apply for amounts constituting restitution or paid to come into compliance with law. TCJA further limited the deductibility of such amounts to those identified in a court order or settlement agreement.

State Revenues: **Exhibit 1** details the bill’s estimated State revenue effects by provision and by fund. As shown in the exhibit, State revenues increase by an estimated \$37.3 million in fiscal 2027, including \$32.6 million in general funds, due to the foregone acceleration

of depreciation deductions against Maryland taxable income and the addition of excluded QSBS gain back to income. Future years reflect the projected net effect of (1) foregone deductions and exclusions and (2) the offsetting effect of depreciation deductions that, absent the bill, would have been taken in a previous year. This estimate does not reflect any State revenues that may be generated by the bill's addition modification for certain deductible restitution amounts, which cannot be reliably estimated but are not expected to be significant.

Exhibit 1
Quantified State Revenue Effects
Fiscal 2027-2031
(\$ in Millions)

	<u>FY 2027</u>	<u>FY 2028</u>	<u>FY 2029</u>	<u>FY 2030</u>	<u>FY 2031</u>
<i>By Decoupling Provision</i>					
§ 168(k) Bonus Depreciation	\$15.8	\$14.1	\$9.0	\$6.4	\$4.8
§ 179 Expensing Allowance	1.4	1.3	1.2	1.2	1.1
§ 1202 QSBS Gain Exclusion	20.0	20.8	23.1	25.6	28.4
<i>By Fund</i>					
General Fund	\$32.6	\$32.0	\$29.8	\$29.9	\$31.1
HEIF	0.8	0.7	0.4	0.3	0.2
TTF	3.9	3.5	3.1	2.9	2.9
Total State Revenue Effect	\$37.3	\$36.2	\$33.3	\$33.2	\$34.3

HEIF: Higher Education Investment Fund

QSBS: qualified small business stock

TTF: Transportation Trust Fund

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

Source: Comptroller's Office; Department of Legislative Services

This estimate is based on an analysis by the Comptroller's Office of State and federal income tax return data and estimated federal revenue effects of relevant OBBBA provisions published by the U.S. Joint Committee on Taxation.

State Expenditures: TTF expenditures for local highway user revenue grants increase by an estimated \$0.5 million in fiscal 2027; \$0.3 million in fiscal 2028; \$0.2 million in fiscal 2029; and \$0.1 million in each of fiscal 2030 and 2031. General fund expenditures for the Comptroller's Office increase by an estimated \$150,000 in fiscal 2027 for one-time programming costs.

Local Revenues: Local income tax revenues and local highway user revenues increase beginning in fiscal 2027 due to increases in personal and corporate taxable income, respectively. As shown in **Exhibit 2**, in fiscal 2027, local revenues increase by an estimated total of \$11.4 million, including \$11.0 million in local income tax revenues and \$0.5 million in local highway user revenues. Future years reflect the local share of highway user revenues and the projected net effect of delayed deductions and ongoing addition modifications. This estimate does not reflect any local revenues that may be generated by the bill’s addition modification for certain deductible restitution amounts, which cannot be reliably estimated but are not expected to be significant.

Exhibit 2
Quantified Local Revenue Effects
Fiscal 2027-2031
(\$ in Millions)

	<u>FY 2027</u>	<u>FY 2028</u>	<u>FY 2029</u>	<u>FY 2030</u>	<u>FY 2031</u>
Local Income Tax Revenue	\$11.0	\$11.0	\$11.1	\$11.8	\$12.6
Local Highway User Revenue	0.5	0.3	0.2	0.1	0.1
Total Local Revenue Effect	\$11.4	\$11.3	\$11.3	\$11.9	\$12.7

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

Source: Comptroller’s Office; Department of Legislative Services

Additional Information

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

Designated Cross File: None.

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

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