

Department of Legislative Services
Maryland General Assembly
2026 Session

FISCAL AND POLICY NOTE
First Reader

Senate Bill 163

(Senator West)

Budget and Taxation

**Income Tax - Addition Modification for Federal Tax-Exempt Income -
Alterations**

This bill specifies that the income tax addition modification for certain income exempted by federal law or treaty from federal but not State income tax does not apply to foreign earned income within the meaning of § 911(b)(2) of the Internal Revenue Code (IRC). **The bill takes effect July 1, 2026, and applies to tax year 2026 and beyond.**

Fiscal Summary

State Effect: It is assumed that the bill simply clarifies existing law and does not materially affect State revenues, as discussed below. The Comptroller's Office can make related updates to tax form instructions and guidance with existing budgeted resources.

Local Effect: It is assumed that the bill does not materially affect local revenues. Local expenditures are not affected.

Small Business Effect: None.

Analysis

Current Law: To the extent excluded from federal adjusted gross income, Tax-General Article § 10-204(c) requires a resident to add back to income the amount of salary, wages, or other compensation for personal services that is exempted by federal law or treaty from federal income tax but not State income tax. The Comptroller's Office advises that the requirement applies to, for example, wages earned in Maryland by a foreign national that are exempt from federal income tax due to a treaty but that are nonetheless subject to Maryland income tax.

Foreign Earned Income Exclusion

Section 911 of the IRC allows a qualified individual to elect to exclude foreign earned income (as defined) from gross income for federal income tax purposes. The exclusion is available to an individual whose tax home is in a foreign country and who is (1) a citizen of the United States and establishes to the satisfaction of the Secretary of the Treasury that the individual has been a *bona fide* resident of a foreign country or countries for an uninterrupted period that includes an entire taxable year or (2) a citizen or resident of the United States and is present in a foreign country or countries for at least 330 full days during any period of 12 consecutive months.

“Foreign earned income” is defined as the amount received by an individual from sources within a foreign country or countries which constitute earned income attributable to services performed by such individual during the qualifying period. It does not include amounts received as a pension or annuity; paid by the United States or an agency thereof to an employee of the United States or an agency thereof; included in gross income by reason of IRC § 402(b) (taxability of a beneficiary of a nonexempt trust) or § 403(c) (taxability of a beneficiary under a nonqualified annuity or annuity purchased by an exempt organization); or received after the close of the tax year following the tax year in which the services to which the amounts are attributable are performed.

The exclusion is limited to the amount of foreign earned income computed on a daily basis at an annual rate equal to a specified inflation-adjusted exclusion amount. For tax year 2026, the exclusion amount is \$132,900.

Cosgrove v. Comptroller

The question of whether § 10-204(c) of the Tax-General Article requires a Maryland resident to add back the amount of any excluded foreign earned income on the Maryland income tax return was presented to the Maryland Tax Court in the case of *Cosgrove v. Comptroller*. The Cosgroves filed an amended Maryland income tax return excluding their § 911 foreign earned income and claiming a Maryland income tax refund for two years. The Comptroller initially denied the Cosgroves’ refund claim and, on administrative repeal, determined that § 10-204 requires the addition of federally-excluded foreign earned income for State and local income tax purposes. However, prior to the Tax Court hearing, the Comptroller issued without explanation a refund to the Cosgroves with interest on the tax paid on the foreign earned income. The Comptroller subsequently filed a motion to dismiss, which was granted by the Tax Court and upheld by the Maryland Appellate Court. In its opinion, the Maryland Appellate Court advised that the General Assembly should examine § 10-204 and clarify its application with respect to foreign earned income. *Cosgrove v. Comptroller of Md.*, 263 Md. App. 147, 172 (2024).

State/Local Revenues: The Comptroller's Office has advised the Department of Legislative Services that the Comptroller's position is that the addition modification under Tax-General Article § 10-204(c) does not apply to foreign earned income within the meaning of the IRC § 911 foreign earned income exclusion. Thus, this analysis assumes that the bill simply codifies the Comptroller's interpretation of existing law. While the bill's clarification to § 10-204(c) may increase utilization of the foreign earned income exclusion on the Maryland income tax return, it is assumed that any resulting impact on State general fund revenues or local income tax revenues is not material.

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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sj/hlb

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