



**MARYLAND
LEGAL AID**

Advancing
**Human Rights and
Justice for All**

Senate Bill 0380

Income Tax – Subtraction Modification – Water Affordability Assistance

In the Senate Budget and Taxation Committee

Hearing on February 22, 2023

Position: FAVORABLE

Maryland Legal Aid (MLA) submits its written and oral testimony on SB 0380 at the request of bill sponsor Senator Mary Washington.

MLA asks that the Committee report **favorably** on Senate Bill 380, which would end the taxation of water bill assistance granted by state or local government, ending the perverse practice of penalizing low-income residents for receiving assistance because they are low-income. MLA is Maryland’s largest private, civil non-profit law firm, providing free legal services to indigent Maryland residents. MLA assists individuals and families in every Maryland county with a wide array of civil legal issues, including protecting people from the epidemic of the loss of housing across the state. MLA is a non-profit law firm that provides free legal services to the State’s low-income and vulnerable residents.

SB0380 would eliminate from taxable income any water bill assistance received from a local government or the State of Maryland.

Any welfare benefits that are received from a “public welfare fund” based upon need are not considered income for IRS purposes.¹ IRS guidelines are clear: Water bill assistance provided to homeowners is income-based and comes from a public welfare fund. It is therefore not taxable under IRS guidelines.

SB 0380 is necessary, however, to clarify that water bill assistance is non-taxable income even where its funding source is not a “public welfare fund.” The need for clarity arises presently in the City of Baltimore’s “Water for All” income-based billing program. However, as detailed below, the importance of SB 0380 extends throughout the state.

Under the “Water for All” program, homeowners and tenants typically receive a credit based on their income levels. This credit is accounted for directly in the customer’s billing. Whereas this direct form of the credit works elegantly for properties that are single-metered, it cannot be implemented for a tenant in a master-metered multi-unit building. This type of water-payer is responsible for a share of water and

¹ IRS Publication 525: Taxable and Non-Taxable Income, <https://www.irs.gov/pub/irs-pdf/p525.pdf>.

sewer charges for their entire building and pays their share to the landlord, rather than directly to the utility. (The landlord is the City’s customer.) If this water-payer tenant is income eligible for a “Water for All” credit, they may receive the credit in the form of a reimbursement payment. To account for this transaction of water bill assistance, the City issues a 1099-MISC form.

Under advice from outside counsel, the City of Baltimore takes the view that this direct-to-tenant payment of water bill assistance is taxable income, regardless of IRS guidelines. Although the City has not shared their legal analysis with stakeholders in the implementation of the “Water for All” program, one might assume that, under the City’s view of these credits, the dollars paid out to the tenant derive from general water utility revenue – *not* from a separate “public welfare fund” for water bill assistance. It is possible, too, that the City is unsure how the IRS would treat these direct-to-tenant payments under the aforementioned guidelines. The City may issue the 1099s in an abundance of caution.

HB0538 is necessary to eliminate this ambiguity and ensure that a local government may make direct-to-tenant payments for water bill assistance without issuing a 1099-MISC form. This bill would clarify that water bill assistance is not taxable income and would therefore prevent the City from issuing these 1099s.

Without passage of SB0380, the tax treatment of water bill assistance payments will harm low-income residents.

Low-income Marylanders generally do not have the funds to afford to hire an accountant to go over their tax documents with them, so they are more likely to report a 1099 for water bill assistance in their gross income. This can have several adverse consequences. As noted in the 2022 report *Water Affordability in Maryland*, tenants “lose as much as a quarter of the benefit [of the Water for All credit] to taxes. The assistance would also be factored into their total annual income and could potentially disqualify them for other means-tested financial benefits they receive, such as subsidized housing, SNAP, Social Security, or disability benefits.”²

There is a \$10,300.00 limitation on non-work income for a person to be eligible for the Earned Income Tax Credit (EITC). It is possible that a tenant may incorrectly report their water bill assistance as income to the IRS, which will cause the earned income tax credit to be eliminated or limited incorrectly. In addition, every three years, millions of dollars of tax refunds go unclaimed by taxpayers, especially low-

² Maryland Advisory Committee to the U.S. Commission on Civil Rights, *Water Affordability in Maryland* 10 (July 2022), <https://www.usccr.gov/files/2022-07/md-sac-water-affordability.pdf>

income taxpayers.³ If tenants receive a 1099 for water bill assistance, this may make it less likely that they file a return, fearing incorrectly that they will owe money to the IRS. If they fail to file a tax return, they then will not receive the tax refund that they are entitled to.

Amid rising water unaffordability, localities need the clarity of SB0380 to innovate systemic solutions.

Water bill assistance is critical to achieving affordability for Maryland’s low-income homeowners and renters. The U.S. Environmental Protection Agency defines water unaffordability at more than 2 percent of household income.⁴ The Maryland Advisory Committee to the U.S. Committee on Civil Rights found that “[u]nder this definition, water is unaffordable across the state of Maryland. In fact, for households at 50 percent of the federal poverty rate, water is only affordable in three of the state’s 38 PUMAs (Public Use Microdata Areas).”⁵

Water and sewer service rates have increased sharply in recent years. The increasing cost is not isolated to Baltimore City, where repair of aging systems drove up rates by 30% between 2019 and 2021 and will continue to push rates by 3% annually from 2022 through 2025.⁶ Facing similar infrastructure and budget needs, WSSC implemented back-to-back rate hikes of over 6% over the past two years in Montgomery County and Prince George’s County.⁷ Last year, the private company Maryland Water Service, Inc.’s 3,500 customers faced rate hikes of 30% in Bel Air and Joppa, 68% in Cumberland, and 255% in Severn.⁸

While federal dollars have recently become available for water bill assistance, first through the CARES Act and presently in the form of the Low Income Household Water Assistance Program, localities must anticipate that federal funding will taper off or fail to cover the full extent of need. It will be necessary for localities to innovate long-term affordability mechanisms.

³ IRS Press Release, March 25, 2022, <https://www.irs.gov/newsroom/irs-has-1-point-5-billion-in-refunds-for-people-who-have-not-filed-a-2018-federal-income-tax-return-april-deadline-approaches>.

⁴ *Id.* at 7.

⁵ *Id.*

⁶ Colin Campbell, “Baltimore water rates will increase 30 percent in next three years,” The Baltimore Sun, Jan. 9, 2019, <https://www.baltimoresun.com/maryland/baltimore-city/bs-md-ci-water-rate-hike-20190109-story.html>; Baltimore City Public Works, FY 2023-2025 Water/Sewer/Stormwater Rates, <https://publicworks.baltimorecity.gov/proposed-rates>.

⁷ Steve Bohnel, “County Council recommends up to 7% increase in WSSC water rates for upcoming year,” MoCo360, Nov. 1, 2022, <https://moco360.media/2022/11/01/county-council-recommends-up-to-7-increase-in-wssc-water-rates-for-upcoming-year>.

⁸ Elizabeth Janney, “Proposed Water Rate Hike In Bel Air Prompts Hearing,” Patch.com, Feb. 7, 2022, <https://patch.com/maryland/belair/proposed-water-rate-hike-bel-air-prompts-hearing>.

Baltimore City is a shining example of such innovation. In 2019, Baltimore City Council passed robust measures to limit water and sewer costs to 3 percent of household income. The Water Accountability and Equity Act (WAEA) enacted income-based water and sewer billing for both homeowners and renter households earning less than 200% of the federal poverty level. Instead of cutting some residents out of the program, WAEA extends this affordability measure even to tenants in multi-unit, master-metered buildings. As described above, implementation of “Water for All” raises challenging questions. SB0380 will help the City of Baltimore answer those questions and continue building out a bold program. Equally, for the benefit of constituents outside Baltimore, HB0538 achieve would bring clarity needed by any local governments that are or may become interested in income-based billing.

Because this bill clarifies that water bill assistance is categorically not taxable, **Maryland Legal Aid urges the Committee to issue a FAVORABLE report on SB0380.** If you have any questions, please contact William Steinwedel, (410) 951-7643, wsteinwedel@mdlaborg.org, or Zafar Shah, (410) 951-7672, zshah@mdlaborg.org.