

Department of Legislative Services
 Maryland General Assembly
 2022 Session

FISCAL AND POLICY NOTE
 Enrolled - Revised

Senate Bill 405

(The President, *et al.*) (By Request - Administration)

Budget and Taxation

Ways and Means

**Income Tax - Retirement Income Subtraction Modifications and Senior Credit
 (Retirement Tax Elimination Act of 2022)**

This Administration bill creates a nonrefundable credit against the State income tax for a resident (1) who is at least age 65 and (2) whose federal adjusted gross income does not exceed \$100,000 (\$150,000 if married filing jointly). The amount of the tax credit is equal to (1) \$1,000 for an individual or if only one of the individuals filing a joint return is an eligible individual and (2) \$1,750 if married filing jointly and both individuals are at least age 65. The value of the tax credit is reduced for certain taxpayers if specified Board of Revenue Estimates are below a certain amount. The bill also expands the State subtraction modification for retired law enforcement; correctional officer; and fire, rescue, and emergency services personnel. **The bill takes effect July 1, 2022, and applies to tax year 2022 and beyond.**

Fiscal Summary

State Effect: General fund revenues decrease by \$291.9 million in FY 2023. The FY 2023 general fund revenue loss is accounted for by the \$350.0 million in tax relief assumed in the FY 2023 budget. Future year revenues reflect projected growth in eligible taxpayers and retirement income. General fund expenditures may increase by \$80,000 in FY 2023 due to implementation costs at the Comptroller’s Office.

| (\$ in millions) | FY 2023 | FY 2024 | FY 2025 | FY 2026 | FY 2027 |
|------------------|-----------|-----------|-----------|-----------|-----------|
| GF Revenue | (\$291.9) | (\$301.6) | (\$311.6) | (\$321.9) | (\$332.5) |
| GF Expenditure | \$0.1 | \$0 | \$0 | \$0 | \$0 |
| Net Effect | (\$292.0) | (\$301.6) | (\$311.6) | (\$321.9) | (\$332.5) |

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

Local Effect: Local income tax revenues will decrease by slightly less than \$600,000 annually beginning in FY 2023. Local expenditures are not affected.

Small Business Effect: The Administration has determined that this bill has a meaningful impact on small business (attached). The Department of Legislative Services (DLS)

disagrees with the assessment as discussed below. (The attached assessment does not reflect amendments to the bill).

Analysis

Bill Summary:

Senior Tax Credit

For a tax year in which the current fiscal year general fund estimate in the September Board of Revenue Estimates report is more than 7.5% below the March general fund estimate issued in the same year, the amount of the tax credit is limited to (1) \$500 for an individual whose federal adjusted gross income is between \$50,000 and \$100,000 and (2) \$875 for married filing jointly with federal adjusted gross income of between \$100,000 and \$150,000 (\$500 if married filing jointly and only one individual is at least age 65).

Retired Law Enforcement; Correctional Officer; and Fire, Rescue, and Emergency Services Personnel

Under current law, the maximum value of the subtraction modification for retired law enforcement; correctional officer; and fire, rescue, and emergency services personnel who are age 55 to 64 is reduced by the amount of Social Security benefits received. After this adjustment, the maximum value is further limited to \$15,000. Retired law enforcement officers; correctional officers; and fire, rescue, or emergency services personnel who are age 65 or older or are totally disabled qualify and claim the State pension exclusion in the same manner as other eligible retirees as described below.

Beginning in tax year 2022, the bill allows all eligible individuals for retired law enforcement; correctional officer; and fire, rescue, and emergency services personnel who are at least age 55 to exempt the first \$15,000 in qualified retirement income. This subtraction modification is not reduced by the amount of Social Security benefits received and replaces the existing subtraction modification that can be claimed under current law. Retirees who are at least age 65 or are totally disabled can qualify and claim the State pension exclusion for retirement income that is not excluded under this retirement income subtraction.

Current Law:

State Pension Exclusion – All Eligible Individuals

Maryland law provides a pension exclusion (in the form of a subtraction modification) for individuals who are at least 65 years old or who are totally disabled. Under this subtraction

modification, up to a specified maximum amount of taxable pension income (\$34,300 for 2021) may be exempt from tax. The maximum exclusion allowed is indexed to the maximum annual benefit payable under the Social Security Act and is reduced by the amount of any Social Security payments received (Social Security offset). Military retirees who are at least age 65 or are totally disabled can qualify and claim the State pension exclusion for retirement income that is not excluded under the military retirement income subtraction.

Social Security benefits and benefits received under the federal Railroad Retirement Act are totally exempt from the Maryland income tax, even though they may be partly taxable for federal income tax purposes. In addition to the special treatment of Social Security and other retirement income, other income tax relief is provided to senior citizens regardless of the source of their income. In addition to the regular personal exemption available to all taxpayers, an additional exemption amount of \$1,000 may be claimed by an elderly or blind individual.

Law Enforcement Officers; Correctional Officers; and Fire, Rescue, or Emergency Services Personnel

Retired law enforcement officers; correctional officers; and fire, rescue, or emergency services personnel who are age 65 or older or are totally disabled qualify and claim the State pension exclusion in the same manner as other eligible retirees as described above.

Chapters 153 and 154 of 2017 established a pension exclusion for retired law enforcement officers or fire, rescue, or emergency services personnel. Retirement income qualifies for this exclusion if the individual is between the ages of 55 and 64, and the retirement income is attributable to employment as a law enforcement officer or as a fire, rescue, or emergency services personnel of the United States, the State, or a local jurisdiction. Emergency services personnel includes emergency medical technicians and paramedics.

Chapters 573 and 581 of 2018 extended eligibility to correctional officers. An eligible retiree includes an individual who was employed in (1) a State correctional facility; (2) a local correctional facility; (3) a juvenile facility; and (4) a facility of the United States that is equivalent to a State or local correctional facility or juvenile facility in the State.

The maximum exclusion in the tax year is limited to \$15,000.

State Revenues: Beginning with tax year 2022, the bill (1) creates a nonrefundable tax credit for certain residents who are at least age 65 and (2) expands the State subtraction modification for retired law enforcement; correctional officer; and fire, rescue, and emergency services personnel. As a result, State revenues will decrease by \$291.9 million in fiscal 2023. **Exhibit 1** shows the projected State revenue loss from the bill.

Exhibit 1
Projected State Revenue Loss
Fiscal 2023-2027
(\$ in Millions)

| | <u>FY 2023</u> | <u>FY 2024</u> | <u>FY 2025</u> | <u>FY 2026</u> | <u>FY 2027</u> |
|---------------------------|-----------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| Senior Tax Credit | (\$291.2) | (\$300.8) | (\$310.7) | (\$320.9) | (\$331.5) |
| Subtraction Modification* | (0.8) | (0.8) | (0.9) | (1.0) | (1.0) |
| Total | (\$291.9) | (\$301.6) | (\$311.6) | (\$321.9) | (\$332.5) |

**Retired Law Enforcement; Correctional Officer; and Fire, Rescue, and Emergency Services Personnel*

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

Source: Comptroller's Office; Department of Legislative Services

The tax credit estimate reflects the impact the credit would have had in tax year 2020 and increased by about 4% annually to reflect growth in tax returns. In tax year 2020, about 310,000 taxpayers would have benefited from the proposed tax credit.

The subtraction modification estimate is based on the number of retirees who claimed the subtraction modification in tax year 2020, adjusted for the provisions of the bill.

State Expenditures: The Comptroller's Office reports that it may incur a one-time general fund expenditure increase of \$80,000 in fiscal 2023 for data processing changes to the income tax return processing and imaging systems and systems testing.

Local Revenues: Local income tax revenues decrease by about 3% of the total net State subtraction modifications claimed. Local revenues will decrease by slightly less than \$600,000 annually beginning in fiscal 2023.

Small Business Impact: DLS notes that the primary beneficiaries of the bill are not small businesses. A portion of the proposed income tax reduction may be used by individuals for additional spending at Maryland small businesses; however, this potential benefit does not account for any negative impact to small businesses that could result from a reduction in spending and/or an increase in taxes that may be needed in order to balance State and local budgets.

Additional Information

Prior Introductions: None.

Designated Cross File: HB 420 (The Speaker, *et al.*) (By Request - Administration) - Ways and Means.

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

Fiscal Note History: First Reader - March 18, 2022
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ANALYSIS OF ECONOMIC IMPACT ON SMALL BUSINESSES

TITLE OF BILL: Retirement Tax Elimination Act of 2022

BILL NUMBER: SB 405

PREPARED BY: Governor's Legislative Office

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

While there are other reasons for retirees to leave the State, it is clear that financial reasons are a factor. Studies indicate that Maryland ranks near the bottom in the country in being tax friendly to retirees and that more retirees migrate from the State than to the State. This bill will encourage retirees to stay in the State and further will be an incentive for retirees who live in other states to migrate here. This will benefit small businesses frequented by retirees.

This bill will also provide retirees who live in the State with more income that they can use at small businesses. While it is not possible to quantify the impact of this bill on small businesses we believe it will have a significant positive impact.