Department of Legislative Services

Maryland General Assembly
2019 Session

FISCAL AND POLICY NOTE
First Reader

House Bill 1046 (Delegate Johnson, *et al.*)
Ways and Means

Income Tax Subtraction Modification - Qualified Retired Public Safety Employee (Hometown Heroes Act of 2019)

This bill expands the State income tax subtraction modification for retired law enforcement; correctional officers; and fire, rescue, or emergency services personnel by (1) exempting 100% of eligible retirement income, phased in over two years and (2) extending eligibility to retirees who are between age 50 and 54. **The bill takes effect July 1, 2019, and applies to tax year 2020 and beyond.**

Fiscal Summary

State Effect: General fund revenues decrease by $6.9 million in FY 2021 due to additional retirement income being exempted. Future year estimates reflect projected growth in retirement income and the phase-in specified by the bill. Expenditures are not affected.

($ in millions)	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024
GF Revenue	$0	($6.9)	($16.0)	($16.4)	($16.7)
Expenditure	0	0	0	0	0
Net Effect	$0.0	($6.9)	($16.0)	($16.4)	($16.7)

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

Local Effect: Local revenues decrease by $4.5 million in FY 2021 and by $10.9 million in FY 2024. Local expenditures are not affected.

Small Business Effect: None.

Analysis

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 ($30,600 for 2018) 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).

The "Social Security offset" is the reduction in the maximum pension exclusion allowed under current law for an individual. The Social Security offset was established at the same time as the pension exclusion. Given that Social Security benefits are exempt from Maryland income tax even though benefits are partially taxable for federal purposes, the offset works to equalize the tax treatment of individuals who receive their retirement benefits from different sources by reducing the amount of the allowable exclusion by the amount of any Social Security benefits received.

One significant feature of the current pension exclusion is that it is limited to income received from an employee retirement system. Eligible employee retirement systems are retirement plans established and maintained by an employer for the benefit of its employees and qualified under Sections 401(a), 403, or 457(b) of the Internal Revenue Code. These include defined benefit and defined contribution pension plans, 401(k) plans, 403(b) plans, and 457(b) plans. However, individual retirement arrangements, Keogh plans, and simplified employee pension plans are not considered employee retirement systems.

Law Enforcement Officer; Correctional Officer; 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. The maximum exclusion in the tax year is limited to $15,000.

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.

State Revenues: Additional retirement income may be exempted from the State income tax beginning in tax year 2020. It is assumed that individuals (1) do not adjust withholdings and estimated payments and (2) can claim a subtraction modification equal to the greater of 50% or $15,000 in tax year 2020. As a result, general fund revenues decrease by $6.9 million in fiscal 2021. **Exhibit 1** shows the estimated impact of the bill on State and local revenues.

Exhibit 1
State and Local Revenue Impacts
Fiscal 2020-2024
($ in Millions)

	FY 2020	FY 2021	FY 2022	FY 2023	FY 2024
State	$0.0	($6.9)	($16.0)	($16.4)	($16.7)
Local	0.0	(4.5)	(10.5)	(10.7)	(10.9)
Total Revenues	**$0.0**	**($11.4)**	**($26.5)**	**($27.0)**	**($27.6)**

The estimated impact of exempting additional public safety retirement income is based on the number of retirees who claimed the subtraction modification in tax year 2017. This estimate is increased to account for (1) correctional officers and those employed in a correctional facility or juvenile facility who were not eligible in tax year 2017 and (2) the expansion to public safety retirees who are between age 50 and 54.

Local Revenues: Local income tax revenues decrease as a result of subtraction modifications claimed against the personal income tax. Local revenues decrease by $4.5 million in fiscal 2021 and by $10.9 million in fiscal 2024, as shown in Exhibit 1.

Additional Information

Prior Introductions: None.

Cross File: None.

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

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an/hlb

Analysis by: Robert J. Rehrmann

Direct Inquiries to:
(410) 946-5510
(301) 970-5510