HB 460

Department of Legislative Services
Maryland General Assembly
2005 Session

FISCAL AND POLICY NOTE

House Bill 460 (Delegate Cluster, *et al.*)
Ways and Means

Income Tax - Subtraction Modification for Teachers' Retirement Income

This bill creates a subtraction modification under the Maryland income tax for the first $5,000 in income resulting from the retirement income of a State elementary or secondary public school teacher. Teacher retirement income exempted under this bill cannot be counted towards the State pension exclusion exemption.

The bill takes effect July 1, 2005 and applies to tax year 2005 and beyond.

Fiscal Summary

State Effect: General fund revenues could decrease by approximately $5.5 million in FY 2006. Out-year revenue losses reflect a 4% annual increase in the number of eligible retirees. No effect on expenditures.

($ in millions)	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
GF Revenue	($5.5)	($5.7)	($6.0)	($6.2)	($6.5)
Expenditure	$0	$0	$0	$0	$0
Net Effect	($5.5)	($5.7)	($6.0)	($6.2)	($6.5)

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

Local Effect: Local revenues would decrease by approximately $3.6 million in FY 2006, increasing to $4.3 million by FY 2010. Expenditures would not be affected.

Small Business Effect: None.

Analysis

Current Law: There is no subtraction modification specifically for teachers' retirement income, but the retirement income received by a teacher is eligible for the State pension exclusion.

Maryland law provides a pension exclusion subtraction 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 ($20,700 maximum for 2004) 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. The pension exclusion has been a part of the Maryland income tax since 1965.

The "Social Security offset" is the reduction in the maximum pension exclusion allowed under the current law by the 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, the offset works to equalize the tax treatment of individuals who receive their retirement benefits from different sources by reducing the amount of Social Security benefits received.

Additional Income Tax Treatment for Elderly Individuals

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 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. Each individual age 65 or older: (1) is allowed a $1,000 personal exemption in addition to the regular exemption of $2,400 allowed to all individuals; and (2) can earn more income without being required to file taxes.

State Revenues: Subtraction modifications could be claimed beginning in tax year 2005. As a result, general fund revenues would decrease by approximately $5.5 million in fiscal 2006. Future year losses increase by approximately 4% annually.

The estimate is based on the following facts and assumptions:

- there were 45,496 retirees in the State teachers' retirement and pension systems in fiscal 2004;

- based on federal Bureau and Labor Statistics data, it is estimated that 62% of the retirees in the teachers' retirement and pension systems are elementary and secondary teachers who would qualify for the proposed subtraction modification;

- for tax year 1997, approximately 38% of returns with pension income also had a pension exclusion. Therefore, it is assumed that 62% of eligible teacher retirees would claim the proposed subtraction modification;

- approximately 19% of retirees live out-of-state and will not claim the subtraction modification;

- the number of retirees in the State teachers' retirement and pension systems increased by approximately 4% annually from 1997 to 2003. It is assumed that this rate of increase continues from 2004 to 2009.

Local Revenues: Local revenues would decrease by approximately 3.1% of the State subtraction taken in tax year 2005. In fiscal 2006 the decrease would be approximately $3.6 million. Future year revenues decrease as the amount of the total State subtraction increases, totaling approximately $3.8 million in fiscal 2007, $4.0 million in fiscal 2008, $4.2 million in fiscal 2009, and $4.3 million in fiscal 2010.

Additional Information

Prior Introductions: SB 709/HB 791, identical bills, were introduced at the 2004 session. HB 791 received an unfavorable report from the House Ways and Means Committee. SB 709 was withdrawn.

Cross File: None.

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

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