

Department of Legislative Services  
 Maryland General Assembly  
 2000 Session

FISCAL NOTE  
 Revised

Senate Bill 490 (Senators Jacobs and Hooper)

Budget and Taxation

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**Income Tax - Subtraction Modification - Military Compensation**

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This bill extends eligibility for the subtraction modification for military pay under the Maryland State income tax to all active duty military personnel.

This bill takes effect July 1, 2000, and applies to all taxable years beginning after December 31, 1999.

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**Fiscal Summary**

**State Effect:** General fund revenues would decrease by an estimated \$14.6 million in FY 2001. Future years reflect 3.5% annual wage growth, 1% personnel increases, and reduced income tax rates. No effect on expenditures.

(in millions)	FY 2001	FY 2002	FY 2003	FY 2004	FY 2005
GF Revenues	(\$14.6)	(\$14.2)	(\$13.9)	(\$13.6)	(\$13.3)
GF Expenditures	0.0	0.0	0.0	0.0	0.0
Net Effect	(\$14.6)	(\$14.2)	(\$13.9)	(\$13.6)	(\$13.3)

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

**Local Effect:** Total local government revenue loss of approximately \$8.1 million in FY 2001; \$7.9 million in FY 2002; \$7.8 million in FY 2003; \$7.6 million in FY 2004; and \$7.4 million in FY 2005.

**Small Business Effect:** None.

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## Analysis

**Current Law:** Military personnel serving overseas are allowed a subtraction modification under the State income tax. The amount of the exemption varies depending on the individual's rate of pay. The subtraction includes the first \$15,000 of military pay that is: (1) attributable to military service of the individual who is in active service of any branch of the armed forces; and (2) attributable to military service of the individual outside the United States. In addition, the amount of the subtraction is: (1) reduced dollar for dollar in the amount by which military pay received by the individual exceeds \$15,000; and (2) reduced to zero if the amount of military pay received by the individual exceeds \$30,000.

**Background:** Under federal law, military personnel (including former military personnel) may exclude from gross income any qualified military benefits that they receive. Qualified military benefits include any allowance or in-kind benefit that:

- U.S. armed forces members or their dependents receive by virtue of the members' status or service in the military; and
- the member could exclude from gross income on September 9, 1986, under another law, regulation, or administrative practice in effect at that time.

To qualify as a qualified military benefit, the benefit must meet one of two criteria. Either it must meet the definition listed above or it must qualify for exclusion from gross income under some other section of the Internal Revenue Code.

Military personnel below the grade of commissioned officer may exclude from gross income any compensation they receive while serving in a combat zone. For commissioned officers, the exclusion is limited to the maximum amount of combat-zone pay for enlisted personnel.

A combat zone means any area that the President designates, by executive order, as an area in which U.S. armed forces are or have been engaged in combat. A combat zone includes a qualified hazardous duty area. Recent examples of qualified hazardous duty areas include Bosnia, Herzegovina, Croatia, and Macedonia.

This combat pay deduction flows through to the Maryland income tax since the Maryland form begins with federal adjusted gross income.

**State Fiscal Effect:** The exhibit below presents the savings to an enlisted member of the armed forces who lists Maryland as his or her home state of record. The individual is assumed to be stationed in Maryland and receives \$14,500 in military pay for tax year 2000. As the exhibit indicates, the State tax savings to the individual as a result of the bill is \$703.

**State Tax Savings For Tax Year 2000 Resulting from Military Income Subtraction**

	<u>Current Law</u>	<u>SB 490</u>
Subtraction Allowed	\$0	\$14,500
State Tax Savings	\$0	\$703

General fund revenues would decrease by approximately \$14.6 million in fiscal 2001 based on the following facts and assumptions.

- There were 20,611 active duty military personnel whose home state of record was Maryland in 1998 with wages totaling \$306,974,717 (average pay of \$14,894).
- Personnel will increase by 1% annually and wages will grow by about 3.5% annually.

Military personnel who are stationed in Maryland, but whose home state of record is not Maryland, are not subject to the Maryland State income tax.

To the extent that wages grow at a rate that is more or less than 3.5% annually, the general fund revenue loss will be more or less than estimated.

**Local Fiscal Effect:** Local revenues would decline by approximately 2.67% of the total subtraction taken, or 55% of the State loss, for military income. Based on the estimate above, the reduction would be \$8.1 million for fiscal 2001.

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## Additional Information

**Prior Introductions:** None.

**Cross File:** A similar bill (HB 171) was introduced in the House and assigned to the House Ways and Means Committee.

**Information Source(s):** Comptroller of the Treasury (Bureau of Revenue Estimates), Department of Legislative Services

**Fiscal Note History:** First Reader - February 14, 2000

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Analysis by: Mike Sanelli

Direct Inquiries to:  
John Rixey, Coordinating Analyst  
(410) 946-5510  
(301) 970-5510