HB 1215

Department of Legislative Services

Maryland General Assembly
2004 Session

FISCAL AND POLICY NOTE

House Bill 1215 (Delegate O'Donnell)
Ways and Means

Income Tax - Subtraction Modification for Military Retirement Income

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This bill increases from $2,500 to $5,000 the maximum amount allowed under the income tax subtraction modification for military retirement income. The bill repeals the requirements that an individual be at least 55 years old on the last day of the taxable year and have been an enlisted member of the military at the time of the retirement. The bill increases from $17,500 to $35,000 the level of federal adjusted gross income above which the maximum subtraction is reduced. The level of adjusted gross income at which no subtraction is allowed is increased from $22,500 to $45,000.

The bill takes effect July 1, 2004 and applies to tax year 2004 and beyond.

Fiscal Summary

State Effect: General fund revenues would decrease by $4.2 million in FY 2005. Out-year revenue losses reflect a 1.2% annual increase in the number of retirees and a 2.5% average annual increase in military retirement income. Expenditures would not be affected.

($ in millions)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
GF Revenue	($4.2)	($4.3)	($4.4)	($4.4)	($4.5)
Expenditure	$0	$0	$0	$0	$0
Net Effect	($4.2)	($4.3)	($4.4)	($4.4)	($4.5)

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

Local Effect: Local revenues would decrease by approximately $2.6 million in FY 2005 increasing to $2.7 million in FY 2009. Expenditures would not be affected.

Small Business Effect: None.

Analysis

Current Law: Social Security benefits and benefits received under the Railroad Retirement Act are totally exempt from the Maryland income tax, even though they may be partly taxable for federal income tax purposes.

Maryland law also provides a pension exclusion subtraction for individuals who are at least 65 years old or who are totally disabled. Under the subtraction modification, some taxable pension income ($19,900 for 2003) may be exempt from tax. The maximum exclusion is the maximum annual benefit under the Social Security Act and is reduced by the amount of any Social Security payments received. Thus, a retiree is allowed to deduct the lesser of: (1) the amount of pension income actually received; or (2) the maximum Social Security benefit reduced by the amount of Social Security received. For tax year 1995 the average amount excluded under this pension exclusion was just over $6,500. The pension exclusion is estimated to cost the State approximately $60 million a year.

An additional exclusion is provided for military retirement income. Under State law, the first $2,500 of military retirement income received by an individual can be subtracted from federal adjusted gross income for the taxable year provided that the individual is at least 55 years of age on the last day of the taxable year and was an enlisted member of the military at the time of retirement. This subtraction is reduced by 50% of the amount by which the federal adjusted gross income exceeds $17,500. No subtraction is allowed for individuals having federal adjusted gross income over $22,500.

State Fiscal Effect: General fund revenues would decrease by $4.2 million in tax year 2004. It is assumed that the State revenue reductions would occur in the fiscal year following the year that tax returns were filed. Consequently, general fund revenues decrease by $4.2 million in fiscal 2005. The estimate is based on the following facts and assumptions:

- according to the Department of Defense, $879,163,000 was paid to 46,262 military retirees in Maryland in tax year 2002;

- average military retirement income for these retirees was $19,004;

- according to the *2003 Retired Military Almanac*, 70.5% of active duty military were formerly enlisted personnel;

- approximately 60% of U.S. veterans were ages 55 and over in 1999, according to the *2000 U.S. Statistical Abstract;* and

- the number of retirees increases by 1.2% annually and average military retirement pay increases by 2.5% annually.

Local Fiscal Effect: Local revenues would decrease by approximately 2.8% of the State subtraction taken in tax year 2004. In fiscal 2005 the decrease would be approximately $2.6 million. Future year revenues would decrease by approximately 1.2% annually as the amount of the total State subtraction increases.

Additional Information

Prior Introductions: HB 601 of 2003, HB 408 of 2002, and HB 446 of 2001 were not reported from the House Ways and Means Committee.

Cross File: None.

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

Fiscal Note History: First Reader - March 17, 2004
mh/mdr

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