

Department of Legislative Services  
Maryland General Assembly  
2006 Session

FISCAL AND POLICY NOTE

Senate Bill 666

(Senator Middleton, *et al.*)

Budget and Taxation

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**Income Tax - Subtraction Modification - Retired Military Personnel Employed  
in Critical Workforce Areas**

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This bill creates a subtraction modification for the first \$20,000 in income received by a U.S. armed forces retiree that is attributable to employment in the State: (1) as a school teacher; (2) as a firefighter; (3) as an ambulance or rescue squad member; or (4) in a health care occupation that is either determined to be in an area of shortage or eligible to receive health personnel shortage incentive grants.

The bill takes effect July 1, 2006 and applies to tax years 2006 through 2010. The bill terminates December 31, 2010.

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**Fiscal Summary**

**State Effect:** General fund revenues could decrease significantly in FY 2007 through 2011 due to subtraction modifications being claimed against the personal income tax by eligible individuals (maximum \$950 per eligible individual). The amount of decrease depends on the number of individuals who work in qualifying occupations specified by the bill and cannot be reliably estimated. Expenditures would not be affected.

**Local Effect:** Local income tax revenues would decrease by approximately 3% of the total State subtraction modification taken (maximum \$600 per eligible individual). Local income tax revenues could decrease significantly in FY 2007 through 2011.

**Small Business Effect:** None.

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## Analysis

**Current Law:** Military retirees can qualify for existing tax credits as discussed below.

A subtraction modification 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.

Maryland law also 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 (\$21,500 maximum for 2005) 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 allowable exclusion by 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 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. 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.

**Background:** Chapter 94 of 2003 established the Task Force to Study the Financial Impact of Retired Military Service Personnel on the Economy of the State. The task force issued its final report in December 2003. Among its findings was that in 2000 there were approximately 42,600 military retirees living in Maryland. The task force estimated

that median household income of military retirees was \$71,484 compared with a median household income of \$42,151 for all Maryland households. The average income reported by military retirees was \$83,435, of which \$18,266 was attributable to retirement pay and \$65,169 was derived from second career employment and other sources. These military retiree households were estimated to pay approximately \$163 million in State and local income taxes. Approximately one-half of military retirees were under the age of 60 and a little more than one-quarter were 50 years old or younger.

According to the Defense Manpower Data Center (DMDC), 44,014 military retirees received retirement income from the Department of Defense (DoD) in the month of September 2004. This includes individuals who served in the Army (including Maryland National Guard), Navy, Marines, and Air Force. In addition, DMDC reports that 1,083 Coast Guard retirees received retirement income.

According to the Bureau of Labor Statistics (BLS), approximately 13,240 individuals in November 2004 were employed as firefighters or emergency medical services personnel. There were approximately 56,200 public school teachers in 2004 and approximately 13,800 private school teachers in 2001. Generally, new public school teachers are required to have teaching degrees, although some hires can qualify under a conditional license or under the limited resident teacher certificate program. Qualifications for private school teachers vary and are not subject to State certifying standards.

Health occupations that can qualify under the health personnel shortage incentive grant program include physical, respiratory, and occupational therapists; radiographers, lab technicians; medical technologists; pharmacists; registered nurses or licensed practical nurses; and family practice physicians.

Health occupations that can qualify as being an area of shortage include cytotechnologists; radiation technologists; hospital pharmacists; physical, respiratory, and occupational therapists; and registered nurses or licensed practical nurses.

**State Revenues:** The bill provides that subtraction modifications could be claimed by eligible individuals beginning in tax year 2006. General fund revenues could decrease significantly in fiscal 2007 through 2011 due to subtraction modifications being claimed against the personal income tax by eligible individuals. The amount of the decrease depends on the number of individuals who work in qualifying occupations specified by the bill and cannot be reliably estimated.

In addition to military retirees who are hired in a qualifying occupation in the future, military retirees who already work in a qualifying occupation can also claim the subtraction modification. This total amount of eligible individuals in each year cannot be

reliably estimated at the time. However, general fund revenues would decrease by a maximum of \$950 per eligible individual. Local government revenues would decrease by approximately \$600 per eligible individual.

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### **Additional Information**

**Prior Introductions:** None.

**Cross File:** None.

**Information Source(s):** Bureau of Labor Statistics, Maryland State Department of Education, National Center for Education Statistics, Department of Legislative Services

**Fiscal Note History:** First Reader - March 20, 2006  
ncs/hlb

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