HB 195

Department of Legislative Services
2013 Session

FISCAL AND POLICY NOTE

House Bill 195 (Delegate Cardin, *et al.*)
Ways and Means

Income Tax - Subtraction Modification - Military Health Care Pensions - Health Care Workforce Shortage

This bill expands the existing military retirement income subtraction modification by exempting 50% of the specified military retirement income of an individual who commits to living and working in the State for a period required by the Comptroller and works in a health care field identified as having a health care workforce shortage. In order to qualify, the individual must have federal adjusted gross income (FAGI) of $65,000 or less. The Comptroller's Office is required to adopt regulations, in consultation with the Department of Health and Mental Hygiene (DHMH) and the Governor's Workforce Investment Board, to implement the provisions of the bill.

The bill takes effect July 1, 2013, and applies to tax year 2014 and beyond.

Fiscal Summary

State Effect: General fund revenues may decrease beginning in FY 2015 due to additional retirement income being exempted. Assuming 250 individuals qualify for the exemption each year, State revenues decrease by $121,300 annually. Expenditures are not affected.

(in dollars)	FY 2014	FY 2015	FY 2016	FY 2017	FY 2018
GF Revenue	$0	($121,300)	($121,300)	($121,300)	($121,300)
Expenditure	0	0	0	0	0
Net Effect	$0	($121,300)	($121,300)	($121,300)	($121,300)

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

Local Effect: Local income tax revenues may decrease beginning in FY 2015 due to additional retirement income being exempted. Under the assumption above, local revenues decrease by $76,600 annually. Expenditures are not affected.

Small Business Effect: None.

Analysis

Current Law: Chapter 226 of 2006 (SB 22) expanded a $2,500 military retirement income subtraction that was previously limited to enlisted military members with a federal adjusted gross income of $22,500 or less. Under Chapter 226, an individual may exempt the first $5,000 of military retirement income from State and local taxation if the retirement income resulted from service in an active or reserve component of the Armed Forces of the United States or in the Maryland National Guard.

Under Chapter 226, retirees from active duty with the Commissioned Corps of the Public Health Service, National Oceanic and Atmospheric Administration (NOAA), or the Coast and Geodetic Survey qualified for the subtraction modification, but only if separated from service after July 1, 1991. Chapter 552 and 553 of 2007 (SB 419/HB 392) eliminated this restriction and allowed all of the individuals described previously to qualify for the subtraction modification, without regard to the date of separation from employment.

Maryland law also provides a pension exclusion subtraction modification for individuals who are at least age 65 or who are totally disabled. Up to a specified maximum amount of taxable pension income ($27,100 for 2012) 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. Military retirement income exempted under the subtraction modification cannot be counted toward the State pension exclusion.

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. In addition to the regular personal exemption available to all taxpayers, an additional exemption amount of $1,000 may be claimed by an elderly or blind individual. Each individual age 65 or older can also earn more income without being required to file taxes.

Background: According to the Defense Manpower Data Center (DMDC), 49,681 military retirees received a total of $112.0 million in retirement income from the Department of Defense in September 2011. This includes individuals who served in the Army (including the Maryland National Guard), Navy, Marines, and Air Force. On an annualized basis, this retirement income totaled $1.34 billion. This amount includes retirees who receive disability payments. Disability payments resulting from active service in the Armed Forces, NOAA, Public Health Service, or the foreign service are not taxable for State income tax purposes because those payments are exempt from federal taxation. In addition, DMDC reports that 1,302 Coast Guard retirees and 7,100 military and Coast Guard survivors received retirement income during 2011.

According to the Office of Commissioned Corps Force Management Information System, 762 Maryland residents who retired from the Commissioned Corps of the Public Health Service received a total of $52.1 million, or an average of $68,300, in retirement income during 2005.

State Revenues: Additional retirement income may be exempted beginning in tax year 2014. As a result, general fund revenues will decrease beginning in fiscal 2015. However, the amount of the revenue loss cannot be reliably estimated and depends on the percentage of military retirees in the State who are qualified to work as health care workers, and would opt to work and meet the requirements of the bill. Given that the average military pension received in 2011 was about $27,000, an individual will typically qualify only if the individual's additional yearly income (including compensation from the eligible health care job) was less than $38,000.

General fund revenues decrease in fiscal 2015 by an estimated $510 for each qualifying retiree under age 65 and by $260 for each retiree age 65 and over. **Exhibit 1** lists the total estimated revenue losses depending on the number of retirees who qualify. It is assumed that one-tenth of eligible individuals are age 65 and over.

Individuals under age 65 would benefit on average by a greater amount since they do not qualify for the State pension exclusion, which can be used to exempt military retirement income above and beyond any amount subtracted under the current military retirement income subtraction modification. Revenue losses will also depend on the extent of time an individual receives the tax benefit.

Exhibit 1
State and Local Revenue Loss

Number of Qualifying Retirees	State	Local
50	$24,300	$15,300
100	48,500	30,600
250	121,300	76,600
500	242,500	153,200
750	363,800	229,800
1,000	485,000	306,300

Local Revenues: Local income tax revenues decrease by about 3% of the total net State subtraction modification claimed in tax year 2014. Exhibit 1 lists the potential local income tax revenue impact beginning in fiscal 2015.

Additional Information

Prior Introductions: HB 532 of 2012 received a hearing in the House Ways and Means Committee, but no further action was taken. Similar legislation was introduced in the 2009 and 2010 sessions. HB 722 of 2010 received a hearing in the House Ways and Means Committee, but no further action was taken. HB 536 of 2009 received a hearing in the House Ways and Means Committee, but was subsequently withdrawn.

Cross File: None.

Information Source(s): Comptroller's Office, Defense Manpower Data Center, Department of Defense (Office of Actuary), National Oceanic and Atmospheric Administration, Office of Commissioned Corps Force Management Information System, Department of Legislative Services

Fiscal Note History: First Reader - February 7, 2013
ncs/jrb

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