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FISCAL IMPACT REPORT

SPONSOR Duran DATE TYPED 3/01/2005 HB _____

SHORT TITLE Income Tax Deduction for Military Pensions SB 852

ANALYST Taylor

REVENUE

| Estimated Revenue | | Subsequent Years Impact | Recurring or Non-Rec | Fund Affected |
|-------------------|--------------|----------------------------|-------------------------|------------------|
| FY05 | FY06 | | | |
| (\$6,000.0) | (\$12,000.0) | (Similar) | Recurring | General Fund |

(Parenthesis () Indicate Revenue Decreases)

Relates to HB 27, HB 50, SB 450, SB 94, SB349

SOURCES OF INFORMATION

LFC Files
Taxation and Revenue Department (TRD)

SUMMARY

Senate Bill 852 provides a state income tax exemption for military retirement pensions, provided the person was honorably discharged and served continuously for 90 days in the U.S. Armed Forces. The bill is applicable to tax years beginning on or after January 1, 2005.

FISCAL IMPLICATIONS

This bill would decrease state income tax revenues by an estimated \$ 6.0 million in FY05 and \$12.0 million in FY06 million and subsequent years. Assumptions used to derive this estimate are based on information provided by the Taxation and Revenue Department for similar bills. The full year (FY06) estimate assumes:

- there are 21,300 military retirees in the state;
- average annual pension is \$17,650;
- the average applicable tax rate is 3.2 percent
- The average relief per eligible tax payer is \$564 (multiply \$17,650 by 3.2 percent)
- The full year fiscal impact is a revenue decrease of \$12.0 million (Multiply \$564 by 21,300 retirees).
- The lower impacts for FY05 reflects the fact that bill would be effective for half of FY05.

TRD's table reporting the number of military retirees and average monthly pay for all states is attached (see page 3).

ADMINISTRATIVE IMPLICATIONS

TRD has reported that similar bills would have moderate administrative implications that can be handled with existing resources.

OTHER SUBSTANTIVE ISSUE

TRD analyses on similar legislation raised the following issues:

- The measure encourages military retirees to move to New Mexico.
- Individuals with incomes and other circumstances similar to people receiving the proposed exemption are likely to view it as unfair, especially when they compete with the retirees for jobs, and when the retirees are individuals with relatively high incomes. According to information the "military com" website (<http://usmilitary.about.com/>) military retirement pay can be over \$9,000 monthly for high-ranking officers retiring in 2004.
- Reducing state income tax liability tends to increase federal income tax liability because state income taxes are deductible against federal liability.

BT/njw:lg
Attachment

Illustration: Number of Retirees and Total Military Pay by State

Retirees By State*

| State | Army | Navy | Marine Corps | Air Force | Total DoD |
|-------------------|----------------|----------------|----------------|----------------|------------------|
| Alabama | 25,033 | 6,691 | 1,623 | 15,371 | 48,718 |
| Alaska | 2,761 | 652 | 133 | 4,302 | 7,848 |
| Arizona | 13,828 | 7,888 | 3,008 | 23,480 | 48,204 |
| Arkansas | 8,108 | 4,644 | 969 | 10,722 | 24,443 |
| California | 34,713 | 83,245 | 18,396 | 61,339 | 197,693 |
| Colorado | 16,586 | 5,299 | 1,299 | 21,640 | 44,824 |
| Connecticut | 3,006 | 4,986 | 584 | 2,166 | 10,742 |
| Delaware | 1,592 | 897 | 207 | 4,052 | 6,748 |
| Dist. of Columbia | 1,756 | 627 | 139 | 1,033 | 3,555 |
| Florida | 44,392 | 58,862 | 7,851 | 67,465 | 178,570 |
| Georgia | 40,385 | 11,109 | 3,421 | 21,094 | 76,009 |
| Guam, MI | 614 | 783 | 76 | 482 | 1,955 |
| Hawaii | 5,558 | 3,965 | 979 | 3,654 | 14,156 |
| Idaho | 2,554 | 2,511 | 480 | 4,802 | 10,347 |
| Illinois | 10,283 | 8,012 | 1,848 | 12,079 | 32,222 |
| Indiana | 8,947 | 4,421 | 1,377 | 6,396 | 21,141 |
| Iowa | 3,736 | 2,528 | 584 | 3,026 | 9,874 |
| Kansas | 9,014 | 2,943 | 788 | 6,446 | 19,191 |
| Kentucky | 14,033 | 3,442 | 944 | 4,959 | 23,378 |
| Louisiana | 9,531 | 4,921 | 1,337 | 11,159 | 26,948 |
| Maine | 2,898 | 4,004 | 511 | 3,681 | 11,094 |
| Maryland | 16,835 | 12,810 | 2,063 | 12,322 | 44,030 |
| Massachusetts | 7,406 | 5,798 | 1,314 | 6,412 | 20,930 |
| Michigan | 9,336 | 6,266 | 1,562 | 8,077 | 25,241 |
| Minnesota | 5,515 | 3,907 | 832 | 4,854 | 15,108 |
| Mississippi | 7,344 | 5,708 | 921 | 10,227 | 24,200 |
| Missouri | 13,078 | 6,850 | 2,078 | 11,222 | 33,228 |
| Montana | 1,911 | 1,516 | 360 | 3,223 | 7,010 |
| Nebraska | 2,336 | 1,798 | 340 | 7,886 | 12,360 |
| Nevada | 4,808 | 5,669 | 1,449 | 12,816 | 24,742 |
| New Hampshire | 2,828 | 2,087 | 436 | 4,037 | 9,388 |
| New Jersey | 10,028 | 5,386 | 1,226 | 5,423 | 22,063 |
| New Mexico | 5,516 | 2,928 | 723 | 11,144 | 20,311 |
| New York | 14,443 | 8,307 | 2,319 | 10,536 | 35,605 |
| North Carolina | 30,979 | 11,599 | 10,214 | 17,671 | 70,463 |
| North Dakota | 960 | 436 | 66 | 2,239 | 3,701 |
| Ohio | 12,226 | 8,036 | 2,348 | 17,921 | 40,531 |
| Oklahoma | 13,229 | 4,494 | 1,134 | 14,149 | 33,006 |
| Oregon | 5,883 | 6,759 | 1,358 | 6,689 | 20,689 |
| Pennsylvania | 18,018 | 11,686 | 3,251 | 12,148 | 45,103 |
| Puerto Rico | 7,539 | 415 | 131 | 942 | 9,027 |
| Rhode Island | 1,406 | 3,177 | 246 | 932 | 5,761 |
| South Carolina | 17,707 | 12,548 | 2,858 | 16,248 | 49,361 |
| South Dakota | 1,513 | 792 | 132 | 2,978 | 5,415 |
| Tennessee | 18,744 | 9,979 | 2,374 | 12,254 | 43,351 |
| Texas | 65,305 | 23,760 | 6,258 | 77,830 | 173,153 |
| Utah | 3,321 | 1,805 | 431 | 5,875 | 11,432 |
| Vermont | 1,424 | 679 | 142 | 1,027 | 3,272 |
| Virginia | 39,097 | 47,543 | 7,841 | 25,641 | 120,122 |
| Virgin Islands | 183 | 49 | 6 | 44 | 282 |
| Washington | 22,706 | 21,840 | 2,252 | 20,481 | 67,279 |
| West Virginia | 3,889 | 2,208 | 684 | 2,889 | 9,670 |
| Wisconsin | 6,580 | 4,025 | 963 | 4,906 | 16,474 |
| Wyoming | 985 | 715 | 135 | 2,309 | 4,144 |
| Other | 10,486 | 5,553 | 883 | 8,707 | 25,629 |
| Total | 642,892 | 469,558 | 105,884 | 651,407 | 1,869,741 |

*As of September 30, 1999

Retired Military Monthly Pay By State (In Thousands)**

| State | Army | Navy | Marine Corps | Air Force | Total DoD |
|-------------------|----------------|----------------|----------------|----------------|------------------|
| Alabama | 35,542 | 8,086 | 2,075 | 22,048 | 64,752 |
| Alaska | 3,088 | 765 | 122 | 5,273 | 9,248 |
| Arizona | 19,140 | 10,203 | 4,226 | 35,871 | 69,441 |
| Arkansas | 9,159 | 5,575 | 1,147 | 14,220 | 30,101 |
| California | 43,382 | 113,119 | 27,044 | 93,177 | 276,722 |
| Colorado | 23,403 | 7,167 | 1,715 | 37,311 | 69,596 |
| Connecticut | 3,136 | 6,609 | 517 | 2,680 | 12,941 |
| Delaware | 1,839 | 1,037 | 232 | 5,403 | 8,513 |
| Dist. of Columbia | 2,100 | 899 | 138 | 1,220 | 4,357 |
| Florida | 44,392 | 58,862 | 7,851 | 67,465 | 263,126 |
| Georgia | 40,385 | 11,109 | 3,421 | 21,094 | 101,102 |
| Guam, MI | 614 | 783 | 76 | 482 | 2,329 |
| Hawaii | 5,558 | 3,965 | 979 | 3,654 | 20,332 |
| Idaho | 2,554 | 2,511 | 480 | 4,802 | 13,541 |
| Illinois | 10,283 | 8,012 | 1,848 | 12,079 | 39,076 |
| Indiana | 8,947 | 4,421 | 1,377 | 6,396 | 23,671 |
| Iowa | 3,736 | 2,528 | 584 | 3,026 | 10,393 |
| Kansas | 9,014 | 2,943 | 788 | 6,446 | 25,013 |
| Kentucky | 14,033 | 3,442 | 944 | 4,959 | 27,745 |
| Louisiana | 9,531 | 4,921 | 1,337 | 11,159 | 33,481 |
| Maine | 2,898 | 4,004 | 511 | 3,681 | 13,360 |
| Maryland | 16,835 | 12,810 | 2,063 | 12,322 | 64,021 |
| Massachusetts | 7,406 | 5,798 | 1,314 | 6,412 | 22,815 |
| Michigan | 9,336 | 6,266 | 1,562 | 8,077 | 26,787 |
| Minnesota | 5,515 | 3,907 | 832 | 4,854 | 16,238 |
| Mississippi | 7,344 | 5,708 | 921 | 10,227 | 29,469 |
| Missouri | 13,078 | 6,850 | 2,078 | 11,222 | 40,180 |
| Montana | 1,911 | 1,516 | 360 | 3,223 | 8,759 |
| Nebraska | 2,336 | 1,798 | 340 | 7,886 | 16,926 |
| Nevada | 4,808 | 5,669 | 1,449 | 12,816 | 35,100 |
| New Hampshire | 2,828 | 2,087 | 436 | 4,037 | 12,786 |
| New Jersey | 10,028 | 5,386 | 1,226 | 5,423 | 24,918 |
| New Mexico | 5,516 | 2,928 | 723 | 11,144 | 29,861 |
| New York | 14,443 | 8,307 | 2,319 | 10,536 | 35,069 |
| North Carolina | 30,979 | 11,599 | 10,214 | 17,671 | 94,212 |
| North Dakota | 960 | 436 | 66 | 2,239 | 4,127 |
| Ohio | 12,226 | 8,036 | 2,348 | 17,921 | 47,831 |
| Oklahoma | 13,229 | 4,494 | 1,134 | 14,149 | 40,263 |
| Oregon | 5,883 | 6,759 | 1,358 | 6,689 | 25,538 |
| Pennsylvania | 18,018 | 11,686 | 3,251 | 12,148 | 52,869 |
| Puerto Rico | 7,539 | 415 | 131 | 942 | 6,544 |
| Rhode Island | 1,406 | 3,177 | 246 | 932 | 7,477 |
| South Carolina | 17,707 | 12,548 | 2,858 | 16,248 | 66,821 |
| South Dakota | 1,513 | 792 | 132 | 2,978 | 6,571 |
| Tennessee | 18,744 | 9,979 | 2,374 | 12,254 | 54,733 |
| Texas | 65,305 | 23,760 | 6,258 | 77,830 | 249,520 |
| Utah | 3,321 | 1,805 | 431 | 5,875 | 15,588 |
| Vermont | 1,424 | 679 | 142 | 1,027 | 3,784 |
| Virginia | 39,097 | 47,543 | 7,841 | 25,641 | 215,527 |
| Virgin Islands | 183 | 49 | 6 | 44 | 372 |
| Washington | 22,706 | 21,840 | 2,252 | 20,481 | 92,777 |
| West Virginia | 3,889 | 2,208 | 684 | 2,889 | 10,379 |
| Wisconsin | 6,580 | 4,025 | 963 | 4,906 | 17,141 |
| Wyoming | 985 | 715 | 135 | 2,309 | 5,283 |
| Other | 10,486 | 5,553 | 883 | 8,707 | 36,194 |
| Total | 642,892 | 469,558 | 105,884 | 651,407 | 2,535,320 |

**The monthly amount of payment (net pay) is before deductions for withholding taxes and allotments but after deductions for survivor benefits.

Source: http://www.military.com/Resources/ResourceFileView?file=retirees_stats.htm#Monthly

Department of Military Affairs
Proposed Amendment

Section 1. Change the following from:

“[NEW MATERIAL] EXEMPTION--MILITARY RETIREMENT PAY.--For the purpose of promoting economic development in New Mexico, an amount not to exceed fifty percent of military retirement pensions received by a veteran during the taxable year is exempt from taxation. For the purposes of this section, “veteran” means a person who has been honorably discharged from membership in armed forces of the United States and has served in the armed forces of the United States on active duty continuously for ninety days.”, to:

“[NEW MATERIAL] EXEMPTION--MILITARY RETIREMENT PAY.—For the purpose of promoting economic development in New Mexico, an amount not to exceed fifty percent of military retirement pay received by a military retiree, whether from regular or non-regular military service, is exempt from taxation”.

DISCUSSION

The reason to omit the term “veteran” and “membership in the armed forces” is because neither term are Title 10, or Title 32, military pay retirement status; rather, such terms are veteran’s “status’s”, as defined by Title 38 U.S.C. Section 101(2) and 38 C.F.R. Section 3.1(d)(2004). Unnecessary confusion is thus created because Title 38 “veteran” status has nothing to do with military retirement pay that flows from either Title 10 or Title 32 military service status, not a Title 38 veteran’s status that discusses veteran’s benefits or disability rights. Similarly, the language that states a veteran is someone who... “has served in the armed forces of the United States on active duty continuously for ninety days” is a veteran’s law term for threshold eligibility for veteran’s pensions, as per 38 C.F.R. Section 3.3(a)(1)(i); (a)(2)(i)(ii) and (iii). However, there is no longer a so-called “minimum period of active duty”, meaning 90-days of active duty or even 181-days of active duty, to define veteran’s status eligibility. The current legal standard to define a “veteran” is either a “twenty-four month period of continuous active duty,” or the “full period for which [the veteran] was called or ordered to active duty”, as per 38 U.S.C. Section 5303(A)(b); 38 C.F.R. Section 3.12(a)(1)(2004), such as in the case of a mobilized National Guardsmen for “365” or “565” days. In any case, however, the proposed Bill has confused military retirement with veteran’s status, which are wholly dissimilar concepts. Last, in this same regard, the proposed Bill speaks of “military retirement pensions”: there is no such thing. There is either an earned military retirement pay, as per Title 10 or Title 32, for years of service, or there is a veteran’s “pension”, as per Title 38, which coinciden-

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tally requires a “ninety day period of continuous wartime service for non-service-connected disability-based pension”, as per Title 38 U.S.C. Section 1512; 38 C.F.R. Section 3.3. The proposed Bill, however, is fatally flawed as drafted for the reasons herein stated and otherwise need to be remedied.