F I S C A L   I M P A C T   R E P O R T

SPONSOR Adkins **ORIGINAL DATE LAST UPDATED** 2/5/15 **HB** 302

SHORT TITLE Uniformed Service Retiree Tax Deduction **SB**

ANALYST Dorbecker

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY15	**FY16**	**FY17**	**FY18**	**FY19**		
	($10,000.0)	($23,500.0)	($24,000.0)	($24,500.0)	Recurring	General Fund

Parenthesis ( ) indicate revenue decreases

Duplicates SB 316

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)
Department of Veteran Services (DVS)

SUMMARY

Synopsis of Bill

House Bill 302 creates a new section of the Income Tax Act to create a deduction for the retirement or retainer pay of a uniformed services retiree or a surviving spouse. The bill caps the deduction at $50,000 per taxable year.

The purpose of the deduction is to encourage uniformed services retirees to move to the state. The bill describes the process of claiming the deduction as prescribed by TRD and requires the department starting in 2018, to compile and present an annual report to legislative committees on the deduction including the number of tax payers claiming the deduction, the aggregate amount of deductions claimed, and any other information necessary to evaluate the effectiveness of the deduction. The bill includes definitions of uniformed services and uniformed services retirees.

There is no effective date of this bill. It is assumed the new effective date is 90 days after this session ends. The provisions of the act apply to taxable years beginning on or after January 1, 2015.

FISCAL IMPLICATIONS

LFC staff used about half of TRD's estimated fiscal impact of the bill because TRD assumes there are approximately 40,000 retirees currently living in the state. LFC took into account confirmation from DVS the current number of uniformed services retirees and their spouses living in the state is about 20,000. LFC staff used TRD's methodology of an identical bill introduced during the 2014 session (SB 246) and applied the average historical growth rate for armed forces retirees and surviving spouses to the retiree population estimate. The estimated number of qualifying retirees and their spouses was multiplied by the average annual retiree payment or the average annual surviving spouse payment from the Department of Defense. The average annual retiree payment and the average annual surviving spouse payment were adjusted for inflation using the most recent five-year average inflation rate of 1.5 percent.

This bill may be counter to the LFC tax policy principle of adequacy, efficiency and equity. Due to the increasing cost of tax expenditures revenues may be insufficient to cover growing recurring appropriations.

Estimating the cost of tax expenditures is difficult. Confidentiality requirements surrounding certain taxpayer information create uncertainty, and analysts must frequently interpret third-party data sources. The statutory criteria for a tax expenditure may be ambiguous, further complicating the initial cost estimate of the expenditure's fiscal impact. Once a tax expenditure has been approved, information constraints continue to create challenges in tracking the real costs (and benefits) of tax expenditures.

SIGNIFICANT ISSUES

DVS notes the average age of a military retiree in the state is 46 years old with an average annual retirement income of $50,000 or less. Military retirees that depend solely on this income will likely seek to be employed full or part-time to subsist. This means the military retiree's personal income received from their full or part-time employment is fully taxed under current law. According to DVS, most of the military retirees in the state are married and their spouse's income is also fully taxed. Also, the department believes the bill will have a positive effect in the state's economy through an increase in gross receipts tax revenue caused by higher spending levels of military retirees with higher disposable income.

According to DVS, figures provided by the Small Business Administration show approximately 10 percent of all small businesses are owned by military veterans and 47 percent of military retirees are self-employed. DVS assumes military retirees who are small-business owners will likely create jobs and further assist local economies if their personal income tax burden is reduced by the bill.

DVS reports there are currently approximately over 21,000 military retirees and surviving spouses living in the state. Only 28 percent of all military retirees come from the Officers Corps; the remaining 72 percent of retirees come from the enlisted corps. According to the Retirement and Separations office at Kirtland Air Force Base, figures show that for FY13, 95 percent of those who retired decided to leave the state.

DVS reports the state is in a comparatively not favorable position with neighboring states as they offer the following incentives for military retirees:

- 1. Arizona - $2500 credit
- 2. Colorado – Up to $20,000 income exclusion
- 3. Texas – No state income tax
- 4. Utah – up to $9,600 exclusion
- 5. Oklahoma – up to $5,500 income exclusion

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is met with the bill's requirement to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose.

ADMINISTRATIVE IMPLICATIONS

It is assumed TRD would estimate a minimal administrative impact of this bill based on the analysis of SB 246 (2014 session). The department would need to revise forms, instructions and publications for personal income tax. GenTax and all web applications will need to be revised. All changes can be made at minimal cost during the annual re-write of the personal income tax program.

TECHNICAL ISSUES

This bill does not contain a sunset date. The LFC recommends adding a sunset date.

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

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