

**Department of Legislative Services**  
 Maryland General Assembly  
 2021 Session

**FISCAL AND POLICY NOTE**  
**First Reader**

Senate Bill 574 (The President)(By Request - Administration)  
 Budget and Taxation

**Income Tax - Subtraction Modification - Military Retirement Income**

This Administration bill expands the existing military retirement income tax subtraction modification by exempting 100% of military retirement income from State taxation. The exemption is phased in over two years, beginning with tax year 2021. **The bill takes effect July 1, 2021.**

**Fiscal Summary**

**State Effect:** General fund revenues decrease by \$18.4 million in FY 2022 due to additional military retirement income being exempted. The Governor’s proposed FY 2022 operating budget assumes that general fund revenues will decrease by \$18.4 million due to the expansion of the subtraction modification. Future year estimates reflect projected growth in retirement income and the phase-in specified by the bill. Expenditures are not affected.

(\$ in millions)	FY 2022	FY 2023	FY 2024	FY 2025	FY 2026
GF Revenue	(\$18.4)	(\$27.8)	(\$28.3)	(\$28.9)	(\$29.1)
Expenditure	0	0	0	0	0
Net Effect	(\$18.4)	(\$27.8)	(\$28.3)	(\$28.9)	(\$29.1)

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

**Local Effect:** Local revenues decrease by \$12.0 million in FY 2022 and by \$19.0 million in FY 2026. Local expenditures are not affected.

**Small Business Effect:** The Administration has determined that this bill has minimal or no impact on small business (attached). The Department of Legislative Services concurs with this assessment.

## Analysis

**Current Law/Background:** Chapter 226 of 2006 expanded a \$2,500 military retirement income tax subtraction modification that was previously limited to enlisted military members with federal adjusted gross income of \$22,500 or less. An individual can exempt certain military retirement income from State and local taxation if the retirement income resulted from service (1) in an active or reserve component of the U.S. Armed Forces; (2) as a member of the Maryland National Guard; or (3) as an active duty member with the Commissioned Corps of the Public Health Service, the National Oceanic and Atmospheric Administration, or the Coast and Geodetic Survey. The subtraction modification can also be claimed by a surviving spouse or ex-spouse.

Legislation enacted in the 2015 and 2018 sessions expanded the maximum value of the subtraction modification to:

- \$15,000 for individuals who are at least age 55; and
- \$5,000 for all other individuals.

Maryland law provides a pension exclusion (in the form of a subtraction modification) 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 (\$33,100 for 2020) 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 (Social Security offset). Military retirees who are at least age 65 or are totally disabled can qualify and claim the State pension exclusion for retirement income that is not excluded under the military retirement income subtraction.

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.

**State Revenues:** Additional retirement income can be exempted beginning in tax year 2021. The amount that may be exempted is equal to (1) the greater of \$15,000 or 50% of eligible income in tax year 2021 and (2) 100% of eligible income beginning in tax year 2022. It is assumed that individuals adjust withholdings and estimated payments. As a result, revenues will decrease by \$18.4 million in fiscal 2022.

**Exhibit 1** shows the projected State and local revenue loss from exempting military retirement income. The estimated impact of exempting additional retirement income is based on the number of retirees who claimed the subtraction modification in tax year 2019, adjusted for the provisions of the bill.

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**Exhibit 1**  
**Projected State and Local Revenue Loss**  
**(\$ in Millions)**

	<b><u>FY 2022</u></b>	<b><u>FY 2023</u></b>	<b><u>FY 2024</u></b>	<b><u>FY 2025</u></b>	<b><u>FY 2026</u></b>
State	(\$18.4)	(\$27.8)	(\$28.3)	(\$28.9)	(\$29.1)
Local	(12.0)	(18.1)	(18.5)	(18.9)	(19.0)
<b>Total Revenues</b>	<b>(\$30.4)</b>	<b>(\$45.9)</b>	<b>(\$46.7)</b>	<b>(\$47.8)</b>	<b>(\$48.1)</b>

Source: Department of Legislative Services

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**Local Revenues:** Local income tax revenues decrease by about 3% of the total net State subtraction modifications claimed. Local revenues will decrease by \$12.0 million in fiscal 2022 and by \$19.0 million in fiscal 2026, as shown in Exhibit 1.

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**Additional Information**

**Prior Introductions:** SB 279 of 2020 received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Its cross file, HB 361, received a hearing in the House Ways and Means Committee, but no further action was taken. Similar legislation was introduced in the 2017, 2018, and 2019 sessions.

**Designated Cross File:** HB 734 (The Speaker)(By Request - Administration) - Ways and Means.

**Information Source(s):** Comptroller's Office; Department of Legislative Services

**Fiscal Note History:** First Reader - February 8, 2021  
rh/hlb

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**ANALYSIS OF ECONOMIC IMPACT ON SMALL BUSINESSES**

TITLE OF BILL: **Income Tax - Subtraction Modification - Military Retirement Income**

BILL NUMBER: HB 734/SB 574

PREPARED BY: Governor's Legislative Office

**PART A. ECONOMIC IMPACT RATING**

This agency estimates that the proposed bill:

  X   WILL HAVE MINIMAL OR NO ECONOMIC IMPACT ON MARYLAND  
SMALL BUSINESSES

**OR**

       WILL HAVE MEANINGFUL ECONOMIC IMPACT ON MARYLAND  
SMALL BUSINESSES

**PART B. ECONOMIC IMPACT ANALYSIS**