



STUDY ON INCREASING STATE TAX REVENUE BY RETAINING AND ATTRACTING RETIRED MILITARY SERVICE PERSONNEL (RMSP)

Prepared by the
MARYLAND RETIRED VETERANS TASK FORCE (MRVTF)

January 27, 2015



INTRODUCTION

For the past 12 years, the Maryland Retired Veterans Task Force (MRVTF) has been seeking State income tax relief for the retired pay of Retired Military Service Personnel (RMSP) living within the State. This effort was initiated as a method of providing long term tax revenue to Maryland by incentivizing retirees to take up State residency. This proposal is no different than state and local governments' offering tax credits to businesses as an incentive to locate in Maryland. It is an incentive to retirees already recognized and approved by law in 26 other states. In the case of Maryland, surrounding states (PA, DE, and NJ) offer significant tax incentives to reside in their states and commute to employment in Maryland. NY and WV also offer tax incentives for those who want to reside in the Mid-Atlantic area in competition with Maryland.

In its December 2003 study, Maryland's General Assembly-directed Report of the Task Force to Study the Financial Impact of Retired Military Service Personnel on the Economy of the State included this statement in the Executive Summary: “. . . if Maryland does not exempt military retirement pay from State and local income taxes . . . countless others will opt to move to military retiree-friendly states.” Recent issues related to Maryland's new taxes and increasing tax rates, and the exit of higher income residents to avoid these taxes, makes this effort even more critical.

Every year since 2003, bills to exempt military retired pay from taxation have been introduced in both the House of Delegates and the Maryland Senate. Despite the support of the Veterans Caucus of the Maryland General Assembly, none of these bills have received the requisite support from the Governor and Legislative leadership to get them to the floor of the General Assembly. At present only \$5,000 of military retired pay is exempt from Maryland income taxes. There is no evidence that this current minimal tax savings is a sufficient incentive to attract more RMSP and their families to Maryland to take up residency and pursue second careers.

On March 17, 2011, in written testimony for House Bill 774, Income Tax-Military Retirement Income to the House Ways and Means Committee, Comptroller of the State of Maryland Peter Franchot stated in part: “. . . this serves Maryland's best interest by encouraging service men and women to make Maryland their home once they retire. With our current military facilities and the additional military personnel who will come as the result of Base Realignment and Closure, the potential benefits to the state are significant.”

In February 2014, in concern over the failure of the program to gain traction, representatives of the MRVTF met with the Mr. Franchot and requested his guidance. His recommendation to the MRVTF was to update the original study with the most currently available figures, including publicly available data on the tax revenue implications of the full exemption over a period of time. This report responds to that recommendation, and provides additional new data relative to individuals working in Maryland but residing in neighboring states.

Respectfully submitted to members of the Maryland State Government.

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EXECUTIVE SUMMARY

This report is an update and expansion of an original 2003 Task Force Report authorized under SB280. The results of this updated report are the following:

- There are approximately 53,339 Retired Military Service Personnel (RMSP) living in Maryland. In tax year 2011, the average Adjusted Gross Income reported by RMSP was \$128,525, of which \$27,636 was attributable to Military Retirement Income (MRI).
- In 2011, RMSP paid \$285,571,784 in State and local income taxes. RMSP households spent \$837,699,620 on taxable goods, generating \$50,261,997 in sales tax revenue.
- In 2011, Maryland RMSP tax payers claimed \$42,514,021 in real estate taxes paid.
- RMSP health care costs to the state are negligible because the vast majority of RMSP and their family members are covered the Department of Defense (DOD) TRICARE Program.
- RMSP generate countless jobs for Maryland health care providers. For example, in 2008, the DOD awarded a 5 year, fixed price contract to Johns Hopkins Uniformed Services Family Health Plan to provide health care services to RMSP, their families and survivors that totaled over \$1.1 billion dollars.
- 26 States exempt all military retired pay from income taxes, including 9 that have no personal income taxes.
- Maryland exempts only \$5,000 in military retirement pay. Most Mid-Atlantic States provide better tax relief to RMSP. The average annual RMSP population growth rate for Maryland is among the lowest in the Mid-Atlantic region at 1.5% per year for the last 10 years. Even with no tax relief, Virginia's average RMSP growth rate was 1.7%.
- The average annual income (wages, tips, salary) for RMSP exceeds that of all Maryland tax payers by over 43%. This is a direct result of age, work history, management and technical skills, security clearances and family make up (i.e., working spouses). These higher wage earners represent exactly the type of individual that the State is trying to retain and attract.
- Every RMSP who retires or remains in the State adds to the State tax coffers at a rate 28% higher than the average tax payer. Even with additional tax relief, RMSP will contribute to State revenue at a significantly higher level than the average tax payer.
- Nearly every dollar in additional RMSP tax relief will result in higher consumer spending within the State. There will be increased tax revenue from sales, business and property taxes. This will lead to increased job availability as increased spending allows businesses to expand. This will significantly mitigate concerns over attaining tax neutrality.

- According to data gathered by the MRVTF, nearly 1 in 5 personnel at Aberdeen/Edgewood are not Maryland residents. A full 28% of employees at Walter Reed National Military Medical Center do not have residence in Maryland. The vanpool system at Fort Meade indicates that large number of individuals commute daily from designated pick up points in PA and VA.
- The MRVTF knows of no formal program by the State to recruit or retain residents currently departing the state due to tax concerns. Immediate tax relief for RMSP in Maryland is a fiscally sound, viable option to quickly start to attract and retain these valuable individuals, and effectively increase the numbers of tax payers on the State roles.

PART I — TASK FORCE REPORT (UPDATE OF ORIGINAL STUDY)

This report follows the format of the original 2003 General Assembly-directed Task Force Report, and includes updated answers to the questions provided in SB480 that authorized the Task Force. The military retirees are referred to in this report as Retired Military Service Personnel (RSMP).

1. Determine the number of RMSP in the State of Maryland

There were 53,339 persons in Maryland with a 1099 Form from the Defense Finance and Accounting Service (DFAS), Cleveland, Ohio, (identified by EIN) in tax year 2011. (Office of the Comptroller)

2. Determine the number of RMSP engaged in a second career or secondary employment of any kind.

The Comptroller's Office collected the following data from 43,452 tax year 2011 federal income tax returns with Maryland addresses matched to the 53,339 individuals. Note: The number of Federal returns with Maryland addresses is smaller than the number of individuals receiving retirement pay for several reasons, including (a) military retirees could be married to each other and therefore only file one return; (b) the retirees could move out of state and therefore receive a 1099 form with a Maryland address but file a Federal tax return from another state; and (c) retirees could have income that does not meet the minimum Federal filing requirement.

- There are 32,056 returns claiming wage and salary income.
- There are 903 returns with Schedule C (self-employment) income, but no wage/salary income.
- There are 721 returns with partnership income, but no wage, salary, or self-employment income.

Thus, the number of RSMP with a second career or secondary employment is a maximum of 33,680. Up to 32,056 RMSP may be working for others, although some unknown number of those returns reflect income from a spouse's job on joint returns. Similarly, the 164 returns showing business income indicates that 1624 additional RMSP and/or their spouses had income from a business and not from being employed by others. (Office of the Comptroller)

3. Average income of RMSP, including secondary employment income or secondary career income, military retirement income or other retirement income.

Total income of \$5,584,664,133 as reported on 43,452 tax returns for tax year 2011 where one or more people had military retirement income. **Average income: \$128,525.** For comparison purposes, the adjusted gross income of all Maryland residents was \$183,953,496,000, for an average income of \$81,059. The number of returns is smaller than the number of 1099s issued by DFAS because some individuals may not have met filing requirements (mostly due to low incomes), some may report a different state of record for tax purposes, and some RMSP may be married to each other and thus filing joint returns.

In tax year 2011, RMSP paid \$285,571,784 in State and local income taxes (\$175,576,647 State; \$109,995,137 local). For comparison, the average State income tax paid by RMSP was \$4,424, and for all Marylanders that owed State tax the average was \$3,141. RMSP taxpayers who owed local income tax paid an average of \$2,786 in local income tax, and for all Marylanders who owed local income tax, the average was \$2,030. (Office of the Comptroller)

4. The value of any additional benefits or programs available to Retired Military Service Personnel.

As with the original December 2003 study, no data are available to quantify any such State benefits. However, it should be noted that due to medical benefits provided by the military through TRICARE, the State does not have to cover any RMSP medical costs. Also, current Federal GI Bill education benefits provide significant student funding support for State institutions.

5. The average expenditures by RMSP on an annual basis for goods and services, and the estimated sales taxes generated by RMSP in the State.

Based on the expenditure patterns of various income classes in the Consumer Expenditure Survey, RMSP households spent an average of \$837,699,620 on taxable goods, generating \$50,261,977 in sales tax revenue. (Office of the Comptroller)

6. Average expenditures in the form of state, county and local government services provided to RMSP and their families.

As with the original December 2003 study, no data are available to quantify such benefits.

7. The cost of health care services provided by the State to Retired Military Service Personnel and their families.

The cost of health care services paid by the State to Retired Military Service Personnel are negligible, except possibly for those who are employed by the State who opt to take advantage of coverage provided to them by their employers. The only direct payment that the State might be liable for is if a uniformed services beneficiary became Medicaid-eligible. This would be rare because RMSP and surviving spouses receive military retirement pay.

The Department of Defense TRICARE Program or the U.S. Department of Veterans Affairs covers the vast majority of military retirees under 65 and their families. Because TRICARE relies heavily on the services of private sector physicians, laboratories, drug stores and hospitals, RMSP generate hundreds of millions of dollars in revenue for Maryland health care providers. As an example, effective October 1, 2008, the Defense Department awarded a fixed price contract to Johns Hopkins Uniformed Services Family Health Plan (USFHP) to provide health care services to active duty family members, all military retirees and their eligible family members, including those 65 years of age and older. The value of the base year contract (\$226,117,226) and 4 additional year options was approximately \$1,130,585,000. (TRICARE Management Activity)

8. Determine the average State, county and local real estate taxes paid by RMSP on an annual basis.

On tax year 2011 federal tax returns, 31,296 RMSP tax payers claimed \$142,514,021 in real estate taxes paid, an average of \$4,554. For comparison, the average for all Maryland taxpayers was \$4,221. There is no way to determine how much of that amount was paid on Maryland property. Assuming the full amount was paid on Maryland property, and using weighted average tax rates, the distribution would be:

Distribution of Real Estate Taxes Paid by Jurisdiction

Jurisdiction	Real Estate Taxes Paid	Percentage of Real Estate Taxes Paid
County	\$120,181,581	84.3%
Municipal	\$ 8,796,551	6.2%
State	\$ 13,535,889	9.5%
Total	\$142,514,021	100%

Source: Office of the Comptroller

9. Review a comparison of total tax burden in the State for military retirees as compared to other states.

Nationally, 26 states do not tax military retired pay (9 states have no personal income taxes and 17 others exempt all military retired pay). Several other states offer varying retired military pay exemptions based on age, disability status and/or total income.

Most neighboring States provide more favorable tax relief than Maryland:

- New York: Does not tax military retired pay
- New Jersey: Does not tax military retired pay
- Pennsylvania: Does not tax military retired pay
- Delaware: First \$2,000 exempt if under age 60; \$12,500 exempt over age 60
- Virginia: No tax relief for military retired pay
- West Virginia: Waives up to \$2,000 from taxes, and may also exclude the product of (a) number of years of service times (b) 2% of retired pay, up to a maximum of \$30,000.

According to the Tax Foundation’s April 2014 report titled Annual State-Local Tax Burden Rankings FY2011, Maryland had the **7th highest state-local income tax burden in the country**, measured as a percent of state income.

10. Review a comparison of the total tax burden in the State, including provisions of State law exempting retirement income and military income from taxation and any other property tax or other tax benefits for military retirees as compared to other states.

The International Association of Assessing Officers surveys every state periodically on property assessment practices. A review of their most recent version of the “IAAO Assessment Administration Practice Survey” reveals no change to the practices found during the review for the 2003 report. Few

states provided any property tax exemptions. These exemptions were limited to disabled veterans, and there was no clear indication that retirement status affected eligibility.

According to a publication called "Property Taxes by State," from Tax-Rates.org – [The 2014 Tax Resource](#), Maryland has the 25th highest median property tax rate in the Nation as a percentage of home value (.87%). The tax benefits for veterans provided by any state would not appreciably change the property tax burden in those states relative to Maryland, and would have a marginal impact when considering the circumstances of individual military retirees.

PART II — EFFECT OF TAX RELIEF IMPLEMENTATION FOR RMSP OVER TIME (5 YEARS)

Following the recommendation of the Comptroller of the State of Maryland to update the report, the Task Force looked at the effect of implementation of tax relief for RMSP over a period of 5 years. The figures were compiled by the Office of the Comptroller's Bureau of Revenue Estimates, and were based on achieving a "revenue neutral" position. (See Tables 1 – 4 on pages 9 and 10) The bottom line assessment, based on projected military retirement income in Maryland, is that phasing in additional tax relief at the rate of \$5,000 per year for a period of 5 years beginning in July 2015, would decrease projected State tax revenue over that period. What was not computed was the amount of tax revenue still projected from the balance of the military retirees' earnings, nor the projected net tax revenue increase from each new retiree after excluding retired military pay.

Several points need to be made or can be inferred with reference to the Tables:

- The average annual income (wages, tips, salary) for Maryland RMSP exceeds that of all MD taxpayers by 43%. This is directly the result of the age, work history, management and technical skill sets, government security clearances, and family make up (i.e., working spouses) of the RMSP. The average RMSP in Maryland is among the higher wage earners in the State, and represents the type of individual that the State is trying to retain and attract.
- The average taxable pension of the RMSP from all sources is nearly 6.7 times the state average, providing nearly 10.4% of all state taxable pensions and annuities. This will continue at some rate once tax relief is approved, but will likely still far exceed the average.
- Maryland has had an average annual migration of approximately 710 RSMP to the state for the last ten years (2003 – 2013). This is an average growth rate of 1.5% per year during that period. During that same period, DE saw an average growth rate of 2.0%, and VA's rate was 1.7% (Note: VA provides no State tax relief to RMSP.) As a single metric, achieving revenue neutrality would require an increased annual migration, and an increase can reasonably be expected. However, beyond that, every RMSP who does establish residency provides a net tax revenue increase to the State income tax coffers at a rate 28% higher than the average taxpayer. In addition, their increased level of annual wage income (43% higher) adds to the State's intake of sales and property taxes. Even with additional tax relief, the average RMSP will contribute to state revenue at a significantly higher level than the average MD taxpayer.
- Nearly every dollar in tax relief provided to RMSP will result in increased discretionary consumer spending within the State. This has been evident with the current nation-wide consumer

spending increase due to lower fuel prices. As a result, there will be increased tax revenue from sales, business and property taxes, and the potential for increased job availability as increased spending allows businesses to expand. This will mitigate much of any tax neutrality concerns.

- The MRVTF position is that there is no increased tax burden on the State in implementing tax relief to RMSP. Every RMSP will bring a net percentage increase to State revenue that far exceeds any loss of receipts due to tax relief.

Table 1 -- Personal Income Tax Effect: Exempt All Military Retirement Income (MRI)	
# of 1099-R's showing MRI (# individuals with MRI in MD)	53,349
# of MD Final Tax Returns with SSN's from those 1099-R's (# MD returns with MRI)	43,801
Total Federal Adjusted Gross Income of Retired Military	5,609,214,144
Total MRI	1,424,156,436
Total Non-MRI of Retired Military	4,185,057,708
Average MRI	27,636
Average Non-MRI	78,447
Current MD MRI Subtraction (per Recipient)	5,000
Average Potential Additional MRI Exemption	22,636
# Returns Currently Claim Max MRI Subtraction (Potentially Exempt more MRI)**	23,618
# Returns with MRI	43,801
# Retired Military Currently Claiming Max Subtraction (Potentially Exempt more MRI)	28,766
Total Potential Additional MRI Exempted from Taxation	651,156,021
Effective Tax Rate on Retired Military	4.75%
MD Income Tax Effect of Exempting all Military Income	<u>(30,929,911)</u>
<p><i>**Taxpayers over 65 can exempt military retirement income through Maryland's Pension Exclusion Subtraction, allowing an exemption amount of up to \$31,300 in tax year 2011 per payee. An estimated 8,327 returns exhibited total taxable pension Income (net of MRI and all other forms of pension income) of less than \$31,300 per payee in tax year 2011 (i.e. all MRI is already exempt from taxation). Additionally, approximately 15,291 returns with MRI did not exhibit a subtraction for MRI of the full \$ 5,000 amount, though only 1,446 of these returns were associated with MRI less than \$5,000. It is assumed these individuals will not experience a decrease in tax liability as a result of exempting all MRI from Maryland income taxation.</i></p>	

Table 2 -- Migration of Retired Military Required for Exemption Revenue Neutral	
Current Tax on All Income of Retired Military	240,140,839
Total Tax on Retired Military if All MRI Exempt from Tax	209,210,928
Current Average Tax on All Income of Retired Military	4,501
Average Tax on Retired Military if All MRI Exempt from Tax	3,927
Average Current Tax on MRI	575
# of Retired Military needed to Migrate for Exemption to be Revenue Neutral	<u>7,877</u>

	Retired Military		All MD Taxpayers	
	Total	Avg.	Total	Avg.
Wages, salaries, tips, etc.	3,287,915,393	75,065	149,275,313,000	52,177
Taxable interest	40,214,958	918	1,775,547,000	621
Ordinary dividends	75,592,642	1,726	4,387,026,000	1,533
Taxable refunds	37,774,835	862	1,401,071,000	490
Alimony received	4,086,730	93	-	-
Business income of (loss)	55,460,999	1,266	6,181,856,000	2,161
Capital gain or (losses)	50,830,023	1,160	7,877,256,000	2,753
Other gain of (losses)	(6,516,190)	(149)	-	-
Taxable IRA distributions	149,241,321	3,407	4,296,090,000	1,502
Taxable pensions and annuities	1,627,829,619	37,164	15,718,175,000	5,494
Rents, royalties, parts, S corps, trusts	48,852,981	1,115	11,063,816,000	3,867
Farm income of (loss)	(2,784,912)	(64)	-	-
Unemployment compensation	13,700,134	313	1,125,032,000	393
Taxable social security benefits	259,947,894	5,935	4,565,808,000	1,596
Taxable other income	(3,554,254)	(81)	-	-
Total MD Income Taxes		4,021		3,141

	TY 1	TY 2	TY 3
Total MD Income Tax Effect	(6,832,018)	(13,664,036)	(20,496,053)
Average Tax on Retired Military	4,375	4,247	4,119
# of Retired Military needed to Migrate	1,740	3,480	5,220
	TY 4	TY 5	
Total MD Income Tax Effect	(27,328,071)	(30,929,911)	
Average Tax on Retired Military	3,990	3,923	
# of Retired Military needed to Migrate	6,960	7,877	
	FY 2016	FY 2017	FY 2018
Total MD Income Tax Effect***	(13,664,036)	(17,080,045)	(23,912,062)
	FY 2019	FY 2020	
Total MD Income Tax Effect***	(29,128,991)	(30,929,911)	

***Fiscal year revenue effect differs according to timing of enactment. Scenario shows enactment for tax year 2015 and effective date of July 1, 2015

Data provided by Office of the Comptroller — State of Maryland

PART III — ECONOMIC DECISION: OUT-OF-STATE RESIDENCE — MARYLAND EMPLOYMENT

When a military member has served on active duty in Maryland, he or she may opt to retire elsewhere for a number of reasons. The most significant are economic and family-related. A major insurance company for military service personnel, USAA, in the “Winter 2014” edition of its USAA Magazine, identified the “Ten Best Places for Military Retirement”. The states identified did not tax military retirement pay at all. Many military members do not consider Maryland as a retirement option simply because of the of the tax burden. The purpose of this section is to report the findings regarding how military retirees can, and do, retain residences in nearby states that do not tax military retired pay at all, or as heavily as is done in Maryland.

The MRVTF conducted surveys and contacted representative military installations in an attempt to estimate the number of out-of-state employees who are working at selected facilities. This in no way is considered a precise measurement of the numbers, nor is it a definitive indication of the number of RMSP who live outside of the State and commute to Maryland to avoid taxes on their military retired pay. However, it is indicative of the ease of commuting and the magnitude of movement to Maryland for employment.

ABERDEEN PROVING GROUND

Statistics provided by the Aberdeen Proving Ground (APG) CSSC Regional BRAC office, based on data from the APG Human Resources Office dated October 28, 2013, showed the following residency percentages for all Department of Defense civilian employees (approximately 12,000).

- Maryland 81.2%
- D.C. 0.04%
- Delaware 3.8%
- Pennsylvania 5.4%
- Virginia 1.2%
- All Other 8.3%

(Note: This does not include approximately 10,000 contractor employees which could be extrapolated to similar percentages of residency)

WALTER REED NATIONAL MILITARY MEDICAL CENTER

On Monday morning, December 22, 2014, a license plate survey was conducted at the Staff Parking Garage at Walter Reed. A total of 714 vehicles were surveyed with the following breakout:

- Maryland 71.6%
- Virginia 11.3%
- D.C. 4.8%
- Pennsylvania 2.0%
- New York 0.8%
- All Other 9.1%

Walter Reed National Military Medical Center has approximately 7,000 personnel on staff, mostly civilian. These individuals perform duties 24/7, and park at various facilities on-site.

FORT MEADE

Information provided on www.meaderide.com/commuting-options/vanpool/ provides details on vanpools to support commuters who work at Fort Meade. Each van carries from 7 to 15 people. Vanpools to Fort Meade operate daily from numerous locations in Maryland, as well as the following out-of-state locations: York, Hanover and Chambersburg, Pennsylvania; and Alexandria, Fairfax, Fredericksburg, Manassas, Reston, Springfield, Sterling and Vienna, Virginia.

It is recognized that most commuters to this military installation do not participate in car pools. Fort Meade is currently home to approximately 11,000 military personnel, and has more than 56,000 employees in total. It is Maryland's largest employer.