

NORTH CAROLINA GENERAL ASSEMBLY

LEGISLATIVE FISCAL NOTE

BILL NUMBER: HB 1438 (First Edition)

SHORT TITLE: Exempt Certain Military Pay from Income Tax

SPONSOR(S): Representatives Warner and M. Crawford

FISCAL IMPACT					
	Yes (X)	No ()	No Estimate Available ()		
	<u>FY 2001-02</u>	<u>FY 2002-03</u>	<u>FY 2003-04</u>	<u>FY 2004-05</u>	<u>FY 2005-06</u>
REVENUES:					
General Fund:					
Stationed outside NC	\$0	\$21,265,000	\$21,265,000	\$21,265,000	\$21,265,000
Stationed in NC		No Estimate Available			
EXPENDITURES					
PRINCIPAL DEPARTMENT(S) & PROGRAM(S) AFFECTED: Department of Revenue					
EFFECTIVE DATE: This act is effective for taxable years beginning on or after January 1, 2002.					

BILL SUMMARY: This legislation amends G.S. 105-134.6(b) by adding a new section that allows a deduction from NC taxable income for compensation paid by the US Armed Forces for military service performed outside the state during that taxable year. This deduction is allowable for any active duty full-time officer, enlistee, or draftee who is a legal resident of North Carolina and performing duties outside of the state.

BACKGROUND INFORMATION: The Soldiers' and Sailors' Civil Relief Act provides a variety of civil protections for active duty military personnel. This legislation was enacted in 1940, and has been amended 11 times to keep pace with military and economic changes. Among the civil protections authorized by this act, is the protection from paying personal property and income tax in both the state of legal residence and the state where the soldier or sailor is stationed. For example, under this act, a legal resident of NC stationed in VA need only pay NC personal income tax. Conversely, military personnel stationed in NC may declare their residence in a state with no personal income tax such as AK, FL, NV, NH, SD, TN, TX, WA, or WY, and pay no personal income tax. The 10 states most populated by NC residents in the military are as follows:

	State	NC Resident Personnel
1	VA	3697
2	CA	1820
3	GA	1535
4	SC	1044
5	TX	1023
6	HI	692
7	KY	578
8	FL	559
9	MD	469
10	WA	450

ASSUMPTIONS AND METHODOLOGIES: According to the Department of Defense Statistical Report of Personnel and Readiness, there are approximately 25,500 military personnel who declare North Carolina as their legal residence. Of these residents, approximately 20,000 are stationed in locations other than the state. Of these 20,000 enlisted persons, approximately 53% are married with an average of 2 dependents. The remaining 47% are single. The mean salary for military personnel in the state is \$30,000. This demographic information was provided by the Finance and Accounting office of the Department of Defense.

According to the Income Tax Division of the Department of Revenue, there is no current income exemption or tax credit available to NC resident military personnel living outside of the state. There is, however, a NC income tax credit for the state income tax paid by the spouse of military personnel to the other state. Therefore, the annual estimated revenue loss for married enlisted personnel is equal to the amount of state income tax revenue currently collected from these individuals, minus the estimated credits given to the spouses of married military personnel. For the approximately 10,800 married enlisted residents stationed outside the state, the average salary is \$50,000. This average gross annual salary is based on the assumption that the mean military salary in the state is \$30,000 and the average spouse earns approximately 66% of the income of the primary earner (\$30,000 + \$20,000). For the purposes of this fiscal note, it will be assumed that the typical resident military married couple stationed elsewhere will file jointly and utilize the NC credit for income tax paid by the spouse in the other state. The NC income tax credit is estimated by applying the standard deductions and marginal tax rates of the 49 other states to the spouse's \$20,000 average non-military income to determine individual tax credits. These individual credits were then summed according to the number of NC military residents stationed in each of the other 49 states to estimate the group credit. The income tax credit for this married group of qualified residents is approximately \$17 million. Assuming a standard deduction, personal exemption for four individuals, and a \$60 child income tax credit per dependent (average of 2), the

annual state tax liability for this group is approximately \$22.9 million. Deducting the credit paid for out of state taxes, the combined tax liability for this group is approximately \$6 million.

For the approximately 9,500 single enlisted residents stationed outside the state, the average salary is \$30,000. Assuming a standard deduction and personal exemption, the adjusted annual tax liability for this group is approximately \$15.2 million. Combining the tax liability estimates for single and married groups results in the net NC revenue loss. The estimated annual revenue loss to the General Fund from this legislation is approximately **\$21.3 million**.

A chart outlining the income, standard deductions, exemptions, credits, and tax liabilities for both groups is presented below:

NC Res Living in NC Qualified Residents	25,435 (5046) 20,389	Mean Gross Inc	Std Ded	Pers Exemp	Adj Inc	Ind Gross Tax Liab	2 Dep Inc Tax Credit	Adj Tax Liab	Unadj NC Rev Loss	NC Rev	Out of State Tax Credits	Adjusted NC Rev loss
Single	9,583	\$30,000	(\$3,000)	(\$2,500)	\$24,500	\$1,588		\$1,588	\$15,213,013			\$15,213,013
Married	10,806	\$50,000	(\$5,000)	(\$10,000)	\$35,000	\$2,238	(\$120)	\$2,118	\$22,881,705	\$16,829,242		\$6,052,463
									\$38,094,718			\$21,265,476

While the Department of Defense maintains detailed records as to where NC residents are permanently stationed, they do not maintain records of temporary deployment by state of legal residence. It is not possible to estimate the number of NC residents who are temporarily deployed to locations outside of the state, nor the average number of days that they are deployed. Therefore, there is no estimate available for the fiscal impact from temporary deployment of NC resident military personnel.

FISCAL RESEARCH DIVISION 733-4910
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DATE: July 9, 2001



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