

Franchise Tax Board

ANALYSIS OF ORIGINAL BILL

Author: Melendez Analyst: Michelle Chan Bill Number: AB 2329
 Related Bills: See Legislative History Telephone: 845-6805 Introduced Date: February 21, 2014
 Attorney: Bruce Langston Sponsor: _____

SUBJECT: Exclusion/Military Combat-Related Special Compensation Or Concurrent Retirement & Disability Payments

SUMMARY

This bill would exclude from gross income two specific combat-related types of payments for taxable years beginning on or after January 1, 2015.

RECOMMENDATION

No position.

Summary of Suggested Amendments

Amendments 1 through 5 resolve a technical concern by deleting reference to Combat-Related Special Compensation excluded from gross income under current federal and state law.

Amendment 6 would clarify the definition of Concurrent Retirement and Disability Pay.

REASON FOR THE BILL

The reason for this bill is to provide tax relief for California veterans receiving certain combat-related injury compensation or disability pay.

EFFECTIVE/OPERATIVE DATE

As a tax levy, this bill would be effective immediately upon enactment and specifically operative for taxable years beginning on or after January 1, 2015.

ANALYSIS

FEDERAL/STATE LAW

Federal law excludes amounts received by an individual as disability income from combat-related injuries. Combat-related injuries are defined as injuries that were incurred as a direct result of armed conflict, while engaged in extra-hazardous service, or in the performance of duty under conditions simulating war. Additionally, gross income does not include compensation received for active service as a member of the Armed Forces of the United States below the grade of a commissioned officer for any month the individual was serving in a combat zone or hospitalized

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as a result of wounds, disease, or injury incurred in a combat zone. Commissioned officers are allowed to exclude similar pay up to the maximum level received by enlisted personnel. In addition, benefits under laws administered by the Department of Veterans Affairs (VA), including disability compensation, are not subject to federal or state income tax.

Before 2002, federal law prohibited the concurrent receipt of military retired pay and disability compensation from the VA for the same period of service. Consequently, the retired pay of a military retiree was reduced by the amount of disability compensation received from the VA.

In 2002, federal law was amended to authorize the payment of additional compensation for a combat-related disability, known as Combat-Related Special Compensation (Special Compensation) (10 USC sec. 1413a) to certain military retirees. This payment is authorized under Title 10, United States Code, section 1413a, and is considered disability compensation, which is excluded from gross income.

In 2003, federal law was further amended to authorize the payment of additional retired pay to military retirees whose retired pay was reduced because of receiving disability compensation from the VA. The additional retired pay, known as Concurrent Receipt of Disability Pay (Disability Pay), authorized under Title 10, United States Code, section 1414, is subject to federal and state income tax.

California conforms to the federal gross income exclusions for compensation for combat-related injuries and disability pay, and the exclusion of veteran's benefits, without exception.

THIS BILL

This bill would, for taxable years beginning on or after January 1, 2015, exclude from gross income two specific forms of payments, Special Compensation and Disability Pay, as described above, to an "eligible individual".

This bill would define "eligible individual" as an active, reserve, or retired member of the United States military who served on active duty.

IMPLEMENTATION CONSIDERATIONS

Implementing this bill would not significantly impact the department's programs and operations.

TECHNICAL CONSIDERATIONS

Because Special Compensation payments are excluded from gross income under current federal and state tax laws, it is unnecessary to include those payments in this bill. Amendments 1 through 5 would remove reference to the Special Compensation payments.

Amendment 6 is suggested to clarify the definition of Disability Pay to avoid disputes between taxpayers and the department.

LEGISLATIVE HISTORY

AB 2004 (Knight, 2011/2012) similar to this bill, would have allowed an individual to exclude from gross income two specific combat-related types of payments for taxable years beginning on or after January 1, 2013. AB 2004 failed to pass from Assembly Revenue and Taxation Committee by the constitutional deadline.

AB 1077 (Anderson, 2009/2010) would have allowed an individual to exclude retirement pay and survivor annuities received as a result of active service in the military from gross income. AB 1077 failed to pass from the Assembly Revenue and Taxation Committee by the constitutional deadline.

SB 401 (Wolk, Chapter 14, Statutes of 2010) provides specified date of conformity to the Internal Revenue Code, including the sections that exclude from gross income combat-related injury pay and combat-related disability pay.

OTHER STATES' INFORMATION

The states surveyed include *Florida, Illinois, Massachusetts, Michigan, Minnesota, and New York*. These states were selected due to their similarities to California's economy, business entity types, and tax laws.

Florida only has a corporation income tax; therefore, this personal income tax exclusion is not applicable.

Illinois, Massachusetts, Michigan, Minnesota, and New York generally conform to federal rules for military combat-related pay.

FISCAL IMPACT

This bill would not significantly impact the department's costs.

ECONOMIC IMPACT

Revenue Estimate

Estimated Revenue Impact of AB 2329 As Introduced February 21, 2014 For Taxable Years Beginning On or After January 1, 2015 Assumed Enactment After June 30, 2014 (\$ in Millions)		
2014-15	2015-16	2016-17
- \$11	- \$19	- \$19

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill.

SUPPORT/OPPOSITION

Support: None provided.

Opposition: None provided.

ARGUMENTS

Proponents: Supporters could argue that this bill would provide needed tax relief for certain California veterans who are disabled and taxed on a portion of their military retirement disability pay.

Opponents: Some could argue that this bill would create a federal and California difference in the treatment of Disability Pay. The federal government treats this type of pay as taxable.

POLICY CONCERNS

This bill would create a difference between federal and California tax law, thereby increasing the complexity of California tax return preparation.

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FRANCHISE TAX BOARD'S
PROPOSED AMENDMENTS TO
AB 2329 as Introduced February 21, 2014

AMENDMENT 1

On page 2, lines 2-3, strikeout "Combat-Related Special Compensation or".

AMENDMENT 2

On page 2, strikeout lines 7 through 10, inclusive.

AMENDMENT 3

On page 2, line 11, strikeout "(2)", and insert:

"(1)"

AMENDMENT 4

On page 2, line 15, strikeout "(3)", and insert:

"(2)"

AMENDMENT 5

On page 2, line 19, strikeout "Combat-Related Special Compensation or".

AMENDMENT 6

On page 2, strikeout lines 12 through 14 inclusive, and insert:

"received as provided in Section 1414 of Title 10 of the United States Code by an eligible individual."