



## Analysis of Amended Bill

Author: Brough

Sponsor:

Bill Number: AB 2394

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Amended: March 19, 2018

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Related Bills: See Legislative  
History

**Subject:** Exclusion/Military Retirement Income

### Summary

The bill would, under the Personal Income Tax Law (PITL), exclude from gross income certain retirement pay received for military service.

**Recommendation – No position.**

### Summary of Amendments

The March 19, 2018, amendments removed provisions of the bill related to survivor benefits in the Military and Veterans Code and replaced them with the provisions discussed in this analysis.

This is the department's first analysis of the bill.

### Reason for the Bill

The reason for the bill is to provide tax relief for retired members of the United States Armed Forces.

### Effective/Operative Date

As a tax levy, this bill would be effective immediately upon enactment and operative for taxable years beginning on or after January 1, 2018.

### Federal/State Law

Existing federal and state laws provide that gross income includes all income from whatever source derived, including compensation for services, business income, gains from property, interest, dividends, rents, and royalties, unless specifically excluded.

Under federal and state tax laws, gross income excludes certain types of income for an individual's active service in the United States (U.S.) Armed Forces including, but are not limited to: military death benefits paid to qualified survivors, military pay for time served in combat zones, and the premium paid into a survivor annuity account for the qualified survivors of military personnel.

The term “U.S. Armed Forces” includes all regular and reserve components of the uniformed services that are subject to the jurisdiction of the Secretary of Defense, the Secretary of the Army, the Secretary of the Navy, or the Secretary of the Air Force, and each term also includes the Coast Guard. The members of such forces include commissioned officers and personnel below the grade of commissioned officers in such forces.<sup>1</sup>

For federal and state purposes, military retirement pay received by a taxpayer is generally taxable.

### **This Bill**

This bill would, under the PITL, for taxable years beginning on or after January 1, 2018, exclude from gross income any retirement pay received by a taxpayer from the federal government for military service performed in the Armed Forces of the United States, the reserve component of the Armed Forces of the United States, of the National Guard.

### **Implementation Considerations**

The department has identified the following implementation concern. Department staff is available to work with the author’s office to resolve this and other concerns that may be identified.

If this bill is enacted in late September or October of 2018, the department would have developed the forms and instructions for the 2018 taxable year. Thus, the department may incur additional costs to develop alternative forms and instructions in the short time frame necessary to ensure they are available for taxpayers to comply with the reporting requirement.

### **Legislative History**

AB 528 (Gray, 2017/2018) would have excluded from gross income a percentage of qualified retirement pay received by a taxpayer from the federal government for military service performed in the Armed Forces of the United States, the reserve component of the Armed Forces of the United States, or the National Guard. AB 528 failed to pass out of the Assembly by the constitutional deadline.

AB 1275 (Gray, 2015/2016), would have excluded from gross income the retirement pay received by a taxpayer from the federal government for military service performed in the U.S. Armed Forces, the reserve component of the U.S. Armed Forces, or the National Guard. AB 1275 would have also excluded the gross income survivor benefits received by a taxpayer from the federal government. AB 1275 failed to pass out of the Assembly by the constitutional deadline.

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<sup>1</sup> See Revenue and Taxation Code section 17022.

AB 505 (Melendez, 2015/2016), would have excluded from gross income the additional retired pay to military retirees, known as concurrent retirement and disability pay payments. AB 505 failed to pass out of the Assembly 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 out of the Assembly by the constitutional deadline.

### **Other States' Information**

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

*Illinois, Massachusetts, Michigan, Minnesota and New York* all allow an exclusion from gross income for retired pay received pursuant to a retirement plan for members of the U.S. Armed Forces.

### **Fiscal Impact**

The department's costs to implement this bill have yet to be determined. As the bill moves through the legislative process, costs will be identified.

### **Economic Impact**

#### Revenue Estimate

This bill would result in the following revenue loss:

Estimated Revenue Impact of AB 2394 as Amended March 19, 2018  
For Taxable Years Beginning On or After January 1, 2018  
Assumed Enactment after June 30, 2018

(\$ in Millions)

Fiscal Year	Revenue
2018-2019	- \$150
2019-2020	- \$95
2020-2021	- \$95

This analysis does not account for changes in employment, personal income, or gross state product that could result from this bill or for the net final payment method of accrual.

## Revenue Discussion

Based on data from the United States Department of Defense (DOD), California military retirees received approximately \$340 million per month, or \$4 billion per year in retirement payments in 2016. This amount is grown by 1 percent annually based on the observed growth rate for retirement payments over the last five years, resulting in an income exclusion of \$4.1 billion in the 2018 taxable year. This amount is then multiplied by an estimated average tax rate for qualified taxpayers of 2.5 percent, resulting in an estimated revenue loss of \$95 million in the 2018 taxable year.

The estimates are converted fiscal-year estimates and then rounded to arrive at the amounts shown in the above table.

## Support/Opposition<sup>2</sup>

Support: National Guard Association of California, Military Officers Association of America – CA Council of Chapters.

Opposition: None provided.

## Arguments

Proponents: Some may argue that this bill would provide much needed tax relief for retired members of the United States Armed Forces.

Opponents: Some may argue that this bill would favor one group of taxpayers over another creating inequity amongst taxpayers.

## Policy Concerns

This bill lacks a sunset date. Sunset dates generally are provided to allow periodic review of the effectiveness of a tax benefit by the Legislature.

This bill would establish an exclusion from gross income for which federal law has no counterpart, thus increasing nonconformity.

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<sup>2</sup> As provided by the staffer.