DEPARTMENT OF TAXATION
2024 Fiscal Impact Statement

1. **Patron** Hyland F. "Buddy" Fowler

2. **Bill Number** HB 1407

House of Origin:
X **Introduced**
_____ **Substitute**
_____ **Engrossed**

Second House:
_____ **In Committee**
_____ **Substitute**
_____ **Enrolled**

3. **Committee** House Finance

4. **Title** Income Tax Subtraction; Military Retirement Benefits; Uniformed Services.

5. **Summary/Purpose:**

This bill would expand the military benefits income tax subtraction by changing the definition of "military benefits" to include retirement income received for service in the uniformed services of the United States, which includes the United States Armed Forces, the commissioned corps of the National Oceanic and Atmospheric Administration, and the commissioned corps of the United States Public Health Service. Under current law, the subtraction is only allowed for military retirement income received for service in the United States Armed Forces.

If passed during the 2024 General Assembly Session, this bill would be effective July 1, 2024.

6. **Budget amendment necessary:** Yes.
Item(s): Page 1, Revenue Estimates

7. **Fiscal Impact Estimates are:** Preliminary (See Line 8.)
7b. Revenue Impact:

Fiscal Year	***Dollars***	***Fund***
2025	($680,000)	GF
2026	($570,000)	GF
2027	($610,000)	GF
2028	($650,000)	GF
2029	($690,000)	GF
2030	($730,000)	GF

8. **Fiscal implications:**

Administrative Costs

The Department of Taxation ("the Department") considers implementation of this bill as routine and does not require additional funding.

Revenue Impact

Based on data from the U.S. Coast Guard Pay and Personnel Center, which manages the retirement programs for the Commissioned Corps of the National Oceanic and Atmospheric Administrative and the United States Public Health Service, the proposed legislation would decrease General Fund revenues by an estimated $680,000 in FY 2025, $570,000 in FY 2026, $610,000 in FY 2027, $650,000 in FY 2028, $690,000 in FY 2029, and $730,000 in FY 2030.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: Yes.

As currently drafted, the expansion of the subtraction to all uniformed servicemember's would take effect on July 1, 2024, which is in the middle of the taxable year for taxpayers who file on a calendar basis. To ensure that the credit expansion covers the entirety of Taxable Year 2024, the following amendment is suggested:

> Line 231, Insert: "2. That the provisions of this bill are effective for taxable years beginning on and after January 1, 2024."

Because of the broadness of the term "retirement income," this subtraction could be interpreted to apply to distributions from defined contribution plans. If the intent is to limit this subtraction to amounts received from a uniformed service member's pension only, the Department suggests the following clarifying technical amendment:

> Line 101 after "Virginia or federal law."
> Insert: For the purposes of this subtraction, "retirement income" means any amounts received from a uniformed servicemember's pension plan.

11. Other comments:

Virginia Military Tax Preferences

Taxpayers may subtract the following military-related items for the purposes of computing Virginia taxable income:

- Wages or salaries received for service in the Virginia National Guard, not exceeding income for thirty-nine days of service or $3,000, whichever is less. This subtraction only applies to persons in the ranks of O3 and below.

- All military pay and allowances earned while serving in a combat zone or qualified hazardous duty area, to the extent they were included in federal adjusted gross income.

- $15,000 of military basic pay for military personnel on extended active duty for periods in excess of ninety days. The subtraction amount is reduced dollar-for-dollar by the amount which the taxpayer's military basic pay exceeds $15,000 and will be reduced to zero if such pay is equal to or exceeds $30,000.

- The amount of military death gratuity payments received after September 11, 2001, by survivors of military personnel who are killed in the line of duty. This subtraction amount must be reduced dollar-for-dollar by the amount that is allowed as an exclusion from federal adjusted gross income to the survivor on his or her federal income tax return.

- Any amount received as military retirement income by an individual awarded the Congressional Medal of Honor.

- Up to $10,000 of military benefits in Taxable Year 2022, up to $20,000 in Taxable Year 2023, up to $30,000 in Taxable Year 2024, and up to $40,000 in Taxable Year 2025 and each taxable year thereafter. For Taxable Years 2022 and 2023, the subtraction is limited to recipients of such military benefits that are age 55 and older.

For taxable years beginning on or after January 1, 2011, Virginia exempts from taxation the real property, including the joint real property of a husband and wife, and the land, not exceeding one acre, upon which the real property is situated of any military veteran who has been rated by the VA to have a 100 percent service-connected, permanent, and total disability, and who occupies the real property as his or her principal place of residence. The surviving spouse of a veteran may also qualify for this exemption, so long as the following conditions are met: the veteran's death occurred on or after January 1, 2011; the surviving spouse does not remarry; and the surviving spouse continues to occupy such real property as his or her principal place of residence.

<u>Virginia's Individual Income Tax Modifications</u>

Federal Adjusted Gross Income

Virginia's Individual Income Tax substantially conforms to federal income tax law by using federal adjusted gross income ("FAGI") as the starting point for computing Virginia income taxes. Virginia law then provides various modifications to FAGI that must be taken into account that figure in determining Virginia taxable income.

Virginia Adjusted Gross Income

When completing a Virginia individual income tax return, a taxpayer starts with the amount of FAGI reported on his federal return. A taxpayer then calculates Virginia adjusted gross income by making two types of adjustments: (1) "additions" which increase the amount of income taxable by Virginia and (2) "subtractions" which reduce such amount. These adjustments are made only to the extent that they have not already been included or excluded from FAGI.

Virginia Taxable Income

The taxpayer calculates his Virginia taxable income by making another type of modification referred to as "deductions," which further reduce the amount of income taxable by Virginia.

These modifications are made regardless of federal treatment unless specifically stated otherwise in the provision.

Please find below an illustration of how taxable income is computed for federal and Virginia income tax purposes and how they interrelate:

Federal Income Tax	Virginia Income Tax
+Wages and Other Income	*=Federal Adjusted Gross Income ("FAGI")*
+Federal Adjustments	+Virginia Additions (only if not included in FAGI)
-Federal Adjustments	-Virginia Subtractions (only if not excluded from FAGI)
=Federal Adjusted Gross Income ("FAGI")	*=Virginia Adjusted Gross Income ("VAGI")*
-Federal Standard Deduction or Itemized Deductions	-Virginia Standard Deduction or Federal Itemized Deductions (depends on federal election)
-QBI Deduction	-Deduction for Virginia Exemptions
	-Virginia Deductions (regardless of federal treatment)
=Federal Taxable Income	*=Virginia Taxable Income*

Because this bill would expand the military benefits income tax subtraction, the amount allowed under this bill could be taken whether the taxpayer choses to take the Virginia standard deduction or itemized their deductions.

<u>Proposed Legislation</u>

This bill would expand the military benefits income tax subtraction by changing the definition of "military benefits" to include retirement income received for service in the uniformed services of the United States, which includes the United States Armed Forces, the commissioned corps of the National Oceanic and Atmospheric Administration, and the commissioned corps of the United States Public Health Service. Under current law, the subtraction is only allowed for military retirement income received for service in the United States Armed Forces.

The expanded definition of "military benefits" under this bill would apply to the following:

- Retirement income received for service in the uniformed services of the United States as such term is defined under federal law;

- Qualified military benefits received pursuant to a section of the Internal Revenue Code regarding certain military benefits;

- Benefits paid to the surviving spouse of a veteran of the Armed Forces of the United States under the Survivor Benefit Plan program established by the U.S. Department of Defense, and

- Retirement income paid to the surviving spouse of a veteran of the uniformed services of the United States for such veteran's service.

If passed during the 2024 General Assembly Session, this bill would be effective July 1, 2024.

Similar Legislation

SB 10 is identical to this bill.

SB 61 and **HB 1292** would establish an individual income tax subtraction for firefighter retirement income.

HB 518 would establish an individual income tax subtraction for certain individuals receiving Foreign Service retirement income.

HB 651 would remove the age requirement from the individual income tax subtraction for "military benefits."

SB 662 would establish an individual income tax subtraction for state police retirement income.

cc : Secretary of Finance

Date: 1/31/2024 SJH
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