



GOVERNOR'S OFFICE OF
BUDGET AND PROGRAM PLANNING

Fiscal Note 2025 Biennium

Bill information:	
SB0104 - Exempt retired military pensions from state income tax (Fuller, John)	
Status:	As Amended in House Committee

- Significant Local Gov Impact
 Needs to be included in HB 2
 Technical Concerns
 Included in the Executive Budget
 Significant Long-Term Impacts
 Dedicated Revenue Form Attached

FISCAL SUMMARY

	<u>FY 2024</u> <u>Difference</u>	<u>FY 2025</u> <u>Difference</u>	<u>FY 2026</u> <u>Difference</u>	<u>FY 2027</u> <u>Difference</u>
Expenditures:				
General Fund	\$0	\$0	\$0	\$0
Revenue:				
General Fund	(\$831,000)	(\$4,350,000)	(\$4,547,000)	(\$4,741,000)
Net Impact-General Fund Balance:	<u>(\$831,000)</u>	<u>(\$4,350,000)</u>	<u>(\$4,547,000)</u>	<u>(\$4,741,000)</u>

Description of fiscal impact: As amended by the House Committee of the Whole, SB 104 exempts, for up to five years, a portion of certain military retirement pay from Montana personal income tax for taxpayers who become residents of the state after June 30, 2023, or who were a resident of the state before receiving military retirement income and remained a resident. The income exclusion would be available starting in TY 2024 and sunsets after TY 2033.

FISCAL ANALYSIS

Assumptions:

Department of Revenue (DOR)

- Currently, tenure based military retirement income and survivor benefits are Montana taxable income.
- As amended, SB 104 exempts the lesser of 50% of military retirement pay and survivor benefits or the taxpayer's "Montana source wage income" from income tax starting in TY 2024. For the bill, "Montana source wage income" is the taxpayer's wages, salary tips and other compensation for services performed in the state, and net income from a trade, business, profession, or occupation carried out in the state, and net income from farming activities carried on in the state. The exemption is limited to taxpayers who become residents of the state after June 30, 2023, or who were a resident of the state before receiving military pension or military retirement income and remained a resident after receiving military pension or military retirement income. The exemption can only be claimed for five consecutive years after the taxpayer meets the exemption limitation.

3. SB 104 as amended; the exemption created by SB 104 expires at the end of TY 2033.
4. Most retirement income is reported on 1099-R forms provided by the U.S. Treasury e-File (MeF) program. That data shows 7,983 Montana full-year resident filers, in TY 2021, received retirement income from the U.S. Department of Defense’s Defense Finance and Accounting Service. Since not all taxpayers file their returns through a MeF electronic filing provider, only about 90% of total reported taxable retirement income is reported electronically. Taxable military retirement income reported on MeF Montana Forms 1099-R likely undercounts actual military retirement income by 10%. The 7,983 recipients of electronically recorded military retirement income reported \$215.7 million of such income in TY 2021. After adjusting for coverage, it is estimated that total Montana taxable military retirement income was about \$240 million in TY 2021.
5. SB 104, as amended by the House, limits the exemption to veterans who become a resident of the state after June 30, 2023, or those who were a resident of the state before receiving military pension or retirement income and remained a resident after receiving the military income. As the Department of Revenue cannot verify the date military retirement income was first received for the approximately 8,870 (7,983/0.90) current full-year resident filers, (see technical note #1) it is assumed that each taxpayer would qualify for the exemption the first tax year the exemption is available and will claim the exemption for five years.
6. The DOR income tax model (with HJ 2 assumptions) was modified to incorporate the military income exemption in SB 104 as amended. The estimated income and tax liability under SB 104 were compared to current law income and tax liability. The comparisons show that exempting a portion of military retirement income starting in TY 2024 would reduce full-year resident tax liability as follows:

Tax Liability Under Current Law and SB 104 as Amended			
Tax Liability (Millions)			
Tax Year	Current Law	SB 104	Change in Revenue
2024	\$1,832.790	\$1,829.375	(\$3.415)
2025	\$1,924.211	\$1,920.644	(\$3.568)
2026	\$2,050.048	\$2,046.337	(\$3.711)
2027	\$2,121.827	\$2,117.981	(\$3.846)

7. As SB 104 makes significant changes, some taxpayers will adjust their withholding and estimated payments. It is assumed that 80% of TY 2024 and 20% of TY 2025 tax liability changes will be collected in FY 2025. Similar timing is anticipated to continue in subsequent years.
8. The change in full-year resident tax liability was converted to fiscal years based on the factors used in HJ 2 (FY 2024 and FY 2025) and HJ 2 consistent assumptions for FY 2026 and FY 2027.
9. After applying the conversion factors, income tax revenue is estimated to be reduced by \$831,000 in FY 2024, \$4.35 million in FY 2025, \$4.547 million in FY 2026, and \$4.741 million in FY 2027
10. The changes made by SB 104 can be made as part of the DOR annual change process at no additional expense.

<u>Fiscal Impact:</u>	<u>FY 2024</u>	<u>FY 2025</u>	<u>FY 2026</u>	<u>FY 2027</u>
	<u>Difference</u>	<u>Difference</u>	<u>Difference</u>	<u>Difference</u>
Department of Revenue				
FTE	0.00	0.00	0.00	0.00
<u>Expenditures:</u>				
Personal Services	\$0	\$0	\$0	\$0
TOTAL Expenditures	\$0	\$0	\$0	\$0
<u>Funding of Expenditures:</u>				
General Fund (01)	\$0	\$0	\$0	\$0
TOTAL Funding of Exp.	\$0	\$0	\$0	\$0
<u>Revenues:</u>				
General Fund (01)	(\$831,000)	(\$4,350,000)	(\$4,547,000)	(\$4,741,000)
TOTAL Revenues	(\$831,000)	(\$4,350,000)	(\$4,547,000)	(\$4,741,000)
<u>Net Impact to Fund Balance (Revenue minus Funding of Expenditures):</u>				
General Fund (01)	(\$831,000)	(\$4,350,000)	(\$4,547,000)	(\$4,741,000)


Long-Term Impacts:

1. This fiscal note assumes that taxpayers who were receiving military pension income before TY 2024 would qualify for the pension exemption for a 5-year period, starting TY 2024. The MeF data and matched Montana tax returns suggest that there are approximately 270 new recipients of military retirement income each year, holding the pool of military retirement income relatively stable over time. SB 104’s costs would peak in TY 2028 (FY 2029) and then decrease by around 80% after the initial group of qualifying taxpayers reach their fifth year claiming the exemption and can no longer claim the exemption.

Technical Notes:

1. As amended in the House , the proposed bill limits the income tax exemption to taxpayers “who was a resident of the state before receiving military pension or military retirement income and remained a resident after receiving military pension or military retirement income.” Verifying this condition for the exemption for some taxpayers is expected to be difficult, or impractical, and would require significant time by the department.
2. Many Montanans that serve in the armed forces maintain Montana as their “home of record” when posted out of state and are not required to file Montana resident income taxes when serving elsewhere. They would have to re-establish Montana residency before being eligible for the military retirement income exclusion.

NO SPONSOR SIGNATURE

	5/1/23		5-1-23
<i>Sponsor's Initials</i>	<i>Date</i>	<i>Budget Director's Initials</i>	<i>Date</i>