

**REPORT OF THE  
VIRGINIA DEPARTMENT OF VETERANS SERVICES  
AND VIRGINIA DEPARTMENT OF TAXATION**

# **Feasibility Study of Exempting Military Retirement Income from Taxation (HJR 674, 2019)**

**TO THE GOVERNOR AND  
THE GENERAL ASSEMBLY OF VIRGINIA**



## **HOUSE DOCUMENT NO. 14**

**COMMONWEALTH OF VIRGINIA  
RICHMOND  
2019**





# COMMONWEALTH of VIRGINIA

## *Department of Veterans Services*

Steven J. Combs  
Acting Commissioner

Telephone: (804) 786-0220  
Fax: (804) 786-0302

November 25, 2019

The Honorable S. Chris Jones  
Chairman, House Appropriations Committee  
900 East Main St, 13<sup>th</sup> Floor  
Richmond, VA 23219

The Honorable Emmett Hanger  
Co-Chairman, Senate Finance Committee  
900 East Main St, 14<sup>th</sup> Floor  
Richmond, VA 23219

The Honorable Thomas K. Norment  
Co-Chairman, Senate Finance Committee  
900 East Main St, 14<sup>th</sup> Floor  
Richmond, VA 23219

*Delivered via electronic mail*

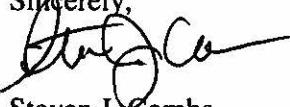
Re: House Joint Resolution 674 (HJ674), 2019 General Assembly

Dear Chairmen Jones, Hanger, and Norment:

Please find attached the report to the Governor and General Assembly pursuant to HJ674, which requested that the Department of Veterans Services (DVS) and the Department of Taxation (TAX) study the feasibility of exempting military retirement income from taxation.

The report consists of an Executive Summary, Powerpoint presentation on our findings, and a Powerpoint presentation with Case Studies that compares the competitiveness of Virginia with other states. All master data collected including spreadsheets, research materials, and notes, are available upon request.

On behalf of the DVS-TAX study team, thank you for this opportunity to research this issue. Please let me know if we may provide additional information.

Sincerely,  
  
Steven J. Combs  
Acting Commissioner

Cc: Delegate Luke Torian  
The Honorable Carlos Hopkins, Secretary of Veterans and Defense Affairs  
Mr. Craig Burns, Commissioner, TAX  
HJ674 Work Group Members



## **HJ674 Study - Requesting the Department of Veterans Services and the Department of Taxation to study the feasibility of exempting military retirement income from taxation.**

---

### **EXECUTIVE SUMMARY**

#### **BACKGROUND**

In 2017, a study by The Matrix Group and The Roosevelt Group examined the impact of exempting military retirement income from state taxation. The 2017 Matix/Roosevelt study concluded that:

- “By exempting all military retiree pensions from state income tax, the Commonwealth would incur nearly \$145 million in foregone tax revenue during the first year... – almost twice as much as the Secretary of Veterans and Defense Affairs FY 2017 budget;” and
- Additionally, the study found that “implementing a tax exemption on military pensions as a means of attracting military retirees has not proven to be effective in states with large populations.

In 2019, Delegate Luke Torian introduced the resolution HJ674, which requested that the Virginia Department of Veterans Services (DVS) and the Virginia Department of Taxation (TAX) jointly study the feasibility of exempting military retirement income from taxation, in response to a request by the JLC (Joint Leadership Council of Veterans Service Organizations) to reexamine and build upon the 2017 Matrix/Roosevelt report.

#### **HJ674 STUDY – AGENCY ROLES**

DVS and TAX formed a joint workgroup (see *Appendix B* for list of members). As part of the HJ647 study:

DVS studied the costs and benefits across states affecting veterans and retirees (*see detail in PowerPoint report*) that:

- Consider all tax types (e.g., income, sales, and property taxes) across all states (& Washington DC);
- Consider tax exemptions specific to military retirees across all states—plus services and programs offered;
- Focus on 12 states with the most military retirees;
- Show a slightly rising population of military retirees in Virginia, which suggest the state remains an attractive destination for retirees; and
- Compare two case studies of a “typical” Virginia military retiree and how the various tax exemptions and structures would affect him or her in: Alexandria, VA; Houston, TX; Raleigh-Durham, NC; or Jacksonville, FL.

TAX estimated the fiscal impact on Virginia’s tax revenue of a range of options for an income tax exemption (*see detail in PowerPoint report*) that:

- Account for Virginia-specific conditions—notably the means-tested exemption available to all retirees age 65 and older (despite no exemption for military retirees specifically);

- Rely heavily on data/forecasts from the U.S. Departments of Defense and Veterans Affairs; and
- Outline five potential courses of action the General Assembly could take (a full exemption, and four other options)

## **HJ674 STUDY – STATE COMPARISONS**

A majority of states exclude all or a portion of retirement pay from taxable income, according to sources including the National Conference of State Legislatures (NCSL). Depending on the state, the retirees eligible for these exemptions can range from military-only to all retirees. Eligibility also can be limited to age 65 and older or extend to retirees age 64 and younger.

For example, 20 states provide a full military retirement pay exemption and another nine states do not tax state income.<sup>1</sup> Among the remaining states, Virginia is among 19 that offer a partial exemption to retirees age 65 and older.<sup>2</sup> Virginia also is among nine states (including Washington D.C.) that offer no exemption to retirees age 64 and younger.<sup>3</sup>

It is important to note that categorizing states by exemption status does not provide a complete picture. For example, a report from the financial company Kiplinger found that 10 states with a full military retiree tax exemption are “not tax-friendly” or are “least tax-friendly” to all retirees or all residents. Kiplinger’s rates Virginia as “tax-friendly” for all retirees and says, “The Old Dominion offers some tax breaks to retirees. It does not tax Social Security benefits, and residents 65 and older can deduct up to \$12,000 per person of income, which may be subject to income-eligibility limits. Virginia’s property taxes are modest (with breaks for seniors available), and its sales tax low.” Meanwhile, CNBC, the financial cable network, named Virginia the top state for business.<sup>4</sup>

## **SUMMARY OF THE FIVE POLICY OPTIONS**

Five policy options for an exemption were estimated for the House Appropriations and Senate Finance Committees to consider. Our research does not include a cost-benefit analysis of each of these options to consider. What this study did find is that:

- Although Virginia offers no income tax exemption specific to military retirees, the state is “tax friendly” to retirees in part because it offers an exemption to those age 65 and older that is means-tested for certain taxpayers.
- Virginia is attractive to military retirees because it has built many unique assets through the strong support from the General Assembly and several Governors, including the V3 program, world-class educational institutions, wrap-around supportive services led by the

<sup>1</sup> Full-exemption states: AL, AR, CT, HI, IL, IA, KS, LA, ME, MA, MI, MN, MS, MO, NJ, NY, OH, PA, WV, WI;  
No-tax states: AK, FL, NV, NH, SD, TN, TX, WA, WY

<sup>2</sup> Partial exemption to age 65 and older: AZ, CO, DE, GA, ID, IN, KY, MD, MT, NE, NM, NC, OK, OR, RI, SC, UT, VT, VA.

<sup>3</sup> No exemption to age 64 and younger: CA, ID, NM, ND, RI, UT, VT, VA, DC.

<sup>4</sup> Source: <https://www.cnbc.com/2019/07/09/virginia-is-americas-top-state-for-business-in-2019.html>

DVS Virginia Veteran and Family Support service line and a state-wide appreciation for our military and the valuable leadership skills and abilities they bring to our communities.

Below are five options estimated by TAX, (*see detail in PowerPoint report*) chosen from among a range of policy options available in other states, and have been brought up by retirees to DVS:

- A full military retirement income tax exemption in Virginia = -\$295 million revenue loss by 2027
- Other policy options include:
  - Refundable tax credit of \$5,000 = -\$783 million loss by 2027
  - Fixed subtraction of \$40,000 = -\$247 million
  - Full exemption for retirees age 65 and older only = -\$112 million
  - Phased-in fixed subtraction rising from \$10,000 to \$40,000 over four years for retirees age 65 and older only = -\$97 million

### Comparison of Policy Options for Exempting Military Retirement Pay

Cost of other policy options as share of baseline full exemption

Virginia FY	Baseline Full Exemption Cost (\$M)*	Number of Retirees	Refundable tax credit <sup>1</sup>	Fixed subtraction <sup>2</sup>	Exemption for Age 65+ only <sup>3</sup>	Phased-in Fixed subtraction for Age 65+ only <sup>4</sup>
2020	-\$112.6	152,005	338%	85%	33%	15%
2021	-\$229.7	152,682	332%	85%	33%	21%
2022	-\$239.2	153,290	320%	85%	34%	28%
2023	-\$249.4	153,909	309%	85%	35%	30%
2024	-\$260.4	156,010	298%	84%	36%	32%
2025	-\$272.0	156,330	287%	84%	36%	32%
2026	-\$283.6	156,540	276%	84%	37%	32%
2027	-\$295.2	156,642	265%	84%	38%	33%

\* Assumes 1/1/2020 effective date and no adjustment for timing of passage; For a normal revenue impact, FY 2020 impact would be shifted to FY 2021

<sup>1</sup> Tax credit of \$5,000

<sup>2</sup> Fixed subtraction of \$40,000

<sup>3</sup> Full exemption only if age 65 & older; no exemption for younger age groups

<sup>4</sup> Fixed subtraction rising from \$10,000 to \$40,000 over four years for age 65 and older

### CONCLUSION

The General Assembly tasked DVS and TAX to convene a joint working group to study the feasibility of exempting military retirement income from taxation and evaluate the effects of phasing in a full exemption of military retirement income over a four-year, five-year, or six-year period or any other time period the Agencies deem appropriate. DVS and TAX considered the impact of fully exempting military retirement income of Virginia’s current population of veterans, the projected effect of such an exemption of Virginia’s competitiveness as a desirable state of residence and the revenue losses associated with fully exempting military retirement income (HJ674, Appendix A).

DVS and TAX are thankful to all staff who contributed to this report and for all their hard work and due diligence to consider all options (Appendix B). We hope the General Assembly finds this report helpful.

## **SUMMARY OF APPENDICES AND ATTACHMENTS**

Appendix A: House Joint Resolution 674 (HJ674), 2019 General Assembly

Appendix B: Work Group Team

Attachment 1: Formal report (as a PowerPoint presentation) with all the above information in text and charts.

Appendix 2: two case studies examined the competitiveness issue, and is also presented as a PowerPoint presentation

All raw data was compiled in Excel spreadsheets, and is available upon request.



# APPENDIX A

## HJ674

2019 SESSION

ENROLLED

### HOUSE JOINT RESOLUTION NO. 674

*Requesting the Department of Veterans Services and the Department of Taxation to study the feasibility of exempting military retirement income from taxation. Report.*

Agreed to by the House of Delegates, February 4, 2019

Agreed to by the Senate, February 20, 2019

WHEREAS, over half of the states exempt military retirement income or a portion thereof from taxation; and

WHEREAS, Maryland, North Carolina, and West Virginia, which share a border with Virginia, either partially or fully exempt military retirement income from taxation; and

WHEREAS, Virginia currently exempts military retirement income from taxation only if the taxpayer is a recipient of the Congressional Medal of Honor; and

WHEREAS, Virginia should strive to maintain its reputation as a veteran-friendly state and, more importantly, strive to reward veterans for their service to Virginia and the United States by fully exempting military retirement income from state income tax; now, therefore, be it

RESOLVED by the House of Delegates, the Senate concurring, That the Department of Veterans Services and the Department of Taxation (the Agencies) be requested to convene a joint working group to study the feasibility of exempting military retirement income from taxation.

In conducting their study, the Agencies shall evaluate the effects of phasing in a full exemption of military retirement income over a four-year, five-year, or six-year period or any other time period the Agencies deem appropriate. The Agencies shall consider (i) the impact of fully exempting military retirement income on Virginia's current population of veterans, (ii) the projected effect of such exemption on Virginia's competitiveness as a desirable state of residence for veterans in comparison with other states, (iii) the revenue losses associated with fully exempting military retirement income from state income tax, and (iv) any other factors the Agencies deem relevant. The Agencies shall review any other issues and make recommendations as appropriate.

All agencies of the Commonwealth shall provide assistance to the Agencies for this study upon request.

The Agencies shall complete their meetings by November 30, 2019, and shall submit to the Governor and the General Assembly an executive summary and a report of their findings and recommendations for publication as a House or Senate document. The executive summary and report shall be submitted as provided in the procedures of the Division of Legislative Automated Systems for the processing of legislative documents and reports no later than the first day of the 2020 Regular Session of the General Assembly and shall be posted on the General Assembly's website.

ENROLLED

HJ674ER

## APPENDIX B

### WORK GROUP TEAM

#### *Veterans and Defense Affairs/ Virginia Department of Veterans Services*

Kathleen Jabs  
*Deputy Secretary  
Veterans and Defense Affairs*

Steven J. Combs  
*Acting Commissioner*

Carrie Ann Alford  
*Director of Policy & Planning*

Bryan Harrison  
*Policy Analyst*

Tammy Davidson  
*Director of Finance*

#### *Virginia Department of Taxation*

Charles W. Hartgrove, ICMA-CM  
*Chief Deputy Commissioner*

William White  
*Assistant Commissioner, Office of Tax Policy*

Kristin Collins  
*Policy Development Director*

Aisha Yededji  
*Lead Economist, Policy Development*

Frank Badillo  
*Economist*

Matthew Huntley  
*Lead Tax Policy Analyst*

Stuart Carter  
*Chief Economist*

Sam Bosch  
*Management Analyst*

Ryan Cunningham  
*Tax Policy Analyst*

# HJ674 Study

Requesting the Department of Veterans Services (DVS) and the Department of Taxation (TAX) to study the feasibility of exempting military retirement income from taxation

October 11, 2019

- ▶ In 2017, a study by The Matrix Group and The Roosevelt Group, concluded that:
  - ▶ “By exempting all military retiree pensions from state income tax, the Commonwealth would incur nearly \$145 million in foregone tax revenue during the first year... – almost twice as much as the Secretary of Veterans and Defense Affairs FY 2017 budget.”
  - ▶ Additionally, the study found that “implementing a tax exemption on military pensions as a means of attracting military retirees has not proven to be effective in states with large populations.
- ▶ In 2019, Delegate Luke Torian introduced HJ674, which requested a joint DVS-TAX study in response to a request by the JLC to reexamine and build upon the 2017 work.
- ▶ In this study:
  - ▶ DVS has compared costs and benefits across states affecting veterans and retirees.
  - ▶ TAX has estimated the fiscal impact on Virginia’s tax revenue of a range of options for an income tax exemption.

## DVS's state comparisons:

- ▶ Consider all tax types (e.g., income, sales, and property taxes) across all states (& Washington DC)
- ▶ Consider tax exemptions specific to military retirees across all states—plus services and programs offered
- ▶ Focus on 12 states with the most military retirees
- ▶ Show a slightly rising population of military retirees in Virginia, which suggest the state remains an attractive destination for retirees
- ▶ DVS developed two case studies (see Appendix A) of a “typical” Virginia military retiree and how the various tax exemptions and structures would affect him or her in: Alexandria, VA; Houston, TX; Raleigh-Durham, NC; or Jacksonville, FL.

## TAX's fiscal impact:

- ▶ Accounts for Virginia-specific conditions—notably the exemption available to all retirees age 65 and older that may be means-tested (despite no exemption for military retirees specifically)
- ▶ Relies heavily on data/forecasts from the U.S. Departments of Defense and Veterans Affairs
- ▶ Outlines five potential courses of action the General Assembly could take (a full exemption + four other options)

- ▶ Five policy options for an exemption were estimated for the House Appropriations and Senate Finance Committees to consider. Our research does not include a cost-benefit analysis of each of these options to consider. What this study did find is that:
  - ▶ Although Virginia offers no income tax exemption specific to military retirees, the state is “tax friendly” to retirees in part because it offers an exemption to those age 65 and older that may be means-tested for certain taxpayers.
  - ▶ Virginia is attractive to military retirees because it has built many unique assets through the strong support from the General Assembly and several Governors, including the V3 program, world-class educational institutions, wrap-around supportive services led by the DVS Virginia Veteran and Family Support service line and a commonwealth-wide appreciation for our military and the valuable leadership skills and abilities they bring to our communities.
- ▶ The following slides show in detail how DVS and TAX conducted the research and reached their conclusions.

- ▶ Congressional Research Service (CRS) Report “Military Retirement: Background and Recent Developments” July 12, 2019 <https://fas.org/sgp/crs/misc/RL34751.pdf>
- ▶ The military retirement system is a government-funded, noncontributory, defined benefit system...currently includes monthly compensation for qualified active and reserve retirees, disability benefits for those deemed medically unfit to serve, and a survivor annuity program for the eligible survivors of deceased retirees. Military retirees are also entitled to nonmonetary benefits including exchange and commissary privileges, medical care through TRICARE, and access to Morale, Welfare and Recreation (MWR) facilities and programs.
- ▶ Currently, there are three general categories of military retiree –
  - ▶ active component,
  - ▶ reserve component, and
  - ▶ disability retiree.

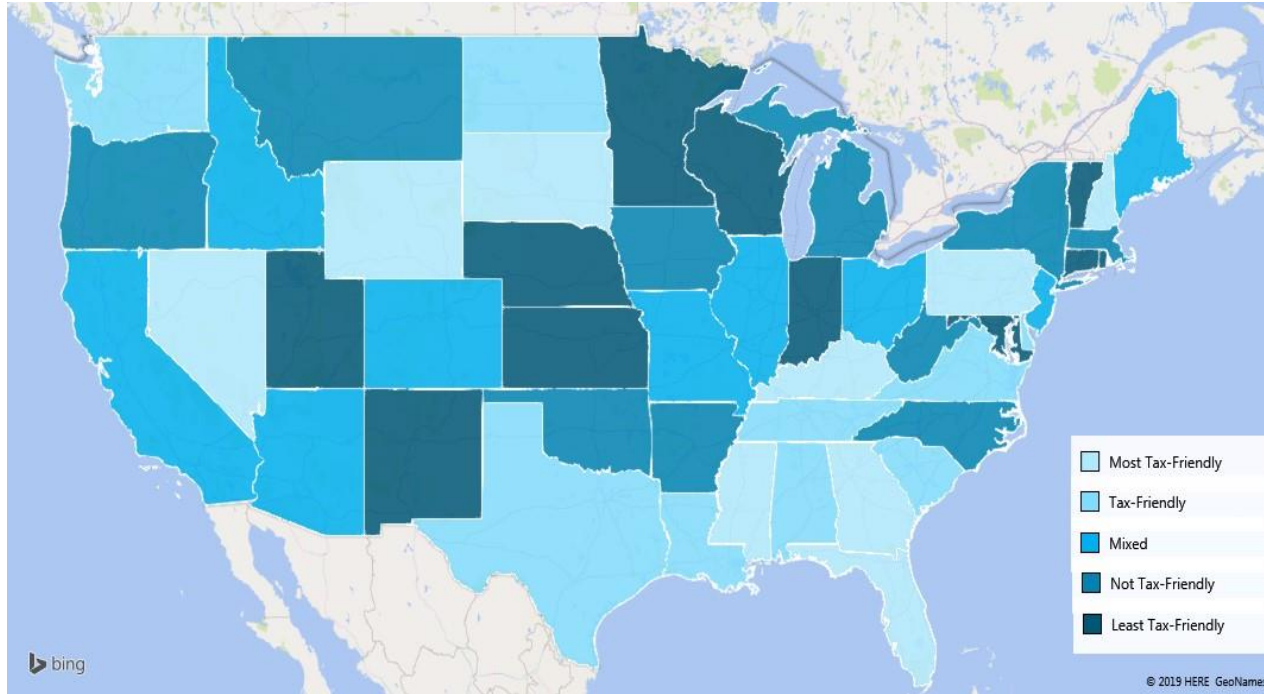
Active component personnel are eligible for retirement (i.e., vested) after completing 20 years of service (YOS). Reserve personnel are eligible after 20 years of creditable service based on a points system, but do not typically begin to draw retirement pay until age 60. Finally, those with a disability retirement do not need to have served 20 years to be eligible for retired pay; however, they must have been found unqualified for further service due to a permanent, stable disability.

- ▶ **Code of Virginia § 2.2-2000.1. Definitions.**
- ▶ "Active military, naval, or air service members" means military service members who perform full-time duty in the Armed Forces of the United States, or a reserve component thereof, including the National Guard.
- ▶ "Veteran" means any person who has received an honorable discharge and (i) has provided more than 180 consecutive days of full-time, active-duty service in the armed forces of the United States or reserve components thereof, including the National Guard, or (ii) has a service-connected disability rating fixed by the United States Department of Veterans Affairs.
- ▶ "Service-connected" means, with respect to disability, that such disability was incurred or aggravated in the line of duty in the active military, naval, or air service.
- ▶ "Service disabled veteran" means a veteran who (i) served in the active military, naval, or air service, (ii) was discharged or released under conditions other than dishonorable, and (iii) has a service-connected disability rating fixed by the U.S. Department of Veterans Affairs.



Comparing Virginia to other states, Kiplinger rates Virginia as tax-friendly for retirees.

## Kiplinger's State Tax-Friendliness Ratings for Retirees



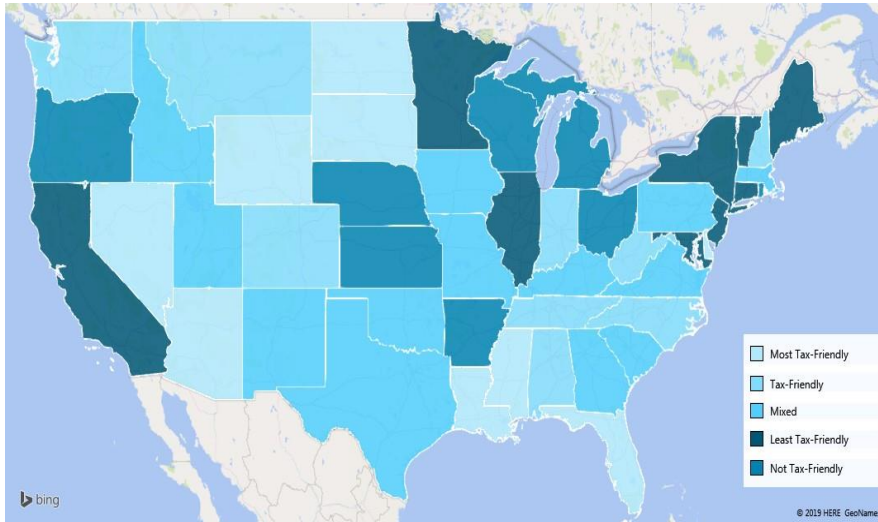
Note: Alaska is rated as Most Tax-Friendly and Hawaii is rated as Tax-Friendly.

Source: Kiplinger and Microsoft Excel 3D Maps



For all residents (not just retirees), Kiplinger rates Virginia's tax-friendliness as mixed.

## Kiplinger's State Tax-Friendliness



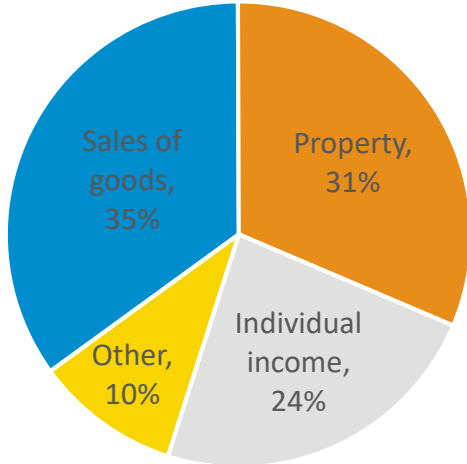
- ▶ For retirees, Virginia earns a tax-friendly rating due to several tax breaks for residents age 65 and older, including income tax deductions, property tax breaks for seniors, and a low sales tax.
- ▶ For all residents, Virginia's overall tax rating is mixed, with generally low property taxes and a low sales tax but a levy on grocery purchases.

Note: Alaska is rated as Most Tax-Friendly and Hawaii is rated as Least Tax-Friendly.

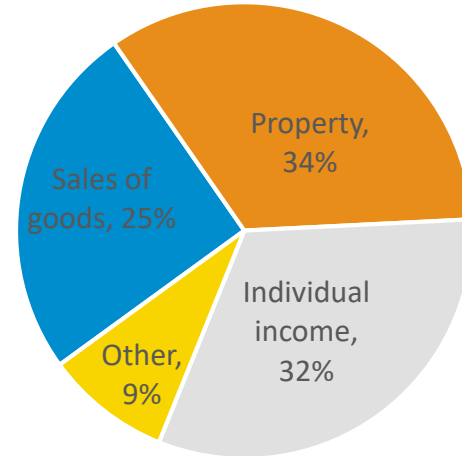
Source: Kiplinger and Microsoft Excel 3D Maps

Compared to other states, Virginia collects a higher share of revenue through individual income taxes but a lower share of revenue through sales taxes.

### What Average State Taxes



### What Virginia Taxes



Note: Sales of goods Includes both the General Sales and Selective Sales categories of the U.S. Census Bureau. Property includes whole, real and personal, and tangible or intangible. Figures include revenues collected by both state and local governments.

Source: U.S. Census Bureau, 2016 Annual Surveys of State and Local Government Finances

The states listed below have the highest numbers of retired veterans and the highest monthly payments by DOD. The following slides compare Virginia to these states.

## Rank by Retirees and Payments

Rank		State	Number Retired	Paid By DOD	Monthly Payment*	Share	
Retired	Payments					Retired	Payments
1	1	Texas	215,818	197,473	\$472,762	10%	10%
2	2	Florida	202,840	189,804	\$463,534	9%	10%
<b>3</b>	<b>3</b>	<b>Virginia</b>	<b>157,821</b>	<b>150,426</b>	<b>\$452,105</b>	<b>7%</b>	<b>10%</b>
4	4	California	154,736	141,711	\$328,349	7%	7%
5	6	Georgia	99,645	91,262	\$204,596	5%	4%
6	5	North Carolina	99,354	91,711	\$217,133	5%	5%
7	7	Washington	74,910	69,754	\$163,636	3%	4%
8	8	Alabama	61,866	57,850	\$130,667	3%	3%
9	9	South Carolina	61,196	57,257	\$126,858	3%	3%
10	10	Arizona	57,457	53,494	\$123,200	3%	3%
11	11	Tennessee	57,089	52,729	\$113,474	3%	2%
12	12	Maryland	55,680	51,724	\$132,773	3%	3%

\*Monthly payment in thousands.

Source: U.S. Department of Defense, Statistical Report on the Military Retirement System

Virginia ranks low among the states in terms of tax collections as a percentage of personal income.

## State and Local Tax Revenue as a Percentage of Personal Income

<u>State</u>	<u>State and Local Tax Revenue per Capita</u>	<u>Personal Income per Capita</u>	<u>Percent of Personal Income</u>
California	\$6,091 (8)	\$57,625 (6)	10.6% (11)
Maryland	\$6,047 (9)	\$58,934 (5)	10.3% (14)
North Carolina	\$3,919 (32)	\$42,707 (37)	9.2% (29)
Washington	\$5,041 (17)	\$55,415 (10)	9.1% (32)
Arizona	\$3,563 (44)	\$40,456 (42)	8.8% (36)
Texas	\$4,015 (29)	\$46,092 (28)	8.7% (37)
Georgia	\$3,663 (42)	\$42,657 (38)	8.6% (40)
<b>Virginia</b>	<b>\$4,562 (23)</b>	<b>\$53,345 (11)</b>	<b>8.6% (41)</b>
South Carolina	\$3,436 (48)	\$40,325 (44)	8.5% (42)
Alabama	\$3,204 (50)	\$39,260 (47)	8.2% (46)
Tennessee	\$3,324 (49)	\$43,961 (33)	7.6% (48)
Florida	\$3,483 (46)	\$46,208 (27)	7.5% (49)
<i>United States</i>	<i>\$4,951</i>	<i>\$49,883</i>	<i>9.9%</i>

Note: Rank among all states in parentheses.

Sources: U.S. Census Bureau, 2016 Annual Surveys of State and Local Government Finances and Annual Estimates of the Resident Population; and Bureau of Economic Analysis

Compared to the average state, Virginia collects more revenue per capita from the individual income tax but less revenue per capita from state and local sales taxes.

## State and Local Tax Revenue per Capita

State	Sales Tax Revenue per Capita*		Property Tax Revenue per Capita**		Individual Income Tax Revenue per Capita	
	Amount	Rank	Amount	Rank	Amount	Rank
<b>Virginia</b>	<b>\$1,156</b>	<b>(44)</b>	<b>\$1,546</b>	<b>(19)</b>	<b>\$1,455</b>	<b>(10)</b>
Alabama	\$1,572	(29)	\$548	(50)	\$743	(36)
Arizona	\$1,716	(20)	\$1,056	(34)	\$571	(40)
California	\$1,841	(15)	\$1,563	(17)	\$2,060	(5)
Florida	\$1,767	(18)	\$1,265	(29)	\$0	(44)
Georgia	\$1,284	(43)	\$1,160	(32)	\$1,013	(27)
Maryland	\$1,626	(26)	\$1,552	(18)	\$2,283	(2)
North Carolina	\$1,417	(36)	\$975	(38)	\$1,186	(15)
South Carolina	\$1,096	(45)	\$1,164	(31)	\$780	(33)
Tennessee	\$1,876	(14)	\$837	(45)	\$49	(44)
Texas	\$2,011	(8)	\$1,760	(13)	\$0	(44)
Washington	\$3,107	(2)	\$1,434	(24)	\$0	(44)
<i>United States</i>	<i>\$1,730</i>		<i>\$1,558</i>		<i>\$1,165</i>	

Note: Rank among all states in parentheses.

\*Includes both the General Sales and Selective Sales categories of the U.S. Census Bureau.

\*\*Includes whole, real and personal, and tangible or intangible property.



Sources: U.S. Census Bureau, 2016 Annual Surveys of State and Local Government Finances and Annual Estimates of the Resident Population; and Bureau of Economic Analysis



## State Tax Rates

■ Lowest tax rates   
 □ Middle-tier of tax rates   
 ■ Highest tax rates

State	Sales Tax	Real Property Tax	Individual Income Tax
	Average Combined State and Local Tax Rates <sup>1</sup>	% of Owner-occupied Housing Value <sup>2</sup>	Highest Marginal Tax Rate <sup>3</sup>
<b>Virginia</b>	<b>5.65%</b>	<b>0.84%</b>	<b>5.75%</b>
Alabama	9.14%	0.37%	5.00%
Arizona	8.37%	0.64%	4.54%
California	8.56%	0.70%	13.30%
Florida	7.05%	0.89%	No state income tax
Georgia	7.29%	0.88%	5.75%
Maryland	6.00%	1.00%	5.75%
North Carolina	6.97%	0.81%	5.25%
South Carolina	7.43%	0.52%	7.00%
Tennessee	9.47%	0.68%	No state income tax
Texas	8.19%	1.62%	No state income tax
Washington	9.17%	0.85%	No state income tax

<sup>1</sup> Figures are based on tax rates and do not consider differences in tax bases; sales tax structures vary widely among states. For example, of the 12 states, Virginia (2.5%), Alabama (included in base), and Tennessee (4.0%) levy taxes on grocery purchases.

<sup>2</sup> Rates based on 2017 data.

<sup>3</sup> North Carolina imposes a 5.25% flat tax. Tennessee currently taxes dividends and interest only (2%). The income floors for the highest marginal tax rates vary by state; for example, the income floor for the highest tax bracket is \$17,000 in Virginia and \$1 million in California. As a result, "tax friendliness" depends on an individual's income level.



Three states offer no tax exemption to retirees age 65 and older.  
 Nineteen states, including Virginia, offer a partial exemption or special provision.  
 Twenty states offer a full exemption and nine state levy no state income tax.

## States by Type of Exemption for Retirees age 65 and older

★ = Military focused    \$ = Means-tested

<u>No Exemption (3)</u>	<u>Partial Exemption or Special Provision (19)</u>			<u>Full Exemption (20)</u>			<u>No State Income Tax (9)</u>	
California	Arizona	Kentucky	Oregon	Alabama ★	Louisiana	New Jersey ★	Alaska	Tennessee*
North Dakota	Colorado	Maryland ★	Rhode Island \$	Arkansas ★	Maine	New York ★	Florida	Texas
Washington DC	Delaware	Montana \$	South Carolina ★	Connecticut ★	Massachusetts	Ohio ★	Nevada	Washington
	Georgia	Nebraska ★	Utah \$	Hawaii	Michigan ★	Pennsylvania	New Hampshire*	Wyoming
	Idaho	New Mexico \$	Vermont \$	Illinois	Minnesota ★	West Virginia ★	South Dakota	
	Indiana	North Carolina	<u>VIRGINIA</u> \$	Iowa ★	Mississippi	Wisconsin ★		
		Oklahoma ★		Kansas	Missouri			

\* New Hampshire and Tennessee tax interest and dividends but not pension income or earned income.



Nine states, including Virginia, offer no tax exemption to retirees age 64 and younger.  
 Thirteen states offer a partial exemption or special provision.  
 Twenty states offer a full exemption and nine state levy no state income tax.

## States by Type of Exemption for Retirees age 64 and younger

★ = Military focused    \$ = Means-tested

### No Exemption (9)

California  
 Idaho  
 New Mexico  
 North Dakota  
 Rhode Island  
 Utah  
 Vermont

**VIRGINIA**

Washington DC

### Partial Exemption or Special Provision (13)

Arizona  
 Colorado  
 Delaware  
 Georgia  
 Indiana  
 Kentucky  
 Maryland ★

Montana \$  
 Nebraska ★  
 North Carolina  
 Oklahoma ★  
 Oregon  
 South Carolina ★

### Full Exemption (20)

Alabama ★    Louisiana    New Jersey ★  
 Arkansas ★    Maine    New York ★  
 Connecticut ★    Massachusetts    Ohio ★  
 Hawaii    Michigan ★    Pennsylvania  
 Illinois    Minnesota ★    West Virginia ★  
 Iowa ★    Mississippi    Wisconsin ★  
 Kansas    Missouri

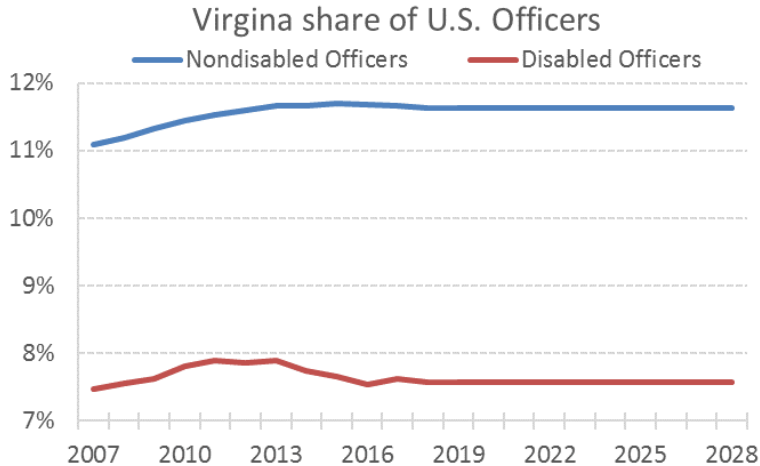
### No State Income Tax (9)

Alaska    Tennessee\*  
 Florida    Texas  
 Nevada    Washington  
 New Hampshire\*    Wyoming  
 South Dakota

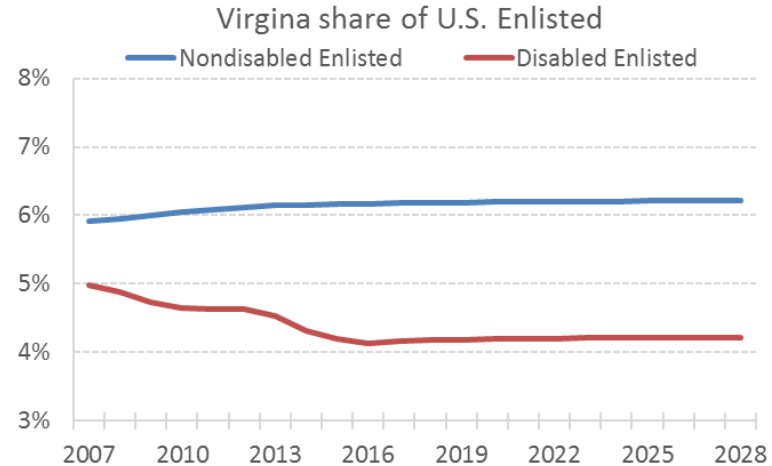
\* New Hampshire and Tennessee tax interest and dividends but not pension income or earned income.

## Virginia share of US:

- ▶ Officers remains constant.
  - ▶ Both nondisabled and disabled officers.



- ▶ Enlisted continues to grow slightly.
  - ▶ Both nondisabled and disabled enlisted.



Below are five options estimated by TAX from among a range of policy options that are available in other states or that have been brought up to DVS by retirees:

- ▶ A full military retirement income tax exemption in Virginia = -\$295 million revenue loss by 2027
- ▶ Other policy options include:
  - ▶ Refundable tax credit of \$5,000 = -\$783 million loss by 2027
  - ▶ Fixed subtraction of \$40,000 = -\$247 million
  - ▶ Full exemption for retirees age 65 and older only = -\$112 million
  - ▶ Phased-in fixed subtraction rising from \$10,000 to \$40,000 over four years for retirees age 65 and older only = - \$97 million

Other options range in cost from one-third or less to more than full-exemption cost

## Comparison of Policy Options for Exempting Military Retirement Pay

### Cost of other policy options as share of baseline full exemption

Virginia FY	Baseline Full Exemption Cost (\$M)*	Number of Retirees	Refundable tax credit <sup>1</sup>	Fixed subtraction <sup>2</sup>	Exemption for Age 65+ only <sup>3</sup>	Phased-in Fixed subtraction for Age 65+ only <sup>4</sup>
2020	-\$112.6	152,005	338%	85%	33%	15%
2021	-\$229.7	152,682	332%	85%	33%	21%
2022	-\$239.2	153,290	320%	85%	34%	28%
2023	-\$249.4	153,909	309%	85%	35%	30%
2024	-\$260.4	156,010	298%	84%	36%	32%
2025	-\$272.0	156,330	287%	84%	36%	32%
2026	-\$283.6	156,540	276%	84%	37%	32%
2027	-\$295.2	156,642	265%	84%	38%	33%

\* Assumes 1/1/2020 effective date and no adjustment for timing of passage; For a normal revenue impact, FY 2020 impact would be shifted to FY 2021

<sup>1</sup> Tax credit of \$5,000

<sup>2</sup> Fixed subtraction of \$40,000

<sup>3</sup> Full exemption only if age 65 & older; no exemption for younger age groups

<sup>4</sup> Fixed subtraction rising from \$10,000 to \$40,000 over four years for age 65 and older

Sources: U.S. Department of Defense, Statistical Report on the Military Retirement System, and Valuation of the Military Retirement System  
 US Department of Veterans Affairs, National Center for Veterans Analysis and Statistics (NCVAS),  
 Virginia Department of Taxation, Policy Development Division

Like full-exemption, most other options eclipse or approach \$200 million annual cost

## Comparison of Policy Options for Exempting Military Retirement Pay

Virginia FY	Cost of other policy options					
	Baseline Full Exemption Cost (\$M)*	Number of Retirees	Refundable tax credit <sup>1</sup>	Fixed subtraction <sup>2</sup>	Exemption for Age 65+ only <sup>3</sup>	Phased-in Fixed subtraction for Age 65+ only <sup>4</sup>
2020	-\$112.6	152,005	-\$380	-\$96	-\$37	-\$17
2021	-\$229.7	152,682	-\$763	-\$195	-\$77	-\$48
2022	-\$239.2	153,290	-\$766	-\$203	-\$82	-\$67
2023	-\$249.4	153,909	-\$770	-\$211	-\$88	-\$76
2024	-\$260.4	156,010	-\$776	-\$220	-\$93	-\$82
2025	-\$272.0	156,330	-\$781	-\$229	-\$99	-\$87
2026	-\$283.6	156,540	-\$782	-\$238	-\$106	-\$92
2027	-\$295.2	156,642	-\$783	-\$247	-\$112	-\$97

\* Assumes 1/1/2020 effective date and no adjustment for timing of passage; For a normal revenue impact, FY 2020 impact would be shifted to FY 2021

<sup>1</sup> Tax credit of \$5,000

<sup>2</sup> Fixed subtraction of \$40,000

<sup>3</sup> Full exemption only if age 65 & older; no exemption for younger age groups

<sup>4</sup> Fixed subtraction rising from \$10,000 to \$40,000 over four years for age 65 and older

Sources: U.S. Department of Defense, Statistical Report on the Military Retirement System, and Valuation of the Military Retirement System  
 US Department of Veterans Affairs, National Center for Veterans Analysis and Statistics (NCVAS),  
 Virginia Department of Taxation, Policy Development Division

Including impact of adjusting for time of passage

**Cost to Exempt Military Retirement Pay from Virginia Individual Income Tax\***

Year	Tax Year		Virginia FY	Fiscal Year		Revenue impact adjusting for time of passage***	
	Full Exemption Impact (\$M)	Phased-in Fixed Subtraction for Age 65+ impact (\$M)**		Full Exemption Impact (\$M)	Phased-in Fixed Subtraction for Age 65+ impact (\$M)**	Full Exemption Impact (\$M)	Phased-in Fixed Subtraction for Age 65+ impact (\$M)**
2020	-\$225	-\$33	2020	-\$113	-\$17		
2021	-\$234	-\$63	2021	-\$230	-\$48	-\$342	-\$65
2022	-\$244	-\$72	2022	-\$239	-\$67	-\$239	-\$67
2023	-\$255	-\$80	2023	-\$249	-\$76	-\$249	-\$76
2024	-\$266	-\$84	2024	-\$260	-\$82	-\$260	-\$82
2025	-\$278	-\$89	2025	-\$272	-\$87	-\$272	-\$87
2026	-\$289	-\$94	2026	-\$284	-\$92	-\$284	-\$92
2027	-\$301	-\$100	2027	-\$295	-\$97	-\$295	-\$97

\*Effective for TY beginning 1-1-2020

\*\* Fixed subtraction rising from \$10,000 to \$40,000 over four years for age 65 and older

\*\*\* Assumes passage in 2020 GA session with FY 2020 impact reflected in FY 2021 budget

Sources: U.S. Department of Defense, Statistical Report on the Military Retirement System, and Valuation of the Military Retirement System  
 US Department of Veterans Affairs, National Center for Veterans Analysis and Statistics (NCVAS),  
 Virginia Department of Taxation, Policy Development Division



## Key sources

- ▶ **History of US & Virginia retirees & pay:** U.S. Department of Defense (DOD), 2018 Statistical Report on the Military Retirement System
- ▶ **Forecast of US retirees & pay:** DOD, 2018 Valuation of the Military Retirement System
- ▶ **History of US retirees by age:** DOD 2018 Statistical Report on the Military Retirement System
- ▶ **History & forecast of US & Virginia veterans:** US Department of Veterans Affairs (VA), National Center for Veterans Analysis and Statistics (NCVAS)

## Key data points

	Virginia Retirees*	Avg. annual pay	Total pay (\$B)
2018	150,426	\$36,066	\$5.4 billion
2028F	156,550	\$47,685	\$7.4 billion
CAGR**	0.4%	2.8%	3.2%

### Age <65

2018	90,463	\$34,607	\$3.1 billion
2028F	86,645	\$45,756	\$3.9 billion
CAGR**	-0.4%	2.8%	2.4%

### Age 65 & older

2018	59,963	\$38,267	\$2.3 billion
2028F	69,905	\$50,595	\$3.5 billion
CAGR**	1.5%	2.8%	4.4%

\* Excludes Coast Guard retirees; includes disabled retirees; FFY

\*\* Compound Annual Growth Rate

- ▶ **Group-specific:** Each part of an estimate is based on taxable income calculations appropriate to the specific group (i.e., primarily related to age (<65 vs 65+) and income)
- ▶ **Taxable income:** Takes into account estimated asset income, age deduction, personal exemption, age exemption and standard deduction to derive a Taxable Percentage.
- ▶ **Taxable Benefits:** Derived by applying Taxable Percentage to retirement benefits.
- ▶ **Revenue Loss:** Derived by applying Virginia tax rate to Taxable Benefits.
- ▶ **Revenue Loss by policy option:** Generally, the approach is to calculate the revenue preserved by the policy—then add that to the baseline full exemption cost to derive the net revenue loss with the policy.



- ▶ **Expanding to five age brackets:** While the baseline estimate is based on two age splits (under age 65 vs. 65 and older), the age-based policy estimate requires further splitting the age breaks to five: (<45, 45-54, 55-64) and (65-74, 75 and older)
- ▶ **Further splits based on two sources:**
  - ▶ Historical US-level data on age splits of *retirees* from the DOD statistical report
  - ▶ Forecast of Virginia-level data on age splits of *veterans* from US Department of Veterans Affairs, National Center for Veterans Analysis and Statistics (NCVAS)
- ▶ **Retirement pay by age group.** Estimated relative to known pay for Under 65/65 and older by using data from the 2017 American Community Survey, PUMS microdata for Virginia (i.e., Index ratio from ACS data applied to DOD payment data)

- ▶ **US-level forecast:** Forecast of total US retirees and pay by officer or enlisted; nondisabled or disabled is pre-determined by DOD valuation report.
- ▶ **Virginia-level forecast:** Virginia retirees and pay by officer or enlisted; and disabled or nondisabled are forecast relative to US-level data (as a share or ratio).
  - ▶ **Virginia retirees:** Forecast as a share of US retirees by officers, enlisted, disabled officers, and disabled enlisted. Forecast makes assumptions about trends going forward.
  - ▶ **Virginia retiree split at age 65:** Forecast relative to distribution of Virginia *veterans* under age 65/65 & older (Historical *retiree* split based on actual data from DOD statistical report).
  - ▶ **Virginia retirement pay:** Forecast for all Virginia retirees aggregated from indices for groups (officers, enlisted, disabled officers, and disabled enlisted) relative to US-level groups. Policy estimates, however, assume pay for groups grows at same aggregate rate to simplify methodology.

## HJ674 Study

### Case Study:

# Costs for Military Retirees to Reside in Four Different States

Bryan Harrison,  
DVS Summer Policy Analyst  
William & Mary School of Public Policy



- *Current DOD actuarial data, as well as circumstantial observations of DVS staff in our service lines assisting veterans and retirees with transition, employment, VA benefits and more, show that retirees are staying in Virginia. The hypothesis is that this is for economic, education and other opportunities that outweigh any lower cost of living and tax advantages promised by other states.*
- **Study Parameters: Research two typical Virginia separating service members about to retire. What are the annual costs associated with moving to each state? What are the tax advantages?**
  - A retired officer with 40 years of service and \$189,000 annual retirement pay
  - A retired enlistee with 24 years of service and \$47,200 annual retirement pay
- **Scenario for each retiree:**
  - Similar job offers for \$100,000 annual salary in Alexandria, VA; Houston, TX; Jacksonville, FL; and Raleigh-Durham, NC
  - Retiree has a spouse and at least one child in or about to begin college, and will purchase a house, and a new car.

➤ *For the raw data behind this case study please see corresponding Appendix A: Case Study Excel Spreadsheet*

Although real property taxes and fees on comparable homes are generally higher in Virginia, taxes and fees paid as a percentage of home value are lowest in Virginia.

### Retired Officer – More Expensive Home Purchase and 90% Disability Rating

<u>City</u>	<u>Value</u>	<u>Property Taxes and Fees</u>	<u>Percentage of Home Value</u>
Alexandria, VA	\$1,000,000	\$11,907	1.19%
Houston, TX <sup>1</sup>	\$625,000	\$11,659	1.87%
Jacksonville, FL	\$450,000	\$7,488	1.66%
Raleigh, NC	\$500,000	\$6,048	1.21%

### Retired Enlistee – More Expensive Home Purchase and 90% Disability Rating

<u>City</u>	<u>Value</u>	<u>Property Taxes and Fees</u>	<u>Percentage of Home Value</u>
Alexandria, VA	\$625,000	\$7,576	1.21%
Houston, TX <sup>2</sup>	\$300,000	\$7,156	2.39%
Jacksonville, FL	\$300,000	\$4,785	1.59%
Raleigh, NC	\$325,000	\$4,020	1.24%

### Retired Officer – Less Expensive Home Purchase and 50% Disability Rating

<u>City</u>	<u>Value</u>	<u>Property Taxes and Fees</u>	<u>Percentage of Home Value</u>
Alexandria, VA	\$625,000	\$7,576	1.21%
Houston, TX <sup>2</sup>	\$300,000	\$7,156	2.39%
Jacksonville, FL	\$300,000	\$4,785	1.59%
Raleigh, NC	\$325,000	\$4,020	1.24%

### Retired Enlistee – Less Expensive Home Purchase and 50% Disability Rating

<u>City</u>	<u>Value</u>	<u>Property Taxes and Fees</u>	<u>Percentage of Home Value</u>
Alexandria, VA	\$500,000	\$6,163	1.23%
Houston, TX <sup>3</sup>	\$250,000	\$5,528	2.21%
Jacksonville, FL	\$250,000	\$3,884	1.55%
Raleigh, NC	\$275,000	\$3,440	1.25%

Note: All numbers are rounded to the nearest dollar value.

See appendix for methodology and sources..

<sup>1</sup> Estimates based on residence in Bellaire; <sup>2</sup> Estimates based on residence in Nassau Bay; <sup>3</sup> Estimates based on residence in Pasadena

Sales tax payments are significantly lower in Virginia. Initial vehicle taxes and fees are lower in Houston and Raleigh.

**Sales Taxes: Retired Officer (\$289,000 income)**

<u>City</u>	<u>General Sales</u>	<u>Groceries</u>	<u>Meals</u>	<u>Total</u>
Alexandria, VA	\$3,412	\$191	\$434	\$4,037
Houston, TX	\$8,940	Exempt	\$0	\$8,940
Jacksonville, FL	\$7,450	Exempt	\$0	\$7,450
Raleigh, NC	\$6,653	Exempt	\$87	\$6,740

**Sales Taxes: Retired Enlistee (\$147,000 income)**

<u>City</u>	<u>General Sales</u>	<u>Groceries</u>	<u>Meals</u>	<u>Total</u>
Alexandria, VA	\$1,734	\$150	\$246	\$2,130
Houston, TX	\$4,544	Exempt	\$0	\$4,544
Jacksonville, FL	\$3,787	Exempt	\$0	\$3,787
Raleigh, NC	\$3,382	Exempt	\$49	\$3,431

Note: All numbers are rounded to the nearest dollar value.  
See appendix for methodology and sources.

Since Virginia collects a larger portion revenue from the individual income tax than many states, it requires the highest income tax payment.

### Income Taxes – Retired Officer

<u>City</u>	<u>Income Taxes Paid*</u>
Alexandria, VA	\$16,395
Houston, TX	\$0
Jacksonville, FL	\$0
Raleigh, NC	\$5,250

### Income Taxes – Retired Enlistee

<u>City</u>	<u>Income Taxes Paid*</u>
Alexandria, VA	\$8,207
Houston, TX	\$0
Jacksonville, FL	\$0
Raleigh, NC	\$7,518

In North Carolina, the retired officer qualifies for a full military retirement pay tax exemption, resulting in a lower income tax paid than the retired enlistee (who qualifies for a \$4,000 exemption).

\*Assumes all income is taxable (no deductions or non-veteran exemptions).

Note: All numbers are rounded to the nearest dollar value.

If the retired officer or enlistee has a 90% disability rating or higher, the retiree's child qualifies for a tuition and fee waiver in Virginia. In Virginia, personal property tax exemptions (partial or full) are not statewide, but dependent on the locality.

### Average College Tuition and Fees at Public Four-Year Institutions (2018-19)

<u>City</u>	<u>90% Disability Rating</u>	<u>50% Disability Rating</u>
Alexandria, VA	\$0	\$13,490
Houston, TX	\$10,300	\$10,300
Jacksonville, FL	\$6,360	\$6,360
Raleigh, NC	\$7,220	\$7,220

### Vehicle Purchase – 2019 Toyota Camry (\$24,095 MSRP)

<u>City</u>	<u>Sales Tax</u>	<u>Property Tax</u>	<u>Registration, Title, and License Plates</u>	<u>Fuel Tax</u>	<u>Total</u>
Alexandria, VA	\$1,000	\$831	\$66	\$101	\$1,998
Houston, TX	\$1,506	\$0	\$113	\$83	\$1,702
Jacksonville, FL	\$1,687	\$0	\$353	\$130	\$2,169
Raleigh, NC	\$723	\$279	\$138	\$150	\$1,291



## Methodology: Real Property Taxes and Fees

- **Home Value**
  - Assumes that purchase price and home value are equal.
  - Prices are based on data from Zillow and the National Association of Realtors, using comparable homes with approximately 2,500 square feet, four bedrooms, and three bathrooms.
- **Property Taxes and Fees**
  - The real property tax rate for Alexandria is \$1.13 per \$100.
  - The real property tax rates for Houston vary by municipality. A 90% disabled veteran receives a \$12,000 exemption and a 50% disabled veteran receives a \$10,000 exemption. Residents also receive exemptions for county taxes, school district taxes, and city taxes, which vary by municipality.
  - The real property tax rate for Jacksonville is about \$1.80 per \$100. A 90% and 50% disabled veteran receive a \$5,000 exemption. Residents also receive a homestead exemption of \$50,000, including a \$25,000 exemption on non-school district taxes.
  - The real property tax rate for Raleigh is about \$1.16 per \$100.
  - Fees include storm water, refuse/waste disposal, and recycling.

## **Methodology: Real Property Taxes and Fees**

- **Sources:** Zillow, National Association of Realtors, City of Alexandria, Harris County Tax Assessor-Collector and Voter Registrar, Duval County Property Appraiser, Wake County Tax Administration, TexVet, Florida Department of Revenue, City of Houston, Bellaire Texas Code of Ordinances, City of Nassau Bay, Pasadena Texas Code of Ordinances, City of Jacksonville and Duval County, and City of Raleigh
- Figures are based on the most recent county/city data provided as of July 2019.

## Methodology: Sales Taxes

- **General Sales:** Each state's general sales taxes paid (from U.S. Census Bureau, 2016 Annual Surveys of State and Local Government Finances) as a percentage of per capita personal income (based on figures from U.S. Census Bureau, 2016 Annual Surveys of State and Local Government Finances and the Bureau of Economic Analysis) is applied to the retiree's total retirement income and salary (assumes all income comes from these two sources). Estimates are based on median values; most individuals with higher incomes pay a smaller percentage of income in sales taxes than those with lower incomes.
- **Groceries and Meals Taxes:** Groceries and meals expenditures privy to taxes are based on food at home and food away from home figures from the Consumer Expenditure Survey, U.S. Bureau of Labor Statistics, September 2018. Virginia imposes a 2.5% groceries tax; Alexandria (5%) and Raleigh (1%) levy meals taxes. Other sources: Tax Foundation, City of Alexandria, and Wake County Tax Administration

## Methodology: Vehicle Taxes and Fees

- Vehicle taxes are \$5.33 per \$100 in Alexandria. Cars valued between \$20,001 and \$25,000 received maximum tax relief of \$453.05. Vehicle taxes are about \$1.16 per \$100 in Raleigh. Additional tax and fee information was collected from the following sources: Virginia, Texas, and North Carolina Departments of Motor Vehicles; Florida Department of Highway Safety and Motor Vehicles; City of Alexandria; Harris County Tax Office; Texas Comptroller of Public Accounts; Florida and North Carolina Departments of Revenue; Wake County Tax Administration; and Tax Foundation.
- Fuel tax payments are based on estimated miles driven per year and state/local gasoline tax rates. Miles driven are estimated using average annual miles per driver by age group figures from the U.S. Department of Transportation, Federal Highway Administration. This figure is applied to the state/local gasoline tax rate. Virginia charges a \$0.162 mile per gallon fuel excise tax as well as a \$0.006 per gallon petroleum tank storage fee and a wholesale tax in Northern Virginia of \$0.076 per gallon, which are assumed to be passed along to consumers. Texas charges a state excise tax of \$0.20 per gallon. Florida charges a \$0.04 per gallon excise tax and a total imposed tax of \$0.31425 per gallon in Duval County. North Carolina charges a \$0.362 per gallon excise tax and a \$0.0025 per gallon inspection tax for a total tax of \$0.3645 per gallon. Sources: America Petroleum Institute State Motor Fuel Taxes, Virginia Department of Motor Vehicles, Texas Comptroller of Public Accounts, Florida Department of Revenue, and North Carolina Department of Revenue



