

BILL # SB 1010

TITLE: national guard compensation; tax subtraction

SPONSOR: Waring

STATUS: Senate Engrossed

PREPARED BY: Jeremy Olsen

FISCAL ANALYSIS

Description

This bill allows taxpayers to subtract up to \$5,000 from their taxable income for any compensation, bonus, and allowance received during the year for service in the military. This bill becomes effective for taxable years after December 31, 2006.

Estimated Impact

Beginning in FY 2008, this bill would result in a maximum loss of \$(5.1) million in General Fund revenue annually. If the Legislature extends the current one-year income tax subtraction for all active duty military compensation, the incremental impact of this particular bill would be no greater than \$(1.9) million.

Analysis

The cost of this bill cannot be exactly determined due to a lack of data on the adjusted gross income for eligible taxpayers and the unknown number of taxpayers who would be eligible for the income tax credit. However, a potential outcome of the bill was estimated using a set of simplifying assumptions.

Based on a report published by The Maguire Company and the ESI Corporation, and information provided by the Arizona National Guard, an estimated 21,400 Arizona residents serve full time in the military, 5,400 serve as reservists, and 7,200 are enlisted in the National Guard, totaling 34,000 Arizonans in military service. If all servicemen and women are considered eligible for the full \$5,000 subtraction from taxable income, then the total annual income subtraction for all military taxpayers would be \$170 million. Assuming an average marginal tax rate of 3%, this bill would reduce their total tax liability by \$(5.1) million. The marginal rate of 3% reflects incomes between \$30,000 and \$40,000.

The Department of Emergency and Military Affairs reports that soldiers enlisted for active duty often claim residency in states with no state income taxes for tax purposes. In addition, the department reports that reservists can be assigned to units outside of their home state, meaning they would be ineligible for the credit. It is, therefore, likely that the actual reduction to income tax revenues will be less than the \$(5.1) million estimate.

Laws 2005, Chapter 303 allowed individuals to subtract all compensation received for active duty service as a member of the armed forces only for the taxable year ending December 31, 2006. The above estimate assumes that this provision will not be extended to FY 2007.

Both HB 2795 and SB 1033 would make the reduction enacted in Chapter 303 permanent. If either of those bills is enacted, then the incremental impact of SB 1010 would be applicable only to reservists and members of the National Guard. If the 21,400 active duty soldiers were removed from the above estimate and no reservists or national guardsmen were called up to active duty during the course of the year, then a total of 12,600 would be eligible for the tax credit. The total annual income subtraction for reservists would be \$63 million, which would reduce their tax liability by \$(1.9) million.

Local Government Impact

The Urban Revenue Sharing formula distributes 15% of income taxes collected 2 years prior to incorporated cities and towns. The bill, therefore, could reduce these distributions by up to \$(765,000) on an annual basis.