

Current Military Pension State Tax Status



To be directed to benefits website click on map in presentation view

*State taxes as of 13 Jan 21. Conditions or limitations apply. Check state law. See the MyArmyBenefits state fact sheets at https://myarmybenefits.us.army.mil/Home/Benefit_Library/State_Territory_Benefits.html for details.

Why Military Pension Tax Exemption First

Potential Benefits

- **Military Retiree Profile**
 - The estimated 14,000 service members retiring from North Carolina's military population of well over 100,000 active service members, and making the choice to stay in North Carolina can expect to pay state taxes on their military retirement income. This taxation impacts the most recent group of retiring Servicemembers who very likely served in combat at least once, if not multiple times, since 1990
 - On average military retirees are under 50 years of age³ with over 20 years of work history and a desire to start a second career
 - Most retired military personnel are homeowners, pay property and sales taxes, but generally have relatively low demand on local government services due to few if any school-age children in the households
- **State Tax Impact – a possible increase of \$35M/year after 5-10 Years**
 - Increased **taxable income** of \$50,000 per household for each new retiree, totaling \$250 million per year in five years—in addition to the proposed exempt retirement income flowing into the state of \$30,000 per household, or **\$150 million** per year in five years
 - Increased **defense contractor activity**, associated with prospective strategies to leverage the more attractive environment for military retirees to increase North Carolina's disproportionately low share of defense contracts from 1% of the total to 2%--potentially bringing in **\$2 billion** in additional corporate revenue to the state, \$200 million in taxable profits, and \$400 million in salaries of new employees
 - An additional **\$225 million** per year in **new business revenue** associated with the 10 percent of the new retirees forecast to come to the state over a five year period who start their own businesses
 - Indirect **revenue flows of \$1 billion** or more as the incomes associated with the growth in retirees and associated businesses circulate throughout the state's economy.
 - Supports the **North Carolina Military Affairs Commission - (NCMAC) 2020 Strategic Plan – Resolution signed on the 16th of February.**

References

- <https://myarmybenefits.us.army.mil/Benefit-Library/State/Territory-Benefits>
- <https://www.militaryonesource.mil/>
- McElveen, Gregory. Costs and Benefits of Proposed Military Retirement Pay Exemptions in the State of North Carolina. *Preliminary Working Draft*, April 1st 2020. Fayetteville State University
- Coleman, Larry. State Income Tax Exemption for Military Pensions: A Win for Veterans and for North Carolina. January 3rd 2020
- [2020 Strategic Plan, North Carolina Military Affairs Commission, 2020](#)

Preliminary Working Draft—April 1, 2020

COSTS AND BENEFITS OF PROPOSED MILITARY RETIREMENT PAY EXEMPTIONS IN THE STATE

OF NORTH CAROLINA

Gregory McElveen
Fayetteville State University

INTRODUCTION

The purpose of this paper is to assess the costs and benefits of proposals to exempt all military retirement pay from North Carolina income tax. Such proposals are of particular interest to the economically distressed, Tier 1 counties in which the largest military installations in the state are located. For Cumberland County, the location of Fort Bragg; Onslow County, the location of Camp Lejeune; and Wayne County, the location of Camp Lejeune, the potential incremental economic benefits of adding thousands of skilled, mature, working-age adults and their spouses, supported by full military retirement benefits could be significant. In addition to being a catalyst for new income streams for the state, retired military personnel tend to be net contributors to local government tax resources. Most retired military personnel are homeowners, pay property and sales taxes, but generally have relatively low demand on local government services due to few if any school-age children in the households. This paper will estimate the extent to which exemption of military retirement pay from state income taxes is likely to result in increases in the number of military members choosing to retire in North Carolina, and the extent to which the lost tax revenue is likely to be offset by increased tax collections from other sources.

BACKGROUND

Currently the first 54,000 of all federal, state, and local retirement pay can be exempted from North Carolina state income tax. Beyond that, retirement pay associated with government employment is exempted only for those who had at least 5 years of service as of 1989 (the year in which legislative changes were made in retirement pay treatment).

Prior to 1989 the state of North Carolina exempted retirement pay of local and state government employees from state income taxes, but did not similarly exempt the retirement pay of federal employees residing in the state. In 1989 a U.S. Supreme Court decision held that a 1931 law precluded states from enacting income tax policies which discriminated against federal employees relative to the tax treatment of state employees. The Supreme Court decision required that if state and local employees were given a tax exemption, federal employees had to be given the same exemption. At that point, the North Carolina state legislature decided that it would not be affordable to extend the retirement exemption to federal employees residing in the state, so instead the retirement exemption was rescinded for state and local employees. After a former state employee—Judge Bailey—sued the state for breach of contract for talking away previously agreed upon retirement benefits, the state agreed to a settlement by which all government employees (federal, state, and local) who were considered vested in their retirement plans as of 1989 (defined as having at least 5 years of service as of 1989), would be exempted from state taxation of government retirement benefits. All other government employees vesting after 1989 could only exempt the first 54,000 of their retirement pay.

State Income Tax Exemption for Military Pensions: A Win for Veterans and for North Carolina

By Larry Coleman

North Dakota and Indiana recently became the 30th and 31st states to fully exempt military retirement pay from state income tax. North Carolina is not included in the 31 states that offer military retirees a full exemption on state income taxes. The North Carolina Legislature has a great opportunity to acknowledge those who have protected our state and nation, while significantly contributing to the state's overall economy, by joining other states in passing legislation that would provide income tax relief for the retirement pay of the Servicemembers of the Armed Forces of the United States.

Currently in North Carolina, only those military members who have five or more years of creditable service as of August 12, 1989, have their military retirement pay exempted from state income tax. More than likely those Servicemembers retiring from North Carolina's military population of well over 120,000 and making the choice to stay in North Carolina can expect to pay state taxes on their military retirement income. This taxation impacts the most recent group of retiring Servicemembers who very likely served in combat at least once, if not multiple times, since 1990. Taxation of their retirement income can be a serious consideration in deciding in which state to retire.

On average military retirees are under 50 years of age, with over 20 years of work history and a desire to start a second career. This type of employee profile is exactly what is needed to fill civilian or contractor positions within North Carolina's military and defense sector. Currently, the military and defense sector makes up about 10% of all the state's employment, and federal military expenditures contribute over \$11 billion to the state's economy each year, ranking 4th in the United States. Since military retirees have a choice about where they retire and draw their military pensions, as the number of states that exempt military retirement pay from state income taxes increase, North Carolina will be at a clear disadvantage in retaining potential talent that significantly contributes to the overall economy of the state.

While no current study is available for North Carolina, a recent study by Clemson University in South Carolina models the benefits of an increase in military retiree migration as a result of state tax exemption for military retirement pay. The model looks at an increase of military retiree migration to the state of 1%, 2.5%, or 5%. Even with only a 2.5% increase in military retirees and despite the loss of income tax revenue, the study predicts a net

¹ <http://www.militaryonesource.mil/10306.html>
² <https://www.militaryonesource.mil/10306.html>
³ <https://www.militaryonesource.mil/10306.html>
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⁸ <https://www.militaryonesource.mil/10306.html>
⁹ <https://www.militaryonesource.mil/10306.html>
¹⁰ <https://www.militaryonesource.mil/10306.html>



NORTH CAROLINA MILITARY AFFAIRS COMMISSION

A RESOLUTION IN SUPPORT OF LEGISLATION TO EXEMPT MILITARY RETIREMENT PAY FROM STATE TAXATION

WHEREAS, the purpose of the North Carolina Military Affairs Commission is to provide advice, counsel and recommendations to the Governor, the North Carolina General Assembly, the Secretary of the Department of Military and Veterans Affairs, the Secretary of Commerce and the State agencies on initiatives, programs and legislation that will continue and increase the role that North Carolina's military installations, the National Guard and Reserves play in America's defense strategy and the economic health and vitality of the State.

WHEREAS, military retirees bring skills, work ethic and professional self-discipline that is valued by employers nationwide.

WHEREAS, military retirees often continue to work after retirement in a second career, sometimes starting companies and employing others.

WHEREAS, most military retirees generate more income in their second career than they make in their retirement pay.

WHEREAS, military retirees bring their family members with them to their new home, many of whom earn their own income, spend money at local businesses, and otherwise contribute to the local economy far beyond just what the retiree contributes.

WHEREAS, the State needs to retain and attract military retirees for the benefit of the retirees, the citizens, and the economy of North Carolina.

WHEREAS, many states have exempted military retirement pay from taxation and have gained significant benefits to their economies and workforces as a result.

NOW, THEREFORE, BE IT RESOLVED that the North Carolina Military Affairs Commission does hereby recommend to the North Carolina General Assembly that it enact legislation exempting military retirement pay from taxation.

ADOPTED, this 16th day of February 2021

NORTH CAROLINA MILITARY AFFAIRS COMMISSION
BY: 
Greg Martin
Chairman