

701—302.80(422) Exemption for military retirement pay. Retirement pay received by taxpayers from the federal government for military service performed in the armed forces, armed forces reserves, or national guard is exempt from state income tax. In addition, amounts received by a surviving spouse, former spouse, or other beneficiary of a taxpayer who served in the armed forces, armed forces reserves, or national guard under the Survivor Benefit Plan are also exempt from state income tax. The retirement pay is only deductible to the extent it is included in the taxpayer's federal taxable income.

302.80(1) Coordination with pension exclusion. The exclusion of retirement pay is in addition to the exclusion, provided in rule 701—302.47(422), of pensions and other retirement benefits for disabled individuals, individuals who are 55 years of age or older, surviving spouses and survivors. In addition, taxpayers who do not qualify for the exclusion in rule 701—302.47(422) and who receive retirement pay under federal law that combines retirement pay for both uniformed service and the federal civil service retirement system or federal employees' retirement system must prorate the retirement pay based on years of service.

EXAMPLE: A single taxpayer who is not disabled and is 50 years of age receives \$60,000 as a federal pension during the tax year. The taxpayer has 20 years of military service and 10 years of civilian employment with the federal government. The military retirement pay portion is \$40,000 (20 years, divided by 30 years, multiplied by \$60,000). The taxpayer can exclude \$40,000 of military retirement pay. The taxpayer may not exclude the \$20,000 of civilian retirement pay since it does not qualify for the exclusion in rule 701—302.47(422) because the taxpayer is under 55 years of age and is not disabled.

302.80(2) Coordination with filing threshold and alternate tax. The military retirement pay is excluded from the calculation of income used to determine whether an Iowa income tax return is required to be filed pursuant to 701—subrules 301.1(1) and 301.5(10) through 301.5(13). In addition, the military retirement pay is excluded from the calculation of the special tax computation for all low-income taxpayers except single taxpayers pursuant to rule 701—301.9(422) and is excluded from the calculation of the special tax computation for taxpayers who are 65 years of age or older under rule 701—301.15(422).

302.80(3) Iowa withholding. The amount of military retirement pay is excluded from the calculation of payments used to determine whether Iowa tax should be withheld from pension and annuity payments as determined pursuant to 701—subrule 307.3(4).

This rule is intended to implement Iowa Code sections 422.5 and 422.7.

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