



## TAXATION OF MILITARY INCOME

*By Kate Watkins and Louis Pino*

This issue brief provides an overview of filing considerations for military service persons and tax breaks for military income.

### Colorado Income Tax Military Filing

Active duty service members file their tax returns in their state of legal residence, or domicile. Service persons who are Colorado residents are required to pay Colorado taxes, but may qualify to file as a nonresident or to postpone filing, depending on where they are stationed.

**Nonresident status.** A service member who is a full-year Colorado resident and spends at least 305 days of the tax year stationed outside of the United States for active military duty may file as a nonresident of Colorado.<sup>1</sup> Nonresident service persons are not required to report or pay state income taxes on their military income, but are required to pay taxes on any nonmilitary income that is earned in Colorado or from a Colorado business.

A service member's spouse may file as a nonresident if he or she accompanies the service member outside of the country for at least 305 days of the tax year. As a nonresident, the spouse would still be required to pay taxes on income earned in Colorado or from a Colorado business. Qualifying service persons and/or their spouse may indicate a

nonresident election on state tax form 104PN when filing a tax return.

**Combat zones.** Service persons stationed in a combat zone may postpone filing and paying state income taxes, without interest or penalty, until 180 days after their assignment in the combat zone ends.<sup>2</sup> If a tax refund is expected, service persons may prefer to authorize a designated power of attorney to file their income tax returns using form DR 0145. If a tax return is filed within the 180-day extension, service persons are advised to write the name of the applicable combat zone across the top of the income tax return.

### Tax Breaks for Military Income

Colorado's income tax is based on federal taxable income. As such, any federal income tax exemptions or deductions claimed by a taxpayer, such as active duty pay earned in a combat zone, reduces federal taxable income and carries through to Colorado state taxable income ([Colorado Income Tax Issue Brief](#)).

Colorado also allows several state income tax modifications to qualifying active duty or retired military personnel that may reduce the amount of Colorado state income taxes owed. Each is described below.

**Reacquisition of residency deduction.** Beginning in tax year 2016, qualifying active

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<sup>1</sup>Section 39-22-103 (8), C.R.S.

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<sup>2</sup>Section 39-22-610, C.R.S.

duty military members who reacquire residency in Colorado are not required to pay taxes on their active duty military income. To qualify, Colorado must be the active duty military member's home of record and the member must change his or her state of legal residence to Colorado on or after January 1, 2016. The active duty member may change his or her legal state of residence from Colorado, to another state, and back to Colorado anytime on or after January 1, 2016, to qualify.

A service person's *home of record* is the state in which the service member resided at the time he or she first joined the military. The home of record generally never changes unless it was erroneously or fraudulently recorded initially. A service person's home of record may or may not be the same as his or her legal state of residence.

Under federal law, service persons may not change their state of legal residence for tax purposes alone, and must actually reside in the state and be able to provide evidence of intent to make the state his or her permanent home.

Evidence of intent to make Colorado one's legal state of residence for purposes of claiming the deduction includes the following actions made in Colorado:

- registering to vote;
- purchasing residential property or an unimproved residential lot;
- titling and registering automobile(s);
- notifying the state of previous legal residence of the change in residency; or
- preparing a new last will and testament, that indicates Colorado as the state of legal residence.

Qualifying service persons may either deduct compensation received from their taxable income or may elect not to withhold taxes on the wages earned from active duty. If the service person's only source of income is military income, he or she is not required to file a Colorado income tax return.<sup>3</sup>

<sup>3</sup>Section 39-22-110.5, C.R.S.

**Retirement income deduction.** Persons aged 55 to 64 as of December 31 of the tax year may exclude up to \$20,000 of retirement income claimed as federal taxable income from state taxable income. Persons aged 65 and older may exclude up to \$24,000 of their retirement income.<sup>4</sup>

The retirement income deduction is not limited to military retirement income or military service persons. Retirement income may include military pensions or annuities, Thrift Savings Plan disbursements, non-military retirement income, such as 401K distributions, and Social Security benefits.

**Military Family Relief Fund grant deduction.** Beginning in tax year 2014, grants from the Military Family Relief Fund may be excluded from taxable income to the extent that they are included as federal taxable income.<sup>5</sup> Grants are administered by the [Colorado National Guard Foundation, Inc.](http://www.colorado.gov/national-guard-foundation)

**For more information ...**

For more information on Colorado income taxes, visit the Colorado Department of Revenue website:

<http://www.colorado.gov/pacific/tax/income-tax-individual-file>

For information on federal tax breaks for military personnel, visit the Internal Revenue Service website:

<http://www.irs.gov/uac/tax-breaks-for-the-military>

<sup>4</sup>Section 39-22-104 (4)(f), C.R.S.

<sup>5</sup>Section 39-22-104 (4)(p), C.R.S.