

Retirement income



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Introduction

This information will help you decide how to report your pension or annuity income on your Oregon income tax return. It will also explain the retirement income credit. Although pensions and annuities are different, the term “pension” is used here to describe both.

Read one of the following federal publications to determine how to report your pension. Pamphlets are available from the Internal Revenue Service. Call toll-free 1-800-TAX-FORM (1-800-829-3676), or go to the IRS website at www.irs.gov.

- Publication 17, *Your Federal Income Tax*.
- Publication 524, *Credit for the Elderly or the Disabled*.
- Publication 575, *Pension and Annuity Income*.
- Publication 590, *Individual Retirement Arrangements (IRAs)*.
- Publication 721, *Tax Guide to U.S. Civil Service Retirement Benefits*.

What is taxable by Oregon?

Federal income tax rules generally determine the amount of your pension that is taxed by Oregon. However, you may subtract some pensions on your Oregon return that were taxed on your federal return.

These pensions are not taxed by Oregon:

- Social Security benefits.
- Veterans Administration benefits.
- Railroad Retirement Board benefits.

Oregon allows a subtraction for part or all of the payments you receive from the federal pension system. See page 4.

Full-year and part-year residents. Most retirement income is subject to Oregon tax when received by an Oregon resident. This is true even if you were a nonresident when you earned the income. However, you may subtract some or all of your federal pension income from Oregon income. See page 56.

For other exceptions, see **Previously taxed employee retirement plans** and **Previously taxed IRA conversions**.

Nonresidents. Oregon does not tax your retirement income if you are a nonresident who is not domiciled in Oregon. If you are an Oregon nonresident who is still domiciled in Oregon, any Oregon-source retirement income is taxable by Oregon. This applies to most forms of retirement income taxed by Oregon, including public pension plans, corporate retirement plans, Keogh plans, simplified employee pensions (SEPs), and IRAs. For the definition of “domicile,” see page 16.

Example: Hiro has always resided and worked in Oregon. On January 5, 2006, he retired, sold his Oregon residence, and moved temporarily to Arizona to work. He intends to remain in Arizona for two years and then return to Oregon.

He did not acquire another residence outside Oregon. He receives an Oregon-sourced pension and interest income.

Hiro has not given up his Oregon driver’s license, and his vehicles are registered with the state of Oregon. He has not changed his voter registration to another state.

Hiro has not shown an intent to give up Oregon as his home and acquire a permanent home elsewhere. Based on these facts, Hiro is domiciled in the state of Oregon. Although Hiro is taxed as a nonresident (his interest income is not taxed by Oregon), his Oregon-source retirement income is taxable by Oregon.

Retirement income means income from:

- Qualifying employer pension and profit-sharing plans exempt from tax under Internal Revenue Code (IRC) Section 401(a).
- Annuity plans [IRC Sec. 403(a) and IRC Sec. 403(b)].
- Cash or deferred compensation arrangements [IRC Sec. 401(k) plans and IRC Sec. 457 plans].
- Simplified employee pension plans [IRC Sec. 408(k)].
- Individual retirement arrangements [IRC Sec. 408(a) and IRC Sec. 408(b)].
- Plans for federal, state, or local government employees [IRC Sec. 414(d)].
- Pay for uniformed service members under chapter 71 of Title 10 of the United States Code.
- Trusts that were created before June 25, 1959 [IRC Sec. 501(c)(18)].

Payments received after termination of employment qualify if the payment is made under a plan, program, or arrangement maintained solely for the purpose of providing retirement benefits that exceed the amounts allowed under the qualified retirement plans described above.

Payments received from nonqualified deferred compensation plans [as described in IRC Sec. 3121(v)(2)(C)] qualify if the payments are part of a series of substantially equal periodic payments made:

- For the life or life expectancy of the recipient, or
- For a period of at least 10 years.

Retirement income does not include income received from:

- Social Security,
- Stock options,
- Restructured stock plans,
- Severance plans, or
- Unemployment compensation.

Taxpayers who have Oregon as their domicile are taxed as residents, unless they meet the requirements to be taxed as nonresidents. To be taxed as a nonresident, you must meet **all** of the following requirements:

- You do not maintain a permanent residence in Oregon for yourself or for your family during any part of the year, and
- You maintain a permanent residence outside Oregon during the entire year, and
- You spend less than 31 days of the year in Oregon.

Previously taxed employee retirement plans

Oregon allows residents to subtract payments from an individual retirement account (IRA), Keogh plan, Simplified Employee Pension (SEP) plan, and certain government plans if another state has already taxed contributions or a portion of the contributions to the plan.

The payments must be included in federal adjusted gross income. **All** of the following conditions must be met for the contributions to qualify:

- Contributions were made while a nonresident of Oregon.
- No previous state income tax deduction, exclusion, or exemption was allowed or allowable at the time contributions were made.

- No previous state income tax deduction, exclusion, credit, subtraction, or other tax benefit has been allowed for the contributions.
- Contributions have been taxed by another state.

The subtraction continues until all qualifying contributions are recovered.

Example 1: Mildred lived in California. From 1980 to 1996 she contributed to an IRA. In 1980 and 1981 she contributed \$1,500 each year. From 1982 through 1996 she contributed \$2,000 each year.

Both federal and California allowed a maximum deduction of \$1,500 for 1980 and 1981. For 1982 through 1986, federal allowed a maximum of \$2,000, and California allowed a maximum of \$1,500. Both federal and California allowed a maximum of \$2,000 for 1987 through 1996.

Mildred contributed \$2,500 ($\500×5 years, 1982–1986) with no deduction allowed on her California returns.

Mildred retired and moved to Oregon in June 2007. She receives payments of \$350 a month from the California IRA. These payments are subject to Oregon tax because she is now an Oregon resident. However, Oregon will allow Mildred to subtract the contributions that California has already taxed (\$2,500).

Mildred received seven payments of \$350 in 2007 for a total of \$2,450. She can subtract the entire \$2,450 for 2007. In 2008, she will receive 12 payments of \$350 for a total of \$4,200. Mildred will be able to subtract the balance of \$50 ($\$2,500 - \$2,450$). From that point on, no subtraction on the Oregon return for recovery of contributions is allowed.

Example 2: Use the same facts as in Example 1, except Mildred lived and worked in Washington before moving to Oregon. When she made contributions, she was allowed a federal deduction each year. However, she didn't get a state tax deduction, because Washington does not have an income tax. After retiring and moving to Oregon, Mildred receives the same payments as above. She does not qualify for the Oregon subtraction because her contributions were not taxed by another state.

Previously taxed IRA conversions

Oregon allows a subtraction for converting a traditional individual retirement account (IRA) to a Roth IRA, if the IRA is taxed by another state. You must include the payments in federal income.

Example: Susan lived in New York in 2007. In March, she converted her \$100,000 traditional IRA to a Roth IRA.

In September, she moved to Oregon. New York state will tax her IRA when she becomes a nonresident. Susan can subtract the amount included in federal income when she files her 2007 Oregon tax return.

U.S. government interest in IRA or Keogh distribution

Interest and dividends on U.S. bonds and notes are exempt from state tax. See page 58. Answer the questions below to see if you have a subtraction on your Oregon return for exempt income related to your retirement distributions.

1. Did you have any distributions from a self-employed retirement plan or an individual retirement account (IRA)?
2. Was any part of your self-employed retirement plan or your IRA invested in U.S. bonds and notes?
3. Did you include your self-employed retirement plan or IRA distribution in your 2007 federal adjusted gross income (AGI)?

If you answered “yes” to **all** the questions above, you’ll have an “other subtraction” on your Oregon return for the retirement plan exempt earnings included in your distribution.

Use the worksheet below to calculate your subtraction.

Worksheet

1. Total account balance at year end. 1. _____
2. Add current year distributions. 2. _____
3. Line 1 plus line 2. 3. _____
4. Total exempt earnings on account at year end. 4. _____
5. Total exempt part of distributions from all prior years. 5. _____
6. Line 4 minus line 5, but not less than -0-. 6. _____
7. Line 6 divided by line 3. Oregon exempt ratio. 7. _____
8. Line 2 multiplied by line 7. Oregon exempt portion of current year’s distribution. 8. _____

Example: Donna retired last year and began taking distributions of \$10,000 each year from her IRA. The IRA is invested in U.S. government securities. Donna uses the following information to calculate her subtraction for years 1 and 2:

Worksheet	Year 1	Year 2
1. Total account balance at year end.	\$100,000	\$95,000
2. Add current year distribution.	+ 10,000	+ 10,000
3. Line 1 plus line 2.	<u>\$110,000</u>	<u>\$105,000</u>
4. Total exempt earnings on account at year end.	\$ 40,000	45,000
5. Total exempt part of distributions from all prior years.	-0-	3,636
6. Line 4 minus line 5, but not less than zero.	<u>\$40,000</u>	<u>\$41,364</u>
7. Line 6 divided by line 3. Oregon exempt ratio.	<u>.3636</u>	<u>.3939</u>
8. Line 2 multiplied by line 7. Oregon exempt portion of current year’s distribution.	<u>\$3,636</u>	<u>\$ 3,939</u>

Federal pension income

You may be able to subtract some or all of your taxable federal pension included in 2007 federal income. This includes benefits paid to the retiree or the beneficiary. It does not include disability payments if you have not attained the minimum retirement age. The subtraction amount is based on the number of months of federal service before and after October 1, 1991:

- If all of your months of federal service occurred before October 1, 1991, subtract 100 percent of the taxable federal pension income you reported on your federal return.
- If you have no months of service before October 1, 1991, you cannot subtract any federal pension.
- If your service was both before and after October 1, 1991, you will subtract a percentage of the taxable federal pension income you reported on your federal return. To determine your percentage, divide your months of service before October 1, 1991, by your total months of service. Once you determine the percentage, it will remain the same from year to year.

Example 1: Jared worked for the U.S. Department of Agriculture from May 24, 1975, until July 8, 2006. He worked a total of 373 months—196 months before October 1, 1991. In 2006, he received federal

pension income of \$32,000. He can subtract 52.5 percent ($196 \div 373$) or \$16,800 ($.525 \times \$32,000$) of his federal pension. Jared will continue to subtract 52.5 percent of his federal pension from Oregon income in future years.

Use this worksheet to determine your federal pension income subtraction amount:

1. Federal pension income included in federal AGI. 1. _____
2. a. Months of service from _____ (fill in federal service start date) to October 1, 1991. a. _____ months*
- b. Months of service from _____ (fill in federal service start date) to _____ (fill in federal service retirement date). b. _____ months**

Divide the number of months on line a by the total number of months on line b. Round the decimal to three places. Enter here. This is your federal pension subtraction percentage. 2. _____

3. Multiply line 1 by the decimal on line 2. This is your federal pension subtraction. 3. _____

* **Federal service start date:** If your federal service start date was the 1st through the 15th of a month, include the entire month when counting federal service.

If your federal service start date was the 16th through the end of a month, do not include the first partial month of service. Start counting the months of federal service with the first full month.

** **Federal service retirement date:** If your federal service retirement date was the 1st through the 15th of a month, do not count this final partial month when counting the total months of federal service.

If your retirement date was the 16th through the end of the month, include the entire month when counting the total months of federal service.

Keep a copy of this worksheet with your permanent tax records. **You will continue to use the same percentage**, from line 2, to determine your federal pension subtraction in future years.

Example 2: Dinah served in the U.S. Air Force from November 23, 1984, through February 7, 2007. She received \$22,000 in pension benefits in 2007. The following worksheet shows how Dinah will determine her federal pension subtraction for 2007.

1. Federal pension income included in federal AGI. 1. \$22,000
2. a. Months of service from November 23, 1984, to October 1, 1991. a. 82 months
- b. Months of service from November 23, 1984, to February 7, 2007. b. 270 months
- Divide the number of months on line a by the total number of months on line b. Round the decimal to three places. This is your federal pension subtraction percentage. 2. .311
3. Multiply line 1 by the decimal on line 2. This is your federal pension subtraction. 3. \$6,842

Nonresidents. Claim a subtraction for federal pension income only if you reported it on your Oregon return. Oregon does not tax your retirement income unless you have kept Oregon as your domicile.

Retirement income tax credit

Who can claim the credit?

If you were **age 62 or older** on December 31, 2007, and receiving taxable retirement income, you can qualify for this credit. Retirement income includes payments **in Oregon taxable income** from:

- State or local government public pensions.
- Employee pensions.
- Individual retirement plans.
- Employee annuity plans.
- Deferred compensation plans including defined benefits, profit sharing, and 401(k)s.
- Federal pensions (includes military) not subtracted from Oregon taxable income.

How do you qualify for the credit?

- Your household income is less than \$22,500 (\$45,000 if married filing jointly), **and**
- Your Social Security and/or Tier 1 Railroad Retirement Board benefits are less than \$7,500 (\$15,000 if married filing jointly), **and**
- Your household income plus your Social Security and Tier 1 Railroad Retirement Board benefits is less than \$22,500 (\$45,000 if married filing jointly).

You can claim this credit or the credit for the elderly or the disabled, but not both.

How much is the credit?

Use the following worksheet to calculate your credit:

- | | |
|--|----------|
| 1. Enter the retirement income of the eligible individual(s) (Form 40, line 8; or Form 40N or 40P Oregon column, lines 16 and 17). | 1. _____ |
| 2. Enter any federal pension income subtracted from Oregon income. See page 56. | 2. _____ |
| 3. Net Oregon taxable pension. Line 1 minus line 2. | 3. _____ |
| 4. Enter \$7,500 (\$15,000 if married filing jointly). | 4. _____ |
| 5. Enter both spouses' total Social Security and Tier 1 Railroad Retirement Board benefits. | 5. _____ |
| 6. Line 4 minus line 5, but not less than -0-. | 6. _____ |

- | | |
|---|-----------|
| 7. Enter your household income. See the next section to determine household income. | 7. _____ |
| 8. Household income base. Enter \$15,000 (\$30,000 if married filing a joint return). | 8. _____ |
| 9. Line 7 minus line 8, but not less than -0-. | 9. _____ |
| 10. Line 6 minus line 9, but not less than -0-. | 10. _____ |
| 11. Enter the smaller of line 3 or line 10. | 11. _____ |
| 12. Multiply line 11 by 9% (.09). This is your credit. | 12. _____ |

No carryforward. The credit cannot be more than your tax liability for Oregon. Any credit not used this year is lost.

What's included in household income?

Household income generally includes all income (both taxable and nontaxable) each spouse received during the year. Include gross income reduced by adjustments as reported in your federal adjusted gross income (AGI).

You also need to include items not in your federal AGI. These items include but are not limited to:

- Veteran's and military benefits.
- Gifts and grants (total amount minus \$500).
- Disability pay.
- Nontaxable dividends (other than "return of capital").
- Inheritance.
- Insurance proceeds.
- Nontaxable interest.
- Lottery winnings.
- Railroad Retirement Board benefits (Tier 2 only).
- Scholarships.

See the household income checklist on page 119 for more help.

Do not include:

- Social Security and Tier 1 Railroad Retirement Board benefits.
- Your state tax refund.
- Pension income excluded from federal AGI that is a return of your contributions.
- Pensions that are rolled over into an IRA.

To determine household income, you must separate income (or loss) from businesses, farms, rentals or royalties, and dispositions of tangible or intangible property. Combine all income from similar sources for net income or loss. Any net loss from the source is limited to \$1,000. Net operating loss carrybacks or carryforwards are not allowed. Capital loss carryforwards are not allowed.

Example 1: Jack owns a farm and has a \$4,000 loss. He is also in a partnership whose main activity is farming. Jack has income from the partnership of \$1,500. His net farm loss is \$2,500. He may claim only \$1,000 of this loss to compute his household income. Any net loss Jack has from other sources is also limited to \$1,000 each. If Jack is claiming more than a \$1,000 loss on any line, he must attach a worksheet showing his computations.

If the combined total of your depreciation, depletion, and amortization deductions is more than \$5,000, you must add the excess back into household income. You must also increase your household income by the Oregon income tax modification for depletion in excess of basis.

Example 2: Callie has a business with gross income of \$32,000 for the year. She has a \$11,000 depreciation deduction. Other business expenses are \$24,500. She reports a business loss for federal purposes of \$3,500. She recomputes her business income for household income purposes. The allowable depreciation deduction is limited to \$5,000. She reports is \$2,500 business income, computed as follows: $\$32,000 - (\$5,000 + \$24,500) = \$2,500$.

Taxpayer assistance

General tax information www.oregon.gov/DOR
Salem 503-378-4988
Toll-free from an Oregon prefix 1-800-356-4222

Asistencia en español:
Salem 503-378-4988
Gratis de prefijo de Oregon..... 1-800-356-4222

TTY (hearing or speech impaired; machine only):
Salem 503-945-8617
Toll-free from an Oregon prefix 1-800-886-7204

Americans with Disabilities Act (ADA): Call one of the help numbers for information in alternative formats.