

Military Personnel

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Income Tax Fact Sheet 5

Minnesota forms you may need: M1, M1C, M1CD, M1CR, M1ED, M1LTI, M1M, M1NR, M1PR, M1WFC, M1X, M14, M99, M23

Fact Sheet

Military personnel often have questions about their Minnesota income tax obligations. Because they often are stationed in a place other than their state of residence, they have questions about:

- where to file their income tax returns,
- which forms to file,
- which sources of income are taxable, and
- what refunds or credits they are entitled to.

This fact sheet should help answer these questions.

What's new for 2009?

Credit for military service in a combat zone increased to \$120 for each month of service in 2009

Members of the military who served in a combat zone or hazardous duty area any time in 2009 may now be eligible for a credit of \$120 for each month of service. See page 4 for more information.

Credit for military service in a combat zone for September 11, 2001 to December 31, 2006 expires soon!

The military service credit for months of service from September 11, 2001 to December 31, 2006 expires October 15, 2010.

Military subtraction expanded for National Guard and Reserves

Beginning with tax year 2009, members of the National Guard and Reserves can now subtract pay received for training and certain types of qualifying active service within Minnesota. Training includes annual training and drill weekends.

Credit for past military service

A nonrefundable credit of up to \$750 is available for veterans of the military, including the National Guard and Reserves, who have served in the military for at least 20 years or have a 100 percent service-related disability. Income limits apply. See page 4 for more information.

Nonresident spouse of a military member stationed in Minnesota

The Military Spouses Residency Relief Act (Public Law 111-97) was signed into law on November 11, 2009, and may affect the Minnesota income tax filing requirements for nonresident spouses of military personnel, effective for tax year 2009. See page 3 for more information.

Military subtraction - qualifying service

US/UN Military (Army, Navy, Air Force and Marines)

For 2009, all income earned from federal active service in the US/UN Military is allowed a subtraction. Federal active service includes service or duty under U.S. Code, title 10; as required by federal law, regulation or order; and travel to or from that service or duty. Federal active service also includes being on medical hold under active duty orders for community-based health care operations while recuperating from an injury. Federal active service excludes federally funded state active service.

National Guard and Reserves

For 2009, all income earned from service in the National Guard or Reserves is entitled to a subtraction. However, Active Guard Reserve (AGR) income and pay received for employment by the State of Minnesota Department of Military Affairs is not allowed a subtraction. Additionally, state active duty pay for National Guard members is allowed a subtraction.

Determining residency

Members of the military and their spouses remain domiciled in the state in which they have established permanent residency until they take the necessary steps to change their residency (see *Military Spouse Residency Relief Act* on page 3). This is true regardless of where you are stationed during the year. Therefore, if you enter the armed forces as a Minnesota resident, you remain domiciled in Minnesota unless positive action is taken to abandon your Minnesota residency and establish a domicile in another state.

If you are a resident of another state who is stationed in Minnesota, being in Minnesota for over half of the year does not make you a resident of Minnesota. The 183-day rule does not apply to military members or their spouses, unlike civilian nonresidents. (For details on the 183-day rule, see Fact Sheet 1, *Residency*.)

If you are a military person who lives with your spouse, both you and your spouse will usually have the same state of residence for tax purposes (see *Military Spouse Residency Relief Act* on page 3). An exception to this rule is if you and your spouse had different states of residence at the time of your marriage. In this case, you may maintain your separate states of residence until positive action is made to change your residency.

For more information on residency, including instructions on how to change residency, see Fact Sheet 1, *Residency*.

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This fact sheet is intended to help you become more familiar with Minnesota tax laws and your rights and responsibilities under the laws. Nothing in this fact sheet supersedes, alters or otherwise changes any provisions of the tax law, administrative rules, court decisions or revenue notices. Alternative formats available upon request.

Note: If you have had an actual change of residence, be sure to change your state of residence with your paymaster (use Military Form DD2058). Keep in mind that changing your state of residence with your paymaster or moving from one duty station to another does not in itself constitute a change of residence.

Income and filing requirements

Once you've determined where you are a resident, you can determine what Minnesota forms you need to file, what income is taxable and any credits you may be entitled to claim.

Minnesota residents

If you are a resident of Minnesota for the entire year and are required to file a federal income tax return, you must also file Minnesota Form M1, *Individual Income Tax Return*. However, if your gross income included on your federal return, minus any compensation received for federal active duty, is less than the minimum filing requirement for the year (\$9,350 for 2009), you are not required to file a Minnesota return.

Subtractions

As a Minnesota resident, you must pay Minnesota tax on taxable income you received from all sources. **However, you are allowed subtractions for the following compensation, if included in federal taxable income:**

- federal active duty under U.S. Code Title 10
- state or federal active service (under U.S. Code Title 10 and Title 32) such as ADSW (ADOS), natural disaster emergency response and missing persons searches performed by members of the National Guard or Reserves
- National Guard and Reserves duties
- Reenlistment bonus

Active Guard Reserve (AGR) Program compensation and pay to civilian employees of the military or State Military employees are not allowed as a subtraction, regardless of whether the income was earned inside or outside Minnesota, unless the individual has been ordered to Federal Active Service (Title 10) duty.

Use Schedule M1M, *Income Additions and Subtractions*, to claim these subtractions. If you had nonmilitary income taxed by another state while you were a Minnesota resident, you may qualify for a credit on taxes paid to another state (see Schedule M1CR, *Credit for Income Tax Paid to Another State*).

Part-year residents and nonresidents of Minnesota

Even though your military pay is not taxed by Minnesota during the period of time you are a nonresident, you may be required to pay Minnesota tax on other types of income you received or earned in Minnesota, such as income from a civilian job, business income and gambling winnings.

As a part-year resident or nonresident of Minnesota, you are required to file Form M1 if your Minnesota gross income meets the minimum filing requirement for the year (\$9,350 for 2009).

Minnesota gross income includes income you received from all sources (including sources not in Minnesota) while you were a Minnesota resident, and any income you earned in Minnesota or from sources in Minnesota while you were a nonresident.

If you were a part-year resident or nonresidents, your gross Minnesota income includes:

- wages (not including nonresident military pay), salaries, fees, commissions, tips or bonuses for work performed in Minnesota

- deferred income wages earned in Minnesota, such as severance pay, equity based pay and other non-statutory deferred compensation
- gross rents and royalties from property located in Minnesota
- gains from the sale of land or other tangible property located in Minnesota
- gains from the sale of a partnership interest, to the extent that the partnership had property or sales in Minnesota
- gain on the sale of goodwill or income from an agreement not to compete connected with a business operating in Minnesota, to the extent that the income of the business for the year preceding the year of sale was assigned to Minnesota
- gross income from a business located in Minnesota or a profession conducted partly or entirely in Minnesota including any Minnesota gross income you may have received as a shareholder of an S corporation or as a partner of a partnership
- gross winnings from gambling in Minnesota

Although gross income determines whether you must file a Minnesota return, only net income is taxed.

If you're required to file a Minnesota return, part-year residents and nonresidents must also complete Schedule M1NR, *Nonresidents/Part-Year Residents*, to determine the income taxable to Minnesota.

If you're a resident of another state required to file a Minnesota return, you are allowed a subtraction for your active duty military pay (see Schedule M1M), and your military pay is removed when calculating Minnesota tax (see Schedule M1NR).

If you're not required to file a Minnesota return and Minnesota taxes were withheld from your income or you paid estimated tax, you must file Form M1 and Schedule M1NR to receive a refund. Follow the steps provided in the instructions for Schedule M1NR.

See Fact Sheet 2, *Part-Year Residents*, or Fact Sheet 3, *Nonresidents*, for more information.

How to file

If you are a Minnesota resident with a nonresident or part-year resident spouse, do not include your excluded military pay (pay taken as a subtraction on Schedule M1M) in Column B of Schedule M1NR when determining the income ratio.

The Military Spouses Residency Relief Act

Effective for 2009, federal legislation signed into law on November 11, 2009, amended the Servicemembers Civil Relief Act to allow spouses of active duty members of the military to keep their state of residence when moving with their military spouse. This legislation prohibits states from taxing the income for services performed by the non-military spouse who is a nonresident.

Resident spouse of a military member stationed outside of Minnesota

Spouses of active duty military members may now keep their state of residence when moving to be with their military spouse. If your nonmilitary spouse is a Minnesota resident, his or her income is fully taxable to Minnesota and a return is required to be filed with Minnesota when they are required to file a federal

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return. If your spouse is not required to file a return, he or she may wish to file in order to claim any refundable credits they may be eligible for. The income exclusion applies to “personal service income”, outlined below.

Your non-military spouse should apply for exempt status with their employer so that withholding to the other state is not taken out of their pay. However, they may be required to make estimated tax payments to Minnesota, since there will be no withholding to Minnesota on that income.

Nonresident spouse of a military member stationed in Minnesota

For Minnesota income tax purposes, a spouse of an active duty military member may be exempt from Minnesota tax on personal service income performed in Minnesota, if the following three requirements are met:

- The military member is present in Minnesota on military orders,
- The non-military spouse is in Minnesota solely to be with the military member, and
- The non-military spouse maintains residency in another state.

If your nonresident spouse meets these requirements, they should apply for exempt status with their Minnesota employer. If withholding was taken out of their wages, they must file a return with Minnesota in order to get the money refunded using Form M1 and Schedule M1NR. They may also take a subtraction for nonresident military pay on line 26 of Schedule M1M and line 20 of Schedule M1NR.

Since most of Minnesota’s credits are based on the percentage of income taxable to Minnesota, you may not qualify for credits.

Documentation

To support your nonmilitary spouse’s exempt withholding status, you should provide the following documents when requested:

- a copy of your current military orders, assigning you to your post of duty, and
- Form DD 2058, *State of Legal Residence Certificate*.

Personal service income

Personal service income is considered compensation derived from the performance of personal or professional services provided by the taxpayer. This income is subject to Social Security tax. Business income, such as income from rents, royalties, estates, trusts or partnerships, which is not subject to Social Security, is not eligible for the exclusion and should be assigned to MN based on the three factor formula when the business is partially located here.

Examples of personal service income include:

- wages, salaries, tips, commissions, and bonuses earned by employees in the course of their employment,
- scholarship income that requires personal service for which the student receives a W-2 form, and
- compensation to sole proprietors providing personal services. Common examples of professions or trades in which a taxpayer receives compensation as a sole proprietor include: accountant, attorney, barber, carpenter, doctor, engineer, insurance salesman, repairman, etc.

Federal foreign earned income exclusion

If you and/or your spouse earned income in a foreign country, other than military pay, you may qualify for the federal foreign earned income exclusion. If you qualify and your foreign earned income is excluded on your federal return, this income will not be taxed by Minnesota. For more information, see IRS Publication 54, federal Form 2555 or federal Form 2555EZ.

Military pensions

Military pensions of Minnesota residents are taxable by Minnesota. Therefore:

- if you move into Minnesota, your pension becomes taxable once you become a Minnesota resident, even if the pension was earned prior to moving to Minnesota.
- if you move out of Minnesota and establish a new state of domicile, your pension is not taxed by Minnesota.

Home sales

Minnesota follows the federal guidelines. You may exclude the gain on the sale of your Minnesota home if you excluded it federally. However, you must include the gain as household income when filing Form M1PR, *Minnesota Property Tax Refund*.

Death while serving in Armed Forces

If a military member dies while in active service, that member’s Minnesota income tax liability will not be imposed for that year, and any outstanding debts for prior year taxes and penalties will be abated. A claim for refund of any tax paid may be filed within seven years from the date the return was filed for any years in which the decedent was in active service.

Example: Peter, a Minnesota resident, died in service in Iraq in 2009. He joined the U.S. Marines in 2007 and was in active service ever since. He filed Minnesota state income tax returns and paid tax to Minnesota for tax years 2007 and 2008. He filed the returns on April 15, 2008 and April 15, 2009, respectively. To the extent that there was any state income tax liability for 2009, it is forgiven. Peter’s heirs will have until April 15, 2015 and April 15, 2016 to file an amended return for a refund of the state taxes paid for 2007 and 2008, respectively.

If the taxpayer filed a joint return for any year, the tax abated or refunded will be based on the following ratio: Divide the tax liability the military member would have paid had he or she filed a separate return by the total tax liability they would have paid had they each filed separate returns.

Eligibility for Minnesota credits

Military personnel are eligible for the same credits as civilians. For example, if you:

- qualify for the federal earned income credit and have Minnesota assignable earned income, see Schedule M1WFC, *Minnesota Working Family Credit*.
- have Minnesota source earned income and have child or dependent care expenses or had a child born during the year, see Schedule M1CD, *Child and Dependent Care Credit*.
- paid state tax to Minnesota and to another state on the same income while a Minnesota resident, see Schedule M1CR.
- had educational expenses for your qualifying child(ren) in grades K–12 and had Minnesota assignable income, see the

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M1 instructions, Schedule M1ED, *K-12 Education Credit*, and Income Tax Fact Sheet 8.

- are married, filing a joint Minnesota return and both you and your spouse have taxable earned income, taxable pension or taxable Social Security income, see the M1 instructions for the marriage credit.
- paid long-term care insurance premiums and have Minnesota assignable income, see Schedule M1LTI, *Long-Term Care Insurance Credit*.
- served in a combat zone or qualified hazardous duty area anytime on or after September 11, 2001, see Form M99, *Credit for Military Service in a Combat Zone*.
- are a partner, shareholder or beneficiary, see Schedule KPI, KS or KF you received from the entity for any pass-through credits.
- have Minnesota taxable income that falls within the lowest income bracket, you may qualify for a refundable lower income motor fuels tax credit. See M1 instructions for more information.

For information on all available income tax credits, see the M1 instruction booklet. Some credits may be prorated for part-year residents or nonresidents.

Military service credit

If you served in a combat zone or qualified hazardous duty area anytime on or after September 11, 2001, you may be eligible for a refundable credit.

Note: The military service credit for service from September 11, 2001 to December 31 2006 expires October 15, 2010.

For months of service in 2009, the credit is \$120 for each month or part of a month you served in a combat zone, during which time your military records indicate Minnesota as your home of record. For months of service from September 11, 2001 to December 31, 2008, the credit is \$59 for each month or part of a month of service.

To claim the credit based on your service, complete Form M99, *Credit for Military Service in a Combat Zone*, and mail it to the department with the appropriate military records. To claim credit for service in:

- 2009, use the 2009 Form M99
- 2008, fill out the 2008 Form M99
- 2007, use the 2007 Form M99
- 2001-2006, fill out the 2006 Form M99

You can find these forms on our website at www.taxes.state.mn.us.

If the person is deceased, his or her estate, surviving spouse or dependent may qualify for the credit. As of 2008, the estate of a deceased service member, who died prior to 2006 without a surviving spouse or dependent, may claim the credit back to September 11, 2001. In addition, the death no longer needs to be combat related. To claim the credit, Form M99 must be filed with Schedule M23, *Claim for Credit Due a Deceased Taxpayer*. Prior to 2006, law allowed only the surviving spouse or dependent to be eligible to claim the credit, and only if the decedent died in a combat zone or as a result of injuries sustained in a combat zone.

Credit for past military service

Beginning with tax year 2009, if you (and/or your spouse if filing a joint return) are a veteran of the military, including the National Guard and reserves, you may qualify for a nonrefundable credit of up to \$750 each for past service.

You may qualify if you have been separated from service and:

- have served in the military for at least 20 years, or
- have a service-related disability rated by the U.S. Department of Veterans' Affairs as being 100 percent total and permanent.

To qualify for the full credit, your federal adjusted gross income (from line 37 of federal Form 1040, line 21 of Form 1040A or line 4 of Form 1040EZ) must be \$30,000 or less. The amount of your credit is reduced by 10 percent of federal adjusted gross income in excess of \$30,000. Veterans with income over \$37,500 are not eligible for the credit. See Schedule M1C, *Nonrefundable Credits*.

Minnesota estimated tax

If you have income taxable by Minnesota that is not subject to withholding (for example, rental, self-employment, business or unemployment income) and you expect to owe more than \$500 in tax, you are required to pay quarterly estimated tax. For further information, see the *Individual Estimated Tax Instructions*, available on our website.

If you are a Minnesota resident who is stationed in Minnesota, you may want to ask your paymaster to withhold Minnesota income tax from your military pay to avoid having to pay estimated tax.

Homestead status and property tax refund State-paid real estate tax (homestead) credit

Homestead status is an important factor in determining residency. You may be asked by the department to supply information regarding your residency.

If you are a resident for property tax purposes, you are a resident for income tax purposes.

Homestead classification for absent military members

Legislation passed in 2006 made active duty military members, who are absent from Minnesota solely for active duty, eligible for the homestead classification on acquired property even if the property has not been occupied as a homestead by the person or a member of their family.

To qualify, the military member must notify the county assessor in the county of purchase, and must identify that their absence is due to military service. Upon return from the service, the military member must notify the assessor, and will be granted an abatement for the difference between nonhomestead and homestead taxes for the current year and the preceding two years, not to exceed the time in which the person owned the property.

Homeowner or renter refunds

If you are a Minnesota resident who is in the military—regardless of where you are stationed—and you own or rent a home in Minnesota, you may qualify for a property tax refund. See Form M1PR, *Property Tax Refund*, and instructions.

When applying for the refund, be sure to include any non-taxable income, such as combat or hazardous duty pay, as household income.

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Nonresident military personnel do not qualify for property tax refunds, unless his or her spouse is a full- or part-year resident of Minnesota.

Property tax exclusion for disabled military members

Honorably discharged disabled veterans are eligible for an annual exclusion from property taxes of up to \$300,000 in market value on their homesteaded property.

To qualify for this exclusion, the veteran must be honorably discharged from the military (their discharge papers, such as Form DD-214, must signify this) and certified by the United States Veterans Administration as having a service connected disability. Veterans with a 70 percent disability rating or higher are eligible for a market value exclusion of \$150,000, while those who are totally (100 percent certified) and permanently disabled are eligible for the \$300,000 exclusion.

However, properties that qualify for this exclusion do not qualify for the residential homestead market value credit provided under M. S. 273.1384, subd. 1.

Agricultural homesteads are eligible for this exclusion on the house, garage and one immediate acre of land.

Application process. Applications are available from the local county assessor's office and must be submitted for the exclusion by July 1 of the current year's market value for taxes paid in the next year. Those with a rating of 70 percent or higher must reapply every year. Veterans who are totally and permanently disabled do not need to reapply after the initial approval and the property will continue to qualify until there is a change in the ownership or use of the property. (A surviving spouse can also continue to qualify under this provision as long as they own and reside on the property.)

Military extensions

Federal active duty military personnel

If you are an active duty military personnel in a presidentially designated combat zone or contingency operation, you may file and pay your Minnesota income taxes up to 180 days after the last day you are in the combat zone or the last day of any continuous hospitalization for injuries sustained while serving in the combat zone. When you file your Form M1, enclose a separate sheet clearly stating that you were serving in a **combat zone**.

If you are stationed outside the United States but are not involved in combat zone operations, you have until October 15 to file your return. However, to avoid a late payment penalty, you must pay at least 90 percent of your total tax by April 15. Penalty and interest will be assessed on any tax not paid by the regular due date. Unlike the federal rules, Minnesota does not allow an extension to pay your tax.

Military reservists and National Guard members

For those in a combat zone, Minnesota follows federal rules. For those not in a combat zone, below are guidelines for extensions for Minnesota military reservists and National Guard members on federal active duty:

- If you are called to active service in the United States, you qualify for a six-month extension.
- If you are called to active service abroad, the extension is for the period you served abroad plus six months.

If you owe tax and the amount due is paid in full with the return by the extension date, no interest or late payment/filing penalties will be assessed.

If a married couple files "married filing joint," your spouse gets the same extension. If a tax return is filed and the liability is paid within the extension period, there will be no penalty or interest assessed on the balance due. Keep in mind that the time you can generally be audited is three and one-half years from the due date of the return or the date you file, whichever is later.

If you qualify for a military extension, you do not need to file anything with the state of Minnesota prior to filing your return. When you file your Form M1, enclose a separate sheet stating that you are filing under the **military extension**.

Suspension of Statute of Limitations during period of disability

Taxpayers with a "financial disability" (defined in IRC 6511(h) as someone who is unable to manage his or her financial affairs by reason of a medically determinable physical or mental impairment) have the 3 ½ year time frame in which they must file suspended for the time in which they are disabled.

When filing a claim for a refund, you must provide proof of the disability (an explanation of the situation and a statement from a health care professional) along with the return or in response to an appeal denying the refund outside statutory claim.

Need forms?

If you need forms, you may:

- download forms, fact sheets and other tax-related information at: www.taxes.state.mn.us
- photocopy the forms you need at a neighborhood library
- call 651-296-4444 or 1-800-657-3676 to have forms mailed to you
- write to: Minnesota Tax Forms, Mail Station 1421, St. Paul, MN 55146-1421.