



SENATE BILL 105: 2021 Appropriations Act, Sec. 42.1A: Eliminate Tax on Military Pension Income

2021-2022 General Assembly

Committee:		Date:	January 26, 2022
Introduced by:		Prepared by:	Trina Griffin Staff Attorney
Analysis of:	Sec. 42.1A of S.L. 2021-180		

OVERVIEW: Section 42.1A of S.L. 2021-180 exempts the following military retiree income from taxation:

- Military retirement pay received by a retired member of the Armed Forces of the United States who served at least 20 years or was medically retired.
- Payments from the Survivor Benefit Plan to a beneficiary of a retired member of the Armed Forces of the United States who served at least 20 years or was medically retired.

This section is effective for taxable years beginning on or after January 1, 2021.

CURRENT LAW: Members of the military pay federal income tax on their retirement pay. For taxable years 2019 through 2021,¹ North Carolina residents pay a flat 5.25% income tax rate on their adjusted gross income unless it is otherwise exempt. There is an income tax exemption of retirement pay for a retired member of the military who vested prior to August 12, 1989. Prior to 1989, North Carolina tax law provided a \$3,000 income tax exclusion for military retirees. For taxable years beginning on or after 1989, and before 2014, North Carolina tax law provided a \$4,000 income tax exclusion for military retirees who did not vest prior to August 12, 1989 and a full exemption for military retirees who vested before August 12, 1989. The tax simplification and reform legislation enacted in 2013 eliminated the \$4,000 income tax exemption for governmental retirees, including military retirees, effective for taxable years beginning on or after January 1, 2014. Military retirees who vested before August 12, 1989, continue to receive a full State income tax exemption of their military retirement income under the Bailey court decision.

BILL ANALYSIS: Section 42.1A of S.L. 2021-180 exempts the following from State income tax:

- Military retirement pay received by a retired member of the Armed Forces of the United States who served at least 20 years in the military or was medically retired from the military. Severance pay received for separation from the military would not be exempt.
- Payments from the Survivor Benefit Plan to a beneficiary of a retired member of the Armed Forces of the United States who served at least 20 years in the military or was medically retired from the military.

EFFECTIVE DATE: This section is effective for taxable years beginning on or after January 1, 2021.

¹ Per Section 42.1 of S.L. 2021-180, the individual income tax rate is phased down to 3.99% over 6 years. The rate for tax year 2022 is 4.99%.

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Senate Bill 105

Page 2

BACKGROUND: The Survivor Benefit Plan is a Department of Defense sponsored and subsidized program that provides up to 55 percent of a service member's retired pay to an eligible beneficiary upon the death of the member. The payments are in the form of an annuity and are adjusted for inflation.