

How Iowa Seniors Will be Taxed Changes Coming With 2006 Legislation

The way senior citizens pay state income taxes will begin to change dramatically next year. Beginning with income earned in 2007 (returns filed in 2008), Iowans age 65 or over will pay no income tax if their modified adjusted gross income (MAGI) is below a threshold. The threshold for a couple is \$24,000, for individuals \$18,000. Beginning in January 2009, those tax-exempt thresholds will rise to \$32,000 (couples) and \$24,000 (individuals). The current no-tax thresholds, or low-income exemptions, (\$13,500 for couples, \$9,000 for individuals), will remain for those under 65. Also under the new Iowa law, a full exemption will be phased in for Social Security income over eight years. Currently, at least 50 percent of Social Security income is exempt (up to 100 percent for lower income seniors). The details of Senate File 2408 are explained below.

Zero Tax Threshold Raised

- The income level at which a person begins to pay tax is currently \$13,500 (married) or \$9,000 (single). Starting in 2007, the thresholds for all persons age 65 or older, and for the spouse of a person age 65 or older regardless of the spouse's age, will be higher.
- For the 2007 and 2008 tax years (which are the same as calendar years), married couples (whether filing jointly or separately), unmarried heads of household, and surviving spouses will be exempt from income tax if their modified adjusted gross income (MAGI) is \$24,000 or less. All other persons will be exempt if income is \$18,000 or less.
- For 2009 tax years and later, the exempt income thresholds are raised to \$32,000 (couples) and \$24,000 (individuals).
- For purposes of calculating the threshold, modified adjusted gross income includes all income normally included in Iowa Net Income (line 26 of the Iowa 1040), plus the exempt portion of pension income and the portion of Social Security benefits made exempt by SF2408.

Tax Calculation Changed

- If a couple's or individual's income exceeds the no-tax threshold, then they must calculate their income tax in the regular way. (They might still pay no income tax because of the exemptions for Social Security and pension income, however.) In calculating the "regular tax," the taxpayer excludes from income the first \$6,000 of pensions (\$12,000 for married couples, prorated between them) and at least half of Social Security benefits. This is unchanged from current law.
- For married couples, surviving spouses and unmarried heads of household, it will be necessary (as it is under current law) to also calculate an "alternate tax." The alternate tax will be equal to the top tax rate (currently 8.98 percent) times MAGI in excess of the threshold. Under current law, the top rate is applied to the sum of net income (line 26) and exempt pension income. The taxpayer then pays whichever is lower, the regular tax or the alternate tax. For example, a married couple with \$34,500 in income (MAGI) in 2009 will not be automatically exempt because their MAGI exceeds the \$32,000 threshold by \$2,500. The alternate tax would be 8.98 percent of \$2,500, or \$225. If the regular tax exceeded \$225, they would pay only \$225. If the regular tax were less than \$225, they would pay the regular tax.

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- For all other persons, there is no alternate tax (under current law or under the new law), but the regular tax cannot reduce their total net income below the threshold amount. For example, a single woman in 2009 with \$24,500 in MAGI is not automatically exempt because her MAGI exceeds the \$24,000 threshold by \$500. Her regular tax could be in excess of \$500, but this would reduce her income below \$24,000; therefore, her tax is limited to \$500.

The Remaining Tax on Social Security Benefits will be Phased Out

- Currently, at least 50 percent of Social Security benefits are exempt from tax in Iowa, and most Iowan's pay no tax at all on Social Security because their income is below a certain level. Under the new law, a person must first calculate how much of their Social Security income is taxable in the same way as current law. Then a percentage of this taxable amount is deducted. The percentage starts at 32 percent for 2007 and 2008 and rises each year thereafter until it reaches 100 percent in 2014. In other words, starting in 2014 all Social Security benefits are exempt from tax for all taxpayers.

Answers to Common Questions



Is it true that seniors will now pay tax only on taxable income above the new zero-tax thresholds?

No. The thresholds are compared to MAGI to see if seniors fall under the zero-tax threshold. If MAGI is below the threshold they owe no tax and need go no further. If MAGI is above the threshold, then they must compute their Iowa income tax based on total taxable income, not taxable income above the threshold. See examples below.



Under the new law, does the pension exclusion still apply?

Yes it does. This was not changed. If your MAGI exceeds the threshold, you will have to calculate your regular tax, and taxable income will include only the portion of pension income above the \$6,000 exclusion (\$12,000 for married couples.)



Under the new law, will seniors have to calculate the amount of Social Security income taxable under the old law every year, even though that Social Security income is fully exempt?

Yes. The new law complicates tax filing for seniors. During the eight-year phase out period, the taxable amount of Social Security income must be calculated just as it is now, and then a percentage of that is exempted. When the phase out is complete, many will still have to do this calculation in order to determine whether their MAGI is under the threshold, and (if it is not) to determine if the alternate tax (based on MAGI) is higher or lower than the regular tax. Filing could have been simplified if the law had defined MAGI simply to include either all Social Security income, or no Social Security income.

Examples

The tables on the following pages illustrate the effects of the new law when the Social Security exemption has been fully phased in (tax year 2014). Iowa taxes are calculated using the standard deduction and tax rates in effect for 2006, since we do not know what those will be in 2014. Separate tables show the calculation of taxes for the same taxpayers under current law.

Single Persons

- #1 This person's Social Security and pension income is already fully exempt under current law, and his or her other income is not high enough to produce any tax liability, so there is no benefit from SF2048 despite total income (MAGI) falling below the threshold.
- #2 This person's income is the same as #1, but consists mostly of non-exempt income (interest, dividends). As a result, this person would pay \$483 in tax under current law but would pay no tax under the new law because MAGI is below the threshold.

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- #3 This person's income exceeds the no-tax threshold slightly; he or she would pay the lesser of the regular tax of \$275 and the income in excess of the threshold (\$375). Tax would have been \$439 under current law.
 - #4 This person, with \$50,000 in total income, would pay \$1,249 under current law but only \$732 under the new law because of an additional \$8,000 in Social Security benefits that are not taxable.

Married Couples

- #1 This couple's Social Security and pension income is already fully exempt; their \$14,000 in other income is not high enough to produce any tax liability under current law, so they gain nothing from the new law.
- #2 This couple's income exceeds the threshold slightly; they pay the alternate tax of \$60 because it is less than the regular tax of \$329 (both amounts after credits). Under existing law they would have paid \$509.
- #3 This couple, with a total income of \$72,000, would have paid \$621 under current law. Under the new law, their regular tax is reduced to \$125 because of the Social Security exemption, and this is less than the alternate tax.

Iowa Income Tax For Single Persons* Age 65 and Older

Social Security fully exempt (tax year 2014); tax based on 2006 rates

	1	2	3	4
Income from All Sources				
A Social Security benefits	14,000	5,000	18,500	18,000
B Pensions, IRAs, annuities	5,000	2,000	8,000	12,000
C Other (interest, dividends, wages)	6,000	18,000	13,500	20,000
D Total	25,000	25,000	40,000	50,000
Taxable Social Security Benefits				
E One-half of Social Security benefits	7,000	2,500	9,250	9,000
F All other income (B + C)	11,000	20,000	21,500	32,000
G Provisional income	18,000	22,500	30,750	41,000
H Exempt amount	25,000	25,000	25,000	25,000
I Excess provisional income (G - H)	0	0	5,750	16,000
J One-half of excess provisional income	0	0	2,875	8,000
K Taxable social security benefits under prior law (lesser of E or J)	0	0	2,875	8,000
L Applicable phase-out percentage	100%	100%	100%	100%
M Additional exemption under SF2408 (K times L)	0	0	2,875	8,000
N Taxable social security benefits (K - M)	0	0	0	0
Taxable Pensions & Annuities				
O Maximum exclusion	6,000	6,000	6,000	6,000
P Pensions, IRAs, annuities (= B)	5,000	2,000	8,000	12,000
Q Exclusion (smaller of O, P)	5,000	2,000	6,000	6,000
R Taxable portion (P - Q)	0	0	2,000	6,000
Low Income Exemption				
S Social security income exempted by SF2408 (M)	0	0	2,875	8,000
T All other income (B + C)	11,000	20,000	21,500	32,000
U Modified Adjusted Gross Income (MAGI)	11,000	20,000	24,375	40,000
V Threshold	24,000	24,000	24,000	24,000
W Excess income (MAGI above threshold)	0	0	375	16,000
Is total net income less than threshold?	Yes	Yes	No	No
If Yes, tax is zero; if No, compute tax below				
Regular Tax Calculation				
X Taxable social security (= N)	0	0	0	0
Y Taxable pensions (= R)	0	0	2,000	6,000
Z Other income (= C)	6,000	18,000	13,500	20,000
AA Iowa Net Income: Line 26 of 1040	6,000	18,000	15,500	26,000
AB Less: Federal tax deduction	1,825	1,825	2,920	5,750
AC Less: Standard Deduction (2006 level)	1,650	1,650	1,650	1,650
AD Taxable Income: line 42 of 1040 (AA - AB - AC)	2,525	14,525	10,930	18,600
AE Income Tax (2006 rates)**	14	543	335	792
AF Exemption Credits (regular + senior)	60	60	60	60
AG Net Regular Tax:	0	483	275	732
Actual Tax				
AH Regular tax, but not more than excess income (smaller of AG or W)	0	0	275	732

*Unmarried persons who are not a head of household or surviving spouse

**Calculated using 2006 tax rate schedule; will vary slightly from amounts in tax table

Iowa Income Tax For Single Persons* Age 65 and Older

Current law; tax based on 2006 rates

	1	2	3	4
Income from All Sources				
A Social Security benefits	14,000	5,000	18,500	18,000
B Pensions, IRAs, annuities	5,000	2,000	8,000	12,000
C Other (interest, dividends, wages)	6,000	18,000	13,500	20,000
D Total	25,000	25,000	40,000	50,000
Taxable Social Security Benefits				
E One-half of Social Security benefits	7,000	2,500	9,250	9,000
F All other income (B + C)	11,000	20,000	21,500	32,000
G Provisional income	18,000	22,500	30,750	41,000
H Exempt amount	25,000	25,000	25,000	25,000
I Excess provisional income (G - H)	0	0	5,750	16,000
J One-half of excess provisional income	0	0	2,875	8,000
N Taxable social security benefits (lesser of E or J)	0	0	2,875	8,000
Taxable Pensions & Annuities				
O Maximum exclusion	6,000	6,000	6,000	6,000
P Pensions, IRAs, annuities (= B)	5,000	2,000	8,000	12,000
Q Exclusion (smaller of O, P)	5,000	2,000	6,000	6,000
R Taxable portion (P - Q)	0	0	2,000	6,000
Low Income Exemption				
U Net Income: Line 26 of 1040 (C + N + R)	6,000	18,000	18,375	34,000
V Threshold	9,000	9,000	9,000	9,000
Is income less than threshold?	Yes	No	No	No
If Yes, tax is zero; if No, compute tax below				
Regular Tax Calculation				
X Taxable social security (= N)	0	0	2,875	8,000
Y Taxable pensions (= R)	0	0	2,000	6,000
Z Other income (= C)	6,000	18,000	13,500	20,000
AA Iowa Net Income: Line 26 of 1040	6,000	18,000	18,375	34,000
AB Less: Federal tax deduction	1,825	1,825	2,920	5,750
AC Less: Standard Deduction (2006 level)	1,650	1,650	1,650	1,650
AD Taxable Income: line 42 of 1040 (AA - AB - AC)	2,525	14,525	13,805	26,600
AE Income Tax (2006 rates)**	14	543	499	1,309
AF Exemption Credits (regular + senior)	60	60	60	60
AG Net Regular Tax:	0	483	439	1,249

*Unmarried persons who are not a head of household or surviving spouse

**Calculated using 2006 tax rate schedule; will vary slightly from amounts in tax table

Iowa Income Tax For Married Couples Filing Separately* Age 65 and Older
 Social Security fully exempt (tax year 2014); tax based on 2006 rates

	1			2			3		
	Filer	Spouse	Total	Filer	Spouse	Total	Filer	Spouse	Total
Income from All Sources									
A Social Security benefits	4,000	4,000	8,000	10,000	10,000	20,000	18,000	18,000	36,000
B Pensions, IRAs, annuities	2,000	2,000	4,000	1,500	2,500	4,000	8,000	8,000	16,000
C Other (interest, dividends, wages)	7,000	7,000	14,000	13,000	13,000	26,000	10,000	10,000	20,000
D Total	13,000	13,000	26,000	24,500	25,500	50,000	36,000	36,000	72,000
Taxable Social Security Benefits									
E One-half of Social Security benefits			4,000			10,000			18,000
F All other income (B + C)			18,000			30,000			36,000
G Provisional income			22,000			40,000			54,000
H Exempt amount			32,000			32,000			32,000
I Excess provisional income (G - H)			0			8,000			22,000
J One-half of excess provisional income			0			4,000			11,000
K Taxable social security benefits under prior law (lesser of E or J)			0			4,000			11,000
L Applicable phase-out percentage			100%			100%			100%
M Additional exemption under SF2408 (K times L)			0			4,000			11,000
N Taxable social security benefits (K - M)			0			0			0
Taxable Pensions & Annuities									
O Each spouse's share of total pensions	50%	50%		38%	63%		50%	50%	
P Maximum exclusion (prorated for couples)	6,000	6,000	12,000	4,500	7,500	12,000	6,000	6,000	12,000
Q Pensions, IRAs, annuities (= B)	2,000	2,000		1,500	2,500		8,000	8,000	
R Exclusion (smaller of P, Q)	2,000	2,000		1,500	2,500		6,000	6,000	
S Taxable portion (Q - R)	0	0		0	0		2,000	2,000	
Low Income Exemption									
T Social security income exempted by SF2408 (M)	0	0	0	2,000	2,000	4,000	5,500	5,500	11,000
U All other income (B + C)	9,000	9,000	18,000	14,500	15,500	30,000	18,000	18,000	36,000
V Modified Adjusted Gross Income (MAGI)	9,000	9,000	18,000	16,500	17,500	34,000	23,500	23,500	47,000
W Threshold			32,000			32,000			32,000
X Excess income (MAGI above threshold)			0			2,000			15,000
Is net income less than threshold?			Yes			No			No
If Yes, tax is zero; if No, compute tax below									
Regular Tax Calculation									
Y Taxable social security (= N)	0	0		0	0	0	0	0	0
Z Taxable pensions (= S)	0	0		0	0		2,000	2,000	
AA Other income (= C)	7,000	7,000		13,000	13,000		10,000	10,000	
AB Iowa Net Income	7,000	7,000		13,000	13,000		12,000	12,000	
AC Less: Federal tax deduction	949	949	1,898	2,818	2,933	5,750	4,140	4,140	8,280
AD Less: Standard Deduction (2006 level)	1,650	1,650		1,650	1,650		1,650	1,650	
AE Taxable Income: line 42 on 1040 (AB - AC - AD)	4,401	4,401		8,533	8,418		6,210	6,210	
AF Regular Income Tax (2006 rates)**	58	58	116	227	222	449	123	123	245
Alternate Tax Calculation									
AG Maximum tax rate			8.98%			8.98%			8.98%
AH MAGI in excess of threshold (= X)			0			2,000			15,000
AI Alternate tax (AG x AH)			0			180			1,347
Actual Tax									
AJ Smaller of regular tax (AF) or alternate tax (AI)			0			180			245
AK Exemption Credits (regular + senior)	60	60	120	60	60	120	60	60	120
AL Net Tax:			0			60			125

*Also applies to unmarried persons who are not a head of household or surviving spouse

**Calculated using 2006 tax rate schedule; will vary slightly from amounts in tax table

Iowa Income Tax For Married Couples Filing Separately* Age 65 and Older

Current law; tax based on 2006 rates

	1			2			3		
	Filer	Spouse	Total	Filer	Spouse	Total	Filer	Spouse	Total
Income from All Sources									
A Social Security benefits	4,000	4,000	8,000	10,000	10,000	20,000	18,000	18,000	36,000
B Pensions, IRAs, annuities	2,000	2,000	4,000	1,500	2,500	4,000	8,000	8,000	16,000
C Other (interest, dividends, wages)	7,000	7,000	14,000	13,000	13,000	26,000	10,000	10,000	20,000
D Total	13,000	13,000	26,000	24,500	25,500	50,000	36,000	36,000	72,000
Taxable Social Security Benefits									
E One-half of Social Security benefits			4,000			10,000			18,000
F All other income (B + C)			18,000			30,000			36,000
G Provisional income			22,000			40,000			54,000
H Exempt amount			32,000			32,000			32,000
I Excess provisional income (G - H)			0			8,000			22,000
J One-half of excess provisional income			0			4,000			11,000
N Taxable social security benefits (lesser of E or J)			0			4,000			11,000
Taxable Pensions & Annuities									
O Each spouse's share of total pensions	50%	50%		38%	63%		50%	50%	
P Maximum exclusion (prorated for couples)	6,000	6,000	12,000	4,500	7,500	12,000	6,000	6,000	12,000
Q Pensions, IRAs, annuities (= B)	2,000	2,000		1,500	2,500		8,000	8,000	
R Exclusion (smaller of P, Q)	2,000	2,000	4,000	1,500	2,500		6,000	6,000	
S Taxable portion (Q - R)	0	0	0	0	0	0	2,000	2,000	4,000
Low Income Exemption									
V Net Income: Line 26 of 1040 (C + N + S)			14,000			30,000			35,000
W Threshold			13,500			13,500			13,500
Is income less than threshold?			No			No			No
If Yes, tax is zero; if No, compute tax below									
Regular Tax Calculation									
Y Taxable social security (= N)	0	0	0	2,000	2,000	4,000	5,500	5,500	11,000
Z Taxable pensions (= S)	0	0		0	0		2,000	2,000	
AA Other income (= C)	7,000	7,000		13,000	13,000		10,000	10,000	
AB Iowa Net Income: Line 26 of 1040	7,000	7,000		15,000	15,000		17,500	17,500	
AC Less: Federal tax deduction	949	949	1,898	2,818	2,933	5,750	4,140	4,140	8,280
AD Less: Standard Deduction (2006 level)	1,650	1,650		1,650	1,650		1,650	1,650	
AE Taxable Income: line 42 on 1040 (AB - AC - AD)	4,401	4,401		10,533	10,418		11,710	11,710	
AF Income Tax (2006 rates)**	58	58	116	317	312	629	370	370	741
Alternate Tax Calculation									
AG Maximum tax rate			8.98%			8.98%			8.98%
AH Net income plus exempt pension income (V + R)			18,000			30,000			35,000
AI Income in excess of threshold (AH - W)			4,500			16,500			21,500
AJ Alternate tax (AG x AI)			404			1,482			1,931
Actual Tax									
AK Smaller of regular tax (AF) or alternate tax (AJ)			116			629			741
AL Exemption Credits (regular + senior)	60	60	120	60	60	120	60	60	120
AM Net Tax:			0			509			621

*Also applies to unmarried persons who are not a head of household or surviving spouse

**Calculated using 2006 tax rate schedule; will vary slightly from amounts in tax table