

**VOLUME 7B, CHAPTER 24: “COMPUTATION OF WAGES SUBJECT TO
FEDERAL INCOME TAX WITHHOLDING (FITW)”**

SUMMARY OF MAJOR CHANGES

All changes are denoted by **blue font**.

Substantive revisions are denoted by an asterisk (*) symbol preceding the section, paragraph, table, or figure that includes the revision.

Unless otherwise noted, chapters referenced are contained in this volume.

Hyperlinks are denoted by **bold, italic, blue, and underlined font**.

The previous version dated **August 2015** is archived.

PARAGRAPH	EXPLANATION OF CHANGE/REVISION	PURPOSE
All	Updated chapter and format to comply with administrative instructions.	Revision
240101	Changed title from “Overview” to “Purpose” to comply with current administrative instructions.	Revision
240902	Deleted paragraph due to information not relevant to this chapter.	Deletion

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CHAPTER 24

**COMPUTATION OF WAGES SUBJECT TO FEDERAL INCOME TAX
WITHHOLDING (FITW)**

2401 GENERAL

***240101. Purpose**

The purpose of this chapter is to provide information on retired pay subject to FITW. FITW is based on payments actually or constructively paid, regardless of the date on which they are earned. Retired pay is paid constructively when it is credited to the account or set apart for a retiree so that he or she may draw on it at any time, although it is not actually reduced to possession. It must have been credited to or set apart for the retiree without any substantial limitation or restriction as to the time or manner of payment or condition under which it is to be made and brought within the retiree's control and disposition.

240102. Authoritative Guidance

The bibliography at the end of this chapter lists the authoritative references.

2402 RETIRED PAY SUBJECT TO FITW AND NOT SUBJECT TO FITW

240201. Gross Retired Pay Subject to FITW

Retired pay is income and constitutes wages subject to FITW, except as otherwise indicated in this chapter.

240202. Gross Retired Pay Not Subject to FITW

The gross retired pay of a member is not subject to FITW if the member's retired pay is computed only on the basis of percentage of disability, and the member is on the temporary or permanent disability retired lists, if:

A. On or before September 24, 1975, the member was entitled to receive retired pay computed on the basis of percentage of disability Title 26, United States Code (U.S.C.), [sections 104\(a\)\(4\) and 104\(b\)\(2\)\(A\)](#);

B. On September 24, 1975, he or she was a member of the Armed Forces (or Reserve Component thereof) or under a binding written commitment to become such a member (26 U.S.C. § 104(a)(4) and § 104(b)(2)(B)); or

C. The member receives disability retired pay because of a combat-related injury. The term "combat-related injury" means personal injury or sickness incurred as a direct result of armed conflict, or while engaged in extra hazardous service, or under conditions simulating war,

or caused by an instrument of war. This determination is made by the applicable Service at the time of discharge. See [Department of Defense Instruction \(DoDI\) 1332.18](#).

2403 EFFECT OF DISABILITY COMPENSATION AWARD ON FITW

A member is entitled to exclude the disability compensation, additional amount, and retroactive disability compensation from the taxable portion of retired pay.

240301. Disability Compensation

Disability compensation is the maximum amount that a member would be entitled to receive upon application to the Department of Veterans Affairs (VA).

240302. Additional Amount

An additional amount is the difference between a prospective VA disability compensation award and the amount excluded under section 2402.

240303. Retroactive Disability Compensation

The retroactive disability compensation is the amount of a VA disability compensation award not previously excluded from retired pay.

2404 GROSS PAY PARTIALLY TAXABLE

For members who are entitled to have their retired pay computed based on both percentage of disability and years of service, a portion of their retired pay may be subject to FITW. Any reduction of wages subject to FITW for disability retired pay must meet one of the conditions set forth in paragraph 240202.

240401. Post September 30, 1949

Compute the wages subject to FITW for members retired for disability on or after October 1, 1949, as follows:

A. If the member is placed on the Permanent Disability Retired List, subtract retired pay based on the percentage of disability from retired pay based on the years of service. The result of such subtraction is the amount of wages subject to FITW.

B. If the member is placed on the Temporary Disability Retired List, use one of these methods:

1. If the member's disability rating is 50 percent or more, compute as in subparagraph 240401.A.

2. If the member's disability rating is less than 50 percent and retired pay is computed based on years of service, subtract the amount of retired pay the member would have received if such pay were computed solely on the actual percentage of disability from the pay based on years of service, the result of the subtraction is the amount of wages subject to FITW.

3. If the member's disability rating is less than 50 percent and the member elects to receive disability retired pay based on the percentage of disability, the retired pay received is not subject to FITW.

240402. Before October 1, 1949

The wages subject to FITW for members who retired before October 1, 1949, fell into two categories. Such retired pay was either based on years of service and was fully taxable or it was based on disability and was nontaxable. Members retired for physical disability before October 1, 1949, were assigned a disability rating for purposes of computing retired pay entitlement under the provisions of the Career Compensation Act. These members could either continue to receive the nontaxable retired pay they were receiving on September 30, 1949, or elect to receive retired pay computed under the provisions of the Career Compensation Act based on the percentage of disability assigned or years of active service. If members chose to have their pay computed based on the Career Compensation Act, their wages subject to FITW were computed as described in paragraph 240202 or subparagraph 240401.A.

2405 FITW WAGE REDUCTIONS FROM DEDUCTIONS AND COLLECTIONS

Deductions and collections that reduce the amount of wages subject to FITW include participation in Retired Serviceman's Family Protection Plan (RSFPP), participation in Survivor Benefit Plan (SBP), and VA Disability Compensation.

240501. Participation in Retired Serviceman's Family Protection Plan (RSFPP)

The amount of the member's retired pay subject to FITW is reduced by the full amount of the RSFPP costs deducted from the member's retired pay in order to participate in the RSFPP. This deduction did not reduce taxable income until the tax laws were changed to permit a dollar-for-dollar reduction effective January 1, 1966. The tax implication for a member who pays for this protection by direct remittance is discussed in section 2409.

240502. Participation in Survivor Benefit Plan (SBP)

The amount of the member's retired pay subject to FITW is reduced by the full amount of the SBP costs deducted from the member's retired pay in order to participate in the SBP. The tax implication for a member who pays for this protection by direct remittance is discussed in section 2409.

240503. Veterans Affairs (VA) Disability Compensation

There is a waiver of military retired pay when a member receives disability compensation

or a pension from the VA.

Note: If a member is entitled to concurrent retirement and disability pay on or after January 1, 2014, the waiver provision does not apply.

A. If the member's gross retired pay is fully subject to FITW, subtract the amount of the VA waiver applied to wages. The VA waiver reduces the member's retired pay entitlement.

B. In the case of a member retired because of physical disability, reduce wages subject to FITW, if any, by the amount of the VA waiver applied or the portion of the member's retired pay based on the actual percentage of disability, whichever is greater.

2406 U.S. CITIZENS ABROAD

The retired pay of members who temporarily or permanently reside in a foreign country is subject to FITW as if they resided in the United States or its possessions. Thus, apply the withholding rules in section 2402.

2407 ARREARS OF PAY

See Chapter 30 for taxation policies that apply to deceased members and their beneficiaries.

2408 COLLECTION OF DELINQUENT TAXES

240801. Voluntary Withholding

A retiree may, with the consent of the Internal Revenue Service (IRS), have deductions made from his or her retired pay to satisfy a debt due to tax delinquency. The class T allotment has been designated to allow a member to make payments to [the IRS](#) in this manner.

240802. Involuntary Withholding

If a retiree neglects or refuses to pay his or her Federal income tax liability within 10 days after receiving notice of liability, the cognizant IRS District Director can collect the amount by placing a levy on the member's retired pay. The IRS is required to give the member 10 days' notice that a levy will be executed. This notice normally is included with the notification of liability. See Chapter 28.

2409 TAXABILITY OF SBP/RSFPP PREMIUMS

Premiums deducted from retired pay for SBP/RSFPP will reduce taxable retired pay.

2410 PROCESSING CORRECTION OF RECORDS CASES

If payment is made as the result of a correction of military records, that payment is processed as follows:

241001. Amounts Previously Paid and Reported

When amounts previously paid and reported as FITW wages are not subject to FITW as a result of the correction, the member is provided either a corrected IRS Form 1099-R, Distributions From Pension, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc., for the 3 calendar years before the year that the correction action is made or a letter citing the “before” and “after” amounts for each calendar year involved. The member may obtain a tax refund, if any is due, from the IRS based on his or her total tax liability for 3 years. In accordance with 52 Comp. Gen. 420 (1973), a claim for the refund of income taxes paid in years prior to the 3-year period may be treated as a claim for pecuniary benefits under [10 U.S.C. § 1552](#) and paid pursuant to the record correction.

241002. Retired Pay Subject to FITW

When the member’s retired pay is subject to FITW, the payment is reported as FITW wages from applicable current year appropriations reserved for such payment.

2411 TAXABILITY AND WITHHOLDING OF DISABILITY SEVERANCE PAY

See Volume 7A, Chapter 35.

2412 TAXABILITY OF RETIRED PAY FOR FLEET RESERVIST/FLEET MARINE CORPS RESERVIST NOT PHYSICALLY QUALIFIED FOR RETENTION IN THE FLEET RESERVE/FLEET MARINE CORPS RESERVE (FR/FMCR)

The retired pay of a member of the FR/FMCR who is transferred to the retired list, when found not physically qualified for retention in the FR/FMCR (as stated in Chapter 2, [subparagraph 020101.B](#)), is subject to FITW.

