AARP Public Policy Institute

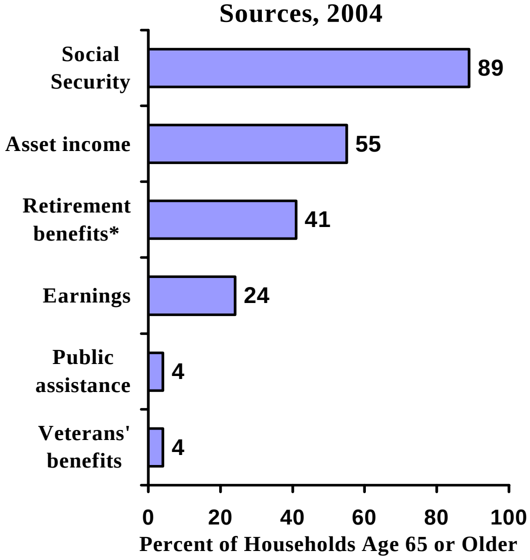
ISSUE BRIEF

STATE TAXATION OF SOCIAL SECURITY AND PENSIONS IN 2006

Introduction

The tax treatment of Social Security benefits and pension income by state governments is a critical concern for older Americans because these are two of their primary sources of income. As shown in Figure 1, in 2004, nearly 9 out of 10 households age 65 or older[1] received Social Security benefits, and about 2 in 5 (41 percent) received other retirement income benefits.

Figure 1
Percentage of Households Age 65 or Older Receiving Social Security Benefits and Other Income Sources, 2004



*Includes private pensions and annuities; government employee pensions; Railroad Retirement; and IRA, Keogh, and 401(k) payments.
Source: Social Security Administration, Office of Policy, Office of Research, Evaluation, and Statistics, *Income of the Aged Chartbook, 2004* (Washington, DC: U.S. Government Printing Office, September 2006), p.3.

In 2006 the percentage of income from different sources for persons age 65 or older was 39 percent from Social Security benefits, 16 percent from pension income (company or union pension, federal government retirement, military retirement, and Railroad Retirement), 24 percent from earnings, and 13 percent from dividends and interest.[2] At the upper ends of the income scale, people relied more on pension income; at lower income levels, people were more dependent upon Social Security benefits (see Table 1). Social Security benefits made up at least half of total income for 66 percent of Social Security beneficiaries in 2004.[3]

Since 1984, the federal government has taxed a portion of the Social Security and Railroad Retirement benefits of higher-income beneficiaries. Social Security benefits are taxed if the "provisional income"[4] of beneficiaries exceeds $25,000 for single persons or $32,000 for married couples filing jointly.

From 1984 to 1993, if provisional income exceeded the $25,000 or $32,000 thresholds, the amount of benefits subject to taxes was the lesser of:

(a) One-half of the excess of provisional income over the threshold amount, or

(b) One-half of Social Security benefits and Railroad Retirement Social Security equivalent benefits.

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[1] Households (which the Social Security Administration calls aged units) can be a married couple living together with either the husband or wife age 65 or older, or a person age 65 or older who does not live with a spouse.

[2] Bureau of the Census, Current Population Survey (CPS), March 2007 (Washington, DC: Bureau of the Census, 2007). The CPS is conducted by the Bureau of the Census for the Bureau of Labor Statistics.

[3] Social Security Administration, Office of Policy, Office of Research, Evaluation and Statistics, *Income of the Aged Chartbook, 2004* (Washington, DC: U.S. Government Printing Office, September 2006), p.4.

[4] Provisional income in tax year 2006 was defined as the sum of (1) federal adjusted gross income (AGI) (excluding Social Security benefits, the deduction for student loan interest, and the deduction for domestic production activities), (2) tax-free interest income, and (3) one-half of Social Security benefits.

Table 1
Shares of 2006 Aggregate Income for Persons Age 65 or Older by Income Range (in percents)

Income Sources	First Quartile Up to $9,762	Second Quartile $9,762 to $16,397	Third Quartile $16,397 to $29,586	Fourth Quartile $29,586+	All Persons Age 65 or Older
Social Security Benefits	85%	81%	57%	20%	39%
Pension Income	2	6	17	20	16
Dividends and Interest	5	6	9	16	13
Earnings	1	3	10	35	24
Other Income	7	4	7	9	8
Total	100	100	100	100	100

Source: Bureau of the Census, *Current Population Survey, March 2007* (Washington, DC: Bureau of the Census, 2007).

However, in 1994, the percentage of Social Security benefits that were taxable increased for some higher-income taxpayers (as described below under the Omnibus Budget Reconciliation Act of 1993 [OBRA 93]).

Because the income thresholds of $25,000 and $32,000 have not been indexed for inflation, as incomes increase each year, a greater proportion of Social Security beneficiaries is likely to pay taxes on their benefits. To illustrate, in tax year 1984, about 8 percent of beneficiaries paid taxes on their benefits; whereas, the Congressional Budget Office (CBO) estimates that about 39 percent of beneficiaries had some benefits taxed in 2003 (using 2000 population and income data).[5]

Moreover, in tax year 2004, about 58 percent of all Social Security benefits reported on the federal income tax form were taxable.[6] These data refer only to taxpayers who filed income tax returns. About half of households with one person age 65 or older either were not required to file a return or had no tax liability.

The Omnibus Budget Reconciliation Act of 1993 (OBRA 93)

Since 1994, some Social Security beneficiaries have paid even higher federal income taxes than before on their Social Security benefits because of a provision of OBRA 93.

There is no change in taxable Social Security due to OBRA 93 if provisional income is between $25,000 and $34,000 (single filers) or between $32,000 and $44,000 (married, filing jointly). At these income levels, up to 50

5 U.S. House of Representatives, Committee on Ways and Means, *2004 Green Book* (Washington, DC: U.S. Government Printing Office, March 2004), p.1-25.

6 Special Tabulation of Tax Year 2004 Individual Complete Report File, Statistics of Income Division, IRS, August 2007.

percent of the Social Security benefits may be taxed.

However, OBRA 93 increased the percentage of benefits that may be taxed from 50 percent to 85 percent for those whose provisional incomes are greater than $34,000 (single filers) or $44,000 (married, filing jointly) (see Tables 2 and 3).

Table 2
Maximum Percentage of Social Security Benefits That May Be Taxed for Single Households (in percents)

Provisional Incomes	Pre-OBRA 93	Post-OBRA 93
$0 to $25,000	0%	0%
$25,001 to $34,000	50	50
$34,001+	50	85

Table 3
Maximum Percentage of Social Security Benefits That May Be Taxed for Married Households Filing Jointly (in percents)

Provisional Incomes	Pre-OBRA 93	Post-OBRA 93
$0 to $32,000	0%	0%
$32,001 to $44,000	50	50
$44,001+	50	85

For taxpayers whose provisional incomes exceed the higher thresholds, the amount of benefits subject to tax is the lesser of:

(a) 85 percent of Social Security benefits and Railroad Retirement Social Security equivalent benefits, or

(b) 85 percent of income over the higher OBRA 93 threshold, plus the smaller of

(1) $4,500 (single filers), $6,000 (married, filing jointly), or

(2) 50 percent of the Social Security benefit amount.[7]

Like the pre-OBRA 93 thresholds, none of these new thresholds are indexed for inflation. In 2001, approximately 6.7 million tax returns were filed by persons who were required to pay higher Social Security federal income taxes due to OBRA 93.[8]

Many states' income taxes are directly tied to the federal tax code because their taxable

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[7] Laurel Beedon and Alison Shelton, *Will Your Social Security Benefits Be Taxed?* (Washington, DC: AARP, August 2001), p.1.

[8] Estimate based on the AARP-Barents Group Individual Income Tax Model.

base begins with federal adjusted gross income or federal taxable income. Therefore, changes in the income tax base at the federal level, such as those resulting from the inclusion of Social Security benefits in income, will automatically result in higher or lower state income taxes unless state legislatures enact provisions offsetting the federal action.

State Taxation of Social Security Benefits

Currently, 26 of the 41 states (and the District of Columbia) that have broad-based personal income taxes do not tax Social Security benefits. The 15 states that tax Social Security benefits are Colorado, Connecticut, Iowa, Kansas, Minnesota, Missouri, Montana, Nebraska, New Mexico, North Dakota, Rhode Island, Utah, Vermont, West Virginia, and Wisconsin.

The impact of higher state taxes on Social Security benefits among the 15 states that tax the benefits has been lessened because of actions some of the states have taken. Wisconsin, Iowa, and Connecticut did not pass on the higher OBRA 93 Social Security taxes. Wisconsin and Iowa require beneficiaries to pay income tax on up to 50 percent of Social Security benefits based on the original thresholds of $25,000 for single filers and $32,000 for married couples filing jointly.

Connecticut subjects only taxpayers whose federal adjusted gross income is $50,000 or more (single filers) or $60,000 or more (married, filing jointly) to taxation of their Social Security benefits. For those taxpayers who are affected, only up to a maximum of 25 percent of benefits can be taxed.

Starting in 2008, Wisconsin will no longer tax Social Security benefits. Iowa is phasing out the taxation of Social Security benefits from 2007 to 2014.

Missouri is phasing out the taxation of Social Security benefits from 2007 to 2012 through income deductions for taxpayers age 62 and older whose adjusted gross income equals $85,000 or less (single filers) or $100,000 or less (married, filing jointly). These deductions are reduced by one dollar for each dollar that a taxpayer's adjusted gross income exceeds these income thresholds.

Colorado, Minnesota, New Mexico, Utah, and West Virginia allow Social Security benefits to be deducted as part of a retirement income exemption (as described in the notes in Table 2).

Beneficiaries in Iowa, Missouri, Montana, North Dakota, and Utah who pay more in federal income taxes on Social Security benefits will pay less in state taxes, since federal taxes are either fully (Iowa, North Dakota) or partially (Missouri, Montana, and Utah) deductible from taxable income. However, only taxpayers who itemize can deduct federal taxes in Montana, and only those who use the ND-2 form can deduct federal taxes in North Dakota.

Some beneficiaries in Montana also get an exclusion from Social Security benefits based on differences between the federal and Montana tax bases.

State Taxation of Pension Income in 2006

Relevant Supreme Court Cases

Prior to 1989, many states fully exempted state pensions from income taxation. In March 1989, the U.S. Supreme Court's *Davis v. Michigan* decision (489 U.S. 803) ruled that states must treat federal pensioners at least as well as they treat their state pensioners. The Court expanded this decision in April 1992, ruling in *Barker v. Kansas* (503 U.S. 594) that states are prohibited from taxing the pension benefits of U.S. military retirees while exempting the pensions of state and local government retirees.

An issue not addressed by *Davis* was whether states affected by that decision must give refunds to federal retirees who had paid taxes under laws that had been struck down by that decision. In June 1993, the U.S. Supreme Court gave its first direct ruling on this matter in *Harper v. Virginia Department of Taxation* (509

U.S. 86). The Court did not require states to pay refunds, but ruled that they would have to "provide relief consistent with federal due process principles" if state "predeprivation procedures" were unavailable.

Predeprivation procedures are any means by which state governments allow taxpayers to contest a tax before it is paid. This relief could involve refunds. All affected states have settled with or have paid affected federal retirees.

<u>State Treatment of Pension Income in 2006</u>

Most states that impose an income tax exempt at least part of pension income from taxable income. Various types of pension income (private, military, federal civil service, and state or local government) are often treated differently for tax purposes.

Table 4 summarizes the state income tax treatment of pension income for tax year 2006 for the 41 states and the District of Columbia that have a broad-based income tax. The table describes pension exemptions for *single filers* only.

In Table 4, the final column (income restrictions) reveals only whether pensioners' incomes preclude them from receiving *any* state exemption; it does not indicate whether exemption *amounts* are reduced based on income levels. The notes to Table 2 give more detail about other state retirement income exclusions and credits (e.g., exclusions based on *all* retirement income, not just pension income), other filing status information, and age and income restrictions (both for pension income and other retirement income).

Only three states—Illinois, Mississippi, and Pennsylvania—fully exempt all public and private pensions from taxation.

Seven states fully exempt public pensions (federal civil service; military; and state and local government pensions) from taxes, but do not fully exempt private pensions. These states are Alabama, Hawaii, Kansas, Louisiana, Massachusetts, Michigan, and New York.[9]

In Hawaii, employee contributions and pension earnings are exempt from tax in noncontributory private pensions (where contributions are only from employers). However, private pensions involving employee contributions are partially taxable with only earnings attributable to employee contributions being subject to tax. Alabama fully exempts public pensions, but exempts only those private pensions that are defined benefit plans.

Twelve states and the District of Columbia offer pension exemptions that vary by type, with public pensions generally being treated more favorably than private pensions.[10]

Many states offer at least partial exemptions from state taxes for some types of pensions. Ten states specifically offer identical partial exemptions for public and private pensions. These are Arkansas, Colorado, Delaware (under age 60), Iowa, Maine, Missouri, Montana, Oklahoma, South Carolina, and Utah (under age 65).

Delaware (age 60 and older), Georgia, Minnesota, New Mexico, Utah (age 65 and older), Virginia, and West Virginia provide the same partial exemptions for all income sources, not just for pension income (both public and private).

Five states (California, Connecticut, Nebraska, Rhode Island, and Vermont) allow no exemptions or tax credits for pension and other retirement income that is counted in federal adjusted gross income.

Most in-state government pensions are taxed the same as out-of-state government pensions. However, Arizona, Idaho, Kansas, Louisiana,

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[9] Of the seven states, Kansas, Louisiana, Massachusetts, Michigan, and New York fully exempt in-state government pensions but not out-of-state government pensions.

[10] These states are Arizona, Idaho, Indiana, Kansas, Kentucky, Louisiana, Massachusetts, Michigan, New York, North Carolina, North Dakota, and West Virginia.

Massachusetts, Michigan, and New York provide greater tax relief for in-state government pension plans than for those that are out-of-state. The District of Columbia also provides greater tax relief for District of Columbia government pensions than for state government pensions.

Michigan and Massachusetts do not tax residents who receive public pensions from other states if those states do not tax out-of-state government pensions of residents who were Michigan or Massachusetts employees.

Pension and other income exemptions are reduced dollar for dollar by Social Security and/or Railroad Retirement benefits in Idaho, Indiana (for federal civil service pensioners only), Maine, Maryland, Minnesota, and North Dakota.

<u>Age Limitations</u>

Thirty-six states and the District of Columbia offer exemptions or tax credits primarily for pension and other retirement income. Fifteen of those states and the District of Columbia require pensioners to be a minimum age (varying from 50 to 65) to receive a tax exemption or credit.[11]

<u>Income Limitations</u>

Tax exemption amounts or tax credits for pension and other retirement income vary with taxpayer income in seven of the states (Minnesota, Missouri, Montana, New Mexico, Ohio, Oregon, and Utah).

Even though the pension exemption amount does not vary with income in New Jersey and Oklahoma, pensioners are ineligible for the exemption if their income exceeds certain income limits ($100,000 for single filers in New Jersey and $37,500 for single filers in Oklahoma).

<u>Taxation of Nonresident State Pensions</u>

Starting in tax year 1996, states were prohibited from taxing distributions from nonresident pension and other retirement income plans because of Public Law No. 104-95 (passed by Congress in December 1995). Most retirement plans of nonresidents are now exempt because of this law. Examples of nonresident retirement income that is still taxable include nonqualified plans that are periodically paid out over fewer than 10 years and various forms of compensation (such as stock options, severance pay lump sums, and incentive bonuses) that are typically granted to highly compensated employees.

Former residents who earn taxable nonqualified pension income must file nonresident income tax forms. In most states with an income tax, that tax can be credited against the income tax owed to the state of former residence.

The tax treatment of lump-sum distributions varies considerably by state, but most offer some kind of income averaging for tax purposes.

State Taxation of IRAs in 2006

Three states (New Jersey, Massachusetts, and Pennsylvania) do not allow IRA contributions to be deducted from taxable income. Of the three, only Pennsylvania does not tax IRA earnings of taxpayers age 59 1/2 years or older, since these earnings are treated like pension income, which is tax exempt.

Conclusions

Two of the primary sources of income for persons age 65 and older are Social Security benefits and pension income. Most states provide more favorable income tax treatment of Social Security benefits and pension income than the federal government.

Even though some taxpayers may pay a federal tax on Social Security benefits, many of them do not pay a state tax because only 15 states and the District of Columbia levy an

[11] These states are Colorado, Georgia, Idaho, Indiana, Iowa, Louisiana, Maryland, Minnesota, New Jersey, New Mexico, New York, North Dakota, Oregon, Pennsylvania, and Virginia.

income tax on Social Security benefits. Moreover, in many cases, fewer benefits are taxed by the 15 states than by the federal government.

Most states with a broad-based income tax exempt at least part of pension income from taxation. In addition, many of these states tax public pensions more favorably than private pensions resulting in inequities between the taxation of public and private pensions.

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Table 4
State Income Tax Treatment of Social Security Benefits and Pension Income, 2006
(single filers)

		Exemption by Pension Type					
State	Is Social Security Tax Exempt?	Private Exemption	Military Exemption	Federal Exemption	State and Local Exemption	Age Minimum for Pension Exclusions?	Income Restrictions for Pension Exclusions?
Alabama	Yes	None/Full	Full	Full	Full	No	No
Arizona	Yes	None	$2,500	$2,500	$2,500	No	No
Arkansas	Yes	$6,000	$6,000	$6,000	$6,000	No	No
California	Yes	None	None	None	None	N/A	N/A
Colorado	No	$24,000/$20,000	$24,000/$20,000	$24,000/$20,000	$24,000/$20,000	Yes	No
Connecticut	No	None	None	None	None	N/A	N/A
Delaware	Yes	$12,500/$2,000	$12,500/$2,000	$12,500/$2,000	$12,500/$2,000	No	No
District of Columbia	Yes	None	$3,000	$3,000	$3,000	Yes	No
Georgia	Yes	$25,000	$25,000	$25,000	$25,000	Yes	No
Hawaii	Yes	Full/Part	Full	Full	Full	No	No
Idaho	Yes	None	$24,636	$24,636	$24,636	Yes	No
Illinois	Yes	Full	Full	Full	Full	No	No
Indiana	Yes	None	$2,000	$2,000	None	Yes	No
Iowa	No	$6,000	$6,000	$6,000	$6,000	Yes	No
Kansas	No	None	Full	Full	Full	No	No
Kentucky	Yes	$41,110	---------------------------- See notes -----------------------			No	No
Louisiana	Yes	$6,000	Full	Full	Full	Yes	No

Table 4
State Income Tax Treatment of Social Security Benefits and Pension Income, 2006
(single filers)
(continued)

State	Is Social Security Tax Exempt?	Private Exemption	Military Exemption	Federal Exemption	State and Local Exemption	Age Minimum for Pension Exclusions?	Income Restrictions for Pension Exclusions?
		Exemption by Pension Type					
Maine	Yes	$6,000	$6,000	$6,000	$6,000	No	No
Maryland	Yes	$22,600	$22,600 to $27,600	$22,600	$22,600	Yes	No
Massachusetts	Yes	None	Full	Full	Full	No	No
Michigan	Yes	$40,920	Full	Full	Full	No	No
Minnesota	No	-- See notes --------------------------------------				Yes	Yes
Mississippi	Yes	Full	Full	Full	Full	No	No
Missouri	No	$6,000	$6,000	$6,000	$6,000	No	Yes
Montana	No	$3,600	$3,600	$3,600	$3,600	No	Yes
Nebraska	No	None	None	None	None	N/A	N/A
New Jersey	Yes	$15,000	Full	$15,000	$15,000	Yes	Yes
New Mexico	No	-- See notes --------------------------------------				Yes	Yes
New York	Yes	$20,000	Full	Full	Full	Yes	No
North Carolina	Yes	$2,000	Full/$4,000	Full/$4,000	Full/$4,000	No	No
North Dakota	No	None	$5,000	$5,000	$5,000/ None	Yes	No
Ohio	Yes	-- See notes --					
Oklahoma	Yes	$10,000	$10,000	$10,000	$10,000	No	Yes
Oregon	Yes	-- See notes --					

Table 4
State Income Tax Treatment of Social Security Benefits and Pension Income, 2006
(single filers)
(continued)

State	Is Social Security Tax Exempt?	Exemption by Pension Type: Private Exemption	Military Exemption	Federal Exemption	State and Local Exemption	Age Minimum for Pension Exclusions?	Income Restrictions for Pension Exclusions?
Pennsylvania	Yes	Full	Full	Full	Full	See notes	No
Rhode Island	No	None	None	None	None	N/A	N/A
South Carolina	Yes	$3,000/ $10,000	$3,000/ $10,000	$3,000/ $10,000	$3,000/ $10,000	No	No
Utah	No	$4,800/$7,500	$4,800/$7,500	$4,800/$7,500	$4,800/$7,500	No	Yes
Vermont	No	None	None	None	None	N/A	N/A
Virginia	Yes	-- See notes --------------------------------------				Yes	Yes
West Virginia	No	None	$22,000	$2,000	Full/$2,000	No	No
Wisconsin	No	None	Full	None/Full	None/Full	No	No

Sources (for table and accompanying notes): 2006 state income tax forms and telephone survey of state revenue offices.

Notes:

N/A stands for not applicable.

Seven states—Alaska, Florida, Nevada, South Dakota, Texas, Washington, and Wyoming—are excluded because they have no personal income tax.

Two states—New Hampshire and Tennessee—are excluded because they have limited income taxes.

Alabama—Private defined benefit pensions are tax-exempt. All out-of-state government pensions are tax-exempt if they are defined benefit plans.

Arizona—All out-of-state government pensions are fully taxed.

Arkansas—The total exemption from all pension plans cannot exceed $6,000 per taxpayer. The exemption refers to income from public or private retirement systems, plans, or programs. Distributions from Simplified Employee Pension (SEP) plans do not qualify. However, IRA distributions can be included as part of the $6,000 exemption if a taxpayer is age 59 ½ or older. All out-of-state government pensions also qualify for the $6,000 exemption. Persons age 65 or older who do not qualify for the $6,000 deduction qualify for a $20 tax credit per taxpayer.

California—All out-of-state government pensions are fully taxed.

Colorado—Pensioners age 55 to 64 qualify for a $20,000 pension and annuity exemption; pensioners age 65 or older qualify for a $24,000 pension and annuity exemption. The exemptions pertain to periodic payments received as a result of: personal services performed prior to retirement, contributions to retirement plans that were tax-deferred, lump-sum distributions from pension or profit-sharing plans, IRA distributions, self-employed retirement account distributions, annuities, and federally taxable Social Security benefits. All out-of-state government pensions qualify for the pension exemptions.

Connecticut—All out-of-state government pensions are fully taxed. Starting in tax year 2008, military pensioners are eligible for a 50 percent exclusion on their federal taxable military pension.

Delaware—Persons under age 60 receive a $2,000 pension exemption; persons age 60 or older receive a $12,500 retirement exemption. The $12,500 retirement exemption covers qualified retirement plans (such as IRA distributions, 401(k) plans, Keogh plans, and government deferred compensation [section 457] plans). In addition, the exemption covers dividends, capital gains, interest, and net rental income from real property. Out-of-state government pensions qualify for the pension and retirement exemptions.

District of Columbia—Taxpayers age 62 or older qualify for the $3,000 exemption. The exemption covers military retired pay, pension income, and annuity income from the District of Columbia government or the federal government. All state government pensions are fully taxed.

Georgia—Taxpayers who are age 62 or older or are permanently disabled can claim retirement income exemptions (including pension income, IRA distributions, interest, dividends, alimony, and capital gains) for a maximum exemption of $25,000 per taxpayer. Taxpayers can exempt up to $4,000 of earned income towards the $25,000 exemption. The $25,000 exemption will increase to $30,000 in tax year 2007 and to $35,000 for tax year 2008 and thereafter. All out-of-state government pensions are eligible for the $25,000 exemption.

Hawaii—Private defined benefit pensions are exempt as are other employer-funded plans (such as profit-sharing and defined contribution plans). Private pensions featuring employee contributions are partially taxable; only earnings attributable to employee contributions are taxable. Public pension income or annuities are exempt. All out-of-state government pensions are tax-exempt.

Idaho—Pensioners must be age 65 or older, or age 62 or older and disabled, to qualify for the public pension exemption. Public pension exemption amounts are $24,636 (single filers) and $36,954 (married, filing jointly). These amounts are adjusted annually according to the maximum worker's retirement benefit under Social Security. The exemption amounts are reduced by the amount of Social Security and Railroad Retirement benefits received. Allowable state/local pension exemptions are pensions from a city's police retirement fund or from the state's retirement fund for fire fighters. Out-of-state government pensions are fully taxed.

Illinois—Exempt pension/retirement income includes qualified employee benefit plans, simplified employee pension (SEP) plans, IRA distributions, 401(k) plans, government retirement or government disability plans, Railroad Retirement income, lump-sum distributions of appreciated employer securities, and early distributions from qualified plans and IRAs. All out-of-state government pensions are tax-exempt.

Indiana—Federal civil service pensioners must be age 62 or older to claim the $2,000 pension exemption, and it is offset by the Social Security and Railroad Retirement benefits received. Military pensioners must be age 60 or older to claim the exemption. Out-of-state pensions are fully taxed.

Iowa—Taxpayers age 55 or older or disabled can claim an exemption of $6,000 (single filers) or $12,000 (married, filing jointly) from pensions, annuities, self-employed retirement plans, deferred compensation, IRA distributions, or other retirement plan benefits. Out-of-state government pensions qualify for the exemptions.

Kansas—Exempt public pension income includes federal civil service and military pensions, Kansas government pensions, and lump-sum distributions from the Kansas Public Employee's Retirement System (KPERS). All out-of-state government pensions are fully taxed.

Kentucky—Kentucky state and local employees as well as federal employees retiring before January 1, 1998, receive a full exemption of their public pensions. Those retiring after that date receive an exemption of their public pensions based on the amount of the individual's service time prior to January 1, 1998, compared to his or her total service time. Both out-of-state and public pensioners are eligible for at least a $41,110 exemption. Exempt public pensions are federal pensions, Kentucky state and local pensions, Railroad Retirement benefits, and disability pension income. Exempt private pension income includes defined benefit pensions, IRA distributions, 401(k) distributions, annuities, and disability retirement income.

Louisiana—Taxpayers must be age 65 or older to qualify for the $6,000 (single filers) or $12,000 (married, filing jointly with both spouses age 65 or older) private pension/retirement exemption. The private retirement exemption pertains to pensions and annuity income. Out-of-state government pensioners qualify for the private pension/retirement exemption.

Maine—The $6,000 exemption for non-military pensions is reduced by taxable and nontaxable Social Security and Railroad Retirement benefits. Eligible qualified pension plans that are covered by the exemption include those under Internal Revenue Code section 401(a) (including the Savings Incentive Match Plan for Employees [SIMPLE]), section 403 (annuities), and section 457(b) (state and local government/tax-exempt organizations/eligible deferred compensation plans). Distributions from IRAs (including SIMPLE retirement accounts),simplified employee pension (SEP) plans, and benefits from ineligible deferred compensation plans *do not* qualify for the exemption. Out-of-state government pensions are eligible for the $6,000 exemption.

Maryland—Pensioners must be age 65 or older and/or totally disabled to qualify for up to a $22,600 exemption, which is reduced by Social Security and federal Railroad Retirement benefits. Exempt income includes pensions, annuities, or endowment income from employee retirement systems (not including IRA distributions, Keogh plans, or deferred compensation plans). The exemption amount changes annually according to the maximum benefit received under the Social Security Act. Out-of-state government pensions qualify for the $22,600 exemption. Military pensioners may be eligible for an exemption of up to $5,000 for military retirement income. Any part of military retirement income that is applied toward the $5,000 exemption cannot be used toward the $22,600 pension exemption.

Massachusetts—Pension income from other state or local governments that do not tax pension income from Massachusetts public employees is exempt from taxable income. Other states or local governments must have a specific deduction, exclusion, or exemption for pension income that applies to Massachusetts state or local contributory public pension plans or have no income tax.

Michigan—Private pension income is tax exempt up to $40,920 (single filers) or $81,840 (married, filing jointly). The maximum allowable exemptions for private pensions are reduced by the amount of any public pension deduction claimed. Examples of exempt income are pension plans that define eligibility for retirement and set contribution and benefit amounts in advance, qualified retirement plans for the self-employed, IRA distributions (received after age 59 1/2), and qualified life annuities for taxpayers age 65 or older. Taxpayers age 65 or older may deduct interest, dividends, and capital gains up to $9,128 (single filers) or $18,255 (married, filing jointly). These deductions are reduced by any pension exemption taken. Michigan has reciprocal agreements with other states. That is, if another state does not tax out-of-state government pensions of former Michigan state or local government employees who are now citizens of the other state, then Michigan will not tax Michigan residents who receive public pensions from those other states. Otherwise, out-of-state government pensions qualify for the same exemptions as private pensions.

Minnesota—Taxpayers age 65 or older or those who are permanently disabled (receiving federal disability income) who qualify can be exempt from *any* income source (including taxable Social Security benefits)— $9,600 (single filers) or $12,000 (married, filing jointly)— less the following: nontaxable Social Security benefits, Railroad Retirement benefits, nontaxable veterans' pensions and benefits, and one-half of federal adjusted gross income (AGI) of more than $14,500 (single filers or married, filing jointly if one spouse is under age 65 and one is age 65 or older) or $18,000 (married, filing jointly if both spouses are age 65 or older). To qualify for the above exemptions, the AGI of single filers must be less than $33,700, and Railroad Retirement benefits and nontaxable Social Security benefits must be less than $9,600. For married taxpayers filing jointly (in which both spouses are age 65 or older or are disabled), the AGI must be less than $42,000, and Railroad Retirement benefits and nontaxable Social Security benefits must be less than $12,000.

Mississippi—Retirement income that qualifies for the exemption includes income from public pensions, annuities, and deferred compensation plans. Out-of-state government pensions are tax-exempt.

Missouri—Taxpayers qualify for the $6,000 exemption if their Missouri adjusted gross income (not including taxable Social Security benefits) is less than $25,000 per year (single filers) or $32,000 (married, filing jointly). Exemptions are phased out for taxpayers whose income is greater than $31,000 (single filers) or $44,000 (married, filing jointly, assuming that both spouses are receiving pensions). Out-of-state government pensioners qualify for the $6,000 exemption. Taxpayers cannot receive more than a combined exemption of $6,000 from both private and public pension income.

Starting in 2007, taxpayers receiving public pensions can deduct $6,000 or 20 percent of their pension income (whichever is greater). The 20 percent figure will gradually increase annually from 20 percent in 2007 to 100 percent in 2012. The deduction amount is reduced by one dollar for every dollar that a taxpayer's adjusted gross income exceeds $85,000 (single filers) or $100,000 (married, filing jointly). The deduction amount cannot exceed the maximum Social Security benefit. In addition, the deduction amount is reduced by any Social Security benefits that are untaxed by the federal government. Out-of-state government pensioners also qualify for the higher deduction amount.

Montana—The $3,600 exemption pertains to qualified pensions, annuities, Keogh plans, Simplified Employee Pension (SEP) plans, deferred compensation, and IRA distributions. The exemption does not include premature distributions. Out-of-state government pensioners qualify for the $3,600 exemption. The $3,600 exemption is reduced by $2 for every $1 that the federal AGI exceeds $30,000. The exemption is entirely phased out when income reaches $31,800 (single filers) or $33,600 (married, filing jointly, when both spouses have pension income).

Nebraska—Out-of-state government pensions are fully taxed.

New Jersey—Taxpayers must be age 62 or older or disabled (as defined by the Social Security Administration), and their gross income cannot exceed $100,000 to qualify for pension exemptions. The exemptions include taxable pensions, annuities, and IRA withdrawals. Since employee contributions to pensions or annuities have been taxed previously, they are not taxed when they are withdrawn. Out-of-state government pensioners qualify for the $15,000 (single filers) or $20,000 (married, filing jointly) exemption. Taxpayers age 62 or older who do not claim the maximum pension exclusions of $15,000 (single filers) or $20,000 (married, filing jointly) and whose gross income is $100,000 or less are eligible to apply the unclaimed portion of their pension exclusion to other types of income if their wages, net business profits, partnership income, and S Corporation income are $3,000 or less. In addition, taxpayers age 62 or older who are unable to receive Social Security or Railroad Retirement benefits, but who would have been eligible for benefits had they been covered by either program, can deduct up to $3,000 (single filers) or $6,000 (married, filing jointly) in other retirement income.

New Mexico—Taxpayers age 65 or older whose income is $28,500 or less (single filers) or $51,000 or less (married, filing jointly) may exempt up to $8,000 per eligible taxpayers from *any* income source (including Social Security benefits) depending on the level of their adjusted gross income. Taxpayers who are age 100 or more are exempt from New Mexico's income tax.

New York—Taxpayers must be age 59 ½ or older to qualify for a $20,000 exemption from private pensions, annuities, IRA distributions, Keogh plans, and disability income. Pensions from New York state and local governments, the military, and the federal civil service are tax-exempt. Out-of-state government pensions can be deducted as part of the $20,000 exemption.

North Carolina—North Carolina state and local government retirees and federal retirees who worked for 5 years or more (as of August 12, 1989) can receive a full pension exemption from their defined benefit public pension plans (based on the "Bailey settlement"). This benefit also applies to the state's 401(k) and 457 plans if the retiree contributed to the plan prior to August 12, 1989. Other government retirees receive up to a $4,000 exemption per taxpayer. However, pensioners cannot claim the $4,000 exemption for the same pension income that they already claimed as a full deduction (based on the "Bailey settlement"). Out-of-state government pensions also qualify for the $4,000 pension exemption.Total private and public pension exemptions for retirees may not exceed $4,000 per taxpayer for those who do not qualify for the full public pension exemption. Exempt private pension income is paid by an employer to a former employee under a retirement plan to provide payments after the employee leaves.

North Dakota—Public pension exemptions are reduced by the amount of Social Security benefits received, and pensioners must file the ND-2 form to qualify. Military pensioners must be at least 50 years old to qualify for the $5,000 exemption. Only highway patrol, city police, and city firefighters qualify to receive the $5,000 exemptions under state/local retirement pension plans. Out-of-state government pensions are fully taxed.

Ohio—Tax credits are available for retirement income. These credits vary by retirement income and range from $25 (retirement income of more than $500 but not more than $1,500) to $200 (retirement income of more than $8,000). To qualify for the retirement income credit, a taxpayer must be receiving retirement benefits; annuities; or distributions from a pension, retirement, or profit-sharing plan. The income must be retirement related and be included in Ohio adjusted gross income. Out-of-state government pensions can be applied toward the retirement income credit.

Oklahoma—The $10,000 public pension exemption covers the pensions of retirees from Oklahoma state and local governments, the military, and the federal civil service. For military retirees, the exemption equals 50 percent of retirement benefits or $10,000 (whichever is greater); for other public pensions, retirees can deduct up to $10,000. Taxpayers whose adjusted gross income is $37,500 or less (single filers) or $75,000 or less (married, filing jointly) are eligible for the private pension exemption. Total public and private exemptions cannot exceed $10,000 per person. Out-of-state government pensions qualify for the $10,000 private exemption.

Oregon—Federal pensioners who worked prior to October 1, 1991, can deduct part or all of their federal pension income. Federal pensioners retiring before October 1, 1991, receive a full exemption for federal pensions. Those retiring after that date receive an exemption for their federal pension based on the amount of the individual's service time prior to October 1, 1991, compared to his or her total service time. Taxpayers age 62 or older whose household incomes (excluding Social Security benefits) are less than $22,500 (single filers) or $45,000 (married, filing jointly) are eligible for a retirement income tax credit if they have not received more than $7,500 (single filers) or $15,000 (married, filing jointly) in Social Security and Tier 1 Railroad Retirement benefits and if their household income, Social Security benefits, and Tier 1 Railroad Retirement benefits are less than $22,500 (single filers) or $45,000 (married, filing jointly). This retirement income tax credit can be as much as 9 percent of retirement income depending on the level of total income, Social Security benefits, and Tier 1 Railroad Retirement benefits. The credit can be applied to the following income: public and private pensions, individual retirement plans, deferred compensation plans, and employee annuity plans. Out-of-state government pensions can be applied toward the retirement income tax credit.

Pennsylvania—Taxpayers who receive retirement income from plans whose benefits would be subject to additional taxes under Internal Revenue Code sections 72 (q) or 72 (t) must be age 59 ½ or older and terminated from employment to exempt this income. Exceptions to this age requirement apply to Internal Revenue Code sections 72 (q) (2) or 72 (t) (2). Traditional defined benefit plans have no age requirements for exempting retirement income. Exempt retirement income includes private and public pensions, annuities, Keogh plans, Simplified Employee Pension (SEP) income, deferred compensation plans, and IRA distributions. Out-of-state government pensions are tax-exempt as long as taxpayers meet the age requirement described earlier.

Rhode Island—Out-of-state government pensions are fully taxed.

South Carolina—Retirees under the age of 65 can deduct up to $3,000 of their qualified retirement income. Retirees age 65 or older can deduct up to $10,000 of their qualified retirement income. Qualified retirement income includes all public employee retirement plans defined in Internal Revenue Code sections 401, 403, 408, and 457 as well as IRA distributions, Keogh plans, and military retirement. In addition to the qualified retirement exemption of $10,000, taxpayers age 65 or older qualify for a senior deduction of $15,000 (single filers) or $30,000 (married, filing jointly if both spouses are age 65 or older) against any taxable income. However, the senior deduction is reduced by any qualified retirement exemption taken.

Utah—Taxpayers under the age of 65 may exempt up to $4,800 in pensions, annuities, and taxable Social Security benefits. Out-of-state government pensions qualify for the $4,800 exemption. Taxpayers age 65 or older may exempt up to $7,500 from *all* income sources. Exclusions for both age groups are subject to a $1 reduction for every $2 of federal AGI (plus interest on line 8b of federal form 1040 plus any lump-sum distribution amount) in excess of $25,000 (single filers) or $32,000 (married, filing jointly).

Vermont—Out-of-state government pensions are fully taxed.

Virginia—Taxpayers who were born before January 1, 1939, may claim a deduction of up to $12,000 from *any* income source regardless of their income. Taxpayers who were born on or between January 2, 1939, and January 1, 1942, are also eligible for the deduction; however, the deduction amount depends on the taxpayer's modified federal adjusted gross income, which excludes taxable Social Security benefits. The $12,000 deduction is reduced one dollar for every dollar that the taxpayer's modified adjusted gross income exceeds $50,000 (single filers) or $75,000 (married filers).

West Virginia—The West Virginia Teachers Retirement System, West Virginia Public Employees Retirement System, and federal pensions qualify for the $2,000 pension exemption. West Virginia state or local police, deputy sheriffs, or firefighters receive a full pension exemption. Taxpayers who are age 65 or older or are permanently disabled qualify for up to an $8,000 exemption from any income source including taxable Social Security benefits. However, the $2,000 pension exemption for federal, state, and local pensioners; the full pension exemption for public safety officials; interest or dividends on United States or West Virginia obligations (which are subject to federal tax but exempt from state tax); and the $22,000 military exemption count toward the $8,000 ceiling. Out-of-state government pensions qualify for the $8,000 exemption.

Wisconsin—First, pension income from some federal agencies, such as the Coast Guard, may be subtracted from taxable income. Second, federal civil service pensioners and some state/municipal pensioners who retired prior to January 1, 1964, (or became a member of the retirement system as of December 31, 1963, and then retired at a later date) qualify for a tax exemption on their pension income. Third, beneficiaries of pensioners who met those requirements also qualify. For state and local government retirees, only certain Milwaukee City, Milwaukee County, and the Wisconsin teachers' retirement systems qualify for exemptions subject to the conditions discussed above. Out-of-state government pensions are fully taxed.