

Income Tax Exemptions for Retirement Income

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Issue

Briefly explain the state tax exemptions for retirement income, including changes made in the FY 24-25 budget act. This report updates OLR Report [2022-R-0099](#).

Summary

State law provides income tax exemptions for Social Security benefits, railroad retirement benefits, military retirement pay, pension and annuity income, teacher pension income, and individual retirement account (IRA) distributions. In most cases, exemption eligibility and exemption amounts are determined based on a taxpayer's total federal adjusted gross income (AGI).

All taxpayers qualify for the Social Security benefits exemption, but taxpayers with AGIs greater than \$100,000 (for joint filers) or \$75,000 (for other filing statuses) qualify only for a partial exemption. Tier I and II railroad retirement benefits and military retirement pay are fully exempt from income tax, regardless of total AGI. Taxpayers with Teachers' Retirement System (TRS) income qualify for a 50% exemption regardless of their AGI.

Currently, taxpayers with AGIs of less than \$75,000 or \$100,000 (as applicable) are fully exempt from income tax on their pension and annuity income and partially exempt from income tax on IRA income (the IRA exemption does not fully phase-in until the 2026 tax year). Until the 2024 tax year, those with incomes equal to or greater than these amounts do not qualify for the pension and annuity or IRA income exemptions. However, the FY 24-25 budget act eliminates this cliff for the 2024 tax year and beyond by increasing the eligibility thresholds and correspondingly phasing out the exemptions.

Social Security Income

By law, Connecticut exempts from its income tax (1) Social Security income the federal government exempts from the federal income tax and (2) depending on a taxpayer's filing status and AGI, some or all of the Social Security income the federal government taxes ([CGS § 12-701\(20\)\(B\)\(x\)](#)). (OLR Report [2018-R-0271](#) explains the federal Social Security exemption.)

Taxpayers may deduct 100% of their federally taxable Social Security income if their AGI is below (1) \$75,000 for single filers and married people filing separately or (2) \$100,000 for joint filers and heads of household. Taxpayers with AGIs equal to or greater than these thresholds qualify for a partial exemption through which no more than 25% of their total Social Security benefits received is subject to tax ([CGS § 12-701\(a\)\(20\)\(B\)\(x\)\(III\)](#)).

Railroad Retirement Benefits and Military Retirement Pay

Taxpayers may deduct 100% of their (1) tier I and tier II railroad retirement benefits (which are generally exempt from state and local income tax under the federal Railroad Retirement Act of 1974 (45 U.S.C. § 231m)) and (2) military retirement pay ([CGS § 12-701\(a\)\(20\)](#)).

Pension and Annuity Income

General Pension and Annuity Exemption

The law fully exempts qualifying pension and annuity income (including 401(k), 403(b), or 457(b) plans) from income tax for taxpayers with federal AGIs below (1) \$75,000 for single filers, married people filing separately, and heads of household or (2) \$100,000 for married people filing jointly. Pension and annuity income is fully taxable for taxpayers with AGIs equal to or greater than these thresholds through the 2023 tax year ([CGS § 12-701\(a\)\(20\)\(B\)\(xxi\)](#)), as amended by [PA 23-204 \(§ 377\)](#)). However, beginning with the 2024 tax year, the FY 24-25 budget act eliminates this cliff by gradually phasing out the exemption for taxpayers with income greater than these income thresholds (see "Changes in FY 24-25 Budget Act" below).

Teacher's Retirement System (TRS) Pension Income

Beginning with the 2021 tax year, taxpayers may deduct 50% of TRS pension income from their Connecticut taxable income. For the 2016-2020 tax years, the deduction was 25%. Taxpayers who are eligible for both the general pension and annuity exemption and the TRS pension exemption may take whichever one is most favorable to them ([CGS § 12-701\(a\)\(20\)\(B\)\(xx\)](#)).

IRA Income

Enacted in the FY 22-23 budget act, existing law exempts an increasing portion of income-eligible taxpayers' IRA income, other than income from Roth IRAs, until it is fully exempt in the 2026 tax year, as shown in Table 1 ([CGS § 12-701\(a\)\(20\)\(B\)\(xxviii\)-\(xxx\)](#)), as amended by [PA 23-204 \(§ 377\)](#).

Table 1: Schedule for Deducting Percentage of IRA Income From Connecticut Income Taxes

| Tax Year | Percent of IRA Income Exempt |
|---------------------|------------------------------|
| 2023 | 25 |
| 2024 | 50 |
| 2025 | 75 |
| 2026 and thereafter | 100 |

Taxpayers qualify for the exemption if their AGI is less than the same thresholds that apply to the pension and annuity income exemption (see above), and those with incomes equal to or greater than those thresholds do not qualify for the exemption in the 2023 tax year. However, beginning with the 2024 tax year, the FY 24-25 budget act eliminates this cliff by gradually phasing out the exemption for taxpayers with income greater than these income levels (see “Changes in FY 24-25 Budget Act” below).

Changes in FY 24-25 Budget Act

Currently, the general pension and annuity exemption and the IRA income exemption end abruptly for taxpayers with incomes at or above the AGI eligibility thresholds. The FY 24-25 budget act eliminates this cliff starting with the 2024 tax year by increasing the eligibility thresholds and correspondingly phasing out the exemptions ([PA 23-204 \(§ 377\)](#)).

Specifically, beginning with the 2024 tax year, the act expands eligibility for these exemptions to cover taxpayers with federal AGIs less than (1) \$100,000 for single filers, married people filing separately, and heads of household and (2) \$150,000 for joint filers. But for taxpayers whose income exceeds the current eligibility thresholds (i.e., \$75,000 and \$100,000, as applicable), the act gradually reduces the amount of pension, annuity, and IRA income taxpayers may deduct until the exemption fully phases out at \$100,000 or \$150,000, as applicable. Table 2 shows the percentage of this income taxpayers may deduct based on their AGI and filing status.

**Table 2: General Pension and Annuity Exemption and
IRA Exemption Phase-Out Schedule, Beginning With 2024 Tax Year**

| Federal AGI (\$) | | |
|---|------------------------|---------------|
| Single, Married Filing Separately, or Head of Household | Married Filing Jointly | Deduction (%) |
| < 75,000 | < 100,000 | 100.0 |
| 75,000 to 77,499 | 100,000 to 104,999 | 85.0 |
| 77,500 to 79,999 | 105,000 to 109,999 | 70.0 |
| 80,000 to 82,499 | 110,000 to 114,999 | 55.0 |
| 82,500 to 84,999 | 115,000 to 119,999 | 40.0 |
| 85,000 to 87,499 | 120,000 to 124,999 | 25.0 |
| 87,500 to 89,999 | 125,000 to 129,999 | 10.0 |
| 90,000 to 94,999 | 130,000 to 139,999 | 5.0 |
| 95,000 to 99,999 | 140,000 to 149,999 | 2.5 |
| ≥ 100,000 | ≥ 150,000 | 0.0 |

In the case of the IRA exemption for the 2024 and 2025 tax years, the deduction percentage listed in Table 2 applies to the portion of income the law allows as an exemption, not to all IRA income. For example, a single filer with \$80,000 in federal AGI and \$50,000 in IRA income would be able to deduct \$13,750 of that income in the 2024 tax year (i.e., 50% of IRA income, multiplied by 55%).

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