

Taxation of Retirement Benefits

All Funds

**THE DIVISION OF PENSIONS AND BENEFITS CANNOT PROVIDE TAX ADVICE.
CONSULT THE IRS (1-800-TAX-1040), OR THE NJ DIVISION OF TAXATION (609) 292-6400,
OR YOUR TAX ADVISOR FOR ASSISTANCE.**

This fact sheet contains general information about federal and New Jersey State income taxes and your retirement benefits.

HOW ARE MY RETIREMENT BENEFITS TAXED FOR FEDERAL PURPOSES?

Retirement benefits (except for Accidental Disability retirement and Accidental Death benefits) are subject to federal income tax. However, if you paid tax on any of your contributions to the retirement system in the past, the portion of your monthly retirement benefits representing a return of your previously-taxed contributions is not taxable.

Currently, contributions made to the retirement system are tax-exempt. However, contributions made to the retirement system prior to January 1, 1987, were taxed as were any purchases of optional pension service credit made before 2002. After January 1, 2002, some purchases of service credit may have been made with previously-taxed money. Therefore, if you began contributing to the retirement system prior to January 1, 1987, or if you purchased service credit since then, all or a portion of your total contributions may have been previously subject to federal tax.

The rate at which you can recover your previously-taxed contributions is determined in part by your retirement date:

If you retired before August 1, 1986 — you were able to fully recover your contributions before having to pay tax on your benefits. Once you recovered your contributions, your benefits became fully taxable. The exception is if you did not fully recover your contributions within the first three years of retirement. In that case, you had to recover your contributions under the IRS expected return rule explained below.

If you retired on or after August 1, 1986 — you must recover your contributions under the expected return rule. Under this rule, you recover your contributions evenly over your expected lifetime or the combined lifetime of you and your pension beneficiary. This means that only a small portion of each monthly benefit is considered a return of your previously-taxed contributions and is tax-free.

CALCULATING THE NON-TAXABLE AMOUNT UNDER THE EXPECTED RETURN RULE

If you retired after July 1, 1986, and before November 1, 1996 — your monthly nontaxable amount is determined using life expectancy tables found in *IRS Publication 939*.

If you retired on or after November 1, 1996 — the following tables found in *IRS Publication 575* (Simplified Method) are used to determine your monthly nontaxable amount:

TABLE A
Benefits Payable To Retiree Only*

Age of Retiree (at retirement)	Number of Payments
55 or less	360
56-60	310
61-65	260
66-70	210
71 or more	160

*For those retired on or after November 1, 1996, and before December 1, 1997, Table A is used even if benefits are payable to the retiree and the retiree's survivor.

TABLE B
Benefits Payable To Retiree and Beneficiary

Combined Age of Retiree (at retirement) and Beneficiary	Number of Payments
110 or less	410
111-120	360
121-130	310
131-140	260
141 or more	210

The following examples illustrate how the monthly nontaxable amount is computed using Tables A and B:

Example 1 — A PERS member, whose previously-taxed contributions equaled \$12,000, retires at age 62 and chooses to receive the maximum allowance (designating no monthly pension to a surviving beneficiary). **Table A** is used because benefits are payable to the **retiree only**. The \$12,000 is divided by 260, which produces a monthly tax-free amount of \$46.15. The balance of the monthly pension is subject to federal income tax.

Example 2 — A TPAF member, whose previously-taxed contributions equaled \$15,000, retires at age 60 and chooses to receive benefits under Option 2 (designating the same monthly pension to the surviving beneficiary). **Table B** is used because benefits are payable to the retiree **and the retiree's beneficiary**. The designated beneficiary is the same age as the retiree. The \$15,000 is divided by 360, which produces a monthly tax-free amount of \$41.67. The balance of the monthly pension is subject to federal income tax.

HOW LONG WILL THE NON-TAXABLE PORTION CONTINUE?

For those who retired after December 31, 1986, the monthly nontaxable amount remains in effect until all of your previously-taxed contributions are fully recovered. At that point your benefits become fully taxable.

For those who retired before December 31, 1986, the monthly nontaxable amount is effective for as long as you or your survivor receive benefits.

If benefits cease before your previously-taxed contributions are fully recovered, the remaining balance can be claimed as a deduction on the income tax return of the last recipient, provided you retired on or after July 1, 1986. If you retired before July 1, 1986, no deduction is allowed for unrecovered contributions.

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WITHHOLDING FEDERAL INCOME TAX FROM YOUR PENSION CHECK

Each new retiree will automatically receive a federal withholding tax *Form W-4P* near the date of retirement. The Division of Pensions and Benefits is required by federal law to **automatically withhold federal income tax** from your pension check, based on a status of married with three allowances if you do not complete a *W-4P*. The *W-4P* allows you to elect no withholding or, if you want withholding, to inform us of your tax filing status so that we can withhold the proper amount.

WITHHOLDING NJ STATE INCOME TAX FROM YOUR PENSION CHECK

If you live in New Jersey you will automatically receive a New Jersey State withholding tax *Form NJ W-4P* near the date of retirement. Most retirees will not be subject to New Jersey income tax until they recover in pension checks the amount of contributions, they made to the retirement system while working. If you will not recover your total contributions within three years of retirement, refer to the instructions for the *Form NJ-1040* to determine how your pension is taxed. You can find information on both the three-year rule and the general rule methods in the instructions for the *Form NJ-1040*.

If you are at least 62 or considered disabled by Social Security, you may exclude the following amounts of retirement income from New Jersey income tax for the tax year indicated below.

Retirement Income Exclusions

Tax Year	Married Filing Jointly	Single	Married Filing Separately
2003 – 2016	\$20,000	\$15,000	\$10,000
2017	\$40,000	\$30,000	\$20,000
2018	\$60,000	\$45,000	\$30,000
2019	\$80,000	\$60,000	\$40,000
2020	\$100,000	\$75,000	\$50,000

Note: Beginning with tax year 2005, the “Retirement Income Exclusions” listed above are limited to taxpayers with gross income of \$100,000 or less. Please see the instructions for the *Form NJ-1040*, or contact the New Jersey Division of Taxation or a professional tax advisor for further information.

Unlike federal income tax, **withholding for New Jersey income tax is completely voluntary. No New Jersey income tax will be withheld unless you authorize it by completing a *Form NJ W-4P*.** The amount withheld must be at least \$10 per month in even dollar amounts (no cents). If you need help deciding whether or not to have New Jersey income tax withheld or how much tax to have withheld, you can contact the New Jersey Division of Taxation at (609) 292-6400.

If you live outside New Jersey, you are not required to pay New Jersey income tax on the pension you receive from the retirement system. The Division of Pensions and Benefits does not withhold income tax for other states. Check with your home state’s tax office to determine if your pension is taxable in your state of residence.

CHANGING YOUR WITHHOLDING AMOUNT

Retirees can now quickly and easily change their tax withholdings online using the Member Benefits Online System (MBOS). Find out more about MBOS at: www.nj.gov/treasury/pensions

If you do not change your withholding online, you must submit a *Form W-4P* or *NJ W-4P* to the Division of Pensions and Benefits. Forms can be found on the Internet at: www.nj.gov/treasury/pensions

If you do not have Internet access, you can contact the Division of Pensions and Benefits at (609) 292-7524 to obtain the form.

QUESTIONS COMMONLY ASKED AFTER RETIREMENT**Will I receive a statement of pension income for tax purposes?**

Yes. retirees receive *Form 1099-R* at the end of January each year, covering the previous tax year. This shows the gross retirement allowance; how much is subject to federal income tax; and the amounts, if any, that were withheld for federal and New Jersey income tax.

Am I taxed on the reimbursement of Medicare premiums?

No. Some State employees and all employees of boards of education or county colleges who retired with 25 or more years of service, or on a disability retirement, and are enrolled in the State Health Benefits Program are reimbursed in their pension checks for the Medicare Part B premiums they pay to Social Security. If you receive this Medicare reimbursement, the gross amount of your pension checks will be greater than the gross amount shown on your *Form 1099-R* because the Medicare reimbursement is not taxable. The Medicare premium reimbursement is subtracted from your total gross income to determine the gross pension reported to the IRS.

Is my disability pension taxable?

If you are receiving a disability pension, your benefits are not subject to New Jersey income tax until you reach age 65.

If you are receiving an *Accidental* Disability pension, — or if you are a survivor receiving *Accidental* Disability or *Accidental* Death benefits — the Division of Pensions and Benefits reports your benefit as exempt from federal income tax.

Ordinary Disability pensions are subject to federal tax to the same extent as other pensions.

This fact sheet has been produced and distributed by:
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