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Bill Analysis

Version: As Introduced

Primary Sponsor: Rep. Robinson

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SUMMARY

- Exempts pension income and survivor benefits of retired public safety personnel from state income tax.
- Reimburses the Local Government Fund and Public Library Fund for their shares of revenue reductions resulting from the exemption.

DETAILED ANALYSIS

Deduction for public safety retirement pay

The bill permits retired public safety personnel receiving age or service retirement allowance payments to deduct the full amount of those payments when computing their state income tax liability. The deduction also applies to payments received by a surviving spouse, child, or parent of a deceased public safety retiree under a survivor benefit plan. The following pension plans qualify for the deduction:

- Ohio Police and Fire Pension Fund;
- Highway Patrol Retirement System;
- Public Employees Retirement System (PERS) if the retiree obtained eligibility for retirement based on service credits accrued as a law enforcement or public safety officer, or if the retiree would have qualified for the Ohio Public Safety Officers Death Benefit Fund had they been killed in the line of duty immediately before retirement;
- Cincinnati Retirement System if the retiree would have qualified for the Ohio Public Safety Officers Death Benefit Fund had they been killed in the line of duty immediately before retirement;
- Federal Civil Service Retirement System, Federal Employees Retirement System, or any successor federal retirement program if the payments are attributable to service credit

accrued in the performance of duties that are comparable to state or local public safety personnel.[1]

The payments are deductible only to the extent that they were included in the taxpayer's federal adjusted gross income (FAGI), the base upon which a taxpayer's Ohio taxable income is determined. Under continuing law, Ohio public employees do not owe federal or Ohio tax on contributions into the pensions system while they are employed, but the full amount of the distributions they receive during retirement is generally included in FAGI. In contrast, federal employees pay federal and Ohio tax on the income they contribute to the pension system. Once retired, only the portion of the pension distribution that exceeds the amount contributed is included in FAGI.[2]

Retirement income credit

Payments deducted under the bill are excluded when computing the retirement income credit that is available, under continuing law, to taxpayers aged 65 years and older whose individual or adjusted gross income (less personal exemptions) for the taxable year is less than $100,000. Calculation of the retirement income credit varies depending on whether the retiree claims the credit on an annual basis or on the basis of a lump-sum distribution of income. For retirees who claim the annual credit, the credit ranges from $25 for retirement income of at least $500, to $200 for retirement income of at least $8,000. Retirees who receive a lump-sum distribution of retirement income may claim a one-time credit equivalent to receiving the annual credit each year of the retiree's expected remaining life according to actuarial tables.[3]

School district and municipal income taxes

The deduction authorized by the bill does not affect the tax base for school district income taxes. The bill requires any taxpayer that makes the deduction for state income tax purposes to add back the deducted amount when computing their school district taxable income if the school district uses Ohio Adjusted Gross Income (OAGI) as its tax base. Consequently, retirement pensions and survivor benefits remain taxable for school district income tax purposes to the same extent as under current law.[4]

The bill's exemption also does not affect the municipal income tax base. Continuing law, unchanged by the bill, requires municipal corporations to exempt all pension income from taxation.[5]

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[1] R.C. 5747.01(A)(44).

[2] See the Internal Revenue Service Government Retirement Plans Toolkit, which is available on the IRS's website: irs.gov.

[3] R.C. 5747.055, not in the bill.

[4] R.C. 5748.01.

[5] R.C. 718.01, not in the bill.

Local Government Fund and Public Library Fund

Continuing law requires that a certain percentage of tax revenue credited to the GRF be disbursed monthly to counties, townships, municipal corporations, and other types of subdivisions through the Local Government Fund (LGF) and to public libraries, park districts, and some other subdivisions through the Public Library Fund (PLF). Under current law, 1.7% of GRF tax revenue is credited both to the LGF and PLF. Reductions in GRF tax revenue from any cause therefore reduces the amount credited to the LGF and PLF proportionately.

The bill requires the Director of OBM to increase the monthly payment to the LGF and PLF to offset the monthly amount of revenue forgone to the GRF because of the bill's deduction, as estimated by the Tax Commissioner, multiplied by the percentage of GRF taxes required to be transferred to each fund. Essentially, the bill holds the LGF and PLF harmless from revenue loss resulting from the deduction.[6]

Interaction with federal tax law

Federal law prohibits states from discriminating between federal and state employees in taxing their compensation: "The United States consents to the taxation of pay or compensation [of a federal officer or employee] . . . by a duly constituted taxing authority having jurisdiction, if the taxation does not discriminate against the officer or employee because of the source of the pay or compensation."[7] The United States Supreme Court has, on numerous occasions, held that the statute applies to retirement benefits paid for government service. Consequently, a state that permits state or local government employees to claim an income tax deduction for retirement benefits must permit similarly situated federal government employees to claim the same deduction.[8]

The bill uses the Court's terminology in the *Dawson* opinion, extending the deduction to federal retirees that perform "comparable" duties. However, as noted above, federal government employee pensions are taxed differently than state and local employee pensions. Since federal law allows state and local employees – but not federal employees – to make pension plan contributions on a "pretax" basis, state and local retirees will likely accrue a greater benefit from the bill's deduction.

In effect, the bill exempts the full pension of state and local government retirees but only the investment earnings of federal government retirees. To obtain an equivalent result, the bill would need to allow federal public safety employees to deduct contributions to, as well as payments from the federal pension system. It is not clear from the Court's holding in *Dawson* that such an extension is required by federal law; particularly given that the timing differences in pension taxation stem from the Internal Revenue Code.

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[6] R.C. 131.44 and 131.51.

[7] 4 United States Code § 111.

[8] See, e.g., *Dawson v. Steager,* 586 U.S. 171 (2019), and *Davis v. Michigan Dept. of the Treasury*, 489 U.S. 803 (1989).

HISTORY

Action	Date
Introduced	05-15-24

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