

Department of Finance and Administration

Legislative Impact Statement

Bill: SB234

Bill Subtitle: TO CREATE AN INCOME TAX EXEMPTION FOR POLICE AND FIRE RETIREMENT AND SURVIVOR BENEFITS.

Basic Change :

Sponsor: Senator A. Clark

SB234 provides a full income tax exemption for retirement benefits received by a police officer or firefighter and for survivor benefits funded by the retirement pay of a police officer or firefighter. This exemption is provided to police officers as follows:

- A non-civilian employee of the Arkansas State Police;
- A non-civilian employee of the Arkansas Law Enforcement Training Academy;
- A non-civilian employee of a municipal or county police agency or a suburban improvement district located in Arkansas or another state.

Firefighters that would qualify for the exemption are as follows:

- A non-civilian employee of the Arkansas Fire Training Academy;
- A non-civilian employee of a municipal, county, fire protection district maintaining standards established by the Arkansas Local Police and Fire Retirement System;
- A non-civilian employee of a rural fire protection corporation or a suburban improvement district located in Arkansas in another state.

Currently, the first \$6,000 of retirement benefits received by a police officer or firefighter are exempt from income tax and the remainder of that income is taxable. This bill is effective for tax years beginning on and after January 1, 2018.

Revenue Impact :

FY2018 \$1.3M reduction to General Revenue

FY2019 and after of \$2.6M per year reduction to General Revenue

[This revenue impact is based on the assumption that this bill would only exempt retirement pay from a plan for police officers and firefighters and not retirement pay received by a firefighter or police office from other sources.]

Taxpayer Impact :

Police officer and firefighter retirement benefits would no longer be subject to income tax.

Resources Required :

Tax forms and instructions will need to be revised, along with programming of the processing system.

Time Required :

Adequate time is provided.

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Procedural Changes :

None.

Other Comments :

None.

Legal Analysis :

Enactment of the full retirement exemption for police and firefighters, as provided in SB234, will likely violate the doctrine of intergovernmental immunity as provided in 4 U.S.C. § 111. This statute, which is coextensive with intergovernmental tax immunity, provides, "The United States consents to the taxation of pay or compensation for personal service as an officer or employee of the United States...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."

This provision was interpreted by the Arkansas Supreme Court in the case of *Pledger v. Bosnick*, 306 Ark. 45, 811 S.W.2d 286 (1991) when considering an Arkansas law that provided a full exemption for the retirement income received by state employees and a \$6,000 exemption for all other retirees, including federal retirees. In its analysis of the Arkansas law, the Supreme Court stated:

[4 U.C.S § 111] constitutes an affirmative statutory grant of immunity from discriminatory state taxation equal to the constitutional Doctrine of Intergovernmental Tax Immunity, which applies between the states and the federal government and among the states themselves. Thus, if we find in this case that the Arkansas tax scheme discriminates against retirees from the federal government or other states when compared to the treatment given retirees from the State of Arkansas, we must find that the tax is in violation of the Constitutional Doctrine of Intergovernmental Tax Immunity.

The court then concluded that the full exemption for state employee retirement did violate federal law. SB234 would enact a retirement exemption for some state and local government retirees that would not be extended to retirees of the federal government or to all retirees of other states. The proposed language of SB234 presents the same constitutional infirmities identified by the Arkansas Supreme Court in the Bosnick case.

In addition, it is unclear whether Page 3, Lines 2-3 of the bill could be read to apply an exemption to retirement benefits received from other sources by a retired police officer or firefighter that is unrelated to their police or firefighting benefits. It may be recommended that the bill be amended to clarify that retirement benefits derived from service as a police officer or firefighter.