This case would have been a lot more interesting had it gone the other way. In an unanimous decision the Supreme Court held in Dawson v. Steager that West Virginia violated a federal statute by taxing all the retirement benefits of former federal law enforcement employees but not certain state law enforcement employees.

4 U.S.C. § 111 allows states to tax the pay of federal employees only “if the taxation does not discriminate . . . because of the source of the pay or compensation.” James Dawson, a former U.S. Marshal, sued West Virginia alleging it violated this statute because it taxed his pension but not the pensions of certain state law enforcement employees. The West Virginia Supreme Court found no discrimination because relatively few state employees received the tax break and the statute’s intent was to benefit those state retirees not harm federal retirees.

In an opinion written by Justice Gorsuch the Supreme Court struck down West Virginia’s statute and held that a state “violates §111 when it treats retired state employees more favorably than retired federal employees and no ‘significant differences between the two classes’ justify the differential treatment.” “West Virginia expressly affords state law enforcement retirees a tax benefit that federal retirees cannot receive.” And all parties agreed that there aren’t significant differences in the job duties of U.S. Marshals and the tax-exempt state law enforcement retirees.

Making the same arguments the West Virginia Supreme Court accepted, West Virginia pointed out that its tax scheme helps only very few state law enforcement officers. But the Court noted “Section 111 disallows any state tax that discriminates against a federal officer or employee—not just those that seem to us especially cumbersome.” Likewise, the Supreme Court refused to uphold West Virginia’s statute because it isn’t intended to harm federal retirees calling the state’s interest in adopting a discriminatory tax “irrelevant.”

The United States noted that Massachusetts and New Mexico state courts have upheld state and local employee retirement-benefit tax exemptions similar to West Virginia’s while courts in Missouri, Arkansas, and Colorado have struck them down. But it appears that as of 2015 only West Virginia and Connecticut (see Table 2) disfavor federal government employees versus state employees in exempting taxing retirement benefits.

It may be that state legislatures have rejected providing more favorable tax treatment to state and local retirees than federal retirees for policy reasons. It is also possible state legislatures not done so because of uncertainty in the law. Now the law is no longer uncertain: state and local government retirees may not receive tax breaks similarly-situated federal retirees are ineligible to receive.

By:
Friday, February 22, 2019 at 02:44 PM
Tags:
Supreme Court | Tax | discriminatory tax | income tax | retirees | Policy Area | Economics and Finance | Tax and Budget | Revenue
Source URL:

Links