

**LEGISLATIVE SERVICES AGENCY  
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**FISCAL IMPACT STATEMENT**

**LS 6559**

**BILL NUMBER:** HB 1165

**NOTE PREPARED:** Dec 15, 2010

**BILL AMENDED:**

**SUBJECT:** Taxation of civil service annuities.

**FIRST AUTHOR:** Rep. Kersey

**FIRST SPONSOR:**

**BILL STATUS:** As Introduced

**FUNDS AFFECTED:**  **GENERAL**  
 **DEDICATED**  
 **FEDERAL**

**IMPACT:** State & Local

**Summary of Legislation:** This bill provides a 100% income tax deduction, beginning in 2016, for federal civil service annuity income received by an individual or the individual's surviving spouse after subtracting Social Security benefits and railroad retirement benefits. It phases in the deduction from 2012 through 2015. It removes the requirement that an individual must be at least 62 years of age to be eligible for the federal civil service annuity income tax deduction. The bill also provides that an individual's surviving spouse may be eligible for the federal civil service annuity income tax deduction.

**Effective Date:** July 1, 2011.

**Explanation of State Expenditures:** *Department of State Revenue (DOR):* The DOR would incur some administrative expenses relating to the revision of tax forms, instructions, and computer programs to reflect the phase-in of the 100% income tax deduction for civil service annuities. The DOR's current level of resources should be sufficient to implement the change.

**Explanation of State Revenues:** *Summary* - The bill would reduce Adjusted Gross Income (AGI) Tax liabilities of certain individual taxpayers who receive federal civil service retirement benefits, including surviving spouses. The provisions of this bill would require the annuity to be offset by social security and railroad retirement benefits, as is required now. The bill phases in a 100% income tax deduction over five years. In years 2012 through 2015 the deduction is equal to the greater of a percentage of the annuity (20%, 40%, 60%, and 80%, respectively) or \$12,000. The potential revenue losses due to the increase in the deduction are summarized in the table below, and are in addition to the revenue losses which are occurring under the current deduction limits.

<b>Tax Year</b>	<b>Fiscal Year</b>	<b>Deduction Amount</b>	<b>Annual Revenue Loss</b>
2012	2013	Greater of 20% of the annuity payment or \$12,000	\$13.4 M
2013	2014	Greater of 40% of the annuity payment or \$12,000	\$13.4 M
2014	2015	Greater of 60% of the annuity payment or \$12,000	\$18.6 M
2015	2016	Greater of 80% of the annuity payment or \$12,000	\$24.8 M
2016	2017	100% of the annuity payment	\$31.9 M

The estimates are based upon the average annuities received by retirees and surviving spouses, and whether the average amounts multiplied by the applicable percentage were greater than \$12,000. In some cases, \$12,000 was greater than the average annuity multiplied by the applicable percentage. This is why the estimated annual revenue loss for tax years 2012 and 2013 is similar. Also, because the deduction is calculated based on the difference between the annuity payment and the total amount of social security and railroad benefits, these estimates may be less to the extent that those eligible for the deduction receive social security and railroad retirement benefits.

*Background Information* - Under current statute, taxpayers may deduct up to \$2,000 in civil service annuity income. The deduction is equal to the difference between \$2,000 and the total amount of social security and railroad retirement benefits received by the taxpayer. State tax return data indicates that 4,159 taxpayers deducted approximately \$7.1 M in civil service annuity pay from AGI in 2008. This amount resulted in a revenue loss of about \$240,000. From 2003 to 2008, this deduction declined by an average of 1.3% per year. Data from the U.S. Office of Personnel Management indicates that there were about 25,000 federal retirees and about 8,000 surviving spouses of federal retirees residing in Indiana in 2009. These individuals received \$805 M in civil service annuity payments during 2009, with the average annuity to retirees equal to about \$27,000. The average survivor's benefit was about \$15,000. The total payments to retirees and their spouses in Indiana increased, on average, 4% over the past 10 years.

The bill increases the deduction beginning in tax year 2012, thus, the fiscal impact of the phase-in will commence in FY 2013. Revenue collected from the AGI tax on individuals is deposited in the state General Fund.

**Explanation of Local Expenditures:**

**Explanation of Local Revenues:** Because the increase in the civil service retirement deduction would serve to decrease taxable income, counties imposing local option income taxes could potentially experience a minimal decrease in revenue from these taxes.

**State Agencies Affected:** DOR.

**Local Agencies Affected:** Counties with local option income taxes.

**Information Sources:** OFMA Income Tax Databases, 1996-2008; Lynn Wehner, Federal Office of Personnel Management.

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