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United States Supreme Court Hears Oral Argument Involving Differential State Tax Treatment of Federal / State Government Retirement Benefits

By Jeff Reed

On December 3, 2018, the United States Supreme Court heard oral argument in *Dawson v. Steager* , a case addressing West Virginia's personal income tax regime, which exempts state employee retirement benefits without offering the same exemption to federal employee retirement benefits.

A retired US marshal living in West Virginia challenged the differential treatment under the doctrine of intergovernmental tax immunity, codified in 4 USC 111. The West Virginia circuit court ruled in the marshal's favor, but the West Virginia Supreme Court reversed, holding the statutory scheme constitutional. The US marshal appealed to the United States Supreme Court and the Court granted certiorari.

At oral argument, several justices expressed skepticism about the West Virginia scheme. In particular, they had trouble squaring it with *Davis v. Michigan*, 489 U.S. 803 (1989), a case holding that states cannot exempt state pensions while taxing federal pensions. A few justices asked whether there are factual differences between the state and federal jobs that might justify the difference in treatment. Based on oral argument, it seems most likely that the West Virginia scheme will be struck down or the case will be remanded to the lower court for additional fact-finding.

A decision is expected in 2019. The decision is expected to have implications for state statutes that distinguish between federal and state government employee retirement benefits. More broadly, the factual posture of the case highlights that some states decouple from the federal tax treatment of pensions and retirement benefits, so the state tax consequences of pension and retirement benefits is something that should be considered.