



January 12, 2010
Pennsylvania Inheritance Tax
No. INH-10-001
Taxation of SERS Benefits Payable to Estate

ISSUE

Whether payments from a State Employees' Retirement System ("SERS") annuity are subject to Pennsylvania Inheritance Tax where the payments are made to (1) a retired SERS member's ex-wife ("Taxpayer") as per an Approved Domestic Relations Order ("ADRO") and (2) subsequently to Taxpayer's testamentary beneficiary after her death?

CONCLUSION

Payments from a SERS annuity are not subject to Pennsylvania Inheritance Tax whether paid under an ADRO or to a last named beneficiary on file with SERS.

FACTS

A retired SERS member was receiving a monthly SERS retirement annuity. At retirement, the member had elected a SERS retirement option that provided a maximum annuity during his lifetime but all future distributions would cease upon the member's death.

After retirement, the member and Taxpayer divorced. As per an ADRO, the remaining SERS annuity payments were to be divided between the member and Taxpayer. Further, the ADRO specified that upon Taxpayer's death (and assuming the member was still alive and receiving annuity payments) any remaining payments would inure to Taxpayer's estate.

Taxpayer died in 2009, while member was alive and continuing to receive SERS annuity payments. At issue is whether the SERS annuity payments that pass to Taxpayer's estate are subject to Pennsylvania Inheritance Tax.

DISCUSSION

Generally, payments made to a taxpayer under a domestic relations order would be subject to Pennsylvania Inheritance Tax. However, regardless of whether SERS benefits are paid to a retired member or an alternate payee, the benefits remain exempt from Pennsylvania state or local taxation. 71 Pa.C.S. § 5953(a)(1). See also, *Marshall v. State Employees' Retirement System*, 887 A.2d 351 (Pa. Cmwlth. 2005).

The State Employees Retirement Code plainly states that SERS benefits shall not be subject to any levy, garnishment or attachment, albeit with a few limited exceptions. 71 Pa.C.S. § 5953(a)(1). These exceptions include the assignment of benefits to "alternate payees" under ADRO's. 71 Pa.C.S. § 5953(a)(3). "Alternate payees" are defined by the Retirement Code to include "any spouse, former spouse . . . who is recognized by a domestic relations order as having a right to receive all or a portion of the moneys payable to that member under this part." 71 Pa.C.S. § 5102.

Here, it is undisputed that Taxpayer possessed a lawful right to the SERS annuity payments under the ADRO. Further, the ADRO specifically mandated that any future annuity payments due after the death of Taxpayer would inure to Taxpayer's estate. Consequently, Taxpayer's estate remains entitled to a portion of each subsequent SERS annuity payment paid until the member's death.



In *Stegmaier Estate*, the Pennsylvania Supreme Court definitively held that the exemption contained within the Retirement Code of “any benefit or right accrued or accruing to any person” was applicable to benefits paid to the estate of a deceased beneficiary where the beneficiary did not receive a SERS annuity in full prior to his death. *Stegmaier Estate*, 424 Pa. 4 (1967).

The *Stegmaier* decision is persuasive to the facts at hand. The Court determined that SERS benefits, whether paid to a retired member, a retired member’s beneficiary or that beneficiary’s estate, were exempt from Pennsylvania Inheritance Tax. The Court determined that under these three scenarios, distributions were made to either a member or an alternate payee under the Code and as such, the payments retained their nature as exempt transfers for inheritance tax purposes. Under the facts at hand, it is clear that the payments made to Taxpayer were made to Taxpayer in her capacity as an alternate payee under the Retirement Code.

Further, it is significant that the ADRO required that payments from member to Taxpayer be made directly from the SERS annuity and not from an additional source of income, and that the ADRO addressed the possibility that Taxpayer may predecease the member. This supports the position that Taxpayer and later Taxpayer’s estate received exempt SERS annuity payments rather than taxable distributions made under a domestic relations order.

¹ An Approved Domestic Relations Order is defined by the State Retirement Code as any domestic relations order which has been determined to be approved under section 5953.1 of the Retirement Code. 71 Pa.C.S. § 5102; *Titler v. State Employees’ Ret. Board*, 768 A.2d 899 (Pa. Cmwlth. 2001).