

4.11 Pension Protection Act of 2006 (PPA)

2007 was the first tax year that Section 845 of the PPA was effective. Section 845 allows a retired federal law enforcement officer, firefighter, and a member of certain other small groups to **exclude** up to \$3,000 of their FERS annuity from federal income taxes for amounts paid for health insurance or long-term-care insurance premiums. The requirement for these premiums to be deducted directly by OPM out of your annuity has been removed. This provides annuitants a similar benefit that active federal employees enjoy with “premium conversion.” These PPA-covered positions are called **Public Safety Officers (PSO)**. For those of you whose annual FEHBP premiums do not reach the \$3,000 amount, consider having your long-term care premium also deducted by OPM so that you reach the \$3,000 ceiling and receive full tax benefits. There was an attempt in early 2024 to increase the maximum exclusion to \$6,000 per year, but that did not make it into law.

If both spouses work for the federal government and the PSO is retiring first, you must do a little bit of math. If your annual premiums are \$3,000 per year or less, then either spouse can carry the FEHBP. If the annual premiums exceed \$3,000 per year, consider keeping the FEHBP with the onboard employee so you take full advantage of premium conversion, which uses pre-tax dollars to pay FEHBP premiums. If both spouses work for the federal government and the non-PSO spouse is retiring first, it will make better sense financially to have the FEHBP carried by the onboard PSO spouse so that you can still utilize premium conversion.

The most current OPM ruling on this matter is dated June 2007 (Benefits Administration Letter (BAL) 07-201¹³³). Do not be confused by earlier OPM memos, which were incorrect. This benefit absolutely applies to retired federal PSOs. The IRS has instructions on page 17 of Publication 721¹³⁴, “Tax Guide to U.S. Civil Service Retirement Benefits,” which mirror the instructions above. Most tax preparation software packages now have the capability to account for this in an automated fashion. TurboTax has this capability. You may have to override fields and handwrite “PSO” on your tax return. If you know anyone that failed to claim this exclusion, he or she can file amended tax returns to claim the savings for up to three previously filed years.

I have been writing about this benefit for many years now, and this topic continues to be in the top ten items that I receive email inquiries about. I’ve had CPAs argue with me that this benefit doesn’t exist! It is real and it does exist.

Also read Chris Barfield’s explanation of this benefit, “Public Safety Officer Deduction Explained.”¹³⁵

¹³³ <https://www.opm.gov/retire/pubs/bals/2007/07-201.pdf>

¹³⁴ <https://www.irs.gov/pub/irs-pdf/p721.pdf>

¹³⁵ <https://www.barfieldfinancial.com/new-blog/public-safety-officer-deduction-explained>