STATE OF DELAWARE
DEPARTMENT OF FINANCE
DIVISION OF REVENUE
601 DELAWARE AVENUE
WILMINGTON, DELAWARE 19899

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## PERSONAL INCOME TAX

- Tax Sheltered Annuities - Basis - Modification

QUESTION: Are payments into tax sheltered annuities deductible from Delaware gross income in 1971 and future years? Will the basis of the annuity be different for State and Federal purposes if payments to the annuity started before 1/1/71?

Payments to approved tax sheltered annuities in 1971 and subsequent years are deductible from Delaware gross income. The adjusted gross income reported on the Federal return will be the same as the State return. Taxpayers will not be required to make any statement on the Delaware return.

On payments made prior to 1971 and where taxpayers were required and did not deduct these payments on the Delaware return the basis would be different. Taxpayers, therefore, upon the receipt of income from the Tax Sheltered Annuity would have to compute the amount reportable to the state and make their modification on the return.

Taxpayers who have moved into Delaware and had a Tax Sheltered Annuity in another state would report as income the same amount as on their Federal return. No adjustment will be necessary and no statement made.

Taxpayers who entered into agreements and/or started payments in 1971 will have the same basis in Delaware as in the Federal return and no adjustment is required.

Taxpayers who have made payments prior to 1971 and have not deducted these amounts from Delaware income in prior years are entitled to recover tax free the amounts on which they already paid tax. It is suggested they use the following method to recover their cost.

$$\frac{\text{Amount paid and not deducted in prior years}}{\text{Total amount paid}} = \text{percentage of recovery}$$

## EXAMPLE

Assume taxpayer has paid into a tax sheltered annuity $5,000 prior to 1971 and not reduced Delaware income during that period. He has also paid into the Tax Sheltered Annuities $5,000 beginning 1/1/71 and reduced his gross income by that amount. His investment in the Tax Sheltered Annuity is $10,000. The reduced amount for Delaware purposes would be 50% until he recovers his $5,000. At that time the entire amount would be taxable and no adjustment to the Federal return will be made.

It is recommended that taxpayers keep records to substantiate the proposed reduction from Federal to State income to be reported. These should include copies of prior year Federal and State returns to determine the basis for Delaware purposes. Modification of income should be on a separate sheet of paper and in detail.

J. H. Kennedy

J. H. Kennedy
Director of Revenue

jvm

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