

AN ALERT FROM THE BDO EXECUTIVE AND HR SERVICES PRACTICE

BDO KNOWS: COMPENSATION & BENEFITS



► SUBJECT

QUALITY STORES FICA MATTER SETTLED BY SUPREME COURT - SEVERANCE PAYMENTS ARE SUBJECT TO FICA TAX

► SUMMARY

In a unanimous decision on March 25, 2014, the Supreme Court held in favor of the government that the broad definition of wages in section 3121, for purposes of taxes under the Federal Insurance Contributions Act ("FICA"), includes severance payments made to the Quality Stores employees (*United States v. Quality Stores, Inc.*, No. 12- 1408 (2014)).

The Court's opinion tracks very closely to the analysis and arguments in the government's brief, including reliance on *Rowan Cos. V. United States*, 452 U.S. 247 (1981). This decision established the principle that (i) simplicity of administration and (ii) consistent interpretation of statutory language dictate that the definition of "wages" should generally be the same for purposes of FICA taxes and federal income tax withholding.

In fact, the Court's interpretation of the types of separation payments that are excludable from FICA tax is arguably narrower than the criteria the Service used in Rev. Rul. 90-72 for payments under a supplemental unemployment benefits trust arrangement. So it remains to be seen whether the Service will seek to modify or revoke this ruling (and the earlier rulings from the 1950s).

Accordingly, there is no need to file protective claims for FICA taxes paid on 2010 severance payments before April 15, 2014, based on the Sixth Circuit's decision in *Quality Stores*, or to pursue claims previously rejected by the Service.

CONTACT:

ANDREW GIBSON
404-979-7106
agibson@bdo.com

TONY DASILVA
617-239-7036
tdasilva@bdo.com

PETER KLINGER
415-490-3214
pklinger@bdo.com

IRA MIRSKY
301-634-4959
imirsky@bdo.com

CARL TOPPIN
212-885-8331
ctoppin@bdo.com

JOAN VINES
301-634-0250
jvines@bdo.com

► BACKGROUND

In *Quality Stores*, the United States Court of Appeals for the Sixth Circuit held that payments made by a company to employees as part of a severance program were not subject to FICA taxes. The court's decision was in conflict with the decision of the United States Court of Appeals for the Federal Circuit in *CSX Corp. v. United States*, 518 F.3d 1328 (Fed. Cir. 2008), that the payments were dismissal pay subject to FICA tax. Accordingly, the Supreme Court agreed to review the Sixth Circuit's holding that supplemental unemployment compensation benefit payments—a term which includes severance pay—were not subject to FICA tax.

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