
Government requests extension to file Supreme Court petition in *Quality Stores* as important April 15 deadline quickly approaches

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In brief

On March 25, the US Supreme Court granted the government an extension to file the petition requesting consideration of the issue in *Quality Stores* as to whether certain severance payments are wages for FICA tax purposes. The due date of the petition is now May 3, 2013. Unfortunately, this extension does not change the fact that employers that made severance payments during 2009 must file a claim by April 15, 2013 in order to protect their right and those of the affected employees to a FICA tax refund.

In detail

The issue in *Quality Stores* is whether SUB pay is wages for FICA tax purposes. SUB pay is a type of severance payment made to employees as a result of an involuntary reduction in force. It is the position of the IRS that severance pay must be linked to the receipt of state unemployment insurance benefits in order to qualify as SUB pay. As a result, lump-sum severance payments or periodic payments of severance pay that are not linked to state unemployment insurance cannot qualify for the exemption from FICA taxes. In *CSX Corp. v. United States*, the United States Court of Appeals for the Federal Circuit adopted and applied this definition and held that SUB pay constituted

wages for FICA purposes. The Sixth Circuit disagreed with this interpretation and held that severance payments do not need to be linked to state unemployment insurance in order to qualify for the exception from FICA taxes, creating a split between federal circuit courts.

What's next?

The IRS estimates that the total dollar amount at stake as a result of the *Quality Stores* decision is over \$1 billion. Given the circuit split, the amount at issue and the desirability of a standardized rule, the IRS is expected to seek Supreme Court review. If the Supreme Court grants review and concurs with the Sixth Circuit, employers should be able to obtain refunds for FICA taxes paid on

severance payments made to employees on account of involuntary workforce reductions. If the Supreme Court declines to hear the case, the IRS may grant refunds to employers whose principal places of business are located in the Sixth Circuit (that is, Kentucky, Michigan, Ohio, and Tennessee) and continue to contest refund claims elsewhere. However, in order for any employer to obtain a future refund based on *Quality Stores*, the employer must file a refund claim.

Employer action required

The deadline for filing protective claims for 2009 is quickly approaching - employers must file by April 15, 2013 in

order to preserve their rights to a future refund. All employers that have paid severance in connection with involuntary workforce reductions should consider filing refund claims. A protective claim preserves the employer's right to receive a FICA tax refund in the event the Supreme Court agrees to review the *Quality Stores* decision and decides in favor of the taxpayer.

The process for filing protective refund claims is relatively straightforward. To be valid it must contain key information, such as the essential nature of the claim and the contingencies affecting the claim. It does not have to state a particular dollar amount.

Outside the Sixth Circuit, the IRS has been denying refund claims and will

likely continue to do so until final resolution of the *Quality Stores* case. A taxpayer has two years from the date of the Notice of Claim Denial to file a refund suit in the US District Court or in the US Court of Federal Claims. Alternatively, a taxpayer may file an administrative appeal within 30 days. If the issue remains unresolved at the end of the two year period, an employer should consider filing Form 907, *Agreement to Extend the Time to Bring Suit*, to preserve its right to receive a FICA tax refund either through the IRS Appeals Office or through the courts. Inside the Sixth Circuit, the IRS has suspended all action with respect to the *Quality Stores* claims.

Employers should continue to withhold FICA taxes on all severance

payments made to workers as a result of an involuntary reduction in force until the issue is ultimately resolved. In addition, it is imperative that employers maintain employee wage data in order to perfect its refund claims if the matter is ultimately resolved in favor of the taxpayer.

The takeaway

Employers that made severance payments in 2009 in connection with involuntary reductions in force should consider filing protective tax refund claims by April 15, 2013. In addition, employers should monitor the two year period for filing suit, continue to withhold on future SUB payments, and maintain adequate records.

Let's talk

For more information, contact your PwC team or the authors:

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