

April 3, 2014

U.S. Supreme Court Rules That Severance Payments are Taxable Under FICA

On March 25, 2014, the United States Supreme Court ruled that severance payments made to involuntarily terminated employees are taxable under the Federal Insurance Contributions Act, 26 U.S.C. § 3101 *et seq.* ("FICA"). The Court's ruling in *United States v. Quality Stores, Inc.*, No. 12-1408, 572 U.S. __ (2014), resolves a Circuit split on this issue.

In 2001, Quality Stores, Inc., an agricultural-specialty retailer, terminated thousands of employees prior to entering Chapter 11 bankruptcy proceedings. The company reported the severance payments as wages on W2 forms and paid the required taxes, but later filed a refund claim seeking more than \$1 million in FICA taxes. The Court reversed the decisions of the District Court and Sixth Circuit, which had both held that severance payments were not "wages" under FICA. Justice Kennedy, writing for the Court, concluded that because the severance payments "were made to employees terminated against their will, were varied based on job seniority and time served, and were not linked to the receipt of state unemployment benefits," the severance payments constituted taxable wages under "FICA's broad definition."

It is important to review your severance agreements and policies to ensure that they are in compliance with this ruling. If you have any questions about this, or any other aspect of the Court's decision, please contact Laura Monaco at (212)-758-7754 or any other attorney at the Firm.

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