

FICA TAXATION OF POST-EMPLOYMENT BENEFITS: A STATUTORY PUZZLE AND SOCIOPOLITICAL CONUNDRUM

I. AN INTRODUCTION TO THE SOCIOPOLITICAL CONUNDRUM

“Great cases, like hard cases, make bad law.”¹ One might wonder, then, what can be expected of cases that are both great and hard? This Note discusses such an issue—the imposition of FICA tax on severance payments—and the result has been cases that present highly technical, reasoned analyses with conflicting conclusions. While it may seem doubtful that this issue deserves such an admittedly dramatic description,² upon closer inspection, it appears warranted: this issue involves sympathetic stakeholders on both sides, the political minefield of the payroll tax, the complexity of the tax code, conflicting legal authority, and a sensitive, post-recession economic backdrop, and now, an imminent Supreme Court case.

The 2012 election cycle and the political negotiations arising from the attempt to avoid the “fiscal cliff” shortly thereafter³ reignited debate on the role of social insurance programs and notions of shared responsibility. The expiration of a payroll tax cut, effective January 1, 2013,⁴ also reminded working Americans of their own role in funding Social Security and Medicare, and, to some, signaled a political calculation that the Social Security and Medicare programs need that extra percentage of taxpayers’

1. *N. Sec. Co. v. United States*, 193 U.S. 197, 400 (1904) (Holmes, J., dissenting). Justice Holmes clarified that “great cases are called great, not by reason of their real importance in shaping the law of the future, but because of some accident of immediate overwhelming interest which appeals to the feelings and distorts the judgment.” *Id.* at 400–01.

2. See BRYAN A. GARNER, *A DICTIONARY OF MODERN LEGAL USAGE* 398 (2d ed. 1995) (warning that the “hard cases make bad law” “cliché is probably used as frequently today as it ever was—and sometimes unmeaningfully.”).

3. Ben Bernanke, chairman of the Federal Reserve, coined the phrase “fiscal cliff” to refer to the consequences our economy could face if Congress was unable to agree on a deficit-reduction bill. For a straightforward explanation of the fiscal cliff and related issues, see Jackie Calmes, *Demystifying the Fiscal Impasse That Is Vexing Washington*, N.Y. TIMES, Nov. 16, 2012, at A20, available at <http://www.nytimes.com/2012/11/16/us/politics/the-fiscal-cliff-explained.html>. See also Editorial, *A Tepid Fiscal Agreement*, N.Y. TIMES, Jan. 1, 2013, at A18, available at <http://www.nytimes.com/2013/01/01/opinion/a-tepid-agreement-on-the-fiscal-cliff.html>.

4. See IRS PROVIDES UPDATED WITHHOLDING GUIDANCE, IR-2013-1 (Jan. 3, 2013), available at <http://www.irs.gov/uac/Newsroom/IRS-Provides-Updated-Withholding-Guidance-for-2013> (Last updated Jan. 24, 2013) (“[E]mployers should also begin withholding Social Security tax at the rate of 6.2 percent of wages paid following the expiration of the temporary two-percentage-point payroll tax cut in effect for 2011 and 2012.”).

income more than the taxpayers do.⁵ At the heart of all of this discussion is the Federal Insurance Contributions Act (FICA), the chapter in the tax code that created a payroll tax on employees and employers to contribute to the funding of Social Security and Medicare programs.⁶

The taxation of severance payments, in particular, adds a layer of complexity to the sociopolitical issues that are already presented by FICA, Social Security, and Medicare. On the one hand, furthering the lofty goals of Social Security and Medicare and continuing to provide much-needed support to elderly Americans might suggest the need to reach as broad of a tax base as possible. On the other hand, severance payments are an especially delicate source of income. As our country emerges from a recession, many Americans are unemployed; those fortunate enough to receive some form of severance payment from their former employers may be without another source of income for an extended period of time, thereby making a tax on that severance payment particularly burdensome.⁷ It becomes clear that there are many conflicting interests at stake and that no matter how the calculation is resolved, one side faces a discernible loss of revenue or income at a time when neither can afford it.⁸

5. See *infra* note 67; PAYROLL TAX CUT TO BOOST TAKE-HOME PAY FOR MOST WORKERS; NEW WITHHOLDING DETAILS NOW AVAILABLE ON IRS.GOV, IR-2010-124 (Dec. 17, 2010), available at <http://www.irs.gov/uac/Payroll-Tax-Cut-to-Boost-Take-Home-Pay-for-Most-Workers;-New-Withholding-Details-Now-Available-on-IRS.gov> (Last updated Aug. 3, 2012); PAYROLL TAX CUT EXTENDED TO THE END OF 2012; REVISED PAYROLL TAX FORM NOW AVAILABLE TO EMPLOYERS, IR-2012-27 (Feb. 23, 2012), available at <http://www.irs.gov/uac/Payroll-Tax-Cut-Extended-to-the-End-of-2012;-Revised-Payroll-Tax-Form-Now-Available-to-Employers> (Last Updated Aug. 4, 2012). For a not-so-gentle reminder that the expiration of the payroll tax holiday is not *really* a tax increase, see Tony Nitti, *Dear America: Your Higher Payroll Taxes Are Not The Result Of A Tax Increase*, FORBES (Jan. 14, 2013, 10:37 PM), <http://www.forbes.com/sites/anthonymitti/2013/01/14/dear-america-your-higher-payroll-taxes-are-not-the-result-of-a-tax-increase>. See also Zachary A. Goldfarb, *Amid Standoff, End of a Long Era of Falling Taxes*, WASH. POST, Jan. 1, 2013, at A01.

6. See I.R.C. § 3128 (2006).

7. In April 2013, 37.4% of unemployed persons had been unemployed for twenty-seven weeks or longer. BUREAU OF LABOR STATISTICS, U.S. DEP'T OF LABOR, ECONOMIC NEWS RELEASE, TABLE A-12, UNEMPLOYED PERSONS BY DURATION OF UNEMPLOYMENT, available at <http://www.bls.gov/news.release/empst.t12.htm> (Last modified Oct. 22, 2013). Many view payroll taxes as regressive, placing a greater burden on lower-income workers than those earning a higher income, adding another layer to the already-delicate discussion. See, e.g., Paul Krugman, *Lucky Ducky Redux*, N.Y. TIMES (Apr. 8, 2010, 5:09 PM), <http://krugman.blogs.nytimes.com/2010/04/08/lucky-ducky-redux>. But see Kip Hagopian & Lee E. Ohanian, *Payroll Taxes Are 'Regressive'? Time to Rethink That Idea*, WALL ST. J., Oct. 30, 2012, at A23, available at <http://online.wsj.com/article/SB10000872396390443684104578063140488175464.html> (suggesting that these payroll taxes are not actually regressive, despite common claims to the contrary).

8. This Note intends to take no position on the normative desirability of these programs, but rather, assumes for the sake of argument that, at the very least, maintaining Social Security and Medicare in some form is an important political objective. The term "side" is used loosely here and is not intended to evoke feelings of conflict between the Government and the people. Rather, the conflict is one between interests; on one "side" is the interest of the Government in generating revenue to fund

This particular issue, whether severance payments are “wages” subject to FICA taxation, has been characterized as a “straightforward, but legally-confounding question,”⁹ but, as will be discussed, it is generous to refer to this issue as “straightforward” at all. In September 2012, the Sixth Circuit decided *In re Quality Stores*,¹⁰ holding that the payments were not taxable. Because the Federal Circuit had previously held that the payments *are* taxable as wages,¹¹ most recently in the 2008 case *CSX Corporation v. United States*,¹² the Sixth Circuit opinion created a circuit split. With such complex political, social, and economic interests implicated in the determination that severance payments are (or are not) subject to FICA tax, a disagreement among the circuit courts of appeal creates a renewed urgency for due consideration of the Social Security and Medicare programs and the FICA tax that funds them.

In Part II, this Note examines the historical context of Social Security and Medicare, subsequently providing a descriptive overview of FICA and the severance payments at issue. Part III discusses the factual background of *In re Quality Stores*¹³ and *CSX Corporation v. United States*,¹⁴ the cases

Social Security and Medicare, and on the other “side” is the interest of the individual in limiting tax liability upon termination from employment. Surely the people have a strong interest in Social Security and Medicare, based on their status as entitlement programs, and surely the Government has an interest in lessening the burden of unemployment on its citizens. In short, while framed as a conflict between “sides,” this issue has an enormously broad reach that affects all Americans.

9. *In re Quality Stores, Inc.*, 424 B.R. 237, 239 (W.D. Mich. 2010), *aff'd*, 693 F.3d 605 (6th Cir. 2012). The Court, in further framing the issue before it, noted the complexity of the analysis:

The few courts that have addressed this issue, or variations of it, have reached directly opposing outcomes. Where one court has found severance payments to be subject to taxation, the next has reached the opposite conclusion. The fact that the Internal Revenue Service has itself charted a path of “reverse-course” rulings on this issue since the 1950s only adds to the difficulties faced by the courts in attempting to reach a reasoned resolution by explaining and accounting for this repeated change in agency position.

To say that these differing rulings are simply the product of results-oriented decision-making is tempting, but unsupportable. The courts have not only diligently wrestled with the justification for their conclusions, but also endeavored to fashion some appropriate, logical framework for the analysis of this issue.

Id. at 240. For a brief overview of the issue and a discussion of the practical stakes, see generally Laura Saunders, *When Severance Pay Is Subject to Payroll Tax*, WALL ST. J., Oct. 26, 2012, at B9, available at <http://online.wsj.com/article/SB10001424052970203937004578079192865327704.html>.

10. 693 F.3d 605 (6th Cir. 2012), *reh'g en banc denied*, 2013 WL 673917, 111 A.F.T.R. 2d 2013-494 (6th Cir. 2013).

11. See generally Jeremy L. Hirsh, Note, *The Wages of Not Working: FICA Liability for Severance Payments in Associated Electric Cooperative, Inc. v. United States*, 54 TAX LAW. 811 (2001) (discussing *Associated Elec. Coop., Inc. v. United States*, 226 F.3d 1322 (Fed. Cir. 2000), a predecessor to *CSX Corp. v. United States*, 518 F.3d 1328 (Fed Cir. 2008)).

12. *CSX Corp.*, 518 F.3d 1328.

13. 693 F.3d 605.

14. 518 F.3d 1328.

that created a circuit split on the issue of withholding FICA tax from severance payments. Part IV will introduce each component of the relevant authority on this issue and will undertake a detailed analysis of the courts' treatment of the authority. Finally, in Part V, this Note will weigh the competing interests and various options and propose both a short-term solution for courts and a long-term solution for Congress.

II. HISTORY AND BACKGROUND: THE MAKINGS OF A "GREAT CASE"¹⁵

A. *Social Security and Medicare: History, Status, and Sustainability*

With all discussions of normative desirability and feasibility aside, Social Security and Medicare play an important role in the lives of the programs' beneficiaries and in our society.¹⁶ To understand the political, economic, and social importance of Social Security and Medicare, one must understand their background. These programs were enacted only after great difficulty and remain a proud accomplishment of our political system, despite any discord surrounding their present operation. The political discourse from the beginnings of both of these programs is strikingly similar; there is a recurring sense of urgency and social necessity followed by a deep appreciation of the difficulty of their design and enactment.¹⁷

1. *A Brief History of Social Security*

The Social Security Act,¹⁸ enacted in 1935, was designed to protect against the "hazards and vicissitudes of life."¹⁹ As the first comprehensive social welfare policy, "[t]he Social Security Act provided a policy

15. *N. Sec. Co. v. United States*, 193 U.S. 197, 400 (1904) (Holmes, J., dissenting); *see supra* text accompanying note 1.

16. There is little room to dispute that, if nothing else, Social Security and Medicare play an important role in our society because of their size. In 2011, the combined cost of Social Security and Medicare was about 8.5% of GDP. SOC. SEC. ADMIN., STATUS OF THE SOCIAL SECURITY AND MEDICARE PROGRAMS: A SUMMARY OF THE 2012 ANNUAL SOCIAL SECURITY AND MEDICARE TRUST FUND REPORTS 2, *available at* <http://www.ssa.gov/oact/TRSUM/tr12summary.pdf> [hereinafter TRUSTEES' REPORTS]. Unarguably, these programs can be a matter of life and death for their beneficiaries.

17. *See infra* text accompanying notes 21–23.

18. 42 U.S.C. § 301 et seq. (2006).

19. ANDREW DOBELSTEIN, UNDERSTANDING THE SOCIAL SECURITY ACT: THE FOUNDATION OF SOCIAL WELFARE FOR AMERICA IN THE TWENTY-FIRST CENTURY 3 (2009) (quoting H.R. Doc. No. 73-397 (1934)). *See generally* *Social Security History*, SSA.GOV, <http://www.ssa.gov/history/> (last visited Nov. 7, 2013) (providing a historical overview of the Social Security Act).

framework for administering retirement and unemployment insurance as well as providing welfare payments to aged adults, the disabled blind, and children.”²⁰ Upon signing, President Roosevelt recognized the attempt “to frame a law which will give some measure of protection to the average citizen and to his family against the loss of a job and against poverty-ridden old age.”²¹

Despite constitutional challenges, the Social Security Act has been upheld as within Congress’s power to levy a tax for the promotion of the general welfare.²² In validating the constitutionality of the tax imposed on wages to fund Social Security, the Supreme Court echoed the theme of necessity, noting, “the number of the unemployed mounted to unprecedented heights” and declaring, “[i]t is too late today for the argument to be heard with tolerance that in a crisis so extreme the use of the moneys of the nation to relieve the unemployed and their dependents is a use for any purpose narrower than the promotion of the general welfare.”²³

The implementation program for Social Security is, in essence, a “contractual relationship between those who worked and were taxed to ensure economic benefits for themselves and their dependents.”²⁴ Many studies have attempted to address “whether an individual or group of persons can expect to get a ‘fair’ return in the form of benefits for the tax

20. DOBELSTEIN, *supra* note 19, at 3.

21. Presidential Statement on Signing the Social Security Act (Aug. 14, 1935), *available at* <http://www.ssa.gov/history/fdrstmts.html#signing>. President Roosevelt further explained:

This law, too, represents a cornerstone in a structure which is being built but is by no means complete. It is a structure intended to lessen the force of possible future depressions. It will act as a protection to future Administrations against the necessity of going deeply into debt to furnish relief to the needy. The law will flatten out the peaks and valleys of deflation and of inflation. It is, in short, a law that will take care of human needs and at the same time provide the United States an economic structure of vastly greater soundness.

22. *See* U.S. CONST. art. I, § 8.

23. *Charles C. Steward Mach. Co. v. Davis*, 301 U.S. 548, 586–87 (1937). The Court vividly described the circumstances of the passage of the Social Security Act:

During the years 1929 to 1936, when the country was passing through a cyclical depression, the number of the unemployed mounted to unprecedented heights. Often the average was more than 10 million; at times a peak was attained of 16 million or more. Disaster to the breadwinner meant disaster to dependents. Accordingly the roll of the unemployed, itself formidable enough, was only a partial roll of the destitute or needy. The fact developed quickly that the states were unable to give the requisite relief. The problem had become national in area and dimensions. There was need of help from the nation if the people were not to starve.

Id. at 586. Later, in *United States v. Silk*, 331 U.S. 704, 712 (1947), the Court reinforced the notion that the Social Security Act is “an attack on recognized evils in our national economy.”

24. DOBELSTEIN, *supra* note 19, at 27.

contributions made.”²⁵ Recognizing that the program is designed “to provide a minimally adequate ‘floor of protection’” for low-earning workers in addition to “a reasonably equitable return for even the highest-paid workers,” it is noted that the structure creates “divergent rates of return for different groups of workers.”²⁶ Notably, however, the “monetary and social value of the program to higher-paid workers transcends the amount of benefits that they may personally expect to receive.”²⁷ Under this view, even if the financial returns are lower than a private investment or annuity, there is a discernible benefit to all workers.²⁸

Although it “resembles its original form,” the Social Security Act has “expanded beyond anything envisioned by its 1935 developers.”²⁹ As of June 30, 2013, there were approximately 57,469,000 beneficiaries, and eighty-eight percent of the population over the age of sixty-five received Social Security benefits.³⁰ Still, Social Security is “a cornerstone in a structure [that is] by no means complete” on its own.³¹ Medicare adds to that structure.

2. A Brief History of Medicare

Medicare was signed into law on July 30, 1965.³² In his remarks on the date the bill was signed, President Johnson paid homage to the

25. Yung-Ping Chen & Stephen C. Goss, *Are Returns on Payroll Taxes Fair?*, in *SOCIAL SECURITY IN THE 21ST CENTURY* 76, 76 (Eric R. Kingson & James H. Schulz eds., 1997).

26. *Id.*

27. *Id.* Chen & Goss note:

Absent Social Security, many lower-paid workers could not save enough to provide a minimally adequate retirement income and would thus require some form of public assistance in their old age. The mandatory withholding of Social Security payroll taxes from the lower-paid workers assures that they will make some reasonable contribution toward the cost of their retirement income. The resulting cost to the higher-paid of subsidizing the retirement income needs of the lower-paid is thus almost certainly less when financed through the Social Security program than if, for example, it were financed with income taxes through public assistance.

Id. at 76–77.

28. *Id.* This basic assumption that there is *some* benefit to all workers is intended to be non-controversial and underlies the discussion in this Note.

29. DOBELSTEIN, *supra* note 19, at 3.

30. SOCIAL SEC. ADMIN., FACT SHEET ON THE OLD-AGE, SURVIVORS, AND DISABILITY INSURANCE PROGRAM (July 24, 2013), available at http://www.ssa.gov/OACT/FACTS/fs2013_06.pdf.

31. Presidential Statement on Signing the Medicare Bill (July 30, 1965), available at <http://www.lbjlib.utexas.edu/johnson/archives.hom/speeches.hom/650730.asp> (quoting from President Roosevelt’s Statement on Signing the Social Security Act).

32. Medicare was enacted in the Social Security Amendments of 1965, Pub. L. 89–97, 79 Stat. 286.

foundational work in the passage of the Social Security Act, echoing its rhetoric and crediting the efforts of President Truman twenty years earlier. “[T]he need for this action is plain”, he said, “and it is so clear indeed that we marvel not simply at the passage of this bill, but . . . that it took so many years to pass it.”³³

Medicare is a complex program, the intricacies of which are beyond the scope of this Note.³⁴ At its core, however, Medicare provides certain health insurance to individuals over age sixty-five, and to certain disabled individuals under age sixty-five.³⁵ Medicare “Part A” provides hospital insurance,³⁶ and “Part B” provides supplementary medical insurance benefits.³⁷ Medicare “Part C,” also known as “Medicare+Choice” provides an alternative to Parts A and B and allows beneficiaries to receive their insurance benefits from certain private providers.³⁸ Medicare “Part D” provides prescription drug coverage.³⁹

Medicare’s primary purpose is fundamentally different from that of Social Security—it endeavors to provide federal health insurance to the elderly, rather than provide retirement income.⁴⁰ Medicare is funded in part by payroll taxes, just like Social Security, but because of its different purpose, the logic of a Medicare payroll tax is different from the basis of Social Security.⁴¹ While a Social Security payroll tax is premised in part on a contractual relationship between those who work and the Social Security Administration, thus creating an earnings-related benefit, a Medicare payroll tax takes the form of social insurance.⁴²

33. Presidential Statement on Signing the Medicare Bill, *supra* note 31.

34. Unfortunately, those seeking its benefits cannot brush aside Medicare’s complexities so quickly. See JONATHAN OBERLANDER, *THE POLITICAL LIFE OF MEDICARE* 52 (2003) (discussing relevant studies and noting that “[q]uite simply, many of the elderly do not understand the limitations of Medicare coverage”).

35. 42 U.S.C. § 426 (2006).

36. See 42 U.S.C. § 1395c (2006).

37. See 42 U.S.C. § 1395j (2006).

38. See 42 U.S.C. § 1395w-21 (2006 & Supp. V 2012).

39. See § 1395w-101 (2006 & Supp. V 2012).

40. OBERLANDER, *supra* note 34 at 17. This system is unique in that “no other industrial democracy . . . has compulsory health insurance for its elderly citizens alone, and none has started its program with such a beneficiary group.” *Id.* (quoting Theodore Marmor, *Coping with a Creeping Crisis: Medicare at Twenty*, in *SOCIAL SECURITY: BEYOND THE RHETORIC OF CRISIS* 178 (Theodore R. Marmor & Jerry L. Mashaw eds., 1988).

41. *Id.* at 76.

42. See DOBELSTEIN, *supra* note 19, at 27. See also OBERLANDER, *supra* note 34, at 76. Although Social Security is in part a contract between workers and the Social Security Administration, it does have a social insurance aspect, similar to Medicare. The programs have many similarities, but their differences are important in shaping policy discussions. See *supra* notes 20–21 and accompanying text.

3. *The Status and Sustainability of Social Security and Medicare*

Despite a steady increase in the payroll tax rate over time,⁴³ projections show that Social Security and Medicare “are not sustainable under currently scheduled financing and will require legislative action to avoid disruptive consequences.”⁴⁴ Naturally, the 2012 election cycle brought these programs—and their projected longevity—to the front of public discourse once again. The Democratic and Republican party platforms addressed Medicare and Social Security,⁴⁵ as did the candidates in the presidential debates.⁴⁶ Discussions surrounding the “fiscal cliff” further revived the ongoing debate again in December 2012.⁴⁷ Despite the sense of urgency and what seemed to be an ideal forum for substantively addressing the role of Social Security and Medicare in our country, much was left to be dealt with later.⁴⁸

43. See *infra* Part II.B for a discussion of FICA, the payroll tax at issue.

44. TRUSTEES’ REPORT, *supra* note 16, at 1.

45. The Democratic Platform characterized the Republican budget proposal as one that would “end Medicare as we know it,” contending further that “Medicare is a sacred compact with our seniors” that must be preserved. The Platform concluded: “Democrats believe that Social Security and Medicare must be kept strong for seniors, people with disabilities, and future generations. Our opponents have shown a shocking willingness to gut these programs to pay for tax cuts for the wealthiest, and we fundamentally reject that approach.” DEMOCRATIC NATIONAL CONVENTION, MOVING AMERICA FORWARD: 2012 DEMOCRATIC NATIONAL PLATFORM, available at <http://assets.dstatic.org/dnc-platform/2012-National-Platform.pdf>.

By contrast, the Republican Platform focused on the cost of these programs, arguing that it was “already harming job creation and growth” and that “projections of future spending growth are nothing short of catastrophic, both economically and socially.” REPUBLICAN NATIONAL CONVENTION, BELIEVE IN AMERICA: 2012 REPUBLICAN PLATFORM 23, available at <http://www.gop.com/wp-content/uploads/2012/08/2012GOPPlatform.pdf>. However, the Platform contended that the Republican Party was “committed to saving Medicare . . . by modernizing it, by empowering its participants, and by putting it on secure financial footing.” *Id.* at 21. But see Gary King & Samir S. Soneji, *Social Security: It’s Worse Than You Think*, N.Y. TIMES, Jan. 6, 2013, at SR4, available at <http://www.nytimes.com/2013/01/06/opinion/sunday/social-security-its-worse-than-you-think.html> (arguing that while President Obama and Governor Romney agreed that Social Security should not be changed, “both were utterly wrong”).

46. Jeff Zeleny & Jim Rutenberg, *Obama and Romney, in First Debate, Spar Over Fixing the Economy*, N.Y. TIMES, Oct. 4, 2012, at A1, available at <http://www.nytimes.com/2012/10/04/us/politics/obama-and-romney-hold-first-debate.html>. In the first presidential debate, President Obama suggested that health care costs must be lowered to sustain Medicare, but that structural changes to Social Security are not necessary. See *Transcript of the First Presidential Debate*, N.Y. TIMES (Oct. 3, 2012), <http://www.nytimes.com/2012/10/03/us/politics/transcript-of-the-first-presidential-debate-in-denver.html>. Governor Romney noted his agreement that Social Security should not be changed for people aged 60 or older. See *id.* His position on Medicare was that President Obama had planned to cut the program and that he, as president, would continue Medicare but also offer private vouchers as an option to seniors. See *id.*

47. See *supra* note 3.

48. The Trustees’ Report urges: “If lawmakers act sooner rather than later, they can consider more options and more time will be available to phase in the changes, giving the public adequate time

These concerns, however, do not necessarily signal imminent demise for Social Security or Medicare. In fact, some commentators argue that we should generally “have confidence in the long-run viability of” the Social Security trust fund (OASDI)⁴⁹ because, in part, of its great flexibility.⁵⁰ This flexibility is, “namely, that both benefit and financing provisions can be altered to meet changing social, economic, and demographic conditions.”⁵¹ Important aspects of this flexibility are, of course, the structure and sources of funding.

B. The FICA Payroll Tax

FICA, the Federal Insurance Contributions Act,⁵² funds Social Security and Medicare by imposing a tax on “every individual” equal to a certain percentage of “wages . . . received by him with respect to employment.”⁵³ “Employment” is defined broadly to include “any service, of whatever nature, performed . . . by an employee for the person employing him.”⁵⁴ The term “wages” means, with certain enumerated exclusions, “all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash.”⁵⁵

The tax is collected by the employer, who “deduct[s] the amount of the tax from the wages as and when paid.”⁵⁶ The employer also pays its own share—an “excise tax” equal to a percentage of the wages paid to its employees.⁵⁷ The percentage deducted from employees’ wages is equal to the percentage that employers pay; in effect, each party pays half of the total tax collected on each employee’s wages.⁵⁸

to prepare.” TRUSTEE’S REPORT, *supra* note 16, at 1. However, if the “fiscal cliff” negotiations are any indication, such action is unlikely to take materialize. See Janet Hook, Corey Boles & Siobhan Hughes, *Congress Passes Cliff Deal*, WALL ST. J., Jan. 2, 2013, <http://online.wsj.com/article/SB10001424127887323320404578215373352793876.html> (referring to the passage as breaking a “rancorous stalemate,” but leaving “a host of issues unresolved and guarantee[ing] continued budget clashes between the parties”).

49. See TRUSTEES’ REPORTS, *supra* note 16, at 1; see also *infra* text accompanying notes 60–61.

50. Robert J. Myers, *Will Social Security Be There for Me?*, in SOCIAL SECURITY IN THE 21ST CENTURY, *supra* note 25, at 208, 214–15.

51. *Id.* at 215.

52. I.R.C. §§ 3101–3128 (2006 & Supp. V 2012).

53. I.R.C. § 3101(a) (2006 & Supp. V 2012).

54. I.R.C. § 3121(b) (2006 & Supp. V 2012).

55. I.R.C. § 3121(a) (parentheses in original).

56. I.R.C. § 3102 (2006 & Supp. V 2012).

57. I.R.C. § 3111(a) (2006 & Supp. V 2012).

58. See I.R.C. § 3111(a)-(b) (currently requiring the employer to pay 6.2% of its employees’ wages to Old-Age, Survivors, and Disability Insurance, plus 1.45% to Hospital Insurance) and I.R.C.

FICA-generated revenue is credited to four separate trust funds managed by the Department of the Treasury.⁵⁹ The Old-Age and Survivors Insurance (OASI) Trust Fund pays retirement and survivors benefits, while the Disability Insurance (DI) Trust Fund pays disability benefits.⁶⁰ These two trust funds together are known as OASDI, which collectively pay Social Security benefits.⁶¹ The Hospital Insurance (HI) Trust Fund pays for inpatient hospital care, while the Supplementary Medical Insurance (SMI) Trust Fund covers Medicare Part B and Medicare Part D.⁶² The Social Security Administration notes that in 2011, “44.8 million people received OASI benefits, 10.6 million received DI benefits, and 48.7 million were covered under Medicare.”⁶³

Prior to the enactment of Social Security, the proposed funding structure, i.e. the tax plan, created discord among policymakers who were considering “how to schedule the taxes over time and how to blend payroll taxes and general revenues.”⁶⁴ At a time when ninety-five percent of Americans did not pay income taxes, a payroll tax seemed to be the most viable option for generating revenue; various proposals, however, showed the program incurring a deficit by 1967.⁶⁵ President Roosevelt insisted on a structure that would not allow a deficit, and committee staff ultimately developed a plan in which employees and employers would pay a combined 2% tax on the first \$3000 of income (each paying 1%), with the combined percentage increasing to 5% by 1957 (whereby the employee and the employer would each pay 2.5%).⁶⁶ As of January 1, 2013, employees and employers each pay a 7.65% payroll tax to fund Social Security and Medicare programs.⁶⁷

§ 3101(a)-(b) (establishing the same percentages for Old-Age, Survivors, and Disability Insurance and Hospital Insurance, respectively).

59. TRUSTEES' REPORTS, *supra* note 16, at 1.

60. *Id.*

61. *Id.*

62. *Id.* Part B covers physician and outpatient services, while Part D covers prescription drug benefits.

63. *Id.*

64. Edward D. Berkowitz, *The Historical Development of Social Security in the United States*, in SOCIAL SECURITY IN THE 21ST CENTURY, *supra* note 25, at 22, 24.

65. See Berkowitz, *The Historical Development of Social Security in the United States*, in SOCIAL SECURITY IN THE 21ST CENTURY, *supra* note 25, at 22, 24.

66. Berkowitz, *The Historical Development of Social Security in the United States*, in SOCIAL SECURITY IN THE 21ST CENTURY, *supra* note 25, at 22, 24.

67. Since 1990, the FICA tax rate has been 7.65% (including Social Security tax of 6.2% and hospital insurance tax of 1.45%) for employees and employers, or a combined percentage of 15.3%. See I.R.C. § 3101(a)-(b) (2006 & Supp. V 2012); SOCIAL SEC. ADMIN., SOCIAL SECURITY & MEDICARE TAX RATES, available at <http://www.ssa.gov/oact/progdata/taxRates.html> (website last modified Mar. 8, 2012). The payroll tax was lowered for the years 2011 and 2012 as part of the Tax

C. Severance Payments

With this background on Social Security, Medicare, and FICA in mind, the ensuing discussion will require an understanding of the other major element of this issue: severance payments. As if the sociopolitical-sensitivity level were not high enough by virtue of the payroll tax and its role in funding social welfare programs, adding severance payments to the equation introduces the complication of post-recession recovery and ongoing unemployment issues.

The term “severance payments” encompasses a broad range of payments to individuals whose employment has been terminated in some way. The payments can arise from layoffs, as part of an early retirement program, or they can resemble a pension benefit.⁶⁸ Generally speaking, however, this type of payment is governed by an employment contract and is strictly a matter between the employer and the employee.⁶⁹ Broadly speaking, severance packages provide a form of security for both the employer and the employee, hence their place in many employment agreements.⁷⁰

Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010. Pub. L. No. 111-312, 124 Stat. 3296. This reduced the Social Security tax withholding from 6.2% of wages to 4.2% of wages. The hospital insurance tax remained at 1.45%, so each of employers and employees paid a total of 5.65% in 2011 and 2012. See PAYROLL TAX CUT TO BOOST TAKE-HOME PAY FOR MOST WORKERS; NEW WITHHOLDING DETAILS NOW AVAILABLE ON IRS.GOV, IR-2010-124 (Dec. 17, 2010), available at <http://www.irs.gov/uac/Payroll-Tax-Cut-to-Boost-Take-Home-Pay-for-Most-Workers;-New-Withholding-Details-Now-Available-on-IRS.gov>. See also I.R.C. § 3111(a)-(b) (2006 & Supp. V 2012); I.R.C. § 3101(a)-(b) (2006 & Supp. V 2012); and *supra* text accompanying note 58.

68. Severance payments to corporate chief executives are a popular news item. These payments tend to be triggered by retirement, or by boards of directors asking the executive to step down. For a discussion of some of the largest CEO severance packages between 2001–2011, see generally Nathaniel Parish Flannery, *Executive Compensation: The True Cost of the 10 Largest CEO Severance Packages of the Past Decade*, FORBES (Jan. 19, 2012, 5:35 PM), <http://www.forbes.com/sites/nathanielparishflannery/2012/01/19/billion-dollar-blowout-top-10-largest-ceo-severance-packages-of-the-past-decade/> (noting that Jack Welch, formerly of General Electric, received \$417 million in severance pay in 2001). When examining such figures, however, it is important to note that many of these executives’ packages involve contractual benefits payable upon retirement. By contrast, this Note focuses on the taxability of severance payments paid upon an involuntary termination. For a detailed discussion of several CEOs’ severance payments and the circumstances surrounding their departures, see Paul Hodgson & Greg Ruel, *Twenty-One U.S. CEOs with Golden Parachutes of More Than \$100 Million*, GMI RATINGS (Jan. 2012), <http://www3.gmiratings.com/home/2013/07/twenty-one-u-s-ceos-with-golden-parachutes-of-more-than-100-million-jan-2012/> (cited in Flannery, *supra*).

69. See *Wages: Severance Pay*, DOL.GOV, <http://www.dol.gov/dol/topic/wages/severancepay.htm> (last visited June 1, 2013). Severance pay is not required by the Fair Labor Standards Act. See also *elaws: Fair Labor Standards Act Advisor*, DOL.GOV, <http://www.dol.gov/elaws/faq/esa/flsa/007.htm> (last visited June 1, 2013).

70. For a discussion of three mutually-exclusive economic hypotheses as to the purpose of severance payments, see THE WORLD BANK, REFORMING SEVERANCE PAY: AN INTERNATIONAL

This Note is focused on severance payments made either in conjunction with an involuntary layoff or those made to employees who voluntarily terminate their employment; pension-type payments are beyond the scope of this discussion.⁷¹ Further, it is a particular subset of severance payments that is at issue—payments classified as “supplemental unemployment compensation benefits,” (or “SUB payments”), as defined in I.R.C. § 3402(o)(2)(A):

[A]mounts which are paid to an employee, pursuant to a plan to which the employer is a party, because of an employee's involuntary separation from employment (whether or not such separation is temporary), resulting directly from a reduction in force, the discontinuance of a plant or operation, or other similar conditions, but only to the extent such benefits are includible in the employee's gross income.⁷²

In its 2008 decision in *CSX Corporation v. United States*,⁷³ the Federal Circuit held that even if a particular severance payment meets the I.R.C. § 3402(o) definition of “supplemental unemployment benefits,” it is within the scope of the definition of “wages” under FICA⁷⁴ and therefore subject to FICA withholding.⁷⁵ The Sixth Circuit's 2012 decision in *In re Quality Stores, Inc.*⁷⁶ created a split among the circuit courts of appeal

PERSPECTIVE 43–46 (Robert Holzmann and Milan Vodopivec eds., 2012). The hypotheses are: (1) a “social benefit program,” (2) a “human resource instrument,” and (3) an “employment protection device.” *Id.* at 44–46. First, the social benefit plan hypothesis discusses the role of some employers in creating a “safety net” where “public systems were minimal or nonexistent.” *Id.* at 45. The human resources instrument hypothesis takes both a short-term and long-term approach. In the short-run, severance plans “make[] mass dismissals socially and politically more palatable,” when needed for restructuring purposes. *Id.* The longer-term human resources aspect is the preservation of employee morale and “avoiding potential damage caused by departing workers if they are not appropriately compensated.” *Id.* Finally, the hypothesis of severance payments as an employment protection device postulates that the costs of terminating an employee may serve to protect employees; “[f]iring costs emerge from the mandated benefits, the permitted causes . . . and ruling by the courts on what is a fair dismissal.” *Id.* at 46. It is noted, however, that this hypothesis “carries a negative connotation with economists.” *Id.*

71. In the nature of pensions, tenure-termination payments have been the subject of controversy concerning whether they are taxable as FICA wages. For a discussion of this issue and related cases, see generally Robert J. Tepper & Craig G. White, *Academic Early Retirement: Do Tenure Buyout Payments Warrant Unique Employment Tax Treatment?*, 35 OKLA. CITY U. L. REV. 169 (2010) and Nicole Occhuizzo, *Taxing Tenure: An Examination of How the Federal Insurance Contribution Act (FICA) Has Been Applied to Tenure Buyouts*, 62 TAX LAW. 189 (2008).

72. I.R.C. § 3402(o)(2)(A) (2006 & Supp. V 2012). See *infra* notes 152–53 and accompanying text.

73. 518 F.3d 1328 (Fed. Cir. 2008).

74. See *infra* Part IV.

75. *CSX Corp.*, 518 F.3d at 1344–45.

76. 693 F.3d 605 (6th Cir. 2012).

when it concluded that severance payments that fit the § 3402(o) definition of SUB payments are not “wages” and therefore not subject to FICA.⁷⁷

III. AN INTRODUCTION TO THE CIRCUIT SPLIT

A. *Federal Circuit*: CSX Corporation v. United States

In the 1980s, CSX Corporation (“CSX”) faced financial difficulties and implemented certain “financial arrangements that encouraged employees to separate from the company, while cushioning the effect on the employees of the company’s reduction in the size of its workforce.”⁷⁸ Simply put, CSX offered payments to employees who left the company and the dispute before the court arose from the proper tax treatment of these payments.⁷⁹

There were several categories of payments at issue in *CSX*. First were employees, who were laid off and were paid “a percentage of their average monthly compensation” for a length of time that “depended on each employee’s length of service.”⁸⁰ Second were employees whose positions were eliminated, but who “remained subject to recall on an as-needed basis.”⁸¹ This second category of employees remained on the active payroll and were guaranteed a “minimum compensation per pay period.”⁸² Third were employees who were offered payments for agreeing to leave their position. These employees could be further categorized: some received the payment “in lieu of layoff benefits,” while others accepted the payment in lieu of remaining in their current positions.⁸³ Fourth, certain managerial employees were terminated—first voluntarily, in exchange for

77. *Id.* at 613.

78. *CSX Corp.*, 518 F.3d at 1330. This case involved tax paid under FICA and the Railroad Retirement Act (RRTA). The court considered only the portion of the dispute relating to FICA, as the parties agreed that “wages” under FICA and “compensation” under RRTA have the same meaning for determining the issue of this case. *Id.* at 1330–31.

79. *Id.* at 1330.

80. *Id.* at 1332.

81. *Id.*

82. *CSX Corp., Inc. v. United States*, 52 Fed. Cl. 208, 219 (2002).

83. *CSX Corp.*, 518 F.3d at 1332. The employees opting to receive the separation payment in lieu of layoff benefits were not electing to separate from employment, but “to resolve the uncertainty associated with a separation from employment of an indefinite duration (i.e., the layoff) in favor of a permanent separation.” *Id.* (quoting *CSX Corp.*, 52 Fed. Cl. at 220). These payments are contrasted to payments made to employees who chose to leave their positions, thus making the termination voluntary. *See id.*

a severance payment, or later, involuntarily, also accompanied by a severance payment.⁸⁴

In two opinions, considering non-managerial payments⁸⁵ and managerial payments,⁸⁶ respectively, the trial court first considered each of the severance payments individually to determine whether they were “SUB” payments, as that term is defined in I.R.C. § 3402(o).⁸⁷ The trial court ultimately concluded that SUB payments are not taxable as “wages” under FICA, so the payments that it had classified as SUB payments were not “wages,” while other payments may be taxable.⁸⁸

The first category of non-managerial employees’ payment, compensation given to employees who were laid off, was classified as a SUB payment by the trial court.⁸⁹ The second category, payments made to employees whose positions were eliminated but who were subject to recall as needed, were not classified as SUB payments.⁹⁰ The third category of payments, offered to some employees in lieu of layoff benefits and to others as compensation for agreeing to terminate their position, was classified by the trial court as SUB payments in the former instance, but not in the latter.⁹¹

The lower court ultimately held that supplemental unemployment benefits are not wages for the purposes of FICA, and the payments it classified as SUB payments were then not subject to the FICA tax.⁹² Accordingly, based on the definition of “supplemental unemployment compensation benefits” in I.R.C. § 3402(o), a payment is not taxable under FICA if it (1) is paid to an employee, “pursuant to a plan to which the employer is a party;” (2) the payment is “because of an employee’s involuntary separation from employment . . . resulting directly from a

84. *Id.* at 1332.

85. *CSX Corp.*, 52 Fed. Cl. 208.

86. *CSX Corp., Inc. v. United States*, 58 Fed. Cl. 341 (2003).

87. *See CSX Corp.*, 52 Fed. Cl. at 218; *CSX Corp.*, 58 Fed. Cl. at 346.

88. *See CSX Corp.*, 52 Fed. Cl. at 216 (“[N]o FICA taxes apply to such payments”).

89. *Id.* at 217–18.

90. *Id.* at 219.

91. *CSX Corp.*, 52 Fed. Cl. 220–21. Payments made to employees in lieu of layoff benefits were considered SUB payments, which the lower court concluded was not taxable. *Id.* at 220. By contrast, payments made to employees in lieu of remaining in their existing position were not SUB payments, and thus taxable. *Id.* The decision to terminate employment was the employee’s, so it was not “involuntary” under § 3402(o). *Id.* The court construed payments to managerial employees consistently with those made to non-managerial employees; payments made to managerial employees who voluntarily opted for the payment rather than to remain in their current positions were not SUB payments, while the payments made to employees who were laid off were SUB payments. *See CSX Corp.*, 58 Fed. Cl. at 346.

92. *CSX Corp.*, 52 Fed. Cl. at 216.

reduction in force,” the discontinuance of a plant or operation, or other similar conditions; and (3) the employee is actually separated from employment, either temporarily or permanently.⁹³

On appeal in 2008, the Federal Circuit reversed the lower court holdings, concluding that supplemental unemployment benefits *are* within the scope of “wages” taxable under FICA, primarily because the definition of SUB payments in § 3402(o), an income tax provision, is inapplicable to FICA.⁹⁴

B. Sixth Circuit: In re Quality Stores

Quality Stores, “the largest agricultural-specialty supplier in the country,” had an involuntary Chapter 11 petition filed against it in October 2001.⁹⁵ “Prior to November 2001,” the court explained, “Quality Stores [had] closed sixty-three stores and nine distribution centers and [had] terminated seventy-five employees in the corporate office.”⁹⁶ Quality Stores later closed its 311 remaining stores, three distribution centers, and terminated the rest of its employees.⁹⁷ The company “made severance payments to those employees whose employment was involuntarily terminated” under two separate plans.⁹⁸ These severance payments “resulted directly from a reduction in force or the discontinuance of a plant or operation,” by stipulation of the parties.⁹⁹

The two separate severance payment plans were categorized as the “Pre-Petition Severance Plan” and the “Post-Petition Severance Plan.”¹⁰⁰ The Pre-Petition Plan provided for payment based on “job grade and management level in the organization.”¹⁰¹ The Post-Petition Plan “was

93. *Id.* at 218. These elements are based strictly on the definition of “supplemental unemployment benefits” in I.R.C. § 3402 (2006 & Supp. V 2012).

94. *CSX Corp., Inc. v. United States*, 518 F.3d 1328, 1345 (Fed. Cir. 2008).

95. *In re Quality Stores, Inc.*, 693 F.3d 605, 608 (6th Cir. 2012).

96. *Id.*

97. *Id.*; see also *In re Quality Stores, Inc.*, 383 B.R. 67, 69 (Bankr. W.D. Mich. 2008).

98. *Quality Stores*, 693 F.3d at 608.

99. *Id.*

100. *Id.*

101. *Id.* The court noted:

The President and CEO received eighteen months of severance pay. Senior management executives received twelve months of severance pay, while all other managers and employees received one week of severance pay for each full year of service. These severance payments were not tied to the receipt of state unemployment compensation, and they were not attributable to the provision of any particular services by the employees. Quality Stores made the severance payments on the normal payroll schedule. Salaried employees received an average of 11.4 weeks of severance pay, while hourly employees received an average of 4.2 weeks of severance pay.

Id.

designed to encourage employees to defer their job searches and dedicate their efforts and attention to the company by assuring them that they would receive severance pay if their jobs were eliminated.”¹⁰²

Quality Stores withheld FICA taxes from the employees’ payments and made the employer contribution on the severance payments. It filed a tax return for these payments, and the IRS neither denied nor made the return. Quality Stores then filed an adversary action in the bankruptcy court for return of the FICA taxes paid, arguing that the severance payments were not “wages” and, therefore, were not subject to FICA.¹⁰³ At issue in the adversary action was \$1,000,125 in taxes paid, including both the employer share and the employees’ share.¹⁰⁴

In the adversary action, the bankruptcy court found that the payments at issue were SUB payments and that SUB payments were not subject to FICA taxation.¹⁰⁵ Because this decision was released just before the Federal Circuit decision in *CSX Corporation v. United States*,¹⁰⁶ the Government moved for reconsideration after *CSX Corporation*, which the bankruptcy court granted.¹⁰⁷ The court ratified its decision on

102. *Id.* To be eligible for payment under the Post-Petition Plan, “an employee was required to complete the last day of service as scheduled.” *Id.* Under this plan:

Company officers received between six and twelve months of severance pay, while full-time salaried and hourly employees who had been employed for at least two years received one week of severance pay for every full year of service, up to a maximum of ten weeks for salaried employees and five weeks for hourly employees. Those workers with less than two years of service received one week of severance pay.

Id. at 608–09. Like the Pre-Petition Plan, these payments “were not tied to the receipt of state unemployment compensation, nor were they attributable to the provision of any particular services.” *Id.* at 609. The payments “were paid in a lump sum . . . because the companies were liquidating and it was not practical administratively to pay the amounts over time.” *Id.* In sum, “on average, salaried employees received 5.2 weeks of severance pay, while hourly employees received 3.1 weeks of severance pay. About 900 employees did not receive any severance pay because they were hired immediately by successor companies.” *Id.*

103. *Id.*

104. *Id.* Quality Stores had permission from 1,850 of its former employees to file a tax return on their behalf. The court noted:

Of the total \$1,000,125 in FICA tax at issue, \$382,362 is attributed to severance payments made under the Pre-Petition Severance Plan, consisting of \$214,000 for the employer share and \$168,362 for the employee share. Further, of the total amount of FICA tax at issue, \$617,763 is attributed to severance payments made under the Post-Petition Severance Plan, consisting of \$357,127 for the employer share and \$260,636 for the employee share.

Id.

105. *In re Quality Stores*, 383 B.R. 67, 77–78 (Bankr. W.D. Mich. 2008).

106. *See CSX Corp. v. United States*, 518 F.3d 1328 (dated Mar. 6, 2008); *Quality Stores*, 383 B.R. 67 (dated Mar. 3, 2008).

107. *In re Quality Stores, Inc.*, 105 A.F.T.R. 2d 2010-1237 (Bankr. W.D. Mich. 2008); *see also In re Quality Stores, Inc.*, 424 B.R. 237, 240 (W.D. Mich. 2010) (discussing this procedural history).

reconsideration, and on appeal, the district court affirmed the bankruptcy court's decision.¹⁰⁸

On further appeal, the Sixth Circuit reconsidered whether the payments at issue fit the definition of a "supplemental unemployment benefit" and looked to the statutory language of the federal income tax withholding provisions¹⁰⁹ and the corresponding Treasury regulations¹¹⁰ as a first source. The court then parsed this definition into five elements that determine whether a payment is a SUB payment:

Congress has provided that a SUB payment is: (1) an amount paid to an employee; (2) pursuant to an employer's plan; (3) because of an employee's involuntary separation from employment, whether temporary or permanent; (4) resulting directly from a reduction in force, the discontinuance of a plant or operation, or other similar conditions; and (5) included in the employee's gross income.¹¹¹

The court concluded that all of the severance payments paid by Quality Stores to its former employees fit within this five-element test and that designation of a payment as a SUB payment means that it is not within the scope of "wages" under FICA.¹¹²

IV. AUTHORITY AND ANALYSIS: THE STATUTORY PUZZLE

At its core, the issue of whether SUB payments are taxable under FICA is one of statutory interpretation that demands an in-depth analysis of the text of the statute itself. While imposing a tax on "wages" may seem to be a relatively straightforward mechanism, there has been a great deal of

108. *Quality Stores*, 424 B.R. at 246.

109. *See In re Quality Stores, Inc.*, 693 F.3d 605, 618 (6th Cir. 2012); I.R.C. § 3402(o)(2)(A) (2006 & Supp. V 2012); *see also supra* text accompanying note 72.

110. *See Quality Stores*, 693 F.3d at 618. Treasury Regulation § 31.3401(a)-1(b)(14)(ii) is identical to I.R.C. § 3402(o)(2)(A).

111. *Quality Stores*, 693 F.3d at 611.

112. The court analyzed these elements as applied to the payments at issue:

The parties stipulated below that: (1) Quality Stores made the payments to employees; (2) pursuant to company plans; (3) because of the employees' permanent separation from employment; and (4) resulting directly from a reduction in force or the discontinuance of a plant or operation. Although the parties' stipulation did not contain any reference to gross income as contemplated by the fifth element of the statutory test, as a matter of law the SUB payments were included in the employees' gross incomes. *See* I.R.C. § 61 (generally "gross income means all income from whatever source derived" with certain inapplicable exceptions). The statutory definition does not require that SUB payments be tied to an employee's receipt of state unemployment compensation benefits, nor does the statute make any distinction between periodic payments or one-time payments made in a lump sum.

Id. at 611-12.

litigation on specific factual scenarios and whether they fall within the definitions of employee, employer, and wages, for example.¹¹³ Generally, on these issues, courts have favored a broad interpretation of FICA to effect the remedial policy goals of the Social Security Act.¹¹⁴ The context in which courts must decide whether severance payments are subject to FICA taxation requires due consideration of the status quo ante and a mind toward the ensuing remedial goal of Social Security and Medicare.¹¹⁵

FICA imposes a tax “on the income of every individual . . . equal to [certain] percentages of the wages . . . received by him with respect to employment.”¹¹⁶ For the purpose of this tax, the term “wages” is defined as “all remuneration for employment, including the cash value of all

113. See I.R.C. § 3121 (2006 & Supp. V 2012).

114. See, e.g., *CSX Corp. v. United States*, 518 F.3d 1328, 1333 (Fed. Cir. 2008) (citing *Soc. Sec. Bd. v. Nierotko*, 327 U.S. 358, 365-66 (1946)) (noting that the definitions under I.R.C. § 3121(b) are interpreted broadly); see also *United States v. Silk*, 331 U.S. 704 (1947) *abrogation recognized in* *Nationwide Mut. Ins. Co. v. Darden*, 503 U.S. 318 (1992). In *Silk*, the Court considered the definition of “employee” for the purposes of a Social Security tax, and emphasized the policy goals of the Social Security Act. See *Silk*, 331 U.S. at 711-12. The Court reiterated some of the themes of necessity that resounded in the political discourse surrounding the enactment of the Social Security Act:

The Social Security Act of 1935 was the result of long consideration by the President and Congress of the evil of the burdens that rest upon large numbers of our people because of the insecurities of modern life, particularly old age and unemployment. It was enacted in an effort to coordinate the forces of government and industry for solving the problems. The principal method adopted by Congress to advance its purpose was to provide for periodic payments in the nature of annuities to the elderly and compensation to workers during periods of unemployment. Employment taxes, such as we are here considering, are necessary to produce the revenue for federal participation in the program of alleviation.

Id. at 710 (internal footnote omitted); see also *supra* note 21 and accompanying text. In addition to the enactment discourse, the language in *Silk* also echoed the Court’s earlier decision in *Charles C. Steward Mach. Co. v. Davis*, 301 U.S. 548 (1937), in which the Court upheld a Social Security tax as within Congress’s power to tax for the general welfare; see *supra* text accompanying note 23.

115. Principles of statutory interpretation have long recognized the competing interests at stake in any particular tax law. See, e.g., HENRY CAMPBELL BLACK, *HANDBOOK ON THE CONSTRUCTION AND INTERPRETATION OF THE LAWS* 515 (2d ed. 1911) (noting that tax laws should be “construed strictly” to the extent that they may “deprive the citizen of his property by summary proceedings,” but “otherwise tax laws ought to be construed with fairness, if not liberality, in order to carry out the intention of the legislature and further the important public interests which such statutes subserve.”); see also ANTONIN SCALIA & BRYAN A. GARNER, *READING LAW: THE INTERPRETATION OF LEGAL TEXTS* 359 (2012). Garner and Scalia framed the general rule as requiring that “‘exemptions from taxation are to be construed narrowly’ . . . and that doubts regarding them ‘must be resolved against the taxpayer.’” *Id.* (internal footnotes omitted). Scalia and Garner observed that the applicable rule on this topic had previously been to resolve doubts “in favor of the exemption” and that the rule had reversed course over time. *Id.* at 359-60. They concluded:

Without some textual indication, there is no reason to give statutory exceptions anything other than a fair (rather than a “narrow”) interpretation. The expressions to the contrary find their source either in a judicial proclivity to make difficult interpretive questions easy, or else in an inappropriate judicial antagonism to limitations on favored legislation.

Id. at 363. Garner and Scalia instead suggest ignoring this rule entirely. *Id.* at 362.

116. I.R.C. § 3101(a) (2006 & Supp. V 2012).

remuneration (including benefits) paid in any medium other than cash.”¹¹⁷ The central issue in these cases, and in this Note, is whether the income tax provision that includes “supplemental unemployment compensation benefits” (SUB payments) under a section that extends income tax withholding to payments “other than wages” and requires treatment of the payments “as if [they] were a payment of wages” can mean that SUB payments are not, *in fact*, wages and, by extension, are not within the scope of FICA’s taxation on wages.¹¹⁸

This issue is complex for several reasons, even aside from the highly apparent complexity of the just-stated argument. First, as noted, the provision addressing treatment of SUB payments falls under the income tax provisions—SUB payments are not addressed in the FICA tax provisions. The first wrinkle, then, is whether the income tax definitions apply to FICA provisions; to address this issue, Subpart A will discuss the bridge—*Rowan Companies, Inc. v. United States*, and the circuit courts’ analyses thereof.¹¹⁹ The second challenge in this issue is the sheer complexity of the tax provisions involved. Subpart B will provide an analysis of the text of the relevant tax code provisions, followed by a discussion of the courts’ respective statutory interpretations. Finally, the issue is complicated by the “reverse-course” revenue rulings that the IRS has published since the 1950s, which will be discussed in Subpart C, but generally and as analyzed by the circuit courts.¹²⁰

A. *The Link Between FICA and Income Tax Provisions: Rowan Companies v. United States*

The Supreme Court in *Rowan Companies, Inc. v. United States* held that Congress intended for FICA, FUTA (the Federal Unemployment Tax Act)¹²¹ and the income tax provisions to have the same definition of

117. I.R.C. § 3121(a) (2006 & Supp. V 2012).

118. I.R.C. § 3402(o) (2006 & Supp. V 2012). *See infra* notes 160–61 and accompanying text.

119. 452 U.S. 247 (1981).

120. *In re Quality Stores, Inc.*, 424 B.R. 237, 240 (W.D. Mich. 2010). The court observed: “The fact that the Internal Revenue Service has itself charted a path of ‘reverse-course’ rulings on this issue since the 1950s only adds to the difficulties faced by the courts in attempting to reach a reasoned resolution by explaining and accounting for this repeated change in agency position.” *Id.*

121. The Federal Unemployment Tax Act, while relevant to the topics at issue, is beyond the scope of this Note. FUTA is not paid by employees and it is not deducted from their wages. FUTA is paid only by employers, and is separate from Social Security and Medicare taxes paid under the FICA tax. *Employment Taxes*, IRS.GOV, <http://www.irs.gov/Businesses/Small-Businesses-&-Self-Employed/Employment-Taxes-2> (last updated Nov. 4, 2013).

wages.¹²² In *Rowan*, an employer provided meals and lodging for employees working on offshore oil rigs, but “did not include the value of the meals and lodging in computing its employees’ ‘wages’” for FICA withholding purposes.¹²³ When conducting an audit, the IRS included this value in the calculation of wages for FICA, but not for income tax withholding, acting “consistently with . . . Treasury Regulations that interpret the definition of ‘wages’ in FICA and FUTA to include the value of these meals and lodging, whereas the substantially identical definition of ‘wages’ in [the income-tax withholding provisions] is interpreted by Treasury Regulations to exclude this value.”¹²⁴ The Court held, and the Government conceded, that the exclusion of the cost of meals and lodging in the calculation of wages for income tax withholding was proper.¹²⁵ Yet, despite its concession as to the income tax calculation, the Government still argued that the value of the meals and lodging should be included in the calculation of wages for FICA taxation purposes, based on Treasury Regulations §§ 31.3121(a)-1(f) and 31.3306(b)-1(f).¹²⁶ The Court noted,

122. *Rowan*, 452 U.S. at 257. The Court concluded:

In sum, Congress intended in both the Revenue Act of 1942 and the Current Tax Payment Act of 1943 to coordinate the income-tax withholding system with FICA and FUTA. In both instances, Congress did so to promote simplicity and ease of administration. Contradictory interpretations of substantially identical definitions do not serve that interest. It would be extraordinary for a Congress pursuing this interest to intend, without ever saying so, for identical definitions to be interpreted differently.

Id.

123. *Id.* at 249.

124. *Id.* at 250 (internal footnote omitted).

125. *Id.* at 250–51. The Court looked to Treasury Regulation §31.3401(a)-1(b)(9), under which an employer excludes the value of meals or lodging from “wages” if the employee also excludes that value from his or her gross income. Treas. Reg. § 31.3401(a)-1(b)(9) (2012). In order for an employee to exclude the value from gross income, the Court looked to the “convenience-of-the-employer rule” of I.R.C. § 119, which provides for exclusion “if the employer furnished both the meals and lodging for its own convenience, furnished the meals on its business premises, and required the employee to accept the lodging on the business premises as a condition of employment.” *Rowan*, 452 U.S. at 251. The Court found that the requirements of § 119 were satisfied, meaning employees would exclude the value from their gross wages, and, in turn, the employer should exclude the value from wages, as well.

See id.

126. *Id.* at 251–52. These regulations applied to FICA and FUTA, respectively, and were codified at 26 CFR §§ 31.3121(a)-1(f) and 31.3306(b)-1(f) (1980). The regulations were (and are) identical and provided:

Ordinarily, facilities or privileges (such as entertainment, medical services, or so-called ‘courtesy’ discounts on purchases), furnished or offered by an employer to his employees generally, are not considered as remuneration for employment if such facilities or privileges are of relatively small value and are offered or furnished by the employer merely as a means of promoting the health, good will, contentment, or efficiency of his employees. The term ‘facilities or privileges,’ however, does not ordinarily include the value of meals or lodging furnished, for example, to restaurant or hotel employees, or to seamen or other employees

“If valid, these regulations dictate that the value of the meals and lodging provided by petitioner to its employees on offshore rigs was includable in ‘wages’ as defined in FICA and FUTA, even though excludable from ‘wages’ under the substantially identical definition in § 3401(a) for income-tax withholding.”¹²⁷ In other words, despite the nearly identical statutory language in the FICA, FUTA, and income tax definitions of “wages,” the regulations at issue would cause these provisions to operate inconsistently.

After discussing the legislative history of the Acts establishing income-tax withholding and the congressional intent “to promote simplicity and ease of administration,” the Court held that “[i]t would be extraordinary for a Congress pursuing this interest to intend, without ever saying so, for identical definitions to be interpreted differently.”¹²⁸ The Court concluded, “The plain language and legislative histories of the relevant Acts indicate that Congress intended its definition to be interpreted in the same manner for FICA and FUTA as for income-tax withholding.”¹²⁹ In reaching that result, the Court found the Treasury Regulations to be invalid, as they “fail to implement the statutory definition of ‘wages’ in a consistent or reasonable manner.”¹³⁰

While discussing a different factual issue from that presented here, *Rowan* stands for the proposition that the definitions of “wages” between the income tax provisions and FICA are functionally identical.¹³¹ This forms the basis for taxpayers to make a statutory argument based on income tax provisions, extended via *Rowan* to FICA.¹³²

1. Federal Circuit and Sixth Circuit Analyses of *Rowan*

Although the courts ultimately reach different conclusions on the overarching issue before them, the Federal Circuit and Sixth Circuit agreed on the role of *Rowan*. The arguments presented by the Government

aboard vessels, since generally these items constitute an appreciable part of the total remuneration of such employees.

Rowan, 452 U.S. at 252.

127. *Id.*

128. *Id.* at 257.

129. *Id.* at 263.

130. *Id.* The reasoning here was that since the Treasury Regulations for FICA and FUTA could be read to include in “wages” some payments that were not included in “wages” under the income tax provision, the regulations were invalid as inconsistent with the statutory language, which the Court interpreted as requiring these definitions to be the same.

131. *See supra* text accompanying note 129.

132. *See infra* Part IV.B.

in each of these two cases centered on the legacy of *Rowan* in light of the 1983 “decoupling amendment” to FICA.¹³³ This amendment provides: “Nothing in the regulations prescribed for purposes of chapter 24 (relating to income tax withholding) which provides an exclusion from ‘wages’ as used in such chapter shall be construed to require a similar exclusion from ‘wages’ in the regulations prescribed for [FICA].”¹³⁴ The legislative history to the 1983 decoupling amendment shows a congressional intent to treat “wages” differently under FICA and the income tax provisions.¹³⁵ This provision, which “gives the IRS the ability to establish distinctions between the two statutory definitions” of wages under FICA and the federal income tax provisions, is said to supersede *Rowan*.¹³⁶

When confronted with this argument, however, the lower courts in both circuits noted the need for an applicable regulation, which has not yet been promulgated.¹³⁷ Without such a regulation, “[s]imply put, the holding of *Rowan* remains in place.”¹³⁸ The Sixth Circuit in *Quality Stores* followed this reasoning outright.¹³⁹ The Federal Circuit in *CSX Corp.* relied on one of its earlier holdings that noted there was no regulation to implement the decoupling provision, and thereby rejected the contention that *Rowan*’s

133. Social Security Amendments of 1983, Pub. L. No. 98–21, 97 Stat. 65 (1983).

134. I.R.C. § 3121(a)(23) (2006 & Supp. V 2012) (parenthetical in original).

135. “Since the security system has objectives which are significantly different from the objective underlying the income tax withholding rules . . . amounts exempt from income tax withholding should not be exempt from FICA unless Congress provides an explicit FICA tax exclusion.” S. Rep. No. 98–23, at 42 (1983), reprinted in 1983 U.S.C.C.A.N. 143, 183; H.R. Rep. No. 98–25(I), at 80 (1983), reprinted in 1983 U.S.C.C.A.N. 219, 299. The court cited both reports in *CSX Corp. v. United States*, 518 F.3d 1328, 1343 (Fed Cir. 2008)).

136. *In re Quality Stores, Inc.*, 383 B.R. 67, 78 (Bankr. W.D. Mich. 2008). The court characterized the argument as: “According to the IRS, these amendments contain a ‘decoupling’ provision that specifically rejects *Rowan*’s conclusion that wages should be defined the same for purposes of income tax withholding and FICA taxation.” *Id.* at 73; see also *Canisius Coll. v. United States*, 799 F.2d 18, 21 (2d Cir. 1986) (“Congress in 1983 overturned the general premise of *Rowan* by enacting provisions that ‘decoupled’ the interpretations of FICA and FUTA wages from the interpretation of wages for income-tax purposes.”).

137. See *Quality Stores*, 383 B.R. at 78 (“Although the ‘decoupling’ provision gives the IRS the ability to establish distinctions between the two statutory definitions, such distinctions must be made through the promulgation of valid regulations. No such regulations exist.”); see also *CSX Corp., Inc. v. United States*, 52 Fed. Cl. 208, 213 (2002). The court characterized the decoupling provision as “not self-executing” and noted:

[I]ts operation depends on the promulgation of regulations that in fact establish distinctions between wages for income-tax withholding purposes and wages for FICA-tax withholding purposes. Absent such regulations, this court has no basis for distinguishing between the content of the term “wages” for income-tax withholding purposes and the content of that term for FICA-tax withholding purposes.

Id.

138. *CSX Corp.*, 52 Fed. Cl. at 213.

139. See *In re Quality Stores, Inc.*, 693 F.3d 605, 618–19 (6th Cir. 2012).

central premise had become invalid.¹⁴⁰ In accord with its precedent, the Federal Circuit Court noted its disagreement with the Government's argument that "after 1983, the term 'wages' in FICA must be interpreted without reference to the same term in the income tax withholding statutes."¹⁴¹

The circuit courts' agreement on this issue is important. First, it solidifies the issue as one primarily of statutory interpretation, since the courts are in agreement as to the primary starting point.¹⁴² Second, it is clear that the respective outcomes of these cases may have been different in the presence of a relevant Treasury Regulation, which has important implications for resolving the circuit split down the road.¹⁴³

B. The Heart of the Debate: The Tax Code Statutory Analysis

Accepting the proposition from *Rowan* that FICA and the federal income tax provisions have the same definition of "wages," the next step in the analysis is to understand that definition.¹⁴⁴ The income tax definition (§ 3401) and the FICA definition (§ 3121) both provide that wages are "all remuneration" "for services performed by an employee for his employer,"¹⁴⁵ or "for employment"¹⁴⁶ (respectively), "including the cash value of all remuneration (including benefits) paid in any medium other than cash."¹⁴⁷ Determining the scope of "wages" is essential to the tax provisions, as wages provide the basis for federal income tax withholding and for FICA tax withholding; the two taxes are automatically deducted from employees' pay.¹⁴⁸ The issue, then, seems relatively

140. *CSX Corp.*, 518 F.3d at 1344, (citing *Anderson v. United States*, 929 F.2d 648, 650 (Fed. Cir. 1991) (holding that the 1983 amendments decoupled the two definitions only inasmuch as it "allow[ed] the Treasury to promulgate regulations to provide for different exclusions from 'wages' under FICA than under the income tax withholding laws"). It is interesting to note that the Federal Circuit in *CSX Corp.* was bound by its earlier decision in *Anderson*, which, as noted, affirmed the proposition of *Rowan*. While the *CSX Corp.* court was able to find that severance payments are wages, even though it agreed with *CSX* that *Rowan* was applicable, the analysis may have been less strained if the court had been able to disavow *Rowan*.

141. *Id.* at 1344–45.

142. *See id.* Because the court in *CSX Corp.* was bound by its precedent that *Rowan* still stands, its analysis took a different approach, relying more heavily on what it saw as the logic of the statutory analysis, combined with the IRS positions stated in revenue rulings. *See infra* Part IV.C.

143. *See infra* Part V.

144. *See supra* text accompanying note 129.

145. I.R.C. § 3401(a) (2006 & Supp. V 2012).

146. I.R.C. § 3121(a) (2006 & Supp. V 2012).

147. I.R.C. §§ 3121, 3401 (parenthetical in original).

148. *See* I.R.C. § 3402(a)(1) (2006 & Supp. V 2012) ("[E]very employer making payment of wages shall deduct and withhold upon such wages a tax determined in accordance with tables or

straightforward—are severance payments “wages,” and thus subject to FICA withholding? The definition of “wages,” itself, does not directly answer this question, as “remuneration for employment” does not explicitly include severance payments. Of course, FICA is silent on the issue as well, but the more expansive income tax chapter provides a starting point; since §§ 3401 (income tax provisions) and 3121 (FICA) have the same definition of wages, per *Rowan*, comparing statutory treatment of “wages” across the two provisions is a sound approach.

Starting, then, with the income tax provisions, § 3402(o) provides for an extension of federal income tax withholding to “certain payments other than wages.”¹⁴⁹ Under that section, these non-wage payments “shall be treated as if [they] were a payment of wages by an employer to an employee for a payroll period.”¹⁵⁰ Treating these payments as if they were wages means that the employer withholds an established percentage of the payments as federal income tax.¹⁵¹ Section 3402(o)(1) lists three specific types of payments that should be treated as if they are wages:

- (A) any supplemental unemployment compensation benefit paid to an individual,
- (B) any payment of an annuity to an individual, if at the time the payment is made a request that such annuity be subject to withholding under this chapter is in effect, and
- (C) any payment to an individual of sick pay which does not constitute wages (determined without regard to this subsection), if at the time the payment is made a request that such sick pay be subject to withholding under this chapter is in effect. . . .¹⁵²

The inclusion of “supplemental unemployment compensation benefits” is the link to the discussion at issue. Section 3402(o) defines supplemental unemployment compensation benefits as:

amounts which are paid to an employee, pursuant to a plan to which the employer is a party, because of an employee's involuntary separation from employment (whether or not such separation is

computational procedures prescribed by the [Treasury] Secretary.”); *see also* I.R.C. § 3102(a) (2006 & Supp. V 2012) (“[T]he tax . . . shall be collected by the employer of the taxpayer, by deducting the amount of the tax from the wages as and when paid.”).

149. I.R.C. § 3402(o) (2006 & Supp. V 2012).

150. I.R.C. § 3402(o)(1)(C).

151. *See* I.R.C. § 3402(a)(1) (2006 & Supp. V 2012).

152. I.R.C. § 3402(o)(1)(A)-(C).

temporary), resulting directly from a reduction in force, the discontinuance of a plant or operation, or other similar conditions, but only to the extent such benefits are includible in the employee's gross income.¹⁵³

By way of summary thus far, the analysis begins with *Rowan*, which stands for the proposition that “wages” means the same thing under the income tax provisions and FICA.¹⁵⁴ The next step is to determine whether severance payments are “wages,” but neither the income tax provision nor FICA explicitly include this type of payment in its definition.¹⁵⁵ The income tax provisions, however, provide for certain payments to be treated as if they are wages, and thus subject them to withholding, and supplemental unemployment compensation benefits are included in this list.¹⁵⁶

The question remains as to whether § 3402(o), an income tax provision, should also apply to FICA. One argument against similar treatment stems from the fact that FICA was amended in 1983 to add the so-called “decoupling provision” to § 3121(a).¹⁵⁷ The direct counterargument, as discussed, is that the decoupling amendment applies only to the extent that it “allow[s] Treasury to promulgate regulations to provide for different exclusions from ‘wages’ under FICA than under the income tax withholding laws,” but that no such regulation exists.¹⁵⁸ The long-term role of the decoupling argument, therefore, is unresolved. But the Federal Circuit and Sixth Circuit are in agreement that without such a regulation, the decoupling amendment has not changed the fact that FICA and the income tax chapter have the same definition of “wages.”¹⁵⁹

The proposition that the FICA definition of “wages” is identical to the income tax definition of “wages” forms the basis for an indirect application of § 3402(o) to FICA’s definition of wages. The argument contends that, because § 3402(o) provides that certain payments should be treated “as if” they are wages must mean that they are not, *in fact*, wages.¹⁶⁰ Even if § 3402(o) is not directly applicable to FICA, the

153. I.R.C. § 3402(o)(2)(A).

154. *See supra* text accompanying note 129.

155. *See supra* text accompanying note 147.

156. *See supra* text accompanying notes 152–53.

157. *See supra* text accompanying notes 133–35.

158. *Anderson v. United States*, 929 F.2d 648, 650 (Fed. Cir. 1991) (quoted in *CSX Corp. v. United States*, 518 F.3d 1328, 1344 (Fed. Cir. 2008)).

159. *See supra* text accompanying notes 139–41.

160. *See, e.g., CSX Corp.*, 518 F.3d at 1341. The opposing sides to this argument appear to take counterintuitive positions, given the language in the income tax provisions. The Government seeks to

argument follows, it applies indirectly: these payments that are to be treated “as if” they are wages under § 3402(o), are *not* wages under § 3401, which is the general definition of wages for the federal income tax provisions.¹⁶¹ If these payments are not wages under § 3401 (income tax provisions), they cannot be wages under § 3101 (FICA), either, since these definitions are the same.¹⁶² Accordingly, severance payments should not be subject to FICA taxation, as they are not wages, because being “wages” is a statutory prerequisite to FICA withholding.¹⁶³

This statutory analysis forms one of the bases for the major difference in approaches in the Federal Circuit and in the Sixth Circuit. Accordingly, their analyses will be discussed separately.

1. Federal Circuit Statutory Analysis

The court in *CSX Corporation* took the position that § 3402(o), which provides for withholding from certain payments other than wages, “applies only for purposes of chapter 24 [the federal income tax provisions] and certain procedural provisions relating to chapter 24.”¹⁶⁴ The court continued: “Congress’s decision to restrict the scope of the rule set forth in Section 3402(o) to chapter 24 suggests that Congress did not intend that rule, or any implication that might be drawn from that rule, to be applied outside the context of income tax withholding.”¹⁶⁵ Under this approach, whether a type of payment fits within the § 3402(o) definition of SUB payments is not relevant to determining whether it is “wages” under FICA, as § 3402(o) does not apply to FICA.

The employer-taxpayer, CSX, argued for the indirect application previously discussed: because § 3402(o) provides for treatment of SUB

establish that § 3402(o) does not apply to FICA. This may appear confusing, since the terms of § 3402(o) result in income tax withholding from SUB payments, so one might think that if § 3402(o) applies to FICA, then it would result in withholding for FICA. Opponents of imposing FICA tax on SUB payments, by contrast, do seek to incorporate § 3402(o) into FICA, but strictly for definitional purposes, rather than operational effect. To avoid confusion, one must remember that the only overlap between FICA and the income tax provisions is their definitions—operation of provisions within a particular chapter do not apply to the tax code generally, unless otherwise specified. Section 3402(o) is not a generally applicable provision, so the arguments based on this section involve only the application of definitions.

161. *See id.*

162. *See id.*; *see also* *Rowan Cos. v. United States*, 452 U.S. 247, 263 (1981).

163. *See* I.R.C. § 3402(a)(1) (2006 & Supp. V 2012); *see also* Thomas W. Meagher & Clara J. Kim, *SUB Plans Resurface in Tough Economic Times*, 37 TAX MGMT. COMP. PLAN. J. 150, 154 (2009) (briefly summarizing the argument).

164. *CSX Corp.*, 518 F.3d at 1341.

165. *Id.*

payments as if they are wages, they must not be wages as defined in § 3401, and since § 3401 has the same definition as the FICA provision (§ 3121), per *Rowan*, the severance payments cannot be wages for FICA withholding.¹⁶⁶ While agreeing with CSX's interpretation of *Rowan*,¹⁶⁷ the court did not agree with its logic. The court noted:

To say that all payments falling within a particular category shall be treated as if they were a payment of wages does not dictate, as a matter of language or logic, that none of the payments within that category would otherwise be wages. For example, to say that for some purposes all men shall be treated as if they were six feet tall does not imply that no men are six feet tall.¹⁶⁸

Thus, the court reasoned, while *Rowan* still stands, as does the proposition that “wages” has the same meaning under the income tax provision as under FICA, the statutory interpretation offered by CSX was inaccurate and illogical.¹⁶⁹ Rather, the court limited application of § 3402(o) to the federal income tax chapter and concluded that § 3402(o) “does not require that FICA be interpreted to exclude from ‘wages’ all payments that would satisfy the definition of SUB in section 3402(o)(2)(A).”¹⁷⁰ In short, whether a type of payment fits the § 3402(o) definition of SUB payments is not relevant to its classification as “wages” under FICA. The court ultimately found that the payments at issue were subject to FICA taxation,¹⁷¹ aided in part by its interpretation of the Revenue Rulings discussed below.¹⁷²

2. Sixth Circuit Statutory Analysis

The Sixth Circuit took a more direct approach. Recognizing an ambiguity in § 3402(o), the court turned to its title and the legislative history to guide its interpretation.¹⁷³ As for the title, the court noted that use of the phrase “other than wages” in the subsection titled “Extension of

166. *See id.*; *see also supra* text accompanying notes 160–63.

167. *See supra* text accompanying note 141.

168. *CSX Corp.*, 518 F.3d at 1342.

169. *See id.*

170. *Id.*; *see also supra* Part IV (discussing the Federal Circuit's analysis of “dismissal payments” as opposed to “SUB payments” in light of applicable revenue rulings).

171. *CSX Corp.*, 518 F.3d at 1352 (“[T]he payments to the various groups of employees who were accorded benefits in connection with CSX's reduction in force were all ‘wages’ or ‘compensation’ as those terms are used in FICA and the RRTA.”).

172. *See infra* Part IV.C.

173. *See In re Quality Stores, Inc.*, 693 F.3d 605, 612 (6th Cir. 2012).

withholding to certain payments other than wages” suggested acknowledgement that the payments listed in that section were not, in fact, wages.¹⁷⁴

Turning to the legislative history, the court concluded that Congress intended to enact § 3402(o) for the convenience of taxpayers.¹⁷⁵ “In light of this clear congressional intent,” the court approved the bankruptcy judge’s reasoning that SUB payments are only treated *as if* they are wages for federal income tax withholding, but are not *actually* wages under that provision. Accordingly, given the effect of *Rowan*,¹⁷⁶ they are also not wages under FICA.¹⁷⁷ This conclusion is in direct conflict with the Federal Circuit’s conclusion on the same issue.¹⁷⁸

In short, the basis for the courts’ disagreement is twofold. First, the courts disagree as to whether the direct approach—applying § 3402(o) to FICA—is proper. Second, the courts disagree about the logic of the indirect approach—extending § 3402(o) (which addresses payments “other than wages”), via § 3401 (the definition of “wages” for the federal income tax chapter), to § 3121 (the functionally identical definition of “wages” for the FICA chapter).¹⁷⁹

This complicated issue of statutory interpretation might ordinarily be aided in part by looking to the IRS’s revenue rulings on point. Such is not the case here, however. Despite analyzing the same rulings, regulations, and statutory provisions, the Federal Circuit and Sixth Circuit came to irreconcilable conclusions as to the proper interpretation of the revenue rulings.

174. I.R.C. § 3402(o) (2006 & Supp. V 2012); *Quality Stores*, 693 F.3d at 612.

175. See *Quality Stores*, 693 F.3d at 612–13. The court summarized its findings accordingly:

When § 3402(o) was enacted in 1969, Congress recognized that SUB payments “are not subject to [federal income tax] withholding because *they do not constitute wages or remuneration for services*.” Because SUB payments “are generally taxable income to the recipient,” however, Congress decided to require federal income tax withholding on SUB payments to alleviate any unexpected income tax burden on employees for the calendar year in which the payments were made. Congress stressed “that *although these benefits are not wages*, since they are generally taxable payments they should be subject to withholding to avoid the final tax payment problem for employees.” As a result of the enactment of § 3402(o), the “withholding requirements . . . *on wages* are to apply to these non-wage payments.”

Id. (emphasis added by the court) (citations omitted).

176. See *supra* text accompanying notes 136–39.

177. See *Quality Stores*, 693 F.3d at 613. The court summarized: “Because Congress has provided that SUB payments are not ‘wages’ and are treated only as if they were ‘wages’ for purposes of federal income tax withholding, such payments are not ‘wages’ for purposes of FICA taxation.” *Id.* at 616.

178. See *supra* notes 166–70 and accompanying text.

179. See *supra* note 166 and accompanying text.

C. *What Does the IRS Have To Say About All of This? The “Reverse-Course” Revenue Rulings*

The Internal Revenue Service’s revenue rulings offer guidance on the agency’s interpretation of particular issues within the tax code. Regarding the inclusion of certain non-wage payments as within the reach of FICA tax, however, the IRS “has itself charted a path of ‘reverse-course’ rulings on this issue since the 1950s [which] only adds to the difficulties faced by the courts in attempting to reach a reasoned resolution by explaining and accounting for this repeated change in agency position.”¹⁸⁰

Starting in 1956 with Rev. Rul. 56-249, the IRS stated its position that a particular form of severance payments was not “wages.”¹⁸¹ The payments at issue were paid to individuals from a “trust created pursuant to [a company’s] supplemental unemployment benefit plan.”¹⁸² In its ruling, the IRS cited the specific factors that prevented this particular type of payment from being classified as wages, including a contingency involving the eligibility requirements for state unemployment benefit programs.¹⁸³

In three subsequent rulings, Rev. Rul. 58-128, Rev. Rul. 59-227, Rev. Rul. 60-330, the IRS broadened its classification of the types of payments that are non-wages.¹⁸⁴ First, Rev. Rul. 58-128 held that a supplemental

180. *In re Quality Stores, Inc.*, 424 B.R. 237, 240 (W.D. Mich. 2010).

181. Rev. Rul. 56-249, 1956-1 C.B. 488.

182. *Id.* at 489.

183. *Id.* at 492. The Ruling enumerated the determinative characteristics of these payments as follows:

- (1) the benefits are paid only to unemployed former employees of *M Company* who are on layoff from the Company;
- (2) eligibility for benefits depends on the meeting of prescribed conditions subsequent to the termination of the employment relationship with *M Company*;
- (3) benefits are paid by the trustees of independent trust funds;
- (4) the amount of a weekly benefit payable under the plan is based upon (a) the amount of the weekly benefit payable under the appropriate State unemployment compensation laws, (b) the amount of other remuneration allowable under such State unemployment compensation laws, and (c) the amount of straight-time weekly pay after withholding of all taxes and contributions;
- (5) the duration of weekly benefits payable under the plan depends upon a combination of (a) the number of accumulated credited units, and (b) the fund position;
- (6) a right, if any, to benefits does not accrue until a prescribed period after the termination of the employment relationship with *M Company* has elapsed;
- (7) the benefits ultimately paid are not attributable to the rendering of particular services by the recipient during the period of his employment; and
- (8) no employee has any right, title, or interest in or to any of the assets of the fund or in or to any Company contributions thereto until such time as he is qualified and eligible to receive a benefit therefrom.

Id.

184. *See CSX Corp. v. United States*, 518 F.3d 1328, 1335-36 (Fed. Cir. 2008) (briefly discussing these rulings).

unemployment benefit plan that was initiated by the employer unilaterally, rather than as part of a collective bargaining agreement, was not within the definition of wages for FICA purposes.¹⁸⁵ Second, Rev. Rul. 59-227 extended this non-wage treatment to payments made as one lump sum, rather than over an extended period of time.¹⁸⁶ Finally, in Rev. Rul. 60-330, the IRS concluded that payments made directly by an employer, rather than through a trust as part of a supplemental unemployment benefit plan, would not be subject to FICA taxation.¹⁸⁷

In 1960, Congress enacted I.R.C. § 501(c), which explicitly provided tax exemption for trusts that were used to pay supplemental unemployment compensation benefits.¹⁸⁸ It also supplied its own definition of supplemental unemployment compensation benefits.¹⁸⁹ Accordingly, the basis for a changing course emerged, and in Rev. Rul. 71-408, the IRS determined that certain “dismissal payments made to former employees by a company which had terminated its operations” were taxable wages under FICA.¹⁹⁰ In this ruling, the IRS cited the regulations implementing FICA and the income tax provisions. Particularly, the IRS noted:

Sections 31.3121(a)-1(i), 31.3306(b)-1(i), and 31.3401(a)-1(a)(5) of the Employment Tax Regulations provide that remuneration for employment, unless specifically excepted, constitutes ‘wages’ even though at the time paid the individual is no longer an employee.

185. Rev. Rul. 58-128, 1958-1 C.B. 89, 89-90. The payments at issue in Rev. Rul. 56-249 were created as part of a collective bargaining agreement. *See* 1958-1 C.B. at 489. So, Rev. Rul. 58-128 directly broadened the “non-wage” classification.

186. *See* Rev. Rul. 59-227, 1959-2 C.B. 13, 14. Payments made under a trust, as in Rev. Rul. 56-249, were paid on a continuing basis. *See* 156-1 C.B. at 489-90. Again, this ruling represented a direct extension of the non-wage classification.

187. *See* Rev. Rul. 60-330, 1960-2 C.B. 46, 47-48. To summarize, these three rulings extended the non-wage designation to payments that were paid under a trust or directly by an employer, were created under a collective bargaining agreement or by the employer unilaterally, and to payments that were paid on a continuing basis or as one lump sum. In other words, these rulings encompassed most types of post-employment benefit plans offered by employers.

188. Pub. L. No. 86-667, 74 Stat. 534 (1960).

189. I.R.C. § 501(c)(17)(D) (2006 & Supp. V 2012) provides:

The term “supplemental unemployment compensation benefits” means only—

(i) benefits which are paid to an employee because of his involuntary separation from the employment of the employer (whether or not such separation is temporary) resulting directly from a reduction in force, the discontinuance of a plant or operation, or other similar conditions, and

(ii) sick and accident benefits subordinate to the benefits described in clause (i).

190. Rev. Rul. 71-408, 1971-2 C.B. 340, 340.

Section 31.3401(a)-1(b)(4) of the regulations specifically provides, for purposes of income tax withholding, that all payments made by an employer to an employee on account of dismissal, that is, involuntary separation from the service of the employer, constitute 'wages' regardless of whether the employer is legally bound by contract, statute, or otherwise to make the payments.¹⁹¹

The IRS acknowledged the presence of the familiar issue as to whether the income tax provision can be extended to FICA.¹⁹² To bridge this issue, the IRS looked to the history of FICA and noted that, prior to 1950, the term "wages" explicitly excluded "dismissal payments which the employer was not legally required to make."¹⁹³ In 1950, however, Congress passed the Social Security Act Amendments of 1950, which deleted this exclusion.¹⁹⁴ The Revenue Ruling then quoted a passage from a House Report on these 1950 amendments providing: "a dismissal payment, which is any payment made by an employer on account of involuntary separation of the employee from the service of the employer, will constitute wages."¹⁹⁵ It is important to note here that Rev. Rul. 71-408 framed the issue as involving "dismissal payments," as defined in the House Report and the Treasury Regulations above, rather the statutorily defined "supplemental unemployment benefits."¹⁹⁶ A similar approach was taken in Rev. Rul. 74-252, where the IRS concluded that a contractually agreed-upon "dismissal payment" for early termination by the employer was a form of "wages" subject to FICA.¹⁹⁷

In 1977, the IRS issued Rev. Rul. 77-347 to address the enactment of I.R.C. § 3402(o), the statutory provision extending income tax withholding to certain payments other than wages, including SUB payments.¹⁹⁸ In that

191. *Id.* at 341.

192. *Id.*

193. *Id.*

194. Pub. L. No. 81-734 64 Stat. 477, 546 (1950).

195. Rev. Rul. 71-408, 1971-2 C.B. at 341 (quoting H.R. Rep. No. 81-1300 (1950)).

196. *See supra* text accompanying notes 189, 191, and 195; *see also* CSX Corp. v. United States, 518 F.3d 1328, 1337 (Fed Cir. 2008).

197. Rev. Rul. 74-252, 1974-1 C.B. 287, 288; *see also In re* Quality Stores, Inc., 693 F.3d 605, 618 (6th Cir. 2012).

198. Rev. Rul. 77-347, 1977-2 C.B. 363. The Federal Circuit provided a useful summary of the circumstances leading to the enactment of § 3402(o):

During the 1960s, SUB payments were treated, for income tax purposes, as ordinary income to the recipient, but not as wages for purposes of either the income tax withholding statutes or FICA. It soon became evident, however, that treating SUB payments in that manner was creating a problem. Because SUB payments were not treated as wages, income tax was not withheld from SUB payments that were made to employees. Yet because SUB payments were included in gross income, the failure to withhold from those payments meant

ruling, the IRS concluded that payments made from a trust fund established pursuant to a supplemental unemployment compensation plan are not “wages” for the purposes of FICA, even though they were not tied to a state unemployment benefit program.¹⁹⁹ Here the IRS clarified that the payments considered in Rev. Rul. 56-249 are within the statutory definition of “supplemental unemployment benefits” under § 3402(o) and that while this type of payment is subject to income tax withholding, it is not a form of wages for FICA.²⁰⁰ This focus on SUB payments is in contrast to the non-statutory “dismissal payments” discussed in Rev. Ruls. 71-408 and 74-252.²⁰¹

Finally, in Rev. Rul. 90-72, the IRS announced: “the definition of SUB pay under section 3402(o) is *not* applicable to FICA or FUTA. For FICA and FUTA purposes, SUB pay is defined solely through a series of administrative pronouncements published by the Service.”²⁰² In this ruling, the IRS concluded that to be exempt from “wages” under FICA, SUB payments “must be linked to the receipt of state unemployment compensation and must not be received in a lump sum.”²⁰³ This ruling contended that it “restore[d] the distinction between SUB pay and dismissal pay by re-establishing the link between SUB pay and state unemployment compensation set forth in Rev. Rul. 56-249.”²⁰⁴ Further, “benefits provided in the form of a lump sum are not considered linked to state unemployment compensation for this purpose, and are therefore not excludable from wages as SUB pay.”²⁰⁵ The effect of Rev. Rul. 90-72, in short, was to clarify that only a specific type of payments are “SUB payments,” which would not be subject to FICA withholding, while providing that “dismissal payments,” broadly defined, are wages for FICA purposes. This ruling also provided that the definition of SUB payments, for FICA purposes, came from administrative pronouncements, rather than from § 3402(o).

that employees who received those payments were encountering large tax obligations attributable to the SUB payments at the end of the taxable year.

CSX Corp., 518 F.3d at 1336. To address this problem, I.R.C. § 3402(o) was added as part of the Tax Reform Act of 1969, Pub. L. No. 91-172, to extend federal income tax withholding to SUB payments, even though they were not “wages.” *CSX Corp.*, 518 F.3d at 1336.

199. Rev. Rul. 77-347, 1977-2 C.B. at 363.

200. *Id.*

201. *See supra* notes 196-97 and accompanying text.

202. Rev. Rul. 90-72, 1990-2 C.B. 211, 211-12 (quoted in *CSX Corp.*, 518 F.3d at 1339) (emphasis added).

203. *Id.* at 211.

204. *Id.* at 212.

205. *Id.*

The revenue rulings from 1956 to 1990 do not provide definitive guidance, although Rev. Rul. 90-72 appears to delineate the IRS's position as finding most of the severance payments at issue in this Note to be within the scope of "wages" by defining them as "dismissal payments." While the Federal Circuit and Sixth Circuit each provided a detailed analysis of these rulings, the courts have reached different conclusions.

1. Federal Circuit Analysis of the Revenue Rulings

The Federal Circuit in *CSX Corp.* took a detailed approach to analyzing the Revenue Rulings dating back to 1956. It considered CSX's reliance on Rev. Rul. 77-347, the first Ruling after the addition of I.R.C. § 3402(o), which held that benefits paid from a trust fund are not wages, even if the plan is not tied to a state unemployment benefit plan. The court ultimately rejected this reliance as improper, instead considering the particular factual circumstances at issue in the 1977 Ruling.²⁰⁶ Taking a holistic approach and considering all of the rulings as harmonious, the court rejected CSX's analogy to Rev. Rul. 77-347.²⁰⁷ The court summarized its conclusion accordingly:

If the 1977 revenue ruling stood for the proposition that all payments fitting the definition of SUB under section 3402(o) are deemed non-wages for purposes of FICA, as CSX contends, the 1965, 1971, and 1974 revenue rulings would appear to have been silently overruled. Rather than interpret the 1977 revenue ruling to have such a dramatic (but unannounced or unrecognized) effect, we think the 1977 revenue ruling is better interpreted to have the more modest effect of announcing that payments under a plan satisfying the definition of SUB in section 3402(o)(2)(A) are subject to income tax withholding, and payments under a plan having similar characteristics to the one in Rev. Rul. 56-249 are not subject to taxation under FICA.²⁰⁸

The Federal Circuit took care to discuss what it considered an important distinction between "dismissal payments," as discussed in earlier revenue rulings, and "supplemental unemployment benefits" as defined in § 3402(o).²⁰⁹ Under the Treasury Regulations, "not all dismissal

206. See *CSX Corp.*, 518 F.3d at 1337-38.

207. *Id.* at 1338.

208. *Id.*

209. See *id.* at 1338-41.

payments would constitute SUB payments, but all SUB payments would qualify as dismissal payments.”²¹⁰ The court noted that this distinction is not problematic within the confines of the income tax provisions in Chapter 24 of the tax code, as both types of payments are subject to withholding.²¹¹ But, the court contended, if the § 3402(o) definition of SUB payments is construed to apply to other provisions of the tax code, such as FICA, and it is interpreted to exclude SUB payments from “wages,” this would create a conflict with other courts’ treatment of dismissal payments as wages under FICA.²¹² Because the court had already rejected the statutory argument that § 3402(o) applies to FICA,²¹³ it classified the payments at issue as dismissal payments, and thus subject to FICA withholding.²¹⁴

2. Sixth Circuit Analysis of the Revenue Rulings

As if to foreshadow the present split among circuit courts of appeal, the bankruptcy court in *Quality Stores* asserted that “[r]evenue rulings do not have the binding force of statutory provisions or the presumption of correctness of the regulations,” thereby establishing that it would not give ultimate weight to a particular ruling.²¹⁵ In sharp contrast to the Federal Circuit’s approach, the Sixth Circuit relied on Rev. Rul. 77-347 to support its conclusion.²¹⁶ The Sixth Circuit characterized its differing approach from *CSX* as follows:

210. *Id.* at 1340. The court cited Treasury Regulation § 31.3401(a)-1(b)(4), which defines dismissal payments as “[a]ny payments made by an employer to an employee on account of dismissal, that is, involuntary separation from the service of the employer,” and Treas. Reg. § 31.3401(a)-1(b)(14)(ii), which defines supplemental unemployment compensation benefits as

“amounts which are paid to an employee pursuant to a plan to which the employer is a party, because of the employee’s involuntary separation from the employment of the employer, whether or not such separation is temporary, but only when such separation is one resulting directly from a reduction in force, the discontinuance of a plant or operation, or other similar conditions.”

Id.

211. *Id.* at 1340-41.

212. *Id.* at 1341 (citing *Abrahamsen v. United States*, 228 F.3d 1360 (Fed. Cir. 2000)); *Greenwald v. United States*, 2000 WL 16939 (S.D.N.Y. Jan. 10, 2000); *McCorkill v. United States*, 32 F. Supp. 2d 46 (D. Conn. 1999); *Meehan v. Comm’r*, 122 T.C. 396 (2004).

213. See *supra* Part IV.B.1 for a discussion of the Federal Circuit’s statutory analysis.

214. *CSX Corp.*, 518 F.3d at 1352. In concluding that dismissal payments are within the scope of FICA “wages,” the Federal Circuit relied on the 1950 amendments to the Social Security Act, which deleted an explicit exclusion of “dismissal payments” from the definition of “wages.” See *supra* text accompanying notes 193-95; see also *CSX Corp.*, 518 F.3d at 1345-46.

215. *In re Quality Stores, Inc.*, 383 B.R. 67, 75 (Bankr. W.D. Mich. 2008).

216. See *In re Quality Stores, Inc.*, 693 F.3d 605, 619 (6th Cir. 2012) (“Thus, Rev. Rul. 77-347 is consistent with both our conclusion and that of the bankruptcy court that because SUB payments are

In *CSX Corp.*, the Federal Circuit adopted the IRS's eight-part administrative definition of SUB pay set out in Rev. Rul. No. 56-249 and Rev. Rul. 90-72 rather than the express statutory definition provided by Congress in § 3402(o). That court characterized the payments before it as “dismissal pay” subject to FICA tax.²¹⁷

By contrast, we resolve the tension between the statutory enactments and the IRS revenue rulings in favor of the expressed will of the legislature. Applying the five-part definition that Congress enacted in § 3402(o)(2)(A), the payments made by Quality Stores to its former employees qualify as SUB payments, not “dismissal pay.” And as we have explained, SUB payments are not subject to FICA tax.²¹⁸

Like the issue of statutory interpretation, the courts’ approaches to the Revenue Rulings from 1956 to 1990 represent another fundamental departure in the courts’ analyses, offering further evidence of the need for a definite resolution.²¹⁹

D. Bridging the Circuit Split: A Summary

The Sixth Circuit in *Quality Stores* concluded: “We agree with the Federal Circuit on one final important point: ‘We acknowledge that this issue of statutory construction is complex and that the correct resolution of the issue is far from obvious.’”²²⁰ Neither the FICA statute nor the Treasury Regulations explicitly address SUB payments.²²¹ Instead, the courts looked to the provisions of the tax code that cover federal income tax withholding and used the definitions therein, particularly I.R.C.

not ‘wages’ and are only treated as if they were ‘wages’ under § 3402(o), SUB payments also are not ‘wages’ under FICA.”).

217. *Quality Stores*, 693 F.3d at 619 (internal citations omitted). By way of reminder, the court in *CSX Corp.* concluded that § 3402(o) did not apply to FICA, *see supra* text accompanying note 164.

218. *Quality Stores*, 693 F.3d at 619. The Sixth Circuit also contended that the Revenue Rulings conflicted with congressional intent. *Id.* at 616-17. The trial court in *CSX Corp.* had previously declined to consider the multi-part definition laid out in Rev. Rul. 56-249. *See CSX Corp. v. United States*, 52 Fed. Cl. 208, 217 (2002) (noting that the definition laid out in Rev. Rul. 56-249 was “not incorporated into I.R.C. § 3402(o)” by Congress, despite the fact that Congress presumably knew of the ruling at the time it enacted § 3402(o)).

219. *See infra* Part V.

220. *Quality Stores*, 693 F.3d at 620 (citing *CSX Corp. v. United States* 518 F.3d 1328, 1340 (Fed Cir. 2008)).

221. *See id.* at 611 (“Whether SUB payments are ‘wages’ under FICA is a complex question because the FICA statute does not expressly include or exclude SUB payments, nor do the Treasury regulations promulgated under FICA address the subject.”).

§ 3402(o).²²² Section 3402(o) defines “supplemental unemployment benefits” and provides that they should be treated “as if” they are a payment of wages for purposes of the federal income tax provisions.²²³ The courts take differing views of this provision and whether it requires a reading that the SUB payments are wages, and then, whether this income tax provision can be applied to FICA provisions. Contributing to this complexity is the lack of clear, discernible guidance on point, as demonstrated by the changing position of the IRS in its revenue rulings. The fact that each court conducted a painstakingly detailed analysis, only to reach opposite conclusions, shows that there is no simple legal answer. Further, the sociopolitical post-recession climate shows that there is no simple policy answer either.

V. A GREAT CASE AND A HARD CASE, BUT BAD LAW?

Issues of the type in this Note—those with broad importance, diverse stakeholders, and puzzling legal authority—give rise to the potential for seemingly arbitrary, ends-dictated judicial decisionmaking simply because the ambiguity in the legal authority makes it amenable to both sides of an argument. If ever there was such a thing, this form of decisionmaking is a likely precursor to “bad law.”

The Supreme Court will consider *In re Quality Stores* on appeal in the near future,²²⁴ which may provide the binding authority needed to generate uniformity and thereby mitigate the “bad law” potential in lower-court decisions. In theory, a Supreme Court decision will serve the singular goal of interpreting the statute—“find[ing] the meaning of some not very difficult words.”²²⁵ In its decision, then, the Court should provide an

222. *See id.* (“We observe that, for purposes of federal income tax withholding, I.R.C. § 3402, Congress adopted a definition of ‘wages’ that is nearly identical to the definition of ‘wages’ included in FICA.”); *CSX Corp.*, 518 F.3d at 1331 (noting “the general rule that the term ‘wages’ has the same meaning for FICA as for the income tax laws”); *see also* *Rowan Cos. v. United States*, 452 U.S. 247 (1981).

223. I.R.C. § 3402(o)(1) (2006 & Supp. 2012).

224. *See Quality Stores*, 693 F.3d at 605, *cert. granted*, 81 USLW 3680, 2013 WL 2370291 (2013).

225. *N. Sec. Co. v. United States*, 193 U.S. 197, 401 (1904) (Holmes, J., dissenting); *see also supra* note 2 and accompanying text. In *Northern Securities Co.*, the Court held that the Sherman Act applied to a securities company. *See id.* at 360 (majority opinion). Justice Holmes’s dissent could aptly apply to the issue in this Note:

Great cases, like hard cases, make bad law. For great cases are called great, not by reason of their real importance in shaping the law of the future, but because of some accident of immediate overwhelming interest which appeals to the feelings and distorts the judgment. These immediate interests exercise a kind of hydraulic pressure which makes what previously was clear seem doubtful, and before which even well settled principles of law will bend.

answer to the statutory puzzle. Of course, given the soundness in both the Sixth Circuit's and the Federal Circuit's opinions, conducting a purely legal analysis resulting in any clear conclusion is, quite apparently, no simple task.

That said, reconsideration of one piece in the statutory puzzle could provide a helpful basis for moving toward a decision. Both the Sixth Circuit and the Federal Circuit considered *Rowan Companies, Inc. v. United States*²²⁶ for its proposition that "wages" has the same definition under FICA as it does under the income tax provision.²²⁷ The 1983 "decoupling amendment" provided that an income tax regulation creating certain exclusions from "wages" should not be construed to require a similar exclusion from "wages" in FICA regulations.²²⁸ It remains ineffective, however, in the absence of an applicable Treasury regulation. The amendment simply "gives the IRS *the ability* to establish distinctions between the two statutory definitions" of wages, a power which has not yet been exercised.²²⁹

While the Sixth Circuit and Federal Circuit were bound by *Rowan*, the Supreme Court is not. Even without expressly overruling *Rowan*, the Court may take the "decoupling amendment" as persuasive and decline to apply *Rowan* to this analysis. Removing *Rowan* from the picture undermines the analytical basis for applying the income tax provision to FICA. Thus, the analysis would focus only on whether the particular severance payments at issue fall within the FICA definition of wages, with

What we have to do in this case is to find the meaning of some not very difficult words. We must try,—I have tried,—to do it with the same freedom of natural and spontaneous interpretation that one would be sure of if the same question arose upon an indictment for a similar act which excited no public attention, and was of importance only to a prisoner before the court. Furthermore, while at times judges need for their work the training of economists or statesmen, and must act in view of their foresight of consequences, yet, when their task is to interpret and apply the words of a statute, their function is merely academic to begin with,—to read English intelligently,—and a consideration of consequences comes into play, if at all, only when the meaning of the words used is open to reasonable doubt.

Id. at 400–01 (Holmes, J., dissenting).

226. 452 U.S. 247 (1981).

227. *See Rowan*, 452 U.S. at 263; *supra* Part IV.A.

228. I.R.C. § 3121(a) (2006 & Supp. V 2012).

229. *In re Quality Stores, Inc.*, 383 B.R. 67, 78 (Bankr. W.D. Mich. 2008) (emphasis added). The court characterized the argument as: "According to the IRS, these amendments contain a 'decoupling' provision that specifically rejects *Rowan*'s conclusion that wages should be defined the same for purposes of income tax withholding and FICA taxation." *Id.* at 73; *see also* *Canisius Coll. v. United States*, 799 F.2d 18, 21 (2d Cir. 1986) ("Congress in 1983 overturned the general premise of *Rowan* by enacting provisions that 'decoupled' the interpretations of FICA and FUTA wages from the interpretation of wages for income-tax purposes.").

no consideration of the income tax provision.²³⁰ Such an approach would more truly be characterized as simply “find[ing] the meaning of some not very difficult words.”²³¹

Despite the difficulty in answering this question from a strictly legal perspective with no reference to policy matters, a comprehensive answer that addresses *both* the statutory puzzle *and* the sociopolitical conundrum would best come from Congress or perhaps an applicable Treasury regulation.

Purportedly, Congress would stand in the best position to bring to bear the various policy matters in a comprehensive analysis as it rewrites the law.²³² Medicare and Social Security require attention,²³³ at which time Congress could also clarify the exact scope of FICA. Of course, an issue involving any *one* of Social Security, Medicare, a payroll tax, and unemployment is akin to a political minefield. In this sense, it is not difficult to understand why politicians may prefer not to take a position on an issue that combines *all* of those thorny components and leads to a discernible loss to at least one major stakeholder.²³⁴ Even if one entirely sets aside partisan politics and re-election motives, there is no straightforward answer. However ideal it may be in the abstract, the possibility of a congressional response is remote under even the best of circumstances.²³⁵

A more plausible middle ground, one allowing for broader policy consideration would come in the form of a Treasury regulation. As noted, promulgation of regulations that clarify whether FICA and the income tax provisions are to be given the same definition *and* treatment of “wages” would allow courts to refine their analyses.²³⁶ Of course, this regulation would only guide future courts’ analyses as to the applicability of *Rowan*, and it would not guarantee a uniform outcome, as the question would still remain a complicated issue of statutory interpretation.²³⁷

230. See I.R.C. § 3121(a) (2006 & Supp. V 2012).

231. *N. Sec. Co. v. United States*, 193 U.S. 197, 401 (1904) (Holmes, J., dissenting).

232. See *Quality Stores*, 693 F.3d at 620 (“While the Supreme Court may ultimately provide us with the correct resolution of these difficult issues under the law as it currently stands, only Congress can clarify the statutes concerning the imposition of FICA tax on SUB payments. Our role is to interpret the statutory law as it presently exists, and we have done that today.”).

233. See *supra* note 48.

234. See *supra* note 8 and accompanying text.

235. It is likely that even a more cohesive Congress than the present one might struggle to come to a consensus on whether severance payments are “wages” under FICA. As discussed, it is a politically thorny issue. That said, given the present state of our sharply divided Congress, it is unclear that this issue will receive such careful attention in the near future.

236. See *supra* notes 135 and 143 and accompanying text.

237. In the absence of *Rowan* as a piece to this puzzle (and depending on the exact Treasury

Any solution, be it legislative, regulatory, or judicial, is going to be imperfect because of a structural inability for any such response to consider all relevant components of the broader issue. However apparently simple in implementation, a single answer will have major consequences for at least one group of stakeholders and the potential for broad consequences for all involved parties. The upcoming Supreme Court decision is much needed to promote uniformity among the courts confronting this and similar issues, but ideally, at some point in the future, a thoughtful and comprehensive response will come from Congress.

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regulation that would be promulgated), courts would be left to analyze the particular severance payments at issue, and then to determine whether they are “wages” as that term is defined in I.R.C. § 3121(a), with no consideration of the analogous income tax provisions. Varying approaches to statutory interpretation could still prevent unanimity on this issue, depending on how the Supreme Court decides this case.

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