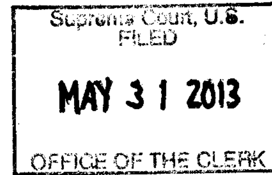
Supreme Court, U.S.
FILED
MAY 31 2013
OFFICE OF THE CLERK

No. 12-1408

In the Supreme Court of the United States

UNITED STATES OF AMERICA, PETITIONER

v.

QUALITY STORES, INC., ET AL.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

PETITION FOR A WRIT OF CERTIORARI

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QUESTION PRESENTED

Whether severance payments made to employees whose employment was involuntarily terminated are taxable under the Federal Insurance Contributions Act, 26 U.S.C. 3101 *et seq.*

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PETITION FOR A WRIT OF CERTIORARI

The Solicitor General, on behalf of the United States, respectfully petitions for a writ of certiorari to review the judgment of the United States Court of Appeals for the Sixth Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App., *infra*, 1a-30a) is reported at 693 F.3d 605. The opinion of the district court (App., *infra*, 33a-54a) is reported at 424 B.R. 237. The opinion of the bankruptcy court (App., *infra*, 55a-77a) is reported at 383 B.R. 67.

JURISDICTION

The judgment of the court of appeals was entered on September 7, 2012. A petition for rehearing was denied on January 4, 2013 (App., *infra*, 31a-32a). On March 25, 2013, the Chief Justice extended the time within which to file a petition for a writ of certiorari to and including May 3, 2013. On April 22, 2013, the Chief Justice fur-

ther extended the time to May 31, 2013. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

STATUTORY AND REGULATORY PROVISIONS INVOLVED

Relevant statutory and regulatory provisions are reproduced in the appendix to this petition. App., *infra*, 84a-214a.

STATEMENT

1. Social Security and Medicare benefits are financed through taxes collected under the Federal Insurance Contributions Act (FICA or the Act), 26 U.S.C. 3101 *et seq*. FICA taxes are imposed on both employers and employees, and both elements of the tax are imposed on all "wages" paid by an employer or received by an employee "with respect to employment." 26 U.S.C. 3101(a) and (b), 3111(a) and (b). FICA defines "wages" in relevant part as "all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash." 26 U.S.C. 3121(a) (2006 & Supp. V 2011). The Act defines "employment" in turn as "any service, of whatever nature, performed * * * by an employee for the person employing him." 26 U.S.C. 3121(b) (2006 & Supp. V 2011).

Section 3402(*o*) of Title 26 deals with withholding of income tax and is entitled "[e]xtension of withholding to certain payments other than wages." 26 U.S.C. 3402(*o*). The provision states a "[g]eneral rule" that, for purposes of Chapter 24 of Title 26 (dealing with income-tax withholding) and certain related provisions, "any supplemental unemployment compensation benefit paid to an individual * * * shall be treated as if it were a payment of wages by an employer to an employee for a payroll period." The term "[s]upplemental unemployment compensation benefits" is defined to mean "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 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." 26 U.S.C. 3402(*o*)(2)(A).

2. In 2001, respondent Quality Stores, Inc. (Quality Stores) and several affiliated companies entered into bankruptcy proceedings. Both before and after their entry into bankruptcy, respondents terminated thousands of their employees. Those employees received severance payments from respondents pursuant to two separate plans. App., *infra*, 2a-3a. The question presented here is whether those severance payments are taxable as "wages" under FICA.

a. Under the terms of the pre-petition severance plan, any employee who was terminated for general business reasons (like the closing of a store or a plant) received severance pay based on his job grade and management level in the organization. The President and Chief Executive Officer received 18 months of severance pay; senior management executives received 12 months of severance pay; and other managers and employees received one week of severance pay for each full year of service. The amount of the severance pay was equal to the employee's regular salary for the covered period, and respondents made the severance payments on their normal payroll schedule. Under the pre-petition plan, 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. App., *infra*, 3a-4a.

The post-petition severance plan was designed to encourage remaining employees to defer their job searches and to dedicate their time and efforts to the company. As a result, to be eligible for severance pay under the post-petition plan, an employee had to complete his last day of service as scheduled by the company. For those employees who did so, company executives received between six and 12 months of severance pay; full-time salaried and hourly employees who had been employed by the company 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); and salaried and hourly employees with less than two years of service received one week of severance pay. All of these post-petition severance amounts were paid as a lump sum at the end of an employee's service. Under the post-petition plan, salaried employees received an average of 5.2 weeks of severance pay, while hourly employees received an average of 3.1 weeks of severance pay. App., *infra*, 4a.

b. For federal income-tax purposes, respondents reported the payments as wages on W-2 forms and withheld federal income tax. Respondents also treated the severance payments as taxable under FICA; they withheld and remitted to the Internal Revenue Service (IRS) both the FICA tax that they owed as employers and the FICA tax that their employees owed. In September 2002, however, respondents filed for a refund of approximately $1 million in FICA tax that they had paid as employers and that they had paid on behalf of roughly 1850 employees between late 1999 and mid-2002. Respondents subsequently filed the present adversary proceeding in the bankruptcy court seeking a refund of the $1 million in FICA tax. App., *infra*, 5a-6a.

3. a. The bankruptcy court granted summary judgment to respondents. App., *infra*, 55a-77a. The court's analysis focused not on the relevant FICA provisions, but on 26 U.S.C. 3402(*o*), which addresses the withholding of income tax. Based on the parties' stipulation of certain facts, the bankruptcy court found that the severance payments at issue here fall within Section 3402(*o*)(2)(A)'s definition of "supplemental unemployment compensation benefits." *Id.* at 63a-64a.[1] The court also accepted respondents' argument that "supplemental unemployment compensation benefits," as defined in Section 3402(*o*)(2)(A), "are not wages for income tax withholding purposes, but * * * are merely treated as if they were wages." *Id.* at 63a-64a (emphasis omitted). The bankruptcy court further concluded that Congress intended the definition of "wages" to be the same for purposes of income and FICA tax withholding, and it inferred that because "supplemental unemployment compensation benefits are not wages for purposes of income tax withholding, they are likewise not wages under FICA." *Id.* at 76a-77a (internal quotation marks omitted). The court found support for its conclusion in the decision of the Court of Federal Claims (CFC) in *CSX Corp.* v. *United States*, 52 Fed. Cl. 208 (2002).

b. After the bankruptcy court issued its decision in this case, the Federal Circuit reversed the CFC decision

[1] The government stipulated that the severance payments at issue resulted from "an employee's involuntary separation from employment, resulting directly from a reduction in force or the discontinuance of a plant or operation." 05-80573-jdg, Doc. No. 21, at 4 (Bankr. W.D. Mich. Aug. 15, 2006). The parties further stipulated that the severance payments at issue were not tied to the receipt of state unemployment compensation and were not attributable to the rendering of any particular services by employees to respondents. See *id.* at 4-5.

on which the bankruptcy court had relied. See *CSX Corp.* v. *United States*, 518 F.3d 1328 (2008). The Federal Circuit held in *CSX Corp.* that the severance payments at issue in that case, which were made in connection with a company's reduction in force, were "wages" subject to FICA taxation. See *id.* at 1352. In light of the Federal Circuit's intervening decision in *CSX Corp.*, the government filed a motion for reconsideration in the present case. The bankruptcy court granted the government's motion but "ratified" its previous opinion and order without explanation. App., *infra*, 78a-80a.

4. The district court affirmed. App., *infra*, 33a-54a. The court recognized that FICA broadly defines the term "wages," and it agreed with the government that severance payments do not fall within any of the "statutory exceptions to [that] broad definition." *Id.* at 41a; see *id.* at 49a. The district court ruled in respondents' favor, however, on the same rationale as the bankruptcy court. The district court determined that the severance payments at issue here fall within Section 3402(*o*)(2)(A)'s definition of "supplemental unemployment compensation benefits"; that Section 3402(*o*) reflects Congress's view that any payments covered by that definition are not wages for purposes of income-tax withholding; and that such payments therefore should not be treated as wages for purposes of FICA tax withholding. See *id.* at 49a-50a. The district court acknowledged that its decision was in conflict with the Federal Circuit's decision in *CSX Corp.* See *id.* at 51a-52a.

5. The court of appeals affirmed. App., *infra*, 1a-30a. Like the bankruptcy and district courts, the court of appeals did not rest its decision on the text of the relevant FICA provisions. Rather, the court reasoned that, under this Court's decision in *Rowan Cos., Inc.* v. *United*

States, 452 U.S. 247 (1981), "the statutory term 'wages' should be interpreted consistently in the statutes governing FICA and the federal income tax." App., *infra*, 19a. The court further concluded that the severance payments at issue here fall within the definition of "supplemental unemployment compensation benefits" in Section 3402(*o*)(2)(A). *Id.* at 11a.

The court of appeals explained that, under Section 3402(*o*)(1), "any payment made to an employee that meets the statutory definition of a [supplemental unemployment compensation] payment 'shall be treated *as if it were a payment of wages* by an employer to an employee for a payroll period.'" App., *infra*, 11a (quoting 26 U.S.C. 3402(*o*)(1)) (emphasis added by court of appeals). The court found that "the necessary implication arising from [the italicized] phrase is that Congress did not consider [supplemental unemployment compensation] payments to be 'wages,' but allowed their treatment as wages to facilitate federal income tax withholding for taxpayers." *Id.* at 11a-12a. The court further reasoned that, if such payments "are not 'wages' but are only treated as if they were 'wages' for purposes of federal income tax withholding, then [such] payments also are not 'wages' under the nearly identical definition of that term found in the FICA statute." *Id.* at 13a-14a. Like the district court, the court of appeals recognized that its decision was in conflict with the Federal Circuit's decision in *CSX Corp.* See *id.* at 20a.

REASONS FOR GRANTING THE PETITION

FICA broadly defines the term "wages" as all remuneration received for any service performed by an employee. See 26 U.S.C. 3121(a) and (b) (2006 & Supp. V 2011). The severance payments at issue in this case fit comfortably within that broad definition, which encom-

passes "the entire employer-employee relationship for which compensation is paid to the employee by the employer." *Social Sec. Bd.* v. *Nierotko*, 327 U.S. 358, 366 (1946). For several decades, moreover, the IRS has taken the position that payments like these are FICA wages, and Congress has taken no action to override that determination.

In holding that the severance payments here are not subject to FICA tax, the court of appeals did not suggest that those payments fall outside the applicable definition of "wages." Rather, the court relied on what it perceived to be the negative implication of 26 U.S.C. 3402(*o*), which mandates withholding of income tax from certain payments made to terminated employees. The court inferred that, because Section 3402(*o*)(2) states that any supplemental unemployment compensation benefit "shall be treated as if it were a payment of wages" for purposes of federal income-tax withholding, such payments should *not* be treated as wages for purposes of FICA taxation. As the Federal Circuit recognized in a factually analogous case, Section 3402(*o*) does not support that inference. See *CSX Corp.* v. *United States*, 518 F.3d 1328, 1340-1342 (2008). And, as the court below acknowledged (App., *infra*, 20a), the Sixth Circuit's decision in this case squarely conflicts with the Federal Circuit's decision in *CSX Corp.*

In addition to being in conflict with decisions of this Court and other courts of appeals, the question presented here is both recurring and important; the amount at issue for this and other claims exceeds $1 billion and is expected to grow. In light of the administrative importance of the issue, and the square circuit conflict, this Court's review is warranted.

A. The Decision Below Is Incorrect

1. a. FICA taxes finance Social Security and Medicare benefits. They are imposed on both employers and employees, and both elements of the tax are imposed on all "wages" paid by an employer or received by an employee "with respect to employment." 26 U.S.C. 3101(a) and (b), 3111(a) and (b). FICA defines "wages" in relevant part as "all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash." 26 U.S.C. 3121(a) (2006 & Supp. V 2011). The Act defines "employment" in turn as "any service, of whatever nature, performed * * * by an employee for the person employing him." 26 U.S.C. 3121(b) (2006 & Supp. V 2011). FICA thus defines "wages" to include "all remuneration" paid for "any service" performed by an employee. On their face, those inclusive terms "import a breadth of coverage." *Mayo Found. for Med. Educ. & Research* v. *United States*, 131 S. Ct. 704, 715 (2011) (*Mayo Found.*) (quoting *Nierotko*, 327 U.S. at 365); *id.* at 709.

That broad definition of "wages" easily encompasses the severance payments at issue here. Those payments were undoubtedly a form of "remuneration." See, *e.g.*, *Black's Law Dictionary* 1409 (9th ed. 2009) (defining "remuneration" as "[p]ayment; compensation"); *Webster's Third New International Dictionary of the English Language* 1921 (1993) (defining "remunerate" as "to pay an equivalent to (a person) for a service, loss, or expense: recompense, compensate") (capitalization omitted); 8 *Oxford English Dictionary* 439 (1st ed. 1933) (defining "[r]emuneration" as "[r]eward, recompense, repayment; payment, pay"); see also *Nierotko*, 327 U.S. at 364 (concluding that "[s]urely" an award of back pay for an employee's wrongful discharge "is 'remuneration'").

Those payments were also made in return for "any service, of whatever nature, performed" by the employee. 26 U.S.C. 3121(b) (2006 & Supp. V 2011). The payments were calculated by reference to individual employees' positions, length of service, and former salaries.

This case involves payments made under two different severance plans, depending on whether employees were terminated before or after respondents entered into bankruptcy. Both plans made payments (either on a periodic basis or as a lump sum) once employees had been terminated, and both plans thus compensated those employees for their previous service. App., *infra*, 3a-4a. The post-petition plan served the further purpose of ensuring that, once respondents had entered bankruptcy, remaining employees would have an incentive to defer their job searches and dedicate their time and efforts to the company. *Id.* at 4a. Those employees who did so were then compensated for providing that additional service.

Both the pre-petition and post-petition severance plans at issue here provided compensation to employees for "service" that those employees had rendered to respondents. By defining "employment" expansively to include "any service, of whatever nature," FICA encompasses not only compensation for an employee's performance of specific functions but also compensation (like a bonus or severance payment) that accounts more generally for an employee's entire performance over some period of time. See, *e.g.*, *Rivera* v. *Baker West, Inc.*, 430 F.3d 1253, 1258 (9th Cir. 2005) (discussing "the broad, inclusive nature of 'employment'"); *Hemelt* v. *United States*, 122 F.3d 204, 209 (4th Cir. 1997) (same). FICA's inclusive definition of the terms "wages" and "employment" includes compensation based on and aris-

ing out of the employer-employee relationship, unless that type of compensation is excepted from the scope of the Act. The link between respondents' payments and the employees' prior service is particularly clear in this case because the amounts of the various employees' payments were calculated by reference to the positions those individuals had held within respondents' work force, the length of time the employees had worked for respondents, and the salaries they had earned during their periods of service.

b. FICA contains specific exceptions to both "wages" and "employment"—*i.e.*, types of remuneration that do not constitute wages, see 26 U.S.C. 3121(a)(1)-(23) (2006 & Supp. V 2011), and types of services that do not constitute employment, see 26 U.S.C. 3121(b)(1)-(21) (2006 & Supp. V 2011). This Court has observed that the specificity of the exceptions is an additional reason why the terms "wages" and "employment" should be construed broadly. See *United States* v. *Silk*, 331 U.S. 704, 711-712 (1947) ("The very specificity of the exemptions * * * and the generality of the employment definitions indicates that the terms 'employment' and 'employee,' are to be construed to accomplish the purposes of the legislation.") (footnote omitted); cf. *Mayo Found.*, 131 S. Ct. at 715 ("[W]e have instructed that 'exemptions from taxation are to be construed narrowly.'") (quoting *Bingler* v. *Johnson*, 394 U.S. 741, 752 (1969)). Respondents do not contend, and the court of appeals did not hold, that the severance payments at issue here fall within any of the statutory exceptions to "wages."

c. Between 1956 and 1990, the IRS issued numerous Revenue Rulings addressing whether particular payments to terminated employees should be treated as "wages" for purposes of income-tax or FICA withhold-

ing. See generally *CSX Corp.*, 518 F.3d at 1335-1340. Under the framework the IRS developed during that period, the severance payments at issue in this case are clearly FICA "wages."

i. In the mid-1950s, several large industrial employers adopted plans pursuant to collective bargaining in which the employers agreed to fund trusts that would supplement state unemployment compensation benefits for workers who were terminated. See *CSX Corp.*, 518 F.3d at 1334. Those supplemental benefits depended for their effectiveness on their not being treated as "wages," because employees in many States were ineligible for unemployment benefits if they were receiving wages from employers. As a result, if the supplemental benefits paid by employers were treated as wages, many employees would lose the state unemployment benefits that their employers' payments were intended to supplement. See *id.* at 1335.

In 1956, the IRS issued a Revenue Ruling addressing the status, for income-tax and FICA purposes, of payments made by one such trust. See Rev. Rul. 56-249, 1956-1 C.B. 488. The IRS identified eight different factors as supporting the conclusion that those payments were not "wages." The IRS explained, *inter alia*, that "the amount of [such] benefit[s] * * * is based upon * * * the appropriate State unemployment compensation laws." *Id.* at 492.

The plan at issue in the 1956 Revenue Ruling was the result of collective bargaining, and it created a trust to make periodic payments to terminated employees. Over the next four years, the IRS issued a series of Revenue Rulings explaining that the principles of the 1956 Revenue Ruling would apply with equal force to plans that were unilaterally instituted by an employer, Rev. Rul.

58-128, 1958-1 C.B. 89; that made lump sum rather than periodic payments to employees, see Rev. Rul. 59-227, 1959-2 C.B. 13; and that made payments directly to employees rather than through a trust, see Rev. Rul. 60-330, 1960-2 C.B. 46. The IRS specified, however, that in order not to result in the payment of "wages," plans had to be "similar in all material details" to the plan at issue in the 1956 Revenue Ruling. Rev. Rul. 58-128, 1958-1 C.B. at 90; see Rev. Rul. 60-330, 1960-2 C.B. at 48.

ii. Until 1950, the FICA definition of "wages" excluded "[d]ismissal payments which the employer is not legally required to make." 26 U.S.C. 1426(a)(4) (1946). In 1950, however, Congress amended FICA to eliminate that exception. See Social Security Act Amendments of 1950, ch. 809, 64 Stat. 477. Both before and after the passage of Section 3402(*o*), the IRS issued Revenue Rulings concluding that various types of dismissal payments were "wages." In 1965, the IRS ruled that "[l]ump sum separation and severance allowances paid to laid-off employees in the railroad industry" constituted "wages" subject to income-tax withholding and "compensation" subject to taxation under the Railroad Retirement Tax Act (which is the equivalent of FICA in the railroad industry). Rev. Rul. 65-251, 1965-2 C.B. 395. In 1971, the IRS ruled that "[d]ismissal payments made to former employees" were "wages" subject to both FICA tax and income-tax withholding. Rev. Rul. 71-408, 1971-2 C.B. 340. In that case, a company went out of business and made payments to terminated employees with five years or more service with the company. *Id.* at 341. As in this case, "[t]he computation of the amount of each employee's award took into account the employee's rate of pay and years of service." *Ibid.* The IRS concluded that

"the amounts of dismissal payments [were] 'wages' for purposes of [FICA]." *Ibid.*

iii. In 1990, the IRS set forth in detail its position on the relationship between the two categories of payments described above and the criteria that govern the determination whether particular payments to terminated employees are FICA "wages." The IRS explained that, to be exempt from FICA's definition of "wages," payments made to terminated employees must be "linked to state unemployment compensation" and "designed to supplement the receipt of state unemployment compensation." Rev. Rul. 90-72, 1990-2 C.B. 211, 212. Under that approach, the severance payments at issue here clearly are not exempt from FICA taxation because they are wholly unconnected to state unemployment compensation. Rather, like the dismissal payments found to be FICA "wages" in the 1971 Revenue Ruling, the payments are calculated by reference to individual employees' positions, length of service, and former salaries.

2. The court of appeals did not rest its analysis on the FICA provisions that define the terms "wages" and "employment," 26 U.S.C. 3121(a) and (b) (2006 & Supp. V 2011). Rather, the court relied on 26 U.S.C. 3402(*o*), which governs the withholding of federal income tax. App., *infra*, 10a-14a. Section 3402(*o*) is entitled "[e]xtension of withholding to certain payments other than wages" and states that "any supplemental unemployment compensation benefit paid to an individual * * * shall be treated *as if it were a payment of wages* by an employer to an employee for a payroll period." 26 U.S.C. 3402(*o*)(1)(A) (emphasis added).

The court of appeals held that the severance payments at issue in this case fall within the definition of "supplemental unemployment compensation benefit"

contained in Section 3402(*o*)(2)(A). See App., *infra*, 11a. Based on Congress's directive that any such payment "shall be treated as if it were a payment of wages" for purposes of income-tax withholding, the court inferred that payments covered by that definition are not *in fact* wages for income-tax purposes. See *id.* at 11a-12a. The court further determined that, under this Court's decision in *Rowan Cos., Inc.* v. *United States*, 452 U.S. 247 (1981), "the statutory term 'wages' should be interpreted consistently in the statutes governing FICA and the federal income tax." App., *infra*, 19a. The court concluded that, because (in its view) respondents' severance payments "are not 'wages' but are only treated as if they were 'wages' for purposes of federal income tax withholding, then [such] payments also are not 'wages' under the nearly identical definition of that term found in the FICA statute." *Id.* at 13a-14a. The court of appeals' chain of reasoning reflects significant misunderstandings of Section 3402(*o*)'s text, history, and purpose.

a. The court of appeals gave insufficient weight to the prefatory language of Section 3402(*o*)(1), which states that the rules therein—including the rule that supplemental unemployment compensation payments shall be treated as wages for purposes of income tax withholding—apply "[f]or purposes of this chapter (and so much of subtitle F as relates to this chapter)." The applicability of Section 3402(*o*)(1) is thus expressly limited to Chapter 24 (income tax withholding) and those portions of Subtitle F (matters of procedure and administration) that relate to Chapter 24. By contrast, FICA is codified at Chapter 21 of the Internal Revenue Code. As the Federal Circuit has explained, "Congress's decision to restrict the scope of the rule set forth in [S]ection 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." *CSX Corp.*, 518 F.3d at 1341. The court of appeals therefore should have construed FICA's definition of "wages" with reference to its own terms, not by drawing inferences from Section 3402(*o*).

b. The history of Section 3402(*o*) belies any suggestion that the provision was intended to exempt from FICA taxation payments that would otherwise be treated as FICA "wages." Rather, Section 3402(*o*) was Congress's response to a different problem dealing with a particular category of unemployment compensation benefits. As explained above, the IRS determined in 1956, and confirmed in later Revenue Rulings, that certain payments linked to state unemployment compensation schemes should not be viewed as "wages." The IRS's 1956 Revenue Ruling noted, however, that such payments were nevertheless "includible in the gross incomes" of recipients. Rev. Rul. 56-249, 1956-1 C.B. at 488; see *CSX Corp.*, 518 F.3d at 1336.

Because those supplemental payments were taxable as income to recipients, but were not subject to income-tax withholding as "wages," recipients found themselves subject to substantial tax obligations when they filed their returns. See *CSX Corp.*, 518 F.3d at 1336. In 1969, at the Treasury Department's suggestion, Congress enacted Section 3402(*o*) to address that particular problem. Section 3402(*o*) provides that "any supplemental unemployment compensation benefit paid to an individual * * * shall be treated as if it were a payment of wages by an employer to an employee for a payroll period." 26 U.S.C. 3402(*o*)(1)(A). Section 3402(*o*) thus ensures that supplemental unemployment compen-

sation benefits, even if not deemed wages, are subject to income-tax withholding by employers. Section 3402(*o*) also defines the term "supplemental unemployment compensation benefits" broadly to encompass the different types of plans that employers had developed prior to its enactment. See 26 U.S.C. 3402(*o*)(2)(A); see also *CSX Corp.*, 518 F.3d at 1336-1337.

As explained above, the IRS has long distinguished, for both FICA and income-tax purposes, between different types of payments made by employers to terminated employees. In enacting Section 3402(*o*), Congress did not seek either to redraw the line that the IRS had drawn, or to restrict the IRS's authority (within the limits established by other provisions of law) to determine which such payments should be treated as "wages." See Rev. Rul. 90-72, 1990-2 C.B. at 211 (explaining that "[t]he definition of [supplemental unemployment compensation benefit] pay under [S]ection 3402(o) is not applicable for FICA * * * purposes"). Congress simply addressed a practical difficulty that had arisen by reason of the fact that certain non-wage payments were still part of the recipient's gross income and therefore were ultimately subject to federal income tax even in the absence of withholding.

c. On its face, Section 3402(*o*)(2)(A)'s broad definition of "[s]upplemental unemployment compensation benefits" encompasses *both* the payments linked to state unemployment compensation that the IRS had historically treated as non-wage income, and the dismissal payments that the IRS had viewed as "wages." So long as Section 3402(*o*) is given only the effect that its language literally dictates (*i.e.*, that "supplemental unemployment compensation benefits" as defined in the statute be subject to income-tax withholding), the breadth of the statutory

definition is of no practical concern. "For purposes of chapter 24 (income tax withholding), it was not important for Congress to define [supplemental unemployment compensation benefit] payments narrowly or to distinguish between [supplemental unemployment compensation benefit] payments and 'dismissal' payments, since both were treated similarly for withholding purposes." *CSX Corp.*, 518 F.3d at 1340. If, in some of its applications, Section 3402(*o*) mandates withholding of income tax from payments that would *already* be subject to income-tax withholding, no practical harm is done.

The breadth of the statutory definition creates anomalous results, however, if payments within that definition are viewed for all purposes as non-wage income. As the Federal Circuit explained in *CSX Corp.*, "if [S]ection 3402(*o*) is deemed to render all [supplemental unemployment compensation benefit] payments (as defined therein) non-wages, and if the non-wage character of [supplemental unemployment compensation benefit] payments (as so defined) is deemed to apply to FICA, [Section 3402(*o*)] creates a square conflict with the treatment of dismissal payments as wages under FICA since 1950." 518 F.3d at 1341. Neither the text nor the history of Section 3402(*o*) provides any sound basis for construing it to override IRS practice in that manner. Section 3402(*o*) applies by its terms only for purposes of specified income-tax-related provisions, see pp. 15-16, *supra*, and it was designed to *increase* the incidence of income-tax withholding. If Congress had sought to *eliminate* FICA withholding from the sorts of dismissal payments that the IRS had historically treated as FICA wages, the language it used in Section 3402(*o*) would

have been a remarkably oblique way of accomplishing that result.

To be sure, Section 3402(*o*) reflects Congress's understanding that *some* of the payments encompassed by the statutory definition of "supplemental unemployment compensation benefits" would not otherwise be viewed as "wages." The provision would have served no useful purpose if *all* such payments were already subject to income-tax withholding. But "[t]o 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." *CSX Corp.*, 518 F.3d at 1342 (emphasis added).[2]

Thus, Section 3402(*o*) simply directs that payments encompassed by the statutory definition will be subject to income-tax withholding *whether or not* they would

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[2] The court of appeals also relied in part on the title of Section 3402(*o*), "Extension of withholding to certain payments other than wages." The court stated that "[t]he phrase 'other than wages' supports our conclusion that Congress knew that it was extending federal income tax withholding to payments 'other than wages' when it enacted [Section] 3402(*o*)." App., *infra*, 12a-13a. Under the government's reading, however, the purpose and effect of Section 3402(*o*) was to extend income-tax withholding to "payments other than wages," namely the payments related to state unemployment compensation that the IRS had treated, in the 1956 Revenue Ruling and subsequently, as non-wage income. The fact that the statutory definition of "supplemental unemployment compensation benefits" also encompasses some wage payments neither vitiates that intent nor renders the government's reading inconsistent with the title of Section 3402(*o*).

otherwise be "wages." The provision does not explicitly address, and has no logical bearing on, the determination whether particular payments to terminated employees are subject to FICA taxation. Rather, that determination is governed by other provisions of law. And, once Section 3402(*o*) is understood to be irrelevant to questions of FICA taxation, the severance payments at issue here clearly constitute FICA "wages." See pp. 8-14, *supra*.

B. The Decision Below Conflicts With Decisions Of This Court And Other Courts Of Appeals

1. The court of appeals' decision is inconsistent with this Court's decision in *Nierotko, supra*. In that case, an employee had been wrongfully discharged and was ordered to be reinstated by his employer with back pay. See 327 U.S. at 359-360. The question in *Nierotko* was whether the back pay award constituted "wages" under the Social Security Act, which defined that term in the same way as FICA. See *id.* at 362-363.

In applying that statutory definition, the Court in *Nierotko* first held that "the back pay is remuneration." 327 U.S. at 364 (internal quotation marks omitted). It then held that the back pay was awarded for the employee's "service," even though he had not worked during the period of his wrongful discharge. The Court explained that "[t]he very words 'any service . . . performed . . . for his employer,' with the purpose of the Social Security Act in mind, import breadth of coverage. They admonish us against holding that 'service' can be only productive activity." *Id.* at 365. The Court concluded that "'service' as used by Congress in this definitive phrase means not only work actually done but the entire employer-employee relationship for which com-

pensation is paid to the employee by the employer." *Id.* at 365-366.

The Court's reasoning in *Nierotko* indicates that the severance payments at issue here constitute wages for FICA purposes. Respondents' severance payments were compensation for "service, of whatever nature, performed" by their employees, 26 U.S.C. 3121(b) (2006 & Supp V. 2011), because those payments were based on, and made on account of, "the entire employer-employee relationship," *Nierotko*, 327 U.S. at 366. The amount of employees' severance payments depended on their level of seniority, length of service with the company, and regular rate of pay. See pp. 3-4, *supra*. All of those factors depend on "the entire employer-employee relationship," and all of them are usual factors associated with determining the level of an employee's compensation. Just as this Court in *Nierotko* rejected the notion that "[a] back pay award differs from other pay," 327 U.S. at 368 (internal quotation marks omitted), the court of appeals should have rejected respondents' argument that a severance payment differs in kind from other types of pay received by employees in return for services rendered to their employers.

2. Nor does it matter that, unlike in *Nierotko*, the severance payments at issue here were made at the conclusion of employees' work for respondents. In *Otte* v. *United States*, 419 U.S. 43 (1974), former employees of a corporation that had declared bankruptcy filed claims with the trustee for unpaid wages. See *id.* at 45. The trustee proposed to pay the claims without withholding federal income and FICA taxes. See *id.* at 46. This Court held that such withholding was necessary. See *id.* at 49-51. The Court observed that the relevant income-tax provisions defined "wages" as remuneration for ser-

vices that an employee "performs or performed." *Id.* at 49. The Court thus reasoned that the statutory language "speaks in the past tense as well as the present and thereby plainly reveals that a continuing employment relationship is not a prerequisite for a payment's qualification as 'wages.'" *Id.* at 49-50. "The situation is the same with respect to FICA withholding," the Court explained, because "the payments clearly are 'wages' under that statute, even though again, at the time of payment, the employment relationship between the bankrupt and the claimant no longer exists." *Id.* at 51; see 26 U.S.C. 3121(b) (2006 & Supp. V 2011) (referring to "service, of whatever nature, *performed*" by an employee) (emphasis added).[3]

3. Since *Nierotko* and *Otte*, the Third and Federal Circuits have held that various types of severance payments made at the conclusion of a worker's employment relationship are "wages" for FICA purposes. See, *e.g.*, *University of Pittsburgh* v. *United States*, 507 F.3d 165, 171-172 (3d Cir. 2007) (early retirement payments to

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[3] The court of appeals' reliance (App., *infra*, 9a) on *Coffy* v. *Republic Steel Corp.*, 447 U.S. 191 (1980), is misplaced. Although *Coffy* involved payments made to laid-off employees, see *id.* at 198-199, the Court did not address whether those payments were "wages" for either FICA or income-tax purposes. Rather, the disputed issue was whether those payments were "perquisites of seniority" to which a returning veteran was entitled under the Vietnam Era Veterans' Readjustment Assistance Act of 1974. See *id.* at 193. In holding that the payments were covered by that statute, the Court emphasized that the payments were "in the nature of a reward for length of service, and do not represent deferred short-term compensation for services actually rendered." *Id.* at 205. *Nierotko* makes clear, however, that payments from an employer to an employee may be FICA "wages" even if they do not compensate the employee "for services actually rendered."

faculty members were "wages" taxable under FICA); *Abrahamsen* v. *United States*, 228 F.3d 1360, 1365 (Fed. Cir. 2000) (same; buyout payments to employees who agreed to resign or retire and release the employer from liability), cert. denied, 532 U.S. 957 (2001). Indeed, the Sixth Circuit itself reached the same conclusion in a similar case. See *Appoloni* v. *United States*, 450 F.3d 185, 191-192 (2006) (severance payments to public school teachers who agreed to resign statutory tenure rights and their teaching positions were "wages" taxable under FICA), cert. denied, 549 U.S. 1165 (2007). The Eighth Circuit has held that early retirement payments to high-level administrators, but not those made to tenured faculty members, were "wages" taxable under FICA, on the theory that the payments to tenured professors were made in exchange for relinquishment of contractual and constitutionally-protected rights, rather than as compensation for services rendered. See *North Dakota State Univ.* v. *United States*, 255 F.3d 599, 600 (2001). None of those courts treated 26 U.S.C. 3402(*o*) as in any way relevant to the determination whether particular payments were FICA "wages."

The Third and Federal Circuits have also recognized that when, as here, the amount of a payment to a departing employee is based on factors like the employee's salary and years of service to the company, those factors indicate that the payment is compensation for past services rendered by the employee. The payment therefore arises from the employer-employee relationship and constitutes "wages" for FICA purposes. See, *e.g.*, *University of Pittsburgh*, 507 F.3d at 172 ("[E]ligibility for the Plans * * * was based on the employee's age and years of service. These requirements link the Plan payments to past services for the employer * * * and

weigh heavily in favor of treating the payments as wages."); *Abrahamsen*, 228 F.3d at 1365 ("[T]he agreements set the amount of the lump-sum cash payments using a formula based on the departing employee's salary and years of service * * * . This formula further associates the payments with the employer-employee relationship."). Again, the Sixth Circuit recognized the same thing in its earlier decision in *Appoloni*. See 450 F.3d at 191 ("[T]he eligibility requirements for qualifying for a payment—that a teacher served a minimum number of years—indicate the payments were for services performed."). Applying that reasoning here would have resulted in a different outcome.

4. Most recently, the Federal Circuit held in *CSX Corp.* that severance payments made in connection with a company's reduction in force are "wages" for purposes of FICA taxation. See 518 F.3d at 1352. In *CSX Corp.*, a group of railroad companies responded to financial difficulties by paying a number of their employees to leave their jobs or reduce their hours. See *id.* at 1330. The Federal Circuit followed the majority of courts of appeals in determining that a severance payment "designed to induce the employee to leave or to cushion the effect of a separation * * * constitute[s] taxable wages and compensation." *Id.* at 1348; see *id.* at 1347-1349. In so concluding, the Federal Circuit rejected the very argument that the Sixth Circuit adopted here: namely, that all severance payments encompassed by Section 3402(*o*)(2)(A)'s definition of "supplemental unemployment compensation benefits" should be considered nonwage payments for FICA purposes. See *id.* at 1341-1345. The decision below thus squarely conflicts with the Federal Circuit's decision in *CSX Corp.*, as the

courts below recognized. See App., *infra*, 20a, 51a-52a. This Court's review is warranted to resolve the conflict.

C. The Question Presented Is Recurring And Exceptionally Important

The proper tax treatment of severance pay under FICA is an issue of exceptional importance. According to the IRS, that question is currently pending in eleven cases and more than 2400 administrative refund claims, with a total amount at stake of more than $1 billion. That figure is expected to grow. In addition, the decision below has significant potential implications outside the tax context with respect to the administration of Social Security and Railroad Retirement Act benefits. A payment's designation as "wages" affects whether employees earn wage credits, which in turn affects the amount of benefits that employees accrue. See 42 U.S.C. 401 *et seq.*; see also 20 C.F.R. 404.1001. In light of the substantial effect that the decision below will have both on the public fisc and on employers and employees in the Sixth Circuit, this Court's review is warranted.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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MAY 2013