Internal Revenue Service
Office of Federal, State and Local Governments

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FSLG Newsletter – January 2013

This is the semiannual newsletter of the office of Federal, State and Local Governments (FSLG) of the Internal Revenue Service. Our mission is to ensure compliance by Federal, state, and local governmental entities with Federal employment and other tax laws through review activities, as well as through educational programs.

For more information, visit our web site at www.irs.gov/govt/fslg. For account-related assistance, contact Customer Account Services at 1-877-829-5500. To identify a local FSLG Specialist, see the directory at the end of this newsletter.

The explanations and examples in this publication reflect the interpretation by the IRS of tax laws, regulations, and court decisions. The articles are intended for general guidance only, and are not intended to provide a specific legal determination with respect to a particular set of circumstances. You may contact the IRS for additional information. You may also want to consult a tax advisor to address your situation.

Federal, State and Local Governments

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FSLG ACCOMPLISHMENTS IN FISCAL YEAR 2012 AND PLANS FOR FISCAL YEAR 2013

FY 2012 was as busy and demanding a year for Federal, State and Local Governments (FSLG) as it was for most of the government entity sector. Budget constraints continue to test federal agencies and state and local government entities alike. FSLG remains committed to providing quality service and, like most government entities, we continue to look at new and alternative means to get the job done.

In FY 2012, we ramped up our outreach efforts to focus more on innovative ways of delivering information to you to help you comply with your tax responsibilities. We achieved this by leaning heavily on less costly types of presentations, such as, webinars and phone forums, and less on face-to-face outreach. Both saved precious travel dollars for your organization and ours and increased the number of participants. This effort included two informative webinars and two nation-wide phone forums, dealing with topics from Section 218 (from the SSA's code) complex transactions to worker classification issues. Each of these events was well attended and received. You can view the recorded events at www.tax.gov.

In FY 2012, we examined over 2,600 tax returns. Issues addressed included worker reclassification, employment taxes on fringe benefits, settlement payments, various international taxes, and information return reporting. In addition to examinations, FSLG conducted 840 compliance checks. Compliance checks continue to play an important enforcement role for FSLG. A compliance check does not examine returns or assess tax, but assesses the level of taxpayer compliance. Typically, a compliance check includes filing compliance related to Forms 941, 944, 945, W-2, and the 1099 series.

We were very happy to hear of your satisfaction with the examination process. Customer satisfaction surveys are sent to all government entities that were examined. While no one likes to be examined, a vast majority of our customers have consistently indicated overall satisfaction with the examination experience. This year the overall satisfaction rating increased from 72% to 75%. At the same time, overall dissatisfaction dropped from 8% to 6%. FSLG continues to incorporate your suggestions into the examination process and will continue to make the examination experience as positive as possible.

In FY2013, FSLG will continue to maintain an effective balance between traditional compliance work and educational activities.

FSLG's FY 2013 outreach program will include teleconferences, webinars, and phone forums; and will target larger events to make the most efficient use of resources. FSLG will continue to conduct outreach with various stakeholder groups which will focus on the Service-wide implementation of the Affordable

Care Act (ACA) provisions, international tax compliance, and traditional employment tax and information reporting issues.

FSLG continues its partnership with the National Conference of State Social Security Administrators (NCSSSA) and the Social Security Administration to assess Section 218 Agreement coverage in each state and to address this issue using a unified approach. FSLG is working cooperatively with these organizations to assess the Section 218 framework of each state to identify commonalities, differences and problem areas in an effort to improve our outreach and service delivery. In addition, it continues to collaborate with SSA in addressing important legal questions and identifying opportunities for improvement related to Section 218 compliance.

In FY 2013, FSLG expects a reduction in compliance checks and examinations due to reduced staffing and modifications to the types of examinations conducted. FSLG will devote significant resources to complete examinations selected for the Service wide Employment Tax National Research Program (ET-NRP). ET-NRP is an examination project designed to develop data to identify and quantify the tax gap related to employment taxes. It will increase the number of examinations with potential international tax issues, the number of large entity examinations, and will continue to conduct examinations in all market segments. FSLG expects to address a greater volume of claims for refund primarily related to Section 218 Agreement coverage issues. FSLG will use “soft letter” campaigns when warranted to address small, targeted non-compliance issues and encourage self-correction. FSLG will continue to support the Service-wide Voluntary Classification Settlement Program.

FORM 8300 REQUIREMENTS FOR GOVERNMENT ENTITIES

Clerks of federal or state courts who receive more than $10,000 in cash as bail for an individual charged with certain state or federal crimes involving a controlled substance, racketeering, or money laundering must file, for each transaction, Form 8300, Report of Cash Payments Over $10,000 Received in a Trade or Business, within 15 days to the IRS. These clerks must furnish a copy of the filed Form 8300 or a written statement with the same information to the U.S. Attorney for the jurisdiction(s) in which the individual resides and in which the crime occurred. A clerk is the clerk’s office or the office, department, division, branch, or unit of the court that is authorized to receive the bail.

Cash, for this purpose, consists of coins and currency of the United States or a foreign country. Cash could also include cashier’s checks, bank drafts, traveler’s checks or money orders with a face value of $10,000 or less. Cash does not include personal checks drawn on the payer’s own account, regardless of the amount. It also does not include cashier's checks, bank drafts, traveler's checks, or money orders with a face value of $10,000 or more; these items would have been reported by the financial institution that issued them.

Generally, you must file Form 8300 if you receive more than $10,000 in cash from one individual as a result of one transaction. If multiple cash payments are made to satisfy bail and the initial payment does not exceed $10,000, all bail payments for the same individual charged with the applicable offense must be aggregated and you must file a Form 8300 when the aggregate bail payments exceed $10,000. This does not apply if payments are for separate bail requirements.

There are potential civil penalties for failure to file Form 8300 and failure to furnish a statement to the individual identified on the Form 8300. The penalty is $100 for failure to file and $100 for failure to furnish a statement to the payer.

If required, Form 8300 is due by the 15th day after the cash bail is received. Form 8300 should be filed by mailing the forms to the IRS at Detroit Computing Center, P.O. Box 32621, Detroit, MI 48232. A copy (or comparable statement) should be furnished to the U.S. Attorney(s). A statement is also required to be furnished to each payer of bail named on the Form 8300 by January 31 of the year following the transaction. The statement must include the name and address of the clerk's office, amount of cash that was reported to the IRS, and notification that the cash transaction was reported to the IRS and applicable U.S. Attorneys. The clerk's office must retain a copy of the Form 8300 for five years from the date of filing.

It is important to file all required Forms 8300. The information obtained from the form is used by the Internal Revenue Service and the Financial Crimes Enforcement Network (FinCen) to combat money laundering, which in turn helps authorities to stop tax evasion, drug dealing, terrorist financing and other criminal activities.

For additional information, see Form 8300, and Publication 1544, Reporting Cash Payments of Over $10,000 (Received in a Trade or Business). Information is also available at the Financial Crimes Enforcement Network (FinCen) website at www.fincen.gov/forms/bsa_forms/.

EXCLUSION OF WORK-RELATED DISABILITY BENEFITS UNDER IRC SECTION 104

State and local governments that provide work-related disability benefits for their employees need to be aware of the criteria for excluding such payments from income under section 104 of the Internal Revenue Code, to ensure proper reporting on Form 1099-R.

Generally, an individual’s gross income includes all income from whatever source derived, including compensation for services. However, Code section 104 and its regulations exclude from gross income amounts received by an employee under a workmen's compensation act or under a statute in the nature of a workmen's compensation act that provides compensation to the employee for personal injury or sickness incurred in the course of employment. For payments to be treated as being “under a statute in the nature of a workmen’s compensation act,” three criteria must be satisfied:

1. The right to the benefit must be established by statute. Any state, county or municipal law may be treated as a statute. However, a union contract is not a statute.

2. The benefit must be for disability due to personal injuries or sickness incurred in the course of employment. If the benefit is available to any disabled employee, without regard to whether the disability was incurred on or off the job, it is not in the nature of workmen’s compensation and is not excludable. In some circumstances, it may be presumed that a particular illness is job related, but the presumption must be rebuttable based on evidence.

3. The benefit must not be determined by reference to the employee's age, length of service, or prior contributions. If the amount of a benefit is determined partly by reference to age, service or prior contributes, and partly independent of those factors, the independent part is excludable under section 104, and the balance is not.

The following examples illustrate the application of these rules:

Example 1: A state statute provides a retirement benefit for any employee who is permanently and completely disabled, in an amount equal to the greater of 1) 66.6% of the employee’s final compensation, or 2) the employee’s vested retirement benefit based on age and years of service. Result: No part of this benefit is excludable under section 104, because it is not limited to disability due to on-the-job injury or illness.

Example 2: The facts are the same facts as Example 1, except that the benefit is only for disability due to on-the-job injury or illness. Result: The benefit is excludable under section 104, up to 66.6% of final compensation. Any benefit in excess of 66.6% is determined by reference to the employee’s age and service, and therefore includible in gross income under Code section 72.

Example 3: The facts are the same facts as in Example 2, except that the benefit is ½ the employee’s final compensation plus the actuarial equivalent of the employee’s contributions to the retirement plan. Result: The benefit is excludable under section 104, up to ½ the employee’s final compensation. Any amount in excess of ½ final compensation is determined with reference to the employee's prior contributions, and is includible in gross income under section 72.

Example 4: A city ordinance provides that if a police officer or firefighter who has been employed by the city for five consecutive years develops tuberculosis, it shall be conclusively presumed that the tuberculosis is job related, and the employee shall be allowed to retire with a benefit of 100% of final compensation. Result: Because the presumption that the tuberculosis is job related is not rebuttable, the benefit would cover non-job related illness and is not in the nature of workmen's compensation. Therefore the benefit is not excludable under section 104.

Example 5: The facts are the same facts as in Example 4, except that the presumption that the tuberculosis is job related is rebuttable based on evidence, and an appropriate authority must find that the illness is job related. Result: The benefit is fully excludable under section 104.

Example 6: The facts are the same as in Example 5, except that the ordinance also provides that if and when the disabled retiree dies, the surviving spouse shall continue to receive a benefit equal to ½ the benefit payable to the retiree. Result: The benefit payable to the surviving spouse is fully excludable under section 104.

PROPOSED REGULATIONS ISSUED ON ADDITIONAL MEDICARE TAX

A new Additional Medicare Tax goes into effect starting in 2013. The 0.9 percent Additional Medicare Tax applies to an individual's wages, Railroad Retirement Tax Act compensation, and self-employment income that exceeds a threshold amount based on the individual's filing status.

The threshold amounts are:

- $250,000 for married taxpayers who file jointly,
- $125,000 for married taxpayers who file separately, and
- $200,000 for all other taxpayers.

An employer is responsible for withholding the Additional Medicare Tax from wages or compensation it pays to an employee in excess of $200,000 in a calendar year.

The IRS and the Treasury Department have issued proposed regulations on the Additional Medicare Tax. Comments may be submitted electronically, by mail or hand delivered to the IRS.

For additional information on the Additional Medicare Tax, see our questions and answers.

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