



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, DC 20224

January 15, 2002

OFFICE OF
CHIEF COUNSEL

Number: **200227003**
Release Date: 7/5/2002
UIL: 61.00-00

PRENO-144975-01
CC:ITA:B4

MEMORANDUM FOR MAUREEN O'BRIEN
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FROM: Heather C. Maloy
Associate Chief Counsel
(Income Tax & Accounting)

SUBJECT: Senior Citizens Tax Abatement Program

You have asked us whether citizens over the age of 60 ("senior citizens") who, pursuant to a program authorized by Massachusetts law, receive property tax abatements of up to \$500 for performing certain volunteer services for participating municipalities may exclude the abatements from gross income. On April 5, 2001, Massachusetts State Senator Richard Moore wrote a letter (copy attached) to the IRS Taxpayer Advocate in Boston asking why the abatements could not be considered tax-exempt. We have examined the underlying statute and two CCAs issued by CC:TEGE. We conclude that payments under the program are includible in the gross income of the recipients.

Overview of Massachusetts Program. Under Massachusetts law cities and towns may establish a program (the "Program") allowing senior citizens "to volunteer to provide services to such city or town. In exchange for such volunteer services the city or town shall reduce the property tax obligations" of those senior citizens.¹ The maximum abatement under the program is \$500 for any tax year, which is credited at a rate of not more than the Massachusetts minimum wage. Participating cities and towns must keep, and furnish to each participating senior citizen, a record of his or her hours of service and the amount of the property tax reduction. The state law also provides that the amount by which property tax "is reduced in exchange for the provision of services" are not income, wages, or employment for state taxation, withholding, unemployment insurance, or workers' compensation purposes. However, the senior citizens are public employees for purposes of municipal tort liability.

State law permits participating cities and towns to create local rules to implement the Program consistent with the intent of the statute. The Massachusetts Department of Revenue has advised cities and towns that they should adopt rules to determine, *inter alia*, any income limitations on eligibility.

¹Mass. Ann. Laws ch. 59 § 5K (Law. Co-op 1990).

More than 50 Massachusetts cities and towns have adopted the program.² Some towns have limited participation in the program to senior citizens whose income does not exceed certain amounts, as determined by the town.³ Newspaper articles and town websites indicate that towns permit as few as five and as many as 70 senior citizens to participate in the Program annually.

Prior Chief Counsel Advice. On April 24, 2000, CC:TEGE issued a CCA to an IRS office in Massachusetts, basically concluding that a senior citizen must include in income and wages for Federal Insurance Contributions Act (FICA) purposes (i) the \$500 tax abatement and (ii) the employee portion of the FICA tax, if paid by the town and not reimbursed by the senior citizen.⁴ The IRS local office included these conclusions in its April 24, 2000, letter to the Massachusetts Department of Revenue.

On July 10, 2001, CC:TEGE issued a CCA to SB/SE Area Counsel reaffirming its prior guidance.⁵ The rationale for concluding the abatement is income is that it is compensation for services. The conclusion that a town's payment of the employee portion of the FICA tax is also income and wages is based on the principle that payment by an employer of the income taxes assessable against an employee constitutes additional income taxable to the employee. *Old Colony Trust Co. v. Commissioner*, 279 U.S. 716 (1929); Rev. Rul. 86-14, 1986-1 C.B. 304.

Based on the CCAs, participating senior citizens have gross income of \$541.41 and participating towns would pay \$82.82 in FICA taxes for each participant (if the town pays the employee portion of the FICA).⁶ Sen. Moore's principal objection is to the

²David Bushnell, *Seniors Willing to Work for Towns Can Earn \$500 Rebate on Taxes*, Boston Globe, February 18, 2001 at 9. The Boulder, Colorado County Government website states that local governments in California, Colorado, Minnesota, New York, and Virginia also have similar programs.

³Each town may adopt its own limits. For example, Hull's income limit is \$15, 500 (\$18,500 if married, Dedham's is \$30,000 (\$40,000 if married), and Natick's is \$40,000. Wilmington requires participants to have limited financial resources. Uxbridge, however, proposes to impose income limits only if it has more than a certain number of applicants.

⁴CCA 2000-25-030 (publicly released on June 23, 2000).

⁵CCA 2001-32-025 (publicly released on August 1, 2001). In both CCAs, CC:TEGE did not have enough facts to conclude that the senior citizens were employees, but inferred from the facts it was likely they were employees.

⁶Because \$500 of the earnings is credited to a senior citizen's property tax bill, the \$500 credit is deductible under § 164 even though state law treats it as an abatement or reduction in tax. See *Consolidated Edison Co. of New York Inc. v. United States*, 93-2 U.S.T.C. ¶ 50,644 (2d Cir. 1993) (discounted prepayment of property taxes yields income in the amount of the discount, with a § 164 deduction equaling the cash prepayment plus the discount income).

conclusion regarding FICA taxes because towns are not willing to both pay FICA taxes and lose property tax revenues.

Discussion. CC:ITA concurs with CC:TEGE that the \$500 tax abatements and a town's payment of a senior citizen's share of the FICA tax are income subject to federal income tax. We have examined potentially applicable exclusions, but none applies. For example, there is no gift under § 102 because there is a *quid pro quo*.⁷ Likewise, the exclusions from income under § 108 do not apply because the real property tax debt is not discharged; it is fully paid in kind with the income senior citizens receive from the services they provide. As discussed below, we also believe that the general welfare exception does not apply.

Absent needs-based criteria, it is clear that the general welfare exception does not apply. In situations not involving a natural disaster or catastrophe, the exception has generally been limited to payments by governmental entities to individuals experiencing economic need (usually tested by income level). The IRS' position is that governmental payments made to individuals simply because they are elderly are not needs based. Specifically, Rev. Rul. 76-131, 1976-1 C.B. 16 holds that payments made by the state of Alaska to individuals at least 65 years of age who have maintained an Alaska domicile for at least 25 years under a program to continue their residence in the state did not qualify under the general welfare exception because the payments were made regardless of financial status, health, educational background, or employment status.⁸ In contrast, Rev. Rul. 78-170, 1978-1 C.B. 24, concludes that the exception applies to an Ohio program that helped senior citizens reduce their winter energy costs. Under that program, however, the total annual income of recipients could not exceed \$7,000.

We are equally convinced that the general welfare exception does not apply to tax abatements made by localities that limit participation to senior citizens with lower income. Payments do not qualify under the general welfare exception if they are made for services rendered. Rev. Rul. 72-340, 1972-2 C.B. 31. Rev. Rul. 71-425, 1971-2 C.B. 70, and Notice 99-3, 1999-1 C.B. 271, provide examples of situations in which the IRS has applied the general welfare exception to certain governmental welfare payments, even though the recipient had to perform work activities to receive the payments. However, the payments in those situations were subsistence payments (*i.e.*, welfare) received directly from a state or local welfare agency, the amount of which were determined under the applicable welfare law, and based on need of the recipient and his family.

⁷*Porten v. Commissioner*, T.C. Memo. 1993-73

⁸Based on the rationale of the revenue ruling, we do not believe that the fact that the Alaska statute explicitly stated that the payments were not considered a form of public relief and that the payments were not based on need distinguishes the Massachusetts statute.

The Massachusetts program is clearly distinguishable. Services performed by the senior citizens partially satisfy their property tax liabilities. By rendering these services they are working off (*i.e.*, earning income to pay) their property taxes. We have not issued published guidance concluding that governmental payments made in such circumstances are not for services rendered so as to qualify under the general welfare exception. Further the abatements under the Program are distinguishable from the payments in Rev. Rul. 71-425 and Notice 99-3 because the abatements are not characterized as welfare, received directly from a state or local welfare agency, or a substitute for a welfare-type payment. Further, the amount of the payment is not determined by the applicable welfare law.

Moreover, the language of enabling legislation also indicates that abatements are consideration for services rendered. Thus, the statute states “In **exchange** for such volunteer services, the city or town shall reduce the real property tax obligation of such person” and “the amount of the property tax obligation that is reduced in **exchange** for the provision of services” is not income for certain purposes. [Emphases added]. We also note that town websites and newspaper articles generally describe the Program as a “tax **work-off** abatement or program.” That the workers are called “volunteers” is not determinative, as the tax forgiveness is clearly provided in consideration for work done. In addition, it appears that at least some towns clearly intend to derive a substantial benefit from the services performed by the senior citizens. For example, one town requires qualified applicants to be interviewed by the department head upon referral, another requires participants to “have needed job skills,” and a third will attempt to match the skills and interests of applicants to the needs of the town.⁹ Thus, the Program, by providing a part-time or temporary workforce to a participating town, is similar to the state program in Rev. Rul. 74-413, 1974-2 C.B. 333, which provided unemployed persons with short-term employment in disaster relief activities. The ruling holds that the payments are compensation for services rendered and, therefore, includible in the participants’ gross income.

If you have any questions, please call Sheldon Iskow of CC:ITA:4 at (202) 622-4920.

⁹Sen. Moore’s letter acknowledges that the state law has the dual purposes “to assist elderly taxpayers with the increasing burden of taxation and to provide some additional help to town departments.”