



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

OFFICE OF
CHIEF COUNSEL

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Dear 

This is in response to your request for general information regarding the taxation of supplemental payments. As we understand the facts you have provided, the supplemental payments consist of thirteen weeks vacation pay provided to retired union employees pursuant to a negotiated labor agreement. The supplemental payments were paid from the employer's general assets and were not paid from pension funds nor were any funds previously set aside for this purpose.

As a general matter, apart from the procedure for issuing a formal opinion, as described in Revenue Procedure 2004-1, 2004-1 I.R.B. 1, the Internal Revenue Service is not able to provide binding legal advice applicable to particular taxpayers. In the absence of a request for formal guidance, we are only able to provide general information. Accordingly, in response to your request, we have reviewed the facts provided to us and set forth below general information, which we hope will be helpful to you.

Under Subtitle C of the Internal Revenue Code (the Code), Chapters 21, 23 and 24, respectively, employment taxes consist of the Federal Insurance Contributions Act tax (FICA), the Federal Unemployment Tax Act tax (FUTA), and the Collection of Income Tax at Source on Wages (income tax withholding). Employment taxes are imposed on wages paid with respect to employment. Code section 3401(a) provides that "wages" for income tax withholding purposes means all remuneration for services performed by an employee for his employer. Code section 3121(a) defines the term "wages" for FICA purposes as all remuneration for employment, with certain exceptions. Section 3121(b) defines "employment" as any service, of whatever nature, performed by an employee for the person employing him, with certain specific exceptions. Although there are

differences in the statutory exceptions to what constitutes wages and employment, the general definitions of the terms wages and employment for FUTA purposes are similar to the definitions for FICA purposes. See Code section 3306(b), (c).

The Code allows employers to maintain various types of “qualified” retirement plans. An employer’s plan must meet specific requirements under the Code to be recognized as a qualified plan. To encourage employers to adopt qualified plans, Congress also provided for numerous tax advantages that apply only to qualified plans. One of these tax advantages is that contributions to and benefits paid from qualified plans are generally excepted from FICA and FUTA taxes. Section 3121(a)(5)(A) of the Code, which applies to qualified pension plans, provides an exception from wages for any employer payment made to, or on behalf of, an employee or his beneficiary “from or to a trust described in section 401(a) which is exempt from tax under section 501(a) at the time of such payment.” Similarly, Code section 3306(b)(5)(A) provides that wages does not include remuneration paid from a “trust described in section 401(a).” However, payments from a trust described in section 401(a) are includable in income. Code section 3405 provides special rules for income tax withholding with respect to such payments.

Payments from an employer to an employee that are not paid from a qualified retirement plan are generally considered to be wages subject to employment taxes, unless some specific exception applies. Moreover, remuneration for employment, unless specifically excepted, constitutes “wages” subject to employment taxes even though at the time paid the relationship of employer and employee no longer exists between the person in whose employ the services were performed and the individual who performed them. See Employment Tax Regulations section 31.3121(a)-1(i); 31.3306(b)-1(i); and 31.3401(a)-1(a)(5).

If you have any questions regarding this matter please contact [REDACTED] (Employee Identification [REDACTED]) of my staff [REDACTED] can be reached at [REDACTED]

Sincerely,

Lynne Camillo, Branch Chief
CC:TEGE:EOEG:ET2
Tax Exempt and Government Entities