



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

OFFICE OF
CHIEF COUNSEL

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The Honorable Tim Johnson
United States Senator
405 East Omaha Street, Suite B
Rapid City, SD 57701

Attention:

Dear Senator Johnson:

I am responding to your inquiry dated December 17, 2010, on behalf of your constituent, _____ is a widow of a former employee of _____. Upon his death, _____ former employer paid _____ a lump sum and transmitted a payment to the IRS to cover any federal taxes due on the lump sum (a tax gross-up). _____ has learned that she must include in her gross income the lump sum and tax gross-up payments. _____ believes that the law should consider these payments as a form of life insurance payments and therefore excluded from gross income.

Gross income does not include amounts received under a life insurance contract, if the amounts are paid by reason of the death of the insured (section 101(a) of the Internal Revenue Code) (Code). Because the payments to and on behalf of _____ were not made pursuant to a life insurance contract, she must include them in gross income in the year of receipt.

Formerly, the Code excluded from the gross income of beneficiaries certain death benefits not exceeding \$5,000 if paid by or on behalf of an employer and by reason of the death of the employee (former section 101(b) of the Code). In 1996, however, Congress repealed this exclusion effective for decedents dying after August 20, 1996. The IRS must apply the law as enacted by Congress. Only Congress can change the tax treatment of payments made to beneficiaries by reason of the death of an employee or former employee.

I hope this information is helpful. If you have any additional questions, please contact me or _____, Identification Number _____ at _____.

Sincerely,

Michael J. Montemurro
Chief, Branch 4
Office of Associate Chief Counsel
(Income Tax and Accounting)