



One Minute Memo[®]

Some Severance Held Exempt from FICA Again

Consider Filing Protective Refund Claims

A Federal District Court in Michigan, in a case involving the bankruptcy of the Quality Stores discount chain, has held that some types of severance pay are exempt from social security taxation under the Federal Insurance Contributions Act (FICA), and that the employer was entitled to a refund of FICA tax that it had previously paid on the severance. While the decision is certain to be appealed by the IRS, employers who have made significant severance payments in open tax years (generally 2006 or later) may want to consider filing protective claims for refund of FICA payments until the matter is resolved.

Claims for refund of FICA paid in 2006 generally must be filed no later than April 15, 2010.

The *Quality Stores* decision may seem to many employers like a case of *déjà vu*. Eight years ago, the Court of Federal Claims reached the same conclusion in a case involving severance paid by CSX Corporation, and many employers filed refund claims based on the CSX case. The IRS placed a hold on processing CSX refund claims and eventually succeeded in having the CSX decision reversed on appeal.

The same thing may happen with the *Quality Stores* decision. However, *Quality Stores* will be appealed to a different Circuit Court of Appeals than the court that reversed CSX. If the *Quality Stores* decision is upheld on appeal, it will cause a split in authority between the Courts of Appeals, which could lead to a resolution by the Supreme Court, or by Congress. In the meantime, simply filing a refund claim may be relatively inexpensive, and would protect the possibility of a large tax recovery if *Quality Stores* is upheld. This is particularly true for employers who have paid substantial severance in connection with reductions in force (RIFs).

Claims for refund of FICA generally must be filed no later than April 15 of the third year following the year in which the FICA is paid, which means that employers have until April 15, 2010, to file claims for a refund of FICA paid in 2006. Not all severance is potentially eligible for the FICA exemption under *Quality Stores*. The decision applies only to severance paid under a plan that covers involuntary terminations resulting from a RIF, plant closing, or similar conditions.

If you have any questions regarding the FICA exemption, please contact the Seyfarth Shaw attorney with whom you normally work or any [Employee Benefits attorney](#) on our website.

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