



## Key Takeaways from *United States v. Quality Stores, Inc.*

On March 25, 2014, the US Supreme Court ruled in favor of the IRS in *United States v. Quality Stores, Inc.* holding that severance payments are taxable as FICA wages. The Supreme Court's ruling also prevents taxpayers from receiving FICA refund claims.

However, severance paid as Supplemental Unemployment Benefits ("SUB-Pay") to involuntarily laid-off employees that is linked to the receipt of state unemployment insurance ("UI") benefits and not paid in a lump sum is FICA exempt.

### OVERVIEW

- The Court unanimously rejected a \$1 million refund bid by defunct agricultural specialty retailer Quality Stores, and said severance payments the company made to 3,100 people were subject to FICA tax;
- The case had broad implications on whether employers continue to provide SUB-Pay benefits, which are linked to the receipt of state UI benefits which, pursuant to the IRS's administrative position going back to the 1950s, is not subject to FICA or FUTA taxes;
- In addition, more than \$1 billion in FICA tax protective refund claims filed by employers across the country will not be paid;
- Under the Court's ruling SUB-Pay Plans will remain valid.

### KEY EMPLOYER TAKEAWAYS

- In light of the Court's ruling, the only way to get a guaranteed FICA tax savings is to have a SUB-Pay Plan that is compliant with IRS rulings;
- Companies that implement a SUB-Pay Plan can supplement the receipt of their former employee's amount of state UI benefits thereby reducing their severance costs by as much as 45% (or more);
- SUB-Pay benefits are exempt from employer FICA, FUTA and SUTA taxes and employee FICA taxes;
- As with severance plans, once a SUB-Pay Plan is established it can continue to be used indefinitely for any involuntary staff reductions;
- SUB-Pay Plans are complex in nature, but TMS is an expert in developing and administering such plans for Fortune 1000 companies, and can streamline the process for you -- from plan design and approval, to implementation and ongoing administration.

### SUMMARY OF SUB-PAY BENEFITS

#### ***Benefits to the Employer:***

- Saves a minimum of 7.65% in severance costs from FICA tax savings or up to 45% when state UI benefits are coordinated with separation pay;
- Payments are exempt from both FUTA and SUTA taxes;
- Plans are customized based upon the specific financial and cultural objectives of each employer;
- Reduces the administrative burden and costs when the company outsources the communication, support and assistance to the laid-off worker to a third-party administrator for the duration of their plan;
- The company can outsource the laid-off worker's support and assistance to a third-party administrator for the duration of their plan.



**Benefits to the Employee:**

- Provides 7.65% more separation pay because SUB-Pay is not subject to FICA tax;
- SUB-Pay Plans are paid on a periodic basis which provides the former employee with steady income during their reemployment transition and may reduce the additional tax burden associated with lump-sum severance payments;
- A dedicated SUB-Pay Plan partner provides laid-off workers with a ready resource to help them during their transition period including individual call center assistance plus, IVR and web support services;
- Provides laid off workers with an "advocate" to help them with state UI benefit claim opening or issues that may come up.