



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224
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OFFICE OF
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INTERNAL REVENUE SERVICE NATIONAL OFFICE FIELD SERVICE ADVICE

MEMORANDUM FOR LINDA R. DETTERY
AREA COUNSEL SB/SE:AREA1

FROM: Jerry E.Holmes
Chief, Employment Tax Branch 2
CC:TEGE:EOEG:ET2

SUBJECT: Senior Citizen Property Tax Abatement Program

This Chief Counsel Advice responds to your memorandum dated June 15, 2001. In accordance with I.R.C. § 6110(k)(3), this Chief Counsel Advice should not be cited as precedent.

LEGEND

Date 1 = [REDACTED]
State = [REDACTED]
Program = [REDACTED]
Date 2 = [REDACTED]
Age A = [REDACTED]
X Dollars = [REDACTED]
Y Dollars = [REDACTED]
Date 3 = [REDACTED]

ISSUE

Whether an abatement in real estate taxes of up to X Dollars per year, in exchange for services rendered by senior citizens pursuant to a State program which exempts such abatements from state tax, constitutes income for federal income tax purposes and wages for Federal employment tax purposes.¹

¹The question presented in the Request for Field Service Advice is phrased in terms of whether such remuneration is considered "barter income." Since, as discussed below, the abatement in property taxes constitutes wages, a discussion of "barter income" would be inapposite.

CONCLUSIONS

The property tax abatements earned under the property tax work-off program are income subject to federal income tax. Since the maximum amount of compensation under the program is less than one withholding exemption, in most circumstances, the employer will not be required to withhold income tax.

Property tax abatements earned under the program constitute wages subject to FICA tax. The amount of wages paid is equal to the amount of the property tax liability forgiven. If the employer pays the workers' portion of FICA tax and does not seek reimbursement, the employees will receive additional income subject to FICA tax in the amount of the employees' FICA tax liability paid by the employer. There is an information reporting requirement applicable to all wages subject to FICA. FUTA taxes are not applicable.

FACTS

On Date 1, the State amended its laws to add a provision known as the Program which became effective as of Date 2. Under this law, cities and towns in the State are permitted to establish property tax write off programs wherein participating taxpayers, who must be over Age A, "volunteer" services to municipalities in exchange for a reduction in their property tax obligations. The State law permits seniors to earn up to a maximum of X Dollars in property tax reduction per fiscal year. The maximum amount of credit per hour that the taxpayers are entitled to receive for their services is capped by the State's minimum wage law, Y Dollars per hour, effective Date 3. The property tax reductions are accounted for as abatements. The abatements under the work-off program are in addition to any other property tax exemptions that may be available under State law. Under State law, the property tax abatements earned for services under the work-off program are not considered income for purposes of State taxation, withholding, unemployment insurance or workers' compensation. However, persons providing service under the program are considered public employees for purposes of municipal tort liability.

LAW

A. Income Tax

Section 61(a) of the Code defines gross income as all income from whatever source derived, including compensation for services.

Section 1.61-1(a) of the Income Tax Regulations states that: "Gross income includes income realized in any form, whether in money, property, or services. Income may be realized, therefore, in the form of services, meals, accommodations, stock, or other property, as well as in cash."

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).

Employer payment of an employee's FICA tax liability under Code section 3101, without deducting the payment from the employee's pay or otherwise receiving reimbursement from the employee, constitutes additional income to the employee for federal income tax purposes. Rev. Rul. 86-14, 1986-1 C.B. 304.

Section 31.3401(a)-1(b)(6) of the Employment Tax Regulations states that the term "wages," for purposes of income tax withholding, includes any amount paid by an employer in satisfaction of the employee's FICA tax liability imposed by section 3101 of the Code, without deduction from the remuneration of, or other reimbursement from, the employee.

B. Employment Tax

Taxes under the Federal Insurance Contributions Act (FICA) consist of an old-age, survivors, and disability insurance (OASDI) portion and a hospital insurance (Medicare) portion. FICA taxes are computed as a percentage of "wages" paid by the employer and received by the employee with respect to "employment." In general, all payments of remuneration by an employer for services performed by an employee are subject to FICA taxes, unless the payments are specifically excepted from the term "wages" or the services are specifically excepted from the term "employment."

Section 3121(b)(7) of the Code generally excludes from "employment" services performed in the employ of any State, or any political subdivision thereof, or any wholly-owned instrumentality of any one or more of the foregoing, unless an agreement under Section 218 of the Social Security Act (section 218 agreement) is in effect.

Section 3121(b)(7)(F) limits the exclusion contained in section 3121(b)(7) of the Code to include within the definition of employment services performed in the employ of any State, or any political subdivision thereof, or any wholly-owned instrumentality of any one or more of the foregoing, by an individual who is not a member of a retirement system of such state, political subdivision or instrumentality.²

²There are five exceptions set forth in section 3121(b)(7)(F) which make applicable the general exclusion contained in section 3121(b)(7) to services performed by individuals who are not members of a State sponsored retirement plan. Examples of such services include services performed by an individual to relieve that individual of unemployment, by an inmate or patient of a hospital or home, certain emergency

The term “wages” is defined in section 3121(a) of the Code as “remuneration from employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash,” with certain exceptions.

Section 31.3121(a)-1(c) of the Employment Tax Regulations states: “The name by which the remuneration for employment is designated is immaterial. Thus, salaries, fees, bonuses and commissions on sales or on insurance premiums, are wages if paid as compensation for employment.”

Section 31.3121(a)-1(d) of the Employment Tax Regulations states: “Generally the basis upon which the remuneration is paid is immaterial in determining whether the remuneration constitutes wages. Thus, it may be paid on the basis of piecework, or a percentage of profits; and it may be paid hourly, daily, weekly, monthly or annually.”

Section 31.3121(a)-1(e) of the Employment Tax Regulations states: “Generally the medium in which the remuneration is paid is also immaterial. It may be paid in cash or something other than cash as for example goods, lodging, food or clothing. Remuneration paid in items other than cash shall be computed on the basis of the fair market value of such items at the time of payment.”

Under section 3121(a)(6) of the Code, the term “wages” does not include the payment by the employer of the employee portion of FICA imposed by section 3101 in the case of domestic services provided in the private home of the employer or for agricultural labor. However, subject to that exception, if an employer pays the employee portion of the FICA tax on behalf of an employee, that amount is considered as additional wages for FICA purposes. See Rev. Rul.86-14, 1986-1 C.B. 304. Revenue Procedure 81-48, 1981-2 C.B. 623, provides the formula used for calculating the additional amount of wages resulting from an employer’s payment of the employee’s FICA tax obligation.³

Section 6051(a) of the Code requires information reporting from every person required to deduct and withhold the employee portion of the FICA tax from an employee. The requirement applies to all payments subject to FICA tax, regardless of the amount. The information is reported on Form W-2.

services, services performed by an elected official or solely on the basis of fees.

³For taxes paid prior to January 1, 1981, an employer’s payment of the employee’s portion of FICA tax was excluded from the employee’s wages for FICA purposes. Former section 3121(a)(6)(A). This provision was amended by section 1141 of the Omnibus Budget Reconciliation Act of 1980, Pub. L. 96-499, 1980-2 C.B. 509, to provide an exclusion from wages for payment only for domestic service and agricultural labor. Given this amendment, an employer’s payment of employee FICA tax liability constitutes additional wages absent a specific exclusion.

Code section 3306(c)(7) provides that taxes under the Federal Unemployment Tax Act (FUTA) do not apply to compensation for services in the employ of a state, any political subdivision thereof, or any instrumentality of any one or more of the foregoing which is wholly owned by one or more states or political subdivisions.

ANALYSIS

Although under the State statute the abatements are not considered “income” for tax purposes, the state law treatment of the amounts in question is not determinative of the federal tax treatment. While state law governs the nature of legal interests and rights created under state law, “the federal tax consequences pertaining to such interests and rights are solely a matter of federal law.” Forest v. Commissioner, 97-1 U.S.T.C. (CCH) P50, 118 (1st Cir. 1996), aff’g T.C. Memo. 1995-377. See also, Delancy v. Commissioner, 99 F.3d 30 (1st Cir. 1996); Brabson v. U.S., 73 F.3d 1040 (10th Cir. 1996). Similarly, the fact that the workers are called “volunteers” is not determinative, as the tax forgiveness is provided in consideration for work done.

The abatements in property tax described above in exchange for services constitute income under section 61 of the Code. The amount of income is equal to the amount of the property tax abatement. If the municipality pays the employee’s FICA tax obligation imposed under section 3101 of the Code without receiving reimbursement from the employee, the amount of that payment will constitute additional income to the employee under section 61. Rev. Rul. 86-14, 1986-1 C.B. 304. Although section 3402(a) of the Code requires employers to deduct and withhold income tax, the maximum amount of remuneration permitted under the program is less than one withholding exemption. Accordingly, in most circumstances, the municipalities will not be required to withhold income tax from participants in the program. The municipalities, however, should require the employees to complete Forms W-4. The municipalities are also required to file Forms W-2, reporting all wages.

The services performed by the taxpayers for a municipality under the work-off program will constitute “employment” as defined in section 3121(b) of the Code unless the taxpayers are participants in a state sponsored retirement plan as defined in section 3121(b)(7)(F).⁴ The property tax abatement will constitute wages under section 3121(a). If the employer pays the taxpayer’s portion of FICA taxes imposed under section 3101 without reimbursement, the taxpayer will receive

⁴If the taxpayer is not a participant in a state sponsored retirement plan, the services provided for the municipality may still fall outside of the definition of employment if the services fall within one of the five categories listed in section 3121(b)(7). However, even if the services performed fall outside of the definition of employment due to the operation of Code section 3121(b)(7), the hospital insurance portion of the FICA tax may be applicable pursuant to section 3121(u) of the Code.

additional wages in the amount of that payment. Although we do not have enough facts to support an analysis of the issue, it appears as though the part-time, minimum wage workers hired to work off their property tax will be considered employees as defined in section 3121(d) of the Code.

Based on the foregoing, the employment tax consequences of receiving property tax abatements in exchange for services under the work-off program are as follows. Since the workers in question are most likely employees, the amounts that they earn under the program will be subject to FICA tax. The amount of wages will be equal to the value of the property tax liability forgiven. Since the workers will receive no cash remuneration, the Employer will be required to pay both portions of the FICA tax. If the employer does not seek reimbursement from the employee for the employee's portion of FICA tax, that portion will be wages for FICA tax purposes subject to additional FICA tax. There is an information reporting requirement applicable to all wages subject to FICA. FUTA taxes are not applicable.

This writing may contain privileged information. Any unauthorized disclosure of this writing may have an adverse effect on privileges, such as the attorney client privilege. If disclosure becomes necessary, please contact this office for our views.

Please call if you have any further questions.

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Office of the Assistant Chief Counsel
(Exempt Organizations/Employment
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