Internal Revenue Service

Number: **200626036**
Release Date: 6/30/2006
Index Number: 3101.00-00, 3111.00-00, 3402.00-00, 6051.00-00, 61.30-00

Department of the Treasury
Washington, DC 20224

[Third Party Communication:
Date of Communication: Month DD, YYYY]

Person To Contact:
, ID No.
Telephone Number:

Refer Reply To:
CC:ITA:B04
PLR-158822-05
Date:
March 07, 2006

Legend:

State =

Statute =

Program =

$Z = $

Dear :

This letter is in response to your request for a ruling dated November 8, 2005, regarding State's information reporting, income tax withholding, and employment tax obligations with respect to leave transferred by State employees under Program. You request rulings that the State does not have any such obligations with respect to State employees that transfer leave under Program on the ground that the leave so transferred is not includible in the State employees' gross income. You also request rulings that the State has information reporting, income tax withholding, and employment tax obligations with respect to amounts paid to survivor of a deceased employee under Program on the ground that such amounts constitute gross income (for income tax purposes) and wages (for employment tax purposes) of the deceased employee.

FACTS

State establishes personnel rules pursuant to Statute. Pursuant to Statute and memos of understanding resulting from collective bargaining between State and particular unions, State has established Program, under which certain State employees may donate vacation and other similar accrued leave to the leave bank of a deceased State correctional guard or highway patrol officer who dies while in service but not in the line of duty. State then pays the cash value of the donated leave to the survivor of the deceased guard or officer. The value of the donated leave may not exceed $Z.

LAW AND ANALYSIS – GROSS INCOME ISSUE

Section 61 of the Internal Revenue Code provides that, except as otherwise provided by law, gross income means all income from whatever source derived, including compensation for services.

A basic principle of tax law is that a taxpayer's assignment to another person of his or her right to receive compensation for personal services does not relieve the taxpayer of the tax liability on the assigned income. *See Lucas v. Earl*, 281 U.S. 111 (1930), and *Helvering v. Eubank*, 311 U.S. 122 (1940), 1940-2 C.B. 209.

One exception to this principle is described in Rev. Rul. 90-29, 1990-1 C.B. 11, involving a leave-sharing plan established by an employer. Under the plan, employees who suffer medical emergencies may qualify to receive leave surrendered to the employer by other employees or leave deposited by its employees in an employer-sponsored leave bank. The ruling holds that an employee who surrenders leave to the employer or deposits it in the leave bank does not realize any income and incurs no deductible expense or loss, either upon the surrender or deposit of the leave or its use by the recipient. The ruling also concludes that the leave recipient must include the leave received in gross income as compensation.

A second exception involves leave-based donation programs to aid the victims of Hurricane Katrina. Notice 2005-68, 2005-40 I.R.B. 622, provides that the Internal Revenue Service will not assert that cash payments an employer makes to § 170(c) organizations (such as charities) in exchange for vacation, sick, or personal leave that its employees elect to forgo constitute gross income or wages of the employees if the payments are: (1) made to the § 170(c) organizations for the relief of victims of Hurricane Katrina; and (2) paid to the § 170(c) organizations before January 1, 2007.

We believe that Program is distinguishable from the narrow exceptions described above. Program is not a medical emergency leave program within the scope of Rev. Rul. 90-29 because it does not provide an employee with pay during a time that he or she is facing a personal or family medical emergency. Rather, it resembles a program to pay a death gratuity to survivors of a deceased employee. Also, it is outside the

scope of Notice 2005-68 because it was not designed specifically to aid the victims of Hurricane Katrina.

Because Program does not satisfy either of the exceptions described above, the tax consequences to State employees who transfer leave pursuant to Program are governed by the anticipatory assignment of income doctrine. Applying the doctrine to the facts of this case, we conclude that a State employee's assignment of his or her right to receive vacation and other similar accrued leave under Program will not relieve the employee of the tax liability on the assigned leave. Therefore, a State employee must include in income under § 61 as compensation for services provided by that employee to his or her employer, vacation and other similar accrued leave that the employee transfers pursuant to Program.

LAW AND ANALYSIS – EMPLOYMENT TAX ISSUE

Sections 3101 and 3111 impose Federal Insurance Contribution Act (FICA) taxes on wages. Section 3301 imposes Federal Unemployment Tax Act (FUTA) tax on an employer with respect to wages as paid by an employer with respect to employment. Also, § 3402(a)(1) provides, generally, that every employer making payment of wages must deduct and withhold upon such wages federal income taxes. Wages, for purposes of income tax withholding (ITW), is defined in § 3401(a) as all remuneration for services performed by an employee for his employer, with certain exceptions not here relevant. Sections 3121(a) and 3306(b) provide similar definitions of wages for purposes of FICA tax and FUTA tax, respectively.

Liability for employment taxes arises when there has been an actual or constructive payment of wages to the employee. Section 31.3121(a)-2(a) of the Employment Tax Regulations generally provides for FICA tax purposes that wages are considered paid by an employer at the time they are actually or constructively paid. Section 31.3121(a)-2(b) provides that wages are constructively paid when they are credited to the account of or set apart for an employee so that they may be drawn upon by him at any time although not then actually reduced to his possession. However, to constitute payment, the wages must be credited to or set apart for the employee without any substantial limitation or restriction as to the time or manner of payment or condition upon which payment is made, and must be made available to him so that they may be drawn upon at any time, and their payment brought within his own control and disposition. Section 31.3301-4 for FUTA purposes and § 31.3402(a)-1(b) for ITW purposes contain similar provisions.

Section 6051(a) requires every person who is obligated to deduct and withhold from an employee a tax under § 3101 (*i.e.*, employee FICA) or § 3402 (*i.e.*, income tax withholding) to furnish each employee with respect to remuneration paid by such person to such employee during the calendar year a written statement reflecting, among other items, the amount of wages paid and the amount of FICA tax and income tax withheld.

Generally, absent some specific exception, under the actual and constructive rules set forth above for determining wages, wages are paid to an employee when the employee receives the value of leave, whether such value is given directly to such employee or assigned by such employee to another. Such wages are reportable on Form W-2, Wage and Tax Statement, and subject to FICA, FUTA, and ITW of the employee. As previously discussed, for federal income tax purposes, State employees who transfer vacation and other similar accrued leave pursuant to Program must include in gross income the value of the leave so transferred, as required by the anticipatory assignment of income doctrine. Accordingly, the value of any leave transferred by a State employee pursuant to Program is wages, reportable on the tranferor-employee's Form W-2.

HOLDING

The value of the vacation and other similar accrued leave transferred by State employees under Program is reportable on the employee's Form W-2, and is subject to FICA tax, FUTA tax, and ITW.

Under section 4.02(1) of Rev. Proc. 2006-3, 2006-1 I.R.B. 122, 129, the Service ordinarily will not issue letter rulings on any matter in which the determination is primarily one of fact. Because the reasons that State employees may transfer leave to Program is primarily one of fact, we cannot express an opinion regarding the federal tax consequences of the subject payments to the survivors who receive the cash value of the transferred leave under Program.

A copy of this letter must be attached to any income tax return to which it is relevant. We enclose a copy of the letter for this purpose. Also enclosed is a copy of the letter showing the deletions proposed to be made when it is disclosed under § 6110.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any item discussed or referenced in this letter. This letter ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

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