Internal Revenue Service Department of the Treasury

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199910052

Person to Contact:
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Telephone Number:
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Refer Reply to:
CC:EBEO:6 PLR-117062-98

Date: DEC 8 1998

Attn:

Taxpayer =

State =

Statute =

Dear

This responds to your ruling request of August 7, 1998, on behalf of Taxpayer concerning the proper federal income tax treatment of certain retirement disability benefits paid to municipal employees under the Statute.

The Taxpayer, a division of the State, provides disability retirement benefits to policemen and firemen pursuant to the Statute. Subdivision b of the Statute provides that a member shall be entitled to retirement for disability incurred in the performance of duty if, at the time the application is filed, he is: (1) physically or mentally incapacitated for performance of duty as the natural and proximate result of a disability not caused by his own willful negligence sustained in such service and while actually a member of the policemen's and firemen's retirement system, and (2) actually in service upon which his membership is based. However, in a case where a member is discontinued from service, either voluntarily or involuntarily, subsequent to sustaining a disability in such service, application may be made not later than two years after the member is discontinued from service and provided that the member meets the requirements of subdivisions a and b of the Statute.

Subdivision d of the Statute provides that after the member files an application for disability benefits, the member shall be given one or more medical examinations. If it is determined that the member is physically or mentally incapacitated for the performance

of duty pursuant to subdivision b of the Statute and ought to be retired, he shall be so retired. Such retirement shall be effective as of a date approved.

Subdivision f of the Statute provides a retirement allowance payable upon retirement for disability incurred in the performance of duty consisting of a pension of one-half of his final average salary plus an annuity which shall be the actuarial equivalent of the member's accumulated contributions, if any.

You request a ruling that the disability retirement payments made under the Statute, to the extent they do not exceed one-half of the members' final average salary, are made under a statute in the nature of a workmen's compensation act and are, therefore, excludable from the recipients' gross income and not subject to information reporting.

Section 61(a) 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.

Section 104(a)(1) of the Code provides that gross income does not include amounts received under workmen's compensation acts as compensation for personal injuries or sickness.

Section 1.104-1(b) of the Income Tax Regulations states that section 104(a)(1) of the Code excludes from gross income amounts received by an employee under a workmen's compensation act or under a statute in the nature of a workmen's compensation act that provides compensation to the employee for personal injury or sickness incurred in the course of employment. Section 104(a)(1) also applies to compensation which is paid under a workmen's compensation act to the survivor or survivors of a deceased employee. Section 104(a)(1) does not apply to a retirement pension or annuity to the extent it is determined by reference to the employee's age or length of service, or the employee's prior contributions, even though the employee's retirement is occasioned by an occupational injury or sickness. Section 104(a)(1) also does not apply to amounts which are received as compensation for a non-occupational injury or sickness nor to amounts received as compensation for an occupational injury or sickness to the extent that they are in excess of the amount provided in the applicable workmen's compensation act or acts.

In Rev. Rul. 85-104, 1985-2 C.B. 52, the Service considered a statute under which the participants who were disabled due to work related injury or sickness receive the greater of a fixed percentage of base salary or an amount computed on the basis of years of service. The Service concluded that an amount up to the percentage of base

salary specified by the statute would be excludable from the participants' gross incomes under section 104(a)(1) of the Code and any excess, because it would be computed on the basis of length of service, would not be excludable under section 104(a)(1).

Section 3402 of the Code provides that, except as otherwise provided in section 3402, every employer making payment of wages shall deduct and withhold upon such wages a tax determined in accordance with table or computational procedures described by the Secretary of the Treasury. Amounts excludable from gross income under section 104(a)(1) of the Code are not "wages" subject to income tax withholding under section 3402 of the Code.

Section 3121(a) of the Code provides, with certain exceptions, that for Federal Insurance Contributions Act (FICA) taxes, the term "wages" means all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash.

Section 3121(a)(13) of the Code provides that the term "wages" for purposes of section 3121 does not include any payment or series of payments by an employer to an employee or any of his dependents which is paid (A) upon or after the termination of an employee's employment relationship because of (i) death, or (ii) retirement for disability, and (B) under a plan established by the employer which makes provision for his employees generally or a class or classes of his employees (or for such employees or class or classes of such employees and their dependents), other than such payment or series of payments which would have been paid if the employee's employment relationship had not been so terminated.

The Statute limits retirement disability benefits to members who become physically or mentally incapacitated as a result of an on-the-job injury and is a statute in the nature of a workmen's compensation act.

Retirement disability benefits paid under the Statute, to the extent they do not exceed one-half of the member's final average salary, are excludable from the recipients' gross income under section 104(a)(1) of the Code. Benefits paid under the Statute which constitute an annuity based on the actuarial equivalent of the members' accumulated contributions, if any, are not excludable from the recipients' gross income.

Retirement disability benefits which are excludable from the recipients' gross income are not subject to information reporting.

Except as specifically ruled on above, no opinion is expressed or implied with respect to the application of any provision of the Code or the regulations to any provision of the Statute.

This ruling letter is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

Sincerely,

Harry Beker
Chief, Branch 6
Office of the Associate
Chief Counsel
(Employee Benefits and
Exempt Organizations)

Enclosures:
Copy of this letter
Copy for section 6110 purposes.