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COMMONWEALTH OF PENNSYLVANIA
DEPARTMENT OF REVENUE



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REVIEW COMMISSION

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Mr. Robert E. Nyce
Executive Director
Independent Regulatory
Review Commission
Fourteenth Floor
Harristown 2
333 Market Street
Harrisburg, PA 17101

Dear Mr. Nyce:

Enclosed please find the Department of Revenue's draft final form regulations relating to termination pay, severance pay and early retirement incentive programs; and supplemental unemployment benefit plan.

We would appreciate it if you could convey your comments to this office by March 16, 2001. Comments received by this date will be considered in the drafting of the final form regulations.

Thank you for your anticipated input and assistance in promulgating these regulations.

Sincerely,

Douglas A. Berguson
Senior Assistant Counsel

Enclosures

DAB:AMD:tlch

FACE SHEET
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Copy below is hereby approved as to form and legality. Attorney General

By: _____
(DEPUTY ATTORNEY GENERAL)

DATE OF APPROVAL

Check if applicable
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Copy below is hereby certified to be true and correct copy of a document issued, prescribed or promulgated by:

PA Department of Revenue

(Agency) 15-413
Document/Fiscal Note No. _____
Date of Adoption: _____
By: Larry P. _____
Secretary of Revenue
Title: _____
(Executive Officer, Chairman or Secretary)

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Copy below is hereby approved as to form and legality. Executive or Independent Agencies.

By: _____

Date of Approval

(Deputy General Counsel)
(Chief Counsel, Independent Agency)
(Strike inapplicable title)

Check if applicable. No Attorney General approval or objection within 30 days after submission

NOTICE OF FINAL RULEMAKING

DEPARTMENT OF REVENUE

61 Pa. Code §§101.1 and 101.6

Personal Income Tax

Termination Pay, Severance Pay and
Early Retirement Incentive Programs

PREAMBLE

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The Department of Revenue (Department), under the authority contained in section 354 of the Tax Reform Code of 1971 (TRC) (72 P.S. § 7354), by this order amends 61 Pa. Code Chapter 101. General Provisions, sections 101.1 and 101.6 (relating to definitions; and compensation) to read as set forth in Annex A.

Purpose of Regulation

This regulatory change clarifies the taxation of termination pay, severance pay, early retirement incentive programs and programs offered by employers to provide benefits to employees in addition to those in qualifying retirement plans upon separation from service.

The regulation also interprets section 301(d) of the TRC (72 P.S. § 7301(d)) to mean that Federal insurance benefits paid under the Railroad Retirement Act and guaranteed payments to a partner of a partnership for services to the partnership are excluded from compensation.

Explanation of Regulatory Requirements

Section 101.1 (relating to definitions) is amended by adding the definitions of limited plan of termination, qualified annuity and severance pay for use in the regulation. Section 101.6(a) is amended by updating the list of examples of compensation. Section 101.6(c)(3) is amended to reflect the Department's interpretation of the Pennsylvania Income Tax law with regard to Federal insurance benefits paid under the Railroad Retirement Act. Text from § 101.6(a) is deleted and moved to a new paragraph (13) in § 101.6(c). Paragraph (13) reflects the Department's interpretation of the Pennsylvania Income Tax law with regard to guaranteed payments to a partner of a partnership for services to the partnership. The numbering of this new paragraph was changed from the proposal because of the Department's adoption of Regulation 15-402, relating to payments for employee welfare benefit plans and cafeteria plans.

Finally, a new subsection (m) is added to § 101.6 to explain superannuation requirements and the voluntary discontinuance of a plan. The lettering of this new subsection was changed from the proposal because of the Department's adoption of Regulation 15-402.

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Affected Parties

This regulation could affect all employers with early-out incentive programs and employees receiving severance pay.

Comment and Response Summary

Notice of proposed rulemaking was published at 30 Pa. B. 2371 (May 13, 2000). The proposal is being adopted with changes as set forth in Annex A.

No comments were received from the public during the public comment period. No comments were received from the House and Senate Finance Committees. The Department did receive comments from the Independent Regulatory Review Commission (IRRC).

Amendments to the proposed rulemaking in response to comments are as follows:

(1) IRRC indicated that the phrase "in advance" in subparagraph (ii) of the definition of "limited plan of termination" was unclear and requested that the Department be more specific. In response to IRRC's request, the Department has amended the provision by adding an explanatory phrase that modifies "in advance" and provides the necessary clarity.

(2) In its comments, IRRC was unsure what was meant by the phrase "or subject in any manner to anticipation, assignment or pledge by" as it was used in subparagraph (iii) of the definition of "severance pay" in § 101.1 and asked the Department to explain its necessity. To clarify its intent, the Department amended the subparagraph by deleting the phrase IRRC found unclear and adding language that more clearly explains the provision.

Amendments initiated during the Department's internal review of the regulation are as follows:

(1) For clarity, the definition of qualified annuity was amended by adding the phrase "any of the following periods."

(2) As referenced in the proposal preamble, certain proposed amendments to § 101.6 would need to be reclassified with the adoption of Regulation 15-402. Regulation 15-402 was adopted at 30 Pa.B. 3938 (August 5, 2000); therefore, proposed § 101.6(c)(10) has been moved to paragraph (13) and proposed § 101.6(e) has been moved to subsection (m).

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(3) In addition, an error occurred in the publication of the proposal at § 101.6(e)(1), instead of "he" the text appeared as "the firm." The incorrect text was deleted and "he" was added.

Fiscal Impact

The Department has determined that the amendments will have no fiscal impact on the Commonwealth.

Paperwork

The amendments will not require additional paperwork for the public or the Commonwealth.

Effectiveness/Sunset Date

The amendments will become effective upon final publication in the Pennsylvania Bulletin. The regulation is scheduled for review within five years of final publication. No sunset date has been assigned.

Contact Person

The contact person for an explanation of the amendments is Anita M. Doucette, Office of Chief Counsel, PA Department of Revenue, Dept. 281061, Harrisburg, Pennsylvania 17128-1061.

Regulatory Review

Under section 5(a) of the Regulatory Review Act (71 P.S. § 745.5(a)), on May 3, 2000, the Department submitted a copy of the notice of proposed rulemaking, published at 30 Pa.B. 2371, to IRRC and the Chairpersons of the House Committee on Finance and the Senate Committee on Finance for review and comment. In compliance with section 5(c) of the Regulatory Review Act (71 P.S. § 745.5(c)), the Department also provided IRRC and the Committees with copies of all comments received, as well as other documentation.

In preparing these final-form regulations, the Department has considered the comments received from IRRC, the Committees and the public.

These final-form regulations were (deemed) approved by the Committees on _____ and were (deemed) approved by IRRC on _____, in accordance with section 5.1(e) of the Regulatory Review Act (71 P.S. § 745.5a(e)).

Findings

The Department finds that:

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(1) Public notice of intention to amend the regulations has been duly given under sections 201 and 202 of the act of July 31, 1968 (P.L. 769, No. 240) (45 P.S. §§ 1201 and 1202) and the regulations thereunder, 1 Pa. Code §§ 7.1 and 7.2.

(2) The amendments are necessary and appropriate for the administration and enforcement of the authorizing statute.

Order

The Department, acting under the authorizing statute, orders that:

(a) The regulations of the Department, 61 Pa. Code, are amended by amending Chapter 101. General Provisions, sections 101.1 and 101.6 to read as set forth in Annex A.

(b) The Secretary of the Department shall submit this order and Annex A to the Office of General Counsel and the Office of Attorney General for approval as to form and legality as required by law.

(c) The Secretary of the Department shall certify this order and Annex A and deposit them with the Legislative Reference Bureau as required by law.

(d) This order shall take effect upon publication in the Pennsylvania Bulletin.

LARRY P. WILLIAMS
SECRETARY OF REVENUE

02/14/01

CONTINUATION SHEET
FOR FILING DOCUMENTS
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ANNEX A

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Title 61. Revenue, Part I. Department of Revenue, Subpart B.
General Fund Revenues, Article V. Personal Income Tax, Chapter
101. General Provisions.

§ 101.1. Definitions.

The following words and terms, when used in this article,
shall have the following meanings, unless the context clearly
indicates otherwise:

* * *

Limited plan of termination - A plan that has one or more of
the following attributes:

(i) The plan, when begun, is scheduled to be complete on a
certain date or upon the occurrence of one or more specified
events.

(ii) The number, percentage or class of employes whose
services are to be terminated are specified in advance OF THE
EMPLOYES' TERMINATIONS OF SERVICE.

(iii) The plan is otherwise temporary or limited.

* * *

Qualified annuity - An arrangement under which the payee is
entitled to equal, or substantially equal, periodic payments,

paid not less frequently than annually, for ANY OF THE FOLLOWING PERIODS:

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(i) The life of the participant, or, if applicable, the joint lives of the recipient and recipient's designated beneficiary.

(ii) The life expectancy of the participant, or, if applicable, the joint life expectancies of the recipient and recipient's designated beneficiary.

(iii) A period of at least 10 years.

* * *

Severance pay - A payment made upon separation from employment under:

(i) A plan which has both of the following attributes:

(A) Payments are not contingent solely upon an employe's retirement from service or being the same age as, or older than, the earliest retirement age under a qualifying retirement benefit plan or qualifying retirement income plan sponsored by the employer.

(B) Total payments cannot exceed twice the employe's annual compensation during the year preceding the employe's termination.

(ii) A plan under which all payments to any plan participant are completed within 120 months of the participant's termination.

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(iii) A plan under which no benefit is, OR ONLY REDUCED BENEFITS ARE payable to, or subject in any manner to anticipation, assignment or pledge by, an employee except upon voluntary separation from the employment of the employer before CAN BE TAKEN, ASSIGNED, PLEDGED OR OTHERWISE CHARGED OR DEALT WITH BY, ANY PLAN PARTICIPANT AFTER the participant reaches normal retirement age or service.

(iv) A plan, including a stock bonus or profit-sharing plan formed by a trust that meets the requirements for qualification described in section 401 of the IRC (26 U.S.C.A. § 401) or employe stock ownership plan, with one or more of the following attributes:

(A) The amount of earnings on contributions (or allocations of contributions or earnings) and amount of benefits are determined with regard to the current or accumulated profits or losses of the employer.

(B) The employer can contribute only in those years when it has current or accumulated profits.

(C) The employer's contributions can fluctuate depending on the level of its profits.

(D) The employer's contributions are made out of current or accumulated profits.

(E) Distributions are paid with respect to stock of a corporation which is held by an employee stock ownership plan.

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(v) A plan under which the accrued benefit payable to each vested participant who does not die before the payment starting date is neither paid nor payable in the form of a qualified annuity.

(vi) A limited plan of termination.

* * *

§ 101.6. Compensation.

(a) Compensation includes items of remuneration received [by an employe or casual employe], directly or through an agent, in cash or in property, based on payroll periods or piecework, for services rendered as an employe or casual employe, agent or officer of an individual, partnership, [but not guaranteed payments to a partner for services rendered to the partnership,] business or nonprofit corporation, or government agency. These items include salaries, wages, commissions, bonuses, stock options, incentive payments, fees, tips, dismissal, termination or severance payments, early retirement incentive payments and other additional compensation contingent upon retirement, including payments in excess of the scheduled or customary salaries provided for those who are not terminating service, rewards, vacation and holiday pay, paid leaves of absence, payments for unused vacation or sick leave, tax assumed by the employer, or casual employer signing bonuses, amounts received under employe benefit plans and deferred compensation

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arrangements, and other remuneration received for services rendered.

* * *

(c) Compensation does not mean or include any of the following:

* * *

(3) [Payments commonly recognized as] Federal old age [or retirement benefits paid to persons retired from service after reaching a specified age or after a stated period of employment] insurance benefits payable under 42 U.S.C.A. § 401 et seq., Railroad Retirement Act benefits payable under 45 U.S.C.A. §§ 228 or § 231 et seq. or any retired or retainer pay of a member or former member of a uniformed service computed under 10 U.S.C.A. § 1401. [Retirement pay includes a distribution of a lump sum upon retirement, but does not include a severance payment by an employer to an employe who terminates employment without retiring. A payment of the latter type shall be considered compensation, if paid upon termination of employment, rather than as a retirement income, to the extent that the payment exceeds the employe's contribution to any plan out of which the payment may be made.]

* * *

~~(10)~~ (13) Guaranteed payments to a partner for services rendered to the partnership.

* * *

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(e) (M) For purposes of this section:

(1) A person who separated from service before satisfying superannuation requirements shall be deemed to be retired from service upon reaching retirement age, regardless of whether ~~the firm~~ HE has permanently and wholly withdrawn from active working life or not.

(2) The voluntary discontinuance of a plan within 3 years after it has taken effect, for any reason other than business necessity, will be evidence that such plan was temporary and limited.

02/05/01