

Internal Revenue Service

Department of the Treasury

Number: **200226018**
Release Date: 6/28/2002
Index Number: 104.02-00, 6041.03-00,
6049.01-00, 3406.02-00

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:PA:APJP:01/PLR-162874-01

Date:

March 22, 2002

Legend

Employer =

Employee =

Company =

Date 1 =

Date 2 =

State A =

Dear :

This is in response to your request dated November 13, 2001, and supplemental correspondence for a private letter ruling under section 6041, section 6049, and section 3406 of the Internal Revenue Code (Code). Specifically, you request the following rulings with respect to each of the periodic payments made by Company on behalf of Employer:

1. That Company is not required to file an information return under either section 6041 or section 6049 of the Code; and
2. That Company is not required to engage in backup withholding under section 3406 of the Code since no portion of any of the periodic payments constitutes a "reportable payment" within the meaning of section 3406.

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You represent that each payment meets the requirements of section 104(a)(1) of the Code and the regulations thereunder as payment in discharge of a claim for workmen's compensation. In addition, you have requested that, for purposes of this ruling request, we assume that the payments are not attributable to deductions allowed under section 213 of the Code.

Facts

On Date 1, Employee began working for Employer. After sustaining severe injuries during the course of employment on Date 2, Employee was placed on disability. In accordance with the laws of State A, Employee subsequently filed a claim for workmen's compensation with Employer. Employer denied the claim and Employee appealed. The two parties eventually agreed to settle the claim.

As part of the settlement agreement, Employer will pay workmen's compensation to Employee in the form of an initial sum of cash with subsequent periodic payments. The total amounts received by Employee will be paid in complete satisfaction of the claim. Each of the periodic payments will be made at a specified time under the agreement and Employee may not change the timing or amount of the payments at any time. Likewise, Employee may not sell, mortgage, encumber, or otherwise assign any portion of the payments at any time.

In addition, Employee has agreed to accept periodic payments made by Company on behalf of Employer. Any amounts paid by Company will be pursuant to a periodic payment purchase agreement between Employer and Company. Under the terms of the purchase agreement, Company will become the sole obligor of the claim. In accordance with the settlement agreement, Company will make each of the periodic payments at a specified time, and neither the timing nor amount of the payments shall change at any time prior to satisfaction of the claim. The total amounts paid to Employee pursuant to the claim will not exceed the amounts provided for under applicable state law.

Law and Analysis

Information Reporting under Section 6041

Section 6041 of the Code provides that all persons engaged in a trade or business and making payment in the course of such trade or business to another person of wages, compensations, remunerations, or other fixed or determinable gains, profits, and income of \$600 or more in any taxable year must file an information return with respect to such payments.

Section 104(a)(1) of the Code provides that, except in the case of amounts attributable to deductions allowed under section 213 for any prior taxable year, gross income does not include amounts received under workmen's compensation acts as compensation for

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personal injuries or sickness.

Likewise, section 1.104-1(b) of the Income Tax Regulations (regulations) provides that section 104(a)(1) 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 which provides compensation to an employee for personal injuries or sickness incurred during the course of employment. In addition, section 1.104-1(b) states that the exclusion does not apply to amounts received as compensation for an occupational injury to the extent that they are in excess of the amount provided in the applicable workmen's compensation act or acts.

Under the workmen's compensation law of State A, no release of liability or settlement agreement for payment of workmen's compensation benefits is valid unless approved by the state. Until approved as required by the State A labor code, amounts received under the settlement agreement do not qualify as workmen's compensation benefits under State A law and, therefore, are not excludable from gross income under section 104(a)(1) of the Code. However, upon approval of the settlement agreement by State A, amounts received will be excludable from gross income under section 104(a)(1). Therefore, upon approval of the settlement agreement in accordance with the State A labor code, Company will have no information reporting requirements under section 6041 with respect to the periodic payments.

Information Reporting under Section 6049

Section 6049 of the Code provides that every person who makes payments of interest aggregating \$10 or more to any other person during any calendar year, or who receives payments of interest as a nominee and who makes payments aggregating \$10 or more during any calendar year to any other person with respect to the interest so received, shall make a return according to the forms or regulations prescribed by the Secretary, setting forth the aggregate amount of such payments and the name and address of the person to whom paid.

Company is not required to file information returns under section 6049 of the Code with respect to any of the periodic payments to Employee. Each payment will be made in accordance with the settlement agreement between Employer and Employee as compensation for injuries sustained during the course of employment. The total amounts received by Employee will be paid in complete satisfaction of the claim, and none of the periodic payments will include interest. As such, Company will have no information reporting requirements under section 6049 with respect to the periodic payments.

Backup Withholding under Section 3406

Section 3406(a) of the Code provides that, in the case of any reportable payment and where certain circumstances exist, the payor shall deduct and withhold from such payment a tax equal to the product of the fourth lowest rate of tax applicable under

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section 1(c) and such payment.

Section 3406(b) of the Code states that the term "reportable payment" means any reportable interest or dividend payment, and any other reportable payment.

Company is not required to engage in backup withholding with respect to any of the periodic payments to Employee to the extent that the payments are excludable under section 104(a)(1) of the Code. Amounts paid pursuant to workmen's compensation acts and excluded from income under section 104 are not reportable payments. Therefore, Company is not required to engage in backup withholding with respect to such payments.

Conclusion

Based on the information provided and the representations made, upon approval of the settlement agreement in accordance with the State A labor code, we conclude the following with respect to the periodic payments:

1. That Company is not required to file information returns under section 6041 or section 6049 of the Code; and
2. That Company is not required to engage in backup withholding under section 3406 of the Code.

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

Sincerely,
John J. McGreevy
Assistant to the Branch Chief, Branch 1
Office of the Assistant Chief Counsel
(Administrative Provisions and Judicial Practice)

Enclosures (2):

- Copy of this letter
- Copy for section 6110 purposes