

STATE CONTROLLER'S OFFICE  
PERSONNEL/PAYROLL SERVICES DIVISION  
P. O. BOX 942850  
Sacramento, CA 94250-5878

DATE: December 29, 2010

PAYROLL LETTER #10-022

TO: All Agencies/Campuses in the Uniform State Payroll System

FROM: Lisa Crowe, Chief  
Personnel/Payroll Services DivisionRE: **INTERNAL REVENUE SERVICE DOCUMENT REQUEST - SETTLEMENTS**

As announced in Payroll Letter #10-021, the Internal Revenue Service (IRS) is conducting an audit of the State of California for tax years 2008 and 2009. The IRS is currently reviewing employment related settlement payments made by the State and has requested data for tax year 2008. Please see the attached Information Document Request Number EMT-004. The Internal Revenue Service has also issued a memo dated December 9, 2010, which explains the reason for this request and clarifies the different types of settlement payments.

**To ascertain the requested information, please complete the attached Agency/Campus Settlement Information Sheet and return it to our office no later than January 4, 2011. The return instructions are included at the end of the information sheet. Our office will compile the data and provide it to the IRS. They may subsequently request additional information after completing their review of the data. Agencies and campuses will be contacted should further information be requested by the IRS.**

If you have any questions regarding the Internal Revenue Service Audit, please contact Jennifer Rocco, Tax Support Manager (916) 322-8105 or [jrocco@sco.ca.gov](mailto:jrocco@sco.ca.gov).

LC:JR: TSS

Attachments: Information Document Request  
Internal Revenue Service Memo  
Agency/Campus Settlement Information Sheet

Form 4564	Department of the Treasury Internal Revenue Service <b>INFORMATION DOCUMENT REQUEST</b>	Request Number EMT-004
TO: (Name of Taxpayer and Co. Div. or Branch) (Include Entity Number) State Controller State of California  Please return with listed documents to requester listed below	Subject: Employment Taxes	Tax Period(s): 2008
	GSain No. 1504	Submitted to: Taxpayer
	Dates of Previous Requests None	

Description of Documents Requested

Subject: Settlements

1. During the period under examination, did this entity, agency, department and/or its insurance carrier(s) pay any settlement(s)/award(s)/judgment(s) for back pay, lost compensation, punitive damages, or similar such item to any of its current, former, or prospective worker(s) as a result of a court action, an arbitration proceeding, or a negotiation in lieu of a court action? If yes, please provide the following:
  - a. Name/SSN
  - b. Payment amount
  - c. Payment type
  - d. Information return issued

*IDR Response Due Date: next appointment, May 4, 2010*

Date Information Received By IRS: \_\_\_\_\_  
(Initials) (Date)

From:	Name and Title of Requester Leslie Van Buren FSLG Specialist ID# 77-1944 Phone # 408-817-6356	Date March 2, 2010
	Office Location – Internal Revenue Service, ATTN: MS:7600:LVB 55 S. Market Street San Jose, Ca. 95113-2324	

DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
Washington, D. C. 20224



TAX EXEMPT AND  
GOVERNMENT ENTITIES DIVISION

December 9, 2010

**MEMORANDUM**

**FOR:** Lisa Crowe, Chief of Payroll Services Division

**FROM:** Leslie Van Buren, FSLG Specialist

Leslie Van Buren  
Digitally signed by Leslie Van Buren  
DN: cn=Leslie Van Buren, email=leslie.vanburen@irs.gov, o=IRS, ou=IRS, c=US  
Date: 2010.12.09 13:20:40 -0800

**SUBJECT:** 2008 Examination Plan

The following Information Documents:

- a) Outstanding items due:
  - 1) EMT-04, items #1, #a, #b, #c, & #d
- b) In order for the examination team to make a determination of the correct treatment of employment-related settlement payments, we must examine 4 items as listed below. Please complete the attached spreadsheet in response to IDR EMT-04 identified in #a above.
  - 1) The character of the payment and the nature of the claim that gave rise to the payment. For example, a payment could be for a lost wages claim brought under Title VII of the Civil Rights Act of 1964. See item #c below for further details on character of the payment.
  - 2) Determine whether the payment constitutes an item of gross income.
  - 3) Determine whether the payment is wages for employment tax purposes (Federal Insurance Contributions Act (FICA), and income tax withholding).
  - 4) Determine the appropriate reporting for the payment and any attorneys' fees (Form 1099 or Form W-2).
- c) Payment type: **Character of the payment and nature of the claim.** Whether a payment is includable in gross income and whether it is wages for purposes of employment taxes depend upon the character of the payment. The following describes the types of settlement payments or awards that may be received in connection with an employment-related dispute.

**A. Character of the payment**

1. **Severance pay.** Severance pay is a payment made by an employer to an employee upon the involuntary termination of employment. The right to receive severance pay and the amount of severance pay are usually based on the employee's length of service.
2. **Back pay.** Back pay is compensation paid to an individual to compensate the individual for remuneration that would have been received up to the time of settlement or court award but for the employer's wrongful conduct. For example, back pay is awarded to an employee if the employee is illegally terminated by an employer, or to an applicant for employment who is not hired for illegal reasons. Under those circumstances, the back pay relates to a period when no services for

the employer were performed. Certain federal statutes, *e.g.*, Title VII of the Civil Rights Act of 1964, and the Age Discrimination in Employment Act (ADEA) of 1967, specifically authorize the recovery of back pay as a remedy for unlawful agency conduct.

3. **Front Pay.** Front pay is paid to an individual to compensate the individual for remuneration that would have been received after the settlement date or court award but for the employer's wrongful conduct and the circumstances – *e.g.*, extreme animosity between the employer and employee – which make it impracticable to place the employee in the position.
4. **Compensatory damages.** Compensatory damages include compensation for physical injury and non-physical injury, *e.g.*, humiliation and defamation, and for the intangible elements of personal injury such as emotional distress and pain and suffering.
5. **Consequential damages.** Consequential damages are compensation for damage, loss, or injury that do not flow directly and immediately from the act of the party, but are consequences or results of such act.
6. **Punitive/liquidated damages.** Generally, liquidated and punitive damages are not directly related to the actual loss incurred. Liquidated damages are amounts that parties agree to pay in the event of a breach of an agreement as a substitute for compensatory damages. Liquidated damages may also be imposed by statute, *e.g.*, the Fair Labor Standards Act of 1938 and the Equal Pay Act of 1963. Punitive damages punish the wrongdoer for wrongful conduct. An award of punitive damages against the government is possible only when the government waives its sovereign immunity, *e.g.*, the Civil Rights Act and the Americans with Disabilities Act, below.
7. **Restoration of benefits.** Restoration of benefits may include the payment of health insurance premiums, Thrift Savings Plan employer and employee contributions, and other retirement contributions.

**The receipt of these items will assist in completing the examination the week of 1/4/2011. Please submit information in electronic format by 1/4/2011.**

**Agency/Campus Settlement Information Sheet**  
**\*Please provide this information for tax year 2008 only\***

- |  |  |
|--|--|
| 1. Did your agency/campus pay a settlement for <i>severance pay</i> ?                              | <input type="checkbox"/> Yes <input type="checkbox"/> No |
| 2. Did your agency/campus pay a settlement for <i>back pay</i> ?                                   | <input type="checkbox"/> Yes <input type="checkbox"/> No |
| 3. Did your agency/campus pay a settlement for <i>front pay</i> ?                                  | <input type="checkbox"/> Yes <input type="checkbox"/> No |
| 4. Did your agency/campus pay a settlement for <i>compensatory damages</i> ?                       | <input type="checkbox"/> Yes <input type="checkbox"/> No |
| 5. Did your agency/campus pay a settlement for <i>consequential damages</i> ?                      | <input type="checkbox"/> Yes <input type="checkbox"/> No |
| 6. Did your agency/campus pay a settlement for <i>punitive/liquidated damages</i> ?                | <input type="checkbox"/> Yes <input type="checkbox"/> No |
| 7. Did your agency/campus pay a settlement for <i>restoration of benefits</i> ?                    | <input type="checkbox"/> Yes <input type="checkbox"/> No |
| 8. Did your agency/campus pay a settlement that <i>does not fit into one of these categories</i> ? | <input type="checkbox"/> Yes <input type="checkbox"/> No |
| 9. Did your agency/campus issue <i>Form W-2's</i> for any of these payments?                       | <input type="checkbox"/> Yes <input type="checkbox"/> No |
| 10. Did your agency/campus issue <i>Form 1099's</i> for any of these payments?                     | <input type="checkbox"/> Yes <input type="checkbox"/> No |
| 11. Did your agency/campus issue <i>Form 1042S's</i> for any of these payments?                    | <input type="checkbox"/> Yes <input type="checkbox"/> No |

\_\_\_\_\_  
Entity/Agency/Department Name

\_\_\_\_\_  
Name of Preparer

\_\_\_\_\_  
Fund Account(s) used to pay settlements

\_\_\_\_\_  
Title

\_\_\_\_\_  
Agency Code

\_\_\_\_\_  
Telephone Number

\_\_\_\_\_  
General Ledger Account(s)/Sub Account(s)  
used to pay settlements

\_\_\_\_\_  
E-mail address

\_\_\_\_\_  
Number of payees

\_\_\_\_\_  
\$  
Total amount of settlements paid

**Please fax your completed form to Jennifer Rocco, Tax Support Manager, State Controller's Office at (916) 322-0664.**