

# CALIFORNIA FRANCHISE TAX BOARD

Legal Ruling No. 365

November 5, 1973

## PENSIONS: DISABILITY RETIREMENT PENSIONS AND DEATH BENEFITS

### Syllabus:

Disability retirement pensions and death benefits payable to San Francisco police and fire personnel, whose injury or death was service incurred, are excluded from gross income so long as the benefits payable are not measured by the members service retirement allowance. When so measured the benefits are taxable. Taxable benefits are not excluded from gross income as sick pay after retirement age is reached.

Advice has been requested as to whether disability retirement pensions and death benefits, resulting from service incurred injury or death, payable to police and fire personnel of the City and County of San Francisco are excluded from gross income or are taxable. That City's retirement plan, contained in the City Charter, provides different benefits to police and fire personnel depending upon when they entered service. Hereinafter references to charter sections are to those contained in that city's Charter recently recodified in April, 1972.

Under the so-called "old Charter provisions" (Sections 8.540(b)(c) for policemen and 8.565(a)(b) for firemen), applicable to police and fire personnel who are members of their respective departments on January 8, 1932, the disability pension and death benefit payable is not affected or measured by the members qualification for normal service retirement. The monthly disability benefit payable is one-half the members monthly compensation payable for life. The death benefit payable to the decedent's widow is the disability benefit of the decedent would have received if he lived.

The so-called "new Charter provisions" applicable, for the most part, to police and fire personnel entering service after January 8, 1932 (Sections 8.547 and 8.548 for policemen, Sections 8.571 and 8.572 for firemen) do provide benefits which are affected by a members qualification for a service retirement allowance. These sections provide, in the event of service incurred disability, the members disability will be rated as would a typical industry injury. The rated percentage of the members monthly salary constitutes the monthly disability pension benefit until the member qualifies for his service retirement allowance. At that time the members service retirement allowance constitutes the benefit to which he is entitled. A member qualifies for service retirement after twenty-five years of service and after attaining age 50. The service retirement allowance is 55 percent of the members final monthly compensation. If death occurs in the line of duty and the member is qualified

for a service retirement allowance, and death benefit payable to the decedent's widow is the decedent's service retirement allowance. If death occurs before the member is qualified for service retirement, his entire monthly compensation constitutes the death benefit until such time as the decedent would have qualified for service retirement had he lived. At that time the member's service retirement allowance constitutes the widow's death benefit.

Though generally all income is includible in gross income, Revenue and Taxation Code §17138(a)(1) specifically excludes from gross income amounts received under a Workmen's Compensation Act for personal injuries or sickness incurred in the course of employment. The regulations thereunder, tit. 18, Cal. Admin. Code 17138(b), extend the exclusion to amounts received pursuant to a statute in the nature of a Workmen's Compensation Act. That regulation provides the exclusion also applies to death benefits payable under such an act. The Charter provisions above described evidence a statutory plan to provide compensation for police and fire personnel injured or killed in the line of duty. As such the plan is one in the nature of a Workmen's Compensation Act. Frye v. United States, 72 Fed.2d 405 (1947); Legal Ruling 178, March 7, 1956, CCH 201-132, P-H 58,641.

However, the statutory exclusion from gross income of amounts received under a Workmen's Compensation Act does not apply to the extent the benefit received is determined by reference to the employee's age or length of service, even though the employee's retirement is occasioned by an occupational injury or sickness. Regulation 17138(b), supra. The benefits payable under the old Charter provisions are never so measured. Thus, disability retirement pension and death benefits payable thereunder are excluded from gross income for the life of the member. The death benefit payable is likewise excluded from the widow's gross income.

Since disability retirement pensions under the new Charter provisions are determined by age and length of service once the member has qualified for service retirement, the exclusion of such benefits from gross income lasts only so long as the member was unqualified for his service retirement allowance. When service retirement qualification occurs the benefit payable thereafter is taxable. Similarly, the widow's death benefit under the new Charter provisions, so long as it is not measured by the decedent's service retirement allowance is excluded from her gross income. When her benefit is measured by the decedent's service retirement allowance, the benefit is thereafter taxable.

Legal Ruling 349, April 26, 1972, CCH 204-904, P-H 58,598 holds benefits payable to widows of deceased San Francisco police and fire personnel, whose deaths were service incurred, are non-taxable. The benefits were held to be payments in the nature of amounts received under a Workmen's Compensation Act. That Ruling, however, makes no distinction between benefits payable under the old and new Charter provisions. Accordingly, Legal Ruling 349 is withdrawn.

Assuming the disabled employee would have worked but for his disability, the disability retirement pension benefit payable after a member has qualified for service retirement under the new Charter provisions is not excluded from gross income under the sick pay exclusion formula contained in Revenue and Taxation Code Section 17139(d). That statute requires the amounts received under plan must be wages, or the equivalent thereof, payable because the employee is absent from work because of personal injury or sickness. The position of the Internal Revenue Service, with which the Franchise Tax Board concurs, is an employee is not absent from work once he reaches retirement age. Internal Revenue Code Regulation 1.105-(a)(3)(i). Retirement age is further defined in the federal regulations to be the earliest age at which an employee may retire without disability and without consent of his employer and yet receive immediate retirement benefits computed at the full rate allowed by the retirement plan or plan benefits proportionate to completed service. Internal Revenue Code Regulation 1.79-2(b)(3)(i). Since a disabled policeman or fireman under the new Charter provisions receives the full service retirement benefit to which he is entitled once he qualifies for service retirement, the benefits thereafter paid to him are not eligible for the sick pay exclusion. Two federal cases have held invalid the federal regulation (Regs. 1.105-4(a)(3)(i)) which denies the sick pay exclusion to disability retirement benefits payable after the employee qualifies for service retirement (assuming the employee would have worked but for his disability). Brooks v. United States, 473 Fed.2d 829 (CA-6, 1973) affirming 339 Fed. Supp. 1031; Walsh v. United States, 322 Fed. Supp. 613 (1970). Though recognizing this contrary authority exists, the Franchise Tax Board will continue to concur with the position of the Internal Revenue Service, at least until a greater weight of authority determines the federal regulation invalid or the regulation itself is changed. Accordingly, until such time, retirement benefits payable to disabled San Francisco policemen and firemen, after such personnel has qualified for service retirement under the new Charter provisions, are not excludable from gross income under the sick pay formula contained in Revenue and Taxation Code Section 17139(d).