TAX APPEAL BOARD OF THE STATE OF DELAWARE

Neale A. and Jacqueline B. Gow,
Petitioners,

v.

Director of Revenue,
Respondent.

DOCKET NO. 835

Before: Joseph S. Yucht, Esquire, Chairman; John H. Cordrey, Esquire, Vice Chairman; Harry B. Roberts, David Eppes and Regina Dudziec, Members.

Jerome K. Grossman, Esquire of Bayard, Handelman & Murdoch, P.A. for Petitioners.

Joseph Patrick Hurley, Jr., Esquire, Deputy Attorney General for Respondent.

DECISION

John H. Cordrey, Esquire, Vice Chairman. The Board decided that the lump sum payment received by Petitioners, out-of-state residents, from E.I. duPont deNemours & Company ("duPont") pursuant to a voluntary termination incentive program ("VTI") was not taxable in Delaware. The basis for the Board's decision was that the payment was not "for personal services (i) rendered in this State, or (ii) attributable to employment in this State and not required to be performed elsewhere." 30 Del. C. Section 1122(b)(1). The matter was appealed to the Superior Court and the Honorable Bernard Balick reversed the Board stating: "The act of retiring

was a personal service required in return for the payment."

The Board did not rule on Petitioner's argument that a portion of the VTI payment should be excluded from Delaware taxation as the Board held the payment was not taxable. The Superior Court, therefore, remanded the case to the Board for determination of whether some portion of the payment should be excluded. This is the Board's decision on remand.

Judge Balick's decision states that Petitioner's act of retiring was a personal service required in return for the payment. Petitioner has placed no evidence in the record through which this Board may find that the act of retirement was not rendered in this State. The Board must therefore find that the service was rendered in this State as Petitioner has the burden of proof to show the income should not be taxed and has failed to meet that burden.

As the VTI payment is subject to taxation, the next inquiry is whether some portion should be excluded under 30 Del.C. Section 1122 (f). That provision permits allocation and apportionment of income and deductions under rules prescribed by the State Tax Commissioner.

Tax Ruling 82-7 provides in pertinent part:

> The voluntary termination incentive payments may be included in the formula used for determining the portion of taxable wages which are subject to apportionment for days worked out of the state during the last year of employment.

Thus, following the Ruling, Petitioner should include the VTI payment in his Delaware taxable income for the year in which he received the payment (1983) at the percentage established during his last year of employment (1982).

The Delaware Supreme Court has held in Burpulis v. Director of Revenue, Del. Supr., 498 A.2d 1082 (1985) that regulations issued with

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Jerome K. Grossman, Esquire of Bayard, Hendelman & Murdoch, P.A. for Petitioners.

Joseph Patrick Hurley, Jr., Esquire, Deputy Attorney General for Respondent.

DECISION AND ORDER

John H. Cordrey, Esquire, Vice Chairman. The parties have stipulated to the facts of the case. They are contained in the stipulation which is attached hereto as "Exhibit A", and an affidavit of Jerome K. Grossman, which was admitted at Oral Argument pursuant to consent of Respondent's attorney and attached hereto as "Exhibit B", and both incorporated herein by reference. A brief summary of the facts show that Petitioner, Neale A. Gow, was an out of state resident who received a lump sum payment from E. I. duPont de Nemours & Company, hereinafter ("DuPont"), pursuant to a voluntary termination incentive program (hereinafter "VTI") instituted at Petitioner's Delaware office.

The sole question presented to the Board is whether the VTI payment is taxable in Delaware pursuant to 30 Del. C. §1122 (b)(1). That statute provides:

(b) Income and deductions having source within this State. -- Items of income, gain, loss and deduction derived from, or connected with, sources within this State are those items attributable to:

(1) Compensation, other than pensions, as an employee in the conduct of the business of an employer, for personal services (i) rendered in this State, or (ii) attributable to employment in this State and not required to be performed elsewhere;

Petitioners assert that the VTI payment constitutes a pension as that term is used in §1122 (b). The parties have stipulated that a definition of "Pension" is not found in the Delaware Code. The parties have also stipulated that the VTI payments are not a "qualified retirement plan" under section 401(a) of the Internal Revenue Code of 1954, but are paid pursuant to an "employee welfare benefit plan" as that term is defined in the Employee Retirement Income Security Act of 1974 (hereinafter "ERISA").

The Division of Revenue has promulgated Tax Ruling 82-7 which provides that VTI payments "... do not constitute and cannot be considered the equivalent of pension income ..." The Division of Revenue is permitted to make regulations, so long as the regulations are consistent with Title 30 of the Delaware Code, which interpret tax statutes. There is nothing inconsistent with Title 30 Tax Ruling 82-7 in the determination of that the VTI payment is not a pension, therefore it is controlling. Burpulis v. Director of Revenue, Del. Supr. 498 A.2d 1082 (1985).

Even in the absence of Tax Ruling 82-7, the Board would hold that VTI payments are not pension income. The VTI payments do not meet the dictionary definition of "pension" cited by Respondent. The VTI payment was instituted to provide "...

employees with an incentive to retire early ..." Factual Stipulation 13. This is not the purpose generally underlying a pension.

The next issue is whether the VTI payments are "... compensation ... as an employee in the conduct of the business of an employer, ..." 30 Del. C. §112(b)(1).

Neither party contends that the VTI payments are not "compensation." Petitioners contend that the compensation was not received "as an employee" because the VTI payments were made after Mr. Gow had ceased being an employee of DuPont. Petitioners agrue "as" means "while, when" and thus the payments (compensation) were not made while (as) Mr. Gow was an employee, and therefore are not included in his Delaware income.

If the Board were to accept Petitioners' logic, all sums received by a non-resident after terminating the employment with a Delaware employer would not be taxable. An employee who is fired on Wednesday and receives his paycheck, for his wages previously earned, on the following Friday would not be subject to tax on those wages since he was not an employee "when" he received his salary payment.

Clearly this is not what the Legislature intended. The more logical meaning of "as an employee", in the context of this statute, is "in the capacity, character, condition, or role of an employee." See Websters New Collegiate Dictionary.

For the foregoing reasons we hold that the VTI payment is compensation, other than pensions, as an employee. The sole issue remaining is whether the payment is "... for personal services (i) rendered in this State, or (ii) attributable to employment in this State and not required to be performed

elsewhere." §1122(b)(1)

The Division of Revenue cites numerous cases in which it has been held, in various contexts, that payments for cancellation of a right or refraining from activities is taxable or ordinary income.

Whether or not the payments are income is not the questions; the question is whether the payments are for personal services. Respondent quotes from Salvage v. Comm., 2nd Cir., 76F.2d 112 (1935) and states "compensation paid for refraining from labor would seem to be taxable income no less than compensation for services to be performed." This quotation points out that refraining from labor is not the same as performing services. It is without question that compensation for performing services and refraining from labor are taxable under the Federal tax laws.

Delaware, on the other hand, provides that a non-resident should be taxed only for compensation received for personal services rendered in Delaware. Respondent's contention that the VTI payments are "income" is, therefore, correct but immaterial.

At oral argument, counsel for Respondent answered the question of what personal services were rendered in Delaware by Petitioner by stating: "The services that were rendered in Delaware were the election to retire, which is part of the employment agreement, the continuation of employment from the date of election to the date of termination. That's all." The facts stipulated in this case make no mention of where the election to retire (Delaware or some other state) was made. Even if it were assumed that the election was made in Delaware,

the election to retire is not the personal service which resulted in the VTI payment. Mr. Gow refraining from working for DuPont is what caused him to receive the payment. The non-rendering of personal services for DuPont, in Delaware or elsewhere, is the underlying reason for the payment.

Continuing employment after the election is not personal service which brings this payment within the realm of §1122. It has been conceded that Mr. Gow continued to receive his normal compensation for the services he performed. Respondent would have this Board find that had DuPont required cessation of work at the same moment that the employee made the election this would be different from the instant case. Instead, the Board finds that Mr. Gow's short term employment after the election was made was not a personal service for which he was compensated with the VTI payment.

Thus there are no personal services rendered by Petitioner for which he was compensated by the VTI payment. §1122(b)(1) requires the compensation paid to a non-resident be for personal services rendered in this State to be taxable in Delaware. As this material element is missing, Petitioners' VTI payment is not included as Delaware taxable income.

The Division has promulgated Tax Ruling 82-7 concerning VTI payments and the regulation provides that the payments are taxable to non-residents. Burpulis, supra, requires that a regulation, when issued with proper authority, be entitled to the force and effect of law of long as it is consistent with Title 30 of the Delaware Code.

Neither party has suggested that Tax Ruling 82-7 was issued without requisite authority. Petitioners contends that the portion of the regulation which holds a VTI payment is compensation for personal services rendered in Delaware is inconsistent with Title 30, and we agree.

The ruling starts by comparing the payments to "severence pay." Even if the two were equivalent, the ruling fails to explain the personal services rendered in this State. The Ruling either overlooks the requirement of (i) or (ii) of §1122(b)(1) or states that the "payments are for services rendered currently" without even the slightest hint of the rationale behind the conclusion.

In light of the previous discussion concerning the requirement that the compensation be for personal services and relate to either (i) or (ii) of §1122(b)(1) to be taxable in the instant case; we find that Tax Ruling 82-7 is inconsistent with Title 30 to the extent that it holds that the VTI payments are for personal services rendered in this State or attributable to employment in this State and not required to be performed elsewhere.

In light of our holding, it is unnecessary to address Petitioners' alternative argument that only a portion of the VTI payment should be included in the Petitioners Delaware taxable income.

For the foregoing reasons the Notice of Assessment issued by the Director of Revenue in the instant matter is reversed.

IT IS SO ORDERED.

John N. Cordrey

Joseph S. Yuchs

Harry B. Reid

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