**No. 17-1042**

IN THE
# Supreme Court of the United States

BNSF RAILWAY COMPANY,

*Petitioner,*

V.

MICHAEL D. LOOS,

*Respondent.*

**On Petition For A Writ of Certiorari To The United States Court of Appeals for the Eighth Circuit**

## REPLY BRIEF FOR PETITIONER


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## CORPORATE DISCLOSURE STATEMENT

The corporate disclosure statement contained in the petition for a writ of certiorari remains accurate.

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## REPLY BRIEF FOR PETITIONER

Petitioner BNSF has asked this Court to consider the question whether a railroad's payment to an employee for time lost from work is subject to tax under the Railroad Retirement Tax Act. The Act defines taxable compensation as "any form of money remuneration paid to an individual for services rendered as an employee to one or more employers." 26 U.S.C. § 3231(e). The Internal Revenue Service has interpreted the statutory language to include "amounts paid for an identifiable period during which the employee is absent from the active service of the employer . . . as well as pay for time lost." 26 C.F.R. § 31.3231(e)-1(a)(3)-(4). The Eighth Circuit acknowledged that "[u]nder this regulation, damages for lost wages fit within the definition of 'compensation.'" (App. 19a.) However, the Eighth Circuit found that "the RRTA is unambiguous" and rejected the IRS's interpretation. (App. 24a.)

BNSF's petition demonstrated that the Eighth Circuit's decision conflicts with the decision of the Sixth Circuit in *Hance v. Norfolk Southern*, 571 F.3d 511 (6th Cir. 2009), and that three state supreme courts within the Eighth Circuit have also reached decisions that conflict with each other on the same point. (Pet. 2-3, 20-21.) This conflict places BNSF and other railroads in an untenable position: tax liabilities are different in state and federal courts in the same geographic location. As Respondent recognizes, the tax liability can be significant. (Opp. 16.) This differential tax treatment opens the door to forum-shopping. The railroad industry has a significant interest in the uniform administration of

these federal tax laws. Only this Court can resolve this multi-faceted division of authority.

## I. The Decision Below Deepens The Conflict Over RRTA Taxation Of Lost Wages

Respondent does not dispute that the Eighth Circuit's decision enhances a conflict among the appellate courts. He acknowledges that "four State courts have reached different conclusions on RRTA taxation of FELA judgments …." (Opp. 7.) On one side are the Supreme Court of Nebraska, the Supreme Court of Iowa, and the Pennsylvania intermediate court. As Respondent admits, these three courts "concluded that FELA judgments are taxable" under the RRTA. (Opp. 8.) The fourth court is the "Missouri Supreme Court, which concluded FELA judgments are not taxable." (Opp. 7.) The Eighth Circuit similarly held that damages for lost wages are not taxable. (App. 24a.) Respondent agrees that "the question of whether FELA satisfactions are subject to RRTA taxes is certainly important …." (Opp. 7.)

In light of these admissions, it appears that all parties agree that the criteria for this Court's review are present in this case. There is a conflict involving a federal circuit court and the highest courts of three States on an important matter. *See* Rule 10(a). The Association of American Railroads explains that the issue presented "has implications beyond FELA time lost awards." (AAR Amicus Br. 3) The Eighth Circuit's reasoning creates serious doubt as to the taxability of other forms of time-lost payments such as severance pay, vacation pay, holiday pay, and sick

pay. In 2016 alone, the railroads paid out at least $1.9 billion in such benefits, which were subject to railroad retirement taxes. (*Id.* at 12.) Respondent does not disagree.

Respondent nevertheless contends that the Court should deny review because the Missouri Supreme Court's reasoning "is more thorough …." (Opp. 7.) This statement simply reflects Respondent's skewed view of the merits, not a dissolution of the conflict. Courts in Nebraska and Iowa remain bound by those rulings of their state supreme courts. Review by this Court is needed to resolve the conflict in the courts on this important issue.

The decision below also creates a conflict among the federal circuit courts. The Sixth Circuit held that the railroad "will be required to report and pay" employment taxes on that award because the RRTA and its accompanying regulations cover "all 'compensation' to employees, including payment 'for time lost.'" *Hance*, 571 F.3d at 523. The Eighth Circuit reached the opposite conclusion and held that time-lost damages are not taxable under the RRTA. (App. 24a.) Respondent tries to avoid the circuit conflict by reframing the issue presented, limiting its scope to FELA awards. (Opp. i, 6.) But the specific claim underlying the award of lost wages –the FELA claim – had no bearing on the Eighth Circuit's resolution of the legal issue. (App. 20a-24a.) And despite Respondent's contrary contention (Opp. 6-7),

the federal district courts are also divided on this issue.[1]

The petition also pointed out that the reasoning of the Eighth Circuit – that the "plain text" of the RRTA refers only to "services that an employee actually renders" (App. 20a) – was inconsistent with the reasoning of two of this Court's opinions. Pet. 25-26, *citing Soc. Sec. Bd. v. Nierotko*, 327 U.S. 358, 365-66 (1946); *United States v. Quality Stores, Inc.*, 134 S. Ct. 1395, 1400 (2014)). Respondent points to immaterial factual distinctions in those cases but does not dispute the legal principle established by them:

> We think that "service" as used by Congress in this definitive phrase means not only work actually done but the entire employer-employee relationship for which

[1] *See Larson v. Wisconsin Central, Ltd.*, No. 10-C-446, 2012 WL 359665, at *2 (E.D. Wis. Feb. 2, 2012) ("The employer railroad must withhold applicable Tier 1 and Tier 2 taxes and the employee's Medicare tax obligations from payment of any judgment."); *Cheetham v. CSX Transp.*, No 06-cv-704, 2012 WL 1424168 (M.D. Fla. Feb. 13, 2012) (awards for lost wages under the Family Medical Leave Act are subject to withholding under the RRTA); *see also Windom v. Norfolk So. Ry.*, No. 10-407, 2012 WL 6096990, at *2 (M.D. Ga. Dec. 9, 2012) (stating that the railroad "might have a plausible argument for a set off" if it could show that it paid or would have to pay the taxes).

> compensation is paid to the employee by the employer.

*Nierotko*, 327 U.S. at 365-66. Thus, the reasoning of the Eighth Circuit's opinion, with its narrow focus on the performance of actual services in determining whether "compensation" was received, is contrary to this Court's precedent.

## II. Respondent's Faulty Arguments on the Merits Confirm that Review is Warranted

Perhaps most telling in Respondent's opposition brief is what it does not do: defend the court of appeals' decision on its own terms. The Eighth Circuit held that "damages for lost wages did not fit within the plain meaning of the RRTA." (App. 20a.) Conspicuously absent from the opposition brief is any defense of the Eighth Circuit's holding or actual reasoning. Instead, Respondent offers a series of rationales that no court has ever accepted despite the significant body of case law that has accumulated in this area. In fact, many of the arguments raised in the opposition brief were either not raised by Respondent in the litigation below or were rejected by the Eighth Circuit. Respondent's failure to defend the rationale of the decision below is a sign that certiorari is warranted.

For example, Respondent claims that "the IRS itself" has never "issued any regulation or guidance" on this issue. (Opp. 9.) He is wrong on both counts. The IRS's regulation defines compensation to include "pay for time lost." 26 C.F.R. § 31.3231(e)-1(a)(3)-(4). As the Eighth Circuit explained in this case, damages for lost wages "fit well within" the scope of

this regulation. (App. 19a.) Moreover, in a 1980 Technical Advice Memorandum, the IRS set forth its position that the railroad was required to withhold RRTA taxes from lost damages awarded in a FELA case.[2] The IRS concluded: "We therefore believe the payment received by the [railroad] employee for loss of earnings can reasonably be described as compensation for time lost and comes within the definition of compensation for RRTA purposes." IRS Technical Advice Memorandum, 1980 WL 137627. Thus, the IRS has issued both a regulation and additional guidance on the question presented here.

Respondent also argues that juries typically award in FELA cases only net, take-home wages. (Opp. 15.) The case that he cites – *Norfolk & W. Ry. Co. v. Liepelt*, 444 U.S. 490 (1980) – deals only with federal *income* taxes. RRTA taxes are separate taxes and fundamentally different than federal income taxes. *See CSX Transp., Inc. v. Miller*, 46 So.3d 434, 460 (Ala. 2010). Thus, the jury's instruction in this case was specifically limited to *income* taxes: "The Respondent will not be required to pay any federal or state income taxes on an amount that you award." (Dist. Ct. ECF No. 125 at 24.) There is no basis to conclude that the jury deducted RRTA taxes from the

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[2] *See* IRS Technical Advice Memorandum (TAM) 8115012; 1980 WL 137627 (Dec. 18, 1980). While TAMs have no precedential force, they are a useful as an indication of the IRS's position and may be viewed as substantial authority by a court. *See, e.g., Rowan Cos. v. United States*, 452 U.S. 247, 262 n.17 (1981).

award in this case. The jury awarded $30,000 in past lost wages for a 5-month period in 2011. This amount was *more than* Respondent's net wages *for the entire year* in 2010. Thus, Respondent never claimed in the litigation below – either in the post-trial papers or in the Eighth Circuit – that the jury had already deducted RRTA taxes from its award of lost wages.

Respondent asserts for the first time in his opposition brief that no RRTA taxes are owed because he was "not a BNSF employee when BNSF partially satisfied the judgment." (Opp. 6.) This is immaterial. There is no requirement that the employment relationship still exist at the time the judgment is entered or the payment is made. *See* 26 U.S.C. §3231(e)(1); *Jacques v. United States R.R. Retirement Bd.*, 736 F.2d 34, 39-41 (2d Cir. 1984). It is undisputed that the jury awarded lost damages to Respondent for the period of time in which he *was* employed by BNSF – December 19, 2010 to May 16, 2011. (App. 4a.)

Respondent emphasizes that the employee should be able to decide whether his award for lost damages gets taxed. (Opp. 15.) Under the RRTA, however, the employee does not unilaterally control the imposition of employment taxes. The railroad is required to withhold taxes on "all 'compensation' to employees" – regardless of whether the employee asks for the retirement benefits. *Hance*, 571 F.3d at

523; 26 U.S.C. §3231(e)(1).[3] The IRS rejected a similar argument in the 1980 Technical Advice Memorandum. *TAM*, 1980 WL 137627 (explaining that, once the jury awarded a specific amount of lost wages, the employee cannot later try to apportion the amounts differently). The RRTA's legislative history shows that the employee union's representative was aware that taxes would be imposed on "pay for time lost" but favored this definition anyway because it would "increase the creditable months of service of railroad workers."[4] Giving the same meaning to "compensation" under the RRTA and the RRA provides harmony and stability by ensuring adequate funding for the very retirement benefits the employees will receive. *See Hance v. Norfolk S. Ry. Co.*, 571 F.3d at 542; *Liberatore v. Monongahela Ry. Co.*, 140 A.3d 16, 29-30 (Pa. Sup. Ct. 2016).

Respondent seeks to discourage certiorari by mentioning a statutory provision that the court of appeals did *not* invoke. He argues that, even if lost damages fit within the definition of compensation,

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[3] When BNSF reported the payment of lost wages in this case to the federal agencies, the Railroad Retirement Board gave Respondent additional credit towards his retirement benefits. (Dist. Ct. ECF No. 162 at 9.)

[4] *Railroad Retirement, Hearings on S. 293 before the Senate Committee on Interstate Commerce*, 79th Cong. 1st Sess. at 390 (July 23-26, 1945) (Statement by Murray W. Latimer on behalf of the Railway Labor Executives Association).

they are excludable under 26 U.S.C. § 104(a)(2). (Opp. 13.) This is incorrect. Section 104 provides an *income* tax exclusion. It creates an exemption for personal injury awards from "gross income," which is used in computing income tax. 26 U.S.C. § 61. It thus pertains to a different statutory definition ("gross income") for purposes of a different tax (income tax). The exclusion in Section 104(a) is not part of the RRTA. Railroad retirement taxes are based on "compensation" as that term is defined in the RRTA. 26 U.S.C. §§ 3201, 3202(a), 3231(e).[5]

The IRS has consistently recognized that federal income taxes and RRTA taxes apply differently to personal jury awards. It held in two Revenue Rulings that the exemption in Section 104 has no bearing on the RRTA tax treatment for time lost.[6] It

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[5] When Congress wanted to incorporate exclusions from income taxes into the RRTA and thereby make them exclusions from RRTA taxes, it did so expressly. *See, e.g.*, 26 U.S.C. §§ 3231(e)(10) – (11). However, Congress did not designate Section 104 as an exclusion that would apply to the RRTA's definition of compensation.

[6] *See* Rev. Rul. 61-1, 1961-1 C.V. 14, 1996 WL 12630 (Jan. 1961) ("The fact that in this case 'time lost payments' constitute compensation for the purposes of taxes imposed by the Railroad Retirement Tax Act is not controlling for Federal income tax purposes."); Rev. Rul. 85-97, 1985-2 C.B. 5, 1985 WL 287177 (July 1985) (explaining that Revenue Ruling 61-1 "states that the fact that the 'time lost payments' constituted compensation for purposes of the taxes imposed by the Railroad Retirement

(Continued …)

also held in a Technical Advice Memorandum that Section 104 exempts a FELA award for lost wages from federal income taxes but that it does *not* exempt that same award from RRTA taxes. *TAM*, 1980 WL 137627. Thus, the IRS's consistent and longstanding views on this issue would be entitled to deference. *See Liberatore v. Monongahela Ry. Co.*, 140 A.3d at 29-30.

Railroad retirement taxes are significant to railroads and their employees. Here, for example, the amount of RRTA taxes owed by Respondent in each year from 2005 to 2012 was *greater* than the amount of federal taxes withheld. And this is just a start. As Respondent acknowledges, "While in this case Loos would suffer a discount of only $3,765, in cases with larger damages awards the consequences are more severe. *Loy*, for example, concerned a $29,247.25 tax liability." (Opp. 16.) This is more than enough to provide an incentive for forum-shopping and certainly enough to be perceived as unfair discrimination between taxpayers in different fora.

In short, review is warranted. The parade of empty merits arguments in the opposition brief only highlights the problematic nature of the Eighth Circuit's decision and the need for a definitive resolution.

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Tax Act does not preclude the application of the exclusion from gross income under section 104(a)(2)").

## III. This Is An Ideal Vehicle To Address the Exceptionally Important Issue

This case is the ideal vehicle to resolve the conflict for three reasons. First, the factual predicate is clear: a special verdict confirms the exact amount of pay for time lost. Respondent seeks to raise questions about whether he "request[ed]" an award. (Opp. 10.) It is not apparent why a request is necessary, but it is clear that Respondent asked a jury to award him with pay for lost time, and the jury did so.

Second, the legal predicate is clear. The IRS regulation defines compensation as including "pay for time lost." 26 C.F.R.§31.3231(e)-1(a)(4) (App. 46a-47a.) Respondent points out that an additional regulation elaborating on "items included as compensation" stated that it included "a payment . . . made to an employee with respect to a personal injury." (Opp. 9.) But there is nothing indicating that the deletion of this example was intended to narrow the scope of the IRS regulation, which on its face continues to include amounts paid to an employee that is absent from active service.

Third, the agency position is clear. The Eighth Circuit, in its opinion in this case, acknowledged that this judgment fell within the agency regulation: "Under this regulation, damages for lost wages fit well within the definition of 'compensation.'" App. 19a. The IRS has repeatedly filed amicus briefs confirming that FELA judgments reflecting damages for time lost fall within the regulation. (Pet. 32 n.13.)

The Railroad Retirement Board has made the same point. The publication cited by respondent (Opp. 14 n.8) says: "The employee's portion of the railroad retirement tax liability is usually withheld from the gross amount of the award." *Railroad Retirement Service Credits and Pay for Time Lost* (May 2008). Another publication available on the Railroad Retirement Board website, explains: "Examples of pay for time lost include . . . [a] personal injury award or settlement which allocates a portion of the damages as lost wages for a specific period following the date of the injury." Form IB-4 (03-17) Pay for Time Lost from Regular Railroad Employment at 4 (available at https://www.rrb.gov/Benefits/IB-4). It contains an entire section entitled, "HOW IS PAY FOR TIME LOST ALLOCATED WHEN THERE IS A COURT ORDERED JUDGMENT?" *Id.* at 9. There is no doubt that the agency regulations and guidance on pay for time lost apply to "satisfactions of judgments" as well as to settlements.

This Court should end the endless battles in the federal and state courts over the taxation of FELA and other pay-for-time-lost awards.

## CONCLUSION

This Court should grant the petition for certiorari.

Respectfully submitted,

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