

**Occupational Safety and Health Administration
Directorate of Whistleblower Protection Programs (DWPP)
Taxability of Settlements Desk Aid**

Disclaimer:

This Desk Aid is intended to provide general background information for OSHA personnel regarding the potential tax treatment of payments in whistleblower settlements as of the last updated date below. This desk aid is solely for the benefit of the Government. No duties, rights, or benefits, substantive or procedural, are created or implied by this Desk Aid and its contents are not enforceable by any person or entity against the Department of Labor or the United States. This Desk Aid is based on IRS guidance that is non-precedential and subject to change and is not a substitute for parties seeking advice from their own tax adviser.

Recommended practices:

- OSHA should inform parties that OSHA cannot provide complainants or respondents with individual tax advice and that the parties are themselves responsible for compliance with Internal Revenue Code, case law, and guidance and may need to seek advice from their own tax adviser.
- OSHA can talk with parties generally about potential taxability of settlements, including (1) the possibility of employer withholding applicable taxes if settlement is for wages and (2) the parties' responsibility to report and pay any applicable taxes on settlement amounts.
- OSHA can try to ensure that the settlement agreement expressly states the allocation of payment between wages and other amounts if there are multiple claims or damages. This will help determine the taxability of settlement amounts later if it becomes an issue.

Type of Payment	Gross Income?	Wages?	Reporting Requirement
Lost Compensation <i>Back pay (including bonuses, overtime, & benefits), front pay, or severance pay</i>	Yes	Yes	<ul style="list-style-type: none"> - Respondent should report income with applicable payroll taxes and withholdings deducted. - Respondent should generally provide complainant with a W-2. - Complainant should report as "Wages, salaries, tips, etc."
Attorney's Fee <i>Amounts awarded to complainant for legal services</i>	Yes (however, amount may be deductible)	No	<ul style="list-style-type: none"> - Generally regardless of whether payment is made directly to the attorney, attorney's fees are considered to belong to complainant and are considered income. - Where the settlement provides a clear allocation attorney's fees: <ul style="list-style-type: none"> • Attorney's fees are not considered wages, respondent should provide complainant and attorney with a 1099-MISC, and complainant should report as "Other Income." - Where the settlement DOES NOT provide a clear allocation of attorneys' fees: <ul style="list-style-type: none"> • Attorney's fees are considered wages. Respondent should provide W-2 to complainant and may need to provide 1099-MISC to attorney. • Complainant should report as "Wages, salaries, tips, etc."
Punitive Damages <i>Damages awarded to complainant to punish the respondent</i>	Yes	No	<ul style="list-style-type: none"> - Complainant responsible for reporting income and paying any applicable taxes - Even if awarded in connection with settlement payments for physical injuries and physical sickness, punitive damages are not excluded from gross income. - Respondent should provide complainant and attorney with 1099-MISC. - Complainant should report as "Other Income."
Emotional Distress/Pain and Suffering <i>Damages awarded to complainant for mental distress</i>	Yes - with exceptions	No	<ul style="list-style-type: none"> - Complainant responsible for reporting income and paying any applicable taxes (though taxable amount reduced by amount spent on medical care attributable to emotional distress) - Respondent should provide complainant with a 1099-MISC. - Complainant should report as "Other Income." - Exceptions. Not taxable if: <ol style="list-style-type: none"> 1) damages are caused by a physical injury or sickness and, 2) damages do not exceed payments made for medical care attributable to emotional distress.
Physical Injury <i>Damages awarded to complainant for observable or documented bodily harm</i>	No - with exceptions	No	<ul style="list-style-type: none"> - Not taxable to the extent that amount is reimbursement for medical expenses. - Exception. Taxable if complainant already deducted medical expenses in prior years (report as "Other Income").

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Interest	Yes	No	- Respondent should provide complainant a 1099-INT (report as “Interested Income”) if interest exceeds a threshold amount. As of 9/29/2015 that amount is \$600.
Lump Sum <i>Not recommended. Agreements should indicate allocation of compensation.</i>	Yes	Yes	<ul style="list-style-type: none"> - If lump sum is not allocated between lost compensation and other amounts, IRS may regard the settlement amount as lost compensation. - Both complainant and respondent could suffer negative tax consequences if IRS believes settlement amount should have been regarded as wages and was misclassified.

Last Updated September 30, 2015