

810-3-19.1-.01 Severance Pay Exemption. (Amended)

(1) DEFINITIONS. The following terms have these meanings for the purposes of this rule:

(a) Administrative Downsizing. A reduction in the employer's workforce or discontinuance or relocation of the operations of the employer in accordance with a business plan. Administrative downsizing does not include:

1. The transfer or exchange of employees between related taxpayers as described in 26 U.S.C. §267.

2. The transfer or exchange of employees to another legal entity with such employees continuing to perform essentially the same or related duties for the former employer.

(b) Displaced from Employment. Termination of the employer/employee relationship due to an employee's job being abolished or relocated.

(c) Employee. A common law or statutory employee as defined by the Internal Revenue Code.

(2) Severance Pay Qualification. To qualify for the exemption, the payment must be:

(a) Received pursuant to a plan of administrative downsizing which has been submitted to and approved by the department

(b) Received from the employer under the following conditions.

1. As severance pay, unemployment compensation, termination pay, or from a supplemental income plan.

2. By an employee who is terminated, laid off, fired, or displaced from employment.

3. As a result of administrative downsizing.

(3) Exemption Allowed by Tax Year.

(a) For tax years beginning January 1, 2020, the exemption is limited to the first fifty thousand dollars (\$50,000) severance pay received in each tax year for each displaced worker.

(b) For tax periods beginning on or after January 1, 1997 through December 31, 2019, the exemption is limited to the first twenty-five thousand dollars (\$25,000) received in any year for each displaced worker.

(c) Severance pay, whether paid as a lump sum or in installments, granted prior to January 1, 1997, is not exempt from Alabama individual income taxation.

(4) Alabama income tax withholding requirements for the employer do not apply to payments exempted under this section if the employer has obtained exemption approval from the department.

(5) Qualifying Payments. If all other requirements of this section are met, qualifying payments for this exclusion include but are not limited to:

(a) Certain union benefits.

(b) Certain payments received from voluntary employee's beneficiary associations.

(c) Certain payments to laid-off employees from company-financed, supplemental unemployment compensation benefit plans, also known as "guaranteed annual wage plans".

(6) Non-qualifying Payments. Payments made to employees not qualifying for this exemption include but are not limited to:

(a) Payments made for accumulated sick leave, annual leave, vacation time, or unused benefits unless only offered as an incentive or inducement for early retirement.

(b) Cancellation of contract payments made to independent contractors or others not deemed to be employees of the payor.

(c) "Parachute payments" or any other payments made due to termination of employment for any reason other than administrative downsizing.

(d) Retirement benefits received as a result of a voluntary retirement due to administrative downsizing.

(e) Payments made by the employer in compensation for services (previous or future), repurchase, redemption, or retirement of stock or similar equity interests, or any interest therein or option thereto, or in consideration of a non-compete agreement, contractual or legal claim.

(7) Exemption of a payment from income taxes is allowed only when the substance of the transaction fairly meets the requirements of this rule and the statute. The form of the transaction is usually unimportant.

(8) Application for Exemption Approval Required by Employers. Employers must apply for approval of the exemption by submitting a written request to the department. In the request, employers must submit their plan for administrative downsizing that includes, but is not limited to:

- (a) A complete description of the benefits paid to the displaced employee(s).
- (b) A complete description of the downsizing plan itself, that includes, but is not limited to:
 - 1. The number and description of employees affected.
 - 2. The reasons for administrative downsizing.
- (c) The aggregate amount of benefits to be paid to affected employees which will be exempt from Alabama individual income taxation.
- (d) The request must be filed at least annually if the administrative downsizing plan continues into the next year.

(9) Termination due to Misconduct. Notwithstanding anything to the contrary herein, neither the employer nor the employee is exempted from the income tax withholding requirements if the employee was terminated, fired, or constructively fired through voluntary resignation due to misconduct. Likewise, employees who were terminated, fired, or constructively fired through voluntary resignation due to misconduct are not allowed to take the tax exemption on their income tax return.

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