2002

United States v. Cleveland Indians: FICA and FUTA Taxes v. The Social Security Act - Why Have Different Definitions For Identical Language?

Jeffrey C. Honaker

UNITED STATES V. CLEVELAND INDIANS:[1] FICA AND FUTA TAXES V. THE SOCIAL SECURITY ACT – WHY HAVE DIFFERENT DEFINITIONS FOR IDENTICAL LANGUAGE?

"The nation should have a tax system that looks like someone designed it on purpose."

William Simon[2]

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1. 532 U.S. 200 (2001). Professional baseball was first played in Cleveland in 1869. Cleveland Indians Baseball Company Inc., *at* http://www.scripophily.net/clevin.html (last visited Feb. 21, 2002). In 1901 the Cleveland Spiders ball club became a charter member of the American League of Professional Baseball Clubs. *Id.* Cy Young played for Cleveland early in the 20th century. *Id.* The Indians (the team took that name in 1915 after trying out the Blues, Naps, and Molly McGuires) beat the Brooklyn Dodgers to win the 1920 World Series, topped the Boston Braves to take another World Series in 1948, and claimed the American League pennant in 1954. *Id.* A major slump followed, with player performance, fan attendance, and club finances suffering through most of the next three decades. *Id.* The 1960s and 1970s brought multiple ownership changes, as well as rumors that the struggling team would move to Seattle or New Orleans, among other cities. *Id.* Real estate tycoon Richard Jacobs and his brother David paid $35 million for the Indians in 1986. *Id.* By aggressively recruiting coaches, talented young players, and management, Jacobs steered the organization back to the top ranks of baseball. *Id.* Instead of spending money on skyrocketing player salaries, he invested in the team's farm system which nurtured young players. *Id.* Jacobs also made fan loyalty a priority by focusing marketing efforts on introducing fans to up-and-coming players and was instrumental in the development of Cleveland's downtown Gateway Sports and Entertainment Complex, which includes (the modestly named) Jacobs Field and Gund Arena, home of the Cleveland Cavaliers pro basketball franchise. *Id.* Jacobs Field was opened in 1994. *Id.* The team won the American League Central Division each year between 1995 and 1998, and made it to the World Series in 1995 and 1997 (losing to the Atlanta Braves and the Florida Marlins, respectively). *Id.* In 1998 the company raised $60 million in an IPO (but the team lost the pennant race that year to the New York Yankees). *Id.* The following year Jacobs struck while the iron was hot, announcing his intention to sell the team (The Tribe clinched its fifth consecutive AL Central title that year). *Id.* In early 2000 Lawrence Dolan, an attorney from Ohio, set a Major League Baseball record by paying $323 million for the franchise, which became private once again. *Id.*

2. The Quote Garden, Quotations About Taxes, *at* http://www.quotegarden.com/taxes.html (last visited Feb. 1, 2002). William Edward Simon served as the Secretary of the Treasury under Presidents Nixon and Ford. *William Simon – philanthropist, Nixon's treasury secretary – dead at 72*, CNN.com news *at* http://www.cnn.com/2000/ALLPOLITICS/stories/06/03/simon.obit.02/index.html (last visited Feb. 1, 2002). After leaving office, Simon, sometimes referred to as the "energy czar," returned to business where he was credited with developing the concept of a "leveraged buyout." *Id.*

I. INTRODUCTION

The Cleveland Indians were set to face off against the Internal Revenue Service in the 2001 World Series of Taxation.[3] This meeting would not be their first. The parties battled in both 1999[4] and 2000[5] where the Indians, almost effortlessly, disposed of the I.R.S.[6] This meeting, however, would be different for two reasons.

First, the umpires on the field this year would be the most respected umpires in the world – the Justices of the United States Supreme Court.[7] Second, due to the nature of this contest, there would be no "next season" for the defeated party.[8]

Nevertheless, Mr. Simon's greatest legacy may be his decision to give his estimated $350 million fortune to charities such as AIDS hospices and low-income educational organizations. *Id.* Mr. Simon passed away in 2000. *Id.*

3. *See Cleveland Indians*, 532 U.S. 200 (2001). Author's note: For those who are unfamiliar with baseball, this sentence draws an analogy between the Major League Baseball World Series and the Supreme Court of the United States. The MLB World Series is the grand finale of the MLB season, pitting the champions of the two respective MLB leagues against each other, playing for the title of World Series Champions, which is the ultimate goal of the MLB year. They are similar in the sense that the World Series is as far as a team can go in baseball and the Supreme Court is as far as a litigant can go in the U.S. legal system.

4. Cleveland Indians Baseball Co. v. United States, 1999 WL 72866 (N.D. Ohio Jan. 25, 1999). In this case, the United States District Court for the Northern District of Ohio relied upon the authority of *Bowman v. United States*, 824 F.2d 528 (6th Cir. 1987), *overruled in part by* 532 U.S. 200 (2001), to find for the Cleveland Indians, holding that a settlement for backwages should be allocated to the period where the wages were not paid as usual. *Id.* For greater analysis of this District Court case, see *infra* notes 63-70 and accompanying text. For analysis of the *Bowman* decision, see *infra* notes 35-39 and accompanying text.

5. Cleveland Indians Baseball Co. v. United States, 215 F.3d 1325, 2000 WL 659028 (6th Cir. May 10, 2000). Here, the Court of Appeals for the Sixth Circuit found itself bound by *Bowman v. United States*, 824 F.2d 528 (6th Cir. 1987), *overruled in part by* 532 U.S. 200 (2001), in finding that a settlement for backwages must be allocated to the period where the wages were not paid as usual. *Id.* For more on this Court of Appeals case, see *infra* notes 71-74 and accompanying text. For analysis of the *Bowman* decision, see *infra* notes 35-39 and accompanying text.

6. *See* discussion *infra* Parts III.B.2, III.B.3. The Cleveland Indians were able to dispose of the I.R.S. relatively "effortlessly" because the District Court and Court of Appeals for the Sixth Circuit determined themselves to be bound by Sixth Circuit precedent announced in *Bowman*. In *Bowman*, the Court of Appeals for the Sixth Circuit held that backpay should be allocated to the period in which it should have been paid. *Bowman*, 824 F.2d at 530. For a discussion of *Bowman* see *infra* notes 35-39 and accompanying text.

7. Continuing with the baseball analogy, in baseball, umpires play a role in baseball similar to the role judges play in the U.S. legal system. Both umpires and judges are charged with the duty to serve as impartial arbiters of an adversarial event. While judges enforce the laws of the land, umpires enforce the rules of Major League Baseball.

The Justices of the United States Supreme Court participating in the *Cleveland Indians* case are as follows: Justices Ginsburg (who delivered the opinion of the Court), Rehnquist (Chief Justice), Stevens, O'Connor, Kennedy, Souter, Thomas, Breyer, (all joining in the judgment) and Justice Scalia (who filed a concurring opinion). *Cleveland Indians*, 532 U.S. 200 (2001).

8. Authors note: This is where the World Series/Supreme Court analogy ends. The World

In each of these three years, the parties had argued over the timing of taxes assessed under the Federal Insurance Contribution Act (FICA) and the Federal Unemployment Tax Act (FUTA).[9] The Cleveland Indians took the position that FICA and FUTA taxes were calculated as of the year wages should have been paid.[10] The I.R.S. asserted that said taxes were taxed when the wages were actually paid.[11]

This Note examines the issue of whether FICA and FUTA taxes are assessed at the time wages should have been paid, or at the time the wages are actually paid.[12] Part II examines the background of this issue by parsing the applicable case law.[13] Part III contains a statement of the facts,[14] the procedural history,[15] and the United States Supreme Court's decision in *Cleveland Indians*.[16] Part IV analyzes the *Cleveland Indians* decision.[17]

Series is an annual event. Therefore, each team who does not win the World Series can at least prepare to try to win it next season. However, there may be no "next season" for an issue that has been fully considered and decided by the Supreme Court of the United States.

9. *Cleveland Indians,* 532 U.S. 200 (2001). *Id.* FICA is tax on both employees and employers, based on wages paid, used to fund Social Security and Medicare. *Id.* at 205. FUTA, taxes only employers, based on wages paid, and is used to fund unemployment benefits. *Id.* For full consideration of FICA *see infra* notes 18-24 and FUTA *see infra* notes 25-30.

10. *Id.* Allocating wages to the year they should have been paid would relieve the Cleveland Indians of any additional FICA or FUTA tax liability. *Cleveland Indians*, 532 U.S. at 206.

11. *Id.* Allocating the wages to the period when actually paid would subject the Cleveland Indians (and some of their former employees) to additional FICA and FUTA tax liability. *Id.*

12. *See infra* Parts II-III. The Supreme Court of the United States ultimately holds that FICA and FUTA taxes are assessed when actually paid. *Cleveland Indians*, 532 U.S. at 220.

13. *See infra* notes 18-50 and accompanying text. This section explains FICA and FUTA taxes and examines *Bowman v. United States*, 824 F.2d 528 (6th Cir. 1987), *overruled in part by* 532 U.S. 200 (2001), *Hemelt v. United States*, 122 F.3d 204 (4th Cir. 1997), and *Walker v. United States*, 202 F.3d 1290 (10th Cir. 2000), all of which figure into the analysis of either FICA, FUTA, or backpay in general.

14. *See infra* notes 51-59 and accompanying text. This section provides the backdrop to the *Cleveland Indians* litigation.

15. *See infra* notes 60-74 and accompanying text. This section follows the *Cleveland Indians* case from the district court to the Sixth Circuit Court of Appeals.

16. *See infra* notes 75-103 and accompanying text. This section provides insight to the Supreme Court's decision in *Cleveland Indians*.

17. *See infra* notes 104-198. This section examines the *Cleveland Indians* decision, offering concepts not discussed in the Supreme Court's opinion.

II. BACKGROUND

A. FICA[18]

FICA[19] imposes a tax upon both employees[20] and employers,[21]

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18. FICA taxes have generally not been the focus of popular culture. However, FICA humor has made its way into one popular television show, *Friends*, where a character (Rachel) demonstrates that many employees do not understand the FICA deduction. In one episode, Rachel receives her first ever paycheck and says: "God, isn't this exciting? I earned this. I wiped tables for it, I steamed milk for it, and it was totally - (OPENS ENVELOPE) -not worth it. Who's FICA? Why's he getting all my money? I mean, what – Chandler, look at that." Friends: The one with George Stephanopoulos (NBC television broadcast Oct. 13, 1994), http://epguides.com/friends/ (unofficial episode list) (last visited Feb. 22, 2002).

19. The full text of FICA is found at 26 U.S.C. §§ 3101-3128 (1994 & Supp. 1998).

20. 26 U.S.C. § 3101(a) (2001). "Employee" is defined at 26 U.S.C. § 3121(d) (2001), as follows:

> (d) Employee. For purposes of this chapter, the term "employee" means—
>
> (1) any officer of a corporation; or
>
> (2) any individual who, under the usual common law rules applicable in determining the employer-employee relationship, has the status of an employee; or
>
> (3) any individual (other than an individual who is an employee under paragraph (1) or (2)) who performs services for remuneration for any person—
>
> (A) as an agent-driver or commission-driver engaged in distributing meat products, vegetable products, fruit products, bakery products, beverages (other than milk), or laundry or dry-cleaning services, for his principal;
>
> (B) as a full-time life insurance salesman;
>
> (C) as a home worker performing work, according to specifications furnished by the person for whom the services are performed, on materials or goods furnished by such person which are required to be returned to such person or a person designated by him; or
>
> (D) as a traveling or city salesman, other than as an agent-driver or commission-driver, engaged upon a full-time basis in the solicitation on behalf of, and the transmission to, his principal (except for side-line sales activities on behalf of some other person) of orders from wholesalers, retailers, contractors, or operators of hotels, restaurants, or other similar establishments for merchandise for resale or supplies for use in their business operations; if the contract of service contemplates that substantially all of such services are to be performed personally by such individual; except that an individual shall not be included in the term "employee" under the provisions of this paragraph if such individual has a substantial investment in facilities used in connection with the performance of such services (other than in facilities for transportation), or if the services are in the nature of a single transaction not part of a continuing relationship with the person for whom the services are performed; or
>
> (4) any individual who performs services that are included under an agreement entered into pursuant to section 218 of the Social Security Act.

26 U.S.C. § 3121(d).

21. 26 U.S.C. § 3111(a) (2001). Although the FICA statute is replete with references to the term "employer," the act fails to define the term. Robyn L. Robinson, *A Discussion of the Application of FICA and FUTA to Indian Tribes' On-Reservation Activities*, 25 AM. INDIAN L. REV.

which is used to fund the federal social security program.[22] The dollar amount of the tax equals a percentage of the wages paid by the employer to the employee.[23] Before one is able to determine the amount of tax due in any year, it is important to know the tax year to which the wages are attributable.[24]

37, 39 (2000-2001).

22. FICA has been summarized as follows:

> The Federal Insurance Contribution Act (FICA) finances a Federal system of old age, survivors, disability, and hospital insurance that is generally referred to as social security and Medicare. Employers are required to withhold and pay social security and Medicare taxes for a private household employee, if $1,000 or more in cash wages are paid during a year. The law does not apply to a worker who is a spouse, a child under age 21 or a parent working in the home. There are exceptions to a parent working in the home which can be found in the instructions for filing Form 942. Earnings for household workers (such as baby sitters) under age 18 are exempt from the FICA unless household employment is the worker's primary occupation.
>
> After Social Security numbers were assigned during the New Deal, the first Federal Insurance Contributions Act (FICA) taxes were collected, beginning in January 1937. Special trust funds were created for these dedicated revenues. Benefits were then paid from the monies in the Social Security Trust Funds. As of 1997, more than $4.5 trillion has been paid into the Trust Funds, and more then $4.1 trillion has been paid out in benefits. The remainder is currently on reserve in the Trust Funds and will be used to pay future benefits.
>
> For 1997, the social security tax is 6.2% for both the employer and the employee (12.4% total). This applies to the first $65,400 paid to the employee. The Medicare tax is 1.45% for both the employer and the employee (2.9% total). This applies to all wages paid to the employee. FICA is embodied in Chapter 21 of the Internal Revenue Service code.

Federal Insurance Contribution Act, *at* http://cw.prenhall.com/bookbind/pubbooks/burns4/medialib/docs/fica.htm (last visited Feb. 1, 2002) (citing http://www.dol.gov/dol/wb/public/wb_pubs/finhoush.htm). This explains the spirit of FICA, but it is important to note that one of the numbers in the FICA formula has changed. The "wage cap," listed above as $65,400, stood at $76,200 for the year 2000 and $80,400 for 2001. I. R. S., Dep't of the Treasury, Pub. No. 15, Circular E, Employer's Tax Guide (2001).

23. The employee provision is found at 26 U.S.C. § 3101 and the employer provision is found at 26 U.S.C. § 3111. Thus, the statute is divided between those provisions that apply employers and those that apply to employees.

24. 26 U.S.C. § 3101(a) (2001) and 26 U.S.C. § 3111(a) (2001).

These portions of FICA follow:

> § 3101 Rate of tax
>
> (a) Old-age, survivors, and disability insurance. In addition to other taxes, there is hereby imposed on the income of every individual a tax equal to the following percentages of the wages (as defined in section 3121(a)) received by him with respect to employment (as defined in section 3121 (b)) - -
>
> | In cases of wages received during: | The rate shall be: |
> |---|---|
> | 1984, 1985, 1986, or 1987 | 5.7 percent |
> | 1988 or 1989 | 6.06 percent |
> | 1990 or thereafter | 6.2 percent. |

26 U.S.C. § 3101(a).

B. FUTA

FUTA[25] is an excise tax imposed upon employers, based on having individuals in their employ.[26] The FUTA tax is used to fund the federal unemployment program, which confers benefits to workers during temporary periods of unemployment.[27] The FUTA tax is calculated as a percentage of wages[28] the employer[29] has paid to the employee, and this tax rate differs with respect to the calendar year in which the wages were paid.[30]

C. Generally

Under FICA, employee taxes are assessed with respect to the

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§ 3111 Rate of tax

(a) Old-age, survivors, and disability insurance. In addition to other taxes, there is hereby imposed on every employer an excise tax, with respect to having individuals in his employ, equal to the following percentages of the wages (as defined in section 3121 (a)) paid by him with respect to employment (as defined in section 3121(b)) - -

In cases of wages paid during:	The rate shall be:
1984, 1985, 1986, or 1987	5.7 percent
1988 or 1989	6.06 percent
1990 or thereafter	6.2 percent.

26 U.S.C. § 3111(a).

25. The full text of FUTA can be found at 26 U.S.C. § 3301-3320 (2001).

26. 26 U.S.C. § 3301 (2001). While both the employer and employee pay FICA taxes, only the employer is taxed under FUTA. Kirsten Harrington, *Employment Taxes: What can the Small Businessman Do?*, 10 AKRON TAX J. 61, 61-62 (1993).

27. Harrington, *supra* note 26, at 62.

28. Generally, "wages" under FUTA apply only to the first $7,000 paid to an employee. 26 U.S.C. § 3306(b)(1) (2001). *See also* Robinson, *'supra* note 21, at 40 (citingI.R.S., Dep't of the Treasury, Pub. No. 15, Circular E, Employer's Tax Guide (2000)).

29. "Employer" is defined, in part, as a person who:

(a) during any calendar quarter in the calendar year or the preceding calendar year paid wages of $1,500 or more, or (b) on each of some 20 days during the calendar year or during the preceding calendar year, each day being in a different calendar week, employed at least one individual in employment for some portion of the day.

26 U.S.C. § 3306(a)(1) (2001).

30. 26 U.S.C. § 3301 (2001). Section 3301 follows:

§ 3301 Rate of tax

There is hereby imposed on every employer (as defined in section 3306(a)) for each calendar year an excise tax, with respect to having individuals in his employ, equal to- -

(1) 6.2 percent in the case of calendar years 1988 through 2007; or

(2) 6.0 percent in the case of calendar year 2008 and each calendar year thereafter; of the total wages (as defined in section 3306(b)) paid by him during the calendar year with respect to employment (as defined in section 3306(c)) .

Id. Also affecting an employer's final tax liability is § 3302 which provides allows the employer credits for different reasons, including contributions made to state unemployment funds. 26 U.S.C. § 3302 (2001).

calendar year in which the "wages are paid."[31] In general, wages are paid to an employee when they are actually or constructively distributed and wages are received by an employee when they are paid to the employee.[32] Prior to 1987, there was a dearth of authority on the issue of whether backpay[33] of wages should be taxed in the year they should have been paid, or the year they are actually paid for FICA purposes.[34]

D. Bowman v. United States

In *Bowman v. United States*, the Court of Appeals for the Sixth Circuit considered how backpay should be treated for FICA purposes.[35] The *Bowman* court found guidance in only one case, *Social Security Board v. Nierotko*.[36] On the authority of *Nierotko*, the *Bowman* court

31. Bowman v. United States, 824 F.2d 528, 529 (6th Cir. 1987), *overruled in part by* 532 U.S. 200 (2001) (citing Treas. Reg. § 31.3101-3 (1954)) (*Bowman* held that for back pay treated as wages, FICA tax attaches at the time the employee should have been paid, not when the employee actually receives the money).

32. *Bowman*, 824 F.2d at 529 (citing Treas. Reg. § 31.3121(a)-2(a) (1954)).

33. The concept of backpay is illustrated in the following hypothetical: Taxpayer earns $40,000 compensation in 1987. Taxpayer sues his employer, claiming that he should have been paid $60,000 based on $40,000 base salary he received and $20,000 in sales commission, which the employer did not pay. In 1988, taxpayer receives a judgment against employer for the $20,000, which the court determines were payable as wages in 1987.

The question is whether the parties are taxed on the $20,000 in 1987 when the wages should have been paid, or in 1988 when the wages were actually paid. See *supra* note 24 and accompanying text. If the tax is allocated to 1987, the tax on the $20,000 will be $1,140 for both the employer and taxpayer, but if the tax is allocated to 1988, the tax is $1,212 for both. *See id.* While the difference in this hypothetical ($72 each) is relatively small, it becomes much more an issue if the employer owes backpay to many different employees.

34. *See Bowman*, 824 F.2d at 530. *Bowman* held that FICA taxes are assessed as of the time the employee should have been paid. *Id.*

35. *Id.* at 528. This case arose from a settlement where Ford Motor Company entered into a settlement with Mr. Bowman over Mr. Bowman's race discrimination suit. *Id.* Ford withheld FICA taxes on the wages for the year in which Mr. Bowman was actually paid and Mr. Bowman brought this action for a refund of FICA withheld, arguing that it should have been allocated to the year in which he should have received the wages. *Id* at 529.

36. Social Sec. Bd. v. Nierotko, 327 U.S. 358 (1946). Before *Bowman*, no authority existed for the treatment of backpay specifically for FICA purposes. *See Bowman.* However, backpay had been addressed by the United States Supreme Court in a different context. Social Sec. Bd. v. Nierotko, 327 U.S. 358 (1946). Interestingly, *Nierotko* was not addressed by either litigant in *Bowman*. *Bowman*, 824 F.2d at 530. The Court attributed this to the fact that the case was brought *pro se* and submitted on briefs. *Id.* Accordingly, the Court "entered an order requesting the Government to address the reasoning of the *Nierotko* decision in a supplemental submission to the Court." *Id.* In *Nierotko*, the Supreme Court of the United States considered whether backpay awarded to an employee pursuant to the National Labor Relations Act constitutes "wages" under the Social Security Act, and if so, in what period should such "wages" be allocated? *Nierotko*, 327 U.S. at 359. The Court first found that the backpay in question did constitute "wages." *Id.* at 370. Furthermore, the Court held that such backpay is attributable to the period in which it should have been paid. *Id.*

held that backpay should be allocated to the period in which it should have been paid.[37] The Court agreed with the Government's contention that *Nierotko* was factually distinguishable from *Bowman*.[38] Nevertheless, the Court found *Nierotko* to be "compelling and applicable" and because the Government had not convinced the Court that different reasoning should apply, the Court held that backpay wages are allocated to the year in which they should have been paid.[39]

E. Hemelt v. United States

FICA backpay issues surfaced again in *Hemelt v. United States*[40] In

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37. *Bowman*, 824 F.2d at 530. The Government attempted to distinguish *Nierotko* by arguing that because *Nierotko* and *Bowman* involved different legislation (National Labor Relations Act versus FICA), different policy considerations were present. *Id.* Furthermore, the Government pointed out that the cases were factually distinguishable in that *Nierotko* involved benefits and *Bowman* involved taxes. *Id.*

> Central to the Bowman court were the following passages from *Nierotko*, quoted in the *Bowman* opinion:
>
> Petitioner further questions the validity of the decision of the circuit court of appeals on the ground that it must be inferred from the opinion that the backpay must be allocated as wages by the Board to the "calendar quarters" of the year in which the money would have been earned, if the employees had not been wrongfully discharged. We think this inference is correct.
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> . . .
>
> If, as we have held above, backpay is to be treated as wages, we have no doubt that it should be allocated to the periods when the regular wages were not paid as usual.

Id. (quoting *Nierotko*, 327 U.S. at 370). Applying the above reasoning, the *Bowman* Court stated, "[w]here there is no good reason not to apply the same principle, we advance the clarity, symmetry and fairness of the system by using the same principle of allocation." *Bowman*, 824 F.2d at 530.

38. *Id.* The Court noted that the instant case involved taxation as opposed to *Nierotko*, which dealt with back wages in the benefits context. *Id.*

39. *Id.* The Court stated:

> [I]f the payments are in fact for prior years and if, under *Nierotko*, they should be attributable to prior years for purposes of eligibility and other incidents of Social Security benefits and administration, we can see no reason for not applying this same principle in allocating the incidents of taxation.

Id.

40. Hemelt v. United States, 122 F.3d 204 (4th Cir. 1997). In *Hemelt*, the plaintiffs brought an action to recover FICA and other taxes that had been withheld form their class-action suit brought under the Employee Retirement Income Security Act (ERISA) of 1974. *Id.* In the underlying case, *McLendon v. Continental Group, Inc.*, 660 F. Supp. 1553 (D.N.J. 1987), summary judgment was granted for plaintiffs, finding Continental wrongfully terminated employment of plaintiffs to avoid liability for plaintiffs' pensions under ERISA. *Id.* at 206.

The first issue in *Hemelt* was whether the settlement payments constituted taxable wages. *Id.* The plaintiffs argued that the purpose of the settlement was to compensate them for personal injuries and therefore the payments are excluded from taxable income under § 104(a)(2) of the Internal Revenue Code and not subject to FICA. *Id.* Disagreeing with all plaintiffs' arguments, the court found that the payments were "wages." *Id.* A second issue arose when plaintiffs argued that even if the award was subject to taxation, the applicable tax rate is the rate which prevailed in the

considering how FICA backpay issues should be addressed, the *Hemelt* court did not consider the reasoning announced in *Bowman*. Rather, the Court placed unquestioning reliance on the Treasury Regulation contained in 26 C.F.R. §31.3121(a)-2(a), which states that an employee receives wages when they are actually paid to him.[41] The Court concluded that FICA taxes were correctly withheld at the time the settlement was paid to plaintiff taxpayers.[42] The Court reasoned that the Treasury Regulation directly addressed the issue before them and the taxpayers failed to prove the Regulation inapplicable.[43]

F. Walker v. United States

The question of when wages are taxed arose again in *Walker*.[44] *Walker* did not involve FICA taxes, but rather a claim for a refund of taxes paid under the Self Employment Contributions Act (SECA).[45] The issue in *Walker* was whether the Walkers were liable for SECA taxes for payments received in the years 1992 to 1995, when the payments were made for services Mr. Walker performed between 1971 and 1975.[46] The Tenth Circuit held that the Walkers were liable for the taxes in

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years to which the wages were attributable. *Id.* at 210.

41. *Id.* at 210.

42. *Id.* at 210-11. The Court's entire analysis of this issue is contained in the following paragraph:

> Taxpayers' final claim, that the payments they received should be allocated to the years to which they are attributable and taxed at the rate prevailing in each of those years, is also meritless. It is clear under the Treasury Regulations that "wages" are to be taxed for FICA purposes in the year in which they are received. See *26 C.F.R. § 31.3121(a)-2(a)* ("In general, wages are received by an employee at the time that they are paid by the employer to the employee.") Furthermore, taxpayers have provided no evidence of how they would have us allocate their awards among the years to which they are supposedly attributable (not to mention the awards of the other five thousand class members). Thus, we could not undertake such allocation even if we were allowed to do so, and FICA taxes were properly withheld from the settlement awards at the time they were paid to the taxpayers.

Id.

43. *Id.*

44. Walker v. United States, 202 F.3d 1290 (10th Cir. 2000).

45. *Id.* at 1291.

46. *Id.* Mr. Walker entered into a contingency fee agreement in 1972 with Telex Corporation whereby Mr. Walker represented Telex in antitrust litigation against IBM. *Id.* at 1290-91. Mr. Walker and Telex were later unable to agree on the fee due Mr. Walker. *Id.* at 1291. Following litigation, Mr. Walker and Telex agreed to a settlement, paying Mr. Walker $2,350,000 over 20 years. *Id.* The Walkers paid taxes on these annual payments until 1995, when he filed for a refund of taxes paid in 1992, 1993, and 1994. *Id.* The IRS demanded payment of the taxes for 1995, which the Walkers made. *Id.* The Walkers sought refunds back to 1992 because the statute of limitations had run on any claims they had for a refund of taxes paid prior to 1992. *Id.*

question.[47] The *Walker* opinion ended by disregarding *Nierotko* and *Bowman*, as well as the Social Security Administration's decision regarding the treatment of Mr. Walker's Social Security and Medicare benefits.[48] The Court reasoned that the rationale employed in *Nierotko* was "inapposite" and *Bowman's* holding was "unpersuasive."[49] Accordingly, the Court found Treasury Regulation §1.1402(a)-1(c) compelled it to hold the Walkers liable for taxes in the year payment was received, even though the Walkers would not have been subject to the tax in the year payment should have been made.[50]

III. STATEMENT OF THE CASE

A. Statement of the Facts

The Major League Baseball Players' Association[51] (Players'

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47. *Id.* The court relied on the following quote from Treasury Regulation §1.1402(a)-1(c):

> Gross income derived by an individual from a trade or business includes gross income received (in the case of an individual reporting income on the cash receipts and disbursement method) . . . in the taxable year from a trade or business even though such income may be attributable in whole or in part to services rendered or other acts performed in a prior taxable year as to which the individual *was not subject to the tax on self-employment income.*

Id. at 1292. (emphasis added). Mr. Walker argued that the regulation was inapplicable to him because the regulation applies only to persons who were not subject to self-employment tax in the year to which the wages are attributable. *Id.* Mr. Walker asserts that not only was he subject to self-employment tax in 1975, but also that he paid the maximum amount of SECA taxes in that year and therefore cannot have a tax liability for wages earned in or before 1975, but received subsequent to said years. *Id.* The court dispensed of Mr. Walker's argument, stating ". . .that a plain, common-sense reading of Treas. Reg. § 1.1402(a)-1(c) compels us to conclude that the Walkers owed SECA taxes on the Telex payment received in 1992 through 1995, regardless of whether, in 1975, Mr. Walker was subject to self-employment taxes." *Id.*

48. The Court's consideration of other decisions follows:

> Finally, the fact that the Social Security Administration attributed the Telex payments to Mr. Walker's 1975 earnings for purposes of Social Security and Medicare benefits does not alter our conclusion. The Social Security Administration is a different agency, implementing a different statutory scheme. Indeed, as the United States points out, a specific statute excludes the Telex payments from Mr. Walker's gross income for Social Security benefits purposes. See *42 U.S.C.* § *403*(f)(5)(D)(ii). We also find *Social Sec. Bd. v. Nierotko*, 327 U.S. 358, 90 L. Ed. 718, 66 S. Ct. 637 (1946) inapposite and *Bowman v. United States*, 824 F.2d 528 (6th Cir. 1987) unpersuasive.

Walker, 202 F.3d at 1293.

49. *Id.*

50. *Id.*

51. The Major League Baseball Player's Association is the collective bargaining representative for Major League Baseball players and assists players in negotiating various other issues. Bigleagues.com powered by Yahoo! Sports-FAQ, *at* http://bigleaguers.yahoo.com/mlbpa/faq.html (last visited Mar. 7, 2002).

Association) became involved in a dispute with the Major League Baseball Clubs[52] (Clubs) involving their collective bargaining agreement.[53] The Players' Association alleged that the Clubs had violated the collective bargaining agreement regarding free agents, by restricting their ability to move within the league.[54]

The cause was submitted to arbitration where the Clubs were found to have violated the player's free agency rights.[55] In 1990, the parties settled for a total of $280 million.[56] Prior to paying, the Clubs asked for and received a private letter ruling from the IRS that described the tax treatment of said payments.[57] Although the Cleveland Indians did not agree with the proposed tax treatment of the non-interest portion of the payments, they paid the taxes and filed a claim for a refund of FICA and FUTA taxes paid during 1994.[58]When six months had passed without a response from the IRS, the Cleveland Indians filed suit against the

52. The term "Major League Baseball Clubs" is a collective reference to all the individual teams in the Major League Baseball Association.

53. Cleveland Indians Baseball Co. v. United States, 1998 WL 180623 at *1 (N.D. Ohio Jan. 28, 1998).

54. *Id.* The Clubs colluded not to aggressively bid for the services of free-agent players, thereby artificially depressing the salaries most free agents would have received in absence of the collusion. *See* Jack Torry, *Tribe Takes on Government in Battle Over Tax Refund*, COLUMBUS DISPATCH, Feb. 21, 2001, at 6C.

55. *Cleveland Indians*, 1998 WL 180623, at *1. Particularly, the Clubs were found to have violated a bargaining agreement clause that prohibited the Clubs ". . . from taking concerted action to interfere with the free agency rights of their players," which affected the player's labor market and artificially depressing wages of those who would be free agents in future seasons. Cleveland Indians Baseball Co. v. United States, 1999 WL 72866 at *1 (N.D. Ohio Jan. 25, 1999).

56. *Cleveland Indians*, 1998 WL 180623, at *1. The $280 million represented the amount the Clubs were to pay in the aggregate. *Id.* The amount was then divided by 26 (the total number of Clubs in the league at the time) to determine what each Club's liability. *Id.* The Indians' share was $610,000, plus $219,638 in interest for the 1986 season and $1,457,848, plus $409,119.17 in interest for the 1987 season. *Id.* The arbitration decision did not make any determination of the specific amounts due any individual players. *Id.* These matters were considered in a separate proceeding. *Id.*

57. *Cleveland Indians*, 1998 WL 180623, at *1. The District Court's opinion summarized the tax treatment as follows:

> On October 18, 1995, the IRS ruled as follows: (1) the non-interest portion of the Settlement Payments does constitute wages subject to FICA and FUTA taxes; (2) the interest portion does not constitute wages, and, thus, is not subject to those taxes; and (3) the settlement payments should be taxed in the year paid, 1994, rather than the years to which they relate, 1986 and 1987 (the 1994 rate is, of course, higher than either the 1986 or 1987 rate).

Id.

58. *Id.* The Cleveland Indians actually made payments to the players in 1994. *Cleveland Indians,* 1999 WL 72866, at *1. The FICA taxes were paid in April of 1994 and the FUTA taxes were paid in January of 1995. *Id.*

Government seeking a refund of taxes paid.[59]

B. Procedural History

1. Discovery Motions

The early stages of litigation in *Cleveland Indians Baseball Co., v. United States* centered on a dispute over what documents were subject to discovery.[60] The United States filed a motion to compel the Cleveland Indians to produce documents or, in the alternative, to dismiss the action as a sanction for discovery violations.[61] This initial proceeding resulted in the United States' motion to compel being granted in part and denied in part.[62]

2. Federal District Court

The gravamen of the Cleveland Indians's complaint was first addressed by the United States District Court for the Northern District of

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59. *Cleveland Indians*, 1998 WL 180623, at *1. The complaint claimed (specifically) that the payments made were not for wages, and even if they were considered payments for wages, they should be attributed to the tax rates prevailing in 1986 and 1987 rather than 1994. *Id.*

The Cleveland Indians was not the only team to litigate the issue of FICA and FUTA taxes on the $280 million settlement. Attorney Daniel L. Goldberg, who filed a similar suit on behalf of the Boston Red Sox, estimated that as of February, 2000, about 6 teams had filed suit. Laurel J. Sweet, *Red Sox will slug it out with IRS*, BOSTON HERALD, Feb. 18, 2000, at 4.

60. *Cleveland Indians*, 1998 WL 180623, at *1.

61. *Id.* The early case management plan indicated that the parties did not anticipate the need for extensions in the discovery plan. *Id.* at *2. However, it was not too long before the defendant contacted the Court, pointing out difficulties. *Id.* Defendant served requests for admissions, interrogatories and requests for production of documents on the plaintiff on the Cleveland Indians at the end of July 1997. *Id.* Defendant had not received responses to these requests as of October of 1997. *Id.* At one point, the plaintiff's case was nearly dismissed. *Id.* During an October 29, 1997 conference call, the Court ordered the plaintiff to produce certain documents by the seventh of the following month or face dismissal for failure to prosecute. *Id.* The Court captured the tone of early discovery correspondence in the following passage from the Court's opinion:

> The letter does not expressly mention, not does it suggest, that plaintiff had any objections to the document requests at the time. In fact, none of the correspondence dated prior to November, 1997 indicates that plaintiff's delay in responding to defendant's discovery requests was due to objections it might have had. Moreover, earlier correspondence between the parties reveals that plaintiff had frequently asserted a variety of excuses for its failure to comply with the defendant's discovery requests, made promises to respond, and then failed to carry through with those promises. A perusal of the correspondence between the parties reveals that plaintiff's "check's in the mail" approach to discovery continued unabated until this Court's intervention.

Id.

62. *Cleveland Indians*, 1998 WL 180623, at *3.

Ohio.[63] By this point, the parties had resolved all but the main issue of what tax year the wages were subject to for FICA and FUTA taxes.[64] Ironically, the main issue, the single source of disagreement, was not an issue that the parties truly disagreed upon for purposes of litigation at the District Court level.[65]

The Cleveland Indians relied upon the authority of *Bowman* and *Nierotko*, arguing that the District Court was bound to rule in their favor.[66] The United States candidly agreed that the *Bowman* decision applied to the facts of their case and that the Court appeared to be bound to follow *Bowman*.[67] However, the United States argued that *Bowman* was wrongly decided.[68]

The District Court followed *Bowman* and ordered the United States to refund the $97,202.20 in FICA and FUTA taxes plus interest, which had been paid by the Cleveland Indians in 1994.[69] Furthermore, the Court declined to provide the United States with ammunition for appeal as the United States had requested.[70]

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63. Cleveland Indians Baseball Co. v. United States, 1999 WL 72866 (N.D. Ohio Jan. 25, 1999).

64. *Id.* at *1. The most significant change in plaintiff's position was the fact that for purposes of this proceeding they agreed with the United States that the non-interest portion of the payments did constitute back-pay for wages. *Id.* Prior to this agreement the Cleveland Indians took the position that the non-interest payments were not on account of wages for services rendered, but were instead damages for breach of the Collective Bargaining Agreement. *Id.*

65. *Id.* at *2. The parties were arguing over what the law should be, not what the law actually was. *Id.* The parties agreed that the specific issue had been decided earlier by the Sixth Circuit in *Bowman v. United States* 824 F.2d 528 (6th Cir. 1987), *overruled in part by* 532 U.S. 200 (2001). *Id.*

66. *Cleveland Indians*, 1999 WL 72866, at *2.

67. *Id.*

68. *Id.* The United States largely treated proceedings at the District Court level as a "preseason" or "exhibition" exercise to preserve their arguments for appeal where they planned to have *Bowman* overruled. *Id.*

69. Cleveland Indians, 1999 WL 72866, at *2.

70. *Id.* The United States had asked the Court to give at least some thought to its arguments as if *Bowman* did not exist. *Id.* The Court stated:

> Apparently not fully content with the prospect of an appeal from the record as it stands, moreover, the government goes on to ask this Court to "consider" its arguments regarding the wisdom of *Bowman* and "issue a decision which reflects what this Court would do if it were given the privilege of a clean slate upon which to draw its decision." While this Court, of course, has considered all of the government's arguments, and has examined all authority cited by both parties, it is disinclined to issue what is essentially an advisory opinion, particularly in the face of a clear, unanimous directive from a distinguished Sixth Circuit panel.

Id. (citations omitted). The Court further noted that the United States would be free to argue issues not addressed in *Bowman* if they follow through with an appeal including the fact that at least one court has disagreed with *Bowman.Id.* Presumably, the Court was referring to the Fourth Circuit's decision in *Hemelt*, which held FICA and FUTA taxes are to be assessed in the year they are

3. Federal Court of Appeals for the Sixth Circuit

The United States brought an appeal in the Sixth Circuit, which was heard by a three judge panel.[71] As in the District Court, the United States argued that *Bowman* was wrongly decided on more than one ground.[72] Nevertheless, the United States conceded that the very issue before the Court had been decided in *Bowman*.[73] Relying upon *Bowman*, the Court of Appeals affirmed the District Court's decision in favor of the Cleveland Indians.[74]

C. United States Supreme Court Decision

1. Plain Language

The Supreme Court's analysis of the issue presented began with a general summary of the arguments made by the United States and the Cleveland Indians. First, the United States argued that 26 U.S.C. §3111(a) is clear in its use of the words "wages paid during a calendar year."[75] The United States sought to bolster their argument by pointing out that Congress specifically chose the statute's current language to replace the language in the 1935 Social Security Act.[76]

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actually received by the employee. *Id.* See *supra*, notes 40-43 and accompanying text.

71. Cleveland Indians v. United States, 215 F.3d 1325, 2000 WL 659028 at **2 (6th Cir. May 10, 2000). The United States requested an en banc hearing. *Id.* The court denied the request and assigned the case to the three judge panel. *Id.* Additionally, the Court reviewed the record *de novo* because the appeal involved questions of statutory interpretation. *Id.*

72. *Id.*

73. *Id.*

74. *Id.* The Court noted in their opinion that even if they did agree with the arguments presented by the United States, they still could not reverse the decision of the District Court because 6th Circuit case law prohibits one appellate panel from overruling the decision of another appellate panel. *Id.* Only the Court of Appeals sitting en banc (or of course, the Supreme Court of the United States) could overrule *Bowman*. *Id.* Therefore, the decision in the Court of Appeals was effectively made when the case was referred to a three judge panel in lieu of being argued en banc.

75. United States v. Cleveland Indians Baseball Co., 532 U.S. 200, 209 (2001). Petitioner's brief to the Supreme Court points out that the FICA statute taxes "wages . . . paid" during the calendar year and that Congress did not carve out an exception for back wages. Petitioner's Brief at 12, United States v. Cleveland Indians Baseball Co., 532 U.S. 200 (2001) (No. 00-203). Petitioners further argue that plain language of the statutes dictates the "back wages are taxed in the year in which they are paid and not in the year in which the services were performed or would have been performed but for the wrongful conduct of the employer." *Id.*

76. *Cleveland Indians*, 532 U.S. at 209. The 1935 Act stated that wages were taxed "with respect to employment during the calendar year." *Id.* The Treasury Department interpreted this to mean that wages were taxed according to "the rate in effect at the time of the performance of the services for which the wages were paid." *Id.* at 209-10. In 1939, Congress changed the 1935 language so the tax rates would apply to "wages paid during the calendar year" rather than the time

2. *Nierotko* and Legislative Symmetry

The Cleveland Indians were able to persuade the Court that *Nierotko* undermined the United States's contention that the plain language of the FICA and FUTA statutes precluded further examination.[77] In *Nierotko*, the Supreme Court found that backpay should be allocated to the periods where it should have been paid.[78] The *Cleveland Indians* Court was most concerned by the fact that the *Nierotko* Court found no conflict between an allocation back rule for backpay and §209(g), which based eligibility for benefits on the number of quarters in which wages have been paid.[79] Based on the holding in *Nierotko*, the Court determined that they must look beyond the plain meaning of the phrase "wages paid during a calendar year" to determine the issue before the Court.[80]

The Cleveland Indians argued that if *Nierotko* read the "wages paid" language in the 1939 Act to allow "allocation-back" rule for benefits eligibility, the same 1939 "wages paid" language must operate in the same manner for tax purposes.[81] However, the Court did not

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the services were performed. *Id.* at 210. The 1939 language remains virtually unchanged. *Id.*

77. *Cleveland Indians*, 532 U.S. at 210. The following is the Supreme Court's brief summary of the facts in *Nierotko*:

> In *Nierotko*, the National Labor Relations Board had ordered the reinstatement of a wrongfully discharged employee with "back pay" covering wages lost during the period from February 1937 to September 1939. The employer paid the award in July 1941. The primary question presented and aired in the Court's opinion was whether backpay for a time in which the employee was not on the job should nevertheless count as "wages" in determining the employee's eligibility for Social Security benefits. Notwithstanding the contrary view of the Social Security Board and the Bureau of Internal Revenue, the Court held that backpay covering the wrongful discharge period met the definition of "wages" in the 1935 Act.

Id. at 210 (citations omitted).

78. *Cleveland Indians*, 532 U.S. at 210-11.

79. *Id.* In other words, the *Nierotko* court's decision accepted that the language of § 209(g), which referred to wages paid in a quarter, included wages that should have been paid, but were not actually paid. *Id.* The Court did not discern between wages *actually* paid and wages that *should* have been paid. *See Id.*

80. *Id.*

81. *Cleveland Indians*, 532 U.S. at 212. This marked the point in the case where the Cleveland Indians's ship began to take on water. The Court quickly pointed out that *Nierotko* did not deal with taxation. *Id.* The Court speculated that the underlying concern in the *Nierotko* holding was that the Social Security benefits scheme would be harmed if a culpable employer were able to reduce the quarter of coverage an employee would be entitled to but for the conduct of the employer. *Id.* There is no similar concern in the taxation context because "there is no direct relation between taxes and benefits at the level of an individual employee." *Id.* Furthermore, the "contributions" made pursuant to the Social Security tax do not create a property right on the part of the contributor in the way private pension contributions create a property right against the government. *Id.*

believe *Nierotko* compelled a "symmetrical construction" of the "wages paid" language in the contexts of taxation and benefits eligibility.[82]

With respect to Congressional intent, the Court did not believe FICA and FUTA legislation was concerned with worker benefits so much as fiscal administration.[83] As tax rates change in time, Congress anticipated "difficulties and confusion" would arise in taxation of back pay.[84] Therefore, the "wages paid" language in the 1939 Amendments was intended to remedy the potential "difficulties and confusion" by taxing wages in the period they were paid and received without reference to when the wages were earned.[85]

The Cleveland Indians next argued that "Congress incorporated *Nierotko's* treatment of backpay into the tax provisions when it amended the Social Security Act shortly after *Nierotko* was decided."[86] The Court disagreed.[87] Citing House and Senate Committee Reports, the Court was skeptical of the suggestion that Congress even considered *Nierotko*.[88] Furthermore, the Court re-emphasized the tax/benefits distinction in declining to apply the *Nierotko* Court's interpretation of "wages paid" to the instant case.[89]

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82. *Id.* at 213. "Although we generally presume that 'identical words used in different parts of the same act are intended to have the same meaning' the presumption 'is not rigid,' and 'the meaning [of the same words] well may vary to meet the purposes of the law.'" *Id.* (citations omitted) (quoting Atlantic Cleaners & Dyers, Inc. v. United States, 286 U.S. 427, 433 (1932)). "The tendency to assume that a word which appears in two or more legal rules, and so in connection with more than one purpose, has and should have precisely the same scope in all of them . . . has all the tenacity of original sin and must constantly be guarded against." *Id.* (citing Walter Wheeler Cook, *"Substance" and "Procedure" in the Conflict of Laws*, 42 YALE L.J. 333, 337 (1933)).

83. *Cleveland Indians*, 532 U.S. at 213.

84. *Id.* at 214. In making the 1939 Amendments, Congress appeared to be cognizant of the fact that workers will often earn money in pay period number 1 that the employer will not pay until pay period number 2, because in some situations it is impossible to have determined amounts due by the close of the first pay period. *Id.* Apart from the facts of *Cleveland Indians*, backpay is quite normal in instances where an employee is entitled to a percentage of profits or royalties that require calculation and cannot be determined until the employer has closed his books for the year. *Id.* (citing S. Rep. No. 734, 76th Cong., 1st Sess., at 75).

85. *Id.* (citing H.R. Rep. No. 728, 76th Cong., 1st Sess., at 58).

86. *Id.* at 214-15. Before 1946, FICA and FUTA wages taxed wages "paid . . . with respect to employment during" a year. *Id.* In 1946, the language was changed to the current "wages paid" language that was already present in § 209(g) and interpreted in *Nierotko*. *Id.* Therefore, the Cleveland Indians argue that when Congress amended the tax provisions, they were in fact codifying the backpay rule announced in *Nierotko*. *Id.*

87. *Id.*

88. *Cleveland Indians*, 532 U.S. at 215-16. "Far from indicating an intent to codify *Nierotko*, those reports suggest that Congress, if it considered *Nierotko* at all, considered it an exception to the general rule for measuring "wages" in a given year." *Id.* (footnote omitted).

89. *Id.*

Because the concern that animates *Nierotko's* treatment of backpay in the benefits

3. Opportunistic Behavior

The Cleveland Indians argued that the rule proposed by the United States will tax some wages that should not be taxed and vice versa, thereby creating opportunities for employers to take advantage of the system.[90] The Cleveland Indians argued that Congress could not have intended to create tax windfalls and reward employers for wrongfully withholding payments.[91] Such inequities would not exist under a rule allocating wages to the year in which they should have been paid.[92]

While the Court agreed that the United States's rule would operate somewhat arbitrarily, it justified this operation by looking at the purpose of the tax.[93] The Court determined that Congress intended to create a system that was "both efficiently administrable and fair" and this legislation simply demonstrates the difficulty inherent in meeting both aims.[94]

4. Deference to the Commissioner and Treasury Regulations

The Court's opinion closed by suggesting that courts should be conservative when interpreting the tax code.[95] Courts defer to the Commissioner's regulations, provided they "implement the

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> context has no relevance to the tax side, it makes no sense to attribute to Congress a desire for conformity not only with respect to the general rule for measuring "wages," but also with respect to *Nierotko's* backpay exception.

Id. at 216 (citations omitted). The Court believed that if a pure "statutory symmetry" argument were to be considered, *Nierotko* would not be considered because *Nierotko* was not concerned with tax. *Id.* Accordingly, this would leave only the tax code and its corresponding legislative history for consideration. *Id.*

90. *Id.* at 216-17. The Court demonstrated this possibility in the following illustration:

> Under the [United States's] rule, an employee who should have been paid $100,000 in 1986, but is instead paid $50,000 in 1986 and $50,000 in backpay in 1994, would owe more tax than if she had been paid the full $100,000 due in 1986. Conversely, a wrongdoing employer who should have paid an employee $50,000 in each of five years covered by a $250,000 backpay award would pay only one year's worth of employment taxes (limited by the annual ceilings on taxable wages) in the year the award is actually paid.

Id. at 217.

91. *Id.* Applying the United States's proposed rule, similar anomalies would exist in other provisions of the tax code. *Id.*

92. *Id.*

93. *Id.* at 218. In *Nierotko*, to allocate the wages to the period in which they were paid would always harm the employee and cut across the point of providing for employee benefit eligibility. *Id.* On the other hand, there is no such unfairness in the tax arena because the IRS will win some and lose some depending on the specific facts. *Id.*

94. *Id.* at 218.

95. *Id.* "[W]e do not sit as a committee of revision to perfect the administration of the tax laws." (quoting United States v. Correll, 389 U.S. 299, 306-07 (1967)).

congressional mandate in some reasonable manner."[96] In this case, the regulations provide that the tax attaches when the wages are paid by the employer.[97] Additionally, the Court cited Revenue Rulings, which construed back wages as taxable in the year they are actually paid.[98] "Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law."[99] Accordingly, the judgment of the Sixth Circuit Court of Appeals was reversed in favor of the United States.[100]

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96. *Cleveland Indians*, 532 U.S. at 219 (quoting United States v. Correll, 389 U.S. 299, 307 (1967)). This is done because "Congress has delegated to the Secretary of the Treasury and his delegate, the Commissioner of Internal Revenue, not to the courts, the task of prescribing 'all needful rules and regulations for the enforcement' of the Internal Revenue Code." National Muffler Dealers Ass'n, Inc., v. United States, 440 U.S. 472, 477 (1979).

Furthermore, this policy "helps guarantee that the rules will be written by 'masters of the subject' . . . who will be responsible for putting the rules into effect." *Cleveland Indians*, 532 U.S. at 219 (quoting *National Muffler Dealers*, 440 U.S. at 477) (quoting United States v. Moore, 95 U.S. 760, 763 (1877)).

97. *Cleveland Indians*, 532 U.S at 219.

98. *Id.*

> We need not decide whether the Revenue Rulings themselves are entitled to deference. In this case, the Rulings simply reflect the agency's longstanding interpretation of its own regulations. Because that interpretation is reasonable, it attracts substantial judicial deference. *Thomas Jefferson Univ. v Shalala*, 512 U.S. 504, 512, 114 S.Ct. 2381, 129 L.Ed.2d 405 (1994). We do not resist according such deference in reviewing an agency's steady interpretation of its own 61-year-old regulation implementing a 62-year-old statute.

Cleveland Indians, 532 U.S. at 220. *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984) is one of the leading cases dealing with deference to administrative interpretations. *See* Mary L. Heen, *Plain Meaning, the Tax Code and Doctrinal Incoherence*, 48 HASTINGS L. J. 771 (1997). However, *Chevron* has not enjoyed as much popularity in tax as in other areas of law. *Id.* For a discussion of *Chevron's* application to administrative tax law, see David A. Brennen, *Treasury Regulations and Judicial Deference in the Post-Chevron Era*, 13 GA. ST. U.L. REV. 387 (1997).

This Note does not focus on the issue of judicial deference to administrative regulations largely because the *Cleveland Indians* Court explicitly stated that its decision did not state whether the Revenue Rulings were entitled to deference. However, the following sources provide an explanation of judicial deference issues: Brennen, *supra*; Linda Galler, *Judicial Deference to Revenue Rulings: Reconciling Divergent Standards*, 56 OHIO ST. L. J. 1037 (1995); Lee G. Knight & Ray A. Knight, *A New Approach to Judicial Review of Interpretive Regs*, 65 J. TAX'N 326 (1986); Russell L. Weaver, *Judicial Interpretation of Administrative Regulations: The Deference Rule*, 45 U. PITT. L. REV. 587 (1984) (arguing that the Supreme Court conveniently relies upon, or wholly ignores the judicial deference rule to reach the result they desire).

99. *Cleveland Indians*, 532 U.S. at 220. The Court apparently considers Congressional silence tantamount to approval of the Treasury Regulations. *Id.* However, it has been argued that Congressional silence is a "poor beacon to follow" and that those who rely on such silence, "walk on quicksand." John C. Grabow, *Congressional Silence and the Search for Legislative Intent: A Venture into "Speculative Unrealities,"* 64 B.U. L. REV. 737 (1984).

100. *Cleveland Indians*, 532 U.S. at 220.

5. Concurrence by Justice Scalia

Justice Scalia agreed that the tax statutes did not fully address the issue before the Court.[101] Additionally, Justice Scalia was not convinced that the tax and benefits statutes were so different so as to warrant giving different meanings to identical statutory language.[102] In the end, the Court should defer to the I.R.S. regulations because their treatment of the benefit and tax statutes were both reasonable, neither of the statutory interpretations were compelled, and the term "wages paid" did not require an identical result.[103]

IV. ANALYSIS

The Supreme Court's decision in *United States v. Cleveland Indians*, while attempting to provide a final answer to the issue of FICA and FUTA taxes, left open many questions. First, the Court seemed to ignore precedent that despite their assertions to the contrary, appears to decide the issue before the Court. Second, the Court acknowledged, and even fueled, ambiguity in the tax code by essentially stating that the actual words in the tax code do not necessarily mean what they appear to mean. Finally, the decision places too much power in an employer's hands relative to his employees.

A. The 1935 Social Security Act and the 1939 and 1946 Amendments

Understanding the 1935 Social Security Act (1935 Act), the 1939 Amendments, and the 1946 Amendments is essential to understanding one of the Cleveland Indians' most powerful arguments,[104] which was virtually ignored by the Court.

Congress passed the 1935 Act to establish old-age benefits.[105] These benefits are funded through employment taxes on wages.[106] Title VIII of the 1935 Act taxed employers and employees based on a percentage of wages "paid" or "received" "with respect to employment

101. *Id.* at 220-21. In fact, Justice Scalia would have framed the issue a bit differently from the majority and asked "whether *damages awards compensating an employee for lost wages* should be regarded for tax purposes as wages paid when the award is received, or rather as wages paid when they would have been paid but for the employer's unlawful actions." *Id.* (emphasis in original).

102. *Id.*

103. *Cleveland Indians*, 532 U.S. at 221-22.

104. Brief for Respondent at 13, United States v. Cleveland Indians Baseball Co., 532 U.S. 200 (2001) (No. 00-203).

105. *Id.*

106. *Id.*

during the calendar year [].”[107] The Bureau of Internal Revenue interpreted this language to mean that taxes were “assessed on wages payable for services performed during a given year, even if not actually paid during that year.”[108]

The 1935 Act, however, was only meant to provide a foundation for the Social Security Act and accordingly, Congress amended the act in 1939.[109] The 1939 Amendments defined both eligibility for Social Security benefits and liability for the Social Security taxes using the “wages” “paid” language.[110] In the benefits context, the 1939 Amendments created a new section 209 which made eligibility benefits dependant on “wages” “paid.”[111] Similarly, on the tax side, the 1939 Amendments altered the Internal Revenue Code to assess Social Security taxes (the tax provisions at issue in *Cleveland Indians*) on the basis of “wages” “paid” or “received” during a calendar year.[112] Therefore, it is imperative to understand that the 1939 Amendments created a “wages paid” rule in both the benefits eligibility and tax arenas.[113]

Nierotko interpreted the “wages paid” language in section 209(g) of the 1939 Amendments and not the 1935 Act.[114] *Nierotko* was decided in 1946.[115] However, *Nierotko* was decided a few months before Congress completed the 1946 Amendments.[116]

In the 1946 Amendments, Congress amended section 209(a) of the benefits provisions to incorporate the “wages paid” language of section 209(g) that *Nierotko* had just interpreted to allow for backpay.[117] “By using the same “wages paid” language in the amendment of section 209(a) that was already in place in section 209(g), Congress is presumed to have intended the 1946 Act to be interpreted consistently with

107. *Id.*

108. *Id.*

109. *Id.* The 1939 Amendments were the most substantial amendments to this Act as they substantially altered both the benefits and tax provisions and provided the basic structure we see in the Act today. *Id.*

110. *Id.* at 14.

111. *Id.*

112. *Id* at 15-16.

113. *Id* at 16.

114. *Id* at 20. Section 209(g) was a benefits eligibility provision. *Id.* Additionally, the Respondent’s (Cleveland Indians) brief points out that now the government “does not even acknowledge the statutory “wages paid” basis of *Nierotko’s* relation-back holding, even though it was the Government that relied upon section 209(g) of the 1939 Act in its argument to the Court in *Nierotko*.” *Id. See also supra* note 77 for a brief summary of *Nierotko*.

115. Social Sec. Bd. v. Nierotko, 327 U.S. 358 (1946).

116. *See* Brief for Respondent at 21, *Cleveland Indians* (No. 00-203).

117. *Id.* at 20-21.

Nierotko.[118] The "wages paid" language in subsections (a) and (g) of section 209 must have meant the same thing.[119] There is no logical explanation for these sections to have different meanings with respect to the "wages paid" language.[120]

Because *Nierotko's* "wages paid" interpretation is incorporated into section 209(a) of the 1946 Amendments, it is also incorporated into the 1946 Amendments of the tax titles.[121] The House Report indicates that Congress used the same "wages paid" language in the 1946 Amendments to amend the definition of FICA and FUTA "wages" in the tax provisions to conform with section 209(a).[122] This fact undercuts any argument for applying different rules to the benefit and tax titles.[123]

B. In Pari Materia Construction[124]

In addition, the United States argued that Social Security tax provisions should not be construed *in pari materia* with the Social Security benefits provisions because the Social Security Administration is a different agency with a different statutory framework.[125] Interestingly, the United States argued on the other side of the fence in 1945 when they argued that the "wages paid" language in the 1939 Amendments was used "advisedly" and had the same meaning as the

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118. *Id.* at 21 (citing Cannon v. Univ. of Chicago, 441 U.S. 677, 696-99 (1979)). When Congress uses the same language from a statute in a later version of the statute, it is assumed that judicial interpretations of the prior version will apply. *Id.*

119. '*Id. See also, infra* note 129 and accompanying text stating that "identical words used in different parts of the same act are intended to have the same meaning."

120. 'Brief for Responsent at 21, *Cleveland Indians* (No. 00-203). In other words, why would they use the same words, which were just interpreted to allow backpay, if Congress in fact intended the exact opposite interpretation? *But see* Lawrence Zelenak, *Thinking About Nonliteral Interpretations of the Internal Revenue Code*, 64 N.C. L. Rev. 623 (1986). Zelenak argues:

> The Internal Revenue Code has a way of saying one thing while seeming to mean something else. Literal interpretations, based on the language of the Code, often conflict with interpretations based on the structure or policy of the Code. In the past four years, the United States Supreme Court has decided at least five cases involving conflicts between language-based interpretations of the Code and interpretations based on statutory structure or policy. The Court, however, has not consistently articulated any general principles for dealing with such conflicts.

Id. at 624 (citations omitted).

121. Breif for Respondent at 21, *Cleveland Indians* (No. 00-203).

122. *Id.* (citing H.R. Rep. 79-2447, at 35 (1946)).

123. *Id.*

124. *In pari materia* generally means, "on like subject matter." STEVEN H. GIFIS, BARRON'S LAW DICTIONARY 253 (4th ed. 1996). Statutes or documents that are "in pari materia" are read together as having the same general purpose and construction. *Id.*

125. Brief for Respondent at 22, *Cleveland Indians* (No. 00-203). The Court ultimately found the two to be different in kind. *Cleveland Indians*, 532 U.S. 200 (2001).

"wages paid" language in the tax amendments which were at issue in *Cleveland Indians*.[126] If the United States remained faithful to its prior argument, they would be forced to agree that *Nierotko* should control the *Cleveland Indians* decision.[127] At any rate, these contradictory arguments should have caused the Court to discredit the United States' argument due to inconsistency.[128]

Furthermore, the general rule is that "identical words used in different parts of the same act are intended to have the same meaning."[129] This rule was in effect before the 1939 Amendments. The argument for identical meaning is further strengthened by the fact that Congress has unmistakably worked to keep the tax and benefits provisions symmetrical.[130]

C. *Statutory language and plain meaning*[131]

The United States argued that the FICA and FUTA provisions that

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126. 'Brief for Respondent at 22, *Cleveland Indians* (No. 00-203).

127. *Id.*

128. *Id.* (citing Norfolk S. Ry. v. Shanklin, 120 S. Ct. 1467, 1474 -76 (2000)). *Cf.* Lawrence Zelenak, *Should Courts Require the Internal Revenue Service to be Consistent?*, 40 TAX L. REV. 411 (1985) (stating that the Internal Revenue Service offends the principle of administrative consistency more than any other agency).

129. Brief for Respondent at 23, *Cleveland Indians* (No. 00-203). (citing Sorenson v. Secretary of Treasury, 475 U.S. 851, 860 (1986)) (quoting Helvering v. Stockholms Enskilda Bank, 293 U.S. 84, 87 (1934)) (quoting Atlantic Cleaners & Dyers, Inc. v. United States, 286 U.S. 427, 433 (1932)).

However, courts have declined to read tax statutes *in pari materia* with non-tax statutes because the statutes are assumed to have different purposes. Samuel B. Sterrett, *Use of Industry Definitions in Interpretation of the Internal Revenue Code: Towards a More Systematic Approach,* 16 VA. TAX REV. 1, 13 (1996). Additionally, some words have different meanings within the Code itself. *Id* at 12. Therefore, the *Cleveland Indians* decision does little more than reinforce the utter lack of uncertainty in interpreting the tax code.

130. Brief for Respondent at 23, *Cleveland Indians* (No. 00-203).

> Congress has been vigilant to ensure symmetry in the benefits and tax titles. For example, in 1983, it corrected a disjunction whereby employer contributions to simplified employee pensions (SEPs) were wages for benefits purposes but not for tax purposes by amending the statute to require the same treatment of those contributions in both titles.

Id. at n.12 (citing H.R. Rep. No. 98-25, at 77 (1983), *reprinted in* 1983 U.S.C.C.A.N. 219, 296).

131. One must wonder if the search for "plain meaning" is a wholly futile endeavor. As Justice Frankfurter stated:

> Anything that is written may present a problem of meaning, and that is the essence of the business of judges in construing legislation. The problem derives from the very nature of words. They are symbols of meaning. But unlike mathematical symbols, the phrasing of a document, especially a complicated enactment, seldom attains more than approximate precision. If individual words are inexact symbols, with shifting variables, their configuration can hardly achieve invariant meaning or assured definiteness.

make reference to "wages paid during a calendar year" clearly dictate that (1) wages are taxed in the year they are actually paid; and (2) that the year in which they should have been paid is of no consequence.[132] The Court agreed with the Cleveland Indians's assertion that *Nierotko* precluded the "plain meaning" interpretation urged by the United States.[133] This conclusion was compelled because the statutory language in *Nierotko* was virtually identical to the FICA and FUTA "wages paid during a calendar year" language.[134] The *Nierotko* Court had no reservations in allocating the currently paid wages back to the year in which they should have been paid.[135] In other words, the *Nierotko* Court stated, at least tacitly, that statutory language such as "wages paid during a calendar year" is not sufficient to prevent the wages from being allocated back to the period in which they should have been paid.[136]

Mindful of the *Nierotko* decision, the *Cleveland Indians* Court stated that the FICA and FUTA provisions in question did not "have a plain meaning that preclude[d] allocation of backpay to the year it should have been paid."[137] This conclusion was necessary because, otherwise, the Court would have had to overrule *Nierotko* to find that the statutory language precluded allocation of backpay to the period in which the wages should have been paid.[138] Overruling *Nierotko* would have done more harm than good as the allocation back rule for social security benefits was an established rule of law that had likely been relied upon by many since the *Nierotko* decision.[139] The Court seemed to suggest that the question of overruling *Nierotko* was moot regardless as the Court may be bound be *stare decisis*.[140]

Russell L. Weaver, *Judicial Interpretation of Administrative Regulations: An Overview*, 53 U. CIN. L. REV. 681, n.67 (1984).

132. United States v. Cleveland Indians Baseball Co., 532 U.S. 200, 209 (2001).

133. *Id.* at 210-11.

134. *See id.*

135. *Id.*

136. *See* Social Sec. Bd. v. Nierotko, 327 U.S. 358, 370 (1946).

137. *Cleveland Indians*, 532 U.S. at 211.

138. *See id.* at 211-12. The Court noted that the United States did not even argue that *Nierotko's* allocation back rule for benefits eligibility purposes should be overruled. *Id.*

139. *See id. Nierotko* was decided in 1946, so at the time of the *Cleveland Indians* decision, *Nierotko's* allocation back rule had been a rule of law for about fifty-five years. Social Sec. Bd. v. Nierotko, 327 U.S. 358 (1946). Therefore, it is likely that employees and others had relied upon the rule as a wholly acceptable practice during this time and to overrule *Nierotko* may produce very undesirable results.

140. *Cleveland Indians*, 532 U.S. at 212. The Court noted in a parenthetical that "*stare decisis* is most compelling where a pure question of statutory construction is involved." *Id.* (quoting Hilton v. South Carolina Public Railways Comm'n, 502 U.S. 197, 205 (1991)).

D. Lack of symmetry between Social Security benefits and the tax code

Next, the Court rejected the Cleveland Indians' argument that because the language interpreted in *Nierotko* was the same as the "wages paid" language presently at issue, that the latter must be interpreted exactly as the former and allow backpay allocations to the time wages should have been paid.[141] The Court focused on the fact that *Nierotko* dealt with Social Security benefits and not with taxation.[142] The Court then *speculated* that the holding in *Nierotko* was based on the underlying benefits scheme in the Social Security legislation.[143] However, even a cursory reading of the *Nierotko* Court's decision as to the "allocation back" rule indicates that the Court did not explain the rationale for its decision to allow the "allocation back" rule.[144] Therefore, any proposed rationale for the *Nierotko* decision, including that given by the *Cleveland Indians* Court, constitutes pure speculation.

Admittedly, the rationale forwarded by the Court is plausible, but perhaps Occam's razor dictates a different rationale.[145] The more simple rationale for the *Nierotko* Court's decision may be more intuitive. If you are supposed to get $50,000 in year one, but an employer wrongfully withholds it until year three, to what year should we allocate the receipt?[146] One might believe that we should allocate payment back to year one, because that way we can mathematically create the illusion that the wrongful act never occurred.[147]

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141. *Cleveland Indians,* 532 U.S. at 212. The Court observed:

> Because *Nierotko* read the 1939 "wages paid" language for benefits eligibility purposes to accommodate an allocation-back rule for backpay, the Company urges, the identical 1939 "wages paid" language for tax purposes must be read the same way. We do not agree that the latter follows from the former like the night, the day.

Id.

142. *Id.* "*Nierotko* dealt specifically and only with Social Security benefits eligibility, not with taxation." *Id.*

143. *Id.* The Court stated: "[t]he Court's allocation holding in *Nierotko in all likelihood* reflected concern that the benefits scheme created in 1939 would be disserved by allowing an employer's wrongdoing to reduce the quarters of coverage an employee would otherwise be entitled to claim toward eligibility." *Id.* (emphasis added).

144. *See* Social Sec. Bd. v. Nierotko, 327 U.S. 358 (1946).

145. Occam's razor is a principle of logic that instructs one to make as few assumptions as possible in searching for an answer. Occam's Razor, *at* http://pespmc1.vub.ac.be/OCCAMRAZ.html (last modified Jul. 7, 1997). In other words, for many unknowns, there are an infinite number of possibilities and one should avoid making too many assumptions because the most simple or obvious answer is most often the correct one. *Id.*

146. Of course we would first hope that the person would ask "why does it matter to what year the payment is allocated?" *See supra* note 24 and accompanying text. In the present case, the obvious reason is that the tax liability of the employer and employee would differ from year one to year three. *Id.*

147. We can accomplish 'financial time travel' and undo the fact that an employer has

Again, the *Cleveland Indians* Court was concerned with the fact that refusal to apply an "allocation back" rule in *Nierotko* would reduce the quarters of coverage the employee would otherwise be able to claim, which would disserve the intent of the Social Security benefits provisions.[148] Because the Court found no similar concern underlying the tax code, the Court determined the two were different in kind.[149] In fact, the Court refused to apply a symmetrical construction of the "wages paid" language based on the aforementioned difference between the tax code and the Social Security provisions.[150]

Next, the Court noted that generally, identical words have the same meaning, but that it is not a bright-line rule as sometimes one word will have more than one meaning.[151] However, the Court did not fully justify treating the "wages paid" language as an exception to the rule instead of applying the general rule which assumes the same meaning. The Court also noted that ". . . to assume that a word which appears in two or more legal rules . . . . . " has the same meaning in both contexts, ". . . . . has all the tenacity of original sin. . . . . ."[152] While this rule generally makes sense, we are not dealing with one word. The term "wages paid"

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wrongfully withheld an employee's wages. At least financially, we can make it as if the wrongful act did not occur. It is true that the employee may be less than financially whole because of attorney's fees or other costs, but these would be a result of choice and policy, not inability.

148. *Cleveland Indians,* 532 U.S. at 212. The Court thought it would be unfair to allow an employer's wrongdoing to reduce the quarters of coverage an employee would otherwise be entitled to receive. *Id.* This author wonders why the Court does not find unfairness when the wrongful act of an employer causes an arbitrary increase in the employee's tax liability.

149. *Id.* at 212-13. The Court stated:

> Although Social Security taxes are used to pay for Social Security benefits in the aggregate, there is no direct relation between taxes and benefits at the level of an individual employee. As the Company itself acknowledges, "Social Security tax 'contributions,' unlike private pension contributions, do not create in the contributor a property right to benefits against the government, and wages rather than [tax] contributions are the statutory basis for calculating an individual's benefits."

Id. (citations omitted).

150. *Id.* The Court is correct in stating that the tax code is different from the Social Security Act. It is hard to imagine anyone arguing that FICA and FUTA are *exactly* the same. However, is that enough to treat them differently for purposes of backpay? This author asserts that simply proving one act to be different from another, proves very little. The Court did not go further and demonstrate why the difference was so stark as to warrant different treatment between FICA and the Social Security Act. Of course, apples are different from oranges, but that does not mean they should be put on opposite sides of the grocery store. Each is still a fruit. Here, the tax code and the Social Security Act are different, but they are the same in that they employed identical "wages paid" language. *See supra* note 134 and accompanying text. The Court did assert a reason for the different treatment of the tax provisions and the Social Security Act. This reasoning and a criticism of the reasoning is presented *infra* notes 158-181 and accompanying text.

151. *Id. See also supra* note 82 and accompanying text.

152. *Id.* (citing Cook, *supra* note 82, at 337).

is of course two words, which constitutes a phrase.[153]

Therefore, the Court used a false analogy by equating a rule for singular words to a rule applying to phrases.[154] Even if it is true that one word should not be assumed to always have the same meaning in a statute, this is not to say that a phrase cannot provide more accuracy in meaning than a single word.[155]

The Court committed the same error by relying on *Atlantic Cleaners & Dyers, Inc. v. United States*.[156] *Atlantic Cleaners* focused on the meaning of a single word, the word "trade" which is a word with a broad definition base.[157] Therefore, it is unfair to apply the same logic to the phrase "wages paid" because *Atlantic Cleaners* did not analyze whether a phrase duplicated in legislation should be assumed to mean the same in both places.

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153. A phrase is a "sequence of words intended to have a meaning." AMERICAN HERITAGE DICTIONARY (3d ed. 1994). While the difference between one word and two words may appear to be merely a hypertechnical difference, it is truly relevant because a single word may be accidentally used in two different pieces of legislation where the word has a different meaning in each statute.

154. A false analogy is described as follows:

> In an analogy, two objects (or events), A and B are shown to be similar. Then it is argued that since A has property P, so also B must have property P. An analogy fails when the two objects, A and B, are different in a way which affects whether they both have property P.

False Analogy, *at* http://www.datanation.com/fallacies/falsean.htm (last visited Feb. 1, 2002).

155. The following illustrates the difference: If Congress uses the word "wages" in a statute, most would agree that "wages" may be an ambiguous term, subject to numerous different meanings. However, if Congress instead used the phrase "gross wages," or "taxable wages" the meaning is clearer than "wages."

156. Atlantic Cleaners & Dyers, Inc. v. United States, 286 U.S. 427 (1932). *See also supra* note 82 and accompanying text. The Court cited *Atlantic Cleaners & Dyers, Inc. v. United States* for the proposition that identical words in the same act are generally intended to have the same meaning but that in certain circumstances, the meaning of words may vary depending on the "purposes of the law." United States v. Cleveland Indians, 532 U.S. 200, 213 (2001).

157. Atlantic Cleaners & Dyers, Inc. v. United States, 286 U.S. 427, 437 (1932). In fact, the word "trade" has at least seven different meanings – four meanings when used as a noun and three when used as a verb. AMERICAN HERITAGE DICTIONARY (3d. ed. 1994).

1. Intent of the respective statutes[158]

Central to the Court's decision was its belief that the Social Security statute analyzed in *Nierotko* differed in kind from the FICA and FUTA statutes.[159] However, the Court identifies the intent of the respective statutes much too narrowly. Under the Court's rationale, the language of two different statutes could never be entitled to a symmetrical interpretation because no two statutes have precisely identical intent.[160] The fact that one statute focused on Social Security benefits and the other two statutes focused on taxation was all the difference the Court needed to seal the statutes in separate and distinct logical compartments.[161]

However, for the Court, this narrow interpretation comes at the expense of any broader interpretation that is concerned with fairness and equity for the employer and employees. The Court made a value judgment, which determined that a future decrease in Social Security benefits is a greater evil than a present increase in tax liability.[162] This comparison ends up the same – the employer or employee ends up with less money and the government ends up with more.[163] Even Justice

158. Some object to the idea of analyzing intent and legislative history as a useful guide. Justice Scalia, a textualist, does not believe courts should turn to legislative history in an attempt to ascertain Congressional intent. Heen,*supra* note 98, at 782. Textualism limits an interpreter to a law dictionary, a regular dictionary, and generally the contents of the United States Code to determine the meaning of words in a statute. Deborah A. Geier, *Textualism and Tax Cases*, 66 TEMPLE L. REV. 445, 449 (1993). Justice Scalia generally finds clarity in every statute and therefore, does not need to look further. *Id.* Furthermore, Justice Scalia disapproves of references to "original intent" as he believes that the statutory language reflects the true legislative purpose. *Id.* at 450. This line of thinking was succinctly summarized by Oliver Wendell Holmes who said, "[w]e do not inquire what the legislature meant; we ask only what the statute means." *Id.* at 445.

Additionally, in ascertaining intent, it is interesting to note that conflicting canons of statutory construction have dismantled what once was statutory construction, now allowing judges to choose whether to look at legislative history based on the judge's desired result. *See* Zelenak, *supra* note 120, at 630. Long ago, Professor Karl Llewellyn identified twenty-eight pairs of contradictory canons of statutory construction used in judicial opinions. *Id.* Here, the most relevant pair is "[a] statute cannot go beyond its text," and "[t]o effect its purpose a statute may be implemented beyond its text." *Id.*

159. *Cleveland Indians*, 532 U.S. at 216. *See supra* note 150 and accompanying text.

160. *See id.*

161. *See id.* Justice Scalia noted in his concurrence:

> [T]he Court's principal reason for assigning the identical language a different meaning in the present case – leaving aside statements in testimony and Committee Reports that I have no reason to believe Congress was aware of – is that tax assessments do not present the equitable considerations implicated by the potential arbitrary decrease of benefits in Nierotko.

Cleveland Indians, 532 U.S. at 220-21 (citation omitted).

162. *Cleveland Indians*, 532 U.S. at 220.

163. *See id.*

Scalia suggested in his concurrence that the "statutory intent" distinction the Court attempted to make, may in truth be an illusory distinction.[164]

Furthermore, the Court believed that the concern in the Social Security statute was worker eligibility for benefits, whereas the FICA and FUTA provisions were concerned with fiscal administrability.[165] However, looking at the facts presented in *Cleveland Indians*, it is wholly unclear why a system that taxes in the year of receipt is more easily administered than a system that taxes as of the time the wages should have been paid. In the instant case, the more administrable method would have been to allocate the wages back, because doing so would create no additional tax liability for the Cleveland Indians or the employees receiving the wages.[166] What could be more fair or administrable? According to the Supreme Court it is easier and more administrable to allocate the wages to the year in which they are paid, thereby creating two different tax rates for wages earned in a single year.[167]

2. Ease of administration

For FICA and FUTA purposes, there is no inherent difficulty in attributing wages to the period in which they were earned. In any year, the process is the same – you simply multiply the wages by the applicable tax rate (which depends on the year the wages are attributable to) and apply the statutory cap which limits the amount of wages subject to the tax.[168]

First, the wages subject to the tax will be the same regardless of the

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164. *Id.* Justice Scalia wrote:

> But the Court acknowledges that departing from Nierotko will produce arbitrary variations in tax liability. As between an immediate arbitrary increase in tax liability and a deferred arbitrary decrease in benefits, I cannot say the latter is the greater inequity. The difference is at least not so stark as to cause me to regard the two regulatory schemes as different in kind, which I would insist upon before giving different meanings to identical statutory texts.

Id. at 221 (citations omitted).

165. *Cleveland Indians,* 532 U.S. at 212-13. The Court believed that the purpose of an act focused on worker eligibility for benefits would be frustrated by refusing to apply an allocation back rule for wages, but apparently the Court did not feel there was any risk of frustrating the FICA and FUTA statutes which the Court believed to be focused on fiscal administrability. *Id.*

166. *Cleveland Indians,* 532 U.S. at 206. The employees and the employer (Cleveland Indians) already paid taxes in the past years up to the statutory ceiling. *Id.*

167. This assumes, as in the case of the Cleveland Indians, that a different tax rate existed when the second set of wages was paid. *See supra* note 22 and accompanying text.

168. *See supra* note 22 and accompanying text.

applicable tax period.[169] Therefore, this "wages" part of the formula generally plays no relevance in determining which tax method is more easily applied.[170]

Second, regardless of the year to which the wages are attributed, one must still look at the statute to determine the applicable tax rate.[171] In other words, applying the tax rate in which the wages are received is no simpler than using the rate in effect when the wages should have been paid, because either way you must refer to the statute.[172]

Third, you apply the statutory cap only after you have decided to which year the wages are attributable.[173] This cap may be different depending on the year to which the wages are attributed.[174] However, just as with the applicable tax rate, you will have to look at the statute to determine the statutory cap regardless of what year to which the wages are attributable.[175] Therefore, attributing the wages to the year they are actually paid is no easier than attributing the wages to the periods in which they should have been paid because no calculations are spared by doing the former.[176] In fact, the latter will often be easier, as it would have been for the Cleveland Indians, because the employer may have already met the statutory cap for the year the wages should have been paid.[177] In this case, there is no need to go through any calculations.[178]

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169. That is not to say that the amount of tax will be the same. It means that if you earned $50,000, regardless of when you receive it, you receive $50,000 (exclusive of interest and other considerations). *See supra* note 24 and accompanying text. It is only once you have a determined amount of wages that you can begin the tax analysis. *Id.*

170. What this generally will affect, especially when using the allocation back rule, is whether the wages are beyond the statutory cap for a given year. *See supra* note 24 and accompanying text. However, this has to do with the statutory cap, which cannot be applied until you have already decided what year the wages are attributable to. *See supra* notes 22-24 and accompanying text.

171. *See supra* note 22.

172. *Id.* Assume the wages should have been paid in 1987, but instead, the wages are paid in 1990. Whether you attribute the wages to 1987 or to 1990 you will have to refer to the statute to know what tax rate applies. *Supra* note 24. Therefore, neither system is per se easier to apply.

173. *See Cleveland Indians*, 532 U.S. at 208. This statutory cap differs from year to year, so you must first know what tax year applies before you can apply the statutory cap. *Supra* note 22.

174. *Id.* For example, in the year 2000, the cap stood at the first $76,200 of wages, whereas in 2001 the cap was $80,400. I.R.S., Dep't of the Treasury, Pub. No. 15, Circular E, Employer's Tax Guide (2001).

175. *See supra* note 24.

176. Authors note: The Court never really explains why an "actually paid" standard is more easily applied than a "allocation back" rule. Therefore, this author is not certain what accounting difficulties the Court fears. One would think that the accounting difficulties would be at least as present when applying an "allocation back" rule in the Social Security benefits context, but the Court was willing to carve out an exception for just that in *Nierotko*. *See supra* note 36.

177. *See supra* note 166 and accompanying text (stating that the Cleveland Indians had already paid up to the statutory cap and would not be subject to any tax under an "allocation back" rule).

178. *See supra* note 166 and accompanying text. Once you apply the statutory cap and find

Furthermore, the Court insists upon an "ease of administration" reasoning for attributing wages to the period where they are paid.[179] The Court pointed out that Congress knew an employee's annual wages might be "based on a percentage of profits, or on future royalties, the amount of which cannot be determined until long after the close of the year."[180] When the delay in wages is merely an annually recurring administrative delay, it may be reasonable to tax the wages when actually received. However, this is not a valid reason to tax a one-time back pay award in the year it is actually received when the delay is not attributable to an administrative accounting delay.[181]

E. Inequities in taxation and the potential for strategic behavior

The Cleveland Indians explained that under the United States' proposed rule, some wages that should not be taxed would be taxed and some wages that should be taxed would not be taxed.[182] The Cleveland

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that the employer has paid up to the cap for the applicable year, you do not have anything left to calculate. If ease of administration is what you are looking for, it does not get any easier than this because there is no tax to levy or to pay.

179. *Cleveland Indians*, 532 U.S. at 214. The Court stated:

> The 1939 Amendments adopting the "wages paid" rule for taxation reflected Congress' worry that, as tax rates increase from year to year, "difficulties and confusion" would attend the taxation of wages payable in one year, but not actually paid until another year. Congress understood that an employee's annual compensation may be "based on a percentage of profits, or on future royalties, the amount of which cannot be determined until long after the close of the year." Requiring employers to "estimate unascertained amounts and pay taxes and contributions on that basis" would "cause a burden on employers and administrative authorities alike." Congress correctly anticipated that "[t]he placing of [FICA and FUTA] tax[es] on the 'wages paid' basis [would] relieve this situation." "Under the amendment the rate applicable would be the rate in effect at the time that the wages are paid and received without reference to the rate which was in effect at the time the services were performed."

Id. (citations omitted).

180. *Id.* (quoting S. Rep. No. 734, 76th Cong., 1st Sess., at 75). The Court does not explain what they mean by using this quote, but it is not too hard to imagine a situation using the example of wages. Assume that an employee on the last day of the year, December 31st. Unless the employee is being paid cash, we know that the employee will not be paid on the on the 31st for her work on the 31st. In these situations we all know that the employee will receive her paycheck and include it as income in the following year. However, the Court does not explain why a rule that applies to wages that are subject to an administrative delay should be treated the same as *wrongfully withheld* wages that are not subject to a mere administrative delay.

181. An "allocation back" rule is not necessary for the common administrative delay. Most employees expect such a delay. However, the Court's reasoning does not apply with equal force to a one-time lump sum, as was the subject of the *Cleveland Indians* litigation. *See supra* note 56.

182. *Cleveland Indians*, 532 U.S. at 217.

> Under the Government's rule, an employee who should have been paid $100,000 in 1986, but is instead paid $50,000 in 1986 and $50,000 in backpay in 1994, would owe more tax than if she had been paid the full $100,000 due in 1986. Conversely, a

Indians demonstrated additional instances where the United States' proposed rule would create the potential for strategic behavior.[183] The argument the Cleveland Indians presented seemed to make a great deal of sense: strategic behavior can be eliminated and fairness can be maximized by attributing backpay awards to the period in which they should have been paid.[184]

The Court, however, was content to point out that Congress often places fairness at war with efficient administration in the tax code.[185] In this instance, fairness was slain by administration. Further, the Court felt that unfairness is acceptable as long as it falls arbitrarily on either the government or the taxpayer.[186] However, there are at least two problems with this reasoning.

First, we are not just dealing with the government and a single taxpayer. We actually have two taxpayers, the employer and the employee.[187] The employer is given incentive to withhold wages and pay them all at once in a later year so the employer will only have to claim one years worth of FICA. If the wages were attributed back to the period in which they should have been paid, the employer would not

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> wrongdoing employer who should have paid an employee $50,000 in each of five years covered by a $250,000 backpay award would pay only one year's worth of employment taxes (limited by the annual ceiling on taxable wages) in the year the award is actually paid. The Government's rule thus appears to exempt some wages that should be taxed and to tax some wages that should be exempt.

Id.

183. *Id.* Another example arises from the fact that in the case of disability benefits, because benefits included in a backpay award would be exempt from FICA if the employee was not working for the employer six months prior to the award, regardless of whether the benefits should have been paid within that six month window. *Id.*

184. *Id.* For and example of how strategic behavior is likely to occur see *supra* note 182.

185. *Cleveland Indians*, 532 U.S. at 218.

> Given the practical administrability concerns that underpin the tax provisions, we cannot say that the Government's rule is incompatible with the statutory scheme. The most we can say is that Congress intended the tax provisions to be both efficiently administrable and fair, and that this case reveals the tension that sometimes exists when Congress seeks to meet those twin aims.

Id.

186. *Id.* at 217. The Court distinguished this from *Nierotko* and the Social Security benefits provisions by pointing out that under the Social Security benefits provision, allocating backpay to the period *in which it is received* could never work in favor of the employee. *Id.* at 218.

> The Government's rule sometimes disadvantages the taxpayer, as in this case. Other times it works to the disadvantage of the fisc, as the Company's examples show. The anomalous results to which the Company points must be considered in light of Congress' evident interest in reducing complexity and minimizing administrative confusion within the FICA and FUTA tax schemes.

Id. (citation omitted).

187. *See supra* note 22 (explaining that FICA is levied against both employer and employee).

have an incentive to cheat because he knows he will be liable for taxes in each year he employed the employee.

Second, this rationale ignores the fact that the employee, the "small guy," is the one most often hurt and any windfall benefit to the employee will likely be illusory. As a matter of fairness, when the government has drafted a statute such as the FICA statute at issue here, it seems equitable to give the benefit to the taxpayer because a few thousand dollars is worth more to the employee than the government.[188] If the legislature meant to say something else in the legislation, they may now do so and thereafter, the law will be crystal clear for all parties.

Additionally, when the employee may appear to have benefited by receiving a backpay award that is taxed in one year instead of two years, the employee has probably not truly benefited.[189] It is true that the employee will pay FICA for only one year and therefore "escape" a second year of FICA taxes if we attribute wages to the year in which they are received.[190] However, this hardly benefits the employee. Assuming the first year for the employee is 1986, the employee would have been liable for $2,394 in FICA taxes.[191] He will save this amount in FICA taxes and pay only in 1987, where his FICA tax will equal $2,496.60.[192] Therefore, if the wages were paid as they should have been the employee would have paid $4,890.60[193] in FICA tax but instead will only be liable for the $2,496.60 in 1987.[194]

The employee has saved a couple thousand dollars in FICA taxes, but is this truly a desirable consequence? After all, the employee had no income to show in 1986. Given the choice, would an employee choose to receive no salary for a year in exchange for a $2,394 tax savings? It is highly unlikely that the average employee could afford this deferral.

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188. The FICA taxes at issue in *Cleveland Indians* were less than $100,000 total for eight employees, or an average of about $12,400 per player. *Cleveland Indians*, 532 U.S. at 207. Of course, one could argue that taxes are worth more to the taxpayer than the government and therefore, the benefit should always fall on the taxpayer's side. This is an unacceptable argument where the tax code is clear, but the argument is very attractive where the legislature has not made the law clear. In these cases, a contra proferentum approach may be appropriate.

189. For purposes of this example, we will assume the employee should have been paid $50,000 per year for two years, but the employer wrongfully withholds the pay and subsequently pays $100,000 in year two. *See supra* note 182.

190. *See supra* note 182. Instead of paying taxes on $50,000 in year one and $50,000 in year two, the employee will pay tax FICA tax on $100,000 in year two and no FICA tax in year one.

191. *Cleveland Indians*, 532 U.S. at 205-06. In 1986, the tax rate was 5.7 percent on wages up to $42,000 (5.7 percent x $42,000 = $2,394). *Id.*

192. *Id.* In 1987, the tax rate was 5.7 percent on wages up to $43,800 (5.7 percent x $43,800 = $2,496.60). *Id.*

193. ($2,394 + $2,496.60 = $4,890.60)

194. *See supra* note 182.

Additionally, the employee may have to hire an attorney and sue to obtain the wages. Litigation would likely consume any tax savings the employee might have realized.

It is true that an allocation back rule in this precise instance would do more harm than good because the employee would be liable for about twice as much tax and the employee still went a year without pay.[195] However, if wages were allocated back, the employer's incentive to wrongfully withhold wages for FICA purposes disappears.[196] This incentive is likely the greatest concern of the employee. In other words, most employees would be happy to receive their wages and pay the FICA tax as opposed to saving $2,500 in FICA taxes and not receiving wages for an entire year or more. The point is that contrary to the Court's assertion, the employee does not truly win just because they might save a couple thousand dollars under a "taxed when received" rationale, because the Court's position fails to account for many relevant factors.[197] Therefore, the FICA provision is much more like the Social Security statute than the Court would have you believe, because allocating wages to the year in which they are actually paid does not *truly* benefit the employee.[198]

V. CONCLUSION

In deciding the *Cleveland Indians* case, the Court ignored some very convincing arguments for statutory symmetry in the Social Security benefits provisions interpreted in *Nierotko* and the Social Security tax provisions. In addition, the Court failed to provide adequate support for its decision to ignore *Nierotko's* authority, which provided uniformity and predictability. Finally, the Court fueled ambiguity in the tax code because the Court appears to treat the tax code definitions as wholly isolated from any language that would otherwise rationally inform the tax code.

Jeffrey C. Honaker

195. *Id.* For an illustration of this concept, see *supra* notes 189-194 and accompanying text.

196. *See supra* note 182 and accompanying text. This of course assumes that the employer, who knows that he owes a tax, will in fact pay it. Any employer can withhold wages if he so chooses, but the point here is that an employer has more to gain from withholding wages under a "when received" rule than under an "allocation back" rule. *See id.*

197. *See supra* notes 184-97 and accompanying text.

198. *See supra* notes 184-97 and accompanying text (explaining that the apparent benefits an employee receives under a "wages paid" rule are more than consumed by other non tax factors).