



CIRCULAR

STATE OF NEW JERSEY

DEPARTMENT OF THE TREASURY

NO.: 06-10-OMB	ORIGINATING AGENCY: OFFICE OF MANAGEMENT AND BUDGET	PAGE 1 OF 3
EFFECTIVE DATE: 04-10-06	EXPIRATION DATE: INDEFINITE	SUPERSEDES: 02-08-OMB (FORMATTING CHANGES ONLY)
SUBJECT: PAYMENT OF LAWSUIT AWARDS AND SETTLEMENTS		
ATTENTION: DIRECTORS OF ADMINISTRATION AND CHIEF FISCAL OFFICERS		
FOR INFORMATION CONTACT: MICHAEL W. HENRY		PHONE: (609) 292-0051

I. PURPOSE

The State of New Jersey is required to determine whether payments of lawsuit awards and settlements are taxable income to recipients in accordance with Internal Revenue Service regulations. This circular relates solely to taxability under the Internal Revenue Code.

In accordance with NJSA 59:11-1, payments of **all** tort claims or claims for indemnification against the State must be recommended by the Attorney General or his designee. In addition, payments of tort claims or claims for indemnification **exceeding \$7500** must be approved by the Director, Office of Management and Budget (OMB).

II. CRITERIA

Guidelines on whether a lawsuit award or settlement is taxable are as follows:

A. Taxable

1. All punitive damages, whether received in relation to a physical or non-physical injury.
2. Compensatory damages, if received in relation to a non-physical injury. Includes payments for emotional distress due to employment discrimination.
3. Interest on awards and settlements.

B. Non-Taxable

1. Compensatory damages, if received in relation to a physical injury or sickness. Includes payments for emotional distress due to physical injuries or sickness.
2. Payments received for out-of-pocket medical expenses incurred to treat physical injuries or sickness.

3. Payments received for out-of-pocket medical expenses incurred to treat emotional distress due to either physical or non-physical injuries or sickness.

C. Back Pay

1. A payment made to an employee or former employee representing back pay is considered wages for employment tax purposes.

III. AGENCY PROCEDURES

Agencies must insure that the procedures below are followed when processing a settlement for payment.

- A. If the award or settlement recommended by the Attorney General's office is not back pay and the full amount is paid to the claimant or jointly to the attorney and claimant, agencies should :

1. Obtain a Settlement Agreement and Final Release.
2. Obtain a completed W-9. Claimant's social security number or attorney's employer identification number will become the vendor ID.
3. Complete a State of New Jersey Payment Voucher. If the payment is:
 - a) Taxable and paid to claimant: Use the claimant's vendor ID and charge object code 5811, Lawsuit Awards and Settlements – Taxable.
 - b) Taxable and paid to attorney: Use the attorney's vendor ID and charge object code 5812, Lawsuit Awards and Settlement Fee – Taxable.
 - c) Taxable and paid jointly to claimant and attorney: Use the attorney's vendor ID and charge object code 5812, Lawsuit Awards and Settlement Fee – Taxable.
 - d) Non-Taxable: Use the appropriate vendor ID and charge object code 5813, Lawsuit Awards and Settlements – Non-Taxable.
 - e) Interest paid to claimant or attorney: Use the appropriate vendor ID and charge object code 3857, Interest Payment – Settlement.
4. Payment Approvals:
 - a) If payment exceeds \$7500, the claim must be submitted to OMB's Accounting Bureau for approval by the Director, OMB in accordance with NJSA 59:11-1. Items 1-3 above should be included in request for approval.
 - b) Accounting transactions requiring OMB approval **should not be fully approved** in NJCFS by the agency. OMB will apply the final level of approval.
 - c) OMB approval is not required for claims less than \$7500.

- B. If the award or settlement directs the State to pay the claimant's attorney fees exclusive of the award:
1. Obtain a Settlement Agreement and Final Release.
 2. Obtain a completed W-9. Attorney's employer identification number will become the vendor ID.
 3. Complete a State of New Jersey Payment Voucher. Use the attorney's vendor ID and charge object code 3630, Legal Services – Lawsuit Awards and Settlements.
 4. Payment Approvals: See A. 4 above.
- C. If the award or settlement recommended by the Attorney General's office is back pay for any amount, provide OMB Centralized Payroll with the following:
1. Settlement Agreement and Final Release.
 2. Supplemental Payroll Proof for payment to the recipient.
 3. Indication of the salary account to be charged.

Note: When an award or settlement contains several different types of payments, each type must be handled as noted above. For example, if both back pay and taxable damages are included in the award or settlement, each payment must be processed separately.

IV. ISSUANCE OF FORMS 1099 AND W-2

Taxable payments of lawsuit awards and settlements must be reported to the Internal Revenue Service using Forms 1099 or W-2.

- A. By using object code 5811 and the claimant's vendor ID, a 1099-MISC will be issued to the claimant by OMB, reporting the payment amount as Other Income.
- B. By using object code 5812 and the attorney's vendor ID, a 1099-MISC will be issued to the attorney by OMB, reporting the payment as Gross Proceeds Paid to an Attorney.
- C. By using object code 3630 and the attorney's vendor ID, a 1099-MISC will be issued to the attorney by OMB, reporting the payment amount as Other Income.
- D. By using object code 3857, a 1099-MISC will be issued to the claimant or attorney by OMB, reporting the payment amount as Interest Income.
- E. For back pay settlements or awards, OMB Centralized Payroll will issue a W-2 to the claimant.

Charlene M. Holzbaur
Director