



Office of the Secretary
Department of Finance



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Memorandum

Date : November 12, 2021 SFM 2022-022

To : All Federal Employees

From : Secretary, Department of Finance

Subject : **Commonwealth of the Northern Mariana Islands (CNMI), Division Revenue and Taxation (DRT) Announcement 2021-1 –Taxation of Cost-of-Living Allowances (COLA) paid to Federal employees under the CNMI Wage and Salary Tax (WST)**

The purpose of this announcement is to provide guidance regarding imposition of the CNMI wage and salary tax on cost-of-living allowances paid to federal employees.

Background

COLA is established under 5 U.S. Code § 5941, which provides for additional payments to employees based on living costs and conditions of environment for federal employees stationed outside continental United States or Alaska.¹ Specifically, 5 U.S. Code § 5941 states, in relevant part:

- (a) Appropriations or funds available to an Executive agency, except a government-controlled corporation, for pay of employees stationed outside the continental United States or in Alaska whose rates of basic pay are fixed by statute, are available for allowances to these employees. The allowance is based on—
- (1) living costs substantially higher than in the District of Columbia.
 - (2) conditions of environment which differ substantially from conditions of environment in the continental United States and warrant an allowance as a recruitment incentive; or
 - (3) both of these factors.

The purpose of COLA is to enable a federal employee in a non-foreign area to maintain purchasing power similar to that of a comparable federal employee in Washington, D.C. See Report by United States General Accounting Office, FPCD-81-48 (May 13, 1981).

The United States Office of Personnel Management (OPM) establishes COLA rates based on price differences between the COLA area and the Washington, DC area. 5 C.F.R. § 591.208. OPM calculates COLA by using categories for various consumer expenditures and assigns weights for each expenditure type. *Id.* Housing constitutes one of nine major expenditures

¹ Federal employees stationed in the CNMI are entitled to COLA as part of the Guam/CNMI COLA area. 5 C.F.R. § 591.201.

OPM calculates COLA by using categories for various consumer expenditures and assigns weights for each expenditure type. *Id.* Housing constitutes one of nine major expenditures groups factored into OPM's calculations for a COLA area. *See* 5 C.F.R. § 591.211. Other categories of expenditures include food; clothing; transportation; household furnishings and supplies; medical; education and communication; recreation; and miscellaneous. *Id.*

Analysis/Discussion

The CNMI WST does not have an exclusion for COLA payments. Under 4 CMC § 1201, the CNMI imposes a tax on an employee's total wages and salaries. The definition of "wages and salaries" is as follows:

- (dd) "Wages and Salaries" means the total amount of money or the value of other consideration received by an employee to the extent that such money or other consideration is received for services sourced within the Commonwealth. Wages and salaries shall not include:
- (1) Wages and salaries received from the United States by active members of the Armed Forces of the United States.
 - (2) Reasonable per diem and travel allowances to the extent that they do not exceed any comparable Commonwealth Government rates.
 - (3) Rental value of a home furnished to any employee, or a reasonable rental allowance paid to any employee to the extent the allowance is used by the employee to rent or provide a home.
 - (4) Any payment of medical or hospitalization expenses or insurance premium paid by an employer or insurance company to or on behalf of an employee or insured.
 - (5) Payments made to or on behalf of an employee or to his beneficiary from the CNMI Retirement program or a plan that qualifies under Subchapter D, Subtitle A of the NMTIT to the extent allowed under NMTIT § 402(G)(1).
 - (6) Any payment in the form of a scholarship, fellowship, grant, stipend or the like made to any student while he is a full-time, bona fide student at an educational institution as defined by § 170(b)(1)(A)(ii) of the NMTIT. Provided, however, that if the payment is made for services rendered, the student must receive college credit(s) for the performance of the services and the services must further the student's education, curriculum, or course of study.
 - (7) Any benefit payment from the United States, Trust Territory, or Northern Marianas Social Security Administration

4 CMC § 1103(d)(d).

Subsection (3) of section 1103 provides an exclusion from WST for reasonable rental allowances paid to an employee to the extent the allowance is used by the employee to rent or provide a home. COLA payments compensate employees for cost of living increases in nine categories of expenditures, with housing being one category. Therefore, COLA payment amounts that are attributable to housing, which OPM calculates based on the comparative cost difference between housing in Guam/CNMI and the Washington, DC area, are the only amounts that are excludable under 4 CMC § 1103(d)(d)(3). COLA payment amounts that are attributable to the other eight categories (food, clothing,

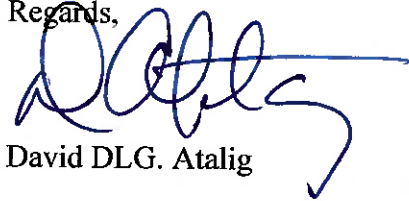
transportation, household furnishings and supplies, medical, education and communication, recreation, and miscellaneous) are subject to the WST.

Therefore, in computing WST, COLA recipients are only permitted to exclude from “wages and salaries” the portion of COLA allocated to housing, which is the comparative cost difference between housing in Guam and the Washington, DC area, if such amounts are actually used to rent or provide a home.

Any compensation received by an employee, other than the amounts actually used for housing, does not fall within any other exclusion provided under Section 1103(d)(d).

Any questions regarding this announcement may be sent to info@dof.gov.mp or you may call the Division of Revenue & Taxation at 670-664-1040.

Regards,

A handwritten signature in blue ink, appearing to read 'D. Atalig', with a long horizontal stroke extending to the right.

David DLG. Atalig