**New York State Department of Taxation and Finance**
**Office of Counsel**

TSB-A-20(5)I
Income Tax
October 20, 2020

STATE OF NEW YORK
COMMISSIONER OF TAXATION AND FINANCE

ADVISORY OPINION

The Department of Taxation and Finance received a Petition for Advisory Opinion from [ REDACTED ] (Petitioner). Petitioner asks about the personal income tax consequences of distributions from the Suffolk County 401(a) Terminal Pay Plan (the Plan) and other eligible retirement plans that are funded, at least in part, by a lump sum distribution transferred in a direct trustee to trustee transfer from the Plan to another retirement plan.

We conclude that the Plan distributions and other eligible retirement plan distributions funded with rollover contributions from the Plan do not qualify for the subtraction modification under Tax Law § 612(c)(3)(i). However, those distributions will qualify for the $20,000 subtraction modification under Tax Law § 612(c)(3-a) to the extent that the pension distributions are included in Petitioner's federal adjusted gross income (FAGI) and otherwise meet the requirements of that section.

**Facts**

Petitioner is employed by a county in New York State. He is a union member of the County's Detectives Association, Inc., (DA). In 2015, the County changed the way the monetary value of a DA employee's sick, personal, vacation and veterans leave is paid upon retirement.[1] Previously, the value of any accumulated sick, personal, vacation and veterans leave was paid in cash.[2] Beginning in 2015, and pursuant to a Memorandum of Agreement between the DA and the County, the parties agreed to mandatory participation of all DA bargaining unit employees in the Plan.[3]

Under the terms of the agreement, the County agrees to contribute to the Plan the monetary value of an employee's accumulated leave at retirement up to the Internal Revenue Code (IRC) § 415(c) limits allowed for IRC § 401(a) plans that would otherwise be paid to participants in cash at retirement. No other contributions or elective salary deferrals are allowed. DA employees do not have the option to receive a cash payment for accumulated leave in lieu of this contribution. However, the excess of any contributions to the Plan above the IRC § 415(c) limits, if any, will be paid to the employee in cash at retirement. Also, the amounts contributed to the Plan are always 100% vested in the employee; the employee chooses how the amounts are invested; and the balance of the employee's account is immediately available for withdrawal by the employee at any time after

[1] Employees who separate from service for any reason other than retirement will be ineligible to participate in the Plan.
[2] The literature from the Plan administrator states that the Plan was set up to help governmental units and their employees save up to 7.65% of Social Security and Medicare taxes and to defer income taxes for employees on eligible Plan contributions.
[3] The County and various employee bargaining units have also negotiated the Plan into their respective employment agreements.

retirement. The literature distributed by the Plan administrator states that no income tax is imposed on the employee for the amounts contributed until money is withdrawn from the Plan. It also states that funds may be rolled over to an IRA or other eligible retirement plan, which results in continued deferral of a participant's income tax obligation after money is withdrawn from the Plan.[4] Petitioner asks whether a cash distribution to Petitioner from the Plan or from funds that were rolled over from the Plan to an IRA or other eligible retirement plan are subject to New York State income tax.

**Analysis**

The New York taxable income of a resident individual is the individual's New York adjusted gross income (NYAGI), less his or her New York deduction and New York exemptions. Tax Law § 611(a). Tax Law § 612(a) states that the NYAGI of a resident individual means the individual's FAGI with the modifications specified in Tax Law § 612. Tax Law § 612(c)(3)(i) provides that, to the extent includible in gross income for federal income tax purposes, pensions paid to officers and employees of New York State, its subdivisions, and agencies will be subtracted from an individual's FAGI in computing NYAGI. Section 112.3(c)(1) of the New York State Personal Income Tax Regulations (Regulations) provides that pensions and other retirement benefits (including, but not limited to, annuities, interest and lump sum payments) paid to a public officer or public employee will qualify for the subtraction modification pursuant to Tax Law § 612(c)(3)(i) if the benefits relate to the services performed by the public officer or public employee and all or a portion of the benefits are actually contributed (rather than merely being deemed contributed) by New York State, its political subdivisions and its agencies. 20 NYCRR 112.3(c)(1)(i)(a).

In addition to the modification above, up to $20,000 of income from pensions and annuities that are not subject to the subtraction modification provided by Tax Law § 612(c)(3) is eligible for the subtraction modification provided by Tax Law § 612(c)(3-a) if certain requirements are met: (1) the pension and annuity income must be included in FAGI, (2) the taxpayer must be age 59 ½ or over, (3) the distributions must be periodic payments (except for distributions from an IRA or a self-employed retirement plan - Keogh), (4) the pension and annuity must be attributable to personal services performed by the individual prior to his retirement from employment, and (5) the distributions must arise from an employer-employee relationship or from contributions to a retirement plan that are tax deductible under the IRC. Tax Law § 612(c)(3-a); *see also,* 20 NYCRR 112.3(c)(2)(i)(a)-(d).

In order to determine if the distributions from the Plan qualify as pensions paid to a public officer or public employee under Tax Law § 612(c)(3)(i), it must be determined if the benefits relate to the services performed by Petitioner. 20 NYCRR 112.3(c)(1)(i)(a). In this case, participation in the Plan is mandatory and limited to the County employees who retire directly from service with the County. Therefore, Petitioner can accumulate benefits in the Plan only if he is an employee of the County at the time of his retirement. Accordingly, benefits from the Plan are related to Petitioner's service as a public employee within the meaning of Regulation § 112.3(c)(1)(i).

In addition, 20 NYCRR 112.3(c)(1)(i) requires that all or a portion of the retirement benefits are actually contributed to, rather than merely being deemed contributed to, by the County. In this case, the County, both prior to the establishment of the Plan, and currently, provides its employees with

[4] This opinion expresses no advice as to the federal tax consequences of these transactions.

sick, personal, vacation and veterans leave benefits each year. The amount of leave earned by an employee, the provisions governing the use of leave accruals and the ability to carry over unused leave credits to future years have not changed or been enhanced due to the Plan's establishment. Also, the accrued leave benefits, both prior to establishing the Plan and after, remain 100% vested in the employee when the leave benefits are earned. Prior to establishing the Plan, the employee had a right to receive the cash value of his or her accrued leave at retirement. After establishing the Plan, the employee still maintains a 100% vested right to the accrual pay made to the Plan and will be able to withdraw the account balance. Changing the method for paying at retirement an employee's accrued leave benefits does not change the character of the payment. The contribution of the monetary value of an employee's accrued leave benefits to the Plan pursuant to the Memorandum of Agreement between the DA and the County is not an actual contribution of retirement benefits by the County within the meaning of Tax Law § 612(c)(3)(i). Therefore, the distributions from the Plan or another retirement plan funded with the Plan distributions do not qualify for the subtraction modification under Tax Law § 612(c)(3)(i). However, the distributions may qualify for the subtraction modification under Tax Law § 612(c)(3-a) to the extent that the pension distributions are included in Petitioner's federal adjusted gross income (FAGI) and otherwise meet the requirements of that section.

In a prior advisory opinion, TSB-A-09(10)I, the Department concluded that distributions from a taxpayer's IRC § 403(b) tax deferred annuity ("TDA") rolled over to an IRA qualified for the public pension exclusion under Tax Law § 612(c)(3)(i) and 20 NYCRR 112.3(c)(1). In that opinion, the collective bargaining agreement entered into between a school district and the union representing teachers and other employees required the district to contribute an amount equaling the cash value of 40% of taxpayer's accrued sick leave to the TDA upon the employee's retirement (up to the contribution limits under IRC § 415), and further provided that employees could not receive a cash payment for the accrued sick leave instead of the mandatory contribution to the TDA. Because Petitioner was not allowed to receive cash for the accrued sick leave, and the bargaining agreement required the district to pay over the value of the accrued sick leave to the TDA, the opinion concluded that the sick leave benefits were actually contributed to the TDA by the district and the TDA qualified as a public pension plan under Tax Law § 612(c)(3)(i) and Regulation 112.3(c)(1).

We believe TSB-A-09(10)I fails to properly interpret the employer contribution requirement of 20 NYCRR 112.3(c)(1) and reaches an incorrect conclusion. In this earlier advisory opinion, the requirement to contribute a portion of a school district employee's previously earned and unused sick leave at retirement to the TDA, or to pay the employee in cash for such accrued leave if the IRC § 415(c) limits were exceeded, did not change the character of the TDA from a plan that is fully funded by employee contributions into a public pension plan where an employer makes authorized contributions in addition to what the employee contributes. The value of the accrued sick leave contributed to the TDA was not an employer contribution within the meaning of Tax Law §

612(c)(3)(i) and 20 NYCRR 112.(3)(c)(i), and the distributions from the TDA or any other distributions from another retirement plan funded with the TDA distributions do not qualify for the subtraction modification under Tax Law § 612(c)(3)(i).[5] Therefore, the conclusions in TSB-A-09(1)I to the extent they conflict with the advice herein are incorrect.

DATED: October 20, 2020

/S/
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NOTE: An Advisory Opinion is issued at the request of a person or entity. It is limited to the facts set forth therein and is binding on the Department only with respect to the person or entity to whom it is issued and only if the person or entity fully and accurately describes all relevant facts. An Advisory Opinion is based on the law, regulations, and Department policies in effect as of the date the Opinion is issued or for the specific time period at issue in the Opinion. The information provided in this document does not cover every situation and is not intended to replace the law or change its meaning.

[5] It is also noted that Education Law § 3109 only authorizes a school district, in its discretion, to enter into a written agreement with any employee of such school district or board to reduce the annual salary of the employee for purposes of purchasing an annuity or investing in a custodial account as permitted under IRC § 403(b) and does not provide for other contributions.