



Advisory Opinion: TSB-A-24(8)I

The Department of Taxation and Finance received a Petition for Advisory Opinion from [REDACTED]. Petitioner asks whether a distribution of funds from a tax deferred annuity (TDA), administered by the Teachers' Retirement System of New York City (TRS NYC), is exempt from New York State and New York City income taxes under two scenarios: (1) the beneficiaries take a lump sum distribution from the TRS NYC TDA after the death of the annuity owner, and (2) the beneficiaries take distributions after rolling over TRS NYC TDA funds from the decedent account owner to an inherited individual retirement account (IRA), which distributions may include earnings accrued after TDA funds are rolled over to the IRA. We conclude that (1) a lump sum distribution from the TDA will be tax exempt from New York State and City income taxes; and (2) the distribution of funds from the inherited IRA will be exempt from New York State and City income taxes only to the extent of the amount of the TDA funds rolled over to the inherited IRA. Any gains accrued on the IRA after the date the TDA funds were rolled over to the inherited IRA are subject to New York State and City income tax unless the accrued gains qualify for the exclusion under Tax Law § 612(c)(3-a).

Facts

Petitioner is the executor and a beneficiary of the estate of a New York City public school teacher. The decedent was 75 years old at the time of her death and had been taking required minimum distributions from the TRS NYC TDA. Petitioner, and others, inherited funds from decedent's TRS NYC TDA. Petitioner asks to what extent the inherited distributions from the TRS NYC TDA are tax exempt under the following two situations.

Situation 1: the beneficiaries take a lump sum distribution from TRS NYC TDA after the death of the annuity owner.

Situation 2: the beneficiaries take distributions after rolling over TRS NYC TDA funds to an inherited IRA, in which case the distributions may include earnings accrued after the TRS NYC TDA funds are rolled over to the inherited IRA.

Analysis

Article 16, § 5 of the New York State Constitution provides that "all salaries, wages and other compensation, except pensions, paid to officers and employees of the state and its subdivisions and agencies shall be subject to taxation." Education Law § 3109-A provides that a person employed by the Board of Education of the City of New York may agree to reduce his or her annual salary and become a participant in a TRS NYC TDA program. The TRS NYC TDA is an annuity program authorized by IRC § 403(b) and maintained pursuant to New York City Administrative Code § 13-582. The TRS NYC TDA is

a voluntary defined contribution plan funded exclusively through deferred salary reductions of the participant.¹

Tax Law § 612(c)(3)(i) provides a subtraction modification for pensions to officers and employees of this state, its subdivisions and agencies to the extent includible in gross income for federal income tax purposes. 20 NYCRR 112.3(c)(1)(i) provides that pensions and other retirement benefits (including but not limited to annuities, interest, and lump sum payments) paid to a public employee or the beneficiary of a deceased public employee of New York State, its subdivisions or agencies or the federal government, that are included in federal adjusted gross income (“FAGI”), that relate to services performed as a public employee, and all or a portion of which are actually contributed to by New York State, shall be subtracted from FAGI in determining the New York adjusted gross income of a resident individual.

Tax Law § 612(c)(3-a) provides a subtraction modification for pensions and annuities not excluded by § 612(c)(3) above and not exceeding \$20,000 if the pension and annuity income is: 1) included in FAGI, 2) received in periodic payments except as otherwise provided, 3) attributable to personal services performed by the individual prior to retirement from employment, and 4) received by an individual who has attained the age of 59½. See Tax Law § 612(c)(3-a) and 20 NYCRR 112.3(c)(2)(i). Also, if a payment to an individual would have qualified for the exemption, except that the individual was deceased, a beneficiary of the decedent may claim the exclusion under this section. However, if the deceased has more than one beneficiary, the \$20,000 must be allocated among the beneficiaries in the same ratio as the distribution so that the modification of all beneficiaries does not exceed \$20,000 in the aggregate. See Tax Law § 612(c)(3-a) and 20 NYCRR 112.3(c)(2)(iv).

In TSB-A-02(9)l, the Department determined that distributions received by a petitioner from his TRS NYC TDA 403(b) plan were exempt from New York State and New York City personal income tax pursuant to Administrative Code § 13-561. Also, in TSB-03(5)l, the Department determined that distributions from an IRA, established by means of a tax-free rollover or direct transfer of amounts received from a Petitioner’s TRS NYC TDA 403(b) plan, represent a return of nontaxable funds to the extent of the amount of the annuity that was rolled over, but the exemption does not apply to interest and other earnings earned on the IRA fund subsequent to the rollover.

While a distribution from the TRS NYC TDA would be exempt from New York State and New York City personal income taxes pursuant to NYC Administrative Code § 13-561 if a distribution was made during decedent’s lifetime, the Administrative Code does not specifically address the taxation of such benefits to the beneficiary of a deceased participant in the TRS NYC TDA 403(b) plan. We conclude that it is appropriate to treat income attributable to deceased participants in the TRS NYC TDA 403(b) plan akin to the treatment of income attributable to deceased participants in New York State pension plans pursuant to Tax Law § 612(c)(3) and 20 NYCRR 112.3(c)(1).² Therefore, in Situation 1, where the beneficiaries receive a lump sum distribution from the TRS NYC TDA after the death of

¹ The NYC Teacher’s Retirement Plan also has a defined benefit qualified pension plan that is not the subject of this petition.

² Tax Law § 612(c)(3) and 20 NYCRR § 112.3(c)(1) do not apply to the distributions from the TRS NYC TDA 403(b) plan because those provisions require that all or a portion of the funds must be actually contributed, and not merely deemed contributed, by the public employer. In this case the funds were contributed only by the employee.

the decedent annuity owner, the distribution will not be subject to New York State or New York City tax when those distributions are included in the beneficiaries' FAGI.

Regarding Situation 2, we similarly conclude that the distribution of funds from the inherited IRA will be exempt only to the extent of the TRS NYC TDA 403(b) funds rolled over to the inherited IRA. See TSB-03(5)l; cf Matter of Kane, Tax Appeals Tribunal, December 21, 2016. Any distributions of income or gains accrued after the date the TRS NYC TDA funds were rolled over to the inherited IRA will not be exempt from New York State or New York City personal income tax. However, these latter distributions and any distributions from other IRA or retirement accounts may be eligible for the \$20,000 subtraction modification under Tax Law § 612(c)(3-a) to the extent the other requirements of that section are satisfied. Moreover, each beneficiary that receives a distribution from the decedent is only entitled to a portion of the \$20,000 subtraction modification based on the beneficiary's portion of the distribution so that the subtraction modification of all beneficiaries does not exceed \$20,000 in the aggregate. See Tax Law § 612(c)(3-a) and 20 NYCRR 112.3(c)(2)(iv).

Dated: April 24, 2024

/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.