

STATE OF NEW YORK

DIVISION OF TAX APPEALS

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In the Matter of the Petition	:	
of	:	
<b>WALTER AND JEANETTE MUSLINER</b>	:	SMALL CLAIMS
	:	DETERMINATION
	:	DTA NO. 821426
for Redetermination of a Deficiency or for Refund of New	:	
York State Personal Income Tax under Article 22 of the	:	
Tax Law for the Year 2002.	:	

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Petitioners, Walter and Jeanette Musliner, filed a petition for redetermination of a deficiency or for refund of New York State personal income tax under Article 22 of the Tax Law for the year 2002.

A small claims hearing was held before James Hoefer, Presiding Officer, at the offices of the Division of Tax Appeals, 340 East Main Street, Rochester, New York, on December 13, 2007 at 10:45 A.M. Petitioners appeared pro se. The Division of Taxation appeared by Daniel Smirlock, Esq. (Peter Tagliavento).

Since neither party elected to reserve time for the submission of a post hearing brief, the three-month period for the issuance of this determination commenced as of the date the hearing was held.

***ISSUE***

Whether payments received by petitioner Walter Musliner from the Kodak Unfunded Retirement Income Plan and the Kodak Excess Retirement Income Plan constituted pension or annuity payments such that petitioners were properly entitled to exclude from their New York adjusted gross income \$20,000.00 of such payments pursuant to Tax Law § 612(c)(3-a).

***FINDINGS OF FACT***

1. Petitioner Walter Musliner (petitioner) was employed by the Eastman Kodak Company (Kodak) in the Rochester, New York, area from 1965 to 1991. Petitioner was initially employed at Kodak as a chemist, and during the tenure of his employment petitioner eventually rose to become a laboratory head, the position he held at the time of his retirement. Petitioner described his position as a laboratory head as the lowest level of management at Kodak.

2. Effective December 1, 1991, Mr. Musliner retired from Kodak at age 52. Petitioner was a participant in the Kodak Unfunded Retirement Income Plan and the Kodak Excess Retirement Income Plan (the Kodak Plans) and, as a result, was entitled to receive payments thereunder upon his retirement. A memo dated December 20, 1991, from Kodak's Director of Employee Benefits - Retirement and Savings Plans, advised petitioner as follows:

Acting on behalf of Eastman Kodak Company, I am pleased to inform you that your pension benefit payable from the Kodak Excess Retirement Income Plan and/or the Kodak Unfunded Retirement Income Plan will be paid to you in the following form based on your 12/01/1991 retirement.

<u>Form of Payment</u>	<u>Payment Amount</u>
Monthly Single Life Annuity . . . . .	\$2,032.32

3. After his retirement, petitioner did not perform any services, either as an employee or as a consultant, for Kodak. From the date of his retirement until August 2000, the Kodak Plans were administered by Metropolitan Life Insurance Co. Effective September 2000, a new administrator of the Kodak Plans was appointed to replace Metropolitan Life Insurance Co.

4. During the period that Metropolitan Life Insurance Co. was the administrator of the Kodak Plans, petitioner received a Federal Form 1999-R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, Etc. The Federal

Form 1099-R for the years 1991 through 1999 reflected a gross distribution and taxable distribution to Mr. Musliner, at boxes "1" and "2a," respectively, in the amount of \$24,387.84 (i.e., the monthly single life annuity aggregate payment of \$2,032.32 from the Kodak Plans times 12 months). For the year 2000, petitioner received a Federal Form 1099-R from Metropolitan Life Insurance Co. which reported a gross distribution and taxable distribution to Mr. Musliner, at boxes "1" and "2a," respectively, in the amount of \$16,258.56 (i.e., the monthly single life annuity aggregate payment of \$2,032.32 times the eight months in 2000 during which Metropolitan Life Insurance Co. was the administrator of the Kodak Plans).

5. For the balance of the 2000 tax year, petitioner received a Federal Form W-2 (Wage and Tax Statement) reflecting wages, tips, other compensation, at box "1," and nonqualified plans, at box "11", in the amount of \$8,129.28 (i.e., the monthly single life annuity aggregate payment of \$2,032.32 times four months). The employer's name on this Federal Form W-2 was Kodak Non Qualified Plan, Employer Identification Number 25-1864109. For tax years subsequent to 2000, petitioner received a Federal Form W-2 issued by Kodak Non Qualified Plan, Employer Identification Number 25-1864109, which reported wages, tips, other compensation, at box "1," and non-qualified plans, at box "11," in the amount of \$24,387.84 (i.e., the monthly single life annuity aggregate payment of \$2,032.32 times 12 months).

6. Since petitioner turned age 59½ in 1998, his New York State personal income tax return for said year claimed that the portion of income received from the Kodak Plans after he reached age 59½ was eligible for the pension or annuity income exclusion allowed pursuant to Tax Law § 612(c)(3-a). The Division of Taxation (Division) questioned petitioner regarding how the pension or annuity income exclusion claimed on the 1998 return was calculated and, after reviewing petitioner's response, the Division concluded that petitioner properly computed

the pension or annuity income exclusion for the 1998 tax year. As noted earlier, the income received by petitioner from the Kodak Plans for the 1998 tax year was reported on Federal Form 1099-R and the Division, for the 1998 tax year, did not question whether the payments qualified for the Tax Law § 612(c)(3-a) pension or annuity income exclusion.

7. Petitioners timely filed a joint New York State Resident Income Tax Return for the year 2002. Petitioners' return for 2002 reported wages, salaries, tips, etc. at Line "1" in the amount of \$25,898.00, and this amount included, inter alia, the \$24,387.84 received by Mr. Musliner from the Kodak Plans. As previously noted, for all periods after August 2000, the income received by Mr. Musliner from the Kodak Plans was reported as wages on a Federal Form W-2 issued by Kodak Non Qualified Plan. For the 2002 tax year, the Federal Form W-2 issued by Kodak Non Qualified Plan reported \$24,387.84 of wage income, which was the monthly single life annuity aggregate payment of \$2,032.32 received by petitioner from the Kodak Plans multiplied by 12 months.

8. In computing New York adjusted gross income on their 2002 income tax return, petitioners claimed a subtraction modification in the amount of \$20,000.00, the maximum amount allowed per taxpayer, for the pension and annuity income exclusion provided for in Tax Law § 612(c)(3-a). The Division, on November 28, 2005, issued a Notice of Deficiency to petitioners asserting that \$901.00 of personal income tax was due, together with interest, for the 2002 tax year based on the disallowance of the claimed \$20,000.00 pension and annuity income exclusion. In order to stop the accrual of further interest charges, petitioners paid the additional tax and interest as asserted due in the Notice of Deficiency, and in this proceeding they seek a refund of the tax paid, plus interest. The basis for the Division's disallowance of petitioners'

claimed \$20,000.00 pension and annuity income exclusion was best explained in a letter dated April 14, 2006 as follows:

The subtraction from income has been disallowed as not specifically authorized under Section 612 of the New York State Tax Law.

Income reported by Kodak non-qualified plan is considered wages and is correctly reported on your wage and tax statement.

New York State tax law Section 612(c)(3-a) states that pensions and annuities qualify for the \$20,000.00 pension exclusion, not wages. Section 3401(a) of the Internal Revenue Code defines wages as essentially all remuneration for services performed by an employee for an employer. Section 3401(a) of the IRC also defines or lists types of income that are excluded from the definition of wages. Qualified pension plans under Section 401(a) of the Internal Revenue Code are excluded from the definition of wages in Section 3401(a). There is nothing in Section 3401(a) that excludes this non-qualified plan from the definition of wages, and the employer correctly reports the income on Form W-2. Therefore, the income is wages because it meets the federal definition of wages and would not qualify for the pension and annuity income exclusion.

9. The Kodak Excess Retirement Income Plan was approved on November 20, 1975 and became effective January 1, 1976. The relevant provisions of the Kodak Excess Retirement Income Plan provided as follows:

#### **Purpose of Plan**

1.1 This Plan implements the intent of providing retirement benefits by means of both a funded and an unfunded plan. This Plan is an excess benefit plan as defined in section 3(36) of the Employee Retirement Income Security Act of 1974 and is designed to provide retirement benefits payable out of the general assets of the Company where benefits cannot be paid under the Funded Plan because of Code section 415 and the provisions of the Funded Plan which implement such section.

\* \* \*

#### **Eligibility**

3.1 All employees eligible to receive a benefit from the Funded Plan shall be eligible to receive a benefit under this Plan if their benefits cannot be

fully provided by the Funded Plan due to the benefit limitations imposed by Code section 415.

10. The Kodak Unfunded Retirement Income Plan was approved July 27, 1990 and became effective September 1, 1990. As pertinent to this proceeding, the Kodak Unfunded Retirement Income Plan provided as follows:

#### **Purpose of Plan**

1.1 This Plan implements the intent of providing retirement benefits by means of both a funded and an unfunded plan. This Plan is maintained primarily for the purpose of providing deferred compensation for a select group of management and highly compensated employees as described in section 201(2) of the Employee Retirement Income Security Act of 1974 and is designed to provide retirement benefits payable out of the general assets of the Company where benefits cannot be paid under the Funded Plan because of Code section 401(a)(17) and the provisions of the Funded Plan which implement such section and/or because deferred compensation is ignored in defining compensation for purposes of calculating benefits under the Funded Plan.

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#### **Eligibility**

3.1 All employees eligible to receive a benefit from the Funded Plan shall be eligible to receive a benefit under this Plan if they have deferred any portion of their compensation pursuant to a duly authorized and executed deferred compensation agreement or plan and/or their benefit cannot be fully provided by the Funded Plan due to the compensation limitations imposed by Code section 401(a)(17).

#### ***CONCLUSIONS OF LAW***

A. Tax Law § 612(a) provides that the adjusted gross income of a resident individual is his Federal adjusted gross income with certain addition and subtraction modifications provided for in subsections (b) and (c) of Tax Law § 612. The specific subtraction modification at issue in this matter is set forth at Tax Law § 612(c)(3-a)

which provides, as is relevant here, that a taxpayer's Federal adjusted gross income is to be reduced for:

*Pensions and annuities received by an individual who has attained the age of fifty-nine and one-half . . . to the extent includible in gross income for federal income tax purposes, but not in excess of twenty thousand dollars, which are periodic payments attributable to personal services performed by such individual prior to his retirement from employment, which arise (i) from an employer-employee relationship or (ii) from contributions to a retirement plan which are deductible for federal income tax purposes (emphasis added).*

B. The Commissioner's regulations at 20 NYCRR 112.3(c)(2)(i)(a-d) contain the following provisions with respect to the Tax Law § 612(c)(3-a) pension and annuity income exclusion:

- (a) the pension and annuity income must be included in federal adjusted gross income;
- (b) the pension and annuity income must be received in periodic payments (except where otherwise provided in this paragraph [i.e., distributions from an individual retirement account (IRA) or self-employed retirement plan (Keogh)]);
- (c) the pension and annuity income must be attributable to personal services performed by such individual, prior to such individual's retirement from employment, which arises from either an employer-employee relationship or from contributions to a retirement plan which are tax deductible under the Internal Revenue Code (e.g. [IRA] or [Keogh]); and
- (d) such individual receiving the pension and annuity income must be 59½ years of age or over.

C. Although the term "pension" is not further defined, the term "annuity" is specifically defined in the Commissioner's regulations at 20 NYCRR 132.4(d)(2) as follows:

(2) Definition. To qualify as an *annuity*, a pension or other retirement benefit must meet the following requirements:

(i) It must be paid in money only, not in securities of the employer or other property.

(ii) It must be payable at regular intervals, at least annually, for the life of the individual receiving it, or over a period not less than half of such individual's life expectancy as of the date payments begin.

(iii) It must be payable:

(a) at a rate which remains uniform during such life or period; or

(b) at a rate which varies only with:

(1) the fluctuation in the market value of the assets from which such benefits are payable; or

(2) the fluctuation in a specified and generally recognized cost-of-living index; or

(3) the commencement of social security benefits; or

(c) in such a manner that the total of the amounts payable is determinable at the annuity starting date either directly from the terms of the contract or indirectly by the use of either mortality tables or compound interest computations, or both, in conjunction with such terms and in accordance with sound actuarial theory. The term *annuity starting date* in the case of any contract or plan is the first day of the first period for which an amount is received as an annuity by the individual under the contract or plan.

(iv) the individual's right to receive it must be evidenced by a written instrument executed by his employer, or by a plan established and maintained by the employer in the form of a definite written program communicated to his employees.

D. A review of Tax Law § 612(c)(3-a) and the above cited regulations reveals that five criteria must be met in order for a pension or annuity payment to qualify for the subtraction modification. These five statutory criteria require that the payment must:

1. be received by an individual aged fifty-nine and one-half or older,
2. be includible in gross income for federal tax purposes,



3. be periodic,
4. be attributable to personal services performed by the individual prior to his retirement from employment, and
5. arise from an employer-employee relationship or from an employee's tax deductible contributions to a retirement plan.

E. In the instant matter, petitioner has established that he met each of the criteria set forth in Tax Law § 612(c)(3-a). As stated in the memo from Kodak's Benefits Center, Mr. Muslinger receives a monthly payment from the Kodak Plans in the amount of \$2,032.32. This payment is consistently and specifically termed a pension plan payment, a pension benefit, and a monthly single life annuity. A letter from Kodak dated September 12, 2005 specifically states that the \$2,032.32 monthly amount represent "non-qualified pension plan payments and are not payments from a deferred compensation plan." The \$2,032.32 payment commenced on the December 1, 1991 "annuity start date" and has remained constant and unchanged since its inception upon Mr. Musliner's retirement from Kodak on such date. It is paid pursuant to the two Kodak Plans in which petitioner participated. Under the facts set forth above, this payment meets the definition of a pension or annuity benefit payment set forth in Tax Law § 612(c)(3-a) and the Commissioner's regulations at 20 NYCRR 112.3(c)(2)(i)(a-d) and 20 NYCRR 134.4(d)(2), and thus qualifies for the subtraction modification.

F. The petition filed herein is well drafted and details, in 6 single spaced pages, 7 errors allegedly made by the Division and proposes 16 facts. In contrast, the Division's position is not clearly expressed in any manner or detail. The Division's Answer to the petition, a one-page double spaced document, simply denies the allegations contained in the petition and affirmatively states "the exclusion was disallowed because Petitioner's [sic] failed to report the \$20,000.00 as income on the relevant return." Petitioners' position on the legal issue presented

herein is clearly set forth in the petition and other documents presented at hearing. The Division chose not to file a post hearing brief and is apparently satisfied that its legal position is adequately stated in the one paragraph contained in its letter of April 14, 2006 (*see* Finding of Fact “8”).

G. The Division’s reliance on Tax Law § 607(a) and various withholding tax provisions of the Internal Revenue Code (IRC) for support that the \$2,032.32 monthly payment petitioner received from the Kodak Plans was wage income, and not pension or annuity income, is rejected. Tax Law § 607(a) provides, in relevant part, that the terms:

used in this article shall have the same meaning as when used in a comparable context in the laws of the United States relating to federal income taxes, unless a different meaning is clearly required but such meaning shall be subject to the exceptions and modifications prescribed in this article or by statute.

This provision has little application to the matter at hand. As noted in Conclusion of Law “A”, the New York adjusted gross income of a taxpayer is his federal adjusted gross income with certain addition and subtraction modifications. Since the dispute herein concerns the subtraction modification contained in Tax Law § 612(c)(3-a), and since the Legislature has provided specific defining language relative thereto in the statute, there is no need to resort to federal law, regulations and rules to reach a determination on this issue. Furthermore, after reviewing the provisions of the IRC relied upon by the Division, I believe that said provisions are of little value in resolving this dispute. The manner by which the IRC provides for income and FICA taxes to be withheld from payments made by both qualified and nonqualified pension plans and how those payments are reported for Federal income tax purposes, either on Form 1099-R or Form W-2, is not dispositive as to whether such payments constitute pensions or annuities. For the year at issue, petitioner had been retired from Kodak for over 10 years, had not been employed by

Kodak during 2002 in any capacity and had not performed any services for Kodak in 2002. Accordingly, notwithstanding petitioner's receipt of a Federal Form W-2 for the 2002 tax year, it cannot be found that the income reported on the Form W-2 constituted current wages, i.e., remuneration for services performed by an employee for an employer. The income in question was clearly a pension enhancement benefit that petitioner received pursuant to two written retirement plans maintained by his employer. Whether the pension or annuity payment is from a qualified or nonqualified plan is not a criteria upon which entitlement to the subtraction modification is based, and the Division may not add additional criteria beyond those set forth in the statute. As petitioner points out, eligibility for the subtraction modification focuses on the character of the pension or annuity payment in the hands of the retiree and not upon the means by which the employer has chosen to finance the pension benefit, which funding method is a matter of corporate financial discretion. Ultimately, the nature of the payment itself, and not the manner in which the payor entity reports that payment for FICA or income tax withholding tax purposes, determines the correct tax treatment thereof for purposes of Tax Law § 612(c)(3-a).

H. The petition of Walter and Jeanette Musliner is granted; the Division's Notice of Deficiency dated November 28, 2005 is canceled and the Division is hereby directed to refund to petitioners the sum of \$901.00, plus such interest as allowed by law.

DATED: Troy, New York  
March 13, 2008

/s/ James Hoefer  
PRESIDING OFFICER