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INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

AUG 14 2000

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MEMORANDUM FOR Director, EP Rulings and Agreements T:EP:RA

FROM: Chief, Executive Compensation Branch, DC/ACC:TEGE:EB:EC
SUBJECT: [REDACTED]

You asked for assistance on rulings one and three of the ruling request for [REDACTED]. Currently, employees may accumulate up to 90 days of unused sick leave; unused sick leave in excess of 90 days is forfeited. Employees (or their beneficiaries) hired before June 30, 1996 may receive cash (based on a formula set forth in a collective bargaining agreement) in lieu of unused sick leave if they die while employed by the [REDACTED] or if they retire. Employees hired after June 30, 1996 and employees hired before that date but who terminate employment other than by death or retirement are not entitled to receive payment for accumulated but unused sick leave.

The proposed transaction will permit [REDACTED] employees who have accumulated [REDACTED] days of sick leave to elect to contribute up to [REDACTED] days of unused sick leave to the [REDACTED] qualified deferred compensation plan (Plan) at the rate of [REDACTED] % of the employee's regular gross pay for the days.

1. Ruling Request 1: Constructive Receipt of Income

Ruling request 1 states that the proposed Sick Leave Exchange will not result in actual or constructive receipt of income under section 451 by any employee who is eligible to participate in the program. We conclude that the Sick Leave Exchange program will not result in actual or constructive receipt of income by such employees under section 451.

a. Proposed Language for Ruling

We recommend the following language be included in the ruling:

i. Discussion of applicable law

Section 451 of the Code and Treas. Reg. § 1.451-1(a) provides that under the cash receipts and disbursements method of accounting, an amount is includable in gross income when actually or constructively received.

Treas. Reg. § 1.451-2(a) provides that income is constructively received in the taxable year during which it is credited to the taxpayer's account, set apart for the taxpayer or otherwise made available so that the taxpayer may draw upon it at any time. However, income is not constructively received if the taxpayer's control of its receipt is subject to substantial limitations or restrictions.

ii. Application of law to facts

In the proposed transaction, unused accumulated sick leave will be used by the employee as needed, accumulated for future use, exchanged for a contribution to the Plan, or forfeited if the number of unused days exceeds 90. The Sick Leave Exchange program does not give eligible employees the right to receive payment for unused sick leave. A contribution to an employee's account under the Plan as a result of the Sick Leave Exchange program is not income credited to the taxpayer's account under Treas. Reg. § 1.451-2(a). Therefore, the proposed exchange will not result in actual or constructive receipt of income under section 451 by an eligible employee.

2. Ruling Request 3: Application of FICA Tax Withholding

Ruling request 3 states that the proposed contributions by the Zoo to the Plan pursuant to an employee's election under the Sick Leave Exchange is not includible in the employee's gross wages under section 3121. We are assuming that you will conclude that the amounts contributed are nonelective employer contributions and not contributions pursuant to a qualified cash or deferred arrangement under section 401(k). Given this assumption, we conclude that the amounts contributed are not includible as wages under section 3121.

a. Proposed Language for Ruling

We recommend the following language be included in the ruling:

i. Discussion of applicable law

Section 3121(a)(5)(A) provides in general that the term "wages" shall not include any payment made to, or on behalf of, an employee or his beneficiary from or to a trust described in section 401(a) of the Code. However, section 3121(v)(1)(A) states that "wages" includes any employer contribution under a qualified cash or deferred arrangement (as defined in section 401(k)) to the extent the contribution was not included in the employee's gross income under section 402(3)(e).

ii. Application of law to facts

In the proposed transaction, the contribution to the Plan is a nonelective employer contribution and not a contribution under a qualified cash or deferred arrangement (as defined in section 401(k)). Therefore, the general rule under section 3121(a)(5)(A) applies, and the contributions are not included in wages under section 3121.