

Internal Revenue Service

Department of the Treasury

Number: **200301022**
Release Date: 01/03/2003
Index Number: 4976.01-00

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:TEGE:EB:HW-PLR-156971-01

Date:

September 26, 2002

Legend

Taxpayer =

State =

Insurance Company A =

Insurance Company B =

Insurance Company C =

Date A =

Date B =

Associations =

Industry =

X =

Dear _____ :

This is in response to your correspondence dated October 11, 2001, on behalf of Taxpayer, requesting a ruling regarding the applicability of section 4976 to the distribution of Taxpayer assets to participating employers.

FACTS

Taxpayer is a taxable trust originally created in 1952, when certain employers engaged in the Industry within the State entered into an agreement for the purpose of procuring group life, disability, hospitalization, medical, and related insurance benefits for their employees. In 1993, the trust was restated to expand coverage to include employers that were members of the Associations.

PLR-156971-01

The plan provided through Taxpayer (the Plan), provided group insurance coverage to employer members of the Associations and their employees. As of Date B, more than 400 employers participated in the Plan. Since its establishment, the trustees of Taxpayer have procured insurance coverage for employees of employers participating in the Plan through a variety of insurance companies. During the most recent time period, from Date A through Date B, Taxpayer contracted with Insurance Company A and Insurance Company B to provide medical insurance, dental insurance, life insurance, and disability insurance. Medical, dental, and life insurance coverage were all provided through Insurance Company A.

Trustees of the Taxpayer selected the insurance carriers, insurance policies, and established separate benefit options providing various schedules of benefits, deductibles, co-insurance and other features. All insurance premiums paid to the insurance carriers were paid with monies contributed by participating employers. All benefit options were available to all participating employers. The employers then paid a monthly contribution to the Taxpayer based on the options selected and the number of participants. Taxpayer assets were only used to pay claims, insurance premiums, and for administrative expenses.

It is represented that Taxpayer is and has always consisted of a welfare benefit fund that is part of a ten or more employer plan as described in section 419A(f)(6) of the Code. In particular, it is represented that more than one employer always contributed to the Plan, no employer normally contributed more than ten percent of the total contributions of all the employer contributions to the Plan, and the Plan has never maintained experience-rating arrangements with respect to individual employers.

Your ruling request does not indicate that you are requesting a ruling on the issue of whether the Taxpayer satisfies the section 419A(f)(6) exception for ten or more employer plans, and we are not ruling on that issue. Rather, in addressing the issue raised in your request (the applicability of section 4976(b)(1)(C)), we are relying on the representation that the Taxpayer satisfies the section 419A(f)(6) exception.

Insurance Company A notified Taxpayer that it sold its group insurance business to Insurance Company C, which does not offer insurance coverage in the State of the type provided through the Taxpayer. Trustees of Taxpayer were unable to locate appropriate alternative coverage. As a result, the trustees of Taxpayer voted to terminate Taxpayer effective Date B. As of that date, the balance remaining in the trust was \$X. In accordance with the trust agreement, the Trustees of Taxpayer plan to distribute this balance (less paid run off claims and increased by after-tax earnings earned from termination to the time of distribution), to the employers participating in the Plan as of Date B in proportion to their contributions (using a formula that approximates relative contributions paid and does not take into account claims paid).

PLR-156971-01

RULING REQUESTED

The distribution of the balance remaining in Taxpayer to employers participating in the Plan at the time of trust termination will not result in these employers incurring an excise tax pursuant to Code section 4976(b)(1)(C).

LAW AND ANALYSIS

Section 419(a) of the Code provides that contributions paid or accrued by an employer to a welfare benefit fund are not deductible under Chapter 1 of the Code but, if they would otherwise be deductible, are (subject to the limitation of section 419(b)) deductible under section 419 for the taxable year in which paid.

Section 419(e)(1) of the Code provides that the term "welfare benefit fund" means any fund that is part of a plan of an employer, and through which the employer provides welfare benefits to employees or their beneficiaries. Section 419(e)(3)(B) defines "fund" to include a trust that is not exempt from tax under Chapter 1.

Section 419A(f)(6)(A) of the Code provides that Subpart D of Chapter 1 of Subtitle A of the Code (consisting of sections 419 and 419A) shall not apply to any welfare benefit fund that is part of a ten or more employer plan. However, section 419A(f)(6)(A) further provides that this exception does not apply to any plan that maintains experience-rating arrangements with respect to individual employers. Section 419A(f)(6)(B) of the Code provides that the term "ten or more employer plan" means a plan to which more than one employer contributes and to which no employer normally contributes more than ten percent of the total contributions contributed under the plan by all employers.

Section 4976(a) of the Code imposes an excise tax in the amount of 100 percent of the amount of any disqualified benefit provided by a welfare benefit plan. Section 4976(b)(1) provides that the term "disqualified benefit" means --

(A) any post-retirement medical benefit or life insurance benefit provided with respect to a key employee if a separate account is required to be established for such employee under section 419A(d) and such payment is not from such account,

(B) any post-retirement medical benefit or life insurance benefit provided with respect to an individual in whose favor discrimination is prohibited unless the plan meets the requirements of section 505(b) with respect to such benefit (whether or not such requirements apply to such plan), and

PLR-156971-01

(C) any portion of a welfare benefit fund reverting to the benefit of the employer.

Section 4976(b)(3) of the Code provides that section 4976(b)(1)(C) does not apply to any amount attributable to a contribution to the fund that is not allowable as a deduction under section 419 for the taxable year or any prior taxable year.

Taxpayer is a welfare benefit fund within the meaning of section 419(e)(1), because it is part of an employer plan, and participating employers provided welfare benefits to their employees through Taxpayer.

It is represented that Taxpayer is part of a ten or more employer plan to which the exception provided by section 419A(f)(6) applies. Based upon that representation, contributions made by participating employers to Taxpayer were not "allowable as a deduction under section 419 for the taxable year or any prior taxable year" within the meaning of section 4976(b)(3) of the Code. Accordingly, pursuant to section 4976(b)(3), section 4976(b)(1)(C) does not apply to amounts attributable to those contributions, including any distribution of the remaining balance in Taxpayer to employers that participated in the Plan at the time of Taxpayer's termination.

CONCLUSION

Pursuant to section 4976(b)(3), section 4976(b)(1)(C) does not apply to the distribution of the balance remaining in Taxpayer to employers that participated in the Plan at the time of Taxpayer's termination.

This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3) of the Code provides that it may not be used or cited as precedent. Except as specifically ruled above, no opinion is expressed as to the federal tax consequences of the transaction described above under any provision of the Code. Specifically, this ruling addresses neither of the following issues: (1) whether Trust is in fact a ten or more employer plan to which the exception provided under section 419A(f)(6) applies; and (2) whether distribution of the balance in Taxpayer at the time of termination will result in the realization and recognition of gross income to recipients of the distribution under section 61.

Sincerely,

MARK SCHWIMMER
Senior Technician Reviewer
Division Counsel/Associate Chief Counsel
(Tax Exempt and Government Entities)