DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

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Date: NOV 2 0 2000

Contact Person:

Identification Number:

Telephone Number:

T:EO:2

Employer Identification Number:

LEGEND:

M =
N =
O =

Dear Sir or Madam:

This is in reply to the request for a ruling regarding the termination of an employee benefit plan and the transfer of the funds remaining therein to several organizations described in section 501(c)(3) of the Internal Revenue Code.

M is a business trust established pursuant to an order of the United States Bankruptcy Count in connection with the insolvency of N. It is the successor in interest and assignee of certain assets and obligations of N including those relating to the welfare benefit plans previously operated by N. It has been represented that other than completion of the proposed transactions regarding the welfare benefit plans, the function and purpose of M has been substantially completed and it is expected that M will be dissolved shortly after the funds are transferred in accordance with this proposed transaction.

N provided its employees a series of welfare benefits through a flexible benefits plan. These benefits included a health care plan and a dependent care plan. O is a trust which was used by N to hold and invest the contributions it made and to pay or provide benefits to employees pursuant to the plans. It has been represented that O is recognized as exempt under section 501(c)(9) of the Code. All benefits owed under the health care and dependent care plans have been paid and there are no outstanding benefit claims or liabilities. M intends to use a portion of the remaining balance in each plan and the monies currently in O, to pay all outstanding administrative expenses. It will then amend the governing instruments for the plans and the trust and transfer all the remaining funds to various specified charities. It has been represented that the administrative expenses will be insubstantial.

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Re:

As amended in the letter of July 11, 2000, the following rulings have been requested:

1. None of the transfers to the Charities of funds held by O under the health care plan or the dependent care plan will be treated as a reversion under section 4976 of the Code or result in the imposition of the 100 percent excise tax under section 4976 of the Code on M or O.

2. None of the transfers to the Charities of funds held by O under the health care plan or the dependent care plan will result in unrelated business taxable income to M or O.

Section 501(c)(9) of the Code provides for the exemption from federal income tax of voluntary employees' beneficiary associations providing for the payment of life, sick, accident, or other benefits to the members of such association or their dependents or designated beneficiaries if no part of the net earnings of such association inures (other than through such payments) to the benefit of any private shareholder or individual.

Section 1.501(c)(9)-1 of the Income Tax Regulations provides that for an organization to be described in section 501(c)(9), it must be an employees' association; membership in the association must be voluntary; the organization must provide for the payment of life, sick, accident, or other benefits to its members; and there can be no inurement (other than by payment of permitted benefits) to the benefit of any private shareholder or individual.

Section 1.501(c)(9)-4(a) of the regulations provides that no part of the net earnings of an employees' association may inure to the benefit of any private shareholder or individual other than through the payment of permissible benefits. Whether prohibited inurement has occurred is a question to be determined with regard to all the facts and circumstances.

Section 1.501(c)(9)-4(d) of the regulations provides that it will not constitute prohibited inurement if, on termination of a plan established by an employer and funded through an association described in section 501(c)(9), any assets remaining in the association, after the satisfaction of all liabilities to existing beneficiaries of the plan, are applied to provide, either directly or through the purchase of insurance, life, sick, accident or other benefits within the meaning of section l.50l(c)(9)-3 pursuant to criteria that do not provide for disproportionate benefits to officers, shareholders, or highly compensated employees of the employer. Similarly, a distribution to members upon the dissolution of the association will not constitute prohibited inurement if the amount distributed to members are determined pursuant to the terms of a collective bargaining agreement or on the basis of objective and reasonable standards which do not result in either unequal payment to similarly situated members or in disproportionate payments to officers, shareholders, or highly compensated employees of any employer contributing to or other funding the employees' association. Except as otherwise provided in the first sentence of this paragraph, if the association's corporate charter, articles of association, trust instrument or other written instrument by which the association was created, as amended from time to time, provides that on dissolution its assets will be distributed to its member's contributing employers, or if in the absence of such provision the law of the state in which the association was created provides for such distribution to the contributing employers, the association is not described in section 501(c)(9).

Section 511(a) of the Code imposes a tax on the "unrelated business taxable income" of organizations described in section 501(c).

Section 512(a)(1) of the Code defines the term unrelated business taxable income as gross income derived by any organization from any unrelated trade or business (as defined in section 513) regularly carried on by it less allowable deductions directly connected with the carrying on of such trade or business both computed with the modifications provided in section 512(b).

Re:

Section 513(a) of the Code provides that the term "unrelated trade or business" means any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by such organization of its charitable, educational, or other purpose or function constituting the basis for its exemption under section 501.

Section 4976(a) of the Code imposes an excise tax on an employer equal to 100 percent of any disqualified benefit provided by an employer-maintained welfare benefit fund.

Section 4976(b)(1)(C) of the Code defines "disqualified benefit" to include any portion of a welfare benefit fund reverting to the benefit of the employer.

Rev. Rul. 68-223, I968-1 C.B. 154 provides that the transfer of funds from a non-exempt employees" welfare fund to an employees" trust forming part of a pension plan will not, of itself, disqualify the plan and trust under the provisions of section 401(a) of the Code nor affect the exempt status of the trust under section 501(a).

The information submitted establishes that M is the successor to N's obligations and as such is treated as a plan sponsor for the purposes of sections 501(c)(9) and 4976 of the Code. It has been represented that none of the welfare plans originally established by N have any outstanding debts or obligations other than an insubstantial amount of administrative fees. However, O has unused amounts remaining from its health and dependent care plans. You propose to terminate the plans and the trust and donate the remaining funds to charities. It has been represented that once this proposed transaction has been completed M will be dissolved.

As a general rule the return of any portion of the funds held in a welfare benefit fund for the benefit of an employer is a disqualified benefit and subjects the plan sponsor to the section 4976(a)(2) excise tax. However, the section 4976 excise tax was enacted to establish a meaningful sanction that would prohibit an employer from accumulating funds in a qualifying trust on a tax free basis and subsequently modifying the plan so it would cease to qualify for exemption. It was felt the previously existing sanctions, loss of exemption or deductions for future contributions were insufficient determents. Here, M is the court appointed successor to N and for the purposes of this ruling would be considered a plan sponsor. For the purposes of this situation, outside of the bankruptcy proceedings neither M nor N have any continuing business purpose. The sole remaining action is for M as the successor to N is to close the bankruptcy estate. Therefore the funds remaining in the trusts will not be used to enhance or improve N's or any of its principals economic position or reputation in the community or to pay any obligations that N might still owe. Even though M is the successor in interest to N, it has no business or interest in these funds and they will not be used for its benefit. Therefore neither M or N will benefit by reason of the transfer of the remaining funds. Furthermore, it has been represented that M will be dissolved after the remaining funds are distributed to charity. Therefore, there is no tax abuse as a result of the transaction and imposing the 4976(a)(2) excise tax is not appropriate.

Accordingly, based on the information submitted we have concluded that:

1. None of the transfers to the charities of funds held by O under the health care plan and the dependent care plan will be treated as a reversion under section 4976 of the Code or result in the imposition of the 100 percent excise tax under section 4976 of the Code on M or O.

2. None of the transfers to the Charities of funds held by O under the health care plan and the dependent care plan will result in unrelated business taxable income to M or O.

Re:

This ruling is directed only to the organization that requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited as precedent.

We are informing the Ohio TE/GE Customer Service Office of this ruling. Because this letter could help resolve any question about O's exempt status, a copy of it should kept in its permanent records.

If there are any question about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter. For other matters, including questions concerning reporting requirements, please contact the Ohio TE/GE Customer Service Office.

Sincerely Yours,

Joseph Chasin
Acting Manager,
Exempt Organizations
Technical Group 2