Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Date:
November 20, 2003

A =

B =

C =

Court =

X =

Year 1 =

Year 2 =

Date 1 =

Date 2 =

Date 3 =

Dear :

This letter responds to a letter, dated Date 1, submitted on behalf of A by A's authorized representative, requesting certain rulings under the Internal Revenue Code.

The information submitted states that A is a tax exempt business league under section 501(c)(6) of the Code. A has arranged for its members to purchase health insurance for their employees at competitive prices. During Year 2, A arranged for such insurance through B. A's members, not A, paid the policy premiums and dealt with B or its agents on the policy. A also offered this health insurance to its own employees.

B is the product of various corporate mergers. As pertinent here, in Year 1, A arranged for health insurance through C. In that year, C merged with B. Under the merger agreement, in the event of a future demutualization of B, members of C, including A, were locked into a value for C. Accordingly, upon a future demutualization of B, the value of the demutualized company attributable to C would be allocated to B's members.

On Date 2, B converted from a mutual fund company to a stock insurance company. As a result of this conversion, B was required to pay consideration, known as demutulization proceeds to its policyholders in exchange for their proprietary rights in the mutual company. For purposes of the demutualization process, B considered A, not A's members, as the policyholder. Accordingly, upon the demutualization of B, A received X number of shares of B stock, the value associated with the value of C.

A's board of directors considered numerous alternatives for allocating and distributing the demutualization proceeds to its members. Ultimately, A filed an interpleader action on Date 3 in Court.

Section 468B(g) provides that nothing in any provision of law shall be construed as providing that an escrow account, settlement fund, or similar fund is not subject to current income tax. The Secretary shall prescribe regulations providing for the taxation of any such account or fund whether as a grantor trust or otherwise.

Prop. Reg. § 1.468B-9(a) provides that a fund that is not a qualified settlement fund under section 1.468B-1 is a disputed ownership fund if –

(i) It is established to hold money or property subject to conflicting claims of ownership;

(ii) The escrow account, trust, or fund is subject to the continuing jurisdiction of the court; and

(iii) Money or property cannot be paid or distributed from the escrow account, trust, or fund to, or on behalf of, a claimant or transferor without the approval of the court.

Prop. Reg. § 1.468B-9(c)(1) provides that for federal income tax purposes a disputed ownership fund is treated as the owner of all assets that it holds. A disputed ownership fund is treated as a C corporation for purposes of subtitle F of the Internal Revenue Code, and the administrator of the fund must obtain an employer identification number for the fund, make all required income tax and information returns, and deposit

all payments of tax. Also, except as otherwise provided in this section a disputed ownership fund is taxed as if it were either –

(i) A qualified settlement fund under section 1.468B-2 if all the assets transferred to the fund by or on behalf of the transferors are passive investment assets, for example, cash or cash equivalents, stock, and debt obligations; or

(ii) A C corporation in all other cases.

Prop. Reg. § 1.468B-9(c)(2) provides that if there is a more appropriate method of taxing a disputed ownership fund than as provided in paragraph (c)(1) of this section, the claimants to the fund may submit a private letter ruling request proposing an alternative method of taxation.

Prop. Reg. § 1.468B-9(h)(1) provides that this section applies to disputed ownership funds established after the date of publication of final regulations in the Federal Register.

Prop. Reg. § 1.468B-9(h)(2) provides that with respect to disputed ownership fund established after August 16, 1986, but on or before the date of publication of final regulations in the Federal Register, the Internal Revenue Service will not challenge a reasonable, consistently applied method of taxation for income earned by the fund, transfers to the fund, and distributions made by the fund.

Based solely on the facts and representations submitted we concluded that the Internal Revenue Service will not challenge A's treatment of the trust created by the interpleader action as a grantor trust of A.

Except as specifically set forth above, no opinion is expressed concerning the federal tax consequences of the transactions described above. In particular, no opinion is expressed or implied concerning the method of selection of the participants who will receive distributions from the interpleader fund or the formulas used to make such determinations. We also express no opinion as to whether any distributee of the proceeds may reduce their income by basis attributable to nondeductible premiums. Lastly, no opinion is expressed or implied as to whether A or any other person would be treated as the grantor or owner of any portion of the Fund under §§ 671 through 678.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

Jeffery G. Mitchell
Senior Technician Reviewer, Branch 7
Office of Associate Chief Counsel
(Income Tax & Accounting)

Enclosures (2)