

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

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Date:  
October 5, 2011

Trust:

Agreement:

Board:

City:

Participating  
Employers:

Statute 1:

Statute 2:

Executives:

System:

Date 1:

Date 2:

Dear \_\_\_\_\_ :

This letter responds to a letter from your authorized representatives dated June 17, 2011, submitted on behalf of the Trust, requesting a ruling that the Trust's income is excludable from gross income under § 115 of the Internal Revenue Code. The Trust represents the facts as follows.

#### FACTS

The City maintains health plans in which retirees of the City and of Participating Employers (jointly, the Employers) – as well as the retirees' eligible spouses, registered domestic partners, and dependents entitled to coverage (referred to collectively as "beneficiaries") – may participate to obtain medical care (as defined by § 213(d)) pursuant to Statute 1. The Trust was established under the Agreement and pursuant to Statute 2 to fund these benefits. Contributions to the Trust, made by the Employers and their employees, shall be used solely for benefits, expenses, and other charges properly allocable to the plans.

The Board serves as the trustee of the Trust with exclusive authority and control over the administration and management of the Trust. The Board consists of five members. Three of the members are appointed one each by each of the Executives, and two are elected one each from among active employees and retired members of the System.

The Board appoints one or more persons or entities as administrator of the Trust. The administrator is responsible for accepting contributions to the Trust and forwarding those funds to the Board-selected custodian, as well as for crediting the deposits to the appropriate sub-trusts, if any.

The Board is responsible for investing and reinvesting the assets of the Trust and, beginning Date 1, for paying benefits from the Trust to those retirees and their beneficiaries entitled to health care coverage under Statute 1. Before Date 2, no Trust disbursements, other than for reasonable Trust administration expenses, shall be made.

The Agreement provides that at no time will Trust assets be used for, or diverted to, purposes other than funding health care benefits under the plans for retirees and

their beneficiaries, and for paying the reasonable expenses of administering the Trust and plans. The Agreement further provides that no part of the Trust's net earnings may inure to the benefit of a private person, and that no private person may participate in, or benefit from, the operation of the Trust.

The Board may amend the Agreement at any time and in any manner permitted by State law and not inconsistent with § 115. An Employer may dissolve the Trust with respect to that Employer. After paying, or making reasonable provision to pay, all liabilities of the Trust with respect to the terminating Employer, the Board will distribute the remaining Trust property allocable to that Employer. In no event will Trust assets be transferred to an entity that is not a political subdivision of the State or an entity whose income is excluded from gross income under § 115.

The Trust represents that the Participating Employers are political subdivisions or § 115 entities. It represents also, with respect to domestic partners, that the Board will make reasonable efforts to identify individuals who do not qualify as § 152 dependents, and the Board will include in retirees' income the cost of the City's portion of health care coverage for any such individuals.

#### LAW AND ANALYSIS

Section 115(1) provides that gross income does not include income derived from any public utility or the exercise of any essential government function and accruing to a state or any political subdivision thereof.

In Rev. Rul. 77-261, 1977-2 C.B. 45, income from an investment fund, established under a written declaration of trust by a state, for the temporary investment of cash balances of the state and its participating political subdivisions, was excludable from gross income for federal income tax purposes under § 115(1). The ruling indicated that the statutory exclusion was intended to extend not to the income of a state or municipality resulting from its own participation in activities, but rather to the income of a corporation or other entity engaged in the operation of a public utility or the performance of some governmental function that accrued to either a state or municipality. The ruling points out that it may be assumed that Congress did not desire in any way to restrict a state's participation in enterprises that might be useful in carrying out projects that are desirable from the standpoint of a state government and which are within the ambit of a sovereign properly to conduct. In addition, pursuant to § 6012(a)(2) and the underlying regulations, the investment fund, being classified as a corporation that is subject to taxation under subtitle A of the Code, was required to file a federal income tax return each year.

In Rev. Rul. 90-74, 1990-2 C.B. 34, the income of an organization formed, funded, and operated by political subdivisions to pool various risks arising from their obligations regarding public liability, workers' compensation, or employees' health is

excludable from gross income under § 115. In this ruling, private interests did not materially participate in the organization, nor did they benefit more than incidentally from the organization.

The Trust provides health care benefits to retired employees of the Employers, as well as to eligible beneficiaries of those retirees. Providing health benefits to former public employees constitutes the performance of an essential government function. Based upon Rev. Rul. 90-74 and Rev. Rul. 77-261, the Trust performs an essential governmental function within the meaning of § 115(1).

The funding and provision of retiree health benefits through the Trust satisfies the obligation of the Employers to provide those benefits; thus, the income of the Trust accrues to the Employers, all of which are political subdivisions or entities the income of which is excluded from gross income under § 115. No private interests participate in, or benefit from, the operation of the Trust other than as providers of goods or services. The benefit to retired employees is incidental to the public benefit. Upon dissolution, no Trust assets will be distributed to an entity other than a state, a political subdivision, or a § 115 entity. See Rev. Rul. 90-74.

#### RULING

Based solely on the facts and representations submitted by the Trust, we conclude that the income of the Trust is derived from the exercise of an essential governmental function and will accrue to a state or a political subdivision thereof for purposes of § 115(1). Consequently, we rule that the Trust's income is excludable from gross income under § 115(1).

Except for the specific ruling above, we express or imply no opinion concerning the federal tax consequences of the facts of this case under any other provision of the Code. Specifically, no representation is made that contributions or premiums paid on behalf of, or benefits received by, employees, former employees, retirees, spouses, dependents, or others will be tax-free. This ruling concerns only the federal tax treatment of the Trust's income and may not be cited or relied upon as to any matter relating to the taxation of accident or health contributions or benefits.

Under a power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

This ruling is directed only to the taxpayer who requested it. According to § 6110(k)(3), this ruling may not be used or cited as precedent.

Sincerely,

SYLVIA HUNT  
Assistant Branch Chief  
Exempt Organizations  
Office of Division Counsel /  
Associate Chief Counsel  
(Tax Exempt & Government Entities)

enclosures: copy for § 6110 purposes