In re: ____________________

LEGEND

Company A=

Company B=

Company C=

Year 1=

Year 2=

Policy=

Trust=

Dear ____________________:

This is in response to your ruling request dated November 4, 2011, requesting rulings on a proposed transaction described below.
FACTS

Company B is a wholly owned subsidiary of Company A. In Year 1, Company A purchased certain assets from Company C and then transferred those assets to Company B. Company B discontinued operations in Year 2.

You represent that, pursuant to a collective bargaining agreement, Company B retirees are eligible for post-retirement life insurance and post-retirement medical benefits. The post-retirement life insurance is provided through Policy’s life insurance funding account (LIFA), which you represent is a welfare benefit fund within the meaning of section 419(e) of the Internal Revenue Code. Company B maintains Trust, which you represent is a voluntary employees’ beneficiary association (VEBA) described in section 501(c)(9), to provide post-retirement medical benefits to the same group of retirees.

You represent that no contributions have been made by Company A or any related company (as described in subsections (b), (c) or (m) of section 414) to the LIFA to provide benefits for represented employees.

You represent that all deductions for years prior to 1986 for contributions made to the LIFA were made in accordance with section 162. You further represent that all deductions for years after 1985 for contributions made to the LIFA were made in accordance with section 419A(f)(5).

The proposed transaction is for the LIFA to purchase a guaranteed life insurance policy, and then transfer the assets that exceed the amount necessary to guaranty the life insurance benefits directly to Trust.

RULING REQUESTED

You have requested a ruling that the transfer of excess assets from the LIFA to Trust to provide medical benefits for the same group of retired employees pursuant to the collective bargaining agreement will not result in a reversion to Company B under section 4976(b)(1)(C).

LAW

Section 419(e)(1) of the Code defines the term “welfare benefit fund” to include any fund through which the employer provides welfare benefits to employees or their beneficiaries. The term “fund” is defined in section 419(e)(3) to include an organization described in section 501(c)(9), and also, to the extent provided in regulations, any account held for an employer by any person.
Section 419(a) provides that contributions paid or accrued by an employer to a welfare benefit fund shall not be deductible under Chapter 1 of the Code, but if they would otherwise be deductible, shall (subject to the limitation of section 419(b)) be deductible under section 419 for the taxable year in which paid.

Section 419(b) limits the employer’s deduction under section 419(a) to a welfare benefit fund’s qualified cost for the taxable year. The qualified cost of a welfare benefit fund for a taxable year is defined in section 419(c)(1) as the sum of the qualified direct cost for the taxable year and, subject to the limitation of section 419A(b), any addition to a qualified asset account for the taxable year. Under section 419(c)(2), the qualified cost for any taxable year is reduced by the welfare benefit fund’s after-tax income for the taxable year.

Section 419(c)(3)(A) provides that the term “qualified direct cost” means, with respect to any taxable year, the aggregate amount (including administrative expenses) that would have been allowable as a deduction to the employer with respect to the benefits provided during the taxable year, if those benefits were provided directly by the employer and the employer used the cash receipts and disbursements method of accounting.

Section 419(c)(3)(B) provides that, for purposes of section 419(c)(3)(A), a benefit is treated as provided when that benefit would be includible in the gross income of the employee if provided directly by the employer (or would be so includible but for any provision of Chapter 1 of the Code excluding that benefit from gross income).

Section 419A(a) defines the term “qualified asset account” to include any account consisting of assets set aside to provide for the payment of medical or life insurance benefits.

Section 419A(b) provides that no addition to any qualified asset account may be taken into account under section 419(c)(1) to the extent such addition results in the amount of such account exceeding the account limit.

Section 419A(f)(5)(A) provides that no account limits shall apply in the case of a qualified asset account under a separate welfare benefit fund under a collective bargaining agreement.

Section 1.419-1T, Q&A-2(a) of the regulations, provides that section 419 generally applies to contributions paid or accrued with respect to a welfare benefit fund after December 31, 1985, in taxable years of employers ending after that date.

Section 1.419-2T, Q&A-1 provides, in pertinent part, that neither contributions to nor reserves of a collectively bargained welfare benefit fund shall be treated as exceeding
the otherwise applicable limits of section 419(b), 419A(b), or 512(a)(3)(E) until the earlier of: (i) The date upon which the last of the collective bargaining agreements relating to the fund in effect on the date of issuance of final regulations concerning such limits terminates, or (ii) the date three years after the issuance of final regulations.

Section 1.419A-2T, Q&A-2 states:

(1) For purposes of Q&A-1, a collectively bargained welfare benefit fund is a welfare benefit fund that is maintained pursuant to an agreement which the Secretary of Labor determines to be a collective bargaining agreement and which meets the requirements of the Secretary of the Treasury as set forth in paragraph (2) below.

(2) Notwithstanding a determination by the Secretary of Labor that an agreement is a collective bargaining agreement, a welfare benefit fund is considered to be maintained pursuant to a collective bargaining agreement only if the benefits provided through the fund were the subject of arms-length negotiations between the employee representatives and one or more employers, and if such agreement between employee representatives and one or more employers satisfies Code section 7701(a)(46). Moreover, the circumstances surrounding a collective bargaining agreement must evidence good faith bargaining between adverse parties over the welfare benefits to be provided through the fund. Finally, a welfare benefit fund is not considered to be maintained pursuant to a collective bargaining agreement unless at least 50 percent of the employees eligible to receive benefits under the fund are covered by the collective bargaining agreement.

(3) In the case of a collectively bargained welfare benefit fund, only the portion of the fund (as determined under allocation rules to be provided by the Commissioner) attributable to employees covered by a collective bargaining agreement, and from which benefits for such employees are provided, is considered to be maintained pursuant to a collective bargaining agreement.

(4) Notwithstanding the preceding paragraphs and pending the issuance of regulations setting account limits for collectively bargained welfare funds, a welfare benefit fund will not be treated as a collectively bargained welfare benefit fund for purposes of Q&A-1 if and when, after July 1, 1985, the number of employees who are not covered by a collective bargaining agreement and are eligible to receive benefits under the fund increases by reason of an amendment, merger, or other action of the employer or the fund. In addition, pending the issuance of such regulations, for purposes of applying the 50 percent test of paragraph (2) to a welfare benefit fund that is not in existence on July 1, 1985, “90-percent” shall be substituted for “50-percent.”

Section 1.162-10 provides, in part, that amounts paid or accrued within the taxable year for a sickness, accident, hospitalization, medical expense, or similar benefit plan, are
deductible under section 162(a) if they are ordinary and necessary expenses of the trade or business.

Section 1.162-10T, Q&A-2, provides that section 419 generally applies to contributions paid or accrued with respect to a welfare benefit fund after December 31, 1985, in taxable years of employers ending after that date.

Section 4976(a) of the Code imposes a 100 percent excise tax if an employer maintains a welfare benefit fund and there is a disqualified benefit provided during any taxable year.

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

Section 4976(b)(3) 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.

ANALYSIS:

You represent that all deductions for years prior to 1986 for contributions made to the LIFA (before the effective date of section 419) were in accordance with section 162. Under section 4976(b)(3), amounts attributable to contributions made prior to the effective date of section 419 are not subject to the section 4976(b)(1)(C) excise tax. Accordingly, the proposed transfer of any amounts attributable to pre-1986 contributions to the LIFA will not result in a reversion to the benefit of the employer within the meaning of section 4976(b)(1)(C).

You represent that all deductions for years after 1985 for contributions made to the LIFA were in accordance with section 419A(f)(5). Amounts attributable to contributions made to the LIFA after 1985 will not revert to Company B because those amounts will be used by Trust to provide collectively bargained for post-retirement medical benefits. Accordingly, the proposed transfer of those amounts will not cause a reversion to Company B within the meaning of section 4976(b)(1)(C).

The rulings contained in this letter are based upon information and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. While this office has not verified any of the material submitted in support of the request for rulings, it is subject to verification on examination.

Except as expressly provided herein, no opinion is expressed or implied concerning the tax consequences of any aspect of any transaction or item discussed or referenced in this letter.
This ruling is directed only to the taxpayer requesting it. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

Janet Laufer
Senior Technician Reviewer
Health & Welfare Branch
Office of Division Counsel/Associate Chief
Counsel (Tax Exempt & Government Entities)