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Person To Contact:

Telephone Number:

Refer Reply To:
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PLR-138562-15

Date:
May 25, 2016

Legend

Authority =
State =
Hospital =
County =
Act =
Ordinance =
County Defined Benefit Plan =
County Defined Contribution Plan =

Dear :

This letter responds to a letter from your authorized representative dated November 23, 2015, as well as subsequent correspondence, submitted on behalf of Authority, requesting rulings that:

(1) Authority's income is excludable from gross income under section 115(1) of the Internal Revenue Code (Code);

(2) (a) Authority is an instrumentality within the meaning of sections 3121(b)(7) and 3306(c)(7); and accordingly, (b) remuneration paid to Authority's employees is not subject to the taxes imposed under the Federal Unemployment Tax Act (FUTA), (c) remuneration paid to an employee of the Authority is subject to social security taxes imposed under sections 3101(a) and 3111(a) of the Code if the employee is covered under an agreement under section 218 of the Social Security Act ("section 218 agreement"); (d) remuneration paid to an employee of the Authority is not subject to social security taxes if the employee is a participant in the County Defined Contribution Plan provided the employee is not covered under a section 218 agreement, (e) remuneration paid to an employee of the Authority is not subject to social security taxes if the employee is a participant in the County Defined Benefit Plan provided the employee is not covered under a section 218 agreement; and

(3) Authority is a successor employer to the County for purposes of determining whether the maximum wage base exception provided by section 3121(a)(1) applies.

FACTS

State passed the Act in order to facilitate Hospital continuing in its mission as a public hospital with improved organizational and operational structure that allows for greater flexibility, responsiveness, and innovation. The Act authorizes the County Board of Supervisors (County Board) to pass Ordinance creating Authority and to transition Hospital and its operations to Authority. The Act provides that Authority will be a public agency that is a local unit of government separate and apart from the county and any other public entity for all purposes.

The purpose of Authority is to provide medical care for County's indigent population, to achieve continued viability of the Hospital, and to provide an ongoing material benefit to County and its residents.

To accomplish its purpose, Authority is authorized by statute to enter into joint ventures with any public or private entity. However, Authority represents that it is not a party to any joint venture with any private non-governmental entity.

Ordinance establishing Authority provides that substantially all of the assets of Hospital and related health care resources shall be transferred to Authority. Authority represents that County will transfer to Authority all the real property, buildings, fixtures, equipment, supplies, and other assets necessary to operate Hospital, and that immediately thereafter employees will be transferred directly and immediately from the employ of County to the employ of Authority.

Ordinance provides that Authority shall not be an agency, division, or department of County or any other public entity, but shall be an instrumentality of County for purposes of participating in the County's Retirement Plan and other governmental plan.

Ordinance provides for a transitional governing board consisting of the Chief Executive Officer (CEO) of Hospital, a person engaged in the administration of Hospital appointed by the CEO, the County Administrative Officer, and one County executive appointed by the County Administrative Officer. The County Administrative Officer is the chair of the transitional governing board. The transitional governing board is to function for the exclusive purpose of facilitating the transfer of Hospital and its operations to Authority in advance of the appointment of the Governing Board of Authority. Any action taken by the transitional governing board may be taken only after a unanimous vote in favor of the action. The transitional governing board shall cease upon its dissolution by the County Board, or shall automatically be dissolved upon the assumption of office of sufficient members of the Governing Board to constitute a quorum allowing Authority to conduct business.

Under County law, the Authority Governing Board shall consist of the County Administrative Officer (ex officio), a member of the Hospital medical staff, and five members of the community at large appointed by the County Board, none of whom shall be a physician. Announcement of community member vacancies and Hospital medical staff vacancies on the Governing Board shall be posted on County and Authority web sites, at Hospital, and via press release. The applications for positions on the Authority Governing Board will be reviewed by a committee consisting of the County Counsel, the CEO of Hospital, and the County Administrative Officer. The completed applications of all qualified applicants are submitted to the County Board at least 30 days prior to the scheduled meeting of the County Board to consider appointment of an individual to fill any vacancy on the Governing Board.

The County Board will select the five community members and the medical staff member of the Governing Board from the pool of qualified applicants as reviewed by the reviewing committee discussed in the preceding paragraph. Under Ordinance, applications from all qualified applicants for the Governing Board shall be provided to the County Board, and the County Board selects the new appointees. With respect to selection of the member of the Hospital medical staff on the Governing Board, the County Board conducts interviews before making the selection.

Ordinance provides that Authority shall have the ability to retain surplus revenues for uses consistent with its purposes. If Authority participates in the County treasury pool, Authority is required to deposit all revenues received in the treasury pool, and the treasurer shall immediately credit and apply on its books any and all revenues so deposited to the repayment of any temporary transfers made to Authority by County.

Ordinance provides that the County Board shall either approve or reject Authority's annual budget in its entirety; the County Board shall not approve or reject individual line items in the budget. Authority shall conduct and fund an independent annual audit by an audit firm approved by the County Board and shall provide copies of all final audits of

Authority or the Hospital to the County Board. Authority shall provide the County Board upon request with a plan to address audit findings requiring corrective action, and a report of corrective action taken. The County Board shall approve the initial and any successive CEO of Authority prior to his or her appointment by Authority. The County Board may participate in the evaluation of the CEO and shall have the authority to remove the CEO.

Authority shall obtain the approval of the County Board prior to entering into or incurring any debt other than (1) debt which has a repayment term of less than one year and (2) debt secured only by private property. Authority may request that the County Board levy a tax on behalf of Authority. If the County Board approves the proposal to levy the tax, it shall call the election to seek voter approval and place the appropriate measure on the ballot for that election. The County Board may, at the request and on behalf of Authority, contract for services or purchase items as it deems necessary, appropriate, or convenient for the conduct of Authority's activities consistent with its purposes. The County shall provide or arrange for legal services to Authority, and shall bill Authority accordingly. The County Board shall have the right to approve certain actions by Authority, which include, among other things: (a) transfer of substantially all of the assets, operations, or control of Hospital from Authority; (b) relocation or replacement of the acute care hospital; (c) replacement or acquisition of any new acute care hospital; and (d) establishment or acquisition of new health care programs or facilities that have an annual operating budget that exceeds a certain percentage of Authority's total annual operating budget; (e) elimination of certain services; (f) establishment or operation of certain types of health plans; and (g) operation or ownership of any facility or clinic located outside of County.

County Board shall adopt the initial governing Bylaws for Authority, which it may amend from time to time. The Bylaws shall become operative upon approval by a majority vote of the County Board. Any changes or amendments to the Bylaws shall be by majority vote of the County Board.

Employees of Authority are deemed to be employees of County under County Defined Benefit Plan and are eligible to participate in the plan. Employees transferring to Authority will maintain equivalent positions and benefits seniority. Although the financial obligations of Authority are generally not obligations of County or State, County is obligated to make employer contributions to County Defined Benefit Plan for legacy employees in the event Authority fails to do so and, in the event of Authority's dissolution or bankruptcy, County is also obligated to make employer contributions to County Defined Benefit Plan for Authority employees hired after the transfer of Hospital from County to Authority. Authority represents that the benefits provided under the County Defined Benefit Plan are at least equal to the Primary Insurance Amount under social security.

County Defined Contribution Plan is a mandatory plan under which 7.5 percent of a participant employee's compensation is deferred and required to be contributed to the plan. An eligible employee for purposes of the County Defined Contribution Plan includes all common law part-time, temporary, and seasonal employees of the County who are not eligible to participate in the County Defined Benefit Plan, the County pension plan for physician employees or any other County retirement plan which satisfies the requirements of section 218 of the Social Security Act. The County Defined Contribution Plan is intended to be a plan described in section 457(b) of the Code and to meet the definition of a "retirement system" under section 3121(b)(7)(F) of the Code. The plan provides that all amounts of deferred compensation shall at all times be and remain as assets of the participant. The plan also provides that any and all interest or other income payable on any of the participant's investments of deferred compensation also shall be an asset of the participant. The plan covers employees of eligible employers pursuant to section 457(e) who adopt the plan and meet certain additional conditions. The Authority intends to adopt the plan and become an eligible employer in an agreement between Authority and County.

County Board has the power to dissolve Authority. In the event of dissolution, County Board shall provide for the disposition of Authority's assets, obligations, and liabilities to County or another State or public entity for a public purpose.

LAW AND ANALYSIS

1. Income Excluded from Gross Income under Section 115

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

Rev. Rul. 77-261, 1977-2 C.B. 45, holds that income generated by an investment fund that is established by a state to hold revenues in excess of the amounts needed to meet current expenses is excludable from gross income under section 115(1) of the Code, because such investment constitutes an essential governmental function. The ruling explains that the statutory exclusion is 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 an entity engaged in the operation of a public utility or the performance of some governmental function that accrues to either a state or political subdivision of a state. 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 that are within the ambit of a sovereign to conduct.

Rev. Rul. 90-74, 1990-2 C.B. 34, holds that the income of an organization formed, funded, and operated by political subdivisions to pool various risks (casualty, public

liability, workers' compensation, and employees' health) is excludable from gross income under section 115(1) of the Code because the organization is performing an essential governmental function. The revenue ruling states that the income of such an organization is excluded from gross income so long as private interests do not participate in the organization or benefit more than incidentally from the organization. The benefit to the employees of the insurance coverage obtained by the member political subdivisions was deemed incidental to the public benefit.

By providing hospital and medical care to County's residents, including the indigent population in particular, Authority promotes public health. Promoting public health is an essential government function within the meaning of section 115(1) of the Code. See Rev. Rul. 77-261.

No part of the net earnings of Authority inures to the benefit of, or is distributable to, any private entity or individual. No private interests are involved or participate in the Authority. Upon dissolution, assets of the Authority must be distributed to County or another State or other public entity. Thus, the Authority's income accrues to a state or a political subdivision of a state within the meaning of section 115(1) of the Code. See Rev. Rul. 90-74.

Based solely on the facts and representations submitted, Authority's income is excludable from gross income under section 115(1) of the Code.

2. Instrumentality Issue

Federal Insurance Contributions Act (FICA) taxes are imposed on wages as defined in section 3121 of the Code. The term "wages" is defined in section 3121(a) as all remuneration for employment, unless specifically excepted. "Employment" is defined in section 3121(b) as including any service of whatever nature, performed by an employee for the person employing him or her, with certain exceptions. FICA taxes include the Old-Age, Survivors, and Disability Insurance Tax (social security taxes) and hospital insurance taxes (Medicare taxes). Social security taxes are imposed by sections 3101(a) (employee's portion) and 3111(a) (employer's portion). Medicare taxes are imposed by sections 3101(b) (employee's portion) and 3111(b) (employer's portion). The Additional Medicare Tax is imposed under section 3101(b)(2) and consists of the employee's portion only.

Section 3121(b)(7) provides an exception from the definition of employment for service performed in the employ of a State or any political subdivision thereof, or any instrumentality of one or more of the foregoing which is wholly owned thereby, except that the paragraph shall not apply in the case of certain services. The section 3121(b)(7) exception does not apply if the service is covered under an agreement entered into pursuant to section 218 of the Social Security Act ("section 218 agreement"). Generally, the exception provided by section 3121(b)(7) applies if the

employee of the State, political subdivision, or instrumentality is a member of a retirement system of such State, political subdivision or instrumentality and if the employee is not covered under a section 218 agreement.

Rev. Rul. 57-128, 1957-1 C.B. 311, sets forth six factors that are used to determine whether an organization is an instrumentality of a state or political subdivision which is wholly owned thereby:

- (1) Whether the organization is used for a governmental purpose and performs a governmental function;
- (2) Whether the performance of the organization's function is on behalf of one or more states or political subdivisions;
- (3) Whether there are any private interests involved, or whether the states or political subdivisions involved have the powers and interests of an owner;
- (4) Whether control or supervision of the organization is vested in public authority or authorities;
- (5) If express or implied statutory or other authority is necessary to the creation and/or use of such an instrumentality, and whether such authority exists; and
- (6) The organization's degree of financial autonomy and the source of its operating expenses.

Generally, the exception provided by section 3121(b)(7) does not apply for Medicare tax purposes. The rules governing Medicare taxation of services performed by employees of states and political subdivisions and instrumentalities are in section 3121(u)(2). Generally, remuneration paid for services of an employee of a state, local government, or one of their instrumentalities is subject to Medicare taxes unless the continuing employment exception provided by section 3121(u)(2)(C) applies. Generally, the continuing employment exception from Medicare taxation in section 3121(u)(2)(C) may apply if the employee has been continuously employed by the same governmental entity and was performing services prior to April 1, 1986.

Section 3301 imposes on every employer (as defined in section 3306(a)) for each calendar year the tax under the FUTA equal to a certain percentage of wages. Section 3306(b) provides that wages for FUTA purposes means all remuneration for employment with certain specific exceptions. Employment is defined in section 3306(c) for FUTA purposes as including services performed by an employee for an employer with certain specific exceptions. Section 3306(c)(7) provides an exception from employment for FUTA tax purposes for services performed in the employ of a State, or any political subdivision thereof, or in the employ of an Indian tribe, or any

instrumentality of one or more of the foregoing which is wholly owned by one or more States or political subdivisions or Indian tribes.

In determining whether Authority is an instrumentality of County wholly owned by County for purposes of FICA and FUTA, we consider the factors set forth in Rev. Rul. 57-128. With respect to the first factor, Authority is used for a governmental purpose and performs a governmental function. The provision of medical care to County's indigent population and the provision of public medical care qualify as a governmental purpose. Also, providing medical care to the public is considered a governmental function.

With respect to the second factor, the performance of its function is on behalf of County. Authority is providing and promoting health care for the indigent residents of County and for the benefit of the residents of County.

With regard to the third factor, there are no private interests involved and County has powers and interests of an owner. Authority is run by the Governing Board, which is appointed by the County Board, with the County Administrative Officer serving ex-officio. A member of the Governing Board may be removed by the County Board during his or her term with or without cause. The County Board approves the annual budget of Authority. The County Board approves the CEO of Authority and has the authority to remove the CEO. The County Board, in its discretion, may find and declare by adoption of a resolution that Authority shall cease to exist and cause Authority to be dissolved. In event of dissolution, the County Board shall provide for the disposition of Authority's assets, obligations, and liabilities. Authority is required to conduct and fund an independent annual audit by an audit firm approved by the County Board. County retains control over any transfer of operations and/or any subleasing of Hospital.

With regard to the fourth factor, some control and supervision of Authority is vested in County. The County Board appoints and can remove board members, adopts and amends the Bylaws of Authority, and can dissolve Authority. The County Board approves the CEO of Authority and has the authority to remove the CEO. The County Board approves the annual budget. Authority must obtain the approval of the County Board before incurring any debt other than debt of less than one year, or debt secured by personal property.

With regard to the fifth factor, State law passed legislation (Act) that authorized the creation of Authority by County law (Ordinance).

The sixth factor is the degree of financial autonomy and the source of operating expenses. The operating expenses of the Authority are paid by a combination of public funding and Authority's own income. Authority may ask the County to levy a tax on its behalf. Authority may borrow money from County. The County Board may make purchases and contract for services on behalf of Authority. County will pay

contributions for the pensions of legacy employees and upon dissolution or bankruptcy, County will pay the employer contributions of newly-hired employees. Upon dissolution, the County Board shall provide for the disposition of any remaining Authority assets, including transfer of such assets to County or another State or public entity for a public purpose. County retains the ultimate responsibility for indigent medical care, even though the care will be performed by Authority.

Therefore, after consideration of the factors set forth in Rev. Rul. 57-128, we conclude that Authority is an instrumentality wholly owned by County for purposes of section 3121(b)(7) and 3306(c)(7).

Whether FUTA tax applies to the remuneration paid to employees of Authority

Because Authority is an instrumentality wholly owned by County, services in the employ of authority are excepted from employment by section 3306(c)(7). Therefore, remuneration paid for services in the employ of Hospital is not subject to FUTA tax.

Whether social security tax applies to the remuneration paid to employees of Authority

If an employee of a state, political subdivision, or instrumentality thereof is covered under an agreement under section 218 of the Social Security Act, the employee's remuneration is subject to social security taxes. See section 3121(b)(7)(E). When an employee is not covered under a section 218 agreement, the employee's remuneration is generally subject to social security taxes unless the employee is a member of a retirement system. Section 31.3121(b)(7)-2 of the regulations provides rules for determining whether an employee is a "member of a retirement system." These rules generally treat an employee as a member of a retirement system if he or she participates in a system that provides retirement benefits, and has an accrued benefit or receives an allocation under the system that is comparable to the benefits he or she would have or receive under Social Security. In the case of part-time, seasonal and temporary employees, this minimum retirement benefit is required to be nonforfeitable.

Section 31.3121(b)(7)-2(e)(2) of the regulations provides that a plan must provide a minimum level of benefits to an employee for the employee to qualify as a member of a retirement system. Under section 31.3121(b)(7)-2(e)(2)(ii), a defined benefit retirement system maintained by a State, political subdivision or instrumentality thereof meets the requirements of section 31.3121(b)(7)-2(e)(2) with respect to an employee on a given day if and only if, on that day, the employee has an accrued benefit under the system that entitles the employee to an annual benefit commencing on or before his or her Social Security retirement age that is at least equal to the annual Primary Insurance Amount the employee would have under Social Security. For this purpose, the Primary Insurance Amount an individual would have under Social Security is determined as it would be under the Social Security Act if the employee had been covered under Social Security for all periods of service with the State, political subdivision or instrumentality,

had never performed service for any other employer, and had been fully insured within the meaning of section 214(a) of the Social Security Act, except that all periods of service with the State, political subdivision or instrumentality must be taken into account (i.e., without reduction for low-earning years). Rev. Proc., 91-40, 1991-2 C.B. 694, provides safe harbor formulas for defined benefit retirement systems for purposes of meeting the minimum benefit requirement of the regulations.

A defined contribution retirement system maintained by a State, political subdivision or instrumentality thereof meets the requirements of section 31.3121(b)(7)-2(e)(2) with respect to an employee if and only if allocations to the employee's account (not including earnings) for a period are at least 7.5 percent of the employee's compensation for service for the State, political subdivision or instrumentality during the period. Matching contributions by the employer may be taken into account for this purpose.

Authority states that the County Defined Benefit Plan provides benefits that are in excess of the primary insurance amount under social security. If the County Defined Benefit Plan provides benefits to an employee that are in excess of the primary insurance amount under social security under the specific test set forth in section 31.3121(b)(7)-2(e)(2)(ii) of the regulations or that meets one of the safe harbors described in Rev. Proc. 91-40, 1991-2 C.B. 694, the services of the employee in the employ of Authority are excepted from employment for social security tax purposes, provided the employee is not covered under a section 218 agreement.

A participant in the County Defined Contribution Plan meets the requirements to be a member of a retirement system under section 3121(b)(7)(F), because the plan provides for a 7.5 percent contribution from deferred compensation that is nonforfeitable and that is required to be made with respect to part-time, seasonal and temporary employees. Thus, the services of employees who are not covered under a section 218 agreement and who are covered under the County Defined Contribution Plan whose compensation is deferred as set forth in the plan will be excepted from employment by section 3121(b)(7)(F) and their remuneration will not be subject to social security taxes.

Whether Medicare tax applies to the remuneration paid to employees of Authority

Section 3121(u)(2) provides generally that remuneration paid to employees of states, political subdivisions, or instrumentalities thereof is subject to Medicare tax unless the continuing employment exception provided by section 3121(u)(2)(C) applies. Therefore, remuneration paid to Authority employees is subject to Medicare tax unless the continuing employment exception applies.

3. Successor Employer Issue

With respect to those employees who are subject to social security tax because they are covered under a section 218 agreement, Authority has requested a ruling that it will

qualify as a successor employer to the County for purposes of determining whether the exception from wages for social security tax purposes provided by section 3121(a)(1) applies.

Section 3121(a)(1) provides an exception from the social security tax portion of the FICA for remuneration paid by an employer to an employee with respect to employment during the calendar year after the employer has paid wages to the employee equal to the contribution and benefit base for the year. There is generally no exception from wages for an employer because another employer has already paid wages to the employee equal to the contribution and benefits base during the calendar year. Remuneration paid by the second employer is generally subject to social security taxes on remuneration that is not otherwise excepted up to the amount of a new contribution and benefit base applicable to that employer with respect to the employee. Although the employee can obtain a refund of the employee portion of social security taxes on his or her income tax return to the extent the employee portion of social security taxes has been paid on wages in excess of the contribution benefit base as a result of the employee having two or more employers, the employer is not entitled to a refund of the employer portion of social security tax on such wages.

The predecessor-successor rule in section 3121(a)(1) provides an exception to the general rule that a new contribution and benefit base applies in the case of a second employer. Section 3121(a)(1) provides that, if an employer (referred to as a successor employer) during any calendar year “acquires substantially all the property used in a trade or business of another employer (hereinafter referred to as a predecessor), or used in a separate unit of a trade or business of a predecessor, and immediately after the acquisition employs in his trade or business an individual who immediately prior to the acquisition was employed in the trade or business of such predecessor, then, for the purpose of determining whether the successor employer has paid remuneration ... with respect to employment equal to the contribution and benefit base ..., to such individual during such calendar year, any remuneration ... paid with respect to employment paid ... to such individual by such predecessor during such calendar year and prior to the acquisition shall be considered as having been paid by such successor employer.”

Section 31.3121(a)(1)-1(b)(2) of the regulations provides that three tests must be met for the wages paid, by a predecessor to an employee to be, for purposes of the annual wage limitation, treated as having been paid to such employee by a successor:

- (i) The successor during a calendar year acquired substantially all the property used in a trade or business, or used in a separate unit of a trade or business, of the predecessor;
- (ii) Such employee was employed in the trade or business of the predecessor immediately prior to the acquisition and is employed by the successor in the successor’s trade or business immediately after the acquisition; and
- (iii) Such wages were paid during the calendar year in which the acquisition occurred and prior to such acquisition.

Section 31.3121(a)(1)-1(b)(3) of the regulations provides that the method of acquisition by an employer of the property of another employer is immaterial. The acquisition may occur as a consequence of the incorporation of a business by a sole proprietor or a partnership, the continuance without interruption of the business of a previously existing partnership by a new partnership or by a sole proprietor, or a purchase or any other transaction whereby substantially all the property used in a trade or business, or used in a separate unit of a trade or business, of one employer is acquired by another employer.

Section 31.3121(a)(1)-1(b)(4) of the regulations provides that substantially all the property used in a separate unit of a trade or business may consist of substantially all the property used in the performance of an essential operation of the trade or business, or it may consist of substantially all the property used in a relatively self-sustaining entity which forms a part of the trade or business.

Section 31.3121(a)(1)-1(b)(4) of the regulations provides two examples of the requirement that the successor acquired substantially all the property used in a separate unit of a trade or business. In Example 1, the M Corporation, which is engaged in the manufacture of automobiles, including the manufacture of automobile engines, discontinues the manufacture of the engines and transfers all the property used in such manufacturing operation to the N Company. Under the regulations, the N Company is considered to have acquired a separate unit of the trade or business of the M Corporation, namely, its engine manufacturing unit. In Example 2, the R Corporation which is engaged in the operation of a chain of grocery stores transfers one of such stores to the S Company. The regulations provide that the S Company is considered to have acquired a separate unit of the trade or business of the R Corporation.

Section 31.3121(a)(1)-1(b)(5) of the regulations provides that a successor may receive credit for wages paid to an employee by a predecessor only if immediately prior to the acquisition the employee was employed by the predecessor in his trade or business which was acquired by the successor and if immediately after the acquisition such employee is employed by the successor in his trade or business (whether or not in the same trade or business in which the acquired property is used). If the acquisition involves only a separate unit of a trade or business of the predecessor, the employee need not have been employed by the predecessor in that unit provided he was employed in the trade or business of which the acquired unit was a part.

With regard to the three requirements sets forth in the regulations for successor status, Authority has represented that it will acquire substantially all the assets of Hospital. Hospital qualifies as a separate unit of a trade or business for purposes of the underlying regulations. The employees who will be transferred are employed in the trade or business of the predecessor immediately prior to the acquisition. Authority has also represented that the employees will be employed by Authority in its trade or

business immediately after the asset acquisition. Wages are paid by County during the calendar year prior to the acquisition.

Thus, provided the transfer of employment with respect to a particular employee is immediately after the acquisition of the assets, Authority will qualify as a successor employer under section 3121(a)(1) for purposes of determining whether remuneration paid to the employee in the calendar year is in excess of the contribution and benefit base for social security tax purposes. Thus, Authority may take into account wages paid by the County before the acquisition in determining whether the section 3121(a)(1) exception from wages for social security tax purposes applies.

CONCLUSIONS

(1) The income of Authority is excludable from gross income under section 115 of the code.

(2) (a) Authority is a wholly owned instrumentality of County for purposes of section 3121(b)(7) and section 3306(c)(7).

(b) Remuneration for services in the employ of Authority is not subject to FUTA taxes because Authority is a wholly owned instrumentality under section 3306(c)(7).

(c) Remuneration for services in the employ of Authority by an employee who is covered under a section 218 agreement is subject to social security taxes.

(d) Remuneration for services in the employ of Authority by an employee who is not covered under a section 218 agreement and who is a member of the County Defined Contribution Plan and is deferring and has deferred compensation in accordance with the terms of that plan is not subject to social security taxes.

(e) Remuneration for services in the employ of Authority by an employee who is not covered under a section 218 agreement and who is a member of the County Defined Benefit Plan is not subject to social security tax provided that the employee's benefits under such plan meet the requirements of the specific test set forth in section 31.3121(b)(7)-2(e)(2)(ii) of the regulations or that the employee's benefits under the plan meet one of the safe harbors described in Rev. Proc. 91-40, 1991-2 C.B. 694.

(3) Authority qualifies as a successor employer to County for purposes of determining whether the exception under section 3121(a)(1) applies with respect to employees who are employed by Authority immediately after the acquisition, and thus Authority may take into account wages paid by County before the acquisition in the calendar year in determining whether wages in excess of the contribution and benefit base have been paid to such employees.

This ruling is limited to the facts and representations stated in this letter. Except as expressly provided in this letter, 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 that requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent. In accordance with the Power of Attorney on file, we are sending a copy of this ruling letter to your authorized representatives.

Sincerely,

Theodore R. Lieber
Senior Tax Law Specialist
Exempt Organizations Branch 1
Associate Chief Counsel
(Tax Exempt and Government Entities)