

## Internal Revenue Service

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Department of the Treasury  
Washington, DC 20224

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Person To Contact:  
, ID No.

Telephone Number:

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Date:  
June 06, 2017

### Legend

Employer =

State =

County =

Association =

Trust =

Trustee =

Dear :

This letter responds to a letter from Trust's authorized representative dated December 13, 2016, submitted on behalf of Trust, requesting a ruling that (1) Trust's income is excludable from gross income under Internal Revenue Code ("IRC") § 115 and (2) Trust is not required to file an annual federal income tax return under IRC § 6012(a)(4). Trust represents the facts as follows:

### FACTS

Employer is a governmental entity and political subdivision of State. County is a political subdivision of State. Pursuant to State statute, Employer established Trust to hold and invest assets to pre-fund a program that extends medical and death benefits to certain retired employees of Employer and their eligible spouses and dependents. Association is a statutorily created retirement system in which Employer participates.

Trust will receive contributions from Employer as needed to fund Trust. Trust assets will be used for the exclusive purpose of providing retiree health and welfare benefits and for defraying reasonable administrative and actuarial expenses. Under no circumstances will the assets be used for, or diverted to, any other purpose, except as permitted under IRC § 115 and other applicable law.

Trust is governed by Trustee, which is comprised of a nine member board. Trustee consists of a majority of members who are appointed by County board of supervisors and the remaining members are selected by the members of Trustee. Trustee has investment authority over Trust funds, including the authority to invest funds in investments permitted by State law.

Trust may be dissolved by Employer. However, upon termination of Trust, any remaining assets will be used to provide health and welfare benefits to retirees and their eligible spouses and dependents. Any assets remaining in Trust after satisfying all benefit obligations may be paid to Employer to the extent consistent with IRC § 115. In no event will Trust's assets be distributed or revert to any entity that is not a state, a political subdivision of a state, or another entity the income of which is excluded from its gross income by application of IRC § 115.

Trust represents that no private interests participate in, or benefit more than incidentally from Trust.

## LAW AND ANALYSIS

### Issue 1- IRC § 115(1)

IRC § 115(1) 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 IRC § 115(1), 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 (e.g., casualty, public liability, workers' compensation, and employees' health) is excludable from gross income under IRC § 115(1) 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.

The provision of these health and welfare benefits by Employer constitutes the performance of an essential government function within the meaning of IRC § 115(1). See Rev. Rul. 90-74 and Rev. Rul. 77-261.

No private interests will participate in, or benefit from, the operation of Trust other than as providers of goods or services. The benefit to retirees and eligible spouses and dependents is incidental to the public benefit. See Rev. Rul. 90-74.

As stated above, Trust was formed for the sole purpose of providing a prefunding source for the payment of liabilities for health and welfare benefits to retirees and eligible spouses and dependents of Employer.

Trust's dedication of its corpus and income exclusively for the benefit of the retirees of Employer and their dependents satisfies an obligation of Employer to provide health and welfare benefits to its retired employees. The benefit to Employer's participating retirees, spouses, and their dependents is incidental to the public benefit. Upon termination, all of Trust's assets must be used for funding the postemployment benefits offered by Employer or administrative expenses. Any remaining assets will be distributed to Employer, a political subdivision of State.

#### Issue 2 - IRC § 6012(a)(4)

IRC § 6012(a)(4) provides that every trust having for the taxable year any taxable income, or having gross income of \$600 or over, regardless of the amount of taxable income, must file a return with respect to income taxes under subtitle A.

Section 301.7701-1(b) of the Procedure and Administration Regulations provides, in part, that the classification of organizations that are recognized as separate entities is determined under §§ 301.7701-2 through 301.7701-4(a), unless a provision of the IRC provides for special treatment of that organization.

Section 301.7701-4(a) of the Procedure and Administration Regulations provides, in general, that an arrangement will be treated as a trust under the Code if it can be shown that the purpose of the arrangement is to vest in trustees responsibility for the protection and conservation of property for beneficiaries who cannot share in the discharge of this responsibility and, therefore, are not associates in a joint enterprise for the conduct of business for profit.

Contributions to Trust are to be used to prefund health care coverage and related administrative costs for certain retirees and their dependents. Trustee is charged with the responsibility of protecting and conserving Trust property for the benefit of beneficiaries of Trust pursuant to State law. Beneficiaries of Trust cannot share in the discharge of Trustee's responsibility for the protection and conservation of Trust property and, therefore, are not associates in a joint enterprise for the conduct of a business for profit.

IRC § 6012(a)(4) does not require a trust without taxable income to file a return when gross income is less than \$600. Because Trust's income is excludable from gross income under IRC § 115(1), it is not required to file an annual income tax return.

#### RULINGS

Based solely on the facts and representations submitted by Trust:

- (1) Trust's income is excludable from gross income under IRC § 115; and,
- (2) Trust is not required to file an annual federal income tax return under IRC § 6012(a)(4).

The rulings contained in this letter are based upon information and representations submitted by or on behalf of Trust and accompanied by a penalty of perjury statement executed by an individual with authority to bind Trust and upon the understanding that there will be no material changes in the facts. 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. The Associate office will revoke or modify a letter ruling and apply the revocation retroactively if there has been a misstatement or omission of controlling facts; the facts at the time of the transaction are materially different from the controlling facts on which the ruling was based; or, in the case of a transaction involving a continuing action or series of actions, the controlling facts change during the course of the transaction. See Rev. Proc. 2017-1, § 11.05.

This letter does not address the applicability of any section of the Code or Regulations to the facts submitted other than with respect to the sections specifically described, and, except as expressly provided in this letter, no opinion is expressed or

implied concerning the tax consequences of any aspects of any transaction or item of income discussed or referenced in this letter.

Because it could help resolve questions concerning federal income tax status, this letter should be kept in Trust's permanent records.

A copy of this letter must be attached to any tax return to which it is relevant. Alternatively, if Trust files a return electronically, this requirement may be satisfied by attaching a statement to the return that provides the date and control number of this letter.

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to Trust's authorized representatives.

This ruling letter is directed only to Trust. Section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

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Andrew F. Megosh Jr.  
Senior Tax Law Specialist  
Office of the Chief Counsel  
(Tax Exempt and Government Entities)