

Internal Revenue Service

Department of the Treasury

Number: **200222019**
Release Date: 5/31/2002
Index Number: 106.00-00

Washington, DC 20224

Person to Contact:

Telephone Number:

Refer Reply To:

CC:TEGE:EB:HW-PLR-158362-01

Date:

02/27/2002

LEGEND

Taxpayer =
Plan =

Dear

This is in response to your letter dated October 2, 2001 and subsequent correspondence, requesting rulings on behalf of Taxpayer regarding the federal income tax treatment of benefits provided by Taxpayer to eligible retirees as part of a sick leave conversion plan. We are responding only to your second ruling request concerning whether Taxpayer's contributions to the Plan to provide supplemental medical benefits to retiring employees are excluded from the retirees' gross income under section 106 of the Internal Revenue Code (Code). The rulings you requested under sections 401(h), 401(a), 403(b), and 457 of the Code will be addressed by the Qualified Plans Branch 2 of the Office of Division Counsel/Associate Chief Counsel (TE/GE) which will respond to you directly.

Taxpayer is a school district which provides sick leave benefits to its employees. Taxpayer's employees are permitted a set number of days of sick leave annually and can accumulate any unused sick days in their sick leave account from year to year.

You represent that Taxpayer intends to adopt the Plan which will convert a retiring employee's accumulated unused sick leave into an additional retirement benefit. The conversion of leave would be calculated under a formula established by Taxpayer which will assign a dollar value to the sick days. The retirees do not have the option of taking any amounts in cash.

Under the Plan, Taxpayer will make contributions, measured by the value of the retiring employee's accumulated unused sick leave, to one of the following supplemental benefits prior to an employee's retirement: (1) additional medical coverage which will commence after the lapse of the retiree health insurance provided by Taxpayer and which will continue until the retiree's converted sick leave is exhausted or (2) contributions to a qualified deferred compensation plan which will begin on the date of

the employee's retirement. Taxpayer's contribution to either the supplemental medical benefit or the deferred compensation plan will be based on several factors including the retiring employee's access to other health insurance coverage, the value of the retiring employee's unused accumulated sick leave, and the willingness of Taxpayer's insurance carrier to cover retired employees. At no time does the retiring employee have a choice of contributions to the supplemental medical benefit or the deferred compensation plan.

Section 61(a) of the Code provides that, except as otherwise provided by law, gross income means all income from whatever source derived.

Section 106 of the Code provides that gross income of an employee does not include employer-provided coverage under an accident or health plan.

Section 1.106-1(a) of the Income Tax Regulations provides that the gross income of an employee does not include contributions which his employer makes to an accident or health plan for compensation (through insurance or otherwise) to the employee for personal injuries or sickness incurred by him, his spouse, or his dependents, as defined in section 152. The employer may contribute to an accident or health plan either by paying the premium (or a portion of the premium) on a policy of accident or health insurance covering one or more of his employees, or by contributing to a separate trust fund (including a fund referred to in section 105(e)) which provides accident and health benefits directly or through insurance to one or more of his employees. However, if such insurance policy, trust or fund provides other benefits in addition to accident or health benefits, section 106 applies only to the portion of the employer's contribution which is allocable to accident or health benefits.

Rev. Rul. 62-199, 1962-2 C.B. 38, holds that retirees are considered to be employees for purposes of section 106 of the Code.

Based on the information submitted and on the representations made, we conclude as follows:

Contributions to the proposed Plan to provide supplemental medical benefits to retiring employees are excludable from a retiring employee's gross income under section 106 of the Code.

Except as specifically ruled on above, no opinion is expressed or implied as to the federal tax consequences of the transaction described above under any other provision of the Code.

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

Sincerely,
Harry Beker
Chief, Health and Welfare Branch
Office of Division Counsel/Associate Chief Counsel
(Tax Exempt / Government Entities)

Enclosures:

Copy of Letter

Copy for section 6110 purposes