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Third Party Communication: None

Date of Communication: Not Applicable

Person To Contact:

, ID No.

Telephone Number:

Refer Reply To:

CC:TEGE:EB:HW

PLR-119338-05

Date:

October 13, 2005

Legend

Employer:

Trust Fund:

Plan:

State Retirement Association:

State:

Dear

This responds to your letter of May 13, 2004 and subsequent correspondence, requesting rulings on behalf of Employer concerning the proper Federal income tax treatment of Employer contributions to and payments from the Trust Fund under section 106 of the Internal Revenue Code (Code).

You represent that State Retirement Association is an instrumentality of the State. State Retirement Association maintains and administers a group health plan (the Plan) funded by the Trust Fund that provides medical coverage for individuals who are eligible to enroll in the Plan.

Employer is in the process of merging its retirement system with the State Retirement Association's retirement system. When the merger becomes effective, retired employees of Employer will become covered under the Plan and Employer's current employees will become eligible for coverage under the Plan upon subsequent retirement.

The Plan provides health care benefits for post-retirement health care expenses for retired members and their dependents. Under the Plan, medical coverage is provided through various health insurance plans and self-insured medical reimbursement plans. The medical plans include three health maintenance organizations (HMOs), one point of service plan (POS), two preferred provider organizations (PPOs), and two Medicare supplement plans. Dental HMO and PPO plans, as well as two vision PPO plans are also offered. Premiums are established annually for each plan, and different rates apply for those under and over age 65.

The Trust Fund was established to provide a "premium" subsidy for participants in the Plan and therefore pays a portion or all of the monthly premium for health care coverage up to a certain maximum. All employer contributions are made to the Trust Fund. Under the Plan, coverage is generally paid for jointly by the employer and its retired employees, according to the contribution method established by the particular employer. In the case of insured plans, an employer's share of the premium is paid directly from the Trust Fund to the insurance carrier. In the case of self-insured plans, an employer's subsidy for the cost of coverage is paid directly to the plan. Any additional cost of the health coverage is paid by the benefit recipient. A retired employee's share of the premium is deducted on an after-tax basis from his or her retirement benefit and is remitted directly from the Trust Fund to the insurance carrier or to the self-insured plan. If any amount is due from a retired employee because the employee's share of the premium exceeds the employee's retirement benefit, the retired employee is billed for the balance, and upon payment, the Trust Fund remits the balance directly to the insurance carrier or to the self-insured plan. The premium amount for an active member is collected from the employer. There are no reimbursements made to the benefit recipient from the Trust Fund.

As a condition of the merger, Employer is required to contribute to the Trust Fund an amount equal to the projected cost of its participation in the Plan. Employer will also make ongoing contributions to the Trust Fund to pay for the Employer's share of coverage for retired employees.

Section 61(a)(1) of the Code and section 1.61-21(a)(3) of the Income Tax Regulations provide that, except as otherwise provided in Subtitle A, gross income includes compensation for services, including fees, commissions, fringe benefits, and similar items.

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

Section 1.106-1 of the regulations states 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 the employee, the employee's spouse, or the employee's dependents as defined in section 152 of the Code. The employer may contribute to an accident or health plan either by paying the premium on a policy of accident or health insurance covering one or more of the employees, or by contributing to a separate trust or fund which provides accident or health benefits directly or through insurance to one or more of the employees. However, if the insurance policy, trust or fund provides other benefits in addition to accident or health, section 106 applies only to the portion of the contributions allocable to accident or health benefits.

Coverage provided under an accident and health plan to former employees and their spouses and dependents and also to deceased employees' spouses and dependents is excludable from gross income under section 106. See, Rev. Rul. 62-199, 1962-2 C.B. 38; Rev. Rul. 82-196, 1982-2 C.B. 53; and Rev. Rul. 85-121, 1985-2 C.B. 57.

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

Contributions to the Trust Fund made by Employer pursuant to the Merger Agreement (including lump sum and ongoing contributions) and payments from the Trust Fund which are used exclusively to pay for the accident or health coverage of retired employees and retired employees' spouses and dependents as defined in section 152 (determined without regard to section 152(b)(1), (b)(2), and (d)(1)(B)) are excludable from gross income under section 106 of the Code.

No opinion is expressed concerning the Federal tax consequences of the Trust Fund under sections 105, 115, 6012, 7701 or any other provision of the Code other than those specifically stated herein.

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

In accordance with the Power of Attorney on file with this office, a copy of this letter is being sent to your authorized representative.

Sincerely,

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