

Internal Revenue Service

Department of the Treasury
Washington, DC 20224

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Person To Contact:
, ID No.

Telephone Number:

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Date:
May 24, 2012

Legend

Trust =
City =
State =
Trustee =
Administrator =

Dear :

This letter responds to a letter from your authorized representative dated February 2, 2012, and subsequent correspondence your representative submitted on behalf of the Trust, requesting a ruling that the Trust’s income is excludable from gross income under Internal Revenue Code (“IRC”) § 115. The Trust represents the facts as follows.

FACTS

The City is a State political subdivision. The City established the Trust to hold and invest contributions to fund the City’s obligations to provide health care benefits for eligible retirees of the City and their dependents, in accordance with the terms of certain plans between the City and its employees or bargaining groups (the “Plans”).

Under the terms of the Trust agreement, the City designated the Trustee and the Administrator to serve in their respective positions as trustee and administrator of the Trust. The City may remove the Trustee or the Administrator and designate respective successors upon 90 days prior written notice to the Trustee or the Administrator.

Except for investment income, the income of the Trust consists solely of contributions from the City. No private interests participate in or benefit from the operation of the

Trust, other than for reasonable payment as providers of goods or services. The Trust assets are only available to pay for the insurance premiums to fund the post-employment health care benefits of the employees of the City and their dependents.

The Trust agreement provides that the Trustee shall receive and accept all contributions and shall hold, reinvest, and distribute cash, cash equivalents and securities and their increments, proceeds, earnings, and income solely to provide health and welfare benefits to retirees and their dependents. The City shall direct the Trustee to disburse amounts from the Trust directly to pay the insurance premiums to fund the health care benefits of the participants in the Plans or to reimburse the City for amounts it advances to fund such benefits. The Administrator shall have authority and responsibility for the management, disposition and investment of the Trust assets. The Trustee may invest and reinvest the contributions and Trust assets in cash, cash equivalents, or securities pursuant to the instructions of the Administrator.

The Trust agreement provides that upon any termination of the Trust, the assets of the Trust then held by Trustee, except such assets as may be needed to pay expenses or liabilities of the Trust, shall first be distributed pursuant to the terms of the Plans to provide for the medical benefits of the retirees and their dependents. None of the assets of the Trust will be distributed to any entity that is not the State, a political subdivision of the State, or an entity the income of which is excluded from gross income under IRC §115.

LAW AND ANALYSIS

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. In Rev. Rul. 90-74, private interests neither materially participate in the organization nor benefit more than incidentally from the organization.

The Trust funds the City's obligations to provide for the health benefits of retired employees of the City and their dependents. Providing health benefits to former public employees constitutes the performance of an essential governmental function within the meaning of IRC § 115(1). See Rev. Rul. 77-261 and Rev. Rul. 90-74.

In addition, the income of the Trust accrues to the City. No private interests participate in or benefit from the operation of the Trust, other than as providers of goods or services. The Trust's dedication of its corpus or income exclusively for the benefit of the retirees and their dependents satisfies an obligation the City has assumed or been assigned with respect to providing for the health benefits of its former employees. The benefit to the City's participating employees and their dependents is incidental to the public benefit. All of the Trust's assets that remain upon dissolution of the Trust, after providing for all outstanding obligations, will be distributed to a state, a political subdivision of a state, or an entity the income of which is excludable from gross income under IRC § 115(1). See Rev. Rul. 90-74.

Based on the information and representations submitted on behalf of the Trust, we conclude that:

Because the income of the Trust derives from the exercise of an essential governmental function and will accrue to a state or a political subdivision thereof, the Trust's income is excludable from gross income under IRC § 115(1).

No opinion is expressed concerning the federal tax consequences under any IRC provision other than the one specifically cited above. In particular, no representation is made whether or not contributions or premiums paid on behalf of or benefits received by employees, former employees, retirees, spouses, dependents, or others will be taxable to such recipients. This ruling concerns only the federal tax treatment of the Trust's income and may not be cited or relied upon as to any matter relating to the taxation of accident or health contributions or benefits.

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. IRC § 6110(k)(3) provides that it may not be used or cited as precedent.

In accordance with the Power of Attorney on file with this office, your authorized representative will receive a copy of this letter.

The ruling contained in this letter is 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 ruling, it is subject to verification on examination.

Sincerely,

Kenneth M. Griffin
Chief, Exempt Organizations Branch
(Tax Exempt & Government Entities)