Internal Revenue Service

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Person To Contact:
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Refer Reply To:
CC:TEGE:EB:HW
PLR-113160-13

Date:
August 06, 2013

Legend

City =

State =

Trust A =

Trust B =

Dear :

This is in response to your letter of March 13, 2013, and subsequent correspondence, in which you request rulings on behalf of City concerning the proper treatment for federal tax purposes of contributions that are made to retiree healthcare trusts. City is a municipal corporation in State. City Code provisions establish contribution rates for the City and eligible employees to contribute to fund post-employment healthcare. In addition to the City Code provisions, City entered into collective bargaining or other agreements with various employee groups requiring both City and employees to contribute to the cost of funding retiree healthcare.

The City has established retiree health trusts, Trust A and Trusts B, to receive the employer and employee contributions. Each trust fund is used as a funding vehicle, whereby the administrator of the trust fund accepts the contributions and forwards the contributions to the custodian for holding and administration. The trustees of each trust fund hold, invest, and reinvest the contributions. Benefits are paid from the trust funds.

The City has also adopted Resolutions that incorporate the following representations regarding employee contributions to the retiree healthcare trust funds: (1) Employee contributions are mandatory reductions in salary and will be used solely to fund the trust funds; (2) Employee contributions are a condition of employment with City; (3) Participation in retiree healthcare is mandatory for all employees subject to the coverage terms established by City Code provisions; (4) Employees may not elect to receive salary or benefits in lieu of making the mandatory contributions, and (5) Distributions may be used only for medical expenses described in section 213(d) of the Internal Revenue Code (Code).

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 of the Code, gross income includes compensation for services, including fees, commissions, fringe benefits, and similar items.

However, section 106(a) 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 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 or 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 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 is excludable from gross income under section 106. See Rev. Rul. 62-199, 1962-2 C.B. 32; Rev. Rul. 82-196, 1982-2 C.B. 53.

Section 3101 imposes taxes under the Federal Insurance Contributions Act (FICA) on an employee’s wages. Section 3306 imposes taxes under the Federal Unemployment Tax Act (FUTA). Sections 3121(a) and 3306(b) provide that, with certain exceptions, for

FICA and FUTA tax purposes, the term “wages” means all remuneration for employment, including the cash value of all remuneration (including benefits) paid in any medium other than cash. However, sections 3121(a)(2) and 3306(b)(2) provide that the term “wages” does not include any payment (including any amount paid by an employer for insurance) made to or on behalf of an employee or any of his dependents, for medical or hospitalization expenses. Section 3401(a) of the Code provides that for purposes of federal income tax withholding, “wages” means all remuneration for services performed by an employee for his employer, including the cash value of all remuneration (including benefits) paid in any medium other than cash. However, Rev.Rul. 56-632, 1956-2 C.B. 101, holds that when premiums paid by an employer under policies providing hospital and surgical services are excludable from the employees' gross income under section 106 of the Code, the amounts paid by the employer are not subject to federal income tax withholding.

Based on the information submitted and representations made, we conclude as follows: (1) Mandatory employee contributions that are made to the retiree health trust funds pursuant to City Code provisions, collective bargaining agreements and City Resolutions, are treated as employer contributions and are excludable from City employees’ gross income under section 106 of the Code.

(2) Mandatory employee contributions that are made to the retiree health trust funds pursuant to City Code provisions, collective bargaining agreements and City Resolutions, are not “wages” and are not subject to FICA taxes under section 3121(a), FUTA taxes under section 3306(b) or income tax withholding under section 3401(a) of the Code.

No opinion is expressed concerning the federal tax consequences under 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
Health & Welfare Branch
Office of Division
Counsel/Associate Chief Counsel
(Tax Exempt & Government
Entities)