

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

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Date of Communication: Not Applicable

Person To Contact:  
, ID No.

Telephone Number:

Refer Reply To:  
CC:EEE:EO2  
PLR-135956-18

Date:  
May 29, 2019

Legend

Agency =  
State =  
Trust =

Trustee =

Dear :

This letter responds to a letter from your authorized representative, dated December 6, 2018, requesting a ruling that (i) the Trust's income is excludable from gross income under section 115(1) of the Internal Revenue Code (Code), and (ii), the Trust is classified as a trust for purposes of section 7701(a)(1) of the Code and is not required to file an annual return under section 6012 of the Code. You represent the following facts.

**FACTS**

Agency was established pursuant to the laws of State. Agency is a body politic and an instrumentality of State, exercising public and essential governmental functions. Agency is required under laws of State to make payments for health and welfare benefits to State employee retirees, their spouses, and dependents of retirees under a retiree program. These health and welfare benefits may include, but are not be limited to, medical, prescription drugs, dental, vision, hearing, Medicare Part B or Part D premiums, life insurance, long-term care, and long-term disability insurance.

Agency established the Trust as a funding vehicle for these health and welfare benefits. Agency has appointed Trustee and delegated to Trustee the administrative and investment responsibilities over Trust. Trustee shall also have the responsibility for accepting contributions to the Trust. Contributions to fund the benefits under the Trust shall be designated by Agency, as provided under the law of State. Employee contributions shall not be permitted or accepted.

The Trust's provisions specifically provide that Trust is created for the sole purpose of providing health and welfare benefits for State employee retirees and their eligible spouses and dependents.

The Trust's provisions further provide that no portion of the principal or income of the Trust shall revert to State or Agency, except in a manner consistent with the Code, and no portion of the principal or income of the Trust shall be used for or diverted to any purpose other than meeting the Agency's obligations to provide these health and welfare benefits for retirees (and eligible spouses and dependents) and the payment of reasonable expenses of the program that provides these benefits.

The Trust's provisions also provide that in no event, including dissolution, will Trust assets be distributed to or revert to any entity other than the State, a political subdivision of the State, or an entity whose income is excluded from gross income under section 115 of the Code.

## LAW AND ANALYSIS

### Issue 1- Qualification under section 115(1) of the Code

Section 115(1) of the Code 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 section 115(1) because such investment constitutes an essential governmental function. The ruling states 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 explains 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 (casualty, public liability, workers' compensation, and employees' health) is excludable from gross income under section 115(1) because the organization is performing an essential governmental function. The revenue ruling states that the income of such an organization is excludable 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 Trust's provision of benefits constitutes the performance of an essential governmental function within the meaning of section 115 of the Code. See Rev. Rul. 90-74 and Rev. Rul. 77-261.

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

In no event, including dissolution, will the 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 excludable from its gross income by application of section 115(1) of the Code.

The Trust's income is excludable from gross income under section 115(1) of the Code because the Trust's income derives from the exercise of an essential governmental function and will accrue to a state or a political subdivision.

#### Issue 2- Qualification under sections 6012(a)(4) and 7701(a)(1) of the Code

Section 6012(a)(4) of the Code 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 (Regulations) provides that the classification of organizations that are recognized as separate entities is determined under sections 301.7701-2, 301.7701-3, and 301.7701-4 of the Regulations, unless a provision of the Code provides for special treatment of that organization.

Section 301.7701-4(a) of the Regulations provides that, in general, 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.

Trust enables Agency to set aside funds to be used to satisfy its health and welfare benefit funding obligations. The Trustee is charged with the responsibility of the protection and conservation of the Trust property for the benefit of the beneficiaries of the Trust. The beneficiaries of the Trust cannot share in the discharge of the Trustee's responsibility for the protection and conservation of property and, therefore, are not associates in a joint enterprise for the conduct of business for profit.

As such, the Trust is classified as a trust within the meaning of section 7701(a) of the Code and section 301.7701-4(a) of the regulations. Because Trust's income is excludable from gross income under section 115(1) of the Code, and section 6012(a)(4) of the Code does not require a trust without taxable income to file a return when gross income is less than \$600, the Trust is not required to file an annual income tax return.

### RULING

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

(1) The Trust's income derives from the exercise of an essential governmental function and will accrue to a state or a political subdivision; therefore, the Trust's income is excludable from gross income under section 115(1) of the Code.

(2) The Trust is classified as a trust within the meaning section 7701(a) of the Code and section 301.7701-4(a) of the regulations. Because all of the Trust's income is excludable from gross income under section 115(1) of the Code, the Trust will have no gross income and thus will not be required to file a return under section 6012(a)(4) of the Code.

The ruling contained in this letter is based upon information and representations submitted by or on behalf of the Trust and accompanied by a penalty of perjury statement executed by an individual with authority to bind the 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 a ruling, 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. 2019-1, section 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. Specifically, no representation is made that contributions or premiums paid on behalf of, or benefits received by, employees, former employees, retirees, spouses, dependents, or others will be tax-free. 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 the health and welfare benefits to State employee retirees or their beneficiaries under the program.

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

A copy of this letter must be attached to any tax return to which it is relevant. Alternatively, if the 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 the Trust's authorized representative.

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

Sincerely,

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James Zelasko  
Branch Chief  
Office of the Chief Counsel  
(Employee Benefits, Exempt Organizations  
and Employment Taxes)

cc: