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Person To Contact:
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Date:
December 02, 2013

Legend

Taxpayer:

LLC:

Debtors:

Retiree Welfare Plans:

Dear

This is in reply to your letter dated November 18, 2013 concerning the proper Federal tax treatment of a medical reimbursement plan under §§ 106 and 105 of the Internal Revenue Code (the Code).

Debtors filed voluntary petitions for relief under chapter 11 of title 11 of the Bankruptcy Code. The United States Bankruptcy Court issued an order directing the Office of the United States Trustee to appoint a retiree committee to represent the interests of the

Retiree Welfare Plans' retirees and beneficiaries. The Debtors had historically provided a number of benefits to their retired employees, their surviving spouses and eligible dependents through the Retiree Welfare Plans. The Bankruptcy Court subsequently issued an order approving the settlement agreement in which Debtors and the retiree committee mutually agreed to the termination date of the Retiree Welfare Plans. As part of the settlement agreement, the parties agreed that the Debtors would use the settlement amount to fund a medical reimbursement plan (the Plan).

Taxpayer created the LLC. In accordance with the terms of the settlement agreement the settlement amount was paid by the Debtors to the LLC and subsequently transferred by the LLC to the Taxpayer. The Retiree Welfare Plans were then terminated. The Taxpayer, which is exempt under §501(c)(9) of the Code, funds the Plan from the settlement amount.

Taxpayer represents that only eligible retirees, as provided for by the terms of the settlement agreement, who were receiving, or were eligible to receive benefits under the Retiree Welfare Plans, may become participants and receive benefits under the Plan. These include retired employees of one or more of the Debtors, as well as surviving spouses and eligible dependents.

Taxpayer represents that the allocation made on behalf of each eligible retiree in the Plan will, in general, constitute the maximum reimbursement amount available for the retiree under the Plan, subject to reduction for administrative costs and fees. The retiree will be able to use the full amount allocated to his or her account under the Plan (subject to reduction for costs and fees). The Plan will only reimburse expenses for medical care as defined in §213(d) of the Code including out–of-pocket medical expenses and premiums for medical insurance. Only those medical expenses incurred by a retiree, or such person's spouse, dependents and children who have not attained age 27 as of the end of the taxable year, will be reimbursed. The Plan will reimburse premiums for insurance covering medical care expenses. Any unused portion in an account under the Plan at the end of a calendar year will be carried forward and may be used in a subsequent year until the account is fully spent. No benefits other than reimbursements of medical expenses will be available under the Plan either as cash or other nontaxable or taxable benefits. The Plan will reimburse medical expenses only to the extent such expenses have not been reimbursed from any other source. Each medical expense submitted for reimbursement under the Plan will be substantiated before reimbursement is made. Following the death of a retiree, unused amounts will continue to be available for any remaining beneficiaries of the retiree until the account is fully spent. If any amount remains in the account following the death of the retiree and eligible beneficiaries, such amount will be forfeited.

Section 61(a)(1) of the Code and §1.61-21(a)(3) of the Income Tax Regulations (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 provides that gross income of an employee does not include employer provided coverage under an accident or health plan. Section 1.106-1 of the regulations provides that the gross income of an employee does not include contributions which the employee's 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 or the employee's spouse or dependents (as defined in §152). 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, §106 applies only to the portion of the contributions allocable to accident or health benefits.

Section 105(a) provides that, except as otherwise provided in §105, amounts received by an employee through accident or health insurance for personal injuries or sickness shall be included in gross income to the extent such amounts (1) are attributable to contributions by the employer which were not includible in the gross income of the employee, or (2) are paid by the employer.

Section 105(b) states that except in the case of amounts attributable to (and not in excess of) deductions allowed under §213 (relating to medical expenses) for any prior taxable year, gross income does not include amounts referred to in subsection (a) if such amounts are paid, directly or indirectly, to the taxpayer to reimburse the taxpayer for expenses incurred by the taxpayer for the medical care (as defined in § 213(d)) of the taxpayer or the taxpayer's spouse or dependents (as defined in §152, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B)) and any child (as defined in §152(f)(1)) who has not attained age 27 as of the end of the taxable year. Section 1.105-2 of the regulations provides that only amounts that are paid specifically to reimburse the taxpayer for expenses incurred by the taxpayer for the prescribed medical care are excludable from gross income. Thus, §105(b) does not apply to amounts that the taxpayer would be entitled to receive irrespective of whether or not the taxpayer incurs expenses for medical care.

In Rev. Rul. 2002-41, 2002-2 C.B. 75, an employer sponsors a health reimbursement arrangement (HRA) that is paid for solely by the employer and not through salary reduction contributions. The HRA reimburses substantiated medical care expenses (as defined in § 213(d)) of participating employees and their spouses and dependents (as defined in §152) up to a maximum annual reimbursement amount. Unused amounts from one coverage period are carried forward to subsequent coverage periods. Participating employees have no right to receive cash or any other benefit in lieu of medical expense reimbursements. In Situation 2 of Rev. Rul. 2002-41, the maximum

reimbursement amount under the HRA that is not applied to reimburse medical care expenses before an employee retires or otherwise terminates employment continues to be available after retirement or termination for any medical care expense under § 213(d) incurred by the former employee or the former employee's spouse and dependents. The ruling concludes that coverage and reimbursements made under the HRA are excludable from the gross income of participating employees under §§106 and 105.

Notice 2002-45, 2002-2 C.B. 93, provides that an HRA is an arrangement that: (1) is paid for solely by the employer and not pursuant to salary reduction; (2) reimburses the employee for medical care expenses (as defined in § 213(d)) incurred by the employee and the employee's spouse and dependents (as defined in §152); and (3) provides that any unused portion of the maximum dollar amount available during the coverage period is carried forward to subsequent periods. Notice 2002-45 also provides that benefits under an HRA must be limited to reimbursements of § 213(d) expenses and that all such expense reimbursements must be substantiated to be excludable under §105. Notice 2002-45 further provides that medical care expense reimbursements under an HRA are excludable under §105(b) if the reimbursements are provided to the following individuals: current and former employees (including retired employees), their spouses and dependents (as defined in §152 as modified by the last sentence of §105(b)), and the spouses and dependents of deceased employees.

Based on the information submitted and representations made, we conclude as follows: contributions to and coverage under the Plan and payments and reimbursements of medical expenses made by the Plan will be excludable under §§106 and 105(b) of the Code from the gross income of retirees, their current and surviving spouses, eligible dependents and children who have not attained age 27 as of the end of the taxable year.

No opinion is expressed concerning whether the Plan satisfies the nondiscrimination requirements of §105(h) of the Code and §1.105-11 of the regulations. No opinion is expressed concerning the Federal tax consequences of the Plan under any other provision of the Code other than those specifically stated herein. In addition, no opinion is expressed as to the application of any issue addressed in Notice 2013-54, 2013-40 I.R.B. 287, to the facts of this ruling request.

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.

Sincerely,

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