**Internal Revenue Service**

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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
Date of Communication: Not Applicable

Person To Contact:

Telephone Number:

Refer Reply To:
CC:TEGE:EB:HW
PLR-115397-17

Date:
November 3, 2017

Legend

Taxpayer =

Year =

Retirement Plan =

Date 1 =

Year 2 =

Health Benefit Plan =

Retiree HRA =

Dear :

This letter responds to your April 28, 2017 ruling request, submitted by your representatives, as supplemented by correspondence dated August 28, 2017, October 6, 2017 and October 16, 2017, requesting rulings concerning the tax consequences of a proposed transaction under sections 105 and 401(h) of the Internal Revenue Code (the "Code") and their accompanying regulations.

The following facts and representations are submitted under penalties of perjury in support of your request:

Taxpayer is a full-service bank with offices across the United States, providing corporate, commercial, retail banking, and wealth management solutions. Taxpayer was formed in Year 1 by a corporate integration.

Taxpayer maintained the Retirement Plan, a defined benefit plan qualified under section 401(a) of the Code. The Retirement Plan is a successor plan to a previous retirement plan, and in connection with mergers and purchases involving the formation of the Taxpayer, it was renamed multiple times. The name of the Retirement Plan was changed to its current name effective Date 1.

The Retirement Plan was amended to add a retiree health account described in section 401(h) before the formation of Taxpayer. No employee contributions were required to be made to the Retirement Plan 401(h) account. Taxpayer attests that the Retirement Plan subsequently received a favorable determination letter from the Internal Revenue Service. Taxpayer further represents that the section 401(h) account was not funded, directly or indirectly, by a section 420 transfer and that neither the Retirement Plan nor any of its predecessor plans allowed for or permitted employee contributions.

Until the beginning of Year 2, all eligible active employees and retirees (and eligible dependents) could participate in the Health Benefit Plan. The Health Benefit Plan eligibility provisions were changed beginning Year 2 to only provide coverage for active employees and certain retirees, generally up to age 65. Non-insured retiree health benefits under the Health Benefit Plan are currently being paid from a Voluntary Employee Beneficiary Association (VEBA) trust. Taxpayer represents that it has been projected that the VEBA trust assets will be depleted within five months of the ruling request. Upon exhaustion of the VEBA trust, Taxpayer represents that a portion of any monthly premium for coverage of or payment of claims on behalf of participating retirees (and their covered dependents) under the Health Benefit Plan will be paid through the section 401(h) account of the Retirement Plan to the extent that the participants qualify as “retired employees, their spouses, or their dependents” under section 401(h) of the Code and § 1.401-14 of the Income Tax Regulations (“Eligible Individuals”).

Taxpayer adopted a retiree-only Health Reimbursement Account Plan (“Retiree HRA”), effective the beginning of Year 2. The Retiree HRA, established under section 105 of the Code, reimburses former employees (and certain of their dependents) (the “Retirees and their dependents”), who meet the Retiree HRA’s eligibility criteria, for premiums paid for Medicare or individual health insurance coverage and for any other expense for medical care as defined in section 213(d) of the Code. Retirees and their dependents will be credited with an amount under the Retiree HRA if they enroll in at least one individual medical, dental, or vision policy offered through a private retiree health exchange chosen by Taxpayer.

Taxpayer proposes to use the Retirement Plan’s section 401(h) account to reimburse the eligible expenses of Retiree HRA participants who qualify as Eligible Individuals.

Taxpayer represents that it will amend the Retirement Plan to permit the Retirement Plan's section 401(h) account to provide for distributions to or on behalf of Retirees and their dependents for expenses under the Retiree HRA. Taxpayer represents that no portion of the section 401(h) account will be used to reimburse the expenses of anyone who does not qualify as an Eligible Individual under the Retirement Plan.

Taxpayer further represents that:

(1) The Retiree HRA is a health reimbursement arrangement ("HRA"), as defined in Notice 2002-45, 2002-2 C.B. 93;

(2) The Retiree HRA will, at all times following its implementation as described in the ruling request, remain unfunded, and no retired employee who is an Eligible Individual will be entitled to any amount under the Retiree HRA in excess of the amount required to be reimbursed under the section 401(h) account;

(3) Prior to the satisfaction of all liabilities to provide retiree health benefits, the funds in the section 401(h) account shall not be used or diverted to any purpose other than providing such benefits;

(4) Until reimbursements are made under the Retiree HRA, all Retiree HRA related funds will remain in the section 401(h) account and, in the event of either the Retirement Plan or section 401(h) account termination, all such amounts remaining in the section 401(h) account after satisfaction of all liabilities to provide medical benefits will be subject to section 401(h) (including section 401(h)(5)) and the excise tax on reversions pursuant to section 4980;

(5) Taxpayer does not have a contractual obligation to fund the Health Benefit Plan or the Retiree HRA Plan and may amend or terminate its retiree health plans at any time;

(6) Taxpayer will audit the reimbursements made by the Retiree HRA annually to ensure that only Eligible Individuals' expenses are reimbursed from the Retirement Plan's 401(h) account; and

(7) Taxpayer will amend the Retirement Plan to prohibit discrimination in favor of officers, shareholders, supervisory employees or highly compensated employees in accordance with § 1.401-14(b)(2) of the Income Tax Regulations.

**RULINGS REQUESTED**

Taxpayer requests rulings that:

(1) Use of the Retirement Plan's section 401(h) account to reimburse premiums for Medicare or other health insurance coverage and other Code section 213(d) medical expenses of Retiree HRA participants who are "retired employees, their spouses, or their dependents" under section 401(h) and § 1.401-14 of the Income Tax Regulations will not violate section 401(h) of the Code or § 1.401-14 of the Income Tax Regulations or otherwise cause the Retirement Plan to lose its tax-qualified status under section 401(a) of the Code; and

(2) Reimbursements in accordance with the terms of the Retiree HRA of eligible health plan premiums and section 213(d) medical expenses of Eligible Individuals that are made from the section 401(h) account are excludable from the gross income of those individuals under section 105.

**LAW**

Section 61(a)(1) of the Code and § 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 105(a) of the Code provides that, except as otherwise provided in this section, 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) provides that, except in the case of amounts attributable to (and not in excess of) deductions allowed under section 213 (relating to medical, etc., 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 him for the medical care (as defined in section 213(d)) of the taxpayer, his spouse, his dependents (as defined in section 152, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof), and any child (as defined in section 152(f)(1)) of the taxpayer who as of the end of the taxable year has not attained age 27. Any child to whom section 152(e) applies shall be treated as a dependent of both parents for purposes of this subsection.

Section 106 provides that gross income does not include contributions by the employer to accident or health plans for compensation (through insurance or otherwise) to his employees for personal injuries or sickness. Section 1.106-1 of the Income Tax 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) for personal injuries or sickness to the employee or the employee's spouse or dependents (as defined in section 152 of the Code, determined without regard to subsections (b)(1), (b)(2), and (d)(1)(B) thereof),

and any child (as defined in section 152(f)(1)) of the taxpayer who as of the end of the taxable year has not attained age 27.

Section 401(a) describes requirements for a qualified trust that is created or organized in the United States and forms part of a pension plan of an employer that is for the exclusive benefit of the employer's employees or their beneficiaries. Section 501(a) provides in pertinent part that an organization described in section 401(a) is generally exempt from income tax.

In pertinent part, section 401(h) provides that, under regulations prescribed by the Secretary, and subject to the provisions of section 420, a pension or annuity plan may provide for the payment of benefits for sickness, accident, hospitalization, and medical expenses of retired employees, their spouses and their dependents, but only if --

(1) such benefits are subordinate to the retirement benefits provided by the plan,

(2) a separate account is established and maintained for such benefits,

(3) the employer’s contributions to such separate account are reasonable and ascertainable,

(4) it is impossible, at any time prior to the satisfaction of all liabilities under the plan to provide such benefits, for any part of the corpus or income of such separate account to be (within the taxable year or thereafter) used for, or diverted to, any purpose other than the providing of such benefits, and

(5) notwithstanding the provisions of subsection (a)(2), upon the satisfaction of all liabilities under the plan to provide such benefits, any amount remaining in such separate account must, under the terms of the plan, be returned to the employer. Section 1.401-14(a) of the Income Tax Regulations provides that, under section 401(h) of the Code, a qualified pension or annuity plan may make provision for the payment of sickness, accident, hospitalization, and medical expenses for retired employees, their spouses, and their dependents. The term “medical benefits described in section 401(h)” is used in this section to describe such payments.

Section 1.401-14(b)(1) of the Income Tax Regulations provides that, under section 401(h) of the Code, a qualified pension or annuity plan may provide for the payment of medical benefits described in section 401(h) only for retired employees, their spouses, or their dependents. To be “retired” for purposes of eligibility to receive medical benefits described in section 401(h), an employee must be eligible to receive retirement benefits provided under the pension plan, or else be retired by an employer providing such medical benefits by reason of permanent disability. For purposes of the preceding sentence, an employee is not considered to be eligible to receive retirement benefits

provided under the plan if he is still employed by the employer and a separation from employment is a condition to receiving the retirement benefits.

In Rev. Rul. 2002-41, 2002-2 C.B. 75, an employer sponsors an 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 section 213(d)) of participating employees and their spouses and dependents (as defined in section 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 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 sections 106 and 105.

Notice 2002-45, 2002-2 C.B. 93, describes the tax treatment of HRAs. The notice explains that a tax-favored HRA is an arrangement that (1) is paid for solely by the employer and not pursuant to a salary reduction election or otherwise under a section 125 cafeteria plan; (2) reimburses the employee for medical care expenses (as defined in section 213(d)) incurred by the employee or by the employee's spouse or dependents; and (3) provides reimbursements up to a maximum dollar amount with any unused portion of that amount at the end of the coverage period carried forward to subsequent coverage periods.

**CONCLUSION**

Based on the facts and representations provided by the Taxpayer:

(1) Use of the Retirement Plan's section 401(h) account to reimburse premiums for Medicare or other health insurance coverage and other Code section 213(d) medical expenses of Retiree HRA participants who are "retired employees, their spouses, or their dependents" under section 401(h) and § 1.401-14 of the Income Tax Regulations will not violate section 401(h) of the Code or § 1.401-14 of the Income Tax Regulations or otherwise cause the Retirement Plan to lose it its tax-qualified status under section 401(a) of the Code.

(2) Reimbursements of health plan premiums and section 213(d) medical expenses to Eligible Individuals from the Retirement Plan's section 401(h) account, and in accordance with the terms of the Retiree HRA, are excludable from the gross income of those individuals under section 105.

These rulings are based on the assumption that Taxpayer's Retirement Plan is qualified under section 401(a).

The rulings contained in this letter are based upon information and representations submitted by Taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party, as specified in Rev. Proc. 2017-1, 2017-1 I.R.B. 1, § 7.01(15)(b).

This office has not verified any of the material submitted in support of the request for ruling, and such material 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. 2017-1, § 11.05.

Except as expressly provided above, no opinion is expressed or implied concerning the federal income tax consequences of any other aspects of any transaction or item of income described in this letter ruling.

This letter ruling is directed only to the taxpayer who requested it. Code Section 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, a copy of this letter is being sent to your authorized representatives.

If you have any questions concerning this letter, please contact Karen Levin at (202) 317-5500.

Sincerely,

/s/

Kevin Knopf
Senior Technician Reviewer
Health & Welfare Branch
Office of Associate Chief Counsel
Tax Exempt & Government Entities

cc: