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Department of the Treasury
Washington, DC 20224

Third Party Communication: None
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Person To Contact:
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Telephone Number:

Refer Reply To:
CC:ITA:4
PLR-115083-18
Date: October 29, 2018

TY:

Legend:
Taxpayer =
Parent =
Related Party 1 =
Related Party 2 =
x =

Dear :

This ruling refers to a request for a private letter ruling dated May 2, 2018, concerning whether payments to Taxpayer by Related Party 1 and Related Party 2 as reimbursement of a branded prescription drug fee paid by Taxpayer are includible in Taxpayer's gross income.

FACTS

Related Party 1 is a foreign corporation and the common parent of Related Party 2, a foreign corporation, and Parent, a U.S. corporation. Parent is the common parent of an affiliated group of corporations, which includes Parent's United States subsidiary, Taxpayer (Related Party 1, Related Party 2, Parent, and Taxpayer are collectively referred to as "the Group"). The Group develops, manufactures, and distributes prescription drugs and other medical care products. Related Party 1 and Related Party 2 are the intellectual property holders of the prescription drugs, which they manufacture. Related Party 1 and Related Party 2 contract with Taxpayer to distribute the prescription drugs in the United States. Taxpayer is a limited risk distributor whose operating profit margin approximates x percent of sales of the prescription drugs. All remaining profits accrue to Related Party 1 and Related Party 2.

The Patient Protection and Affordable Care Act, Public Law 111-148 (124 Stat. 119 (2010)), as amended by section 1404 of the Health Care and Education Reconciliation Act of 2010, Public Law 111-152 (124 Stat. 1029 (2010)) (collectively the ACA) imposes a branded prescription drug (BPD) fee on entities that manufacture or import branded prescription drugs for sale to specified government programs. ACA § 9008(d)(2) and Treas. Reg. § 51.2(e) generally require controlled groups to be treated as a single entity for purposes of the BPD fee. Treas. Reg. § 51.2(f) requires controlled groups to select a designated entity to act for the controlled group by (1) filing reports relating to the BPD fee, and (2) paying the BPD fee to the U. S. Treasury. ACA § 9008(d)(3) and Treas. Reg. § 51.8(d) provide that all members of a controlled group are jointly and severally liable for the BPD fee. Taxpayer represents that Taxpayer, Parent, Related Party 1, and Related Party 2 are jointly and severally liable for the BPD fee on sales of branded prescription drugs that are manufactured by Related Party 1 and Related Party 2 and distributed by Taxpayer, because they are part of a controlled group within the meaning of ACA § 9008(d)(2) and Treas. Reg. § 51.2(e).

Although Parent is the named designated entity for the payment of the BPD fee, the Labeler Code of the National Drug Code identifies Taxpayer as the manufacturer or importer of the branded prescription drugs. Taxpayer remits the payment of the fee to the U.S. Treasury on behalf of the Group. Related Party 1 and Related Party 2 reimburse Taxpayer for this fee, according to their contracts with Taxpayer.

Taxpayer has requested a ruling that the payments to Taxpayer from Related Party 1 and Related Party 2 as reimbursement of the BPD fee are not includible in Taxpayer's gross income.

LAW AND ANALYSIS

Section 61 generally provides that gross income means all income from whatever source derived. The term "income" is broadly defined as "instances of undeniable accessions to wealth, clearly realized, and over which the taxpayers have complete dominion." Commissioner v. Glenshaw Glass Co., 348 U.S. 426, 431 (1955).

It is well-established that the payment of the expenses of a taxpayer by another is includible in the taxpayer's gross income. *See, e.g.*, Old Colony Trust v. Commissioner, 279 U.S. 716 (1929). In contrast, a taxpayer does not have gross income when it pays the expenses of another person and the person reimburses the taxpayer for the payments. Expenditures of this nature are analogous to loans in which the taxpayer is the lender and the party for whom the expense is paid (and who reimburses the taxpayer for paying the expense) is a borrower. *See, e.g.*, Rev. Rul. 67-407, 1967-2 C.B. 59. A corollary to these principles is that, when a taxpayer pays the expenses of another person primarily to advance the business interests of the other person, the reimbursements are not includible in the gross income of the taxpayer, notwithstanding

any incidental or indirect economic benefit to the taxpayer. *See, e.g.*, United States v. Gotcher, 401 F.2d 118 (5th Cir. 1968)(expenses paid for auto dealer by European manufacturer for trip to Germany to tour facilities as required by manufacturer held not includible in auto dealer's gross income because the costs for the taxpayer-dealer's trip were incurred primarily for the payor-manufacturer's benefit).

Covered entities must pay a branded prescription drug fee under § 9008 of the ACA. Section 9008(d)(1) defines a covered entity as any manufacturer or importer with gross receipts from branded prescription drug sales. Section 9008(e) defines branded prescription drug sales as sales of branded prescription drugs to any specified government program or pursuant to coverage under such program. These programs are the Medicare Part B program, the Medicare Part D program, the Medicaid program, any program under which branded prescription drugs are procured by the Department of Veterans Affairs, any program under which branded prescription drugs are procured by the Department of Defense, and the TRICARE retail pharmacy program.

Section 51.2(e) of the Branded Prescription Drug Fee Regulations defines a covered entity, in general, as any manufacturer or importer with gross receipts from branded prescription drug sales, including a single-person covered entity or a controlled group.

Section 51.2(i) defines a manufacturer or importer as the person identified in the Labeler Code of the National Drug Code for the branded prescription drug.

Section 51.2(e)(3) defines a controlled group as a group of two or more persons, including at least one person that is a covered entity, that is treated as a single employer under section 52(a), 52(b), 414(m), or 414(o).

Section 51.8(d) states: "In the case of a controlled group that is liable for the fee, all members of the controlled group are jointly and severally liable for the fee. Accordingly, if a controlled group's fee is not paid, the IRS will separately assess each member of the group for the full amount of the controlled group's fee."

Section 51.2(e)(4)(i) provides that a foreign entity subject to tax under section 881 is included within a group under section 52(a) or 52(b).

Section 51.2(e)(4)(ii) provides that a person is treated as being a member of a controlled group if it is a member of the group at the end of the day on December 31st of the sales year.

The branded prescription drug fee is treated as a nondeductible tax under § 275(a)(6) of the Code. *See* ACA § 9008(f)(2) and Treas. Reg. § 51.9(d).

Joint and Several Liability

It is clear from the law cited above and Taxpayer's representations that Taxpayer, Parent, Related Party 1, and Related Party 2 are jointly and severally liable for the branded prescription drug fee that Taxpayer remits on behalf of the Group.

Gross Income

Although Taxpayer arguably receives an accession to wealth when Related Party 1 and Related Party 2 reimburse it for paying the BPD fee, all three parties are jointly and severally liable for 100% of the fee. The IRS has the right to assess and collect the full amount of the fee against any member (or combination of members) of the Group; however, it does not have the right to assess and collect more than 100% of the fee.

Here, the parties have agreed, according to their distribution contracts, that Related Party 1 and Related Party 2 will bear the economic burden of 100% of the BPD fee, because they are the IP holders of the branded prescription drugs and they are the primary economic beneficiaries of the sales of these drugs. Taxpayer receives 100% of the BPD fee from them and pays it directly to the U.S. Treasury in a pass-through transaction. Taxpayer does not have "complete dominion" over these funds, nor does it receive a tax benefit in the form of a deduction from making this payment, because § 275(a)(6) blocks such a deduction.

When viewed in the context of the Group members' respective businesses and contractual relationships with each other, Taxpayer's actions in remitting the BPD fee most closely resemble the actions of a conduit that is merely receiving and paying the liability on behalf of other members of the Group, who are the primary economic beneficiaries of the profits from the branded prescription drug sales. *See, e.g.*, S*even-Up Co. v. Commissioner,* 14 T.C. 965 (1950)(payments received from franchisee bottling companies for a national advertising campaign not includible in franchisor's gross income because franchisor was obliged to spend the funds on the advertising campaign); Rev. Rul. 84-128, 1984-2 C.B. 123 (1984) (subsidiary's *pro rata* payment of shared administrative expenses to parent not includible in parent's gross income).[1]

[1] This situation is distinguishable from that in Rev. Rul. 2013-27, 2013-51 I.R.B. 676, in which an insurance company collected extra amounts from its policy holders to pay a fee imposed on health insurers under the ACA. In that situation, the fee was imposed on the insurer, not jointly on the insurer and its policyholders. The revenue ruling concludes that the fee, whether or not separately stated on the insurer's invoices to its policyholders, was not distinguishable from other costs of doing business that are traditionally passed on to a business's customers. Accordingly, the insurer was not entitled to exclude from gross income the amounts collected from its policyholders for the fee.

CONCLUSION

Based on the information submitted and representations made, we conclude that the payments to Taxpayer by Related Party 1 and Related Party 2 as reimbursement of the branded prescription drug fee are not includible in Taxpayer's gross income under § 61.[2]

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 rulings, it is subject to verification on examination.

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. 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 two of your authorized representatives.

A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, taxpayers filing their returns electronically may satisfy this requirement by attaching a statement to their return that provides the date and control number of the letter ruling.

Sincerely,

Angella L. Warren
Chief, Branch 4
Office of Associate Chief Counsel
(Income Tax & Accounting)

Enclosure

[2] We express no opinion as to whether our conclusion might be different if Taxpayer or another U.S. taxpayer-member of the controlled group were entitled to a deduction for paying the BPD fee, whether the payment was made by direct remittance or by reimbursing a related party for remitting the payment. Because § 275(a)(6) prohibits such a deduction for U.S. taxpayers, we need not consider the effect of such a deduction on our analysis.