Internal Revenue Service

memorandum

FREV-122183-98
CC:EBEO:Br4.JLaufer

date: MAY 14 1999

to: Director, Exempt Organizations Division (OP:E:E0)

from: Assistant Chief Counsel, Employee Benefits and Exempt Organizations (CC:EBEO)

subject: [redacted]
Agreement for Certain Collectively Bargained Welfare Benefits

This responds to your memorandum of December 7, 1998, requesting our assistance with respect to the above-referenced case. In particular, Taxpayer wants to apply excess assets in the Trust to provide welfare benefits to union employees. We have the following comments:

(1) Section 419A(c)(2)

Taxpayer asks that we address the issue of whether the proposed use of the Excess Assets violates the "accumulated reserve" requirement of Code section 419A(c)(2).

Section 419(a) and Section 419A of the Code, enacted as part of the Deficit Reduction Act of 1984 (DEFRA), limit the deductibility of employer contributions to a welfare benefit fund. Pursuant to section 419, the employer's deduction for contributions to a welfare benefit fund for a taxable year is generally limited to an amount necessary to provide benefits for that year (qualified direct cost), plus an addition to a "qualified asset account," up to an "account limit" as set forth in section 419A, minus the fund's after-tax income. A fund's qualified asset account consists of any assets set aside to provide for the payment of (1) disability benefits, (2) medical benefits, (3) supplemental unemployment compensation benefits or severance pay benefits, or (4) life insurance benefits. Pursuant to section 419A(c)(1), the account limit for any qualified asset account for any taxable year is the amount reasonably and actuarially necessary to fund claims incurred but unpaid (as of the close of the taxable year), and administrative costs with respect to those claims. Section 419A(c)(2) provides that the account limit for any taxable year may also include a reserve funded over the working lives of the covered employees and actuarially determined on a level

basis as necessary for post-retirement medical benefits or life insurance benefits to be provided to covered employees. Thus, section 419A(c)(2) provides an exception to the general rule restricting an employer's deduction for contributions to a welfare benefit fund to those contributions reasonably and actuarially necessary to satisfy expenses incurred in the year for which the deduction is taken.

Another exception to that general rule is found in section 419A(f)(5)(A) of the Code, which provides that no account limit applies in the case of any qualified asset account under a separate welfare benefit fund under a collective bargaining agreement.[1] In this case, section 419A(f)(5)(A) and regulation section 1.419A-2T relieved [redacted] from the otherwise applicable "account limit" limitation on its deduction for contributions to the Trust. As section 419A(c)(2) addresses what may be included an "account limit" where that limit applies, it is not relevant in this case. Accordingly, we suggest that you indicate to Taxpayer that you will not rule with respect to this issue.

(2) Section 4976

We agree with EO's determination that the proposed use of excess assets to provide welfare benefits for active union employees will not constitute a prohibited reversion under section 4976(b). The section 419A(f)(5)(A) exception enabled Taxpayer to fully deduct its contributions under section 419. Consequently, any application of Trust funds consistent with a section 419A(5)(A) purpose (i.e., providing

---

[1] As originally enacted, section 419A(f)(5)(A) provided that the Secretary by regulations shall provide for special account limits in the case of any qualified asset account under a welfare benefit fund established under a collective bargaining agreement. Section 1.419A-2T, Q&A-1 states that "neither contributions to nor reserves of such a collectively bargained welfare benefit fund shall be treated as exceeding the otherwise applicable limits of section 419(b), 419A(b), or 512(a)(3)(E) until the earlier of [two dates that are keyed to the adoption of final regulations concerning those limits]." The Service has not published any further regulations on this issue. A literal reading of section 419A(f)(5) suggests relief only from the qualified asset account limits of section 419A(b). However, the relief set forth in Q&A-1 of section 1.419A-2T is also effective with respect to contributions to a collectively-bargained fund to provide non-reservable benefits (that is, benefits other than disability, medical, SUB or severence pay, or life insurance).

welfare benefits pursuant to a collective bargaining agreement) will not give rise to income under the tax benefit rule, and does not constitute a prohibited reversion to the benefit of the employer under section 4976(b)(1)(C).

We have informally discussed our conclusion here with Jim Holland of EP. Jim suggested that any ruling on this issue should include a caveat that our conclusion that there is no prohibited reversion under section 4976(b)(1)(C) is limited to the application of the Trust assets to pay benefits that are provided pursuant to a collective bargaining agreement. At this time, we do not want to imply that we would reach the same conclusion if the welfare benefits provided to active employees were not provided pursuant to a collective bargaining agreement.

[redacted]

[redacted]
FREV-122183-98

[redacted]

[redacted]

(4) Retiree Contributions

Retirees contribute to the Trust, and so a portion of the assets in the Trust consists of participant contributions. We are assuming that no retiree contributions will be applied to provide benefits for other groups of retirees or for active employees, and you should confirm that with Taxpayer. In addition, because the fact of retiree contributions may raise additional issues under Title 1 of ERISA and under federal labor law, you may want to indicate in a footnote to the PLR that you are not addressing those issues.

If you have any questions regarding this memorandum, please call Janet Laufer at 622-6060.

MARY OPPENHEIMER
Assistant Chief Counsel

By: _____
Mark Schwimmer
Chief, Branch 4
Office of the Associate
Chief Counsel
(Employee Benefits and Exempt
Organizations)