

**Internal Revenue Service**

Department of the Treasury  
Washington, DC 20224

Number: **201222018**  
Release Date: 6/1/2012

Third Party Communication: None  
Date of Communication: Not Applicable  
Person To Contact:

Index Number: 115.00-00

, ID No.  
Telephone Number:

Refer Reply To:  
CC:TEGE:EOEG:EO  
PLR-136549-11  
Date:  
February 28, 2012

System:

Board:

Association:

Program:

Trust:

Agreement:

State:

Dear :

This letter responds to a letter from your authorized representatives dated August 18, 2011, as well as subsequent correspondence, submitted on behalf of the Trust, requesting a ruling that the Trust's income is excludable from gross income under § 115 of the Internal Revenue Code. The Trust represents the facts as follows.

**FACTS**

The System is an administrative and investment system created by State law whereby municipal corporations and certain other entities of the State may provide retirement and other benefits to their employees.

The System is governed by a board of trustees created by State law. The Board is composed of elected or appointed officers and elected employees of municipal corporations among the System's membership. Board members may not serve more than 3 consecutive terms.

The Association has received a favorable § 115 ruling letter. The Association is organized as a nonprofit corporation under State law to provide educational, employee benefits, and technical consulting services to municipalities. It is governed by a board of directors, composed of elected and appointed officials.

The Program is a self-insured fund created under State law, administered by the Association, and overseen by the Board. The Program offers various benefit plans and group policies that participating employers may provide their eligible employees. The health and welfare benefits provided by the Program include health, life, accidental death and dismemberment, short-term disability, and dental insurance and other benefits.

Administered by the Association, the Trust, pursuant to State law, pools the contributions of certain governmental employers in order to administer the Trust, to provide health and welfare benefits under the Program, and to provide for risk-sharing among the participating employers. Some of these benefits are self-funded, while others are provided through third-party insurers.

Only an employer as defined by State law (provided that the employer is a State agency, political subdivision, or an entity whose income is excluded under § 115) is eligible to participate in the Trust. Eligible employers may become participating employers by authorizing participation in the Trust by resolution or ordinance, and by executing participation agreements.

The Agreement authorizes the Board to invest and reinvest Trust assets and to pay benefits from those assets (except for benefits payable under a group policy). The Board may delegate this benefit payment authority to the program administrator or its duly authorized representative. The administrator, currently the Association, may be removed and replaced by the Board with or without cause.

The Trust is held for the exclusive benefit of employees of participating employers and their dependents. Trust assets shall be used solely to provide health and welfare benefits to participating employers' eligible employees and their eligible dependents, and to pay reasonable Trust expenses.

The Board may amend the Agreement at any time and in any manner permitted by State law and not inconsistent with § 115. The Board reserves the right at any time

to terminate the Trust. Any monies or other assets remaining after payment of liabilities incurred before termination (self-funded health and welfare benefits and administrative expenses) as well as reasonable and necessary expenses incurred in the termination, shall be distributed on a pro rata basis to participating employers. In no event shall Trust assets be distributed to an entity that is not a state, a political subdivision of a state, or an entity whose income is excluded from gross income under § 115.

An Employer may dissolve the Trust with respect to that Employer. After paying, or making reasonable provision to pay, all liabilities of the Trust with respect to the terminating Employer, the Board will distribute the remaining Trust property allocable to that Employer. In no event will Trust assets be transferred to an entity that is not a political subdivision of the State or an entity whose income is excluded from gross income under § 115.

#### LAW AND ANALYSIS

Section 115(1) provides that gross income does not include income derived from any public utility or the exercise of any essential government function and accruing to a state or any political subdivision thereof.

In Rev. Rul. 77-261, 1977-2 C.B. 45, income from an investment fund, established under a written declaration of trust by a state, for the temporary investment of cash balances of the state and its participating political subdivisions, was excludable from gross income for federal income tax purposes under § 115(1). The ruling indicated that the statutory exclusion was 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 a corporation or other entity engaged in the operation of a public utility or the performance of some governmental function that accrued to either a state or municipality. The ruling points out 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 which are within the ambit of a sovereign properly to conduct. In addition, pursuant to § 6012(a)(2) and the underlying regulations, the investment fund, being classified as a corporation that is subject to taxation under subtitle A of the Code, was required to file a federal income tax return each year.

In Rev. Rul. 90-74, 1990-2 C.B. 34, the income of an organization formed, funded, and operated by political subdivisions to pool various risks arising from their obligations regarding public liability, workers' compensation, or employees' health is excludable from gross income under § 115. In this ruling, private interests did not

materially participate in the organization, nor did they benefit more than incidentally from the organization.

The Trust provides health and welfare benefits to employees of the participating employers and their dependents, as well as risk-sharing among those employers. Providing health and welfare benefits to public employees and risk-sharing among governmental employers constitutes the performance of essential government functions. Based upon Rev. Rul. 90-74 and Rev. Rul. 77-261, the Trust performs an essential governmental function within the meaning of § 115(1).

The funding and provision of health and welfare benefits through the Trust satisfies the obligation of the participating employers to provide those benefits; thus, the income of the Trust accrues to the participating employers, all of which are agencies or political subdivisions of the State, or entities the income of which is excluded from gross income under § 115. No private interests participate in, or benefit from, the operation of the Trust other than as providers of goods or services. The benefit to public employees is incidental to the public benefit. Upon dissolution, no Trust assets will be distributed to an entity other than a state, a political subdivision, or a § 115 entity. See Rev. Rul. 90-74.

#### RULING

Based solely on the facts and representations submitted by the Trust, we conclude that the income of the Trust is derived from the exercise of an essential governmental function and will accrue to a state or a political subdivision thereof for purposes of § 115(1). Consequently, we rule that the Trust's income is excludable from gross income under § 115(1).

Except for the specific ruling above, we express or imply no opinion concerning the federal tax consequences of the facts of this case under any other provision of the Code. 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 accident or health contributions or benefits.

Under a power of attorney on file with this office, we are sending a copy of this letter to your authorized representative.

This ruling is directed only to the taxpayer who requested it. According to § 6110(k)(3), this ruling may not be used or cited as precedent.

Sincerely,

SYLVIA HUNT  
Assistant Branch Chief  
Exempt Organizations  
Office of Division Counsel /  
Associate Chief Counsel  
(Tax Exempt & Government Entities)

enclosures: copy for § 6110 purposes

cc: