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Internal Revenue Service

National Office Technical Advice Memorandum

District Director

Chief, EP/EO Division

Taxpayer's Name:
Taxpayer's Address:

Taxpayer's Identification Number:

Years Involved: 9012 forward

Issues

(1) Does income on an amount set aside as an existing reserve for post-retirement medical or life insurance benefits under section 512(a)(3)(E)(ii) of the Internal Revenue Code act to increase the existing reserve? Do claims for benefits act to decrease the existing reserve?

(2) May the existing reserve for post-retirement medical or life insurance benefits under Code section 512(a)(3)(E)(ii) be used to provide medical benefits for active employees? Would payments for active employee medical benefits affect the characterization of the reserve as an "existing reserve"?

(3)(a) Should all income other than income from an existing reserve be included in computing the unrelated business taxable income ("UBTI") of a voluntary employees' beneficiary association ("VEBA") that is exempt from tax under Code section 501(c)(9), if one account is maintained for the VEBA that consists of four separate claims reserves that are accounted for separately?

(3)(b) Is income from tax-exempt bonds maintained in one of the claims reserves considered "exempt function income"?

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(4) How are amounts set aside in existing reserves and additional reserves for post-retirement medical or life insurance benefits taken into account when computing the UBTI of a VEBA?

(5) What effect, if any, do the filings of separate Forms 990 for each claims reserve have on the computations of UBTI for the years involved? Do such separate filings create separate VEBA's?

Facts

(the "Company") established the (the "Plan") on August 1, 1955. The Plan was funded through a corporation (rather than a trust) that has been recognized as exempt from federal income tax as a VEBA under section 501(c)(9) of the Internal Revenue Code. In 1978, the Company fully funded the accrued liability for the post-retirement medical and dental benefits. As of July 18, 1984, the Company had set aside a total amount of assets in the VEBA equal to $18,031,370 as an existing reserve for post-retirement medical or life insurance benefits under Code section 512(a)(3)(E)(ii). This reserve will hereafter be referred to as the "existing reserve". As of July 18, 1984, the VEBA also contained employer contributions in the amount of $1,880,741 that were not deductible for the Company's taxable year that contained July 18, 1984, or for any prior taxable year. The nondeductible amount was not treated as part of the existing reserve, in accordance with section 1.512(a)-5T, Q&A-4(a) of the regulations.

The existing reserve was held in a bank account from which all claims for post-retirement medical and life insurance benefits would be paid. Until 1991, the VEBA also maintained in the same bank account (under separate accounting) two other claims reserves that provided for the payment of other types of claims. A second reserve provided for medical and dental benefits of active employees (the "active employee medical claims reserve"). A third reserve provided for long-term disability benefits of employees (the "long-term disability reserve"). In 1991, separate bank accounts were established for each of these three reserves. Additionally, a fourth reserve was established in 1992 to provide for post-retirement medical benefits for employees that were active employees as of 1992 (the "post-retirement DEFRA medical reserve"). A contribution of $28,331,843 was made in 1992 to the post-retirement DEFRA medical reserve.

In 1985, a transfer of $4,000,000 was made from the existing reserve to the active employee medical claims reserve account. In 1986, a transfer of $2,500,000 was made from the existing reserve to the active employee medical claims reserve. There were no other transfers from the existing reserve to any other account or reserve after 1986.

On June 29, 1993, the net assets of the corporate VEBA were transferred to four separate trusts. Each trust filed a separate Form 990 for the two day period of June 29 and June 30, 1993. The names of the four trusts are the

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. Each trust has received a favorable determination letter (each dated February 21, 1996), recognizing its status as an exempt organization under section 501(c)(9) of the Code.

Form 990-T was filed by the for the two day period of June 29 and June 30, 1993. Forms 990-T were filed for the VEBA corporation for the fiscal years ended June 30, 1992, and June 30, 1993. The corporate VEBA reported on Form 990 for the taxable year ended June 30, 1993, that the various amounts of assets had been invested in tax-exempt instruments, primarily tax-exempt mutual funds.

Applicable Law

Section 419(a) of the Code provides that contributions paid or accrued by an employer to a welfare benefit fund shall, if they would otherwise be deductible, be deductible (subject to the limitation of subsection 419(b)) under section 419 for the taxable year in which paid.

Section 419(b) of the Code provides that the deduction allowable under section 419(a) shall not exceed the qualified cost of the welfare benefit fund for the taxable year.

Section 419(c) of the Code defines the qualified cost as equal to the sum of the qualified direct cost for the taxable year as defined under section 419(c)(3), plus the amount of any addition to a qualified asset account for the taxable year, subject to the limitation contained in section 419A(b), less the after-tax income of the welfare benefit fund for the taxable year.

Section 419A of the Code defines a qualified asset account and the limitations on additions to that account. Section 419A(b) provides that no addition to any qualified asset account may be taken into account under section 419(c)(1)(B) to the extent such addition results in the amount in such account exceeding the account limit.

Section 419A(c)(2) of the Code provides that the account limit may 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 or life insurance benefits.

Section 419A(f)(7) of the Code provides that the account limit under section 419A(c) is adjusted for existing excess reserves by increasing the account limit by fixed percentages of any existing excess reserves in each of the first four taxable years to which section 419A applies (80 percent for the first such year, reduced 20 percentage points each year for the succeeding three such years). Section 419A(f)(7) applies to welfare benefit funds which, as of July 18, 1984, had assets set aside for purposes described in subsection 419A(a). For purposes of computing the increase under subparagraph 419A(f)(7) for any taxable year, the "existing excess reserve" means the excess (if any) of (1) the amount of assets set aside at the close of the first taxable year ending after July 18, 1984, for purposes described in subsection 419A(a), over (2) the account limit determined under section 419A (without regard to paragraph 419A(f)(7)) for the taxable year for which such increase is being computed.

Section 419A(h) of the Code contains rules for mandatory and permissive aggregation of welfare benefit funds maintained by the same employer. Section 419A(h)(1)(A) requires that all welfare benefit funds of an employer be treated as one fund in applying certain limits imposed by section 419A. This aggregation requirement applies to the following statutory provisions: First, all welfare benefit funds of an employer must be aggregated in calculating the limit imposed by section 419A(c)(4)(A) on the amount of disability benefits payable to an individual and in calculating the limit imposed by section 419A(c)(4)(B) on the amount of SUB (supplemental unemployment compensation benefit) or severance pay benefits payable to any individual that may be taken into account in determining the qualified asset account limit under section 419A(c) applicable to disability, SUB, or severance pay benefits. Second, all welfare benefit funds of an employer must be aggregated in applying section 419A(d)(2) to determine the amount to be treated as an annual addition to a defined contribution plan of a key employee arising out of an allocation to a separate account for post-retirement medical or life insurance benefits payable to that key employee. Finally, all welfare benefit funds of an employer must be aggregated in applying section 419A(e)(2), which imposes a limit of $50,000 on the aggregate amount of post-retirement life insurance provided to any employee that may be taken into account in calculating the amount of the reserve that the employer may fund over the working lives of the covered participants in accordance with section 419A(c)(2).

Section 419A(h)(1)(B) of the Code permits an employer, at its election, to treat two or more of its welfare benefit funds as one fund (other than for purposes of the provisions to which mandatory aggregation rules apply) to the extent that this treatment is not inconsistent with the purposes of section 419, section 419A, or section 512.

Section 501(c)(9) of the Code describes as exempt, as provided under section 501(a), voluntary employees' beneficiary associations providing for the payment of life, sick, accident or other benefits to the members of such association or their dependents or designated beneficiaries, if no part of the net earnings of such association inures (other than through such payments) to the benefit of any private shareholder or individual.

Section 1.501(c)(9)-3(a) of the Income Tax Regulations provides that the life, sick, accident, or other benefits provided by a VEBA must be payable to its members, their dependents, or their designated beneficiaries, and that a VEBA is not operated for the purpose of providing life, sick, accident, or other benefits unless substantially all of its operations are in furtherance of the provision of such benefits.

Section 1.501(c)(9)-4(a) of the regulations provides that no part of the net earnings of a VEBA may inure to the benefit of any private shareholder or individual other than through the payment of benefits permitted by section 1.501(c)(9)-3 of the regulations.

Section 505(c) of the Code provides, in part, that an organization will not be treated as exempt under section 501(c)(9) unless it has given notice to the Secretary of Treasury, in accordance with Treasury regulations.

Section 1.505(c)-1T, Q&A-3 through 8 of the regulations describe the method of notification in accordance with section 505(c) for section 501(c)(9) organizations or trusts organized after July 18, 1984.

Section 511(a) of the Code imposes a tax on the UBTI, as defined in section 512 of the Code, of any organization (other than a trust described in section 511(b) or an organization described in section 501(c)(1)) which is exempt from tax under section 501(a).

Section 511(b) of the Code imposes a tax on the UBTI, as defined in section 512 of the Code, of every trust which is exempt from tax under section 501(a) and which, if it were not for such exemption, would be subject to taxation under subchapter J (relating to estates, trusts, beneficiaries, and decedents).

Section 512(a)(3)(A) of the Code provides that, in the case of an organization described in section 501(c)(9), the term "unrelated business taxable income" means the gross income (excluding any exempt function income), less the deductions allowed by this chapter that are directly connected with the production of the gross income (excluding exempt function income). Both the gross income and the deductions taken into account under this paragraph are computed with certain modifications provided in section 512(b), relating to net operating losses and charitable contributions.

Section 512(a)(3)(B) of the Code defines "exempt function income" as the gross income from dues, fees, charges, or similar amounts paid by members of the organization as consideration for providing such members or their dependents or guests goods, facilities, or services in furtherance of the exempt purposes of the organization. Exempt function income includes all income which is set aside for the payment of life, sick, accident, or other benefits, including reasonable costs of administration directly connected with such purposes.

Section 512(a)(3)(E)(i) of the Code provides that a setaside for the payment of life, sick, accident, or other benefits may be taken into account under subparagraph (B) only to the extent that such set-aside does not result in an amount of assets set aside for such purpose in excess of the account limit determined under section 419A for the taxable year (not taking into account any reserve described in section 419(c)(2)(A) for post-retirement medical benefits).

Section 512(a)(3)(E)(ii)(I) of the Code provides that section 512(a)(3)(E)(i) does not apply to income attributable to an existing reserve for post-retirement medical or life insurance benefits.

Section 512(a)(3)(E)(ii)(II) of the Code provides that the existing reserve for post-retirement medical or life insurance benefits is the greater of the amount of assets set aside for purposes of post-retirement medical or life insurance benefits to be provided to covered employees as of the close of the last plan year ending before the date of the enactment of the Tax Reform Act of 1984 or on July 18, 1984.

Section 512(a)(3)(E)(ii)(III) of the Code provides that all payments during plan years ending on or after the date of the enactment of the Tax Reform Act of 1984 of post-retirement medical benefits or life insurance benefits shall be charged against the reserve referred to in subclause (II). Except to the extent provided in regulations prescribed by the Secretary, all plans of an employer are treated as one plan for purposes of the preceding sentence.

Section 1.512(a)-5T, Q&A-3(a) of the Income Tax Regulations (Temporary) provides that the amounts set aside in a VEBA to provide for the payment of life, sick, accident, or other benefits may not be taken into account for purposes of determining "exempt function income" to the extent that such amounts exceed the qualified asset account limit, determined under sections 419A(c) and 419A(f)(7). In calculating the qualified asset account limit for this purpose, a reserve for post-retirement medical benefits under section 419A(c)(2)(A) is not to be taken into account.

Section 1.512(a)-5T, Q&A-3(b) of the regulations provides that the exempt function income of a VEBA includes member contributions (both employee and employer contributions) and other income of the VEBA (including earnings on member contributions) that is set aside for the payment of life, sick, accident, or other benefits to the extent that the total amount set aside does not exceed the qualified asset account limit for such taxable year of the organization. Accordingly, the unrelated business taxable income of a VEBA for a taxable year of the organization generally will equal the lesser of the income of the VEBA (excluding member contributions), or the excess of the total amount set aside (including member contributions) over the qualified asset account limit (calculated without regard to the otherwise permitted reserve for post-retirement medical benefits) for the taxable year.

Section 1.512(a)-5T, Q&A-4(a) of the regulations states that section 512(a)(3)(E)(iii)(I) of the Code provides that income that is either directly or indirectly attributable to "existing reserves for post-retirement medical or life insurance benefits" will not be treated as unrelated business taxable income.[1] An "existing reserve for post-retirement medical or life insurance

[1] The temporary regulations refer to section 512(a)(3)(E)(iii)(I), rather than section

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benefits" is the total amount of assets actually set aside in a VEBA on July 18, 1984, or the end of taxable year of the VEBA ending before July 18, 1984 (calculated in the manner set forth in Q&A-3), reduced by certain employer contributions to the fund that are nondeductible for the taxable year of the employer containing July 18, 1984, or any prior taxable year and that were made for purposes of providing such post-retirement benefits.

Section 1.512(a)-5T, Q&A-4(b) of the regulations provides that section 512(a)(3)(E)(ii)(I) applies to existing reserves for such post-retirement benefits only to the extent that such "existing reserves" do not exceed the amount that could be accumulated under the principles set forth in Revenue Rulings 69-382, 1969-2 C.B. 28; 69-478, 1969-2 C.B. 29, and 73-599, 1973-2 C.B. 40. Amounts attributable to such excess "existing reserves" are not within the transition rule even though they were actually set aside on July 18, 1984.

Section 1.512(a)-5T, Q&A-4(c) of the regulations provides that all post-retirement medical or life insurance benefits provided after July 18, 1984 are to be charged, first, against the "existing reserves" for post-retirement medical benefits or for post-retirement life insurance benefits (as the case may be) and, second, against all other accounts. For purposes of section 512(a)(3)(E)(ii)(III), all plans of an employer providing post-retirement medical benefits are to be treated as one plan, and all plans of an employer providing post-retirement life insurance benefits are to be treated as one plan.

Section 1.512(a)-5T, Q&A-4(d) of the regulations provides that in calculating the unrelated business taxable income of a VEBA, the total income of the VEBA is reduced by the income attributable to "existing reserves" before such income is compared to the excess of the total amount set aside as of the close of the taxable year over the qualified asset account limit for the taxable year.

Section 103(a) of the Code provides that, except as provided in subsection 103(b), gross income does not include interest on any State or local bond. Section 103(b) provides exceptions to section 103(a) for private activity bonds, arbitrage bonds, and bonds not in registered form. Section 103(c) defines a state or local bond as an obligation of a State or political subdivision thereof.

512(a)(3)(E)(ii)(I), because they were published before the pertinent section was renumbered by section 1851(a)(10)(B) of the Tax Reform Act of 1986. The new numbering will be hereafter referenced in this memorandum.

Rationale

Issue 1 - Does income on an amount set aside as an existing reserve for post-retirement medical or life insurance benefits under section 512(a)(3)(E)(ii) of the Internal Revenue Code act to increase the existing reserve? Do claims for benefits act to decrease the existing reserve?

The existing reserve defined in Code section 512(a)(5)(E)(ii) is established for a different purpose than the "existing excess reserve" defined in Code section 419A(f)(7). The primary purpose of the existing reserve defined in section 512 is to calculate unrelated business income tax (UBIT). The primary purpose of the existing excess reserve defined in section 419A(f)(7) is to phase out, over the four-year period following the effective date of section 419A(f)(7), an increase in the qualified asset account limit calculated under section 419A(c). This technical advice memorandum addresses the effect of the existing reserve for post-retirement medical or life insurance benefits on the calculation of UBIT under section 512; it does not consider the manner in which the account limit under section 419A(c) is affected by the transition rule of section 419A(f)(7). The latter issue was not one of the issues identified in the technical advice request.

The existing reserve established in the Plan on July 18, 1984, was in the amount of $18,031,370. In subsequent years, for the purposes of calculating UBIT, the existing reserve was (1) decreased by net claims (claims minus employee contributions), and (2) increased by realized earnings. By June 30, 1991, the existing reserve, after being accounted for in this fashion, had grown to $27,608,255. According to the information submitted by the Company, realized earnings consisted of earnings only on existing assets; unrealized gains or losses were excluded. Section 1.512(a)-5T, Q&A-4(a) of the regulations states that Code section 512(a)(3)(E)(ii)(I) provides that income that is either directly or indirectly attributable to the existing reserve defined in section 512 will not be treated as unrelated business taxable income (UBTI). Because earnings of the existing reserve are directly attributable to the existing reserve, such earnings shall not be treated as UBTI. Furthermore, earnings on such earnings are indirectly attributable to the existing reserve and also should not be treated as UBTI.

Thus, one method of calculating UBTI so that earnings (and earnings on the earnings) on the existing reserve are not treated as UBTI would be to view the existing reserve as "increasing" in subsequent years, due to income that is directly or indirectly attributable to the existing reserve. Alternatively, the existing reserve could be viewed as "frozen" with the earnings that are not treated as UBTI calculated separately. Either of these approaches should produce the same result.

Section 1.512(a)-5T, Q&A-4(c) of the regulations provides that all post-retirement medical or life insurance benefits provided after July 18, 1984, are to be charged, first, against the existing reserve and, second, against all other amounts. The reduction of the existing reserve under section 512 by the amount by which claims for applicable benefits in years after July 18, 1984 exceed retiree contributions is consistent with this regulation section. The amount must be charged against the existing reserve until the existing reserve has been reduced to zero.

Issue 2 - May the existing reserve for post-retirement medical or life insurance benefits under Code section 512(a)(5)(E)(ii) be used to provide medical benefits for active employees? Would payments for active employee medical benefits affect the characterization of the reserve as an "existing reserve"?

If amounts attributed by the Company to an existing reserve for post-retirement medical benefits were actually set aside in the corporate VEBA on July 18, 1984, for the purpose of providing such benefits, the subsequent use of those funds to pay medical benefits for active employees would not affect the characterization of the reserve as an "existing reserve". See section 1.512(a)-5T, Q&A-4(c) of the regulations.

Whether those amounts were actually set aside for the purpose of providing post-retirement medical benefits is a factual question, which should be determined taking into account all of the facts and circumstances. Facts and circumstances to be taken into account should include how the amounts in the reserve were ultimately applied. However, the information provided to us does suggest that the amounts the Company attributes to the existing reserve had indeed been set aside for the purpose of providing post-retirement medical benefits. Compare, General Signal v. Commissioner, 103 T.C. 216 (1994), aff'd. 142 F.3d 546 (1998). In particular, the Company's submission dated July 31, 1995, indicates that Taxpayer fully funded the accrued liability for the post-retirement medical benefits in 1978, well in advance of the enactment of the Deficit Reduction Act of 1984.[2]

Section 1.512(a)-5T Q&A-4(b) of the regulations provides that the transition rule of section 512(a)(3)(E)(ii)(I) applies to existing reserves for post-retirement benefits only to the extent that those existing reserves do not exceed the amount that could be accumulated under the principles set forth in Revenue Rulings 69-382, 69-478 and 73-599. We are not here opining on whether the requirements of those revenue rulings were, in fact, met. In this regard, the Company states in its submission that the Plan's 1984 actuarial report indicates that the amount of the allowable deductible contribution was calculated based on the principles of Rev. Rul. 73-599.

Issue 3 (a) Should all income other than income from an existing reserve be included in computing the UBTI of a VEBA that is exempt from tax under Code section 501(c)(9), if one account is maintained for the VEBA but consists of four separate claims reserves that are

[2] Even if the use of the existing reserve for active benefits would constitute a reversion under section 4976 of the Code, that section does not apply in this case, because contributions to the existing reserve predate the effective date of section 419 and were therefore not deducted under that section. See section 4976(b)(3).

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accounted for separately?

Issue 3(b) Is income from tax-exempt bonds maintained in one of the claims reserves considered "exempt function income"?

(a) Calculation of UBTI

Section 512(a)(3) and temporary regulation section 1.512(a)-5T provide rules for calculating the exempt function income and UBTI of a VEBA. There is no provision for calculating exempt function income or UBTI separately for each account or reserve within a VEBA. Therefore, UBTI should be computed for the corporate VEBA as a whole, prior to the transfer of assets to four separate VEBA's on June 29, 1993.

With respect to the period beginning on June 29, 1993, since all of the trusts are welfare benefit funds of the same employer, section 419A(h)(1)(A) applies and requires that these four trusts be treated as one fund in determining the account limit components and other amounts specified in that section. The calculation of the UBTI of a welfare benefit fund is not among the calculations expressly subject to mandatory aggregation under section 419A(h)(1)(A), and no regulations have been published prescribing specific methods of calculation for use in a case in which the same employer contributes to two or more welfare benefit funds covering its employees. Moreover, the Company has not elected voluntary aggregation under section 419A(h)(1)(B) of the trusts involved in this ruling request. Therefore, a separate account limit under section 419A must be calculated for each of the trusts maintained by Company.

Because each of the separate trusts qualifies as a VEBA under section 501(c)(9), the determination of UBTI must be made in accordance with the special rules provided under section 512(a)(3), including the limitation on setasides contained in section 512(a)(3)(E). This limitation, in turn, is dependent upon the calculation of the account limit under section 419A. As explained above, however, the calculation of this account limit, as it applies to each of the separate trusts, is not affected by any of the items or account limit components subject to mandatory aggregation. Accordingly, the requirements of section 512(a)(3) will be applied separately to each of the four trusts involved in this case in order to determine the amount of income, if any, of each trust that is subject to UBIT imposed by section 511.

(b) Income from Tax-Exempt Bonds

As provided under Temporary Regulation section 1.512(a)-5T, Q&A-3(b), UBTI of a VEBA for a taxable year generally will equal the lesser of two amounts:

(1) The income of the VEBA for the taxable year (excluding member contributions); or

(2) The excess of the total amount set aside as of the close of the taxable year

(including member contributions) over the qualified asset account limit (calculated without regard to the otherwise permitted reserve for post-retirement medical benefits) for the taxable year.

For purposes of the first prong of the foregoing test, "income of the VEBA" as used in the regulation means "gross income" as used in section 512(a)(3)(A). The term "gross income" is not given a special definition under section 512(a)(3) of the Code, and therefore the meaning of that term under section 61 controls. Code section 61 defines "gross income" as all income from whatever source derived except as otherwise provided. Code sections 101 et seq. specify various exclusions from gross income. Section 103 of the Code generally excludes interest on tax-exempt bonds from gross income. Thus, we conclude that to the extent interest on tax-exempt bonds is excluded from gross income under section 61 by reason of section 103, it is also excluded from gross income of a VEBA under section 512(a)(3). Therefore, such income is not included in the "income of the VEBA" under regulation section 1.512(a)-5T, Q&A 3(b).

However, pursuant to that regulation, the value of the Taxpayer's assets, including amounts received as interest on tax-exempt bonds, would be included in the amount set aside to provide welfare benefits in determining the amount of the "excess setaside" under the second prong of the test, which is the amount by which the amount set aside as of the close of the taxable year exceeds the VEBA's qualified asset account limit as computed generally under sections 419 and 419A of the Code (calculated without regard to the otherwise permitted reserve for post-retirement benefits). Thus, if, in any taxable year of the VEBA, the excess setaside is less than the VEBA's income, the amount of the excess setaside would generally be UBTI to the VEBA.

<u>Issue 4 - How are amounts set aside in existing reserves and additional reserves for post-retirement medical or life insurance benefits taken into account when computing the UBTI of a VEBA?</u>

The calculation of UBTI is adjusted to account for existing reserves and additional reserves in the following manner. The UBTI of a VEBA is equal to the lesser of the income of the VEBA, or the excess of the total amount set aside at the end of the taxable year (including member contributions) over the qualified asset account limit for the taxable year. See section 1.512(a)-5T, Q&A-3(b) of the regulations. The income of the VEBA is adjusted as a result of the transition rule involving an existing reserve under section 512(a)(3)(E). The qualified asset account limit is adjusted as a result of the transition rule involving an existing reserve under section 419A(f)(7). Section 512(a)-5T, Q&A-4(a) of the regulations provides that income that is either directly or indirectly attributable to "existing reserves for post-retirement medical or life insurance benefits" will not be treated as UBTI. Section 1.512(a)-5T, Q&A-4(d) of the regulations provides that in calculating the UBTI of a VEBA, the total income of the VEBA is reduced by the income directly or indirectly attributable to "existing reserves" before such income is compared to the excess of the total amount set aside as of the close of the taxable year over the qualified asset account limit for the taxable year (the "excess setaside").

Section 1.512(a)-5T, Q&A-3(b) provides that the qualified asset account limit is calculated without regard to the otherwise permitted reserve for post-retirement medical benefits. Thus, the excess setaside for a taxable year is generally equal to the difference between the total amount in the account at the end of the year and the qualified asset account limit as computed generally under sections 419 and 419A (without regard to the otherwise permitted reserve for post-retirement benefits).

Issue 5 - What effect, if any, do the filings of separate Forms 990 for each claims reserve have on the computations of UBTI? Do the separate filings create separate VEBA's?

On June 29, 1993, the Company shifted all of the assets of the corporate VEBA to four trusts established for the original four claims reserves that were maintained under the corporate VEBA. The Company filed Forms 990 for the four trusts for the short taxable year covering the period June 29, 1993 and June 30, 1993. The Company filed Forms 990-T for the corporate VEBA and the "Post Retirement DEFRA Excess Trust" for the taxable year ended June 30, 1993. As of June 29, 1993, each of the four separate trusts, which subsequently received favorable determination letters as to their exempt status under section 501(c)(9), is considered a separate VEBA. Accordingly, any calculations of UBTI or UBIT should be done separately for each of the four separate trusts on or after June 29, 1993. The filings of Form 990 did not in themselves create separate VEBA's; the execution of separate trust documents and receipt of favorable determination letters were necessary to create separate VEBA's.

Conclusions

(1) Income on an amount set aside as an existing reserve for post-retirement medical or life insurance benefits under section 512(a)(5)(E)(ii) of the Code acts to increase the existing reserve, and claims for benefits act to decrease the existing reserve.

(2) If amounts attributed by the Company to an "existing reserve for post-retirement medical or life insurance benefits" were actually set aside in the corporate VEBA for that purpose on July 18, 1984, then the subsequent use of those funds to pay medical benefits for active employees would not affect the characterization of the reserve as an "existing reserve".

(3)(a) All income of a VEBA other than income from an existing reserve is included in computing the UBTI of a VEBA, even though the VEBA consists of four separate claims reserves that are accounted for separately.

(3)(b) In computing UBTI, income from tax-exempt bonds is not treated as exempt function income of the VEBA. However, such income affects the amount of assets available to pay benefits, and thus may indirectly affect the computation of UBTI.

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(4) Amounts set aside in existing reserves and additional reserves for post-retirement medical or life insurance benefits are taken into account in accordance with section 1.512(a)-5T, Q&A-4(a) and (d) of the regulations when computing the UBTI of the VEBA.

(5) Separate VEBA's were created by the execution of separate trust documents as of June 29, 1993; the filings of separate Forms 990 did not in themselves create separate VEBA's.

Note that this memorandum addresses only the issues raised in the Request for Technical Advice. Specifically, this memorandum does not address whether deductions taken by the Taxpayer for contributions to the VEBA's were properly computed in accordance with sections 419 and 419A of the Code.

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