TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

200225041

Date: March 25, 2002

UIL: 501.09-00

Contact Person:

Identification Number:

Telephone Number:

T·EO·B3

Employer Identification Number:

A =
B =
M =

N =
O =
P =
X =
Y =

Dear Sir or Madam:

We have considered your ruling request dated July 26, 1999, and subsequent correspondence concerning the tax consequences of a transfer of assets of certain VEBAs upon termination of the acquired corporations by the acquiring corporation and the merger of the VEBA assets with assets held by the VEBAs of the acquiring corporation.

X requests a ruling on the proper treatment of the proposed merger of four voluntary employee welfare benefits trust (VEBA[s]), over which Y, the sponsor, acquired sponsorship through merger or stock purchase, with and into two VEBAs sponsored by Y.

Through merger or stock purchase, Y or its subsidiary acquired the entities which sponsor the following VEBAs: M acquired in March, 1993; N acquired in June, 1993; O acquired in June, 1993; and P acquired in April, 1995. These four acquired VEBAs are collectively referred to as the Orphan VEBAs. The Orphan VEBAs were established to provide funding for medical, dental, death and/or long term disability benefits to be paid under their associated welfare benefit plans. Each of the Orphan VEBAs has only provided benefits which are permissible under section 501(c)(9) of the Internal Revenue Code. For several years, Sponsor's predecessors made contributions to the Orphan VEBAs and deducted those contributions in

236

accordance with the provisions of sections 162, 419, and 419A of the Code. When Sponsor took sponsorship of the Orphan VEBAs, it transferred all employees who were eligible under the plans associated with the Orphan VEBAs to one or more of the following welfare benefit plans of Sponsor, either A or B (hereafter, the "Transferee VEBAs). As a consequence of having transferred all of the participants in the Orphan VEBAs to other plans, X discontinued contributions to the Orphan VEBAs.

On October 17, 2001, upon P's application our office issued an exemption for P under section 501(c)(9) of the Code, as it was discovered that P had not previously received tax exemption from the Internal Revenue Service.

Each of the Transferee VEBAs are exempt from tax under section 501(c)(9) of the Code and each are a welfare benefit plan within the meaning of section 419(e) of the Code.

Because the Orphan VEBAs no longer pay benefits to employees, Sponsor intends to direct Trustee to merge the Orphan VEBAs into the Transferee VEBAs so that the funds held in the Orphan VEBAs can be used to benefit all of Sponsor's eligible employees under the Transferee VEBAs, including those employees who previously participated in the plans associated with the Orphan VEBAs. Under the proposed plan, all of the assets of M, N, O, and P will be transferred to A and B.

You have requested the following rulings:

1. Neither the transfer of the assets of the Orphan VEBAs to the transferee VEBAs nor the use of the assets of the Orphan VEBAs by the transferee VEBAs to future medical, long term disability, and death benefits to eligible active and retired employees of Sponsor will cause a reversion to Sponsor within the meaning of section 4976(b)(1)(C) of the Code that is subject to the excise tax under section 4976(a) of the Code.

2. The proposed transaction will not cause either the Orphan VEBAs or the Transferee VEBAs to cease to be recognized as exempt from Federal income tax under section 501(c)(9) of the Code to the extent that Orphan VEBAs were prior to the proposed transaction, exempt from Federal income tax under section 501(c)(9) of the Code.

3. The proposed transaction will not cause either the Orphan VEBAs or the Transferee VEBAs to incur unrelated business taxable income as defined in section 512 of the Code.

Section 501(c)(9) of the Code provides for the exemption from federal income tax of voluntary employees' beneficiary associations providing for the payment of life, sick, accident, or other benefits to the members of such associations or their dependents or designated beneficiaries if no part of the net earnings of such associations inure (other than through such payments) to the benefit of any private shareholder or individual.

Section 4976(a) of the Code provides that, if an employer maintains a welfare benefit fund, and there is a disqualified benefit provided during any taxable year, there is hereby imposed on such employer a tax equal to 100 percent of such disqualified benefit.

Section 4976(b)(1)(C) provides the term "disqualified benefit" includes any portion of a welfare benefit fund reverting to the benefit of the employer.

Section 511 imposes income tax on unrelated business taxable income as defined in section 512 of the Code.

Section 1.501(c)(9)-4(a) of the Income Tax Regulations provides, in part, that no part of the net earnings of an employees' association may inure to the benefit of any private shareholder or individual other than through the payment of permissible benefits. Whether prohibited inurement has occurred is a question to be determined with regard to all of the facts and circumstances, taking into account the guidelines set forth in this section.

Section 1.501(c)(9)-4(a) of the regulations provides, in part, that it will not constitute prohibited inurement if on termination of a plan established by an employer and funded through an association described in section 501(c)(9), any assets remaining in the association, after satisfaction of all liabilities to existing beneficiaries of the plan, are applied to provide, either directly or through the purchase of insurance, life, sick, accident or other benefits pursuant to the criteria that do not provide for disproportionate benefits to officers shareholders, or highly compensated employees of the employer.

Transferring assets from the Orphan VEBAs to the Transferee VEBAs to pay future medical, long term disability, and death benefits to eligible and active employees of X, including former participants in the Orphan VEBAs, are permissible activities and will not result in prohibited inurement under section 1.501(c)(9)-4(a) of the regulations. Section 1.501(c)(9)-4(d).

Employees of companies acquired by X and Y who participated in the Orphan VEBAs, M, N, O, and P, and benefited under one of such plans are now participating under A or B. The Transferee VEBAs are recognized as exempt under section 501(c)(9) of the Code. Thus, the transfer of assets directly by the Orphan VEBAs to the Transferee VEBAs and the application by A and B to provide medical, long term disability, and death benefits to employees including participants in the Orphan VEBAs, will not result in prohibited inurement.

In addition, because the amounts transferred from the Orphan VEBAs to the Transferee VEBAs will be applied to provide continuing employee medical, long term disability, and death benefits, the amounts in question do not result in a reversion to X, and the transaction will not result in the imposition of tax under section 4976(a).

Unrelated trade or business is defined in section 513 of the Code as any trade or business the conduct of which is not substantially related (aside from the need of such organization for income or funds or the use it makes of the profits derived) to the exercise or performance by an organization of its charitable, educational, or other purpose or function constituting the basis for its exemption. The purpose of the Transferee VEBAs is to provide certain welfare benefits to its members. The transfer of assets of the Orphan VEBAs to the Transferee VEBAs is for the purpose of providing welfare benefits to the members of the Orphan VEBAs and the Transferee

VEBAs. The transfer is substantially related to the exempt purpose of the Orphan VEBAs and the Transferee VEBAs and no unrelated business taxable income results.

Accordingly, we rule as follows:

1. Neither the transfer of the assets of the Orphan VEBAs to the Transferee VEBAs nor the use of the assets of the Orphan VEBAs by the Transferee VEBAs to pay future medical, long term disability, and death benefits to eligible active and retired employees of X will cause a reversion to X within the meaning of section 4976(b)(1)(C) of the Code that is subject to the excise tax under section 4946(a) of the Code.

2. The proposed transaction will not cause either the Orphan VEBAs or the Transferee VEBAs to cease to be recognized as exempt from Federal income tax under section 501(c)(9) of the Code to the extent that such Orphan VEBAs were, prior to the proposed transaction, exempt from Federal income tax under section 501(c)(9) of the Code.

3. The proposed transaction will not cause either the Orphan VEBAs or the Transferee VEBAs to incur unrelated business taxable income as defined in section 512 of the Code.

No opinion is expressed as to whether unrelated business taxable income may arise as a result of the provisions of section 512(a)(3)(E) of the Code.

Pursuant to a power of attorney on file with this office, a copy of this letter is being sent to your authorized representative.

If you have any questions about this ruling, please contact the person whose name and telephone number are shown in the heading of this letter.

This ruling is directed only to the person that requested it. Internal Revenue Code section 6110(k)(3) provides that it may not be used or cited as precedent.

Sincerely,

Robert C. Harper, Jr.
Manager, Exempt Organizations
Technical Group 3