Financial Services - Insurance Tax Bulletin

June 26, 2012

ITB 12-23

IRS denies exempt status to insurance trust

In PLR 201224037, the IRS ruled that an insurance trust failed to meet the burden of proof required for exemption from federal income taxes as required by Section 501(c)(9).

Taxpayer's purpose is to obtain, maintain, renew, and hold insurance policies, whereby participating employers can provide health insurance and other benefits to their employees. Only employers that meet certain specified requirements are entitled to participate in the Trust. In addition, the Trust's objective is to enable small companies to join forces in order to obtain insurance protection through mass purchasing.

The insurance plans are available to sponsoring chambers of commerce and associations through agents or brokers who must be affiliated with the Trust and whose commissions depend on the size of participating groups they enroll. The Trust does not keep records of the compensation of participating employees, including highly compensated ones, and participating employers must make minimum contributions of 75% or 100% of the premiums, depending on the type of industry. Also, only active, full-time employees of participating employers are eligible for coverage.

According to the IRS, a VEBA is a mutual association of employees providing specified benefits to its members or their beneficiaries, which may be funded by either the employees or their employer. In addition, the IRS provided that a VEBA functions primarily as a cooperative device for pooling funds and distributing risks over, and benefits a defined group of employees sharing an employment-related common bond. To that end, the Code exempts from federal income tax VEBA's that provide for the payments of life, accident, or other benefits to its members, if no part of the net earnings, except through the payments, are used to benefit any private shareholder or individual.

The IRS concluded that the Trust did not function primarily as a VEBA because it was not an association of employees whose eligibility is determined by objective standards constituting an employment-related common bond among such individuals. Membership was not defined by reference to a common employer, affiliated employers, coverage under a collective bargaining agreement, or a labor union. In addition, the IRS determined that the Trust failed to satisfy the requirement that it does not discriminate in favor of highly compensated individuals because it did not maintain adequate compensation records.

PwC Observation

Companies should ensure that they satisfy all the requirements for exemption from federal income tax under Section 501(c)(9), and should regularly review and monitor their records to make certain that they continue to qualify for such tax exempt status.

***For further information**, please feel free to contact Anthony DiGilio at (703) 918-4812 or contact your local insurance tax professional.*

Please visit us at: http://www.pwc.com/us/insurance/tax

This document is for general information purposes only, and should not be used as a substitute for consultation with professional advisors.

SOLICITATION

© 2012 PricewaterhouseCoopers LLP. All rights reserved. In this document, "PwC" refers to PricewaterhouseCoopers LLP, a Delaware limited liability partnership, which is a member firm of PricewaterhouseCoopers International Limited, each member firm of which is a separate legal entity.