

PRIVATE LETTER RULING REQUEST UPDATE FOR MPSERS REPORTING UNITS RELATED TO 3% CONTRIBUTIONS TO THE HEALTH CARE TRUST

Facts

Michigan public school districts and other reporting units (“Reporting Units”) participate in the state-sponsored MPSERS Health Care Plan. The State of Michigan (SOM) established the Health Care Trust to fund the post-retirement health benefits for eligible retirants of the Reporting Units, along with their spouses and eligible dependents.

Employer contributions from the Reporting Units, including mandatory contributions from active employees, are deposited in the Health Care Trust and invested among the investments selected by the State Treasurer as the sole investment fiduciary of the Health Care Trust. Pursuant to 2012 PA 300, mandatory contributions are taken from Reporting Unit Employees who, in late 2012, did not make a one-time irrevocable election to opt out of the future right to receive any health benefits (including health insurance premium subsidies) under the MPSERS Health Care Plan. Conversely, the Reporting Unit Employees who, in late 2012, made an irrevocable election to opt-out of receiving any future right to health benefits under the MPSERS Health Care Plan are not subject to a 3% mandatory reduction in their compensation. Once the one-time irrevocable election period closed in early 2013, Reporting Unit Employees became locked in and have not had (and will not in the future have) any individual or discretionary rights to modify or revoke their election, or to make individual elections of any kind with respect to the MPSERS Health Care Plan. Further, neither the Reporting Units nor Reporting Unit Employees have any election as to the level of mandatory contributions that are required to be made to the Health Care Trust. These amounts are calculated and determined by State statute and are mandatory with respect to all eligible Reporting Unit Employees who retain the future right to receive health benefits under the MPSERS Health Care Plan.

The IRS had initially provided confusing and even conflicting information to Reporting Units on the tax treatment accorded to mandatory contributions made to the Health Care Trust. The State of Michigan (through the Office of Retirement Services, “ORS”) attempted to obtain a system-wide answer from the IRS on the proper tax treatment of such mandatory contributions by filing a Private Letter Ruling request with the IRS on March 30, 2016. Unfortunately, the IRS refused to issue a ruling to the SOM on procedural grounds that SOM was not itself the taxpayer for purposes of the rulings requested.

Although no global determinations have yet been issued, since the 2016 filing of the initial PLR request, ORS has confirmed that multiple Reporting Units have received guidance from the IRS as to refund claims that had been submitted relative to federal income and FICA taxes that had been reported, deducted, and remitted under 2012 PA 300, respectively. This guidance suggests that the IRS has concluded—relative to the specific claims at issue—that the retiree healthcare contributions were exempt from federal income and FICA taxes. ORS continues to monitor this situation and is supporting the efforts of the Michigan School Business Officials, their constituents, and all MPSERS reporting units in obtaining favorable federal tax treatment for the contributions deposited into the Health Care Trust.

As a result, ORS is working with a representative Reporting Unit to re-submit a similar PLR request on this issue. ORS has provided copies of the draft PLR request to multiple school association and Reporting Unit representatives, attorneys and tax professionals for comment.

The Ruling Requests currently contemplated would be as set forth below. It is important to note the proposed PLR request deals with all mandatory contributions collected and deposited into the Health Care Trust. Any amounts that were not deposited into the Health Care Trust (such as those under 2010 PA 75 that were refunded pursuant to the Michigan court case) would not be covered by the PLR.

Requested Rulings

Ruling 1: Contributions (including mandatory contributions) that are made to the Health Care Trust pursuant to State law for Reporting Unit Employees participating in the MPSERS Health Care Plan are excludable from Reporting Unit Employees' gross income under Code Section 106.

Ruling 2: Contributions (including mandatory contributions) that are made to the Health Care Trust pursuant to State law for Reporting Unit Employees participating in the MPSERS Health Care Plan are not "wages" subject to FICA taxes under Code Section 3121(a), FUTA taxes under Code Section 3306(b) or income tax withholding under Code Section 3401(a).

Ruling 3: Health benefits (including health insurance premium subsidies) paid from the Health Care Trust pursuant to the MPSERS Health Care Plan to or on behalf of eligible retirants and their eligible spouses and dependents (as defined under Code Section 152 and IRS guidelines) are excludable from retirants' gross income under Code Section 105 and are not "wages" subject to FICA or FUTA taxes or income tax withholding under Code Sections 3121(a), 3306(b) and 3401(a), respectively.