



Department of Technology, Management & Budget
Office of Retirement Services

Federal Tax Implications for 3% Retiree Healthcare Contributions

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Federal Tax Implications for 3% Retiree Healthcare Contributions

The Office of Retirement Services (ORS) has learned that the Internal Revenue Service will soon be issuing determinations on certain “protective claims” filed by individual reporting units in regard to the federal tax treatment of the retiree healthcare contributions remitted under 2012 PA 300. Although formal determinations have not yet been issued, the Internal Revenue Service has informally indicated that it will be treating the retiree healthcare contributions under both 2010 PA 75 and 2012 PA 300 as **exempt from federal income taxes**. In addition, the Internal Revenue Service has informally indicated that the 2010 PA 75 retiree healthcare contributions will be treated as exempt from FICA taxes; however, the final informal indication from the Internal Revenue Service is that the rulings on the “protective claims” will treat **the 2012 PA 300 retiree healthcare contributions as being subject to FICA taxes**.

By way of background, 2010 PA 75 required members of the Michigan Public School Employees’ Retirement System to contribute (up to 3% of their compensation) to the Retiree Healthcare Fund established by 2010 PA 77. Those contributions, being mandatory in nature and “picked up” by the reporting unit as “employer contributions” were collected from July 1, 2010 until September 3, 2012. The retiree healthcare contributions remitted thereunder continue to be held in escrow pending a final resolution of the courts concerning the constitutionality of 2010 PA 75.

In September 2012, the Legislature enacted 2012 PA 300, which continued the retiree healthcare contribution enacted under 2010 PA 75, but also gave members an opportunity to irrevocably elect to discontinue their participation in—and contribution to—the retiree healthcare plan. Whereas the courts have yet to issue a final ruling on the constitutionality of 2010 PA 75, the Michigan Supreme Court ruled, in April 2015, that 2012 PA 300 is constitutional.

In view of the fact that the Michigan Supreme Court has upheld the constitutionality of 2012 PA 300, the Internal Revenue Service has indicated that it is preparing to issue rulings on the protective claims that have been filed by certain individual reporting units regarding the federal tax treatment of the retiree healthcare contributions under 2012 PA 300. As noted above, the Internal Revenue Service has informally indicated that, for federal tax treatment purposes, it views a distinction between the retiree healthcare contributions remitted under 2010 PA 75 and 2012 PA 300, respectively. Accordingly, it is expected that the Internal Revenue Service’s ruling will recognize that the retiree healthcare contributions remitted under 2012 PA 300 (i.e., from September 4, 2012 to present) are subject to FICA taxes.

ORS will update this bulletin as new information becomes available. In addition, ORS is preparing to file a Private Letter Ruling request with the Internal Revenue Service seeking a final determination, on behalf of the Michigan Public School Employees' Retirement System (as the plan's sponsor), regarding the federal tax treatment of the retiree healthcare contributions provided under both 2010 PA 75 and 2012 PA 300. The Office of Retirement Services is in contact and is consulting with various reporting unit organizations, including the Michigan School Business Officials.

In the meantime, individual reporting units are reminded of their obligation to report and remit federal taxes in accordance with the Internal Revenue Code and applicable regulations. Reporting units that have filed protective claims with the Internal Revenue Service regarding the 2012 PA 300 retiree healthcare contributions are encouraged to notify ORS and the Michigan School Business Officials of the status of those claims. Although ORS will continue to apprise reporting units of pertinent developments regarding this issue, individual reporting units are responsible for decisions concerning the handling of—and federal tax consequences stemming from—their own protective claims.

If you have questions regarding federal tax compliance issues, you should consult with a professional in the respective audit, advisory, tax or other professional area.

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