



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

TAX EXEMPT AND  
GOVERNMENT ENTITIES  
DIVISION

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Contact Person:  
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Identification Number:  
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Telephone Number:  
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Employer Identification Number: \*\*\*\*\*

**Legend**

Fund = \*\*\*\*\*

Dear :

This letter responds to your ruling request dated April 12, 2004, regarding the proper treatment of benefits paid under a supplemental unemployment benefit trust currently exempt under Section 501(c)(17) of the Internal Revenue Code ("Code").

**Background**

Fund provides supplemental unemployment benefits to eligible members during periods of unemployment due to layoff, injury, sickness or call-to-jury duty and is tax exempt under section 501(c)(17) of the Code. Funding is based on employer contributions for employees' hours worked at rates specified in collective bargaining

agreements. Benefits are accrued at the rate of one-quarter credit for each 80 hours worked. Members can accumulate a maximum of 52 credits based on contributions received for the hours worked during the previous two years. Credits are reduced for each week of benefits paid. Post-retirement benefits are not provided.

Fund proposes to modify its terms to pay the remaining benefit entitlement of an eligible member who dies while eligible to receive fund benefits to his surviving spouse on a continuing weekly basis until the entitled benefits are exhausted or to pay for health insurance coverage and/or outstanding medical bills for survivors and/or named beneficiaries.

### **Ruling Requested**

Fund requests a ruling that (1) the payment of the remaining supplemental unemployment benefit entitlement of an eligible member who dies while eligible to receive fund benefits to his surviving spouse on a continuing weekly basis until the entitled benefits are exhausted or to pay for health insurance coverage and/or outstanding medical bills for survivors and/or named beneficiaries are considered to be sick and accident benefits subordinate to supplemental unemployment compensation benefits within the meaning of section 501(c)(17)(D)(ii) of the Code; and (2) such payments will not adversely affect the exempt status of Fund under section 501(c)(17) of the Code.

### **Law & Analysis**

Section 501(a) of the Code provides that an organization described in section 501(c) of the Code is exempt from federal income tax.

Section 501(c)(17)(A) of the Code provides for the exemption of:

A trust or trusts forming part of a plan providing for the payment of supplemental unemployment compensation benefits, if--

(i) under the plan, it is impossible, at any time prior to the satisfaction of all liabilities, with respect to employees under the plan, for any part of the corpus or income to be (within the taxable year or thereafter) used for, or diverted to, any purpose other than the providing of supplemental unemployment compensation benefits,

(ii) such benefits are payable to employees under a classification which is set forth in the plan and which is found by the Secretary not to be discriminatory in favor of employees who are highly compensated employees (within the meaning of section 414(q)), and

(iii) such benefits do not discriminate in favor of employees who are highly compensated employees (within the meaning of section 414(q)). A plan shall not be considered discriminatory within the meaning of this clause merely because the benefits received under the plan bear a uniform relationship to the total compensation, or the basic or regular rate of compensation, of the employees covered by the plan.

Section 501(c)(17)(D) of the Code provides that the term "supplemental unemployment compensation benefits" means only--

(i) benefits which are paid to an employee because of his involuntary separation from the employment of the employer (whether or not such separation is temporary) resulting directly from a reduction in force, the discontinuance of a plant or operation, or other similar conditions, and

(ii) sick and accident benefits subordinate to the benefits described in clause (i).

Section 1.501(c)(17)-1 of the Income Tax Regulations ("Regulations"), with regard to supplemental unemployment benefit trusts provides, in pertinent part, that:

**(a) Requirements for qualification.** (1) A supplemental unemployment benefit trust may be exempt as an organization described in section 501(c)(17) if the requirements of subparagraphs (2) through (6) of this paragraph are satisfied.

\* \* \*

(3) The trust is part of a written plan established and maintained by an employer, his employees, or both the employer and his employees, solely for the purpose of providing supplemental unemployment compensation benefits (as defined in section 501(c)(17)(D) and paragraph (b)(1) of Sec. 1.501(c)(17)-1).

\* \* \*

(5) The trust is part of a plan whose eligibility conditions and benefits do not discriminate in favor of employees who are officers, shareholders, persons whose principal duties consist of supervising the work of other employees, or highly compensated employees. See sections 401(a)(3)(B) and 401(a)(4) and sections 1.401-3 and 1.401-4. However, a plan is not discriminatory within the meaning of section 501(c)(17)(A)(iii), relating to the requirement that the benefits paid under the plan be nondiscriminatory, merely because the benefits received under the plan bear a uniform relationship to the total compensation, or the basic or regular rate of compensation, of the employees covered by the plan. Accordingly, the benefits provided for highly paid employees may be greater than

the benefits provided for lower paid employees if the benefits are determined by reference to their compensation; but, in such a case, the plan will not qualify if the benefits paid to the higher paid employees bear a larger ratio to their compensation than the benefits paid to the lower paid employees bear to their compensation. In addition, section 501(c)(17)(B) sets forth certain other instances in which a plan will not be considered discriminatory (see paragraph (c) of section 1.501(c)(17)-2).

(6) The trust is part of a plan which requires that benefits are to be determined according to objective standards. Thus, a plan may provide similarly situated employees with benefits which differ in kind and amount, but may not permit such benefits to be determined solely in the discretion of the trustees.

**(b) Meaning of terms.** The following terms are defined for purposes of section 501(c)(17):

*(1) Supplemental unemployment compensation benefits.* The term “supplemental unemployment compensation benefits” means only:

(i) Benefits paid to an employee because of his involuntary separation from the employment of the employer, whether or not such separation is temporary, but only when such separation is one resulting directly from a reduction in force, the discontinuance of a plant or operation, or other similar conditions; and

(ii) Sick and accident benefits subordinate to the benefits described in subdivision (i) of this subparagraph.

\* \* \*

*(5) Subordinate sick and accident benefits.* In general, a sick and accident benefit payment is an amount paid to an employee in the event of his illness or personal injury (whether or not such illness or injury results in the employee's separation from the service of his employer). In addition, the phrase “sick and accident benefits” includes amounts provided under the plan to reimburse an employee for amounts he expends because of the illness or injury of his spouse or a dependent (as defined in section 152). Sick and accident benefits may be paid by a trust described in section 501(c)(17) only if such benefits are subordinate to the separation payments provided under the plan of which the trust forms a part. Whether the sick and accident benefits provided under a supplemental unemployment compensation benefit plan are subordinate to the separation benefits provided under such plan is a question to be decided with regard to all the facts and circumstances.

Section 1.501(c)(17)-2 of the Regulations provides general rules and definitions with regard to supplemental unemployment benefit trusts:

**(a) Supplemental unemployment compensation benefits.**

Supplemental unemployment compensation benefits as defined in section 501(c)(17)(D) and paragraph (b)(1) of section 1.501(c)(17)-1 may be paid in a lump sum or installments. Such benefits may be paid to an employee who has, subsequent to his separation from the employment of the employer, obtained other part-time, temporary, or permanent employment. Furthermore, such payments may be made in cash, services, or property. Thus, supplemental unemployment compensation benefits provided to involuntarily separated employees may include, for example, the following: Furnishing of medical care at an established clinic, furnishing of food, job training and schooling, and job counseling. If such benefits are furnished in services or property, the fair market value of the benefits must satisfy the requirements of section 501(c)(17)(A)(iii), relating to nondiscrimination as to benefits. However, supplemental unemployment compensation benefits may be provided only to an employee and only under circumstances described in paragraph (b)(1) of section 1.501(c)(17)-1. Thus, a trust described in section 501(c)(17) may not provide, for example, for the payment of a death, vacation, or retirement benefit.

**(b) Sick and accident benefits.** If a trust described in section 501(c)(17) provides for the payment of sick and accident benefits, such benefits may only be provided for employees who are eligible for receipt of separation benefits under the plan of which the trust is a part. However, the sick and accident benefits need not be provided for all the employees who are eligible for receipt of separation benefits, so long as the plan does not discriminate in favor of persons with respect to whom discrimination is proscribed in section 501(c)(17)(A)(ii) and (iii). Furthermore, the portion of the plan which provides for the payment of sick and accident benefits must satisfy the nondiscrimination requirements of section 501(c)(17)(A)(ii) and (iii) without regard to the portion of the plan which provides for the payment of benefits because of involuntary separation.

\* \* \*

**(i) Allocations.** If a plan which provides sick and accident benefits is financed solely by employer contributions to the trust, and such sick and accident benefits are funded by payment of premiums on an accident or health insurance policy (whether on a group or individual basis) or by contributions to a separate fund which pays such sick and accident benefits, the plan must specify that portion of the contributions to be used to fund such benefits. If a plan which is financed in whole or in part by employee contributions provides sick and accident benefits, the plan must specify the portion, if any, of employee contributions allocated to the cost of funding such benefits, and must allocate the cost of

funding such benefits between employer contributions and employee contributions.

Fund is created by employer contributions based on hours worked by a particular employee. Furthermore, benefits available to a particular employee are limited to credits earned, also based on that employee's hours worked. As such, there is a direct correlation between available benefits and the labor of a particular employee. Specific identifiable funding would not exist but for the efforts of a particular employee; in other words, benefits available to a particular employee are derived from that employee's actual hours worked. Consequently, the specific employer funding is essentially a result of the labor of specified employees. It therefore follows that an employee who is eligible to receive benefits under Fund, subject to the operational requirements of Fund, should receive the full benefit of his contributions, whether through exhaustion while eligible to receive benefits or as a benefactor upon death while eligible to receive benefits under Fund.

Benefits are not limited solely to the employee under the statutory and regulatory scheme provided for supplemental unemployment compensation benefits. Rather, the statutory scheme contemplates payments for medical care for the employee's spouse and/or dependents. Under section 1.507(c)(17)-1(b)(5) of the Regulations, "sick and accident benefits" includes amounts provided under the plan to reimburse an employee for amounts he expends because of the illness or injury of his spouse or a dependent (as defined in section 152). Given clear consideration that the statutory scheme permits an employee to receive reimbursements for amounts he expends for his spouse and/or dependents, it is only logical that those individuals receive available benefits upon the untimely death of an employee who is eligible to receive benefits under Fund.

### **Ruling**

Accordingly, based on the facts as represented, we rule as follows :

The payment of the remaining supplemental unemployment benefit entitlement of an eligible member who dies while eligible to receive fund benefits to his surviving spouse on a continuing weekly basis until the entitled benefits are exhausted or to pay for health insurance coverage and/or outstanding medical bills for his surviving spouse or dependents (as defined in section 152 of the Code) are considered to be sick and accident benefits subordinate to supplemental unemployment compensation benefits within the meaning of section 501(c)(17)(D)(ii) of the Code. Accordingly, Fund continues to qualify as a tax-exempt organization under section 501(c)(17) of the Code if it provides for such payments.

This ruling is based on the understanding that there will be no material changes in the facts and representation upon which it is based. Except as we have ruled herein,

we express no opinion as the tax consequences of the transactions under other sections of the Code and Income Tax Regulations.

This ruling will be made available for public inspection under section 6110 of the Code after certain deletions of identifying information are made. For details, see enclosed Notice 437, Notice of Intention to Disclose. A copy of this ruling with deletions that we intend to make available for public inspection is attached to Notice 437. If you disagree with our proposed deletions you should follow the instructions in Notice 437.

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

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.

Sincerely,

/s/

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

Enclosure  
Notice 437