

ADDITIONAL INFORMATION RELATED TO THE OPPORTUNITY TO PARTICIPATE IN AN IRS CLOSING AGREEMENT RELATED TO 3% CONTRIBUTIONS TO THE MPSERS HEALTH CARE TRUST

The State of Michigan (through the Office of Retirement Services, "ORS") provided an update on December 22, 2020 related to the current status of the federal tax treatment of the 3% contributions to the MPSERS Health Care Trust, and also provided the opportunity for each Reporting Unit to participate in and be covered by a Closing Agreement with the Internal Revenue Service (IRS) that favorably resolves the tax treatment of these contributions.

Additional questions have been asked by some Reporting Units and those professionals that are advising them related to this matter. ORS is sensitive to those questions, as well as the time frame for making certain determinations. The time frame has been extended to March 1 as communicated last week. ORS also understands that some reporting units and their counsel do not believe they have enough information to make a decision. Hopefully the additional information that is contained here will help, but please understand (and ORS knows that a large number of reporting units have indicated that they do) that ORS and its counsel do not have access to the full contents of the Closing Agreement, nor can they address every scenario for individual reporting units. That being said, ORS is taking further steps to provide as much additional information as possible in this Supplemental Notice to reporting units.

This Notice attempts to address several additional questions, such as the following:

1. What is the background and context of the proposed Closing Agreement? Is my Reporting Unit obligated to participate in this Closing Agreement?

No. There is no obligation for any reporting unit to participate. None of the reporting units, other than DeWitt Public Schools, has any facts before the IRS for purposes of this Closing Agreement.

The Closing Agreement was a result of a Private Letter Ruling (PLR) Request in 2018 submitted by W. Alan Wilk at Dykema on their behalf (and paid for by MPSERS because MPSERS had paid for the initial, almost identical, PLR Request in 2016). Rather than issue a PLR, the IRS chose to favorably resolve the tax determinations on the MPSERS 3% contributions (for income and FICA purposes) via the proposed Closing Agreement.

With the original PLR Request filed in 2016 by MPSERS, the intent was to obtain a ruling that covered all reporting units at that time. The IRS would not let MPSERS do this because of the technical reason that MPSERS was not a "taxpayer" (reporting unit) in the retirement system. DeWitt Public Schools then volunteered to be that taxpayer and the 2018 PLR Request was filed. As a result, the proposed Closing Agreement includes operative paragraphs that will be issued to them, resulting in favorable tax treatment for the MPSERS 3% contributions by their employees. The opportunity from the IRS that ORS forwarded in the first Notice on December 22, 2020, provides a process that allows other reporting units to also participate in the same Closing Agreement to be issued to DeWitt Public Schools. It will only cover DeWitt Public Schools unless other reporting units voluntarily choose to sign onto the Closing Agreement.

The IRS also discussed doing a Mass Closing Agreement that would apply for all reporting units, but ultimately decided to provide the ability for reporting units to voluntarily opt-in to be a part of this Closing Agreement, for a reduced user fee of \$3,000 (normally \$30,000) per reporting unit.

ORS has proceeded accordingly with the Notice to reporting units related to this opportunity provided by the IRS. ORS and counsel have tried to provide as much information as possible related to the background and substance of the Closing Agreement, including asking the IRS for as much information related to the Closing Agreement that they could provide, which resulted in the IRS disclosing the three

operative paragraphs of the Closing Agreement. That information was sent in the original Notice to reporting units on December 22, 2020. ORS and counsel have been answering additional questions since that initial Notice, and in this Supplement Notice that includes written answers to a number of follow-up questions. ORS and its counsel are not providing any legal or other advice as to whether or not a reporting unit should participate in this Closing Agreement.

It is a voluntary choice. There is no minimum number of reporting units that have to opt-in. ORS is fine if the Closing Agreement is simply signed on behalf of DeWitt Public Schools and no other reporting units. ORS is also fine if all or any number in between of reporting units want to participate. That is a decision that can be made by each reporting unit, with advice from their own counsel and based on their own facts and circumstances.

2. Is the IRS requesting \$3,000 per Reporting Unit to provide guidance on tax treatment of a deduction that the IRS has already acknowledged in communications to Reporting Units is exempt?

Again, there is no obligation for any reporting unit to participate and have funds expended on their behalf. The IRS has set the reduced user fee per taxpayer at \$3,000 for this Closing Agreement. As stated above, each reporting unit will have to decide whether to participate or not. If the reporting unit is comfortable with the IRS communications to the reporting units regarding the current tax treatment of the MPERS 3% contributions, they are certainly free to decline to participate in the Closing Agreement. Likewise, each reporting unit would presumably be free to pursue its own Private Letter Ruling or Closing Agreement based on its own facts and circumstances, if it were not comfortable with the terms, timing, information available, or any other aspect of this Closing Agreement.

3. What is a Closing Agreement?

Internal Revenue Code section 7121 authorizes the IRS and taxpayers to enter into closing agreements. While a closing agreement exhibits some of the attributes of a contract, it is not strictly subject to the law of contracts. Closing agreements are legally binding.

Treasury Regulation Section 301.7121-1(a), states:

“In general. The Commissioner may enter into a written agreement with any person relating to the liability of such person (or of the person or estate for whom he acts) in respect of any internal revenue tax for any taxable period ending prior or subsequent to the date of such agreement. A closing agreement may be entered into in any case in which there appears to be an advantage in having the case permanently and conclusively closed, or if good and sufficient reasons are shown by the taxpayer for desiring a closing agreement and it is determined by the Commissioner that the United States will sustain no disadvantage through consummation of such an agreement.”

4. Is this a “Mass Closing Agreement?”

No. A Mass Closing Agreement covers a class of taxpayers. The IRS has said that a Mass Closing Agreement in the exempt organizations area is unusual. In those cases, individual agreements with each person in the class will only be negotiated in cases where the class consists of 25 persons or less. If the issue and holding are the same for all members of the class and there are more than 25, the IRS has indicated it will enter into Mass Closing Agreement with the taxpayer who is authorized to represent the class. See *1993 EO CPE Text*, p.3.

In this case, the IRS has opted against issuing a Mass Closing Agreement to cover the entire class of Reporting Units, and has instead provided the opportunity for each Reporting Unit to decide on their own whether to sign onto and participate in the Closing Agreement that they have presented.

5. Will the full Closing Agreement be available for review?

IRS representatives have indicated, in part due to disclosure restrictions, that it will not provide the full contents of the Closing Agreement. Although the full contents of the Closing Agreement have not been disclosed by the IRS, upon request, the IRS made available the three operative paragraphs of the Closing Agreement and those were included in their entirety with original Notice to Reporting Units on December 22, 2020. It is our understanding that the IRS believed that this was the best case scenario to reach out to additional Reporting Units that were not part of the initial Private Letter Ruling request on these matters, and that Reporting Units may choose whether to participate or not.

6. What is expected to be in the Closing Agreement?

The first paragraph concludes that amounts deducted from employee compensation for the MPSERS 3% contribution are treated as employer contributions and are not treated as income under section 106 of the Internal Revenue Code. This conclusion is comparable to the original ruling request that ORS requested in prior Private Letter Ruling requests to the IRS.

The second paragraph concludes that amounts deducted from employee compensation for the MPSERS 3% contribution are not treated as “wages” for purposes of FICA taxes under section 3121(a) of the Internal Revenue Code or purposes of income tax withholding under section 3401(a) of the Internal Revenue Code. This conclusion is also comparable to the original ruling request that ORS requested in prior Private Letter Ruling requests to the IRS.

The third paragraph includes certain requirements as a result of the rulings in the first two paragraphs, including filing of Forms W-2c (corrected wage and tax statements) for affected employees for tax years limitation periods that have not expired, and notifying those employees that they can file Forms 1040-X for a refund on their income taxes for affected years.

Upon further inquiry related to the third paragraph, IRS representatives indicated that this was included to focus the Reporting Units on the impact and expected actions related to the employees and the necessary forms that needed to be filed as a result of the findings in the first two paragraphs. Those representatives also indicated that it was expected that the applicable Reporting Units would be filing forms on their own behalf, such as Form 941-X for open time periods.

7. Does the Closing Agreement impact the statute of limitations for filing certain protective, refund and other claims?

Each Reporting Unit will need to take action based on its own circumstances and based on its own counsel, but ORS is not aware that any limitations periods are impacted by the Closing Agreement.

8. Does the Closing Agreement impact the current status of certain protective, refund and other claims that have already been filed?

Each Reporting Unit will need to take action based on its own circumstances and based on its own counsel, but ORS is not aware that any currently valid and timely claims are impacted by the Closing Agreement, other than the Closing Agreement appears to confirm the tax treatment of the MPSERS 3% contributions for income and FICA tax purposes.

9. Will the IRS be providing required transmittal correspondence to participants with the Closing Agreement, or will it fall to each participant to generate the required correspondence with Affected Employees?

ORS is not aware of any specific correspondence that has been provided by the IRS.

10. Are there any additional details related to how Reporting Units can handle various claims in light of favorable tax treatment of the MPSERS 3% contributions?

Without providing specific guidance, ORS has provided general updates on this matter since the IRS began treating these payments favorably for some Reporting Units as far back as 2016. In addition, ORS has been in consultation with Taxpayer Advocate Services (TAS) (which is separate from the IRS departments that are handling the Closing Agreement) related to their information on these matters. TAS has advised Reporting Units to file Forms 941-X (Adjusted Employer's Quarterly Federal Tax Return or Claim for Refund) and to advise affected employees to file Forms 843 (Claim for Refund or Abatement) to recover overpaid employer and employee FICA taxes.

If it would be helpful to Reporting Units in their review of the Closing Agreement, refer to this [March 18, 2020 letter from the National Taxpayer Advocate](#) that the Taxpayer Advocate Service (TAS) asked ORS to distribute last year to the Reporting Units related to the federal tax treatment of the MPSERS 3% contributions.

That letter addresses a number of matters related to the 3% contributions, but focuses on (1) the time limits applicable under Section 6511 of the Internal Revenue Code, (2) those Reporting Units that need to make a refund or protective claim, and (3) the mechanics of how to handle the implementation of a refund. It appears the letter is focused on those Reporting Units that have either not yet stopped withholding FICA and income taxes on the 3% contributions or those that have stopped current withholding, but need to make claims for prior years.

The TAS also indicated at the time that it might be especially time sensitive to some Reporting Units that have not made a refund or protective claim for certain tax years given the upcoming deadline for such a claims at the time of the letter. The TAS letter also provides background on the TAS and their contact information.

11. Are all MPSERS Reporting Units eligible to participate in the Closing Agreement?

Yes, the opportunity to participate in the Closing Agreement covers all MPSERS Reporting Units. As such, ORS sent the December 22, 2020 notice to officials at community colleges, state public universities, self-employing public school academies, district libraries, local and intermediate school districts.

12. Are any MPSERS Reporting Units required to participate in the Closing Agreement?

No. Reporting Units are not required to be part of the Closing Agreement. Reporting Units are encouraged to consult with their own legal, tax and accounting professionals to form their own conclusions based on their own facts and circumstances. Neither ORS nor the Dykema Law Firm are providing any legal counsel to any Reporting Unit regarding whether to be part of the Closing Agreement or any other matters related to the proper tax treatment of employer and employee contributions made to the MPSERS Health Care Trust.

13. Will the Closing Agreement include any representations to Reporting Units that choose not to participate in the Closing Agreement?

No. The Closing Agreement allows the IRS to agree to certain tax determinations with Reporting Units (as taxpayers). The terms agreed to in this Closing Agreement will only cover those Reporting Units that are a party to the Closing Agreement. As a result, the Closing Agreement almost certainly will not include a statement that the IRS commits to not change its enforcement practice during the Closing Agreement period with regard to the tax treatment for Reporting Units that choose not to participate in the Closing Agreement.

14. Does this mean the Reporting Units that do not participate in the Closing Agreement will be treated differently?

No. ORS has no knowledge that choosing not to participate in the Closing Agreement will have any adverse tax consequences as a result of that decision by a Reporting Unit. ORS has been informed by various Reporting Units that a few years ago the IRS treated these 3% contributions differently than the Closing Agreement appears to now conclude, but most of the more recent reports are that they have been treated favorably by the IRS (similar to the operative paragraphs in the Closing Agreement).

15. Can a Reporting Unit ask for their own Private Letter Ruling or Closing Agreement?

ORS is not aware of any reason why a Reporting Unit could not ask for their own ruling. Presumably, a Reporting Unit would need to engage in that submission using the IRS normal method for such request.

16. Will ORS pay the \$3,000 filing fee for each Reporting Unit that chooses to participate in the Closing Agreement?

Yes, ORS has determined that it will make a single payment to the IRS to cover the fee for each participating Reporting Unit. ORS and the IRS are working on the specific mechanics for such a payment based on the number of Reporting Units that elect to participate in the Closing Agreement.

17. Will the \$3,000 filing fee come from MPSERS?

Yes, the expense is being incurred to validate that Reporting Units in MPSERS are properly excluding the 3% contributions from income and FICA taxes. Such expenses will be paid from the reserve for administrative expenses in MPSERS. The reserve for administrative expenses is funded from the reserve for undistributed investment income.

18. Who is W. Alan Wilk and why is he listed on the Form 2848?

W. Alan Wilk is an attorney with the Dykema Law Firm that assists MPSERS with federal tax matters as a Special Assistant Attorney General. He has worked with the IRS on the MPSERS 3% contribution matters for several years and originally assisted in submitting a Private Letter Ruling (PLR) Request on this issue in both 2016 on behalf of MPSERS and 2018 on behalf of DeWitt Public Schools. It was the PLR Request that has resulted in the proposed Closing Agreement.

19. Is ORS, Mr. Wilk or Dykema acting as counsel for the Reporting Units?

ORS has been very clear that, beyond representing a Reporting Unit as provided in Form 2848 to sign the Closing Agreement once a Reporting Unit makes a decision to participate or not, neither ORS nor the Dykema Law Firm are providing any legal counsel to any Reporting Unit regarding that decision of whether to be part of the Closing Agreement or any other matters related to the proper tax treatment of employer and employee contributions made to the MPSERS Health Care Trust. Reporting Units are encouraged to consult with their own legal, tax and accounting professionals to form their own conclusions based on their own facts and circumstances.

20. Does listing Mr. Wilk on the Form 2848 mean he is our attorney?

A Form 2848 is used to authorize an individual to represent you before the IRS in a matter that is specifically named on the Form 2848, which in this case is limited to the signing of the Closing Agreement, if a Reporting Unit chooses to participate. He is listed as an attorney because an authorized individual must be eligible to practice before the IRS, and a licensed attorney is one of the many categories (accountants, actuaries, employees, officers, etc.) that are eligible. He is not engaged as your attorney for any legal advice, and you should consult your own attorney to decide whether or not to participate in the Closing Agreement. Based on your own counsel's advice, he may be authorized via the Form 2848 to sign the Closing Agreement on your behalf.

21. Will we be charged any fees by ORS or Dykema for their involvement in the Closing Agreement?

No. Neither ORS nor Dykema are charging any fees to Reporting Units for helping to facilitate the signing of the Closing Agreement for those Reporting Units who choose to participate.

22. Why does the Form 2848 that was provided included partially completed information that states that the time frame is 2013-2026?

The Form 2848 was originally drafted to include only the dates when the Closing Agreement was being discussed, which was 2019-2021. Upon review of a draft Form 2848 with that time frame by the IRS, the IRS asked that the time frame be updated to reflect 2013-2026. ORS subsequently updated the time frame on the Form 2848. ORS understands that the time frame reflects what the IRS anticipates to be covered by the Closing Agreement, which are those contributions subject to the election window that closed in 2013 (which began as early as PA 300 of 2012 became effective on September 4, 2012).

23. Why is 2026 being contemplated as the end date of the time frame for the Closing Agreement?

As stated in the Treasury Regulation cited above, a Closing Agreement may be in respect of any internal revenue tax for any taxable period ending prior or subsequent to the date of such agreement. In this case, the IRS has indicated that it is willing to issue the Closing Agreement for the prior time periods as indicated and for an additional 5 Years, which would be until 2026. Initial discussions also included no additional time periods and a time period of 1 year, but the last indications were for an additional 5 years. Additionally, upon inquiry, there was no indication that the IRS decision on this matter would be changing effective in tax year 2027, even though further time frames would not technically be covered by the Closing Agreement.

24. Is there a conflict with ORS or Dykema's involvement in the Closing Agreement process?

ORS and Dykema (as ORS counsel) have been involved in this matter from the beginning, including an initial request in 2016 on behalf of MPSERS to have the IRS make a determination as to the income and FICA tax status of the MPSERS 3% contributions by MPSERS participants (Reporting Unit employees). They were then involved in this matter with DeWitt Public Schools, which stepped up to be a representative Reporting Unit in a subsequent and almost identical request in 2018. From a general review, the operative paragraphs of the Closing Agreement appear to resolve these tax matters favorably for the Reporting Units and employees. But as has been made clear, each Reporting Unit should review its own facts and circumstances to decide whether it wants to participate in this Closing Agreement. If any Reporting Unit is uncomfortable with any perceived conflict with ORS or Dykema's involvement, or based on their own individuals reasons, they are not required to participate.

25. Will ORS submit the Form 2848 for each Reporting Unit?

Yes, those Reporting Units that wish to participate in the Closing Agreement can submit their Form 2848 to ORS as provided in the December 22, 2020 notice, and ORS will forward all of them to the IRS following the deadline to submit them.

26. Is it possible that the February 5, 2021 deadline can be extended to accommodate a Reporting Unit that needs to take action to approve participation, but cannot do so until after the current deadline?

Yes, the new deadline is March 1, 2021. ORS heard feedback from many Reporting Units that want their respective boards to be able to meet to deliberate whether to participate in the Closing Agreement. Most reports were that those boards have regular meetings scheduled in February in which they wanted to address this matter. As such, the extended deadline should accommodate those Reporting Unit requests. If a Reporting Unit knows that it wants to participate in the Closing Agreement but cannot meet the new deadline, that Reporting Unit should contact ORS to discuss their anticipated date of approval.

For those Reporting Units that know that they would like to participate, they are encouraged to get their Form 2848 submitted as soon as possible after approval.

27. May a Reporting Unit sign onto the Closing Agreement after it has been signed?

Based on conversations with the IRS, ORS believes this answer is no. It is understood that only the Reporting Units that sign a Form 2848 and have their reduced filing fee paid by ORS will be covered by this Closing Agreement. A Reporting Unit, however, might in the future be able to submit and participate in its own Closing Agreement that it pays for and negotiates with the IRS.

28. Has the IRS stated when it anticipates generating a completed Closing Agreement for your execution on behalf of each participating Reporting Unit?

No, the IRS has not provided a specific date or time frame following the submission of the Form 2848s and payment of the filing fee. As such, ORS continues to encourage Reporting Units to consult with their own professionals to maximize any limitations periods, especially if they anticipate that any delay in generating the Closing Agreement may impact the timing of any action required, including those to obtain refunds for the employer and employee.

29. How will each participating Reporting Unit's participation be denoted on the Closing Agreement?

While the final form of the Closing Agreement has not been disclosed, it has been discussed with the IRS and the initial response is that each Reporting Unit to be covered by the Closing Agreement will likely be listed on an Addendum to the Closing Agreement.

30. Why would a Reporting Unit choose to participate in the Closing Agreement?

Again, ORS is not providing any advice as to whether to participate or not. ORS is aware, however, that some counsel for Reporting Units have indicated that (1) if a Reporting Unit treated the 3% contributions deducted as subject to income and FICA taxes at any time during 2012-present, the Closing Agreement may present the opportunity to take corrective action and obtain a refund of the FICA tax paid by the Reporting Unit [depending on the facts and circumstances as to whether and how any claims were handled at a particular reporting unit]; (2) if a Reporting Unit treated the 3% contributions deducted as exempt from income and FICA taxes, the Closing Agreement will reflect the IRS position that such

treatment was appropriate; and (3) in either case, the Closing Agreement confirms the IRS treatment of the 3% contributions through the end date of the Closing Agreement (which is proposed to be 2026).

31. Why would a Reporting Unit choose not to participate in the Closing Agreement?

Again, ORS is not providing any advice as to whether to participate or not. ORS is aware, however, that some representatives for Reporting Units have indicated that a Reporting Unit might not want to participate if (1) the Reporting Unit deems the administrative time and cost required to participate in the Closing Agreement outweighs its benefits; (2) if the Reporting Unit has consistently treated the 3% contribution as exempt from income and FICA taxes and/or they do not believe the IRS will take a contrary position for their Reporting Unit; (3) they do not want MPERS to expend \$3,000 on their behalf; (4) the Reporting Unit is not comfortable with not seeing the full contents of the Closing Agreement; (5) the Reporting Unit is not comfortable participating in the Closing Agreement that ORS and DeWitt Public Schools (or their counsel) were involved with; or (6) the Reporting Unit is not comfortable with certain terms of the Closing Agreement.

32. What do I do if I have additional questions?

ORS encourages you to contact your legal counsel to discuss any specific facts and circumstances related to your Reporting Unit.

If you have any questions related to the Form 2848 submission or generally about the Closing Agreement process, please contact ORS_Web_Reporting@michigan.gov.