Section 105.—Amounts Received Under Accident and Health Plans

Accident and health plans. This ruling clarifies that amounts reimbursed under a self-insured medical expense reimbursement plan for medical expenses incurred by an employee prior to the adoption of the plan are not excludable from the gross income of the employee under section 105(b) of the Code.

Rev. Rul. 2002–58

ISSUE

Whether amounts reimbursed under a self-insured medical expense reimbursement plan for medical expenses incurred by an employee prior to the establishment of the plan are excludable from the gross income of the employee under section 105(b) of the Internal Revenue Code.

FACTS

Employer M establishes a self-insured medical expense reimbursement plan on December 1 of a year. The plan provides that it is effective as of January 1 of that year. Under the plan, a participating employee is eligible for reimbursement of medical expenses incurred by the employee, the employee's spouse, and dependents (as defined in section 152) during the plan year (January 1 through December 31). Employee A becomes a participant in the plan upon its establishment on December 1.

Prior to the establishment of the plan, Employee A had incurred medical expenses that qualify for reimbursement under the plan and submits those claims for reimbursement to the employer in December. M reimburses A for the medical expenses incurred prior to the establishment of the plan in accordance with the terms of the plan.

LAW AND ANALYSIS

Section 61(a) provides that, except as otherwise provided by law, gross income means all income from whatever source derived.

Section 105(a) provides that, generally, amounts received by an employee through accident or health insurance for personal injuries or sickness shall be included in gross income to the extent such amounts (1) are attributable to contributions by the employer which were not includible in the gross income of the employee or (2) are paid by the employer.

However, section 105(b) provides an exception to the general rule of inclusion under section 105(a). Section 105(b) provides that gross income does not include amounts paid, directly or indirectly, to the taxpayer to reimburse the taxpayer for expenses incurred by him for the medical care (as defined in section 213(d)) of the taxpayer, his spouse, and his dependents (as defined in section 152).

Section 105(e) provides that amounts received under an accident or health plan for employees will be treated as amounts received through accident or health insurance for purposes of sections 105(a) and (b). Section 1.105–5(a) of the Income Tax Regulations provides that an accident or health plan is an arrangement for the payment of amounts to employees in the event of personal injuries or sickness.

In Rev. Rul. 71–403, 1971–2 C.B. 91, an employer established a plan for its employees that qualified as an accident and health plan. All of the employees were covered under the plan and had an enforceable right to be reimbursed for medical expenses from and after the inception of the plan, but not before the inception of the plan. A number of the employees were absent from work on account of personal injury or sickness when the plan went into effect. The ruling held that reimbursements to employees for medical expenses incurred after the inception of the employer's accident and health plan were excludable from gross income even though the employees were unable to work because of injury or sickness when the plan went into effect.

In *American Family Mutual Insurance Co. v. U.S.*, 815 F. Supp. 1206 (W.D. Wis. 1992), the employer established a medical expense reimbursement plan to which section 105 applied. The plan was established in November and made retroactive to January 1 of that same year. Employees were reimbursed for medical expenses incurred before the plan was established. The court concluded that the retroactive accident and health plan was invalid. Thus, reimbursements of medical expenses incurred prior to the establishment of the plan were includible in the employee's gross income and not excludable under section 105(b).

In *Wollenberg v. U.S.*, 75 F. Supp. 2d 1032 (D. Neb. 1999), a calendar year accident and health plan was established in December of the calendar plan year. The plan was effective from January of the plan year. The court held that reimbursements for medical expenses incurred prior to the establishment of the medical expense reimbursement plan were not excludable under section 105(b).

A self-insured medical expense reimbursement plan is treated as accident and health insurance under section 105(e). Thus, medical expense reimbursements that are paid under a plan are excludable from the employee's gross income under section 105(b). However, reimbursements of medical expenses incurred prior to the establishment of a plan are not paid or received under an accident or health plan. Therefore, those amounts are not excludable from an employee's gross income under section 105(b).

HOLDING

Amounts reimbursed under a self-insured medical expense reimbursement plan for medical expenses incurred by an employee prior to the establishment of the plan are not excludable from the gross income of the employee under section 105(b).

EFFECT ON OTHER REVENUE RULINGS

None

DRAFTING INFORMATION

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