200027059

Internal Revenue Service

Department of the Treasury

Washington, DC 20224

Uniform Issue List: 401.00-00

Contact Person:

Telephone Number:

In Reference to:

T:EP:RA:T3

Date:

Attention:

APR 11 2000

Legend:

Corporation A =

Corporation B =

Corporation C =

Department D =

Contract F =

Plan X =

Dear

This is in response to your ruling request dated July 1, 1999, submitted by your authorized representative concerning distributions from Plan X, in accordance with section 401(k) of the Internal Revenue Code (the "Code"). A letter dated July 8, 1999, supplemented the request.

Corporation A, a wholly-owned subsidiary of Corporation B maintainss Plan X. Plan X has also been adopted by other subsidiaries of Corporation B. Plan X is qualified under section 401(a) of the Code.

Corporation A's business operations are performed pursuant to a contract between Corporation A and Department D on a "cost plus award fee" basis, under which Corporation A is reimbursed by Department D for allowable contract expenses. In 1998, Corporation A determined that it needed to concentrate on its core business and to outsource the information services component of its operations to Corporation C, an unrelated corporation. This outsourcing occurred under Contract F which was entered into between Corporation A and Corporation C effective as of March 1, 1999. As a result of this agreement, Corporation

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A terminated 342 information services employees on February 28, 1999, all of whom were hired by Corporation C, effective as of March 1, 1999, to perform work for Corporation A. Contract F expires September 30, 2001, with two one-year renewal options. No sale of assets, sale of a business unit or subsidiary, or corporate reorganization was involved in the outsourcing.

Based on the projected revenues that would be paid to Corporation C, under Contract F, Corporation C determined that the level of required staffing of Contract F could be as few as 270 employees but could not exceed 300 employees. However, Contract F required Corporation C to offer employment to the 342 terminated employees of Corporation A. As a result, at some time after March 1, 1999, Corporation C had to reassign at least 42 "excess" employees to other Corporation C projects that did not involve Contract F ("non-Corporation A work").

When it assumed the computer operations, under Contract F, on March 1, 1999, Corporation C began to identify employees who could be assigned to non-Corporation A work. The training and reassignment process was anticipated by both Corporation A and Corporation C before the March 1, 1999 transition date, but could not be implemented until after such date. In the interim, all employees performed services under Contract F.

Under Contract F, Corporation C performs some of the services at Corporation A's facilities and uses computer hardware and software provided by Corporation A. Approximately 120 employees formerly employed by Corporation A, as of July 1, 1999, are employed by Corporation C at Corporation A's facilities to perform the on-site computer operations part of Contract F. It is projected that between 80 and 100 employees will be required on a regular basis to perform the on-site computer operations. With the exception of the on-site computer operators, Corporation C, not Corporation A, determines the job locations where the contract services will be performed. Other parts of Contract F, mostly software and programming requirements, are performed, as of July 1, 1999, at a facility formerly leased by Corporation A and now leased by Corporation C under a new lease, or at other Corporation C locations. Corporation C is also using the leased facility to perform similar services for non-Corporation A work.

Based on the foregoing, you request the following rulings:

1. That there has been a separation from service as defined in sections 402(e)(4)(A) and 401(k)(2)(B)(i)(I) of the Code, so as to permit a distribution under Plan X with respect to employees who, as of the date of this request and as of October 1, 1999, are performing substantially the same services and job functions for Corporation C as they performed directly for Corporation A on February 28, 1999, but with different benefits, supervisors and policies.

2. That there has been a separation from service as defined in sections 402(e)(4)(A) and 401 (k)(2)(B)(i)(I) of the Code, so as to permit a distribution under Plan X with respect to employees who, as of the date of this request, are performing services for Corporation C on non-Corporation A work exclusively, even though they did not make the change to non-Corporation A work until sometime after March 1, 1999.

3. That there has been a separation from service as defined in sections 402(e)(4)(A) and 401(k)(2)(B)(i)(I) of the Code, so as to permit a distribution under Plan X with respect to employees who, as of the date of this request, are performing services for Corporation C on Contract F, but Corporation C has determined such employees will be assigned exclusively to non-Corporation A work by October 1, 1999.

4. That there has been a separation from service as defined in sections 402(e)(4)(A) and 401(k)(2)((B))(i)(I) of the Code, so as to permit a distribution under Plan X with respect to employees who, as of the date of this request, are performing services for Corporation C, some of which are performed under Contract F and some of which are on non-Corporation A work.

5. That there has been a separation from service as defined in sections 402(e)(4)(A) and 401(k)(2)(B)(i)(I) of the Code, so as to permit a distribution under Plan X with respect to employees who have not been assigned to non-Corporation A work (in whole or in part) by October 1, 1999, but who are assigned to non-Corporation A work (in whole or in part) after October 1, 1999.

Section 401(k)(2)(B)(i) of the Code provides, in relevant part, that distributions from a qualified cash or deferred arrangement may not be made earlier than the occurrence of certain stated events. Section 401(k)(2)(B)(i)(I) further provides that one of these distributable events is "separation from service".

Revenue Ruling 79-336, 1979-2 C.B. 187 provides that an employee will be considered separated from service within the meaning of section 402(e)(4)(A) of the Code only upon the employee's death, retirement, resignation, or discharge, and not when the employee continues on the same job for a different employer as a result of the liquidation, merger, or consolidation, etc. of the former employer (i.e. the "Same Desk Rule"). Revenue Ruling 80-129, 1980-1 C.B. 86 extended this rationale to situations where an employee of a partnership or corporation, the business of which is terminated, continues on the same job for a successor employer formed to continue the business.

In this case, the issue is whether the Same Desk Rule should be applied to the employees who are discharged by Corporation A and reemployed by Corporation C. Although there is no liquidation, merger, transfer of corporate assets or other similar corporate transaction associated with the discharge of those employees, and Corporation A is not related to Corporation C, there is an ongoing relationship between Corporation A and Corporation C through the outsourcing agreement (Contract F). Contract F provided that the 342 employees would move from Corporation A's payroll to Corporation C's payroll and provide services back to Corporation A. Also, on March 1, 1999, the inception of the subject outsourcing, all of the 342 former employees of Corporation A were providing services for Corporation A under Contract F. Thus, the Same Desk Rule should be applied to all these employees. In applying the same desk rule, it is not relevant that employees perform different services and job functions for Corporation C after March 1, 1999, than they were performing for Corporation A.

Accordingly, based on the facts presented, we conclude, with respect to your ruling requests that there has not been a separation from service as defined in sections 402(e)(4)(A) and 401(k)(2)(B)(i)(I) of the Code, from Corporation A, with respect to all the employees described in ruling requests one through five.

The above rulings are based on the assumption that Plan X will be otherwise qualified under sections 401(a) and 401(k) of the Code, and the related trust will be tax exempt under section 501(a) at the time that the above transaction takes place.

This ruling is directed only to the taxpayer who requested it and applies only to Plan X as proposed to be amended as of the date of this ruling. Section 6110(j)(3) of the Code provides that this ruling may not be used or cited as precedent

A copy of this letter has been sent to your authorized representative in accordance with a power of attorney on file in this office.

Sincerely yours,

Frances V. Sloan

Frances V. Sloan, Manager
Employee Plans, Technical Group 3
Tax Exempt and Government Entities Division

Enclosures:
Deleted copy of letter
Notice of Intention to Disclose

CC: