Internal Revenue Service

Department of the Treasury

Washington, DC 20224 200105064

Contact Person:

Telephone Number:

S.I.N. 0401.29-02

In Reference to: T:EP:RA:2

Date: NOV 07 2000

Legend

Company M =
Division N =
Product Line O =
Division P =
Plan X =
City Y =
City Z =

Dear :

This is in response to the ruling request dated March 29, 2000, as supplemented by letters dated August 2, 2000, and October 2, 2000, in which your authorized representative has requested a ruling on your behalf concerning whether distributions to former employees will adversely affect the tax treatment of salary deferrals made to Plan X.

Your authorized representative has submitted the following facts and representations:

Company M sponsors Plan X, a profit sharing plan qualified under section 401(a) of the Internal Revenue Code and whose related trust is exempt from tax under section 501(a) of the Code. It provides employee salary deferrals under section 401(k). Company M is comprised of several divisions, one of which is Division N, and the other, Product Line O, of Division P. Division N and Product Line O have been sold to third parties who are continuing the respective businesses utilizing former Company M employees who were transferred pursuant to the sales. All employees transferred were participants in Plan X. Company M and the third party purchasers are not members of the same controlled group as the term is defined under sections 414(b) and (c), are not members of the same affiliated service group as defined in section 414(m), and are not entities defined in section 414(o).

Division N produced vision systems for packaging systems and maintained its own separate management, accounting and financial functions. In addition, it was responsible for its own advertising, hiring and, firing. The sale was of one hundred percent of Division N's assets, including its manufacturing and office facilities in City Y. All the employees of Division N were terminated from Company M's employment by the sale of assets and all were re-employed by the

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third party.

Product Line O manufactured electro-mechanical controls for direct current electric motors. Of the approximately 130 employees of Division P, Product Line O employed 26 people, 4 of whom were in administration and sales, and the remaining 22 of whom were manufacturing personnel. Product Line O was housed in a separate part of a larger factory building which connected other facilities of Division P. Product Line O utilized its own processing lines, and its personnel occupied areas separate and apart from Division P's operations. While Product Line O's personnel had the power to hire and fire, the financial, human resources, and advertising functions were handled for Product Line O by the employees of Division P. Although Division P's employees provided Product Line O with its financial reports, they were based solely on Product Line O's operations. The asset sale was of one hundred percent of Product Line O's assets, including all of Product Line O's inventory and manufacturing equipment, which was located in City Z. All of the employees were terminated from Company M's employment and were re-employed by the third party.

Company M will continue to sponsor Plan X for its remaining employees. Further, it intends to by the end of the second year following the effective date of the respective transactions distribute all of the funds to those employees who were employed by the third parties. The distributions of all the affected participants' accounts will be made within one taxable year.

Based on these facts and representations, a ruling is requested to the effect that the distributions of the 401(k) account balances in the two situations discussed above to the employees who were re-employed by the respective buyers will not adversely affect the tax treatment of salary deferrals as described in section 402(e)(3) of the Code under Plan X by reason of section 401(k)(10)(A)(ii).

Section 402(e)(3) of the Code provides that contributions by an employer on behalf of an employee to a trust which is a part of a qualified cash or deferred arrangement (as defined in section 401(k)(2)) shall not be treated as distributed or made available to the employee merely because the arrangement includes provisions under which an employee may elect whether contributions to the trust will be made to the trust or received in cash.

Section 401(k)(2)(B)(i) of the Code provides, in relevant part, that amounts attributable to employer contributions and made pursuant to an employee's election may not be distributed from a qualified cash or deferred arrangement earlier than the occurrence of certain stated events, including those described in section 401(k)(10)(A). Section 401(k)(2)(B)(i)(II), when read together with section 401(k)(10)(A)(ii), provides that one of the events that may trigger such a distribution is the disposition by a corporation of substantially all of the assets used by such corporation in the operation of a trade or business. However, such a distribution may be made

only with respect to an employee who continues employment with the corporation acquiring such assets.

Section 401(k)(10)(B) of the Code generally provides that an event shall not be treated as described in section 401(k)(10)(A) with respect to any employee unless that employee receives a lump sum distribution within the meaning of section 402(e)(4)(D) (without regard to subclauses (I) (II) (III) and (IV) of clause (i) therefore) by reason of the event.

Section 402(e)(4)(D) of the Code provides, in relevant part, that the term "lump sum distribution" means the distribution or payment within 1 taxable year to the recipient of the balance to the credit of an employee.

Section 1.401(k)-1(d)(1) of the Income Tax Regulations provides, in relevant part, that amounts attributable to elective deferrals may not be distributed from a cash or deferred arrangement before the occurrence of stated events and provides that one such event is the sale or other disposition by a corporation of substantially all its assets used in a trade or business by the corporation to an unrelated entity or individual. Section 1.401(k)-1(d)(4)(iv) states that, for purposes of section 1.401(k)-1(d)(1)(iv), the sale or disposition of "substantially all" the assets used in a trade or business means the sale or disposition of at least 85% of the assets.

Section 1.401(k)-1(d)(4) of the regulations provides additional rules applicable to distributions upon the sale of assets. Section 1.401(k)-1(d)(4) of the regulations provides, in part, that (i) the seller must maintain the plan, and the purchaser may not maintain the plan after the disposition, (ii) the employee must continue employment with the purchaser of the assets, and (iii) distribution must be in connection with the disposition of assets. Section 1.401(k)-1(d)(4)(iii) provides, in part, that except in unusual circumstances, a distribution will not be treated as having been made in connection with a disposition unless it was made by the end of the second calendar year after the calendar year in which the disposition occurred.

The facts and representations submitted show that Division N maintained its own separate management, accounting, and financial functions. It also was responsible for its own advertising, hiring, and firing. On this basis, we conclude that Division P constituted a trade or business within the meaning of section 401(k)(10)(A)(ii) of the Code.

With respect to Product Line O, the information and representations show that although Division P's employees handled Product Line O's financial, human resources, and advertising functions, Product Line O's personnel had the power to hire and fire personnel. It also utilized its own processing lines, and its personnel occupied areas separate and apart from Division P's operations. Finally, while Division P's employees provided Product Line O with financial reports, these reports were based solely on Product Line O's operations. On this basis, we also conclude

that Product Line O constituted a trade or business within the meaning of section 401(k)(10)(A)(ii) of the Code.

The information and representations submitted show that (1) that Company M sold all of the assets of Division N and Product Line O, which entities constituted trades or businesses, to unrelated third parties, (2) the employees who became employees of the unrelated third parties as a result of the purchase were hired to perform the same service that they performed for Division N and Product Line O, (3) Company M continues to maintain Plan X after the sale of Division N and Product Line O, and (4) the lump sum distributions from Plan X that will be made in connection with the disposition that resulted in the employees transfer to the unrelated third parties will be distributed to these employees by the end of the second year following the effective date of the respective transactions.

On this basis, we conclude that the effect of the distributions of the 401(k) account balances in the two situations discussed above to the employees who were re-employed by the respective buyers will not adversely affect the tax treatment of salary deferrals as described in section 402(e)(3) of the Code under Plan X by reason of section 401(k)(10)(A)(ii).

This ruling is based on the assumption that Plan X is qualified under sections 401(a) and 401(k) of the Code at all times pertinent to this ruling request.

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

(signed) JOYCE E. FLOYD

Joyce E. Floyd, Manager
Employee Plans Technical Group 2
Tax Exempt and Government
Entities Division

Enclosures:
Deleted copy of the letter
Notice 437

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