

Internal Revenue Service

Department of the Treasury

199951047

Washington, DC 20224

Uniform Issue List No.: 401.00-00

Contact Person:

Telephone Numt:

In Reference to:

OP:E:EP:T:4

Date:

SEP 29 1999

Attention:

Legend:

Company A =

Company B =

Company C =

Division D =

Division E =

Division F =

Unit G =

Unit H =

Plan X =

Dear

This is in response to a ruling request submitted on your behalf by your authorized representative in a letter dated July 27, 1998 and supplemented by additional correspondence dated December 3, 1998, and December 14, 1998 concerning the Federal income tax consequences of a proposed transaction under section 401(k)(10)(A)(ii) of the Internal Revenue Code ("Code").

The following facts and representations have been submitted on your behalf.

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Company A is engaged primarily in providing a full range of medical delivery systems and managed health care. Directly and through its subsidiaries, Company A offers (i) group, individual, Medicaid and Medicare health maintenance organization ("HMO") and preferred provider organization ("PPO") plans; (ii) government sponsored managed care plans; (iii) managed care services related to administration and cost containment; (iv) insurance products; and (v) behavioral health, dental, vision and pharmaceutical services.

Company A has divided its operations into six divisions through which it operates its various business lines. Three of the divisions are regional operational divisions through which Company A conducts its PPO and HMO health plan operations. Company A operates other business lines through Divisions D, E, and F. Division D oversees the behavioral health, dental, vision and pharmaceutical operations, as well as managed care services related to administration, bill review and cost containment provided to hospitals and other entities. Division E oversees the operation of a full-serviced managed and insured workers' compensation program and the provision of uninsured workers' compensation administrative services. Division F oversees the administration of contracts entered into by Company B, an indirect wholly owned subsidiary of Company A, with (i) the federal government to provide health care services for individuals covered by the federal health care program, Civilian Health and Medical Program of the Uniformed Services ("CHAMPUS"), and (ii) certain states to provide administrative services only with respect to their managed Medicaid health care programs.

Company B's business operations are divided into two business units. Unit G administers the contracts with the federal government to provide health care services for individuals covered by CHAMPUS in certain states. Unit H administers the "administrative services only" contracts with various states regarding the states' managed Medicaid programs.

Unit H (i) assists each state with which it has an "administrative services only" contract in selecting organizations unaffiliated with Company A and its subsidiaries to provide health care services under the state's Medicaid program and (ii) provides claims processing, customer service, medical management and other administrative services to the health care services organizations selected by the state. Unit H performs services for four states pursuant to a Medicaid enrollment services contract entered into between Company B and the applicable state. A contract with a fifth state lapsed as of December 1997 and was not renewed. The services provided pursuant to each Medicaid enrollment services contract varies depending upon the applicable state laws and procedures for each state's Medicaid program. As of September 8, 1997, 340 employees were employed in performing services under the contracts with the four states.

Unit H is operated in locations that are separate from the other operations of Company A and its subsidiaries. Unit H has its own management employees who are responsible for its day-to-day operations and personnel decisions. However, senior management employees of Company A at Division F and at Company A's headquarter facilities responsible for payroll and certain human resources functions for Company A and its subsidiaries provide some services for Unit H. Payroll and accounts payable for Unit H are processed at Company A's headquarters out of Company B's bank account and the related checks identify Company B as the payor.

Unit H has separate operations in each state for which it provides administrative services, and each state operation has a separate workforce. Each state operation separately accounts for its operations and separately reports to Division F. Each state operation maintains separate accounts and has its own annual budget which was developed by the individual state operation and approved by Division F.

Company A maintains Plan X, a profit sharing plan containing a cash or deferred arrangement within the meaning of section 401(k) of the Internal Revenue Code ("Code"), for its employees and the employees of members of its controlled group. Plan X received a favorable determination letter dated March 10, 1998. A wholly owned subsidiary of Company A maintained a qualified 401(k) plan which received a favorable determination letter dated January 18, 1997. The two plans were merged effective April 2, 1998. Company A is in the process of preparing a determination letter request for the merged Plan.

As of December 24, 1997, Company B sold substantially all the assets of Unit H to Company C, an entity unrelated to Company A and its subsidiaries. All employees of Unit H were offered employment with Company C. No terminated employee was offered employment by Company A or another member of its controlled group. Employees who accepted employment with Company C continued to render substantially the same services as they did for Unit H.

In accordance with the provisions of Plan X, which permit lump sum distributions upon the sale or other disposition of substantially all the assets to an unrelated corporation, Company A desires to make lump sum distributions to employees who accepted employment with Company C.

Your authorized representative further represents: (1) that Company C has never participated in Plan X; (2) Company A has continued to maintain Plan X after the sale of Unit H; and (3) that lump sum distributions from Plan X will be made only if any applicable consent or election required under section 411(a)(11) or section 417 of the

Code is obtained, as required under section 1.401(k)-1(d)(6)(v) of the Income Tax Regulations.

Based on the foregoing facts and representations, your authorized representative has requested the following rulings:

(1) That the sale of substantially all the assets of Unit H by Company B is the disposition of substantially all the assets used by Company B in a trade or business within the meaning of section 401(k)(10)(A)(ii) of the Code, and as a result lump sum distributions by Plan X of the benefits attributable to salary deferral contributions made pursuant to the election of a Unit H employee who has become an employee of Company C in connection with the sale of Unit H are made in accordance with section 401(k)(2)(B) of the Code.

(2) That lump sum distributions made from Plan X to Unit H employees who have become employees of Company C in connection with the sale of Unit H will not adversely affect the tax treatment of salary deferrals to Plan X under section 402(e)(3) of the Code.

Section 402(e)(3) of the Code provides that contributions made 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 nor as contributions made to the trust by the employee merely because the arrangement includes provisions under which the employee has an election whether the contribution will be made to the trust or received by the employee in cash.

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)(II) of the Code, when read together with section 401(k)(10)(A)(ii) of the Code, further provides that one of these stated events is the disposition by a corporation of substantially all of the assets (within the meaning of section 409(d)(2)) used by such corporation in a trade or business of such corporation, but only with respect to an employee who continues employment with the corporation acquiring such assets.

Section 1.401(k)-1(d)(1) of the Regulations provides, that a CODA satisfies (d)(1) only if amounts attributable to elective contributions may not be distributed before the occurrence of one of the events stated in (d)(1)(i) through (d)(1)(iv), and the distributions so permitted also satisfy paragraphs (d)(2) through (d)(6) (to the extent applicable).

The event described in section 1.401(k)-1(d)(1)(iv) of the Regulations is the date of the sale or other disposition by a corporation of substantially all the assets (within the

meaning of section 409(d)(2)) used by such corporation in a trade or business of such corporation to an unrelated corporation.

Section 1.401(k)-1(d)(4)(iv) of the Regulations states that, for purposes of section 1.401(k)-1(d)(1)(iv), the sale of "substantially all" the assets used in a trade or business means the sale of at least 85 percent of the assets.

Section 1.401(k)-1(d)(6)(v) of the Regulations provides that a distribution may be made under section 1.401(k)-1(d) only if any consent or election required under section 411(a)(11) or 417 is obtained.

It has been represented that Unit H operates in locations that are separate from the other operations of Company A and its subsidiaries and is engaged in providing particular services to certain states. Unit H has its own management employees who are responsible for day-to-day operations and personnel decisions. Each state operation of Unit H (1) has a separate workforce, (2) separately accounts for its operations, (3) maintains separate accounts, and (4) has its own budget.

Regarding the first ruling request, based on all the facts and circumstances presented, we have determined that Unit H constituted a trade or business of Company B within the meaning of section 401(k)(10)(A)(ii).

It is further represented that Company B sold more than 85% of the assets of Unit H to Company C. All employees of Unit H were offered reemployment by Company C.

Accordingly, with regard to the first ruling request, we conclude that the sale by Company B of Unit H resulted in a disposition by Company B of substantially all the assets used by it in a trade or business within the meaning of section 401(k)(10)(A)(ii) of the Code, and therefore, if the other applicable requirements set forth in section 1.401(k)-1(d)(4) through (d)(6) of the Regulations are met, lump sum distributions from Plan X to former employees of Unit H who became employees of Company C in connection with the sale of Unit H would be made in accordance with section 401(k)(2)(B) of the Code.

With regard to the second ruling request, based on our ruling on the first request, and provided all other applicable requirements set forth in section 1.401(k)-1(d)(4) through (d)(6) of the Regulations are met, we conclude that lump sum distributions from Plan X to former Unit H employees who have become employees of Company C in connection with the sale of Unit H will not adversely affect the tax treatment of salary deferrals to Plan X under section 402(e)(3) of the Code.

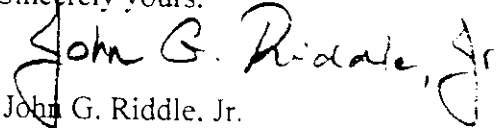
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This ruling is based on the assumption that Plan X is qualified under section 401(a) of the Code at the time of the transaction.

This ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that this private letter ruling may not be used or cited by others as precedent.

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

Sincerely yours,



John G. Riddle, Jr.
Chief, Employee Plans
Technical Branch 4

Enclosures:

- Deleted copy of letter
- Notice of Intention to Disclose
- Copy of Letters to Authorized Representatives