

Retirement Planning Opportunities

Retirement Plans and Controlled Groups

Controlled Group Status Affects Employees Included in Qualified Plan of Either Company

If your clients owns part of two or more businesses, they will have to make sure that the businesses are not considered to be controlled groups before they set up a qualified retirement plan for either of the businesses.

If the businesses are judged to be a controlled group, then all the eligible employees of both companies must be included in the coverage and participation tests for a retirement plan set up by either company.

Parent-Subsidiary Controlled Groups – Definition

There are two types of controlled groups: the parent-subsidiary and the brother-sister. The parent – subsidiary controlled groups are more common in larger companies. They occur when one company owns 80% or more of another.

Brother-Sister Controlled Group – Definition

The brother-sister controlled group is more common in the small business arena. It occurs where five or fewer individuals own 80% or more of the businesses and the same five or fewer people own over 50% of the businesses counting only identical ownership.

Brother-Sister Controlled Group - Example

Let's say that your client Richard is the only employee in his violin repair shop and would like to set up a

retirement plan just for himself in this business. His problem is that he also owns with his friend Bill a seafood restaurant that employs 20 employees. Richard doesn't want to include any of these employees in his retirement plan.

Here is the breakdown of the ownership:

Violin Repair Shop
Richard - 90%
Bill - 10%

Seafood Restaurant
Richard - 50%
Bill - 50%

Five or fewer people do own 80% or more of the businesses so the businesses pass the first test to be a controlled group.

To test for identical ownership, it is easiest to make a chart.

	Violin Shop	Seafood Restaurant	Identical Ownership
Richard	90%	50%	50%
Bill	10%	50%	10%
		Total	60%

Richard owns 90% of one business and 50% of the other so his identical ownership 50%. Bill owns 10% of one and 50% of the other so his identical ownership is 10%.

The total identical ownership (60%) is over 50% so these companies also pass the second test and are considered a controlled group.

Richard cannot set up a retirement plan for his violin repair shop without including the eligible employees from the restaurant in the plan's coverage and participation test.

What if Richard Owned 100% of the Violin Shop?

Let's say that Richard really wants a retirement plan just for himself so he buys 10% of the Violin Repair Shop from Bill. The breakdown of the ownership is now as follows:

Violin Repair Shop
Richard - 100%

Seafood Restaurant
Richard - 50%
Bill - 50%

With the new ownership percentages, the companies are no longer a controlled group, and Richard can set up a retirement plan covering just himself in the violin repair shop.

Five or fewer employees are no longer considered to own 80% of both companies because an individual must own part of both companies to be counted for the 80% rule. Since Bill no longer owns part of both companies, his ownership is not considered for the controlled group rule.

Cautionary Note

Even if the companies are not a controlled group, you should be sure that they are not an affiliated service group because that will also affect which employees must be included in the retirement plan.

Where Can You Get Additional Information?

Please feel free to contact me if you want additional information.