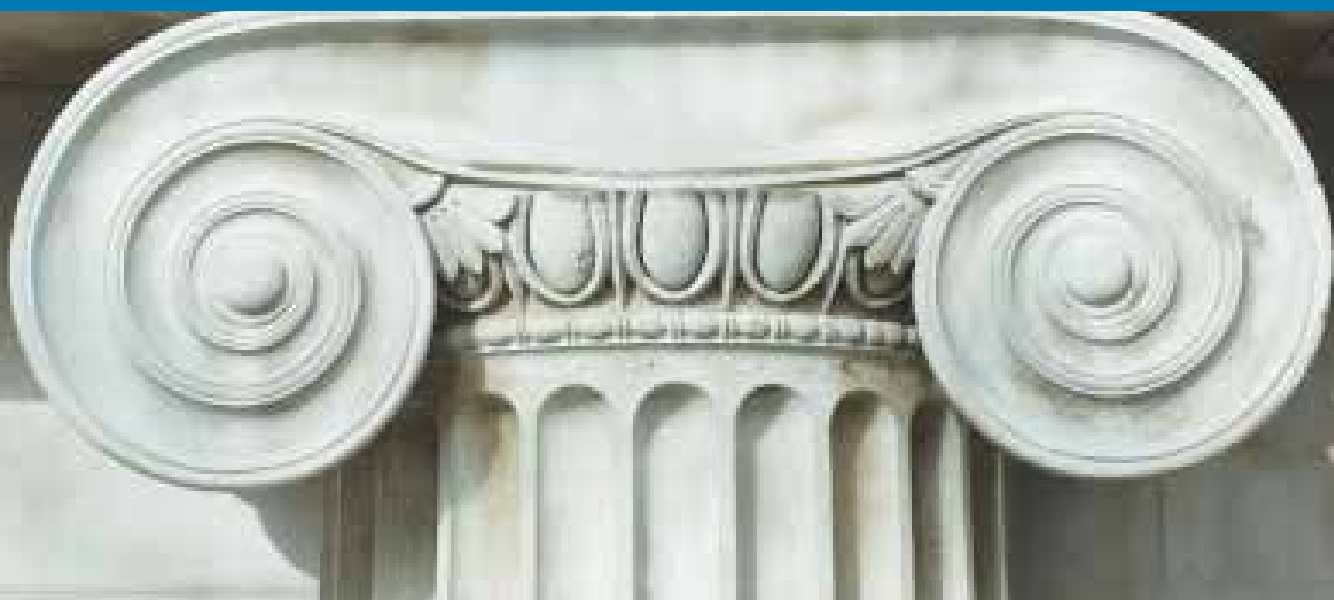


PENTEGRA TECH TIPS



Basic Controlled Group Dynamics

Effect of Being a Related Group of Employers

The effect of being a “related group of employers” under the controlled group and affiliated service group rules is that ERISA qualified plans, sponsored by one or more employer of the group must be subject to nondiscrimination testing as though these related employers were one single employer. In most cases, this means that an ERISA qualified plan sponsored by one employer must “cover” the employees of all employers in the group.

For simplicity, we refer to entities as “employers” throughout this discussion. However, it’s important to understand that an entity does not need to have employees to be considered part of a related group of employers for controlled group or affiliated service group purposes. These groupings are determined based on ownership or service relationships, not whether the entity employs individuals.

Controlled Group Rules are complicated. Employers should always seek a legal determination by their retained counsel who would be in a position to defend the determination that they render. There are of course broader rules and exemptions to be applied that are too exhaustive for this short summary. For instance, constructive ownership rules are not discussed here. Certain information below is derived from ASPPA text.

Controlled Groups – Brother/Sister Control

A Brother/Sister controlled group relationship exists when five (5) or fewer common owners satisfy both the 80% Common Control Test and a 50% Effective Control Test. The 80% Common Control Test is satisfied when the combined ownership among the common owners equals or exceeds 80% with each common owner having

FOR PLAN SPONSOR AND ADVISOR USE ONLY



some amount of ownership, including attribution among family members. The 50% Effective Control Test is satisfied if the combined identical ownership of the common owners is more than 50%. The same five or fewer common owners who were taken into account to satisfy the 80% Common Control Test must be used in the 50% Effective Control Test.

A common owner's identical ownership means the least percentage owned by that person in the businesses being tested. For example, if a person owns 25% of one business and 75% of another business, the owner's identical ownership in the two businesses is 25%.

Controlled Groups – Parent / Subsidiary Control

A Parent/Subsidiary Controlled Group exists when one employer owns 80% or more of another employer's stock (by vote or value). The ownership may extend one level below the parent or multiple levels.

For purposes of applying the limitations under IRC §415, a parent/subsidiary relationship exists when more than 50% control exists.

Affiliated Service Group - Control

An Affiliated Service Group ("ASG") is another type of "related employer group". ASG's exist when one organization regularly provides services to another organization, and an ownership interest exists between the two. There are two types of ASGs: "A-Orgs" and "B-Orgs".

An "A-Org" exists when one entity (the A-Organization) owns another organization (the First Service Organization or FSO) and the A-Org regularly performs services for the FSO. Think of two physicians who own a management group that exists to perform services for the medical practice. Any amount of ownership satisfies the ownership requirement. The "regularly performing services" element is a facts and circumstances test but think in terms of booking all appointments, managing all billing and insurance claims (in the case of a medical practice). In an "A-Org" group, both the A-Org and FSO must be a "service" organization. Revenue consisting of fees, commissions or other compensation for personal services.

A "B-Org" ASG does not require that the "B-Org" be a service organization however the FSO must still be a service organization. To be part of a B-Org group, the B-Org must satisfy all of the following;

- Derive a significant portion of its income from services provided to the FSO ("significant" is a facts and circumstances test)
- Perform services for the FSO of the type normally performed by employees
- Owned at least 10% by persons who are highly-compensated employees (HCEs) of the FSO

Managerial Group—Control

A management group consists of a recipient organization and a management organization. To be an affiliated service group, the management organization's principal business must be the performance of management functions, on a regular and continuing basis, for the recipient organization. The management group test focuses solely on the type and degree of services performed. There is no ownership requirement between the management organization and the recipient organization. Also, the HCEs of the recipient organization need not have any ownership interest in the management organization.

The law does not provide any objective test in determining whether the management organization's principal business is performing management functions for the recipient organization. In normal usage, principal means the main function, suggesting a majority (more than 50%) of the organization's business. Looking at gross receipts for management functions as compared to total receipts would be a reasonable approach.

Summary

As stated above, Controlled Groups (including ASGs and Management Groups) are complicated. When an "Owner" is seeking to exclude the employees of an "affiliated employer", great care must be taken to determine whether control, in some form or fashion, exists.

For all new business, Pentegra requires the disclosure of all ownership interest and we ask that either the Employer or their counsel state whether a controlled group exists. Pentegra's legal department will not render a legal opinion on controlled groups. However, in some instances we may provide our observation of any facts and circumstances presented. We can also provide the contact information for legal counsel we have found to be highly skilled at these determinations.

The information, analyses and opinions set out herein are for general information only and are not intended to provide specific advice or recommendations for any individual or entity. Nothing herein constitutes or should be construed as a legal opinion or advice. You should consult your own attorney, accountant, financial or tax advisor or other planner or consultant with regard to your own situation or that of any entity which you represent or advise.

For more information, contact the
Pentegra Solutions Center at solutions@pentegra.com or 855-549-6689
for expert guidance on how to make the most of the new rules.

Follow our conversation

