Farley Funeral Home, Inc. v. Commissioner, 62 T. C. 150 (1974)

Partners' past service with a predecessor partnership can be counted for eligibility purposes in a successor corporation's qualified pension plan.

Summary

Farley Funeral Home, Inc. adopted a pension plan from its predecessor partnership, allowing employees to count past service with the partnership for eligibility. The issue was whether former partners, now corporate officers, could count their partnership service for eligibility. The Tax Court held that the plan qualified under Section 401(a) and allowed partners' past service for eligibility without discrimination, as all employees were treated uniformly. This decision ensures that former partners and employees alike can utilize past service for pension plan eligibility, promoting fairness in corporate pension schemes.

Facts

Farley Funeral Home, a partnership, established a pension plan on November 2, 1966, excluding partners. The partnership incorporated on October 9, 1967, with the partners becoming officers and shareholders of Farley Funeral Home, Inc. The corporation adopted the partnership's pension plan with amendments, reducing the eligibility service requirement to one year and allowing former partners to use their service with the partnership for eligibility. Two former partners, Schimmel and Estes, were granted coverage using their past service. The Commissioner challenged the plan's qualification under Section 401(a), arguing that counting partners' service discriminated in favor of the prohibited group.

Procedural History

The Commissioner issued a notice of deficiency disallowing the corporation's deductions for contributions to the pension plan, claiming the plan did not meet Section 401(a) requirements. Farley Funeral Home, Inc. petitioned the U. S. Tax Court, which ultimately ruled in favor of the petitioner, finding the pension plan qualified under Section 401(a).

Issue(s)

1. Whether the amended pension plan qualifies under Section 401(a) of the Internal Revenue Code when it allows former partners to count their service with the predecessor partnership for eligibility to participate in the corporate plan.

Holding

1. Yes, because the plan's terms uniformly applied to all employees, including former partners, and did not discriminate in favor of the prohibited group, thus meeting the requirements of Section 401(a).

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Court’s Reasoning

The court focused on the eligibility requirements under the amended plan, which allowed all employees to count service with the predecessor partnership. The court found no discrimination in permitting former partners to use their past service for eligibility, as this treatment was uniform across all employees. The court cited IRS Publication 778 and Section 1. 401-10(b)(4) of the Income Tax Regulations, which support the use of past service for eligibility if applied uniformly. The court also referenced *United States v. Kintner* and *Sherman Construction Corporation v. United States*, where similar issues were addressed favorably. The court rejected the Commissioner’s argument that the plan must meet Section 401(d) requirements, as it was a corporate plan under Section 401(a). The decision emphasized that the plan’s aim was to treat all employees equitably, and denying former partners credit for past service would constitute reverse discrimination.

Practical Implications

This decision allows corporations to recognize former partners’ service with a predecessor partnership for pension plan eligibility, provided the treatment is uniform across all employees. It clarifies that such recognition does not inherently discriminate in favor of the prohibited group, thus maintaining the plan’s qualification under Section 401(a). Practically, this ruling encourages fairness in pension plan eligibility rules, potentially affecting how businesses structure their pension plans during transitions from partnerships to corporations. It may influence future cases involving the integration of past service into new corporate pension plans, emphasizing the importance of non-discriminatory eligibility criteria.

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