Lloyd M. Garland, M. D. , F. A. C. S. , P. A. v. Commissioner, 71 T. C. 1089 (1979)

Section 414(c) is the exclusive test for determining whether employees of related business entities must be aggregated for purposes of evaluating pension plan discrimination under sections 401(a)(4) and 410(b)(1).

Summary

In Lloyd M. Garland, M. D. , F. A. C. S. , P. A. v. Commissioner, the Tax Court ruled that section 414(c) of the Internal Revenue Code is the sole criterion for determining whether the employees of a partnership must be considered employees of an associated professional corporation for pension plan qualification purposes. Dr. Garland's professional association had a pension plan that excluded partnership employees, prompting an IRS challenge. The court held that because the association and partnership were not under common control as defined by section 414(c), the plan did not need to cover the partnership employees, thus qualifying under section 401. This decision clarified the exclusive application of section 414(c) for employee attribution in pension plan discrimination assessments.

Facts

Dr. Lloyd M. Garland established a professional association in Texas on February 1, 1973, and entered into a partnership, the Neurosurgical Unit, with Dr. Jack Dunn, Jr. The association adopted a pension plan that initially included contributions for partnership employees. After ERISA's enactment, the plan was amended to exclude these employees. The IRS issued an adverse determination, asserting that the plan discriminated in favor of Dr. Garland, a shareholder, by not covering the partnership employees. The association contested this determination, leading to the case before the Tax Court.

Procedural History

The association sought a declaratory judgment after the IRS issued a final adverse determination regarding the pension plan's qualification under section 401. The case was submitted to the Tax Court with a fully stipulated administrative record, leading to the court's decision on the applicability of section 414(c) to the case.

Issue(s)

1. Whether section 414(c) is the exclusive test for determining if the employees of a partnership must be considered employees of an associated professional corporation for purposes of sections 401(a)(4) and 410(b)(1).

Holding

1. Yes, because Congress intended section 414(c) to provide a definitive answer to

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the question of employee aggregation for evaluating pension plan discrimination, thereby clarifying and simplifying the application of antidiscrimination provisions.

Court’s Reasoning

The court’s decision hinged on the interpretation of section 414(c) and its legislative history. The court emphasized that Congress enacted this section to address the potential circumvention of antidiscrimination rules through related business entities. The committee report accompanying ERISA’s enactment underscored the intent to clarify this matter, supporting the view that section 414(c) was meant to be the exclusive test for employee attribution. The court also relied on the precedent set in Thomas Kiddie, M. D. , Inc. v. Commissioner, which established that a partner’s control over a partnership, necessary for employee attribution, requires ownership of more than a 50-percent interest. Since Dr. Garland and the association did not meet the control criteria under section 414(c), the court ruled that the partnership employees did not need to be considered employees of the association for pension plan qualification purposes.

Practical Implications

This decision provides clarity for tax professionals and employers in structuring pension plans involving related business entities. It establishes that section 414(c) is the sole criterion for determining whether employees of such entities should be aggregated for pension plan discrimination analysis. Practitioners should ensure that related entities comply with section 414(c)’s common control requirements to avoid adverse determinations. The ruling also impacts how businesses might structure their operations to maintain pension plan qualification, potentially influencing strategic decisions regarding partnerships and corporate affiliations. Subsequent cases, such as Thomas Kiddie, M. D. , Inc. v. Commissioner, have further reinforced the application of section 414(c) as the exclusive test for employee attribution in this context.

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