

## ***Sutherland v. Commissioner, 78 T. C. 395 (1982)***

Employees of failing businesses under common control may be excluded from pension plan coverage requirements when those businesses could not reasonably adopt a permanent plan.

### **Summary**

Sutherland operated a lumber business and two failing aviation companies under common control. The Commissioner rejected Sutherland's pension plans, arguing they did not meet coverage requirements when considering all employees of the controlled group. The Tax Court held that the failing aviation companies should be excluded from the coverage analysis because they could not have adopted a permanent plan in good faith. Focusing on the lumber business alone, the money-purchase plan satisfied the mathematical coverage test, while the annuity plan met the classification test. The decision underscores the importance of considering the viability of businesses within a controlled group when assessing pension plan compliance.

### **Facts**

Robert D. Sutherland owned and operated Sutherland Rocky Mountain Lumber Company, a profitable lumber business. He also owned two aviation companies, Aviation Equities and Trans-America, which were consistently unprofitable and ceased operations in 1977 and 1978, respectively. Sutherland adopted an annuity plan and a money-purchase plan for his lumber business employees in 1977. The Commissioner rejected these plans, arguing they did not meet the coverage requirements of IRC section 410(b)(1) when considering the employees of all three businesses under common control.

### **Procedural History**

Sutherland sought a declaratory judgment from the Tax Court after the Commissioner issued an adverse determination on the qualification of his pension plans. The Commissioner's determination was upheld at the District, Regional, and National Office levels before Sutherland appealed to the Tax Court.

### **Issue(s)**

1. Whether the employees of the failing aviation companies under common control with Sutherland's lumber business must be considered when determining if Sutherland's pension plans satisfy the coverage requirements of IRC section 410(b)(1).
2. Whether Sutherland's pension plans meet the coverage requirements of IRC section 410(b)(1).

### **Holding**

1. No, because the failing aviation companies could not have adopted a permanent plan in good faith due to their financial distress and impending closure.
2. Yes, because the money-purchase plan satisfied the mathematical coverage test and the annuity plan met the classification test when focusing solely on the lumber business employees.

### **Court's Reasoning**

The court applied the principle that a qualified pension plan must be a permanent program for the exclusive benefit of employees. It noted that the regulations and Revenue Rulings emphasize that a plan's permanency is indicated by the employer's ability to continue contributions. The court found that the aviation companies were unable to adopt a permanent plan due to their consistent losses and impending closure. Including their employees in the coverage analysis would be unreasonable and an abuse of discretion by the Commissioner. The court also considered the legislative history of IRC section 414(c), which aimed to prevent discrimination through separate corporate structures, but found that the facts of this case did not align with the intended evil. The court's decision was supported by the fact that the Commissioner was informed of the aviation companies' failures during the administrative process.

### **Practical Implications**

This decision allows employers with failing businesses under common control to exclude those businesses from pension plan coverage requirements if they cannot adopt a permanent plan in good faith. It emphasizes the need for a fact-specific analysis when applying IRC section 414(c). Practitioners should consider the financial viability of businesses within a controlled group when advising on pension plan compliance. This ruling may encourage employers to establish pension plans for viable businesses without the burden of failing entities, ultimately benefiting employees of the surviving concerns. Subsequent cases have cited *Sutherland* when addressing the application of IRC section 414(c) to failing businesses.