

# Controlled and Affiliated Service Groups

May 28, 2015



# Controlled and Affiliated Service Groups

- Welcome! We will begin at 3 p.m. Eastern
- There will be no sound until we begin the webinar. When we begin, you can listen to the audio portion through your computer speakers or by calling into the phone conference number provided in your confirmation email.
- You will be able to submit questions during the webinar by using the “questions” box located on your webinar control panel.



# Controlled and Affiliated Service Groups

May 28, 2015

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- RCM&D
- Roach Howard Smith & Barton
- The Rowley Agency
- Starkweather & Shepley Insurance Brokerage
- Woodruff-Sawyer & Co.
- Wortham Insurance & Risk Management



# AGENDA

- Common Control Terminology
- Parent-Subsidiary Controlled Groups
- Brother-Sister Controlled Groups
- MEWA Risk
- Affiliated Service Groups
- Broker Strategies



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# Controlled & Affiliated Service Groups

- Importance of Knowing these Concepts
  - Affordable Care Act (ACA) rules consider “the employer” to include related entities
    - “Applicable large employer” (ALE) for shared responsibility
    - Determining employer size to identify if in large or small employer market
      - Impacts eligibility for small business exchanges (SHOP)
      - Impacts application of small group market restrictions
    - Eligibility for small business health insurance tax credit
    - Cadillac tax computations
    - Annual ACA reporting under Forms 1094 and 1095
      - “Aggregated ALE group”



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# Controlled & Affiliated Service Groups

- The same ACA “employer aggregation” rules are widely used elsewhere in benefit rules under the Internal Revenue Code
  - §105(h) & ACA nondiscrimination for health plans
  - §125 cafeteria plan nondiscrimination
  - §79 group term life insurance nondiscrimination
  - Dependent care benefits nondiscrimination
  - Fringe benefit and other nondiscrimination rules
  - Qualified retirement plan rules
- Source of the primary controlled & affiliated service group rules
  - Internal Revenue Code §§414(b), (c), (m), (o) & (t)



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# Controlled & Affiliated Service Groups

- Terminology
  - Based on ownership:
    - Controlled Group of Corporations
    - Trades or Businesses Under Common Control
  - Based primarily on operational relationships
    - Affiliated Service Group
  - Generic term
    - Aggregated Employer Group
- Separate tax ID numbers (EIN, or FEIN)
  - Many purposes: Separate EIN ≠ separate employers
  - 1094/1095 reporting: Separate EIN requires separate report



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# What to Look For

- Aggregated employer group rules are complex
- Some arrangements not difficult to identify
- Others can be complicated, for example
  - Multiple family or friends sharing ownership
  - Diverse businesses independently operated
- Learn the “yellow flags” that suggest a closer look is needed
- Know when to recommend expert assistance



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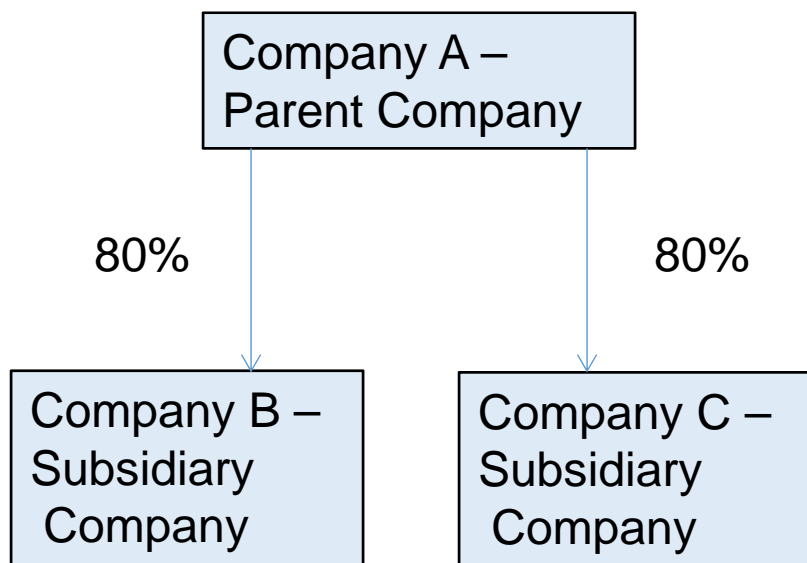




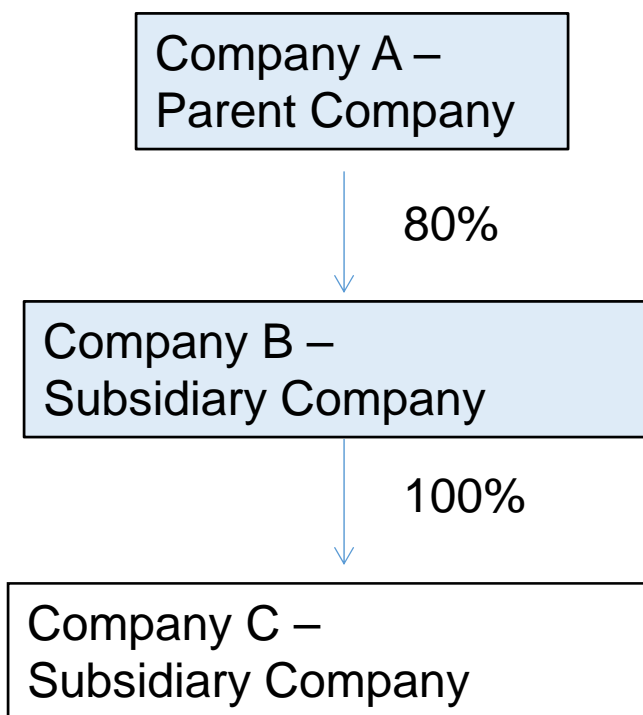
# Basic Controlled Group Structures

- “Parent-Subsidiary” Controlled Group

**General Test:** “Parent” company directly owns at least 80% of one or more other companies in the group. Simplest arrangement is a “core group.”



Shaded entities = “core group” in a parent-subsidiary group; i.e., parent and each entity 80% owned by parent



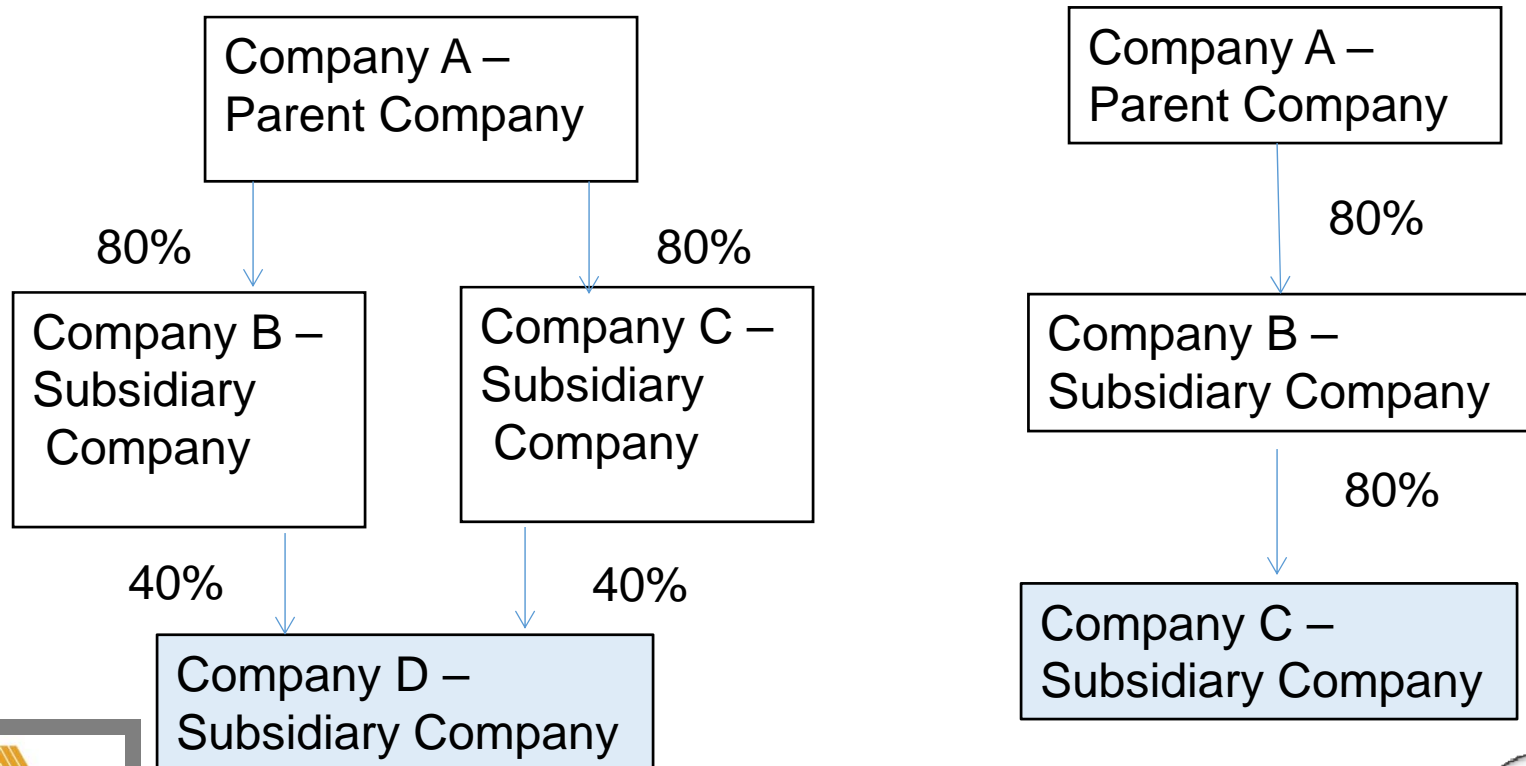
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# Basic Controlled Group Structures

- “Parent-Subsidiary” Controlled Group (*cont’d*)

**Expanding Parent-Subsidiary Controlled Group:** Include entities directly 80% owned by one or more other entities in the group. The shaded entities below are the added entities.



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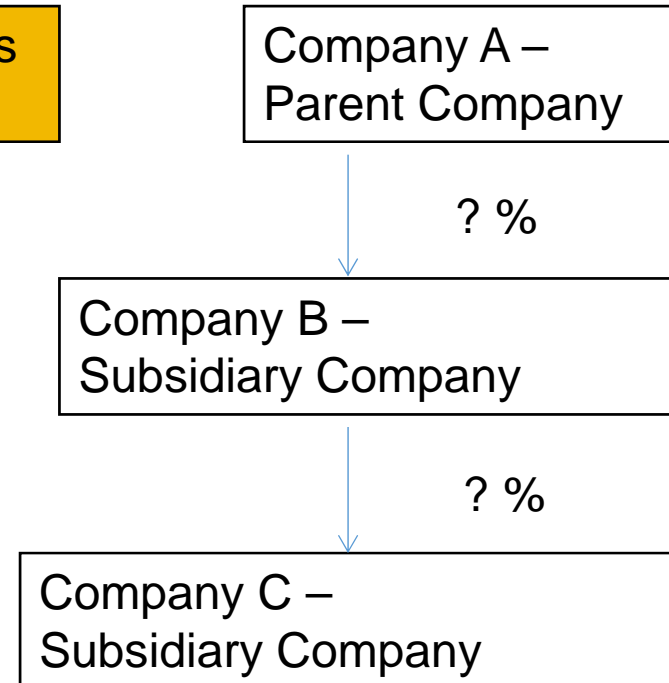


# Basic Controlled Group Structures

- “Parent-Subsidiary” Controlled Group (*Cont’d*)

**Red Flag Test:** One company directly owns at least 80% of another company

**ASK ABOUT OWNERSHIP  
OF AND BY  
ANY PARTICULAR BUSINESS**



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# “Ownership”

- Corporations
  - Voting power of all classes of voting stock , or
  - Value of all classes of stock
- Partnerships
  - Profits interest or capital interest
- Sole Proprietorship
  - The proprietor as legal owner
- Trust or Estate
  - Actuarial interest of grantor, beneficiaries, heirs, etc.
- Certain Exclusions for Treasury Stock & other Situations
  - e.g., subsidiary stock held by officer of parent company that already owns 50% of the subsidiary



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# “Ownership”

- Other Ownership Issues
  - Limited Liability Companies (LLC)
    - Follow the ownership rules for partnerships unless entity has elected to be treated as a corporation for federal tax purposes
  - Tax Exempt Organizations
    - Special rules apply to determine “common control” generally based on whether at least 80% of the directors or trustees are either representatives of or directly or indirectly controlled by another organization
    - Significant facts & circumstances analysis (control, agent, etc.)
    - “Permitted aggregation” if regularly coordinating daily exempt activity
    - Church-controlled organizations excluded from these regulations
  - Public Sector Employers
    - Reasonable good faith interpretation (for Form 1094/1095, may want to use “Designated Government Entity” option)



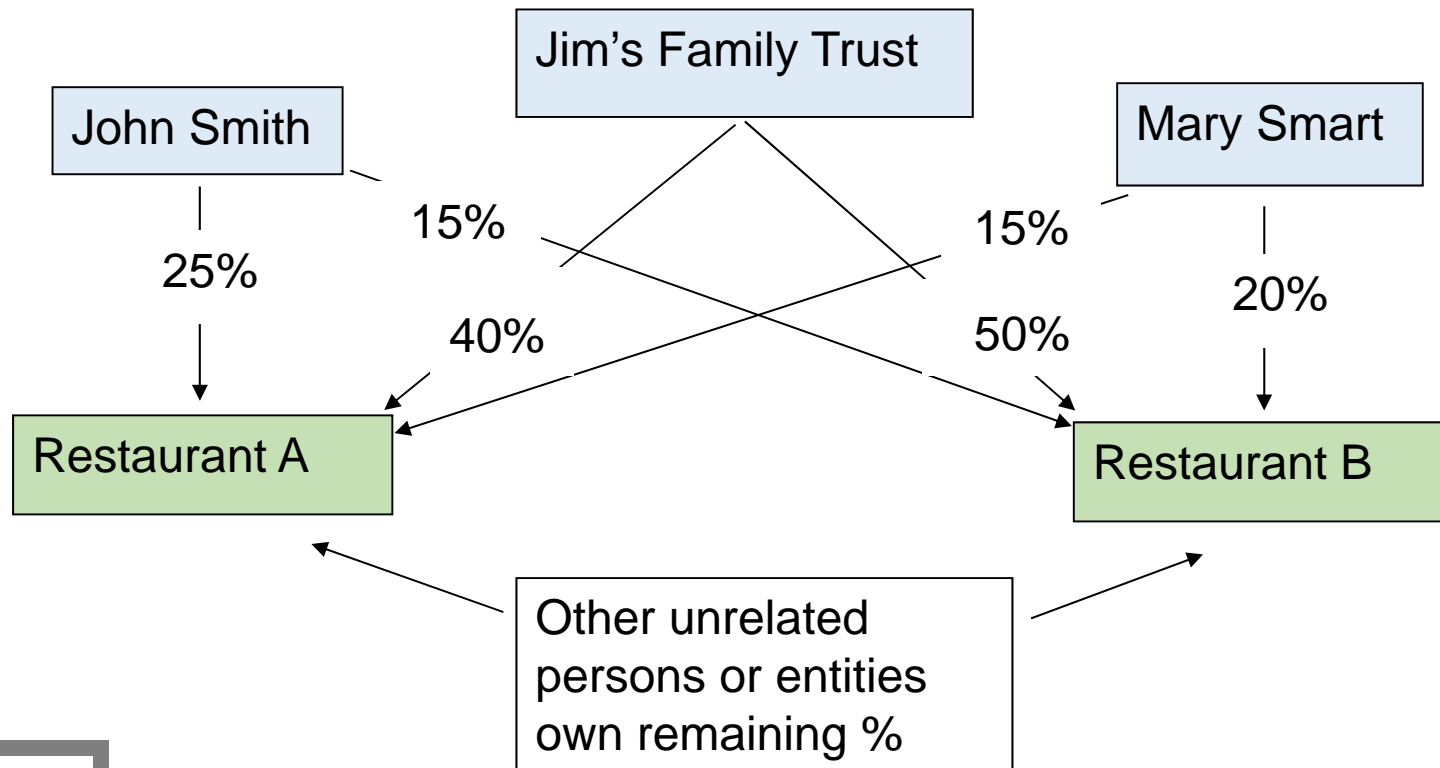
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# Basic Controlled Group Structures

- “Brother-Sister Company” Controlled Group

**General Test:** 5 or fewer individuals, estates or trusts together own, directly or by attribution at least 80% in each of two or more companies.



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# Basic Controlled Group Structures

- “Brother-Sister Company” Controlled Group (Cont’d)
- Key Principles
  - “General Control Test”
    - At least 80% control by the “5 or fewer”
  - PLUS
  - “Effective Control Test”
    - The common % that each of the “5 or fewer” individually has across all companies
    - Added to the common % of each of the other “5 or fewer”
    - Exceeds 50%
    - Counting only those with ownership in all companies



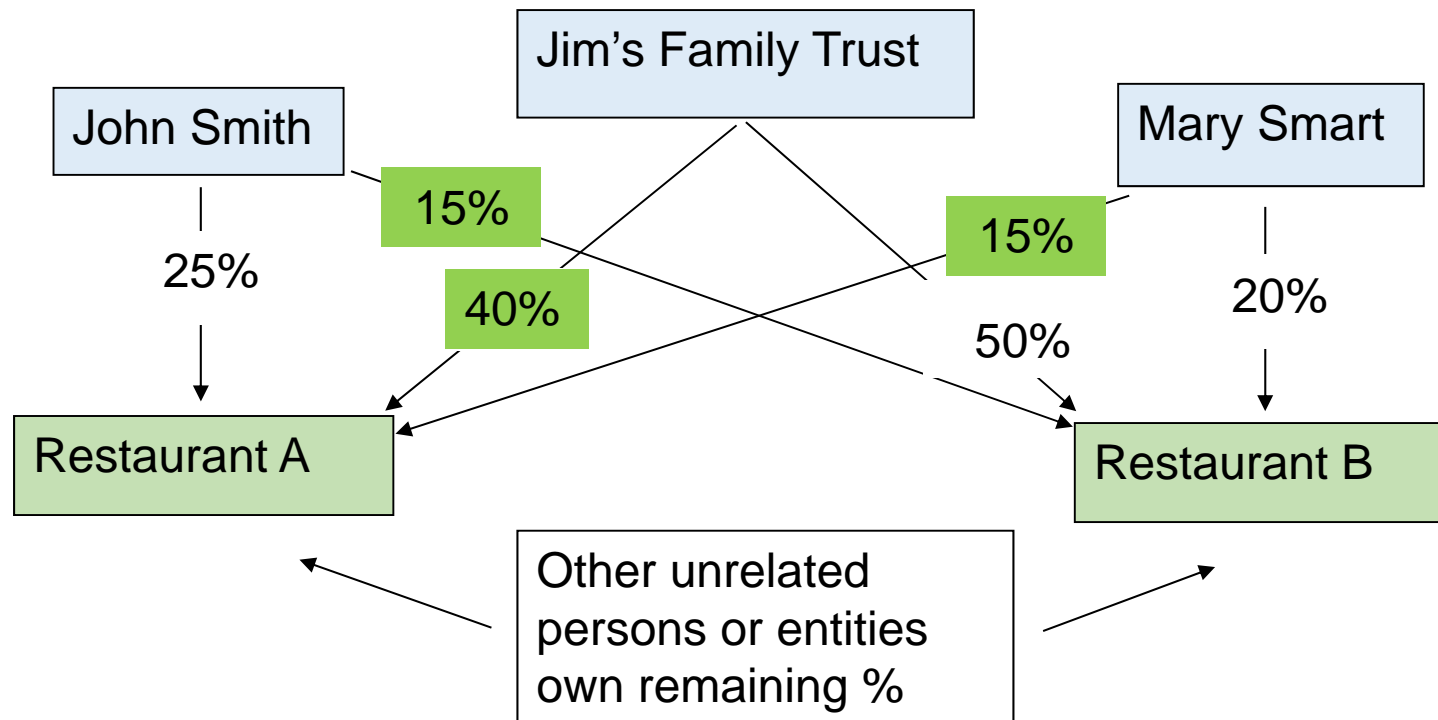
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# Basic Controlled Group Structures

## “Brother-Sister Company” Controlled Group (Cont’d)

**Effective Control Test:** Considering only the smallest % each of the 5 or fewer owns in any company, the total % of all owners exceeds 50%.



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# Basic Controlled Group Structures

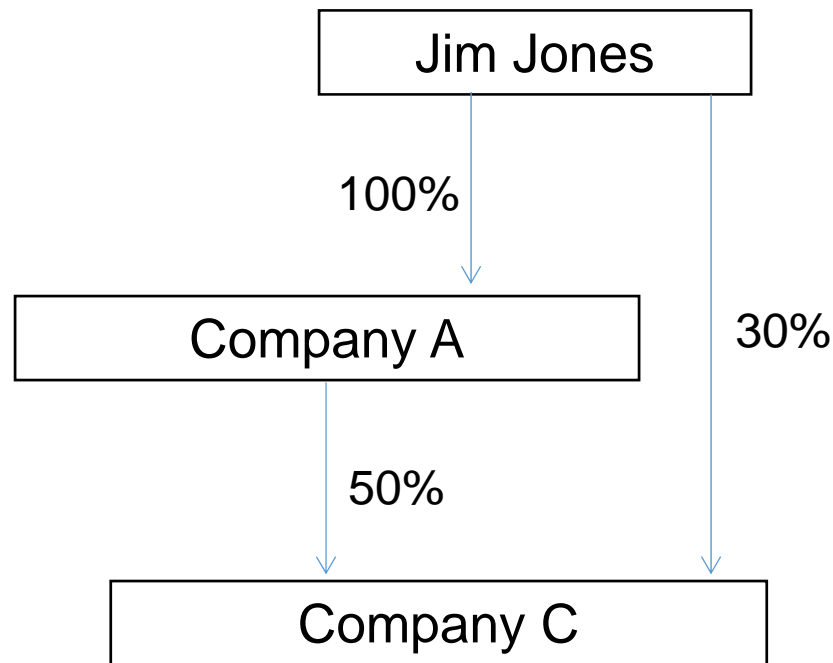
- Ownership Attribution
  - To and from parents, children, grandchildren
  - To and from spouses (includes same sex spouses)
  - To grantors and beneficiaries of trusts
  - To beneficiaries of estates
  - From companies to individuals with 5% ownership



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# Basic Controlled Group Structures



## TEST

You're consulting  
Company A.

Are A and C a  
Controlled  
Group?

**ASK ABOUT OWNERSHIP  
OF AND BY  
ANY PARTICULAR BUSINESS**



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## Brother-Sister Controlled Group

~ TEST ~	RESTAURANT 1	RESTAURANT 2	RESTAURANT 3
OWNER A	45% [20]	33%	20%
OWNER B	25% [15]	33%	15%
OWNER C	15% [15]	34%	25%
OWNER D	15% [15]	0%	40%
A, B & C OWNERSHIP	85%	100%	60%

CONTROLLED GROUP: 1 & 3 ONLY

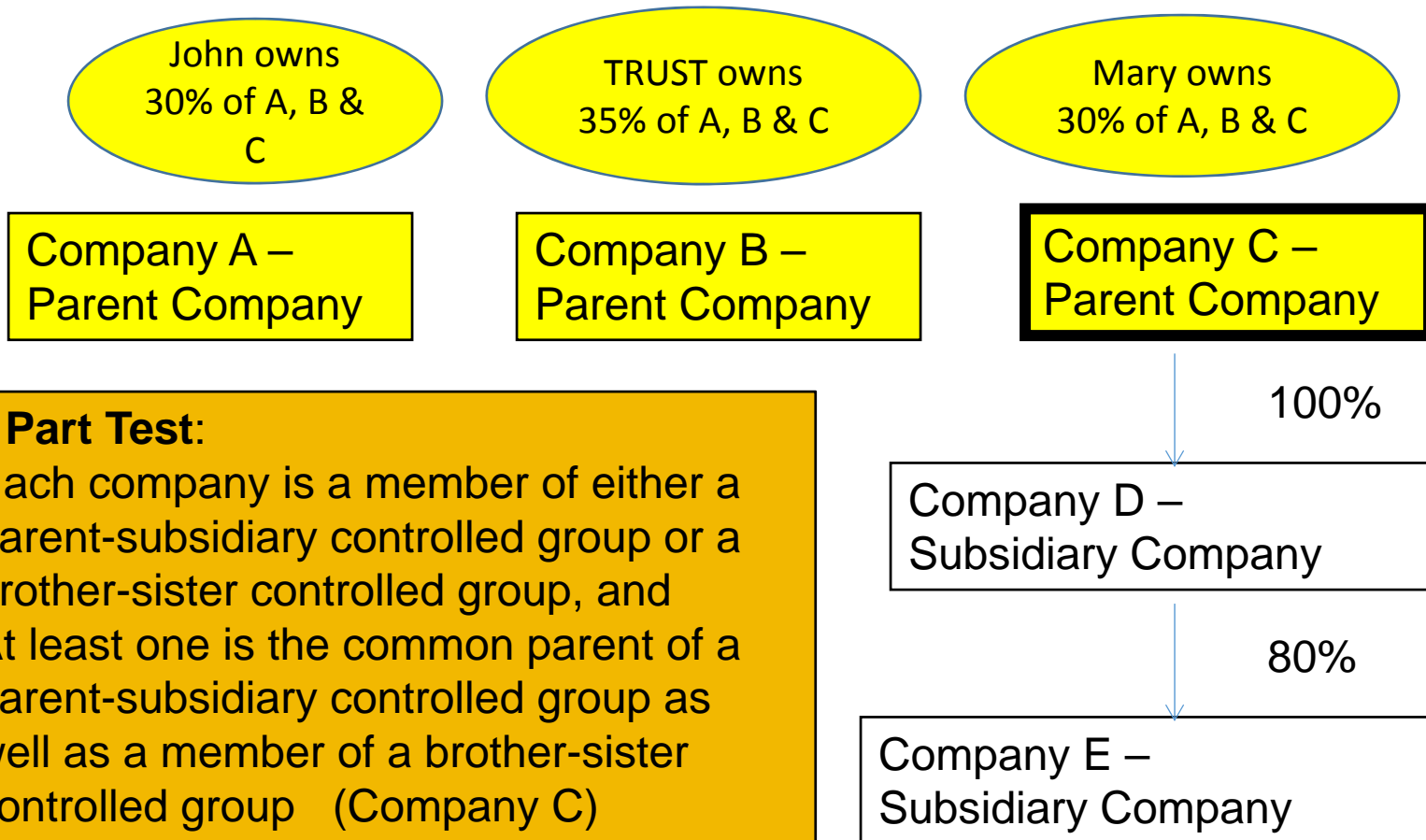


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# Basic Controlled Group Structures

- “Combined Group”



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# Controlled Group & MEWA Risk

- Multiple Employer Welfare Arrangements (MEWA)
  - Health Benefits Covering Two or More Employers (After Applying Controlled Group Rules)
  - State Insurance Laws May Regulate
    - Many prohibit self-funded MEWAs
    - State mandates may apply if permitted
  - ERISA, ACA, Other Complications
    - Who is the common law employer?
    - Initial (advance) and annual Form M-1 filing (but controlled group based on common ownership of 25% instead of 80% only for purposes of M-1 filing obligation)
    - Form 5500 issues



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# Affiliated Service Group Basics

- Concept: Two or more companies with at least one “service organization” that should be considered one employer operationally
  - Focus is on operational relationships, not so much on ownership
  - Rendering services to members within the group
  - Jointly rendering services to third parties
  - “Service organization” is an entity “the principal business of which is the performance of services”
    - Example: Engineering and health care professionals
    - As distinguished from one deriving the majority of its revenue from capital investment (e.g., manufacturing)

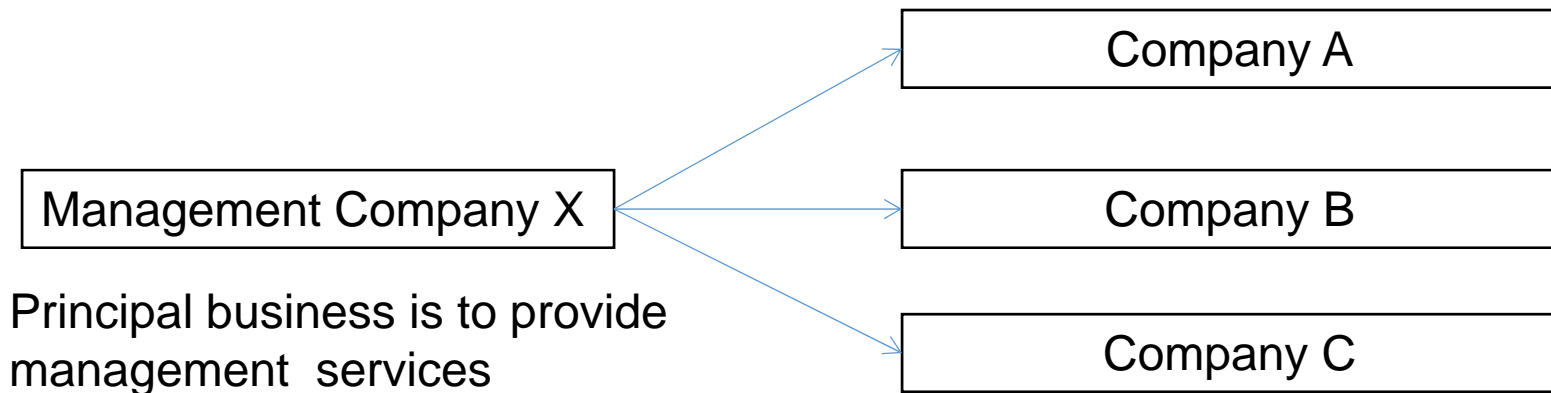


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# Affiliated Service Group Basics

- The “Management Service Organization”
  - Example 1: Principal business of Management Company X is to provide management services on a regular and continuing basis to Company A.
  - Example 2: Same as #1, but X services A, B and C which are related (e.g., may be a brother-sister group, using a 50% vs. 80% rule on common ownership)



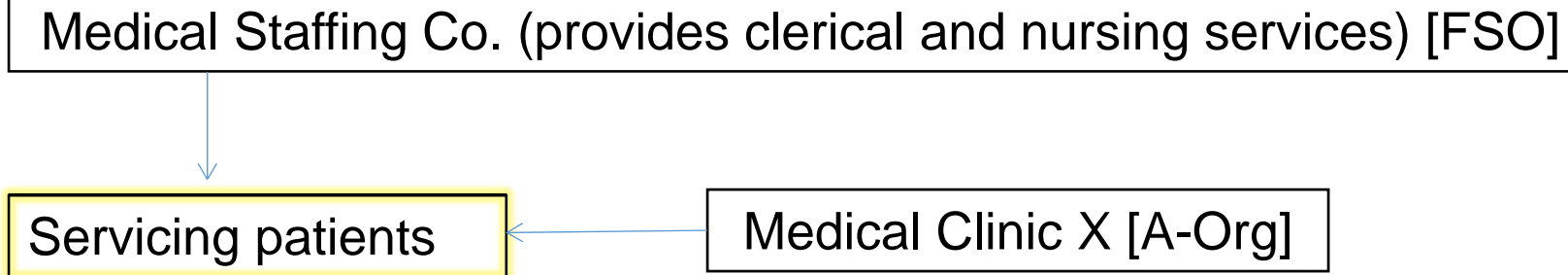
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# Affiliated Service Group Basics

## “A-Organization” and “First Service Organization (FSO)”

Medical Clinic X [A-Org] regularly performs services for, or is associated with, Medical Staffing Co. [FSO] in providing health services to third parties.



### KEY REQUIREMENTS:

- Clinic X is a shareholder or partner in Regional Staffing Co.
- Both the A-Organization and FSO are service organizations.
- If the FSA is incorporated, it must be a professional service corporation



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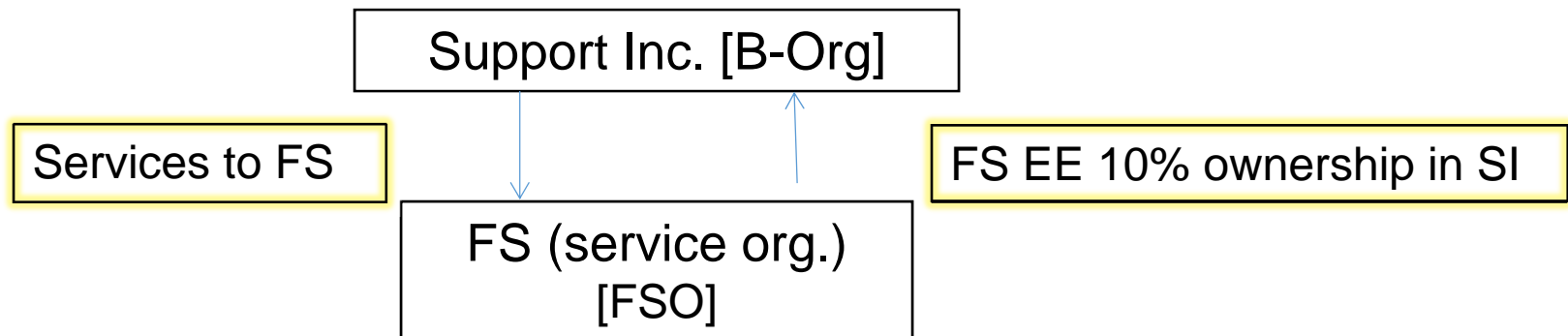




# Affiliated Service Group Basics

## “B-Organization” and “First Service Organization (FSO)”

Financial Services Corp. (FS)[FSO] is a financial services firm. A significant portion of Support Inc.’s (SI) [B-Org] business is providing services to FS of a type historically provided by employees in that business. One or more of the highly compensated employees of FS together own a total of at least 10% of SI.



### KEY REQUIREMENTS:

- At least 10% of B-Org is owned by highly compensated FSO employees.
- The FSO, but not B-Org, must be a service organization.



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# Additional Considerations

- Transferring ownership to avoid controlled group status may create a “predecessor company” that would be combined with the successor company under the ACA
- Carriers have differed in how carefully they examine controlled and affiliated service group relationships
  - The ACA has resulted in more carrier focus
  - They don’t always get it right
- Different members of a controlled or affiliated service group can still have different benefits (but must abide by nondiscrimination rules)



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# Broker Strategies

- Sometimes controlled group status is quite clear (e.g., 1 person owns at least 80% in each of two companies)
- When unclear, the risks merit careful review
- Strategies employed by brokers to address this area include:
  - “Hands Off” – (Will a competitor offer more assistance?)
  - “Conservative” – Provide awareness materials to client and request client to disclose controlled or affiliated group status to agency
  - “Aggressive” -- Facilitate detailed fact-finding on client’s organization and structure to make a joint determination with client on controlled or affiliated service group status



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**Thank you!**

