

*Example 3.* Employer Y has a single plan (Plan B) with a calendar plan year. With respect to the plan year beginning in 1990, employer Y elects to make the look-back year calculation for the 1990 determination year on the basis of the calendar year ending with or within the 1990 determination year. Because employer Y's determination year is the 1990 calendar year there is no lag period and employer Y determines the group of highly compensated employees for purposes of the 1990 calendar plan year on the basis of such plan year alone.

**Q-15:** Is there any transition rule in determining the group of highly compensated employees for 1987 and 1988?

**A-15:** (a) *In general.* Solely for purposes of section 401(k)(3) and (m)(2) and solely for twelve-month plan years beginning in 1987 and 1988, an eligible employer may elect to define the group of highly compensated employees as the group consisting of 5-percent owners of the employer at any time during the plan year and employees who receive compensation in excess of \$50,000 during the plan year. This rule would apply in lieu of the look-back year calculation and determination year calculation otherwise applicable under A-3(a) of this § 1.44(q)-1. In addition, an eligible employer may elect to make the determinations permitted under this transition rule on the basis of the calendar year ending in the plan year and the period by which such plan year extends beyond such calendar year, in accordance with the rules of A-14(b), in lieu of making the determinations under this transition rule on the basis of the plan year for which the determinations are being made.

(b) *Eligible employers.* An employer is an eligible employer under this A-15 if such employer satisfies both of the following requirements:

(1) The employer does not maintain any top-heavy plan within the meaning of section 416 at any time during 1987 and 1988; and

(2) Under each plan of the employer to which section 401(k)(3) or 401(m)(2) is applicable, the group of eligible employees that comprises the highest 25% of eligible employees ranked on the basis of compensation includes at least one employee whose compensation is \$50,000 or below. This requirement must be met separately with respect to each such plan of the employer.

(c) *Uniformity requirement.* An eligible employer may not make the election under paragraph (a) of this A-15 unless the election applies to all of the plans maintained by the employer to which section 401(k)(3) or 401(m)(2) applies.

(d) *Election requirements.* This election is operational and does not require a plan provision.

[T.D. 8173, 53 FR 4967, Feb. 19, 1988, as amended by T.D. 8334, 56 FR 3977, Feb. 1, 1991; T.D. 8548, 59 FR 32916, June 27, 1994]

#### § 1.414(r)-0 Table of contents.

(a) *In general.* Sections 1.414(r)-1 through 1.414(r)-11 provide rules for determining whether an employer is treated as operating qualified separate lines of business under section 414(r) of the Internal Revenue Code of 1986 as added to the Code by section 1115(a) of the Tax Reform Act of 1986 (Pub. L. No. 99-514), as well as rules for applying the requirements of sections 410(b), 401(a)(26), and 129(d)(8) separately with respect to the employees of each qualified separate line of business of an employer. Paragraph (b) of this section contains a listing of the headings of §§ 1.414(r)-1 through 1.414(r)-11. Paragraph (c) of this section provides a flowchart showing how the major provisions of §§ 1.414(r)-1 through 1.414(r)-6 are applied.

(b) *Table of contents.* The following is a listing of the headings of §§ 1.414(r)-1 through 1.414(r)-11.

#### *§ 1.414(r)-1 Requirements applicable to qualified separate lines of business.*

- (a) In general.
- (b) Conditions under which an employer is treated as operating qualified separate lines of business.
  - (1) In general.
  - (2) Qualified separate line of business.
    - (i) In general.
    - (ii) Line of business.
    - (iii) Separate line of business.
    - (iv) Qualified separate line of business.
      - (A) In general.
      - (B) Fifty-employee requirement.
      - (C) Notice requirement.
      - (D) Requirement of administrative scrutiny.
  - (3) Determining the employees of a qualified separate line of business.
- (c) Separate application of certain Code requirements to employees of a qualified separate line of business.
  - (1) In general.
  - (2) Separate application of section 410(b).

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- (i) General rule.
- (ii) Special rule for employer-wide plans.
- (3) Separate application of section 401(a)(26).
- (i) General rule.
- (ii) Special rule for employer-wide plans.
- (4) Separate application of section 129(d)(8) [Reserved]
- (5) Separate application of other Code requirements.
- (d) Application of requirements.
  - (1) In general.
  - (2) Interpretation.
  - (3) Separate operating units.
  - (4) Certain mergers and acquisitions.
  - (5) Governmental and tax-exempt employers.
  - (i) General rule.
  - (ii) Additional rules [Reserved].
  - (6) Testing year basis of application.
    - (i) Section 414(r).
    - (ii) Sections 410(b), 401(a)(26), and 129(d)(8).
    - (7) Averaging rules.
    - (8) Definitions.
    - (9) Effective dates.
  - (i) General rule.
  - (ii) Reasonable compliance.
    - (A) In general.
    - (B) Determination of reasonable compliance.
  - (C) Effect on other plans.
- (e) Additional rules.

*§ 1.414(r)-2 Line of business.*

- (a) General rule.
- (b) Employer determination of its lines of business.
  - (1) In general.
  - (2) Property and services provided to customers.
    - (i) In general.
    - (ii) Timing of provision of property or services.
  - (3) Employer designation.
    - (i) In general.
    - (ii) Ability to combine unrelated types of property or services in a single line of business.
    - (iii) Ability to separate related types of property or services into two or more lines of business.
  - (iv) Affiliated service groups.
- (c) Examples.
  - (1) In general.
  - (2) Examples illustrating employer designation.
  - (3) Examples illustrating property and services provided to customers.

*§ 1.414(r)-3 Separate line of business.*

- (a) General rule.
- (b) Separate organization and operation.
  - (1) In general.
  - (2) Separate organizational unit.
  - (3) Separate financial accountability.
  - (4) Separate employee workforce.

- (5) Separate management.
- (c) Supplementary rules.
  - (1) In general.
  - (2) Determination of separate employee workforce.
  - (3) Determination of separate management.
  - (4) Employees taken into account.
  - (5) Services taken into account.
    - (i) Provision of services to a separate line of business.
    - (ii) Period for which services are provided.
    - (iii) Optional rule for employees who change status.
      - (A) In general.
      - (B) Change in employee's status.
  - (6) Examples of the separate employee workforce requirement.
  - (7) Examples of the separate management requirement.
- (d) Optional rule for vertically integrated lines of business.
  - (1) In general.
  - (2) Requirements.
  - (3) Optional rule.
    - (i) Treatment of employees.
    - (ii) Purposes for which optional rule applies.
  - (4) Examples.

*§ 1.414(r)-4 Qualified separate line of business—fifty-employee and notice requirements.*

- (a) In general.
- (b) Fifty-employee requirement.
- (c) Notice requirement.
  - (1) General rule.
  - (2) Effect of notice.

*§ 1.414(r)-5 Qualified separate line of business—administrative scrutiny requirement—safe harbors.*

- (a) In general.
- (b) Statutory safe harbor.
  - (1) General rule.
  - (2) Highly compensated employee percentage ratio.
  - (3) Employees taken into account.
  - (4) Ten-percent exception.
  - (5) Determination based on preceding testing year.
  - (6) Examples.
- (c) Safe harbor for separate lines of business in different industries.
  - (1) In general.
  - (2) Optional rule for foreign operations.
  - (3) Establishment of industry categories.
  - (4) Examples.
- (d) Safe harbor for separate lines of business that are acquired through certain mergers and acquisitions.
  - (1) General rule.
  - (2) Employees taken into account.
  - (3) Transition period.
  - (4) Examples.
- (e) Safe harbor for separate lines of business reported as industry segments.

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- (1) In general.
- (2) Reported as an industry segment in conformity with Form 10-K or Form 20-F.
- (3) Timely filing of Form 10-K or 20-F.
- (4) Examples.
- (f) Safe harbor for separate lines of business that provide same average benefits as other separate lines of business.
  - (1) General rule.
  - (2) Separate lines of business benefiting disproportionate number of nonhighly compensated employees.
  - (i) Applicability of safe harbor.
  - (ii) Requirement.
  - (3) Separate lines of business benefiting disproportionate number of highly compensated employees.
  - (i) Applicability of safe harbor.
  - (ii) Requirement.
  - (4) Employees taken into account.
  - (5) Example.
- (g) Safe harbor for separate lines of business that provide minimum or maximum benefits.
  - (1) In general.
  - (2) Minimum benefit required.
    - (i) Applicability.
    - (ii) Requirement.
    - (iii) Defined benefit minimum.
      - (A) In general.
      - (B) Normal form and equivalent benefits.
      - (C) Compensation definition.
      - (D) Average compensation requirement.
      - (E) Special rules.
    - (iv) Defined contribution minimum.
      - (A) In general.
      - (B) Modified allocation definition for averaging.
  - (3) Maximum benefit permitted.
    - (i) Applicability.
    - (ii) Requirement.
    - (iii) Defined benefit maximum.
      - (A) In general.
      - (B) Determination of defined benefit maximum.
      - (C) Adjustment for different compensation definitions.
      - (D) Adjustment for certain subsidies.
      - (iv) Defined contribution maximum.
    - (4) Duplication of benefits or contributions.
      - (i) Plans of the same type.
      - (ii) Plans of different types.
      - (iii) Special rule for floor-offset arrangements.
    - (5) Certain contingency provisions ignored.
    - (6) Employees taken into account.

*§ 1.414(r)-6 Qualified separate line of business—administrative scrutiny requirement—individual determinations.*

- (a) In general.
- (b) Authority to establish procedures.

*§ 1.414(r)-7 Determination of the employees of an employer's qualified separate lines of business.*

- (a) Introduction.
  - (1) In general.
  - (2) Purposes for which this section applies.
- (b) Assignment procedure.
  - (1) In general.
  - (2) Assignment for the first testing day.
  - (3) Assignment of new employees for subsequent testing days.
  - (4) Special rule for employers using annual option under section 410(b).
- (c) Assignment and allocation of residual shared employees.
  - (1) In general.
  - (2) Dominant line of business method of allocation.
    - (i) In general.
    - (ii) Dominant line of business.
    - (iii) Employee assignment percentage.
      - (A) Determination of percentage.
      - (B) Employees taken into account.
      - (iv) Option to apply reduced percentage.
    - (v) Examples.
  - (3) Pro-rata method of allocation.
    - (i) In general.
    - (ii) Allocation procedure.
    - (iii) Examples.
  - (4) HCE percentage ratio method of allocation.
    - (i) In general.
    - (ii) Highly compensated employee percentage assignment ratio.
    - (iii) Allocation procedure.
  - (5) Small group method.
    - (i) In general.
    - (ii) Size of group.
    - (iii) Composition of qualified separate line of business.
    - (iv) Reasonable allocation.

*§ 1.414(r)-8 Separate application of section 410(b).*

- (a) General rule.
- (b) Rules of separate application.
  - (1) In general.
  - (2) Satisfaction of section 410(b)(5)(B) on an employer-wide basis.
    - (i) General rule.
    - (ii) Application of facts and circumstances requirements under nondiscriminatory classification test.
    - (iii) Modification of unsafe harbor percentage for plans satisfying ratio percentage test at 90 percent level.
      - (A) General Rule.
      - (B) Facts and circumstances alternative.
  - (3) Satisfaction of section 410(b) on a qualified-separate-line-of-business basis.
  - (4) Examples.
- (c) Coordination of section 401(a)(4) with section 410(b).
  - (1) General rule.
  - (2) Examples.
- (d) Supplementary rules.

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- (1) In general.
- (2) Definition of plan.
- (3) Employees of a qualified separate line of business.
- (4) Consequences of failure.

*§ 1.414(r)-9 Separate application of section 401(a)(26).*

- (a) General rule.
- (b) Requirements applicable to a plan.
- (c) Supplementary rules.
  - (1) In general.
  - (2) Definition of plan.
  - (3) Employees of a qualified separate line of business.
  - (4) Consequences of failure.

*§ 1.414(r)-10 Separate application of section 129(d)(8). [Reserved]*

*§ 1.414(r)-11 Definitions and special rules.*

- (a) In general.

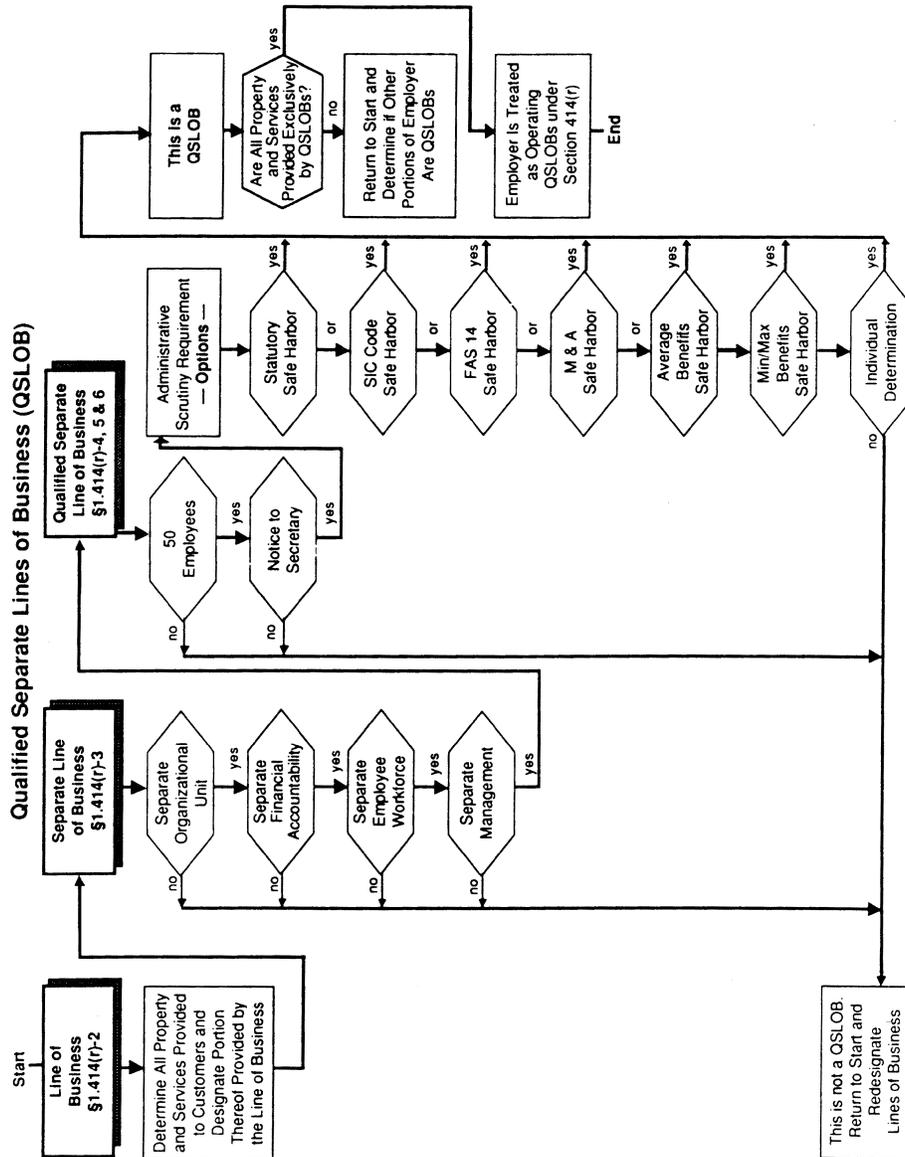
- (b) Definitions.

- (1) In general.
- (2) Substantial-service employee.
- (3) Top-paid employee.
- (4) Residual shared employee.
- (5) Testing year.
- (6) Testing day.
- (7) First testing day.
- (8) Section 401(a)(26) testing day.

- (c) Averaging rules.

- (1) In general.
- (2) Specified provisions.
- (3) Averaging of large fluctuations not permitted.
- (4) Consistency requirements.

(c) *Flowchart.* The following is a flowchart showing how the major provisions of §§ 1.414(r)-1 through 1.414(r)-6 are applied.



[T.D. 8376, 56 FR 63434, Dec. 4, 1991, as amended by T.D. 8548, 59 FR 32916, June 27, 1994]

**§ 1.414(r)-1 Requirements applicable to qualified separate lines of business.**

(a) *In general.* Section 414(r) prescribes the conditions under which an employer is treated as operating quali-

fied separate lines of business. If an employer is treated as operating qualified separate lines of business under section 414(r), certain requirements under the Code may be applied separately with respect to the employees of