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Can a Limited Partnership Have a Pension Plan?

by Tim Plaehn



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A small business can be organized as a sole proprietorship, partnership, corporation or LLC. The tax and employee benefit rules allow a small business of any structure to set up a pension plan for employees. For a company organized as a partnership, the tax rules do make a difference between types of partners, and limited partners may not be allowed to participate in a retirement plan.



Employer-Sponsored for Employees

The types of pension plans that can be used by a small business include 401(k), SEP-IRA, SIMPLE IRA and defined-benefit plans. Most small businesses go with the defined contribution plans such as a 401(k) or IRA based plan rather than the traditional but complicated and expensive defined-benefit plan. A pension plan set up by a business is for the benefit of employees, which can include the owners or partners in the business.

Partners As Owners And Employees

When a business is organized as a partnership, a partner typically is viewed in two ways by the Internal Revenue Service. As an owner, a partner's compensation is her share of the net profits of the business. The partner does not earn wages nor receive a W-2 at the end of the year. Instead, the partner receives a report of her proportionate share of business expenses and earnings to claim on her personal tax return. However, when it comes to benefits, a managing partner participates like an employee and is covered under the company's health plan and is a participant in the partnership-sponsored retirement savings plan.



Limited Partner Limits

Partnerships may have several different types of partners and compensate partners differently. For a partner who works to run and manage a business, his earnings from the business are viewed as earned income for tax purposes. With the earned income, the partner also fills the employee requirements for benefits. A limited partner, because he does not work or provide service toward the daily operation of the business, is more of an investor, and the money paid by a business to a limited partner would be classified as investment income. Limited partners would not participate in the company pension plan.

Real World Example

A visible example of limited partnerships and pension plans are the publicly traded partnerships in which investors can buy into through shares -- technically called units -- trading on the stock exchanges. In this case, there is a company with employees that participate in whatever pension plan the company offers. Investors own limited partnership units in their brokerage accounts and are not part of any employee benefits.

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About the Author

Tim Plaehn has been writing financial, investment and trading articles and blogs since 2007. His work has appeared online at Seeking Alpha, Marketwatch.com and various other websites. Plaehn has a bachelor's degree in mathematics from the U.S. Air Force Academy.

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