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# DOL and IRS Encourage Workplace Retirement Savings for Smaller Employers by Expanding Availability of Multiple Employer Plans

**A multiple employer plan (MEP)** allows employees of unrelated private-sector employers to participate in a single tax-qualified retirement plan sponsored by an employer group or association or a professional employer organization (PEO).[1] Generally, joining an MEP is an efficient way to reduce the cost of establishing and maintaining a broad-based retirement plan that is subject to the Employee Retirement Income Security Act of 1974 (ERISA) by using a common plan administrator and pooled investments.

## Insight

When employers band together and pool resources, they can often reduce costs. For example, mutual funds often charge lower fees to plans with greater assets, so MEPs can allow small businesses to give their employees access to the same low-cost investments that large employers offer. Low investment fees mean the employer is less likely be sued for permitting plan participants to pay excessive investment fees, which has become a litigation trend.

The U.S. Department of Labor (DOL) has long considered so-called "open" MEPs, where the participating employers are unrelated and have no common nexus, not to be one plan for ERISA reporting and disclosure purposes. Rather, the DOL views such arrangements as a collection of single employer plans that use a common administrator and commingled funding vehicles.

Three recent changes in the law may expand the availability of MEPs, which may in turn encourage more small employers to offer workplace retirement plans. Specifically, on July 31, the DOL finalized **rules** so that starting September 30, 2019, chambers of commerce or other certain associations can sponsor a special kind of MEP called an "association retirement plan" (ARP). The DOL also issued relief for MEPs that made certain mistakes on their Form 5500's, as set forth in **Field Assistance Bulletin (FAB) 2019-01** (July 24, 2019). Finally, on July 3, the IRS proposed **rules** that would largely take the bite out of the longstanding "one bad apple rule" for MEPs. Under Internal Revenue Code (IRC) Section 413(c), one participating employer's failure to satisfy any plan qualification requirement, even minor, innocent plan operation errors, could cause the entire MEP to lose its tax-qualified status.

## Association Retirement Plans (ARP)

**Who can sponsor an ARP?** The DOL's final ARP regulation clarifies that employer groups or associations and PEOs can be ''employers'' within the meaning of ERISA for purposes of establishing or maintaining defined contribution retirement plans such as 401(k) plans, but not for defined benefit pension plans. An employer group or association that wishes to sponsor an ARP must satisfy the following criteria:

- Although providing the plan may be the primary purpose of the group or association, the group or association must also have at least one substantial business purpose unrelated to offering the plan, or other employee benefits to its employer members.
    - A substantial business purpose exists if the group would be a viable without the plan or other employee benefits plans.
    - "Business purpose" includes promoting common business interests of its members or the common economic interests in a given trade or employer community and is not required to be a for-profit activity.
- The group or association must have a formal organizational structure with a governing body, by-laws, etc.
- Employer members must control, in both form and substance, the group or association's functions and activities, including controlling the plan.

[1] A PEO is a human resources firm that contractually assumes many employment tasks for its client employers. To be a MEP sponsor, the PEO must perform substantial employment functions on behalf of its client employers.

- Employer members must have a commonality of interest, based on either being in the same trade or industry or having a principal place of business in the same geographic area, which includes metropolitan areas that extend beyond one state.

## Insight

Excluding retirement industry vendors from directly serving as an employer group or association "sponsor" of an ARP may mean that the ARP industry may grow more slowly and organically, as chambers of commerce and other grassroots entities become aware of the change in the law and develop their own MEPs. However, it seems more likely that retirement industry vendors would approach chambers of commerce and other organizations that qualify as bona fide employer groups or associations offering turnkey "one-stop shopping" ARP platforms.

**Can working owners join?** The final regulation permits certain working owners without employees to participate in an ARP. Earlier this year, a federal district court[2] vacated portions of the DOL's final association **health** plan rules[3] based on the DOL's attempt to stretch its interpretation of ERISA Section 3(5)'s definition of "employer" to include working owners who do not have employees. In issuing the final ARP rule, the DOL said that it disagrees with that court's ruling and has filed an appeal. To qualify as a working owner, the individual must satisfy these conditions:

- Must have an ownership right of any nature in a trade or business, whether incorporated or unincorporated, including as a partner or self-employed individual.
- Must earn income from providing personal services to the trade or business.
- Must either (i) work at least 20 hours per week or 80 hours per month, on average, or (ii) have wages or self-employment income from such trade or business that at least equals the working owner's cost of coverage for participation by the working owner and any covered beneficiaries in any group health plan sponsored by the employer group or association in which the individual is participating or is eligible to participate.

The final rule does not extend the working-owner provision to MEPs sponsored by PEOs. Thus, a working owner's trade or business must have at least one common law employee to participate in a PEO's MEP. Working owners without employees generally would not need PEO's employment services like payroll, compliance with federal and state workplace laws, and human resources support.

**Who is the plan's ERISA fiduciary?** Importantly, the ARP rule reduces ERISA fiduciary liability exposure for adopting employers, which many businesses consider to be a major impediment to retirement plan sponsorship. The rule transfers substantial legal risk from employers to professional fiduciaries who are responsible for managing the plan. Employers essentially now only have ERISA fiduciary responsibility for choosing and monitoring the ARP vendors and for timely depositing contributions to the ARP. As plan administrator, the ARP sponsor is responsible for compliance with ERISA's fiduciary, reporting and disclosure obligations, including filing a single Form 5500 for the entire plan.

**What's next for ARPs?** Simultaneously with publishing the final ARP rule, the DOL issued an extensive **request for information** seeking comments on how the program can be improved and expanded. Comments are due October 29, 2019. All or part of the ARP rule may be rescinded if a federal appeals court upholds the federal district court case vacating the DOL's association health plan final rule. Interestingly, the final rules include a severability provision, which provides that if any part of the rule is invalidated, the rest of the rule will continue in full force. It is likely the Supreme Court may have the final say on whether the DOL exceeded its authority in crafting a new, expansive interpretation of ERISA's definition of "employer" in creating association health plans and ARPs. Since the DOL's ARP rule is issued under ERISA, it is separate from the IRS's "one bad apple" MEP rule for tax-qualified retirement plans, discussed below.

## Insight

The final ARP rules do not change existing law regarding "closed" MEPs, i.e., employers that are in the same trade or industry have always been allowed to join together in a MEP and file a single Form 5500. Many believe that the DOL lacks authority to allow true "open MEPs" for unrelated employers, so federal legislation would be needed to allow employers with no common bond or "nexus" to join an ERISA plan and be treated as a single plan and file a single Form 5500. Under current law, unrelated employers participating in a single plan must file separate Form 5500s and each employer is treated as maintaining its own ERISA plan.

[2]State of New York v. United States Department of Labor, 363 F. Supp. 3d 109 (D.D.C. March 28, 2019).

[3]83 Federal Register 28,912 (June 21, 2018). DOL's ARP rules are similar in many respects to DOL's association health plan rules.

## Form 5500 Filing Relief and Special One-Time Extension

**Retroactive penalty relief.** In FAB 2019-01, the DOL recently gave some welcome penalty relief for existing MEPs that incorrectly filed Form 5500s by failing to include a complete list of participating employers for the 2017 and earlier plan years. The relief is solely from ERISA civil penalties for Form 5500 reporting obligations, so there is no relief for any other ERISA or IRC issues. Going forward, DOL expects MEPs to fully comply with the reporting obligations as outlined in the FAB.

**Special 2 ½ month extension to file Form 5500.** The FAB also creates a special, one-time, 2 ½ month extension of time to file the 2018 Form 5500. MEPs should check the "special extension" box under Part I, Line D on the 2018 Form 5500 and enter "FAB 2019-01" as the description to use this extension. MEPs using this special extension do not need to file a Form 5558 with the IRS. The relief provided in the FAB is also available for MEPs that already filed their 2018 Form 5500, provided that such MEPs file an amended annual report for the 2018 plan year that complies with the Section 103(g) reporting requirement by October 15, 2019.

**What's the problem?** In 2014, Congress added Section 103(g) to ERISA as a specific Form 5500 annual report requirement for MEPs, including those sponsored by PEOs. Section 103(g) requires MEPs to include with their Form 5500s a list of participating employers and a good faith estimate of the percentage of total contributions made by such participating employers during the plan year. The DOL issued rules implementing Section 103(g) and updated Form 5500 and its instructions accordingly. However, in reviewing Form 5500s filed in 2015 and later, the DOL observed significant errors in how MEPs were disclosing the list of participating employers. For example, the DOL found filings that:

- Replaced participating employer names with abbreviated names or initials, client numbers, or other labels such as "Client 1," "Client 2," etc.
- Reported only the last 4 digits of participating employers' EINs.
- Included an attachment with no information and a note saying, "Details available upon request."
- Incorrectly listed the PEO as the only participating employer.

While the DOL believes that it provided clear instructions on what was supposed to be included on the list of participating employers, the FAB says that the DOL understands that some PEOs may have been confused. So this one-time, retroactive penalty relief and special 2 ½ month transition period is intended to allow a fresh start so that the DOL receives the information on participating employers in PEOs that DOL was expecting to get in the Form 5500 filings.

## Insights

DOL's insistence that MEPs must disclose a complete and accurate list of participating employers is not surprising, since such disclosure provides necessary data that the DOL and the IRS need to enforce current law and to design new rules for MEP legislation that is likely to pass either this year or next.

Several bills are pending in Congress that would expand MEPs even further, by eliminating the IRS's one bad apple rule and significantly dialing back the DOL's nexus requirement. The bill to watch is the bipartisan "Setting Every Community Up for Retirement Enhancement Act of 2019" **(H.R. 1994)**. The SECURE Act sailed through the House with a 417-3 vote on May 29 and seems likely to be enacted later this year or the next. Even though it is currently stalled in the Senate, there is mounting pressure from Senate Finance Committee Chairman Chuck Grassley (R-IA) and others to overcome the remaining obstacles.

Like all ERISA plans, MEPs that have more than 100 participants at the beginning of the plan year are generally required to attach an independent qualified audit report to their Form 5500. Nothing in the recent DOL guidance changed that requirement.

## IRS Takes a Big Bite Out of the "One Bad Apple" Rule

**Unified plan rule.** For over 40 years, IRC Section 413(c) and Treas. Reg. Section 1.413-2(a)(3)(iv) have provided that if a single participating employer in a MEP is non-compliant with any tax-qualification rules, the entire plan and all the other participating employers are at risk of disqualification. This so-called "one bad apple," or "unified plan," rule has dissuaded many employers from joining a MEP. Although a legislative change would be needed to repeal the rule, the IRS has released a proposed regulation crafting an administrative procedure where a defined contribution MEP could isolate the "bad apple" from the rest of the bushel, thereby limiting the adverse consequences to the offending spun-off plan. The proposed regulation also includes a procedure for suspected plan qualification errors made by the bad apple employer similar to the procedure for known plan qualification failures committed by the offending employer.

**Three strikes and you're out.** Under the proposed rules, the process for dealing with the bad apple is lengthy and complicated. The MEP must give the bad apple employer three written notices following a specified time cadence. If the employer does not take prompt corrective action, the MEP must expel the employer from the plan by automatically spinning off the employer's portion of the MEP into a stand-alone, single employer plan, and terminating the spun-off plan. The MEP also must notify participants in the problematic plan before the spin-off/termination, stop accepting contributions from that employer and notify the IRS on a form that the IRS will create for this purpose. All unvested participants of the bad apple employer will become vested due to plan termination and the MEP will process plan termination distributions to affected participants. Tossing the bad apple out could take a full year to implement.

**Which MEPs are eligible?** To qualify for the relief, the defined contribution MEP must have good internal controls that facilitate overall compliance and cannot be "under examination"; these are some of the same requirements for participating in IRS's Employee Plans Compliance Resolution System (EPCRS) self-correction program for tax-qualified retirement and 403(b) plans. The plan document must also include certain language describing the non-responsive bad apple spin off procedures - but IRS intends to issue a model plan amendment setting out sample language. Finally, the problem must be caused by an unresponsive participating employer and cannot be an overall plan problem.

## Insight

The proposal is unclear about whether the cost of sending the notices to the bad apple employer, along with isolating and terminating that portion of the plan, can be charged to that employer's participants' plan accounts. Perhaps that is an overall cost that the plan as a whole will need to bear.

The proposal isn't clear about whether distributions from the terminated bad apple plan are eligible for rollover, since the source of the funds is a plan that is known to have a qualification failure. Yet, it doesn't seem fair to harm innocent participants who will receive plan termination distributions.