A New Day for MEPs and PEPs
S. Derrin Watson, JD, APM

Comparison of MEP to Controlled Group

Overall Qualification

- By definition, except for coverage and nondiscrimination a multiple employer plan is one plan
- The entire plan must be qualified or the plan as a whole is disqualified
  - “The failure by one employer maintaining the plan (or by the plan itself) to satisfy an applicable qualification requirement will result in the disqualification of the section 413(c) plan for all employers maintaining the plan”
- One bad apple spoils the barrel
ERISA and the Code

- The IRS administers the Internal Revenue Code
  - Qualified plan rules
  - Qualified for tax benefits
    - If you don’t follow the rules, you don’t get the tax benefits
  - Relatively MEP friendly
- The DOL administers ERISA Title I
  - Rules relating to employee pension benefit plans
  - Rules apply whether or not the plan satisfies the tax qualification rules
  - Has been relatively MEP unfriendly

How does this relate to MEPs?

- Many DOL Advisory Opinions rejected the concept that a given MEP is a single plan under ERISA
- Opinions primarily turn on not the types of benefits provided but on whether the arrangement is established or maintained by an employer or by an employee organization
- Key issue for MEP: are the employers a bona fide group or association?
  - Bona fide group: facts and circumstances test
  - Likely not an issue for shared employee or kissing cousin situations

Factors historically used to determine bona fide group status: commonality

- How members are solicited:
  - Who is entitled to participate and who actually participates in the association;
- The process by which the association was formed, the purposes for which it was formed, and what, if any, were the preexisting relationships of its members:
  - The powers, rights, and privileges of employer members that exist by reason of their status as employers; and
- Who actually controls and directs the activities and operations of the benefit program:
  - The employers that participate in a benefit program must, either directly or indirectly, exercise control over the program, both in form and in substance, in order to act as a bona fide employer group or association with respect to the program.
How does this relate to open MEPs?

- DOL Advisory Opinion 2012-04A held that an open MEP is not established by a bona fide group or association of employers
- Not one point in their favor
- Therefore, the MEP isn’t established and maintained by an Employer
- Therefore, the MEP isn’t an ERISA plan
- However, each underlying “employer” has adopted a separate ERISA plan
- So MEP is holding ERISA plan assets – lots of ERISA plans
- Each employer is the plan sponsor of its plan (regardless of what document may say)
- Truly open MEPs are still in the same boat even after new DOL regulations

Pooled Employer Plans (PEP) Authorized

- PEP is single plan under ERISA
  - One Form 5500, one bond, one audit
  - DC qualified plans or IRA arrangements
- Doesn’t apply to:
  - Employers with “common interest other than having adopted the plan” – i.e., pre-SECURE “closed MEP”
  - Multiemployer plan
  - Plan that existed before SECURE unless administrator elects to apply PEP rules
PEP Plan Document Requirements

- Plan designates pooled plan provider (PPP)
- PPP is named fiduciary
- Plan designates trustee (which qualifies as IRA custodian)
  - Other than an employer participating in plan
  - Must be responsible to collect ER contributions
  - Must have and implement reasonable, diligent, and systematic contribution collection procedures
- Each employer retains fiduciary responsibility for
  - Selection and monitoring of PPP and other named fiduciaries
  - Investment and management of assets of that ER's employees
    - Unless named fiduciary has delegated authority to another fiduciary (3(38) advisor)
  - 404(c) protection can apply

PEP Document Requirements (continued)

- No unreasonable fees, restrictions, or penalties re: ceasing participation, receipt of distributions, or asset transfers
- PPP must provide ERs with DOL-mandated disclosures
  - May be provided electronically
- Employers must take actions DOL or PPP determines are needed to administer plan and maintain qualification
  - Including providing disclosures or other information
- Ensure only reasonable costs are imposed on PPP and employers
- ER is plan sponsor with regard to its employees

Pooled Plan Provider (PPP) Requirements

- PPP is plan administrator and named fiduciary
  - Must acknowledge status in writing
- PPP is responsible for all administrative functions, including testing
  - To ensure plan remains qualified
  - Each ER does what is needed to retain plan qualification
- PPP responsible to see bonding requirements satisfied
  - Maximum bond is $1,000,000
- Related employer (414(b), (c), (m)) rules apply to PPP
  - Allows affiliates and subsidiaries to perform designated functions
Form 5500 Information

- Form 5500 for MEP (including PEP) must provide
  - List of employers
  - Good faith estimate of each employer’s percent of:
    - Contributions made during year
    - Aggregate of account balances of the employer
  - Identifying information for PPP (in case of PEP)
- DOL can provide simplified reports for MEPs
  - No more than 1000 participants
  - If no employer has more than 100 participants

<table>
<thead>
<tr>
<th>Act Section</th>
<th>Qualified</th>
<th>Eff. Date</th>
<th>Amendment Needed</th>
</tr>
</thead>
<tbody>
<tr>
<td>101(a)</td>
<td>Yes</td>
<td>PY begin after 12/31/2020</td>
<td>No</td>
</tr>
<tr>
<td>403(b)</td>
<td>Yes</td>
<td>PY begin after 12/31/2020</td>
<td>No</td>
</tr>
<tr>
<td>457(b)</td>
<td>No</td>
<td>PY begin after 12/31/2020</td>
<td>Yes</td>
</tr>
</tbody>
</table>

Bad Apple Rule Softened

- Adds new Code §413(e)
  - Applies to DC multiple employer plans that either:
    - Have employers with common interest outside of plan, or
    - A PEP with a PPP
  - Plan not disqualified as a whole because an employer comply
    - Spin off assets of that employer (per next slide)
    - Doesn’t help if PPP fails to perform duties
  - IRS to publish model plan language for PEPs

<table>
<thead>
<tr>
<th>Act Section</th>
<th>Qualified</th>
<th>Eff. Date</th>
<th>Amendment Needed</th>
</tr>
</thead>
<tbody>
<tr>
<td>101(a)</td>
<td>Yes</td>
<td>PY begin after 12/31/2020</td>
<td>Yes</td>
</tr>
<tr>
<td>403(b)</td>
<td>No</td>
<td>PY begin after 12/31/2020</td>
<td>No</td>
</tr>
<tr>
<td>457(b)</td>
<td>No</td>
<td>PY begin after 12/31/2020</td>
<td>Yes</td>
</tr>
</tbody>
</table>

Overlapping Rules

- PPP must register with DOL and IRS
- DOL and IRS can audit/investments PPPs
- DOL/IRS have broad authorization to issue regulations including:
  - Identify PPP duties
  - Provide that if ER fails to take needed actions:
    - Assets of that ER are spun off to a single employer plan of that employer, to IRAa or other rollover vehicles for participants, or other arrangements DOL/IRS determines
    - That employer (and not the plan or other employers except as provided in guidance) will be liable for that plan.
    - DOL/IRS can waive these requirements if it is in best interests of employees
    - DOL/IRS should take into account whether employer lapse has continued long enough that it “demonstrates a lack of commitment to compliance”
Regulations on PPPs, MEPs

- ER and PPP can comply with good faith interpretation of the law
  - So, you don’t have to wait for regulations to establish PEP
- IRS can issue regs on MEP qualification failures outside of new SECURE rules
  - So they can go forward with proposed bad apple regulation

AHP Regulations Issued June 2018

- Limited to health plans
- Effective 9/18 for fully insured plans
- Allows employers to form associations and the associations to offer health coverage
  - Working owners can participate as employer and employee
- Do not replace prior guidance on commonality
- Give new method to establish single health plan
- Controversial because of PPACA impact
  - Struck down by district court; DOL has appealed
August 31, 2018 Executive Order on MEPs

- Increase availability of MEPs
  - DOL:
    - Clarify and expand circumstances under which employers can adopt MEP subject to appropriate safeguards
    - Increase retirement security for part-time workers, sole proprietors, working owners, and other gig economy workers by expanding access to retirement plans
    - Within 180 days consider issuing rules – Proposed Regs now released
  - IRS
    - Within 180 days consider modifying bad apple rule

Final DOL regs

- 2510.5-55
- Limited to defined contribution plans
- Single plan can be established by
  - Bona fide group or association of employers
    - Very similar to association health plan rules
  - Bona fide PEO
  - Severability clause

Requirements

- Association members must either be
  - In same trade, industry, line of business, or profession
  - In same geographical area
    - Within a single state or
    - A single metropolitan area
Requirements

- Association must have purpose other than providing MEP/health or employee benefits
  - Such as continuing education or business promotion
- MEP/Health program can be primary purpose so long as it isn’t the only purpose

Requirements

- Each employer member participating must employ at least one employee participant
  - Can include working owner
- Group has formal structure with governing body and by-laws

Working owner

- Has ownership right in trade or business, whether or not incorporated
- Earns wages/SE income for providing personal services to business
- Either:
  - Works on average at least 20 hours/week or 80 hours/month, or
  - Comp equals or exceeds cost of any AHP
Requirements

- Employer members must control association and employer plan participants must control plan
  - Issue of both form and substance
- Plan participation is limited to employees of a current employer member of the association, former employees of a current employer member and beneficiaries of such individuals.
  - Required COBRA coverage is an exception to this rule for association health plans

AHP Requirements

- Can’t be health insurer or owned or controlled by health insurer or affiliates
- Must follow nondiscrimination rules
  - Cannot condition membership on health factors

ARP Requirements

- Can’t be bank or trust company, insurance issuer, broker-dealer, or other similar financial services firm (including pension record keepers and third-party administrators), or owned or controlled by such an entity or any subsidiary or affiliate of such an entity, other than to the extent such an entity, subsidiary or affiliate participates in the group or association in its capacity as an employer member of the group or association
Put them together

- SECURE:
  - Starts in 2021
  - Allows pure open MEP
  - Requires PPP; specific plan language
- Final regs:
  - In effect now
  - Works for associations and PEOs
  - Doesn’t allow TPA/investment vendor to establish
  - Old commonality standards?

Requirements

1. The organization performs substantial employment functions on behalf of its client employers, and maintains adequate records relating to such functions;
2. The organization has substantial control over the functions and activities of the MEP, as the plan sponsor, the plan administrator, and a named fiduciary;
3. The organization ensures that each client employer that adopts the MEP acts directly as an employer of at least one employee who is a participant covered under the defined contribution MEP; and
4. The organization ensures that participation in the MEP is available only to employees and former employees of the organization and client employers, and their beneficiaries.
Substantial employment functions

- Facts and circumstances
- Safe harbor: 4 requirements
  - The PEO assumes responsibility for the payment of wages to employees of its client-employers that adopt the plan without regard to client reimbursement.
  - The PEO assumes reporting, withholding, and paying any applicable federal employment taxes for its client-employers that adopt the plan without regard to client reimbursement.
  - The PEO must play “a definite and contractually specified role in recruiting, hiring, and firing workers of its client employers that adopt the MEP.”
  - This can be exercised in tandem with the client employer.
  - It is sufficient if the PEO simply retains the right to recruit, hire and fire workers of its client employers.
  - The PEO must assume responsibility for and has substantial control over the functions and activities of any employee benefits which the service contract may require the PEO to provide.

Proposed regs for DC plans

Taxpayers CANNOT rely!

- MEP can be preserved if MEP administrator follows new regs (once finalized)
  - Escalating series of notices to unresponsive employer
    - Unresponsive employer responds
      - Provides information
      - Makes contribution
      - Takes other corrective action
    - Unresponsive employer requests spin-off to single employer plan
    - MEP administrator spins off assets of unresponsive employer to separate plan, terminates it, and distributes
  - Requires plan amendment to implement rules
  - Requires specific plan practices and procedures
A MEP Administrator's Tale; Act I

- Cast of Characters:
  - MEP Administrator: Diligent Plans
  - Unresponsive Employer: Deadbeat Duds (clothing store owned by Dudley Deadbeat)
  - Plan: 3% Safe Harbor 401(k) MEP, calendar year
  - Known Qualification Failure: Deadbeat Duds failed to contribute $7,500 SH contribution for 2022 by December 31, 2023

The First Notice
"Wake Up and Do Something"

- January 2, 2024, Diligent sends Deadbeat a notice:
  - "You are currently in default of your obligation to make a $7,500 employer contribution to the plan. We ask that, within 90 days, you either: (1) make the required contribution, plus earnings (contact us for an exact number); or (2) tell us to spin off the assets relating to your employees into a single employer plan you establish and maintain. If you take the second option, the law will still require you to make the delinquent contribution to that plan."
- April 1, 2024: 90 days passes with no reply

The Second Notice
"Just Wait Until Your Father Gets Home"

- Diligent must send a second notice within 30 days after expiration of the first notice
- April 8, 2024: Diligent sends Deadbeat a notice
  - "If you do not take action with 90 days, the third (and final) notice will be provided to the Deadbeat Duds participating employees and to the Department of Labor"
- July 7, 2024: 90 days of radio silence
Third Notice
“Now We Mean Business”

- Diligent must send third notice within 30 days after expiration of second notice
- July 22, 2024, Diligent sends notice to Deadbeat, Deadbeat Duds participating employees, and the DOL
  - “We have tried repeatedly to have you make your required $7,500 (plus earnings) contribution for the 2022 plan year. This is your final notice. Ideally, you would make the contribution to this plan within the next 90 days (by October 20). Alternatively, you can choose to have us spin off the assets of your employees to a single employer plan you will administer. You will still need to make the contribution to that plan.
  - “If you do not make the contribution on initiate the spinoff by October 20, 2024, we will stop accepting contributions relating to your employees (including salary deferrals), and we will spin off the assets of your employees to a new plan we administer. We will immediately thereafter terminate that plan and distribute the assets to the employees.”

The Hammer Strikes

- October 20, 2024: Deadbeat lives down to its name
- ASAP: Diligent notifies Deadbeat participants
  - Deadbeat portion of plan is being spun off and terminated
  - No more contributions (including deferrals)
  - ASAP, employees will receive distribution notices; followed by distribution
    - Comply with J&S rules if applicable
    - Contact information for Diligent Plans
  - Diligent notifies IRS of spinoff

Consequences of spinoff

- Defect follows spinoff to new plan
- If employer requests spinoff must cure defects or plan subject to disqualification
- If MEP administrator spins off plan, same administrator, trustee, and terms of old plan
  - Rank-and-file participants treat as qualified plan
    - Can roll distributions over
  - IRS reserves right to go after Dudley Deadbeat
    - Deny rollover treatment
Act 2: Possible Qualification Failure
“What We’ve Got Is a Failure to Communicate”
- Dr Sly participates in Diligent’s MEP
- Diligent learns Sly may be in ASG with Sneaky Surgery Center (SSC)
- Diligent asks Sly for SSC census so Diligent can determine if there is a coverage failure
- Sly doesn’t reply
- Possible qualification failure: We don’t know that there’s a problem

Results
- Same procedure: 3 notices
  - Demand information or spinoff
- Suppose Sly provides data after second notice
  - Coverage failure exists
- Diligent informs Sly of possible actions to address cover failure; no reply
- Now it’s known qualification failure
- Start over with first notice

Effect on EPCRS
- Timing: MEP cannot be under examination at time of first notice
- If IRS audits plan after first notice, and MEP administrator acts diligently
  - Plan not treated as under examination for EPCRS
    - Can self-correct significant failure
    - Can still use VCP