More MEPS—Less Bad Apples

Multiple Employer Plans under the SECURE Act of 2019 and Proposed 2022 Regulations re Exemption from One Bad Apple Rule

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This article discusses the recent expansion of 401(k) and SEP/SIMPLE IRA multiple employer plans (MEPs) of unrelated employers with a pooled plan provider, and March 28, 2022 proposed Treasury regulations, based on the SECURE Act of 2019, to avoid the "one bad apple" rule where one participating employer fails to take the actions required by the Internal Revenue Code or ERISA and causes its portion of the MEP to be disqualified. MEPs administered by a pooled plan provider are becoming more common, particularly in light of recent guidance on how to comply.

MULTIPLE EMPLOYER RETIREMENT PLAN GENERALLY

Multiple employer plans, *i.e.*, plans that are maintained by more than one employer that are not collectively bargained, are subject to the more restrictive requirements under Code § 413(c). Under Code § 413(c), a multiple employer plan is treated as if all the employees were employed by a single employer for the following purposes: age and service requirements of Code § 410(a), the exclusive benefit rule of Code § 401(a)(2); the vesting rules of Code § 411; and the limit on contributions and benefits under Code § 415. For certain other purposes, multiple employer plans are treated as if each employer were maintaining a separate plan, for example: the participation requirements of Code § 410(b); the nondiscrimination requirements of Code § 401(a)(4); the actual deferral percentage (ADP) and average contribution percentage (ACP) tests of Code §§ 401(k) and 401(m); the vesting requirements upon termination or partial termination; the funding and deductions limits for plans established after 1988; the limit on annual compensation of Code § 401(a)(17) and the top-heavy rules of Code § 416. Code § 413(c); Treas. Reg. § 1.413–2 and other related regulations.

ALLOWING UNRELATED EMPLOYERS TO FORM A VALID ERISA MULTIPLE EMPLOYER PLAN (REFERRED TO BY THE SECURE ACT OF 2019 AS A POOLED EMPLOYER PLAN)

Open MEPs as Separate Employee Benefit Plans Under Pre-SECURE Act Law. Where a service provider sets up a retirement plan for multiple "unrelated" employers with no connection to each other and no connection to the service provider other than the provision of retirement services, the DOL had ruled in 2012 that such an arrangement was not one multiple-employer plan under ERISA but rather separate employee benefit plans for each employer.

Pre-SECURE Act Efforts to Expand MEPs. There had been efforts even prior to the SECURE Act of 2019 (discussed below) to expand access to retirement plans by small employers who find it difficult or too expensive to set up their own plans, by allowing such employers to join with other unrelated small employers in a multiple employer defined contribution plan (MEP).

Two significant impediments have made setting up MEPs difficult. One impediment has been that a MEP may be treated by the DOL as separate plans for each employer, especially for non-affiliated employers, requiring separate reporting and disclosure. (Another impediment is the one bad apple rule discussed below.) The DOL in 2019 issued guidance in DOL Reg. § 2510.3-55 to address the above concern regarding MEPs, with expanded rules as to when separate employers who participate in a defined contribution plan would be considered a single ERISA plan rather than multiple ERISA plans.

SECURE Act of 2019 Expansion of Open MEPs (PEPs). The SECURE Act of 2019, P.L. 116-94 (Dec. 20, 2019), expanded the use of multiple employer plans by allowing totally unrelated companies to use a single shared defined contribution "pooled employer plan" (PEP), provided the third-party plan administrator is a "pooled plan provider" that has registered with the DOL and acknowledges that it is a named fiduciary of the plan.

The SECURE Act defines "*pooled employer plan*" in new ERISA § 3(43)(A) as a qualified defined contribution plan or IRA with two or more employers that meets certain additional requirements. Employers in the pooled employer plan need not have a common non-plan-related interest. The plan must designate a pooled plan provider, provide that there will be no unreasonable fees for ceasing participation and provide for certain disclosure. (Note that the Internal Revenue Code does not use the term "pooled employer plan," but rather refers to a section 413(e) multiple employer plan that has a pooled plan provider).

"*Pooled plan provider*" is defined in ERISA § 3(44)(A) as (i) a named fiduciary and plan administrator responsible to perform all administrative duties reasonably necessary to ensure that the plan meets the qualification requirements of Code § 401(a) (or IRA that meets the requirements of Code § 408) and other ERISA requirements, and requiring participating employers to takes actions necessary for the plan to meet the such requirements; (ii) which must register with the DOL as a pooled plan provider; (iii) which must acknowledge its status as a named fiduciary and as the plan administrator; and (iv) which is responsible for ensuring that all persons who handle plan assets or are plan fiduciaries are bonded in accordance with ERISA § 412.

November 2020 DOL Regulations on Registration Requirement for Pooled Plan Providers. The DOL issued regulations in November, 2020, Prop DOL Reg. § 2510.3-44, effective November 16, 2020, pursuant to ERISA § 3(44)(A)(ii) with registration required 30 to 90 days before beginning operations as a pooled plan provider and with certain information about the pooled plan provider on DOL Form PR. Reporting on Form PR is also required if there are changes to the initially reported information or any government agency action or finding of fraud or criminal conduct relating to the assets or the operation of the plan. In addition, a final Form PR is filed on termination or cessation of operations of the pooled plan provider. Form PR must be filed electronically. DOL Reg. § 2510.3-44; Instructions to DOL Form PR.

Increased maximum amount of bond for pooled employer plan. With regard to a fiduciary or person holding assets of a pooled employer plan, the maximum bond amount under ERISA § 412(a) as amended by the SECURE Act of 2019 is $1 million instead of $500,000.

Form 5500 reporting. Form 5500 for all multiple employer plans must include a list of all the employers in the plan, a good faith estimate of the percentage of total contributions made by each employer, and the aggregate account balances attributable to each employer. For pooled employer plans, the Form 5500 now requires identifying information for the pooled plan provider. In addition, the limited scope audit exemption for plans with fewer than 100 participants, which also avoids the need for plan audited financial statements, is modified by the SECURE Act of 2019 to provide that simplified reporting can be used for multiple employer plans that cover fewer than 1,000 participants if no single employer in the plan has 100 or more participants.

Effective date. These regulations applies to plan years beginning after December 31, 2020.

MULTIPLE EMPLOYER PLANS—"ONE BAD APPLE" RULE AND MEPS EXCEPTION

Background. As referenced above, the second impediment to establishing and maintaining MEPs has been the unified-plan rule (also called the "one bad apple" rule) under which if one employer's portion of a multiple employer plan is disqualified the entire multiple employer plan will be disqualified. *See, e.g.*, Treas. Reg. § 1.413-2(a)(3)(iv). The IRS in 2019 gave some relief in Prop. Treas. Reg. § 1.413-2, which would permit an exception to the one bad apple rule if one employer refuses to correct its qualification errors or fails to provide information to the plan administrator regarding a potential disqualification.

Further Relief in SECURE Act from the One Bad Apple Rule Under Code § 413(e). The SECURE Act of 2019 added Code § 413(e), which provides relief for multiple employer qualified plans or multiple SEP/SIMPLE IRA plans of unrelated employers administered by a pooled plan administer from the "one bad apple rule" (also referred to as the uniform rule), that the entire plan will not be disqualified merely because one or more participating employers fail to take actions required by Code §§ 401(a) or 408(a) with respect to the qualified plan or IRA plan. Such relief will only apply if the plan provides that plan assets attributable to employees of the noncompliant employer will be transferred to a plan maintained only by that employer or to an individual tax-favored plans or IRAs and the noncompliant employer would be liable for any plan liabilities due to noncompliance. Code § 413(e) defines "pooled plan provider" substantially the same as ERISA § 3(44). The DOL and Treasury are directed it issue guidance regarding these provisions. These provision applies to plan years beginning after December 31, 2020.

2022 PROPOSED REGULATIONS REGARDING EXEMPTIONS FROM THE "ONE BAD APPLE" RULE FOR SECTION 413(E) MULTIPLE EMPLOYER PLANS OR IRA 2022

2022 Proposed Regulations. On March 28, 2022 the IRS issued proposed Treas. Reg. § 1.413-3 regarding the exception to the "one bad apple" (uniform plan) rule under Code § 413(e) for multiple employer defined contribution plans or IRA plans that are maintained by employers that either (i) have a common interest (other than the sharing of the plan) or (ii) have a common pooled plan provider (each, a "section 413(e) plan").

Conditions. For the 413(e) plan to be entitled to the exception from the one bad apple rule, the following conditions must be met: (i) the section 413(e) plan must describe the first, second and final notices that will be sent for a participating employer failure, the actions the section 413(e) plan administrator will take if an unresponsive participating employer does not either (a) take appropriate remedial action or (b) initiate a spinoff, and that if the unresponsive employer does not act by the 60 days after the final notice, participants of that employer will become fully vested in their accounts; (ii) the section 413(e) plan administrator must satisfy the notice requirements regarding the participating employer failure, implement the plan spinoff if initiated by the unresponsive employer and take the actions set forth in the regulations if the unresponsive participating employer fails to take appropriate remedial action or initiate a spinoff by 60 days after the final notice; and (iii) if the section 413(e) plan has participating employers that do not have a common interest and a "pooled plan provider" is required, the pooled plan provider must perform substantially all of the administrative duties that are required of the pooled plan provider under the regulations, as stated below. Prop. Treas. Reg. § 1.413-3(a)(2).

Pooled Plan Provider. A pooled plan provider is a person (an individual or entity) that: (i) registers as a pooled plan provider with the DOL pursuant to ERISA; (ii) is designated by the plan and acknowledges that it is a named fiduciary and the plan administrator; and (iii) ensures that those who handle assets or are fiduciaries are bonded in accordance with ERISA § 412. A pooled plan provider must: (i) perform all administrative duties reasonably necessary to ensure that the plan remains qualified/in compliance with the Code and ERISA; (ii) monitor compliance with the terms of the plan, the Internal Revenue Code and ERISA; (iii) maintain accurate data and up-to-date participant and beneficiary information; (iv) conduct nondiscrimination, minimum coverage and top-heavy tests under the Internal Revenue Code, as applicable; (v) process all employee investment changes, loans and distribution transactions; (vi) satisfies reporting and notice requirements of the Code and ERISA; and (vii) amends the plan for all statutory-required changes. Prop. Treas. Reg. § 1.413-3(a)(3).

Certain Section 1.413-3 Definitions. (i) "*Participating employer failure*" means failure to provide information or a failure to take action required of it by the regulations; (ii) "*Section 413(e) plan*" is a defined contribution plan IRA plan that either (A) has a common interest other than having adopted the plan or (B) has a pooled plan provider; (iii) "*Section 413(e) plan administrator*" means a plan administrator designated by the section 413(e) plan; and (iv) "*Unresponsive participating employer*" means a participating employer that has a participating employer failure. Prop. Treas. Reg. § 1.413-3(a)(4).

Notices. A section 413(e) plan administrator must provide a "*first notice*" to an unresponsive participating employer describing its failure, the actions the employer must take to remedy the failure, and that employer's option to initiate a spinoff of a separate plan of the unresponsive employer, and consequences if the employer does not comply. If, after 60 days, the employer does not take appropriate remedial action or initiate a spinoff, the section 413(e) plan administrator must provide a "second notice" which must state that if within 60 days the unresponsive participating employer does not takes appropriate remedial action or initiate a spinoff, then a "final notice" describing the participating employer failure and the consequences of not correcting the failure will be provided to participants employed by the employer, their beneficiaries and the DOL. A "final notice" provided within 30 days to participants employed the unresponsive participating employer and their beneficiaries and to the Office of Enforcement of the DOL EBSA must specify the final deadline for an unresponsive participating employer to take remedial action or initiate a spinoff. Prop. Treas. Reg. § 1.413-3(b).

Final Deadline. The final deadline for an unresponsive participating employer to take appropriate remedial action or plan spinoff is 60 days after the final notice. Prop. Treas. Reg. § 1.413-3(c)(1).

Appropriate Remedial Action. If the participating employer's fails to provide required information, appropriate remedial action is by providing the data, documents, or other information requested by the section 413(e) plan administrator. If the participating employer fails to take required action, appropriate remedial action is by taking all actions requested by the section 413(e) plan administrator, such as making corrective contributions. Prop. Treas. Reg. § 1.413-3(c)(2).

Implementing an Employer-Initiated Spinoff. An unresponsive participating employer can initiate a spinoff by directing the section 413(e) plan administrator to spin off the amounts attributable to its employees to a separate qualified plan or IRA plan maintained it. The section

413(e) plan administrator must complete the spinoff as soon as reasonably practicable, which is deemed to be met if the spinoff is completed within 180 days from when the spinoff was initiated. Prop. Treas. Reg. § 1.413-3(d)(2).

Required Actions Following an Employer's Failure to Meet the Deadline—Stop Contributions, Fully Vest Participants and Allowing Each Affected Participant an Individual Rollover to Another Qualified Plan or IRA. If by the time of the final deadline discussed above, the participating employer fails to take appropriate remedial action or initiate a spinoff, then as soon as reasonably practicable, the section 413(e) plan administrator must (i) stop accepting contributions from the unresponsive participating employer and its employees; (ii) give notice that no further contributions will be made and that additional information will follow; (iii) fully vest the employees; and (iv) give the each employee an option for an individual rollover to a qualified plan or IRA. Prop. Treas. Reg. § 1.413-3(e)(1) & (2).

As stated in the previous paragraph, an election must be given to employees of an unresponsive participating employer (following a failure to meet the deadline to take remedial action or initiate a spinoff) to have their account rolled over directly to another qualified plan or an individual IRA, or alternatively the participant's account will remain in the original section 413(e) plan. If no election is made, the default is to remain in the section 413(e) plan. Prop. Treas. Reg. § 1.413-3(e)(3). The option to remain in the plan does not exist if the participant's account is less than $200, in which case such amount will be mandatorily distributed. § 1.413-3(e)(4). Also, if there is a required minimum distribution under IRC § 401(a)(9), such amount must be distributed and cannot be rolled over or remain in the plan. § 1.413-3(e)(4).

Reliance Permitted Beginning March 28, 2022: These proposed regulations may be relied upon beginning March 28, 2022.

COMMENTS

It is not entirely clear to what extent pooled plan providers can delegate their functions to outside third-party administrators, *e.g.*, record-keepers.

The proposed rules only apply to defined contribution and IRA MEPs, but it is unclear if similar rules will be adopted to defined benefit MEPs.

The above proposed regulations, by implementing the unified plan rule for unrelated-employer MEPs, should eliminate a potential barrier to an employer joining such MEPs.