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IRS proposes multiple employer DC plan rules

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IRS proposed regulations would ease the threat of plan disqualification due to "one bad apple" for multiple employer defined contribution plans that meet documentation, notice and process steps. This supplements proposed guidance from DOL in 2018 and efforts on the Hill to expand access to multiple employer plans.

Background

Employers of all sizes may be concerned about how workers who are not covered by an employer-sponsored retirement plan prepare for retirement. Multiple employer plans (MEPs) have long been available to employers with a common nexus, providing an opportunity to employers who wish to take advantage of the benefits of the combination of assets, resources, and shared and reduced costs.

The DOL, in Advisory Opinions 2012-03A and 2012-04A, addressed the ERISA implications of an "open MEP" where there is no commonality of employers participating in the plan ("sufficient common economic or representational interest or genuine organizational relationship for there to be a bona fide employer group or association capable of sponsoring an ERISA plan on behalf of its employer members"). In such case, the arrangement is viewed as a collection of individual plans maintained by the separate employers. Consequently, the separate employers must:

- File Form 5500s for their own plan
- Obtain annual plan audits (assuming there are 100 or more employees participating in the plan)
- Obtain a fidelity bond for their plan

In addition to the foregoing administrative and cost burdens, a major impediment to participation in any MEP is the "one bad apple rule" in which the violation of qualification requirements by one employer can disqualify the entire plan under section 413(c) of the Internal Revenue Code (Code).

Buck comment: The "one bad apple rule" is presumably of lesser concern for plans that cover employers with some sort of commonality because the required nexus of the participating employers is likely to provide a greater degree of cooperation than in the case of an "open MEP."

Due to mounting support in Congress to fix MEPs through legislation and support from the administration in the form of Executive Order 13847, Strengthening Retirement Security in America, nudging DOL and IRS to address the situation, it was time for a change.

DOL is first to step up

First to step up was the DOL which, in October 2018, proposed regulations refining the definition of employer to accommodate defined contribution association and professional employer organization (PEO) MEPs. The DOL did not address quasi-related MEPs (which presumably do have nexus) or open MEPs (which do not). (See our October 30, 2018 *For Your Information*)

Congress is next

The Setting Every Community Up for Retirement Enhancement Act of 2019 (SECURE Act), passed by the House and currently under negotiation in the Senate, would facilitate open MEPs (see our *Legislate* from May 24, 2019) by eliminating the "one bad apple rule" for plans with a "pooled plan provider" unless the pooled plan provider fails substantially in performing his or her administrative duties. The pooled plan provider – registered with the IRS – would be the plan administrator and fiduciary and would be liable for ensuring that the plan meets the requirements of ERISA and the Code, including, among other things, testing, disclosures and bonding. Each employer in the plan would retain fiduciary responsibility for selecting and monitoring the pooled plan provider and any other named fiduciary. An employer in the plan would be liable for its qualification failure and would be required to spin off the assets of its employees into another plan, unless determined otherwise by the IRS.

Finally, IRS is up

Last, but not least, IRS proposed regulations on July 3, 2019, in consultation with the secretary of labor, that address the "one bad apple rule" – here defined as the "unified plan rule" – head on. Under the proposed regulations, a defined contribution MEP would be eligible for an exception to the unified plan rule stemming from certain potential or actual qualification failures due to actions or inactions by a participating employer, if these conditions are satisfied:

- The MEP satisfies certain eligibility requirements (e.g., adoption of appropriate practices and procedures and relevant plan language that details the procedures for addressing participating employer failures)
- The plan administrator provides notice of the participating employer's failure and opportunity to take remedial action or initiates a spinoff if the employer fails to act

- The plan administrator reports the spinoff to the IRS and responds to any IRS request for information in connection with the spun-off plan

IRS' proposal sets out specific timing and content requirements for the plan administrator to follow. The plan administrator would need to provide up to three 90-day notices to an unresponsive employer, with the third going to the DOL as well as plan participants and beneficiaries. If the employer remains unresponsive after the third notice, the plan administrator implements a spinoff (into a plan with the same terms as the MEP) and then terminates the plan. In these plan spinoff-terminations, distributions would still receive favorable tax treatment in accordance with regular plan termination rules; however, the IRS may pursue appropriate remedies against a responsible party. Should the employer initiate the spinoff, it may correct the spunoff plan's qualification issues under the IRS' EPCRS correction procedure.

Treasury and IRS decided not to extend the MEP rules to defined benefit plans in their proposal due to issues such as minimum funding requirements and spinoff rules, but they specifically asked for comments on whether the unified plan rule should be available to those plans.

The proposed rule would not be effective until the final rule is issued. Plan sponsors and administrators may not rely on the proposal in the interim.

In closing

Congress and the agencies appear to have a genuine interest in making MEPs more attractive to employers. Unfortunately, elimination of the "one bad apple rule" does not eliminate other stumbling blocks previously mentioned. Until employers see MEP participation as a net positive, the numbers will not increase. Comments may help and are due to IRS by October 1.

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