Exploring Multiple Employer Plans

by **Allen T. Steinberg** | *Law Offices of Allen T. Steinberg*

Defined contribution (DC) plans are the cornerstone of private sector employers' retirement programs—While 64% of private sector workers have access to a DC plan, only 17% have access to a defined benefit (DB) plan.[1] As the United States has moved to a DC-oriented system, policy makers have recognized some of the risks inherent in such a system—especially the risk that employees will not accumulate adequate assets for retirement.

Policy makers have responded to this risk largely by focusing on creating numerous bells and whistles to encourage employees to contribute to DC plans (including features such as pretax savings, tax-deferred earnings, nontaxable earnings (for Roth deferrals) and the Saver's Tax Credit) as well as other provisions to make it easier for employers to increase employee participation (such as automatic enrollment). Although most of the focus on increasing retirement savings has been on the employee side, there is an increasing focus on the employers that do not sponsor retirement plans and the recognition that lack of access to employer-sponsored plans is another drag on workers' ability to accumulate retirement resources.

Establishing and maintaining a retirement plan can be an expensive and complex proposition. Fees for recordkeepers, investment advisors, auditors—even if paid from plan assets—must be paid. Administering a plan requires either outside expertise (which carries additional fees) or internal personnel (who may lack the expertise or the bandwidth to perform administrative functions, thereby creating additional risk). Indeed, a majority of employers that do not sponsor retirement plans will cite cost or administrative expertise as the major reasons for not establishing a plan. For example, research from the Pew Charitable Foundation found that 37% of employers without plans said that starting a retirement plan is too expensive to set up, and another 22% cited a lack of administrative resources.[2]

AT A GLANCE

- Multiple employer plans (MEPs) established by associations of employers have been around for many years but have benefited from a regulatory boost in recent years.
- The seven key vendors for an association MEP include the recordkeeper, investment advisor, investment/financial education provider, plan administration provider, auditor, vendor management consultant and legal counsel.
- Research has shown that MEPs have higher costs than similarly sized single employer plans—but lower costs than the pre-MEP single employer plans.
- Participating in a larger plan such as a MEP can be seen as a two-edged sword. Employers (and participants) can benefit from enhanced services and lower costs. But a larger plan may attract more attention from plaintiffs' attorneys seeking potential class action litigation.

New Wave of Plan Structures

In response to gaps in employer offerings, policy makers have moved to encourage the use of various employer pooled arrangements that are designed to reduce the cost and administrative burden of plan sponsorship. These include pooled employer plans (PEPs) starting in 2021 pursuant to the Setting Every Community Up for Retirement Enhancement (SECURE) Act, multiple employer plans established by professional employer organizations (PEO MEPs) and multiple employer plans established by associations of employers (association MEPs).

This article will focus on association MEPs and describe some of their key features. This focus on association MEPs over PEPs is based on the fact that there are no PEPs in place yet. And while PEO MEPs are already in existence, the PEOs sponsoring PEO MEPs provide an array of other services to employers. The decision to join a PEO MEP also may be tied to other decisions regarding the PEO's services, while the decision to join an association MEP is more likely to involve a direct comparison of a single employer plan to the MEP.

The Sponsoring Entity

Unlike PEPs (which were not possible without the legislative changes contained in the SECURE Act), association MEPs have been permitted for many years. However, these MEPs have benefited from a regulatory boost in recent years.

The Employee Retirement Income Security Act of 1974 (ERISA) requires that a plan be established or maintained by an "employer" and further states that *employer* "means any person acting directly as an employer, or indirectly in the interest of an employer, in relation to an employee benefit plan" and includes "a group or association of employers acting for an employer in such capacity." Association MEPs are grounded in a simple proposition—that an entity, such as an association of employers, can act as an employer and sponsor a retirement plan for its member entities.

The key to this proposition is that the resulting plan is treated as a single employer plan under ERISA—so it can file a single 5500 and obtain a single audit for a plan that covers these different employers. More importantly, the MEP can be in a better position to negotiate lower pricing for services and can better afford to retain outside administrative services.

The ability of an association of employers to act as an employer is not new; this provision was in the original text of ERISA in 1974. However, final Department of Labor (DOL) regulations issued in 2019 provided guidance on the application of that term and provided association MEPs with a clearer regulatory path.[3]

Under the final regulations, the sponsoring entity must be a "bona fide group or association of employers," and a bona fide group or association of employers includes a group or association that meets the following criteria.

- The group or association also must have at least one substantial business purpose unrelated to offering and providing MEP coverage or other employee benefits to its employer members and their employees.
- Each employer member of the group or association participating in the plan is a person acting directly as an employer of at least one employee who is a participant covered under the plan.
- The group or association has a formal organizational structure with a governing body and has bylaws or other similar indications of formality.
- The functions and activities of the group or association are controlled by its employer members, and the group's or association's employer members that participate in the plan control the plan.
- The employer members have a commonality of interest. Such commonality can be met if the employers are in the same trade, industry, line of business or profession or each employer has a principal place of business in the same region that does not exceed the boundaries of a single state or metropolitan area (even if the metropolitan area includes more than one state).
- The group or association does not make plan participation through the association available other than to employees and former employees of employer members and their beneficiaries.
- The group or association is not a bank or trust company, insurance issuer, broker-dealer or other similar financial services firm, nor is it owned or controlled by such an entity.

These requirements may seem like unnecessary regulatory noise, but they serve a useful purpose. Unlike PEO MEPs

or PEPs, the sponsoring entity in an association MEP is not pursuing the MEP simply as a profit-making endeavor. This allows the sponsoring entity to select vendors without risking a taint of self-interest. This is in stark contrast to fiduciary litigation recently brought against other types of MEPs where the sponsoring entity was alleged to have engaged in prohibited transactions by retaining itself to provide services to the MEP and paying administrative fees to itself.[4]

This structure has the added benefit of bringing together employer human resources (HR) representatives in the plan governing committee. For HR professionals who are often tasked with multiple significant matters of compliance and need to manage their benefits budget while providing benefit plans that are attractive to employees, the committee meetings and discussion provide education and a forum for questions—not only from service providers but also from their peers.

The Vendor Team

In the author's experience, association MEPs have seven key vendors:

- Recordkeeper
- Investment advisor
- Investment/financial education provider
- Plan administration provider
- Auditor
- Vendor management consultant
- Legal counsel.

In some ways, this lineup is similar to the traditional single employer plan, but there are some key differences. At the heart of these differences between the association MEP vendor team and the typical single employer plan is the recognition that the use of an association MEP creates a scale that enables the retention of certain services that would be prohibitively expensive for each participating employer. As discussed below, these "additional" services may serve to better support participants—or better protect the plan.

There are several items to note in considering the vendor team:

- Many smaller single employer plans do not engage a separate entity to provide participant investment/financial education; rather, they rely on the recordkeeper for this function. Use of a recordkeeper to provide this service can create problems; recordkeepers are often financial services firms that offer "education" as a way of promoting proprietary products and services. Rather than supporting the employer-sponsored plan, such conflicted education can undermine it. The scale afforded by a MEP allows employers to separate these functions and obtain nonconflicted participant education.
- Similarly, smaller single employer plans may not have the resources—or feel the need—to retain an outside entity to manage their plan vendors. However, an outside consultant can play a key role in identifying vendors with appropriate expertise, providing initial due diligence, negotiating terms and providing ongoing review of vendor fees and services. These are precisely the practices that demonstrate that the MEP sponsor is acting consistently with ERISA fiduciary obligations. In an era where fiduciary risk is an ongoing concern, this role may prove to be increasingly valuable
- Association MEPs need an entity to serve as plan administrator. Identifying the administrator—and the functions of the administrator—can serve to illuminate some of the key differences between an association MEP and a single employer plan.

In the typical plan sponsored by small- or medium-sized employers, the administrative functions are typically split between the recordkeeper and the employer's internal staff. For example, the recordkeeper may provide services such as performing actual deferral percentage (ADP) and actual contribution percentage (ACP) and 410(b) tests, processing qualified domestic relations orders (QDROs), administering loans and processing distributions. At the same time, the employer's internal staff must handle other key functions—such as determining eligibility to participate, calculating employee and employer contribution amounts, and administering claims-and-appeals procedures.

The author has seen too many instances where employer personnel have made errors in administering a plan, which have resulted in costly self-corrections or Internal Revenue Service (IRS) penalties. In effect, the association MEP provides an opportunity for the employer to fully outsource all administrative functions to a provider with the expertise that

internal personnel do not have—and to gain the added protection that the outside administrator will correct errors and indemnify the employer if there are errors. Employers that have paid the price for administrative errors seem to welcome this opportunity.

Plan Costs

This brings us to the complicated topic of plan costs.[5] In addressing this issue, it is important to note the following.

- The costs for an association MEP cannot be directly compared with the costs for a similarly sized single employer plan. Consider an association MEP with ten employers, each with 500 participants, and a single employer plan with 5,000 participants. As noted above, association MEPs retain an outside administrator to perform functions that were previously performed internally. In the case of the single employer, these functions may still be performed internally—and doing so would make more sense for the single employer than for the ten MEP employers. This makes it difficult—and inappropriate—to simply compare the "cost" of these two different plans. And, although the selection of an outside administrator must be performed in accordance with fiduciary standards, the decision on whether (appropriate) administrative tasks should be borne by the employer or paid by the plan is a settlor function. After all, if the decision to allocate plan costs to the plan were a fiduciary decision, employers would never be able to require payment of fees from plan assets—shifting costs from an employer to a plan could not meet the fiduciary standard that such action be for the "exclusive benefit" of participants—and employers would always be responsible for all plan administrative costs.
- The outside administrator in a MEP has a more complicated task than the administrator of a single employer plan; however, this responsibility is borne by the outside administrator and not the employer. Consider the following: A single employer plan has a single set of features representing the plan design—such as eligibility, employer contributions, vesting and distributions—and the employer (and administrator) needs to deal only with that one set of provisions. In the case of an association MEP, each employer can select its own set of provisions—and the employer still deals with only one set of provisions. However, the outside administrator must be able to implement the full range of all options available to all employers in the MEP. This is more complicated than it seems—A relatively simple adoption agreement has more than a million different permutations that the administrator must support.
- Participation in a MEP may force an employer to address the question of using a per capita fee structure vs. asset-based fee structures. The author believes that the ease of levying asset-based fees across all plan participants has been one reason that plans continue to use this fee structure. However, the MEP structure of varying asset levels by employer as well as by employee will drive MEP vendors to price services on a per capita basis.
- As discussed above, joining a MEP is about more than costs. The ability to provide additional services (such as nonconflicted participant education and fully outsourced administration) represents added value for participants. This makes it more difficult to assess the before-MEP and after-MEP costs. In the author's experience, employers are not eager to join a MEP (even with these additional services) if the MEP brings a net increase in costs—but these same employers are willing to accept some reduction in savings for these same services.

These observations are borne out in a recent Morningstar research paper that observed that MEPs have higher costs than similarly sized single employer plans—but lower costs than the pre-MEP single employer plans.[6]

Risk Management

Moving to a MEP environment—especially an association MEP—forces participating employers to confront the current fiduciary litigation environment.

- The move to a MEP provides an opportunity to move to a structure and design that reflect the current trends in fiduciary risk management and litigation. For example, it may be the opportunity to move to greater use of index funds, nonconflicted participant education and an outside investment advisor.

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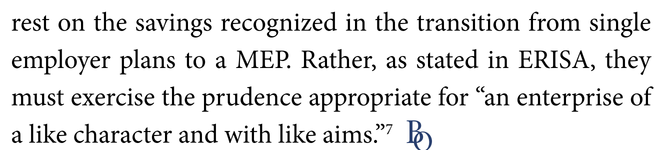
- The selection of MEP vendors also provides an opportunity to negotiate rigorous indemnification provisions. Vendors are attracted to the MEP market. To use the example described above, it is more attractive for a vendor to service one plan with 5,000 participants than ten plans with 500 participants each; MEPs can leverage vendors' desire to work with clients that will offer this kind of increased efficiency—both in negotiating fees and indemnification.
- The nature of fiduciary responsibility shifts in a MEP. Each individual employer remains responsible for the decision to join (or remain in) the MEP—but the responsibility for selecting and retaining each individual vendor is now the responsibility of the plan's governing committee (which, in an association MEP, is going to represent the participating employers). Accordingly, this governing committee needs to obtain its own fiduciary liability insurance; the individual employers' coverage is not likely to extend to participation on a MEP governing committee.

Participating in a larger plan such as a MEP can be seen as a two-edged sword. Employers (and participants) can benefit from enhanced services and lower costs. But a larger plan may attract more attention from plaintiffs' attorneys seeking potential class action litigation. Employers must be prepared to deal with both edges of this sword.

Living in the MEP Environment

This brings us to a closing observation. Employers will be drawn to an association MEP for the combination of lower costs and additional services described above. However, once in the MEP, the plan fiduciaries are now charged with exercising their fiduciary responsibilities in the context of being in a MEP—and this means justifying the reasonableness of vendor fees in that context. This does not mean that MEP fiduciaries must forgo the additional services provided by the MEP. Rather, it means that these fiduciaries cannot simply rest on the savings recognized in the transition from single employer plans to a MEP. Rather, as stated in ERISA, they must exercise the prudence appropriate for "an enterprise of a like character and with like aims."[7] BQ



Endnotes

1. Congressional Research Service, *Worker Participation in Employer-Sponsored Pensions: A Fact Sheet,* April 30, 2019 (Updated December 1, 2020): https://fas.org/sgp/crs/misc/R43439.pdf.
2. See www.pewtrusts.org/-/media/assets/2017/09/employer_barriers_to_and_motivations.pdf.
3. See www.govinfo.gov/content/pkg/FR-2019-07-31/pdf/2019-16074.pdf.
4. *Berkelhammer v. ADP TotalSource Group,* Case 2:20-cv-05696-ES-MAH, Filed May 7, 2020: https://si-interactive.s3.amazonaws.com/prod/planadviser-com/wp-content/uploads/2020/05/11160333/BerkelhammervADPTotalSourceComplaint.pdf. See also *Khan v. Board of Directors of Pentegra Defined Contribution Plan,* involving a non-PEO MEP where the plan sponsor also provided services to the plan: https://s3.amazonaws.com/si-interactive/prod/planadviser-com/wp-content/uploads/2020/09/17150410/KhanvPentegraComplaint.pdf.
5. For example, as noted in a recent survey by Callan, plan costs remain employers' top concern: www.callan.com/wp-content/uploads/2020/01/Callan-2020-DC-Trends-Survey.pdf. And, of course, plan costs remain the source of much fiduciary litigation.
6. *Paperwork or Panacea:* www.morningstar.com/content/dam/marketing/shared/pdfs/Research/Paperwork-or-Panacea.pdf?utm_source=eloqua&utm_medium=email&utm_campaign=&utm_content=23605.
7. 29 USC Section 1104.

AUTHOR

Allen T. Steinberg is an attorney in Evanston, Illinois, where his legal practice focuses on helping employers navigate compliance challenges while designing benefit plans that meet employer and employee needs. He has more than 35 years of experience providing employers with advice, ideas and support for a broad range of benefit plans. During his career, Steinberg has been an associate with a major Chicago law firm and a partner at a global consulting and actuarial firm. Visit his website at https://ERISAstrategies.com.

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