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August 2012

Open MEPs and DOL Guidance: Where Do We Go From Here?

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On May 25, 2012, the Department of Labor (DOL) issued Advisory Opinion 2012-04A, which opined that Open MEPs are not multiple employer plans or, in other words, are not MEPs. That DOL guidance has been well publicized, but it is little understood. This article examines the development of Open MEPs and the likely consequences of the DOL's guidance. The conclusion is that almost, but not quite, all of the advantages of Open MEPs will be retained in one form or another.

The starting point for understanding the development of Open MEPs is that 401(k) plans are complex to operate and create the prospect of fiduciary liability for small companies and closely held businesses and their owners and officers. Some of those companies would prefer to hire a professional fiduciary to choose the service providers, select and monitor the investments, analyze the expenses, and administer the plan. That is not unreasonable, as long as the professional fiduciary is competent and works with reputable providers and experienced advisers. Because of those concerns, trade associations have for many years offered retirement plans and other benefit programs to their member companies. In more recent years, Open MEPs have been established for employers who desired the benefits of a professionally managed retirement plan, but who may not belong to a trade association or who may not have wanted to use a program sponsored by their trade associations. Those so-called Open MEPs have grown rapidly in popularity and have increased the number of employees of small- and mid-sized companies who are covered by qualified retirement plans. However, the Department of Labor, in its controversial advisory opinion, ruled that Open MEPs were not multiple employer plans, but instead a collection of single employer plans with a shared investment fiduciary, plan administrator and funding vehicle. What does that mean for employers who have already adopted Open MEPs or who may be considering participating in such a plan?

> First, and importantly, the DOL position does not affect the tax qualification of the plan or the tax exemption of the trust. Under section 413(c) of the Internal Revenue Code, Open MEPs are specifically permitted. In other words, Open MEPs are authorized under the Internal Revenue Code and the DOL has no authority to interpret the Code. So, from a purely tax perspective, employers don't need to make any changes.

- Some attorneys are saying that the DOL opinion means that employers now must prudently select and monitor the "sponsor"[1] of the MEP. However, from my perspective, that has always been the case. That is, we have always advised employers that, when they decide to participate in an Open MEP—or, for that matter, a trade association MEP—they are making a fiduciary decision. Essentially, the fiduciary decision is to engage the services of the entity that sponsors, or oversees, the arrangement. Since it is a fiduciary decision—and always has been, employers must act prudently to decide whether to participate in the arrangement and must monitor that decision at appropriate intervals.

- The next and obvious question is, if the DOL guidance does not affect the tax qualification of the plan, then what does it affect? Based on our analysis of the ERISA provisions for retirement plans, it has three consequences.

  First, each employer will be considered to sponsor a single plan with shared fiduciaries, investments, administration and trust. As a result, plans that are considered to be "large" plans by the DOL (that is, as a general rule, plans with 100 or more participants) will be required to file audited financial statements with the Form 5500 for their plan. Obviously, for those larger plans, there will be some additional accounting fees. However, that cost will probably be less than expected because (i) the sponsors of the arrangements can negotiate lower accounting fees because there will be a number of plans with almost identical circumstances that are being audited, and (ii) the cost of auditing the MEP itself may no longer be incurred, resulting in a slight savings. Also, keep in mind that, "small" plans—which make up a significant number of the employers who have been participating in MEPs—do not need to have an accountant's audit.

  Second, a Form 5500 will be required for each plan rather than for the MEP as a whole. That will result in some additional cost. However, since there will be a single provider, that is, the sponsor of the new multiple arrangements, most of the information for the 5500s will be held centrally, and since the investment options and most other factors are standard across all of the plans, the increase in cost should not be significant.

  Finally, each plan will need to be covered by an ERISA bond. That could be done either through individual ERISA bonds or through a single bond with individual plan limits.

- On the other hand, some former MEP sponsors may decide that they can continue to offer the most important MEP advantages, but in a single plan and trust scenario. For example, the most common advantages of a MEP arrangement are the engagement of a single fiduciary to oversee the selection and monitoring of the investments, the evaluation and negotiation of expenses, the selection and retention of service providers, the use of knowledgeable RIAs as investment advisers, the responsibility for the administration of the plan, and the preparation and maintenance of plan documentation and related materials. Those same benefits can be provided in an efficient setting if the investments,

1 In this context, the "sponsor" of an Open MEP is the service provider that establishes the plan and administers it on behalf of all the adopting employers. The third-party administrator (TPA) or similar provider that sponsors the MEP is usually also the plan's "named fiduciary" and thus has the responsibility for appointing and monitoring the plan's other service providers.

service providers, administrative procedures, and so on, are consistent across a large number of plans. Similarly, the sponsor of the new single plan arrangement could conveniently provide standardized annual reports to adopting employers about the investments and services of the plan, enabling the adopting employers to fulfill their fiduciary responsibility to monitor the activities of the sponsor of the arrangement as the operating fiduciary.

- Another alternative for minimizing the cost of the changes to accommodate the DOL's new guidance is to use a Direct Filing Entity (DFE), for example, to use a common or collective trust as the funding vehicle. Where a collective or common trust (or other DFE pooled investment entity) is used, the retirement plans will still be individually sponsored, but the investments will be aggregated in the investment pool. In that case, the work necessary for the preparation of the Form 5500 and the accountant's audit, is significantly reduced, as compared to providing those two services to the plans individually. As a result, those administrative costs can be reduced on a per plan basis. And, the individual plans can still enjoy the benefit of using a single, professional fiduciary for purposes of overseeing the management of the investments (and the investment adviser), administering the plan, and so on.

As a result of the DOL guidance, and of these alternative "solutions," the impact on the adopting employers for Open MEPs should be relatively small. Based on the work that we are doing for the sponsors of Open MEPs, those sponsors are taking the responsibility for making the changes to comply with the DOL's guidance, but to continue to operate their plans in a manner that provides efficiencies of scale and fiduciary protections for the adopting employers. So, changes are being made, but based on our experience, those changes are being undertaken by the sponsors of the Open MEPs and the costs are being borne by those sponsors.

So far, this article has discussed the changes that Open MEPs need to make to satisfy the DOL's new Advisory Opinion. But, the flip side of the issue is, what types of MEPs can continue to operate and be consistent with the DOL guidance? While a full discussion of that subject would be too long for this article, here are several key points:

- Generally speaking, trade associations can sponsor MEPs for their members without concern of being challenge by the Department of Labor. However, they need to be legitimate trade associations and not just a facade established for the purpose of providing benefits.
- By definition, an association would ordinarily have a commonality of interest among its members. The most common example is a trade association which consists of businesses that are in a certain industry. It is also possible that an association could have geographic representation of businesses, so long as there was a legitimate business interest in geographic representation. In applying this criterion, the DOL is looking for a substantial, pre-existing relationship related to the core operations of the association members.
- The provision of benefits—both retirement and health and welfare—should be subordinate to the business or economic interests of the association. That is, the primary purpose of the organization needs to be economic, business, financial or other similar purposes. Once the businesses have gathered together on that basis, they can then provide ancillary benefits to their members.

> The members should effectively control the association or employer organization. That should be evident in the voting procedures and in the make-up of the governing body, for example, a board of directors. The members of the association—perhaps acting through the board of directors—should be able to terminate the arrangements with the service providers for the benefit programs.

That is not a full list of everything that can or should be considered. However, as a general rule, if the association or affiliation of employers satisfies those standards, it is probable that it could properly sponsor benefit programs for its employer members.

The foregoing discussion about the DOL's position is intended to be just that . . . my interpretation of the Department of Labor's position. In many ways, I believe the Department's position in the Advisory Opinion is incorrect. However, for the time being at least, it is the most authoritative guidance on the subject. As a result, there is some risk in participating in an Open MEP. Having said that, I believe that the Department will work with Open MEP sponsors to allow them to implement needed changes, without imposing penalties for prior failures to file 5500s and/or to obtain accountant's audits for large plans.

As a result, my advice to employers who have adopted Open MEPs is to contact the Open MEP sponsor in order to gain an understanding of the changes that are going to be made and how they will satisfy the Advisory Opinion. Any of the three alternatives discussed in this article should be acceptable . . . and there may be others. However, I would be concerned if the sponsor of the Open MEP said that it was not going to make changes.